WIFO ■ BULLETIN

No. 1/2014
January 2014

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Sluggish Private Consumption Holding Back the Pace of Recovery

Economic Outlook for 2014 and 2015

Abstract
Leading indicators are signalling an early revival of business activity in Austria, supported mainly by the catching up of investment so far withheld and by strengthening foreign demand from key destinations like Germany and the USA. Still, the momentum of the recovery remains muted as private consumption is constrained by modest wage gains, fragile labour market conditions and fiscal retrenchment. While inflation is set to ease slightly over the projection period, the rate of unemployment will edge up further in 2014.

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JEL-Codes: E32, E66 • **Keywords:** Business Cycle, Economic Outlook, Forecast

For definitions of terms used, see "Methodological Notes and Short Glossary", http://www.wifo.ac.at/wwadocs/form/WIFO-BusinessCycleInformation-Glossary.pdf • All staff members of the Austrian Institute of Economic Research contribute to the Economic Outlook. • Cut-off date: 17 December 2013

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ISSN 1605-4709 •
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In 2013, global economic growth decelerated for the third year in a row. Likewise, the expansion of world trade was lacking momentum, as a rather large part of it is accounted for by the exchange between the crisis-ridden countries of the euro area. With the better business conditions in prospect, trade volumes will pick up (2014 +5.0 percent, 2015 +6.5 percent), and world GDP growth is expected to strengthen gradually to rates of 3.6 percent in 2014 and 4.0 percent in 2015.

Austria's foreign trade is benefitting from a revival in key markets such as Germany, the USA and several countries in East-central Europe. In the regular WIFO Business Cycle Survey, business expectations of domestic firms have turned significantly more optimistic in recent months. The WIFO Leading Indicator points to a gradual recovery of activity, as the improvement on financial markets is extending to the real economy. Yet, the momentum of the recovery remains muted as private consumption is constrained by stagnating net real wages, fragile labour market conditions and fiscal retrenchment. Labour supply is boosted by one-off factors like stricter rules for the access to retirement and the opening of the labour market to workers from Bulgaria and Romania. Since job creation in 2014 will hardly keep pace with the rising labour force, the unemployment rate will edge up to 7.9 percent and remain flat in 2015.

Government finance developments are shaped by one-off factors (auction proceeds, tax agreements with Switzerland and Liechtenstein, capital transfers to banks) and new consolidation measures. The present projections assume tax increases and expenditure cuts improving the budget balance by some € 2 billion in 2014 and € 1 billion in 2015. The financial gap identified by the "accounts check" would, given its composition, have an only marginal expansionary effect that would have to be set against the restrictive impact of the additional consolidation measures expected. These altogether small effects working in opposite direction are likely to offset each other. Real GDP, having edged up by only 0.3 percent in 2013, is projected to grow by 1.7 percent each in 2014 and 2015.

Business conditions in the euro area have improved recently. Yet, fiscal restriction and low inflation complicate the reduction of private household and corporate debt that in a number of countries is very high and even rising in some. Private sector deleveraging is weighing on household consumption, investment and credit extension. With the upswing gaining ground, the current account deficits of the periphery countries may widen again; the external vulnerability of these countries thus remains a cyclical risk.

Table 1: Main results

		2010	2011	2012	2013	2014	2015
		Percentage changes from previous year					
GDP							
Volume		+ 1.8	+ 2.8	+ 0.9	+ 0.3	+ 1.7	+ 1.7
Value		+ 3.2	+ 4.9	+ 2.6	+ 2.3	+ 3.5	+ 3.6
Manufacturing[1], volume		+ 7.6	+ 8.3	+ 1.1	+ 0.8	+ 3.5	+ 4.2
Wholesale and retail trade, volume		+ 2.2	+ 1.3	– 1.7	– 1.3	+ 1.3	+ 2.0
Private consumption expenditure, volume		+ 2.0	+ 0.8	+ 0.5	– 0.1	+ 0.9	+ 1.0
Gross fixed investment, volume		– 1.4	+ 8.5	+ 1.6	– 1.4	+ 3.0	+ 2.1
Machinery and equipment		+ 2.1	+ 14.3	+ 2.1	– 3.5	+ 5.0	+ 3.0
Construction		– 3.9	+ 2.5	+ 2.5	+ 0.5	+ 1.2	+ 1.3
Exports of goods[2]							
Volume		+ 13.6	+ 8.1	+ 0.8	+ 2.5	+ 5.5	+ 6.5
Value		+ 16.7	+ 11.3	+ 1.5	+ 1.8	+ 6.6	+ 7.5
Imports of goods[2]							
Volume		+ 11.7	+ 8.6	– 1.3	+ 0.4	+ 5.5	+ 6.0
Value		+ 16.5	+ 15.3	+ 0.7	– 0.8	+ 6.3	+ 7.2
Current balance	billion €	+ 9.74	+ 4.90	+ 4.93	+ 9.65	+ 11.16	+ 12.18
As a percentage of GDP		+ 3.4	+ 1.6	+ 1.6	+ 3.1	+ 3.4	+ 3.6
Long-term interest rate[3]	percent	3.2	3.3	2.4	2.0	2.0	2.0
Consumer prices		+ 1.9	+ 3.3	+ 2.4	+ 2.0	+ 1.8	+ 1.9
Unemployment rate							
Eurostat definition[4]	percent	4.4	4.2	4.3	4.9	5.2	5.2
National definition[5]	percent	6.9	6.7	7.0	7.6	7.9	7.9
Persons in active dependent employment[6]		+ 0.8	+ 1.9	+ 1.4	+ 0.6	+ 0.8	+ 0.8
General government financial balance according to Maastricht definition							
As a percentage of GDP		– 4.5	– 2.5	– 2.5	– 1.9	– 2.0	– 1.6

