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## Vigorous Upswing in Austria

### Business Cycle Report of May 2011

**Indicators in the world's most important economic regions as well as in Austria point to a vigorous cyclical recovery. Surveys among domestic manufacturing companies reflect strong optimism regarding their current business situation. However, the outlook for the future suggests that the pace of the upswing will slow in the months to come. While inflation rose once again in March, labour market conditions improved further.**

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The global economy is currently growing at a vigorous pace. In many countries in South America and Asia, GDP has not only reached the levels recorded prior to the economic crisis, but has even returned to the original growth path. In Europe and the USA, the momentum has so far been determined by a catch-up effect, with economic output not yet back at pre-crisis levels.

But world market commodity prices continue to rise, mainly on account of strong economic growth and monetary expansion. Brent crude oil prices averaged \$ 114.6 per barrel in March, and rose further in April, topping \$ 126 at times. The prices of other commodities and precious metals also reached record levels. As a result, inflation accelerated considerably globally. Many central banks already saw themselves compelled to raise their key interest rates. While the ECB recently also raised the rate by 0.25 percentage point, the central bank of the USA left the federal funds rate unchanged at around 0 percent.

The US economy grew by 0.4 percent quarter-on-quarter in the first quarter of 2011, more slowly than in the fourth quarter of 2010 (+0.8 percent). Continuing inventory accumulation and private consumption supported growth at the beginning of the year, while the decrease in government spending dampened the result. The contribution from net trade as well as private fixed investment had a neutral effect; notably equipment investment expanded briskly, but the demand for buildings declined. Surveys both among businesses and consumers suggest that growth is likely to continue in the near future.

Economic activity in the euro area remains uneven. Germany's neighbouring export-oriented economies are continuing their recovery. Businesses are still extremely optimistic regarding their production prospects for the coming months. Labour market conditions in these countries are rapidly improving. In some countries along the rim of the euro area, however, economic activity continues to decline or is stagnant. The catch-up process of Central and Eastern European countries got going again after the crisis, developments are largely robust.

In Austria, too, business surveys conducted in the first quarter point to currently robust economic developments, but the momentum is expected to decline again. In the first quarter of 2011, Austria's real GDP grew by 1.0 percent, respectively compared with the previous quarter, rates higher than the euro area average. Industrial output and aggregate production are still slightly their pre-crisis levels, however.

Table 1: Flash estimates of quarterly national accounts

	2009 Fourth quarter	2009 First quarter	2010 Second quarter	2010 Third quarter	2010 Fourth quarter	2011 First quarter
Adjusted for seasonal and working day effects, percentage changes from previous quarter, volume						
<i>GDP, expenditure approach</i>						
Final consumption expenditure						
Households <sup>1</sup>	+ 0.3	+ 0.2	+ 0.2	+ 0.3	+ 0.2	+ 0.2
General government	- 0.3	- 0.5	+ 0.1	- 0.1	- 0.1	- 0.0
Gross capital formation	- 0.8	- 1.3	+ 2.5	+ 3.9	+ 4.3	+ 1.2
Gross fixed capital formation	- 0.8	- 1.2	+ 0.4	+ 1.5	+ 1.2	+ 0.9
Exports	+ 2.8	+ 2.4	+ 4.2	+ 3.3	+ 2.0	+ 3.4
Imports	+ 1.1	+ 2.4	+ 3.9	+ 3.2	+ 2.1	+ 2.4
Gross domestic product	+ 0.4	+ 0.2	+ 1.0	+ 1.1	+ 0.9	+ 1.0
<i>GDP, output approach</i>						
Agriculture, forestry	+ 1.1	+ 0.1	- 0.7	- 0.8	- 0.2	- 0.1
Industry, including energy	+ 1.0	+ 0.0	+ 3.0	+ 3.2	+ 2.5	+ 3.0
Manufacturing	+ 0.7	+ 0.2	+ 3.9	+ 3.6	+ 2.1	+ 2.7
Construction	- 1.3	- 1.6	- 1.5	- 1.1	- 0.6	- 0.1
Wholesale and retail trade; repairs; hotels and restaurants; transport, communication	+ 0.2	+ 0.4	+ 0.6	+ 0.8	+ 0.8	+ 1.1
Financial intermediation; real es- tate, renting and business activities	+ 0.7	+ 0.8	+ 0.9	+ 0.9	+ 0.9	+ 0.7
Other service activities	+ 0.4	+ 0.5	+ 0.5	+ 0.4	+ 0.3	+ 0.2
Taxes on products	+ 0.4	- 0.4	- 0.1	+ 0.6	+ 0.2	- 0.5
Subsidies on products	+ 1.1	+ 1.4	+ 1.1	+ 0.9	+ 0.7	+ 0.3
Percentage change from previous year						
Gross domestic product, volume	- 0.9	+ 0.2	+ 2.5	+ 2.5	+ 3.0	+ 4.2

