Sandra Bilek-Steindl

Signs of Economic Rebound are Increasing

Business Cycle Report of September 2009

After the Austrian economy still contracted also in the second quarter of 2009, at a seasonally and working day adjusted rate of 0.5 percent quarter-on-quarter, (–4.6 percent year-on-year), the recession in the manufacturing sector continues to weaken in the third quarter. Evidence from the latest WIFO business cycle survey suggests that the downturn has already bottomed out. Signs of an economic rebound are increasing also among Austria's main trading partners. The inventory cycle, along with fiscal policy measures, is stabilising global industrial activity. Labour market conditions continue to deteriorate, with notably the industrial and construction sectors experiencing yet another rise in unemployment.

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: 9 September 2009. • E-mail address: Sandra.Bilek-Steindl@wifo.ac.at

According to WIFO's latest quarterly national account data, the pace of contraction in Austrian real GDP eased to a mere 0.5 percent (seasonally and working day adjusted) quarter-on-quarter in the second quarter of 2009 (after –2.7 percent in the first quarter). In its last flash estimate of mid-August, WIFO had estimated GDP to shrink by 0.4 percent quarter-on-quarter. In the fourth consecutive quarter seeing a quarterly negative rate of change, real GDP was thus 4.6 percent below the year-earlier level. The recession in the manufacturing sector appears to have bottomed out. After the pace of decline already moderated in the second quarter (–2.2 percent, following –10.7 percent in the first quarter), leading indicators also point to a further stabilisation. According to WIFO's August business cycle survey, production expectations have improved for the fifth straight time. The inventory cycle also plays a role here: after the dramatic inventory rundown in the first half of 2009, production can be expanded again.

All major leading indicators have hit bottom and are beginning to turn also globally. In the USA, the ISM Purchasing Managers' Index in August for the first time in 13 months reached the 50-percent mark that is indicative of expansion. Consumer confidence, which had picked up in spring, remains subdued, however, owing to the high unemployment rate. In the euro area, the Economic Sentiment Indicator in August improved already for the fourth straight time. The Euroframe Growth Indicator also points to quarter-on-quarter GDP growth in the third quarter of 2009.

Austria's external trade should also recover in the course of an international stabilisation; it usually reacts quickly in the business cycle. The decline in exports already moderated in the second quarter of 2009 (–2.3 percent quarter-on-quarter, after –7.4 percent in the first quarter). With imports falling at a slower pace in the second quarter (–1.5 percent), the contribution from net exports was negative and depressed GDP.

A positive contribution in the second quarter came from private consumption (+0.4 percent, after +0.1 percent in the first quarter), underpinned by the effects of the tax reform and the car-scrapping premium. While the retail sector reported sales increases, business remained poor for wholesalers, who continued to suffer from weak export demand. Having contracted sharply in the first quarter, gross fixed capital formation stabilised, with notably construction investment recovering. The construction sector is expected to strengthen further in the third quarter of 2009. Evidence from WIFO's latest business cycle survey shows that firms' assessment of order books has improved for the second time in a row and employment expectations have also turned more positive.

