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 **ÖSTERREICHISCHES INSTITUT FÜR
WIRTSCHAFTSFORSCHUNG**

**Cyclical Stabilisation, But No
Robust Upturn
Economic Outlook for 2010 and 2011**

December 2009

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Austrian Institute of Economic Research

Abstract

In 2009, economic activity in Austria contracted by 3.4 percent in volume, somewhat less than the euro area average (-3.9 percent). As from the middle of the year, merchandise exports and industrial output started heading up as a result of the expansionary policy stance adopted worldwide. The recovery is set to continue in the months to come, allowing GDP to grow by 1.5 percent in 2010. However, the still low capacity utilisation will hardly provide incentives for higher investment, which is one of the reasons why unemployment will keep rising, to a rate of 8.1 percent of the dependent labour force in 2011. The general government balance will deteriorate to a deficit corresponding to around 5 percent of GDP.

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2009/504/SPE/WIFO project no: 28491

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Medieninhaber (Verleger), Herausgeber und Hersteller: Österreichisches Institut für Wirtschaftsforschung,
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Verlags- und Herstellungsort: Wien

Verkaufspreis: 15,00 € • Download 15,00 €: http://www.wifo.ac.at/www/jsp/index.jsp?fid=23923&id=38081&typeid=8&display_mode=2

Cyclical Stabilisation, But No Robust Upturn

Economic Outlook for 2010 and 2011

In 2009, economic activity in Austria contracted by 3.4 percent in volume, somewhat less than the euro area average (-3.9 percent). As from the middle of the year, merchandise exports and industrial output started heading up as a result of the expansionary policy stance adopted worldwide. The recovery is set to continue in the months to come, allowing GDP to grow by 1.5 percent in 2010. However, the still low capacity utilisation will hardly provide incentives for higher investment, which is one of the reasons why unemployment will keep rising, to a rate of 8.1 percent of the dependent labour force in 2011. The general government balance will deteriorate to a deficit corresponding to around 5 percent of GDP.

The international financial market and economic crisis struck the Austrian economy heavily as from the middle of 2008. Manufacturing output and business investment in machinery and equipment each fell at double-digit rates in 2009. A turnaround set in as from mid-2009, driven primarily by the strongly expansionary stance of monetary and fiscal policy in the worlds' largest economies and by the measures taken at the national level to stabilise domestic activity and the labour market.

As in earlier recoveries, goods exports and manufacturing output are the first to react, heading up since the third quarter 2009 (from the previous period) in response to the pick-up in world trade and demand from major trading partners. International trade is expected to rebound by 7 percent already in 2010, after a fall by 14 percent in 2009. The German economy, taking up nearly one-third of Austrian merchandise exports, emerged relatively early from a particularly severe recession and should grow by 1.5 percent in volume in 2010, above the euro area average of +1.1 percent.

On the back of the worldwide recovery, Austrian volume exports and industrial output should rise by some 4 percent each in 2010. Unlike in many other EU countries, private consumption in Austria remained upward bound (+0.4 percent in volume in 2009) even during the recession, thanks to substantial real wage gains, higher social

transfers and income tax cuts. For 2010, WIFO expects a slight acceleration of household demand growth to +0.7 percent. In such a scenario, real GDP will expand by 1.5 percent in 2010.

Nevertheless, the recovery remains fragile and subject to a number of risks. Thus, there are only few signs to date that the rebound in exports will soon trigger a revival of investment, as has usually been the case in the past. Indeed, results from the WIFO investment survey suggest that the very low capacity utilisation particularly in manufacturing induces firms to cut their investment plans further. WIFO therefore expects corporate spending on business equipment to continue its downward trend (-1 percent in real terms) in 2010. Likewise, construction investment may be reduced once again, by a projected 1 percent. Commercial building and non-subsidised residential building activity are lacklustre, whereas additional construction projects by the Federal Real Estate Agency ("Bundesimmobiliengesellschaft"), the Road Financing Agency (Asfinag) and the Austrian Railways (ÖBB) should largely materialise in 2010.

Major risks also derive from the international environment. In East-central Europe, the debt-financed consumption and construction boom has collapsed. In the Baltic countries, in Romania, Bulgaria and Hungary GDP may therefore decline also in 2010, while the Polish and the Czech economies will enjoy growth rates owing to more resilient private household demand. Uncertainty also relates to the profile of the recovery in Germany after the expiry of the car scrapping premium and of widespread price concessions by car manufacturers. The stabilisation of financial markets and of the banking system remains fragile and the euro appreciation vis-à-vis the dollar will weigh on the revival of business activity in the EU.

