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Slackening Global Economic Activity Dampens Growth Prospects for Austria

Economic Outlook for 2019 and 2020

Slackening Global Economic Activity Dampens Growth Prospects for Austria. Economic Outlook for 2019 and 2020
The Austrian economy has entered a period of moderate growth. The strong momentum enjoyed over the last few years has eased, and firms are looking with less optimism into the future. While foreign trade has a restraining impact on output growth, domestic demand keeps supporting activity. Annual GDP growth in Austria is expected to decelerate from 2.7 percent in 2018 to 1.7 percent in the current year, stabilising at a rate of 1.5 percent in 2020.

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Economic growth in Austria has moderated from the last cyclical boom. Although domestic demand forces are still driving the economy forward, the underlying trend is currently subdued. Main reason is the slackening activity in manufacturing industry which is suffering from sluggish exports in the wake of the global business cycle downturn. Domestic private consumption maintains growth, supported by the solid increase in wages and employment.

In this kind of scenario, real GDP is set to gain 1.7 percent in 2019, hence 1 percentage point less than last year (+2.7 percent). The already high utilisation of productive capacity will not increase further, due i.a. to further investment being undertaken, preventing existing capacity constraints from further exacerbating. In 2020, projected GDP growth of 1.5 percent would be close to the longer-term trend.

Employment growth is set to ease with the slower pace of activity, and the fall in unemployment will grind to a halt, with the prospect of further reduction being vague: although new jobs will be created over the entire forecast period, this may not prevent unemployment from rising, as labour supply will continue to expand. Overall, the number of persons in active dependent employment is likely to increase by 1.6 percent in 2019 and by 1.0 percent in 2020. The jobless rate will edge down slightly to 7.4 percent in 2019 and remain broadly stable in 2020.

Since the last forecast revision, risks have further tilted to the downside and primarily derive from the external environment. Domestic risks, for their part, are on balance upward bound, given the continued support from employment and wages to private consumption. Nevertheless, in view of the downturn in manufacturing, Austria's economy remains highly vulnerable to external turbulence, with the risk of stronger spillovers to the domestic sector. On the whole therefore, downward risks from the external side dominate the outlook for the growth of GDP.

Table 1: Main results

		2015	2016	2017	2018	2019	2020
		Percentage changes from previous year					
Gross domestic product, volume		+ 1.1	+ 2.0	+ 2.6	+ 2.7	+ 1.7	+ 1.5
Manufacturing		+ 1.3	+ 3.5	+ 4.8	+ 4.7	+ 1.0	+ 1.6
Wholesale and retail trade		+ 1.9	+ 1.2	+ 1.1	+ 1.0	+ 1.2	+ 1.2
Private consumption expenditure[1], volume		+ 0.4	+ 1.4	+ 1.4	+ 1.6	+ 1.7	+ 1.6
Consumer durables		+ 1.9	+ 3.0	+ 0.5	− 1.4	− 1.0	+ 2.0
Gross fixed capital formation, volume		+ 2.3	+ 4.3	+ 3.9	+ 3.4	+ 2.3	+ 1.6
Machinery and equipment[2]		+ 4.3	+ 7.8	+ 4.2	+ 3.9	+ 2.4	+ 1.8
Construction		+ 0.1	+ 0.4	+ 3.5	+ 2.8	+ 2.1	+ 1.3
Exports, volume		+ 3.5	+ 2.7	+ 4.7	+ 4.4	+ 2.4	+ 2.7
Exports of goods, fob		+ 3.5	+ 2.1	+ 4.9	+ 5.0	+ 2.5	+ 2.9
Imports, volume		+ 3.6	+ 3.4	+ 5.1	+ 3.0	+ 2.3	+ 2.4
Imports of goods, fob		+ 4.1	+ 3.2	+ 4.2	+ 2.6	+ 2.2	+ 2.6
Gross domestic product, value		+ 3.3	+ 3.5	+ 3.8	+ 4.4	+ 3.4	+ 3.3
	billion €	344.26	356.24	369.90	386.06	399.07	412.15
Current account balance	as a percentage of GDP	1.7	2.5	2.0	2.3	1.8	1.8
Consumer prices		+ 0.9	+ 0.9	+ 2.1	+ 2.0	+ 1.6	+ 1.7
Three-month interest rate	percent	− 0.0	− 0.3	− 0.3	− 0.3	− 0.3	− 0.1
Long-term interest rate[3]	percent	0.7	0.4	0.6	0.7	0.3	0.5
General government financial balance, Maastricht definition	as a percentage of GDP	− 1.0	− 1.6	− 0.8	0.1	0.6	0.6
Persons in active dependent employment[4]		+ 1.0	+ 1.6	+ 2.0	+ 2.5	+ 1.6	+ 1.0
Unemployment rate							
Eurostat definition[5]		5.7	6.0	5.5	4.9	4.6	4.6
National definition[6]		9.1	9.1	8.5	7.7	7.4	7.5

Source: WIFO. 2019 and 2020: forecast. – [1] Including non-profit institutions serving households. – [2] Including weapons systems. – [3] 10-year central government bonds (benchmark). – [4] Excluding persons in valid employment contract receiving child care benefit or being in military service. – [5] As a percentage of total labour force, Labour Force Survey. – [6] As a percentage of dependent labour force, unemployed persons according to Public Employment Service Austria.

1. The starting situation

Austria's economy lately received strong stimulus from both domestic demand and external trade. Growth was driven by lively private consumption and firms' greater appetite for investment. Net exports also added to GDP growth.

In 2018, the Austrian GDP grew by 2.7 percent, at a similar pace as in the year before. During the year, however, the momentum slowed, with quarterly growth of 0.4 percent since the third quarter.

