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Cyclical Upturn Set to Continue, With Risks Persisting

Economic Outlook for 2011 and 2012

The export-driven upswing of economic activity in Austria is expected to continue. Nevertheless, the pace of growth will decelerate markedly in the first half of 2011 as global trade and the expansion in Asia, Latin America and the USA lose momentum; in addition, the planned fiscal consolidation in the euro area and weak competitiveness of the southern European economies will weigh on aggregate demand. Whereas business activity should rebound worldwide in the latter part of 2011 and into 2012, it may remain subdued in the euro area. For Austria, WIFO expects real GDP to expand by 2.2 percent in 2011 and 2.0 percent in 2012. Main driver of demand and output growth are exports, stimulating notably manufacturing and, albeit gradually, business fixed investment. The cyclical revival will help correcting the imbalances on the labour market and in public finances. Yet, at barely below 7 percent of the dependent labour force, unemployment will remain high. The government deficit is likely to narrow to 3.1 percent and 2.7 percent of GDP in 2011 and 2012, respectively.

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Growth of world trade and global industrial output eased significantly during 2010. Particularly in Asia, hitherto the engine of the recovery of the world economy, the expansion has shifted into lower gear since the beginning of the year. One reason is that the repletion of inventories after the crisis has largely run its course, another are the moves of China and other emerging economies to preempt cyclical overheating and reduce the growth momentum somewhat. Still, the economies in Asia and Latin America will remain buoyant in 2011 and 2012 and thereby provide strong incentives to global business activity.

In the USA, GDP remains on a moderate upward trend, with exports and industrial output upward bound. Private consumption has proved surprisingly resilient, given the difficult situation on the labour market and reduced prospects for real estate and construction. In the next few years, growth is unlikely to return to pre-crisis rates. Private households will want to reduce their accumulated debt burden, keeping the saving ratio high and implying restraint on consumption spending and house purchases.

The euro area looks set for a two-speed recovery: Germany and other economies with close ties to Europe's largest economy benefit from the global cyclical upswing and will continue to enjoy healthy growth. In southern Europe and Ireland, on the other hand, severe measures of fiscal restraint and low competitiveness weigh on the return to growth, which will hold back the recovery of the euro area at large. Thus, in the years to come, the expansion will clearly lag behind the rest of the world. In the East-Central European EU countries, however, business activity should regain momentum.

Driven by the strong cyclical revival abroad, notably in Germany, the Austrian economy expanded markedly in the course of 2010. In the third quarter, GDP rose by 0.9 percent in volume from the previous period. The main support came from lively exports which stimulated in particular manufacturing output. Only gradually is the upswing spilling over to corporate investment in machinery and equipment. For the next few months, economic activity can be expected to follow an unabated

upward trend; by mid-2011, however, it is likely to slacken in line with developments abroad. The slowdown of world trade growth and fiscal restraint in the euro area will dampen the pace of exports and of the cyclical recovery altogether. Although investment in machinery and equipment should pick up, the slower progress of the recovery will prevent its reinforcement to a boom. In the second half of 2011, growth should regain momentum and further accelerate in 2012. Due to the strong carry-over from 2010, the annual GDP growth rate will, however, be higher for 2011 than for 2012¹. GDP growth for the whole of 2010 is expected at 2.0 percent, the WIFO forecast for 2011 and 2012 is for rates of 2.2 percent and 2.0 percent, respectively.

Table 1: Main results

		2007	2008	2009	2010	2011	2012	
		Percentage changes from previous year						
GDP								
Volume		+ 3.7	+ 2.2	- 3.9	+ 2.0	+ 2.2	+ 2.0	
Value		+ 5.9	+ 4.1	- 3.1	+ 3.2	+ 3.8	+ 3.8	
Manufacturing¹, volume								
		+ 8.5	+ 3.5	- 14.0	+ 7.0	+ 6.5	+ 5.5	
Wholesale and retail trade, volume								
		+ 2.0	+ 0.9	- 1.4	+ 2.8	+ 1.0	+ 1.0	
Private consumption expenditure, volume								
		+ 0.7	+ 0.5	+ 1.3	+ 1.1	+ 0.9	+ 1.1	
Gross fixed investment, volume								
Machinery and equipment		+ 6.6	+ 7.5	- 14.5	- 2.0	+ 4.5	+ 4.0	
Construction		+ 1.6	+ 1.6	- 6.0	- 4.0	+ 0.7	+ 0.8	
Exports of goods²								
Volume		+ 9.0	+ 0.3	- 18.7	+ 12.3	+ 8.3	+ 8.0	
Value		+ 10.5	+ 2.5	- 20.2	+ 16.0	+ 10.5	+ 9.1	
Imports of goods²								
Volume		+ 7.6	+ 0.2	- 15.1	+ 9.8	+ 6.5	+ 6.5	
Value		+ 9.6	+ 4.7	- 18.4	+ 14.6	+ 9.7	+ 8.1	
Current balance		billion €	+ 9.62	+ 13.76	+ 7.98	+ 10.54	+ 12.34	+ 14.15
As a percentage of GDP			+ 3.5	+ 4.9	+ 2.9	+ 3.7	+ 4.2	+ 4.6
Long-term interest rate³		in percent	4.3	4.4	3.9	3.2	3.0	3.1
Consumer prices			+ 2.2	+ 3.2	+ 0.5	+ 1.8	+ 2.1	+ 1.8
Unemployment rate								
Eurostat definition ⁴	in percent	4.4	3.8	4.8	4.5	4.4	4.5	
National definition ⁵	in percent	6.2	5.8	7.2	6.9	6.8	6.9	
Persons in active dependent employment⁶			+ 2.1	+ 2.4	- 1.4	+ 1.0	+ 0.6	+ 0.5
General government financial balance according to Maastricht definition								
As a percentage of GDP			- 0.4	- 0.5	- 3.5	- 4.1	- 3.1	- 2.7

