

WIFO

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 **ÖSTERREICHISCHES INSTITUT FÜR
WIRTSCHAFTSFORSCHUNG**

**Economic Outlook for 2012 and 2013:
Euro Area Debt Crisis Weighing
Increasingly on Domestic Activity**

June 2012



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Austrian Institute of Economic Research

Abstract

Economic policy in the euro area is confronted with major challenges. Against this background it is extremely difficult to project international and domestic economic developments. The present forecast is based on highly benign assumptions concerning the resolution of the current crisis. Subject to these assumptions, Austria's GDP should grow by 0.6 percent this year and by 1.3 percent in 2013, with uncertainty being particularly high for next year.

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Economic Outlook for 2012 and 2013: Euro Area Debt Crisis Weighing Increasingly on Domestic Activity

Economic policy in the euro area is confronted with major challenges. Against this background it is extremely difficult to project international and domestic economic developments. The present forecast is based on highly benign assumptions concerning the resolution of the current crisis. Subject to these assumptions, Austria's GDP should grow by 0.6 percent this year and by 1.3 percent in 2013, with uncertainty being particularly high for next year.

Latest developments of the sovereign debt crisis in the euro area and the reaction of economic policy currently overshadow the course of the business cycle. The outcome of the Greek elections and the swiftly installed new government have done little so far to reassure financial markets about the situation in the euro area. Interest rates on Italian and Spanish government bonds have increased once again, such that new credit taken up by the two countries aggravates the burden on their public finances, thereby undermining further the confidence of financial markets. At the same time, some euro area countries like Germany and Austria observe important inflows of financial funds which lower the yields on their government bonds. The sizeable differences between interest rates inside Monetary Union give rise not only to economic frictions, but also to political tensions. The lingering uncertainty about a resolution of the crisis has a negative impact on decisions of both investors and consumers. The present forecast is based on assumptions that appear optimistic from the present perspective: Monetary Union is maintained in its present composition (other scenarios would have severe consequences for the banking system that are difficult to predict); the cross-country differences in interest rates on government bonds will diminish and the tight consolidation programmes in the countries concerned will be relaxed to some extent in order to re-allocate funds to support investment-led growth on the international as well as the domestic front.

Under such conditions, the international economic environment should improve and allow upward-bound forces of demand and output to prevail also in Europe. This would be supported by the depreciation of the euro vis-à-vis the dollar.

In such a scenario, the Austrian economy may expand by 0.6 percent in 2012, with growth accelerating to 1.3 percent in 2013. Easing commodity prices would, notwithstanding the decline in the dollar-euro exchange rate, make for a deceleration of inflation to an annual rate of 2.3 percent in 2012 and 1.9 percent in 2013.

Relatively favourable has been the trend on the Austrian labour market since the beginning of the year, which suggests an increase in employment by 1.3 percent for the whole of 2012. In 2013, net job creation should abate to a modest rate of 0.4 percent. The unemployment rate on national definition is projected to rise to 7.1 percent this year and 7.4 percent in 2013.

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.

Average rates of change

The time given refers to the initial and the final value of the period of computation: hence the average rate 2005-2010 comprises as the first rate of change that from 2005 to 2006, and as the last that from 2009 to 2010.

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.iikt.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 - June 2012