On the demand side, the cyclical slowdown has mainly been visible in foreign trade. Austria's exports performed well overall in 2018, but clearly lost momentum during the year with the global downturn. By contrast, the expansion of domestic demand remained stable. Private household consumption again expanded strongly, and companies continued to increase their investment in capital goods (machinery and equipment, and construction).

On the supply side, the slowdown manifested itself primarily in manufacturing. While industrial output kept growing, the pace slackened in parallel with foreign trade. However, developments in sectors mainly relying on internal demand proved highly resilient. Construction activity boomed for the second year in a row, and other business activities also performed strongly.

Private households benefitted from sizeable income gains in 2018. With rising employment and the sustained increase in nominal wages, compensation of employees grew by 4.7 percent year-on-year. Capital income (gross operating surplus and gross mixed income) rose by 4.7 percent, more or less like in the previous year.

On the back of buoyant output growth, the labour market improved further. Total employment kept rising and the jobless rate abated to 7.7 percent of the dependent labour force.

2. Framework conditions

The present forecast incorporates information on developments in the world economy, commodity prices, exchange rates and interest rates that has become available until mid-June 2019. The forecast horizon stretches from the second quarter of 2019 to the fourth quarter of 2020.

Table 2: International economy

	Percentage shares 2018		2015	2016	2017	2018	2019	2020
	Austria's exports of goods	World GDP[1]	GDP volume, percentage changes from previous year					
EU 28			+ 2.3	+ 2.0	+ 2.5	+ 2.0	+ 1.6	+ 1.6
EU 27	67.1	14.0	+ 2.3	+ 2.1	+ 2.6	+ 2.1	+ 1.6	+ 1.7
Euro area	52.0	11.4	+ 2.1	+ 1.9	+ 2.4	+ 1.9	+ 1.3	+ 1.5
Germany	30.2	3.2	+ 1.7	+ 2.2	+ 2.2	+ 1.4	+ 0.8	+ 1.5
Italy	6.5	1.8	+ 0.9	+ 1.1	+ 1.7	+ 0.9	+ 0.1	+ 0.7
France	4.3	2.2	+ 1.1	+ 1.1	+ 2.3	+ 1.7	+ 1.1	+ 1.2
CEEC 5[2]	14.5	1.6	+ 4.0	+ 2.9	+ 4.5	+ 4.5	+ 3.7	+ 3.1
Czech Republic	3.7	0.3	+ 5.3	+ 2.5	+ 4.4	+ 2.9	+ 2.5	+ 2.2
Hungary	3.4	0.2	+ 3.5	+ 2.3	+ 4.1	+ 4.9	+ 4.5	+ 3.1
Poland	3.2	0.9	+ 3.8	+ 3.1	+ 4.8	+ 5.1	+ 4.0	+ 3.4
USA	7.1	15.2	+ 2.9	+ 1.6	+ 2.2	+ 2.9	+ 2.5	+ 1.7
Switzerland	5.0	0.4	+ 1.3	+ 1.6	+ 1.6	+ 2.5	+ 1.4	+ 1.7
UK	2.8	2.2	+ 2.3	+ 1.8	+ 1.8	+ 1.4	+ 1.4	+ 1.3
China	2.7	18.7	+ 6.9	+ 6.7	+ 6.8	+ 6.6	+ 6.2	+ 5.8
Total[3]								
PPP-weighted[4]		51	+ 4.1	+ 3.4	+ 4.0	+ 4.0	+ 3.6	+ 3.2
Export weighted[5]	85		+ 2.4	+ 2.1	+ 2.6	+ 2.3	+ 1.8	+ 1.8
Market growth[6]			+ 3.6	+ 3.5	+ 6.6	+ 4.4	+ 2.4	+ 3.4
Forecast assumptions								
Crude oil prices								
Brent, $ per barrel			52.5	43.7	54.3	71.0	63	58
Exchange rate								
$ per €			1.110	1.107	1.129	1.181	1.12	1.11
Key interest rate								
ECB main refinancing rate[7], percent			0.1	0.0	0.1	0.0	0.0	0.0
10-year government bonds yields Germany, percent			0.5	0.1	0.3	0.4	– 0.0	0.1

Source: WIFO. 2019 and 2020: forecast. – [1] PPP-weighted. – [2] Czech Republic, Hungary, Poland, Slovenia, Slovakia. – [3] EU 27, UK, USA, Switzerland, China. – [4] Weighted by GDP at purchasing power parities in 2018. – [5] Weighted by shares of Austrian goods exports in 2018. – [6] Real import growth of trading partners, weighted by shares of Austrian goods exports. – [7] Minimum bid rate.

