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Cyclical Activity Slackening, But No Recession

Economic Outlook for 2019 and 2020

Cyclical Activity Slackening, But No Recession. Economic Outlook for 2019 and 2020
Economic growth in Austria is gradually decelerating to a moderate pace over the forecast period. The lack of dynamism in the global economy dampens exports and manufacturing output. Yet, favourable financing conditions, fiscal stimulus and resilient private consumption provide support to economic activity. GDP is expected to grow by 1.7 percent in 2019 and 1.4 percent in 2020.

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Global economic activity slackened further in spring 2019. The smouldering trade conflict between the USA and China and the uncertain outcome of the Brexit negotiations dampen investment activity on an international scale, with negative repercussions on industrial production and global trade.

World GDP growth is set to moderate further over the forecast period. Notably manufacturing industry may not have reached the lower turning point yet. While growth remains robust in the USA and many emerging market economies, it suffers in the euro area from sluggishness in German export branches.

An imminent worldwide recession appears nevertheless unlikely. The continued expansionary monetary policy offers benign financing conditions, fiscal policy provides stimulus in some instances, and private consumption remains in many countries on a firm upward path. The risk of a strong increase in oil prices appears limited.

Cyclical activity slackened during spring 2019 also in Austria. Total output gained 0.3 percent in the second quarter from the previous period, the smallest increase since 2015. Exports in particular lost considerable momentum, whereas private consumption continued its stable upward trend. Compared with Germany, the Austrian economy has so far proved rather robust.

Prospects for the second half of 2019 are subdued. Business confidence in Austria's manufacturing sector has dropped markedly, according to the WIFO-Konjunkturtest (business cycle survey); several indicators even suggest a decline in output. Sentiment remains on the whole positive in the construction sector and the service industries. Aggregate demand is sustained by private consumption, driven by favourable developments in employment and household incomes, as well as by fiscal incentives.

In line with the international environment, the economy should reach the lower turning point of the cycle around the end of the year. In 2020, activity is expected to stabilise, while remaining moderate. GDP is projected to grow at an annual rate of

1.7 percent in 2019 and 1.4 percent 2020. Productive capacity utilisation for the overall economy, while receding somewhat, remains above the longer-term trend.

The slowdown of the output cycle will end the recovery on the labour market. Thanks to the still robust job creation in the first six months, the unemployment rate should still ease to 7.4 percent on annual average 2019, before edging up to 7.5 percent in 2020. Consumer price inflation remains firmly under control, at projected rates of 1.6 percent and 1.7 percent in 2019 and 2020 respectively. With tax revenues growing lively, the general government balance will reach a surplus equivalent to 0.6 percent of GDP in 2019, abating to 0.4 percent of GDP next year on account of recently adopted fiscal measures.

Table 1: Main results

		2015	2016	2017	2018	2019	2020
		Percentage changes from previous year					
Gross domestic product, volume		+ 1.0	+ 2.1	+ 2.5	+ 2.4	+ 1.7	+ 1.4
Manufacturing		+ 0.9	+ 4.6	+ 4.7	+ 5.1	+ 1.2	+ 1.4
Wholesale and retail trade		+ 2.1	+ 0.4	+ 0.3	+ 1.9	+ 0.9	+ 1.2
Private consumption expenditure[1], volume		+ 0.5	+ 1.6	+ 1.4	+ 1.1	+ 1.5	+ 1.6
Consumer durables		+ 1.2	+ 2.9	+ 2.2	+ 0.4	− 2.0	+ 2.0
Gross fixed capital formation, volume		+ 2.3	+ 4.1	+ 4.0	+ 3.9	+ 2.9	+ 1.5
Machinery and equipment[2]		+ 4.2	+ 7.2	+ 4.5	+ 4.1	+ 3.2	+ 1.6
Construction		+ 0.1	+ 0.5	+ 3.3	+ 3.7	+ 2.6	+ 1.3
Exports, volume		+ 3.0	+ 3.1	+ 5.0	+ 5.9	+ 2.3	+ 2.3
Exports of goods, fob		+ 3.1	+ 2.7	+ 5.4	+ 6.4	+ 2.0	+ 2.5
Imports, volume		+ 3.6	+ 3.7	+ 5.0	+ 4.6	+ 2.4	+ 2.5
Imports of goods, fob		+ 4.2	+ 3.4	+ 4.4	+ 4.0	+ 1.8	+ 2.2
Gross domestic product, value		+ 3.3	+ 3.8	+ 3.6	+ 4.2	+ 3.6	+ 3.2
	billion €	344.27	357.30	370.30	385.71	399.79	412.41
Current account balance	as a percentage of GDP	1.7	2.7	1.6	2.3	2.5	2.3
Consumer prices		+ 0.9	+ 0.9	+ 2.1	+ 2.0	+ 1.6	+ 1.7
Three-month interest rate	percent	− 0.0	− 0.3	− 0.3	− 0.3	− 0.4	− 0.5
Long-term interest rate[3]	percent	0.7	0.4	0.6	0.7	0.0	− 0.2
General government financial balance, Maastricht definition	as a percentage of GDP	− 1.0	− 1.5	− 0.7	0.2	0.6	0.4
Persons in active dependent employment[4]		+ 1.0	+ 1.6	+ 2.0	+ 2.5	+ 1.6	+ 1.0
Unemployment rate							
Eurostat definition[5]		5.7	6.0	5.5	4.9	4.6	4.6
National definition[6]		9.1	9.1	8.5	7.7	7.4	7.5

Source: WIFO. 2019 and 2020: forecast. – [1] Including non-profit institutions serving households. – [2] Including weapons systems. – [3] 10-year central government bonds (benchmark). – [4] Excluding persons in valid employment contract receiving child care benefit or being in military service. – [5] As a percentage of total labour force, Labour Force Survey. – [6] As a percentage of dependent labour force, unemployed persons according to Public Employment Service Austria.

