

Gerhard Rünstler

Economic Recovery in Third Quarter 2009

Business Cycle Report of November 2009

Global economic conditions improved further in the third quarter of 2009: world trade and economic activity in the industrialised countries expanded for the first time in twelve months. Leading indicators point to a continuation of the upturn. The global economy will nevertheless remain fragile for quite some time. In Austria, GDP grew at a seasonally and working day adjusted rate of 0.9 percent quarter-on-quarter.

All staff members of the Austrian Institute of Economic Research contribute to the Business Cycle Report. • Data processing: Christine Kaufmann, Martha Steiner • Cut-off date: 13 November 2009. • E-mail address: Gerhard.Ruenstler@wifo.ac.at

Seasonally and working day adjusted GDP increased by 0.9 percent in Austria during the third quarter, compared with the previous quarter, according to WIFO's quarterly national accounts flash estimate. Hence Austria for the first time since the second quarter of 2008 again recorded an increase in economic output. GDP was still 2.4 percent lower than a year earlier (second quarter –5.3 percent), though.

This mainly reflects the beginning recovery of the global economy observed in the course of the third quarter. World trade and economic activity in the industrialised countries for the first time since the collapse towards the end of 2008 grew again quarter-on-quarter in the third quarter of 2009. GDP increased by 0.9 percent in the USA (second quarter –0.2 percent), and by 0.4 percent in the euro area (second quarter –0.2 percent). Germany (third quarter +0.7 percent) and neighbouring countries with a supplying industry recorded above-trend growth.

According to business surveys, the upward trend is likely to continue also in the fourth quarter. Firms' production expectations and new orders have improved steadily in the USA and the euro area in recent months. WIFO's October business cycle survey shows that production expectations have brightened increasingly also in Austria, while order book levels have to date risen moderately.

The global recovery was made possible by massive fiscal stimulus in Western industrialised countries and China. Premiums for new car purchases, state transfers and infrastructure investments shored up demand, while subsidising short-time working in some European countries mitigated the effects of the downturn on the labour market.

However, one must not overlook the difficulties still standing in the way of a lasting upturn in the medium term: world trade and production levels are substantially lower than prior to the onset of the crisis. High unemployment rates and household indebtedness in the USA and a few other countries are dampening private consumption. Hence the growth momentum is expected to weaken somewhat at the beginning of 2010 as the car-scrapping premium and other fiscal measures in Europe and the USA expire.

The high rate of growth of the Austrian economy during the third quarter offsets the above-trend decline compared with the euro area observed in the second quarter. It was partly the result of manufacturing output growing at a seasonally adjusted rate of 4.0 percent quarter-on-quarter (second quarter –0.9 percent). The Austrian economy reacted with a slight lag to the favourable economic developments in Europe; in the third quarter, goods exports expanded at a seasonally adjusted quarter-on-quarter rate of 2.1 percent (second quarter –3.2 percent). The inventory build-

up may also have boosted production. Another factor was the increase in construction investment (+1.3 percent) supported by various government measures. Private consumption rose again by 0.1 percent in the third quarter (second quarter +0.1 percent). It developed steadily in the course of the year in spite of the slump, and this year benefits from the low inflation rate and the tax reform.

The Austrian labour market shows first signs of stabilising. In seasonally adjusted terms, employment remained unchanged for two successive months. The number of unemployed persons rose further, however, while that of job vacancies fell. The seasonally adjusted unemployment rate (according to the Austrian definition) stood unchanged at 7.5 percent in October, an increase by 1.4 percentage points from a year earlier. Overall, the situation remains tight, as further layoffs may take place should economic growth be weaker than currently expected.