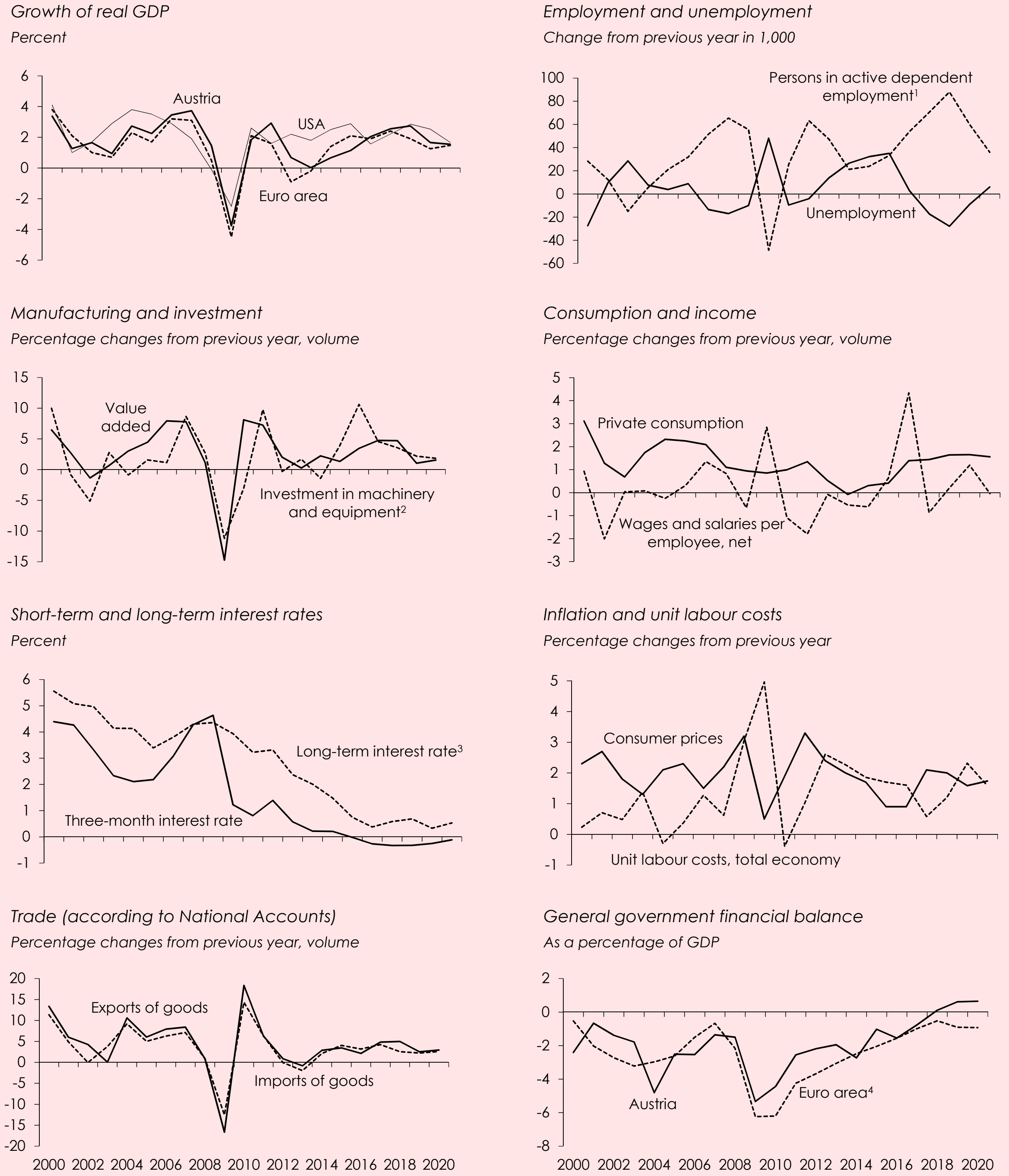
2.1 Gentle slowdown of global economic activity expected

Since the beginning of 2018, global growth of demand and output has been decelerating. Rising uncertainty and high policy risks are likely to have undermined the investment climate and international trade. Yet, the slowdown may also be taken as a return to normal conditions after the steep rise of 2017 in industrialised countries and emerging markets. At present, the world economy is characterised by a high degree of divergence.

Whereas a number of emerging market countries have started recovering from recession, the situation is deteriorating notably in Latin America (Argentina, Brazil and Mexico). Growth in China is also set to move to a still slower pace. The trade barriers recently introduced may, beyond this cyclical effect, weigh on China's growth prospects over the entire forecast period.

In the industrialised world and particularly in the USA, the recent period of robust growth may now be followed by a more moderate path of expansion. While US GDP rose surprisingly strongly in the first quarter of 2019, this was due to a number of one-off factors. Leading indicators still draw a cautiously positive picture of moderate growth. Dampening effects emanate from the fading fiscal stimulus of the tax reform and the uncertainty created by the latent trade conflicts. Monetary policy, on the other hand, is unlikely to be tightened further, given the cyclical slowdown and inflation rates close to target.

Figure 1: Indicators of economic performance



Source: WIFO. 2019 and 2020: forecast. – [1] Excluding persons in valid employment contract receiving child care benefit or being in military service, and unemployed persons in training; break in 2007-08 due to changes in the employment statistics. – [2] Including weapons systems. – [3] 10-year central government bonds (benchmark). – [4] Source: European Commission.

Growth in the euro area has been decelerating since mid-2018, due to weaker external demand, notably from a number of emerging markets, and the persistent trade disputes. Also companies' readiness to invest has slackened. Several benign one-off factors boosted GDP growth in the first quarter of 2019, masking the feeble underlying cyclical momentum. Leading indicators signal a clear downward trend: incoming export orders and the production of investment goods have strongly receded, while business confidence has dropped to a low level, particularly in the manufacturing sector. In such settings, the euro area economy may expand at a moderate pace over the forecast horizon. Political uncertainty and trade tensions will continue to weigh on exports and private investment. Private consumption, on the other hand, should provide support to business activity in view of sustained employment growth and solid gains for wages and salaries.

Growth in the euro area is likely to remain moderate, due to weak foreign demand and low business confidence weighing on investment. Activity will on the other hand be sustained by private consumption that receives stimulus from job creation and higher wages.

Many of Austria's key foreign markets in the East-central EU countries are enjoying booming conditions. Exports from this region benefit from the recovery in Russia. Strong advances in employment and household real incomes offer substantial leeway for higher consumption. The current cyclical upswing is increasingly hitting against capacity constraints, primarily caused by the decline in the working-age population and a shortage of qualified labour. GDP growth in the CEEC-5-countries is expected at 3.7 percent for 2019 and 3.1 percent for 2020. The substantial upward revision of the growth rate for 2019 from last March is explained by a level effect, i.e., the unexpectedly strong performance in late 2018 and in the first quarter of 2019.

For Austria's key export markets, WIFO expects growth rates of 2.4 percent and 3.4 percent for 2019 and 2020 respectively.

2.2 Policy stance moderately expansionary

The projection incorporates all policy measures already adopted or sufficiently specified, such that their implementation is deemed likely. With regard to domestic fiscal policy, only those measures are included that have already been voted by Parliament.