Source: WIFO. – <sup>1</sup> Including private non-profit institutions serving households.

The construction industry is showing only little improvement. While in the surveys businesses assess construction activity clearly more positively, the sustainability of this development is doubtful, given the unfavourable appraisal of order books.

Inflation has been accelerating markedly in Austria since the beginning of the year, and rose in April to 3.1 percent. This is reflected in a real decline in earned income, which is dampening private households' readiness to consume.

In the first quarter of 2011, the Austrian labour market continued to benefit from the economic recovery. However, in April the seasonally adjusted number of persons in dependent active employment stagnated compared with the previous month. But unemployment declined yet again (-0.5 percent, month-on-month). Nevertheless, the seasonally adjusted unemployment rate remained unchanged at 6.6 percent.

US real gross domestic product grew by 0.4 percent quarter-on-quarter in the first quarter of 2011, half the rate for the fourth quarter of 2010, according to first estimates. However, this is not a sign that the economic momentum is trending downwards. Growth in the first quarter was supported by household consumption (+0.7 percent) and renewed inventory accumulation. Gross fixed capital formation almost stagnated (+0.2 percent), owing to slowing demand for construction investment. Residential construction declined again by 1 percent, while investment in non-residential construction fell even more sharply, by -6 percent. Investment in equipment (machinery and vehicles), by contrast, expanded briskly, as in preceding quarters (+2.8 percent).