Source: WIFO. 2013, 2014, 2015: forecast. – [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.

By restraining the purchases of bonds, the US Federal Reserve is about to change the course of monetary policy. Given the favourable real economic and financial conditions, business activity is unlikely to be adversely affected by this move. Fiscal consolidation in 2013 dented business activity only to a limited extent, since it largely relied on revenue-raising measures and private household indebtedness had already dropped markedly before. As suggested by the experience of October 2013, the debt ceiling at present covering expenditure overruns until mid-2014 is likely to be raised further in order to accommodate current government refinancing requirements.

While the VAT increase in 2014 will pull the Japanese economy out of deflation, it will at the same time weigh on business activity. A rise in nominal wages is not yet in sight. In Brazil, demand and output growth is constrained by higher import prices and interest rates, in India also by controls on capital mobility. China and Russia are both moving towards a slower path of potential output growth.

1. World trade resumes growing faster than global output

Growth of global output decelerated in 2013 for the third year in a row. Starting from the euro area, the cyclical slowdown extended to other advanced economies in Europe and overseas and supported the transition in some emerging economies towards lower rates of potential growth. Given the importance of trade among euro area countries, the region's share in world trade is significantly larger than its share in world output. World trade growth therefore continued in 2013 lagging behind the growth of world GDP. Over the forecast horizon, the industrialised countries' contribution to global GDP growth will increase at a somewhat faster pace than that of the emerging market economies, as world output growth is expected to pick up gradually to rates of 3.6 percent in 2014 and 4.0 percent in 2015. World trade will outpace GDP growth, expanding by 5.0 percent and 6.5 percent, respectively.

Table 2: World economy

	2010	2011	2012	2013	2014	2015
	Percentage changes from previous year					
Real GDP						
World	+ 5.2	+ 3.9	+ 3.2	+ 2.8	+ 3.6	+ 4.0
USA	+ 2.5	+ 1.8	+ 2.8	+ 1.7	+ 2.5	+ 3.1
Japan	+ 4.7	− 0.5	+ 1.4	+ 1.8	+ 1.9	+ 1.2
EU 28	+ 2.0	+ 1.7	− 0.4	± 0.0	+ 1.4	+ 1.8
Euro area 17	+ 2.0	+ 1.6	− 0.7	− 0.4	+ 1.1	+ 1.4
Germany	+ 4.0	+ 3.3	+ 0.7	+ 0.5	+ 1.7	+ 1.9
New EU countries[1]	+ 2.2	+ 3.3	+ 0.9	+ 1.3	+ 2.5	+ 3.0
China	+ 10.4	+ 9.3	+ 7.7	+ 7.7	+ 7.9	+ 7.3
World trade, volume	+ 14.6	+ 6.2	+ 2.0	+ 2.5	+ 5.0	+ 6.5
Market growth[2]	+ 11.9	+ 6.5	+ 1.7	+ 2.3	+ 5.5	+ 6.5
Primary commodity prices						
HWWI index, total	+ 28.9	+ 28.6	− 2.8	− 4.0	− 2	± 0
Excluding energy	+ 31.9	+ 19.2	− 14.4	− 7.0	+ 1	+ 2
Crude oil prices						
Brent, $ per barrel	79.5	111.3	111.6	108	105	105
Exchange rate						
$ per euro	1.327	1.392	1.286	1.32	1.30	1.25

Source: WIFO. 2013, 2014, 2015: forecast. – [1] Bulgaria, Czech Republic, Hungary, Latvia, Lithuania, Poland, Romania. – [2] Real import growth of trading partners weighted by Austrian export shares.