Under these circumstances, the cyclical recovery in Austria promises to be slow and may suffer temporary setbacks. WIFO expects real GDP growth of 1.5 percent on annual average 2010 and hardly stronger momentum in 2011 (+1.6 percent). Such flat upward trend will not allow unemployment to decline, given that labour supply is boosted by a growing population of working age and a high reserve of discouraged jobseekers. Even if employment growth should tentatively resume, registered unemployment will rise to nearly 300,000 in 2011 (+70,000 persons in labour market training). Unemployment will by then reach 8.1 percent of the dependent labour force (national definition), the highest rate since 1953, with the risk of the bulk of the recession-induced layoffs becoming long-term unemployed.

The economic crisis also leads to a jump in the government deficit. The slump in tax revenues and the cost of fiscal stimulus programmes will weaken the general government balance to a gap of 5.2 percent of GDP in 2010. A slight improvement to a deficit of 4.8 percent of GDP is expected for 2011 as tax revenues should recover with employment picking up and assuming restraint in government expenditure.

Vienna, 18 December 2009.

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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, 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.ifkt.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".

WIFO
Projections - December 2009

Main results

Percentage changes from previous year

		2006	2007	2008	2009	2010	2011
GDP							
Volume		+ 3.5	+ 3.5	+ 2.0	- 3.4	+ 1.5	+ 1.6
Value		+ 5.2	+ 5.7	+ 4.1	- 1.7	+ 2.1	+ 2.9
Manufacturing¹, volume		+ 9.0	+ 7.3	+ 3.9	- 11.4	+ 4.5	+ 4.0
Wholesale and retail trade, volume		+ 0.8	+ 0.7	+ 0.6	- 2.4	+ 1.0	+ 1.0
Private consumption expenditure, volume		+ 1.8	+ 0.8	+ 0.8	+ 0.4	+ 0.7	+ 0.9
Gross fixed investment, volume		+ 2.4	+ 3.8	+ 1.0	- 7.6	- 1.0	+ 2.0
Machinery and equipment ²		+ 2.0	+ 4.7	+ 0.1	- 12.0	- 1.0	+ 4.0
Construction		+ 2.8	+ 2.9	+ 1.8	- 4.0	- 1.0	+ 0.5
Exports of goods³							
Volume		+ 6.4	+ 9.0	+ 0.3	- 16.8	+ 4.0	+ 6.0
Value		+ 9.5	+ 10.5	+ 2.5	- 19.0	+ 5.6	+ 6.5
Imports of goods³							
Volume		+ 4.1	+ 7.6	+ 0.2	- 11.6	+ 3.2	+ 4.8
Value		+ 8.0	+ 9.6	+ 4.7	- 16.4	+ 5.8	+ 5.3
Current balance	€ bn	+ 7.26	+ 9.62	+ 9.04	+ 6.27	+ 6.82	+ 8.01
	as a percentage of GDP	+ 2.8	+ 3.6	+ 3.2	+ 2.3	+ 2.4	+ 2.7
Long-term interest rate⁴	percent	3.8	4.3	4.3	3.9	3.7	3.8
Consumer prices		+ 1.5	+ 2.2	+ 3.2	+ 0.5	+ 1.3	+ 1.5
Unemployment rate							
Eurostat definition ⁵	percent	4.8	4.4	3.8	5.0	5.4	5.7
National definition ⁶	percent	6.8	6.2	5.8	7.1	7.7	8.1
Persons in active dependent employment⁷		+ 1.7	+ 2.1	+ 2.4	- 1.3	- 0.3	+ 0.3
General government financial balance							
according to Maastricht definition							
as a percentage of GDP		- 1.6	- 0.6	- 0.4	- 4.2	- 5.2	- 4.8

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 and military service.

