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Purchasing Power Increases After Mild Recession. Economic Outlook for 2023 and 2024

Stefan Schiman-Vukan, Stefan Ederer

Purchasing Power Increases After Mild Recession

Economic Outlook for 2023 and 2024

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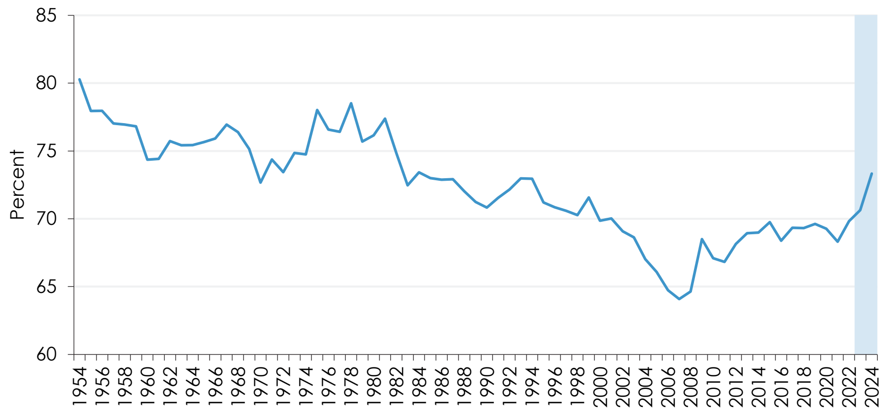
- The energy price shocks of the previous year and a strong destocking lead to an industrial recession in Europe in 2023, which also affects Austria.
- Due to the temporary loss of purchasing power, the other sectors are also losing momentum. Construction suffers particularly from the interest rate increases.
- Nevertheless, the distribution of work among more heads and an increased retention of workers in the downturn ensure a robust labour market.
- With strongly rising real incomes and a recovery in world trade, domestic value added will expand again in 2024.
- Due to the outflow of wealth to commodity-producing countries, compensation for real wage losses increases the wage share.

Development of the wage share

Adjusted for the change in the share of employees in total employment compared to the base year 2015



The wage share is the share of compensation of employees in national income, the other part being essentially profits (capital income minus depreciation). The long-term downward trend of the wage share ended after the financial market and economic crisis in 2009, since then it has been trending upwards (source: Statistics Austria, WIFO. 2023 and 2024: forecast).

"Although the projected wage increases only compensate for inflation, the wage share is increasing as outflows to commodity-exporting countries dampened national income growth."

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Economic Outlook for 2023 and 2024

Stefan Schiman-Vukan, Stefan Ederer

October 2023

Purchasing Power Increases After Mild Recession. Economic Outlook for 2023 and 2024
Subdued purchasing power, high energy prices and sharp interest rate increases lead to a mild recession in Austria in 2023; real GDP is expected to contract by 0.8 percent. In 2024, strong real income growth and a pick-up in world trade will ensure an economic recovery (real GDP +1.2 percent). In construction, however, the recession will intensify.

JEL-Codes: E32, E66 • **Keywords:** Business cycle, economic outlook, forecast

All staff members of the Austrian Institute of Economic Research contribute to the Economic Outlook. For definitions used see "Methodological Notes and Short Glossary", https://www.wifo.ac.at/wwadocs/form/WIFO-BusinessCycleInformation-Glossary.pdf

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Value added in Austria shrank in the summer half-year 2023. Industry is already in recession, but many service sectors have also lost significant momentum. In the construction industry, the strong key interest rate increases have accelerated the trend reversal in residential construction.

Except for the decline in job vacancies, the economic slowdown is hardly reflected in the labour market so far. Employment growth has only slowed in 2023, while unemployment is rising mainly due to higher labour supply. One reason for the robust labour market is the decline in per capita working hours since the COVID-19 pandemic. Furthermore, companies seem to be more likely to retain workers in the downturn to avoid costly recruitment in the upturn.

Like this so-called "labour hoarding", the downturn in industry is not only to be observed in Austria but worldwide, especially since the reduction of precautionary stocks is weighing on production and world trade. Now that inventories are being used up and energy prices have fallen, demand for new goods will rise again in the coming year. In the wake of the global economy, production in Austria will also recover. However, stronger impulses than from industry will come from private households in 2024, whose real incomes will increase strongly due to the delayed adjustment of wages and salaries, pensions and social benefits to inflation.

Austria's inflation differential with important trading partners will remain positive in 2024, but will narrow. Despite the worsened competitive price position, domestic exporters should gain market share in 2023, as they are less affected by the slump in demand for intermediate products and have maintained their competitiveness in special niches. However, due to the delayed decline in demand for capital goods, market share losses are likely in 2024.

All in all, the Austrian economy experiences a mild recession in 2023 due to various exogenous shocks: high price increases as a result of the pandemic, additional energy price shocks due to the Ukraine war and sharp increases in key interest rates. The weakness in economic activity is intended from a monetary policy perspective, as it helps to reduce price pressures. The lagged increase in real incomes will boost purchasing power and provide growth impulses in 2024.

Table 1: **Main results**

	2019	2020	2021	2022	2023	2024
	Percentage changes from previous year					
Gross domestic product, volume	+ 1.5	− 6.6	+ 4.2	+ 4.8	− 0.8	+ 1.2
Manufacturing	+ 0.8	− 7.3	+ 12.7	+ 4.1	− 2.7	+ 0.1
Wholesale and retail trade	+ 2.9	− 3.3	− 1.1	+ 2.1	− 3.0	+ 1.9
Private consumption expenditure[1], volume	+ 0.5	− 8.5	+ 4.2	+ 5.7	+ 0.8	+ 1.8
Consumer durables	+ 0.6	− 2.6	+ 3.7	− 0.3	− 3.6	+ 2.0
Gross fixed capital formation, volume	+ 4.5	− 5.5	+ 6.1	+ 0.1	− 0.5	− 0.5
Machinery and equipment[2]	+ 5.3	− 7.1	+ 9.9	+ 2.0	+ 1.5	+ 2.6
Construction	+ 3.6	− 3.6	+ 1.8	− 2.0	− 2.7	− 4.1
Exports, volume	+ 4.1	− 10.6	+ 9.1	+ 11.2	+ 1.6	+ 2.6
Exports of goods, fob	+ 3.6	− 7.7	+ 12.3	+ 7.1	+ 1.5	+ 2.5
Imports, volume	+ 2.2	− 10.0	+ 14.3	+ 7.9	+ 0.6	+ 2.7
Imports of goods, fob	+ 0.5	− 7.2	+ 15.2	+ 5.1	− 1.9	+ 2.3
Gross domestic product, value	+ 3.1	− 4.1	+ 6.4	+ 10.4	+ 7.1	+ 5.5
billion €	397.15	380.89	405.24	447.22	479.15	505.33
Current account balance as a percentage of GDP	2.4	3.4	1.6	− 0.3	1.5	1.9
Consumer prices	+ 1.5	+ 1.4	+ 2.8	+ 8.6	+ 7.7	+ 4.0
GDP deflator[3]	+ 1.6	+ 2.7	+ 2.1	+ 5.3	+ 8.0	+ 4.2
Three-month interest rate percent	− 0.4	− 0.4	− 0.5	0.3	3.5	4.4
Long-term interest rate[4] percent	0.1	− 0.2	− 0.1	1.7	3.2	4.6
General government financial balance, Maastricht definition as a percentage of GDP	0.6	− 8.0	− 5.8	− 3.5	− 2.4	− 1.6
Persons in active dependent employment[5]	+ 1.6	− 2.0	+ 2.5	+ 3.0	+ 1.0	+ 0.5
Unemployment rate						
Eurostat definition[6]	4.8	6.0	6.2	4.8	5.2	5.2
National definition[7]	7.4	9.9	8.0	6.3	6.5	6.6
Greenhouse gas emissions[8]	+ 1.4	− 7.6	+ 4.9	− 6.1	− 2.4	− 0.6
million t CO_2 equivalent	79.99	73.91	77.53	72.83	71.09	70.67

