

Macro Rapid Response

Germany: industrial production and elections

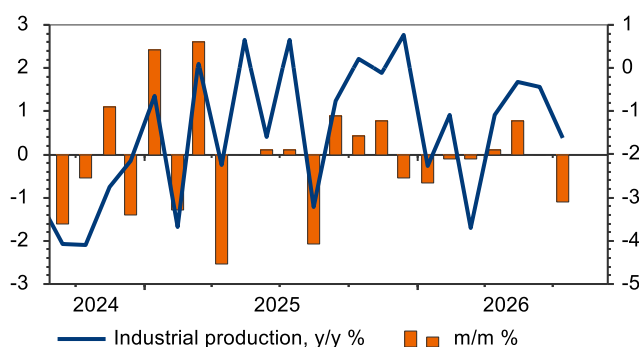
Industrial production fell by -1.1% m/m in July, with an even sharper decline when excluding construction and energy (-2.3% m/m). The contraction is mainly due to one-off factors in the automotive sector, but we believe that low water levels in the Rhine also held back activity. Order data show that demand continues to be driven by major orders, whilst the underlying trend remains subdued. Overall, considering the one-off factors that weighed on activity over the summer, a slowdown in industrial output and GDP is possible in Q3 before a rebound at the end of the year. In the Saxony-Anhalt election, the AfD secured almost 44% of the vote, whilst the CDU suffered a sharp decline. However, the far-right party failed to win enough seats to secure an absolute majority in the regional parliament. The formation of the government therefore remains uncertain. The result confirms the loss of support for the governing parties, particularly in the east of the country. Similar trends could also emerge from the regional elections scheduled for the coming weeks, further complicating cooperation between the CDU and the SPD on politically challenging structural reforms.

One-offs weighed on industrial production in July

In July, German industrial production fell by -1.1% m/m (-1.6% y/y) after the previous month's figure was revised downwards (from +0.2% m/m to zero). Excluding energy (+4.7% m/m, marking the fourth consecutive month of growth) and construction (+0.9% m/m from -1.3%), the decline is even more pronounced: **manufacturing posted a contraction of -2.3% m/m**, bringing an end to a three-month run of growth.

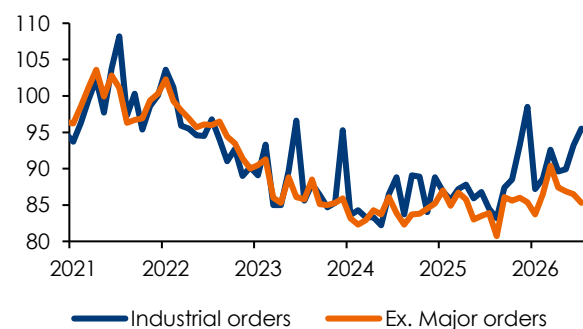
Destatis indicates that much of the decline is attributable to automotive (-9.2% m/m). The decline was affected by a production stoppage lasting several weeks during the retooling of a plant for electric vehicle manufacturing; this is therefore **a one-off factor set to reverse in the coming months**. However, **we believe that the low water levels of the Rhine**, a major waterway for industrial transport, **also held back production** (according to our estimates, this may have reduced growth by around 0.5pp).

Industrial production fell in July after stagnating in June



Source: Intesa Sanpaolo, Destatis

Industrial demand driven by major orders. Core orders remain lacklustre



Source: Intesa Sanpaolo, Destatis

Industrial orders rose by 2.5% m/m in July (+13.1% y/y), following a robust 3.7% m/m increase in June, marking the third consecutive monthly rise. However, this growth was driven by volatile, big-ticket items, particularly in the 'other means of transport' sector (+126.4% m/m). The sector is also thought to have benefited from a strong influx of Airbus orders, concentrated mainly on models for which the Hamburg production hub plays a central role; furthermore, in light of the

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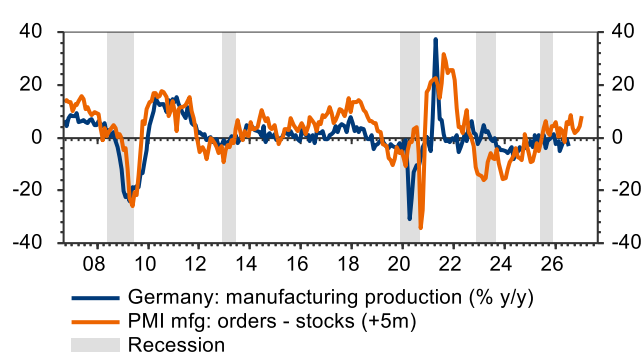
Macroeconomic Research

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information contained in the Ministry of Finance's monthly bulletin, it is plausible that defence-related demand also made a positive contribution.