Table 1: Quarterly national accounts

	2007	2008	2008				2009	
			First quarter	Second quarter	Third quarter	Fourth quarter	First quarter	Second quarter
			Percentage changes from previous quarter					
Adjusted for seasonal and working day effects, volume								
Final consumption expenditure			– 0.2	+ 0.7	– 0.1	+ 0.5	– 0.2	+ 0.4
Households[1]			+ 0.2	+ 0.1	+ 0.1	+ 0.1	+ 0.1	+ 0.4
General government			– 1.2	+ 2.8	– 0.7	+ 1.8	– 1.3	+ 0.4
Cross capital formation			+ 0.2	+ 0.0	– 0.7	– 2.5	– 3.3	– 2.2
Gross fixed capital formation			+ 0.3	– 0.2	– 1.3	– 2.1	– 2.3	– 1.9
Machinery and equipment			+ 0.4	– 0.4	– 2.4	– 4.0	– 4.6	– 4.1
Construction			+ 1.4	+ 0.1	– 0.7	– 1.7	– 2.1	– 1.0
Exports, goods and services			+ 1.3	– 0.9	– 3.2	– 5.4	– 7.4	– 2.3
Goods			+ 2.0	– 1.1	– 3.8	– 7.9	– 9.3	– 3.1
Services			+ 0.4	– 0.4	– 1.0	– 1.4	– 1.4	– 0.6
Imports, goods and services			– 0.6	– 0.4	– 3.1	– 3.9	– 4.5	– 1.5
Goods			– 0.5	+ 0.0	– 3.5	– 4.4	– 5.5	– 2.0
Services			– 0.4	– 1.4	– 2.2	– 2.6	– 2.0	– 1.1
Gross domestic product			+ 1.1	+ 0.3	– 0.4	– 1.0	– 2.7	– 0.5
Manufacturing			+ 3.2	+ 1.3	– 1.7	– 2.8	– 10.7	– 2.2
	2007	2008	2008				2009	
			First quarter	Second quarter	Third quarter	Fourth quarter	First quarter	Second quarter
			Percentage changes from previous year					
Volume, chained prices								
Final consumption expenditure	+ 1.0	+ 1.4	+ 1.7	+ 1.5	+ 1.6	+ 0.8	– 0.7	+ 1.6
Households[1]	+ 0.8	+ 0.8	+ 1.1	+ 0.4	+ 1.4	+ 0.2	– 2.1	+ 2.1
General government	+ 1.7	+ 3.2	+ 3.2	+ 4.6	+ 2.2	+ 2.7	+ 3.4	+ 0.5
Cross capital formation	+ 3.9	+ 0.3	– 1.8	+ 9.5	– 1.9	– 4.9	– 15.1	– 20.5
Gross fixed capital formation	+ 3.8	+ 1.0	+ 0.8	+ 4.2	– 0.1	– 0.7	– 11.4	– 11.0
Machinery and equipment	+ 5.0	– 0.0	– 2.2	+ 7.3	– 1.8	– 3.0	– 16.0	– 20.3
Construction	+ 2.9	+ 1.8	+ 3.8	+ 2.2	+ 0.9	+ 0.9	– 9.6	– 6.2
Exports, goods and services	+ 9.4	+ 0.8	+ 6.9	+ 3.9	+ 1.6	– 8.5	– 18.8	– 18.1
Goods	+ 9.9	+ 0.2	+ 6.4	+ 4.3	+ 2.0	– 11.1	– 21.9	– 22.4
Services	+ 8.0	+ 2.3	+ 7.7	+ 2.4	+ 0.4	– 1.3	– 11.3	– 3.9
Imports, goods and services	+ 7.3	– 0.7	+ 1.9	+ 4.2	– 2.8	– 5.8	– 15.6	– 14.6
Goods	+ 8.3	– 0.5	+ 1.9	+ 4.9	– 3.0	– 5.3	– 16.6	– 16.4
Services	+ 3.3	– 1.8	+ 2.1	+ 1.3	– 2.0	– 7.7	– 11.1	– 7.1
Gross domestic product	+ 3.5	+ 2.0	+ 3.4	+ 3.0	+ 2.3	– 0.3	– 4.7	– 4.6
Manufacturing	+ 7.5	+ 3.9	+ 4.9	+ 6.4	+ 6.0	– 1.4	– 12.7	– 14.9
Gross domestic product, value	+ 5.7	+ 4.1	+ 5.9	+ 6.0	+ 4.6	+ 0.3	– 4.0	– 4.4

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

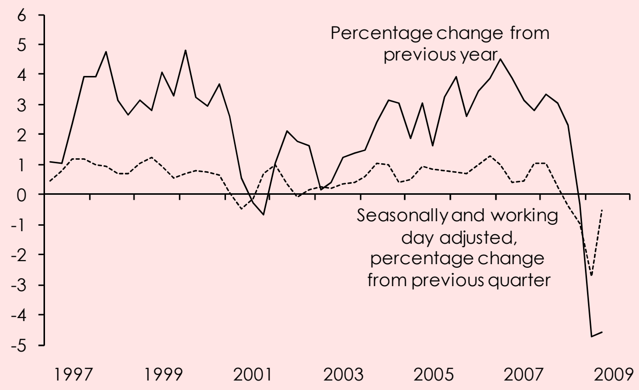
Austria's tourism sector cannot escape the impact of the global economic crisis. With the number of overnight stays declining, value added in the hotel and restaurant sector fell by 0.4 percent quarter-on-quarter in the second quarter.

