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Austrian Economy Experiencing Upswing

Business Cycle Report of August 2010

The improvement in global economic conditions has now also taken full hold of the Austrian economy. Goods exports expanded at an extremely vigorous pace in the second quarter. As a consequence, industrial production surged, and capacity utilisation continued to head toward its long-term average. The labour market also continues to show an upward trend.

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Economic growth accelerated markedly in the second quarter (+0.9 percent in real terms, quarter-on-quarter, first quarter ±0 percent). Notably brisk external demand stimulated production. In April and May, the value of goods exports rose by more than 10 percent each, compared with a year before. Industrial production surged by a similar amount, with the production index (including energy) rising by 7 and 10 percent, respectively, in the two months.

Global trade is the main driver of growth; the German economy, like Austria's, is benefiting considerably from it, exports and industrial production are expanding at a vigorous pace. According to the most recent economic survey in Germany, not only the assessment of current business conditions has improved, but firms have unexpectedly also become clearly more upbeat again about their future outlook. Hence the upward trend is expected to last at least until the autumn of 2010.

The economy overseas, by contrast, has recently lost momentum. In the USA, growth continued to slow in the second quarter of 2010, GDP expanding by 0.6 percent, after +1.2 percent in the fourth quarter of 2009 and +0.9 percent in the first quarter of 2010. Unemployment is hardly falling, in spite of an expansion of production. Business and household surveys point to a further slackening of economic growth in the months to come.

Austria's construction sector continues to fare badly; according to economic survey data and national accounts, production declined yet again in the second quarter. The evidence presented in business surveys does not suggest an improvement in the coming months.

The easing in the labour market observed in recent months continues. In July, employment expanded yet again (persons in active dependent employment +47,200, year-on-year, and +0.2 percent, month-on-month), and unemployment fell once more (–18,200, year-on-year). The seasonally adjusted unemployment rate according to the Austrian method of calculation stood at 6.8 percent in July.

Economic activity losing momentum in the USA and in Asia

The US economy grew at a quarterly rate of 0.6 percent in the second quarter of 2010, a decline from the pace of growth recorded in the first quarter (+0.9 percent; fourth quarter of 2009 +1.2 percent). Demand still expanded vigorously in the second quarter, but was increasingly met by imports. The latter rose by 6.5 percent from the previous quarter, after +2.7 percent in real terms in the first quarter. Private household consumption increased by 0.4 percent compared with the previous quarter, only slightly less than in the first quarter (+0.5 percent). Private investment demand (including inventories), which had surged in the fourth quarter of 2009, continued to pick up markedly (around +6 percent in real terms) also in the second quarter of 2010. The focus shifted from inventory investment to equipment – equipment investment rose by +5.1 percent in real terms quarter-on-quarter, the strongest increase seen in years. Residential investment also expanded by more than 6 percent. Investment in non-residential construction rose again for the first time in two years (+1.3 percent).

While the European economy is experiencing brisk growth, the expansion overseas is slowing.

Table 1: Flash estimates of quarterly national accounts

	2009				2010	
	First quarter	Second quarter	Third quarter	Fourth quarter	First quarter	Second quarter
	Adjusted for seasonal and working day effects, percentage changes from previous quarter, volume					
GDP, expenditure approach						
Final consumption expenditure						
Households[1]	+ 0.3	+ 0.4	+ 0.3	+ 0.2	+ 0.2	+ 0.2
General government	− 1.6	+ 0.2	+ 1.3	− 0.5	+ 0.2	+ 0.2
Gross capital formation	− 5.3	− 4.1	− 0.7	− 0.5	+ 0.4	− 0.2
Gross fixed capital formation	− 4.4	− 1.8	− 0.3	− 1.2	− 2.0	− 0.9
Exports	− 6.5	− 3.2	+ 1.7	+ 2.1	+ 1.0	+ 2.2
Imports	− 5.8	− 2.7	+ 1.0	+ 0.8	+ 1.0	+ 0.4
Gross domestic product	− 2.3	− 0.8	+ 0.6	+ 0.4	− 0.0	+ 0.9
GDP, output approach						
Agriculture, forestry	− 2.3	− 1.9	+ 0.4	+ 1.1	+ 0.1	− 0.2
Industry, including energy	− 8.2	− 2.6	+ 1.0	+ 0.6	− 0.5	+ 2.7
Manufacturing	− 9.6	− 2.5	+ 2.3	+ 0.9	− 0.4	+ 3.0
Construction	− 1.2	− 1.2	− 1.3	− 1.2	− 1.0	− 0.6
Wholesale and retail trade; repairs; hotels and restaurants; transport, communication	− 1.1	− 0.6	− 0.1	+ 0.0	− 0.1	+ 0.5
Financial intermediation; real estate, renting and business activities	− 0.3	− 0.1	+ 0.4	+ 0.8	+ 0.7	+ 0.7
Other service activities	− 0.4	− 0.1	+ 0.3	+ 0.4	+ 0.5	+ 0.6
Taxes on products	− 0.2	+ 0.3	+ 0.9	+ 0.5	− 0.3	− 0.1
Subsidies on products	+ 0.1	+ 0.4	+ 0.8	+ 1.1	+ 1.4	+ 1.1
	Percentage change from previous year					
Gross domestic product, volume	− 5.4	− 5.7	− 3.6	− 0.9	+ 0.0	+ 1.9