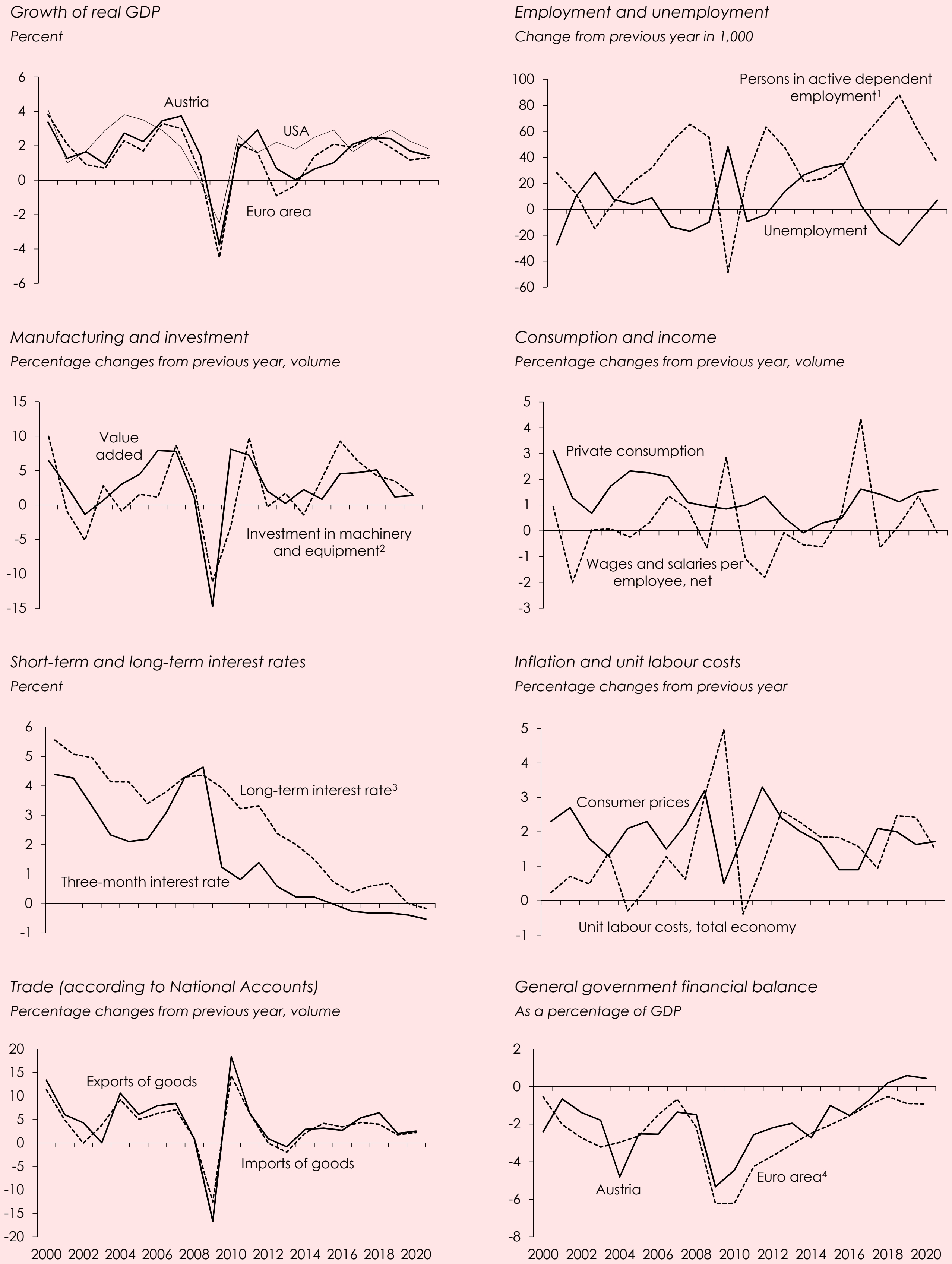
1. World economy expected to grow more slowly, avoiding recession

Global economic activity is losing momentum, with trade volumes and industrial output remaining subdued. Consumption and fiscal incentives sustain overall demand. Expansionary monetary policy offers favourable financing conditions. Oil prices are unlikely to keep rising further.

Global economic activity slackened further in spring 2019. According to CPB, world trade shrank in the second quarter for the third consecutive period, while global industrial output growth slowed once again. The smouldering trade conflict between the USA and China and the uncertain outcome of the Brexit negotiations add to uncertainty worldwide. In all likelihood, many industrialised and emerging market economies have by now passed the peak of the output cycle. These developments dampen new investment, industrial production and trade worldwide. On the other hand, private household consumption in many countries keeps supporting overall demand, preventing a sharper cyclical downturn.

The forecast period is likely to see a further slowdown of world economic growth. Notably the fall in industrial output may not yet have bottomed out. The global Markit Purchasing Managers' Index for the sector was below the threshold signalling expansion during the summer months. In many countries, industrial confidence has dropped significantly from last year. Nevertheless, in some instances a tentative stabilisation of activity has been observed. A global recession is therefore unlikely from today's perspective, while little speaks in favour of a speedy recovery.