Table 1: Flash estimates of quarterly national accounts

	2008			2009		
	Second quarter	Third quarter	Fourth quarter	First quarter	Second quarter	Third quarter
Adjusted for seasonal and working day effects, percentage changes from previous quarter, volume						
<i>GDP, expenditure approach</i>						
Final consumption expenditure						
Households ¹	+ 0.1	+ 0.1	+ 0.1	+ 0.1	+ 0.1	+ 0.1
General government	+ 2.6	- 0.8	+ 1.6	- 1.6	+ 0.2	+ 1.2
Gross capital formation	+ 1.3	- 3.8	- 6.9	- 6.2	- 1.7	+ 1.8
Gross fixed capital formation	+ 0.7	- 1.7	- 2.8	- 2.5	+ 0.1	+ 1.3
Exports	- 1.3	- 3.9	- 5.6	- 5.7	- 2.8	+ 1.4
Imports	- 0.1	- 3.1	- 4.1	- 5.6	- 2.3	+ 0.9
Gross domestic product	+ 0.5	- 0.7	- 1.1	- 2.6	- 0.5	+ 0.9
<i>GDP, output approach</i>						
Agriculture, forestry	- 0.0	- 1.8	- 0.5	+ 0.5	- 2.0	+ 2.8
Industry, including energy	+ 1.0	- 1.9	- 4.1	- 5.1	- 1.8	+ 2.3
Manufacturing	+ 1.0	- 2.2	- 4.9	- 7.4	- 0.9	+ 4.0
Construction	+ 0.7	- 2.7	- 0.7	- 1.4	- 0.6	+ 2.0
Wholesale and retail trade; repairs; hotels and restaurants; transport, communication	+ 0.4	- 2.0	- 1.0	- 2.6	- 0.9	+ 0.1
Financial intermediation; real estate, renting and business activities	+ 0.8	+ 0.0	- 0.5	- 1.7	- 0.3	+ 0.2
Other service activities	+ 0.5	+ 0.4	+ 0.7	+ 0.4	+ 0.5	+ 0.5
Taxes on products	+ 0.5	- 0.9	- 0.8	- 1.3	+ 0.9	+ 0.1
Subsidies on products	+ 1.8	+ 0.3	- 1.1	- 2.6	- 1.6	- 0.7
Percentage change from previous year						
Gross domestic product, volume	+ 3.0	+ 2.3	- 0.3	- 5.2	- 5.3	- 2.4

Source: WIFO. – ¹ Including private non-profit institutions serving households.

Inflation rate developments in the industrialised countries have lately been determined by the high volatility of crude oil prices. Therefore, the consumer price index excluding food and energy is currently a better indicator of medium-term inflation trends; on this basis, the inflation rate in the USA and the euro area was 1.5 and 1.2 percent, respectively, in September. In Austria, headline CPI inflation was 0.1 percent in September; excluding energy and unprocessed food, inflation stood at 1.3 percent.

Global economic conditions improved markedly in the third quarter. Massive fiscal packages launched in the USA, China and – to a somewhat lesser extent – in European countries stimulated demand and initiated the return to GDP growth. According to first estimates, global trade – which had been declining since the fourth quarter of 2008 – expanded by around 5 percent quarter-on-quarter in the third quarter. However, the world trade volume was still almost 20 percent below its peak in April 2008 (according to Centraal Planbureau, the Netherlands). With demand stabilising, firms have begun to rebuild their inventories. After the collapse late in 2008 firms' inventory levels were high and were subsequently reduced in the first half of 2009.

**Global economic
recovery has started**

In the USA, real GDP grew at a seasonally adjusted quarter-on-quarter rate of 0.9 percent in the third quarter of 2009 (second quarter -0.2 percent), following four consecutive quarters of negative growth. The recovery was mainly driven by private consumption, which continues to benefit considerably from fiscal measures. Notably the introduction of a government premium for new car purchases in the third quarter led to a 5.2 percent increase in the consumption of durable goods compared with the previous quarter. Private fixed investment also stabilised in the third quarter, following a sharp drop in the first half of the year. The public deficit for 2009 is forecast to be somewhere between 11 and 12 percent of GDP.

Economies in South-East Asia are benefiting from China's massive fiscal package. Industrial production in China and in countries having strong trading links with China (Korea, Australia) may already have almost reached pre-crisis levels again. One exception here is Japan, which, because of the structure of its exports, has been hit hardest among the big industrialised countries.

