

WIFO

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WIRTSCHAFTSFORSCHUNG**

**Business Cycle Upturn Interrupted
Economic Outlook for 2011 and 2012**

September 2011



Business Cycle Upturn Interrupted Economic Outlook for 2011 and 2012

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Austrian Institute of Economic Research

Abstract

Since the middle of 2011, the international economic environment has deteriorated markedly. In view of rising uncertainty about how to resolve the sovereign debt crisis, investment decisions are being deferred. After a strong expansion by 2.9 percent in 2011, the Austrian economy will grow by a modest 0.8 percent in 2012.

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Business Cycle Upturn Interrupted

Economic Outlook for 2011 and 2012

Since the middle of 2011, the international economic environment has deteriorated markedly. In view of rising uncertainty about how to resolve the sovereign debt crisis, investment decisions are being deferred. After a strong expansion by 2.9 percent in 2011, the Austrian economy will grow by a modest 0.8 percent in 2012.

The recovery of the Austrian economy from the recession of 2008-09 has been lively also in the current year. Overall demand and output grew strongly until mid-year, reaching their pre-crisis levels. For some time, however, business surveys in Austria and abroad point to an imminent deceleration of the growth momentum.

Moreover, since mid-2011, uncertainty among economic agents has mounted sharply, and policy has not been able to dissipate doubts about some countries' ability to service their debt. As a result, interest rates for new issues of government debt drifted up in the countries concerned, thereby adding to the fiscal imbalances. The loss of confidence triggered sharp falls on stock markets especially concentrated on bank titles. Within two months, major European banks lost around half of their stock market value.

The present WIFO forecast for Austria reflects these latest developments only to the extent that they reduce the appetite for corporate investment. For 2011, GDP growth is expected at 2.9 percent, slowing down to 0.8 percent in 2012. Explicitly, no unilateral government default of Greece or any other euro area country is assumed. The forecast takes as given that the euro area continues to exist in its current composition, that interest rates on government debt of euro area countries will not increase substantially further and that stock market values suffer no further significant fall.

Under these assumptions, domestic economic activity will remain broadly flat around the turn of the year, in line with the overall cyclical profile for the EU. A temporary decline of real GDP in one quarter cannot be excluded. According to the

conventional business cycle pattern, economic growth should gradually rebound in the course of 2012.

Labour market developments have been positive so far in 2011. Employment gains continued until August. While the seasonally-adjusted unemployment rate has been heading up for several months, this is partly due to major cuts in government-sponsored job training programmes. The number of persons in dependent active employment, after a projected increase by 1.8 percent in 2011, will likely gain a modest 0.4 percent in 2012, taking the unemployment rate from 6.7 percent to 7.0 percent.

The marked upward drift of consumer prices since the beginning of this year will abate over the next months. Oil prices have been falling for several months which in due course will show up also in the annual increase in the overall price level. Headline inflation is projected at 3.1 percent for 2011, followed by 2.1 percent in 2012.

If the cyclical slowdown does not prove significantly stronger than projected in the present context, a departure from the course of fiscal consolidation would not be necessary. Slower GDP growth will weigh on both public revenue and expenditure. While the structural budget deficit should be reduced as planned, automatic cyclical stabilisers should not be prevented from operating.

Vienna, 28 September 2011

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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, reference is made to "seasonally and working day adjusted changes".

The phrase "changed compared with a year before . . .", on the other hand, describes a 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.

Production Sector

This term comprises the NACE-2008 sections B, C and D (Mining and Quarrying, Manufacturing, Energy Supply) and is here used in an international comparison.

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 (see <http://www.statistik.at/>).

Core inflation as a monetary policy indicator is not clearly defined. WIFO follows the common practice of using the inflation rate excluding the product categories unprocessed food and energy for core inflation. Thus just under 87 percent of the goods and services contained in the consumer price index (CPI 2010) are included in the calculation of core inflation.

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".

