

Economic conditions in Germany

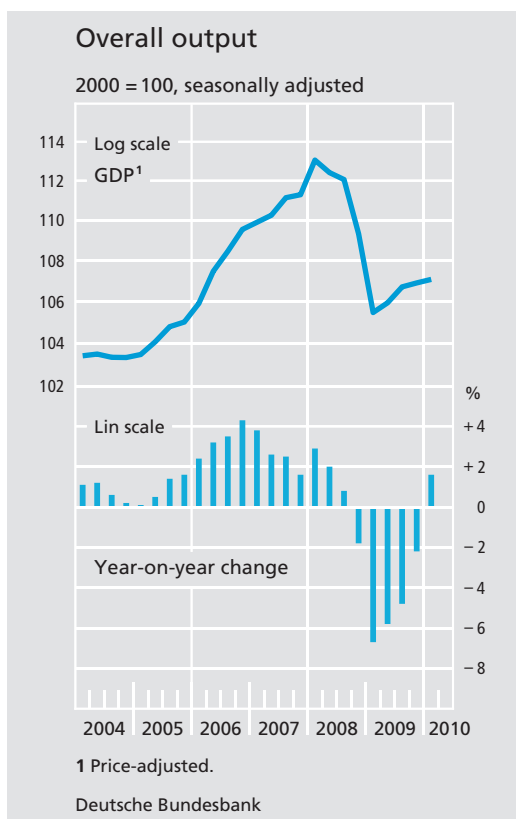
Macroeconomic situation

The upturn in the German economy continued after the start of 2010 despite temporary negative factors. The considerable tensions in the international financial markets in the wake of the escalating debt crisis in Greece and the resulting contagion effects on other euro-area countries have not, so far, been reflected in the real economy. According to the Federal Statistical Office, real gross domestic product (GDP) was 0.2% up on the quarter after seasonal and calendar adjustment. Following an upward revision of the data, a similar increase is now shown for the final quarter of 2009. This means that, on balance, the export-driven trend recovery in the economy outweighed the temporary retarding effects on domestic activity. The exceptionally cold weather and heavy snowfalls in January and February hampered activity in the construction and transport sectors considerably, and the indirect effects of this are likely to have made themselves felt in industry, too. However, not least given the rather favourable orders situation, enterprises rapidly stepped up their production again in March. Households continued to reduce their consumption expenditure following the expiry of the environmental premium for scrapping old cars. Overall output in the reporting period was a calendar-adjusted 1.6% up on the cyclical low of one year earlier.

*Recovery
process held up
by weather*

In the first quarter of 2010, the German economy continued to benefit, first and foremost, from the pick-up in export business. There was a seasonally adjusted 2.6% rise in exports of goods and services on top of a

*Exports again
up considerably*



marked increase in the second half of 2009. Measured in terms of real flows of goods, exports to other euro-area countries grew somewhat more sharply in the reporting period than did exports to countries outside the euro area. However, demand for German products in non-euro-area markets had already risen strongly in the final quarter of 2009. This early turnaround and the rapid pace of economic growth in the emerging market economies (Asia, in particular) along with the increasingly entrenched upswing in the US economy have played a key part in recovering, to date, roughly one-half of the massive downturn in the volume of non-euro-area exports suffered during the financial and economic crisis. By contrast, much less progress has been made in the recovery of exports to euro-area trading partners.

Imports of goods and services increased very sharply in the first quarter of 2010 at a seasonally adjusted 6.1% following a decline of 1.6% in the preceding quarter. It is striking that, after the turn of the year, the German economy increased its real imports of goods from the rest of the euro area by 11¼%; admittedly, the volume of imports from other euro-area countries had been very low before. Imports of goods from non-euro-area countries also increased following the downturn in the preceding quarter and, in the reporting period, were marginally up on their level in the third quarter of 2009. Since the cyclical low, the trend in imports has been only slightly weaker than in exports. Notwithstanding its sharp decline in the period under review, which almost entirely negated the exceptional increase one quarter earlier, the foreign trade surplus was tending to grow again in seasonally adjusted terms, but was, on average, well down on the level reached at the end of the preceding boom.

Very sharp growth in imports

Investment in machinery and equipment increased by a seasonally adjusted 1.6% during the reporting period, offsetting the decline in the final quarter of 2009. With regard to movable fixed assets, the underlying trend in investment is characterised by a sideways movement following the massive correction of investment one year earlier. Among other things, the reporting period saw an increased acquisition of motor vehicles for fleets of passenger cars and pools of commercial vehicles. Evidently, many enterprises were no longer able to defer the necessary investment in replacements in this area. This motive may have also been one of the factors that led to more

Increased investment in machinery and equipment

machinery and equipment being procured. Given the perceptible underutilisation of overall production capacity, the increase in this category of goods was comparatively small, however.

Weather-related decline in construction activity

Although construction investment was clearly hampered by the cold winter weather and heavy snowfalls, the decline, at 3.8%, was on a limited scale in contrast to comparable frosty spells. In the first quarter of 2010, the number of days of ice – measured as an average for Germany as a whole¹ – was more than twice as high as the multi-year seasonal average. The weather-enforced break in outdoor industries was essentially concentrated on the first two months of the year. As early as March it was possible to start catching up on the backlog. Moreover, further construction measures were being planned on a considerable scale during the winter months. According to Ifo surveys, there was only a marginal deterioration in the business situation of architects at the start of the first quarter after the stock of orders at the end of 2009 had reached its highest level for 15 years. Furthermore, construction investment was buoyed up by the fact that the building completion sector – which is much less dependent on weather conditions – was encountering quite a favourable orders situation, not least owing to the government economic stimulus packages, which also provide funds for the renovation of public buildings.