The ECB's monetary policy should remain expansionary throughout 2019. First interest rate moves are not expected before 2021. Monetary conditions therefore remain highly accommodating over the entire forecast period.

In its latest meeting, the ECB Council decided to keep policy-controlled interest rates unchanged (deposit rate –0.4 percent; main refinancing rate 0 percent; marginal lending rate 0.25 percent). The authorities also signalled their intention to keep interest rates at their present levels beyond 2019. Targeted long-term refinancing operations (TLTRO) will be resumed. Hence, the ECB will stick to the expansionary course followed during the last ten years. The prolongation of easy monetary conditions is motivated by persistently low inflation and the cyclical slackening in the euro area. Financing conditions should therefore remain extremely favourable up to the forecast horizon.

With its recommendations concerning the systemic risk buffer and the buffer for systemically important banks ("too big to fail"), the Financial Market Stability Board (FMSB) last year took measures to limit direct and indirect risk concentration (cluster risks). The implicit moderate tightening should not substantially affect credit growth over the forecast period. The FMSB also clarified issues concerning sustainable credit extension, in a first step for real estate loans. At its second meeting in June 2019, the Board decided to keep the countercyclical capital buffer unchanged at 0 percent of the risk-weighted assets, given that the key indicator, i.e., the credit-to-GDP gap[1] was still negative and gave no hint for excessive credit growth.

With the credit-to-GDP gap still negative, macro-prudential regulation incumbent on the Financial Market Stability Board (FMSB) is unlikely to be tightened by a raise in the countercyclical capital buffer.

For the whole year 2019, WIFO expects the general government balance (Maastricht definition) to be in surplus to the tune of 0.6 percent of nominal GDP, with the same surplus ratio to be achieved in 2020. In both years, the government accounts continue to benefit from low debt service cost. The current cyclical downswing in the manufacturing sector will not decisively weaken tax revenue growth. Buoyant receipts from taxes and even more social contributions in 2019 reflect generous wage settlements and lively job creation. The introduction of the family bonus will cause wage tax revenue shortfalls of 0.6 billion € in 2019 and of 1.24 billion € (wage plus assessed income tax) in 2020. The forecast also includes the cut in the work accident insurance contributions as from 2019 (estimated revenue loss of 100 million €) and the VAT rate cut

The continued strong flow of tax revenue improves the general government budget balance. The fiscal policy stance in Austria remains slightly expansionary over the projection horizon.

[1] I.e., the difference between the actual outstanding credit-to-GDP relation and its trend. According to the Basel Committee on Banking Supervision (BCBS) method, a positive gap (i.e., an actual credit-to-GDP relation above trend) indicates excessive credit growth (https://www.fmsg.at/publikationen/risikohinweise-und-empfehlungen/2019/empfehlung-2-2019.html).

from 13 percent to 10 percent for hotel overnight stays (estimated revenues foregone of 120 million €). No allowance is made for the originally-envisaged cut in health insurance contribution rates for small-income earners and for the planned adjustment of income tax scales, nor for the fiscal effects of the merger of social security agencies.

Table 3: Fiscal and monetary policy – key figures

	2015	2016	2017	2018	2019	2020
	As a percentage of GDP					
Fiscal policy						
General government financial balance[1]	– 1.0	– 1.6	– 0.8	0.1	0.6	0.6
General government primary balance	1.3	0.5	1.1	1.8	2.1	2.0
General government total revenue	50.1	48.7	48.4	48.6	48.7	48.4
General government total expenditure	51.1	50.3	49.2	48.5	48.1	47.7
	Percent					
Monetary policy						
Three-month interest rate	– 0.0	– 0.3	– 0.3	– 0.3	– 0.3	– 0.1
Long-term interest rate[2]	0.7	0.4	0.6	0.7	0.3	0.5

Source: WIFO. 2019 and 2020: forecast. – [1] According to Maastricht definition. – [2] 10-year central government bonds (benchmark).

3. Mounting international uncertainty dampens growth in Austria

Results from the regular WIFO-Konjunkturtest (business cycle survey) show a clouding of confidence within Austria's business sector. Both the index for the assessment of the current situation and that for the short-term outlook are receding, mainly driven by the fading optimism of manufacturers. In April and May, the UniCredit Bank Austria Purchasing Managers' Index tentatively signalled contraction of business in industry, for the first time since March 2015. Likewise, the latest reading of the WKÖ-Wirtschaftsbarometer (Austrian Economic Chambers business barometer) confirms the weaker sentiment: forward-looking judgements for the next 12 months are clearly more pessimistic than those expressed on the current situation.

Austria's economy is amidst a period of moderate growth. From the demand side, the slowdown is caused by the slackening of exports and investment. Activity keeps being sustained by private consumption. On the supply side, the weaker dynamics is primarily felt in the manufacturing sector. The cyclical tendency in Austria remains upward bound, albeit from a lower level, in line with developments abroad.