Source: WIFO, ECB, Environmental Agency Austria, Federation of Social Insurances, OeNB, Public Employment Service Austria, Statistics Austria. 2023 and 2024: forecast. – [1] Including non-profit institutions serving households. – [2] Including weapons systems. – [3] Measures purely domestic inflation. – [4] 10-year central government bonds (benchmark). – [5] Excluding persons in valid employment contract receiving child care benefit or being in military service. – [6] As a percentage of total labour force, Labour Force Survey. Due to a revision of the Labour Force Survey methodology planned for the end of June, a forecast of this indicator is currently waived. – [7] As a percentage of dependent labour force. – [8] From 2021: forecast.

1. Global economy loses momentum

In the USA, the business cycle is being supported by expansionary public sector measures. In the euro area, it is now being dampened by the energy price shocks of the previous year.

The expansion of the global economy slowed down in the second quarter of 2023. Global trade in goods contracted for the third consecutive quarter and global industrial production fell. The consumption structure of private households has normalised after the end of the pandemic, with demand increasingly shifting from goods to services again. In addition, after the supply chain problems were resolved, companies reduced their partly high inventories of intermediate products. Third, demand in China also weakened noticeably after the opening effects ended in spring 2023.

In the USA, the business cycle has hardly slowed down so far; consumer spending continues to support demand there. Consumer confidence has remained largely positive until recently, as the labour market is robust and real incomes are rising again after inflation eased. The excess savings from the pandemic have also not yet been fully used up. As a result of government stimulus programmes (Inflation Reduction Act and Chips and Science Act), investment in machinery and equipment and non-residential construction even expanded significantly in the spring. By contrast, industrial production stagnated in the first half of 2023.

In the euro area, many economies are suffering from weak industrial activity. In addition, the service sector also lost momentum in the spring. Overall economic output remained largely unchanged from the fourth quarter of 2022 to the second quarter of 2023. Private household consumption expenditure stagnated in the second quarter, as persistently high inflation reduced real incomes, while high interest rates weighed on residential construction. The situation on the labour market, on the other hand, remains good.

Table 2: **International economy**

	Percentage shares 2021		2019	2020	2021	2022	2023	2024
	Austria's exports of goods	World GDP[1]	GDP volume, percentage changes from previous year					
EU 27	68.7	14.9	+ 1.8	− 5.6	+ 5.7	+ 3.4	+ 0.6	+ 1.4
Euro area	52.0	10.4	+ 1.6	− 6.1	+ 5.6	+ 3.3	+ 0.6	+ 1.2
Germany	29.8	3.3	+ 1.1	− 3.8	+ 3.2	+ 1.8	− 0.6	+ 1.2
Italy	6.8	1.9	+ 0.5	− 9.0	+ 7.0	+ 3.7	+ 0.7	+ 0.6
France	4.0	2.3	+ 1.8	− 7.5	+ 6.4	+ 2.5	+ 0.8	+ 0.6
CEEC 5[2]	15.9	2.2	+ 4.0	− 3.3	+ 6.2	+ 4.2	− 0.1	+ 2.8
Hungary	4.0	0.3	+ 4.9	− 4.5	+ 7.2	+ 4.6	− 1.1	+ 2.6
Czech Republic	3.8	1.0	+ 4.4	− 2.0	+ 6.9	+ 5.1	+ 0.0	+ 3.6
Poland	3.6	0.3	+ 3.0	− 5.5	+ 3.6	+ 2.4	− 0.4	+ 1.2
USA	6.6	15.6	+ 2.5	− 2.2	+ 5.8	+ 1.9	+ 1.9	+ 0.6
Switzerland	5.4	0.5	+ 1.1	− 2.1	+ 5.4	+ 2.6	+ 0.7	+ 1.3
UK	2.7	18.5	+ 6.0	+ 2.2	+ 8.4	+ 3.0	+ 5.0	+ 4.3
China	2.6	2.3	+ 1.6	− 10.4	+ 8.7	+ 4.3	+ 0.7	+ 0.9
Total[3]								
PPP-weighted[4]		52	+ 3.5	− 2.0	+ 6.8	+ 2.8	+ 2.6	+ 2.2
Export weighted[5]	86		+ 1.9	− 5.1	+ 5.9	+ 3.2	+ 0.8	+ 1.4
Market growth[6]			+ 1.7	− 6.1	+ 11.0	+ 5.7	− 0.4	+ 3.2
Forecast assumptions								
Crude oil prices								
Brent, $ per barrel			64.1	43.3	70.7	98.7	84	84
Natural gas price								
Dutch TTF, € per MWh			13.6	9.5	45.9	121.5	43	52
Electricity price Austria								
Base, € per MWh			40.1	33.2	107.2	261.6	109	140
Peak, € per MWh			43.1	36.0	116.8	275.5	115	161
Exchange rate								
$ per €			1.120	1.141	1.184	1.054	1.08	1.08
Key interest rate								
ECB main refinancing rate[7], percent			0.0	0.0	0.0	0.6	3.8	4.5
10-year government bonds yields Germany, percent			− 0.3	− 0.5	− 0.4	1.1	2.5	3.9

Source: WIFO, Bureau of Economic Analysis, European Energy Exchange, Eurostat, ECB, HWWI, IMF, Intercontinental Exchange, OECD, Statistics Austria. 2023 and 2024: forecast. – [1] PPP-weighted. – [2] Czech Republic, Hungary, Poland, Slovenia, Slovakia. – [3] EU 27, UK, USA, Switzerland, China. – [4] Weighted by GDP at purchasing power parities in 2021. – [5] Weighted by shares of Austrian goods exports in 2021. – [6] Real import growth of trading partners, weighted by shares of Austrian goods exports. – [7] Minimum bid rate.