Economic growth also resumed in the euro area in the third quarter (+0.4 percent, second quarter -0.2 percent), with GDP consequently 4.1 percent lower than a year earlier. Developments in the euro area have been quite heterogeneous. While export-oriented economies, notably Germany (second quarter +0.4 percent, third quarter +0.7 percent) and neighbouring countries with a supplying industry (Czech Republic, Slovakia) recorded high growth rates, countries with indebtedness problems (Spain, Hungary) saw their economies shrink further. In Great Britain, GDP fell by 0.4 percent quarter-on-quarter.

Expectations for the fourth quarter are optimistic, as evidenced by business surveys. The OECD's leading indicators suggest that industrial activity will continue to expand in the USA and the euro area. The US Purchasing Managers' Index also rose yet again in October, to 55.7 percent, a reading clearly above the 50-percent mark that is indicative of expansion (September 52.6 percent).

The European Commission's surveys also depict a pick-up in business sentiment in the euro area. Production expectations, order books and the assessment of inventory levels have been improving steadily since March. Unlike in the USA, the values are still well below the respective long-term averages, though.

Consumer confidence has risen steadily in the euro area but has stagnated in the USA since June 2009. This development probably reflects the differences in the evolution of labour markets.

Unemployment growth has slowed recently. In September, the seasonally adjusted unemployment rate was 9.8 percent in the USA, and 9.7 percent in the euro area. In the euro area, the unemployment rate rose at a slower pace than was to be expected, given the decline in production. In some countries (Germany, Italy), government subsidies for short-time working schemes played an important role here. In line with this development, consumer confidence has been improving constantly since April.

The decline in commodity prices as compared to last year has been dampening inflation globally. In the third quarter, the HWWI Index of World Market Prices of Commodities excluding energy in euro terms was 19 percent below the value one year earlier. The index has again followed an upward trend since March 2009, though.

Given the sharp fall in crude oil prices compared with a year earlier, CPI inflation in the OECD stood at -0.4 percent in September, already the fourth consecutive month of negative rates (USA -1.3 percent, euro area -0.3 percent). However, the price of crude oil has again been rising noticeably since the beginning of the year, so that the negative contribution from energy prices to inflation will be reversed towards the end of this year.

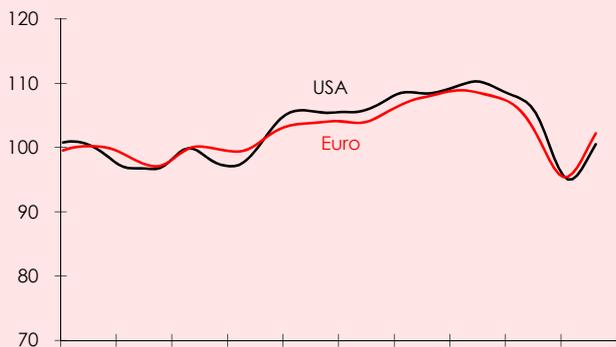
The CPI inflation rate excluding energy and food may currently well be a better indicator of aggregate inflation trends. In September, this rate stood at 1.5 percent in the OECD (USA 1.5 percent, euro area 1.2 percent). It has thus been falling modestly since its peak of 2.4 percent in September 2008.

In the third quarter of 2009 the industrialised countries registered renewed growth for the first time in a year. Leading indicators continue to point upwards. There still exist risks to the upturn, though.

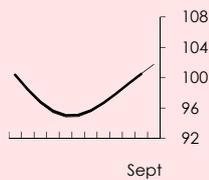
Figure 1: International business climate

Seasonally adjusted, 2000 = 100, 3-month moving average

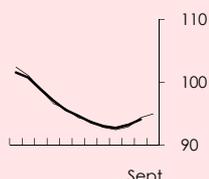
Leading indicators



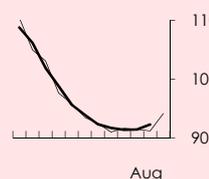
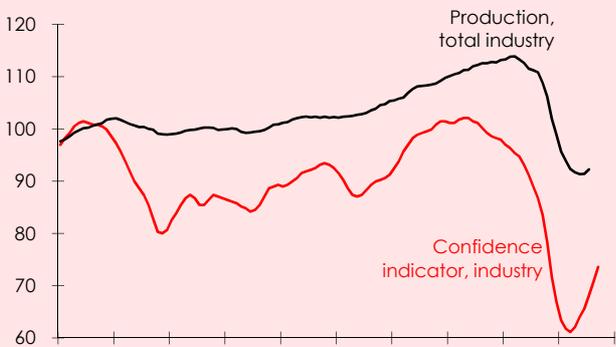
12-month performance