2. Change in monetary stance will not inhibit US upturn

The cyclical recovery of the US economy continues. Indebtedness of private households is abating steadily. The Federal Reserve is encouraging bank lending by targeted measures such as purchases of securitised assets. While the upward trend in asset values is fostering private consumption, it is also adding to risks: the price-to-earnings ratio on stock markets is already exceeding its long-term average, and purchases of real estate are increasingly financed via high-risk investment funds, with returns being leveraged by borrowing[1]. The unemployment rate eased to 7 percent in November. The Central Bank will therefore switch to a less accommodating

[1] IMF, Global Financial Stability Report, Box 1.1, Washington D.C., October 2013.

monetary stance by reducing its bond purchases. The key policy interest rate will only be raised in 2015.

Due to easier financing conditions and a better labour market situation, the cyclical upturn in the USA is able to withstand the increasingly difficult economic policy environment.

Business activity was little affected by fiscal consolidation in 2013, since the latter was largely based on higher revenues generated inter alia via higher social security contributions and tax surcharges on high incomes (top marginal tax rate, capital gains tax), only a small fraction of which is used for consumption. After the experience of the political parties with the raise of the debt ceiling in October 2013, the implicit risk for business activity appears to be lower going forward: the prospect of a severe damage to the world economy through cascade effects in the financial system and popular scepticism vis-à-vis an escalation strategy have eventually prevented a payment default. Although the debt ceiling has been waived only until 7 February 2014, government solvency may nevertheless be ensured up to June 2014, according to the Congressional Budget Office. The present forecast assumes that the debt ceiling will be adjusted in time. The rather benign performance of commodity prices lends support to the upward trend in industrial output observed since 2010. The exploitation of shale oil and shale gas keeps energy prices in the USA low, to the benefit notably of energy-intensive producers. The comparatively favourable conditions in the real economy as well as in the financial sector will therefore allow the crisis-related slump in investment to be made up rather quickly in the years to come. Real GDP is projected to expand by 2.5 percent in 2014 and by 3.1 percent in 2015.

3. Japan ridding itself from deflation via price shocks

Japan will raise VAT from 5 percent to 8 percent in 2014, and further to 10 percent in 2015. In this way, the country will disengage itself from deflation, although wage gains remain subdued.

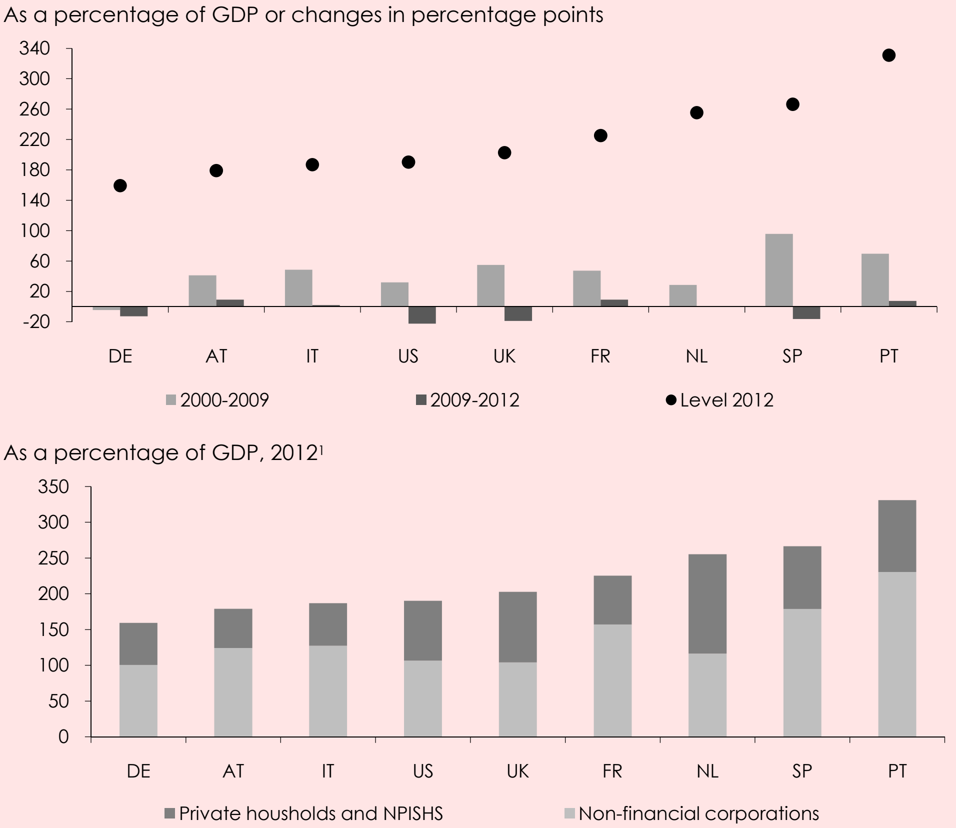
On Japan's financial markets, the announced ultra-expansionary monetary policy was anticipated as from early 2013 by a strong depreciation of the yen. The latter stimulated not only stock market values, but also private consumption. Also the traditionally highly competitive export sector benefited from the lower exchange rate. In the second quarter 2014, the VAT increase from 5 percent to 8 percent will act as a drag on economic activity, which is to be countered by a fiscal stimulus package worth 1 percent of GDP. In the first quarter large-scale pre-emptive buying is expected. A further increase in the VAT rate is envisaged for end-2015. With the depreciation of the yen, energy import prices ratcheted up substantially. Since after the nuclear disaster of Fukushima the majority of nuclear powerplants were switched off, the Japanese economy is even more reliant on energy imports. The VAT increase and higher energy prices will be reflected in the first significant increase in consumer prices since 1992 (with the exception of 1997 and 2008). However, core inflation is unlikely to head up, given the persistently sluggish wage developments. Owing to a substantial statistical carry-over from last year, real GDP is set to expand despite the VAT increase by 1.9 percent in 2014, followed by +1.2 percent in 2015.

