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1030 WIEN, ARSENAL, OBJEKT 20  
TEL. 798 26 01 • FAX 798 93 86

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WIRTSCHAFTSFORSCHUNG**

**Upswing with Stronger Momentum,  
but Subject to Higher Risks**

**Economic Outlook for 2011 and 2012**

Stefan Ederer

**April 2011**



# Upswing with Stronger Momentum, but Subject to Higher Risks

## Economic Outlook for 2011 and 2012

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Austrian Institute of Economic Research

### **Abstract**

The cyclical upswing in Austria continues. Driven by the swift expansion of global activity, exports are posting strong gains. Meanwhile, the momentum is being transmitted to private investment which is set to rise substantially over the forecast period. Short-term indicators suggest that the positive trend will persist. WIFO expects Austria's GDP to increase by 2.5 percent in 2011 and 2.0 percent in 2012. The major risks for the upswing currently derive from the drift in commodity and energy prices, the disaster in Japan and the continued fragility of the international financial system.

Please refer to: [Stefan.Ederer@wifo.ac.at](mailto:Stefan.Ederer@wifo.ac.at)

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# Upswing with Stronger Momentum, but Subject to Higher Risks

## Economic Outlook for 2011 and 2012

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*The cyclical upswing in Austria continues. Driven by the swift expansion of global activity, exports are posting strong gains. Meanwhile, the momentum is being transmitted to private investment which is set to rise substantially over the forecast period. Short-term indicators suggest that the positive trend will persist in the first half of 2011 before moderating somewhat in parallel with developments abroad, under the impact of rising commodity and energy prices and a more restrictive policy stance in both the industrialised and the emerging economies. Further ahead, demand and output growth is set to regain momentum. For Austria, WIFO expects GDP to increase by 2.5 percent in 2011 and 2.0 percent in 2012. The major risk for the upswing currently derives from the drift in commodity and energy prices which may have a substantial impact on the world economy.*

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Growth of the world economy accelerated markedly towards the end of 2010. After a period of stagnation, world trade posted substantial gains. Notably the emerging economies in Asia raised their imports significantly, thereby providing the major impetus for the expansion of demand and output worldwide. Although policy in China and other developing countries tries to avoid cyclical overheating and while rising commodity and energy prices may dampen economic activity, the developing Asian economies will continue to provide important incentives for growth of the world economy. Economies in Latin America, for their part, benefit notably from higher prices for food and other raw materials and should also enjoy lively growth. However, strong capital inflows have recently driven up their exchange rates, weighing on exports and adding to risks of financial market turbulence. Overall, world economic growth should stay robust in the first half of 2011. Thereafter, the pace should moderate somewhat under the impact of rising commodity and energy prices and a more restrictive policy stance in many countries. In 2012, global demand and output growth is set to regain momentum.

In the USA, growth is surprisingly strong. Overall demand is driven by exports, investment and expenditure on durable consumer goods. The persistent weakness of the dollar and the sustained expansionary stance of monetary and fiscal policy are supportive to domestic activity. Weak spots are the real estate market and high indebtedness of both the private and the public sector, whereas the improvement on the labour market should provide positive incentives.

The euro area economy is expected to expand only at a moderate pace up to the forecast horizon. Also, the gap between countries enjoying buoyant growth and those caught in crisis and stagnation will become still wider. Germany and countries with close links to the German economy will continue to benefit from the international upturn. Ireland and several countries in southern Europe will, however, remain in recession, which dampens the prospects for the EU overall.

The Austrian economy will continue its cyclical upswing. Lively activity in Germany gave strong impetus to Austrian exports in 2010. In this way, Austrian manufacturing industry benefited indirectly from the booming emerging market economies. At the same time, the pick-up of investment in machinery and equipment over the last three quarters indicates that the stimulus from exports is being transmitted to domestic capital formation. This trend is likely to persist, as cyclical indicators suggest strong economic growth for the first half of 2011. In the latter part of the year, the expansion should lose some momentum, in parallel to the international cyclical profile. For the whole year 2011, WIFO expects GDP growth at 2.5 percent, followed by an annual average 2 percent in 2012.

