

WIFO

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WIRTSCHAFTSFORSCHUNG**

**Euro Area in Temporary Recession
Economic Outlook for 2012 and 2013**

March 2012



Euro Area in Temporary Recession Economic Outlook for 2012 and 2013

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Austrian Institute of Economic Research

Abstract

The euro area economy is currently in recession. By the middle of the year, however, economic activity is expected to head up again, even if the recovery promises to be subdued given the fiscal restraint in many countries. While the export-oriented sector in Germany and Austria continues to receive stimulus from economies outside Europe, it will nevertheless be affected by sluggish euro area growth. Real GDP in Austria is likely to edge up by 0.4 percent in 2012. Growth in 2013 should strengthen to 1.4 percent, driven by foreign demand, but dampened by fiscal consolidation. The rise in oil prices will prevent a speedy decline in inflation.

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Euro Area in Temporary Recession. Economic Outlook for 2012 and 2013

The euro area economy is currently in recession. By the middle of the year, however, economic activity is expected to head up again, even if the recovery promises to be subdued given the fiscal restraint in many countries. While the export-oriented sector in Germany and Austria continues to receive stimulus from economies outside Europe, it will nevertheless be affected by sluggish euro area growth. Real GDP in Austria is likely to edge up by 0.4 percent in 2012. Growth in 2013 should strengthen to 1.4 percent, driven by foreign demand, but dampened by fiscal consolidation. The rise in oil prices will prevent a speedy decline in inflation.

Like on average in the euro area, business activity in Austria lost momentum during the course of the year 2011. Foreign demand slackened markedly and GDP receded slightly towards the end of the year. As results from Austrian business surveys suggest, the "soft patch" should soon be overcome and growth should resume as from the second quarter 2012. The rebound may nevertheless be muted as many EU governments press ahead with fiscal consolidation and firms as well as private households remain cautious on higher spending. Italy, Austria's second-most important trading partner, has announced sweeping budgetary cuts for this year which will likely lead to a decline in annual GDP. In Hungary, ranking 7th in Austria's export markets, activity will weaken substantially, too. Both developments will weigh on Austria's economic growth this year. In 2013, domestic fiscal policy will also turn more restrictive than anticipated in the forecast of last December, weighing further on the recovery. In this environment, real GDP will only increase by 1.4 percent.

Uncertainty on financial markets seems to have subsided somewhat since the end of 2011. In many euro area countries, long-term interest rates declined, Greece reached an agreement with its creditors and stock markets recorded a clear upward trend. Yet, the crisis in the banking sector does not appear to have been resolved, even if tensions have for now eased to some extent.

The renewed hike in oil prices due to geo-political tensions inhibits a speedy deceleration of inflation, despite the sluggishness of business activity. Domestic consumer

prices are therefore projected to increase by 2.4 percent this year. Only in 2013 will the rate of inflation revert to an annual 2 percent.

The slackening of business activity will also be felt on the labour market. The unemployment rate is expected to rise from 6.7 percent in 2011 to 7.1 percent this year. GDP growth in 2013 will not suffice to turn the trend around, the jobless rate thus heading further up. Also the hitherto lively job creation will ease: the rate of employment growth in 2012 will drop by half from 2011 to 0.8 percent and further to 0.4 percent in 2013.

Methodological Notes and Short Glossary

Period comparisons

Time-series comparisons with the previous period, e.g., the previous quarter, are adjusted for seasonal effects. They also include effects that result from a different number of working days in the period (e.g., Easter). In the text, reference is made to "seasonally and working day adjusted changes".

The phrase "changed compared with a year before . . .", on the other hand, describes a change compared with the same period a year before and refers to unadjusted time series.

The analysis of the seasonally and working day adjusted development provides more precise information about the actual course of economic activity and shows turning points sooner. However, the data are subject to additional revisions as seasonal adjustment is based on statistical methods.

Average rates of change

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

Real and nominal values

In principle, the values shown must be understood as real values, i.e., adjusted for price effects. Whenever values are shown as nominal values (e.g., foreign trade statistics), this is specifically mentioned.