Source: WIFO. – [1] Including private non-profit institutions serving households.

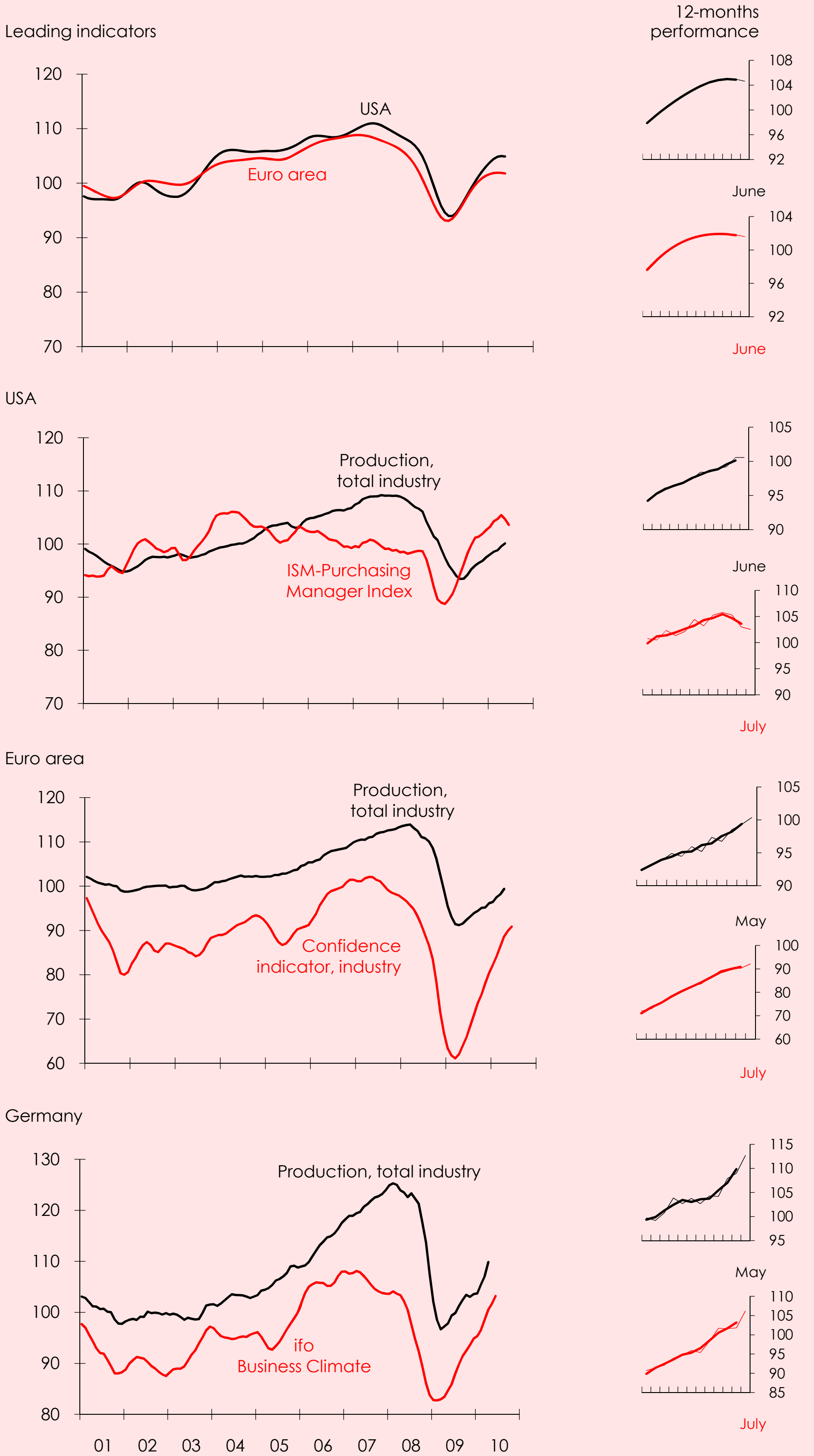
While investment demand is trending up, signs are mounting that growth is slowing again. For instance, in spite of the strong economic recovery, unemployment has not fallen accordingly to date. The close connection with business cycle dynamics observed in the past appears to be decoupling, as the latest labour market data show: in June 2010, the unemployment rate stood at 9.5 percent, only 0.6 percentage points below the peak level of 10.1 percent reached in October 2009. The current expansion of investment will pay off for companies only if private household consumption – the main driver of the US economy – remains resilient. The government transfers to support household incomes have expired, and in coming years it will become necessary also for the USA to take budget consolidation measures. Should the labour market not have recovered by then, this could be a major strain on the US economy.

