

Christian Glocker

# Continued Strong Economic Activity Since the Beginning of the Year

## Business Cycle Report of June 2018

### Continued Strong Economic Activity Since the Beginning of the Year. Business Cycle Report of June 2018

Austrian GDP grew by 0.8 percent in the first quarter of 2018 compared with the previous period, after +0.9 percent in the third and fourth quarter 2017. As a result, the economic momentum continued from the previous year and the boom phase continues. The positive development of the real economy is also reflected in the labour market in an increase in employment and a decline in unemployment. Inflation is currently still unusually restrained.

#### Contact:

**Christian Glocker, MSc:** WIFO, 1030 Vienna, Arsenal, Objekt 20, [christian.glocker@wifo.ac.at](mailto:christian.glocker@wifo.ac.at)

**JEL-Codes:** E32, E66 • **Keywords:** Business Cycle Report

All staff members of the Austrian Institute of Economic Research contribute to the Business Cycle Report. For definitions used see "Methodological Notes and Short Glossary", <https://www.wifo.ac.at/wwadocs/form/WIFO-BusinessCycleInformation-Glossary.pdf> • Cut-off date: 11 June 2018.

**Data processing:** Astrid Czaloun ([astrid.czaloun@wifo.ac.at](mailto:astrid.czaloun@wifo.ac.at)), Christine Kaufmann ([christine.kaufmann@wifo.ac.at](mailto:christine.kaufmann@wifo.ac.at)), Maria Riegler ([maria.riegler@wifo.ac.at](mailto:maria.riegler@wifo.ac.at)), Martha Steiner ([martha.steiner@wifo.ac.at](mailto:martha.steiner@wifo.ac.at))

ISSN 1605-4709 • © Austrian Institute of Economic Research 2018  
Impressum: Herausgeber: Christoph Badelt • Chefredakteur: Michael Böheim ([michael.boeheim@wifo.ac.at](mailto:michael.boeheim@wifo.ac.at)) • Redaktionsteam: Tamara Fellingner, Ilse Schulz, Tatjana Weber • Medieninhaber (Verleger) und Redaktion: Österreichisches Institut für Wirtschaftsforschung • 1030 Wien, Arsenal, Objekt 20 • Tel. (+43 1) 798 26 01-0 • Fax (+43 1) 798 93 86 • <http://bulletin.wifo.ac.at> • Verlags- und Herstellungsort: Wien

Global economic growth is likely to have eased slightly in the first quarter of 2018, but this was due in part to special effects. The forces behind the global upturn remain intact. The good global economic momentum is also reflected in an increase in commodity prices. The image of the leading indicators is still indicative of a favourable further trend in the global economy. Risk factors are uncertainties regarding economic-induced disruptions to global trade flows and geopolitical tensions.

In Austria, the boom phase continues. In the first quarter of 2018, economic output expanded again sharply and thus took the momentum from the previous year. Domestic growth was driven by both domestic demand and foreign trade. The image of the lead indicators has been slightly gloomy in the last few months. Overall, these continue to provide a positive outlook. Renewed acceleration will not become apparent for the coming quarters.

Growth is widely distributed in Austria. Among the components of the domestic economy, the consumption of private households in the first quarter of 2018 proves to be the mainstay of growth. The ongoing improvement in the labour market and a very optimistic consumer sentiment are reflected in the willingness of households to spend. In addition, investments at the beginning of the year once again picked up strongly. The economy also receives additional impetus from foreign trade; however, exports grew somewhat more weakly in the first quarter of 2018 than in the fourth quarter of 2017.

The rate of inflation (CPI) decreased by 0.1 percentage point to 1.8 percent in April (HICP +1.9 percent). The costs of housing, water, energy as well as restaurants and

hotels were the main contributors to the rise in prices. The inflation differential to the euro area average has recently remained constant.

The Austrian labour market is also showing a positive trend. According to preliminary estimates, the number of persons in active dependent employment in May was 98,000 higher than in the previous year (+2.8 percent). The seasonally-adjusted unemployment rate (national definition) remained at 7.7 percent in May.

## 1. Upswing in the global economy intact despite the slump in the first quarter

Global economic growth is likely to have been comparatively low at the beginning of the year. Nevertheless, the forces behind the global recovery are still intact. Especially in the EU countries, the economy expanded more weakly in the first quarter of 2018 following the strong growth rates of the previous year. In Japan, preliminary estimates for the first quarter of 2018 even showed a decline compared to the previous quarter. The picture of the leading indicators is still very positive in Japan, so that an expansion should be expected again in the second quarter, or the provisional estimate for the first quarter could be revised up noticeably. This seems very likely against the backdrop of the traditionally very extensive revisions of Japanese national accounts data.