As the economic outlook brightened, oil prices continued to rise, with the price for Brent crude trading at $ 72 per barrel in August (after around $ 43 at the beginning of the year, its lowest level in 2009). The fall in energy prices compared with a year earlier continues to dampen euro area inflation. Once this steady decline falls out of the year-on-year comparison, energy prices will cease to contribute negatively to inflation. In Austria, the consumer price index fell by 0.3 percent in July. Eurostat estimates euro area inflation at –0.2 percent in August (July –0.7 percent).

As expected, the labour market situation in Austria continues to deteriorate, with a recovery not yet in sight. In August, 238,800 persons were registered as unemployed, an increase by 54,900 or 29.8 percent compared with a year before. Compared with the previous month, the number of persons registered as unemployed also rose at an undiminished pace. This was accompanied by further workforce reductions in August. The seasonally adjusted unemployment rate according to the Austrian definition stood at 7.6 percent in August; according to the definition by Eurostat, the rate was 4.4 percent in July.

Figure 1: Growth of real GDP

Percentage changes from previous period



Source: WIFO.

Global economy stabilising

After the pace of contraction in US economic activity moderated in the second quarter (–0.3 percent, following around –1½ percent in each of the two preceding quarters), industrial activity is likely to have bottomed out in the summer. Industrial production, which had declined almost without exception on a month-on-month basis since January 2008, rose in July 2009 (+0.5 percent). Notably firms in the automotive industry and their suppliers sharply increased production in response to low stocks and the demand stimuli provided by the car-scrapping premium.

Global economic conditions are slowly easing. Fiscal policy measures and the inventory cycle began to stabilise the economy in the second quarter of 2009. However, high unemployment remains a threat to a lasting upturn.

Industrial production generally shows cyclical turning points quickly, but currently temporary effects of the measures taken to stabilise the economy are also beginning to emerge in the data. The inventory cycle, along with fiscal policy measures, is also stabilising the economy – following six quarters of de-stocking in the USA, companies now react even to a modest pick-up in demand with an expansion of production.

