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A-1103 WIEN, POSTFACH 91
TEL. 798 26 01 • FAX 798 93 86

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**Activity Staying Robust, Driven by
Manufacturing and Construction
Economic Outlook for 2007 and 2008**

June 2007

Activity Staying Robust, Driven by Manufacturing and Construction Economic Outlook for 2007 and 2008

Marcus Scheiblecker

Austrian Institute of Economic Research

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Activity Staying Robust, Driven by Manufacturing and Construction

Economic Outlook for 2007 and 2008

The business cycle upturn that started in 2005 is continuing throughout the current year. After an increase of 3.1 percent in 2006, real GDP is expected to expand by 3.2 percent in 2007. While export growth is gradually decelerating, investment is gaining momentum to become the key driver of the upswing. Private household consumption, while picking up this year, still lags behind its normal cyclical profile. The strong pace of growth is leading to a marked increase in the number of jobs and a further decline in unemployment. In 2008, GDP growth is likely to decelerate to 2.5 percent, due to slackening activity in the USA, the strength of the euro and the rise in long-term interest rates.

The latest results of last May from the regular WIFO business survey among domestic companies still give no indication of a slowdown in the lively business activity. For the current year therefore, GDP growth can be expected at a rate of 3.2 percent. Only next year, the slackening of the US economy, the increase in long-term interest rates and the strength of the euro will have a dampening effect on activity in the EU and Austria.

Exports and strengthening investment demand continue to provide the most powerful growth incentives for the time being, benefiting notably the manufacturing and the construction sector as well as commercial services including the cyclically-sensitive personnel service agencies.

As suggested by foreign trade statistics, exports continue to show strong momentum. In the first quarter 2007, the value of goods exports rose by some 9 percent above the year-earlier level. Like in the past, the cyclical slowdown in the USA is assumed to spill over to Europe with some time lag and foreign demand may ebb in the course of the year. The negative repercussions on Austria's foreign trade should, however, be cushioned by continued lively domestic activity in the euro area. Austrian goods

exports should expand by $8\frac{3}{4}$ percent in volume on annual average in 2007, in line with Austria's foreign market growth, followed by a deceleration to a projected $7\frac{1}{4}$ percent in 2008.

Apart from investment in construction, which rose markedly already last year, corporate spending should increase substantially this year also for machinery and equipment. Both the WIFO investment survey and the WIFO business survey among investment goods manufacturers point into that direction. So far, only investment in motor vehicles has been disappointing, although there too, a rebound may be expected for the second half of the year. WIFO expects investment in machinery and equipment to increase by an overall 8 percent in the current year and by a further $4\frac{1}{2}$ percent in 2008. Growth of construction investment, projected at $4\frac{1}{2}$ percent in volume will moderate only little from last year ($+5\frac{1}{4}$ percent). Construction activity should stay lively also in 2008, investment in new projects is expected to increase by $3\frac{1}{4}$ percent.

Private consumption expenditure, while picking up from last year to a rate of $+2\frac{1}{4}$ percent in volume remains comparatively subdued against the background of buoyant overall economic activity. In the first quarter 2007, demand edged up only marginally, which may, however, reflect lower heating energy consumption during the unusually mild winter, an effect likely to be compensated over the subsequent periods. Gains in net household income are predominantly generated this year by the creation of new jobs, while per-capita earnings are expected to remain broadly flat in real terms over the entire forecast period. For this reason, the contribution of private consumption to GDP growth remains distinctly modest in the current cyclical upswing.

Wage developments will not give rise to any inflationary cost pressure, and as a result the sluggish household demand will in turn hold down the increase in consumer prices. Thus, despite the cyclical high and the durability of the upswing, headline inflation in Austria will remain below 2 percent in both years covered by the projections, which marks a notable difference from the experience of past business cycles.

As last year, the labour market is reacting strongly to growing demand and output. The number of people in dependent active employment is expected to go up by 60,000 or 1.9 percent year-on-year in 2007, while unemployment should fall by 15,000,

taking the jobless rate down to 6.3 percent according to the national definition. The benign trend is set to continue into 2008, though losing some momentum: employment is expected to rise by a further 25,000 or 0.8 percent, accompanied by a decline in unemployment by 5,000 to a rate of 6.1 percent.

