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First Signs of Imminent Business Cycle Recovery

Business surveys in Germany and Austria point to a tentative pick-up in expectations for the months to come. However, the current situation in Austrian manufacturing remains bleak, and exports are lower than a year ago. More encouraging are reports from the construction industry and the retail sales sector.

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In Europe, there are as yet no clear signs for a business cycle upturn, but expectations for a global economic recovery have firmed over the last months. Activity in the USA has revived under the impact of policy stimulus, with GDP expanding at a surprisingly strong 3 percent annualised rate in the second quarter. If the – still fragile – upward trend is confirmed, it will have a beneficial impact also on Europe.

Hopes for an international recovery are reflected not only by rising stock market values, but also by business expectations. The global climate index of the Munich-based Ifo Institute released early September rose markedly, from 83.2 for the second to 91.3 for the third quarter. While judgements on the current situation remain subdued, expectations for the next six months have improved substantially in Asia and the USA and to some extent also in Europe. Prospects for the three major economic areas have brightened also according to the OECD leading indicators, although the Secretariat has recently cut the 2003 growth forecast for the euro area from 1 percent to 0.5 percent.

A slight recovery of sentiment in Germany has been registered by the Ifo business climate index for some months already. In the latest survey, the improvement extended for the first time from the forward-looking judgement to that of the current situation. The positive turnaround should be seen in the context of the structural reforms being envisaged. The EU business survey, however, suggests a further weakening of confidence in the EU until July, when the indicator for the manufacturing sector fell markedly. Nevertheless, the rebound in the dollar exchange rate bodes well for strengthening of activity in the USA spilling over to the euro area, even such exchange rate shifts normally take two or three quarters to impact on the real economy.

The early signs of a gradual revival of global activity need to be confirmed over the next few months. Overly optimistic expectations are being moderated by last year's experience, when a similar pick-up was aborted by financial market shocks. It also remains to be seen, to what extent Europe will benefit from the recovery currently visible in the USA and Japan.

In Austria, according to the WIFO business survey, industrial confidence has stabilised at a low level. While orders and production expectations remained flat, judgements on sales prices and business outlook for the next six months turned more positive.

Export data reveal that external stimulus to business activity was lacking until mid-year. According to the balance of payment statistics of the Central Bank (OeNB), current receipts for merchandise exports in the first semester fell by nearly 2 percent year-on-year, whereas the official export statistics (from Statistics Austria) show a 2 percent increase from the year-earlier period for the first five months. According to both sources, exports weakened in the second quarter, probably also due to the strength of the euro.

The tourism business slackened markedly, compared with the last couple of years. From May to July, gross revenues rose by only 1.6 percent from last year, while the number of overnight stays fell markedly. Cyclical weakness world-wide, a late start of school holidays in Germany, and the strength of the euro all had a dampening effect.

By contrast, confidence has further strengthened in the construction industry. This goes in particular for civil engineering, but firms in the building sector also see prospects better now than in the last years. The decline in residential construction has bottomed out.

Retail sales also took a positive development in the first half of 2003, rising by 1.8 percent in volume from the year-earlier period. The deceleration of inflation, boosting real incomes, had a positive impact. The policy debate about the pension reform has apparently not detracted from consumers' willingness to spend, at least not in the very short run. Sales of passenger cars and business vehicles are clearly heading upwards.

Sluggish activity in manufacturing continues to weigh on the labour market. The increase in overall employment by 25,100, as statistically recorded, is mainly accounted for by a higher number of child care benefit recipients (+18,300). The number of jobs in the private sector and in public administration rose by 6,500 year-on-year in August. Job vacancies fell by 800 from a year ago, but the negative gap has narrowed over the last months. The rise in unemployment (+5,400 from last year) has been contained by an expansion of job training activities.

Price developments have also been influenced by the cyclical weakness. Headline inflation has abated to 1.1 percent in recent months, facilitated also by the year-on-year fall in energy prices.