Production Sector

This term comprises the NACE-2008 sections B, C and D (Mining and Quarrying, Manufacturing, Energy Supply) and is here used in an international comparison.

Inflation, CPI und HICP

The inflation rate measures changes in consumer prices compared with a year before. The Consumer Price Index (CPI) is a measure of national inflation. The Harmonised Index of Consumer Prices (HICP) is the basis for comparable measurement of inflation in the EU and for the evaluation of price stability in the euro area (see <http://www.statistik.at/>).

Core inflation as a monetary policy indicator is not clearly defined. WIFO follows the common practice of using the inflation rate excluding the product categories unprocessed food and energy for core inflation. Thus just under 87 percent of the goods and services contained in the consumer price index (CPI 2010) are included in the calculation of core inflation.

WIFO Business Cycle Survey and WIFO Investment Survey

The WIFO Business Cycle Survey is a monthly survey in which around 1,100 Austrian firms are asked to assess their current and future economic situation. The WIFO Investment Survey is conducted twice a year, asking companies about their investment activity (<http://www.iikt.at/>). The indicators are balances between the positive and negative responses expressed as a percentage of the total number of firms sampled.

Unemployment rate

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

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

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

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

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

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Projections - March 2012

Main results

Percentage changes from previous year

		2008	2009	2010	2011	2012	2013
GDP							
Volume		+ 1.4	- 3.8	+ 2.3	+ 3.1	+ 0.4	+ 1.4
Value		+ 3.2	- 2.8	+ 4.1	+ 5.3	+ 2.2	+ 2.9
Manufacturing¹, volume		+ 1.3	- 15.0	+ 7.2	+ 9.9	± 0.0	+ 3.5
Wholesale and retail trade, volume		- 3.0	+ 0.7	+ 3.1	+ 0.1	+ 0.5	+ 0.8
Private consumption expenditure, volume		+ 0.8	- 0.3	+ 2.2	+ 0.6	+ 0.8	+ 0.9
Gross fixed investment, volume		+ 0.7	- 8.3	+ 0.1	+ 5.7	+ 1.1	+ 2.0
Machinery and equipment		- 0.7	- 9.7	+ 4.3	+ 11.3	+ 1.8	+ 3.5
Construction		+ 1.0	- 7.6	- 2.9	+ 2.6	+ 0.4	+ 0.6
Exports of goods²							
Volume		+ 0.5	- 16.8	+ 12.8	+ 7.5	+ 3.5	+ 6.5
Value		+ 2.5	- 20.2	+ 16.7	+ 11.7	+ 4.0	+ 7.9
Imports of goods²							
Volume		+ 0.6	- 14.3	+ 10.3	+ 7.5	+ 3.7	+ 5.7
Value		+ 4.7	- 18.4	+ 16.5	+ 15.1	+ 5.3	+ 7.8
Current balance	€ bn	+ 13.76	+ 7.49	+ 8.46	+ 5.20	+ 4.45	+ 5.84
	as a percentage of GDP	+ 4.9	+ 2.7	+ 3.0	+ 1.7	+ 1.4	+ 1.8
Long-term interest rate³	percent	4.4	3.9	3.2	3.3	2.9	2.9
Consumer prices		+ 3.2	+ 0.5	+ 1.9	+ 3.3	+ 2.4	+ 2.0
Unemployment rate							
Eurostat definition ⁴	percent	3.8	4.8	4.4	4.2	4.6	4.8
National definition ⁵	percent	5.9	7.2	6.9	6.7	7.1	7.5
Persons in active dependent employment⁶		+ 1.7	- 1.5	+ 0.8	+ 1.9	+ 0.8	+ 0.4
General government financial balance							
according to Maastricht definition							
as a percentage of GDP		- 0.9	- 4.1	- 4.4	- 3.3	- 3.0	- 2.6

¹ Value added, including mining and quarrying. ² According to Statistics Austria. ³ 10-year central government bonds (benchmark). ⁴ According to Eurostat Labour Force Survey. ⁵ Public Employment Service Austria, percent of total labour force excluding self employed. ⁶ Excluding parental leave and military service.