Source: WIFO Economic Outlook. – ¹ Value added, including mining and quarrying. – ² According to Statistics Austria. – ³ 10-year central government bonds (benchmark). – ⁴ According to Eurostat Labour Force Survey. – ⁵ According to Public Employment Service Austria, as a percentage of total labour force excluding self employed. – ⁶ Excluding parental leave, military service.

The construction industry remains caught in the crisis, with activity barely picking up over the projection period. Private household consumption acted as a stabilising factor during the economic crisis and is set to follow an upward trend until the forecast horizon, although showing a slower momentum than economic activity overall. The main reason is moderate growth of private incomes, set to pick up only by 2012. The slow pace of private consumption will be mirrored by sluggish trade volume growth in 2011 and 2012.

¹ The growth carry-over denotes the impact of the growth profile within a given year on the annual growth rate of the following year. In 2010, the strong GDP growth in the second and third quarter yields a substantial contribution for 2011. The projected annual growth rate of 2.2 percent can thus be attained even with moderate quarter-on-quarter gains. For 2012, on the other hand, the smaller carry-over from 2011 dampens the annual growth rate despite the projected acceleration in the quarterly rates.

The moderate pace of GDP growth will also be reflected on the labour market. Employment, though steadily heading up, will lose momentum. With labour supply rising further at the same time, unemployment is unlikely to fall from present levels. The jobless rate for 2012 is projected at 6.9 percent on national definitions, equivalent to 4.5 percent in Eurostat terms.

The rate of inflation (CPI) will edge up to 1.8 percent in 2010 and 2.1 percent in 2011, driven by higher energy prices and several indirect tax hikes. Core inflation, however, will increase only little, given the weak upward pressure from unit labour cost. By 2012, the impact of rising energy and food prices will fade, as will the one-off effect of higher indirect taxes. Headline inflation should therefore abate to 1.8 percent.

Thanks to the swift cyclical recovery, the general government deficit for 2010 will turn out at 4.1 percent of GDP, lower than notified last autumn by the Ministry of Finance. The consolidation measures recently adopted should reduce the deficit ratio to 3.1 percent in 2011 and further to 2.7 percent in 2012.

The present forecast is subject to a number of risks: should the recent rise in government bond yields observed in a number of euro area countries continue, the difficulties in these countries' public finances could exacerbate, requiring even more drastic expenditure cuts. This in turn may dampen further aggregate demand in the euro area and jeopardise the stability of Economic and Monetary Union. A further risk surrounds the sluggish recovery in the USA. If financial conditions for private households and government authorities were to deteriorate, this could undermine overall demand and further delay the return to the medium-term growth path.

Growth of world trade has decelerated steadily since early 2010. After gains of 5.2 percent and 3.2 percent in the first and second quarter from the previous period respectively, the third quarter saw a seasonally-adjusted volume increase of only 0.9 percent, according to the Netherlands' Centraal Planbureau (CPB). Amidst the global cyclical recovery from the financial market and economic crisis, global trade has expanded vigorously since early 2009, meanwhile almost returning to its pre-crisis level.

Steady deceleration of world trade growth

The expansion of world trade slowed steadily during 2010, although trade dynamism exhibited significant regional differences. While 2011 may see a further slowdown, a tentative rebound is expected for 2012.

Table 2: World economy

	2007	2008	2009	2010	2011	2012
	Percentage changes from previous year					
<i>Real GDP</i>						
World	+ 5.3	+ 2.8	- 0.6	+ 4.5	+ 4.1	+ 4.6
USA	+ 1.9	± 0.0	- 2.6	+ 2.7	+ 2.2	+ 2.9
Japan	+ 2.4	- 1.2	- 5.2	+ 3.6	+ 1.6	+ 2.0
EU 27	+ 3.0	+ 0.5	- 4.2	+ 1.8	+ 1.7	+ 1.8
Euro area 16	+ 2.8	+ 0.5	- 4.1	+ 1.7	+ 1.5	+ 1.5
Germany	+ 2.7	+ 1.0	- 4.7	+ 3.6	+ 2.4	+ 2.0
New EU countries ¹	+ 5.9	+ 3.9	- 3.3	+ 1.9	+ 2.6	+ 3.6
China	+ 14.2	+ 9.6	+ 9.1	+ 10.5	+ 9.0	+ 9.0
World trade, volume	+ 7.1	+ 2.2	- 12.8	+ 16.0	+ 10.0	+ 10.0
Market growth ²	+ 7.1	+ 3.3	- 13.0	+ 12.3	+ 7.8	+ 7.8
<i>Primary commodity prices</i>						
HWI index, total	+ 3.7	+ 22.4	- 29.2	+ 35	+ 21	+ 13
Excluding energy	+ 9.5	+ 15.6	- 22.7	+ 39	+ 22	+ 19
<i>Crude oil prices</i>						
Brent, \$ per barrel	72.5	97.0	61.5	79	90	95
<i>Exchange rate</i>						
\$ per euro	1.371	1.471	1.393	1.33	1.25	1.20