Figure 1: Indicators of economic performance



Source: WIFO. 2019 and 2020: 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] Source: European Commission.

In view of the global growth slowdown, many central banks have altered their policy stance. In July and September, the US Federal Reserve lowered its key interest rate to a current range from 1.75 percent to 2 percent. Likewise, the European Central Bank reacted by cutting the deposit rate to –0.5 percent in September. It also announced a resumption of longer-term refinancing operations for banks and a new bond purchase programme to the amount of 20 billion € per month as from November. Central banks of other advanced and emerging market economies followed suit by relaxing monetary conditions. Hence, financing conditions should remain extremely favourable over the projection horizon. In addition, a number of countries may adopt fiscal stimulus measures.

Table 2: International economy

	Percentage shares 2018		2015	2016	2017	2018	2019	2020
	Austria's exports of goods	World GDP[1]	GDP volume, percentage changes from previous year					
EU 28			+ 2.3	+ 2.0	+ 2.6	+ 2.0	+ 1.5	+ 1.5
EU 27	67.1	14.0	+ 2.3	+ 2.0	+ 2.7	+ 2.1	+ 1.6	+ 1.6
Euro area	52.0	11.4	+ 2.1	+ 1.9	+ 2.5	+ 1.9	+ 1.2	+ 1.3
Germany	30.1	3.2	+ 1.7	+ 2.2	+ 2.5	+ 1.5	+ 0.5	+ 1.2
Italy	6.5	1.8	+ 0.9	+ 1.1	+ 1.7	+ 0.9	+ 0.1	+ 0.4
France	4.3	2.2	+ 1.1	+ 1.1	+ 2.3	+ 1.7	+ 1.3	+ 1.3
CEEC 5[2]	14.6	1.6	+ 4.0	+ 2.9	+ 4.5	+ 4.5	+ 3.8	+ 3.0
Czech Republic	3.8	0.3	+ 5.3	+ 2.5	+ 4.4	+ 3.0	+ 2.7	+ 2.0
Hungary	3.4	0.2	+ 3.5	+ 2.3	+ 4.1	+ 4.9	+ 4.8	+ 3.0
Poland	3.2	0.9	+ 3.8	+ 3.1	+ 4.8	+ 5.1	+ 4.2	+ 3.2
USA	7.1	15.2	+ 2.9	+ 1.6	+ 2.4	+ 2.9	+ 2.3	+ 1.8
Switzerland	5.0	0.4	+ 1.3	+ 1.7	+ 1.8	+ 2.8	+ 0.8	+ 1.5
UK	2.8	2.2	+ 2.3	+ 1.8	+ 1.8	+ 1.4	+ 1.0	+ 1.2
China	2.7	18.7	+ 6.9	+ 6.7	+ 6.8	+ 6.6	+ 6.2	+ 5.8
Total[3]								
PPP-weighted[4]		51	+ 4.1	+ 3.4	+ 4.1	+ 4.0	+ 3.5	+ 3.2
Export weighted[5]	85		+ 2.4	+ 2.1	+ 2.7	+ 2.3	+ 1.7	+ 1.7
Market growth[6]			+ 3.6	+ 3.5	+ 6.6	+ 4.3	+ 1.8	+ 2.5
Forecast assumptions								
Crude oil prices								
Brent, $ per barrel			52.5	43.7	54.3	71.0	66	63
Exchange rate								
$ per €			1.110	1.107	1.129	1.181	1.12	1.10
Key interest rate								
ECB main refinancing rate[7], percent			0,1	0,0	0.0	0.0	0.0	0.0
10-year government bonds yields Germany, percent			0,5	0,1	0.3	0.4	– 0.3	– 0.5

Source: WIFO. 2019 and 2020: 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 2018. – [5] Weighted by shares of Austrian goods exports in 2018. – [6] Real import growth of trading partners, weighted by shares of Austrian goods exports. – [7] Minimum bid rate.

Oil prices soared after the attack on Saudi-Arabian production sites in September, but have eased thereafter. At around 65 $ per barrel, the reference price for Brent by the end of September was close to the annual average. Temporary hikes had been repeatedly observed in the last years, but have had little effect on business activity. The present forecast assumes that oil production will not be cut further and that the average 2019 price will be at 66 $ per barrel, edging down to 63 $ in 2020.

2. Slower, but still robust growth of the US economy

Growth of US GDP is likely to decelerate. Private consumption remains nevertheless resilient and sustains overall activity.

GDP growth in the USA eased somewhat during the second quarter of 2019, though remaining at a robust +0.5 percent from the previous period. Exports broadly stagnated, dampening industrial production, while consumer demand supported output growth.

Indicators suggest that such divergence will continue. The ISM Purchasing Managers' Index has receded significantly in the last few months, dipping below the threshold of expansion last August. Consumer confidence, however, is unabatedly positive. Unusually low unemployment and healthy wage growth should provide further support to consumption. Unlike in the run-up to the 2008-09 crisis, private household debt has remained broadly stable in the last two years and the savings ratio rather high. Hence, GDP growth, though slowing down, should nevertheless stay robust, at projected rates of 2.3 percent for 2019 and 1.8 percent for 2020.

3. Euro area shaped by sluggish German economy

Germany's export industries are suffering from the global cyclical downturn. In the third quarter, the economy may slip into technical recession. Other euro area countries are affected to a lesser extent.

