

German industrial production soared in July, in complete contrast to the indications from the PMIs and also yesterday's new orders figures. Overall IP rose 4.0% mom, way beyond expectations (median +0.5% mom, SG 0.1%), after a decline of 1.1% in June. Manufacturing, the largest component, surged 4.7% mom, after a 1.1% decline, which pushed the level of production decisively above the pre-crisis peak. Construction output too was much stronger than we expected at +3.2% mom after -3.7% in June. Clearly these data point to much greater growth momentum at the start of Q3 than expected and put substantial upward pressure on forecasts for Q3 GDP – the level of industrial output in July was a cool 3.7% above the Q2 average. Note also that this was the largest increase in production since March 2010 – while the PMI output index slumped 11.9pt in the three months to July...that about says it all about how useful the PMI survey actually is as a guide to the hard data.

The 4.7% gain in manufacturing production was driven by capital goods which jumped 7.5% mom, after -2.8% in June. We suspect that the automobile industry had a large role in this, where output increased 11.4% mom, after a 6.4% decline in June. This could well be a Japan effect, although the auto output data since March have not been particularly weak – in contrast to new registration figures which were very weak in Q2. Be that as it may, the fact is that automobile production has surged well beyond pre-crisis levels. The recent surge in orders for capital goods – perhaps related to the strong orders inflow at the Paris Air Show – may also have aided the strong gain.

Consumer durable production jumped an eye-popping 15.4% mom, but as this sector accounts for just 3% of the overall index, the impact on the overall figures was small (it also came after a 6.3% decline in June). Intermediate goods output was also strong at 2.3% mom after 0.6% in June.

Looking beyond the short term volatility, 3m-o-3m rates of growth indicate continued exceptionally strong momentum in manufacturing, where output is up 2.5% (10.5% saar), led by capital goods at 3.3% and supported by intermediate goods production at 2.5%. Indeed, all the 3m-o-3m rate of growth in July were above those of Q2. That said, the new orders inflow has recently slowed relative to output, suggesting a slower pace of IP growth in coming months.

We continue to be surprised about the robustness of construction. There was a lot of volatility since the harsh winter caused output to slump, only to rebound massively in Q1 as companies sought to come back to production time tables. We expected this level of output, which was well above the existing trend, to be surrendered quickly, but so far the declines have been very modest (Q2 -0.9% qoq, after +13.9% qoq in Q1), and in July construction again expanded. This strength also goes well beyond what construction orders would suggest, but that has been the case for some time now.