At present, household surveys rather show a gradual weakening in consumer sentiment. The Consumer Confidence Index, for example, continued to fall in July after plummeting already in June. Similarly, the Consumer Sentiment Index declined yet again in July, reaching its lowest level since November 2009. The ISM Purchasing Managers' Index, an indicator of production developments in coming months, also fell further in June and July, pointing to a weakening in economic activities.

China's economy also lost some momentum in the second quarter. Following real growth of almost +12 percent year-on-year in the first quarter, the pace of expansion slowed to around +10 percent in the second quarter. Specific economic policy measures are being taken to dampen the strong momentum in some sectors.

Figure 1: International business climate

Seasonally adjusted, 2000 = 100, 3-month moving average



Source: European Commission, Deutsche Bundesbank, ISM (Institute for Supply Management™), ifo (Institute for Economic Research, Munich), OECD.

For Japan, no data are yet available on economic growth in the second quarter. The fourth quarter of 2009 and the first quarter of 2010 saw real GDP expand at the extremely brisk quarterly pace of +1 percent or more. The economy is assumed to have still grown significantly also in the second quarter. In June the Industrial Production Index fell for the first time in four months, though. However, the Bank of Japan's quarterly Tankan business survey conducted in June did not suggest a deterioration in the manufacturing sector in the coming months.

International demand strengthening EU economy

The recovery in the EU has been rather disappointing until now. But the economy is likely to have gained considerable momentum in the second quarter.

While other regions experienced a marked rebound in economic activity once they had overcome the crisis, the EU economy expanded by just approximately ¼ percent in each of the past three quarters. Now the first strong signs of an acceleration of growth are emerging: the Industrial Production Index has been rising briskly since March 2010 (including energy; May +1.0 percent, month-on-month), foreign trade has picked up markedly (May exports to non-EU countries +25 percent, year-on-year, and just under +1 percent on a month-on-month basis).

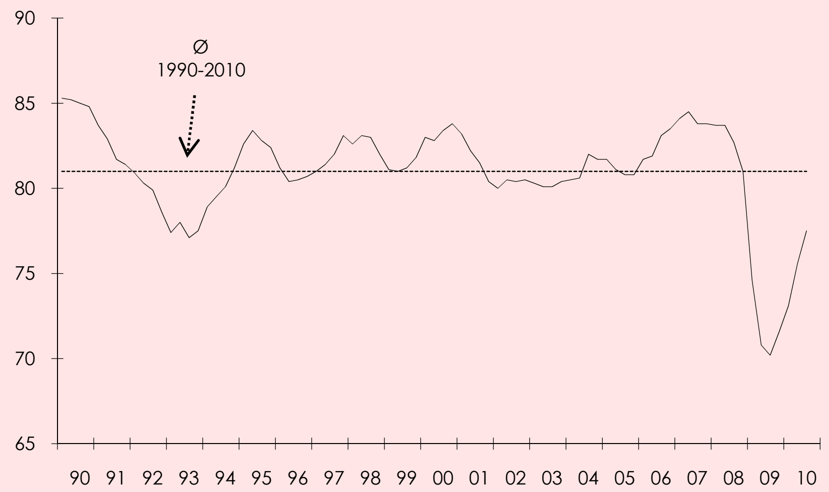
A considerable improvement has lately been noticeable in those EU countries that do not belong to the euro area and had been particularly severely affected by the crisis. Hungary recorded a month-on-month expansion of industrial production of 5.4 percent in May. These are the first tendencies towards a revival after several years not only of weak international demand but equally weak domestic economic activity. The decline in GDP that had lasted for 1½ year came to a halt at the end of 2009, and the first quarter of 2010 saw real GDP advance already by 0.9 percent quarter-on-quarter. Poland, the largest economy among the new EU countries, also saw industrial production rise briskly in May (+3.4 percent, month-on-month).

