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 **ÖSTERREICHISCHES INSTITUT FÜR
WIRTSCHAFTSFORSCHUNG**

**Measures of Cyclical Stabilisation
Showing Early Effects
Economic Outlook for 2009 and 2010**

June 2009

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Austrian Institute of Economic Research

Abstract

In the wake of the international economic crisis, Austrian exports have fallen precipitously year-on-year since early 2009. Yet, the fiscal counter-action taken in the industrialised countries is showing early positive effects. Not only in Austria, but in the entire euro area and the USA, business surveys suggest a stabilisation of demand and output as from the middle of this year. Nevertheless, activity in Austria will once more decline in the second quarter as compared with the previous period. The cyclical pattern is thus broadly in line with the one underlying the previous WIFO forecast of last spring. However, since results for the first quarter turned out weaker than expected, WIFO is taking down its projection for GDP for the whole of 2009 to -3.4 percent. The forecast of a stabilisation in 2010 with a growth rate of 0.5 percent is being maintained.

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Measures of Cyclical Stabilisation Showing Early Effects

Economic Outlook for 2009 and 2010

In the wake of the international economic crisis, Austrian exports have fallen precipitously year-on-year since early 2009. Yet, the fiscal counter-action taken in the industrialised countries is showing early positive effects. Not only in Austria, but in the entire euro area and the USA, business surveys suggest a stabilisation of demand and output as from the middle of this year. Nevertheless, activity in Austria will once more decline in the second quarter as compared with the previous period. The cyclical pattern is thus broadly in line with the one underlying the previous WIFO forecast of last spring. However, since results for the first quarter turned out weaker than expected, WIFO is taking down its projection for GDP for the whole of 2009 to –3.4 percent. The forecast of a stabilisation in 2010 with a growth rate of 0.5 percent is being maintained.

Edging down by 0.4 percent in the fourth quarter 2008 from the previous period, activity in Austria proved more resilient than the euro area average (–1.8 percent) and notably Germany (–2.2 percent). Yet, in early 2009 merchandise exports took a sharp setback also in Austria, and the cyclical downturn gathered momentum. Exacerbated also by one-off factors, real GDP fell by 2.6 percent quarter-on-quarter, at the same pace as in the euro area (–2.5 percent). The updated WIFO forecast maintains the profile of a deceleration of the downward trend in the second quarter, coming to a halt towards the end of the year. This is confirmed by the results from the latest round of the WIFO business survey where firms reported in May for the second time in a row that their situation is down at a low, but with no further worsening expected for the months to come. This is broadly consistent with sample results for Germany, the whole euro area and the USA.

For the second quarter, WIFO therefore projects a smaller decline of GDP than the one seen in the first quarter. In the third quarter, activity is likely to fall no further but stagnate at the level of the previous period. By the end of 2009, growth should tenta-

tively pick up under the impact of the massive fiscal stimulus introduced worldwide. While the measures taken will stabilise economic activity, WIFO does not yet expect a self-sustained economic upturn. Import demand from the USA and from the countries in east-central Europe remains too weak as to provide lasting incentives for the euro area economies. On annual average 2009, domestic output will therefore remain 3.4 percent below the year-earlier level, followed by a modest 0.5 percent pickup in 2010.

The global recession leads to a fall in Austrian merchandise exports by around 15 percent in volume this year. Also tourism exports will recede, by a projected 6.5 percent. While goods exports should start heading up in 2010 (+0.7 percent), tourism exports are set to edge down once again, by 1 percent.

Private household demand is proving resilient to a high degree. Despite lower gains in per-capita gross earnings along with declining employment, a squeeze in income from private financial assets and a looming further rise in unemployment, private consumption will edge up by 0.2 percent in volume this year. This is primarily the result of fiscal expansion. Thanks to the cut in income tax, real income per capita will increase by 3.3 percent net this year, distinctly faster than the +1.8 percent in gross terms.

In the face of the recession, companies hold back on their investment projects. Gross fixed capital formation will contract by almost 6 percent in volume in 2009, with demand for machinery and equipment falling by 11 percent, much more strongly than that for new construction (-1.5 percent). Investment is unlikely to pick up even by 2010.