4. Capital outflows and structural factors clouding the outlook for emerging economies

In 2013, demand and output growth lost considerable momentum in most of the major emerging market economies. India and Brazil which both rely on capital imports for financing their current account deficits suffered from a heavy drain of foreign capital triggered by the expectation of monetary tightening in the USA. The Brazilian real and the Indian rupee lost between 12 percent and 15 percent against the dollar since the beginning of 2013. The Brazilian Central Bank countered the implicit inflation risk by raising the key interest rate stepwise from 7.25 percent to 10 percent in the course of the year, while India introduced capital transaction controls. The dampening cyclical impact of these measures superposes in the short run the potential positive effects of currency devaluation on price competitiveness.

Countries enjoying positive current account balances like Russia and China were little or hardly affected by the international capital shifts. Nevertheless, their growth potential is set to decline. In China, where investment has fuelled growth for years and had reached a record ratio of 47 percent of GDP in 2012, marginal returns on investment are diminishing. This is reflected by the real estate market where entire urban quarters remain uninhabited in some areas. The Russian economy is approaching full utilisation of its productive capacity, with a jobless rate that, like in Brazil, has dropped below its pre-crisis level. The growth momentum remains subdued, given the modest performance of oil prices.

Figure 1: Private sector gross debt



Source: OECD. AT . . . Austria, DE . . . Germany, FR . . . France, IT . . . Italy, NL . . . Netherlands, PT . . . Portugal, SP . . . Spain, UK . . . United Kingdom, US . . . USA. – [1]) France: 2011.

5. High private sector indebtedness weighing on the euro area recovery

Incisive fiscal consolidation and low inflation complicate a reduction of the frequently high debt burden of private households and companies in many euro area countries. Deleveraging acts as a drag on consumption, investment and lending behaviour.

In the third quarter 2013, the euro area rid itself from recession as confidence indicators headed up. The outlook for 2014 and 2015 remains nevertheless subdued. An important factor holding back the recovery is the high level of private debt in many countries. Household debt is particularly high in the Netherlands (Figure 1) where demand is heavily squeezed by debt redemption and interest payments. Corporate debt burden is often higher than that of private households, especially in Portugal, Spain and France. In Italy, companies unable to service their debt from current earnings represent 30 percent of all outstanding debt, in Portugal and Spain 40 percent to 50 percent, in Germany and France only 10 percent[2]. The debt overhang acts as a serious constraint to investment. At the same time, a high stock of bad loans and enhanced equity capital requirements inhibit new lending by banks. In the USA, private households managed to reduce their debt burden since the onset of the financial market crisis, because the public sector was ready to accept a significant increase in its own debt over a longer period of time and insolvency legislation is much more debtor-friendly than in Europe. With the exception of Germany and Spain, private debt has hardly diminished in the euro area, and has even in-

[2] The Economist, Europe's other debt crisis, 26 October 2013.

creased further in some instances. Low inflation and fiscal restriction will continue to complicate debt reduction, adding to the risk of a negative output gap becoming entrenched with internal demand and bank lending sluggish. As fiscal consolidation hampers the reduction of household and corporate debt, high private indebtedness will in turn exacerbate the adverse cyclical effects of budgetary restriction with the private sector being liquidity-constrained.

Figure 2: Indicators of economic performance

Source: WIFO. 2013, 2014, 2015: forecast. – [1] Excluding parental leave, military service, and unemployed persons in training. – [2] 10-year central government bonds (benchmark).

Real GDP in the euro area is projected to expand by a modest 1.1 percent in 2014 and 1.4 percent in 2015. Growth will remain below the threshold of 1 percent p.a. inter alia in Italy, the Netherlands, Spain, Slovenia and Portugal. Growth is expected to exceed the euro area average in Germany, Finland, Austria and Slovakia.