Private consumption down owing to drop in demand for cars

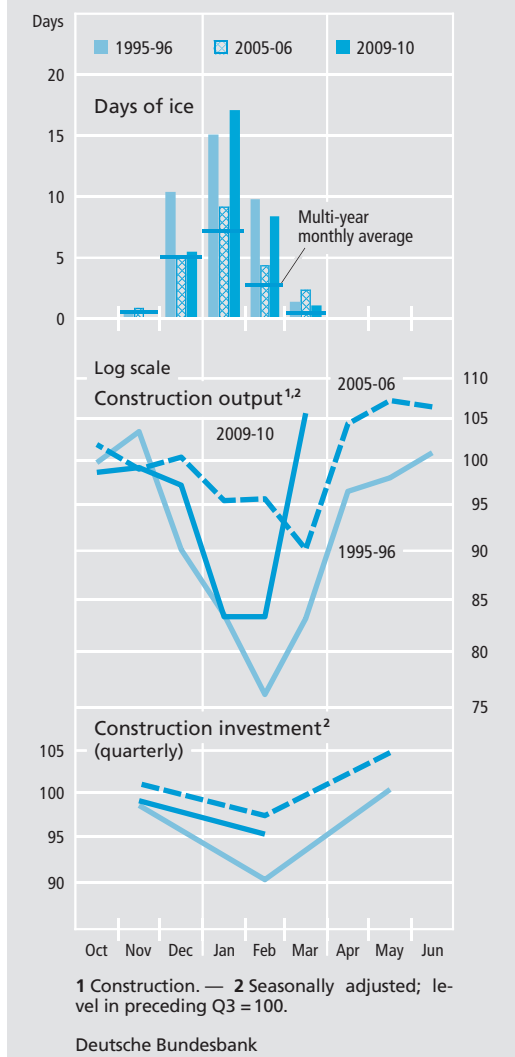
In the first quarter of 2010, households cut back their consumer spending by a seasonally adjusted 0.8% on the quarter in real terms. This was due mainly to the fact that deliveries



of cars to households continued their steep downward trend up to February. Since then, the number of new registrations of non-commercial vehicles has largely remained below its level prior to the introduction of the car scrappage scheme. There was a sharp in-

¹ A "day of ice" is defined as a day on which the highest temperature does not go above freezing point. The indicator used here weights the results of various monitoring stations in accordance with the regional employment structure in the construction sector.

Impact of weather on construction: a comparison of severe winters



crease in sales of light heating oil during the reporting period. This may be connected with the fact that many households had to fill up their tanks early owing to the high level of oil consumption during the cold winter months. Seasonally adjusted retail sales more or less maintained their prior-quarter level. Apart from the above-mentioned special factors, the underlying trend in consumer sentiment appears to be still quite resilient.

Sectoral trends

Industrial output continued its recovery in the first quarter of 2010. With growth at a seasonally adjusted 1.3% on the quarter, the pace of economic activity in this sector showed hardly any change compared with the last three months of 2009 and was therefore still well down on the rate of expansion in the third quarter of last year. One likely contributory factor is that the increase in the flow of orders was somewhat weaker in the fourth quarter of 2009. The very sharp increase in output in March might be an indication that production had not been stepped up at the beginning of 2010 owing, in part, to weather-related delays in the transportation of goods. This is consistent with the finding of the Ifo surveys that manufacturing capacity utilisation shot up by 4½ percentage points to 79¾% of normal full capacity at the beginning of the second quarter.

Further upturn in industrial output ...

At a seasonally adjusted +2% on the quarter, it was again producers of intermediate goods that recorded the sharpest increase during the reporting period. While output of capital goods showed a rise of just under 1%, the increase in the consumer goods sector was moderate. Moreover, identifiable differences exist in sectoral terms with regard to the stage of the cyclical recovery. In the intermediate goods sector, it was the chemicals industry that continued to pick up most; it was the first major industrial sector to have ushered in the trend turnaround and has already made up roughly three-quarters of the loss of output suffered as a result of the recession. In the basic metals sector as in the

... with sectoral discrepancies

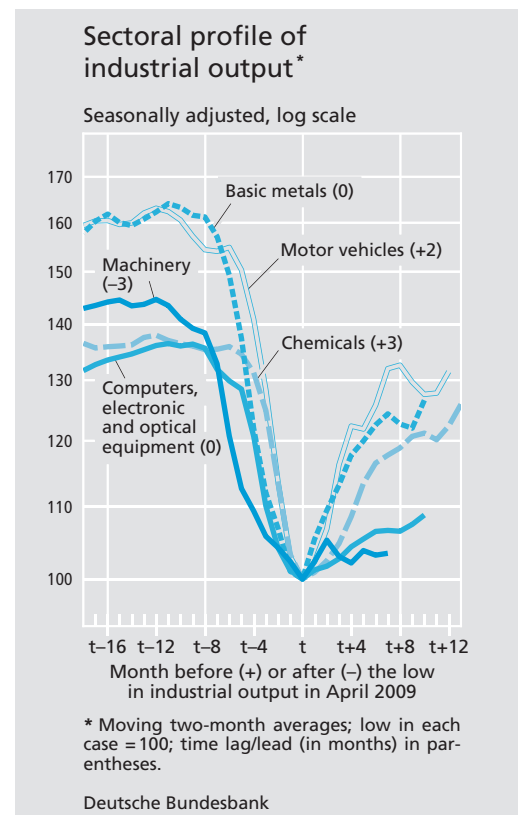
automotive industry, the recovery resumed only after a period of stagnation, which was due mainly to the waning impact of the environmental premium; the upturn had been relatively steep initially owing to the stimulus from the demand for cars. The pick-up in the electrical and mechanical engineering sectors has been rather subdued so far. The fact that production of machinery and equipment has made little progress since its cyclical low is also due the cyclical lag in this sector of industry.