In the group of emerging economies, China continued its high rate of growth by international comparison. So far only data for the first quarter are available for some emerging economies (Brazil +0.4 percent, Mexico +1.1 percent, Thailand +2 percent, India +1.9 percent); these, like the leading indicators, indicate a generally sustained stable expansion.

Overall, the leading indicators for 2018 suggest continued strong growth in the global economy. The Global Purchasing Managers' Index remains at a high level. The Global Composite PMI<sup>1</sup> climbed from 53.8 points in April to 54.0 points in May after a slump in March (figures above 50 points point to an expansion). The Index correctly announced an expansion in each of the last 67 months. The high value of the indicator in May indicates a continuation of the recovery in the manufacturing and services sectors. The sub-indicators show the sectoral breadth of the expected expansion.

### 1.1 Robust growth in the USA

While the US economy did not fully sustain the momentum of recent quarters in early 2018, the overall outlook remains bright. Seasonally-adjusted real GDP grew by 0.5 percent in the first quarter of 2018 compared to the previous quarter. Growth in private consumer expenditure slowed more sharply. After the entry into force of tax relief for private households in January, however, the conditions for private consumption are still favourable, given that labour market development continues to be very good. Already in the second quarter, a significant acceleration is expected. In addition, the strong fiscal expansion and robust foreign demand should support future macroeconomic growth.

The unemployment rate was 3.8 percent in May. The increase in wages is now strengthening, which has already been reflected in increased inflation in recent months: the CPI rose 2.5 percent in April compared to the same month last year, while core inflation accelerated to 2.1 percent.

### 1.2 EU and euro area: upswing intact despite slump

In the euro area, GDP increased by 0.4 percent in the first quarter of 2018, according to first estimates, compared to the previous quarter. Growth was therefore moderate after having been 0.7 percent in the fourth quarter of 2017. Compared to the previous year, this represents an increase of 2.5 percent after +2.8 percent in the fourth quarter of 2017. In line with the trend in the euro area, growth in the EU as a whole slowed

*The decline in growth in the global economy in the first quarter mainly affected European countries and Japan.*

*In the USA, the unemployment rate fell to its lowest level since 2000. The robust economic boom is expected to continue in the coming months.*

<sup>1</sup> This indicator is prepared by J.P. Morgan and IHS Markit in collaboration with the Institute for Supply Management (ISM) and the International Federation of Purchasing and Supply Management (IFPSM).

slightly at the beginning of the year. In the individual member countries, the real economy developed in a noticeably more heterogeneous way than in 2017.

Figure 1: International business climate

Seasonally adjusted, 2015 = 100, 3-month moving average



Source: European Commission, Deutsche Bundesbank, ISM (Institute for Supply Management™), ifo (Institute for Economic Research, Munich), OECD. – <sup>1</sup> Excluding construction.

In Germany, macroeconomic activity expanded significantly less at the beginning of 2018 following the very high growth in the previous year. Real gross domestic product rose by 0.3 percent on a seasonally- and calendar-adjusted quarter-on-quarter basis. However, attenuation was largely due to irregular phenomena such as the exceptionally high number of days off sick and strike days. Both should have affected economic performance, but only in the short term. Similarly, real GDP in France rose much more slowly in the first quarter (seasonally adjusted +0.2 percent, fourth quarter of 2017 +0.7 percent compared to the previous period). In the UK, seasonally-adjusted real GDP rose only 0.1 percent in the first quarter; in the second half of 2017, the economy grew even more strongly. In Italy, growth did not gain momentum in the first quarter of 2018, and economic output increased by 0.3 percent. Among the major EU countries, only Spain (+0.7 percent) and Poland (+1.6 percent) continued to show high growth rates.

Despite the slump in growth, the situation in the euro area employment market improved again in the first quarter. Thus, the number of unemployed continued to decline. The unemployment rate was recently 8.5 percent (April). Reflecting the decline in unemployment, employment growth continued.