Main results

Percentage changes from previous year

		2008	2009	2010	2011	2012	2013
GDP							
Volume		+ 1.4	- 3.8	+ 2.3	+ 3.0	+ 0.6	+ 1.3
Value		+ 3.2	- 2.8	+ 4.1	+ 4.9	+ 2.8	+ 2.8
Manufacturing¹ , volume		+ 1.3	- 15.0	+ 7.2	+ 9.8	+ 1.0	+ 3.0
Wholesale and retail trade , volume		- 3.0	+ 0.7	+ 3.1	+ 0.1	+ 0.5	+ 0.8
Private consumption expenditure , volume		+ 0.8	- 0.3	+ 2.2	+ 0.5	+ 0.8	+ 0.9
Gross fixed investment , volume		+ 0.7	- 8.3	+ 0.1	+ 5.4	+ 1.1	+ 2.0
Machinery and equipment		- 0.7	- 9.7	+ 4.3	+ 10.5	+ 1.8	+ 3.5
Construction		+ 1.0	- 7.6	- 2.9	+ 2.4	+ 0.4	+ 0.6
Exports of goods²							
Volume		+ 0.5	- 16.8	+ 12.8	+ 7.5	+ 3.5	+ 6.2
Value		+ 2.5	- 20.2	+ 16.7	+ 11.7	+ 4.4	+ 7.8
Imports of goods²							
Volume		+ 0.6	- 14.3	+ 10.3	+ 8.0	+ 2.9	+ 5.6
Value		+ 4.7	- 18.4	+ 16.5	+ 15.1	+ 3.8	+ 7.8
Current balance	€ bn	+ 13.76	+ 7.49	+ 8.62	+ 5.86	+ 7.32	+ 8.61
	as a percentage of GDP	+ 4.9	+ 2.7	+ 3.0	+ 2.0	+ 2.4	+ 2.7
Long-term interest rate³	percent	4.4	3.9	3.2	3.3	2.5	2.5
Consumer prices		+ 3.2	+ 0.5	+ 1.9	+ 3.3	+ 2.3	+ 1.9
Unemployment rate							
Eurostat definition ⁴	percent	3.8	4.8	4.4	4.2	4.5	4.8
National definition ⁵	percent	5.9	7.2	6.9	6.7	7.1	7.4
Persons in active dependent employment⁶		+ 1.7	- 1.5	+ 0.8	+ 1.9	+ 1.3	+ 0.4
General government financial balance							
according to Maastricht definition							
as a percentage of GDP		- 0.9	- 4.1	- 4.5	- 2.6	- 2.9	- 2.3

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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Key policy indicators

	2008	2009	2010	2011	2012	2013
Fiscal policy						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 0.9	- 4.1	- 4.5	- 2.6	- 2.9	- 2.3
General government primary balance	+ 1.7	- 1.3	- 1.8	- 0.0	- 0.3	+ 0.2
Monetary policy						
	Percent					
3-month interest rate	4.6	1.2	0.8	1.4	0.9	1.0
Long-term interest rate ¹	4.4	3.9	3.2	3.3	2.5	2.5
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 1.2	+ 0.9	- 2.5	+ 0.1	- 1.3	- 0.5
Real	+ 0.6	+ 0.4	- 2.7	+ 0.7	- 1.4	- 0.7

¹ 10-year central government bonds (benchmark).

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Projections - June 2012

World economy

Percentage changes from previous year

	2008	2009	2010	2011	2012	2013
Real GDP						
World	+ 2.8	- 0.6	+ 5.3	+ 3.9	+ 3.3	+ 3.7
USA	- 0.3	- 3.5	+ 3.0	+ 1.7	+ 2.0	+ 1.8
Japan	- 1.0	- 5.5	+ 4.4	- 0.7	+ 2.1	+ 1.7
EU 27	+ 0.3	- 4.3	+ 2.1	+ 1.5	± 0.0	+ 1.4
Euro area 16	+ 0.4	- 4.3	+ 1.9	+ 1.5	- 0.2	+ 1.1
Germany	+ 1.1	- 5.1	+ 3.7	+ 3.0	+ 0.7	+ 1.4
New member states ¹	+ 4.2	- 3.2	+ 2.3	+ 3.2	+ 1.6	+ 3.2
China	+ 9.6	+ 9.2	+ 10.4	+ 9.2	+ 8.0	+ 8.0
World trade, volume	+ 2.5	- 12.6	+ 14.9	+ 5.7	+ 4.0	+ 6.0
Market growth²	+ 3.0	- 11.4	+ 11.7	+ 6.1	+ 3.0	+ 5.7
Primary commodity prices						
HWWI Index, total	+ 32.7	- 34.7	+ 28.9	+ 28.6	- 3	+ 3
Excluding energy	+ 18.7	- 28.4	+ 31.9	+ 19.2	- 10	+ 15
Crude oil prices						
Brent, USD per barrel	97.0	61.5	79.5	111.3	110	110
Exchange rate						
USD per euro	1.471	1.393	1.327	1.392	1.25	1.20