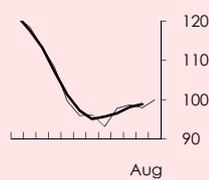
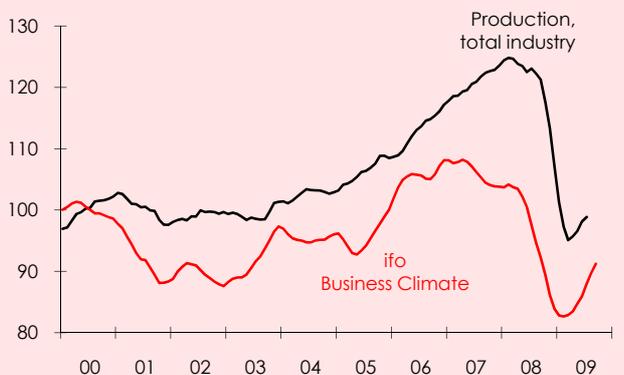
USA



Euro area



Germany



Source: European Commission, Deutsche Bundesbank, ISM (Institute for Supply Management™), ifo (Institute for Economic Research, Munich), OECD.

The Austrian economy grew at a seasonally and working day adjusted rate of 0.9 percent in real terms in the third quarter, after -0.5 percent in the second quarter, according to WIFO's latest flash estimate. Hence, GDP was 2.4 percent below the year-earlier level in the third quarter. The Austrian economy reacted with a slight lag to the rebound in the European economy. Manufacturing value added increased by 4.0 percent (seasonally adjusted) quarter-on-quarter in the third quarter (second quarter -0.9 percent). In line with international developments, the situation in the export sector largely stabilised in the third quarter. Goods exports rose at a seasonally adjusted quarter-on-quarter rate of 2.1 percent (second quarter -3.2 percent), while goods imports grew by 1.3 percent (second quarter -2.3 percent). Hence manufacturing and foreign trade activity increased again for the first time since the first half of 2008. Inventory rebuilding may also have boosted production.

Propped up by various government measures, construction investment increased by 1.3 percent (seasonally adjusted) in the third quarter, compared with the previous quarter (second quarter +0.3 percent). Construction value added grew at a brisk +2.0 percent pace in the third quarter (second quarter -0.6 percent), whereas value added growth in the services sectors trade, accommodation and transport remained stable at +0.1 percent (second quarter -0.9 percent). Business spending on machinery and equipment, on the other hand, remained flat at 0.0 percent (second quarter -1.8 percent), with high excess capacity and difficult financing conditions expected to weigh on it also in the months ahead.

Private consumption rose at a seasonally and working day adjusted rate of 0.1 percent quarter-on-quarter in the third quarter (second quarter +0.1 percent). It grew steadily over the year, and this year benefits from last year's relatively high wage settlements and the tax reform. Net retail sales (excluding cars) remained stable. In the first seven months of 2009 they posted marginal year-on-year gains (in price adjusted terms).

Like the surveys for the euro area, WIFO's business cycle survey in October indicated a further easing of the situation. Notably firms' production expectations improved yet again. The number of firms anticipating an improvement in their business situation over the six-month period ahead is now almost as high as that of firms expecting the situation to deteriorate.

The assessment of current order books, while brightening somewhat, still remained at a rather low level. 50 percent of firms continued to describe their order books as being "insufficient", while still 75 percent of firms in the motor vehicle industry reported a lack of orders. The average capacity utilisation rate rose to 75 percent in October, an increase by 2 percentage points from July.

Business services firms also judge their business situation over the six-month period ahead more positively. Firms in the building construction and civil engineering sectors gave a more optimistic assessment of construction activity. Only the civil engineering sector has also registered rising order book levels, most likely attributable to the expansion of public investment.

