Export boost in spite of political risks

Results of a survey conducted by the Association of German Chambers of Commerce and Industry (DIHK)

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February 2017

Index

Germany at a Glance 04

Economic Situation 07

Business Expectations 13

Export Expectations 23

Investment Intentions 31

Employment Intentions 39

IHK-Economic-Surveys 46

Questionnaire 47

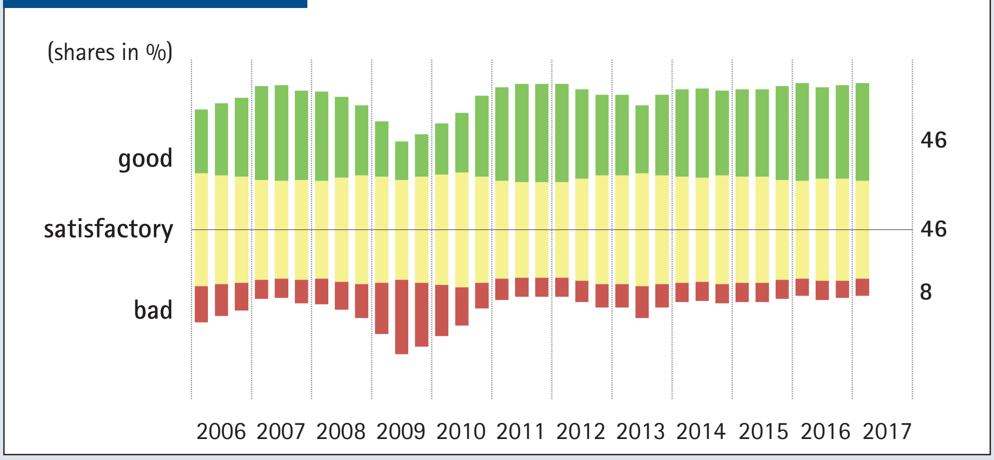
Methodology 48

DIHK-Surveys - time series 49

Germany at a Glance

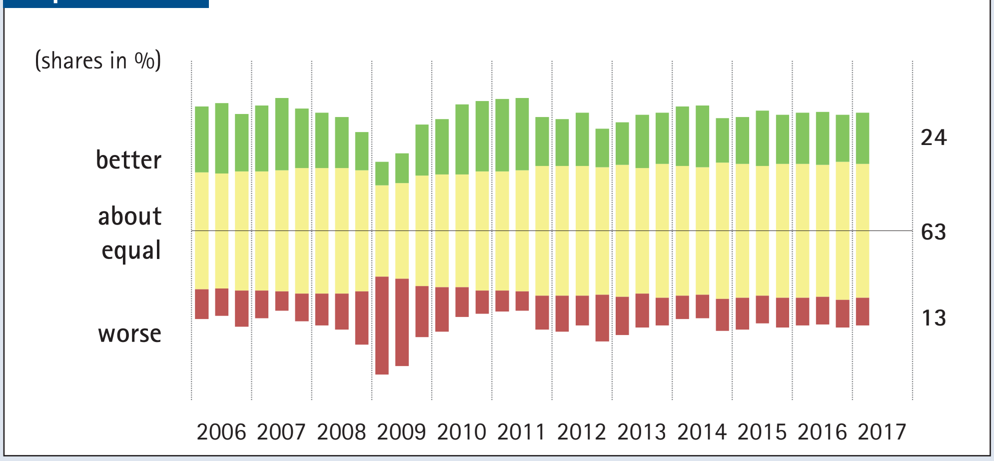
February 2017

Economic Situation



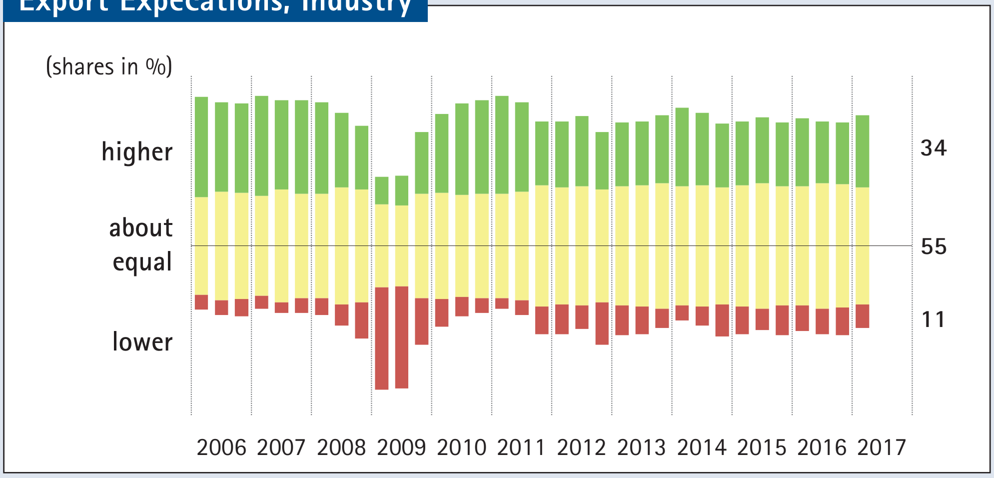
Up to now the economy has been defying the international political upheavals. The business situation of companies is at a record level – better than expected in autumn. The manufacturing industry in particular assesses its situation as being better due to the acceleration in global demand. The trade sector and service providers are also more satisfied. Increasing employment and rising wages are benefiting retail and motor vehicle trade. Housebuilding is in addition being assisted by the low interest rates. The usual seasonal downturn in the construction industry is hardly being felt. Even the assessments of the financial sector have improved again slightly.

Expectations



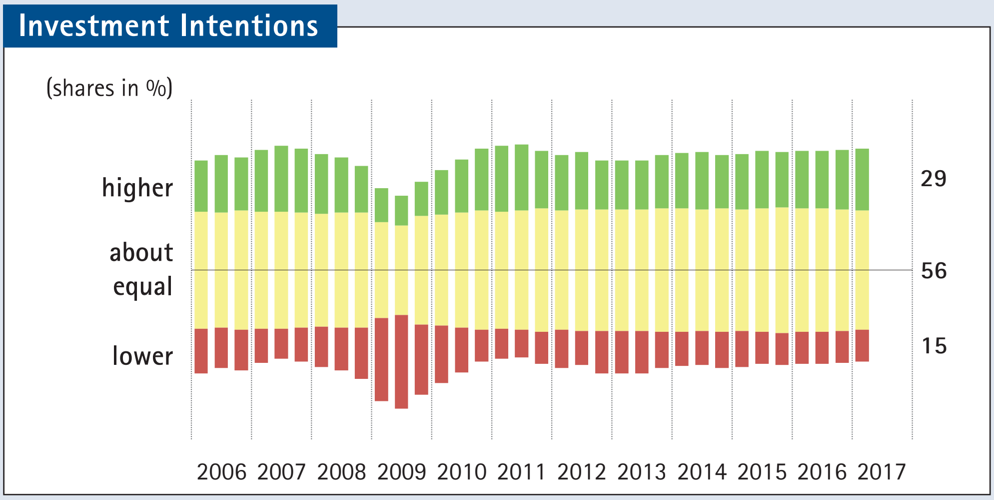
Companies are looking forward to the 2017 business year with confidence. The expectations of businesses are brightening up again. The main drivers are manufacturing and the construction industry. Export companies are counting on world trade overcoming its weak phase for the time being. However, more businesses are again referring to the business risk of „economic policy framework conditions" – particularly in internationally-oriented sectors. The concerns about energy and commodity prices are also growing significantly. These are a cost factor for businesses. In addition, the growth in consumers' purchasing power is not quite as strong as in previous years. For this reason, the optimism in consumer-related industries is hardly growing anymore.

Export Expecations, Industry



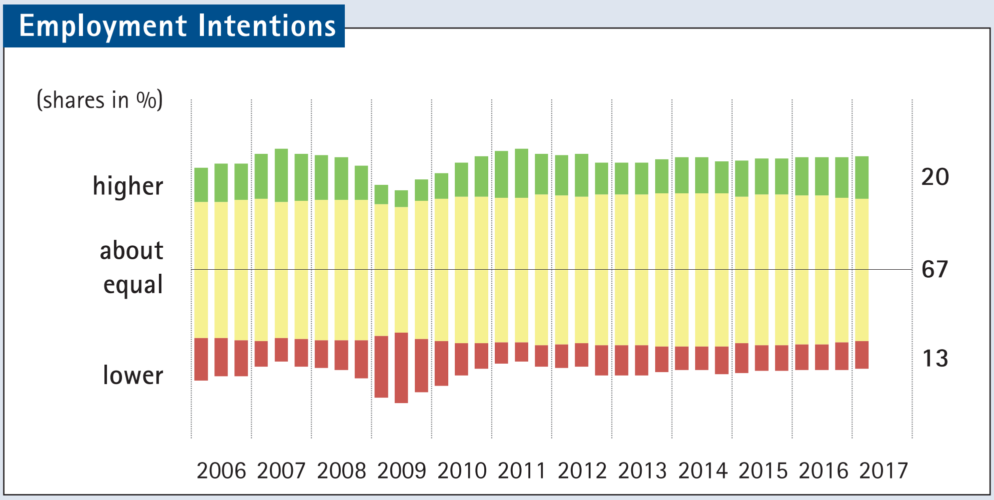
After the weak phase during the last two years, companies are now expecting significantly higher exports. Growth in the American economy is accelerating. The mood in the Eurozone is also becoming brighter. China is continuing to grow, albeit through state support. However, even more companies consider the economic policy conditions to be a threat to their business activities. Reference is made particularly often to protectionist measures of the new US administration and possible counter-reactions. What is more, Brexit increases the economic uncertainty. The rise in the exchange rate risk is an indication of possible turmoil on the foreign currency markets.

Investment Intentions



The investment intentions of companies have again improved slightly. Uplifting factors are the favourable financing environment, the strong consumption and the current improvement in export expectations. Impetus is coming increasingly from the manufacturing industry. In the construction industry, the continuing boom is pushing the investment intentions to record levels. In the service sector, some industries are also reporting new records. The banking sector is intending to invest more, admittedly in many cases with the objective of rationalisation. Overall, the lack of skilled employees is developing into an increasingly limiting factor for investments.

Employment Intentions



The growth in employment enters its twelfth year. The recruitment intentions of companies increase again across all sectors. The boom in house and infrastructure building is providing impetus to the personnel plans of construction companies. The manufacturing industry and service providers are also planning for growth. However, it is becoming increasingly questionable whether companies will be able to implement their recruitment plans. In knowledge-intensive sectors, but also in the construction or hospitality sector, the shortage of skilled workers is becoming worse once again. Signs of a slowdown are coming from some domestic-oriented industries.

Economic Situation

Successful start to the year despite political worries

Up to now the economy has been defying the international political upheavals. The business situation of companies is at a record level – better than expected in autumn. The effects of the "doping" resulting from the low interest rates and low inflation are still being felt. The manufacturing industry in particular assesses its situation as being better at the beginning of 2017 due to the acceleration in global demand. The trade sector and service providers are also more satisfied. Increasing employment and rising wages are benefiting both the retail and motor vehicle trade. Housebuilding is in addition being assisted by the low interest rates. The usual seasonal downturn in the construction industry is therefore hardly being felt. IT service providers evaluate their situation as being better than ever. Even the assessments of the financial sector have improved again slightly.

Situation assessments back to their highest levels

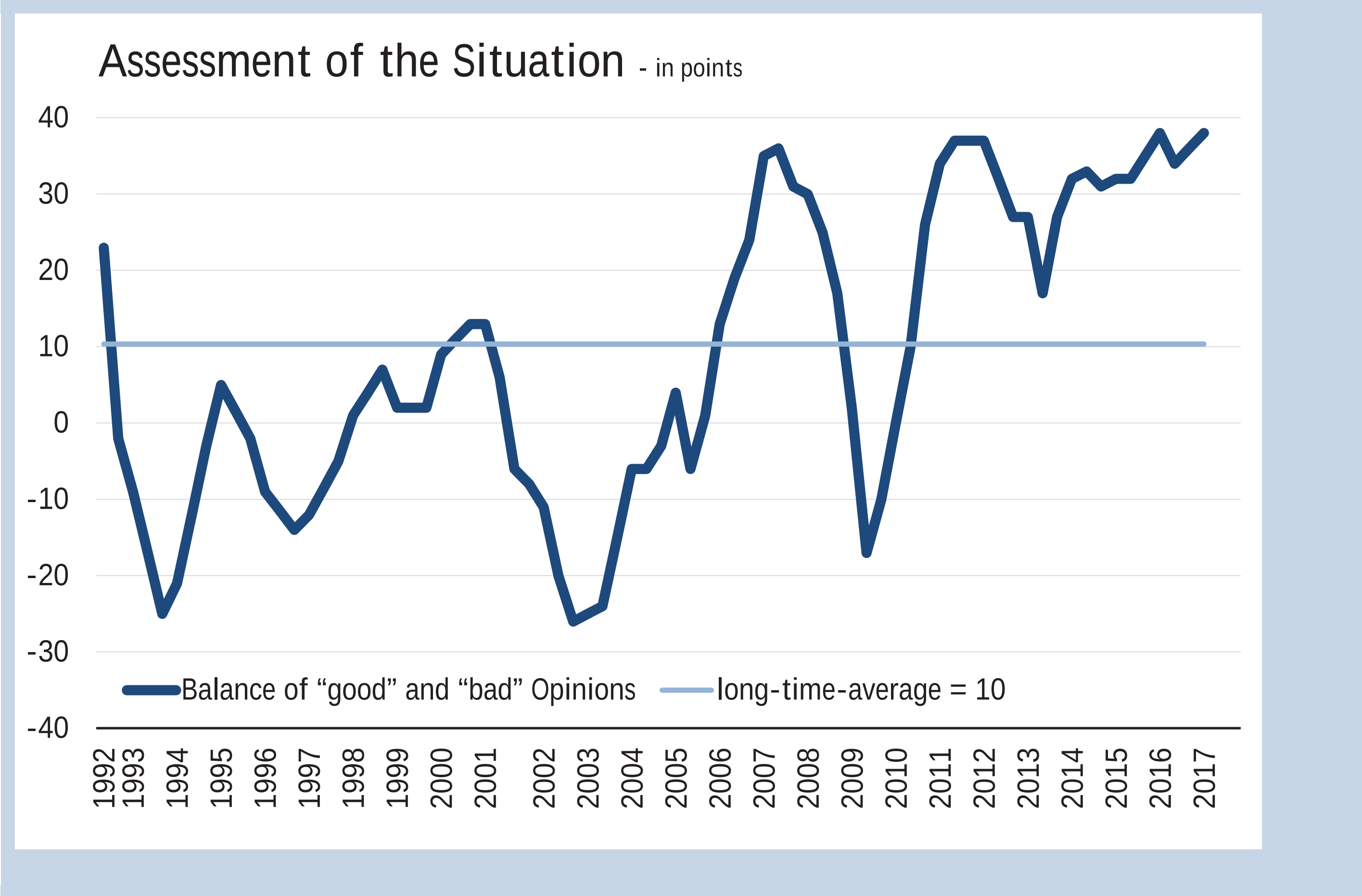
The situation assessments of companies have again reached their record level of the beginning of 2016. The proportion of businesses that describe their business situation as good has risen to 46 percent after 44 percent in the previous survey. Only eight percent describe the business situation as bad. The resulting balance of 38 points is two points higher than in the autumn of 2016. The mood is good on balance in all sectors of the economy – better even than assumed by the companies last autumn. The reason is above all the improvement in world trade which exporters are benefiting from. The unpredictable course taken by the new American government, the upcoming Brexit negotiations as well as international crises and the threat of terror have increased the feeling of uncertainty for companies, but are not yet reflected on balance in a worse assessment of their business situation.