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

	2008	2009	2010	2011	2012	2013
	Percentage changes from previous year, volume					
Private consumption expenditure	+ 0.8	- 0.3	+ 2.2	+ 0.5	+ 0.8	+ 0.9
Durables	+ 3.7	+ 0.9	+ 5.8	+ 0.9	- 0.5	+ 0.5
Non-durables and services	+ 0.5	- 0.4	+ 1.8	+ 0.5	+ 1.0	+ 1.0
Household disposable income	+ 0.9	- 1.7	- 0.3	- 0.3	+ 0.6	+ 1.1
	As a percentage of disposable income					
Household saving ratio¹	11.5	10.7	8.3	7.5	7.4	7.5
Household saving ratio²	11.4	10.1	7.8	7.0	6.8	7.0
	Percentage changes from previous year					
Direct lending to domestic non-banks³	+ 7.4	- 1.3	+ 2.9	+ 2.6	+ 2.6	+ 2.4
Inflation rate						
National	3.2	0.5	1.9	3.3	2.3	1.9
Harmonised	3.2	0.4	1.7	3.6	2.4	1.9
Core inflation ⁴	2.4	1.5	1.2	2.8	2.2	1.8

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.

Productivity

Percentage changes from previous year

	2008	2009	2010	2011	2012	2013
Total economy						
Real GDP	+ 1.4	- 3.8	+ 2.3	+ 3.0	+ 0.6	+ 1.3
Employment ¹	+ 2.1	- 0.9	+ 0.8	+ 1.7	+ 1.2	+ 0.6
Productivity (GDP per employment)	- 0.7	- 2.9	+ 1.5	+ 1.2	- 0.6	+ 0.7
Manufacturing						
Production ²	+ 0.9	- 15.3	+ 7.4	+ 10.2	+ 1.0	+ 3.0
Employees ³	+ 1.7	- 5.3	- 1.3	+ 1.9	+ 1.3	- 0.2
Productivity per hour	- 0.3	- 7.3	+ 5.6	+ 8.4	+ 0.7	+ 2.9
Working hours per day per employee ⁴	- 0.5	- 3.5	+ 3.0	- 0.1	- 1.0	+ 0.3

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

	2008	2009	2010	2011	2012	2013
Wages and salaries per employee¹						
Gross earnings	+ 3.2	+ 1.6	+ 1.2	+ 2.7	+ 3.2	+ 2.2
Gross real earnings²	- 0.0	+ 1.1	- 0.6	- 0.5	+ 0.9	+ 0.3
Net real earnings²	- 0.7	+ 2.9	- 0.8	- 0.8	+ 0.6	± 0.0
Unit labour costs						
Total economy	+ 3.7	+ 4.7	- 0.3	+ 1.4	+ 3.8	+ 1.4
Manufacturing	+ 5.2	+ 15.1	- 5.7	- 4.5	+ 3.6	- 0.8
Effective exchange rate - manufactures						
Nominal	+ 1.1	+ 0.7	- 2.6	+ 0.0	- 1.3	- 0.5
Real	+ 0.6	+ 0.4	- 2.7	+ 0.7	- 1.4	- 0.7

¹ Employees according to National Accounts definition.

² Deflated by CPI.

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Labour market

Changes from previous year (1,000^s)