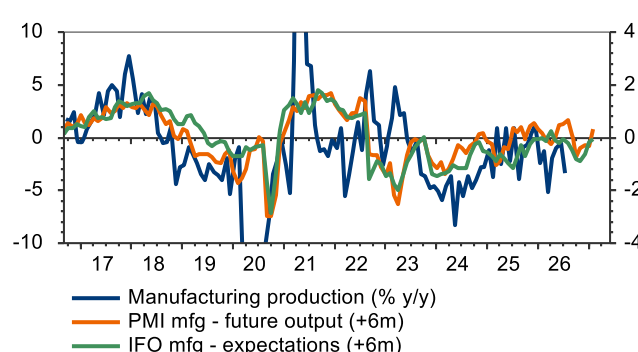
Excluding major orders, however, orders fell by 1.4% m/m, marking the fourth consecutive decline and returning to the lowest levels since January, not far from the 2025 average. The data suggests that, apart from a few sectors supported by large order books and already operating at high levels of capacity utilisation, underlying demand for industrial goods remains weak. **Confidence surveys provide mixed signals: PMIs point to a marked acceleration in orders, whilst the IFO survey is more cautious, although it confirms that, as highlighted by the marked improvement in expectations, the weakest phase of the industrial cycle now appears to be behind us.**

In the current phase PMIs offer the most encouraging signals



Source: Intesa Sanpaolo, IFO, S&P Global

Both IFO and PMI surveys record an improvement of production expectations

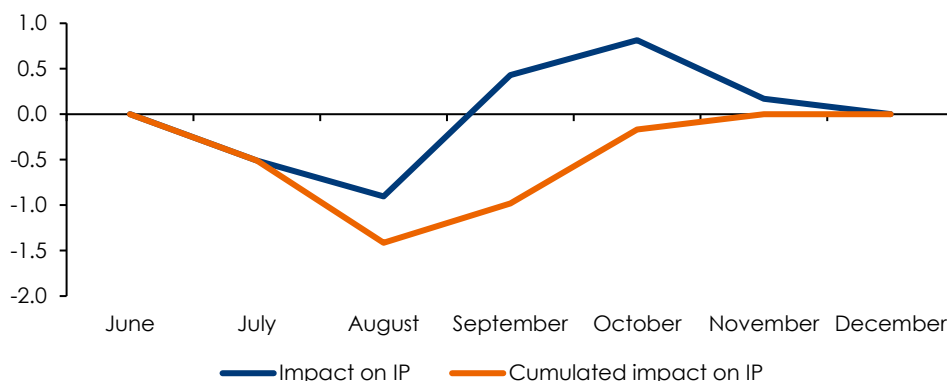


Source: Intesa Sanpaolo, IFO, S&P Global

Given the largely temporary nature of the July decline, production in the automotive sector is expected to rebound in the coming months. However, the ongoing drought could continue to hold back industrial activity. Throughout August, the water level at Kaub remained below the critical threshold, a trend which, according to our estimates, is consistent with a negative impact on industrial production of around 1 percentage point. Conditions have not yet returned to normal, even in the first week of September. **The effect of the drought is, however, expected to be temporary and should give way to a recovery in production once the most critical phase has passed.**

Nevertheless, a further contraction in manufacturing during the summer quarter cannot be ruled out, with possible negative repercussions on GDP as well. The disappearance of these extraordinary factors should subsequently facilitate a rebound in activity towards the end of the year.

