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Highest Employment Growth in Austria Since 2008

Business Cycle Report of September 2017

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The very strong employment momentum strengthened further in the summer. At the same time the economic indicators remained at very high levels, but did not improve any more; the growth rate appears to have reached its maximum. The seasonally adjusted unemployment rate, at 8.5 percent continues to be quite high, in view of this excellent state of the economy.

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Since the beginning of 2017, employment has posted the fastest growth and unemployment the most marked decline since 2008, the cyclical peak prior to the outbreak of the global financial and economic crisis. In the first seven months of 2017, the number of persons in active dependent employment (employment excluding military service and maternity/paternity leave) increased by 66,700 compared with the same period a year before; the employment momentum strengthened further in the summer. The number of persons unemployed declined by 12,800 from January to August compared with a year before, while that of job vacancies amounted to just under 62,000 in August. In view of these extremely favourable cyclical conditions, the unemployment rate (August 8.5 percent, seasonally adjusted) is still quite high (10.2 percent, including persons enrolled in training programmes). The number of older unemployed persons continues to increase – also owing to demographic factors –, while that of young unemployed persons is decreasing. The decline in unemployment among foreign workers in Austria set in late, but has recently intensified. The labour force influx from Eastern Europe continues unabated.

The Austrian economy maintained its strong momentum throughout the summer months. Business survey indicators remain at peak levels, albeit receding slightly in August – expectations for the coming months slightly more so than assessments of the current situation. This suggests that the maximum pace of economic growth has been reached. This is in line with the global economic picture: the impetus provided to world trade by emerging market economies, notably China, has weakened this year, with momentum shifting increasingly to the euro area. Here trade and investment benefit especially from buoyant activity in East Central European countries; but the US economy also keeps growing at a robust pace.

The tourism industry registered a successful first half of the summer season, with more guests arriving especially from Eastern Europe, but also from Germany and the USA. Against this background, the prices of tourism-related services such as restaurant

services, recreational and cultural services continued to rise at above-average rates. Apartment rents remained the second most important driver of inflation, whereas fuel prices barely increased further compared with a year before.

1. Global economy growing vigorously

The global economy has been expanding noticeably for at least a year now, with the upswing intensifying further in summer 2017. Both the USA and Japan and the euro area have been registering robust GDP growth. Owing to fiscal stimulus measures, China's economy remains in a boom phase, but its peak appears to have been surpassed already. At the beginning of the year, India's economy suffered the consequences of an unsuccessful cash reform that caused liquidity shortages; meanwhile, economic activity has stabilised. The export-driven recovery in Brazil, which set in at the beginning of the year, continues, and Russia's economy also remains on a recovery path.

Foreign trade momentum has spread from emerging market economies to the euro area.

Consistent with the upward trend of investment activity observed globally, world trade also gained strength. Following many years of stagnation, a marked recovery in import demand set in in spring 2016; having started from East Asia, it also spread to the emerging market economies of South America and Eastern Europe (Russia) in the course of the year. However, this upward trend has weakened this year, according to most recent data. Goods imports have increased significantly only in the euro area and Japan since the beginning of 2017. The increased demand at first stimulated the goods trade in the respective regions, for East Asia's, Latin America's and Eastern Europe's exports also picked up in 2016. Similar to imports, goods exports have increased only in the euro area so far this year.

1.1 Prices of industrial metals picking up again

The downward trend of commodity prices turned around in 2016 as global economic activity was gaining strength. However, developments have been mixed so far in 2017: energy commodity prices have not increased further. Advances in technologies for the extraction of shale gas using fracking and the fervent expansion of production capacities in North America are keeping international energy prices down. Industrial metal prices also eased during the first half of the year, but prices picked up again in the summer, however not those of energy commodities. This price rise may be largely attributable to speculations about supply shortages: in China, which accounts for 60 percent of the global aluminium production, facilities that are particularly harmful to the environment and therefore have no operating licence are to be increasingly shut down to curb the blatant environmental pollution. The Government of Shandong Province has ordered the closure of plants with an unlicensed capacity of 3.2 million tonnes. In July, the production of aluminium was down by 8 percent compared with a year before. Copper prices were partly inflamed by supply shortages (strikes in Chile and Indonesia). Overall, the upside potential of commodity prices appears to be limited, however, since commodity-rich countries vigorously expanded their production capacities in the face of many years of booming industrial production in China.

