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**Growth Slowing Down
Economic Outlook for 2008 and 2009**

December 2007

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Economic Outlook for 2008 and 2009

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Economic Outlook for 2008 and 2009: Growth Slowing Down

GDP growth in Austria is set to abate from 3.4 percent in 2007 to 2.2 percent in 2008. A first preview to 2009 suggests a rate of growth around 2 percent. Main reason for the deceleration is a weakening of the international environment, as witnessed by the cyclical downturn in the USA, the crisis on financial markets and the appreciation of the euro. In Austria, too, investment growth is losing momentum, and the support to activity from private consumption will be constrained by the meagre gains in real incomes. The latter are squeezed also by a marked rise in inflation, projected at an annual 2.6 percent for 2008. The slowdown of growth will keep the rate of unemployment at 6¼ percent of the labour force (4¼ percent on Eurostat definitions).

Austria's export industry enjoyed a boom in 2006 and 2007, benefiting from favourable economic conditions worldwide, an acquired strong market position in the rapidly growing economies in eastern and south-eastern Europe and its high degree of price competitiveness. Both merchandise exports and manufacturing output expanded by 7 to 8 percent in volume, a pace that even allowed a net increase in the industrial workforce. The business cycle reached its peak in the first half of 2007. Since then, leading indicators like the quarterly WIFO Business Cycle Survey have been signalling a slowdown, mainly because global economic conditions have weakened since last summer:

- Following a slump in real estate prices and residential investment, consumer demand and GDP growth have ebbed in the USA; with growth of real GDP projected at barely above 1½ percent p.a. for 2008 and 2009, a major engine of global growth is losing steam.
- The crisis of confidence and lending on international financial markets is going on: with credit and financing conditions tightening and business confidence weakening, private investment will be affected.

- The substantial appreciation of the euro is weighing on industrial price competitiveness, thereby holding back the major driver of business activity in the euro area; prevailing differentials of both growth and interest rates between the USA and Europe make a further dollar depreciation likely. Euro area GDP is projected to moderate to 1.9 percent and 1.7 percent in volume in 2008 and 2009, respectively.
- Nevertheless, these dampening effects hit the world economy in a period of robust expansion driven mainly by the emerging markets in Asia. Global growth is expected to edge down from slightly above 5 percent in volume in 2007 to around 4½ percent.

WIFO therefore assumes that growth of Austrian exports will decelerate somewhat over the forecast period. Exports of goods and services are expected to increase by 5½ percent in volume per year. As a consequence, also the boom in manufacturing will subside, with value added gaining some 3 percent p.a. Already in 2007, lively exports gave less stimulus than expected to investment in machinery and equipment which edged up by only 5 percent in real terms, despite high corporate earnings. First results from the WIFO investment survey of autumn 2007 point to a slackening of investment growth in 2008. This holds also for the construction sector, where the boom of 2006-07 triggered not only a sizeable increase in employment, but also a jump in prices. While steady growth over the projection period may be expected for civil engineering and residential building, construction of industrial and commercial buildings may lose some momentum. For the whole construction sector, value added may rise by some 2½ percent in volume.

Unlike during the cyclical high from 1998 to 2000, the upswing in 2006 and 2007 has never been transmitted to private household demand which of late has even slowed to a mere 1.6 percent increase. No substantial pick-up in consumer spending should be expected for 2008 either, despite higher wage settlements. The income gains will be offset by a significant acceleration of inflation, with the headline rate rising above 3 percent in the months to come and the annual average for 2008 expected at 2.6 percent. The upward drift is mainly driven by hikes in food and energy prices. The implicit dampening impact on private consumption is particularly noticeable insofar as these items weigh heavily in the consumption basket of the low-income brackets

with a high spending propensity. Household demand, adjusted for inflation, is therefore projected to grow by only 1.9 percent p.a. over the forecast period.