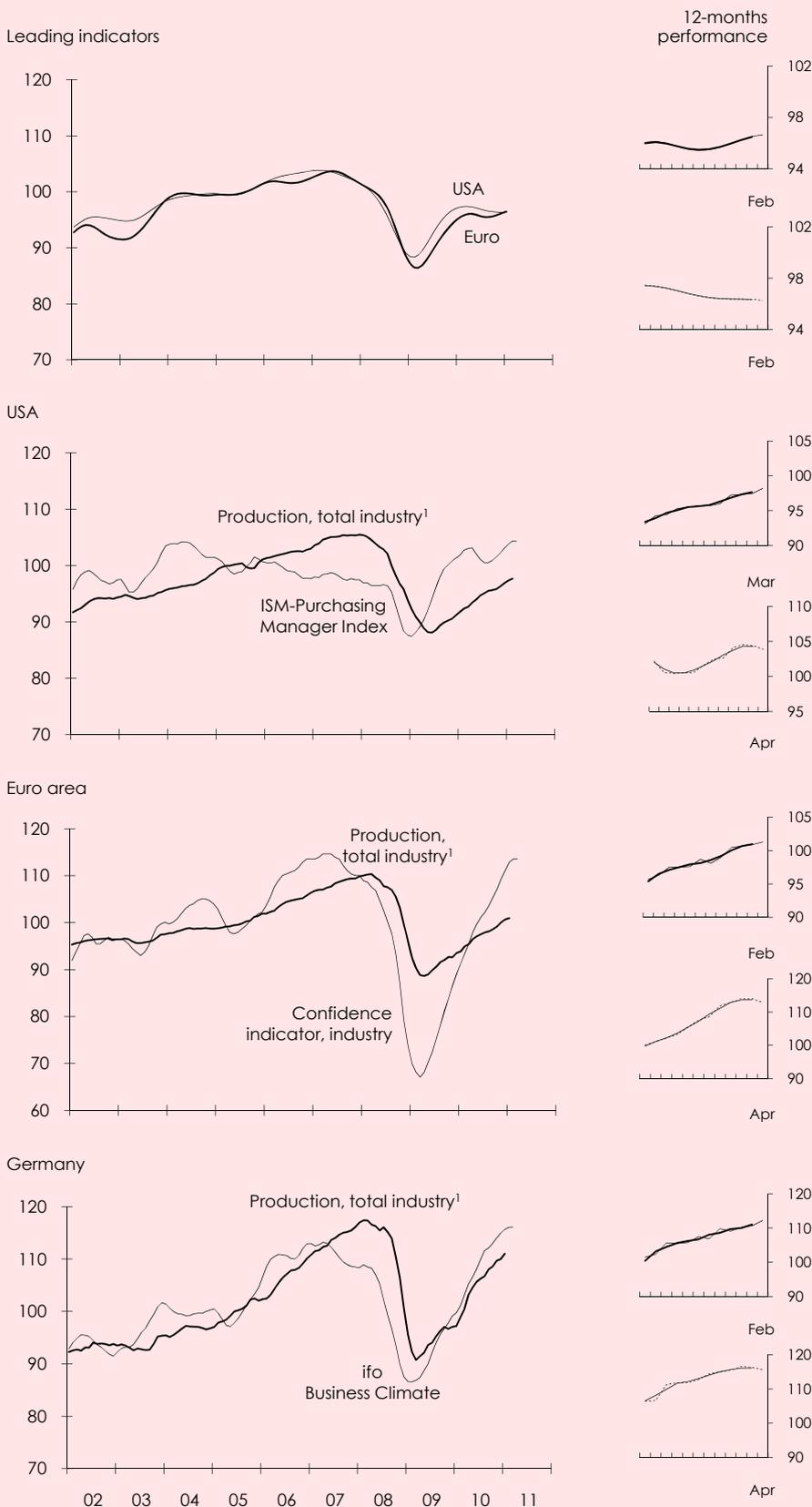
With both exports and imports rising at a quarter-on-quarter rate of about 1 percent in real terms, net exports did not contribute to growth in the first quarter of 2011. While US monetary policy remains expansionary, the renewed decline in public sector demand reflected the government's effort to save (first quarter of 2011 -1.3 percent).

## USA and EU: recovery continues

*In the first quarter of 2011, the US economy grew by 0.4 percent, while the economy in the euro area expanded by 0.8 percent. The majority of businesses in the EU remain highly optimistic regarding their business expectations, although survey results differ considerably across countries. Meanwhile the labour market has also begun to benefit from the economic revival.*

Figure 1: International business climate

Seasonally adjusted, 2005 = 100, 3-month moving average



Source: European Commission, Deutsche Bundesbank, ISM (Institute for Supply Management™), ifo (Institute for Economic Research, Munich), OECD. – <sup>1</sup> Excluding construction.

Industrial production rose again more strongly in March (+0.8 percent), after expanding by a mere 0.1 percent in January and February. This corresponds to a year-on-year increase of around 6 percent. The ISM Purchasing Managers' Index fell back slightly in April 2011 (from 61.2 to 60.4), but still remained at a very high level, pointing to robust growth also in the coming months. Evidence from consumer surveys suggests that consumer demand will also continue to expand strongly in the months ahead.

The US labour market for an unusually long time did not react to the pickup in economic activity. In November 2010, the unemployment rate was 9.8 percent, only 0.1 percentage point lower than a year before. Only around the turn of the year did it fall more sharply. February and March saw another slight decline in the rate, to 8.8 lately.