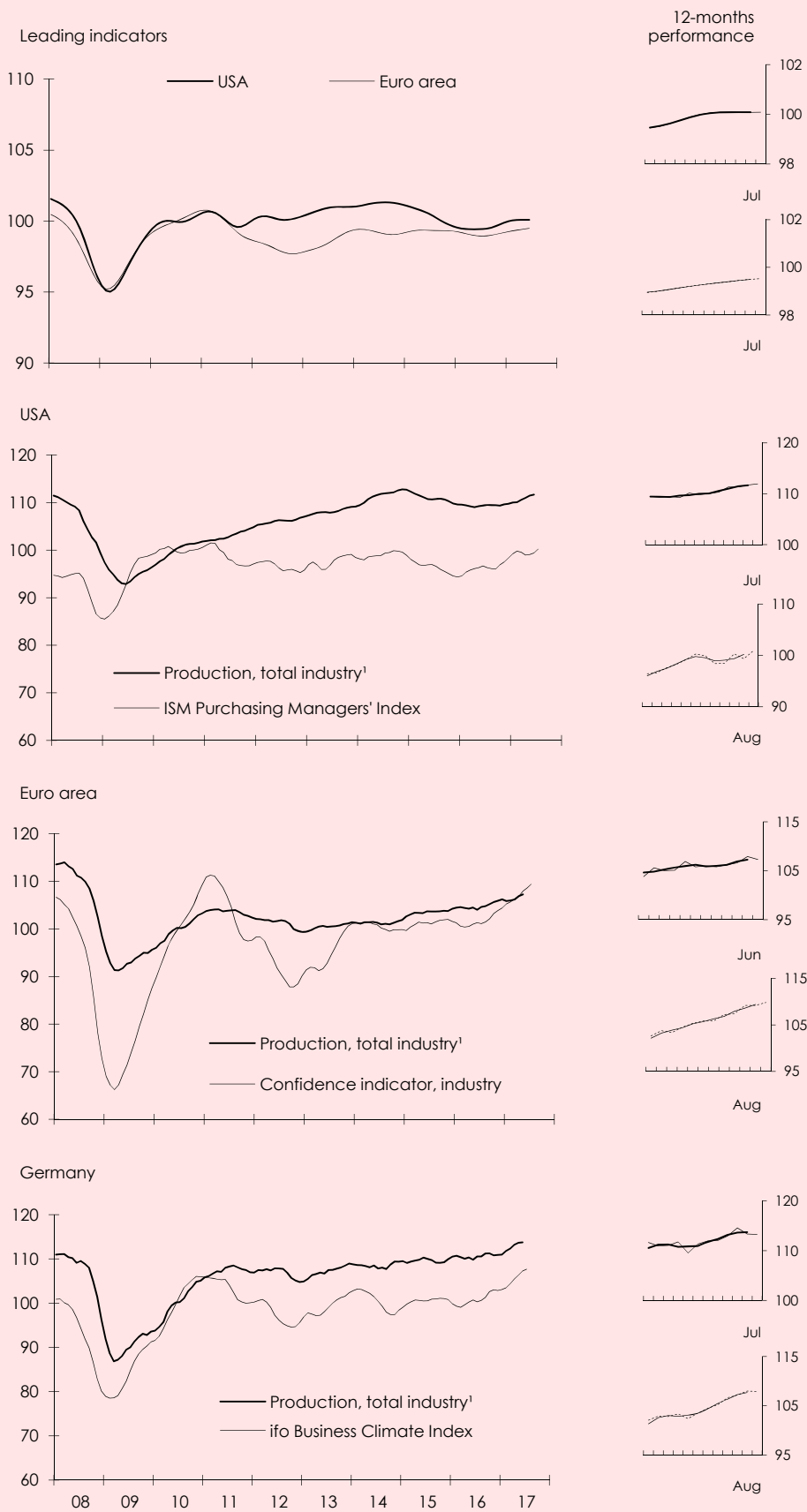
The announcement of a closure of metal extraction facilities in China triggers price increases.

1.2 USA: modest inflation despite very low unemployment

In the USA, aggregate production expanded at a quarter-on-quarter rate of 0.75 percent in the second quarter, according to the second estimate, considerably faster than in the first quarter (+0.3 percent). Especially private household demand for goods and services increased. Although the unemployment rate was already very low at 4.4 percent in August, inflation remained modest: in July, consumer price inflation and the core inflation rate came in at 1.7 percent. At 63 percent, the labour force participation rate is still 3 percentage points lower than it was before the outbreak of the 2009 economic crisis; hence there is still spare capacity in the labour market.

Figure 1: International business climate

Seasonally adjusted, 2010 = 100, 3-month moving average



Source: European Commission, Deutsche Bundesbank, ISM (Institute for Supply ManagementTM), ifo (Institute for Economic Research, Munich), OECD. - ¹ Excluding construction.