The slackening of GDP growth will slow the momentum of job creation. The number of persons in dependent active employment is set to move up by 30,000 in 2008 and a further 22,000 in 2009. These gains will not suffice to make further inroads into unemployment, given the steady increase in the population of working age, rising labour force participation rates and the continued inflow of labour from abroad. WIFO's projection for the total number of unemployed is for an average 220,000 or slightly higher, broadly unchanged up to the forecast horizon. The corresponding jobless rate is 6¼ percent of the dependent labour force (national definition) or 4¼ percent of the total labour force (Eurostat definition).

The slowdown of job creation as well as of profit growth will be reflected, with the usual lag, by a slower growth momentum of government revenues. At the same time, additional spending decided by the Federal government on research, education and social welfare will take effect. WIFO expects that the general government balance in the Maastricht definition will stabilise at a deficit around 0.6 percent of GDP. This outlook is necessarily vague, particularly for 2009 in the absence of budget drafts for all government levels for that year.

With the stimulus from the export boom only partially transmitted to business investment, private demand lacking momentum and the international financial market crisis still unresolved, the cyclical upswing of domestic activity will ebb earlier than hoped-for. Growth of GDP, while once again exceeding the euro area average, will fall slightly below its long-term trend. Under such auspices, a further fall in unemployment has become unlikely, as has the narrowing of the government deficit. Should the external conditions deteriorate even further, the cyclical slowdown may prove sharper than assumed in the present projections.

Vienna, 11 January 2008

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Projections - December 2007

Main results

Percentage changes from previous year

		2004	2005	2006	2007	2008	2009
GDP							
Volume		+ 2.3	+ 2.0	+ 3.3	+ 3.4	+ 2.2	+ 2.0
Value		+ 4.4	+ 3.9	+ 5.1	+ 5.8	+ 4.6	+ 4.0
Manufacturing¹, volume		+ 2.4	+ 3.1	+ 8.8	+ 7.8	+ 3.3	+ 3.0
Wholesale and retail trade, volume		+ 1.1	+ 0.2	+ 1.0	+ 1.3	+ 1.8	+ 1.8
Private consumption expenditure, volume		+ 1.8	+ 2.0	+ 2.1	+ 1.6	+ 1.9	+ 1.9
Gross fixed investment, volume		+ 0.1	+ 0.3	+ 3.8	+ 5.0	+ 2.5	+ 1.9
Machinery and equipment ²		- 1.4	+ 0.7	+ 2.1	+ 5.0	+ 2.5	+ 1.0
Construction		+ 1.3	+ 0.1	+ 5.1	+ 5.0	+ 2.5	+ 2.5
Exports of goods³							
Volume		+ 12.5	+ 3.2	+ 6.8	+ 8.0	+ 6.3	+ 6.0
Value		+ 13.9	+ 5.4	+ 9.5	+ 9.8	+ 7.3	+ 6.5
Imports of goods³							
Volume		+ 11.7	+ 2.8	+ 3.8	+ 7.1	+ 6.2	+ 5.9
Value		+ 12.5	+ 5.9	+ 8.0	+ 8.4	+ 7.5	+ 6.6
Current balance	€ bn	+ 3.99	+ 5.16	+ 7.11	+ 9.32	+ 9.37	+ 10.11
	as a percentage of GDP	+ 1.7	+ 2.1	+ 2.8	+ 3.4	+ 3.3	+ 3.4
Long-term interest rate⁴	percent	4.2	3.4	3.8	4.3	4.1	4.4
Consumer prices		+ 2.1	+ 2.3	+ 1.5	+ 2.1	+ 2.6	+ 2.1
Unemployment rate							
Eurostat definition ⁵	percent	4.8	5.2	4.8	4.3	4.2	4.3
National definition ⁶	percent	7.1	7.3	6.8	6.2	6.2	6.3
Persons in active dependent employment⁷		+ 0.7	+ 1.0	+ 1.7	+ 2.0	+ 0.9	+ 0.7
General government financial balance							
	according to Maastricht definition						
	as a percentage of GDP	- 1.2	- 1.6	- 1.4	- 0.6	- 0.7	- 0.6

¹ Value added, including mining and quarrying. ² Including other products. ³ According to Statistics Austria.