Construction activity and energy production affected by winter weather

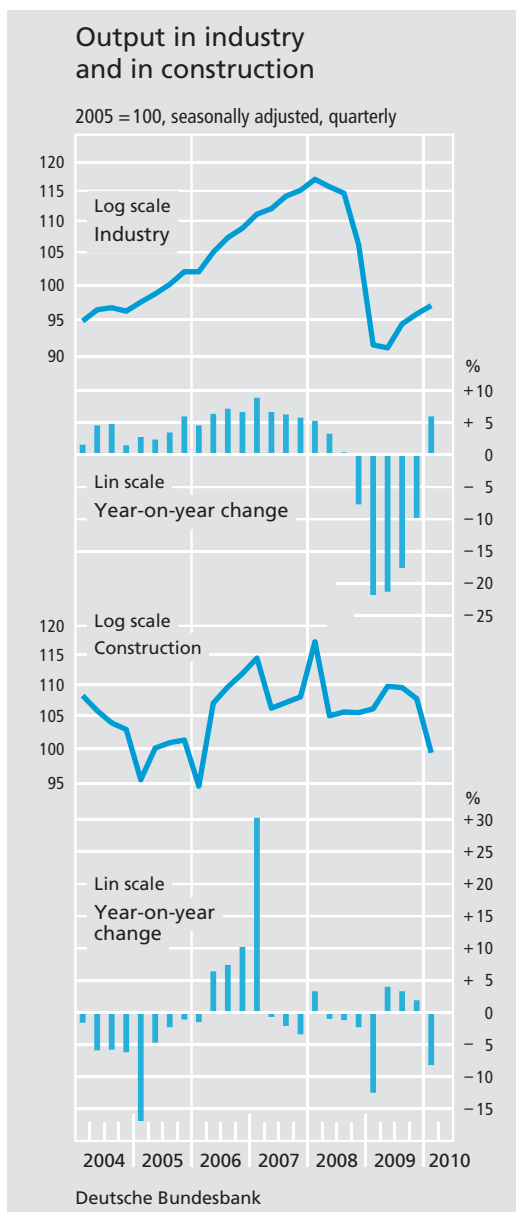
Energy production and construction activity were affected by the weather in the first quarter of 2010. The cold winter led to a marked seasonally adjusted increase in energy production. Construction output, however, was 7.7% down on the quarter, although the building industry had to contend with somewhat smaller losses than the civil engineering sector.

Upturn in most services sectors

Business activity picked up in most services sectors at the beginning of the year. In seasonally adjusted terms, real wholesale sales, which are shaped by business with trade and industry, gained momentum in the first quarter of 2010. In addition, retail sales remained quite stable. Overall, there was a slight fall in sales of motor vehicles, with the decline in sales of new vehicles to households, which no longer had the stimulus of the environmental premium, outweighing the increase in sales to commercial customers. The turnover of hotels and restaurants, which had dropped considerably in the final quarter of 2009, did not show any meaningful improvement in the first quarter of 2010. According to the na-



tional accounts data, the transport and communication sectors suffered losses in the first quarter in seasonally adjusted terms. The weather is likely to have played a part in this, too. The monthly statistics on motorway tolls, for example, indicate that driving was severely hampered by snow and ice in January and February, but increased sharply in March and April. (For more details on the use of motorway toll statistics in the economic analysis, see the box on pages 64-65.) Value added in the financial intermediation sectors and in business-related services showed a perceptible increase after the start of the year. The increase in the public and private services sectors was smaller than in the preceding quarters, however.



Employment and unemployment

*Employment
in 2010
Q1 stable
overall ...*

The labour market situation is still remarkably robust. According to estimates by the Federal Statistical Office, employment in Germany remained virtually unchanged in the first quarter of 2010. While there was a reduction in low-paid part-time jobs, there was a slight increase in employment subject to social security contributions. One factor in this is likely to

have been that weather-related cutbacks in employment in the construction sector were largely offset by seasonal short-time work.

Activity in the labour market after the start of the year was still being shaped by diverging trends which, so far, have largely cancelled each other out. There continued to be marked increases in staffing levels in wholly or partly publicly financed services, while there was a further reduction in employment in the production sector, where the fall in the number of jobs subject to social security contributions was similar in scale to that in the final quarter of 2009. Although the recovery in industrial activity has already made marked progress in some cases, the process of adjusting staff levels appears not to have been completed yet in a number of major sectors. Nevertheless, the number of temporary workers – usually employed, to a large extent, in industry – has been going back up since the second half of 2009.

*... but growing
gap between
sectors*

The fact that there is still a considerable employment overhang when measured against current output is revealed, furthermore, by the fact that short-time work for economic reasons is declining only slowly. In December 2009, this affected 810,000 members of staff; this corresponds roughly to 238,000 employees' work being lost completely. New registrations for short-time work fell by one-third in the first quarter of 2010. Nevertheless, a still quite high level is suggested by the fact that the resources spent for this purpose by the Federal Employment Agency have hardly fallen since the start of the year and