Manufacturing industry on the way back to its old strength

The boom in foreign trade is benefiting manufacturing industry above all. The situation assessment has increased by four to 36 points. It is therefore still somewhat below the average of the economy as a whole. Traditionally, manufacturing assesses its situation slightly better than other sectors, especially during good economic phases. However, this pattern does not currently apply. The reason for this is above all the

Assessment of the Situation (in percent)

	good	satisfactory	bad	balance
February 2015	41	50	9	32
Early Summer 2015	41	50	9	32
Fall 2015	44	47	9	35
February 2016	46	46	8	38
Early Summer 2016	43	48	9	34
Fall 2016	44	48	8	36
February 2017	46	46	8	38



fact that exports and investments have developed to a lesser extent in recent years compared to consumption and construction activities.

More investments around the world...

At the beginning of 2017, capital goods producers see their situation as being significantly more positive than last autumn (40 compared to 34 points). With the rising energy and commodity prices, the growth in global demand is tending to move somewhat further away again at the current margin from consumption towards higher investments – not least for improving energy and material efficiency, a traditional domain of German manufacturers. Mechanical and electrical engineering companies frequently assess their situations as better (increase by seven to 39 points in each case). Manufacturers of all kinds of vehicles (cars, ships, boats, rail vehicles as well as aircraft and spacecraft) are also more satisfied than in the previous survey. The balance in the automotive industry has increased by six to 46 points. The big winners in the capital goods segment include the medical technology industry (increase by eleven to 52 points), where only two percent of companies are currently dissatisfied with their business situation.

... and slightly more consumption

The situation of the consumer goods manufacturers has not improved so much. At 31 points (after the previous level of 30 points), it is however high for this comparatively skeptical main group of the manufacturing industry (long-term average: 15 compared to 21 points in industry as a whole). Stimuli are coming here from the pharmaceutical industry (51 after the previous level of 35 points) and the manufacturers of jewellery, musical instruments, sports equipment and toys (balance: 40 after 32 points previously). In contrast, furniture producers are less satisfied than they were in the autumn of 2016 (decline by four to 37 points).

Housing construction continues to boom

The strong development in housing construction is continuing, supported by favorable interest rates, rising incomes, the housing needs of refugees and the growth in the population, above all in conurbations. The situation assessment of the construction industry has fallen slightly (balance decline from 54 to 52 points), but the winter slowdown is moderate in the seasonal comparison (average: autumn 17 points; beginning of the year 13 points). In comparison to the previous year, which was strong anyway, the balance has increased by a full eleven points. The finishing trade and structural engineering are still in a particularly good situation (unchanged compared to the autumn at 56 compared to 46 points in the previous year and 52 after 53 in the autumn and 42 points in the previous year). Construction-related industries are also benefiting from the increasing interest of many people in their own four walls. The situation assessments of the architectural and engineering firms and the "ceramic, glass and stone processing" industry have risen to record levels (57 after 56 and 39 after the previous level of 32 points respectively). The manufacturers of intermediate goods such as stones and earth, as well as mining (balance: 36 compared to 34 points) is benefiting from the high levels of construction activity. Civil engineering has also been able to improve significantly in the annual comparison (44 after 37 points in the previous year; recently 51 points). The increased spending on infrastructure by central government and the federal states is increasingly being felt by businesses, as well as the investments in broadband expansion.

Traders benefiting from the consumption economy

The situation assessment in the trade sector has improved once again slightly (28 after 26 points previously). The balance is significantly above the long-term average (nine points) and has almost reached its record value (33 points). The good developments in employment, rising wages and higher state transfers are stimulating the domestic economy further. The retail trade is much more satisfied with its situation after the Christmas business (23 compared to 20 points). The vehicle trade and workshops assess their situation as significantly better (31 compared to 27 points). The wholesale trade and trade intermediaries are also benefiting from the stronger developments in foreign trade (33 after 30 points previously).

"Network industry" in a better mood

The stronger industrial activities are also benefiting many associated service providers. Repair and installation companies in particular assess their situation as being significantly better than in the last survey (increase by 13 to 36 points). Further positive impulses are coming from the information industry (46 compared to 43 points), which has reached a new record value. The situation assessment of the company-related service providers has increased slightly and also reached a new record (47 compared to 46 points). For example, the situation balance among research and development institutions has improved significantly (by ten to 34 points). The mood among temporary employment agencies and leasing providers has also improved (by four in each case to 26 and 22 points respectively). Other company-related service providers have had to lower their sights, but still at a high level. These include the cleaning services (32 after the previous level of 41 points), legal and tax consultancies and chartered accountants (57 after the previous level of 60 points). Advertising and market research agencies also assess their business situation as being not quite as good as last time (down to 26 after the previous level of 30 points). The situation assessment among transport and warehouse operators remains stable on balance (at 26 points). Here, the more positive assessment of the transport service providers such as port operators or forwarding agencies (29 after 24 points previously) is compensating for the deterioration in land transport (27 compared to 30 points) where rising fuel prices are spoiling the mood.

Financial sector catching its breath

The financial sector assesses its situation as being better after the low point of last autumn. The situation assessment has increased by six to 33 points. Here the demand situation continues to become less tense, so that the stresses caused by low interest rates and the enormous regulatory requirements are currently being compensated for. Even the banking industry is more satisfied again (balance increase by nine to 28 points). The insurance industry also assesses its situation as better than before (38 after the previous level of 35 points).

Consumer service providers: farewell to the record

The providers of personal services assess their situation as no longer being quite as good as in the previous survey. The balance has fallen from the record level of the previous survey by two to the current level of 37 points. However, the value is still well above the long-term average (18 points). Declines have been recorded in particular by the providers of other personal services such as laundries, hairdressing salons or baths (33 compared to 45 points). In the education sector the balance has also declined (41 compared to 45 points), but even fewer businesses than last time are talking about a bad situation (five after the previous level of ten percent). Among travel agents, as well as health and social services, the situation remains more or less stable (unchanged at 26 and 54 compared to 55 points respectively). In the leisure industry the assessment has even slightly improved (28 compared to 25 points).

Hotel and restaurant industry in a slightly subdued mood

The hotel and restaurant industry is no longer able to benefit so strongly from the consumer economy as in the last survey. The balance has fallen by four to 42 points, albeit starting from the record level of the previous survey. While restaurants and other catering establishments are hardly less satisfied (balance decline by one to 32 points), clouds are appearing on the horizon to dampen the mood of hotels and other accommodation establishments after the record of the autumn (balance decline by five to 47 points). In the field of city tourism, visitor numbers have fallen slightly, starting from the high level of the last survey, as some visitors are concerned about domestic security and terrorism. The unfavorable situation of the Christmas holidays also resulted in slightly fewer overnight visitors. Overall, however, the situation remains good from the perspective of the industry.

Expectations

Broader basis for growth

Companies are looking forward to the 2017 business year with confidence. The expectations of businesses are brightening up again. The main drivers are manufacturing and the construction industry. Export companies are counting on world trade overcoming its weak phase for the time being and expect demand from abroad to grow. However, more businesses are again referring to the business risk of "economic policy framework conditions" – particularly in internationally-oriented sectors such as manufacturing or the transportation industry. The concerns about energy and commodity prices are also growing significantly. These are a cost factor for businesses. In addition, the growth in consumers' purchasing power is not quite as strong as in previous years. For this reason, the optimism in consumer-related industries is hardly growing anymore.

Slight improvement

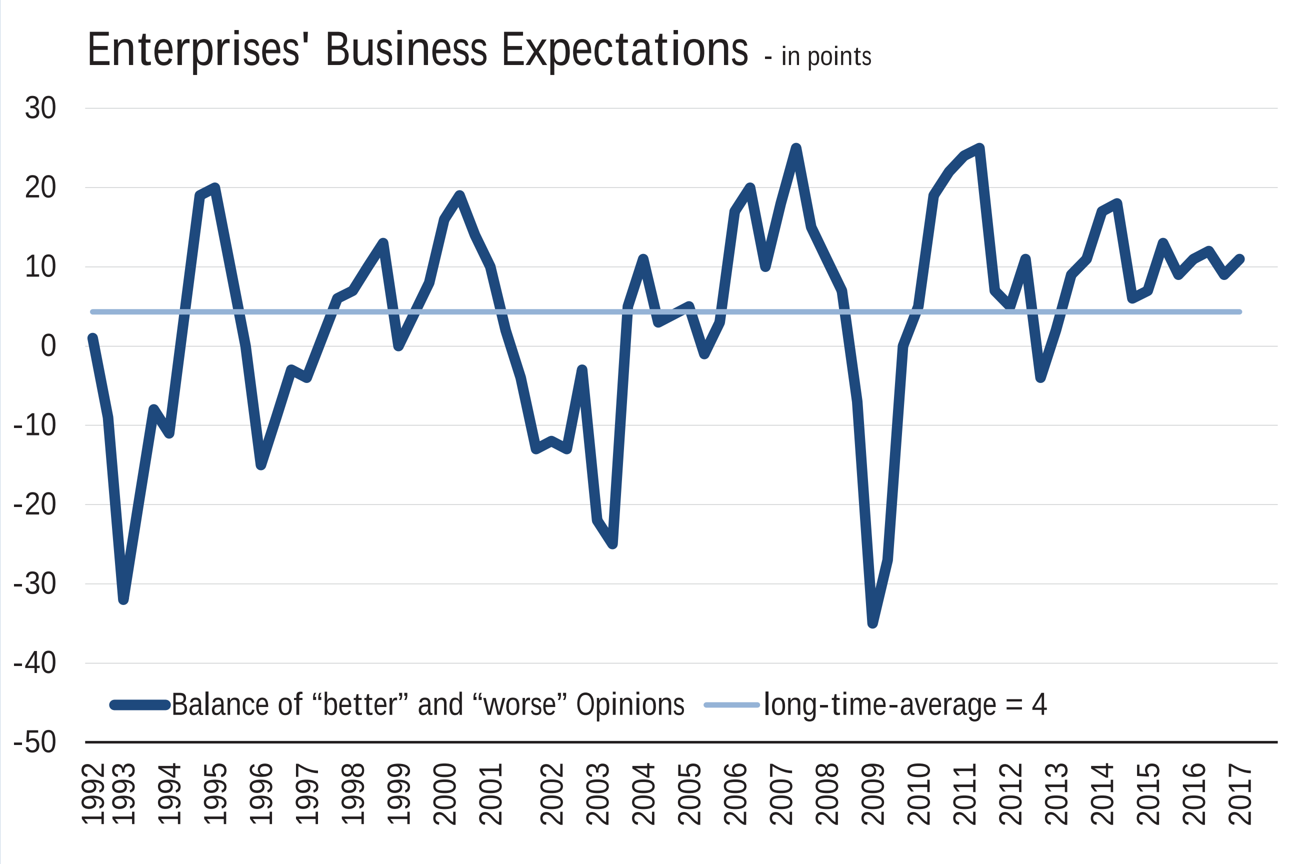
The expectations of businesses have brightened up again after the downturn of the autumn. 24 percent expect better business developments at the beginning of the year for 2017. The percentage of companies who fear a deterioration remains at 13 percent. As a result, the expectation balance as the difference between the two shares has increased by two to eleven points. The share of businesses who are anticipating business developments to remain unchanged has declined by two points, but at 63 percent remains comparatively high (since 2003 an average of just 57 percent).

Upturn:
extended ...

At eleven points, the current balance of business expectations is well above its long-term average (four points) – and that for almost three years, longer than ever before in the DIHK business survey. In previous boom phases, such as 2006/2007 or 2010/2011, the momentum in the economy was indeed significantly higher, but of shorter duration. Since 2014 the economy has been growing by more than 1.5 percent per year, i.e. slightly more strongly than its potential. The latest improvement in expectations suggests that this path of growth will continue. For both foreign and domestic business, fewer businesses than in the autumn of last year expect demand to decline (reduction in references to this risk by five points to 39 percent and three points to 40 percent respectively).

Enterprises' Business Expectations (in percent)

	better	about equal	worse	balance
February 2015	22	63	15	7
Early Summer 2015	26	61	13	13
Fall 2015	23	63	14	9
February 2016	24	63	13	11
Early Summer 2016	25	62	13	12
Fall 2016	22	65	13	9
February 2017	24	63	13	11



... but hardly accelerating

The only slight increase in the expectation balance is at the same time an indication that the economy is only slowly expanding. There are a few factors which are currently preventing any further improvement in momentum: political risks are unsettling investors around the world (increase in the risk of "economic policy framework conditions" from 38 to 43 percent). Furthermore, bottlenecks caused by the shortage of skilled workers are slowing down many companies (at 48 percent this is still the greatest business risk). In addition, rising prices for oil in particular are increasing costs and reducing the room for manoeuvre of consumers (increase in the risk of energy and commodity prices from 25 to 32 percent).

Exports supporting manufacturing industry again ...

Manufacturing industry is expecting business to improve significantly. The reply balance has increased by four to 17 points – the last time it was higher was in 2014. Reduced demand risks are falling in the view of companies (decline by five points in each case to 39 percent for abroad and 44 percent for the domestic market). In the export industry, expectations have improved to a particularly significant extent (balance increase by five points). After the global economy – and world trade in particular – lost a lot of its dynamism last year, there are now increasing signs that this weak phase has been overcome – at least temporarily:

- The United States is benefiting from brisk consumption, as well as short-term stimulus in demand as a result of investments and tax cuts. There are threatening negative effects due to protectionist measures or the rising debt levels, although these are not yet being reflected in foreign sales.

- In China, politicians are currently providing support to the economy again, even if this is only postponing the solving of structural problems to the future.

- The economies of Russia and Brazil are starting to gradually recover again. Other raw material-producing countries are also benefiting from rising prices.