In the period from May to September 2009, tourism sales declined by 1.7 percent from the record level registered a year before (€ 9.02 billion), according to provisional calculations. At -1.2 percent, the number of overnight stays fell at a somewhat slower pace from May to September 2009. The demand from abroad fell by 2.4 percent overall, whereas overnight stays by resident travellers exceeded the year-earlier level by 1.5 percent.

In the first five months of the 2009 summer season, only Burgenland and Vorarlberg posted moderate sales increases. Styria, Upper Austria and Tyrol experienced below-trend drops. Sales in Carinthia were more or less in line with the Austrian average, whereas exceptionally high sales declines were registered in Salzburg, Lower Austria and Vienna. Demand is expected to fall further over the remainder of the year because of the repercussions of the financial and economic crisis.

Austrian economy growing briskly in third quarter

Austrian GDP grew by 0.9 percent quarter-on-quarter in the third quarter of 2009. This high growth rate reflects the upward trend of the European economy, but may in part also be attributable to special factors.

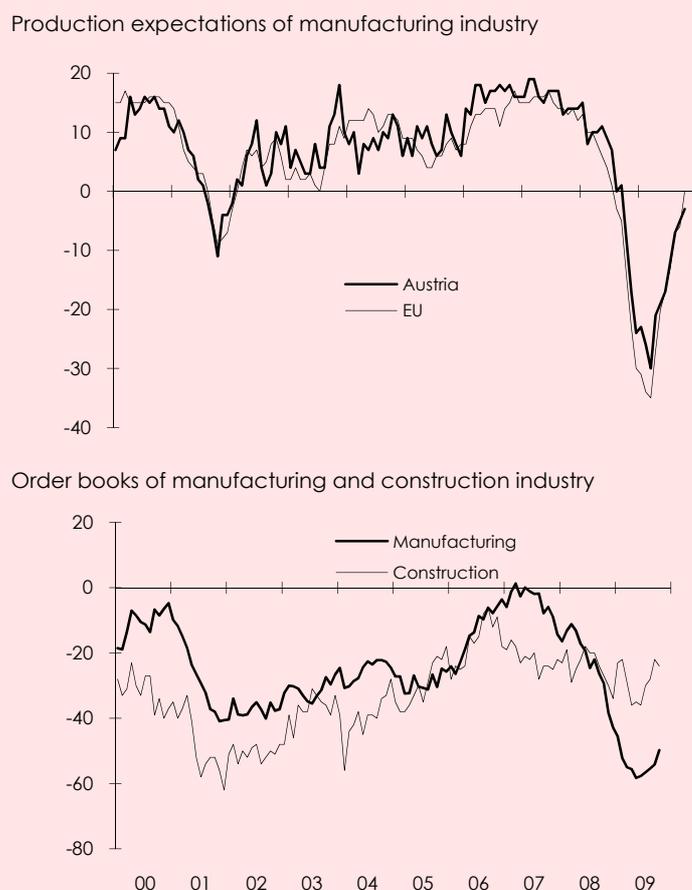
October sees industrial and services sectors more optimistic

Summer tourism posting year-on-year decline

The decline in international consumer demand impaired tourism also in the summer.

Figure 2: WIFO business cycle survey

Differences between the percentage shares of correspondents giving positive and negative replies, seasonally adjusted



Source: European Commission, WIFO business cycle survey.

The labour market typically reacts with a lag of a few months to cyclical trends. However, the figures for October already indicate some stabilisation: for the second month in a row, the seasonally adjusted number of persons in dependent employment remained unchanged compared with the previous month, while unemployment rose by a mere 0.7 percent month-on-month in October (September +1.2 percent). Active employment was thus 1.7 percent (-55,700) lower than a year earlier (September -1.8 percent). All in all, 245,500 persons were registered as unemployed, an increase by 42,700 (21.1 percent) from a year before. The seasonally adjusted unemployment rate was also unchanged at 7.5 percent in October, according to the Austrian method of calculation, an increase by 1.4 percentage points on the same month a year earlier.

The number of job vacancies continued to fall in October (-1.7 percent month-on-month on a seasonally adjusted basis), with the pace of decline moderating somewhat in recent months, though – in the second quarter it had still averaged -2.8 percent per month. In October, the number of vacant jobs was thus 20.6 percent lower than a year earlier.