Due to the rise in raw material and energy prices, consumer price inflation will accelerate markedly to an annual average rate of 2.8 percent in 2011, of which 0.4 percentage points are accounted for by higher indirect taxes decided in the context of fiscal consolidation. These effects will largely fade out in 2011, whereas wage increases may turn out somewhat higher than in 2011. Overall inflation in 2012 is projected at an average 2.4 percent.

Private consumption will follow only a moderate upward trend over the forecast period, given the limited income gains. Higher inflation will even make for a decline in real per-capita earnings in 2011, turning around only in 2012. On the labour market, however, the cyclical recovery will be clearly visible, with strong advances in em-

ployment and declining unemployment, even if the jobless rate will stay above its pre-crisis level: according to national definitions, 6.3 percent of the dependent labour force will be looking for a job by 2012; in the Eurostat definition, 4.0 percent of the total labour force will be out of work.

Lively economic activity and the measures of fiscal consolidation will improve the general government balance. Yet, the statistical inclusion of federal government subsidies to the Austrian Railways (ÖBB) for infrastructure investment into current expenditure will increase the official government deficit. Anticipating the decision on this change in accounting, the general government deficit is projected at 3.4 percent of GDP in 2011 and at a ratio of 3 percent in 2012.

The highest cyclical risks are currently considered to derive from the increase in commodity and energy prices, from the disaster in Japan and from the persistent vulnerability of the international financial system. The present forecast assumes that oil prices and world market quotations for food items will move to a downward path in the course of this year. Further hikes in prices for raw materials, possibly triggered by a deepening crisis in the Arab world, may weigh heavily on the international business cycle upturn. Likewise, the consequences of the natural disaster and the destruction of the nuclear power plants in Japan cannot be fully assessed as yet. Should the latest increase in interest rates for government bonds in the euro area continue and spread to other countries, the situation of government finances in these countries may become more critical and compel the authorities to take further consolidation measures. This could not only dampen further aggregate demand in the euro area, but also add to the fragility of the financial system and potentially jeopardise the stability of Monetary Union.

Vienna, 30 March 2011

*For more details please contact Stefan Ederer, Tel. (1) 798 26 01/464,  
[Stefan.Ederer@wifo.ac.at](mailto:Stefan.Ederer@wifo.ac.at)*

## Methodological Notes and Short Glossary

### *Period comparisons*

Time-series comparisons with the previous period, e.g., the previous quarter, are adjusted for seasonal effects. They also include effects that result from a different number of working days in the period (e.g., Easter). In the text, reference is made to "seasonally and working day adjusted changes".

The phrase "changed compared with a year before . . .", on the other hand, describes a change compared with the same period a year before and refers to unadjusted time series.

The analysis of the seasonally and working day adjusted development provides more precise information about the actual course of economic activity and shows turning points sooner. However, the data are subject to additional revisions as seasonal adjustment is based on statistical methods.

### *Real and nominal values*

In principle, the values shown must be understood as real values, i.e., adjusted for price effects. Whenever values are shown as nominal values (e.g., foreign trade statistics), this is specifically mentioned.

### *Production Sector*

This term comprises the NACE-2008 sections B, C and D (Mining and Quarrying, Manufacturing, Energy Supply) and is here used in an international comparison.

### *Inflation, CPI und HICP*

The inflation rate measures changes in consumer prices compared with a year before. The Consumer Price Index (CPI) is a measure of national inflation. The Harmonised Index of Consumer Prices (HICP) is the basis for comparable measurement of inflation in the EU and for the evaluation of price stability in the euro area (see <http://www.statistik.at/>).

Core inflation as a monetary policy indicator is not clearly defined. WIFO follows the common practice of using the inflation rate excluding the product categories unprocessed food and energy for core inflation. Thus just under 87 percent of the goods and services contained in the consumer price index (CPI 2010) are included in the calculation of core inflation.

