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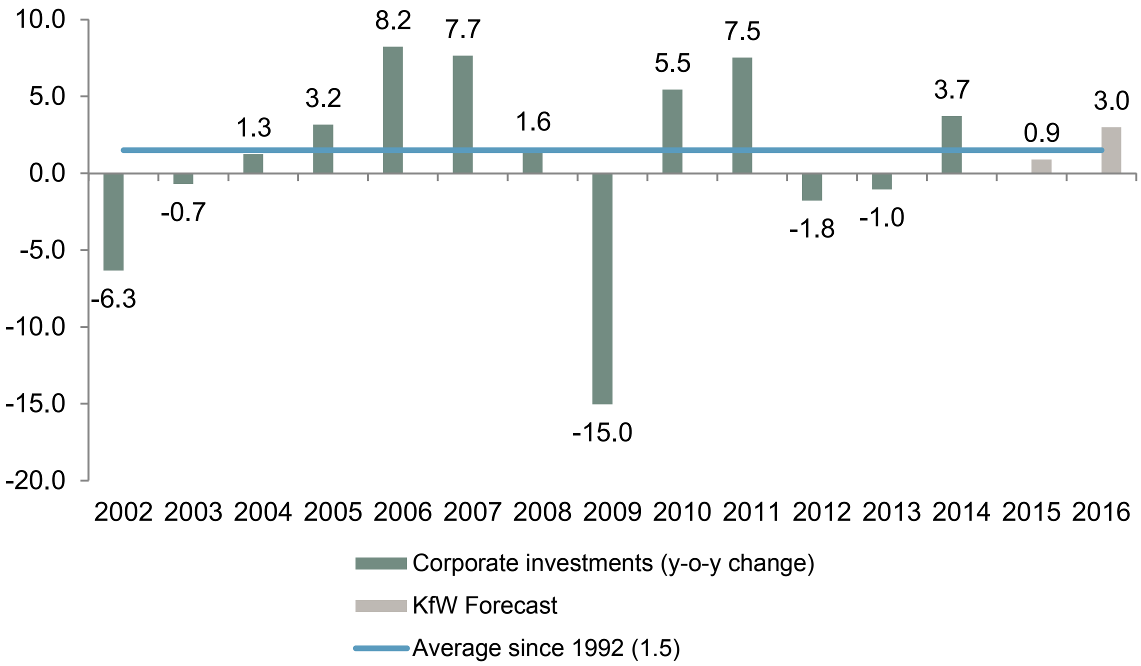
KfW Investment Barometer Germany: May 2015

Corporate investment growing at snail's pace

- ***Overall growth in German corporate investment in 2014 was only achieved thanks to a strong first quarter.***
- ***Given weak levels of investment towards the end of 2014, we expect growth in 2015 to remain at a very modest 0.9 %.***
- ***In both Germany and the euro area, the pace of economic growth is expected to pick up to a certain extent in the coming year. Looking ahead to 2016, we therefore anticipate stronger growth of 3.0 % in corporate investment.***

Corporate investment in Germany, adjusted for price and calendar effects



Source: KfW Economic Research, SNA database: April 2015

Growth in corporate investment rescued in 2014 by strong first quarter

Despite a strong start to the year, by the end of 2014 growth of German corporate investment was in negative territory. Total fourth-quarter investment was down 0.3 % on the preceding quarter – the third consecutive period of declining investment. The overall 2014 figure of 3.7 % year-on-year growth in German corporate investment was only achieved thanks to the strong first quarter.

Available production capacity still not fully utilised

The subdued picture for German corporate investment is mainly a result of demand-side weakness. In 2014, production levels among German companies were just below capacity limits. In fact, average capacity utilisation for the year as a whole stood at 83.9 % compared with the long-term average of around 85 %. We expect this indicator to show a gradual increase over the current year. Our forecast is based on the following considerations:

- While global GDP growth is likely to remain unchanged this year, total output in the industrialised countries is likely to increase at a slightly faster rate than in 2014 on the back of lower oil prices. In the euro area, which makes an important contribution to German GDP, euro weakness should also help to boost the country's balance of trade. At the same time, increased employment will stabilise household demand and contribute to a gradual consolidation of economic growth in the euro area as the year progresses.
- Against this background, the German economy is also well placed to deliver further solid growth. The main factors stimulating domestic demand will be low oil prices and continued improvements in employment figures.
- The ECB's decision to embark on a programme of bond purchases has contributed to further improvement of corporate borrowing conditions. Interest rates are now at historically low levels and credit is readily available.

In this context, German GDP should grow at a somewhat faster rate than potential output in 2015. The resulting increase in capacity utilisation will produce a modest increase in corporate investment. Given weak levels of investment towards the end of 2014, however, we expect year-on-year growth in 2015 to remain at a modest 0.9 %. By the following year, the upswing should be a little more firmly entrenched. We therefore anticipate a slightly faster rate of real growth in Germany over the course of 2016. In turn, this should generate somewhat faster growth of 3.0 % in corporate investment.

The prevailing note in our forecast of the likely trend for corporate investment is one of caution. As such, the main risks are on the upside. If lower energy prices, euro weakness and very expansive monetary policies succeed in producing a stronger than expected economic recovery in Germany, it is entirely possible that German companies will begin to reach their capacity limits this year and decide to go ahead with investments designed to increase that capacity. On the potential downside, however, any escalation of Greece's ongoing debt crisis, strained relations with Russia and the prospect of capital outflows from emerging market economies following any tightening of monetary policy in the United States could undermine the economic outlook for Germany and the world as a whole. If these downside risks materialise, corporate investment is also likely to be hit.

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About the *KfW Investment Barometer*. The KfW Investment Barometer is a quarterly reporting format relating to the three main components of gross fixed capital formation: corporate investment, public investment and private residential construction. This breakdown is not part of the standard programme for the national accounts prepared by the German Federal Statistical Office, but rather KfW uses a separate classification system that is consistent with the national accounts. Corporate investment comprises all investment carried out by the private sector in machinery, commercial construction and other assets (including intellectual property such as research and development as well as software). All investment in the public sector is summarised in its own grouping, as is private residential construction. The KfW Investment Barometer looks in detail at the three components for three of the issues and the fourth issue is reserved for the overall synopsis.