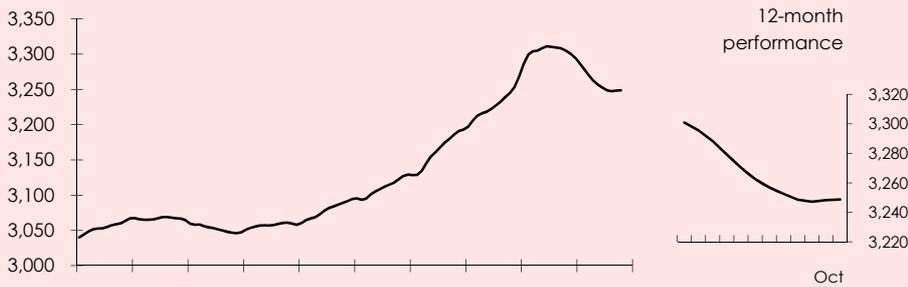
WIFO's business cycle survey in October showed a clear upward trend of employment expectations in the industrial sector. Firms' low capacity utilisation rates remain a risk to employment, though. Up to now, employment has been shrinking less than was to be expected in the light of the sharp decline in production. Apparently many firms kept their staff for the time being, partly financed by short-time-working schemes. There is a risk of unemployment rising further should economic growth be weaker than expected over the coming quarters.

First signs of labour market stabilising

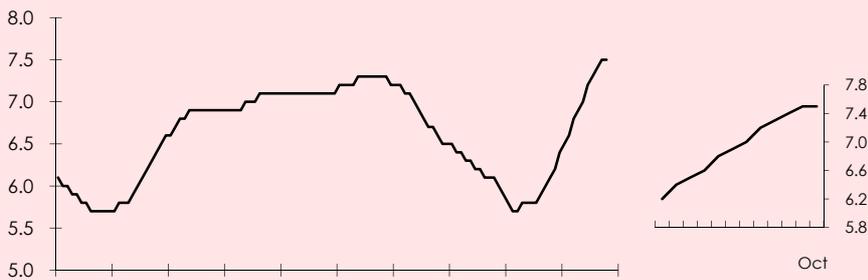
The seasonally adjusted number of persons in dependent employment remained unchanged in the last two months. The number of job vacancies is still falling, though.

Figure 3: Key economic indicators

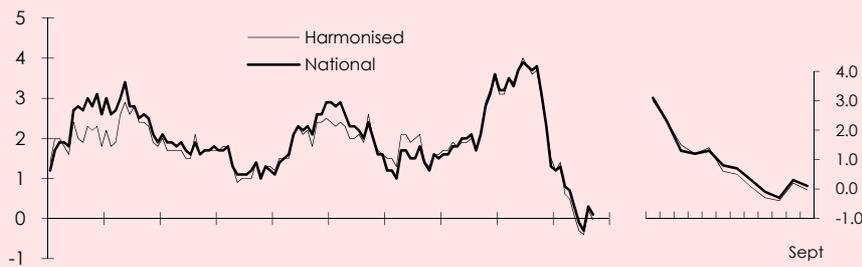
Persons in active dependent employment¹, (1,000), seasonally adjusted



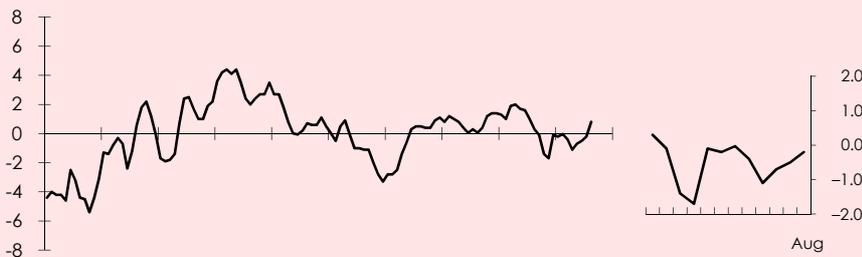
Unemployment rate, traditional Austrian method², seasonally adjusted



Consumer prices, year-to-year percentage changes



Real effective exchange rate, year-to-year percentage changes



10-year central government bonds (benchmark), percent



Source: Public Employment Service Austria, Federation of Austrian Social Security Institutions, Oesterreichische Nationalbank, Statistics Austria, WIFO calculations. – ¹ Excluding parental leave, military service, and unemployed persons in training. – ² As a percentage of total labour force excluding self employed, according to Public Employment Service.