### *WIFO Business Cycle Survey and WIFO Investment Survey*

The WIFO business cycle survey is a monthly survey in which around 1,100 Austrian firms are asked to assess their current and future economic situation. The WIFO investment survey is conducted twice a year, asking companies about their investment activity (<http://www.itkt.at/>). The indicators are balances between the positive and negative responses expressed as a percentage of the total number of firms sampled.

### *Unemployment rate*

Austrian national definition: The number of persons registered as job seekers with the Public Employment Service expressed as a percentage of the dependent labour force. Labour force is the sum of the unemployed and the persons in dependent employment (measured in standard employment relationships). Database: registrations with the Public Employment Service (AMS) and Association of Austrian social insurance agencies.

Definition according to ILO and EUROSTAT: Any person who is not gainfully employed and is actively seeking work is considered unemployed. Gainfully employed persons comprise all persons who during the reference week worked for at least one hour in a self-employed capacity or in paid employment. Persons receiving child-care benefit and apprentices are classified as gainfully employed, whereas persons in military service or persons carrying out alternative service are not. The unemployment rate is the number of unemployed persons expressed as a percentage of the total labour force (unemployed persons plus gainfully employed persons). Database: data from household surveys ("Mikrozensus").

### *Terms used in connection with the national definition of the unemployment rate*

Persons in training: Persons who at a set date are enrolled in AMS (Public Employment Service) training programmes. When calculating the unemployment rate, their number is not taken into account either in the denominator or in the numerator.

Persons in dependent active employment: "Persons in dependent employment" include persons receiving child-care benefit, as well as persons in military service or persons carrying out alternative service with a valid employment contract. By deducting their number one arrives at the number of "persons in dependent active employment".

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Projections - March 2011

## Main results

Percentage changes from previous year

		2007	2008	2009	2010	2011	2012
<b>GDP</b>							
Volume		+ 3.7	+ 2.2	- 3.9	+ 2.0	+ 2.5	+ 2.0
Value		+ 5.9	+ 4.1	- 3.1	+ 3.5	+ 4.5	+ 4.1
<b>Manufacturing<sup>1</sup>, volume</b>		+ 8.5	+ 3.5	- 14.0	+ 6.6	+ 7.0	+ 5.5
<b>Wholesale and retail trade, volume</b>		+ 2.0	+ 0.9	- 1.4	+ 2.8	+ 1.3	+ 1.1
<b>Private consumption expenditure, volume</b>		+ 0.7	+ 0.5	+ 1.3	+ 1.0	+ 1.1	+ 1.1
<b>Gross fixed investment, volume</b>		+ 3.9	+ 4.1	- 8.8	- 1.3	+ 2.6	+ 2.7
Machinery and equipment		+ 6.6	+ 7.5	- 14.5	+ 1.8	+ 5.5	+ 4.5
Construction		+ 1.6	+ 1.6	- 6.0	- 3.4	± 0.0	+ 1.0
<b>Exports of goods<sup>2</sup></b>							
Volume		+ 9.0	+ 0.3	- 18.7	+ 12.7	+ 8.8	+ 8.0
Value		+ 10.5	+ 2.5	- 20.2	+ 16.5	+ 11.0	+ 9.1
<b>Imports of goods<sup>2</sup></b>							
Volume		+ 7.6	+ 0.2	- 15.1	+ 10.9	+ 7.0	+ 6.7
Value		+ 9.6	+ 4.7	- 18.4	+ 16.3	+ 10.0	+ 8.3
<b>Current balance</b>	€ bn	+ 9.62	+ 13.76	+ 7.98	+ 9.01	+ 11.12	+ 13.22
	as a percentage of GDP	+ 3.5	+ 4.9	+ 2.9	+ 3.2	+ 3.7	+ 4.3
<b>Long-term interest rate<sup>3</sup></b>	percent	4.3	4.4	3.9	3.2	3.6	3.8
<b>Consumer prices</b>		+ 2.2	+ 3.2	+ 0.5	+ 1.9	+ 2.8	+ 2.4
<b>Unemployment rate</b>							
Eurostat definition <sup>4</sup>	percent	4.4	3.8	4.8	4.4	4.1	4.0
National definition <sup>5</sup>	percent	6.2	5.9	7.2	6.9	6.4	6.3
<b>Persons in active dependent employment<sup>6</sup></b>		+ 2.1	+ 1.7	- 1.5	+ 0.8	+ 1.6	+ 0.9
<b>General government financial balance</b>							
according to Maastricht definition							
	as a percentage of GDP	- 0.4	- 0.5	- 3.5	- 4.1	- 2.9	- 2.6
	as a percentage of GDP <sup>7</sup>	.	.	.	.	- 3.4	- 3.0