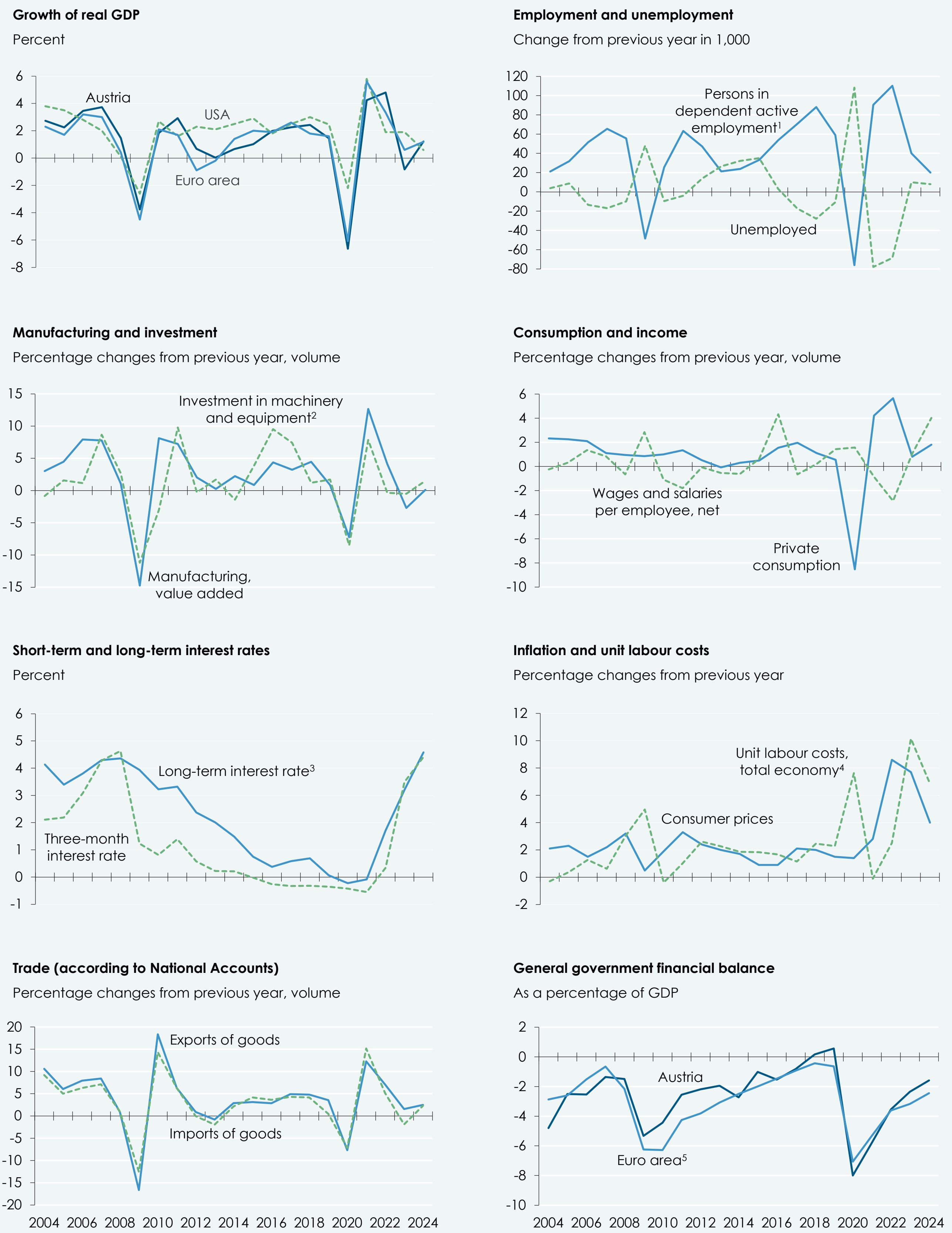
1.1 Downturn in the industrial sector intensifies

Now that the precautionary stocks have been run down, world trade and industrial production will pick up again.

The global economy is likely to grow only moderately in the coming months as industrial weakness persists and high interest rates dampen demand. In the USA, the impetus from private consumption will also subside because the savings accumulated during the pandemic have gradually been reduced and the savings rate is low by historical standards. However, the decline in inflation and its delayed reflection in wage developments will lead to significant increases in real incomes in many places, especially as the labour market remains robust. Household consumption should therefore expand more strongly again in 2024.

Now that the increased inventories have largely been reduced, demand for intermediate goods should normalise. This will stimulate global trade in goods and industrial production. On the other hand, the weak economic development in China continues to have a dampening effect. There, the crisis in the real estate sector is weighing on private household incomes due to its high importance for value added and employment. In addition, real interest rates in many countries will remain significantly higher than before the pandemic.

Figure 1: **Indicators of economic performance**



Source: WIFO. 2023 and 2024: forecast. – [1] Excluding persons in valid employment contract receiving child care benefit or being in military service, and unemployed persons in training; break in 2007-08 due to changes in the employment statistics. – [2] Including weapons systems. – [3] 10-year central government bonds (benchmark). – [4] Including short-time work grants. – [5] Source: European Commission.

Inflation is expected to continue to decline over the forecast period. In view of the high storage levels, Europe's natural gas supply is expected to be secure in the winter of 2023-24 and energy prices are not expected to spike again. Based on quotations on the futures markets, the price of natural gas should remain slightly above the current level until the end of 2024 and thus higher than before the start of the strong price surge in autumn 2021.

2. Economic policy parameters

This forecast takes into account economic policy measures that have already been adopted or sufficiently specified and whose implementation is thus considered likely.

2.1 Monetary policy remains highly restrictive

Starting in mid-2022, the European Central Bank (ECB) has raised its key interest rates several times by a total of 4.5 percentage points; the main refinancing rate has been 4.5 percent since mid-September 2023. In addition, the ECB has started to reduce the securities holdings acquired under the regular purchase programme (Asset Purchase Programme). In contrast, maturing bonds from the Pandemic Emergency Purchase Programme will be fully reinvested until at least the end of 2024 in order to counteract possible yield differentials in the euro area.

WIFO assumes that the interest rate ceiling is reached with the September 2023 increase and that the key interest rates will not be raised further. The annual average interest rate for the main refinancing operations will thus be 3.8 percent in 2023. In view of the stubbornly high inflation, key interest rate cuts are not expected until 2025, so that the key interest rate should remain unchanged at 4.5 percent in 2024 as a whole.