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Projections - September 2011

Main results

Percentage changes from previous year

		2007	2008	2009	2010	2011	2012
GDP							
Volume		+ 3.7	+ 1.4	- 3.8	+ 2.3	+ 2.9	+ 0.8
Value		+ 5.8	+ 3.2	- 2.8	+ 4.1	+ 4.9	+ 2.9
Manufacturing¹, volume		+ 8.1	+ 1.3	- 15.0	+ 7.2	+ 8.0	+ 1.0
Wholesale and retail trade, volume		+ 1.9	- 3.0	+ 0.7	+ 3.1	+ 0.9	+ 0.4
Private consumption expenditure, volume		+ 0.9	+ 0.8	- 0.3	+ 2.2	+ 0.9	+ 0.8
Gross fixed investment, volume		+ 3.6	+ 0.7	- 8.3	+ 0.1	+ 4.0	+ 1.1
Machinery and equipment		+ 6.6	- 0.7	- 9.7	+ 4.3	+ 8.0	+ 1.5
Construction		+ 1.8	+ 1.0	- 7.6	- 2.9	+ 0.7	+ 0.7
Exports of goods²							
Volume		+ 9.0	+ 0.5	- 16.8	+ 12.8	+ 8.5	+ 4.5
Value		+ 10.5	+ 2.5	- 20.2	+ 16.7	+ 11.5	+ 4.5
Imports of goods²							
Volume		+ 7.6	+ 0.6	- 14.3	+ 10.3	+ 7.0	+ 4.5
Value		+ 9.6	+ 4.7	- 18.4	+ 16.5	+ 11.5	+ 4.0
Current balance	€ bn	+ 9.62	+ 13.76	+ 8.53	+ 7.76	+ 8.27	+ 8.54
	as a percentage of GDP	+ 3.5	+ 4.9	+ 3.1	+ 2.7	+ 2.8	+ 2.8
Long-term interest rate³	percent	4.3	4.4	3.9	3.2	3.3	3.2
Consumer prices		+ 2.2	+ 3.2	+ 0.5	+ 1.9	+ 3.1	+ 2.1
Unemployment rate							
Eurostat definition ⁴	percent	4.4	3.8	4.8	4.4	4.2	4.4
National definition ⁵	percent	6.2	5.9	7.2	6.9	6.7	7.0
Persons in active dependent employment⁶		+ 2.1	+ 1.7	- 1.5	+ 0.8	+ 1.8	+ 0.4
General government financial balance							
according to Maastricht definition							
as a percentage of GDP		- 0.9	- 0.9	- 4.1	- 4.6	- 3.1	- 3.1

¹ Value added, including mining and quarrying. ² According to Statistics Austria. ³ 10-year central government bonds (benchmark). ⁴ According to Eurostat Labour Force Survey. ⁵ Public Employment Service Austria, percent of total labour force excluding self employed. ⁶ Excluding parental leave and military service.

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Projections - September 2011

Key policy indicators

	2007	2008	2009	2010	2011	2012
Fiscal policy						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 0.9	- 0.9	- 4.1	- 4.6	- 3.1	- 3.1
according to National accounts	- 1.0	- 1.0	- 4.1	- 4.6	- 3.1	- 3.1
General government primary balance						
	+ 1.9	+ 1.7	- 1.3	- 1.9	- 0.6	- 0.5
Monetary policy						
	Percent					
3-month interest rate	4.3	4.6	1.2	0.8	1.4	1.5
Long-term interest rate ¹	4.3	4.4	3.9	3.2	3.3	3.2
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 1.1	+ 1.2	+ 0.9	- 2.5	+ 0.6	+ 0.9
Real	+ 0.7	+ 0.6	+ 0.4	- 2.7	+ 1.2	+ 0.9

¹ 10-year central government bonds (benchmark).

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World economy

Percentage changes from previous year

	2007	2008	2009	2010	2011	2012
Real GDP						
World	+ 5.4	+ 2.8	- 0.7	+ 5.1	+ 3.8	+ 3.1
USA	+ 1.9	- 0.3	- 3.5	+ 3.0	+ 1.8	+ 1.0
Japan	+ 2.4	- 1.2	- 6.3	+ 4.0	- 0.5	+ 1.5
EU 27	+ 3.1	+ 0.5	- 4.3	+ 1.8	+ 1.7	+ 0.7
Euro area 16	+ 3.0	+ 0.4	- 4.3	+ 1.8	+ 1.6	+ 0.5
Germany	+ 3.3	+ 1.1	- 5.1	+ 3.7	+ 2.9	+ 0.7
New member states ¹	+ 5.9	+ 4.1	- 3.2	+ 2.2	+ 3.0	+ 1.8
China	+ 14.2	+ 9.6	+ 9.2	+ 10.4	+ 9.5	+ 8.5
World trade , volume	+ 7.0	+ 2.5	- 12.7	+ 15.3	+ 6.0	+ 5.0
Market growth ²	+ 7.5	+ 2.9	- 11.5	+ 11.5	+ 8.0	+ 4.0
Primary commodity prices						
HWI Index, total	+ 12.4	+ 31.7	- 34.4	+ 29.0	+ 35	- 6
Excluding energy	+ 17.8	+ 18.3	- 28.0	+ 31.5	+ 25	+ 5
Crude oil prices						
Brent, USD per barrel	72.5	97.0	61.5	79.5	110	100
Exchange rate						
USD per euro	1.371	1.471	1.393	1.327	1.40	1.40

¹ Bulgaria, Czech Republic, Hungary, Latvia, Lithuania, Poland, Romania.