Consumer prices in the USA also reflect the rapid price increases for commodities and agricultural products. In March, the general price level of consumer goods rose at a seasonally adjusted rate of 0.5 percent from the previous month. This corresponds to a year-on-year increase of 2.7 percent. Excluding energy and food, the year-on-year increase was only 1.2 percent.

The euro has gained noticeably against the dollar in recent months; since the beginning of 2011, the exchange rate has appreciated by more than 10 percent. This development, while dampening the impact of soaring commodity prices in the euro area, at the same time is hurting exports.

In the first quarter of 2011, real GDP expanded by 0.8 percent in both the euro area and the EU. In the euro area, the course of economic activity remains divided: the recovery of Germany's neighbouring export-oriented economies continues, while the economies of Greece, Portugal, Ireland and Spain remain mired in crisis.

According to the European Commission's business survey, the assessment of production in the last three months in March reached the highest level since the inception of the survey in 1985. The only time a higher survey value was recorded for the euro area was in May 2000. April saw a moderate decline in the value for both the EU and the euro area. Developments in the coming three months have likewise been assessed more positively so far; here the highest value for the EU since 1995 was recorded in February 2011. In March and April, assessments deteriorated in both the EU overall and the euro area, suggesting momentum will wane in the coming months.

In Greece and Ireland, budget correction efforts are dampening aggregate demand. This process is still in store for Portugal, where the economy got going again after the crisis. Here, economic output declined for the second time in a row in the first quarter of 2011 (-0.7 percent, quarter-on-quarter).

So far, the economic recovery has not been reflected in labour market data for the EU or the euro area as a whole. Employment in both the euro area and the EU barely increased in seasonally adjusted terms in the fourth quarter of 2010 (+0.1 percent). The average seasonally adjusted unemployment rate for a year now has remained at the elevated level caused by the crisis (March EU 9.9 percent, euro area 9.5 percent). However, there are large differences across member countries also in this respect: while unemployment is falling appreciably for instance in Germany, Austria, the Netherlands and Sweden, it is rising in the countries that are in recession.

Having accelerated markedly in previous months, inflation in the euro area rose further to 2.7 percent in March 2011 (February 2.4 percent). Annual consumer price inflation was thus as high as in the USA. In the euro area, too, price increases for energy raw materials were the most important component of inflation. As a result, the ECB for the first time since the outbreak of the economic crisis in the autumn of 2008 raised the key interest rate by 25 basis points to 1.25 percent.

In the first quarter of 2011, the Austrian economy expanded by 1.0 percent compared with the previous quarter, surpassing average growth in the euro area (+0.8 percent). In January and February 2011, industrial production (excluding energy and construction) rose at a seasonally and working day adjusted month-on-

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**Manufacturing key  
driver of economic  
activity**

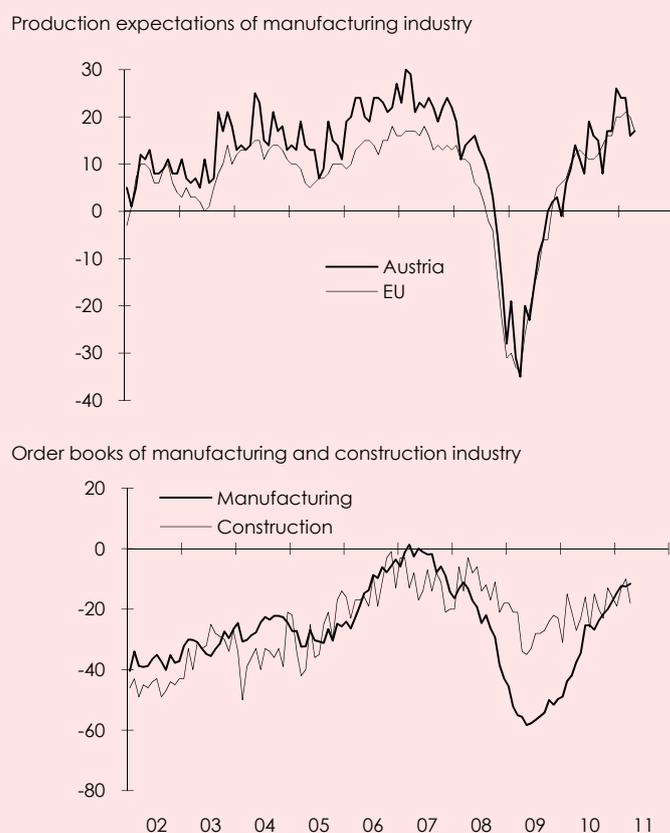
month rate of 2.4 percent and 0.5 percent, respectively. Compared with a year before, this corresponds to an increase of 16.2 percent and 11.3 percent, respectively. Evidence from WIFO's April business cycle survey suggests that the recovery will continue, albeit at a somewhat slower pace than in the first quarter.