<sup>1</sup> Value added, including mining and quarrying. <sup>2</sup> According to Statistics Austria. <sup>3</sup> 10-year central government bonds (benchmark). <sup>4</sup> According to Eurostat Labour Force Survey. <sup>5</sup> Public Employment Service Austria, percent of total labour force excluding self employed. <sup>6</sup> Excluding parental leave and military service.

<sup>7</sup> Calculated considering financial contributions to the Austrian Federal Railways (ÖBB) for compensation of infrastructural investments as government spendings.

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Projections - March 2011

### Key policy indicators

	2007	2008	2009	2010	2011	2012
<b>Fiscal policy</b>						
	As a percentage of GDP					
<b>General government financial balance</b>						
according to Maastricht definition	- 0.4	- 0.5	- 3.5	- 4.1	- 2.9	- 2.6
according to Maastricht definition <sup>1</sup>	.	.	.	.	- 3.4	- 3.0
<b>General government primary balance</b>						
<b>General government primary balance</b>	+ 2.3	+ 2.1	- 0.8	- 1.4	- 0.3	+ 0.1
<b>General government primary balance<sup>1</sup></b>	.	.	.	.	- 0.8	- 0.4
<b>Monetary policy</b>						
	Percent					
3-month interest rate	4.3	4.6	1.2	0.8	1.3	2.3
Long-term interest rate <sup>2</sup>	4.3	4.4	3.9	3.2	3.6	3.8
	Percentage changes from previous year					
<b>Effective exchange rate</b>						
Nominal	+ 1.1	+ 1.2	+ 0.9	- 2.5	- 0.4	- 0.6
Real	+ 0.7	+ 0.6	+ 0.4	- 2.7	- 0.2	- 0.4

<sup>1</sup> Calculated considering financial contributions to the Austrian Federal Railways (ÖBB) for compensation of infrastructural investments as government spendings. <sup>2</sup> 10-year central government bonds (benchmark).



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Projections - March 2011

## World economy

Percentage changes from previous year

	2007	2008	2009	2010	2011	2012
<b>Real GDP</b>						
World	+ 5.3	+ 2.8	- 0.6	+ 5.0	+ 4.2	+ 4.4
USA	+ 1.9	± 0.0	- 2.6	+ 2.8	+ 2.9	+ 3.0
Japan	+ 2.4	- 1.2	- 6.3	+ 3.9	+ 1.0	+ 2.0
EU 27	+ 3.0	+ 0.5	- 4.2	+ 1.8	+ 1.7	+ 1.7
Euro area 16	+ 2.9	+ 0.4	- 4.1	+ 1.7	+ 1.5	+ 1.5
Germany	+ 2.7	+ 1.0	- 4.7	+ 3.6	+ 2.7	+ 1.8
New member states <sup>1</sup>	+ 6.0	+ 4.1	- 2.9	+ 2.3	+ 2.8	+ 3.8
China	+ 14.2	+ 9.6	+ 9.2	+ 10.3	+ 9.5	+ 9.0
<b>World trade</b> , volume	+ 7.4	+ 2.5	- 13.0	+ 15.1	+ 8.0	+ 8.5
<b>Market growth</b> <sup>2</sup>	+ 7.1	+ 3.3	- 13.0	+ 12.6	+ 8.5	+ 7.8
<b>Primary commodity prices</b>						
HWI Index, total	+ 2.6	+ 21.7	- 30.4	+ 36.4	+ 23	+ 5
Excluding energy	+ 8.1	+ 9.5	- 23.6	+ 38.4	+ 18	+ 9
<b>Crude oil prices</b>						
Brent, USD per barrel	72.5	97.0	61.5	79.5	100	100
<b>Exchange rate</b>						
USD per euro	1.371	1.471	1.393	1.327	1.35	1.30

<sup>1</sup> Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania.