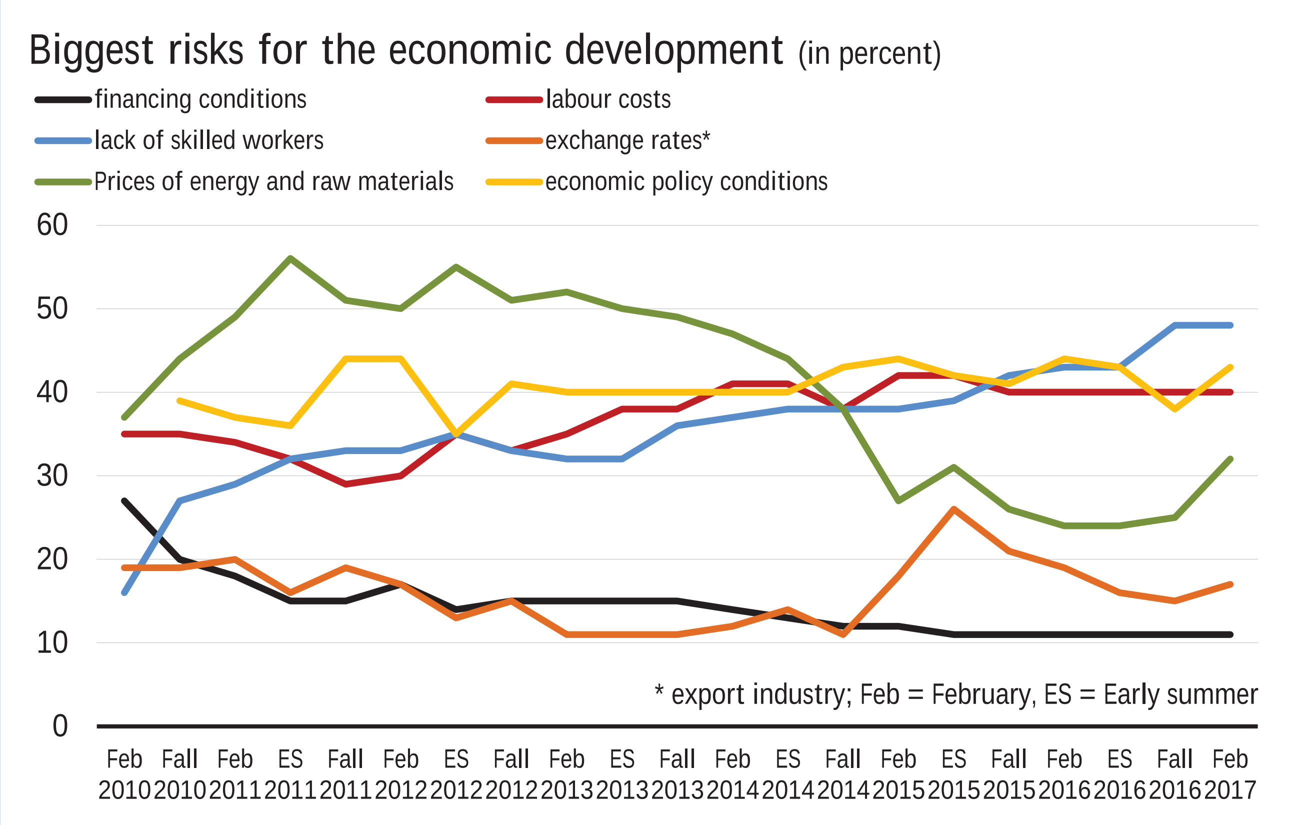
... but risks only postponed

The improved expectations and lower level of concerns about demand for the coming months are associated with a significant increase in the risk of "economic policy framework conditions" (economy as a whole: 43 after the previous level of 38 percent). Companies refer to international political developments as a risk more frequently than in the autumn of 2016. In the view of businesses, these include – for example – the outcome of the election in the United States, Brexit, the consequences of the Russia-Ukraine conflict, the fear of terrorism and the Middle East war, developments in Turkey, China and Italy, as well as increasing protectionism and nationalism. Accordingly, the concerns are increasing more in manufacturing industry, which is particularly dependent on the world economy. Here, 43 percent now see their business developments placed in jeopardy by difficult framework conditions (previous survey: 36 percent). Among the company-related service providers (increase from 33 to 40 percent) and in the transport industry (increase from 35 to 40 percent), concerns about economic policy are also growing - and here too, specifically in view of international developments.

What are the biggest risks for the economic development of your company in the next twelve months?

(in percent; multiple answers possible; *export industry)

	February 2015	Early Summer 2015	Fall 2015	February 2016	Early Summer 2016	Fall 2016	February 2017
domestic demand	48	44	45	45	45	43	40
foreign demand*	45	38	48	44	42	44	39
financing conditions	12	11	11	11	11	11	11
labor costs	42	42	40	40	40	40	40
lack of skilled workers	38	39	42	43	43	48	48
exchange rates*	18	26	21	19	16	15	17
prices of energy and raw materials	27	31	26	24	24	25	32
economic policy conditions	44	42	41	44	43	38	43

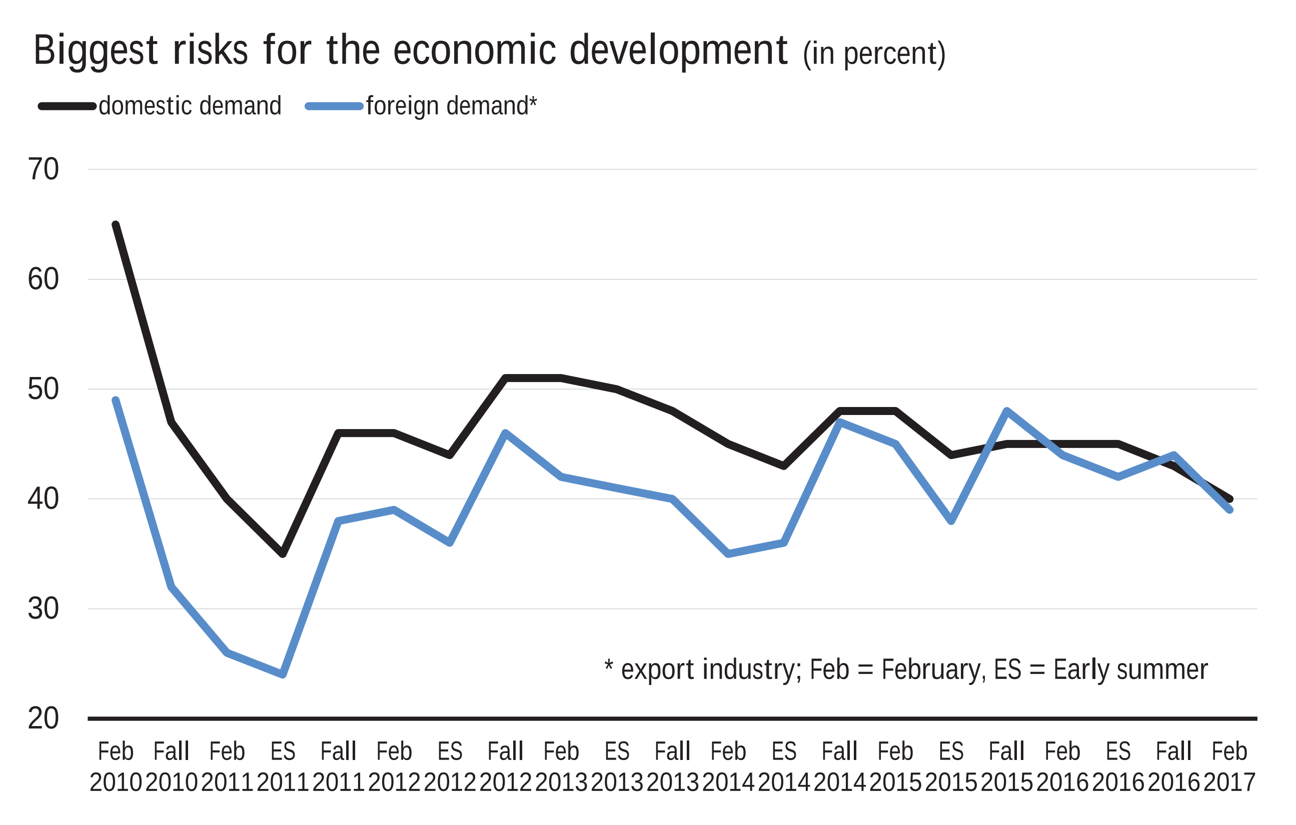


Threat of new exchange rate turmoil

Additionally, there is growing uncertainty about the developments in exchange rates (increase in references to this risk in the export industry from 15 to 17 percent). The unclear course being taken by the new United States government is making forecasts of monetary policy more difficult. This may affect international capital flows and put the central banks under pressure. After a phase of comparatively few fluctuations, the external value of the euro compared to the dollar and other currencies may start to move much faster again as a result.

Raw material costs: price of the global recovery

The booming world economy is also boosting commodity prices. As a result, the costs of oil, industrial and agricultural raw materials are rising. In the manufacturing sector, almost every other company is concerned about the developments in energy and raw material prices (47 percent). This is therefore the greatest business risk once more in this sector – for the first time since 2014. In the transport industry, the risk has climbed by 16 points to 51 percent in the face of rising fuel prices. In construction, the share has risen by nine points to 32 percent. In the trade sector (increase by seven points to 31 percent) and the hospitality industry (by eight points to 40 percent), rising costs for electricity, heating and refrigeration are being felt. Furthermore, due to rising prices the growth in the purchasing power of customers has declined, slowing down business developments in consumer-related industries. Electricity



prices are also being affected by additional charges which the German economy is having to pay for, while foreign competitors are spared. Many businesses explicitly refer to the rising electricity taxes and domestic energy policy as an economic policy risk.

Manufacturers of intermediate goods: hopes for increased demand compensating for cost increases

The manufacturers of intermediate goods are regaining confidence. The expectation balance has risen by six to 18 points and therefore more strongly than in the other main groups of the manufacturing industry. The chemical and glass industries in particular are more optimistic again (balance increase by ten in each case to 25 and 20 points respectively). The metal producers remain cautious for the time being. The balance of five after the previous level of four points is worse than the average of recent years (seven points). Although the concerns about demand have declined significantly in the intermediate goods industry (decrease for domestic and foreign demand by five points each), the rising prices are being felt in full in this energy- and resource-intensive segment. 55 percent of businesses are now worried about the developments in costs – twelve points more than in the autumn of 2016. In the chemicals industry, 63 percent refer to the energy and commodity prices as a risk, while the figure among metal producers is 69 percent and as high as 74 percent in the "mining and quarrying" industry. The economic policy framework conditions are considered to be a risk by more producers of intermediate goods than ever before (42 percent), primarily due to the major concerns about international politics.

Capital goods: optimism for the domestic economy as well

The export-oriented manufacturers of capital goods are benefiting from the recovery of the world economy. The concerns about domestic demand have also decreased noticeably (decline by six points to 44 percent). The expectations have improved on balance by three to 19 points. The car manufacturers in particular are looking forward with confidence to the coming months (balance improvement by eight to 18 points). The risks concerning demand at home and abroad are diminishing. Rising labor costs (43 percent) remain the largest risk. Furthermore, the shortage of skilled workers in the automotive industry has now become greater than ever before (41 percent). Companies working in the field of medical technology are less optimistic than they were in the autumn of 2017, admittedly starting from a high level (balance decline from 28 to 21 points). In the view of this sector, the economic policy framework conditions represent the greatest risk, almost reaching their highest level ever at 47 percent.

Consumption: producers in high spirits...

The expectations of the manufacturers of durable and non-durable goods are undergoing a more stable development. The expectation balance has risen at least slightly by one to 14 points, with the demand risks subsiding. The current improvement is remarkable, since the rising oil prices are reducing the purchasing power of consumers not only here in Germany, but also worldwide. Thanks to rising employment and incomes, the room for manoeuvre of consumers is nevertheless growing in most countries. The breweries are even significantly more optimistic at the beginning of 2017 (balance increase from 24 to 31 points). Furniture manufacturers on the other hand are no longer as confident as in the previous survey (balance decline from 28 to 19 points). In the clothing industry the mood has even deteriorated significantly (balance decrease by 13 to three points). In this sector, the risks of the shortage of skilled workers and labor costs have risen to new record levels (41 and 44 percent respectively).

... motor vehicle trade & service providers as well

The confidence of the other consumer-oriented industries continues at the beginning of 2017. To some extent the expectations have even improved further. In Germany the high wage increases have so far not slowed the growth in employment. As a result, the room for manoeuvre available to consumers is increasing in spite of rising prices. Furthermore, pensions and other transfer services are also rising. For example, the reply balance in the vehicle trade has improved by nine to eleven points, among travel agents by five to eight points and personal service providers by two to 13 points. In the hospitality sector the balance remains unchanged at seven points. Although concerns about domestic demand have fallen here to a minimum of 19 percent (previous survey: 20 percent), at the same time 70 percent of hosts are perceiving the shortage of skilled workers to be a business risk, and 62 percent the development in labor costs. A deterioration in expectations is shown in the retail trade (balance decline by three to two points). As a result the reply balance is only four points above its average, which is one of the lowest in the cross-sector comparison anyway. This also reflects shifts within private consumption from trade to services.

Manufacturing industry pulling up its network

With the improvement in expectations in manufacturing industry, the mood in associated sectors has also brightened up. For example, the expectation balance among the company service providers has climbed from 19 to 20 points. Wholesalers are also a little more optimistic (balance increase from eleven to twelve points). In the transport industry, the optimists slightly outweigh the pessimists again at the start of the year (balance increase by four to two points). The expectations have improved here in all sectors, with aviation being the most confident (balance increase from 16 to 18 points). Companies operating in the field of road freight transport (balance increase from minus two to minus one point) and above all shipping (balance increase from minus eight to minus one point) are at least less skeptical than in the autumn of 2016. At the same time, rising fuel prices are increasingly represent a burden for companies (increase in the risk of energy and commodity prices by 16 points to 51 percent; greatest risk after the shortage of skilled workers).

Upward trend among early cycle companies to be enjoyed with caution

In addition to the transport industry and the manufacturers of intermediate goods, the expectations in the temporary work sector (balance increase by seven to eleven points) and in investment goods leasing (balance increase by 15 to 16 points) are also improving. The temporary employment agencies refer to domestic demand as a risk less often than in any previous survey (19 after the previous level of 23 percent). This clearly indicates growing demand for the flexible use of employees in the economy as a whole. Greater risks in the view of this sector are the shortage of skilled workers (80 percent) and the difficult economic policy framework conditions (new record of 67 percent). It is true that companies from the sectors referred to are often harbingers of economic trends. However, in view of the stable economy in recent years, changes in expectations in these sectors have scarcely been able to live up to their reputation as an indicator of medium-term developments. For this reason, the most recent slight improvement is still no clear sign of sustained acceleration in the economy.