The slump in foreign demand is hitting notably the manufacturing sector whose net output will shrink by 10 percent in volume this year. Meanwhile, the downturn has reached also the service branches whose output usually lags in the business cycle. Distribution, tourism, transport, financial and real estate services will suffer non-negligible losses in 2009. Only public and personal services will still post small output gains.

Inflation is still receding on an annual basis. In May, consumer prices remained virtually constant (+0.3 percent) and the coming months may see even slightly negative rates. For the whole year 2009, WIFO expects headline inflation at a rate of 0.5 per-

cent. In 2010, the rebound in oil prices will push inflation up to 1.2 percent. The cyclically sensitive rate of core inflation is projected to moderate from 1.3 percent in 2009 to 1.1 percent. WIFO considers the dangers of either a sustained period of deflation in the wake of the global recession or of high inflation as a consequence of strong monetary expansion as extremely low.

Given the unfavourable business trend, WIFO is also revising down its labour market outlook. In 2009, the number of people in dependent active employment will fall by 50,400 or 1.5 percent from the previous year. Despite the severe crisis the decline remains nevertheless contained, which is owed largely to government measures to facilitate the recourse to short-time work. In 2010, another 35,000 jobs will be lost on aggregate (–1.1 percent). The number of unemployed will go up by 58,400 this year and a further 39,000 in 2010. The jobless rate as calculated on conventional national definitions will ratchet up to 7.4 percent and 8.5 percent in 2009 and 2010, respectively.

Vienna, 24 June 2009.

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WIFO
Projections - June 2009

Main results

Percentage changes from previous year

		2005	2006	2007	2008	2009	2010
GDP							
Volume		+ 2.9	+ 3.4	+ 3.1	+ 1.8	- 3.4	+ 0.5
Value		+ 5.0	+ 5.3	+ 5.3	+ 4.2	- 1.9	+ 1.4
Manufacturing¹, volume		+ 4.8	+ 9.6	+ 5.5	+ 3.3	- 10.0	± 0.0
Wholesale and retail trade, volume		+ 2.2	- 1.0	+ 1.5	- 0.1	- 2.5	+ 0.5
Private consumption expenditure, volume		+ 2.6	+ 2.4	+ 1.0	+ 0.8	+ 0.2	+ 0.5
Gross fixed investment, volume		+ 2.4	+ 2.6	+ 4.7	+ 1.8	- 5.9	- 1.0
Machinery and equipment ²		+ 5.5	+ 0.9	+ 6.8	+ 2.0	- 11.0	- 1.0
Construction		- 0.4	+ 4.2	+ 2.8	+ 1.7	- 1.5	- 1.0
Exports of goods³							
Volume		+ 3.2	+ 6.8	+ 8.7	+ 0.9	- 15.1	+ 0.7
Value		+ 5.4	+ 9.5	+ 10.5	+ 2.3	- 16.5	+ 1.4
Imports of goods³							
Volume		+ 2.9	+ 4.1	+ 8.0	+ 1.7	- 11.2	+ 0.4
Value		+ 5.9	+ 8.0	+ 9.6	+ 4.3	- 13.6	+ 2.0
Current balance	€ bn	+ 4.92	+ 7.26	+ 8.41	+ 9.82	+ 2.31	+ 2.66
	as a percentage of GDP	+ 2.0	+ 2.8	+ 3.1	+ 3.5	+ 0.8	+ 0.9
Long-term interest rate⁴	percent	3.4	3.8	4.3	4.3	3.7	3.9
Consumer prices		+ 2.3	+ 1.5	+ 2.2	+ 3.2	+ 0.5	+ 1.2
Unemployment rate							
Eurostat definition ⁵	percent	5.2	4.8	4.4	3.8	5.3	5.8
National definition ⁶	percent	7.3	6.8	6.2	5.8	7.4	8.5
Persons in active dependent employment⁷		+ 1.0	+ 1.7	+ 2.1	+ 2.4	- 1.5	- 1.1
General government financial balance							
according to Maastricht definition							
as a percentage of GDP		- 1.6	- 1.6	- 0.5	- 0.4	- 4.3	- 5.8

¹ Value added, including mining and quarrying. ² Including other products. ³ According to Statistics Austria.