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Key policy indicators

	2006	2007	2008	2009	2010	2011
Fiscal policy						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 1.6	- 0.6	- 0.4	- 4.2	- 5.2	- 4.8
according to National accounts	- 1.7	- 0.7	- 0.5	- 4.2	- 5.3	- 4.9
General government primary balance						
	+ 1.1	+ 2.2	+ 2.1	- 1.3	- 2.2	- 1.6
Monetary policy						
	Percent					
3-month interest rate	3.1	4.3	4.6	1.2	1.1	1.2
Long-term interest rate ¹	3.8	4.3	4.3	3.9	3.7	3.8
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 0.2	+ 1.1	+ 1.2	+ 0.5	+ 1.2	+ 0.6
Real	- 0.5	+ 0.7	+ 0.6	± 0.0	+ 0.8	+ 0.2

¹ 10-year central government bonds (benchmark).

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Projections - December 2009

World economy

Percentage changes from previous year

	2006	2007	2008	2009	2010	2011
Real GDP						
World	+ 5.1	+ 5.1	+ 3.1	- 1.0	+ 3.0	+ 3.5
USA	+ 2.7	+ 2.1	+ 0.4	- 2.5	+ 1.7	+ 1.9
Japan	+ 2.1	+ 2.3	- 0.7	- 5.2	+ 1.0	+ 1.2
EU 27	+ 3.2	+ 2.9	+ 0.8	- 4.0	+ 0.9	+ 1.5
Euro area 16	+ 3.0	+ 2.8	+ 0.7	- 3.9	+ 1.1	+ 1.4
Germany	+ 3.2	+ 2.5	+ 1.3	- 5.0	+ 1.5	+ 1.4
New member states ¹	+ 6.5	+ 6.1	+ 3.7	- 3.8	± 0.0	+ 1.8
China	+ 11.6	+ 13.0	+ 9.7	+ 8.6	+ 9.0	+ 8.6
World trade, volume	+ 9.6	+ 7.2	+ 2.4	- 14.0	+ 7.0	+ 8.0
Market growth²	+ 11.2	+ 7.8	+ 3.6	- 15.0	+ 4.5	+ 6.5
Primary commodity prices						
HWWI Index, total	+ 19.7	+ 3.7	+ 22.4	- 31	+ 17	+ 4
Excluding energy	+ 22.0	+ 9.5	+ 15.6	- 25	+ 5	+ 7
Crude oil prices						
Brent, USD per barrel	65.1	72.5	97.0	60.0	80	82
Exchange rate						
USD per euro	1.256	1.371	1.471	1.40	1.50	1.55

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

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

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Projections - December 2009

Private consumption, income and prices

	2006	2007	2008	2009	2010	2011
	Percentage changes from previous year, volume					
Private consumption expenditure	+ 1.8	+ 0.8	+ 0.8	+ 0.4	+ 0.7	+ 0.9
Durables	+ 5.6	+ 3.6	+ 2.2	+ 1.0	+ 0.7	+ 1.5
Non-durables and services	+ 1.4	+ 0.5	+ 0.6	+ 0.3	+ 0.7	+ 0.8
Household disposable income	+ 3.0	+ 1.7	+ 1.7	+ 0.9	+ 0.6	+ 0.5
Household saving ratio						
As a percentage of disposable income	10.8	11.3	12.0	13.0	12.9	12.6
	Percentage changes from previous year					
Direct lending to domestic non-banks¹	+ 4.5	+ 3.6	+ 7.4	- 0.5	+ 1.0	+ 3.8
Inflation rate						
National	1.5	2.2	3.2	0.5	1.3	1.5
Harmonised	1.7	2.2	3.2	0.4	1.3	1.5
Core inflation ²	1.3	1.9	2.4	1.4	1.2	1.4

¹ End of period.

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

Productivity

Percentage changes from previous year

	2006	2007	2008	2009	2010	2011
Total economy						
Real GDP	+ 3.5	+ 3.5	+ 2.0	- 3.4	+ 1.5	+ 1.6
Employment ¹	+ 1.5	+ 1.7	+ 2.3	- 1.1	+ 0.0	+ 0.5
Productivity (GDP per employment)	+ 2.0	+ 1.8	- 0.2	- 2.4	+ 1.4	+ 1.1
Manufacturing						
Production ²	+ 9.2	+ 7.5	+ 3.9	- 11.4	+ 4.5	+ 4.0
Employees ³	+ 0.2	+ 2.6	+ 1.7	- 5.8	- 2.0	- 0.4
Productivity per hour	+ 8.8	+ 5.1	+ 2.7	- 3.2	+ 6.4	+ 4.2
Working hours per day per employee ⁴	+ 0.2	- 0.3	- 0.5	- 2.8	+ 0.2	+ 0.2