⁴ 10-year central government bonds (benchmark). ⁵ According to Eurostat Labour Force Survey. ⁶ Public Employment Service Austria, percent of total labour force excluding self employed. ⁷ Excluding parental leave, military service, and unemployed persons in training.

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Key policy indicators

	2004	2005	2006	2007	2008	2009
<i>Fiscal policy</i>						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 1.2	- 1.6	- 1.4	- 0.6	- 0.7	- 0.6
according to National accounts	- 1.3	- 1.7	- 1.5	- 0.7	- 0.8	- 0.7
General government primary balance	+ 1.6	+ 1.3	+ 1.4	+ 2.1	+ 2.0	+ 2.1
<i>Monetary policy</i>						
	Percent					
3-month interest rate	2.1	2.2	3.1	4.3	4.4	4.2
Long-term interest rate ¹	4.2	3.4	3.8	4.3	4.1	4.4
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 1.5	- 0.7	+ 0.2	+ 1.1	+ 1.5	+ 0.2
Real	+ 1.0	- 1.0	- 0.6	+ 0.7	+ 1.7	- 1.8

¹ 10-year central government bonds (benchmark).

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Projections - December 2007

World economy

Percentage changes from previous year

	2004	2005	2006	2007	2008	2009
Real GDP						
World	+ 5.3	+ 4.8	+ 5.5	+ 5.1	+ 4.6	+ 4.5
Total OECD	+ 3.2	+ 2.6	+ 3.0	+ 2.7	+ 2.2	+ 2.3
USA	+ 3.6	+ 3.1	+ 2.9	+ 2.3	+ 1.6	+ 1.7
Japan	+ 2.7	+ 1.9	+ 2.4	+ 1.8	+ 1.5	+ 1.6
EU 27	+ 2.5	+ 1.8	+ 3.0	+ 3.1	+ 2.3	+ 2.1
EU 15	+ 2.3	+ 1.6	+ 2.8	+ 2.7	+ 1.9	+ 1.7
Euro area	+ 2.0	+ 1.5	+ 2.8	+ 2.7	+ 1.9	+ 1.7
Germany	+ 1.1	+ 0.8	+ 2.9	+ 2.6	+ 1.8	+ 1.8
New member states ¹	+ 5.5	+ 4.7	+ 6.2	+ 6.0	+ 5.5	+ 5.0
China	+ 10.1	+ 10.2	+ 11.1	+ 11.5	+ 10.5	+ 10.0
World trade, volume	+ 10.3	+ 7.2	+ 8.9	+ 6.5	+ 6.8	+ 6.2
Market growth²	+ 9.1	+ 7.4	+ 10.3	+ 7.8	+ 6.3	+ 6.0
Primary commodity prices						
HWWI Index, total	+ 18.5	+ 28.6	+ 19.4	+ 2	+ 5	+ 3
Excluding energy	+ 18.1	+ 5.6	+ 22.0	+ 3	+ 0	+ 5
Crude oil prices						
Average import price (fob)						
Brent, USD per barrel	38.0	55.0	65.1	72.0	85.0	88.0
Exchange rate						
USD per euro	1.243	1.245	1.256	1.37	1.52	1.55

¹ Bulgaria, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovakia, Slovenia.

² Real import growth of trading partners weighted by Austrian export shares.