The Economic Sentiment Indicator for the EU 27 published by the European Commission rose above its long-term average in July 2010. This can be largely attributed to the improvement in sentiment in industry; by contrast, the assessment given by construction firms still remains well below average and is improving only very hesitantly. The sub-index for consumer confidence had risen markedly in the second and third quarters of 2009, but has been stagnant since then.

The capacity utilisation rate of the surveyed companies is quickly approaching its long-term average, though at present it is still as low as at the trough of the crisis of 1993 (Figure 2).

Figure 2: EU 27: Capacity utilisation in manufacturing industry

Percent



Source: European Commission business cycle survey. Following the change to NACE rev. 2 data classification in May 2010, caution should be exercised for comparison with earlier data.

The German economy is currently the driver of economic activity in the euro area.

The German economy is currently the driving force in the euro area. Industrial production (including energy) rose by 2.9 percent month-on-month in May 2010, following a rise of 2.6 percent already in March and 1.1 percent in April. The strong demand for German products is concentrated abroad.

As early as in February 2010 goods exports exceeded the year-earlier level by around 9 percent, followed by 22 percent in March, 18 percent in April and just under 30 percent in May. Hence in May 2010 the value of German exports almost reached the level prevailing in May 2008, prior to the outbreak of the crisis. A sizeable acceleration is noticeable also in month-on-month terms.

In April (latest available data on regional structure), the strongest rise was seen in German exports to Asia (+32 percent, China +47 percent) and to America (+23 percent, USA only +11.5 percent).

Developments in the labour market have also been more positive in Germany than elsewhere in the EU. Notwithstanding the economic crisis, the unemployment rate rose by just an average 0.2 percentage points in 2009, and the seasonally adjusted number of unemployed has been falling since the end of 2009. In June 2010, the unemployment rate was 7.0 percent, down from 7.7 percent in June 2009. Apparently the labour market policy measures did not cause a considerable backlog of unemployed persons and must therefore be regarded as a success. Germany now has the sixth lowest unemployment rate in the EU.

Austrian economy grows briskly thanks to strong export demand

Goods exports picked up markedly in April 2010. The trade with third countries developed more favourably than the intra-EU trade. As a result, industrial production is also growing briskly.

In the first quarter, industrial production in Austria still expanded at a much slower pace (including mining and energy +0.6 percent from the previous quarter) than the average recorded for the euro area and the EU. Business survey results had also suggested a better performance. It was not until April 2010 that production accelerated (+1.6 percent, May +2.0 percent; euro area +0.8 and +1.0 percent, respectively, EU +0.4 and +1.2 percent, respectively), supported by strong foreign demand, which stimulated the external trade in goods. Goods exports, which in the first quarter had exceeded the year-earlier level by a mere 5 percent, rose by 13.6 percent in April. A particularly strong increase was seen in April in exports to Asia (+21.5 percent) and America (+28.3 percent). Unlike Germany, Austria registered an increase in goods exports notably to the USA (+32.0 percent).

As a consequence, Austria's real GDP advanced at a quarterly rate of 0.9 percent in the second quarter, after stagnating at the beginning of the year. WIFO's July business cycle survey conducted on behalf of the EU suggests that the upward trend will persist in the months to come, although the momentum is expected to weaken somewhat relative to the second quarter. Capacity utilisation in manufacturing again reached 81.5 percent, the average for the last five years, which was of course depressed owing to the years of crisis.