		2008	2009	2010	2011	2012	2013
Demand for labour							
Persons in active employment ¹		+ 66.0	- 44.0	+ 31.3	+ 70.5	+ 47.0	+ 20.0
Employees ²		+ 55.6	- 48.5	+ 25.5	+ 63.3	+ 42.0	+ 15.0
<i>Percentage changes from previous year</i>		+ 1.7	- 1.5	+ 0.8	+ 1.9	+ 1.3	+ 0.4
Nationals		+ 31.1	- 43.0	+ 5.8	+ 25.7	+ 11.0	+ 6.0
Foreign workers		+ 24.5	- 5.5	+ 19.7	+ 37.7	+ 31.0	+ 9.0
Self-employed ³		+ 10.4	+ 4.5	+ 5.8	+ 7.2	+ 5.0	+ 5.0
Labour supply							
Population of working age	(15 to 64 years)	+ 27.7	+ 17.3	+ 21.6	+ 37.0	+ 15.0	+ 6.7
	(15 to 59 years)	+ 17.6	+ 11.1	+ 8.9	+ 17.1	+ 14.7	+ 10.8
Labour force ⁴		+ 56.0	+ 4.0	+ 21.8	+ 66.4	+ 65.0	+ 34.5
Surplus of labour							
Registered unemployed ⁵		- 10.0	+ 48.1	- 9.5	- 4.1	+ 18.0	+ 14.5
	1,000 ^s	212.3	260.3	250.8	246.7	264.7	279.2
Unemployed persons in training	1,000 ^s	50.5	64.1	73.2	63.2	67.2	70.2
Unemployment rate							
Eurostat definition ⁶	percent	3.8	4.8	4.4	4.2	4.5	4.8
Percent of total labour force ⁵	percent	5.3	6.5	6.2	6.0	6.4	6.7
National definition ^{5,7}	percent	5.9	7.2	6.9	6.7	7.1	7.4
Employment rate							
Persons in active employment ^{1,8}	percent	65.7	64.7	65.0	65.9	66.5	66.8
Total employment (Eurostat) ^{6,8}	percent	72.1	71.6	71.7	72.1	72.4	72.5

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

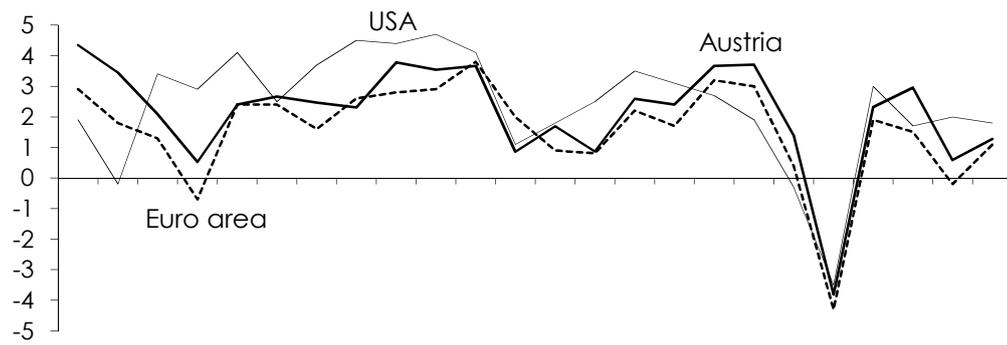
³ According to WIFO. ⁴ Persons in active employment plus unemployment.