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Projections - December 2007

Private consumption, income and prices

	2004	2005	2006	2007	2008	2009
	Percentage changes from previous year, volume					
Private consumption expenditure	+ 1.8	+ 2.0	+ 2.1	+ 1.6	+ 1.9	+ 1.9
Durables	+ 4.0	+ 2.5	+ 1.9	+ 1.9	+ 3.0	+ 2.4
Non-durables and services	+ 1.5	+ 2.0	+ 2.1	+ 1.6	+ 1.8	+ 1.8
Household disposable income	+ 1.9	+ 2.6	+ 2.7	+ 2.3	+ 1.5	+ 1.6
Household saving ratio						
As a percentage of disposable income	8.9	9.3	9.7	10.3	10.1	9.9
	Percentage changes from previous year					
Direct lending to domestic non-banks¹	+ 5.0	+ 4.7	+ 4.5	+ 3.2	+ 3.7	+ 4.3
	Percentage changes from previous year					
Inflation rate						
National	2.1	2.3	1.5	2.1	2.6	2.1
Harmonised	2.0	2.1	1.7	2.1	2.6	2.1
Core inflation ²	1.6	1.5	1.3	1.9	2.3	2.0

¹ End of period.

² Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

Productivity

Percentage changes from previous year

	2004	2005	2006	2007	2008	2009
Total economy						
Real GDP	+ 2.3	+ 2.0	+ 3.3	+ 3.4	+ 2.2	+ 2.0
Employment ¹	+ 0.2	+ 0.8	+ 1.2	+ 1.5	+ 0.6	+ 0.5
Productivity (GDP per employment)	+ 2.2	+ 1.2	+ 2.1	+ 1.9	+ 1.6	+ 1.5
Manufacturing						
Production ²	+ 2.3	+ 3.2	+ 8.8	+ 7.8	+ 3.3	+ 3.0
Employees ³	- 0.6	- 0.8	+ 0.2	+ 2.4	- 0.6	- 0.9
Productivity per hour	+ 2.1	+ 4.6	+ 8.4	+ 5.5	+ 4.4	+ 4.2
Working hours per day per employee ⁴	+ 0.8	- 0.6	+ 0.2	- 0.2	- 0.5	- 0.3

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.

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Projections - December 2007

Earnings and international competitiveness

Percentage changes from previous year

	2004	2005	2006	2007	2008	2009
Gross earnings per employee ¹	+ 1.8	+ 2.3	+ 2.7	+ 2.8	+ 3.5	+ 3.0
Gross real earnings per employee ¹	- 0.0	+ 0.6	+ 1.1	+ 0.7	+ 0.9	+ 0.9
Net real earnings per employee ¹	- 0.0	+ 1.2	+ 0.5	+ 0.1	+ 0.3	+ 0.4
<i>Total economy</i>						
Unit labour costs	- 0.6	+ 1.2	+ 0.4	+ 0.9	+ 2.0	+ 1.5
<i>Manufacturing</i>						
Unit labour costs	- 0.7	± 0.0	- 4.2	- 2.3	- 0.2	- 0.7
Relative unit labour costs ²						
Vis-à-vis trading partners	+ 2.0	+ 0.8	- 2.4	- 1.0	- 0.5	- 1.0
Vis-à-vis Germany	+ 2.3	+ 2.6	- 1.5	+ 0.5	- 0.5	- 0.3
Effective exchange rate - manufactures						
Nominal	+ 1.5	- 0.6	+ 0.2	+ 1.2	+ 1.4	+ 0.2
Real	+ 1.1	- 0.9	- 0.5	+ 0.8	+ 1.6	- 1.8

¹ Employees according to National Accounts definition.

² In a common currency; minus sign indicates improvement of competitiveness.

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Projections - December 2007

Labour market

Changes from previous year (1,000^s)