*Cyclically
induced short-
time work still
at a high level*

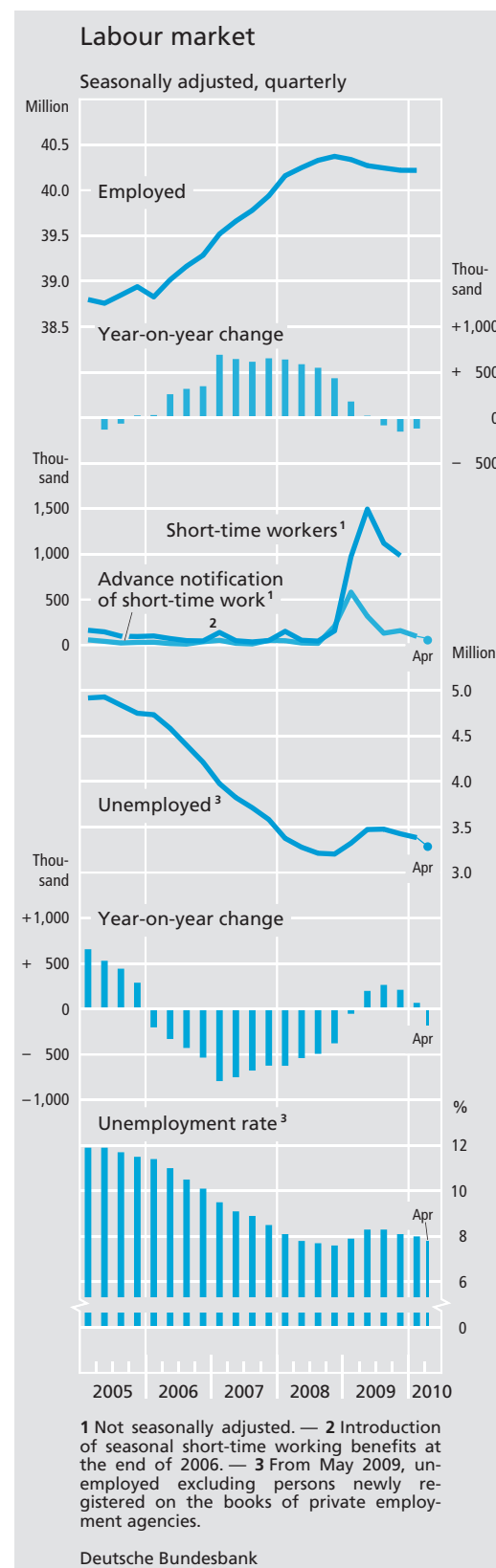
were still around one-half of their peak amount in the second quarter of 2009.

Unemployment down minimally after the start of the year ...

In the first quarter of 2010, the seasonally adjusted number of persons registered as unemployed was 3.38 million. Despite the very cold winter weather, this was 42,000 fewer than in the preceding quarter. This decline is likely to have been due chiefly to the expansion of labour market policy measures. However, seasonally adjusted unemployment in the broader sense, which additionally covers job seekers on the books of employment agencies, participants in training schemes, and the long-term unemployed of more than 58 years of age without the prospect of a job offer, was 9,000 persons higher than in the fourth quarter of 2009. The lower commuter balance may also have had a dampening impact on the unemployment figure. The official unemployment rate stood at a seasonally adjusted 8.0% in the reporting period, and was thus only marginally (0.1 percentage point) higher than the comparable 2009 level. The unemployment rate in the broader sense showed a year-on-year increase of 0.7 percentage point.

... and perceptible decline at the beginning of Q2

In April 2010, the seasonally adjusted unemployment figure showed a marked fall of 68,000 on the month to 3.29 million. The unemployment rate went down to 7.8%. One reason why the decline was so sharp is likely to be that the relevant reference date for the statistics in that month fell within a period of increased recruitment after the end of the Easter holidays.



Information content of toll statistics for economic analysis

In January 2005, Germany implemented a distance-based toll on trucks with a gross vehicle weight exceeding 12 tonnes (heavy trucks). Tolls are collected on all German motorways (*Autobahnen*) as well as on individual stretches of three trunk roads (*Bundesstrassen*). The Federal Office for Goods Transport (*Bundesamt für Güterverkehr*, BAG), which is responsible for collecting tolls, compiles statistics from which it publishes regular monthly findings, beginning with the survey period January 2007. Among other things, the toll statistics cover the mileage of toll-liable heavy trucks by country of origin. This not only makes it possible to conduct structural studies of road goods transport; since the BAG usually publishes its evaluations extremely quickly, only 15 working days after the end of each reporting period, this information is also of relevance to short-term business cycle analysis.

In the last three years, commercial vehicles registered in Germany accounted for almost two-thirds of total toll mileage. For geographical reasons, the vast majority of the remaining mileage was accounted for by trucks from other EU countries. Of the commercial vehicles from non-German EU countries, those registered in the new member states of central and eastern Europe travelled appreciably

greater distances in Germany than trucks from western Europe: in the first group, Polish and Czech vehicles take an outstanding share, while in the second, that of Dutch trucks is comparatively large.

Considerable deviations are to be found in terms of regional structure between the mileage travelled by foreign trucks and the flows of goods in German foreign trade. Given that only a fraction of the goods traded within the EU is transported by road and, moreover, that Germany is only the transit country for a part of the goods transferred, certain discrepancies are to be expected. However, the relatively large shares accounted for by some central and eastern European countries indicate that transport service providers from those countries are overrepresented in terms of road haulage journeys to and from Germany in relation to trade in goods. A further relevant factor is probably that central and eastern European road hauliers are also hired to transport goods within Germany.

Since the minimum number of observed values was obtained, the Bundesbank has calculated the monthly mileage by toll-liable vehicles adjusted for seasonal and calendar effects. In addition to total mileage, data are provided broken down by commercial vehicles registered in Germany and abroad, respectively. The time series poignantly reflect the slump in trade in goods due to the sharp recession in the fourth quarter of 2008 and the first quarter of 2009. Between October 2008 and March 2009, the total toll mileage travelled by heavy trucks per month fell by one-eighth. The onset of economic recovery in the second quarter of 2009 initially brought a rather tentative increase in mileage. Not until March and April 2010 was a clear upward trend recorded.