1.3 Buoyant upswing in East Central Europe

The euro area economy grew by 0.6 percent in the second quarter. Various survey-based and real economic indicators confirm the acceleration of the underlying trend. Meanwhile, the upswing has reached most countries. The quarterly growth rate was 0.6 percent in Germany, 0.5 percent in France, and 0.4 percent in Italy. At +0.9 percent, Spain's economy continued to grow vigorously. In several Eastern European countries, the strong momentum observed in the first quarter persisted and strengthened even further (Czech Republic +2.5 percent, Hungary +0.9 percent, Poland +1.1 percent, Romania +1.6 percent, Latvia +1.2 percent). Unemployment continues to fall in the euro area, with the rate dropping to 9.1 percent in July. Recently, unemployment rates have declined to a greater or lesser extent in all 19 countries of the euro area. Inflation accelerated somewhat and in August stood at 1.5 percent, according to provisional estimates; the core inflation rate reached 1.3 percent, after this important economic indicator had remained below 1 percent for just over three years.

Economic activity in the euro area maintains its robust underlying trend.

2. Austria: economic momentum stabilising at high level

Notwithstanding a slight fall in most indices, the results of WIFO's August Business Cycle Survey show that Austrian companies remain highly optimistic in their assessments of economic conditions and the outlook for the future; the economic climate indicator fell by 1.6 points to 16.3 points, compared with the previous month. For the first time in a year, WIFO's Economic Traffic Light¹ therefore changed from green to yellow in August, signalling a stabilisation of economic activity at a high level.

Business survey indicators receded slightly; economic growth appears to have reached its peak.

In August, both sub-indices of WIFO's Economic Climate Indicator remained below their levels recorded a month earlier. The present situation index fell by 0.8 points to +18.6 points, albeit remaining as high as last recorded in spring 2007. The slight deterioration in the assessment of the present situation is largely attributable to the construction industry, but to some extent also to manufacturing; sentiment in the services sector remained as favourable as previously.

The business expectations index fell somewhat more markedly (-2.3 points to +14.0 points). Hence companies continue to expect the very good economic conditions to improve further in the coming months, albeit at a somewhat slower pace than in previous months. While in August the assessment of future developments barely changed in manufacturing, firms in construction were more optimistic and firms in services more pessimistic than in July regarding the outlook for the coming months.

2.1 Credit conditions improving further

In summer 2017, Austrian companies reported a further improvement in credit conditions. The credit hurdle, i.e., the balance between the shares of companies describing banks' lending practices as accommodative or as restrictive, respectively, was 0 points in August, which was the first time that it was not in negative territory since the beginning of this survey more than five years ago. Hence banks' lending practices are considered to be increasingly less restrictive. The detailed results for companies with borrowing needs do not show any substantial increase in the demand for loans. As in the spring, around 22 percent of the companies surveyed stated that they had borrowing needs in the preceding three months. Only 13 percent of them, hence fewer than on average in recent years, had to make cuts in the amounts and credit conditions originally expected. Around 69 percent of the companies with borrowing needs were able to obtain the amount of loan expected and on the terms expected. 17 percent of the companies with borrowing needs did not obtain a loan because the bank rejected it, or the terms were not acceptable to them, or be-

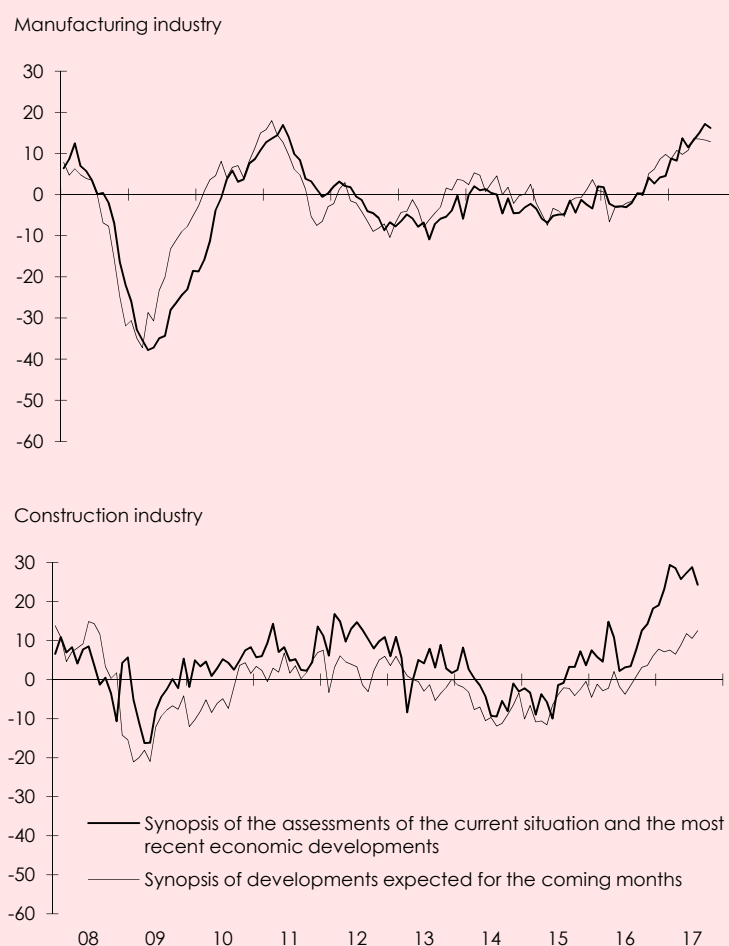
Banks' lending practices are no longer considered to be predominantly restrictive.