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Key policy indicators

	2008	2009	2010	2011	2012	2013
Fiscal policy						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 0.9	- 4.1	- 4.4	- 3.3	- 3.0	- 2.6
according to National accounts	- 1.0	- 4.1	- 4.4	- 3.3	- 3.0	- 2.6
General government primary balance						
	+ 1.7	- 1.3	- 1.7	- 0.6	- 0.3	+ 0.1
Monetary policy						
	Percent					
3-month interest rate	4.6	1.2	0.8	1.4	1.1	1.5
Long-term interest rate ¹	4.4	3.9	3.2	3.3	2.9	2.9
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 1.2	+ 0.9	- 2.5	+ 0.1	- 0.8	± 0.0
Real	+ 0.6	+ 0.4	- 2.7	+ 0.7	- 0.7	± 0.0

¹ 10-year central government bonds (benchmark).

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World economy

Percentage changes from previous year

	2008	2009	2010	2011	2012	2013
Real GDP						
World	+ 2.8	- 0.7	+ 5.2	+ 3.8	+ 3.4	+ 4.0
USA	- 0.3	- 3.5	+ 3.0	+ 1.7	+ 2.0	+ 2.3
Japan	- 1.0	- 5.5	+ 4.4	- 0.7	+ 1.4	+ 1.9
EU 27	+ 0.3	- 4.3	+ 2.0	+ 1.5	+ 0.1	+ 1.6
Euro area 16	+ 0.4	- 4.3	+ 1.9	+ 1.4	- 0.2	+ 1.3
Germany	+ 1.1	- 5.1	+ 3.7	+ 3.0	+ 0.5	+ 1.6
New member states ¹	+ 4.2	- 3.0	+ 2.5	+ 3.2	+ 1.8	+ 3.2
China	+ 9.6	+ 9.2	+ 10.4	+ 9.2	+ 8.2	+ 8.2
World trade, volume	+ 2.5	- 12.6	+ 14.9	+ 5.6	+ 5.0	+ 7.0
Market growth²	+ 2.9	- 11.5	+ 11.4	+ 7.5	+ 3.0	+ 6.0
Primary commodity prices						
HWI Index, total	+ 32.7	- 34.7	+ 28.9	+ 28.6	+ 6	+ 3
Excluding energy	+ 18.7	- 28.4	+ 31.9	+ 19.2	± 0	+ 15
Crude oil prices						
Brent, USD per barrel	97.0	61.5	79.5	111.3	120	120
Exchange rate						
USD per euro	1.471	1.393	1.327	1.392	1.30	1.30

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

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

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Productivity

Percentage changes from previous year

	2008	2009	2010	2011	2012	2013
Total economy						
Real GDP	+ 1.4	- 3.8	+ 2.3	+ 3.1	+ 0.4	+ 1.4
Employment ¹	+ 2.1	- 0.9	+ 0.8	+ 1.7	+ 0.9	+ 0.6
Productivity (GDP per employment)	- 0.7	- 2.9	+ 1.5	+ 1.4	- 0.5	+ 0.8
Manufacturing						
Production ²	+ 0.9	- 15.3	+ 7.4	+ 10.4	± 0.0	+ 3.5
Employees ³	+ 1.7	- 5.3	- 1.3	+ 1.9	- 0.8	- 0.2
Productivity per hour	- 0.3	- 7.3	+ 5.6	+ 8.2	+ 0.8	+ 3.4
Working hours per day per employee ⁴	- 0.5	- 3.6	+ 3.0	+ 0.2	± 0.0	+ 0.3

¹ Dependent and self-employed according to National Accounts definition.

² Value added, volume.

³ According to Federation of Austrian Social Security Institutions.

⁴ According to 'Konjunkturerhebung' of Statistics Austria.