Although the observation period is still fairly short, the results of the toll statistics trace a fairly accurate picture of general economic activity. Yet the question whether, generally speaking, the mileage travelled by heavy trucks is suitable as a leading indicator of economic developments must also be examined rationally. The transport of goods is directly linked to overall economic output through its sectoral contribution to value added and indirectly through the relationship between the production of goods and the transport of goods.

Transport of goods by foreign-registered trucks on German toll roads, by country or region of origin

Average 2007 to 2009; percentage shares

Country or region of origin	Mileage	By comparison: trade in goods ¹
EU	91.9	84.1
Euro area	39.6	57.2
of which		
France	1.0	12.3
Italy	3.7	8.5
Spain	2.2	5.0
Netherlands	13.5	10.2
Central and East European EU countries ²	49.5	13.8
of which		
Poland	24.6	5.0
Czech Republic	10.9	4.3
Hungary	4.8	2.6
Baltic states	5.1	0.6
Other EU countries	2.9	13.1
Non-EU countries	8.1	15.9

¹ Total exports and imports of goods. — ² Where not a member of the euro area. — ³ The transport of goods by non-residents – which may be assumed in the case of foreign-registered toll-liable vehicles – is classified in national accounts as the import of transport services, even

if goods are neither imported nor exported. — ⁴ Besides freight transport by road, the transport sector as defined by the national accounts also includes the conveyance of passengers by road as well as all transport by rail, ship and air. Also included, moreover, are auxiliary trans-

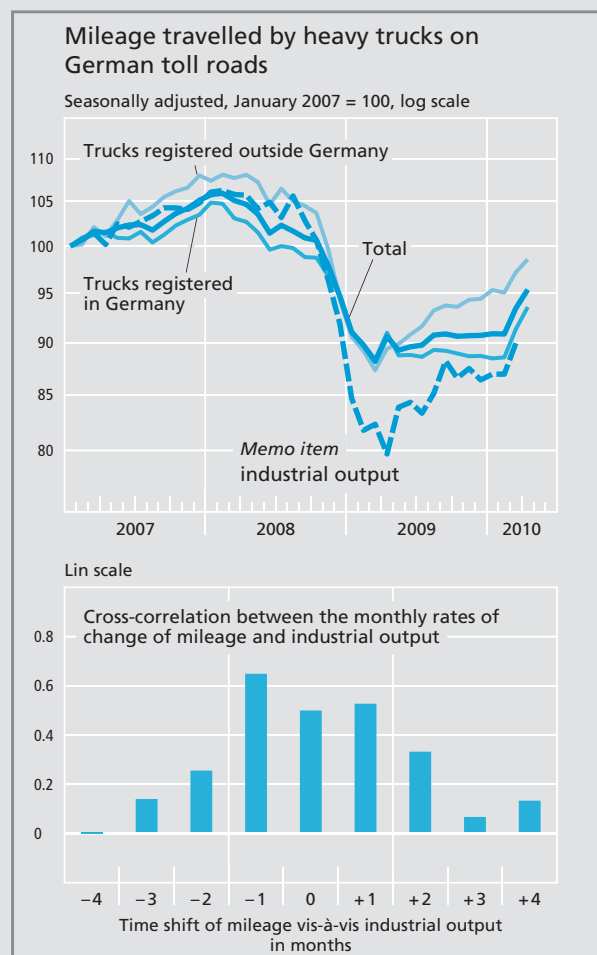
The mileage of German-registered toll-liable vehicles is likely to be closely correlated with the value added of carriers and forwarding agents.³ Assuming that the transport of goods by rail, ship and air develops along similar lines because short-term substitution possibilities are limited, the findings of the toll statistics might offer a suitable approach for assessing the activities in this sector of the economy.⁴ However, the share accounted for by the freight transport industry as a whole in the output of all economic sectors (at basic prices) is rather small at an estimated 2½%.

For this reason, the suitability of toll statistics as an economic indicator is probably better explained by the service function of goods transport for industrial output. Since both in materials management and in production control, large inventories are today for the most part dispensed with, the delivery of commodities and intermediate products – like the subsequent transport of finished goods – is closely linked to the production process as regards the time factor. Thus, the total mileage travelled by all heavy trucks could be a leading indicator of industrial output, and even in the event of a high contemporaneous correlation between the two series a (pseudo) leading indicator property could just result from the fact that the toll statistics are published about three weeks before the corresponding monthly output data. According to the Federal Statistical Office's input-output tables for 2006, the manufacturing industry accounted for demand for about one-third of all direct transport services by land (ie road and rail together). Moreover, only use in trade and in indirect transport services is of quantitative significance.⁵ The relationship between the production of goods and the transport of goods – at least insofar as goods produced in Germany are transferred for commercial enterprises – should tend to grow even closer via the trade channel. In principle, the same applies to the share of the forwarding business, which (in terms of turnover) accounts for about three-fifths of indirect transport services.

According to the statistical analyses in the sample from January 2007 until March 2010, the seasonally adjusted monthly rates of change of toll mileage and industrial output are markedly correlated. Compared with the contemporaneous relationship, the link is even somewhat

port activities (eg cargo handling and storage) and the activities of transport agents such as freight forwarders as well as of travel agents and operators. — 5 It must be noted, however, that input-output

greater assuming either a lead or a lag of one month. This is consistent with the fact that freight services are usually provided before and after the goods production process. The highest correlation, which is based on the role of input supplier, suggests a leading indicator function for industrial output. Thus, forecasts of the trend rate of industrial output should improve if the rate of change of the total mileage travelled by heavy trucks from the previous month is included in the information on which the forecast models are based. Initial econometric results, though promising, must be deemed provisional given the short observation period.



tables do not provide separate data for the transport of passengers and goods, respectively.