6. ECB keeping expansionary stance, Bank of England shifting focus

Against this background it is questionable whether the latest interest rate cut to 0.25 percent by the ECB will have tangible positive effects. It is unlikely to stimulate private demand, since the reduction is marginal and no further substantial cut can be expected due to the zero-interest-rate lower bound. Moreover, under-capitalised commercial banks in some countries will not pass on the rate adjustment to the private sector. It will rather be taken as a move alleviating the financing of fragile institutions, further reducing their incentives to write off non-performing claims. In the UK, house prices have picked up, reviving the real estate sector. In response, the Bank of England has stopped its purchases of mortgage-backed assets and will shift the emphasis of its "funding for lending" programme towards the acquisition of securitised loans to small and medium-sized enterprises.

7. External vulnerability of the euro area remains a risk

Cyclical factors play an important role for the reduction of the current account deficits of the periphery countries. While the projected slight depreciation of the euro should exonerate the foreign trade balance, deficits may increase again in the case of an economic upswing.

The external balance positions of the crisis countries constitute a major downward risk for euro area business activity. The improvement in the current account balances over the last years was largely of a cyclical nature[3], whereas deficits are likely to widen again in a cyclical upswing. In Greece, deficit reduction was largely driven by lower imports which would rebound in a cyclical recovery. In Portugal, lower imports and higher exports contributed to about equal extent to the improvement of the country's external position. The current account balance of Spain improved primarily due to higher exports whereby cyclical factors such as buoyant activity in the emerging market economies played an important role. While wage moderation led to a marginal increase in exports, the implicit dampening effect on imports weakened the current account balance of other periphery countries (Portugal in particular). A brighter domestic situation could thus enhance the external vulnerability of these countries if their current account deficits were to widen again, pushing up further the (already high) foreign debt.

With monetary easing in the USA gathering momentum since mid-2012 (operation Twist, QE 3), the euro exchange rate has regained ground vis-à-vis the dollar. Unlike in the euro area, however, monetary policy in the USA will be tightened over the forecast horizon, lowering the exchange rate to an expected $ 1.25 per euro by 2015 and providing some relief for the external position of the crisis countries.

8. Austria: latest pick-up in business activity but tentative

Having stagnated during the first six months of 2013, Austria's real GDP headed up by 0.2 percent in the third quarter from the previous period. Domestic demand remained flat, although both private consumption and gross fixed investment increased slightly; however, total investment kept receding, albeit at a slower pace. Foreign trade provided positive stimulus, as exports grew by 0.4 percent in the third quarter, after +0.3 percent between April and June. The persistent weakness of domestic demand dampened imports which edged up by only 0.2 percent in the third quarter.

[3] IMF, World Economic Outlook, Box 1.3, Washington D.C., October 2013.

8.1 Positive demand incentives from major trading partners

Foreign trade is benefiting from the upturn of business activity in major destinations like Germany and the USA.

Business conditions in Germany, Austria's largest export market, are expected to further improve over the forecast horizon. Although wages are set to rise only moderately, the benign labour market situation will sustain private consumption. The initiation of the "Macro-economic Imbalance Procedure" by the European Commission has nourished the perception that German domestic demand, and notably investment, is lacking dynamism. The new German government may therefore step up public investment which had been cut in the course of fiscal consolidation since 2011. Given the easy financing conditions, this may trigger additional private investment and reinforce the upward trend observed since the second quarter 2013. German exports which due to the close trade links have a significant impact on activity in Austria, are expected to grow briskly in 2014 and 2015, albeit less than in recent years due to slackening GDP growth in the emerging market economies. In particular exports of machinery to China will be affected by the country's investment boom levelling off. Also Chinese motor car imports are increasingly replaced by local production intended to better accommodate to domestic market requirements[4].

Italy, Austria's second-largest foreign market, is unlikely to provide substantial stimulus: GDP is expected to edge up but marginally in 2014, due to sluggish corporate earnings, poor sales prospects and the pro-cyclical stance of fiscal policy. Apart from receding demand and constrained bank lending, Italy suffers from a number of structural impediments holding back a cyclical recovery, like a highly inefficient judicial system. Prospects are better for some of Autria's trading partners in Eastern Europe. Poland and Slovakia may expect GDP growth attaining or even exceeding 3 percent by 2015. However, the recovery in the Czech Republic and Hungary is likely to prove less buoyant.

Growth of Austria's merchandise exports is projected to accelerate from 2.5 percent in 2013 to 5.5 percent in 2014 and 6.5 percent in 2015. Due to the high import content of exports and the rebound of domestic investment, merchandise imports will pick up from stagnation in 2013 to +5.5 percent in 2014 and +6.0 percent in 2015. The terms-of-trade and the real-effective exchange rate will head further up somewhat in 2014 before easing in 2015.

8.2 Confidence indicators signalling cyclical recovery

Surveys among domestic companies suggest a moderate cyclical recovery being under way. Following the pick-up in financial indicators observed in late 2012, the components of the WIFO Leading Indicator monitoring the real economy have also been pointing up lately.