The general government balance, having narrowed to –1.1 percent of GDP in 2006, is expected to improve further this year. The deficit is projected at 0.7 percent for 2007 and 0.6 percent for 2008. The lower deficit is entirely the result of higher tax revenues on the back of the favourable cyclical conditions. The present projections are based upon the assumption of a rigorous implementation of the planned measures of expenditure restraint.

Vienna, 28 June 2007

*For more details please contact Marcus Scheiblecker, Tel. (1) 798 26 01-245,
Marcus.Scheiblecker@wifo.ac.at*

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Projections - June 2007

Main results

Percentage changes from previous year

		2003	2004	2005	2006	2007	2008
GDP							
Volume		+ 1.1	+ 2.4	+ 2.0	+ 3.1	+ 3.2	+ 2.5
Value		+ 2.4	+ 4.2	+ 3.9	+ 4.7	+ 5.2	+ 4.2
Manufacturing¹, volume		+ 0.1	+ 2.4	+ 2.4	+ 7.7	+ 6.7	+ 3.7
Wholesale and retail trade, volume		+ 0.5	+ 1.3	+ 0.3	+ 1.2	+ 2.2	+ 2.2
Private consumption expenditure, volume		+ 1.3	+ 1.9	+ 1.7	+ 2.0	+ 2.2	+ 2.1
Gross fixed investment, volume		+ 5.9	+ 0.6	+ 0.3	+ 4.3	+ 6.0	+ 3.8
Machinery and equipment ²		+ 6.8	- 0.7	+ 0.1	+ 3.0	+ 8.0	+ 4.5
Construction		+ 5.1	+ 1.6	+ 0.4	+ 5.2	+ 4.5	+ 3.3
Exports of goods³							
Volume		+ 2.6	+ 12.9	+ 2.2	+ 7.1	+ 8.7	+ 7.2
Value		+ 1.9	+ 13.9	+ 5.4	+ 9.5	+ 9.8	+ 7.7
Imports of goods³							
Volume		+ 6.5	+ 11.4	+ 2.3	+ 4.4	+ 8.4	+ 6.6
Value		+ 5.0	+ 12.5	+ 5.9	+ 8.0	+ 9.5	+ 7.5
Current balance	€ bn	-	+ 3.99	+ 5.16	+ 8.22	+ 10.39	+ 11.56
	as a percentage of GDP	-	+ 1.7	+ 2.1	+ 3.2	+ 3.8	+ 4.1
Long-term interest rate⁴	percent	4.2	4.2	3.4	3.8	4.3	4.6
Consumer prices		+ 1.3	+ 2.1	+ 2.3	+ 1.5	+ 1.8	+ 1.9
Unemployment rate							
Eurostat definition ⁵	percent	4.3	4.8	5.2	4.8	4.3	4.2
National definition ⁶	percent	7.0	7.1	7.3	6.8	6.3	6.1
Persons in active dependent employment⁷		+ 0.2	+ 0.7	+ 1.0	+ 1.7	+ 1.9	+ 0.8
General government financial balance							
	according to Maastricht definition						
	as a percentage of GDP	- 1.6	- 1.2	- 1.6	- 1.1	- 0.7	- 0.6

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

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

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Projections - June 2007

Key policy indicators

	2003	2004	2005	2006	2007	2008
<i>Fiscal policy</i>						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 1.6	- 1.2	- 1.6	- 1.1	- 0.7	- 0.6
according to National accounts	- 1.8	- 1.3	- 1.7	- 1.2	- 0.8	- 0.7
General government primary balance	+ 1.3	+ 1.6	+ 1.3	+ 1.6	+ 2.0	+ 2.2
 <i>Monetary policy</i>						
	Percent					
3-month interest rate	2.3	2.1	2.2	3.1	4.1	4.0
Long-term interest rate ¹	4.2	4.2	3.4	3.8	4.3	4.6
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 4.3	+ 1.5	- 0.7	+ 0.2	+ 0.9	+ 0.7
Real	+ 3.3	+ 1.0	- 1.0	- 0.5	+ 0.6	+ 0.6

¹ 10-year central government bonds (benchmark).