	2004	2005	2006	2007	2008	2009
Demand for labour						
Persons in active employment ¹	+ 25.1	+ 37.2	+ 55.9	+ 67.8	+ 34.0	+ 26.0
Employees ²	+ 21.1	+ 31.9	+ 51.5	+ 63.6	+ 30.0	+ 22.0
<i>Percentage changes from previous year</i>	+ 0.7	+ 1.0	+ 1.7	+ 2.0	+ 0.9	+ 0.7
Nationals	+ 9.2	+ 20.0	+ 35.0	+ 41.6	+ 13.0	+ 9.2
Foreign workers	+ 11.9	+ 11.9	+ 16.5	+ 22.0	+ 17.0	+ 12.8
Self-employed ³	+ 4.0	+ 5.3	+ 4.4	+ 4.2	+ 4.0	+ 4.0
Labour supply						
Population of working age (15 to 64 years)	+ 34.4	+ 15.6	+ 18.5	+ 15.5	+ 19.8	+ 20.2
(15 to 59 years)	+ 35.6	+ 48.5	+ 52.8	+ 17.0	+ 10.2	+ 13.7
Labour force ⁴	+ 28.9	+ 45.9	+ 42.4	+ 51.3	+ 33.0	+ 31.0
Surplus of labour						
Registered unemployed ⁵	+ 3.8	+ 8.8	- 13.5	- 16.5	- 1.0	+ 5.0
1,000 ^s	243.9	252.7	239.2	222.7	221.7	226.7
Unemployment rate						
Eurostat definition ⁶	percent	4.8	5.2	4.8	4.3	4.2
Percent of total labour force ⁵	percent	6.4	6.5	6.1	5.6	5.5
National definition ^{5,7}	percent	7.1	7.3	6.8	6.2	6.2
Employment rate						
Persons in active employment ^{1,8}	percent	62.3	62.8	63.6	64.6	65.0
Total employment (Eurostat) ^{6,8,9}	percent	67.8	68.6	70.2	71.1	71.5

¹ Excluding parental leave, military service, and unemployed persons in training. ² According to Federation of Austrian Social Security Institutions. ³ According to WIFO. ⁴ Economically active employment plus unemployment.

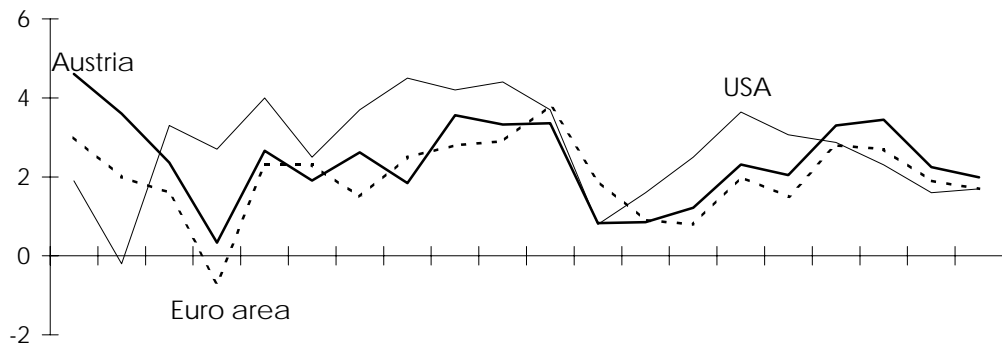
⁵ According to Public Employment Service Austria. ⁶ According to Eurostat Labour Force Survey.

⁷ Percent of total labour force excl. self-employed. ⁸ Percent of population of working age (15 to 64 years).

⁹ Changed survey method.