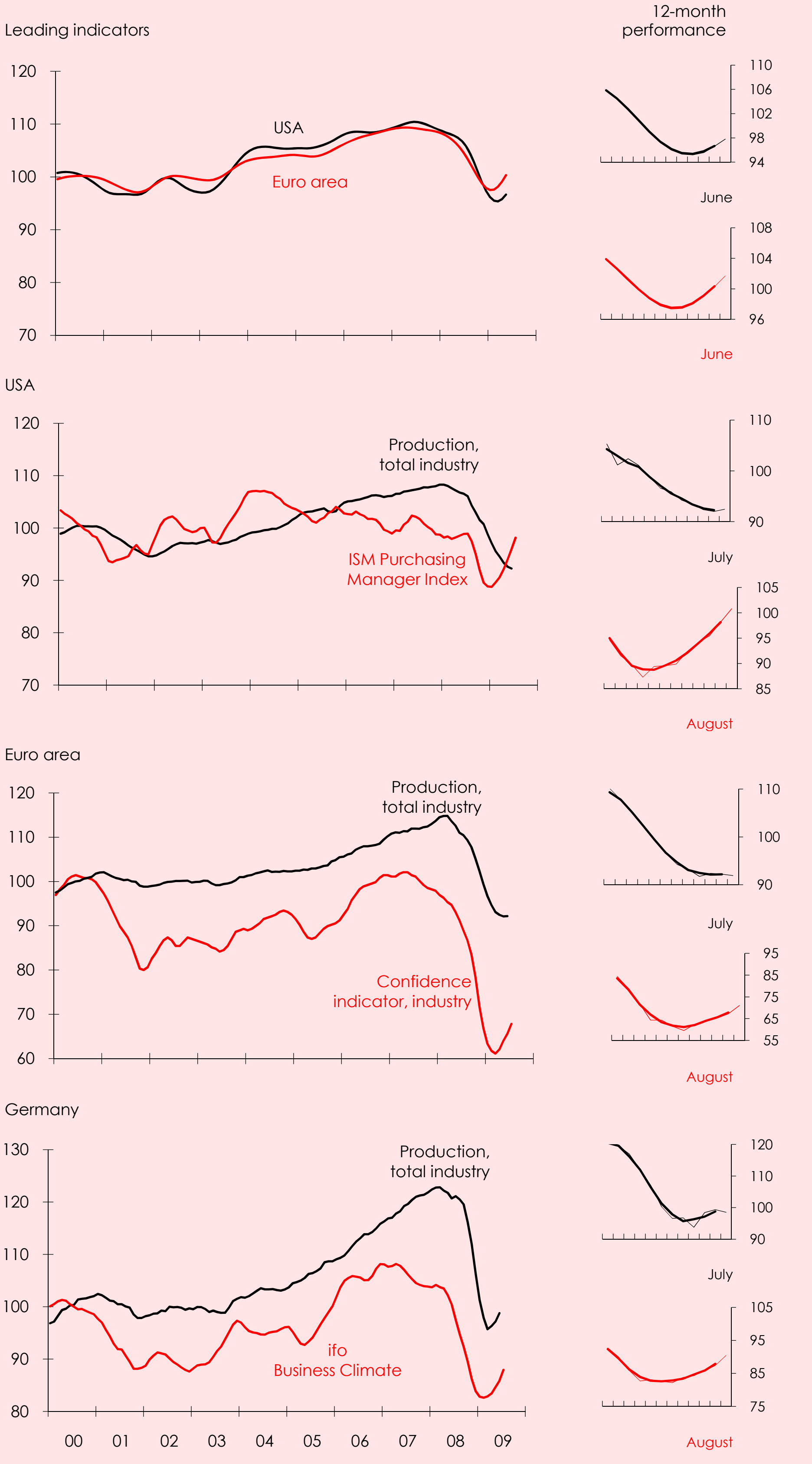
While in the USA corporate sector first signs of a recovery in domestic demand became apparent already in the second quarter, the conditions for private consumption have remained unfavourable; this impedes a lasting upturn. The sharp drop in real estate prices has been stabilising in month-on-month terms since April, but the Case-Shiller Home Price Index in the second quarter of 2009 was still 17 percent below its year-earlier level.

Retail sales stagnated amid constantly rising unemployment (August unemployment rate 9.7 percent). This is also reflected in the evidence presented in consumer confidence surveys, which remained subdued in the summer months.

In the Asian region, economic conditions appear to be easing as well. Following four quarters of negative growth rates, Japan's GDP increased by 0.9 percent quarter-on-quarter in the second quarter. Economic stimulus measures spurred private consumption. Consumer spending rose by 0.8 percent quarter-on-quarter, despite increasing unemployment (July 5.7 percent), which impedes a lasting and self-supporting upturn. Exports to Asian trading partners also rose again vigorously. China's economy is estimated to have again grown by around 8 percent in the second quarter, and clear signs of recovery were visible also in other emerging Asian economies.

Figure 2: International business climate

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



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

EU sees steady improvement in leading indicators

Signs of stabilisation are increasing also in the euro area. Leading indicators have bottomed out; economic policy measures are showing first effects. Unemployment has reached double-digit rates in some countries, however, with continued high levels of unemployment weakening the economy for a long time.

After the decline in economic activity slowed considerably in the second quarter (euro area –0.1 percent, EU –0.2 percent, compared with the previous quarter), leading indicators point to a further improvement in economic conditions in the second half of 2009. In August, the European Commission's Indicator of Consumer and Business Sentiment pointed up already for the fifth straight time. Consequently, it was as high as in autumn 2008 and still well below its long-term trend.