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

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Private consumption, income and prices

	2007	2008	2009	2010	2011	2012
Percentage changes from previous year, volume						
Private consumption expenditure	+ 0.9	+ 0.8	- 0.3	+ 2.2	+ 0.9	+ 0.8
Durables	+ 2.5	+ 4.7	+ 0.9	+ 5.8	+ 1.0	- 0.3
Non-durables and services	+ 0.7	+ 0.4	- 0.4	+ 1.8	+ 0.9	+ 0.9
Household disposable income	+ 2.5	+ 1.3	- 1.3	- 1.4	+ 0.4	+ 0.6
As a percentage of disposable income						
Household saving ratio¹	11.6	11.8	11.1	9.1	8.7	8.5
Household saving ratio²	11.2	11.6	10.4	8.7	8.3	8.1
Percentage changes from previous year						
Direct lending to domestic non-banks³	+ 3.6	+ 7.4	- 1.3	+ 2.9	+ 4.0	+ 3.5
Inflation rate						
National	2.2	3.2	0.5	1.9	3.1	2.1
Harmonised	2.2	3.2	0.4	1.7	3.5	2.3
Core inflation ⁴	1.9	2.4	1.5	1.2	2.7	2.1

¹ Including adjustment for the change in net equity of households in pension fund reserves.

² Excluding adjustment for the change in net equity of households in pension fund reserves.

³ End of period.

⁴ Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

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Projections - September 2011

Productivity

Percentage changes from previous year

	2007	2008	2009	2010	2011	2012
Total economy						
Real GDP	+ 3.7	+ 1.4	- 3.8	+ 2.3	+ 2.9	+ 0.8
Employment ¹	+ 1.9	+ 2.1	- 0.9	+ 0.8	+ 1.7	+ 0.4
Productivity (GDP per employment)	+ 1.8	- 0.7	- 2.9	+ 1.5	+ 1.1	+ 0.4
Manufacturing						
Production ²	+ 8.3	+ 0.9	- 15.3	+ 7.4	+ 8.0	+ 1.0
Employees ³	+ 2.6	+ 1.7	- 5.3	- 1.3	+ 1.8	- 1.2
Productivity per hour	+ 5.9	- 0.3	- 7.3	+ 5.5	+ 5.0	+ 2.8
Working hours per day per employee ⁴	- 0.3	- 0.5	- 3.6	+ 3.1	+ 1.0	- 0.6

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 - September 2011

Earnings and international competitiveness

Percentage changes from previous year

	2007	2008	2009	2010	2011	2012
Wages and salaries per employee¹						
Gross earnings	+ 3.1	+ 3.2	+ 1.6	+ 1.2	+ 2.7	+ 2.5
Gross real earnings²	+ 0.9	- 0.0	+ 1.1	- 0.7	- 0.4	+ 0.4
Net real earnings²	+ 0.9	- 0.7	+ 2.9	- 0.9	- 0.7	+ 0.1
<i>Total economy</i>						
Unit labour costs	+ 1.1	+ 3.7	+ 4.7	- 0.3	+ 1.6	+ 2.1
<i>Manufacturing</i>						
Unit labour costs	- 2.3	+ 5.2	+ 15.1	- 5.7	- 2.9	+ 0.7
Effective exchange rate - manufactures						
Nominal	+ 1.2	+ 1.1	+ 0.7	- 2.6	+ 0.6	+ 0.7
Real	+ 0.8	+ 0.6	+ 0.4	- 2.7	+ 1.2	+ 0.8

¹ Employees according to National Accounts definition.

² Deflated by CPI.