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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Earnings and international competitiveness

Percentage changes from previous year

	2006	2007	2008	2009	2010	2011
Gross earnings per employee ¹	+ 3.2	+ 3.1	+ 2.7	+ 2.3	+ 1.2	+ 1.9
Gross real earnings per employee ¹	+ 1.0	+ 0.5	+ 0.0	+ 1.8	- 0.1	+ 0.4
Net real earnings per employee ¹	+ 0.8	+ 0.4	- 0.5	+ 3.0	- 0.4	+ 0.1
<i>Total economy</i>						
Unit labour costs	+ 1.0	+ 1.1	+ 2.8	+ 5.2	- 0.2	+ 0.8
<i>Manufacturing</i>						
Unit labour costs	- 4.2	- 1.7	+ 1.0	+ 6.9	- 3.9	- 1.8
Effective exchange rate - manufactures						
Nominal	+ 0.2	+ 1.2	+ 1.1	+ 0.4	+ 1.1	+ 0.6
Real	- 0.4	+ 0.8	+ 0.6	± 0.0	+ 0.9	+ 0.2

¹ Employees according to National Accounts definition.

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Labour market

Changes from previous year (1,000^s)

		2006	2007	2008	2009	2010	2011
Demand for labour							
Persons in active employment ¹		+ 55.0	+ 64.8	+ 86.1	- 34.1	- 6.2	+ 12.6
Employees ²		+ 51.5	+ 65.5	+ 76.7	- 43.6	- 11.0	+ 9.8
<i>Percentage changes from previous year</i>		+ 1.7	+ 2.1	+ 2.4	- 1.3	- 0.3	+ 0.3
Nationals		+ 35.0	+ 43.6	+ 53.2	- 37.1	- 9.0	+ 5.3
Foreign workers		+ 16.5	+ 21.9	+ 23.5	- 6.5	- 2.0	+ 4.5
Self-employed ³		+ 3.5	- 0.7	+ 9.4	+ 9.5	+ 4.8	+ 2.8
Labour supply							
Population of working age	(15 to 64 years)	+ 12.8	+ 15.5	+ 27.7	+ 22.1	+ 26.4	+ 30.7
	(15 to 59 years)	+ 47.3	+ 17.1	+ 17.6	+ 15.9	+ 12.3	+ 15.9
Labour force ⁴		+ 41.5	+ 47.9	+ 76.1	+ 13.5	+ 13.8	+ 29.6
Surplus of labour							
Registered unemployed ⁵		- 13.5	- 16.9	- 10.0	+ 47.6	+ 20.0	+ 17.0
	1,000 ^s	239.2	222.2	212.3	259.9	279.9	296.9
Unemployed persons in training	1,000 ^s	57.5	52.7	50.5	63.8	69.8	69.8
Unemployment rate							
Eurostat definition ⁶	percent	4.8	4.4	3.8	5.0	5.4	5.7
Percent of total labour force ⁵	percent	6.1	5.6	5.2	6.4	6.9	7.3
National definition ^{5,7}	percent	6.8	6.2	5.8	7.1	7.7	8.1
Employment rate							
Persons in active employment ^{1,8}	percent	63.9	64.8	66.0	65.2	64.8	64.6
Total employment (Eurostat) ^{6,8}	percent	70.2	71.4	72.1	71.6	70.9	70.7

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

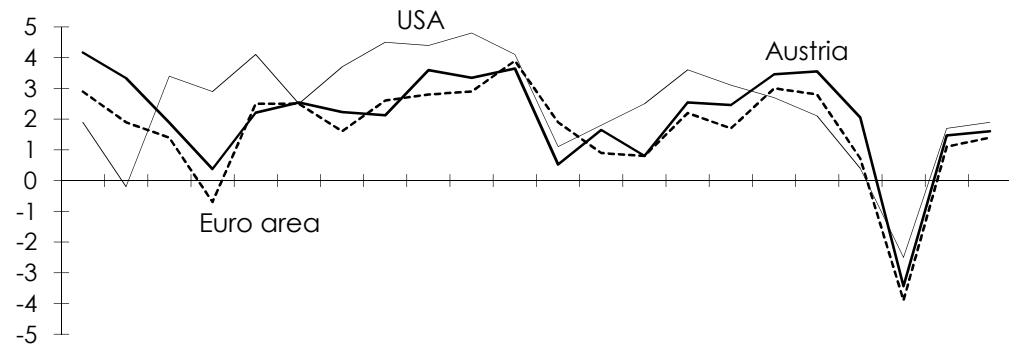
³ According to WIFO. ⁴ Economically active employment plus unemployment.