According to the Euroframe Growth Indicator, economic activity in the euro area will already grow again month-on-month in the third quarter of 2009. Manufacturing activity, which declined at a slower pace in the second quarter, is likely to expand again: new orders in industry rose by 3.1 percent in June, compared with May.

Euro area inflation averaged –0.2 percent year-on-year in August, according to Eurostat's flash estimate. In July, the Harmonised Index of Consumer Prices was 0.7 percent lower than a year before, when the average monthly oil price had peaked. The steady fall in energy prices since August 2008 disappears now from the year-on-year comparison; consequently, the dampening contribution from the energy component to inflation will level out.

The HWWI Index excluding energy raw materials quoted in euros in August was 16.8 below its year-earlier level. Here, too, the price decline has moderated in recent months.

Labour market conditions are weighing on the framework conditions for a sustained economic recovery. The seasonally adjusted unemployment rate has been rising steadily in the euro area since April 2008, reaching 9.5 percent in July 2009. A very strong increase was registered in Ireland (from 4.6 percent in February to 12.5 percent). In Spain, unemployment has been rising already since May 2007 (from 7.9 percent to 18.5 percent in July 2009). In these countries, the sharp drop in real estate values has caused a marked decline in construction production. Continued high levels of unemployment, apart from their negative impact on private consumption and the threat they pose to a self-supporting upturn, also lower the medium-term growth path of economies through loss of human capital.

Production decline halted in Germany

Stabilising global activity is providing support notably to the export-oriented German economy. Having declined for four quarters, real GDP expanded by 0.3 percent quarter-on-quarter in the second quarter of 2009; it still remained 7.1 percent below its year-earlier level, though. Private and public consumption, along with net exports, also stabilised economic activity. In the first half of 2009, car sales rose by 23 percent compared with the previous year. As a result, private consumption in the first six months marginally exceeded the year-earlier level by 0.1 percent. Without the car purchases, private consumption would have declined by 1.0 percent, according to the German Federal Statistical Office.

Industrial production began to stabilise already in May 2009 (in month-on-month terms). A further rebound is expected for the second half of 2009 – in the August Ifo Business Survey, industrial firms for the second consecutive time assessed their current business situation clearly less negatively. The Ifo Business Climate Index, which in addition to the manufacturing sector also comprises the construction industry and the wholesale and retail trade, rose for the fifth time in a row and in August again returned close to its autumn 2008 level.

Austria: Slump in exports and industrial production moderating

After declining at a seasonally and working day adjusted quarterly rate of only 0.5 percent in real terms in the second quarter of 2009, economic activity in Austria is expected to stabilise further in the second half of the year. Following four consecutive quarters of quarter-on-quarter decline, real GDP now stands 4.6 percent below its year-earlier level.

The pace of contraction slowed also in Austria in the second quarter of 2009. Leading indicators point to a further rebound in industrial activity in the third quarter.