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Labour market

Changes from previous year (1,000^s)

		2007	2008	2009	2010	2011	2012
Demand for labour							
Persons in active employment ¹		+ 64.7	+ 66.0	- 44.0	+ 31.3	+ 65.5	+ 17.5
Employees ²		+ 65.5	+ 55.6	- 48.5	+ 25.5	+ 58.0	+ 12.5
<i>Percentage changes from previous year</i>		+ 2.1	+ 1.7	- 1.5	+ 0.8	+ 1.8	+ 0.4
Nationals		+ 43.6	+ 31.1	- 43.0	+ 5.8	+ 25.0	+ 3.0
Foreign workers		+ 21.9	+ 24.5	- 5.5	+ 19.7	+ 33.0	+ 9.5
Self-employed ³		- 0.8	+ 10.4	+ 4.5	+ 5.8	+ 7.5	+ 5.0
Labour supply							
Population of working age	(15 to 64 years)	+ 15.5	+ 27.7	+ 17.3	+ 21.6	+ 32.8	+ 15.0
	(15 to 59 years)	+ 17.1	+ 17.6	+ 11.1	+ 8.9	+ 16.8	+ 14.7
Labour force ⁴		+ 47.8	+ 56.0	+ 4.0	+ 21.8	+ 61.0	+ 28.5
Surplus of labour							
Registered unemployed ⁵		- 16.9	- 10.0	+ 48.1	- 9.5	- 4.5	+ 11.0
	1,000 ^s	222.2	212.3	260.3	250.8	246.3	257.3
Unemployed persons in training	1,000 ^s	52.7	50.5	64.1	73.2	63.2	62.2
Unemployment rate							
Eurostat definition ⁶	percent	4.4	3.8	4.8	4.4	4.2	4.4
Percent of total labour force ⁵	percent	5.6	5.3	6.5	6.2	6.0	6.2
National definition ^{5,7}	percent	6.2	5.9	7.2	6.9	6.7	7.0
Employment rate							
Persons in active employment ^{1,8}	percent	64.9	65.7	64.7	65.0	65.8	65.9
Total employment (Eurostat) ^{6,8}	percent	71.4	72.1	71.6	71.7	72.1	72.2

¹ Excluding parental leave and military service. ² According to Federation of Austrian Social Security Institutions.

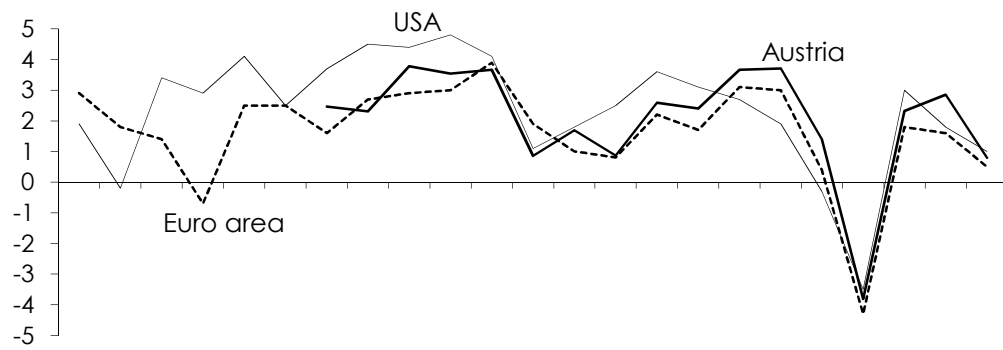
³ According to WIFO. ⁴ Persons in active employment plus unemployment.

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).