<sup>2</sup> Real import growth of trading partners weighted by Austrian export shares.

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Projections - March 2011

## Private consumption, income and prices

	2007	2008	2009	2010	2011	2012
Percentage changes from previous year, volume						
<b>Private consumption expenditure</b>	+ 0.7	+ 0.5	+ 1.3	+ 1.0	+ 1.1	+ 1.1
Durables	+ 2.6	+ 1.7	+ 5.2	- 1.0	+ 0.5	+ 1.0
Non-durables and services	+ 0.5	+ 0.3	+ 1.0	+ 1.2	+ 1.2	+ 1.1
<b>Household disposable income</b>	+ 2.3	+ 0.9	- 0.0	+ 0.0	+ 0.9	+ 0.9
As a percentage of disposable income						
<b>Household saving ratio<sup>1</sup></b>	11.6	11.8	11.1	10.0	9.9	9.7
<b>Household saving ratio<sup>2</sup></b>	11.2	11.6	10.4	9.6	9.4	9.2
Percentage changes from previous year						
<b>Direct lending to domestic non-banks<sup>3</sup></b>	+ 3.6	+ 7.4	- 1.3	+ 2.9	+ 5.0	+ 4.8
<b>Inflation rate</b>						
National	2.2	3.2	0.5	1.9	2.8	2.4
Harmonised	2.2	3.2	0.4	1.7	2.9	2.4
Core inflation <sup>4</sup>	1.9	2.4	1.5	1.2	2.2	2.2

<sup>1</sup> Including adjustment for the change in net equity of households in pension fund reserves.

<sup>2</sup> Excluding adjustment for the change in net equity of households in pension fund reserves.

<sup>3</sup> End of period.

<sup>4</sup> Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

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Projections - March 2011

## Productivity

Percentage changes from previous year

	2007	2008	2009	2010	2011	2012
<b>Total economy</b>						
Real GDP	+ 3.7	+ 2.2	- 3.9	+ 2.0	+ 2.5	+ 2.0
Employment <sup>1</sup>	+ 1.7	+ 2.2	- 0.8	+ 0.8	+ 1.4	+ 0.7
<b>Productivity</b> (GDP per employment)	+ 2.0	- 0.0	- 3.1	+ 1.1	+ 1.1	+ 1.3
<b>Manufacturing</b>						
Production <sup>2</sup>	+ 8.7	+ 3.5	- 14.3	+ 6.7	+ 7.0	+ 5.5
Employees <sup>3</sup>	+ 2.6	+ 1.7	- 5.3	- 1.3	+ 1.2	± 0.0
<b>Productivity per hour</b>	+ 6.3	+ 2.3	- 6.1	+ 5.1	+ 4.7	+ 5.2
Working hours per day per employee <sup>4</sup>	- 0.3	- 0.5	- 3.6	+ 2.8	+ 1.0	+ 0.3

<sup>1</sup> Dependent and self-employed according to National Accounts definition.

<sup>2</sup> Value added, volume.

<sup>3</sup> According to Federation of Austrian Social Security Institutions.

<sup>4</sup> According to 'Konjunkturerhebung' of Statistics Austria.

WIFO  
Projections - March 2011

## Earnings and international competitiveness

Percentage changes from previous year

	2007	2008	2009	2010	2011	2012
<b>Wages and salaries per employee<sup>1</sup></b>						
<b>Gross earnings</b>	+ 3.1	+ 2.9	+ 1.5	+ 1.6	+ 2.5	+ 2.9
<b>Gross real earnings<sup>2</sup></b>	+ 0.9	- 0.3	+ 1.0	- 0.3	- 0.3	+ 0.5
<b>Net real earnings<sup>2</sup></b>	+ 0.9	- 0.9	+ 2.7	- 0.6	- 0.6	+ 0.2
<i>Total economy</i>						
<b>Unit labour costs</b>	+ 0.9	+ 2.7	+ 4.8	+ 0.4	+ 1.4	+ 1.6
<i>Manufacturing</i>						
<b>Unit labour costs</b>	- 2.3	+ 1.1	+ 13.5	- 5.4	- 2.7	- 2.3
<b>Effective exchange rate - manufactures</b>						
Nominal	+ 1.2	+ 1.1	+ 0.7	- 2.6	- 0.4	- 0.6
Real	+ 0.8	+ 0.6	+ 0.4	- 2.7	- 0.2	- 0.4

<sup>1</sup> Employees according to National Accounts definition.

