

Box 4

THE RECOVERY OF PRODUCTION CAPACITY UTILISATION IN THE EURO AREA

There has been a strong rebound in euro area industrial production since the steep fall that occurred from mid-2008 to the beginning of 2009. In mid-2010 the capacity utilisation rate, though increasing, remained below its long-term average. However, there have been various production capacity utilisation developments across industrial groupings and euro area countries, while anecdotal evidence points to selected cases of increasing capacity constraints. Against this background, this box takes a closer look at recent capacity utilisation developments and the factors which are limiting production.

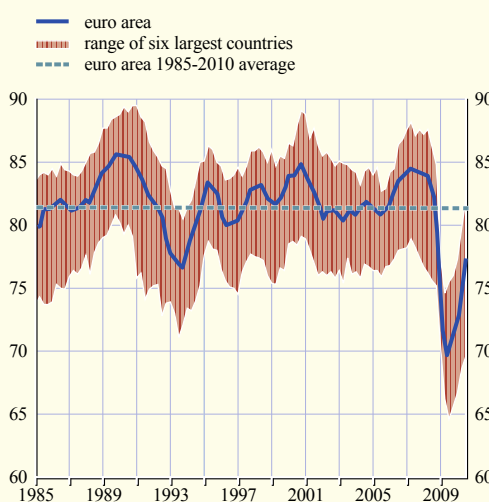
Chart A plots capacity utilisation at the euro area level and its range for the six largest euro area countries. The manufacturing capacity utilisation rate in the euro area was 77% in July 2010, 8 percentage points higher than its trough one year earlier (and a recovery of around half of the peak-to-trough fall). Despite this pronounced rebound, the capacity utilisation rate remains below its long-term average of 81%. It is important to keep in mind that this rate is a euro area average, which masks not only differences across euro area countries – as illustrated by the shaded range in Chart A – but also across industrial groupings, companies and factories. For example, among the euro area countries for which data are available, Belgium, Germany, Malta and Austria all reported manufacturing utilisation rates above or fairly close to their historical averages, after recovering around two-thirds of the peak-to-trough fall in the utilisation rate. In contrast, the capacity utilisation rates in Spain and Italy have so far recovered only around one-third of their peak-to-trough fall.

Looking at developments in the main industrial groupings, the strongest rebound in the utilisation rate has been in the intermediate goods industry. By April 2010 it had recovered around half of the peak-to-trough fall (a rise of 9 percentage points, following a fall of 18 percentage points).¹ The utilisation rate in the capital goods industry has also shown a strong increase (of 7 percentage points), following a marked fall (of 20 percentage points), whereas it rose in the consumer goods industry by a more modest 3 percentage points, after a more limited fall (of 7 percentage points). Chart B goes into more detail by plotting the maximum peak-to-trough loss and the recovery up to April 2010 by industrial grouping. It shows large differences between them. The capacity utilisation rates in the apparel, leather, chemicals, plastics and rubber, electrical, and communication equipment groupings have shown the largest recovery

¹ Detailed information by industrial grouping is available up to April 2010.

Chart A Manufacturing capacity utilisation rate

(percentages)

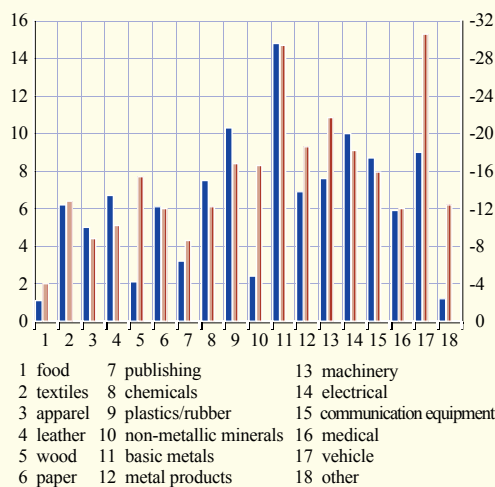


Sources: European Commission and ECB calculations.
Note: The latest observations are for the third quarter of 2010 (July).