Source: WIFO Economic Outlook. – ¹ Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania. – ² Real import growth of trading partners weighted by Austrian export shares.

During and after the crisis, however, the regional pattern was uneven, reflecting different speeds at which the global recovery proceeded. In the emerging markets,

notably in Asia, the positive turnaround occurred much earlier, with goods imports in the region by now well above their pre-crisis level. Yet, since the beginning of 2010, the momentum of the upswing has slowed. In the industrialised countries and in the euro area in particular, where the upturn began later, the momentum lasted longer and only slackened around the middle of the year. In these countries, merchandise imports are still substantially lower than at the time when the crisis broke. The slowdown of world trade growth is paralleled by the trend in global industrial output which likewise weakened gradually during 2010, both in the industrialised countries and the emerging market economies. One reason is that the repletion of inventories after the crisis has now largely been accomplished. Another one is that China and other developing countries are trying to prevent the boom from overheating and to slow the expansion of their economies. Nevertheless, Asia and Latin America will enjoy rapid growth also in 2011 and 2012, thereby providing major stimulus to the entire world economy. After a year-on-year increase of 16 percent in 2010, WIFO expects world trade volumes to expand by 10 percent each in 2011 and 2012.

In the third quarter 2010, the US economy grew by 0.6 percent from the earlier period, somewhat more strongly than in the three months before. Private consumption and business fixed investment in machinery and equipment posted healthy gains, while exports decelerated somewhat, in line with business conditions abroad. Construction investment continued its downward trend.

Recent indicators suggest that the recovery will continue, albeit at a more moderate pace. Retarding factors are the slower momentum of world trade, the slackening of the Asian boom and the expiry of cyclical policy stimulus. While the index of manufacturing output is still heading up, industrial orders already signal a slower expansion going forward. Indicators of consumer confidence are flat, likely reflecting the sluggish improvement of the labour market. The unemployment rate remains high, at 9.8 percent in November. The real estate market is still depressed, with the S&P-Case-Shiller index of house prices still pointing down.

Exports and industrial production should further develop favourably. Also private consumption looks set for sustained growth, even if the household saving ratio may remain substantially higher than before the crisis. A consumption and real estate boom such as the one propelling activity until 2007 will not recur in the years to come: private households need to unwind their high debt levels, and a rebound of activity in the construction and real estate sector is not in sight.

According to its latest announcements, the Fed will maintain its expansionary monetary stance. Additional fiscal stimulus, however, has become less likely after the outcome of last November's Congressional elections. WIFO projects US GDP to grow by 2.7 percent in 2010, 2.2 percent in 2011 and 2.9 percent in 2012.

The euro area economy edged up by 0.4 percent in the third quarter from the previous period. After the strong second quarter, the recovery has thus lost somewhat momentum. Despite the slowdown in world trade growth, business activity was also in the third quarter mainly supported by rising exports. Private and public consumption strengthened likewise, whereas gross fixed investment remained flat.

Current cyclical indicators for manufacturing industry in the euro area remain upward bound. Although incoming orders edged down in September from the previous month, the business survey conducted by the European Commission showed for October and November a significant improvement of output expectations and new orders. Industrial production rebounded in October and capacity utilisation rose to 77.6 percent at the beginning of the fourth quarter, far above the trough of mid-2009 (69.6 percent), though still somewhat below the long-term average of 81.2 percent.

Demand from Asia is unabated and stimulates activity in countries having a competitive export industry. Especially in Germany (+0.7 percent quarter-on-quarter) and several other countries with strong trade links to the German economy (like Austria or Slovakia) GDP rose substantially in the third quarter. The economies, however,

Moderate growth in the USA

The US economy remains on a moderate upward trend. Although growth should pick up towards the forecast horizon, a private consumption and real estate boom of the kind observed before the crisis will not recur. WIFO projects GDP growth at 2.2 percent for 2011 and 2.9 percent for 2012.

Two-speed pattern of euro area economic performance

which had markedly lost competitiveness since entering Monetary Union and where growth before the crisis was driven by booming private consumption and real estate values or by swift public spending increases (Greece, Ireland, Portugal and Spain) are caught in stagnation or continued recession. GDP growth in the third quarter turned out below expectations also in France and Italy.