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Projections - June 2007

World economy

Percentage changes from previous year

	2003	2004	2005	2006	2007	2008
Real GDP						
World	+ 4.0	+ 5.3	+ 4.9	+ 5.4	+ 4.8	+ 4.7
Total OECD	+ 2.0	+ 3.2	+ 2.7	+ 3.2	+ 2.5	+ 2.5
USA	+ 2.5	+ 3.9	+ 3.2	+ 3.3	+ 1.8	+ 2.1
Japan	+ 1.4	+ 2.7	+ 1.9	+ 2.2	+ 2.3	+ 2.0
EU 27	+ 1.3	+ 2.3	+ 1.8	+ 3.0	+ 3.1	+ 2.5
EU 15	+ 1.1	+ 2.1	+ 1.6	+ 2.8	+ 2.9	+ 2.3
Euro area	+ 0.8	+ 2.0	+ 1.4	+ 2.7	+ 2.9	+ 2.3
Germany	- 0.2	+ 1.2	+ 0.9	+ 2.8	+ 2.8	+ 2.2
New member states ¹	+ 4.1	+ 5.4	+ 4.6	+ 6.0	+ 5.5	+ 5.2
China	+ 10.0	+ 10.1	+ 10.2	+ 10.7	+ 10.5	+ 9.5
World trade, volume	+ 5.3	+ 10.3	+ 7.2	+ 9.0	+ 7.5	+ 7.0
Market growth²	+ 5.4	+ 9.1	+ 7.4	+ 10.3	+ 8.5	+ 7.0
Primary commodity prices						
HWWI Index, total	- 4	+ 18	+ 29	+ 19	- 5	+ 0
Excluding energy	- 6	+ 18	+ 6	+ 22	- 2	+ 1
Crude oil prices						
Average import price (cif) for OECD countries	28.4	36.3	50.6	61.1	62.0	64.0
Exchange rate						
USD per euro	1.131	1.243	1.245	1.256	1.34	1.40

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

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

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Projections - June 2007

Private consumption, income and prices

	2003	2004	2005	2006	2007	2008
	Percentage changes from previous year, volume					
Private consumption expenditure	+ 1.3	+ 1.9	+ 1.7	+ 2.0	+ 2.2	+ 2.1
Durables	+ 3.1	+ 5.1	+ 2.2	+ 1.7	+ 3.0	+ 2.5
Non-durables and services	+ 1.1	+ 1.5	+ 1.6	+ 2.0	+ 2.1	+ 2.1
Household disposable income	+ 2.1	+ 2.0	+ 2.1	+ 2.3	+ 2.2	+ 1.8
Household saving ratio						
As a percentage of disposable income	8.6	8.8	9.1	9.4	9.4	9.2
	Percentage changes from previous year					
Direct lending to domestic non-banks¹	+ 1.6	+ 5.0	+ 4.7	+ 4.5	+ 2.9	+ 3.7
	Percentage changes from previous year					
Inflation rate						
National	1.3	2.1	2.3	1.5	1.8	1.9
Harmonised	1.3	2.0	2.1	1.7	1.9	2.0
Core inflation ²	1.3	1.6	1.5	1.3	1.9	1.9

¹ End of period.

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

Productivity

Percentage changes from previous year

	2003	2004	2005	2006	2007	2008
Total economy						
Real GDP	+ 1.1	+ 2.4	+ 2.0	+ 3.1	+ 3.2	+ 2.5
Employment ¹	- 0.0	- 0.0	+ 0.5	+ 1.0	+ 1.6	+ 0.5
Productivity (GDP per employment)	+ 1.1	+ 2.5	+ 1.6	+ 2.1	+ 1.6	+ 2.0
Manufacturing						
Production ²	+ 0.1	+ 2.3	+ 2.6	+ 7.9	+ 6.7	+ 3.7
Employees ³	- 1.7	- 0.6	- 0.8	+ 0.2	+ 1.5	- 0.7
Productivity per hour	+ 1.4	+ 2.0	+ 4.0	+ 7.4	+ 5.2	+ 5.0
Working hours per day per employee ⁴	+ 0.3	+ 0.8	- 0.6	+ 0.2	- 0.1	- 0.5

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.