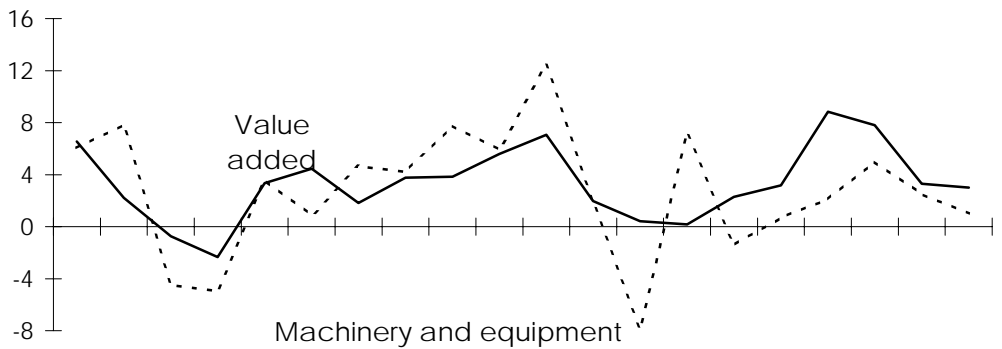
Growth of real GDP

Percent



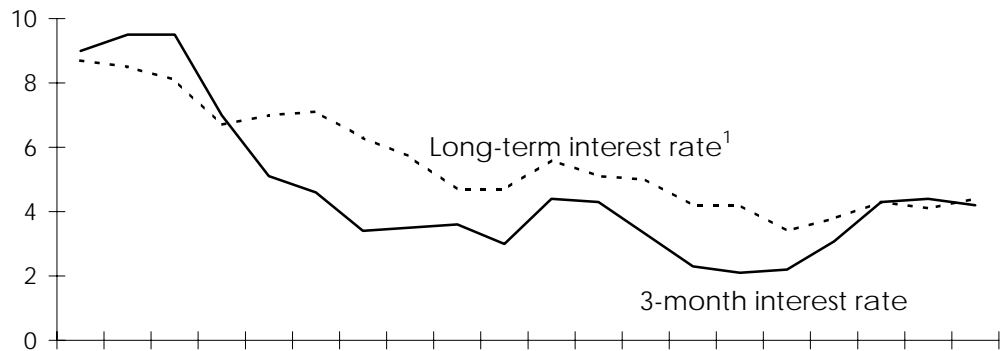
Manufacturing and investment

Percentage changes from previous year, volume



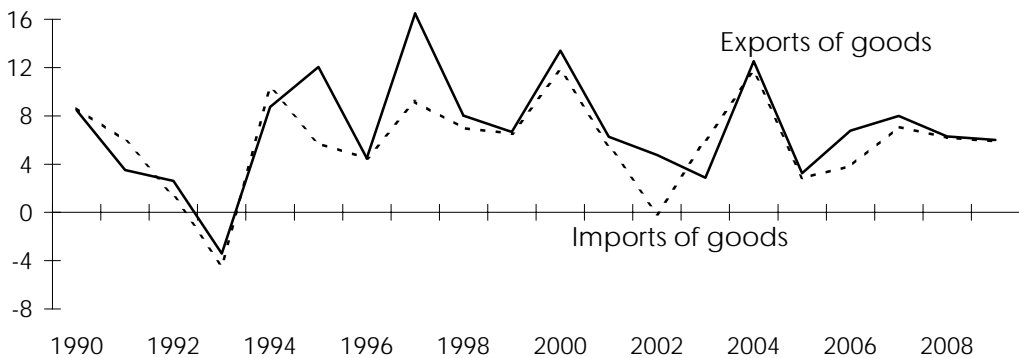
Short-term and long-term interest rates

Percent



Trade

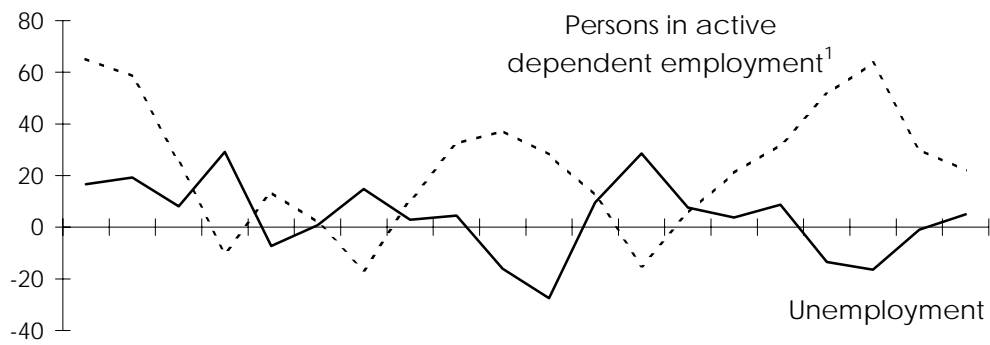
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