While in Germany cyclical indicators are steadily pointing upward, they are broadly stagnating in many other euro area countries. The wide discrepancies in external competitiveness continue to persist. In addition, countries, in particular the southern Europeans and Ireland, have adopted comprehensive measures to consolidate public finances which will dampen aggregate demand over the coming years and heighten the danger of persistence of or relapse into recession. The euro area may thus develop a two-speed recovery, dampening growth prospects for the area altogether. The WIFO projection is for GDP growth of 1.7 percent in 2010 and 1.5 percent in 2011 and 2012, respectively.

In the East-central European countries, the cyclical profile remains uneven. The economies entertaining close trade links with Germany emerged earlier from the crisis and posted strong GDP growth rates in the third quarter 2010. In Poland, the Czech Republic and Hungary, the strong expansion observed in 2010 should extend into 2011 and 2012. The economies of Bulgaria and Romania are likely to stagnate or contract further in 2010, with a tentative rebound in GDP only to be expected over the next few years.

In the Baltic States, the recession after the crisis was particularly severe. Although the economies have meanwhile resumed growth, the pre-crisis levels have not yet been attained. For the eight new EU member countries in East-central Europe, WIFO expects GDP growth of 1.9 percent for 2010, followed by 2.6 percent in 2011 and 3.6 percent in 2012.

Demand and output in Austria expanded markedly in 2010; in the third quarter, GDP edged up by 0.9 percent from the previous period. Exports were the key growth driver, notably deliveries to Germany, thereby stimulating manufacturing production. The positive spill-over to investment in machinery and equipment has so far been hesitant. The upswing will continue into 2011, although the momentum should abate during the first half of the year, in parallel to the trend abroad. The slowdown of world trade growth and euro-area-wide fiscal restraint will dampen the rise in exports and the recovery altogether. While private investment is expected to pick up, the slowdown of activity will prevent the transition to a self-sustained investment cycle. As from mid-2011 and into 2012, business activity is likely to rebound. Due to a high growth carry-over from 2010, the annual GDP growth rate will be higher in 2011 than in 2012. After a rate of 2.0 percent in 2010, WIFO expects GDP to advance by 2.2 percent in 2011 and 2.0 percent in 2012.

Construction activity has not yet overcome the crisis and is unlikely to rebound substantially over the projection period. Private household consumption acted as a stabilising factor during the recession and is set to follow an upward trend until the forecast horizon, although showing a slower momentum than economic activity overall. The main reason is moderate growth of private incomes, set to pick up only by 2012. The slow pace of private consumption will be mirrored by sluggish trade volume growth in 2011 and 2012.

The present forecast is subject to a number of risks. The persistent fragility in the banking sector and of government finances in several euro area countries may exacerbate the fiscal situation and force the authorities to still more drastic retrenchment, with potentially adverse repercussions for area-wide aggregate demand. Those countries who have suffered massive losses of competitiveness, particularly vis-à-vis Germany, since entering EMU will be able to redress their situation only gradually in the absence of close policy co-ordination between member countries. This process implies wage losses and will constrain economic growth over a number of years. In this way, even the stability and internal cohesion of EMU may be put at risk.

The euro area is moving towards a two-speed cyclical profile. Germany and its neighbours with close economic ties benefit from the international upswing. However, the less competitive economies notably in southern Europe which, moreover, are affected by massive fiscal restraint, hold back the area-wide recovery. WIFO expects euro area real GDP to grow by 1.7 percent in 2010, followed by 1.5 percent each in 2011 and 2012.

Economies in East-central Europe gaining strength

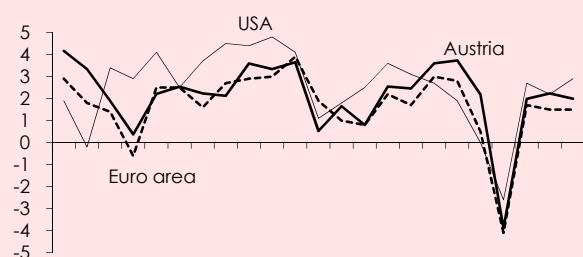
Cyclical upswing in Austria continues

The cyclical upturn in Austria is set to continue, with real GDP expected to grow by 2.2 percent in 2011 and 2.0 percent in 2012. However, the risks from the international environment are substantial.