### 1.3 Volatility on the stock markets is increasing significantly again

As already at the end of February, the development on the stock markets is again worrying: the volatility of stock prices has increased significantly in recent months. The implied volatility index of the Euro Stoxx 50 rose to more than 20 points at the end of May. Although this uncertainty indicator was still below the level of February 2018, the frequency of short-term jumps in volatility appears to be increasing. In the current environment, this is probably shaped by political uncertainties; these are the result of difficulties in forming a government in Italy, politically-induced disruptions in global trade flows, and geopolitical uncertainties. Experience has shown that price corrections on the financial markets are possible at any time due to changed assessments, and even a collapse on the stock markets with consequences for the real economy, such as in the years 2000 to 2002, cannot be ruled out.

*After price losses at the beginning of February 2018, volatility on the stock markets receded noticeably; in May it rose again in the short term, driven by increasing economic uncertainties.*

## 2. Austria: strong growth at the beginning of the year

According to the latest quarterly national accounts of WIFO, GDP in Austria increased by 0.8 percent in the first quarter of 2018 compared to the previous quarter (fourth quarter of 2017 +0.9 percent). Unadjusted GDP was 3.4 percent above the level of the previous year. Compared to the flash estimate, the current calculation shows a slight upward revision (0.3 percentage points compared to the previous year). The strong momentum of the previous year was thus retained in the first quarter of 2018. Growth was driven by both domestic demand and foreign trade. Among the components of the domestic economy, private consumption expenditure continued to be a driver of growth in the first quarter of 2018. The ongoing improvement in the labour market and the very optimistic consumer sentiment are reflected in the high propensity of households to spend. Private consumption expenditure (including non-profit institutions serving households) expanded by 0.4 percent and general government consumption expenditure by 0.3 percent.

Gross fixed capital formation expanded significantly once again in the first quarter of 2018 at 0.9 percent. However, the momentum in machinery and equipment investment eased somewhat (+1.4 percent after +1.9 percent in the fourth quarter of 2017). Growing momentum, however, continued to come from construction investments (+0.7 percent after +0.5 percent in the fourth quarter of 2017).

In the first quarter of 2018, foreign trade had somewhat weaker impulses. Exports again strongly increased at 0.9 percent compared to the previous quarter, but expansion was weaker than in last year's quarters.

*The Austrian economy also grew vigorously in the first quarter of 2018. The expansion was driven by a buoyant domestic economy and foreign trade.*

## 2.1 Leading indicators stabilise

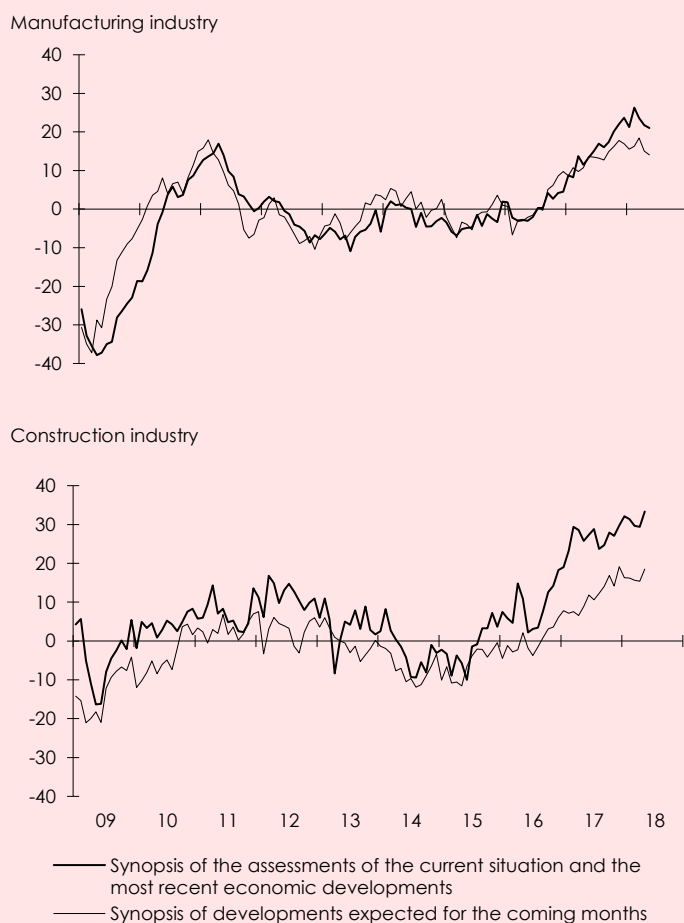
The results of the WIFO-Konjunkturtest (business cycle survey) show a stabilisation of the still very good economic assessment by Austrian companies in May 2018. The current situation has been somewhat better assessed, while the economic expectations remain optimistic.