Demand and output growth in the euro area decreased from the exceptionally high rate in the first quarter that was upward biased by one-off effects. In the subsequent three months, exports barely contributed to quarter-on-quarter growth. Industrial production declined, and so did incoming orders, output expectations and business confidence. Consumer optimism, however, is unabated and the European Commission's Sentiment Indicator (ESI) suggests optimism prevailing.

The performance of the euro area is largely shaped by the weakness of the German economy, whereas in other countries the downswing has so far been less marked. France enjoyed unabated GDP growth in the second quarter, the Spanish economy also proved resilient, while GDP in Italy stagnated. Likewise, cyclical indicators are more positive for many countries than for Germany. Going forward, euro area GDP growth will nevertheless ease markedly from the last few years, to projected rates of 1.2 percent in 2019 and 1.3 percent in 2020.

Germany's GDP shrank slightly for the first time in the second quarter against the earlier period. The crucial manufacturing and export sector suffered more than in many other countries. The weakening global investment activity under mounting uncertainty affects to a particularly high degree the German manufacturing sector with its strong specialisation on investment goods. Few indicators point to an improvement in the second half of the year. GDP is likely to contract also in the third quarter, which would mean a technical recession for the German economy. In particular manufacturing industry would suffer from falling output.

For the time being, however, the economy is in a stage of normal capacity utilisation, no downright recession yet being in sight. Fiscal policy is providing positive incentives, while private consumption is benefitting from benign labour market and income developments. The temporary weakness may not be overcome before 2020 when demand and output growth should return to trend. A strong calendar effect (higher number of working days) will push up GDP growth by 0.4 percentage points next year, leading to an acceleration from 0.5 percent in 2019 to 1.2 percent in 2020.

4. Growth slowing down in Austria

In the wake of the global economic downturn, growth is decelerating in Austria. With exports and industrial production slackening, firms will be less ready to embark on new investment. Private consumption, however, provides continued support to aggregate demand.

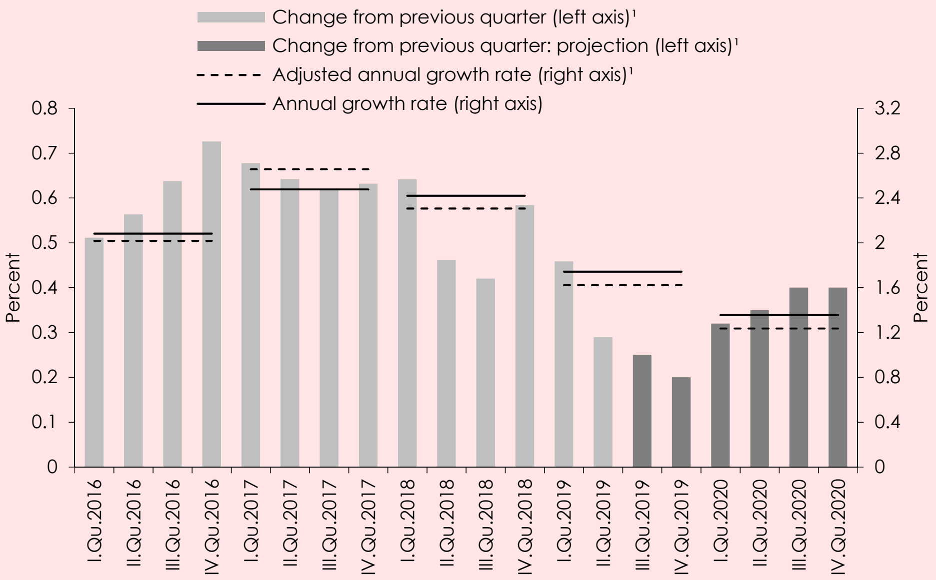
Activity in Austria clearly lost momentum already in 2018 and moderated further in spring 2019. Total output gained 0.3 percent in the second quarter from the previous period, the lowest reading since 2015. Exports in particular slackened, while private consumption kept its stable upward path. Altogether, demand and output have so far proved more resilient than in Germany.

The outlook for the second half of the year is nevertheless subdued. In the latest WIFO-Konjunkturtest (business cycle survey), confidence has dropped mainly in the manufacturing sector, where several indicators even suggest a fall in production. Expectations remain on the whole upbeat in construction and the service branches. The overall trend should nevertheless be heading down for the rest of the year, driven by weaker exports and industrial production. Private consumption, however, still provides firm support to aggregate demand, thanks to favourable employment and income developments.

WIFO's short-term forecasting models suggest that the lower turning point of the cycle may be reached at the end of this year. In 2020, activity should stabilise in line with the external environment, with growth still remaining subdued. Exports may show weak momentum, dampening also business fixed investment. Private consumption is likely to provide further reliable support, not least due to the income-boosting fiscal measures adopted in 2018 and 2019.

Figure 2: Cyclical profile Austria

GDP, volume



Source: WIFO. – [1] Trend-cycle data.

Table 3: Technical breakdown of the real GDP growth forecast

		2017	2018	2019	2020
Growth carry-over[1]	percentage points	+ 1.0	+ 1.1	+ 0.8	+ 0.3
Growth rate during the year[2]	percent	+ 2.6	+ 2.1	+ 1.2	+ 1.5
Annual growth rate	*percent*	*+ 2.5*	*+ 2.5*	*+ 1.7*	*+ 1.4*
Adjusted annual growth rate[3]	percent	+ 2.7	+ 2.3	+ 1.6	+ 1.2
Calendar effect[4]	percentage points	– 0.3	+ 0.0	+ 0.1	+ 0.1

Source: WIFO. 2019 and 2020: 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; trend-cycle data. – [2] Reflects the growth dynamics during a calendar year. Equals the year-on-year growth rate for the fourth quarter; trend-cycle data. – [3] Trend-cycle data. Corresponding figure to OeNB short-term forecast. – [4] Impact of the annual number of working days and the leap day. The sum of the adjusted annual growth rate and the calendar effect may deviate from the unadjusted annual rate, since the latter also includes seasonal and irregular effects.