⁴ 10-year central government bonds (benchmark). ⁵ According to Eurostat Labour Force Survey. ⁶ Public Employment Service Austria, percent of total labour force excluding self employed. ⁷ Excluding parental leave and military service.

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Projections - June 2009

Key policy indicators

	2005	2006	2007	2008	2009	2010
Fiscal policy						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 1.6	- 1.6	- 0.5	- 0.4	- 4.3	- 5.8
according to National accounts	- 1.7	- 1.7	- 0.7	- 0.5	- 4.3	- 5.8
General government primary balance	+ 1.3	+ 1.1	+ 2.2	+ 2.1	- 1.3	- 2.7
Monetary policy						
	Percent					
3-month interest rate	2.2	3.1	4.3	4.6	1.4	1.3
Long-term interest rate ¹	3.4	3.8	4.3	4.3	3.7	3.9
	Percentage changes from previous year					
Effective exchange rate						
Nominal	- 0.7	+ 0.2	+ 1.1	+ 1.2	+ 1.0	± 0.0
Real	- 1.0	- 0.5	+ 0.7	+ 0.6	+ 0.7	± 0.0

¹ 10-year central government bonds (benchmark).

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World economy

Percentage changes from previous year

	2005	2006	2007	2008	2009	2010
Real GDP						
World	+ 4.5	+ 5.1	+ 5.2	+ 2.5	- 1.5	+ 1.8
Total OECD	+ 2.7	+ 3.1	+ 2.7	+ 0.9	- 3.5	+ 0.3
USA	+ 2.9	+ 2.8	+ 2.0	+ 1.1	- 2.7	+ 0.5
Japan	+ 1.9	+ 2.0	+ 2.4	- 0.7	- 5.5	+ 0.5
EU 27	+ 2.0	+ 3.1	+ 2.9	+ 0.9	- 4.0	+ 0.3
Euro area 16	+ 1.7	+ 2.9	+ 2.7	+ 0.8	- 4.2	+ 0.3
Germany	+ 0.8	+ 3.0	+ 2.5	+ 1.3	- 6.0	+ 0.5
New member states ¹	+ 4.7	+ 6.5	+ 6.0	+ 4.0	- 3.0	+ 1.0
China	+ 10.4	+ 11.6	+ 13.0	+ 9.0	+ 6.0	+ 7.0
World trade, volume	+ 7.9	+ 9.5	+ 7.1	+ 2.5	- 15.0	+ 1.0
Market growth²	+ 7.8	+ 11.1	+ 7.6	+ 3.5	- 15.0	+ 0.5
Primary commodity prices						
HWWI Index, total	+ 28.5	+ 19.7	+ 3.7	+ 22.4	- 33	+ 18
Excluding energy	+ 5.6	+ 22.0	+ 9.5	+ 15.6	- 24	+ 5
Crude oil prices						
Brent, USD per barrel	54.4	65.1	72.5	97.0	60	75
Exchange rate						
USD per euro	1.245	1.256	1.371	1.471	1.45	1.45

¹ Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania.

² Real import growth of trading partners weighted by Austrian export shares.

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Projections - June 2009

Private consumption, income and prices

	2005	2006	2007	2008	2009	2010
Percentage changes from previous year, volume						
Private consumption expenditure	+ 2.6	+ 2.4	+ 1.0	+ 0.8	+ 0.2	+ 0.5
Durables	+ 5.9	+ 7.0	+ 6.2	- 1.0	- 2.9	- 0.7
Non-durables and services	+ 2.2	+ 1.9	+ 0.4	+ 1.0	+ 0.5	+ 0.6
Household disposable income	+ 3.1	+ 3.5	+ 2.2	+ 0.7	+ 0.9	+ 0.1
Household saving ratio						
As a percentage of disposable income	9.8	10.8	11.7	11.5	12.0	11.7
Percentage changes from previous year						
Direct lending to domestic non-banks¹	+ 4.7	+ 4.5	+ 3.6	+ 7.4	+ 2.2	+ 3.2
Inflation rate						
National	2.3	1.5	2.2	3.2	0.5	1.2
Harmonised	2.1	1.7	2.2	3.2	0.5	1.3
Core inflation ²	1.5	1.3	1.9	2.4	1.3	1.1

¹ End of period.

² Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

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Projections - June 2009

Productivity

Percentage changes from previous year

	2005	2006	2007	2008	2009	2010
Total economy						
Real GDP	+ 2.9	+ 3.4	+ 3.1	+ 1.8	- 3.4	+ 0.5
Employment ¹	+ 1.1	+ 1.5	+ 1.7	+ 1.9	- 1.2	- 0.7
Productivity (GDP per employment)	+ 1.7	+ 1.9	+ 1.3	- 0.1	- 2.2	+ 1.2
Manufacturing						
Production ²	+ 4.8	+ 9.9	+ 5.5	+ 3.4	- 10.0	± 0.0
Employees ³	- 0.8	+ 0.2	+ 2.6	+ 1.7	- 6.3	- 3.0
Productivity per hour	+ 6.2	+ 9.5	+ 3.2	+ 2.1	- 2.5	+ 3.1
Working hours per day per employee ⁴	- 0.6	+ 0.2	- 0.3	- 0.5	- 1.5	± 0.0

¹ Dependent and self-employed according to National Accounts definition.

² Value added, volume.

³ According to Federation of Austrian Social Security Institutions.

⁴ According to 'Konjunkturerhebung' of Statistics Austria.

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Earnings and international competitiveness

Percentage changes from previous year

	2005	2006	2007	2008	2009	2010
Gross earnings per employee ¹	+ 2.4	+ 3.2	+ 2.3	+ 2.9	+ 2.3	+ 1.2
Gross real earnings per employee ¹	+ 0.1	+ 1.4	+ 0.1	- 0.0	+ 1.8	± 0.0
Net real earnings per employee ¹	+ 0.5	+ 1.2	- 0.1	- 0.4	+ 3.3	- 0.3
<i>Total economy</i>						
Unit labour costs	+ 0.7	+ 1.1	+ 0.8	+ 3.0	+ 4.9	+ 0.0
<i>Manufacturing</i>						
Unit labour costs	- 0.9	- 4.4	- 0.6	+ 1.4	+ 3.7	- 1.3
Effective exchange rate - manufactures						
Nominal	- 0.6	+ 0.2	+ 1.2	+ 1.1	+ 1.1	± 0.0
Real	- 0.9	- 0.4	+ 0.8	+ 0.6	+ 0.8	± 0.0

¹ Employees according to National Accounts definition.

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Labour market

Changes from previous year (1,000^s)

		2005	2006	2007	2008	2009	2010
Demand for labour							
Persons in active employment ¹		+ 37.2	+ 54.9	+ 64.8	+ 86.0	- 54.4	- 39.0
Employees ²		+ 31.9	+ 51.5	+ 65.5	+ 76.7	- 50.4	- 35.0
<i>Percentage changes from previous year</i>		+ 1.0	+ 1.7	+ 2.1	+ 2.4	- 1.5	- 1.1
Nationals		+ 20.0	+ 35.0	+ 43.6	+ 53.2	- 43.8	- 31.2
Foreign workers		+ 11.9	+ 16.5	+ 21.9	+ 23.5	- 6.6	- 3.8
Self-employed ³		+ 5.3	+ 3.4	- 0.7	+ 9.3	- 4.0	- 4.0
Labour supply							
Population of working age	(15 to 64 years)	+ 13.4	+ 12.8	+ 15.5	+ 27.7	+ 20.2	+ 27.5
	(15 to 59 years)	+ 46.5	+ 47.3	+ 17.1	+ 17.6	+ 13.6	+ 13.7
Labour force ⁴		+ 45.9	+ 41.4	+ 47.9	+ 76.0	+ 4.0	± 0.0
Surplus of labour							
Registered unemployed ⁵		+ 8.8	- 13.5	- 16.9	- 10.0	+ 58.4	+ 39.0
	1,000 ^s	252.7	239.2	222.2	212.3	270.7	309.7
Unemployed persons in training	1,000 ^s	48.6	57.5	52.7	50.5	61.8	67.8
Unemployment rate							
Eurostat definition ⁶	percent	5.2	4.8	4.4	3.8	5.3	5.8
Percent of total labour force ⁵	percent	6.5	6.1	5.6	5.2	6.7	7.6
National definition ^{5,7}	percent	7.3	6.8	6.2	5.8	7.4	8.5
Employment rate							
Persons in active employment ^{1,8}	percent	63.0	63.9	64.8	66.0	64.8	63.8
Total employment (Eurostat) ^{6,8}	percent	68.6	70.2	71.4	72.1	70.9	70.0

