July 9, 2024

The industrial evolution continues

Authors
Robin Winkler
+49(0)69-91062178
robin.winkler@db.com

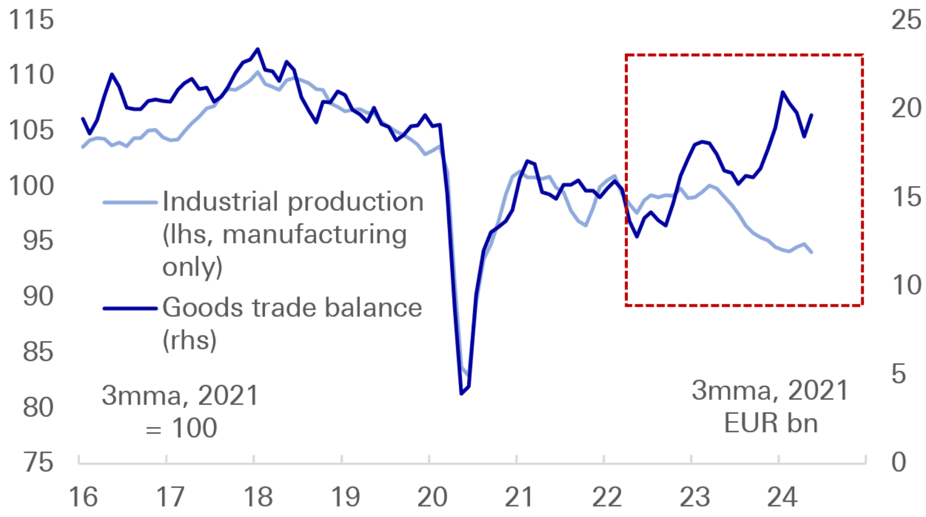
Eric Heymann
+49(69)910-31730
eric.heymann@db.com

www.dbresearch.com

Deutsche Bank Research Management
Robin Winkler

The energy shock of 2022 posed an existential challenge to Germany's export-based and manufacturing-led growth model. Pessimists worried that without cheap energy, Germany would see a structural decline in both its industrial base and its trade surpluses. Optimists argued that the model would adapt to higher energy prices. So where do we stand? As the chart below shows, it is a bit of both.

The industrial base withers, the trade surplus survives



Sources: Deutsche Bank, Haver Analytics

On the one hand, de-industrialization is underway insofar as production volumes in German manufacturing keep declining. The disappointing IP data for May reported on Friday only confirmed this trend. And while most of the decline in 2022 and 2023 came from energy-intensive sectors, so far this year it has come from the less energy-intensive sectors such as mechanical and electrical engineering, where high interest rates have also been a drag. The decline is thus broad-based. As we have argued for a while, we believe this decline in manufacturing production is structural and unlikely to be reversed anytime soon.

On the other hand, Germany's trade surplus in goods is now back to 2019 levels in real terms, as confirmed by the data for May reported today. To be sure, much of the strong recovery in the last year has been about import compression, especially in energy import volumes. Goods export volumes meanwhile have stagnated since 2019, with German companies losing market shares and competitiveness in key export markets. Yet even in the absence of an export boom, it is notable that the trade surplus has remained stable in real terms while the manufacturing base has shrunk.

The robust trade surplus ties in with the stable gross value-added from manufacturing in recent years, as we have noted in previous notes. Thus, while de-industrialization is taking place in volume (and increasingly employment) terms, the industrial contribution to national income has held up. As we have written elsewhere, the energy shock of 2022 triggered a shift in Germany's industrial value chain from volume-based and energy-intensive activities toward high-tech and high-margin activities. We believe it is better seen as an industrial evolution than a de-industrialization.