The surveyed companies on average reported a capacity utilisation rate of 84 percent in April. The highest value of the more recent past, a capacity utilisation rate of close to 85 percent was recorded in the first half of 2007 – during the boom. This shows that capacity utilisation in the manufacturing sector is currently high, although industrial production is still slightly below its pre-crisis level. Apparently the capital stock has declined due to weak investment activity during the crisis. Production may surpass its pre-crisis level again even before the middle of the year. In order to return to its long-term trend growth path (since 2003), however, the momentum would have to remain strong beyond the turn of the year.

*The Austrian economy is recovering production losses caused by the crisis. Capacity utilisation for manufacturing, though not yet back to pre-crisis levels, is already in line with its long-term average. Apparently the capital stock has declined due to weak investment activity during the years of the crisis.*

Figure 2: WIFO business cycle survey

Differences between the percentage shares of correspondents giving positive and negative replies, seasonally adjusted



Source: European Commission, WIFO business cycle survey.

The results of WIFO's April business cycle survey show that the recovery is broad-based. All sectors except the construction supply industry and manufacturers of traditional consumer goods currently assess their production very positively. Scepticism regarding the business cycle outlook is also becoming noticeable in almost all sectors, however.

Measured by the duration of the production decline, Austria's construction industry was hit hardest by the economic crisis. Value added fell again in the first quarter (-0.1 percent in real terms, seasonally adjusted, quarter-on-quarter), continuing the decline persisting since the second half of 2007.

The situation may have stabilised in the first quarter of 2011, although value added is likely to have fallen again compared with a year before. In WIFO's April business cy-

*The situation in the construction industry is not deteriorating further for the time being. Business surveys do not show a clear trend.*

cle survey, businesses assessed their current construction activity more positively. However, this upward trend is concentrated on building construction, notably non-residential construction, while business remains bad in civil engineering.

Tourism sales in the 2010-11 winter season remained 1 percent in nominal terms below their year-earlier level, according to provisional calculations. April data are not yet available, but are expected to change the declining trend only little. A late timing of Easter normally harms domestic tourism as it is used only to a limited extent for a skiing holiday.

The number of overnight stays fell by 0.9 percent during the winter season (November till March), the decline having been equal for resident as well as foreign guests. A strong increase was recorded in overnight stays by guests from Russia (+24.4 percent), Switzerland (+11.9 percent), the USA (+10.2 percent), Belgium (+9.2 percent) and France (+7.0 percent). The important segment of demand from Germany, on the other hand, declined yet again (-5 percent).

This winter has been a good season so far for Vienna as well as Lower and Upper Austria. Styria and Salzburg, by contrast, registered a slight contraction, while some of the other Länder reported sharp declines.

Once the global economy got going again, the demand for crude oil also rose. Since the beginning of 2011, political unrest in North Africa and the Middle East has been adding to the insecurity surrounding a sufficient supply of fossil energy sources. This has led to considerable increases in world market prices for crude oil. Within a year, the price of Brent crude rose by more than 40 percent, to \$ 125 per barrel. Recent months have also seen marked price increases for agricultural products such as coffee and cereals.