According to the regular WIFO Business Cycle Survey, the balance of business expectations expressed last November was positive by the mayority of its subcategories for the first time since November 2011. The outlook has steadily improved during the last few months, albeit at a slow pace. The expectations indicator climbed in particular for the production of manufactures and intermediate goods. Since output of these items typically rebounds at the beginning of an economic upturn, the signs are for an early cyclical recovery. In addition, the order situation in manufacturing has probably turned around, as the downward trend observed since the middle of 2011 has been arrested in the last few months. In November, the assessment of order levels improved markedly. Likewise, the "economic barometer" developed by the Austrian Business Chamber (WKO) had increased in the survey conducted last autumn. For the first time since 2010, the business expectations indicator exceeded the assessment of current business conditions, which is normally the sign of a cyclical turning point. Nevertheless, the general sentiment is still at a low level; firms have cautious expectations for employment and investment, suggesting that the upswing will take hold only gradually.

The WIFO Leading Indicator rose in November for the fourth consecutive month, staying firmly in positive territory. One year ago, the Indicator had reacted mainly to the improvement in stock markets, values and its values became less negative; the

[4] Deutsche Bundesbank, "Zu den Ursachen für die jüngste Schwäche der deutschen Warenexporte nach China"/*Reasons for the latest weakening of German merchandise exports to China*, Monatsbericht/*Monthly Report*, November 2013.

latest positive Indicator readings were driven by upbeat output expectations of domestic manufacturers, the slight (seasonally-adjusted) increase in job vacancies and the hike in the German Ifo Business Climate Index. The fact that the initial brightening of the financial market outlook is now being followed by better key figures for the real economy confirms expectations for a steady, but gradual recovery.

Investment in machinery and equipment, having declined by 3.5 percent in 2013, will catch up on projects so far postponed and expand by a projected 5 percent in 2014, abating to +3 percent in 2015. Construction investment will also profit from the cyclical upswing. While demographic developments fuel demand for new buildings, the fiscal consolidation programme extending over several years constitutes a downward risk. Overall, construction investment is expected to pick up from +0.5 percent in 2013 to +1.2 percent in 2014 and +1.3 percent in 2015.

Initially, the cyclical revival is benefiting from the catching up of investment so far withheld. Residential construction is exposed to a dilemma between rising demand for demographic reasons on the one hand, and the need for fiscal consolidation on the other.

Table 3: Productivity

	2010	2011	2012	2013	2014	2015
	Percentage changes from previous year					
Total economy						
Real GDP	+ 1.8	+ 2.8	+ 0.9	+ 0.3	+ 1.7	+ 1.7
Employment[1]	+ 0.7	+ 1.8	+ 1.4	+ 0.6	+ 0.8	+ 0.9
Productivity (GDP per employment)	+ 1.0	+ 1.0	– 0.5	– 0.3	+ 0.8	+ 0.9
Manufacturing						
Production[2]	+ 7.8	+ 8.3	+ 1.2	+ 0.8	+ 3.5	+ 4.2
Employees[3]	– 1.3	+ 1.9	+ 1.7	± 0.0	+ 0.1	+ 0.3
Productivity per hour	+ 6.0	+ 6.4	+ 0.1	+ 0.9	+ 3.0	+ 3.9
Working hours per day per employee[4]	+ 3.0	– 0.1	– 0.6	– 0.1	+ 0.4	± 0.0

Source: WIFO. 2013, 2014, 2015: forecast. – [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.

8.3 Private consumption lending no support to the upswing

The inflationary impact of the consolidation measures newly adopted can at present be roughly estimated only. They are expected to raise headline inflation by 0.1 percentage point each in 2014 and 2015. Consumer prices would thus increase by an annual rate just below 2 percent, corresponding to the ECB's inflation target for the euro area. For the latter, however, the ECB expects an average rate of little more than 1 percent, the main reason being the cyclical sluggishness and the stagnation or decline of wages in the periphery countries. In Austria, energy prices will rise in step with the gentle upward trend of oil prices, while the drift of food prices should ease. The high level of unemployment will keep wage dynamics in check and core inflation stable. The slight increase in gross real wages per capita will be neutralised by fiscal drag, making for stagnation of net real income per capita. Starting from 2014, the wage ratio (as percent of net national income) will resume its downward trend. Private consumption is projected to edge up by only 1 percent on annual average 2014-15, providing a smaller contribution to GDP growth than in earlier periods of cyclical upswing. Real GDP, having gained a modest 0.3 percent in 2013, is expected to grow by 1.7 percent each in 2014 and 2015.

Inflationary pressure from energy and food prices will ease somewhat over the projection period. Due to the moderate wage dynamics, private purchasing power remains nevertheless subdued.