2.2 Budget deficit gradually declining

The general government budget deficit will continue to decline over the forecast period, starting from 3.5 percent of GDP (2022). On the revenue side, the high rates of price increases will lead to additional tax revenues. On the other hand, inflation-induced increases in public spending on intermediate consumption, wages and salaries, pensions, indexed social benefits and interest will burden the national budget. The offsetting of the fiscal drag from income tax and the reduction in corporate tax rates will lead to lower revenue dynamics over the forecast period.

Pandemic-related expenditures, which still accounted for about 1.5 percent of GDP in 2022, will largely expire. The numerous measures adopted to cushion the real income losses due to increased energy prices and high inflation (inflation-compensation measures, electricity price brake) still weigh on the budget in 2023 but will expire in 2024. There is still a high degree of uncertainty regarding the budgetary effects of the energy cost subsidies and the energy crisis contribution. Overall, WIFO expects a general government budget balance of –2.4 percent of GDP in 2023; in 2024 it will improve to –1.6 percent of GDP.

Table 3: **Fiscal and monetary policy – key figures**

	2019	2020	2021	2022	2023	2024
	As a percentage of GDP					
Fiscal policy						
General government financial balance[1]	0.6	– 8.0	– 5.8	– 3.5	– 2.4	– 1.6
General government primary balance	2.0	– 6.6	– 4.7	– 2.6	– 1.3	– 0.3
General government total revenue	49.2	48.8	50.4	49.6	49.4	49.0
General government total expenditure	48.7	56.8	56.2	53.2	51.8	50.6
	Percent					
Monetary policy						
Three-month interest rate	– 0.4	– 0.4	– 0.5	0.3	3.5	4.4
Long-term interest rate[2]	0.1	– 0.2	– 0.1	1.7	3.2	4.6

Source: WIFO, ECB, OeNB, Statistics Austria. 2023 and 2024: forecast. – [1] According to Maastricht definition. – [2] 10-year central government bonds (benchmark).

3. Business cycle pattern for Austria significantly revised

The Austrian economy suffered heavy losses in the wake of the COVID-19 pandemic but recovered strongly. Real GDP in the second quarter of 2022 was a good 3 percent above the pre-crisis level. Since then, the economy has faced strong headwinds from various directions.

Fuelled by the expansionary orientation of monetary and fiscal policy, the rapid economic recovery initially created price pressure; commodity, producer and consumer prices rose sharply and dampened the purchasing power of private households. This was exacerbated, especially in Europe, by the sharp increases in energy prices following the outbreak of the Ukraine war, with the multiplication of gas prices in particular having a negative impact on industrial production. Finally, high inflation was followed by significant key interest rate hikes by the ECB, which stabilise inflation expectations and provide economic stability in the medium term, but are weighing on economic activity.

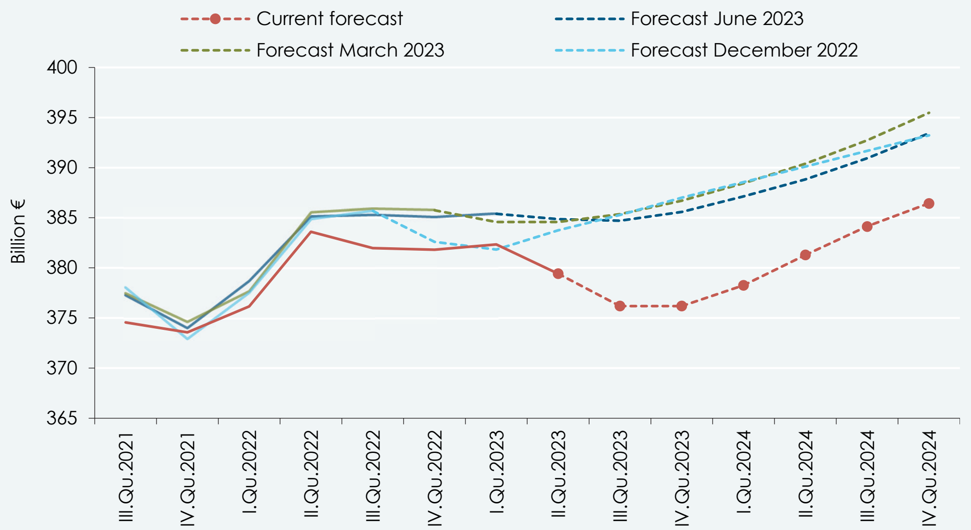
In its December 2022 forecast, WIFO therefore assumed a temporary decline in economic output, and WIFO's Flash Estimates of GDP also indicated declines from the fourth quarter of 2022 at the latest (Figure 2). In contrast, Statistics Austria's calculations in the regular quarterly accounts only showed a stagnation of economic output from spring 2022 onwards. In view of the negative real economic environment, this suggested a certain robustness of the domestic economy, which WIFO took into account in its forecasts of March and June 2023.

However, the first annual national accounts for 2022, which were compiled in September 2023, now paint a different picture of economic development, which is more in line with the earlier WIFO forecasts, the WIFO flash estimates and the results of the WIFO-Konjunkturtest (business cycle survey). According to these, the decline in value added had already started in the second half of 2022 and continued in early 2023. Although the data revision reduces the GDP forecast value for 2023 by only 0.1 percentage point, the economic picture has changed fundamentally. The domestic economy appears to be less resilient to the negative external shocks than previously assumed.

In Austria, the downturn had already started in mid-2022 and intensified in the summer half-year of 2023.

According to the leading indicators, the business cycle is expected to bottom out at the end of 2023. In 2024, domestic value added will expand again.

Figure 2: **Data revisions and forecast of real GDP**



Source: Statistics Austria, WIFO. Seasonally and calendar adjusted according to Eurostat, annualised. The solid lines show the Quarterly National Accounts figures as published and the dashed lines show the forecast based on these figures.