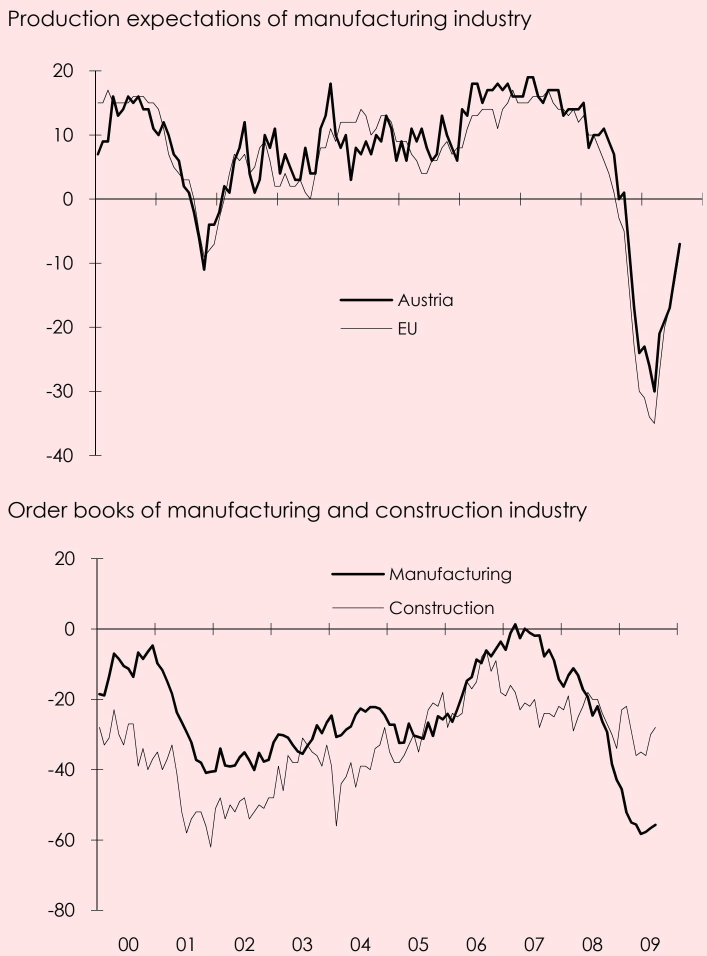
The seasonally adjusted decline in manufacturing value added observed since the third quarter of 2008 eased in the second quarter (–2.2 percent); it may thus have bottomed out already. According to WIFO's latest business cycle survey, the proportion of firms having reduced production in recent months has fallen considerably. The assessment of the business situation has improved further, and production expectations have risen for the fifth consecutive time. More optimistic expectations, in tandem with a more positive assessment of the current situation may signal a cyclical turning-point. A particularly strong improvement was registered in firms' expectations regarding the business situation over the next six months.

Foreign trade, which had set off the contraction with its decline, should quickly recover in the course of an international stabilisation. The downward trend of exports weakened considerably already in the second quarter (first quarter –7.4 percent, second quarter –2.3 percent). Imports fell at a slower pace (–1.5 percent) than exports; consequently, the contribution from net exports was negative and depressed GDP.

In the first five months of 2009, 30.9 percent of exports went to Germany, and 8.5 percent to Italy, according to Austria's foreign trade statistics. 16 percent of Austrian goods were exported to CEE-10 countries. In the first half of 2009, nominal exports were down by 24.5 compared with a year earlier, while imports fell by 21.2 percent.