Table 4: Productivity

	2015	2016	2017	2018	2019	2020
		Percentage changes from previous year				
Total economy						
Real GDP	+ 1.0	+ 2.1	+ 2.5	+ 2.4	+ 1.7	+ 1.4
Hours worked[1]	– 0.4	+ 2.1	+ 1.0	+ 2.0	+ 1.2	+ 1.0
Productivity[2]	+ 1.4	– 0.0	+ 1.4	+ 0.4	+ 0.5	+ 0.4
Employment[3]	+ 0.7	+ 1.5	+ 1.7	+ 1.9	+ 1.4	+ 0.8
Manufacturing						
Production[4]	+ 0.9	+ 4.6	+ 4.7	+ 5.1	+ 1.2	+ 1.4
Hours worked[5]	– 0.1	+ 0.4	+ 1.1	+ 2.7	+ 0.7	– 0.5
Productivity[2]	+ 1.0	+ 4.2	+ 3.6	+ 2.3	+ 0.5	+ 1.9
Employees[6]	+ 0.5	+ 0.5	+ 1.3	+ 3.0	+ 1.3	– 0.1

Source: WIFO. 2019 and 2020: 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).

The pace of GDP growth during the calendar year, which better reflects the cyclical dynamics, will be slower in 2019 than in 2020. Due to a substantial carry-over from the previous year, the annual GDP growth rate for 2019 should be 1.7 percent and thus somewhat higher than the 1.4 percent projected for 2020. As measured by the output gap calculated according to the EU method, capacity utilisation for the overall economy, while slightly decreasing, still remains above trend.

Table 5: Gross value added

At basic prices

	2017	2018	2019	2020	2017	2018	2019	2020
	Billion € (reference year 2015)				Percentage changes from previous year			
Volume (chain-linked series)								
Agriculture, forestry and fishing	4.17	4.34	4.34	4.34	+ 2.5	+ 4.1	± 0.0	± 0.0
Manufacturing including mining and quarrying	64.07	67.31	68.12	69.07	+ 4.8	+ 5.1	+ 1.2	+ 1.4
Electricity, gas and water supply, waste management	9.60	10.12	10.67	10.99	+ 4.8	+ 5.4	+ 5.5	+ 3.0
Construction	20.08	20.87	21.45	21.73	+ 4.3	+ 3.9	+ 2.8	+ 1.3
Wholesale and retail trade	37.78	38.50	38.85	39.31	+ 0.3	+ 1.9	+ 0.9	+ 1.2
Transportation	18.38	19.21	20.21	20.82	+ 3.7	+ 4.5	+ 5.2	+ 3.0
Accommodation and food service activities	16.08	16.55	16.79	17.02	+ 0.2	+ 3.0	+ 1.4	+ 1.4
Information and communication	11.60	11.91	12.22	12.47	+ 2.7	+ 2.7	+ 2.6	+ 2.0
Financial and insurance activities	13.78	13.71	13.82	13.98	+ 3.7	– 0.5	+ 0.7	+ 1.2
Real estate activities	30.42	30.71	31.38	31.95	+ 0.7	+ 0.9	+ 2.2	+ 1.8
Other business activities[1]	31.39	32.34	33.15	33.81	+ 4.2	+ 3.0	+ 2.5	+ 2.0
Public administration[2]	55.21	55.59	56.14	56.65	+ 1.2	+ 0.7	+ 1.0	+ 0.9
Other service activities[3]	8.89	8.85	8.94	8.98	+ 1.5	– 0.4	+ 1.0	+ 0.5
Total gross value added[4]	321.44	329.91	335.96	340.98	+ 2.6	+ 2.6	+ 1.8	+ 1.5
Gross domestic product at market prices	360.14	368.86	375.12	380.46	+ 2.5	+ 2.4	+ 1.7	+ 1.4

Source: WIFO. 2019 and 2020: 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 activites; activities of households (NACE R to U). – [4] Before deduction of subsidies and attribution of taxes on products.

4.1 Difficult external environment weighing on export industry

Slower growth worldwide is dampening export prospects that may cloud further before tentatively improving during 2020.

Over the forecast horizon, Austrian exports are likely to advance at a considerably slower pace than in the last few years. Reasons are the international downturn and the sluggishness in the German manufacturing industry. In the first six months of 2019, exports still proved rather resilient. Unlike for Germany, Austrian shipments to the UK, notably of vehicles, posted strong gains. Likewise, exports to Hungary and France increased significantly.

The export momentum should further abate over the remainder of the year. Although, according to the WIFO-Konjunkturtest (business cycle survey), foreign order levels remained stable during the summer months, the trade statistics show a marked decline from June. Since the beginning of the year, exports to Germany, the major trading partner, were no higher than last year. Following the international trend, exports should reach the lower turning point by the end of the year, before tentatively rebounding in 2020. In view of the low appetite for corporate investment worldwide, the momentum may still be slow. After an increase by 5.9 percent in 2018, exports of goods and services are expected to post volume increases by only 2.3 percent respectively in 2019 and 2020.