Table 4: Gross value added

At basic prices

	2017	2018	2019	2020	2017	2018	2019	2020
	Billion € (reference year 2010)				Percentage changes from previous year			
Volume (chain-linked series)								
Agriculture, forestry and fishing	4.28	4.20	4.20	4.20	+ 3.1	– 1.8	± 0.0	± 0.0
Manufacturing including mining and quarrying	61.26	64.18	64.84	65.85	+ 4.7	+ 4.8	+ 1.0	+ 1.6
Electricity, gas and water supply, waste management	9.72	10.44	10.97	11.29	+ 7.4	+ 7.4	+ 5.0	+ 3.0
Construction	16.52	16.94	17.27	17.49	+ 3.1	+ 2.6	+ 1.9	+ 1.3
Wholesale and retail trade	36.29	36.66	37.11	37.54	+ 1.1	+ 1.0	+ 1.2	+ 1.2
Transportation	16.02	16.92	17.77	18.30	+ 3.0	+ 5.7	+ 5.0	+ 3.0
Accommodation and food service activities	13.50	14.17	14.34	14.48	+ 1.4	+ 5.0	+ 1.2	+ 1.0
Information and communication	10.15	10.44	10.71	10.97	+ 2.6	+ 2.9	+ 2.5	+ 2.5
Financial and insurance activities	12.39	12.33	12.34	12.46	+ 3.4	– 0.5	+ 0.1	+ 0.9
Real estate activities	26.57	27.24	27.93	28.49	+ 1.3	+ 2.5	+ 2.5	+ 2.0
Other business activities[1]	28.36	29.59	30.22	30.81	+ 3.5	+ 4.3	+ 2.1	+ 2.0
Public administration[2]	49.36	49.96	50.63	51.21	+ 1.3	+ 1.2	+ 1.3	+ 1.2
Other service activities[3]	7.74	7.80	7.87	7.91	– 0.1	+ 0.7	+ 1.0	+ 0.5
Total gross value added[4]	291.77	300.36	305.73	310.49	+ 2.6	+ 2.9	+ 1.8	+ 1.6
Gross domestic product at market prices	326.75	335.71	341.27	346.53	+ 2.6	+ 2.7	+ 1.7	+ 1.5

Source: WIFO. 2019 and 2020: forecast. – [1] Professional, scientific and technical activities; administrative and support service activities (NACE M and N). – [2] Including defence, compulsory social security, education, human health and social work activities (NACE O to Q). – [3] Arts, entertainment and recreation; other service activites; activities of households (NACE R to U). – [4] Before deduction of subsidies and attribution of taxes on products.

Manufacturers' expectations are at present close to their long-term average. After the peak reached by leading indicators at the turn 2017-18, this may be taken as "normalisation". The overall pattern of early indicators suggests that the Austrian economy will keep a pace of moderate expansion over the forecast period that is significantly down from the one seen during 2017 and 2018. The current cyclical high has reached its final stage, with growth of demand and output abating towards its trend rate.

3.1 Moderate cyclical dynamics

Given the current external conditions and policy settings, the adjusted annual growth rate of real GDP will ease from 2.7 percent in 2018 to 1.6 percent in 2019 and 1.3 percent in 2020, close to its longer-term trend. In 2019, the moderate expansion is supported by a sizeable statistical carry-over of 0.7 percentage points from 2018. During the year, i.e., the year-on-year growth rate for the fourth quarter, GDP is expected to gain only 1.4 percent (compared with +2.3 percent in 2018). In the first semester, growth is still slackening under the impact of external cyclical conditions; in the second half of the year, a recovery should take hold, before growth converges towards its trend rate in 2020. The projected annual figure for 2020 is the result of subdued growth during the year and an only limited growth carry-over. Due to a higher number of working days, the unadjusted GDP growth rates turn out higher for 2019 and 2020, at 1.7 percent and 1.5 percent respectively.

Economic growth in Austria significantly lost momentum in 2018. In view of the now more clouded outlook signalled by leading indicators, GDP is likely to advance at a slower pace during the projection period. From today's perspective, the current business cycle will be ending soon.

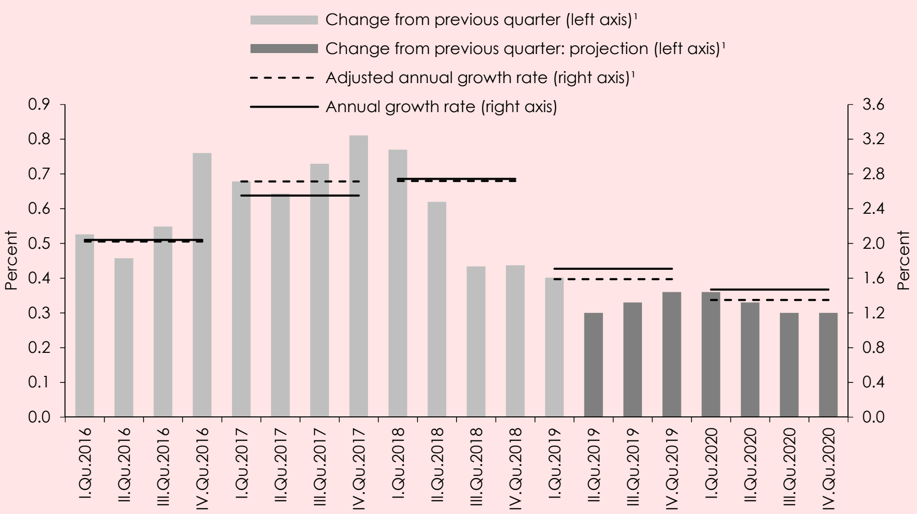
Table 5: Technical breakdown of the real GDP growth forecast

		2017	2018	2019	2020
Growth carry-over[1]	percentage points	+ 1.0	+ 1.1	+ 0.7	+ 0.5
Growth rate during the year[2]	percent	+ 2.9	+ 2.3	+ 1.4	+ 1.3
Annual growth rate	*percent*	*+ 2.6*	*+ 2.7*	*+ 1.7*	*+ 1.5*
Adjusted annual growth rate[3]	percent	+ 2.7	+ 2.7	+ 1.6	+ 1.3
Calendar effect[4]	percentage points	– 0.4	+ 0.0	+ 0.1	+ 0.1

Source: WIFO. 2019 and 2020: forecast. – [1] Impact of year-earlier growth dynamics on growth in the current year. Equals the annual growth rate in the current year, if the level of GDP in the current year remains constant from the fourth quarter of the previous year; trend-cycle data. – [2] Reflects the growth dynamics during a calendar year. Equals the year-on-year growth rate for the fourth quarter; trend-cycle data. – [3] Trend-cycle data. Corresponding figure to OeNB short-term forecast. – [4] Impact of the annual number of working days and the leap day. The sum of the adjusted annual growth rate and the calendar effect may deviate from the unadjusted annual rate, since the latter also includes seasonal and irregular effects.