The demand for consumer goods in Europe and the USA so far has not grown so briskly that production would reach capacity limits and companies would therefore raise their prices. The enormous monetary expansion, the central banks' response to the financial market crisis, might, however, be a cause of surging commodity prices: as it results in low interest rates, speculation may increase. The sizeable changes in the prices of gold and silver also seem to point in that direction.

Commodity price increases are accelerating inflation worldwide, although in many cases production is not yet back to pre-crisis levels. Both the USA and the euro area saw the inflation rate pick up to 2.7 percent in March. However, inflation excluding energy and food stood at 1.2 percent in the USA, while core inflation in the euro area was 1.5 percent.

In Austria, consumer prices also reacted to the commodity price hike. The annual rate of inflation rose to 2.4 percent in January, 3 percent in February, and 3.1 percent in March. The last time it had passed the 3-percent mark had been in October 2008. Inflation excluding mineral oil and food stood at 1.8 percent in March, according to Statistics Austria. Inflation as measured by the Harmonised Index of Consumer Prices increased to 3.3 percent in March (February 3.1 percent).

Real wages are declining noticeably on the back of the sharp upward pressure on consumer prices. According to national accounts statistics, gross nominal wages rose by a mere 3.0 percent year-on-year in the fourth quarter of 2010, whereas employment grew by 1.3 percent. As at the same time consumer prices increased by 2.1 percent, the result was a severe loss of purchasing power. This development continued also in the first quarter of 2011. During this period, the negotiated wage index rose by 1.7 percent, while the average inflation rate stood at 2.8 percent.

In the first quarter of 2011, households increased their consumption expenditure by 0.2 compared with the previous quarter. Although the household saving ratio has been trending downwards so far, consumption growth is expected to remain subdued in the near future. New car registrations increased considerably (January and February +22 percent, on a cumulative basis) as numerous households brought forward car purchases in anticipation of the change of NOVA, the excise duty on cars