¹ Glocker, Ch., Hölzl, W., "Bestimmung einer Konjunkturampel für Österreich auf Basis des WIFO-Konjunkturtests", WIFO-Monatsberichte, 2015, 88(3), pp. 175-183, <http://monatsberichte.wifo.ac.at/57854>.

cause they had not even tried to obtain a loan since they did not stand a chance of getting one.

Figure 2: Results from the WIFO Business Cycle Survey

Indices of the assessment of the current economic situation and of business expectations, seasonally adjusted



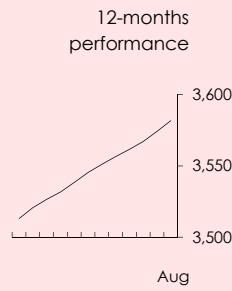
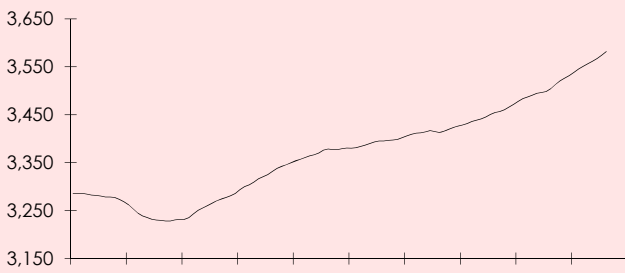
Source: WIFO Business Cycle Survey. Data refer to index points (percentage points) between +100 and -100. Values above 0 imply positive expectations, values below 0 indicate negative expectations.

2.2 First half of summer tourism season successful

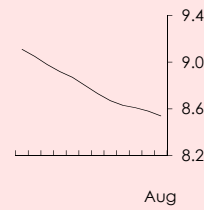
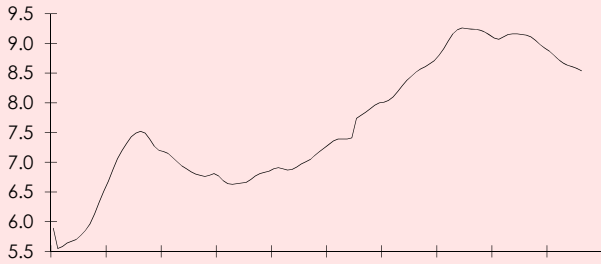
The first half of the 2017 summer season was a success for the Austrian tourism industry, according to estimates by WIFO: revenues rose by 5.4 percent in nominal terms from May to July 2017, compared with the same period a year before, guest arrivals by 5.7 percent, and the number of overnight stays by 4.4 percent. The length of stay declined by 1.2 percent to 3.04 nights on average. From May to July 2017, Austrian accommodation establishments registered a total of around 36 million overnight stays, 69.2 percent of which by foreign guests, whose demand increased much more briskly than that of domestic travellers (+5.8 percent and +1.5 percent, respectively). The by far highest rates of increase were recorded for nights spent by guests from Russia (+31.5 percent), Poland (+15.8 percent), Romania (+11.3 percent) and Hungary (+9.5 percent) as well as from the USA (+7.9 percent). Overnight stays by travellers from Germany, Austria's most important source market, also grew briskly at +6.8 percent, accounting for more than half of the absolute increase in overnight stays. By contrast, nights spent by guests from Switzerland (-0.6 percent), Italy (-0.9 percent), the UK (-1.4 percent) and Belgium (-4.1 percent) remained below their year-earlier levels.