Figure 2: Cyclical profile Austria

GDP, volume



Source: WIFO. – [1] Trend-cycle data.

Due to the muted business activity, capacity utilisation for the overall economy may not increase further until the forecast horizon; the positive output gap is set to narrow, without closing entirely. Hence, the economy is expected to remain in conditions of slightly above-average capacity utilisation.

Table 6: Productivity

	2015	2016	2017	2018	2019	2020
	Percentage changes from previous year					
Total economy						
Real GDP	+ 1.1	+ 2.0	+ 2.6	+ 2.7	+ 1.7	+ 1.5
Hours worked[1]	− 0.4	+ 2.1	+ 1.6	+ 1.7	+ 1.2	+ 1.2
Productivity[2]	+ 1.6	− 0.0	+ 0.9	+ 1.1	+ 0.5	+ 0.3
Employment[3]	+ 0.7	+ 1.4	+ 1.7	+ 1.6	+ 1.4	+ 0.8
Manufacturing						
Production[4]	+ 1.3	+ 3.5	+ 4.8	+ 4.7	+ 1.0	+ 1.6
Hours worked[5]	− 0.1	+ 0.4	+ 1.5	+ 3.3	+ 0.4	− 0.7
Productivity[2]	+ 1.5	+ 3.1	+ 3.2	+ 1.4	+ 0.6	+ 2.3
Employees[6]	+ 0.5	+ 0.6	+ 1.6	+ 2.7	+ 1.1	− 0.4

Source: WIFO. 2019 and 2020: forecast. – [1] Total hours worked by persons employed, National Accounts definition. – [2] Production per hour worked. – [3] Employees and self-employed, National Accounts definition (jobs). – [4] Gross value added, volume. – [5] Total hours worked by employees. – [6] National Accounts definition (jobs).

From the demand side, business activity is driven by the lively domestic components, notably robust private consumption. This is based on stable growth rates of household disposable income. With wage growth decelerating, household disposable income will nevertheless increase less swiftly in 2019 and 2020. On the other hand, the positive income effect from the introduction of the family bonus should add to consumption. Employment growth, even if projected to lose momentum, will also continue to support private demand, since the implicit reduction of income uncertainty lowers the need for precautionary saving. In all, private consumption (+1.6 percent in 2018) should keep advancing at stable rates of 1.7 percent in 2019 and 1.6 percent in 2020.

Table 7: Private consumption, income and prices

	2015	2016	2017	2018	2019	2020
	Percentage changes from previous year, volume					
Private consumption expenditure[1]	+ 0.4	+ 1.4	+ 1.4	+ 1.6	+ 1.7	+ 1.6
Durable goods	+ 1.9	+ 3.0	+ 0.5	− 1.4	− 1.0	+ 2.0
Non-durable goods and services	+ 0.3	+ 1.2	+ 1.5	+ 2.0	+ 1.9	+ 1.5
Household disposable income	− 0.2	+ 2.5	+ 0.5	+ 2.4	+ 1.5	+ 1.4
	As a percentage of disposable income					
Household saving ratio						
Including adjustment for the change in pension entitlements	6.8	7.8	6.8	7.4	7.3	7.2
Excluding adjustment for the change in pension entitlements	6.1	7.1	6.2	6.9	6.7	6.6
	Percentage changes from previous year					
Loans to domestic non-banks (end of period)	+ 1.8	+ 1.8	+ 0.9	+ 4.4	+ 2.5	+ 1.9
	Percent					
Inflation rate						
National	0.9	0.9	2.1	2.0	1.6	1.7
Harmonised	0.8	1.0	2.2	2.1	1.5	1.7
Core inflation[2]	1.7	1.5	2.2	1.9	1.6	1.8

Source: WIFO. 2019 and 2020: forecast. – [1] Private households including non-profit institutions serving households. – [2] Excluding energy and unprocessed food (meat, fish, fruits, vegetables).

Investment growth is expected to slacken. The latest WIFO-Investitionstest (investment survey) still suggests a further increase, albeit at significantly lower rates than previously assumed. According to the WKÖ-Wirtschaftsbarometer, firms' investment plans are still in positive territory, but at their lowest level within the last two years[2]. Construction investment should further provide firm support to GDP growth, with projected gains of 2.1 percent in 2019 and 1.3 percent in 2020 (after +2.8 percent in 2018). Since the positive output gap is set to diminish, companies' need for capacity enlargement will lose importance, making for slower growth of investment in machinery and equipment (2019 +2.2 percent, 2020 +1.8 percent, after +3.6 percent in 2018).

Table 8: Earnings, international competitiveness

	2015	2016	2017	2018	2019	2020
	Percentage changes from previous year					
Wages and salaries per employee[1]						
Nominal, gross	+ 2.0	+ 2.3	+ 1.4	+ 2.5	+ 2.7	+ 1.9
Real[2]						
Gross	+ 1.1	+ 1.4	– 0.7	+ 0.5	+ 1.1	+ 0.2
Net	+ 0.6	+ 4.3	– 0.9	+ 0.2	+ 1.2	– 0.0
Wages and salaries per hour worked[1]						
Real, net[2]	+ 2.0	+ 3.6	– 0.8	– 0.0	+ 1.3	+ 0.0
	Percent					
Wage share, adjusted[3]	69.3	68.4	67.9	67.7	68.2	67.9
	Percentage changes from previous year					
Unit labour costs, nominal[4]						
Total economy	+ 1.7	+ 1.6	+ 0.6	+ 1.2	+ 2.3	+ 1.6
Manufacturing	+ 0.9	– 0.5	– 1.2	+ 1.4	+ 3.1	+ 0.6
Effective exchange rate – manufactured goods[5]						
Nominal	– 2.9	+ 1.2	+ 0.7	+ 1.7	– 0.4	+ 0.3
Real	– 3.1	+ 1.3	+ 1.0	+ 1.7	– 0.8	+ 0.1

Source: WIFO. 2019 and 2020: forecast. – [1] National Accounts definition. – [2] Deflated by CPI. – [3] Compensation of employees as a percentage of national income, adjusted for the change in the share of employees in total employment from base year 1995. – [4] Labour costs in relation to productivity (hourly compensation per employees divided by GDP and value added, respectively, per employed persons' hours worked). – [5] Weighted by exports and imports, real value adjusted by relative HCPI.