Earnings and international competitiveness

Percentage changes from previous year

	2003	2004	2005	2006	2007	2008
Gross earnings per employee ¹	+ 1.9	+ 1.9	+ 1.7	+ 2.6	+ 2.6	+ 2.5
Gross real earnings per employee ¹	+ 0.3	- 0.0	+ 0.0	+ 1.2	+ 0.8	+ 0.6
Net real earnings per employee ¹	+ 0.0	+ 0.1	+ 1.1	+ 0.6	+ 0.1	± 0.0
<i>Total economy</i>						
Unit labour costs	+ 0.7	- 0.8	+ 0.2	+ 0.5	+ 1.0	+ 0.7
<i>Manufacturing</i>						
Unit labour costs	+ 0.8	- 0.8	- 0.6	- 4.4	- 2.2	- 1.5
Relative unit labour costs ²						
Vis-à-vis trading partners	+ 3.6	+ 1.5	+ 1.0	- 2.0	- 0.7	- 1.7
Vis-à-vis Germany	+ 2.1	+ 2.1	+ 3.9	- 0.4	+ 1.0	- 0.5
Effective exchange rate - manufactures						
Nominal	+ 4.3	+ 1.5	- 0.6	+ 0.2	+ 1.0	+ 0.7
Real	+ 3.4	+ 1.1	- 0.9	- 0.5	+ 0.6	+ 0.6

¹ Employees according to National Accounts definition.

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

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Labour market

Changes from previous year (1,000^s)

	2003	2004	2005	2006	2007	2008	
Demand for labour							
Persons in active employment ¹	+ 8.5	+ 25.1	+ 37.2	+ 55.9	+ 65.0	+ 29.5	
Employees ²	+ 5.5	+ 21.1	+ 31.9	+ 51.5	+ 60.0	+ 25.0	
<i>Percentage changes from previous year</i>	+ 0.2	+ 0.7	+ 1.0	+ 1.7	+ 1.9	+ 0.8	
Nationals	- 10.4	+ 9.2	+ 20.0	+ 35.0	+ 41.2	+ 14.3	
Foreign workers	+ 15.9	+ 11.9	+ 11.9	+ 16.5	+ 18.8	+ 10.7	
Self-employed ³	+ 3.0	+ 4.0	+ 5.3	+ 4.4	+ 5.0	+ 4.5	
Labour supply							
Population of working age (15 to 64 years)	+ 37.7	+ 34.4	+ 15.6	+ 18.5	+ 22.9	+ 25.8	
(15 to 59 years)	+ 21.2	+ 35.6	+ 48.5	+ 52.8	+ 24.3	+ 16.1	
Labour force ⁴	+ 16.1	+ 28.9	+ 45.9	+ 42.4	+ 50.0	+ 24.5	
Surplus of labour							
Registered unemployed ⁵	+ 7.7	+ 3.8	+ 8.8	- 13.5	- 15.0	- 5.0	
1,000 ^s	240.1	243.9	252.7	239.2	224.2	219.2	
Unemployment rate							
Eurostat definition ⁶	percent	4.3	4.8	5.2	4.8	4.3	4.2
Percent of total labour force ⁵	percent	6.3	6.4	6.5	6.1	5.7	5.5
National definition ^{5,7}	percent	7.0	7.1	7.3	6.8	6.3	6.1
Employment rate							
Persons in active employment ^{1,8}	percent	62.2	62.3	62.8	63.6	64.5	64.7
Total employment (Eurostat) ^{6,8,9}	percent	-	67.8	68.6	70.2	70.8	70.9

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

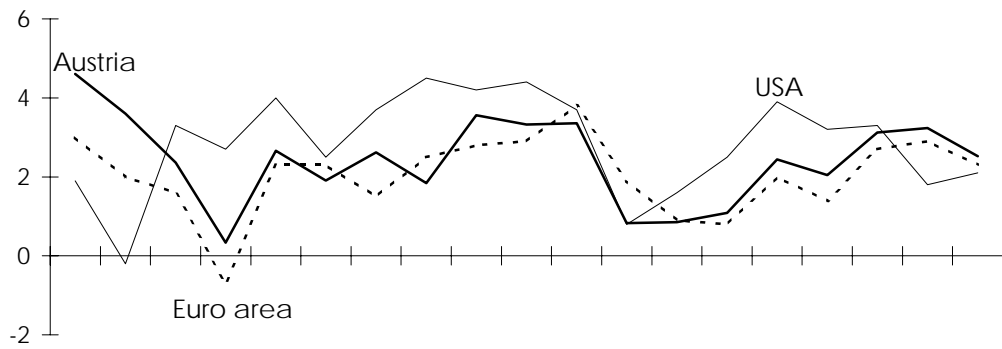
⁵ According to Public Employment Service Austria. ⁶ According to Eurostat Labour Force Survey.

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

⁹ Changed survey method.