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).

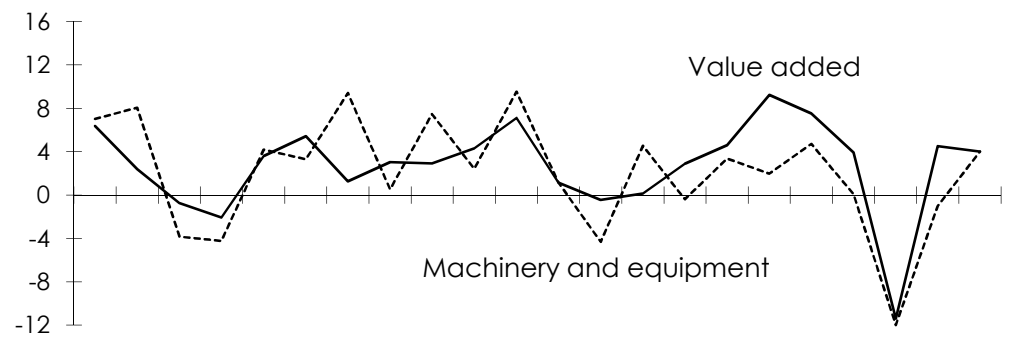
Growth of real GDP

Percent



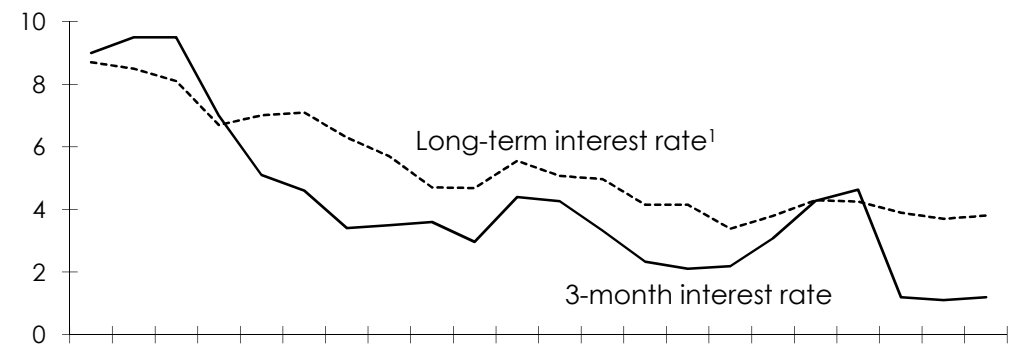
Manufacturing and investment

Percentage changes from previous year, volume



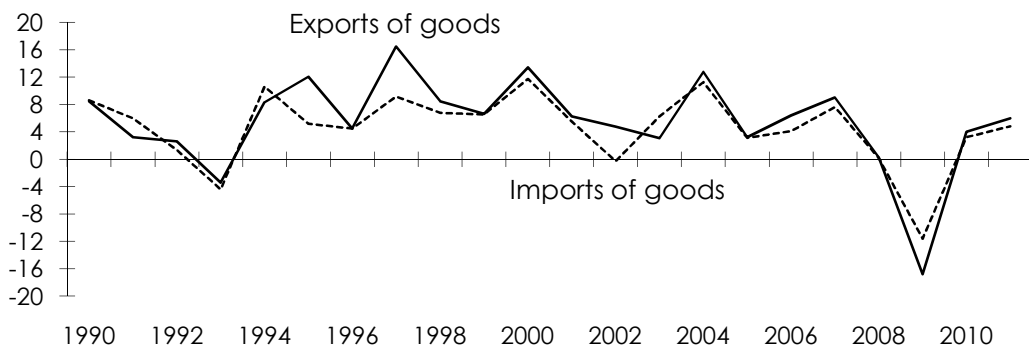
Short-term and long-term interest rates

Percent



Trade

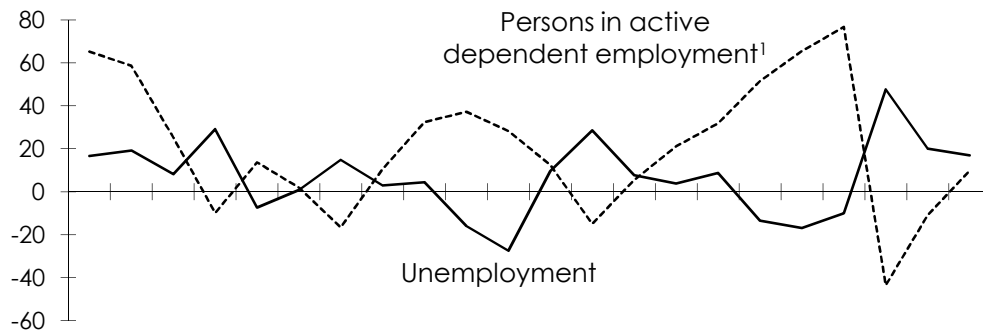