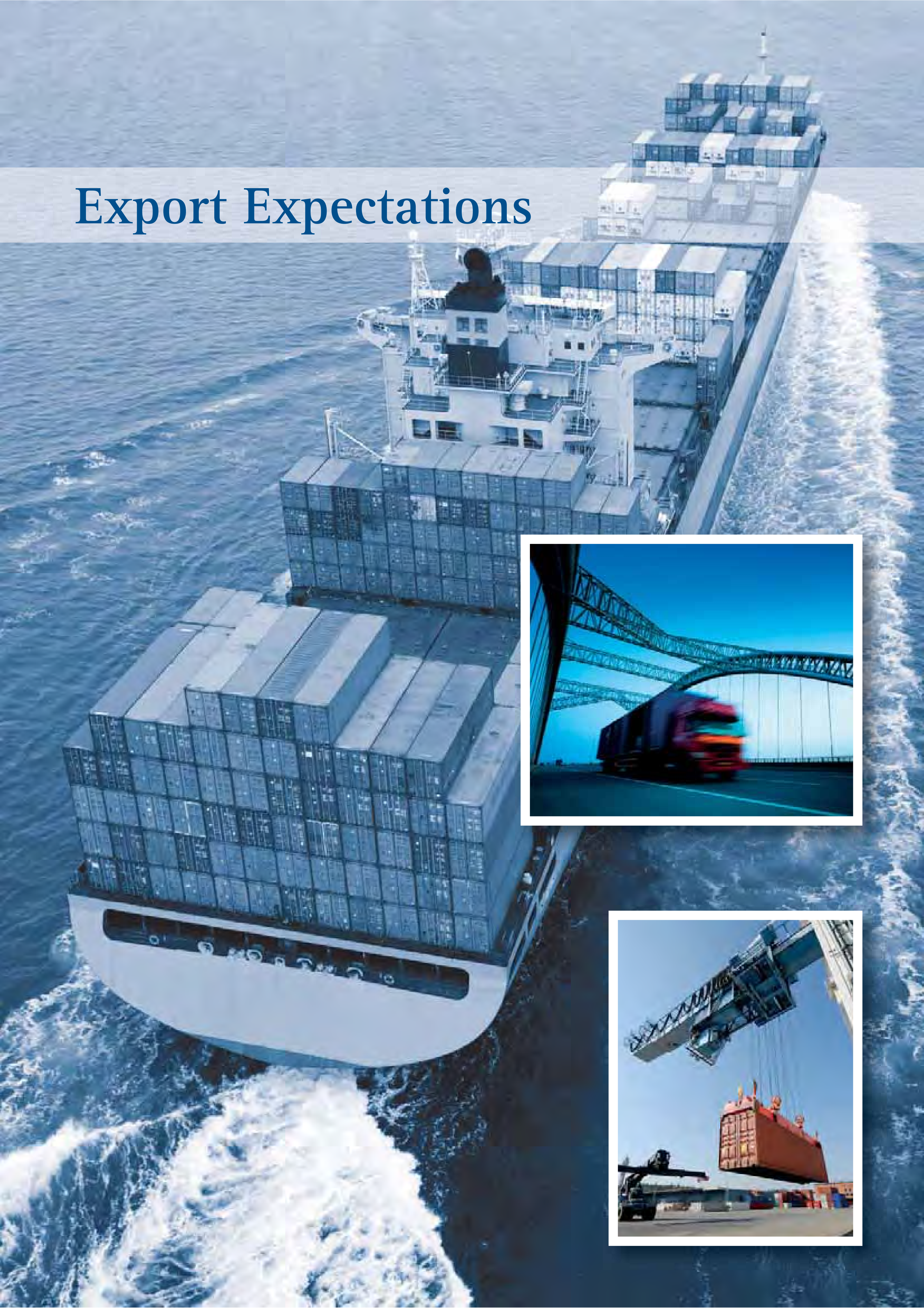
Construction maintaining a fast stroke rate

The construction industry is more optimistic than ever before at the start of a year. The balance has climbed by six to eleven points. Business expectations have improved in all sectors (structural engineering: from seven to 13 points; civil engineering: from zero to three points; the finishing trade: from six to twelve points). Construction activity remains high, particularly in the area of residential construction. The reasons for this are the growing demand for housing by refugees and the influx into the conurbations with simultaneous rises in incomes and favorable financing conditions. Fewer businesses than in any previous survey (since 2010) are afraid of setbacks with respect to domestic demand (34 percent). Even in civil engineering – which has long been buffeted in the face of extremely weak public investments – the risk share has fallen to a new low of 36 percent. This sector is increasingly benefiting from the rise in public funds for infrastructure. However, in many cases the plans are often not moving forward quickly enough due to the lack of personnel. The construction companies are also often searching in vain for skilled employees: the business risk of the "shortage of skilled workers" has reached a record level in civil engineering (74 percent), as well as in construction as a whole (70 percent) and among architecture and engineering firms (58 percent). Because of the difficulty in finding suitable personnel, many construction companies are paying higher wages – rising labor costs are the second-largest risk from the perspective of these business. Additional factors are regulatory hurdles and too little free space for building in many locations.

Hope of bottoming out in the financial sector

The expectations in the financial sector are still clearly pointing in a downward direction. However, the companies are no longer quite so pessimistic as in the autumn of 2016 when they look forward to 2017. The balance has climbed from minus 21 to minus 13 points. On the one hand, the outlook of the insurance companies has improved (balance increase from eight to twelve points). On the other hand, the banking industry is less pessimistic (minus 31 after the previous level of minus 40 points). Although the demand perspectives have improved (decrease in the risk by three points to a record low of 25 percent). At the same time, however, the concerns about deteriorating economic policy framework conditions continue to grow. The proportion has increased from 82 to 85 percent – not only the highest level ever, but also in the cross-sector comparison. Here, the institutes make reference to the increasing tightening of the financial market regulations and above all the low interest rates as a business risk. The "Basel III" regulatory framework has now been put into effect, with the further plans for "Basel IV" having been postponed only for the time being. In addition, the ECB is pursuing an expansionary monetary policy for the time being in spite of the normalisation of inflation. As a result, the low interest rates remain a burden on the banking industry. Furthermore, the ECB may be forced in the medium term to implement an abrupt exit from the relaxed monetary policy.

Export Expectations



Recovery of export expectations

After the weak phase during the last two years, companies are now expecting significantly higher exports. Export expectations are growing more strongly than in the last three years and are above the long-term average for the first time since 2014. World trade is also currently picking up. Growth in the American economy is accelerating, driven by the strong consumer demand. The mood in the Eurozone is also becoming brighter. China is continuing to grow, albeit through state support. While exporters' concerns about demand from abroad are declining, even more companies consider the economic policy framework conditions to be a threat to their business activities. Reference is made particularly often to the protectionist measures of the new US administration and possible counter-reactions. Trade with the United Kingdom has already received a significant setback. What is more, Brexit increases the economic uncertainty. The rise in the exchange rate risk is an indication of possible turmoil on the foreign currency markets. All in all, the expectations for foreign business are positive, while it is unclear to what extent the political risks will become visible in the order books.

Exporters significantly more confident

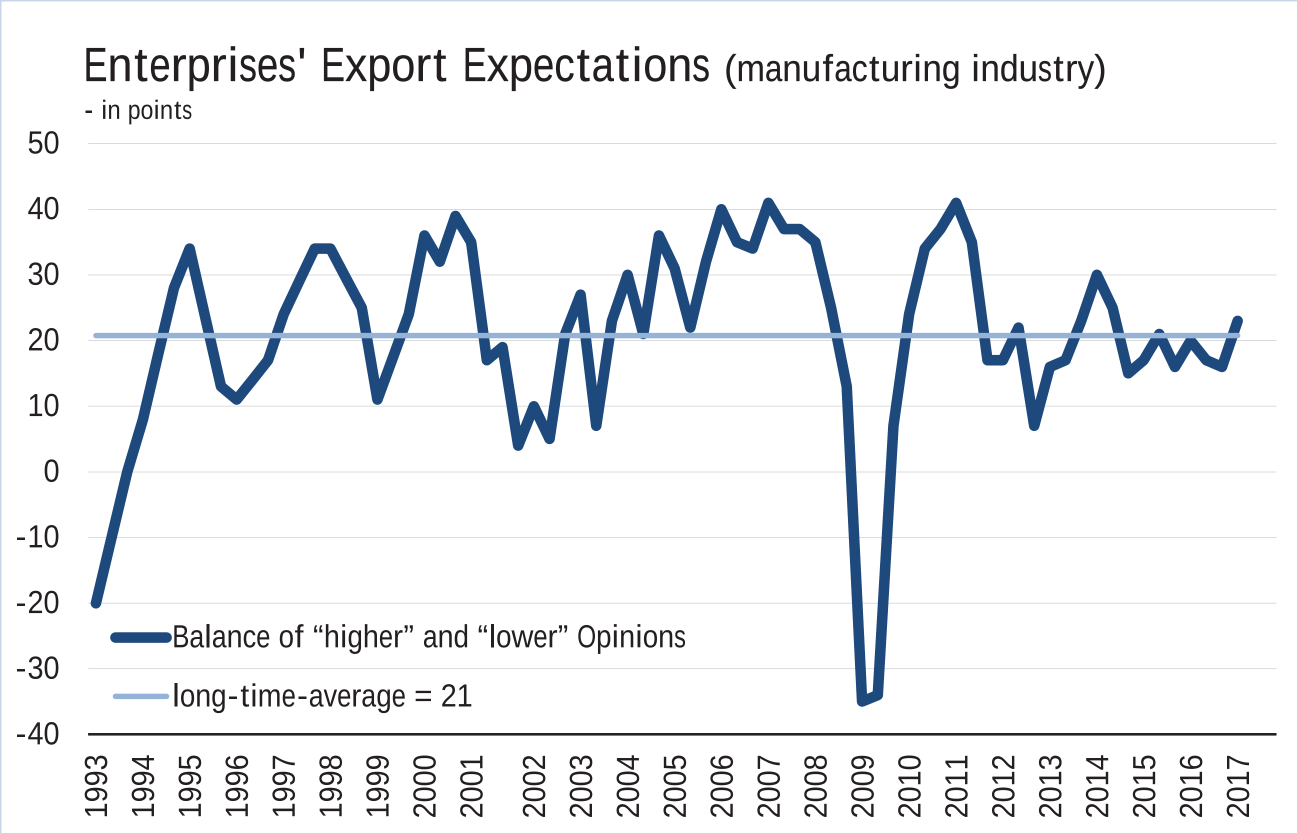
The mood in the export-oriented manufacturing industry has improved noticeably. More than a third of companies (34 percent) expect exports to increase for the next year. Only eleven percent of businesses expect them to decline. The resulting balance of 23 points is a full seven points higher than in the previous survey.

Weak phase in 2016...

There has not been such a strong rise in the export expectations since 2014. After that time the balance remained for almost two years below the long-term average (21 points). During this period the growth in world trade was exceptionally weak (2015: 2.0 percent; 2016: around 1 percent; average 1990-2014: 4.4 percent), The global economy also grew only at a below-average rate in 2016 (2016: 2.9 percent, average 1990-2015: 3.4 percent), One cause of this was the global increase in protectionism. Furthermore, the previous very dynamic growth of many emerging economies came to a standstill, especially in the field of investments. Because the low inflation levels were primarily of benefit to consumers, consumption and services grew more strongly worldwide than foreign trade.

Enterprises' Export Expectations (manufacturing industry; in percent)

	higher	about equal	lower	balance
February 2015	30	57	13	17
Early Summer 2015	31	59	10	21
Fall 2015	30	56	14	16
February 2016	32	56	12	20
Early Summer 2016	29	59	12	17
Fall 2016	29	58	13	16
February 2017	34	55	11	23



... overcome for the time being

At the beginning of 2017, the export expectations have again climbed above their long-term average. This nourishes the hope that the world economy – and above all world trade – will begin to expand again somewhat after their weak phase. The rising prices for oil and other raw materials are also substantiated on the demand side, and therefore a sign of increasing global economic activity. With the rising commodity prices, the global economy is also expected to grow again – driven less by consumption and services, and more by investments and exports. German exporters in particular can benefit from this. The export expectations of the capital goods producers and manufacturers of intermediate goods are displaying a particularly strong improvement (increase in the balance by eight in each case to 26 and 21 points respectively). The prospects of the manufacturers of consumer goods have improved to a less significant extent (increase by five to 24 points). It is questionable whether German industrial companies can also gain new market shares – especially in view of the fact that the above-average rises in unit labor costs and energy prices have recently had a noticeable negative effect on competitiveness. Moreover, the increasing number of protectionist measures remains a brake on the development of world trade.

Producing countries benefiting from rising commodity prices

The price increases for energy and raw materials are providing the producing countries with more room for manoeuvre again, which in turn is boosting demand. Since German exporters are particularly well represented in the investment goods sector, they benefit when countries which are rich in natural resources invest more in materials handling technology, further processing or diversification of their economy. Although the costs of businesses are increasing and the growth in the purchasing power of consumers diminishes worldwide if they spend more on petrol and heating oil or have to put up with price rises for finished products, the improved employment situation with simultaneously rising wages is outweighing this effect in many industrialised countries. As a result, consumer demand continues to grow. The concerns about foreign demand are also decreasing accordingly. At present, 39 percent of exporting industrial companies are worried about the development in demand beyond the border. That is five points less than in the autumn.

Political uncertainty growing

The proportion of industrial businesses which are concerned about economic policy framework conditions has risen to a new record level (43 after 36 percent in the autumn). It is international issues which currently dominate here:

- Change of government in the USA: Concerns about the future policy of the American government is specifically referred to by almost every fifth industrial business. They are afraid of punitive customs tariffs, for example, or other protectionist measures. A risk to the world economy is seen by some businesses in particular as being a negative development in trade relations between the United States and China.

- Brexit: With respect to the announced withdrawal of the United Kingdom from the EU, companies refer above all to further exchange rate risks, as well as the resulting dangers to the EU internal market overall. In particular, the uncertainty about the exact modalities are putting a strain on many companies. In many cases this is a barrier to investments, which in turn is having a negative impact on German equipment suppliers.

- Worldwide trend towards isolation: Beyond the situation in the United States and Brexit, many businesses are concerned that worldwide international cooperation will suffer setbacks. Free trade is being restricted, advantages being questioned.

- Future of Europe: The political and therefore also economic stability of Europe is being jeopardised in the view of many businesses by populist and nationalist trends – not least in advance of elections in Europe. The companies also see threats to the stability of the euro in the banking crisis in Italy or the bankruptcy of a state in the eurozone.

- International crises and terrorism: The political uncertainty in Russia and Turkey are proving a burden on many companies. Some of them also see the continuing war in the Middle East as a threat to their business activities. In addition, the concerns about terrorism are growing both at home and abroad.