8.4 Supply-driven increase in unemployment set to continue

While part-time employment gained further ground in 2013, the number of full-time jobs declined, leading to another fall in hours worked per employee. Also the actual working time of full-time workers diminished, due to a reduction in overtime working hours. This trend is expected to continue over the forecast period, such that employment as measured by the number of hours worked will grow less than the number of persons in active employment. The latter is projected to expand by 0.8 percent p.a., in line with the long-term average, which however will not suffice to accommodate the growing labour supply in 2014. The rate of unemployment is expected to ratchet up from 7.6 percent of the dependent labour force (national definition) in 2013 to 7.9 percent in 2014 and remain flat in 2015. Apart from the increase in the domestic labour force, labour supply developments over the forecast horizon are shaped by one-off factors starting in 2014, such as stricter rules for the

The increase in labour supply is driven by one-off factors like stricter rules for access to retirement and the opening of the labour market to workers from Romania and Bulgaria.

access to retirement and the opening of the labour market to workers from Bulgaria and Romania. In parallel, however, the inflow of workers from the new EU member states (2004) for which labour market access had been liberalised in May 2011 has abated. Given the rather benign labour market outlook for neighbour countries, the Austrian labour market is unlikely to receive additional pressure from the supply side.

Table 4: Private consumption, income and prices

	2010	2011	2012	2013	2014	2015
	Percentage changes from previous year					
Private consumption expenditure	+ 2.0	+ 0.8	+ 0.5	– 0.1	+ 0.9	+ 1.0
Durables	+ 1.6	+ 1.8	+ 0.6	– 4.8	+ 0.8	+ 1.5
Non-durables and services	+ 2.0	+ 0.7	+ 0.5	+ 0.4	+ 0.9	+ 0.9
Household disposable income	– 0.5	– 1.3	+ 1.1	– 1.3	+ 1.6	+ 1.7
	As a percentage of disposable income					
Household saving ratio[1]	8.9	6.7	7.4	6.3	7.0	7.5
Household saving ratio[2]	8.4	6.4	7.0	5.9	6.5	7.2
	Percentage changes from previous year					
Direct lending to domestic non-banks[3]	+ 2.9	+ 2.7	+ 0.0	– 0.2	+ 2.3	+ 2.1
	Percentage changes from previous year					
Inflation rate						
National	1.9	3.3	2.4	2.0	1.8	1.9
Harmonised	1.7	3.6	2.6	2.1	1.9	1.9
Core inflation[4]	1.2	2.8	2.3	2.2	1.9	1.8

Source: WIFO. 2013, 2014, 2015: forecast. – [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.

Table 5: Earnings and international competitiveness

	2010	2011	2012	2013	2014	2015
	Percentage changes from previous year					
Gross earnings per employee[1]	+ 0.9	+ 1.8	+ 2.4	+ 1.9	+ 2.1	+ 2.4
Gross real earnings per employee[2]	– 0.9	– 1.4	– 0.1	– 0.1	+ 0.3	+ 0.5
Net real earnings per employee[2]	– 1.1	– 1.8	– 1.1	– 0.5	± 0.0	+ 0.1
Unit labour costs						
Total economy	– 0.0	+ 0.8	+ 3.0	+ 2.2	+ 1.3	+ 1.5
Manufacturing	– 6.9	– 3.0	+ 3.0	+ 1.7	– 1.0	– 1.2
Effective exchange rate, manufactures						
Nominal	– 2.9	+ 0.1	– 1.7	+ 0.7	+ 0.4	– 0.1
Real	– 3.2	+ 0.5	– 1.7	+ 1.0	+ 0.5	– 0.2

Source: WIFO. 2013, 2014, 2015: forecast. – [1] Employees according to National Accounts definition. – [2] Deflated by CPI.

8.5 One-off factors and consolidation measures shaping the budgetary path

Between 2013 and 2015, the evolution of the budget balance is importantly determined by one-off effects, as from 2014 also by additional consolidation measures to be taken in order to keep public finances on track, following a thorough evaluation of federal revenue and expenditure ("accounts check") by the Ministry of Finance in autumn 2013. On the expenditure side, such one-off factors mainly derive from capital transfers to nationalised banks in distress. On the revenue side, one-off factors relate to tax agreements concluded with Switzerland and Liechtenstein, as well as to the auction of mobile phone licenses. While the capital transfers to banks will burden the budget balance in each year of the forecast period, the one-off receipts from the tax agreement with Switzerland will largely accrue in 2013, those from the agreement with Liechtenstein in 2014. The revenues from the auction of mobile phone licenses materialised in 2013 and, because of their large amount, were largely responsible for the reduction of the general government deficit (in the "Maastricht" definition) to 1.9 percent of GDP as compared with the WIFO projection of October 2013 anticipating a deficit of 2.6 percent of GDP. The somewhat lower capital transfer needed for Hypo Alpe-Adria-Bank AG, low debt service cost and tight budget execution also contributed to the lower-than-projected deficit turnout.