<sup>2</sup> Deflated by CPI.

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Projections - March 2011

## Labour market

Changes from previous year (1,000<sup>s</sup>)

		2007	2008	2009	2010	2011	2012
<b>Demand for labour</b>							
Persons in active employment <sup>1</sup>		+ 64.7	+ 66.0	- 44.0	+ 31.3	+ 58.0	+ 34.0
Employees <sup>2</sup>		+ 65.5	+ 55.6	- 48.5	+ 25.5	+ 52.0	+ 29.0
<i>Percentage changes from previous year</i>		+ 2.1	+ 1.7	- 1.5	+ 0.8	+ 1.6	+ 0.9
Nationals		+ 43.6	+ 31.1	- 43.0	+ 5.8	+ 21.0	+ 11.0
Foreign workers		+ 21.9	+ 24.5	- 5.5	+ 19.7	+ 31.0	+ 18.0
Self-employed <sup>3</sup>		- 0.8	+ 10.4	+ 4.5	+ 5.8	+ 6.0	+ 5.0
<b>Labour supply</b>							
Population of working age	(15 to 64 years)	+ 15.5	+ 27.7	+ 17.3	+ 25.7	+ 30.1	+ 16.9
	(15 to 59 years)	+ 17.1	+ 17.6	+ 11.1	+ 12.0	+ 15.5	+ 16.7
Labour force <sup>4</sup>		+ 47.8	+ 56.0	+ 4.0	+ 21.8	+ 42.0	+ 29.0
<b>Surplus of labour</b>							
Registered unemployed <sup>5</sup>		- 16.9	- 10.0	+ 48.1	- 9.5	- 16.0	- 5.0
	1,000 <sup>s</sup>	222.2	212.3	260.3	250.8	234.8	229.8
Unemployed persons in training	1,000 <sup>s</sup>	52.7	50.5	64.1	73.2	65.2	63.2
<b>Unemployment rate</b>							
Eurostat definition <sup>6</sup>	percent	4.4	3.8	4.8	4.4	4.1	4.0
Percent of total labour force <sup>5</sup>	percent	5.6	5.3	6.5	6.2	5.8	5.6
National definition <sup>5,7</sup>	percent	6.2	5.9	7.2	6.9	6.4	6.3
<b>Employment rate</b>							
Persons in active employment <sup>1,8</sup>	percent	64.9	65.7	64.7	65.0	65.7	66.1
Total employment (Eurostat) <sup>6,8</sup>	percent	71.4	72.1	71.6	71.7	72.2	72.5

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

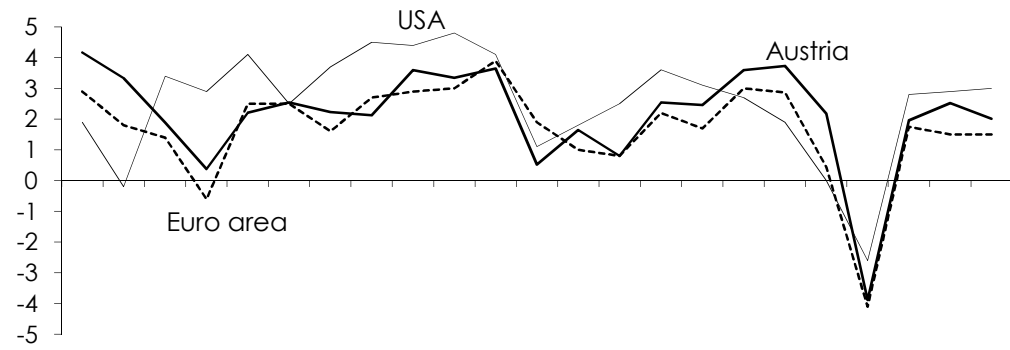
<sup>3</sup> According to WIFO. <sup>4</sup> Persons in active employment plus unemployment.