Figure 1: Indicators of economic performance

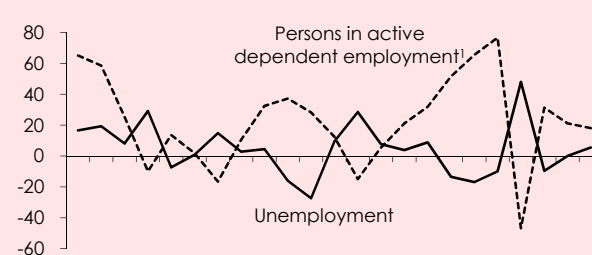
Growth of real GDP

Percent



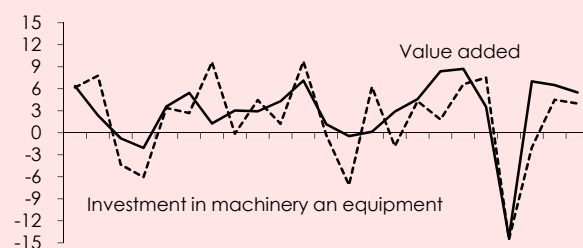
Employment and unemployment

1,000 from previous year



Manufacturing and investment

Percentage changes from previous year, volume



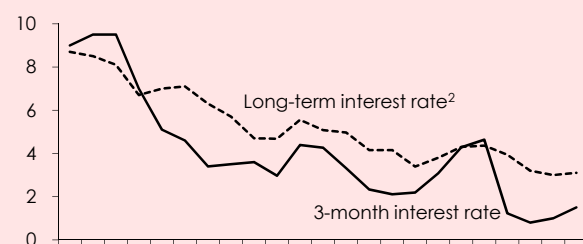
Consumption and income

Percentage changes from previous year, volume



Short-term and long-term interest rates

Percent



Inflation and unit labour costs

Percentage changes from previous year



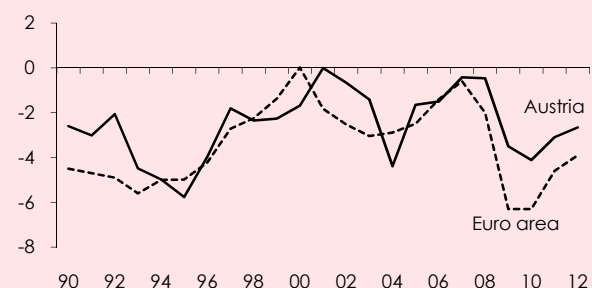
Trade

Percentage changes from previous year, volume



General government financial balance

As a percentage of GDP



Source: WIFO Economic Outlook. – ¹ Excluding parental leave, military service, and unemployed persons in training. – ² 10-year central government bonds (benchmark).

A further risk surrounds the possibility of a more sluggish recovery in the USA than assumed in the present context. If financial conditions for private households and government authorities were to deteriorate, this could undermine overall demand and further delay the return to the medium-term growth path.

The cyclical upswing in Austria has so far been largely driven by exports of goods, which is shaped by the trend of business activity in the major trading partner countries. The strong global recovery, and notably in Germany, has led to a swift expansion of Austrian exports (by 5.5 percent in volume quarter-on-quarter during the three months from July to September). In the first half of 2010, demand was particularly strong from Asia, mostly via exports to Germany. In the course of the year, also deliveries to Switzerland, Russia and the USA developed favourably.

In 2011 and 2012, the slowdown in world trade growth as well as in business activity in the USA and Asia, fiscal policy restraint and modest growth prospects for the euro area will all weigh on the export potential. However, the rebound in neighbouring eastern countries and a further strengthening of Austria's price competitiveness should allow gains in foreign market shares, facilitated also by a weaker euro exchange rate.

Despite the slowdown, world trade will give strong incentives to Austria's exports also in 2011. In 2012, demand and output should rebound at the international level, allowing exports to regain momentum. WIFO expects volume exports of goods to gain 8.3 percent in 2011 and 8.0 percent in 2012.

Growth of commodity imports will trail behind exports, in view of only moderate domestic demand for durable consumer goods and the expected gains in Austria's price competitiveness. Still, stronger corporate investment in machinery and equipment will also boost imports. Overall, the trade balance is nevertheless likely to improve markedly.

The rebound of exports was mirrored by a jump in manufacturing output in the third quarter. The regular WIFO business cycle survey suggests that the upward trend will continue: judgements on order levels improved markedly in October and November, and output as well as overall business expectations are upbeat. In parallel with exports, the expansion of manufacturing production will also shift into lower gear, even if the annual rate of output growth for 2011 will still be high due to the large carry-over from 2010. After a "soft patch" around mid-2011, the pace will re-accelerate on the back of stronger external demand and exports. Manufacturing value added, having gained 7 percent in volume in 2010, is forecast to increase by 6.5 percent and 5.5 percent in 2011 and 2012, respectively.

Of all components of aggregate demand, investment in machinery and equipment is the most cyclically-sensitive, determined by firms' sales and earnings expectations. In Austria, a cyclical upswing is usually initiated by an export push that is later transmitted to machinery and equipment investment. In the second quarter 2010, the fall in investment came to a halt, but a pick-up has been subdued so far. In the third quarter, corporate spending on new business equipment edged up by a mere 0.2 percent in volume from the previous period, although purchases of new machinery rebounded more markedly.

Capacity utilisation has improved importantly since the deep cut during the recession, meanwhile nearly returning to its pre-crisis level. The positive trend in earnings should also raise firms' appetite for spending on new fixed capital. WIFO projects an increase in machinery and equipment investment by 4.5 percent in volume for 2011, followed by +4.0 percent in 2012.

Construction activity remains caught by the crisis. Part of the fiscal stimulus measures are about to expire and have been unable to offset the shortfall in private demand. Residential building suffers from greater caution on the part of private households to incur new debt, in view of uncertain income and job prospects. Even more important is the strain in public finances of the Länder inducing them to less generous granting of housing subsidies. Demand remains sluggish also for commercial building, although the WIFO business cycle survey indicates some improvement in the course of the year. New orders for commercial structures have recently exceeded

Upswing continues to be export-driven

The cyclical upturn has so far been pulled by exports of goods. With the expected slowdown in global trade growth, deliveries abroad are set to lose momentum. Yet, the latter should be sustained by the strengthening competitive position of the Austrian economy.