Methodological Notes and Short Glossary

Period comparisons

Time-series comparisons with the previous period, e.g., the previous quarter, are adjusted for seasonal effects. They also include effects that result from a different number of working days in the period (e.g., Easter). In the text, this is referred to as "seasonally and working day adjusted changes".

The phrase "changed compared with a year before . . .", on the other hand, describes a relative change compared with the same period a year before and refers to unadjusted time series.

The analysis of the seasonally and working day adjusted development provides more precise information about the actual course of economic activity and shows turning points sooner. However, the data are subject to additional revisions as seasonal adjustment is based on statistical methods.

Real and nominal values

In principle, the values shown must be understood as real values, i.e., adjusted for price effects. Whenever values are shown as nominal values (e.g., foreign trade statistics), this is specifically mentioned.

Inflation, CPI und HICP

The inflation rate measures changes in consumer prices compared with a year before. The Consumer Price Index (CPI) is a measure of national inflation. The Harmonised Index of Consumer Prices (HICP) is the basis for comparable measurement of inflation in the EU and for the evaluation of price stability in the euro area (<http://www.statistik.at/>).

WIFO Business Cycle Survey and WIFO Investment Survey

The WIFO business cycle survey is a monthly survey in which around 1,100 Austrian firms are asked to assess their current and future economic situation. The WIFO investment survey is conducted twice a year, asking companies about their investment activity (<http://www.itkt.at/>). The indicators are balances between the positive and negative responses expressed as a percentage of the total number of firms sampled.

Unemployment rate

Austrian national definition: The number of persons registered as job seekers with the Public Employment Service expressed as a percentage of the dependent labour force. Labour force is the sum of the unemployed and the persons in dependent employment (measured in standard employment relationships). Database: registrations with the Public Employment Service (AMS) and Association of Austrian social insurance agencies.

Definition according to ILO and EUROSTAT: Any person who is not gainfully employed and is actively seeking work is considered unemployed. Gainfully employed persons comprise all persons who during the reference week worked for at least one hour in a self-employed capacity or in paid employment. Persons receiving child-care benefit and apprentices are classified as gainfully employed, whereas persons in military service or persons carrying out alternative service are not. The unemployment rate is the number of unemployed persons expressed as a percentage of the total labour force (unemployed persons plus gainfully employed persons). Database: data from household surveys ("Mikrozensus").

Terms used in connection with the national definition of the unemployment rate

Persons in training: Persons who at a set date are enrolled in AMS (Public Employment Service) training programmes. When calculating the unemployment rate, their number is not taken into account either in the denominator or in the numerator.

Persons in dependent active employment: "Persons in dependent employment" include persons receiving child-care benefit, as well as persons in military service or persons carrying out alternative service with a valid employment contract. By deducting their number one arrives at the number of "persons in dependent active employment".

In September, the rate of inflation (as measured by the consumer price index) stood at 0.1 percent. The harmonised inflation rate (HICP) was marginally lower at 0.0 percent, but slightly higher than the euro area average (-0.3 percent).

These distinctly low values are entirely the result of movements in crude oil prices and are expected to be only short-lived. The price of Brent, which had peaked around \$ 140 per barrel in July 2008, fell steadily to \$ 40 in December 2008 and has since risen again to currently close to \$ 80. For this reason, the price index of the expenditure category "transport" in September was still 4.6 percent lower than a year before. However, energy prices are expected to lift inflation again towards the end of the year.

CPI inflation excluding energy and unprocessed food stood at 1.3 percent in September, a decline by 0.6 percentage points from May.

Inflationary pressures remain moderate

The inflation rate is particularly low, a result of the drop in fuel prices compared with a year ago. Excluding energy and unprocessed food, it stood at 1.3 percent in September.

Wholesale prices are beginning to recover, following a sharp decline due to weak demand in 2008. In October, the wholesale price index was 6.2 percent below the year-earlier level – after a decline of still 11.5 percent in July.