<sup>5</sup> According to Public Employment Service Austria <sup>6</sup> According to Eurostat Labour Force Survey.

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

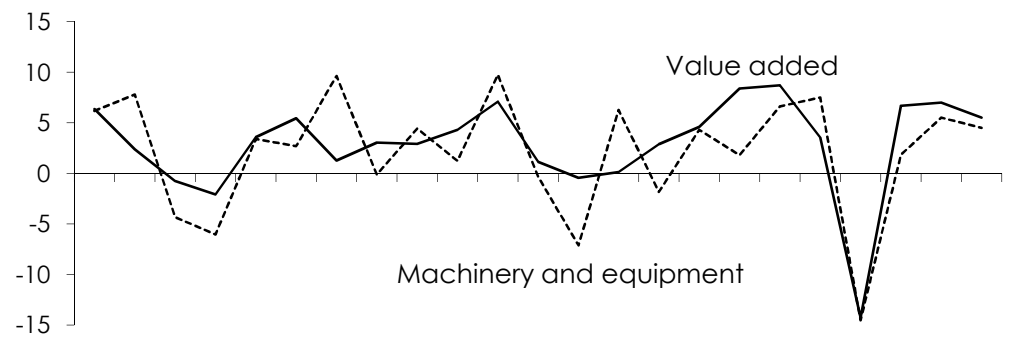
## Growth of real GDP

Percent



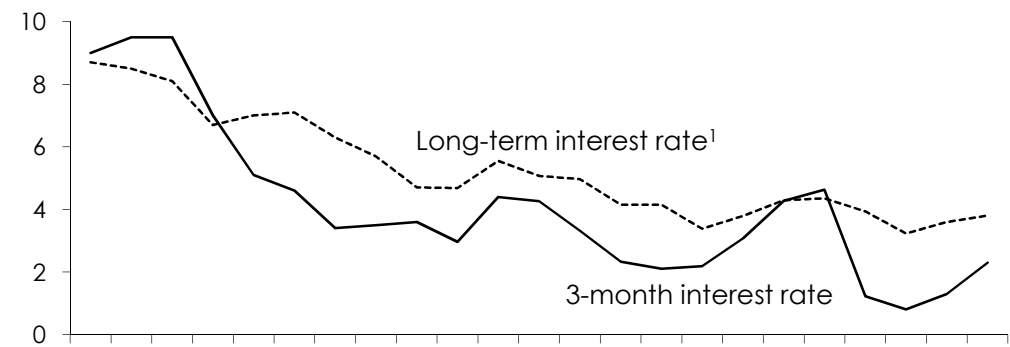
## Manufacturing and investment

Percentage changes from previous year, volume



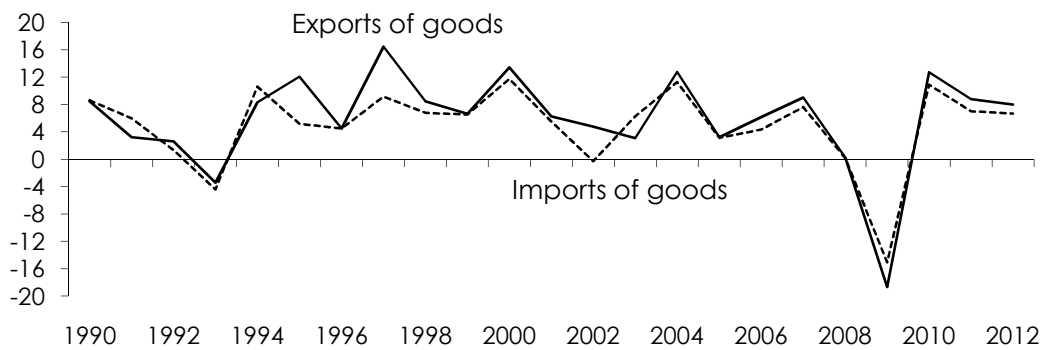
## Short-term and long-term interest rates