Table 4: **Revision of the growth forecast**

GDP, volume

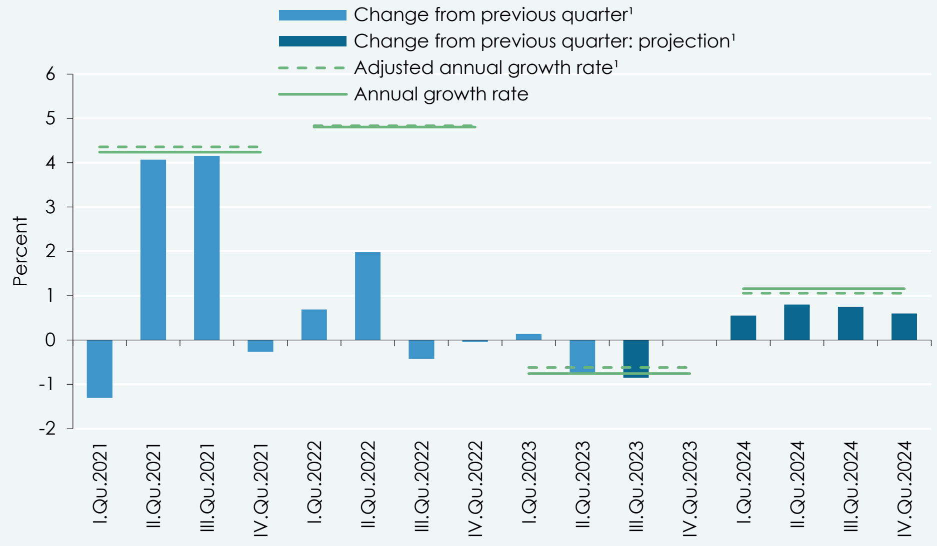
		2023	2024
WIFO Economic Outlook June 2023	percent	+ 0.3	+ 1.4
Data revisions[1]	percentage points	− 0.1	− 0.0
Forecast error for the second quarter of 2023[2]	percentage points	− 0.5	− 0.2
Forecast revision	percentage points	− 0.5	− 0.1
WIFO Economic Outlook October 2023	**percent**	**− 0.8**	**+ 1.2**

Source: WIFO. Based on seasonally and working-day adjusted values according to Eurostat. – [1] Revision of Quarterly National Accounts by Statistics Austria compared with the data available for the preparation of the June 2023 WIFO economic forecast. – [2] At the time of preparing the June 2023 WIFO economic forecast, no Statistics Austria figures had yet been published for this quarter.

According to the latest National Accounts data, economic output fell again in the second quarter of 2023, and at –0.8 percent compared to the previous quarter, it was more severe than at the beginning of the downturn in 2022. Based on the results of the WIFO-Konjunkturtest of September 2023 and a recalculation of the Weekly WIFO Economic Index, a further decline in GDP of a similar magnitude is forecast for the third quarter of 2023. As the leading indicators have not deteriorated further recently, stagnation is assumed for the fourth quarter of 2023. However, growth impulses are not expected until 2024, when real incomes rise, and global economic activity picks up.

Figure 3: **Cyclical profile of Austria**

GDP, volume



Source: WIFO. – [1] Seasonally and calendar adjusted according to Eurostat.

Table 5: **Technical breakdown of the real GDP growth forecast**

		2021	2022	2023	2024
Growth carry-over[1]	percentage points	+ 0.6	+ 2.8	+ 0.2	– 0.6
Growth rate during the year[2]	percent	+ 6.7	+ 2.2	– 1.5	+ 2.7
Annual growth rate	**percent**	+ 4.2	+ 4.8	– 0.8	+ 1.2
Adjusted annual growth rate[3]	percent	+ 4.4	+ 4.8	– 0.6	+ 1.1
Calendar effect[4]	percentage points	+ 0.1	– 0.1	– 0.1	+ 0.1

Source: WIFO. 2023 and 2024: forecast. – [1] Impact of year-earlier growth dynamics on growth in the current year. Equals the annual growth rate in the current year, if the level of GDP in the current year remains constant from the fourth quarter of the previous year; seasonally and calendar adjusted according to Eurostat. – [2] Reflects the growth dynamics during a calendar year. Equals the year-on-year growth rate for the fourth quarter; seasonally and calendar adjusted according to Eurostat. – [3] Seasonally and calendar adjusted according to Eurostat. Comparative figure to the OeNB's economic forecast. – [4] Impact of the annual number of working days and the leap day. The sum of the adjusted annual growth rate and calendar effect may differ from the value of the unadjusted annual growth rate as it also includes seasonal and irregular effects.

3.1 Services stagnate in 2023

After stagnation in services in 2023, their value added will only grow at an average pace in 2024.

In addition to the producing sector, the recession has now also hit the tertiary sector. Although some service activities are still expanding in 2023, they are doing so at a slower pace than in the previous year. This is particularly true for accommodation and food service activities, which have recovered from the slump during the pandemic and are now growing more slowly again. In the cyclically sensitive services sectors, such as trade and transportation, value added shrinks in 2023. Public services (NACE O to Q) also develop only at a subdued pace, as pandemic-related measures such as comprehensive testing have been discontinued. Overall, the tertiary sector, which accounts for a good two-thirds of value added, is expected to stagnate in 2023 and only expand again in 2024 in line with the increase in real disposable household income. However, above-average growth is not expected.

Table 6: **Gross value added**

At basic prices

	2021	2022	2023	2024	2021	2022	2023	2024
	Billion € (reference year 2015)				Percentage changes from previous year			
Volume (chain-linked series)								
Agriculture, forestry and fishing	4.10	4.37	4.11	4.11	+ 6.4	+ 6.6	– 6.0	± 0.0
Manufacturing including mining and quarrying	69.17	72.17	70.22	70.29	+ 12.6	+ 4.3	– 2.7	+ 0.1
Electricity, gas and water supply, waste management	9.77	9.98	10.13	10.25	+ 0.2	+ 2.2	+ 1.5	+ 1.2
Construction	19.13	18.90	18.42	17.72	– 1.1	– 1.2	– 2.5	– 3.8
Wholesale and retail trade	38.63	39.45	38.27	38.99	– 1.1	+ 2.1	– 3.0	+ 1.9
Transportation	16.42	18.21	17.30	17.73	– 0.2	+ 10.9	– 5.0	+ 2.5
Accommodation and food service activities	8.35	12.97	13.49	13.69	– 14.2	+ 55.3	+ 4.0	+ 1.5
Information and communication	13.91	14.30	14.58	14.95	+ 5.9	+ 2.8	+ 2.0	+ 2.5
Financial and insurance activities	16.04	15.85	16.59	17.31	+ 3.1	– 1.2	+ 4.7	+ 4.3
Real estate activities	31.20	31.88	32.04	32.52	+ 0.5	+ 2.2	+ 0.5	+ 1.5
Other business activities[1]	33.11	34.37	34.75	35.48	+ 5.0	+ 3.8	+ 1.1	+ 2.1
Public administration[2]	56.45	58.22	58.34	58.92	+ 4.8	+ 3.1	+ 0.2	+ 1.0
Other service activities[3]	7.51	8.93	9.42	9.61	+ 1.3	+ 18.9	+ 5.5	+ 2.0
Total gross value added[4]	322.42	339.09	337.16	340.82	+ 3.5	+ 5.2	– 0.6	+ 1.1
Gross domestic product at market prices	363.11	380.56	377.41	382.01	+ 4.2	+ 4.8	– 0.8	+ 1.2

Source: WIFO, Statistics Austria. 2023 and 2024: forecast. – [1] Professional, scientific and technical activities; administrative and support service activities (NACE M and N). – [2] Including defence, compulsory social security, education, human health and social work activities (NACE O to Q). – [3] Arts, entertainment and recreation; other service activities; activities of households (NACE R to U). – [4] Before deduction of subsidies and attribution of taxes on products.