3.2 Export growth slowing down

Underlying the projections is the assumption that the current trade policy disputes will not give rise to structural changes in world trade flows. Due to reduced global growth and trade prospects for the entire forecast horizon, Austrian exports will likely expand at significantly lower rates than over the last few years; such reduced prospects are confirmed by companies' export expectations sampled in the context of the WIFO business survey for the European Commission, by assessments on incoming export orders for UniCredit Bank Austria Purchasing Managers' Index, and by export outlook judgements for the WKÖ-Wirtschaftsbarometer[3]. In addition, cyclical buoyancy in East-central Europe, the USA and China is likely to end in an early downswing. Finally, the tentative recovery of the German economy is primarily driven by domestic demand (private consumption and construction), holding only limited benefits for Austrian exports of investment goods. After a gain of 4.4 percent in 2018, overall exports are projected to rise by 2.4 percent in 2019 and 2.7 percent in 2020.

During 2018, import growth was fuelled by robust domestic demand, notably for business machinery and equipment, and additionally boosted by lively exports, given their high import content. With the further slackening of investment in machinery and equipment, domestically-driven import growth will gradually subside and fall behind the pace of exports. Net exports will therefore make a small positive contribution to GDP growth, both in 2019 and 2020.

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[2] Replacement of obsolete business equipment dominates among the declared investment motives. A positive sign is the rising share of new investment (+6 percentage points).

[3] According to the WKÖ-Wirtschaftsbarometer, firms' expectations for their export sales have clearly dropped below the long-term average. Small firms with less than 50 employees are particularly pessimistic in this regard.

Table 9: Expenditure on GDP

Volume (chain-linked series)

	2017	2018	2019	2020	2017	2018	2019	2020
	Billion € (reference year 2010)				Percentage changes from previous year			
Final consumption expenditure	231.14	234.18	237.53	240.67	+ 1.4	+ 1.3	+ 1.4	+ 1.3
Households[1]	166.93	169.67	172.47	175.16	+ 1.4	+ 1.6	+ 1.7	+ 1.6
General government	64.22	64.51	65.06	65.50	+ 1.5	+ 0.4	+ 0.8	+ 0.7
Gross capital formation	82.05	84.68	86.73	88.06	+ 5.6	+ 3.2	+ 2.4	+ 1.5
Gross fixed capital formation	77.14	79.76	81.58	82.88	+ 3.9	+ 3.4	+ 2.3	+ 1.6
Machinery and equipment[2]	27.59	28.58	29.21	29.74	+ 4.6	+ 3.6	+ 2.2	+ 1.8
Construction	33.28	34.21	34.93	35.40	+ 3.5	+ 2.8	+ 2.1	+ 1.3
Other investment[3]	16.44	17.16	17.64	17.95	+ 3.7	+ 4.4	+ 2.8	+ 1.7
Domestic demand	315.37	321.55	326.59	330.84	+ 2.7	+ 2.0	+ 1.6	+ 1.3
Exports	187.86	196.09	200.76	206.25	+ 4.7	+ 4.4	+ 2.4	+ 2.7
Travel	13.86	14.38	14.56	14.77	+ 2.9	+ 3.7	+ 1.3	+ 1.5
Minus imports	176.44	181.70	185.82	190.22	+ 5.1	+ 3.0	+ 2.3	+ 2.4
Travel	7.27	7.73	7.94	8.10	+ 8.6	+ 6.3	+ 2.7	+ 2.0
Gross domestic product	326.75	335.71	341.27	346.53	+ 2.6	+ 2.7	+ 1.7	+ 1.5
Value	369.90	386.06	399.07	412.15	+ 3.8	+ 4.4	+ 3.4	+ 3.3

Source: WIFO. 2019 and 2020: forecast. – [1] Including non-profit institutions serving households. – [2] Including weapon systems. – [3] Mainly intellectual property products (research and development, computer programmes, copyrights).

3.3 Employment growth set to persist

Despite the cyclical downturn, labour supply will continue to increase over the entire projection period. Several factors are at work: rising labour force participation of older workers due to past reforms of the pension system and the steady increase in female activity rates will boost the domestic labour force; at the same time, the number of foreign workers will increase further, mainly from other EU countries.