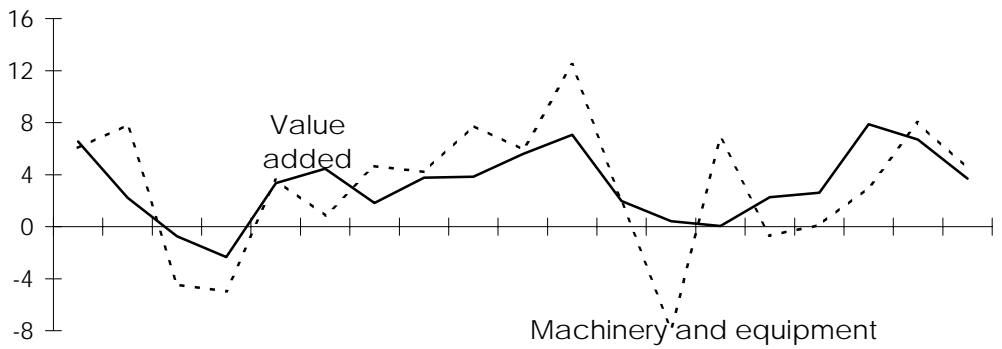
Growth of real GDP

Percent



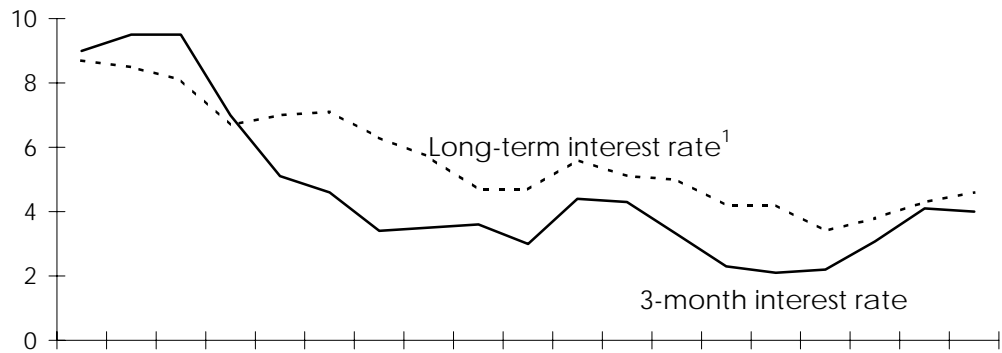
Manufacturing and investment

Percentage changes from previous year, volume



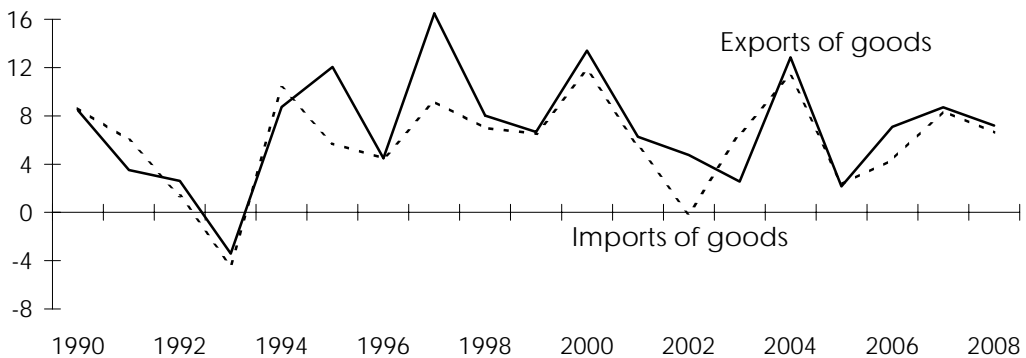
Short-term and long-term interest rates

Percent



Trade

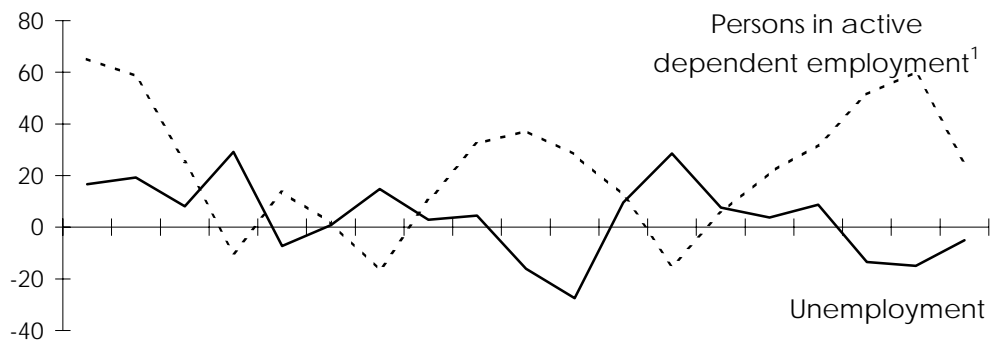
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