*Increasing
employment
intentions
boosting mainly
temporary
employment*

Following major improvements over the past months, both the Ifo employment barometer for trade and industry and the BA-X have now reached values which, in the last upswing, marked the start of a perceptible increase in employment. In contrast to the present situation, utilisation of staffing levels in parts of the economy was significantly higher than – as can be seen from the number of working hours of full-time employees. It may therefore be expected that, this time, firms' and employees' efforts to reduce short-time work, offset negative balances in working hours accounts and increase regular weekly working hours will appreciably delay the positive impact of the cyclical recovery on the labour market. Furthermore, it is mainly temporary work that will benefit initially. This is revealed, not least, by the fact that, according to IAB Job Vacancy Survey, labour demand in the temporary employment sector in the first quarter of 2010 was already well up on the same period of 2009, even though the total number of vacancies actually fell slightly on the year. Even so, the brighter overall economic setting offers the prospect of markedly decreased adjustment pressure even in those sectors hit hard by the economic crisis. Seen in that light, the Federal Government's plans to prolong the extended possibilities of short-time work now until March 2012 harbours the risk that this instrument, designed to bridge temporary losses in production, will in future be used by a greater number of firms which suffer more from structural problems.

Wages and prices

The 2010 pay round was shaped mainly by the currently still depressed level of capacity utilisation, although some settlements also reflect the expectation that the economic recovery will continue. The dominant objective in negotiations in the manufacturing sectors was to safeguard employment. As a result, some of the settlements include extended options for a temporary reduction of weekly working hours. Employee representatives in the metal and chemicals industries entered into pay negotiations without any specific wage demands this time, and wage discussions were concluded comparatively quickly and without fuss. In both of these sectors, there were no increases in scheduled rates of pay for the current year. Instead, one-off payments were agreed, some of which can be staggered according to firms' performance and profitability. While the very short duration of the most recent settlement for the chemicals industry avoids making any commitment for the coming year, rates of negotiated pay in the metal industry have been increased quite considerably, although account has been taken of the continued heightened uncertainty in the business outlook by incorporating into the settlements elements of flexibility for special operational situations. In contrast to the settlements in the private sector, the new pay settlement for central and local government employees provides for scheduled rates of pay rising somewhat more sharply this year than in 2011.

*2010 pay
round with very
moderate
settlements*

The pattern of the wage settlements is reflected in the Bundesbank's statistics on

Moderate wage increase in 2010 Q1 ...

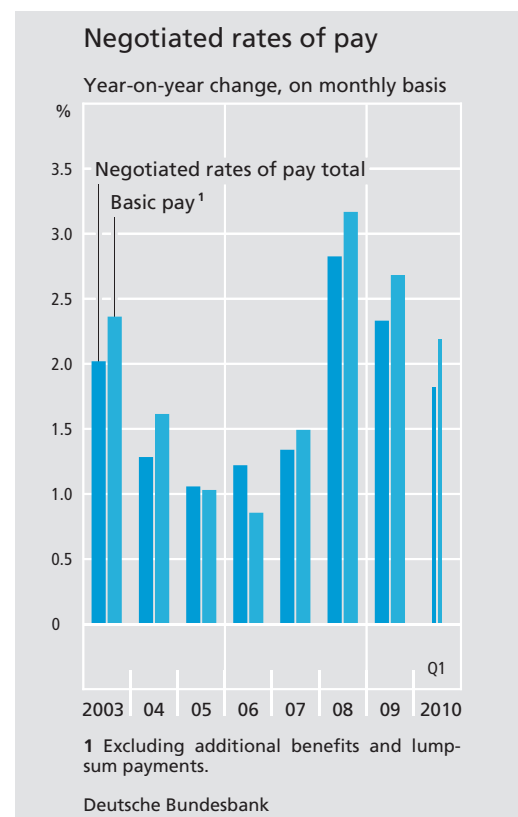
negotiated pay rates inasmuch as, in the reporting quarter, there was a further decline on the year in the monthly rates of basic pay (+2.2%, compared with +2.6% in the final quarter of 2009). This is also shown by the figures of the Federal Statistical Office. However, the year-on-year increase in overall negotiated wages in the first quarter of 2010, at 1.8%, was moderate, as in the previous quarter. Actual earnings (on a monthly basis) went up 1.3% on the year in the reporting period after declining slightly on the whole in 2009. Wage drift fell from -1.6 percentage points in the fourth quarter of 2009 to -0.5 percentage point in the first quarter of 2010.

Growing expansion of sector-specific minimum wages

Minimum wages in the office cleaning and roofing industries were declared generally binding in the period under review. Industry-wide minimum wage levels are likewise planned in the security industry and the care sector. Negotiations on minimum wages have been initiated in other sectors, possibly out of fear of increasing low-wage competition from May 2011 onwards when the last restrictions on the free movement of workers from other EU countries will be abolished in Germany.