Exchange rate: stability in danger

The proportion of companies that see the development of the exchange rate as a risk to their business activities has increased by two points to 17 percent. Even though the trade-weighted exchange rate is not currently undergoing any significant fluctuations, its development is far from being stable. The exchange rate of the pound has recovered to a certain extent since the significant devaluation in the wake of the Brexit decision. Over the year, however, the decline remains at the level of ten percent. This makes German exports to the United Kingdom more expensive. During the course of the Brexit negotiations there could well be further rate fluctuations. The renminbi has also fallen in value significantly. China is currently attempting to stabilise its foreign exchange market. For this, the country is willing to accept controls on the flow of capital, resulting in a noticeable feeling of uncertainty for German companies locally. The exchange rate against the US dollar remains at a favorable level. As a result, German exports are becoming less expensive overseas, while imported competing products from the USA are more expensive. The unclear economic policy course being taken by the USA has however increased the likelihood of turbulence on the foreign exchange markets. More rapid increases in the key interest rate and an expected further appreciation in the value of the dollar might result in massive outflows of foreign exchange from emerging markets and thereby put their economies under pressure. This would increase the costs of exporting companies for hedging their currency risks.

USA: short-term growth with high risks

After a relatively weak last 12 months, growth in the United States is again improving again, albeit on an uncertain path. Employment and consumer demand are developing positively again. In recent times, investments in plant and equipment have also been increasing significantly. However, a feeling of uncertainty is growing among businesses as there is little clarity about the path being taken by the economic and trade policy of the new American government. If – as announced – investments in infrastructure are set to increase, tax relief for companies implemented and extensive deregulation carried out, this will initially also give the economy a boost. In the medium term, however, this is admittedly associated with risks: public debt will continue to grow. Prices are likely to rise faster in view of the full utilisation of capacities and more limited immigration. This might induce the Fed to introduce interest rate rises more quickly – and therefore put a brake on private investments. Furthermore, the implementation of the protectionist measures announced during the election campaign, such as new customs duties or Buy American laws, would have an adverse effect on transatlantic trade. In addition, growth in the United States would also be likely to be negatively affected if the country gives up the efficiency-promoting and price-damping advantages of international competition.

China: stabilisation bought with risks

The expectations of German companies which operate in China with respect to local economic developments have again improved significantly. The proportion of companies that expect an improvement in the economic situation for 2017 has recently risen from 23 (2016) to 29 percent.[1] The Chinese economy continues to be buoyed by

[1] cf. Business Confidence Survey (AHK China), November 2016

massive state support measures such as investments in infrastructure and a very relaxed lending policy on the part of the banks. Domestic consumption has developed into an important driver of the economy. But apart from that, the planned restructuring of the economy is progressing only slowly. Up to now this has largely spared the country the associated skid marks. However, the risks on the financial markets and to the currency remain high. Property prices and construction work continue to increase, exacerbating the risk of overheating. Furthermore, the levels of indebtedness continue to grow. The lack of knowledge about the future structure of trade relations between the United States and China is also increasing the feeling of uncertainty.

Eurozone: growing economy, declining enthusiasm for reform

The medium-term economic expectations of German companies which operate abroad are very positive for the eurozone as a whole.[2] In many countries, rising employment figures are supporting this development. The upturn in the world economy is helping exporters in the euro area. As a consequence, this is again improving the scope for price rises, while monetary policy remains expansionary. As a result, the financial situation is easing further. In addition, the improved expectations for returns on investment and increasing levels of capacity utilisation are promoting the willingness to invest in the eurozone. Ireland and Spain are benefiting from the reforms of the last few years, which are resulting in strong improvements in their economic performance. Although Portugal is currently only growing at a moderate rate, the country is in the process of reversing its successful reform course. The enthusiasm for reform has also suffered in other countries that use the euro as their currency. In Italy and France, economic performance is only improving in small steps. The German companies in Italy are more skeptical about economic developments than in other European countries and are mainly worried about the economic policy framework conditions in the country. The Italian caretaker government is facing significant tasks in attempting to reduce the national debt and restructure the banking system. The debt crisis in Greece is far from overcome.

Good developments in the EU – without the United Kingdom

Brexit left its mark last year as a result of the depreciation of the pound. The uncertainty about the exact modalities remains high. Nevertheless, the positive economic developments in Europe currently predominate. Outside the eurozone, the main drivers of growth are the Czech Republic, Poland and Sweden, which are ensuring well-filled order books for German exporters. Romania and Bulgaria are also enjoying dynamic development.

Emerging countries: upward trend with high risk

In the emerging countries, the economy as a whole is likely to improve overall, not least due to the high degree of dependence on commodity prices in many cases. Developments in Asia remain sound. Furthermore, Russia and Brazil are gradually overcoming the recession. Future developments in Turkey remain uncertain – German companies are currently pursuing a wait-and-see attitude and holding back with their investments. The change of government in the United States is likely to increase the risk for many economies, not only for Mexico. The fear is that there will be trade

[2] cf. AHK World Business Outlook, Autumn 2016

policy and diplomatic disputes, as well as higher volatility of emerging-market currencies as a result.

Manufacturers of intermediate goods benefiting from the strengthening of the world economy

The manufacturers of intermediate goods are benefiting in particular from the gradual strengthening of the global economy. For the next few months, many businesses are expecting exports to rise further (balance of export expectations: 21 after the previous level of 13 points). Businesses operating in the "glass, ceramic and stone processing" sector are particularly optimistic (22 after six points previously). They are benefiting from the renewed slight upturn in construction activity, especially in Northern European countries. The chemical and paper industries are also increasingly expecting higher export levels (34 after 24 points and 24 compared to eight points previously). However, this main group in particular shows that the upward trend is very much associated with risks: the risk of "economic policy framework conditions" has reached its highest level at 42 percent.

High number of capital goods producers expecting more exports

The proportion of companies producing capital goods that expect developments to improve is particularly high at 37 percent (consumer goods manufacturers: 35 percent; manufacturers of intermediate goods: 32 percent), The balance has risen significantly compared to the previous survey (autumn 2016: 32 percent), and is therefore back above its long-term average (25 points) and higher than in the last three years (beginning of 2014: 31 points). In the vehicle construction sector the balance has climbed by a full 19 to 30 points after the low level last autumn. The low interest rates are also likely to boost demand, while for private purchases the positive development in employment is playing an important role. Furthermore, the expectations in the mechanical engineering sector have also improved significantly, as they have among electrical engineering manufacturers (25 compared to 17 and 30 after 24 points previously). Investments have been at a rather low level over the last few years, so that the need to catch up is greater. Over the last three years Europe has seen a continuous rise in capacity utilisation.

Good consumer sentiment being maintained

The producers of durable and non-durable goods see positive developments across a broad front (balance: 24 after the previous level of 19 points). Although the increase of five points is not as marked as in industry as a whole, consumer demand is traditionally known to develop more uniformly. They are benefiting from the good consumer sentiment in many industrialised countries as a result of the improved employment situation and rising wages. This is compensating for the gradually rising level of inflation, which will diminish the purchasing power of consumers in the medium term. The food and feed industry (31 after 24 points previously), the textile, clothing and leather industry (15 after seven points), as well as the manufacturers of jewellery, musical instruments, sports equipment and toys (30 after 20 points) have better expectations. The pharmaceutical industry is also expecting a positive development in exports in many more cases than in the previous survey (increase by 16 to 42 points). In the furniture and beverage industries, on the other hand, the level of optimism has fallen with respect to the export business (30 compared to 33 and 37 compared to 39 points respectively).

Investment Intentions

Investments: advancing in small steps

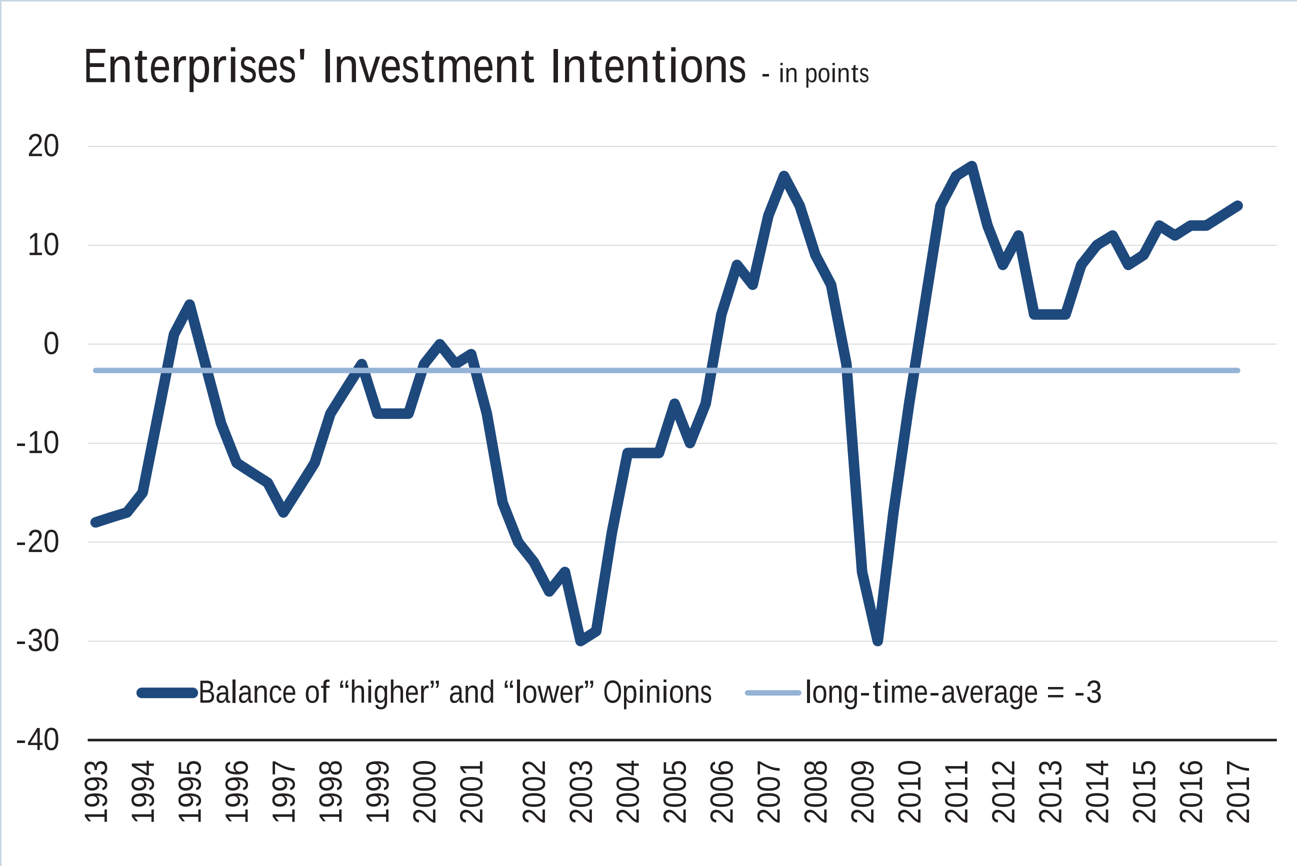
The investment intentions of companies have again improved slightly. The favorable financing environment, the positive developments in consumption and the current improvement in export expectations are encouraging companies to push forward with their plans. The impetus is currently coming increasingly from the manufacturing industry. The vehicle construction sector intends to increase its investment budgets significantly, after a downturn in the previous survey. In the construction industry, the continuing boom is pushing the investment intentions of businesses to record levels. In the service sector as well, some industries are reporting new records, for example the real estate industry, leasing and rental agencies or the catering industry. The banking sector, which is so strongly affected by low interest rates, regulation and digitisation, is also intending to invest more, admittedly in many cases with the objective of rationalisation. Overall, the lack of skilled employees is developing into an increasingly important limiting factor for more investments in Germany as a business location.

Robust overall picture...

The proportion of companies which are expanding their investment budgets has increased by one point to the current level of 29 percent, with 15 percent planning to reduce their investments (56 percent unchanged). The resulting balance of 14 points is one point higher than in the previous survey. The development in the investment intentions of companies over the last three years has been unusually stable. They have now exceeded their long-term average by 17 points. This is a hopeful sign that the investment gap in Germany is at least decreasing gradually. In terms of the individual branches of the economy, manufacturing industry is the most dynamic. The balance here has risen by two to 14 points. The second driving force is construction; there the willingness to invest has climbed on balance by as much as four to nine points – more than ever before. In the services sector the propensity to invest has risen by two points (balance: 16 after the previous level of 14 points) and is therefore no longer far off its record level (18 points). In the trade sector the investment balance remains unchanged at ten points.

Enterprises' Investment Intentions (in percent)

	higher	about equal	lower	balance
February 2015	26	57	17	9
Early Summer 2015	27	58	15	12
Fall 2015	26	59	15	11
February 2016	27	58	15	12
Early Summer 2016	27	58	15	12
Fall 2016	28	57	15	13
February 2017	29	56	15	14



… also in terms of investment motives

There are various motives underlying the increase in the investment budgets. For example, the motives of rationalisation (33 compared to 32 percent in the previous survey), product innovation (also 33 after 32 percent previously), expansion of capacity (30 compared to 28 percent), replacement needs (67 after 65 percent) and environmental protection (15 compared to 14 percent) have increased. For the first time, all of the investment motives surveyed have increased simultaneously (since 2003). This reflects the various challenges and opportunities faced by companies at the same time: digitalisation, rising energy and labor costs, competitive pressure, regulation – above all in the financial sector – as well as increasing demand.

Shortage of skilled workers as an inhibiting factor

54 percent of companies that intend to expand their investment budgets consider the shortage of skilled workers to be a risk to their business. This is six points more than the average for the economy as a whole. Among the businesses which are planning investments to expand their capacities, this figure is as high as 58 percent. This indicates that the shortage of suitable skilled employees is restricting the expansion of many companies. Businesses are postponing investment projects if their profitabil

ity is placed in doubt by problems filling the related vacancies. In 2014 every other company stated that it was investing less due to the shortage of skilled workers.[3]

Manufacturing industry: return to its old strength…

Manufacturing industry is remarkably expansive again in terms of its investment budgets. World trade has overcome its weak phase for the time being, with the consequence that above all the foreign business of companies is gathering momentum again. With the current balance increase of two to 14 points it is – unlike construction – still somewhat off its record level (28 points). Nevertheless, this value represents an upward surge: in the six previous surveys it remained stable at between eleven and 13 points. In manufacturing industry as well, the investment motives of rationalisation (47 percent of companies, after 46 percent in the autumn of 2016), product innovation (40 compared to 38 percent) and capacity expansion (34 after 32 percent) are increasing. Environmental protection and replacement needs remain at the level of the previous survey (20 and 63 percent respectively).