3.2 Producing sector shrinks for two years in a row

The producing sector (industry and construction), on the other hand, is shrinking – and not just in 2023, but in all likelihood also in the coming year. The first intra-year decline in the producing sector already occurred in 2022 due to the massive energy price shocks that hit Europe in the wake of the Russian war of aggression against Ukraine. However, a good first half of the year still ensured positive overall annual growth rates in 2022. The recession continues in 2023, not least because of the ECB's sharp increases in key interest rates, which have made financing new projects much more expensive. They hit construction in particular and especially residential construction. Since monetary tightening is only gradually taking effect, the decline in value added in construction will intensify in 2024, while stagnation is expected for industry.

The pessimistic outlook is supported by the results of the WIFO-Konjunkturtest. The WIFO Business Climate Index, which summarises companies' assessments of the current situation and their expectations, declined in September for the fifth time in a row in manufacturing. In the last 25 years, sentiment was only worse during the 2008-09 recession and the first COVID-19 wave in spring 2020. Following the downturn in the intermediate goods sectors, sentiment has also recently deteriorated in the capital goods sectors. In September, however, the decline was mainly due to assessments of the current situation, while expectations stabilised at a low level. Based on the assumption that the international economic activity will improve in 2024, WIFO forecasts further losses in manufacturing value added until the end of 2023, but a stabilisation or slight recovery in the course of the coming year. For 2024 as a whole, this results in a stagnation of value added in manufacturing.

As in Europe as a whole, domestic industry is also contracting in the face of energy price shocks and sharp interest rate increases.

In construction, the indicators of the WIFO-Konjunkturtest have recently developed similarly to those in manufacturing. However, a bottoming out in construction is less likely than in industry. Currently, residential construction in particular is suffering heavy losses, which is not surprising: the demand for real estate is particularly interest-elastic, as debt financing via mortgage loans plays an important role. The slump in residential construction is thus a direct consequence of the sharp rise in key interest rates. Growth impulses from other segments, such as civil engineering or renovation, are still counteracting this. However, the decline in new residential construction will gradually spill over to other parts of the construction sector, especially the construction-related industries, leading to even greater losses in value added in 2024.

The industrial sector reaches a trough at the end of 2023. In construction, the recession continues in 2024.

3.3 Employment dynamics defy the recession

In view of the weak business cycle, the domestic labour market is proving to be very robust. Despite the decline in value added, employment will be higher on average in 2023 than in 2022. The increase is due to a pronounced statistical overhang, i.e., the fact that the growth during the year was still very strong at the end of 2022. According to the seasonally adjusted data, which are particularly prone to revision at the current margin, employment growth has weakened since the beginning of 2023. Stagnation is expected for the rest of the year, with slight increases again from 2024 onwards.

"Labour hoarding" and lower hours worked per capita ensure high employment levels despite the recession.

The strong employment gains until the beginning of 2023 can only partly be explained by the delayed effect of the business cycle on the labour market, especially since they lasted for an unusually long time. They are probably also a consequence of the high demand for personnel generated by the abrupt resumption of economic activity after the pandemic. According to the WIFO-Konjunkturtest, reports of shortages of labour force as the most important obstacle to production reached record levels in all sectors until recently. The number of vacancies, a pro-cyclical economic indicator, has been falling sharply since the beginning of 2023. However, it seems that even in a weaker business cycle, the staffing needs of many companies were still high enough to make further hiring worthwhile.

Table 7: **Labour market**

	2019	2020	2021	2022	2023	2024
	Change from previous year in 1,000					
Demand for labour						
Persons in active employment[1]	+ 61.4	− 76.6	+ 96.9	+ 115.6	+ 43.0	+ 23.0
Employees[1,2]	+ 58.9	− 76.1	+ 90.4	+ 110.2	+ 40.0	+ 20.0
National employees	+ 12.3	− 53.9	+ 28.1	+ 22.9	− 10.0	− 5.0
Foreign employees	+ 46.6	− 22.2	+ 62.4	+ 87.4	+ 50.0	+ 25.0
Self-employed[3]	+ 2.5	− 0.5	+ 6.5	+ 5.4	+ 3.0	+ 3.0
Labour supply						
Population of working age						
15 to 64 years	+ 11.4	+ 9.9	+ 5.4	+ 48.6	+ 13.0	+ 2.6
Labour force[4]	+ 50.6	+ 31.7	+ 19.0	+ 47.0	+ 53.0	+ 31.0
Labour surplus						
Unemployed[5]	− 10.8	+ 108.3	− 77.9	− 68.6	+ 10.0	+ 8.0
Unemployed persons in training	− 6.8	− 4.9	+ 13.2	− 0.8	− 1.0	− 3.0
	Percent					
Unemployment rate						
As a percentage of total labour force (Eurostat)[6]	4.8	6.0	6.2	4.8	5.2	5.2
As a percentage of total labour force[5]	6.6	8.9	7.2	5.6	5.8	5.9
As a percentage of dependent labour force[5]	7.4	9.9	8.0	6.3	6.5	6.6
	Percentage changes from previous year					
Labour force[4]	+ 1.1	+ 0.7	+ 0.4	+ 1.0	+ 1.1	+ 0.7
Persons in active dependent employment[1,2]	+ 1.6	− 2.0	+ 2.5	+ 3.0	+ 1.0	+ 0.5
Unemployed[5]	− 3.5	+ 35.9	− 19.0	− 20.7	+ 3.8	+ 2.9
Persons (in 1,000)	301.3	409.6	331.7	263.1	273.1	281.1

Source: WIFO, Eurostat, Federation of Social Insurances, Public Employment Service Austria, Statistics Austria. 2023 and 2024: forecast. – [1] Excluding persons in valid employment contract receiving child care benefit or being in military service. – [2] According to the Federation of Social Insurances. – [3] According to WIFO, including liberal professions and unpaid family workers. – [4] Persons in active employment plus unemployed. – [5] According to Public Employment Service Austria. – [6] Labour Force Survey. Due to a revision of the Labour Force Survey methodology planned for the end of June, a forecast of this indicator is currently waived.

The robustness of the labour market is not a purely Austrian phenomenon but can also be observed in other countries. Another reason for this, which is also related to the COVID-19 crisis, is a kind of learning effect: the high demand for labour during the upswing was preceded by layoffs during the crisis. Companies may now increasingly resort to "labour hoarding" if this is more favourable from their point of view than the costly and lengthy search for suitable new workers in the next upswing.