The index of the current assessments for the overall economy in May (seasonally adjusted), with 23.3 points, was 1.8 points above the value of the previous month.

*The image of the leading indicators has been slightly gloomy in the last few months, but overall, they continue to provide a positive outlook.*

Figure 2: Results from the WIFO-Konjunkturtest

Indices of the assessment of the current economic situation and of business expectations, seasonally adjusted



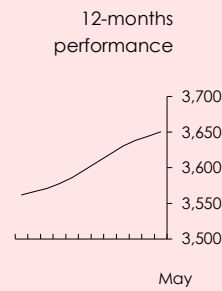
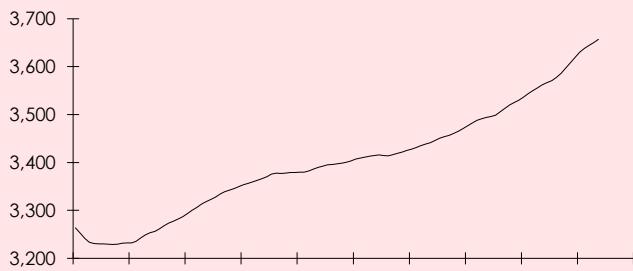
Source: WIFO-Konjunkturtest. Data refer to index points (percentage points) between +100 and -100. Values above 0 imply positive expectations, values below 0 indicate negative expectations.

In contrast, the index of business expectations decreased slightly (-0.6 points) to 16.0 points. As there was improvement in the construction industry, the indices decreased in most of the manufacturing subsectors that are important for the economy. Overall, the index of business expectations signals a further normalisation of economic momentum in the coming months.

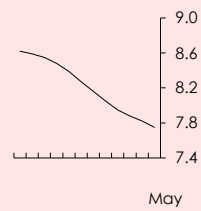
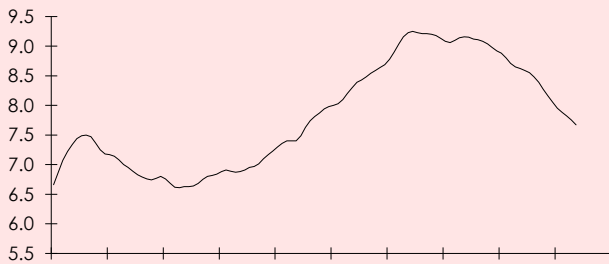
The UniCredit Bank Austria Purchasing Managers' Index shows a similar picture: the decline in the first months of 2018 continued in May. The index has reached the level of spring 2017 after the maximum value of the end of 2017. With a value of 57.3 points, it indicates a continued strong upward trend in the domestic industry. Austrian industry will continue to expand production volumes in the coming months, albeit with slightly flatter rates, primarily because of the slowdown in foreign orders.

Figure 3: Key economic indicators

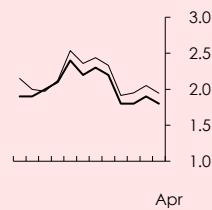
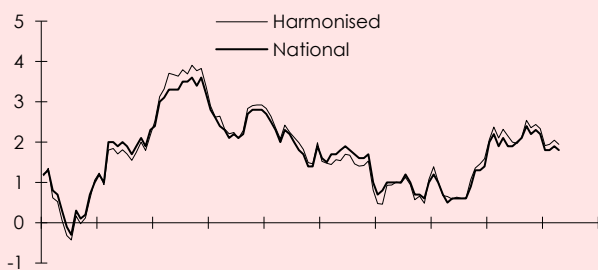
Persons in active dependent employment<sup>1</sup>, 1,000s, seasonally adjusted



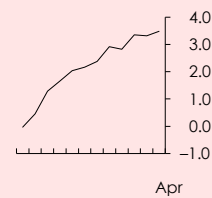
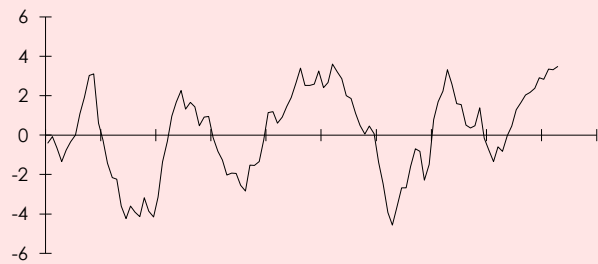
Unemployment rate, traditional Austrian method<sup>2</sup>, seasonally adjusted