… but not the energy-intensive sectors

Manufacturing industry is being subjected in 2017 to additional burdens on electricity costs caused by the country's home-made policy. Businesses consider the rising energy and commodity prices as the greatest threat to their business (47 percent of the risk references compared to 37 percent in the previous survey). Among the companies which are reducing their investment budgets, as many as half see the energy and raw material costs as a business risk. With the impending conversion of the CHP levy and the increase in the Renewable Energy Law levy, many businesses have to expect additional costs – money that is lacking for investments. For example, the chemical industry is reducing its investments slightly on balance (from 20 to 19 points). The picture is also significantly gloomier on the supply side. For example, the investment plans of the energy suppliers have fallen into the negative range for the first time in more than ten years (balance change from minus 14 points to minus two balance points).

Capital goods manufacturers planning major expansion

Capital goods manufacturers are significantly expanding their budgets. They are currently benefiting in particular from fresh stimulus from the export business. The balance here has risen by six to 15 points. The motor vehicle industry is also significantly increasing its investment budgets (balance increase by 15 to 23 points) – admittedly after an equally large downturn in the previous survey. Electrical engineering is also planning considerably higher commitments (balance increase by four to 19 points) – well above the average of the last few years (nine points). Mechanical engineering has been planning remarkably consistent increases for the last few years – the balance has increased by one to eleven points (long-term average nine points).

Manufacturers of intermediate goods and producers of consumer goods

The investment plans in the two other main groups of the manufacturing industry are also expansionary. Consumer goods producers and the manufacturers of intermediate goods have slightly expanded their plans (balance increase by one to 14 and by two

[3] cf. Highlight on Economic Policy: Investment Weakness in Germany, Summer of 2014

happy to invest – with limitations

to 15 points respectively). The latter are also benefiting from the ongoing construction boom. For example, sectors such as "glass, ceramics, stone processing" (balance increase by eight to 18 points), the rubber and plastics industry (balance rise of four to 19 points) and electrical equipment suppliers (balance unchanged at 16 points) in particular intend to invest strongly in order to meet the high demand. The investment motive of expanding capacity is becoming considerably more important in some sectors. Although the manufacturers of consumer goods want to invest more overall, the picture within the main group is ambivalent. The manufacturers of jewellery, musical instruments, sports equipment and toys are increasing their investments vigorously (the balance has increased by 14 to 16 points), as is the food and feed industry (here the balance has risen by eight to 23 points). In contrast, breweries (balance minus eleven to 29 points), the printing industry (balance change by minus seven to minus nine points) or the pharmaceutical industry (balance deterioration by 13 to 20 points) have significantly reduced their investment budgets in some cases.

Construction: The sky is the limit

The investment balance in the construction industry is as high as during the unification boom in 1991. Compared to the previous survey, it has risen by four, and compared to the beginning of 2016 by as many as five points to the current level of nine. The expansive plans are remarkable and follow a long period of weak development in this sector – the average is only minus eleven points. In structural engineering the reply balance has risen by seven to eleven points. The booming field of housing construction has been fully incorporated into the investment plans of these businesses. Never have so many structural engineering companies wanted to expand their investment budgets on balance. Civil engineering is also developing dynamically; the balance has increased by seven to five points (second highest value since 2003). The sector is increasingly benefiting from the growth in public spending on infrastructure, even though this is becoming available more slowly than originally planned due to planning bottlenecks. The enormous pent-up demand in transport investments while the public coffers are also well filled is also an indication of an increase in funds over the long term. Throughout the construction industry, more businesses than in any previous survey since 2003 intend to expand their capacities (25 after the previous level of 22 percent). Furthermore, the rationalisation motive is becoming more and more significant (27 compared to 24 percent) and is therefore ranked in second place among the motives for investment (replacement motive 80 percent). Against the background of the high number of potential employees which the industry is unable to acquire, this is no surprise – the industry sees itself as being forced to compensate for the lack of missing specialists by the increased use of capital. The business risk of the "shortage of skilled workers" has risen again by one point in the construction industry to its current level of 70 percent.

Service providers close to their all-time high

On balance, the service providers also want to increase their budgets, albeit not in all sectors (balance increase by two to 16 points). As a result, the investment intentions are not far away from their record high (18 points). The spending plans of the personal service providers are currently more restrained – the investment balance has fallen significantly by four to 14 points. The plans of the providers of health and social services in particular, as well as the leisure industry, are by no means as expansionary as they were in the autumn of 2016 (balance deterioration by eight to 25 and by seven to eight points respectively). In contrast, the company-related service providers intend to invest more (balance improvement by one to 16 points). The plans of the advertising and market research agencies show a particularly strong increase (by eleven to 16 points). The "labor recruitment and provision of personnel" sector (ten after four points previously), management consultancy firms (16 compared to twelve points) and architecture and engineering offices (15 compared to twelve points) also have plans to further increase their investments. In contrast, the providers of research and development services have lowered their sights – the balance has fallen by five to the current level of 20 points, but nevertheless remains well above the value for the previous year (balance at that time: 15 points). In this industry the economic policy framework conditions have now become the greatest business risk (46 percent).

Banking industry somewhat more confident

The banking industry is still struggling with the consequences of the low interest rate policy, the requirements of additional banking market regulation and digitisation. Although the latter certainly offers new opportunities, the investment plans continue to display a lack of confidence. Although the balance has increased in comparison to the autumn by one point, it still remains in negative territory at minus one point and well below the long-term average (seven points). More than in all other sectors, rationalisation is driving the investment plans in the banking industry (54 percent, overall economy: 33 percent), Within the industry there are however notable differences: while savings and co-operative banks still intend to reduce their investments (minus five and minus three points respectively, no balance change), the commercial banks still have more investment projects in the pipeline than last time (18 compared to ten points). Investments which aim at expanding capacity have made a significant leap – the level in expansion investments in the autumn of 2016 was still eight percent, but has now risen to 18 percent. Equally, the motive of product innovation has risen by ten to 46 percent.

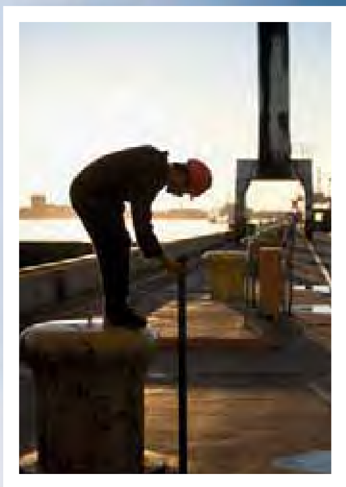
Hotel and restaurant industry more expansive

Starting from a very high level, the hotel and restaurant industry is planning even more extensive investments. The balance has increased by two to its present level of 27 points – close to the record value (30 points). Consumer confidence has been good for a long time. Additionally, the tense security situation in many foreign holiday regions has increased the attractiveness of Germany as a holiday location. As a consequence, businesses operating in the hospitality industry consider the risk of domestic demand to be lower than ever. Hotels and other accommodation businesses are planning to increase their spending once again (30 compared to 29 points previously). The balance in the gastronomy sector is even at its highest level since the surveys began (increase by two to 19 points). However, this is probably also related to new legal requirements for cash registers: these now have to record data electronically and individually in a manner which cannot be changed and store them for at least ten years. For many businesses this means the procurement of new hardware – accordingly, the investment motives of replacement investments (plus three to the current level of 75 percent) have increased, whereas the motive of capacity expansion is declining (from 20 to 17 percent).

Trade: unchanged investment dynamics

The investment intentions in the trade sector remain at the expansive level of the previous surveys (investment balance: ten points, as in the autumn and at the beginning of 2016). The drivers of this in this branch of industry remain the motor trade (balance 16 points, unchanged) and the wholesale trade (twelve points, unchanged), which is benefiting at least in part from the expansion in foreign trade. On the other hand, the retail trade, which has been restrained for several years, is characterised by more cautious investment plans (balance decline by one to five points), as are in particular the trade intermediaries (balance: four after the previous level of nine points). If one considers the focus of the investments, the motive of capacity expansion has become slightly less important among the trading companies (28 compared to 29 percent previously), in contrast to the trend in the economy as a whole (25 after 22 percent). In contrast, rationalisation is becoming more important – with the proportion increasing from 27 to 29 percent. This is also attributable to the progressive structural changes caused by digitisation, as well as increasing competition for the bricks and mortar retail trade, for example from online platforms.

Employment Intentions



Companies want to create even more new jobs

The increase in employment enters its twelfth year. The cross-sector recruitment intentions of companies even increase again. The boom in house and infrastructure building is providing impetus to the personnel plans of construction companies. The manufacturing industry and service providers are also planning for growth. However, it is becoming increasingly questionable whether companies will be able to implement their recruitment plans. In knowledge-intensive sectors such as accountancy, legal and tax advisory services, but also the construction industry, transport and the hospitality sector, the shortage of skilled workers is becoming worse once again. At the same time, high labor costs are forming a "mortgage" for times of economic downturn in many industries. Signs of an employment slowdown are coming from some of the domestic-oriented industries. For example, the retail trade and manufacturers of consumer goods are scaling down their recruitment plans. In the financial and insurance industry, the plans to employ new personnel have reached a record low.

Increases in employment continuing...

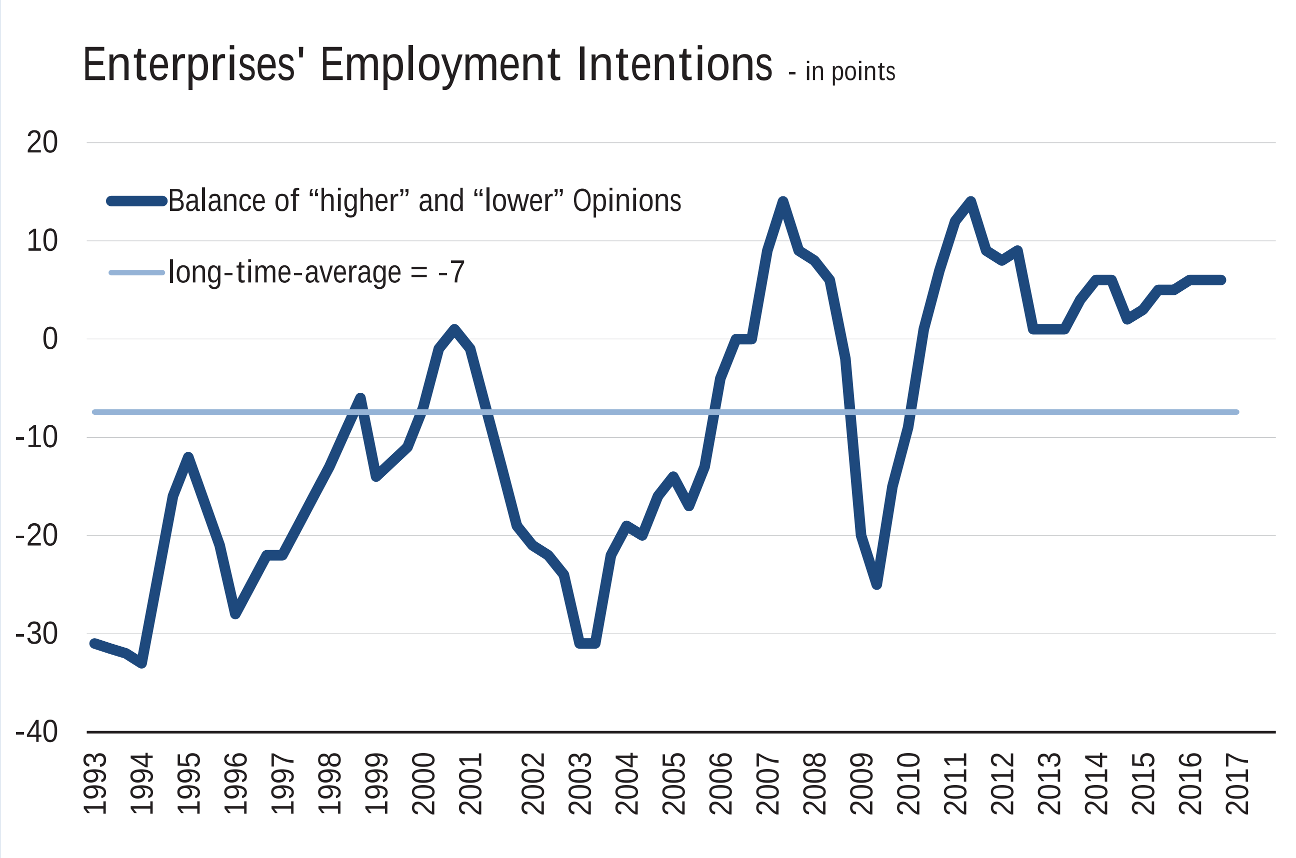
Companies intend to further increase their employment levels considerably on balance in 2017. 20 percent are planning to recruit more staff during the course of the year, one point more than in the autumn of 2016. The share of companies with reduced employment intentions stubbornly remains at the level of 13 percent. More than two thirds of businesses (67 percent) are planning for their workforces to remain unchanged. The balance of the shares with higher and lower employment intentions has improved compared to the previous survey by one to the present level of seven points.

...but being restricted by the shortage of skilled workers

In many industries the shortage of skilled workers means that urgently required positions cannot be filled. At 48 percent, almost every other company refers to the lack of qualified personnel as a risk to its business prospects. As a result, the shortage of skilled workers is also the brightest point on the companies' risk radar at the beginning of 2017. Among the companies with expansive personnel plans, as many

Enterprises' Employment Intentions (in percent)

	higher	about equal	lower	balance
February 2015	17	69	14	3
Early Summer 2015	17	71	12	5
Fall 2015	17	71	12	5
February 2016	18	70	12	6
Early Summer 2016	18	70	12	6
Fall 2016	19	68	13	6
February 2017	20	67	13	7



as 65 percent consider the shortage of skilled workers to be a risk. It is therefore questionable whether the companies will be able to implement their employment plans for the coming year as planned. And they are not only seeking academics, but increasingly also professionally trained specialists. The situation is particularly taut in the construction industry – 86 percent of construction companies with expansive recruitment plans are having to contend with the shortage of qualified skilled employees.

Caught between the shortage of skilled workers and high labor costs

Many companies are wrestling simultaneously with the problems of finding and committing suitable professionals to work for them and the high labor costs. They are offering better conditions to attract and keep suitable personnel. These usually also include higher wages. Accordingly, rising personnel costs are placing an additional burden on many companies, especially in the international competition. Overall, 40 percent of businesses consider high labor costs to be an obstacle to their business. This risk remains stubbornly at a high level and is becoming the mortgage for times in which the surge in the economy subsides again.

- In the fields of passenger road transport and local passenger rail transport, companies continue to report record figures for their employment intentions (balance: six points). At the same time, 56 percent see the shortage of skilled workers as a risk to their business plans (economy as a whole: 48 percent) and 53 percent the high labor costs (overall economy: 40 percent),

- In the road freight sector, even more businesses consider themselves challenged by the combination of the risks associated with the shortage of skilled workers (referred to by 70 percent) and high labor costs (55 percent). Increasing regulation and small margins – particularly due to competitors from Eastern Europe – are proving to be an additional burden on the industry.