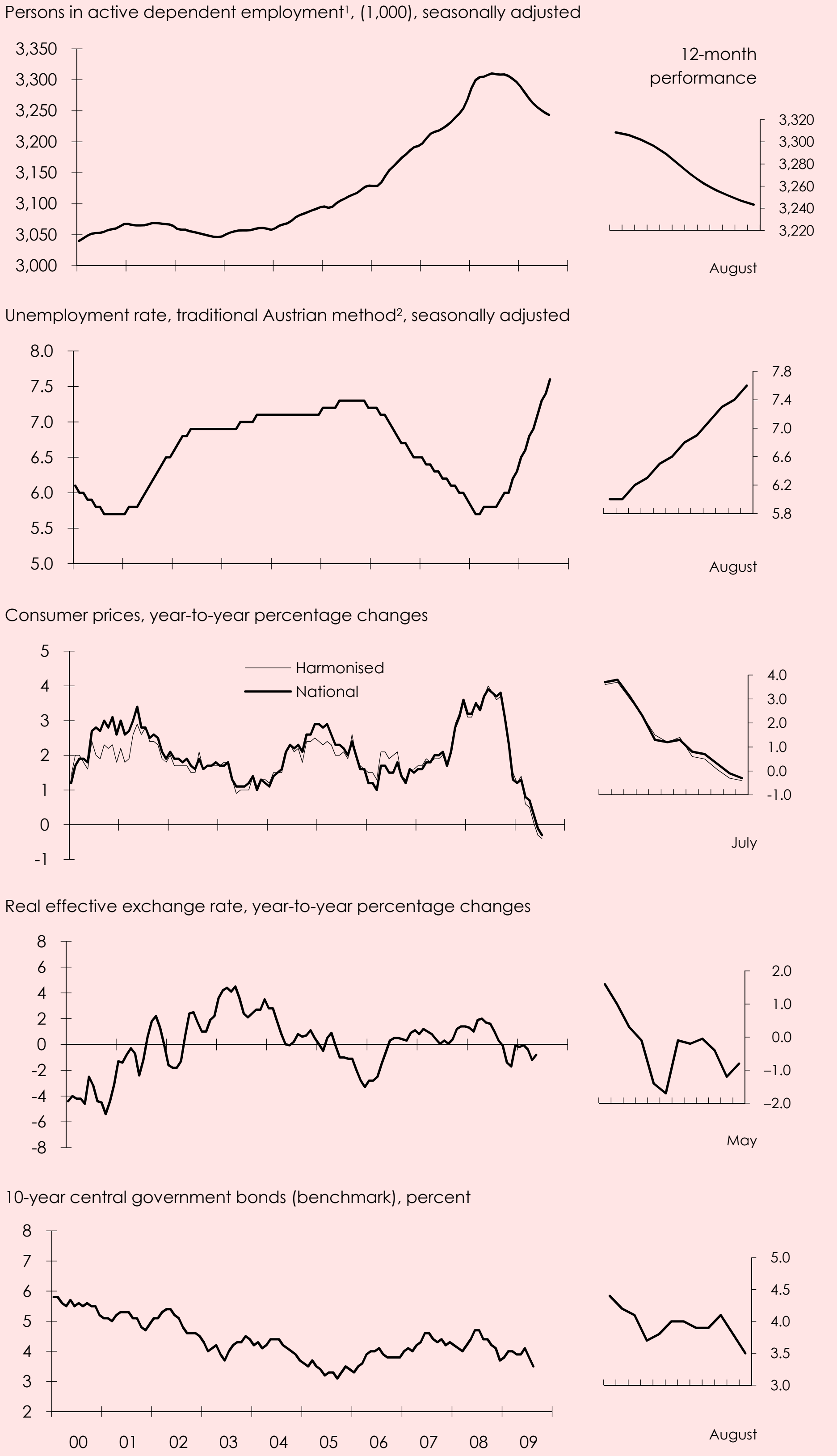
Figure 3: WIFO business cycle survey

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



Source: European Commission, WIFO business cycle survey.

Figure 4: Key economic indicators



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.

Construction value added declining at slower pace

The impact of the crisis is clearly visible in the construction sector: Value added has been declining since the second quarter of 2008. Meanwhile, some stabilisation has been observed here too, with the downward trend slowing in the second quarter of 2009 (–1.2 percent compared with the previous quarter, after –1.7 percent). The recovery is expected to continue in the third quarter of 2009. According to WIFO's latest business cycle survey, firms' assessment of order books has improved for the second time in a row, and expectations regarding employment developments have also become more upbeat.

Trade and consumption supported by tax reform and car-scrapping premium

With the effects of the car-scrapping premium and the tax reform supporting private consumption in the second quarter of 2009, the latter expanded by 2.1 percent year-on-year (+0.4 percent quarter-on-quarter) after a sharp fall in the first quarter of 2009. As a result of these special effects, growth was even higher than on average in the past business cycle.

These effects were also noticeable in the retail sector, where year-on-year nominal sales increases averaged 0.6 percent in the first six months of the year. Developments stabilised in the months from April to June after sales declines in the first quarter.

While retailers and motor vehicle traders benefited from economic stimulus measures, wholesalers registered a marked decline in sales in the second quarter of 2009.

In the wholesale sector, which generally reacts more strongly to cyclical fluctuations, no such special effects of economic policy measures became apparent. With industrial activity decreasing sharply, business slumped already at the end of 2008, and the decline in sales accelerated further until the second quarter. In the first half of 2009, sales were on average 12 percent below year-earlier levels.