Buoyant manufacturing activity

The revival of exports gave rise to strong industrial output gains also in the third quarter. The pace is set to decelerate pari passu with exports.

Fall in investment turning around

The downturn of investment has bottomed out since spring 2010. This indicates a tentative transition from export- to investment-led growth. Going forward, investment is expected to gain momentum.

Construction remains struck by the crisis

expectations and look set for further gains over the projection period as the recovery proceeds and machinery and equipment investment picks up. No turnaround is in sight for civil engineering, where output is likely to contract further given the consolidation efforts at all government levels and cutbacks in infrastructure planning. Total construction value added, after a fall by around 5 percent in 2010, is forecast to edge up by only 0.7 percent in 2011 and 0.8 percent in 2012.

Value added of the construction sector continued to recede in 2010, in spite of the rebound in manufacturing industry and the incentives provided by the fiscal stimulus programmes. The sharp fall will hardly be compensated by a gradual pick-up expected for 2011 and 2012.

Table 3: Productivity

	2007	2008	2009	2010	2011	2012
	Percentage changes from previous year					
<i>Total economy</i>						
Real GDP	+ 3.7	+ 2.2	- 3.9	+ 2.0	+ 2.2	+ 2.0
Employment ¹	+ 1.7	+ 2.2	- 0.8	+ 1.0	+ 0.7	+ 0.5
Productivity (GDP per employment)	+ 2.0	- 0.0	- 3.1	+ 1.0	+ 1.5	+ 1.5
<i>Manufacturing</i>						
Production ²	+ 8.7	+ 3.5	- 14.3	+ 7.0	+ 6.5	+ 5.5
Employees ³	+ 2.6	+ 1.7	- 6.0	- 1.3	+ 0.7	- 0.8
Productivity per hour	+ 6.3	+ 2.3	- 5.4	+ 4.7	+ 5.4	+ 6.4
Working hours per day per employee ⁴	- 0.3	- 0.5	- 3.6	+ 3.5	+ 0.3	- 0.0

Source: WIFO Economic Outlook. – 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.

Private consumption was a stabilising factor of activity during the recession. Even at the peak of the crisis in 2009, it expanded by 1.3 percent year-on-year. In 2010, household spending gained 1.1 percent in volume, and the projection is for further increases of 0.9 percent in 2011 and 1.1 percent in 2012.

Private consumption resilient, but lacking dynamism

Especially the outlays for non-durable consumer goods and services kept growing steadily during the crisis. Spending on durable consumer goods receded, however, in 2010, mainly as a technical correction of large-scale advance purchases of motor cars in 2009 motivated by the fiscal car scrapping premium. It is only as from 2012 that expenditure on consumer durables can be expected to rebound.

Private consumption and retail trade were stabilising factors of activity during the recession. Over the forecast period they will continue to head up, their momentum however being subdued, mainly owing to slow growth of private incomes.

Table 4: Private consumption, income and prices

	2007	2008	2009	2010	2011	2012
	Percentage changes from previous year					
Private consumption expenditure	+ 0.7	+ 0.5	+ 1.3	+ 1.1	+ 0.9	+ 1.1
Durables	+ 2.6	+ 1.7	+ 5.2	- 1.0	- 0.8	+ 0.8
Non-durables and services	+ 0.5	+ 0.3	+ 1.0	+ 1.3	+ 1.1	+ 1.1
Household disposable income	+ 2.3	+ 0.9	- 0.0	+ 0.8	+ 0.4	+ 1.0
As a percentage of disposable income						
Household saving ratio ¹	11.6	11.8	11.1	10.6	10.2	10.0
Household saving ratio ²	11.2	11.6	10.4	10.2	9.7	9.6
Percentage changes from previous year						
Direct lending to domestic non-banks ³	+ 3.6	+ 7.4	- 1.3	+ 2.5	+ 4.0	+ 4.8
Percentage changes from previous year						
Inflation rate						
National	2.2	3.2	0.5	1.8	2.1	1.8
Harmonised	2.2	3.2	0.4	1.8	2.1	1.9
Core inflation ⁴	1.9	2.4	1.5	1.3	1.6	1.7

Source: WIFO Economic Outlook. – ¹ Including adjustment for the change in net equity of households in pension fund reserves. – ² Excluding adjustment for the change in net equity of households in pension fund reserves. – ³ End of period. – ⁴ Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

Thus, private consumption is set to grow steadily over the forecast period, but at a rate below overall GDP. The main reason is the sluggish advance of real disposable income over the entire period. Low wage settlements for the public sector will weigh on per-capita gross earnings in 2011. With headline inflation edging up, net real wages will even decrease in 2011. Only by 2012 will public and private sector wages

move in parallel, implying a small gain in net real wages. Wage drift, which was negative during the crisis, should turn around over the forecast period. With the business cycle revival, effective earnings will surpass contractual wage gains, thereby boosting per-capita wages. Whereas the fiscal consolidation measures will dampen income growth, private households are likely to partly accommodate the squeeze by a further reduction in the saving ratio.