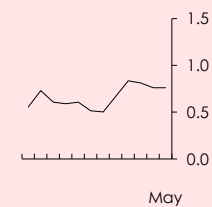
Consumer prices, year-to-year percentage changes



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



10-year central government bonds (benchmark), percent



Source: Public Employment Service Austria, Main Association of Austrian Social Security Institutions, Oesterreichische Nationalbank, Statistics Austria, WIFO calculations. – <sup>1</sup> Excluding persons in valid employment contract receiving child care benefit or being in military service. – <sup>2</sup> As a percentage of total labour force excluding self-employed, according to Public Employment Service.

## 2.2 Declining credit hurdles and favourable financing environment characterise credit growth

In line with the high growth rates of private household consumption, consumer credit increased (2017 +2.5 percent, April 2018 +1.5 percent compared to the previous year, adjusted for depreciation, exchange rate changes, credit transfers, or reclassifications). Residential loans were also expanded (2017 +4.7 percent, April 2018 +4.6 percent, adjusted for depreciation, exchange rate changes, credit transfers, or reclassifications). This is also reflected in the development of real estate prices: residential real estate prices increased by 3.8 percent compared to the previous year, but by 7.3 percent in the first quarter of 2018.

Credit financing also developed very dynamically in the corporate sector. Loans to non-financial companies increased by 4.9 percent in 2017 compared to the previous year and rose by 6.2 percent in April 2018. According to the recent evaluation of credit conditions for domestic companies, this trend is likely to continue. In May, companies again reported an improvement in credit conditions. The credit hurdle<sup>2</sup> recently decreased further. Thus, the trend for a positive assessment of banks' lending practices continued.

Despite the strong increase in lending, the number of companies with credit requirements is still moderately high. As in winter, also in May, 19 percent of companies surveyed reported that they had to borrow in the previous three months, less than on average in 2017 (21 percent). Of the companies with credit needs, around 18 percent had to cut back on their expectations in terms or amount. This value corresponded to the average of past years (18 percent).

## 2.3 Inflation recently slightly flattened

In April, consumer prices rose 1.8 percent year-on-year, slightly lower than in March (+1.9 percent). Decisive for this were price reductions in airline tickets and weaker price increases in cigarettes. Spending on housing, water and energy averaged 2.0 percent year-on-year, impacting overall inflation at +0.39 percentage points. The most important price drivers within this group were rentals for housing. Household energy prices increased moderately, as the rise in heating oil and solid fuel prices was partially offset by the decline in gas prices. In the transport sector, prices rose by an average of 1.3 percent. Spending on fuel increased by 3.3 percent, significantly higher than in March 2018. In the coming months, the inflation rate should increase noticeably, above all because of the significant increase in crude oil prices.

## 2.4 Increasing recovery in the labour market

Strong economic growth continues to foster development in the domestic labour market. According to preliminary estimates, the number of persons in active dependent employment in May was 98,000 higher than in the previous year (+2.8 percent). Seasonally adjusted, the increase over the previous month was 8,500 (+0.2 percent). The expansion of employment thus continues. In the manufacturing and construction sectors in particular, additional workers were hired in April<sup>3</sup>.

The number of unemployed registered with the Public Employment Service Austria (AMS) in May was 31,900 lower than in the previous year (-10.0 percent), and 35,000 (-8.9 percent) lower when including people undergoing training. Seasonally adjusted, the number of unemployed decreased by 0.9 percent compared to the previous month. According to the national definition, the seasonally-adjusted unemployment rate remained at 7.7 percent in May. The year-on-year decline was 0.9 percentage points.

*The favourable financing environment favours credit growth. In addition to a significant increase in residential loans, corporate loans also attracted strong growth. This development is expected to increase in the coming months, mainly due to further declining credit hurdles.*

*The rise in prices in housing, water, energy as well as in the restaurant and hotel sectors has shaped inflation momentum and overall has contributed around 40 percent to the rise in consumer prices.*

*Domestic companies are significantly expanding employment also in May. That is increasingly benefitting the long-term unemployed too.*

<sup>2</sup> The credit hurdle is defined as the balance between the proportion of companies that perceive bank lending to be accommodative (positive values) and the proportion of companies that describe bank lending as restrictive (negative values).

<sup>3</sup> For May 2018, there is no industrial sector information yet available persons in active dependent employment.