Despite the large increase in job vacancies and the increased importance of labour shortages, the 2021-22 recovery was highly employment-intensive. Conversely, hours worked per capita have decreased significantly since the pandemic, which explains part of the strong employment expansion. Until 2022, the reduction in hours per capita was compensated by the increase in employment, and hourly productivity followed its longer-term upward trend. In 2023 and 2024, productivity growth will weaken due to labour hoarding, while hours worked per capita will continue to decline.

Table 8: **Productivity**

	2019	2020	2021	2022	2023	2024
	Percentage changes from previous year					
Total economy						
Real GDP	+ 1.5	− 6.6	+ 4.2	+ 4.8	− 0.8	+ 1.2
Hours worked[1]	+ 1.6	− 8.7	+ 4.7	+ 2.5	+ 0.5	+ 0.5
Productivity[2]	− 0.1	+ 2.3	− 0.5	+ 2.3	− 1.3	+ 0.7
Employment[3]	+ 1.3	− 1.9	+ 2.4	+ 2.8	+ 0.9	+ 0.6
Manufacturing						
Production[4]	+ 0.8	− 7.3	+12.7	+ 4.1	− 2.7	+ 0.1
Hours worked[5]	+ 0.9	− 5.9	+ 5.0	+ 0.6	− 0.0	± 0.0
Productivity[2]	− 0.1	− 1.4	+ 7.3	+ 3.5	− 2.7	+ 0.1
Employees[6]	+ 1.7	− 1.0	+ 0.4	+ 1.3	+ 1.0	± 0.0

Source: WIFO, Statistics Austria. 2023 and 2024: forecast. – [1] Total hours worked by persons employed, National Accounts definition. – [2] Production per hour worked. – [3] Employees and self-employed, National Accounts definition (jobs). – [4] Gross value added, volume. – [5] Total hours worked by employees. – [6] National Accounts definition (jobs).

In addition to the demand for labour, unemployment is also determined by supply. On the supply side, different impulses will have an effect in the forecast period. On the one hand, the integration of refugees into the labour market will increase labour supply. In particular, people from Ukraine, Syria and Afghanistan will be much more present on the domestic labour market, both as employees and as unemployed. On the other hand, the domestic labour force is shrinking. In 2022, for the first time, not only the 15 to 24 and 25 to 49 age cohorts declined, but also the 50 to 64 age cohort. Conversely, the employment rate of older persons will continue to increase as cohorts with higher levels of formal education will follow and as the statutory retirement age for women will gradually increase from 2024. Overall, impulses that increase the labour supply will dominate over the forecast period, so that not only employment but also unemployment will rise.

The economic downturn and the simultaneous expansion of labour supply are causing unemployment to rise.

3.4 Real wage loss is compensated

The continuing need for skilled labour strengthens the trade unions' position in wage negotiations. The good liquidity situation due to inflation also allows many companies to increase wages accordingly. After expanding by a good 8½ percent in 2022, operating surpluses are also expected to increase by 5 percent in 2023 despite the recession. This strong increase, which is unusual for a downturn phase, is made possible by the strong price increases.

For the forecast period, WIFO expects wage settlements to be in line with the respective rolling inflation, i.e., the arithmetic mean of the inflation rates of the past twelve months (according to the CPI). As a result, gross wages per capita will grow at a similar rate in 2024 as in 2023 and will be about 22 percent higher in 2024 than in 2021, when the inflationary push began (CPI 2021-2024: about +22 percent).

Despite this lagged synchronisation of consumer prices and per capita wages, the adjusted wage share jumps in 2024 because national income does not grow at the same rate as compensation of employees. The main reason for this is the loss of wealth due to imported inflation, which is statistically reflected in a deterioration of the terms-of-trade. In 2023 and 2024, the terms-of-trade improve again, but less markedly than they had deteriorated in 2022. Key imported commodities such as natural gas and crude oil will remain more expensive in the medium term than before 2021, so while employees should be able to compensate for the loss of real wages, their share of national income will also increase because it has been reduced by the payments to the crude oil and natural gas producing countries. Accordingly, the corporate operating surpluses are likely to fall in 2024 for the first time since the recession in 2009.

By compensating for real wage losses, the wage share increases, as national income growth has also been reduced by income transfers to commodity-exporting countries.

3.5 Private consumption supports the economy

In addition to wage income, pension income and other monetary social benefits will also increase significantly in value again in 2024 due to the delayed adjustment to inflation. Household consumption will therefore grow more strongly in 2024 than in the previous year, but less dynamically than real disposable income, as the worsening labour market situation, especially the higher risk of job loss, will dampen consumer sentiment.

Public consumption is dampened by the discontinuation of pandemic-related services.

Despite lower growth, private consumption is already the mainstay of the economy in 2023. Purchases of durable consumer goods, which account for about one tenth of private household consumption, are expected to decline – probably an after-effect of the pandemic-related boom. But demand for non-durable consumer goods and services will grow at an average rate in 2023. The cyclically stabilising smoothing of consumption reduces the household savings ratio in 2023 and causes it to rise again in the following year. Public consumption shrinks over the forecast period as pandemic-related services, especially comprehensive testing, are eliminated.

Table 9: **Earnings, international competitiveness**

	2019	2020	2021	2022	2023	2024
	Percentage changes from previous year					
Wages and salaries per employee[1]						
Nominal, gross	+ 2.9	+ 2.2	+ 2.7	+ 4.7	+ 8.2	+ 7.6
Real[2]						
Gross	+ 1.3	+ 0.8	– 0.1	– 3.6	+ 0.5	+ 3.5
Net	+ 1.4	+ 1.6	– 0.9	– 2.9	+ 1.1	+ 4.0
Wages and salaries per hour worked[1]						
Real, net[2]	+ 0.9	+ 9.5	– 3.9	– 2.6	+ 1.6	+ 4.0
	Percent					
Wage share, adjusted[3]	69.6	69.3	68.3	69.8	70.6	73.3
	Percentage changes from previous year					
Unit labour costs, nominal[4]						
Total economy	+ 2.3	+ 7.6	– 0.1	+ 2.5	+10.2	+ 6.8
Manufacturing	+ 3.4	+ 6.2	– 7.6	+ 2.2	+11.5	+ 7.9
Effective exchange rate – manufactured goods[5]						
Nominal	– 0.7	+ 1.4	+ 0.6	– 1.5	+ 2.3	+ 0.5
Real	– 1.1	+ 1.7	+ 0.2	– 1.7	+ 3.4	+ 0.9

Source: WIFO, Statistics Austria. 2023 and 2024: forecast. – [1] National Accounts definition. – [2] Deflated by CPI. – [3] Compensation of employees as a percentage of national income, adjusted for the change in the share of employees in total employment from base year 1995. – [4] Labour costs in relation to productivity (hourly compensation per employees divided by GDP and value added, respectively, per employed persons' hours worked), including short-time work grants. – [5] Weighted by exports and imports, real value adjusted by relative HCPI.