Table 5: Earnings and international competitiveness

	2007	2008	2009	2010	2011	2012
	Percentage changes from previous year					
Gross earnings per employee ¹	+ 3.1	+ 2.9	+ 1.5	+ 1.4	+ 2.0	+ 2.3
Gross real earnings per employee ²	+ 0.9	- 0.3	+ 1.0	- 0.4	- 0.1	+ 0.5
Net real earnings per employee ²	+ 0.9	- 0.9	+ 2.7	- 0.7	- 0.4	+ 0.2
<i>Total economy</i>						
Unit labour costs	+ 0.9	+ 2.7	+ 4.8	+ 0.6	+ 0.5	+ 0.8
<i>Manufacturing</i>						
Unit labour costs	- 2.3	+ 1.1	+13.5	- 5.0	- 3.1	- 3.2
Effective exchange rate, manufactures						
Nominal	+ 1.2	+ 1.1	+ 0.7	- 2.5	- 1.2	- 0.6
Real	+ 0.8	+ 0.6	+ 0.4	- 2.5	- 1.0	- 0.8

Source: WIFO Economic Outlook. – ¹ Employees according to National Accounts definition. – ² Deflated by CPI.

Steady consumption growth benefited turnover and earnings of the trade sector, where value added expanded by 2.8 percent in 2010, above expectations. Wholesale trade in particular was boosted by the upswing in manufacturing. In 2011 and 2012, trade volumes should rise in step with private consumption expenditure. WIFO expects real growth at 1.0 percent per year.

Demand for tourism services is flat in real terms, as value added of hotels and restaurants remains on a downward trend until 2011. Demand is sluggish from both foreign and domestic customers. Nevertheless, the net external surplus on tourism services is sustained by lower spending of domestic travellers abroad. Value added of the tourism sector is unlikely to pick up before 2012.

Higher energy prices, subsequently spilling over to manufactured goods, have led to a pick-up in the annual inflation rate to 1.8 percent for 2010 from the extremely low value for 2009. Some further upward pressure from this side will be felt also in 2011. As part of the government's fiscal consolidation efforts, several indirect taxes and excises will be raised (e.g., mineral oil tax, tobacco tax), adding some 0.4 percentage points to headline inflation for 2011. Upward pressure will be further enhanced by hikes for agricultural commodities on world markets, driving up food prices for consumers. Inflation is thus likely to accelerate to 2.1 percent on annual average 2011.

In 2012, the impact of higher energy and food prices should fade, as will the one-off effect of the indirect tax hikes. Core inflation should barely pick up, in view of the moderate behaviour of unit labour cost over the forecast period. Overall inflation should therefore abate to 1.8 percent on annual average.

With the cyclical recovery, the labour market has improved noticeably. In November 2010, the number of registered unemployed was 13,000 lower than one year ago. As demand and output head further up, employment will increase by an expected 1.0 percent for the whole of 2010. Going forward, however, job creation is set to decelerate in parallel to the slower momentum of output growth. For 2011 and 2012, WIFO expects the number of persons in dependent active employment to increase by 0.6 percent and 0.5 percent, respectively, not enough for further inroads to be made into unemployment, as labour supply will grow at the same time. The

No relief for the tourism industry

Inflationary pressure remains subdued

Higher energy prices and several indirect tax hikes are pushing up consumer prices in 2010 and 2011, while the cyclical component of inflation is largely absent. For 2011, WIFO expects a headline inflation rate of 2.1 percent, abating to 1.8 percent in 2012.

No further improvement in labour market conditions

expected cuts in public spending on active labour market policy, the shift in population structure towards age brackets with high labour force participation (45 to 55 year olds) and the introduction of a guaranteed minimum income will all make for a higher labour force. An element of uncertainty in this regard is the imminent liberalisation of access for workers from the new EU member countries. The present forecast assumes that the implicit impact on the supply of dependent labour will be marginal. After a fall by 9,600 persons in 2010, total unemployment is expected to stabilise over the forecast period. By 2012, the jobless rate should equal 6.9 percent of the dependent labour force or 4.5 percent according to Eurostat definitions.

Employment followed an upward trend in 2010. Going forward, however, the creation of new jobs will level off, leaving the unemployment rate close to a high 7 percent by 2012.