With the slowdown in exports and corporate spending on machinery and equipment, Austria's imports will also advance more slowly, since both exports and investment carry a large foreign content. After +4.6 percent in 2018, imports are projected to gain 2.4 percent in 2019 and 2.5 percent in 2020. The external contribution to GDP growth may thus be close to neutral over the forecast horizon. The current account balance is set to improve somewhat in 2019 on account of lower pressure from import prices.

Table 6: Expenditure on GDP

Volume (chain-linked series)

	2017	2018	2019	2020	2017	2018	2019	2020
	Billion € (reference year 2015)				Percentage changes from previous year			
Final consumption expenditure	256.93	259.65	263.38	267.12	+ 1.3	+ 1.1	+ 1.4	+ 1.4
Households[1]	186.92	189.03	191.86	194.93	+ 1.4	+ 1.1	+ 1.5	+ 1.6
General government	70.01	70.62	71.51	72.18	+ 1.1	+ 0.9	+ 1.3	+ 0.9
Gross capital formation	89.04	92.28	94.69	96.33	+ 4.5	+ 3.6	+ 2.6	+ 1.7
Gross fixed capital formation	84.53	87.85	90.44	91.77	+ 4.0	+ 3.9	+ 2.9	+ 1.5
Machinery and equipment[2]	29.07	30.31	31.37	31.84	+ 6.3	+ 4.3	+ 3.5	+ 1.5
Construction	37.80	39.19	40.21	40.73	+ 3.3	+ 3.7	+ 2.6	+ 1.3
Other investment[3]	17.67	18.36	18.87	19.21	+ 1.7	+ 3.9	+ 2.8	+ 1.8
Domestic demand	347.20	352.79	358.77	364.01	+ 2.4	+ 1.6	+ 1.7	+ 1.5
Exports	197.85	209.49	214.37	219.40	+ 5.0	+ 5.9	+ 2.3	+ 2.3
Travel	15.73	16.39	16.60	16.79	+ 2.9	+ 4.2	+ 1.3	+ 1.2
Minus imports	184.93	193.38	197.96	202.88	+ 5.0	+ 4.6	+ 2.4	+ 2.5
Travel	8.33	9.15	9.35	9.53	+ 8.5	+ 9.9	+ 2.2	+ 2.0
Gross domestic product	360.14	368.86	375.12	380.46	+ 2.5	+ 2.4	+ 1.7	+ 1.4
Value	370.30	385.71	399.79	412.41	+ 3.6	+ 4.2	+ 3.6	+ 3.2

Source: WIFO. 2019 and 2020: forecast. – [1] Including non-profit institutions serving households. – [2] Including weapon systems. – [3] Mainly intellectual property products (research and development, computer programmes, copyrights).

4.2 Investment to be subdued over the forecast horizon

Lively demand for new machinery and equipment early this year and buoyant construction help sustain investment growth in 2019. Next year, capital formation will be overshadowed by slackening final demand.

The pace of private investment slowed markedly in spring 2019, the increase from the first quarter being the smallest since the end of 2016. However, a catch-up effect of vehicle purchases had boosted machinery investment in the fourth quarter of 2018 and the first quarter of 2019, still benefitting the annual growth rate for 2019. In 2020, the business cycle downswing will dampen investment, as firms will turn more cautious in adding to production capacity.

Construction activity has barely lost momentum so far. Going forward, a number of indicators suggest more moderate gains. In 2018 already, the number of building permits fell markedly. Firms' expectations turned somewhat less optimistic, according to the WIFO-Konjunkturtest (business cycle survey), though from a high level. Order levels are still rated high, and firms complain about lack of personnel. Construction price inflation has recently eased, signalling a deceleration of growth.

Table 7: Private consumption, income and prices

	2015	2016	2017	2018	2019	2020
	Percentage changes from previous year, volume					
Private consumption expenditure[1]	+ 0.5	+ 1.6	+ 1.4	+ 1.1	+ 1.5	+ 1.6
Durable goods	+ 1.2	+ 2.9	+ 2.2	+ 0.4	– 2.0	+ 2.0
Non-durable goods and services	+ 0.4	+ 1.5	+ 1.3	+ 1.2	+ 1.9	+ 1.6
Household disposable income	– 0.2	+ 2.6	+ 1.1	+ 1.4	+ 1.5	+ 1.8
	As a percentage of disposable income					
Household saving ratio						
Including adjustment for the change in pension entitlements	6.7	7.7	7.3	7.7	7.6	7.8
Excluding adjustment for the change in pension entitlements	6.1	7.0	6.7	7.0	6.9	7.1
	Percentage changes from previous year					
Loans to domestic non-banks (end of period)	+ 1.8	+ 1.8	+ 0.7	+ 4.6	+ 3.7	+ 2.7
	Percent					
Inflation rate						
National	0.9	0.9	2.1	2.0	1.6	1.7
Harmonised	0.8	1.0	2.2	2.1	1.6	1.7
Core inflation[2]	1.7	1.5	2.2	1.9	1.7	1.8

Source: WIFO. 2019 and 2020: forecast. – [1] Private households including non-profit institutions serving households. – [2] Excluding energy and unprocessed food (meat, fish, fruits, vegetables).

Thanks to the strong base effect of the first six months, total gross fixed investment will enjoy an increase of 2.9 percent for the whole of 2019, which is nevertheless down from the previous years. For 2020, the projection is for an increase by only 1.5 percent.

4.3 Consumer spending remains robust

Private consumption will further sustain business activity. Fiscal measures adopted in 2018 and 2019 boost private incomes. The hesitancy of consumer to buy new motor cars is likely to unwind only in 2020.