In the WIFO business cycle survey, firms in the business services sector gave quite a similar assessment of future business conditions as manufacturers: after the assessment of current and future business conditions had improved considerably, the upward trend flattened in the most recent survey.

No end to crisis in construction

Austria's construction sector has not yet overcome the crisis. Production declined once more in the second quarter (–0.6 percent in real terms from the previous quarter). At present firms do not anticipate a rebound in the near future.

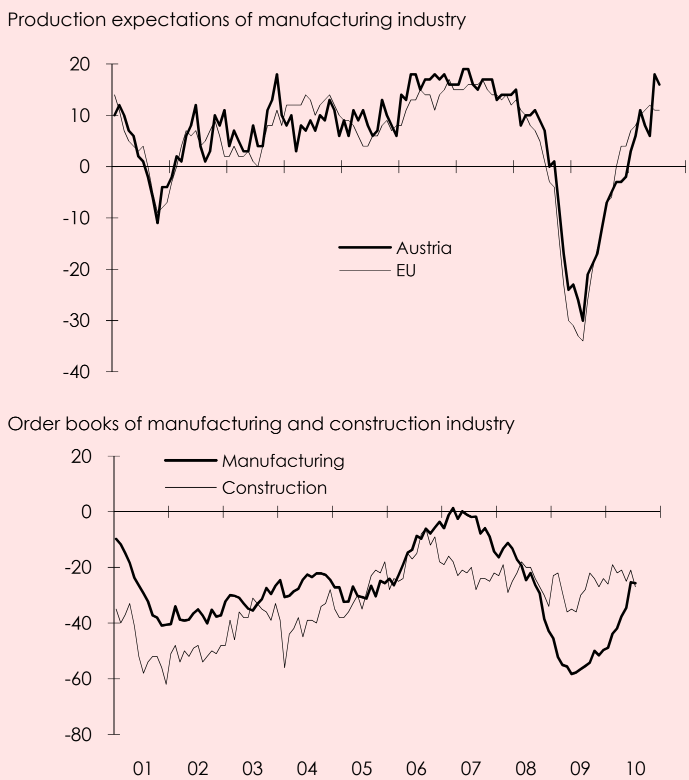
In the second quarter, construction output fell by 0.6 percent from the previous quarter, according to WIFO's quarterly national accounts data. This was the twelfth decline in a row. Hence this sector has been affected considerably longer by the crisis than the extremely cyclically sensitive manufacturing sector, while in the past, as the object of economic policy measures, it had rather had a stabilising effect on the economy. In the most recent crisis the construction sector lacked this function altogether, it collapsed simultaneously with manufacturing.

Public sector demand for civil engineering services was quite subdued during the 2006-07 boom. In 2008, the first year of the crisis, however, the public sector vigorously expanded notably road construction projects, and thus acted counter-cyclically. In 2009, when the crisis reached its peak, investments had to be reduced, though.

In building construction, by contrast, the government acted pro-cyclically in 2006-07. Similar to the private sector, it expanded the extent of the projects considerably. 2008 saw a decline in the number of building permits in the private sector, less on account of the recession but rather because of a counter-reaction to the preceding boom. Private demand for building construction did not collapse until 2009, while public investment had dropped sharply already in 2008. The expansion of public civil engineering projects in 2009 in the face of the economic crisis was not able to offset the drop in private demand.

Figure 3: WIFO business cycle survey

Differences between the percentage shares of correspondents giving positive and negative replies, seasonally adjusted



Source: European Commission, WIFO business cycle survey. Following the change to NACE rev. 2 data classification in May 2010, caution should be exercised for comparison with earlier data.