Percent



## Trade

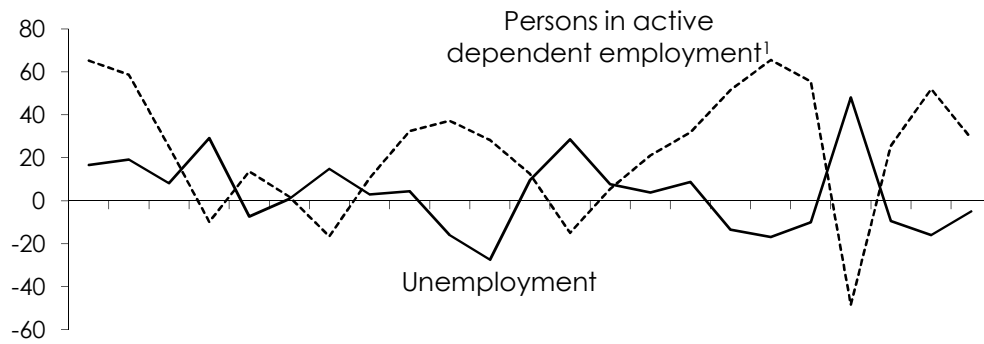
Percentage changes from previous year, volume



<sup>1</sup> 10-year central government bonds (benchmark).

## Employment and unemployment

1,000<sup>s</sup> from previous year



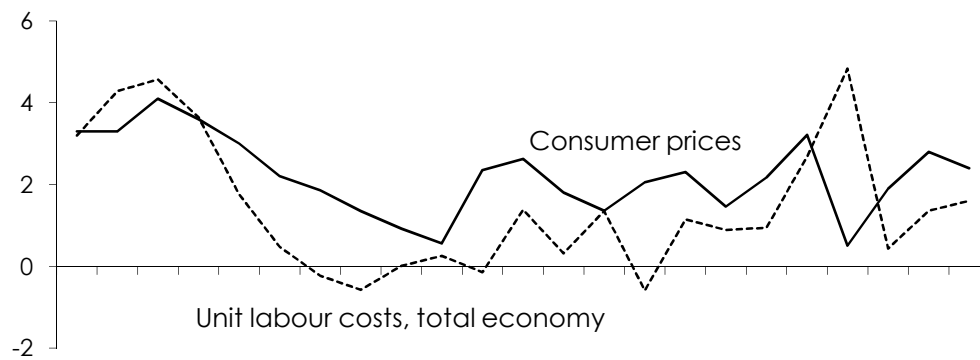
## Consumption and income

Percentage changes from previous year, volume



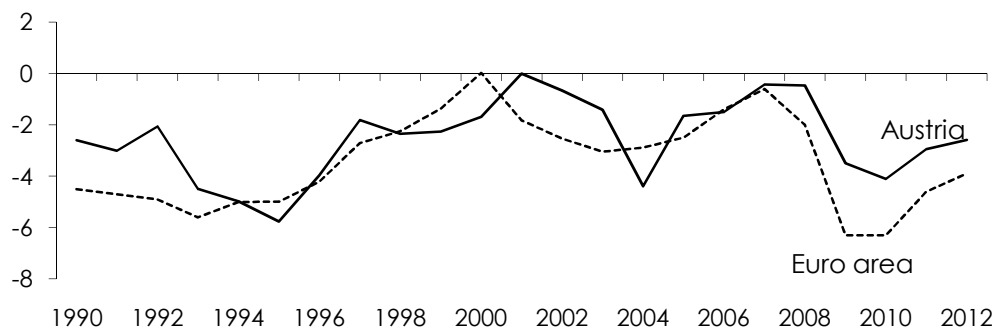
## Inflation and unit labour costs

Percentage changes from previous year



## General government financial balance

As a percentage of GDP



<sup>1</sup> Excluding parental leave, military service, and unemployed persons in training.