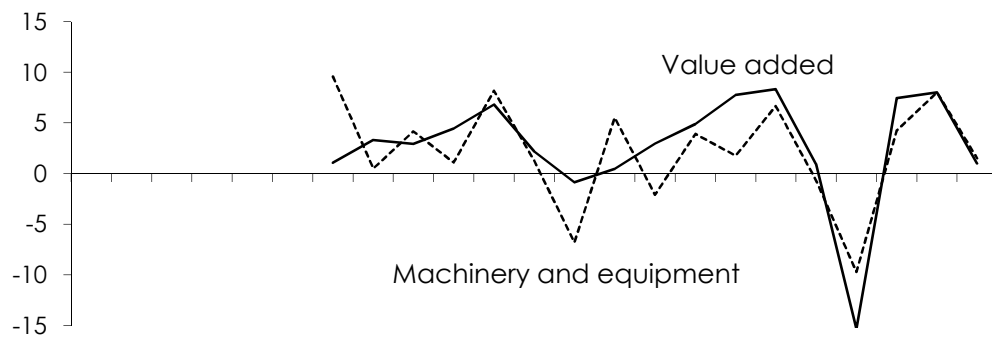
Growth of real GDP

Percent



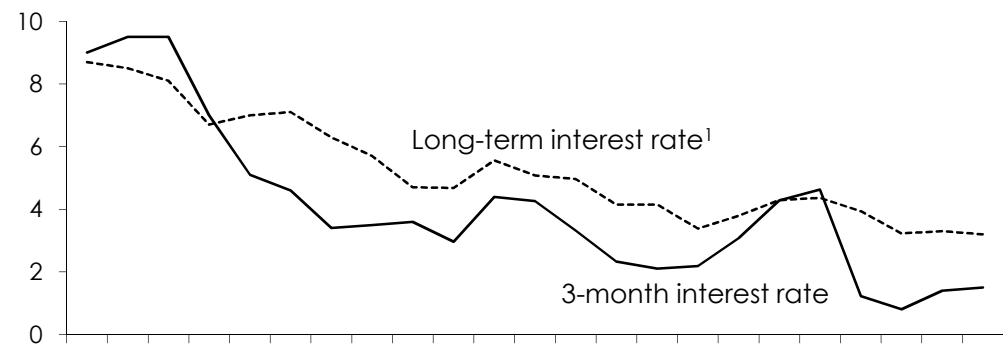
Manufacturing and investment

Percentage changes from previous year, volume



Short-term and long-term interest rates

Percent



Trade

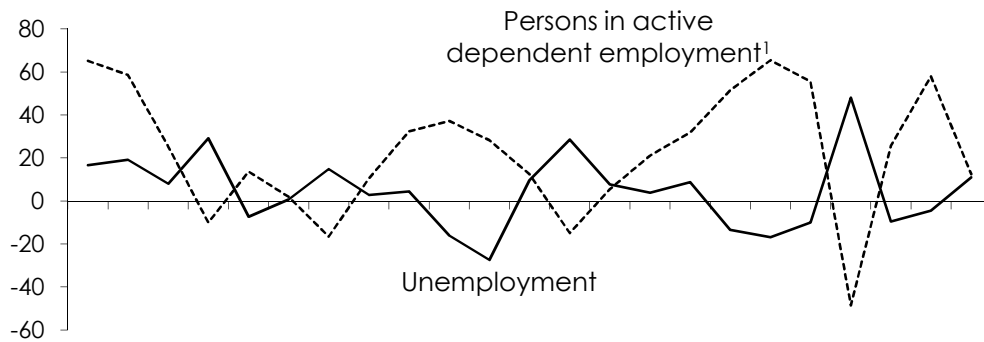
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

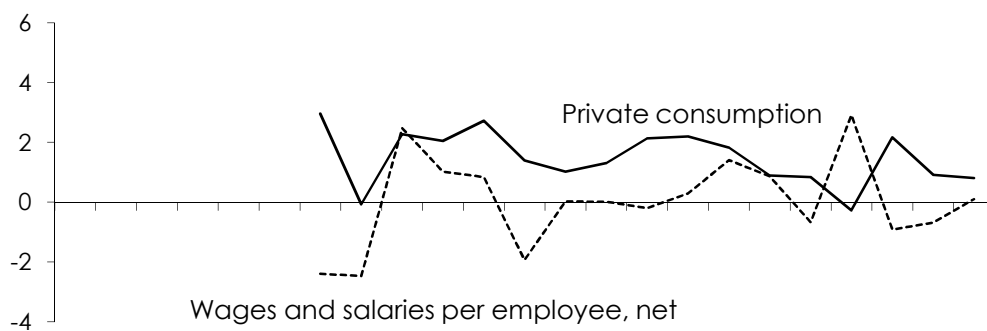
Employment and unemployment

1,000^s from previous year



Consumption and income

Percentage changes from previous year, volume



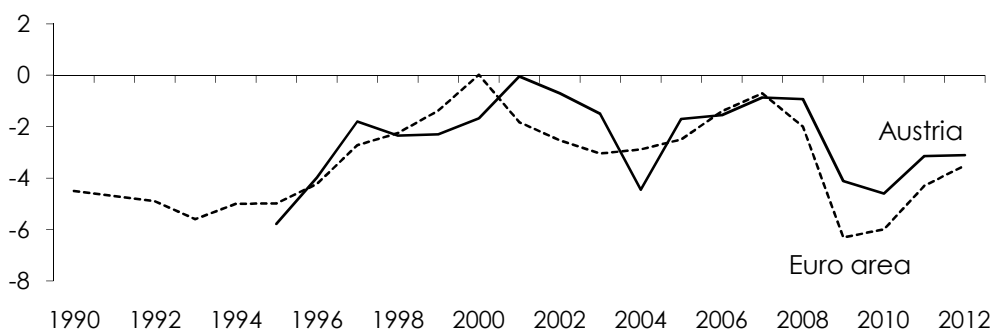
Inflation and unit labour costs

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.