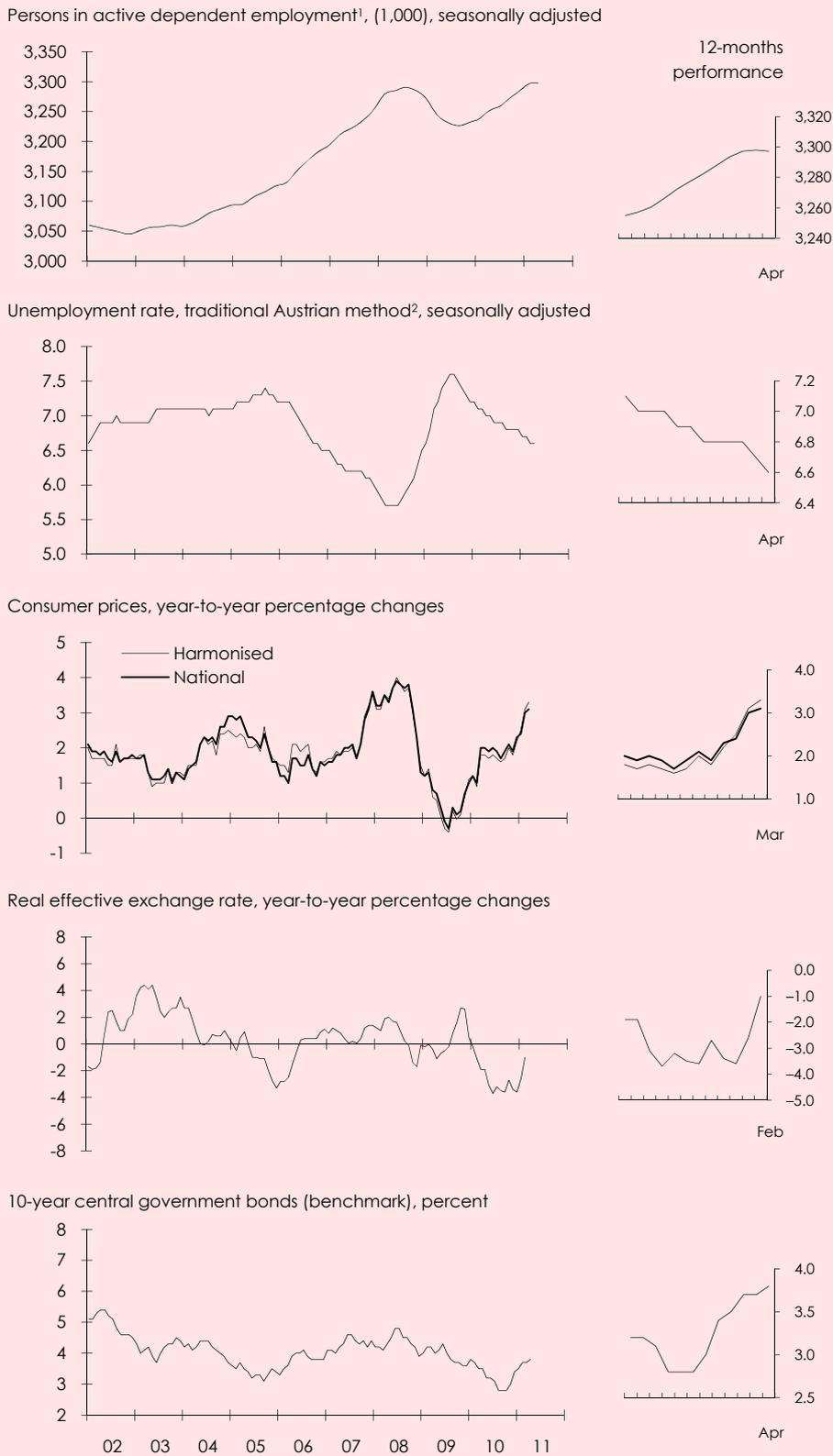
## Late Easter dampens winter season results

## Inflation again topping 3 percent

*In March, inflation as measured by the CPI for the first time since 2008 rose above 3 percent. As then, the price increases were mainly attributable to price rises for mineral oil products.*

(March 2011). Other retail sales are expected to decline in real terms in the first quarter, owing to the late timing of Easter.

Figure 3: Key economic indicators



Source: Public Employment Service Austria, Federation of Austrian Social Security Institutions, Oesterreichische Nationalbank, Statistics Austria, WIFO calculations. – <sup>1</sup> Excluding parental leave, military service, and unemployed persons in training. – <sup>2</sup> As a percentage of total labour force excluding self employed, according to Public Employment Service.

## 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".

Employment in Austria rose further in the first quarter on the back of the strong expansion in production. In the first three months of 2011, the number of persons in dependent active employment rose by about 62,700, or 2 percent, compared with the same period a year before. The seasonally adjusted figures already show a different picture, however: in March and April, employment stagnated. The pre-crisis level

**Labour market  
recovery continues,  
albeit at slower pace**

(July 2008 3,290,700, seasonally adjusted) was surpassed for the first time in January 2011, when employment reached 3,293,600.

Unemployment, on the other hand, continues to decline at an undiminished pace. In the first quarter, the number of persons registered as unemployed with the AMS (Public Employment Service) was down by around 16,100 from a year earlier (-5.4 percent). In April 2011, unemployment declined by 0.5 percent month-on-month, a rate similar to the one registered in March.

The unemployment rate fell to 6.6 percent in April, according to the national method of calculation (March 7.0 percent). Adjusted for seasonal effects, it remained unchanged at 6.6 percent.

*The improvement in labour market conditions is making headway, thanks to buoyant economic activity. Unemployment declined yet again in April, but employment did not rise further. The positive trend, while expected to weaken, should persist in the coming months.*