Private household spending regained strength in the first half of 2019, having eased somewhat in 2018. Consumer confidence has subsided markedly since early 2018, but has stabilised recently, according to the European Commission's business survey. Likely reasons are the introduction of the family bonus early this year and substantial employment and income gains. New car registrations, however, are still far below their year-earlier level, causing a fall in the consumption of durable goods overall.

Private consumption is expected to expand by 1.5 percent in 2019. Next year, the adverse effect of changes in exhaust regulations on car purchases should fade, allowing purchases of durable consumer goods to rebound. The family bonus and fiscal stimulus measures decided in September 2019 will strengthen private incomes markedly in 2020, letting private consumption increase by 1.6 percent.

Table 8: Earnings, international competitiveness

	2015	2016	2017	2018	2019	2020
	Percentage changes from previous year					
Wages and salaries per employee[1]						
Nominal, gross	+ 2.0	+ 2.3	+ 1.6	+ 2.7	+ 2.9	+ 1.8
Real[2]						
Gross	+ 1.1	+ 1.4	− 0.5	+ 0.7	+ 1.2	+ 0.1
Net	+ 0.6	+ 4.3	− 0.7	+ 0.2	+ 1.3	− 0.1
Wages and salaries per hour worked[1]						
Real, net[2]	+ 2.0	+ 3.5	+ 0.1	+ 0.3	+ 1.5	+ 0.1
	Percent					
Wage share, adjusted[3]	69.3	68.0	68.5	68.0	68.0	67.7
	Percentage changes from previous year					
Unit labour costs, nominal[4]						
Total economy	+ 1.8	+ 1.6	+ 0.9	+ 2.5	+ 2.4	+ 1.5
Manufacturing	+ 1.3	− 1.4	− 2.2	+ 1.1	+ 3.3	+ 1.0
Effective exchange rate – manufactured goods[5]						
Nominal	− 2.9	+ 1.2	+ 0.7	+ 1.7	− 0.4	+ 0.2
Real	− 3.1	+ 1.3	+ 1.0	+ 1.7	− 0.8	± 0.0

Source: WIFO. 2019 and 2020: 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). – [5] Weighted by exports and imports, real value adjusted by relative HCPI.

4.4 Recovery of the labour market about to end

Despite employment growth easing, the unemployment rate decreases significantly in 2019. Yet, the turnaround on the labour marked is already under way. Unemployment is likely to edge up in 2020.

The gradual cyclical slowdown is extending to the labour market. During the first eight months of 2019, job creation weakened steadily, as did the decline in unemployment. The turnaround on the labour market is also reflected in the pick-up of unemployment among 55-year-olds and above and persons of reduced health.

The adverse trend is likely to persist over the forecast horizon. The number of persons in active dependent employment should rise significantly less in 2019 (+1.6 percent) than one year earlier, and less again (+1 percent) in 2020.

The rate of unemployment, calculated on national definitions, drops to 7.4 percent of the dependent labour force in 2019, before edging up to 7.5 percent in 2020, when job creation can no longer fully accommodate the increase in labour supply.

In 2019, when the likely lower turning point of the current cycle is reached, the average number of unemployed registered with the Public Employment Service Austria (AMS) will be around 90,000 higher than in 2008. Hence, the now ending upswing has not lasted long enough to offset the strong unemployment increase of the previous years. In particular jobless figures for workers of age 55 and above, of reduced employability for health reasons and of long-term jobseekers had increased substantially.

Table 9: Labour market

	2015	2016	2017	2018	2019	2020
	Change from previous year in 1,000					
Demand for labour						
Persons in active employment[1]	+ 42.5	+ 62.3	+ 76.8	+ 91.6	+ 63.0	+ 39.0
Employees[1,2]	+ 33.2	+ 53.7	+ 70.7	+ 88.0	+ 60.0	+ 36.0
National employees	+ 6.3	+ 17.7	+ 23.8	+ 33.7	+ 15.0	+ 8.0
Foreign employees	+ 27.0	+ 36.0	+ 46.8	+ 54.4	+ 45.0	+ 28.0
Self-employed[3]	+ 9.3	+ 8.6	+ 6.1	+ 3.6	+ 3.0	+ 3.0
Labour supply						
Population of working age 15 to 64 years	+ 52.3	+ 65.8	+ 23.0	+ 13.2	+ 9.6	+ 5.9
Labour force[4]	+ 77.5	+ 65.3	+ 59.4	+ 63.8	+ 53.0	+ 46.0
Labour surplus						
Unemployed[5]	+ 35.0	+ 3.0	– 17.3	– 27.9	– 10.0	+ 7.0
Unemployed persons in training	– 10.2	+ 2.1	+ 4.9	– 3.4	– 8.0	– 1.0
	Percent					
Unemployment rate						
As a percentage of total labour force (Eurostat)[6]	5.7	6.0	5.5	4.9	4.6	4.6
As a percentage of total labour force[5]	8.1	8.1	7.6	6.9	6.6	6.7
As a percentage of dependent labour force[5]	9.1	9.1	8.5	7.7	7.4	7.5
	Percentage changes from previous year					
Labour force[4]	+ 1.8	+ 1.5	+ 1.4	+ 1.4	+ 1.2	+ 1.0
Persons in active dependent employment[1, 2]	+ 1.0	+ 1.6	+ 2.0	+ 2.5	+ 1.6	+ 1.0
Unemployed[5]	+ 11.0	+ 0.8	– 4.9	– 8.2	– 3.2	+ 2.3
Persons (in 1,000)	354.3	357.3	340.0	312.1	302.1	309.1

Source: WIFO. 2019 and 2020: forecast. – [1] Excluding persons in valid employment contract receiving child care benefit or being in military service. – [2] According to the Organisation of Austrian Social Security. – [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.