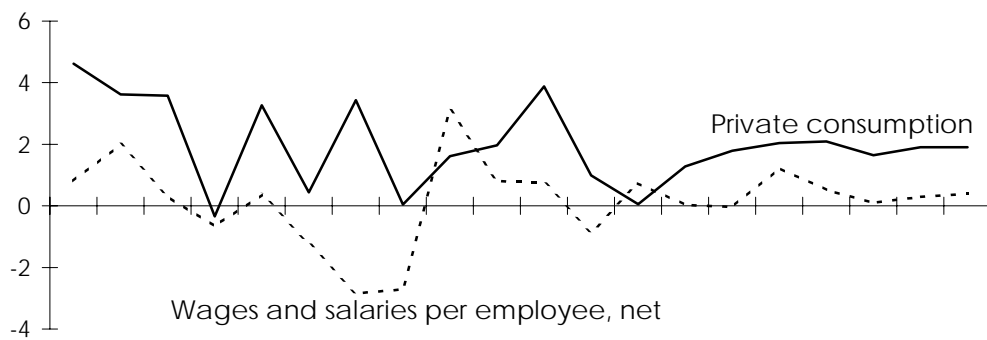
Employment and unemployment

1,000^s from previous year



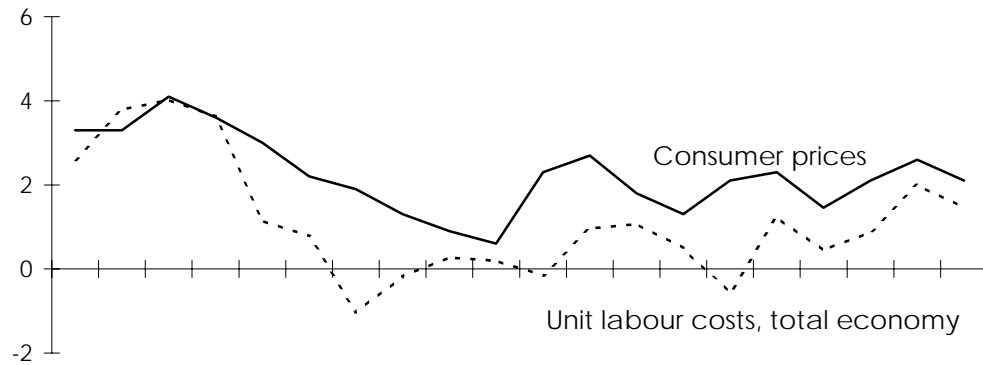
Consumption and income

Percentage changes from previous year, volume



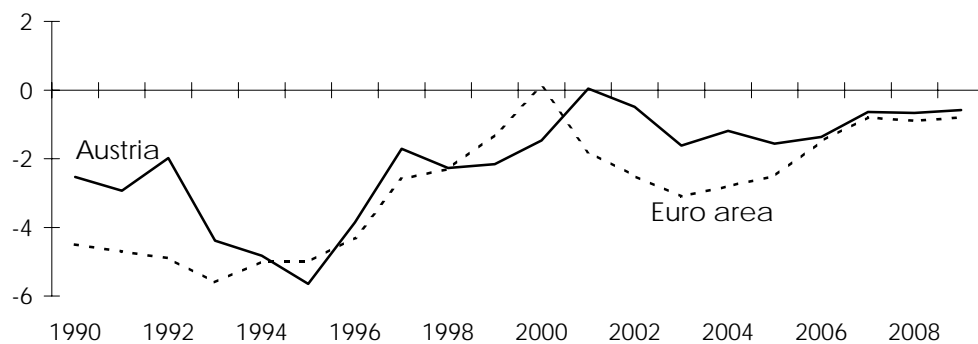
Inflation and unit labour costs

Percentage changes from previous year



General government financial balance

As a percentage of GDP



¹ Excluding parental leave, military service, and unemployed persons in training.

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