- In the hotel and restaurant industry the combination of the shortage of skilled workers and rising labor costs is also causing major problems for companies. Although catering firms still want to recruit additional personnel (balance increase by three to three points), 70 percent of such catering firms complain about the severe shortage of skilled employees and 62 percent about the high labor costs. In this labor-intensive industry, the increase in the statutory minimum wage at the beginning of the year is also playing a significant role.

- Among the health and social services, which are still very willing to recruit (balance: 30 points, previous survey: record level of 37 points), as many as 82 percent of the companies see themselves at a disadvantage due to the lack of suitable personnel, while at the same time the high labor costs represent an above-average and growing business risk (47 compared to 40 percent in the previous survey).

Rising exports increasing the needs of industrial companies to recruit…

Industrial companies have further expanded their recruitment plans. In the processing industry, the willingness to recruit new employees has increased on balance by two to seven points. The employment plans of manufacturing industry are in line with their higher business expectations (expectation balance: increase by four to 17 points). Export businesses in particular are converting the renewed demand into higher employment plans (balance increase by four to ten points, manufacturing industry as a whole: increase by two to seven). Further clear stimuli are being created for the producers of investment goods in particular (balance improvement by five to ten points). For example, the recruitment plans in the mechanical engineering sector are significantly more expansive (balance increase by five to eleven points). The motor vehicle manufacturers have overcome their weak phase, as reflected in improved employment intentions (marked increase by ten to minus one point). Intermediate goods producers also intend to recruit more employees on balance (improvement by three to seven points). In addition, chemical companies are also announcing above-average employment intentions (improvement by three to nine points).

… consumer goods manufacturers the exception

The producers of durable and non-durable goods are reducing their staffing level plans slightly (decline by two to four points) – unlike the other two main groups of the manufacturing industry. Although the concerns about demand are also easing here – and the expectations have improved at least slightly – the labor cost risk has risen significantly (43 after the previous level of 39 percent). For example, food manufacturers have reduced the rate at which they intend to recruit new personnel (balance decline by three to nine points; increase in the labor cost risk from 39 to 43 percent). In the printing industry the reduction in staff numbers is likely to continue (balance decline by six to minus 16 points). Here the concerns about rising labor costs (from 44 to 47 percent) and the main risk of the industry – domestic demand – have increased (69 after the previous level of 71 percent). The manufacturers of jewellery, musical instruments, sports equipment and toys have adjusted their recruitment plans significantly upwards (by nine to 18 points).

At the top with their recruitment plans: the construction industry

The employment plans of construction companies have reached record levels once more. In this branch of the economy, the share of companies with higher employment intentions exceeds the proportion of companies with plans to reduce their levels by nine points. Compared to the autumn of 2016, the companies have increased their employment intentions considerably (by four points). The continuing historically low level of interest rates and the rising demand for housing, especially in the conurbations, is providing a further boost to the personnel plans. For example, the balance in the structural engineering sector has climbed once more to a record level (improvement by three to eight points). The intentions to increase their staffing levels are even more marked among civil engineering companies (balance improvement by five to the current level of seven points), which has long been one of the most skeptical industries (long-term average: minus twelve points). Here, the gradually flowing additional funds for the expansion of public infrastructure are having a particularly strong effect. However, the severe shortage of skilled employees is placing restrictions on the plans all too often. Almost three quarters of civil engineering companies refer to this as a risk to their business activities (74 percent, overall economy: 48 percent),

Construction-related industries also planning to recruit more

The continuing boom in the construction industry is also inducing the companies working in the associated industrial sectors to ramp up their recruitment plans. For example, companies in the "glass, ceramic and stone processing" sector want to increase their workforces considerably (up four to six points), as do rubber and plastics manufacturers (increase by three to twelve points) and electrical equipment providers (increase by seven to 14 points). Supplying service providers such as architecture and engineering firms also intend to translate the high demand for their services into additional employment (increase by four to 27 points).

Employment engine services: running

Growth is also being planned by service companies, which when taken together represent more than half of all workers. On balance the service companies have expanded their employment plans by one point compared to the previous survey (last survey: six points). The plans of the predominantly company-related service providers are pointing upwards and in the significantly expansionary range (22 after the previous level of 20 points). Record levels are also reported by the trade fair, exhibition and congress organisers (27 compared to 21 points). Other company service providers also intend to expand strongly, such as legal and tax consultants and chartered accountants (increase by one to 20 points), management consultants (up by two to 18 points), advertising agencies and market researchers (increase by two to eleven points) and providers of other freelance, scientific and technical services (increase by four to 13 points). The employment plans also remain high among the research and development service providers, even though they are not able to maintain the level of the previous survey (24 points, decline by three points). The employment intentions of the IT service providers remain clearly expansive (34 points, as in the previous year), driven by digitisation. However, at the same time the severe shortage of qualified specialists is also causing the industry many problems (for 56 percent of IT service providers this is a business risk, industry as a whole: 48 percent).

Temporary employees in demand

Temporary employment agencies have more expansive recruitment plans than in the last survey. Compared to the previous survey, the industry has announced a significant increase in its employment intentions (by seven to the current level of 23 points). The balance is therefore almost back to its average of 28 points, one of the highest in the cross-sector comparison. Many companies want to cover their additional staffing requirements – for example during periods of peak demand – with temporary employees. The high demand for temporary employment agency workers is even outweighing the impacts of the reform of the Law on Temporary Employment, as a result of which temporary employment agencies will be exposed to new risks and higher costs from the spring. Even so, the regulation of temporary work has put a damper on the business prospects in the industry – more than two thirds see the economic policy framework conditions as a barrier (68 percent, overall economy 43 percent). Furthermore, more than one in two temporary employment agencies refers to the high labor costs as a risk (increase by five points to 51 percent, overall economy: 40 percent). Moreover, their clients' concerns about acquiring skilled employees is also being felt by the mediators of temporary employees themselves – more than three quarters of the temporary employment agencies consider the lack of specialists to be a business risk (77 percent, overall economy 48 percent). They also experience comparatively high staff turnover levels, as more employees are recruited by the companies where they are temporarily employed.

Change in consumer behaviour: brake signals from the retail trade

In the past it was the service providers who benefited above all from strong domestic consumption, while the climate in the retail sector was mixed. This is also reflected in the employment plans for the coming months. The employment intentions of the predominantly personal service providers are still pointing in an upwards direction (increase by two to the current level of twelve points). For example, companies working in the fields of the arts, entertainment and recreation intend to expand again (increase by nine to the current level of two points). This is enabling the leisure industry to largely make up for the damper it suffered at the end of 2016. At the same time, the retail trade has moved down a gear with its employment plans – here the proportion of companies with expansive and reductive plans cancel each other out at the beginning of 2017 (decline by two to a current balance of zero points). The bricks and mortar retail trade is increasingly feeling the competition from the online mail order business and worried about weakening demand (the business risk of domestic demand is referred to by 52 percent of retailers, overall economy: 40 percent). In contrast, the more export-driven wholesale trade is in a much better position and is expanding its plans once again (increase by two to the current level of ten points). The motor vehicle trade has even reported a record level for its employment plans (increase by five to the present level of eleven points). On balance, the recruitment plans of companies that work in the retail trade have therefore increased by one to the present level of six points.

Refugee numbers affecting employment

Many refugees initially require health and social care, while they take advantage of educational services such as language courses at a later time. This transition is becoming noticeable not only in the business expectations, but also in the employment intentions. Among the health and social services, the stimulus provided by immigration is no longer as significant (balance decrease of seven to the current level of 30 points). On the other hand, the demand for educational offers continues to rise. The education industry intends to recruit significantly more employees at the beginning of 2017 (balance increase by 14 to 17 points). Since the early summer of 2015 the industry has been intending to increase its staffing levels, after the balance from 2003 to 2014 had been clearly in negative territory.

Finance industry planning on reductions

The financial and insurance service providers are restricting their employment plans to a significant extent once more, reaching a new record low (decline by five to the current level of minus 34 points). Tight regulation, the advancing digitisation and margin reductions due to the phase of low interest rates are presenting major challenges to the industry. The pressure to rationalise is high – in no other industry the investment plans are so strongly focused on rationalisation (51 percent, overall economy 33 percent). While the larger commercial banks can still cope comparatively well with the difficult situation (minus 28 points), the employment plans in the co-operative sector (minus 51 points) and above all in the savings bank sector (minus 76 points) have reached historic lows. The insurance industry is also reducing its employment intentions significantly (by eight to the current level of minus 20 points). In no other industry do so many companies refer to the economic policy framework conditions as a business risk as in the financial sector (76 percent). At the same time, the shortage of skilled workers (27 percent, overall economy 48 percent) and high labor costs (29 percent, total amount 40 percent) are of relatively little significance compared to other sectors.

IHK-Economic-Surveys

The regional business surveys of the 79 Chambers of Industry and Commerce can be accessed at:
www.dihk.de/konjunktur

Questionnaire February 2017

How do you assess the current situation of your company?

- good business situation
- satisfactory business situation
- poor business situation

How do you expect your company to develop in the coming 12 months?

- better business situation
- unchanged business situation
- worse business situation

Where do you see the greatest risks in the economic development of your company in the coming 12 months? (more than one answer is possible)

- domestic demand
- foreign demand
- financing
- labor costs
- shortage of skilled workers
- exchange rate
- energy and raw material prices
- economic policy framework conditions, if so...

How do you expect exports to develop for your company in the coming 12 months?

- higher exports
- unchanged exports
- fewer exports

How will the expenditure of your company on domestic investments probably develop in the coming 12 months?

- higher expenditure
- unchanged expenditure
- lower expenditure

What are the main motives on which the planned domestic investments of your company in the next 12 months are based? (more than one answer is possible)

- rationalisation
- product innovation
- capacity expansion
- environmental protection
- replacement requirements

How is the number of employees of your company within Germany expected to develop in the coming 12 months?

- higher number of employees
- unchanged number of employees
- lower number of employees

Methodology

With the current "Export boost in spite of political risks" evaluation, the Association of German Chambers of Commerce and Industry (GCCI) is presenting the results of its latest business survey among the Chambers of Commerce and Industry (CCIs) in Germany. The survey was conducted for the first time in the fall of 1977 (until the early summer of 2013 under the title "Economic Situation and Expectations "). Since the year 2000 it has been conducted three times a year, and before that twice.

The basis of the GCCI results is surveys of companies conducted by a total of 79 CCIs. In the february of 2016 the CCIs evaluated more than 27,000 responses. The regional evaluations of the CCIs can also be retrieved on the Internet at www.dihk.de/konjunktur. The breakdown of the company assessments according to regions is also a special feature of the GCCI survey. Here the North is made up of the federal states of Bremen, Hamburg, Lower Saxony and Schleswig-Holstein, the West of the federal states of Hesse, North Rhine-Westphalia, the Rhineland Palatinate and the Saarland, the East of Berlin, Brandenburg, Mecklenburg-Western Pomerania, Saxony, Saxony-Anhalt and Thuringia and the South of the federal states of Baden-Württemberg and Bavaria.

According to sectors the replies come from manufacturing industry (29 percent), the construction industry (seven percent), the trade sector (22 percent) and service providers (42 percent). The classification of the industrial sectors in the GCCI business survey is based according to the official statistics on the classification of the industrial sectors of 2008. According to size classes the replies are divided up as follows: 33 percent companies with up to nine employees, 14 percent companies with ten to 19 employees, 42 percent companies with 20 to 199 employees, seven percent companies with 200 to 499 employees, two percent companies with 500 to 999 employees, two percent companies with more than 1,000 employees.

The CCIs carry out their random sample in such a way that a representative snapshot of the current situation of local commercial companies is provided (random sample stratified according to sectors, regions and company sizes). The aggregation at the federal level is carried out by means of a regional and sector-related weighting. The responses to the regular economic questions (see questionnaire in the attachment) of businesses with more than 500 employees are weighted with the factor 2 and the responses from businesses with more than 1,000 with the factor 3.

The risks for the economic development at not weighted anymore since fall 2016. The data of previous surveys is corrected correspondingly. Therefore, small deviations from previously published data may occur. In the case of additional questions, the weighting according to size classes is dispensed with if the unweighted proportion of companies is more meaningful.

Where the text refers to a long-term average, this relates in the various sectors of the economy to the period from the autumn of 1991 (situation, expectations) or the autumn of 1992 (export expectations, investment and employment intentions). For the individual sectors, the data that reaches back to 2003 is used to calculate the average value.

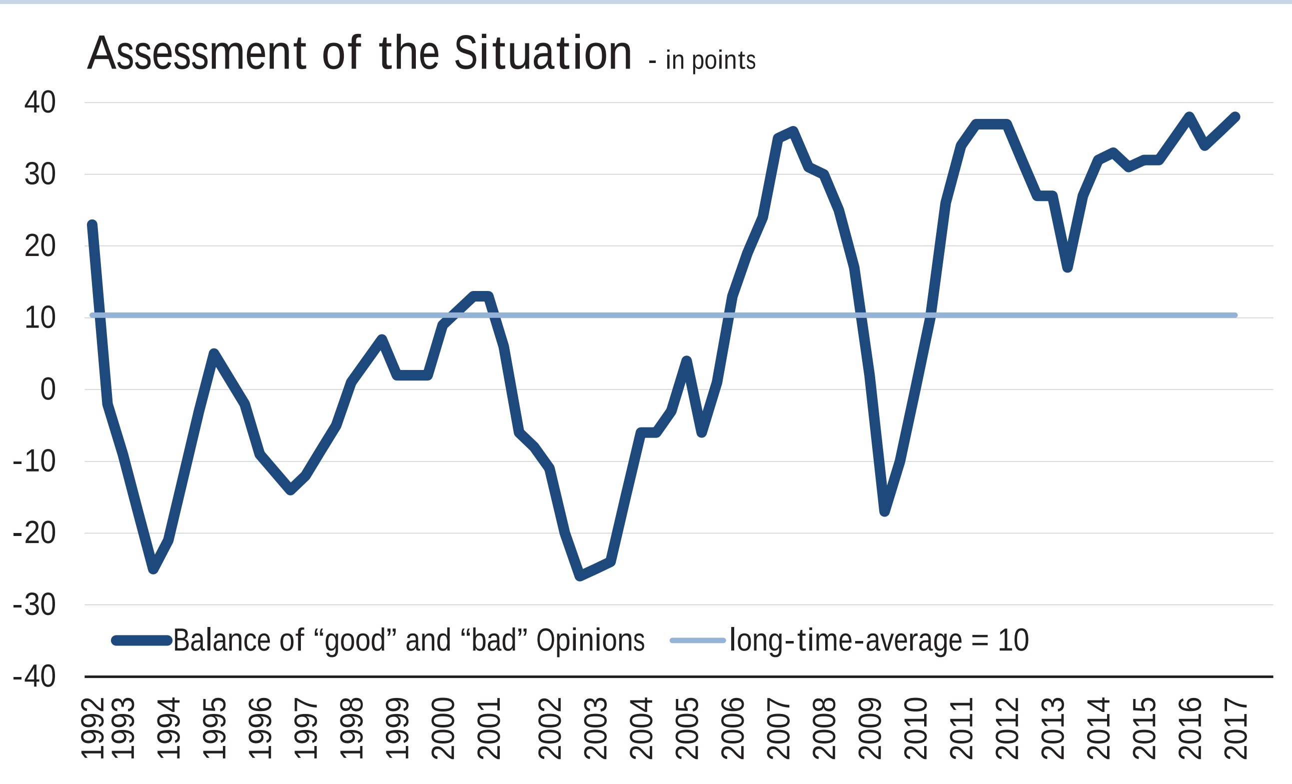
The survey was carried out from the end of December 2016 to the middle of January 2017.