Impact of the Rhine drought on industrial production: we estimate an impact of -0.5pp in July and -1pp in August, before a reversal in the following months



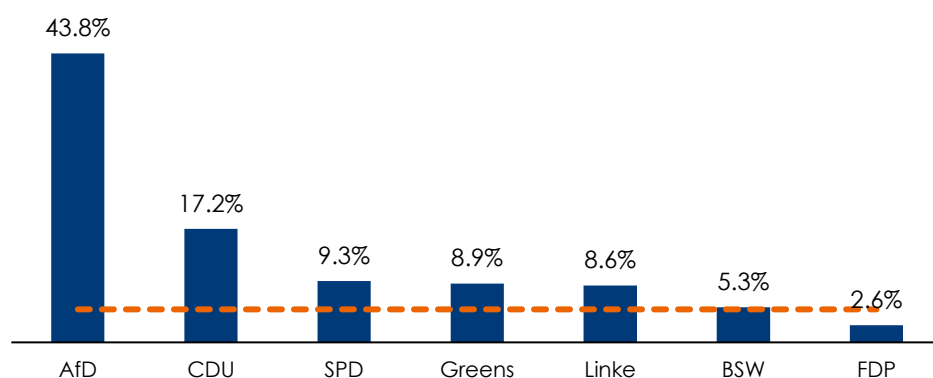
Source: Intesa Sanpaolo elaborations

Overall, the general picture remains one of still-s sluggish underlying demand, with the exception of a few sectors. In particular, the sharp rise in orders for other means of transport is expected to support production in the coming quarters, but already high capacity utilisation rates mean that new orders will only gradually feed through to manufacturing activity. We therefore expect only a moderate recovery in underlying activity in the coming months

Elections in Saxony-Anhalt: an AfD landslide, but the formation of a government remains uncertain

Yesterday, in the elections in the eastern state of Saxony-Anhalt, which saw a record turnout, **the far-right AfD party secured 43.8% of the vote, exceeding expectations and doubling its result from the 2021 election.** The CDU fell to 17.2%, a drop of 19.9 percentage points compared with the previous election. The SPD secured 9.3% of the vote, followed by the Greens (8.9%), the Left (8.6%) and the BSW (5.3%). The FDP, at 2.6%, remains below the 5% threshold required to enter the regional parliament.

Electoral results in Saxony-Anhalt



Source: Intesa Sanpaolo

With 39 seats out of 83, the AfD does not have an absolute majority. At the same time, not even the CDU, SPD, Greens and Linke together have the number of seats required to form a government. An AfD-led majority would therefore require the support, including external support, of the five MPs from the left-wing populist BSW party. The BSW has not ruled out this possibility but has made it conditional on the appointment of an independent Minister President to head the

regional government, a condition that is unlikely to be accepted by the AfD, and in any case the resulting government would inevitably be fragile.

In Saxony-Anhalt, the Minister President is elected by an absolute majority vote in the state parliament. If no candidate secures an absolute majority, a further vote must be held within seven days. If this vote also fails, the State Parliament must decide within 14 days whether to dissolve itself. Should no majority emerge in favour of new elections either, the Minister-President could be elected by a simple majority. **The formation of the new government therefore remains highly uncertain and, whilst an AfD-led government remains a possibility, a prolonged political deadlock cannot be ruled out either.**

It should be noted that **the AfD's main proposals, particularly regarding immigration and fiscal policy, are determined at federal level. Even in areas where the regional government has administrative leeway, the most extreme measures would likely come up against constitutional limits.** Furthermore, in the Bundesrat (the upper house representing the Länder), the party is unlikely to wield decisive influence in the decision-making process.

Saxony-Anhalt, with just over two million inhabitants, is one of the smallest German Länder and cannot be considered fully representative of the national political balance. In any case, **the result confirms the gradual loss of support for the governing parties, particularly in the east of the country.** Similar trends could emerge from the regional elections scheduled for the coming weeks: **ahead of the 20 September elections in Mecklenburg-Western Pomerania, polls suggest the AfD is ahead of the SPD** (which leads the local government); **in Berlin too, the CDU and SPD are losing ground, whilst Die Linke is the leading party and the AfD is third in the most recent polls.**

Whilst these disappointing results for the CDU and SPD do not appear to be sufficient to jeopardise the stability of the governing coalition, they could make further compromises within the majority more difficult and limit the government's ability to push through politically contentious structural reforms.

Appendix

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