Figure 3: Key economic indicators

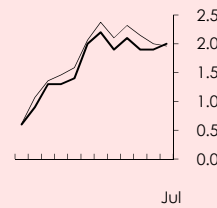
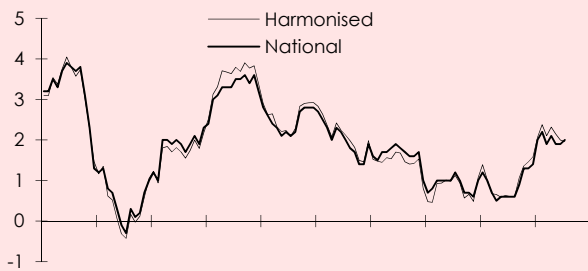
Persons in active dependent employment¹, 1,000s, seasonally adjusted



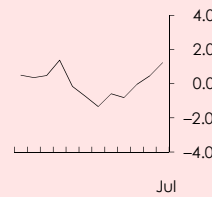
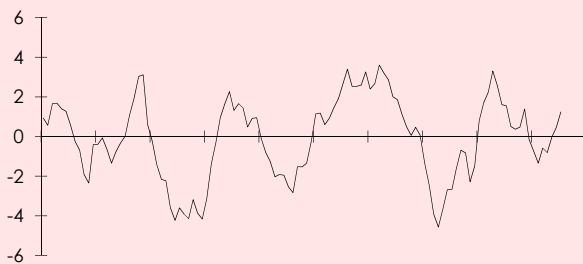
Unemployment rate, traditional Austrian method², seasonally adjusted



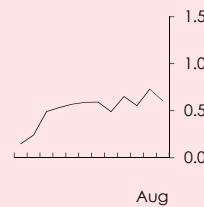
Consumer prices, year-to-year percentage changes



Real effective exchange rate, year-to-year percentage changes



10-year central government bonds (benchmark), percent



Source: Public Employment Service Austria, Main Association of Austrian Social Security Institutions, Oesterreichische Nationalbank, Statistics Austria, WIFO calculations. – ¹ Excluding persons in valid employment contract receiving child care benefit or being in military service. – ² As a percentage of total labour force excluding self employed, according to Public Employment Service.

2.3 Price increases for tourism-related services and housing driving inflation

Consumer price inflation was 2.0 percent in July. Prices picked up again vigorously in those two areas which have been responsible for an above-average inflation rate in Austria for several years now: tourism-related services (restaurant services +3.1 percent, contribution to inflation +0.29 percentage point, package holidays +5.1 percent and +0.13 percentage point, respectively, recreational and cultural services +2.8 percent and +0.12 percentage point, respectively) and housing. Apartment rents paid were up by 4.2 percent in July compared with a year before (inflation contribution +0.21 percentage point). Together, the "restaurants and hotels", "recreation and culture" and "housing, water, energy" components contributed about half (1 percentage point) to overall inflation. The crude oil price did not exert any upward pressure: at 39 € to 45 € per barrel in June and July, it was, on average, as high as in the same period a year before.

Increases in energy commodity prices have already come to a halt.

2.4 Very high employment gains

Since the beginning of 2017, employment has posted the fastest growth and unemployment the most marked decline since 2008. In the first seven months of 2017, the number of persons in active dependent employment rose by 66,700 compared with the same period a year before (+53,700 for all of 2016). The increase accelerated throughout this entire period; in August 2017, the number of persons in active dependent employment was up by 79,000 compared with August 2016, according to provisional data. In parallel with the robust employment expansion, the number of unemployed persons dropped by 12,800, year on year, from January to August (+3,000 for all of 2016). The decline in unemployment of Austrian citizens observed since 2016 has intensified markedly this year: from January to July 2017, the number of persons with Austrian citizenship registered as unemployed was down by 11,600 compared with the same period in 2016. Hence one fifth of the cumulated increase in unemployment since 2012 was offset.

Unemployment is declining, but the labour force maintains its strong growth momentum.

For the first time since 2011, unemployment has declined slightly also among persons from the former guest-worker countries Turkey and Yugoslavia this year, but only around 5 percent of the cumulated increase since then has been offset. Gaining a foothold on the labour market remains difficult for this group of persons, since the influx of (often younger and better-qualified) Hungarian, Romanian, Polish and Slovakian job seekers continues unabated. The favourable evolution of the labour market currently observed masks structural problems caused by the opening of the labour market to people from the East, demographic ageing, and the fact that older persons stay in the workforce longer. As it was not possible for the resulting large numbers of people entering the labour force to be completely absorbed by an expansion of employment, the unemployment rate for the first time rose from 2013 onward, despite the fact that the number of jobs offered did not decline; in addition, the share of long-term unemployed increased markedly. The unemployment rate is still relatively high (August 8.5 percent, seasonally adjusted).