¹ Excluding parental leave and military service. ² According to Federation of Austrian Social Security Institutions.

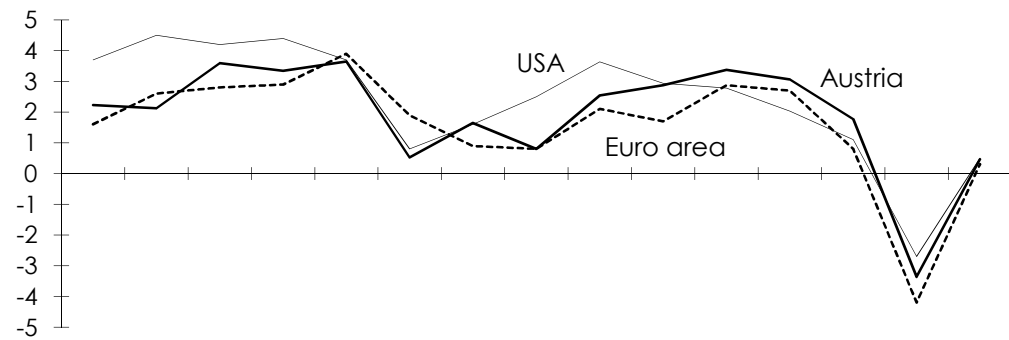
³ According to WIFO. ⁴ Economically active employment plus unemployment.

⁵ According to Public Employment Service Austria ⁶ According to Eurostat Labour Force Survey.

⁷ Percent of total labour force excl. self-employed. ⁸ Percent of population of working age (15 to 64 years).

