NEW ZEALAND FOREIGN AFFAIRS & TRADE
Manatū Aorere

German economic update: supply challenges delay recovery

Market Report

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Prepared by the New Zealand Embassy in Berlin

Summary

- The German economy is recovering from lockdown but more slowly than anticipated. While demand remains strong, supply bottlenecks, logistical issues and rising energy prices are growing concerns, and are delaying a full recovery. Consumer confidence and domestic demand nevertheless continue to rise and are driving the recovery with some volatility depending on perceived COVID-19 risks. German demand and prices for New Zealand products look set to increase. However getting our products to Germany may remain a challenge for some time.

Report

Since our last report in July 2021, the German economy has been recovering but more slowly than anticipated. The second quarter had been expected to mark the beginning of a strong recovery, but with a quarterly growth rate of 1.9% (after 1.9% negative growth in the first quarter and 2-3% estimated growth) it was disappointing. The third quarter saw 1.8% quarterly growth (2.5% year-on-year), a respectable but, again, not stellar, improvement. It is no longer the COVID-19 pandemic and its impact on demand that is causing headaches; but rather a lack of supply, logistical issues, and rising prices, energy in particular. In a worst case scenario, the final quarter of this year could potentially feature stagflation i.e. low or zero growth combined with high inflation.

Lower growth and business confidence than anticipated

Consequently, economic forecasts for this year have been lowered from 3-4% GDP growth to around 2.5% this year, which suggests that Germany's GDP will not return to pre-crisis levels until sometime next year. With demand remaining strong, economic forecasts for 2022 as a whole remain positive with predicted growth of up to 5%.

Business confidence peaked in June but has since decreased to its lowest level since April (when most COVID-19 restrictions were still in place); however the picture is uneven. The manufacturing and trade sectors are experiencing supply shortages and, as a result, falling capacity utilisation. Sentiment in the service sector remains volatile, while confidence in the construction sector is improving. The Purchasing Managers Index® has also slumped to its lowest level in eight months.

The transition to a new federal government, in train since the September election, adds to the uncertainty, as the caretaker government is unlikely to take any bold decisions in response to the current economic challenges. On the other hand, pre-election business fears of a `leftist´ government favouring higher taxation have not eventuated; instead a fairly centrist coalition is expected to emerge.

Lack of inputs and logistical challenges weigh on manufacturing

Manufacturers are reporting full order books but decreasing production, due to a lack of inputs. The situation is particularly severe for the automotive industry, which faces potentially producing only half as many cars as many cars as it did back in 2016, a record year. Carmakers lack semiconductors in particular, but their slowing production is also negatively affecting other suppliers. These log-jams are expected to have considerable impact on the wider supply chain, and sales and exports further down the line.

The shortage of inputs is compounded by logistical challenges. Recent issues such as temporary port closures in China, and the Suez Canal incident, have added to disruptions in the global supply chain. The Port of Hamburg, for example, is now dealing with more arrivals than usual, leading to congestion and further challenges in the hinterland. A growing shortage of truck drivers is another concern. Economic observers suggest the `low point´ in the supply crisis may soon be behind us but to expect disruptions to continue well into the new year.

Consumer confidence and domestic demand are still strong

Consumer confidence and domestic demand continue to increase and are now driving the recovery, with some volatility depending on the perceived remaining COVID-19 risks. Private consumption showed reasonably strong growth in the second and third quarters, compensating for the spending restraint of the preceding months, and driven by a shift in spending from goods to re-opened services (such as travel and hospitality). Consumer confidence is at its highest level since April last year. Consumers are keen to spend, with increasing inflation (currently >4%) working as an incentive – for now – to bring purchases forward.

After months featuring a low infection rate and a strong rollout of vaccines, COVID-19 is now spreading again (potentially marking a fourth wave), facilitated by a stagnating vaccination rate. Having a good two thirds of the entire population now fully vaccinated should deter another full lockdown, although restricted access to services may return for the unvaccinated.

Outlook for New Zealand exports

This year inverted the pattern of New Zealand's exports to Germany. Whereas exports to Germany tend to peak in the first quarter of the year before declining again, this year exports bottomed out in the March quarter before increasing during the June quarter. This is largely attributed to the collapse of New Zealand's tourism services exports (visitors from Germany to New Zealand), whereas goods exports have held up overall during the pandemic. With the end of the latest lockdown in Germany, high saving rates and low unemployment, going forward German demand for New Zealand products may continue to increase. However getting our products to Germany could remain a challenge for some time.

New Zealand exporters may take some comfort in the steady increase in demand and prices. Import prices are currently on average 18% higher than a year ago, propped up by energy prices, marking the sharpest increase in 40 years. Energy aside, import prices have still increased by 10% year-on-year, as commodities and food products have become more expensive. Furthermore, even at higher prices, German retailers are finding it hard to fill orders, with three in four reporting problems in this regard. Particularly affected are bicycle shops, Do-it-Yourself centres, furniture stores and consumer electronics retailers.

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