Table 10: **Private consumption, income and prices**

	2019	2020	2021	2022	2023	2024
	Percentage changes from previous year					
Private consumption expenditure[1]	+ 0.5	– 8.5	+ 4.2	+ 5.7	+ 0.8	+ 1.8
Durable goods	+ 0.6	– 2.6	+ 3.7	– 0.3	– 3.6	+ 2.0
Non-durable goods and services	+ 0.5	– 9.2	+ 4.3	+ 6.3	+ 1.3	+ 1.8
Private household disposable income	+ 0.8	– 2.8	+ 1.8	+ 3.3	+ 0.1	+ 2.8
	As a percentage of disposable income					
Household saving ratio						
Including adjustment for the change in pension entitlements	7.9	13.2	11.2	9.2	8.4	9.3
Excluding adjustment for the change in pension entitlements	7.2	12.7	10.6	8.5	7.9	8.8
	Percentage changes from previous year					
Loans to domestic non-banks (end of period)	+ 4.2	+ 3.7	+ 6.6	+ 5.0	+ 1.0	+ 2.4
Consumer prices						
National	+ 1.5	+ 1.4	+ 2.8	+ 8.6	+ 7.7	+ 4.0
Harmonised	+ 1.5	+ 1.4	+ 2.8	+ 8.6	+ 7.5	+ 3.7
Core inflation[2]	+ 1.7	+ 2.0	+ 2.3	+ 5.1	+ 7.7	+ 5.1

Source: WIFO, OeNB, Statistics Austria. 2023 and 2024: forecast. The values for private household disposable income and the saving rate have been changed since the publication of the economic forecast on 7 October 2022 due to adjustments in the accounting of the climate bonus. – [1] Private households including non-profit institutions serving households. – [2] Excluding energy, food, alcohol and tobacco.

3.6 Foreign trade still robust

The increase in consumer prices peaked in 2022. In the most important trading partners (weighted by the export shares of manufactured goods), the price increase was still somewhat stronger than in Austria; it was particularly high in the Czech Republic, Hungary and Poland. In 2023, however, the price increase is stronger in Austria than in the partner countries. Although inflation rates are still higher in the Central Eastern European countries, price increases in the more important target markets Germany, the USA and Italy are declining more rapidly than in Austria. In 2024, the inflation gap narrows.

In addition to the positive inflation differential, the appreciation of the euro over the forecast period also causes the real effective exchange rate to rise. The resulting deterioration in price competitiveness reduces corporate profits in particular. However, an impact on exports is not yet foreseeable. Foreign tourist arrivals have fully recovered from the pandemic-related slump. Even exports of goods will increase in 2023, mainly thanks to strong exports of machinery to Germany and the USA. This will result in slight market share gains in 2023. However, according to the WIFO-Konjunkturtest, companies report a decline in export orders. Accordingly, exports of goods are likely to expand more slowly than the weighted imports of trading partners in 2024.

In 2023, domestic price increases are significantly higher than in Austria's main trading partners. The inflation gap narrows in 2024.

Table 11: **Expenditure on GDP**
Volume (chain-linked series)

	2021	2022	2023	2024	2021	2022	2023	2024
	Billion € (reference year 2015)				Percentage changes from previous year			
Final consumption expenditure	258.77	269.00	268.99	272.47	+ 5.2	+ 4.0	– 0.0	+ 1.3
Households[1]	181.98	192.28	193.82	197.31	+ 4.2	+ 5.7	+ 0.8	+ 1.8
General government	76.71	76.73	75.20	75.20	+ 7.5	+ 0.0	– 2.0	± 0.0
Gross capital formation	98.77	98.08	94.03	94.51	+ 10.8	– 0.7	– 4.1	+ 0.5
Gross fixed capital formation	92.91	93.02	92.57	92.15	+ 6.1	+ 0.1	– 0.5	– 0.5
Machinery and equipment[2]	29.89	29.78	29.63	30.08	+ 7.9	– 0.4	– 0.5	+ 1.5
Construction	40.31	39.49	38.43	36.85	+ 1.8	– 2.0	– 2.7	– 4.1
Other investment[3]	22.77	23.90	24.85	25.85	+ 12.6	+ 5.0	+ 4.0	+ 4.0
Domestic demand	357.00	367.39	362.07	366.46	+ 6.7	+ 2.9	– 1.4	+ 1.2
Exports	210.94	234.54	238.24	244.52	+ 9.1	+ 11.2	+ 1.6	+ 2.6
Travel	6.68	13.11	14.37	14.82	– 28.6	+ 96.2	+ 9.6	+ 3.1
Minus imports	205.56	221.75	223.06	228.98	+ 14.3	+ 7.9	+ 0.6	+ 2.7
Travel	5.23	8.21	8.90	9.05	+ 56.7	+ 57.0	+ 8.4	+ 1.7
Gross domestic product	363.11	380.56	377.41	382.01	+ 4.2	+ 4.8	– 0.8	+ 1.2
Value	405.24	447.22	479.15	505.33	+ 6.4	+ 10.4	+ 7.1	+ 5.5

Source: WIFO, Statistics Austria. 2023 and 2024: forecast. – [1] Including non-profit institutions serving households. – [2] Including weapon systems. – [3] Mainly intellectual property products (research and development, computer programmes, copyrights).

4. Forecast risks

In manufacturing, the disruption of supply chains during the pandemic led to material shortages and subsequently to precautionary stockpiling, i.e., to even higher demand. Analogously, the large number of new hires in the services sector with simultaneous reporting of further vacancies could be the result of a "labour hoarding" strategy by companies in response to the difficulties in recruiting after the pandemic. Potentially "surplus" staff may also be kept in the company in order to avoid losing skilled workers to the competitors. However, if the expected costs of labour hoarding exceed those of staff recruitment, this could lead to a reduction in employment. There is no evidence of this scenario yet, but it is a key forecasting risk.

An increased risk for the global economy is currently emanating from China, where high levels of corporate and household debt are burdening the construction industry. China's economic weakness has recently also been reflected in falling price levels, which – similar to Japan for a long time – could further dampen demand if a decline in income also sets in.

Risks are still posed by a further escalation of the Ukraine war. In combination with an unusually cold winter, gas supplies in Europe could dwindle rapidly, especially since significant quantities of natural gas and crude oil are still imported from Russia. A shortage could trigger renewed price increases for natural gas and fuel inflation.

Conversely, a faster decline in inflation than assumed in the forecast would give central banks room to lower key interest rates earlier. This would be associated with positive impulses for the global economy.

In Austria, the upcoming National Council elections increase the risk of new fiscal policy measures, that could support the economic activity but also fuel inflation and thus counteract monetary policy.