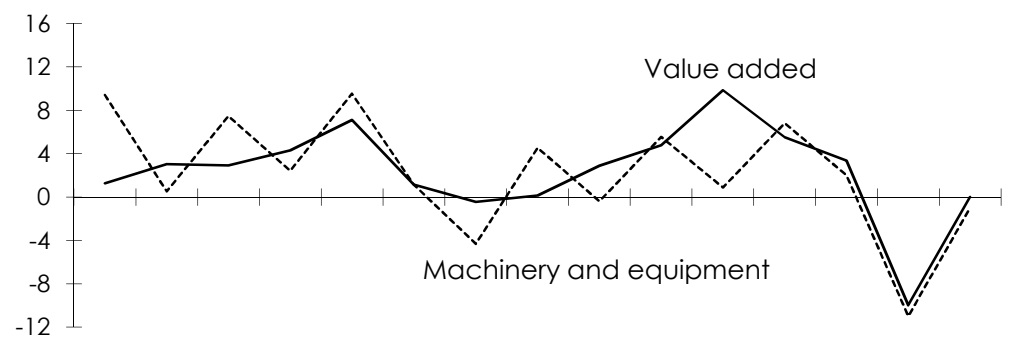
Growth of real GDP

Percent



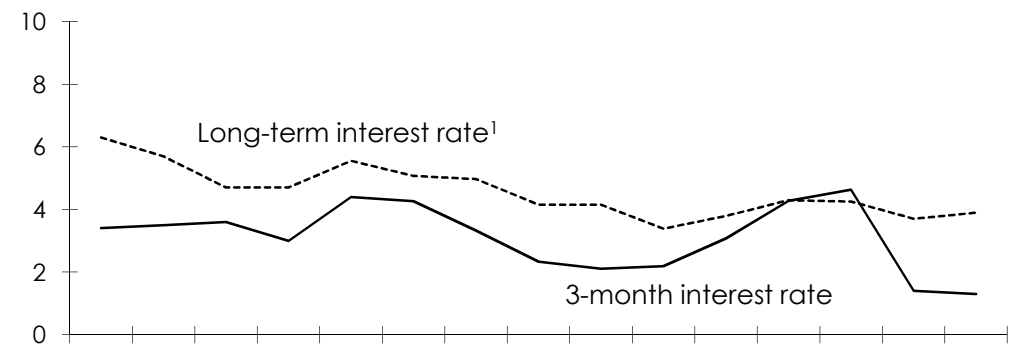
Manufacturing and investment

Percentage changes from previous year, volume



Short-term and long-term interest rates

Percent



Trade

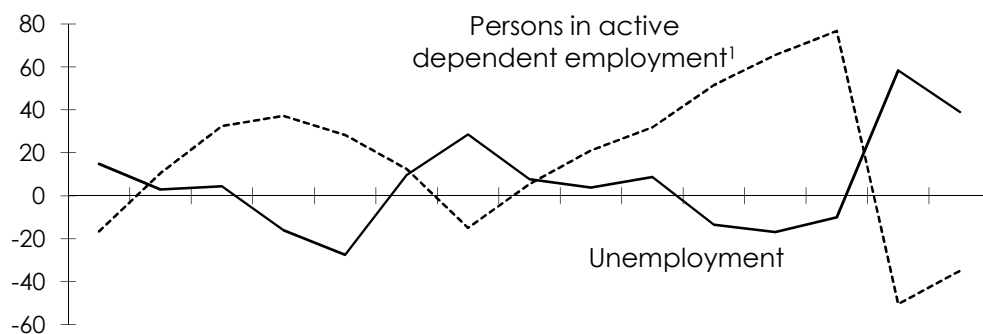
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

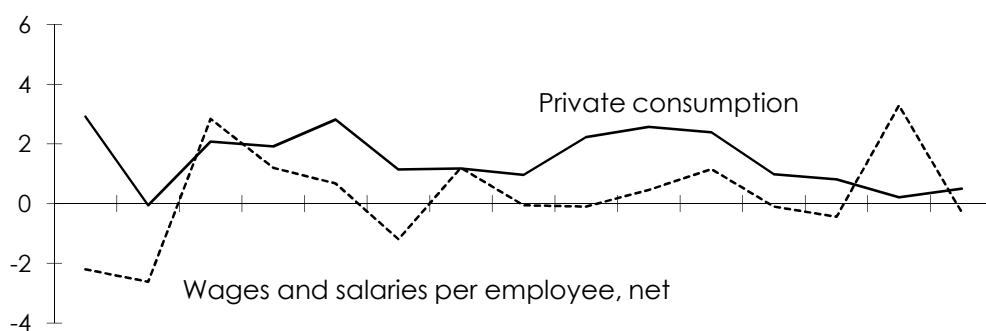
Employment and unemployment

1,000^s from previous year



Consumption and income

Percentage changes from previous year, volume



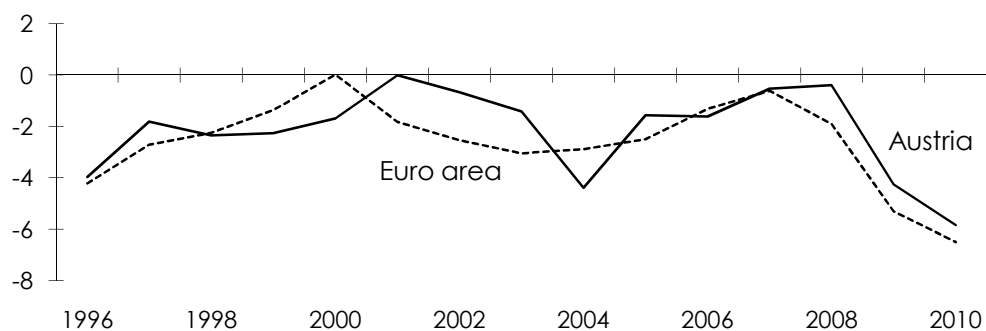
Inflation and unit labour costs

Percentage changes from previous year



General government financial balance

As a percentage of GDP



¹ Excluding parental leave, military service, and unemployed persons in training.