Table 6: Labour market

		2007	2008	2009	2010	2011	2012	
		Changes from previous year, in 1,000						
<i>Demand for labour</i>								
Persons in active employment ¹		+ 68.6	+ 84.2	- 40.6	+ 38.0	+ 27.2	+ 23.5	
Employees ²		+ 65.5	+ 76.7	- 46.8	+ 31.3	+ 21.2	+ 18.0	
<i>Percentage changes from previous year</i>		+ 2.1	+ 2.4	- 1.4	+ 1.0	+ 0.6	+ 0.5	
Nationals		+ 43.6	+ 53.2	- 41.2	+ 14.4	+ 8.3	+ 8.5	
Foreign workers		+ 21.9	+ 23.5	- 5.6	+ 16.9	+ 12.9	+ 9.5	
Self-employed ³		+ 3.1	+ 7.5	+ 6.2	+ 6.7	+ 6.0	+ 5.5	
<i>Labour supply</i>								
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 ⁴		+ 51.7	+ 74.2	+ 7.5	+ 28.4	+ 27.2	+ 29.0	
<i>Surplus of labour</i>								
Registered unemployed ⁵		- 16.9	- 10.0	+ 48.1	- 9.6	±0.0	+ 5.5	
In 1,000		222.2	212.3	260.3	250.7	250.7	256.2	
Unemployed persons in training ⁵		in 1,000	52.7	50.5	64.1	73.2	67.5	62.5
		In percent						
<i>Unemployment rate</i>								
Eurostat definition ⁶		4.4	3.8	4.8	4.5	4.4	4.5	
As a percentage of total labour force ⁵		5.6	5.2	6.4	6.2	6.1	6.2	
National definition ^{5,7}		6.2	5.8	7.2	6.9	6.8	6.9	
<i>Employment rate</i>								
Persons in active employment ^{1,8}		64.9	66.1	65.2	65.6	65.7	65.9	
Total employment ^{6,8}		71.4	72.1	71.6	71.8	71.9	71.9	

Source: WIFO Economic Outlook. – ¹ Excluding parental leave, military service. – ² According to Federation of Austrian Social Security Institutions. – ³ According to WIFO. – ⁴ Persons in active employment plus unemployment. – ⁵ According to Public Employment Service Austria. – ⁶ According to Eurostat Labour Force Survey. – ⁷ As a percentage of total labour force, without self-employed. – ⁸ As a percentage of population of working age (15 to 64 years).

The creation of new jobs will be concentrated on the service sector. Overall productivity growth will therefore be moderate. Employment in manufacturing declined until end-2009, but has tentatively picked up since. Nevertheless, if hourly productivity continues its recent strong advances, manufacturing may lose jobs even with favourable cyclical conditions persisting.

It should be noted that the official employment records established by the social security administration contain some distortions. It is envisaged that starting in 2011 a new centralised and time-consistent data base will be implemented. In this context, employment series are to be re-calculated retroactively as from January 2008, with possible implications also for employment growth rates.

Like in most other industrialised countries, fiscal policy in Austria largely contributed towards stabilising demand and output during the global economic crisis, at the expense of a substantial increase in the government deficit. Yet, the cyclical revival in 2010 generated tax revenues above the budgetary plans, yielding a general government deficit of 4.1 percent of GDP for the year.

Strengthening business activity and fiscal re-trenchment narrowing the budget deficit

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.

Carry-over (in economic growth)

The carry-over identifies the impact of the dynamics of a series (in seasonally adjusted figures) during one year (t_0) on the annual percentage change in the following year (t_1). It is defined as the annual percentage change in year t_1 , if GDP in t_1 remains constant at the level of the fourth quarter of year t_0 (in seasonally adjusted terms).

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/>).

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".

For 2011 and 2012, the government adopted fiscal consolidation measures amounting to € 2.6 billion (0.9 percent of GDP) and € 3.75 billion (1.2 percent of GDP), respectively. Slightly less than half of the total is accounted for by higher revenue, like hikes in indirect taxes (mineral oil tax, tobacco tax) and the introduction of a bank levy. Just over 50 percent of the consolidation amount is achieved via spending

cuts. In this way, the general government deficit will shrink to 3.1 percent of GDP in 2011 and 2.7 percent in 2012, assuming that the consolidation measures will actually be implemented and that the lower government levels (Länder and municipalities) will not exceed their deficit target of 0.6 percent of GDP. The measures will, according to the Ministry of Finance, stabilise the public debt ratio at around 72 percent of GDP as from 2013. However, a comprehensive assessment of government finances has to take into account also the rapidly rising off-budget financial obligations. For federal enterprises alone, the latter will increase from 8.7 percent of GDP in 2007 to 12.4 percent in 2011.

The further strengthening of business conditions and the fiscal consolidation measures adopted by the government will lead to a marked improvement of the budget balance. The general government deficit will narrow from 3.1 percent of GDP in 2011 to 2.7 percent in 2012.

Table 7: Key policy indicators

	2007	2008	2009	2010	2011	2012
	As a percentage of GDP					
<i>Fiscal policy</i>						
General government financial balance						
According to Maastricht definition	- 0.4	- 0.5	- 3.5	- 4.1	- 3.1	- 2.7
According to National Accounts	- 0.6	- 0.5	- 3.5	- 4.1	- 3.1	- 2.7
General government primary balance	+ 2.3	+ 2.1	- 0.8	- 1.4	- 0.4	+ 0.1
	In percent					
<i>Monetary policy</i>						
3-month interest rate	4.3	4.6	1.2	0.8	1.0	1.5
Long-term interest rate ¹	4.3	4.4	3.9	3.2	3.0	3.1
	Percentage changes from previous year					
<i>Effective exchange rate</i>						
Nominal	+ 1.1	+ 1.2	+ 0.9	- 2.5	- 1.2	- 0.6
Real	+ 0.7	+ 0.6	+ 0.4	- 2.5	- 1.0	- 0.8

Source: WIFO Economic Outlook. – ¹ 10-year central government bonds (benchmark).