Motor vehicle traders saw sales decline by 9.4 percent in the first six months of 2009; developments during the year were influenced considerably by the introduction of the car-scrapping premium in April. The repercussions of the economic crisis were also clearly visible in sales volumes recorded by the services sectors (first six months –5.4 percent year-on-year). Notably the sectors "Transport and Storage" were affected by the weak industrial and export activity.

Global economic crisis harms tourism

Tourism sales dropped by 5.3 percent in the first half of the 2009 summer season, compared with the same period in the previous year. The decline in the number of overnight stays was of a similar magnitude (–5.2 percent). Although the year-on-year comparison is partly distorted by weather-related factors, it nevertheless clearly reflects the impact of the financial and economic crisis on Austria's tourism industry. Foreign demand fell at an extremely rapid pace (overnight stays May to July 2009 –7.3 percent year-on-year), whereas bookings by domestic travellers contributed modestly to a stabilisation of the overall result (overnight stays May to July 2009 –0.6 percent).

In the 15 major foreign markets of origin, the demand for stays in Austria receded by 6.6 percent overall in the first half of the 2009 summer season. Demand developments differed greatly across countries, however: Only the number of overnight stays by guests from the Czech Republic was markedly higher than in the previous year (+11.4 percent), while overnight stays by guests from Switzerland also increased somewhat (+2.3 percent). The demand from Belgium receded only marginally (–0.6 percent), whereas the number of nights spent by German guests fell noticeably (–3.9 percent). A sharp decline was recorded in the markets of origin USA (–7.7 percent), Hungary (–14.2 percent), the Netherlands (–16.5 percent), Great Britain (–22.3 percent) and Russia (–44.1 percent). In the case of Great Britain and the USA, the strong euro also played a role.

Inflation rate negative due to base effects

Inflation in Austria has been easing steadily for a year now, and in June and July was in negative territory (–0.1 percent, –0.3 percent). The price decline was driven largely by the fall in prices of fuels and heating oil compared with a year earlier (inflation excluding energy 1.3 percent in July). Unprocessed food prices were also lower than a year ago. Industrial goods prices, however, while being regarded as relatively cyclically sensitive, react only with some lag to changes in demand.

The wholesale price index is much quicker and more volatile than the consumer price index as far as reflecting cyclical fluctuations is concerned. In August 2009, it was 8.6 percent below its year-earlier level.

Inflation in Austria has been driven largely by commodity price developments, and notably by movements in crude oil prices. Following the boom in the summer of 2008 (oil price peaking at $ 140 per barrel) and the subsequent decline to $ 43.1 per barrel in February, crude oil prices once more began to rise moderately in March 2009. In August, one barrel of Brent crude traded at $ 72 per barrel. The price increase is driven by current developments of supply and demand, but also by internationally improved economic expectations and the weak dollar.

Inflation was negative in June and July 2008, owing to the fall in the price of crude oil from its peak in the summer of 2008. This effect will disappear from the year-on-year comparison in the months to come.

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".

The setback in economic activity continues to affect the labour market. In August, 238,800 persons were registered as unemployed, an increase by 54,900 (+29.8 percent) compared with a year before. 57,700 persons were enrolled in vocational training programmes. As in the preceding months, unemployment rose vigorously notably in the cyclically sensitive sectors of manufacturing and construction, despite an expansion of short-time-working schemes. Moreover, those particularly affected are temporary workers and young people, who have not yet gained a foothold in the job market.

Undiminished rise in unemployment

The labour market shows no signs of stabilising, unemployment continues to rise. The cyclically sensitive sectors of manufacturing and construction are particularly affected.

The number of persons registered as unemployed rose at an undiminished pace also on a month-on-month basis (+2 percent, seasonally adjusted). Hence, no easing is yet in sight in the labour market. The number of job vacancies, which is considered a leading indicator, continues to fall.

The seasonally adjusted unemployment rate according to the Austrian definition stood at 7.6 percent in August (July 7.4 percent). According to the definition by Eurostat, the rate was 4.4 percent in July.