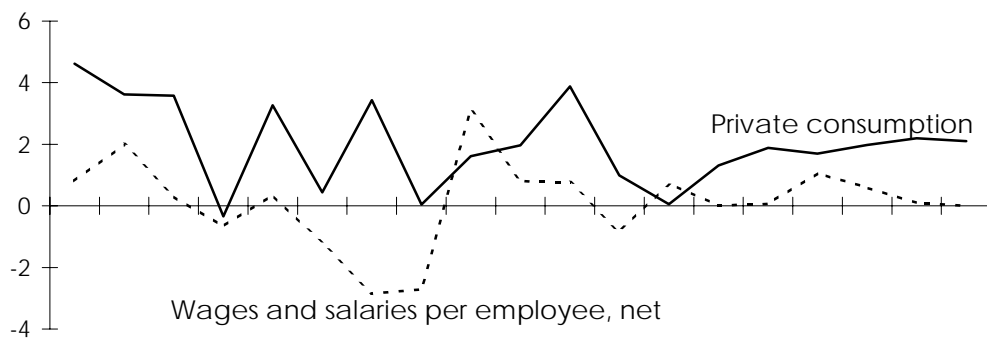
Employment and unemployment

1,000^s from previous year



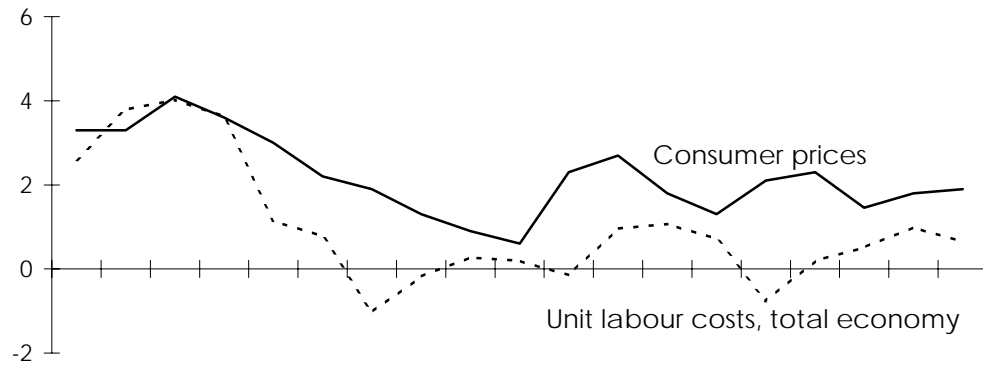
Consumption and income

Percentage changes from previous year, volume



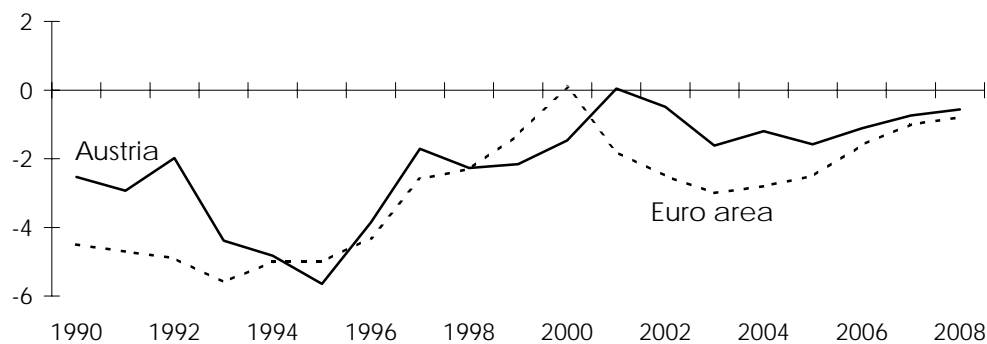
Inflation and unit labour costs

Percentage changes from previous year



General government financial balance

As a percentage of GDP



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

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Wien 3, Arsenal, Objekt 20 • Postanschrift: A-1103 Wien, Postfach 91 • Tel. (+43 1) 798 26 01-0 •
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