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Economic Outlook 2006/2007

Output growth above long-term average for all Orgalime sectors in 2006 - Growth for 4th consecutive year expected in 2007, but at lower rate.

Orgalime's economists are forecasting that output in the European engineering industry, the largest EU manufacturing sector, will rise by some 4.4 percent in 2006. First estimates also expect 2007 to be positive, with output expected to rise by 2.5 percent. The business environment in Europe, with its rising interest rates, tighter fiscal policies, higher input prices and an ever more constraining legal framework point to a deceleration of growth in 2007. As a result, employment in the industry, now standing at some 10 million EU wide is unlikely to change substantially this year and may drop slightly in 2007.

"2006 looks like being a good year for our industry – much better than we initially expected. If last year growth in our industry was essentially export driven, today we are seeing investment growth in the EU. Whether this continues or not will very much depend on the framework conditions of our clients, which are to a large extent all manufacturing sectors" said Adrian Harris, Orgalime Secretary General. "Notwithstanding the European Commission's focus on industrial policy, we are seeing, at best, muted support for the manufacturing sector in many of the countries and some of the other European Institutions."

In most of the EU, growth has accelerated swiftly this year and, with it investment, thereby providing a boost to the engineering industry. In terms of the whole economy, the Scandinavian countries, most of the new EU Member States, Spain, Ireland and the UK are performing well. There is also some growth in other major economies such as Germany and France where domestic demand and especially investment growth developed dynamically. In addition to a stronger domestic demand in Europe, major export markets in Asia and America are also showing healthy growth which is boosting demand for EU engineering products.

A key factor for the engineering industry is overall demand of investment goods, which has risen during 2006: in the second quarter of the year alone, fixed investment in the EU25 showed an estimated growth rate of more than 5 percent, an increase not seen since mid 2000. Demand has been satisfactory as well as the engineering industry's own capital formation, which is expected to grow more than 9 percent this year.

Many business cycle indicators for the engineering industry are positive at present: order intake is generally very satisfactory and inventories of finished goods are low. However, in some countries growth is being constrained by the lack of skilled personnel, which is a rising problem. Some factors point to a deceleration of growth for European engineering industry next year: most central banks in Europe and elsewhere have started to raise interest rates in order to reduce expected inflation which will eventually have a knock on effect on the industry. Tighter economic policy in many countries to meet the EU Stability and Growth pact criteria will also have an impact.

Engineering industry by major branch:

The metal articles industry, which to a large extent is a components industry with many suppliers of intermediate products, is expected to achieve a growth rate of 3 percent this year, well above the long-term average growth of 1.7 percent. All Orgalime members in the metal goods sector are expected to register positive growth in output in 2006. Activity has risen markedly in some of the Nordic countries whereas Italy, France and the UK report below average

growth for the sector. Exports have been a key factor supporting growth in 2006, with total exports reaching 7 percent in volume. At a sub sector level, metal containers, metal tanks and traditional treatment and coating of metals are performing well, while some countries are still reporting a high pressure on suppliers to the automotive sector. In 2007, moderate growth of output at the level of the sector's long term average is expected.

The machinery and equipment industry is expected to see an increase in output of 4.8 percent in 2006, some 2 percent above the long-term average for the industry. A rather strong growth of extra-EU exports of almost 10 percent has been one of the key factors contributing to the growth of the sector. Intra EU trade also grew by some 6.8 percent in 2006 due to rather strong demand of investment goods throughout Europe. In Austria, Finland, Holland and Spain the sector grew strongly in 2006. All sub-sectors are doing well, with the machine tool and mechanical power machinery performing particularly strongly. After more than 2 years of strong demand in investment goods worldwide, new capacity and modern technology has been installed in many companies and therefore demand for this sector's goods is now expected to level off. The growth in extra-EU trade is expected to decelerate fairly rapidly and the EU engineering industries' own capital formation is expected to only reach a modest growth of 3 percent in 2007. As a result, growth in output is expected to slow in 2007 to some 2.3 percent.

The electrical-, instrument and ICT- engineering industry is expected to reach an output growth of some 5.1 percent in 2006. Finland is forecast to achieve double-digit growth rates in 2006 and output will grow considerably in Denmark, Austria, Switzerland, Spain and above average in Sweden, whereas output growth is below average in Slovenia, Norway, UK, the Netherlands, Belgium and Italy. Intra EU trade has been buoyant in 2006 and is expected to grow by 9.3 percent in volume for the sector as a whole.

The outlook for 2007 is still rather positive for the sector as a whole and the volume of production is expected to expand further, but at a slightly lower rate than in 2006 - by 3.3 percent. Some countries expect the growth rate to be unchanged, but the majority expect to see a slowdown or even a significant decrease in growth.

Ends

Summary of Production in European Engineering Industry by Orgalime Sectors

Estimated/ forecast percentage change in volume year on year (NACE 28 to 33)

| Sector of the Industry | 2006 estimate | 2007 forecast |
|---|----------------------|----------------------|
| Metal Articles | 3.0 | 1.6 |
| Mechanical Engineering | 4.8 | 2.3 |
| Electrical, Electronic Engineering, ICT and Instruments | 5.1 | 3.3 |
| Total European Engineering | 4.4 | 2.5 |

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Orgalime, the European Engineering Industries Association, speaks for 36 trade federations representing some 130,000 companies in the mechanical, electrical, electronic and metalworking industries of 24 European countries. The industry employs some 10 million people in the EU and in 2005 accounted for some €1,598 billion of annual output. The industry not only represents more than one quarter of the output of manufactured products but also a third of the manufactured exports of the European Union.

ORGALIME THE EUROPEAN ENGINEERING INDUSTRIES ASSOCIATION

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