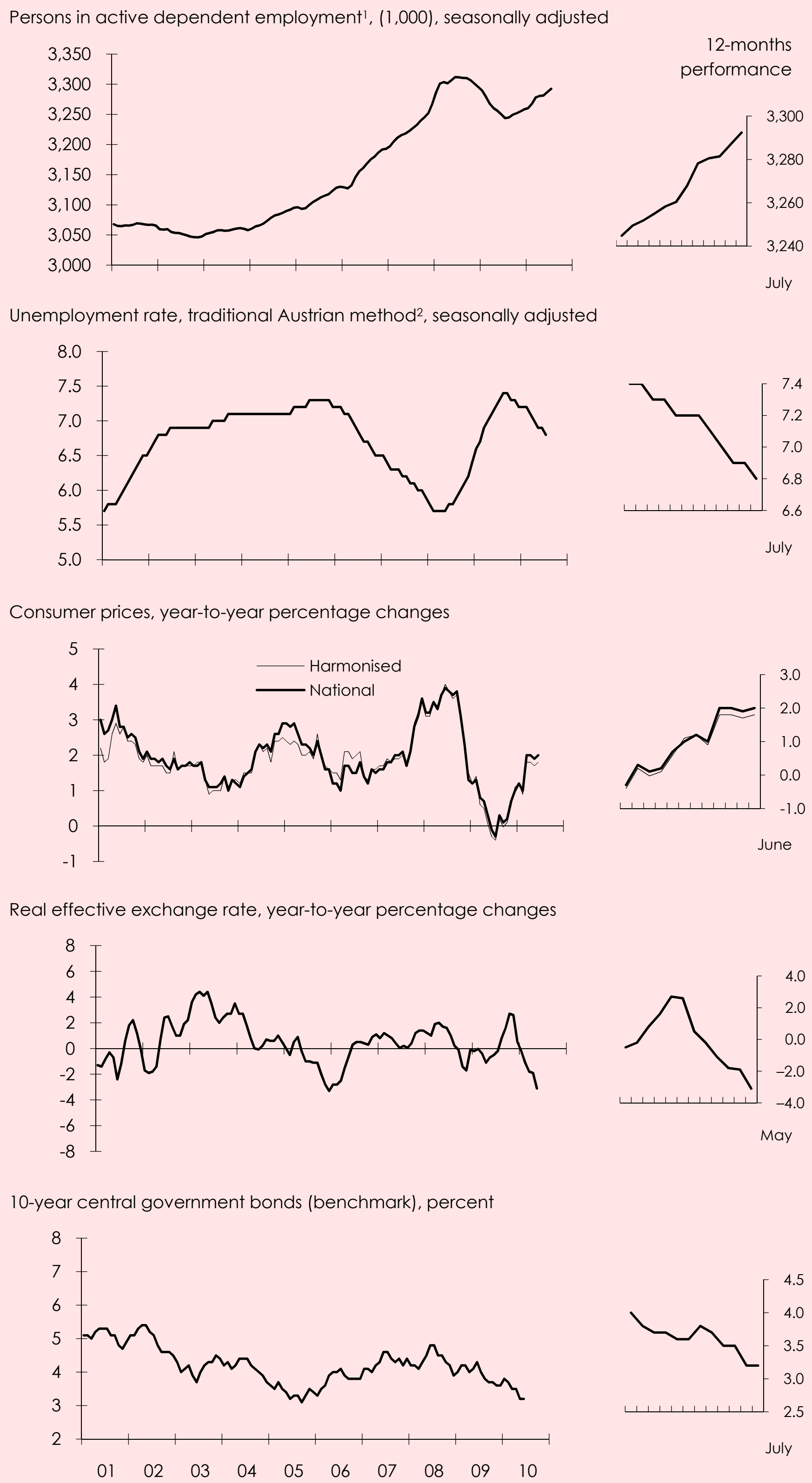
Industrial firms are planning to curtail their construction investment more strongly than they did last year (–20 percent; 2008 and 2009 around –10 percent), according to the investment survey conducted by WIFO in spring 2010. But this demand component portrays only part of the commercial-construction sector, and the investment plans reported are usually revised extensively.

Evidence presented in the WIFO business cycle survey also does not point to an easing of the situation in the construction sector, even though the downward trend should weaken in the coming months. This is suggested by firms' brighter assessment of order books and employment.

Tourism industry remains stable

In May and June 2010, the sales posted by Austria's tourism sector remained 0.7 percent below the year-earlier level. Travellers are likely to have cut down not only on expenditure for board and lodging, but also on additional expenses (culture, purchases, various personal services).

Figure 4: Key economic indicators



Source: Public Employment Service Austria, Federation of Austrian Social Security Institutions, Oesterreichische Nationalbank, Statistics Austria, WIFO calculations. – [1] Excluding parental leave, military service, and unemployed persons in training. – [2] As a percentage of total labour force excluding self employed, according to Public Employment Service.

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 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 (see 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.itkt.at/). The indicators are balances between the positive and negative responses expressed as a percentage of the total number of firms sampled.