DIHK-Surveys - time series

All shares in percent; Balance = Share of „good/better” opinions minus share of „bad/worse” opinions in percentage points

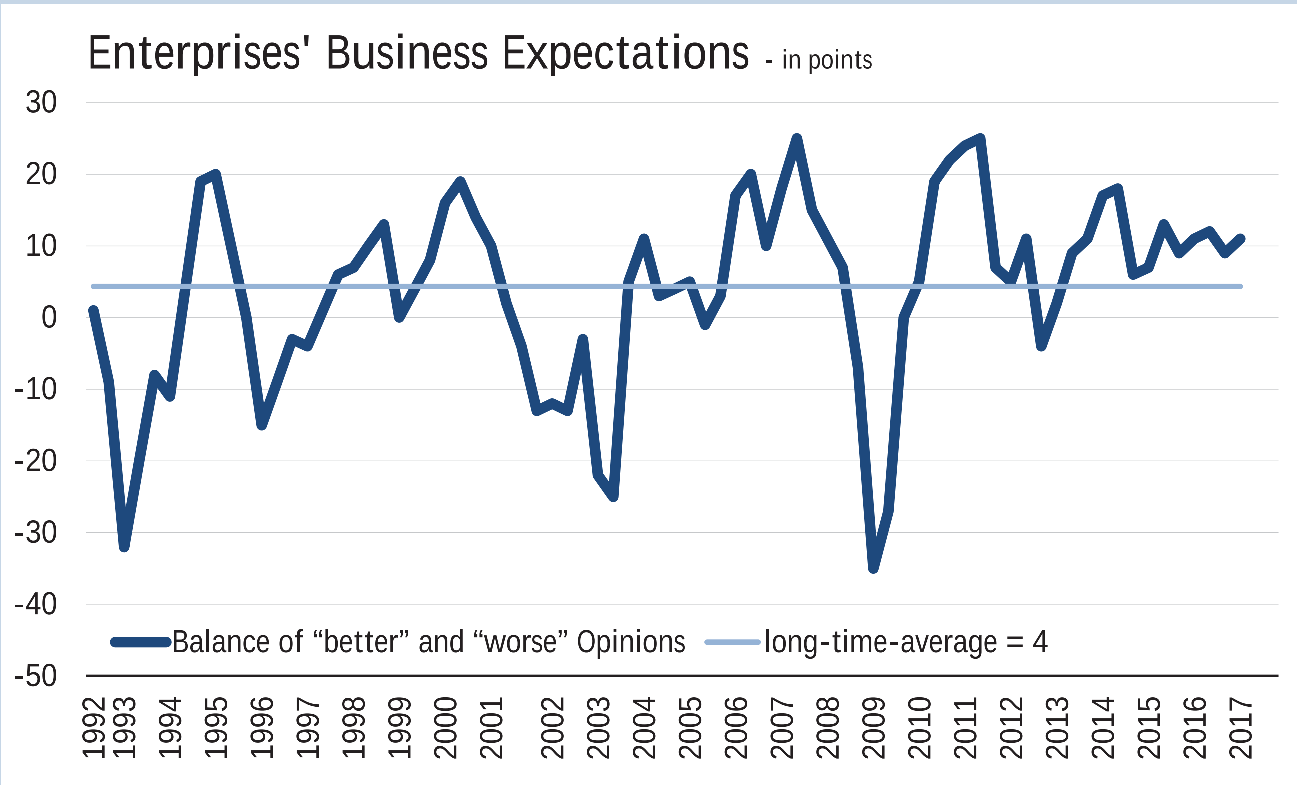
Assessment of the Situation (in percent)

	good	satisfactory	bad	balance
Fall 2010	38	50	12	26
February 2011	44	46	10	34
Early Summer 2011	46	45	9	37
Fall 2011	46	45	9	37
February 2012	46	45	9	37
Early Summer 2012	42	48	10	32
Fall 2012	38	51	11	27
February 2013	38	51	11	27
Early Summer 2013	32	53	15	17
Fall 2013	38	51	11	27
February 2014	41	50	9	32
Early Summer 2014	42	49	9	33
Fall 2014	40	51	9	31
February 2015	41	50	9	32
Early Summer 2015	41	50	9	32
Fall 2015	44	47	9	35
February 2016	46	46	8	38
Early Summer 2016	43	48	9	34
Fall 2016	44	48	8	36
February 2017	46	46	8	38



Enterprises' Business Expectations (in percent)

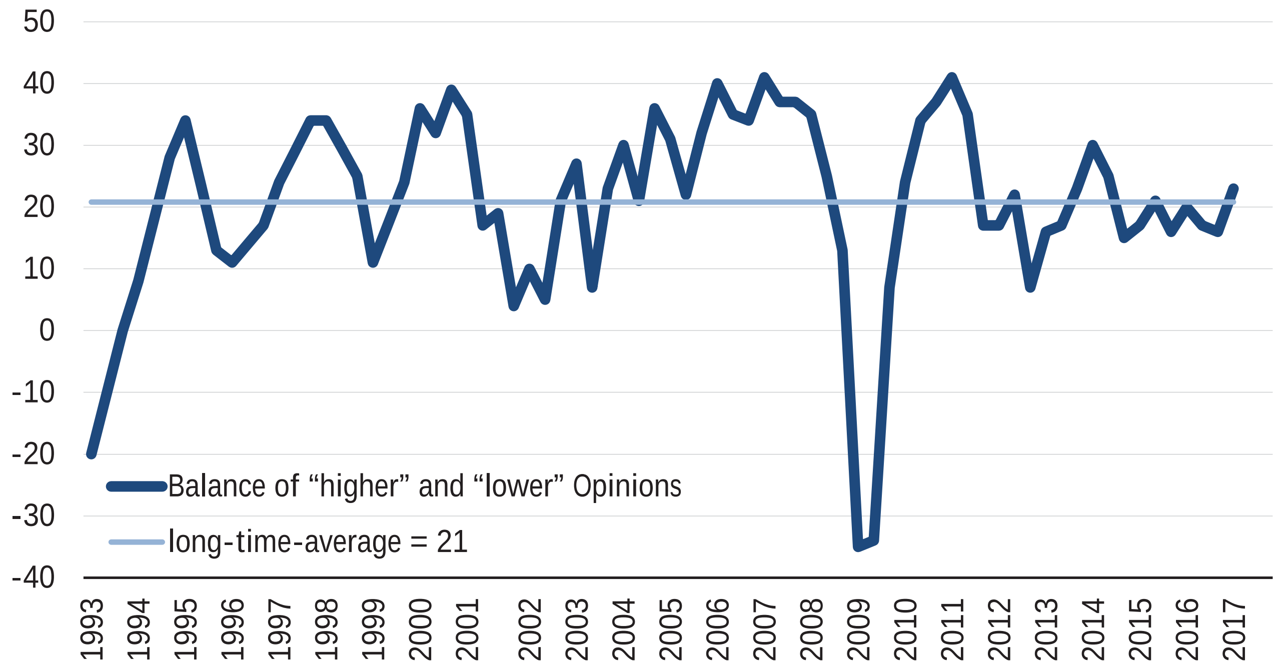
	better	about equal	worse	balance
Fall 2010	33	56	11	22
February 2011	34	56	10	24
Early Summer 2011	34	57	9	25
Fall 2011	23	61	16	7
February 2012	22	61	17	5
Early Summer 2012	25	61	14	11
Fall 2012	18	60	22	-4
February 2013	20	62	18	2
Early Summer 2013	25	59	16	9
Fall 2013	24	63	13	11
February 2014	28	61	11	17
Early Summer 2014	29	60	11	18
Fall 2014	21	64	15	6
February 2015	22	63	15	7
Early Summer 2015	26	61	13	13
Fall 2015	23	63	14	9
February 2016	24	63	13	11
Early Summer 2016	25	62	13	12
Fall 2016	22	65	13	9
February 2017	24	63	13	11



Enterprises' Export Expectations (manufacturing industry; in percent)

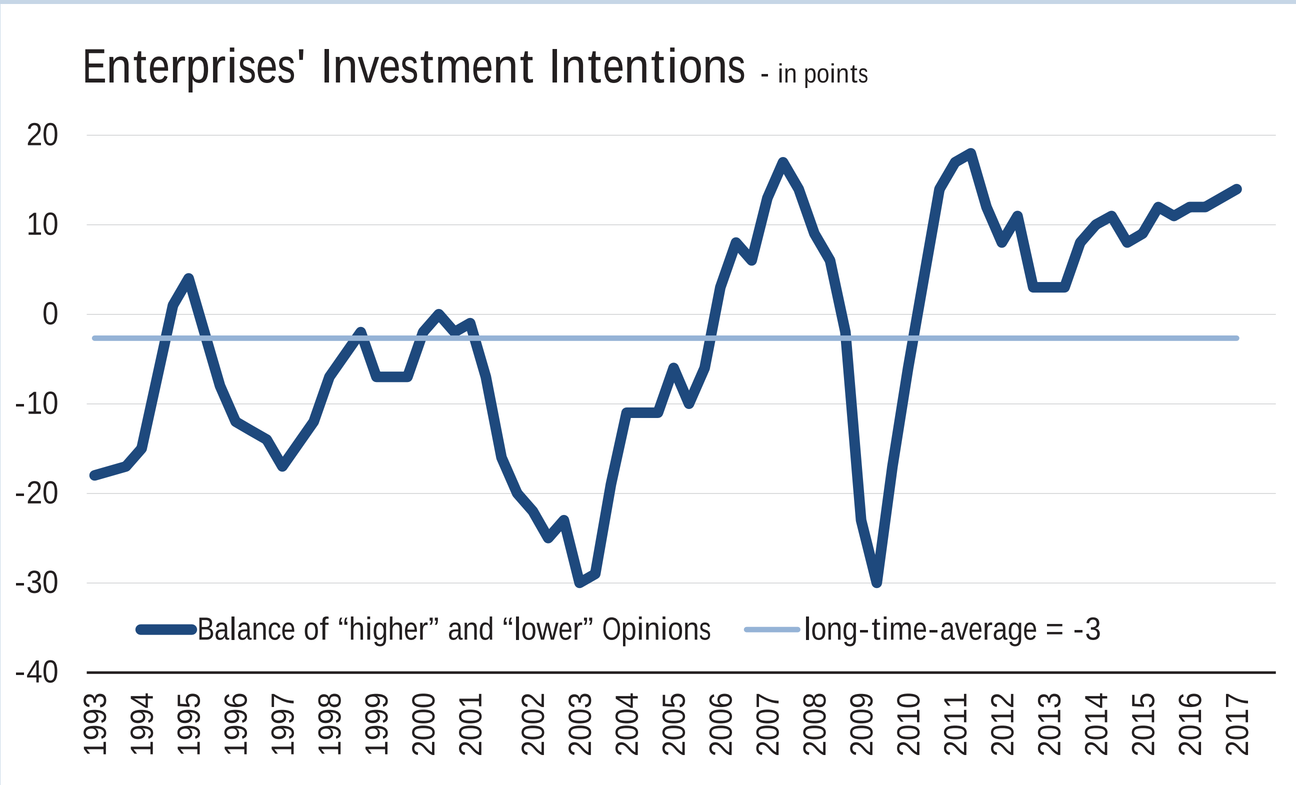
	higher	about equal	lower	balance
Fall 2010	44	49	7	37
February 2011	46	49	5	41
Early Summer 2011	42	51	7	35
Fall 2011	30	57	13	17
February 2012	31	55	14	17
Early Summer 2012	33	56	11	22
Fall 2012	27	53	20	7
February 2013	30	56	14	16
Early Summer 2013	30	57	13	17
Fall 2013	32	59	9	23
February 2014	37	56	7	30
Early Summer 2014	34	57	9	25
Fall 2014	30	55	15	15
February 2015	30	57	13	17
Early Summer 2015	31	59	10	21
Fall 2015	30	56	14	16
February 2016	32	56	12	20
Early Summer 2016	29	59	12	17
Fall 2016	29	58	13	16
February 2017	34	55	11	23

Enterprises' Export Expectations (manufacturing industry)



Enterprises' Investment Intentions (in percent)

	higher	about equal	lower	balance
Fall 2010	29	56	15	14
February 2011	31	55	14	17
Early Summer 2011	31	56	13	18
Fall 2011	27	58	15	12
February 2012	26	56	18	8
Early Summer 2012	27	57	16	11
Fall 2012	23	57	20	3
February 2013	23	57	20	3
Early Summer 2013	23	57	20	3
Fall 2013	25	58	17	8
February 2014	26	58	16	10
Early Summer 2014	27	57	16	11
Fall 2014	25	58	17	8
February 2015	26	57	17	9
Early Summer 2015	27	58	15	12
Fall 2015	26	59	15	11
February 2016	27	58	15	12
Early Summer 2016	27	58	15	12
Fall 2016	28	57	15	13
February 2017	29	56	15	14



Enterprises' Employment Intentions (in percent)

	higher	about equal	lower	balance
Fall 2010	19	69	12	7
February 2011	22	68	10	12
Early Summer 2011	23	68	9	14
Fall 2011	19	71	10	9
February 2012	19	70	11	8
Early Summer 2012	20	69	11	9
Fall 2012	15	71	14	1
February 2013	15	71	14	1
Early Summer 2013	15	71	14	1
Fall 2013	16	72	12	4
February 2014	17	72	11	6
Early Summer 2014	17	72	11	6
Fall 2014	15	72	13	2
February 2015	17	69	14	3
Early Summer 2015	17	71	12	5
Fall 2015	17	71	12	5
February 2016	18	70	12	6
Early Summer 2016	18	70	12	6
Fall 2016	19	68	13	6
February 2017	20	67	13	7

Enterprises' Employment Intentions - in points