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



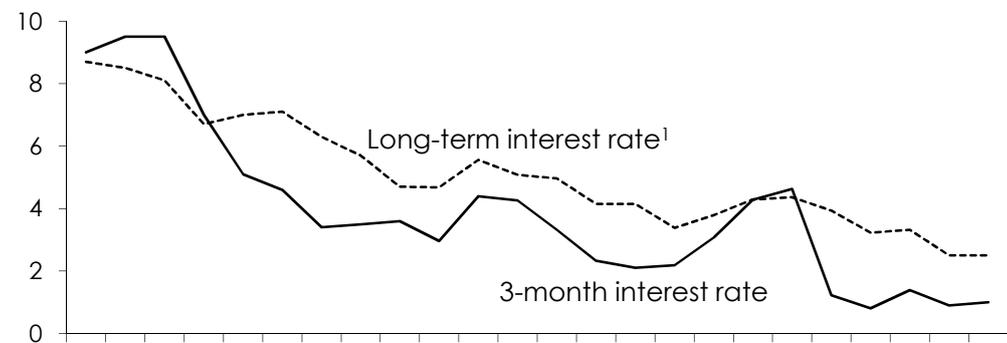
Manufacturing and investment

Percentage changes from previous year, volume



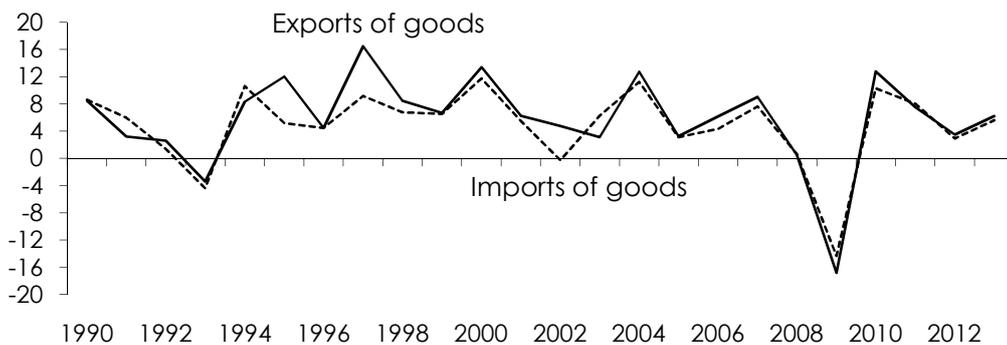
Short-term and long-term interest rates

Percent



Trade

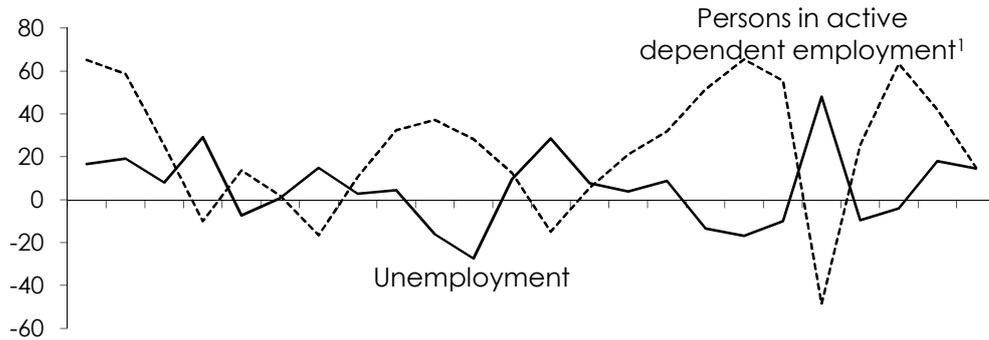
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

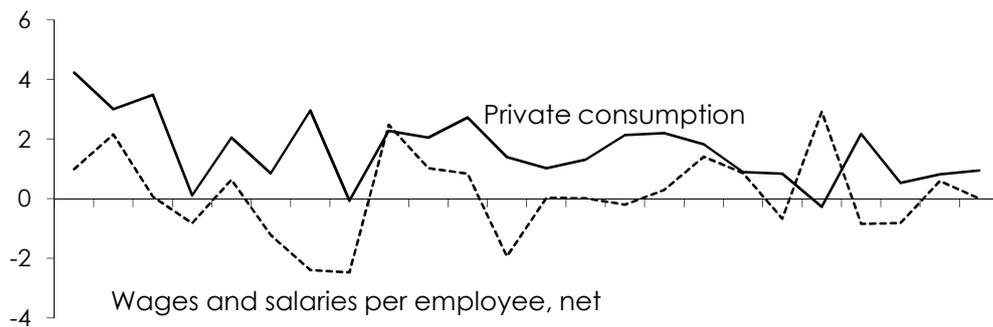
Employment and unemployment

1,000^s from previous year



Consumption and income

Percentage changes from previous year, volume



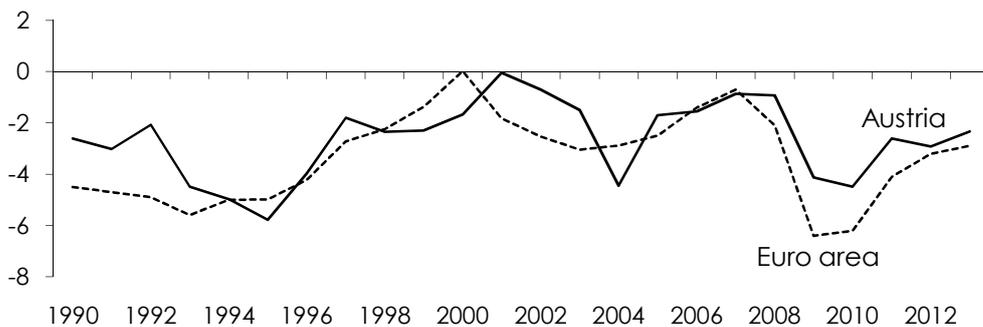
Inflation and unit labour costs

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.