Price trends generally pointing back up

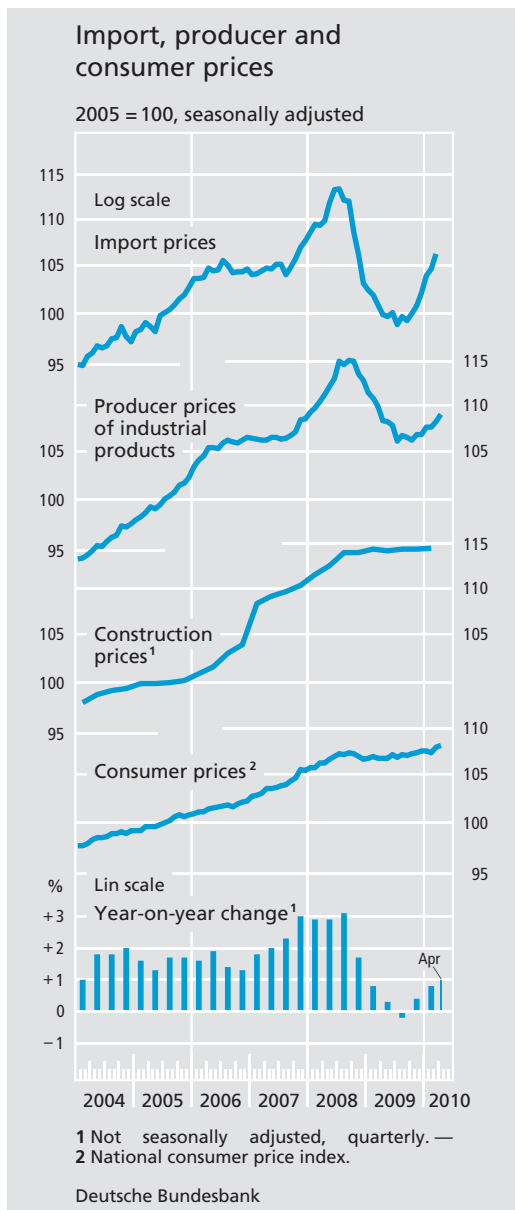
In the first quarter of 2010, prices tended to point back up at all production and distribution stages. The disinflation process observable since the third quarter of 2008 stemming from commodities and ranging through intermediate goods to final products has therefore come to an end and is leading into a similarly gradual countermovement. This development has recently been reinforced by the depreciation of the euro. Overall, import prices were



noticeably up on the quarter in seasonally adjusted terms at 3.9%, and export prices rose by 1.3%. Domestic industrial producer prices were also up sharply at 1.1% with a further 0.7% rise in April. This means that prices are now showing an increase on the year again, although they are still well below the peak levels in the third quarter of 2008. There was a deterioration in the terms of trade owing to the disproportionate rise in import prices. At the consumer level, the sharp increase in crude oil prices and the (principally weather-related) higher cost of food more than offset the slight decline in other goods and services.

At the upstream stages of production, energy prices, in particular, rose sharply. The subindex for exports went up by no less than 12.4% on the quarter in seasonally adjusted

Rising prices at all stages of the economy



terms. In domestic sales, where price fluctuations are usually more moderate owing to the lower percentage of crude oil, the figure was 2.3%. There was also a rise in the prices of intermediate goods. In this case, too, industrial producer prices followed the import sector with a slight time lag and smaller fluctuations (seasonally adjusted +1.2%, compared with +4.5%). In the first quarter, the reversal in the general price trend also led to

the first increase for some while in the prices for final products. It was, above all, the cost of imported consumer goods that went up quite markedly. Even the import prices of capital goods showed a slight increase. Domestic sales present a similar picture. Construction prices were virtually unchanged on the quarter and were only 0.1% up on the year. According to the index of the Association of German Pfandbriefbanks (vdp-Index), the sales prices of residential property fell somewhat in the first quarter of 2010 with a 1½% decline on the year.

Consumer prices were 0.3% up on the quarter in seasonally adjusted terms, which was much the same rate of increase as in the two preceding quarters. As in the final quarter of 2009, this was due in large part to higher energy prices. In addition, food prices went up owing to the weather. The other main components – apart from rents – were down slightly. The increased cost of energy was due chiefly to higher international crude oil prices, which rose at a faster pace owing to the depreciation of the euro, with the prices of heating oil and fuel generally quickly following suit. Added to this was a marked expansion of margins in March. In the case of gas, the delayed adjustment of prices to the fall in crude oil prices in 2008 came to an end. The very cold winter weather impacted, above all, on food prices, especially vegetables. Overall, food was still cheaper than one year earlier, however. Consumers had to pay somewhat less for other durables and semi durables – principally clothing and shoes. The subindex for services also showed a slight decline, mainly because of lower prices in the financial

Consumer prices affected by energy and food

and health sectors as well as cheaper package holidays. The cut in the rate of VAT for accommodation services from 19% to 7% as of 1 January 2010 was not passed on to consumers, however. Housing rents continued their moderate upward trend with an unchanged 1% year-on-year increase. The national consumer price index (CPI) rose 0.7% on the year in the first quarter of 2010, compared with 0.4% in the final quarter of 2009; the HICP inflation rates were 0.8% and 0.4% respectively. The early date of Easter is likely to have been significant in this context.

Further rise in prices in April mainly due to energy

In April, the cost of living increased further by a seasonally adjusted 0.2%, compared with an increase of 0.6% in May. Annual CPI inflation nevertheless fell by 0.1 percentage point to 1.0%. (The HICP figure was likewise 1.0%, compared with 1.2%). It was mainly energy prices that continued to rise. Seasonally adjusted food items were affected by the very cold winter weather. The slight decline in the annual rate was due, above all, to the countermovement to the effect of Easter. Over the short to medium term, prices will be shaped chiefly by the ups and downs on the international forex and commodities markets, whereas upward price pressure stemming from domestic activity is likely to be remain limited for the time being.