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

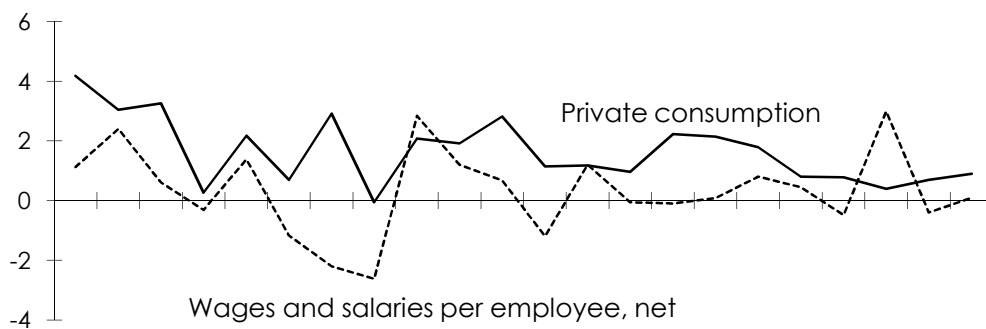
Employment and unemployment

1,000^s from previous year



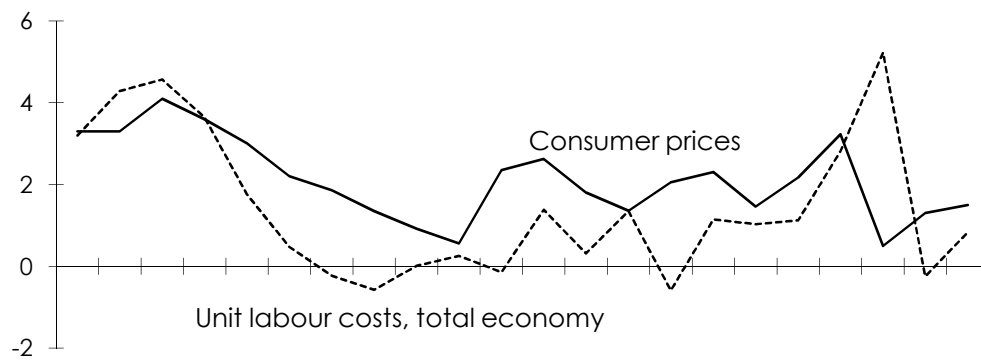
Consumption and income

Percentage changes from previous year, volume



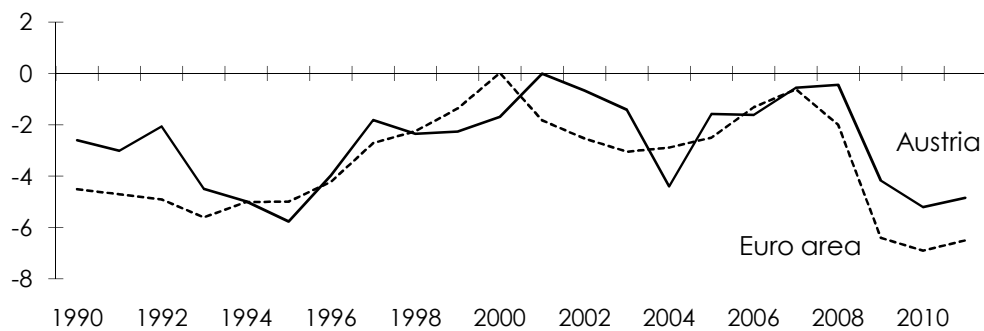
Inflation and unit labour costs

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.