Table 6: Labour market

		2010	2011	2012	2013	2014	2015
		Changes from previous year, in 1,000					
Demand for labour							
Persons in active employment[1]		+ 37.4	+ 67.3	+ 51.7	+ 29.0	+ 32.5	+ 33.0
Employees[2]		+ 25.5	+ 63.3	+ 47.2	+ 20.0	+ 28.0	+ 28.0
Percentage changes from previous year		+ 0.8	+ 1.9	+ 1.4	+ 0.6	+ 0.8	+ 0.8
Nationals		+ 5.8	+ 25.7	+ 9.0	– 10.0	+ 2.0	+ 2.0
Foreign workers		+ 19.7	+ 37.7	+ 38.1	+ 30.0	+ 26.0	+ 26.0
Self-employed[3]		+ 11.9	+ 4.0	+ 4.5	+ 9.0	+ 4.5	+ 5.0
Labour supply							
Population of working age	15 to 64 years	+ 17.3	+ 31.3	+ 18.0	+ 14.0	+ 5.8	+ 8.1
	15 to 59 years	+ 4.9	+ 11.7	+ 22.3	+ 18.0	+ 5.6	+ 1.7
Labour force[4]		+ 27.9	+ 63.2	+ 65.6	+ 55.0	+ 48.5	+ 35.0
Surplus of labour							
Registered unemployed[5]		– 9.5	– 4.1	+ 13.9	+ 26.0	+ 16.0	+ 2.0
In 1,000		250.8	246.7	260.6	286.6	302.6	304.6
Unemployed persons in training[5]	in 1,000	73.2	63.2	66.6	73.6	77.6	80.6
		In percent					
Unemployment rate							
Eurostat definition[6]		4.4	4.2	4.3	4.9	5.2	5.2
As a percentage of total labour force[5]		6.2	6.0	6.3	6.8	7.1	7.1
National definition[5, 7]		6.9	6.7	7.0	7.6	7.9	7.9
Employment rate							
Persons in active employment[1, 8]		65.4	66.2	66.9	67.3	67.8	68.3
Total employment[6, 8]		71.7	72.1	72.5	72.3	72.5	72.9

Source: WIFO. 2013, 2014, 2015: forecast. – [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, excluding self-employed. – [8] As a percentage of population of working age (15 to 64 years).

Table 7: Key policy indicators

	2010	2011	2012	2013	2014	2015
	As a percentage of GDP					
Fiscal policy						
General government financial balance						
According to Maastricht definition	– 4.5	– 2.5	– 2.5	– 1.9	– 2.0	– 1.6
General government primary balance	– 1.8	+ 0.2	+ 0.1	+ 0.7	+ 0.4	+ 0.8
	In percent					
Monetary policy						
3-month interest rate	0.8	1.4	0.6	0.2	0.2	0.2
Long-term interest rate[2]	3.2	3.3	2.4	2.0	2.0	2.0
	Percentage changes from previous year					
Effective exchange rate						
Nominal	– 2.7	+ 0.2	– 1.5	+ 0.7	+ 0.4	– 0.2
Real	– 3.0	+ 0.6	– 1.6	+ 1.0	+ 0.4	– 0.2

Source: WIFO. 2013, 2014, 2015: forecast. – [1] 10-year central government bonds (benchmark).

The systematic evaluation of federal revenue and expenditure trends for the legislation period 2014-2018 carried out in the wake of the general election of autumn 2013 revealed further need for structural consolidation, if the budgetary trajectory outlined in the Austrian Stability Programme for the period 2012-2017 (dating from Spring 2013) were to be adhered to. The present projection assumes that in 2014 a lasting improvement of the general government balance of about € 2 billion will be achieved, reducing the structural deficit accordingly. For 2015, additional structural consolidation measures are assumed to take effect, to the tune of some € 1 billion. The correction measures assumed for 2014 consist to equal amount of higher revenues (restriction of tax concessions, tax increases for tobacco products, new car registration, sparkling wine etc.) and expenditure restraint (downward adjustment of retirement expenditure, wage moderation and personnel reduction in the public sector, cuts to discretionary spending etc.). For 2015, expenditure restraint is assumed to dominate revenue hikes. Moreover, a tight stance of budget execution and favourable debt financing conditions are extrapolated over the entire forecast horizon. On these assumptions, and allowing for expected one-off effects (mainly concerning bank support and tax revenues from the agreement with Liechtenstein), the general government ("Maastricht") deficit is projected at 2.0 percent of GDP for 2014, narrowing to 1.6 percent of GDP in 2015.

The budget projection remains subject to substantial risks and uncertainties. If the consolidation measures assumed were not to be implemented at all, or not to full extent, the deficits for 2014 and 2015 would turn out higher accordingly. In the absence of additional measures, the present forecast would expect the general government deficit at 2.6 percent and 2.4 percent of GDP for 2014 and 2015. In addition, the financial support required for the distressed nationalised banks may give rise to expenditure overruns and lead to a higher deficit than projected in the present context.