Orders received and outlook

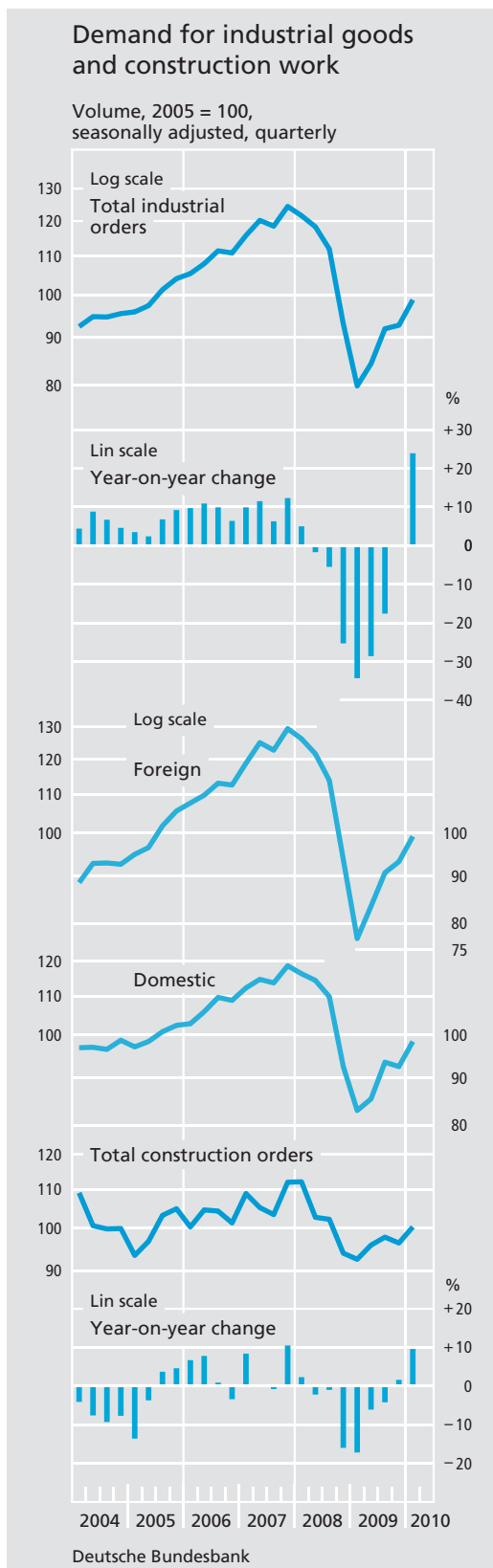
Cyclical upturn in Q2

The cyclical upturn will gain obvious momentum in the second quarter of 2010, not least owing to the elimination of the temporary negative factors in the first few months of

the year. Economic output is likely to grow strongly. Given the quite favourable orders situation, weather-related output losses are likely to be made up quickly. Furthermore, the leading indicators suggest that industrial output will pick up markedly in the second quarter, especially as demand has been well ahead of production during the past few months. Finally, the pattern of private consumption will no longer be impaired as much as it was in the preceding quarters by the fact that new car registrations are returning to normal after the discontinuation of the environmental premium.

Exports remain the main driving force behind the upturn, with firms expecting even stronger stimuli from export business. This applies especially if they have a presence in non-European sales markets, which are currently displaying a rapid pace of economic growth. Moreover, German exporters are benefiting in those countries from the recent shifts in international exchange rates. According to the surveys by the Ifo institute, export expectations in manufacturing have recently advanced into territory where this indicator had last stood during the big export boom of the last upswing. This is also likely to have supported the continued improvement in the business climate in trade and industry as a whole. What should not be overlooked when interpreting the survey indicators, however, is that they generally represent the balance of trend assessments in a condensed form. High index levels therefore mainly reflect the fact that there is a widespread improvement in sentiment in the economy. The surveys do

Favourable export outlook



not take account of either the starting level of the boost or of its strength.

New orders were more buoyant again at the start of 2010. In the first quarter, orders rose by 6.5% in seasonally adjusted terms following a moderate increase of 0.9% in the preceding three-month period. The surge in orders was broadly based across regions. In addition, large orders were received both domestically and from export customers. There was recently a surge in demand from other euro-area countries, which – like domestic demand – had been comparatively weak in the fourth quarter of last year. Orders from non-euro-area countries continued their sharp upward trend. In the reporting period, there was an increase in demand for both intermediate and capital goods. There were, however, somewhat fewer orders of consumer goods in the first quarter of 2010 than in the preceding quarter. Despite this sharp increase, the recovery in the intake of industrial orders has made less progress than is shown by the sentiment indicators. One-half of the overall decline in demand suffered during the downturn has been recovered to date.

Industrial orders more buoyant again

Construction output is likely to be characterised by further catch-up effects in the spring months after already recovering strongly in March. A large number of projects, especially in the building industry, were approved towards the end of last year; the start of construction was delayed, however, by the long period of frost this winter. The orders situation in public sector construction continues to benefit from the boost provided by the economic stimulus packages despite financial

Catch-up effects in construction

constraints at local government level. Demand for residential buildings was lower at the start of the year than in the final quarter of 2009, however.

*Households'
sentiment
undimmed*

Industry's optimism regarding the future outlook for the economy is also shaping households' sentiment. Given the stable labour market situation, the risk of redundancy does not appear to be a paramount concern for many employees. The losses in pay associated with short-time work and the reduction of regular weekly working hours, like the rather moderate prospects for wages and salaries,

are exerting no more than a subdued impact on households' income expectations. This probably also reflects the perceptible increase in their scope for expenditure *per se* owing to the further fiscal policy relief afforded at the beginning of the year. The propensity to purchase is therefore still at a comparatively high level. This represents a good foundation for the consumer climate to go on reinforcing the export-led cyclical upturn on the domestic side. The risk of negative confidence effects stemming from the recent dramatically escalating tensions in the euro area might prove to be a limiting factor in this regard, however.