

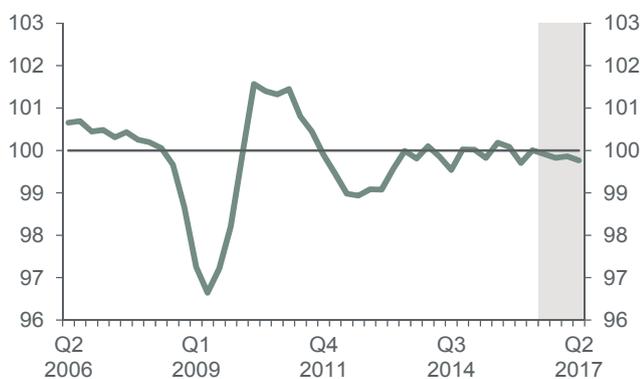
»» Germany's external trade environment remains subdued

2 September 2016

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- External trade is not making any headway
- Obstacles are closer to home
- Private consumption and residential construction generate one-sided import momentum

External trade indicator



Forecast for 3rd quarter 2016 to 2nd quarter 2017.

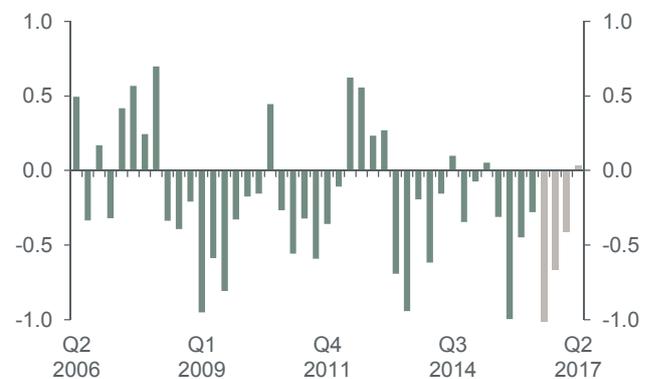
Source: KfW

The indicator of German external trade activity computed by KfW, the KfW External Trade Barometer, reached 100 points in the second quarter of 2016 – exactly the level of its long-term average. It will not be able to consistently maintain this level across the coming four quarters because of the subdued external environment, but will settle down at 99.8 points from the third quarter of 2016, below the average trend.

Indicators for German goods export were still good at the time of the previous quarter forecast, pointing to a continuous improvement during the forecast period. This trend is generally still intact and the indicator for goods exports is expected to improve steadily. Nevertheless, demand from abroad is still being affected by the fallout from the Brexit referendum as well as the coup attempt and its consequences in Turkey. For German exports, Turkey is a moderately sized market in terms of total volume but relatively important for the engineering and automotive industries. The Brexit vote has greater potential to cause negative impacts if the heightened uncertainty spills over to Continental Europe.

However, the bulk of German exports goes to other EU countries. As things stand, both events are therefore

Balance of normalised export and import momentum



expected to have only moderate impacts, but they do add up. Accordingly, export activity will start to pick up from a lower level and the momentum of the recovery will presumably remain below average until the middle of next year.

Import activity is buoyed by continuing robust domestic demand. Next year's economic output is expected to develop at a similar pace as this year, although it will have fewer working days. Businesses are displaying some degree of uncertainty and therefore have less optimistic business expectations as a result of the less favourable external environment, so imports will lose momentum in the forecast period. This sub-indicator will be slightly below its long-term average at the end of the forecast period, at 99.7 points.

In the next quarters, exports will therefore grow more slowly than imports, which will weigh on economic performance. However, the negative influence will weaken during the forecast period. A positive surprise could most likely come from the moderate signs of recovery appearing in the developing and emerging market economies. All in all, however, the German economy will continue to be buoyed by domestic demand. ■

Methodological appendix: Construction of indicators

The external trade indicator is the simple average of the export sub-indicator and the import sub-indicator. The value 100 marks the long-term average. Values above / below 100 represent above-average / below-average growth of imports and exports compared with the previous year.

The indicator as the balance of export and import momentum is the difference between the export sub-indicator and the import sub-indicator. If the value is positive (negative), exports develop more strongly (less strongly) than imports, whereas both factors grow at the same rate when the value is zero.

The indicators and the underlying estimation models are based on quarterly figures. The forecast period comprises four quarters.

Export sub-indicator



Import sub-indicator



Source: KfW

The sub-indicators for imports and exports are obtained from the respective estimated values of an ordinary least squares estimation. All variables used in the estimation are computed as variations on the previous year's quarter and normalised to a mean value of zero and a standard deviation of one based on the period from Q1 1995 to the current margin. The import and export series of the balance of payments statistic are used as dependent variables and deflated with the export and import price index. The explanatory variables used in the export estimation equation are the non-domestic new orders in manufacturing, the Deutsche Bundesbank's indicator of price competitiveness vis-a-vis 56 trading partners and the export-weighted economic trend in the destination countries of German exports on the basis of IMF data and national statistics – where available.

The explanatory variables for imports are domestic use, the domestic new orders in manufacturing, the Baltic Exchange Dry Index as an indicator of international transport costs and a dummy variable. The latter assumes a value of 1 between Q2 2002 and Q1 2006 in order to take into account two structural breaks in the import equation.

Table: Description of variables applied

Description	Forecast	Source of the underlying data
Goods imports and exports based on the balance of payments statistics		Thomson Reuters Datastream: Deutsche Bundesbank
Economic situation of Germany's trading partners weighted with the value of exports	Forecasts based on the IMF's World Economic Outlook and internal economic forecasts; forecast export weights on average for the past four quarters	Thomson Reuters Datastream: IMF, national source.
Domestic use according to national accounts	Autoregressive model	Thomson Reuters Datastream: Federal Statistical Office
Non-domestic new orders in manufacturing	Autoregressive model	Thomson Reuters Datastream: Federal Statistical Office
Domestic new orders in manufacturing	Autoregressive model	Thomson Reuters Datastream: Federal Statistical Office
Indicator of Germany's price competitiveness against 56 trading partners	Autoregressive model	Thomson Reuters Datastream: Deutsche Bundesbank
Baltic Exchange Dry Index	Autoregressive model	Thomson Reuters Datastream: Baltic Exchange