Unemployment rate

Austrian national definition: The number of persons registered as job seekers with the Public Employment Service expressed as a percentage of the dependent labour force. Labour force is the sum of the unemployed and the persons in dependent employment (measured in standard employment relationships). Database: registrations with the Public Employment Service (AMS) and Association of Austrian social insurance agencies.

Definition according to ILO and EUROSTAT: Any person who is not gainfully employed and is actively seeking work is considered unemployed. Gainfully employed persons comprise all persons who during the reference week worked for at least one hour in a self-employed capacity or in paid employment. Persons receiving child-care benefit and apprentices are classified as gainfully employed, whereas persons in military service or persons carrying out alternative service are not. The unemployment rate is the number of unemployed persons expressed as a percentage of the total labour force (unemployed persons plus gainfully employed persons). Database: data from household surveys ("Mikrozensus").

Terms used in connection with the national definition of the unemployment rate

Persons in training: Persons who at a set date are enrolled in AMS (Public Employment Service) training programmes. When calculating the unemployment rate, their number is not taken into account either in the denominator or in the numerator.

Persons in dependent active employment: "Persons in dependent employment" include persons receiving child-care benefit, as well as persons in military service or persons carrying out alternative service with a valid employment contract. By deducting their number one arrives at the number of "persons in dependent active employment".

The number of overnight stays rose slightly in the first two months of the summer season, while sales declined marginally.

The number of overnight stays, by contrast, rose slightly (+0.3 percent), notably because city tourism recovered strongly: excluding the sizeable increase recorded in Vienna, Innsbruck and Salzburg, the number of overnight stays would have been 2 percent lower than last year. While in May and June the number of nights spent by foreign guests fell by 0.4 percent that by resident travellers rose by 1.6 percent.

A particularly strong increase was registered for nights spent by guests from Russia (+34.6 percent), the USA (+23.4 percent), UK (+14.5 percent) and Poland (+13.7 percent). A higher-than-average increase was also observed in the demand from Romania and Sweden (+6.3 percent each), Hungary (+6.0 percent), France (+4.3 percent) and Switzerland (+3.8 percent), whereas a decline was registered in Austria's major source markets the Netherlands (–1.8 percent) and Germany (–4.9 percent), as well as in Italy (–9.6 percent), Belgium (–9.8 percent) and the Czech Republic (–10.6 percent).

Inflation rate unchanged at 2 percent

Against the background of weak economic activity, inflation in Austria in recent months has appeared relatively high. The inflation rate surged to 2.0 percent already in March 2010, and has maintained this level since then (April 2.0 percent, May 1.9 percent, June 2.0 percent). This development is not so much attributable to a pick-up in consumer demand, but rather to the sizeable increase in the prices of mineral oil products. Without this component, the year-on-year price increase would amount to a mere 1.4 percent, according to Statistics Austria.

Compared with a year before, increases were also recorded in June for rents (+4.2 percent) as well as for the prices of car repairs (+3 percent) and insurance services (+2.2 percent), whereas a decline was posted for airline fares (–12 percent) and car prices (–2 percent).

The average price of consumer goods did not increase on a month-on-month basis in June. HICP inflation (the EU Harmonised Index of Consumer Prices) rose by 1.8 percent year-on-year in Austria, as in May only slightly more strongly than on euro-area average (+1.4 percent).

Labour market shows clear trend of improvement

Labour market conditions in Austria continued to ease in July. Employment increased once more, while unemployment fell further.

The marked improvement in economic conditions observed since the second quarter of 2010 was reflected in a renewed increase in the demand for labour in July: the number of persons in active dependent employment rose by 52,500 or +1.6 percent compared with a year before (June +34,600, +1.1 percent). In seasonally adjusted terms, active dependent employment increased by 0.2 percent month-on-month in July (June +0.2 percent).

At the same time, the number of persons registered as unemployed in July was down 20,700 on the year-earlier figure (–8.9 percent). In June, it had fallen by 16,900 (–7.3 percent), with the year-on-year increase in the number of persons enrolled in training programmes – who are not considered unemployed – clearly higher than in July (June 2010 +9,600, July +5,900). Compared with the previous month, developments of the seasonally adjusted number of persons unemployed remained positive in July (–1.0 percent).

The seasonally adjusted unemployment rate (according to the Austrian method of calculation) was 6.8 percent in July, unchanged from June. The unadjusted rate stood at 5.7 percent, 0.6 percentage points lower than a year before.