Table 10: Labour market

	2015	2016	2017	2018	2019	2020
	Change from previous year in 1,000					
Demand for labour						
Persons in active employment[1]	+ 42.5	+ 62.3	+ 76.8	+ 91.6	+ 63.0	+ 39.0
Employees[1,2]	+ 33.2	+ 53.7	+ 70.7	+ 88.0	+ 60.0	+ 36.0
National employees	+ 6.3	+ 17.7	+ 23.8	+ 33.7	+ 17.0	+ 9.0
Foreign employees	+ 27.0	+ 36.0	+ 46.8	+ 54.4	+ 43.0	+ 27.0
Self-employed[3]	+ 9.3	+ 8.6	+ 6.1	+ 3.6	+ 3.0	+ 3.0
Labour supply						
Population of working age 15 to 64 years	+ 52.3	+ 65.8	+ 23.0	+ 13.2	+ 9.6	+ 5.9
Labour force[4]	+ 77.5	+ 65.3	+ 59.4	+ 63.8	+ 54.0	+ 45.0
Labour surplus						
Unemployed[5]	+ 35.0	+ 3.0	– 17.3	– 27.9	– 9.0	+ 6.0
Unemployed persons in training	– 10.2	+ 2.1	+ 4.9	– 3.4	– 9.0	– 2.0
	Percent					
Unemployment rate						
As a percentage of total labour force (Eurostat)[6]	5.7	6.0	5.5	4.9	4.6	4.6
As a percentage of total labour force[5]	8.1	8.1	7.6	6.9	6.6	6.7
As a percentage of dependent labour force[5]	9.1	9.1	8.5	7.7	7.4	7.5
	Percentage changes from previous year					
Labour force[4]	+ 1.8	+ 1.5	+ 1.4	+ 1.4	+ 1.2	+ 1.0
Persons in active dependent employment[1,2]	+ 1.0	+ 1.6	+ 2.0	+ 2.5	+ 1.6	+ 1.0
Unemployed[5]	+ 11.0	+ 0.8	– 4.9	– 8.2	– 2.9	+ 2.0
Persons (in 1,000)	354.3	357.3	340.0	312.1	303.1	309.1

Source: WIFO. 2019 and 2020: forecast. – [1] Excluding persons in valid employment contract receiving child care benefit or being in military service. – [2] According to the Organisation of Austrian Social Security. – [3] According to WIFO, including liberal professions and unpaid family workers. – [4] Persons in active employment plus unemployed. – [5] According to Public Employment Service Austria. – [6] Labour Force Survey.

In 2019, the number of workers in active dependent employment will be 1.6 percent higher than in the previous year, and by 1 percent year-on-year higher in 2020. The trend in the unemployment rate should turn around over the forecast horizon, as the creation of new jobs will no longer suffice to outpace labour supply growth. The jobless rate of 7.7 percent in 2018 will edge down to 7.4 percent in 2019 and may remain broadly stable at 7.5 percent in 2020.

3.4 Inflation to stay moderate

Inflation, as measured by the consumer price index, should stay modest in both years of the projection period, easing from 2.0 percent in 2018 to 1.6 percent in 2019 and 1.7 percent in 2020. Among the external factors making for price stability are weakening import prices, both of commodities and manufactured goods. Domestically, the output gap, while remaining positive, will narrow and thereby attenuate production capacity constraints. Upward pressure on prices should emanate from the increase in unit labour cost that will be further fuelled until the end of 2019 by the wage settlements concluded so far. The sustained firm growth of private consumption, for its part, will exert certain inflationary pressure from the demand side.

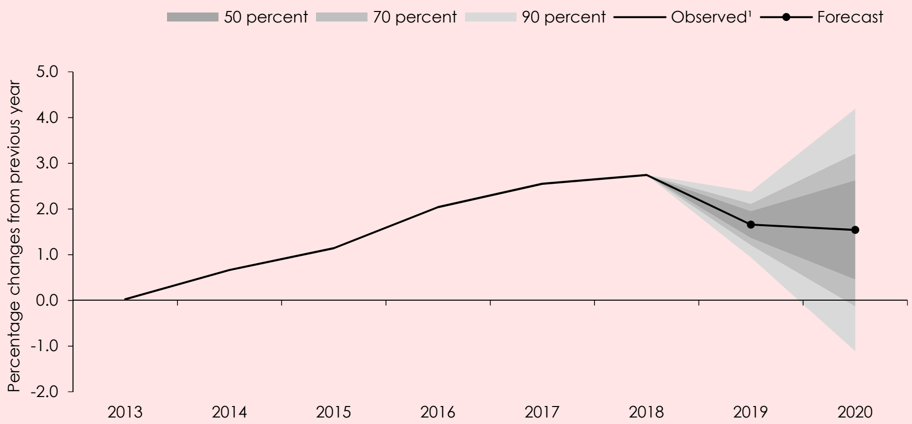
4. The risk environment

The danger of a downright recession with a fall in GDP over several quarters appears low from present perspectives, provided that political risks do not exacerbate further. The 70 percent confidence interval for GDP growth ranges from 1.2 percent to 2.1 percent for 2019 and from –0.1 percent to 3.2 percent for 2020.

The international environment shapes the downward risks to the forecast, whereas domestic developments hold clear upward risks.

Downward risks have definitely increased since March 2019, when the WIFO forecast was last revised. Next to uncertainties about the further course of economic policy, geo-political risks are mounting, such as the conflict between the USA and Iran or Venezuela. In Europe, the outlook is clouded by the uncertainty surrounding the economic policy pursued by the Italian government. An excessive deficit procedure initiated by the EU authorities may give rise to major turbulence on financial markets and undermine the stability not only of Italian public finances, but also of the entire financial sector, as Italian banks hold government bonds to an important extent. Adverse repercussions on the real economy may spread quickly to the Austrian economy and its growth prospects, given its close ties with Italy.

Figure 3: Margins of uncertainty for real GDP



Source: WIFO. Calculated on the basis of ex-post revealed forecast errors. – [1] Uncertainty of measurement: ±0,28 percentage points.

Against this backdrop, GDP growth in the first quarter of 2019 surprised on the upside in many countries. Although a number of benign one-off factors have been at work, the "true" underlying cyclical tendency cannot be firmly assessed at present. Internationally as well as in Austria, leading indicators point towards a lasting cyclical downturn.

The domestic cyclical risks are altogether upward bound. The persistent positive trend of employment and household income may lead to still stronger growth of private consumption than projected in this forecast. The announced tax reform may give an additional boost to disposable income and spur consumption. Nevertheless, the external downward risks dominate the overall assessment of growth prospects for this year and next.