4.5 Low inflation ahead

Inflation subsided markedly towards the end of 2018 and should remain moderate over the forecast period. Import prices of raw materials and finished goods should rise little, given the slackening global cycle. Unit labour cost for the economy as a whole, after rising equally strongly in 2019 as in the year before, should ease in reaction to less generous wage settlements for 2020. The consumer price index (national concept) rises by 1.6 percent in 2019 and by an expected 1.7 percent in 2020.

Table 10: Fiscal and monetary policy – key figures

	2015	2016	2017	2018	2019	2020
	As a percentage of GDP					
Fiscal policy						
General government financial balance[1]	– 1.0	– 1.5	– 0.7	0.2	0.6	0.4
General government primary balance	1.3	0.5	1.1	1.8	2.0	1.7
General government total revenue	50.1	48.6	48.4	48.8	48.9	48.5
General government total expenditure	51.1	50.1	49.1	48.6	48.3	48.1
	Percent					
Monetary policy						
Three-month interest rate	– 0.0	– 0.3	– 0.3	– 0.3	– 0.4	– 0.5
Long-term interest rate[2]	0.7	0.4	0.6	0.7	0.0	– 0.2

Source: WIFO. 2019 and 2020: forecast. – [1] According to Maastricht definition. – [2] 10-year central government bonds (benchmark).

4.6 Buoyant revenues boosting government surplus

The government financial position continued to improve in 2019, thanks to buoyant receipts from wage tax, VAT, corporation tax and social security contributions. Moreover, debt service cost eased as interest rates on government bonds fell in the first six months of the year. On the other hand, in 2018 the government had adopted a number of measures weighing on the budget balance (family bonus, cut of the unemployment insurance contribution rate for low-income earners etc.). The general government balance (Maastricht definition) for 2019 should nevertheless improve to a surplus equivalent to 0.6 percent of GDP.

Despite some fiscal stimulus measures, the general government balance improves markedly in 2019, thanks to lively tax revenue growth and lower interest cost. The budgetary surplus will narrow in 2020, due to the fiscal measures adopted in September 2019.

In September 2019, Parliament adopted a number of fiscal measures with early effects already in 2020. Inter alia, low retirement benefits will be revalued and social security contributions for self-employed reduced. The introduction of the family bonus will still imply revenue losses in 2020. In all, the general government surplus may abate to 0.4 percent of GDP.

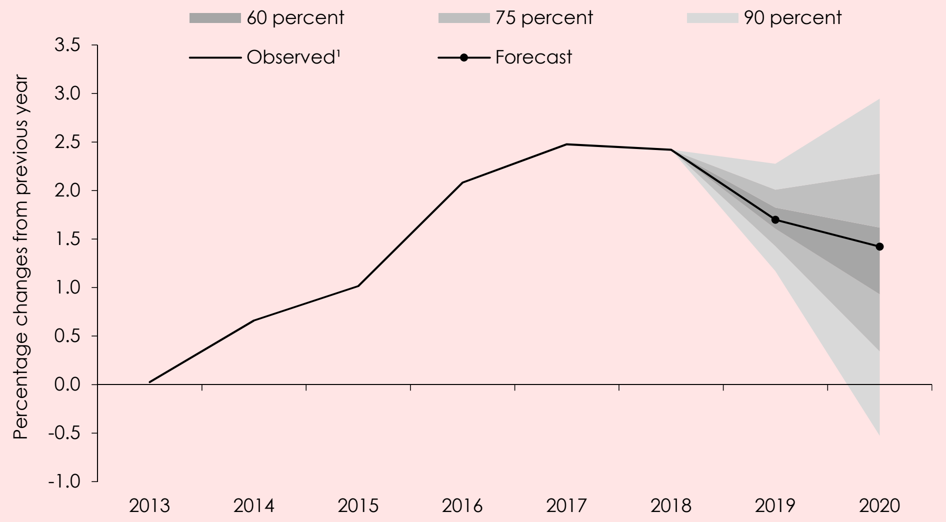
4.7 Forecast risks tilted to the downside

The international environment holds important downside risks to the present forecast. The trade conflict between the USA and China is still in limbo and may exacerbate at any time. In addition, the terms of the UK withdrawal from the EU are still unclear. Lately, the attack on Saudi-Arabian oil production facilities has re-ignited the US conflict with Iran. These elements may all undermine world trade and global business activity to a greater extent than assumed in the present scenario and weigh on the Austrian economy's performance.

The international trade conflict and the uncertain outcome of the Brexit negotiations constitute major forecast risks.

From the present perspective, upside risks are hard to identify. Benign employment and income growth in 2019 may lead to stronger private consumption than anticipated; on the other hand, the gloomier short-term outlook may induce households to greater caution in future spending. Overall, the downward risks should clearly prevail over the forecast horizon. The statistical 75 percent-confidence interval for GDP growth ranges from 1.4 to 2 percent for 2019 and from 0.3 to 2.2 percent for 2020.

Figure 3: Margins of uncertainty for real GDP



Source: WIFO. Calculated on the basis of ex-post revealed forecast errors. For methodology see *Kaniovski* (2019) "Probability Intervals for STATEC Forecasts". – [1] Uncertainty of measurement: ±0,28 percentage points.