Chart B Peak-to-trough loss and recovery in capacity utilisation rates by industrial grouping

(percentage points)

■ recovery from trough (left-hand scale)
 ■ peak-to-trough loss (right-hand scale – inverted scale)

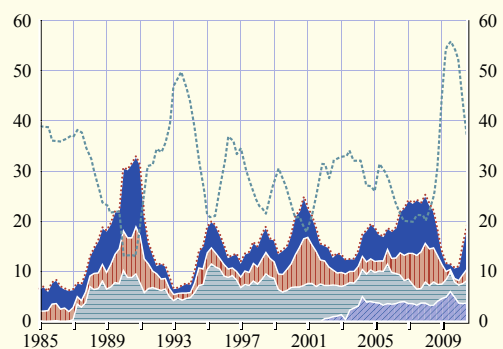


Sources: European Commission and ECB calculations.
 Note: The latest observations are for the second quarter of 2010 (April).

Chart C Production constraints in euro area manufacturing

(percentages)

■ equipment
 ■ labour
 ■ other
 ■ financial
 - - - non-demand-related limits to production
 - - - insufficient demand



Sources: European Commission and ECB calculations.
 Note: The latest observations are for the third quarter of 2010 (July). Financial constraints were not included in the survey prior to 2001.

(as a proportion of the peak-to-trough loss), whereas the capacity utilisation rates in, for example, the wood and non-metallic minerals groupings have recovered only very modestly.

To further analyse the relatively large variations in capacity utilisation rates – and bearing in mind that these rates are, by design, an “average” concept – it may be useful to look at other indicators which are also reported in business surveys, such as the number of companies that report limits to production and the origin of these limits (see Chart C). Given the rebound in sales, the proportion of manufacturers who report limits to production owing to insufficient demand has fallen sharply in recent quarters, to 37%, from the very high peak of 55% reached in mid-2009. Despite this abrupt fall, the percentage was still high in July 2010, remaining higher than at any time since the peak following the 1993 recession. At the same time, the proportion of respondents who report constraints on production due to factors other than insufficient demand has increased particularly sharply, to 19%, which is already above its long-term average of 15%. This strong increase in non-demand-related limits to production is mostly attributable to equipment shortages, whereas there have been fewer reports of labour shortages or financial constraints limiting production.

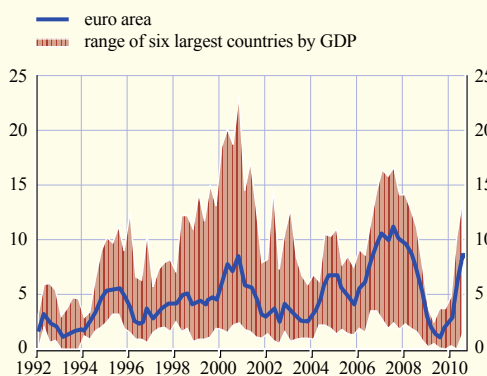
Chart D shows that equipment shortages are signalled by 9% of respondents, which is well above the historical average of 5%, and close to the previous peak levels of 2007 (11%) and 2000/2001 (8%). Here, too, there is some variation across countries and industrial groupings. In Germany, Malta, the Netherlands, Austria and Finland in particular, equipment constraints have been reported as being well above the historical average. Looking at industrial groupings,

electrical equipment, medical machinery, and vehicles tended to report a large number of cases of equipment shortages in April 2010.

Looking ahead, mounting evidence of limits to production due to equipment shortages can be expected to lead to an increase in investment if the companies concerned believe this situation will continue.² Such a rise is also to be expected, given the low base level of investment and the improved liquidity situation of non-financial corporations, which has also been reflected in their net lending position for three consecutive quarters.³ Thus, there are increasingly signs of the production situation in the manufacturing sector in the euro area getting closer to being back to normal.

Chart D Equipment shortages cited as a production constraint in manufacturing

(percentages)



Sources: European Commission and ECB calculations.
Note: The latest observations are for the third quarter of 2010 (July).

2 For a closer look at investment and capacity utilisation, see Box 5, entitled “Business investment, capacity utilisation and demand”, in the April 2010 issue of the Monthly Bulletin.

3 See Box 5, entitled “Integrated euro area accounts for the first quarter of 2010”, in the August 2010 issue of the Monthly Bulletin.