

# Germany

## PMI shows that the recovery is still on track, despite bumpy GDP data

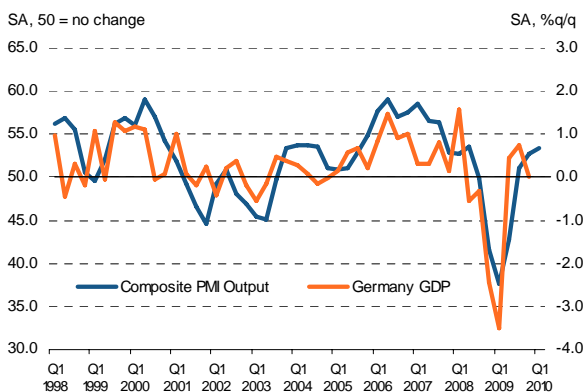
- **GDP data plot volatile growth trend.**
- **PMI data suggest smoother underlying trend of sustained growth.**
- **Weak consumer demand continues to subdue the recovery.**

### PMI puts the GDP setback into perspective

At first glance, today's flat Q4 GDP number for Germany places a question mark over the recovery of the Eurozone's largest economy. While it is true that there has been some payback in recent months, following a remarkable surge in spring/summer 2009, quarterly official data are notoriously volatile and can often paint a confusing picture if looked at in isolation.

A recent example of uncertainty created by quarterly GDP data occurred in Q1 2008, when official figures showed the fastest growth for 16 years, but just three months later we saw the start of the longest and deepest recession in living memory. On the other hand, Markit's Composite PMI, a survey-based measure of combined manufacturing, construction and services output, tends to provide a far smoother gauge of momentum in the German economy. This low noise-to-signal ratio property of the PMI means, for instance, that in early 2008 the PMI was providing a clear advance indication of the substantial slowing in the rate of economic growth that was about to occur.

**Chart 1. German GDP vs. Markit Composite PMI**



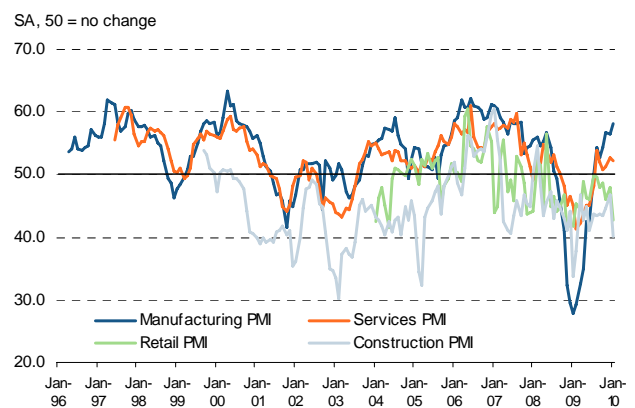
The PMI is also displaying a less volatile trend than GDP data during the recovery. As can be seen in Chart 1, the PMI suggests a more stable upward trend since the worst phase of the recession in Q1 2009. This momentum has been carried forward into the start of 2010, although growth remains weaker than that seen over the 2006-2007 period of expansion.

With the preliminary GDP numbers lacking a detailed breakdown across the economy, we can use the PMIs to estimate the relative performances of different areas of the private sector and can see a mixed picture of momentum at the sector level.

### Rebound led by manufacturing

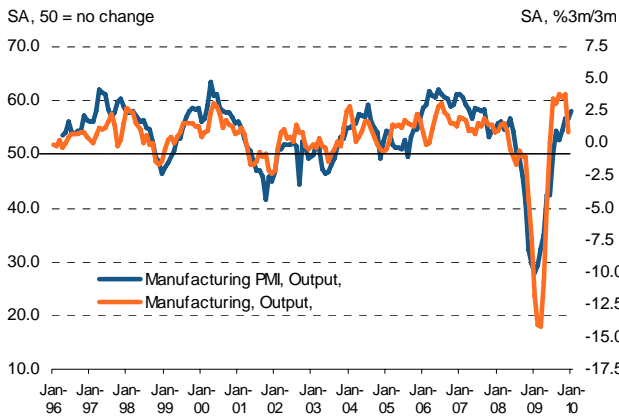
Latest PMI data point to a strong rebound in manufacturing contrasting with moribund services and retail sectors. Additionally, the struggling construction sector took a sharp dip in January, as heavy snowfall caused widespread disruption.

**Chart 2. German PMI data output/sales**



After being the hardest-hit area during the recession, manufacturing has provided the main thrust to growth during the recovery phase. Once again, the official data indicate more volatile short-term movements than the PMI figures, with the PMI broadly smoothing out the sharpest movements of the cycle. The following chart highlights an element of 'payback' in the monthly official series, after it surged ahead of the PMI data in Q3 2009.

**Chart 3. German manufacturing output**

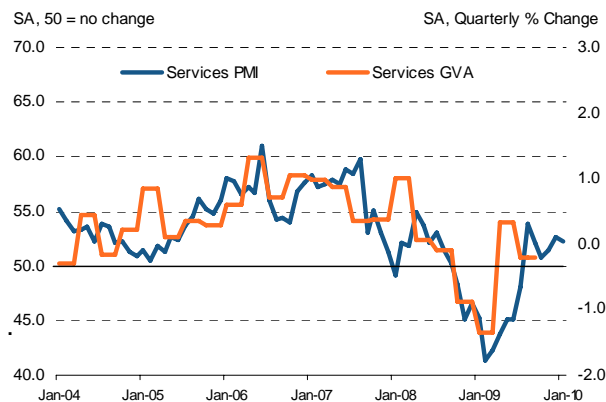


**Private consumption holds back recovery**

While PMI data indicate that underlying momentum in the manufacturing sector remains favourable, the weakness in the services and retail PMIs suggests that final domestic demand is the Achilles heel at this stage in the recovery.

This has clearly affected consumed-facing areas of the service economy, and the sector as a whole has registered only a modest rise in activity in recent months.

**Chart 4. German Service sector**

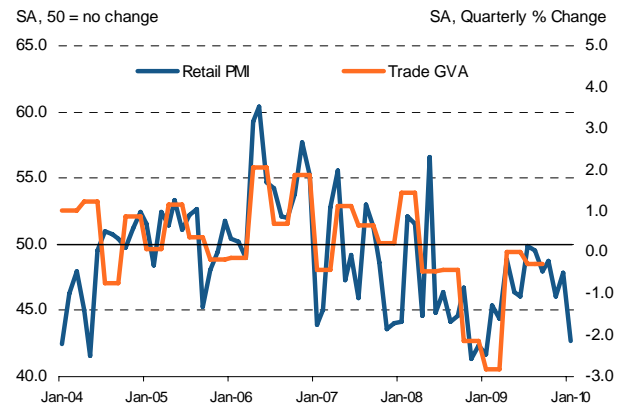


Markit Retail PMI data further highlight that weak household spending has held back the non-manufacturing economy. Retail sales have dipped in recent months following the end of the car scrappage scheme and unusually unfavourable weather conditions.

Consumers are clearly still concerned over the labour market and subdued outlook for incomes, and labour hoarding by companies due to state incentives mean households may have yet to really feel the end of the recession and continue to adjust spending accordingly. This bodes ill for both trade and private consumption,

which had negative contributions to GDP in Q3 2009. The downward trend looks to have continued in Q4, indicating that consumer retrenchment is a lingering cloud over the manufacturing-led recovery in Germany.

**Chart 5. German retail sales**



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