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Private consumption, income and prices

	2008	2009	2010	2011	2012	2013
Percentage changes from previous year, volume						
Private consumption expenditure	+ 0.8	- 0.3	+ 2.2	+ 0.6	+ 0.8	+ 0.9
Durables	+ 3.7	+ 0.9	+ 5.8	+ 0.9	- 0.5	+ 0.3
Non-durables and services	+ 0.5	- 0.4	+ 1.8	+ 0.6	+ 0.9	+ 1.0
Household disposable income	+ 0.9	- 1.7	- 0.3	+ 0.2	+ 0.7	+ 1.0
As a percentage of disposable income						
Household saving ratio¹	11.5	10.7	8.3	7.5	7.3	7.4
Household saving ratio²	11.4	10.1	7.8	7.4	7.3	7.4
Percentage changes from previous year						
Direct lending to domestic non-banks³	+ 7.4	- 1.3	+ 2.9	+ 2.6	+ 2.5	+ 2.7
Inflation rate						
National	3.2	0.5	1.9	3.3	2.4	2.0
Harmonised	3.2	0.4	1.7	3.6	2.5	2.1
Core inflation ⁴	2.4	1.5	1.2	2.8	2.4	2.0

¹ Including adjustment for the change in net equity of households in pension fund reserves.

² Excluding adjustment for the change in net equity of households in pension fund reserves.

³ End of period.

⁴ Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

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Earnings and international competitiveness

Percentage changes from previous year

	2008	2009	2010	2011	2012	2013
Wages and salaries per employee¹						
Gross earnings	+ 3.2	+ 1.6	+ 1.2	+ 2.7	+ 3.2	+ 2.2
Gross real earnings²	- 0.0	+ 1.1	- 0.6	- 0.5	+ 0.8	+ 0.2
Net real earnings²	- 0.7	+ 2.9	- 0.8	- 0.8	+ 0.6	- 0.1
Unit labour costs						
Total economy	+ 3.7	+ 4.7	- 0.3	+ 1.2	+ 3.6	+ 1.3
Manufacturing	+ 5.2	+ 15.1	- 5.7	- 4.5	+ 3.2	- 1.3
Effective exchange rate - manufactures						
Nominal	+ 1.1	+ 0.7	- 2.6	+ 0.0	- 0.8	- 0.1
Real	+ 0.6	+ 0.4	- 2.7	+ 0.7	- 0.7	± 0.0

¹ Employees according to National Accounts definition.

² Deflated by CPI.

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Labour market

Changes from previous year (1,000^s)

		2008	2009	2010	2011	2012	2013
Demand for labour							
Persons in active employment ¹		+ 66.0	- 44.0	+ 31.3	+ 70.5	+ 30.0	+ 20.0
Employees ²		+ 55.6	- 48.5	+ 25.5	+ 63.3	+ 25.0	+ 15.0
Percentage changes from previous year		+ 1.7	- 1.5	+ 0.8	+ 1.9	+ 0.8	+ 0.4
Nationals		+ 31.1	- 43.0	+ 5.8	+ 25.7	+ 10.0	+ 6.0
Foreign workers		+ 24.5	- 5.5	+ 19.7	+ 37.7	+ 15.0	+ 9.0
Self-employed ³		+ 10.4	+ 4.5	+ 5.8	+ 7.2	+ 5.0	+ 5.0
Labour supply							
Population of working age	(15 to 64 years)	+ 27.7	+ 17.3	+ 21.6	+ 32.8	+ 15.0	+ 6.7
	(15 to 59 years)	+ 17.6	+ 11.1	+ 8.9	+ 16.8	+ 14.7	+ 10.8
Labour force ⁴		+ 56.0	+ 4.0	+ 21.8	+ 66.4	+ 48.0	+ 34.5
Surplus of labour							
Registered unemployed ⁵		- 10.0	+ 48.1	- 9.5	- 4.1	+ 18.0	+ 14.5
	1,000 ^s	212.3	260.3	250.8	246.7	264.7	279.2
Unemployed persons in training	1,000 ^s	50.5	64.1	73.2	63.2	65.2	68.2
Unemployment rate							
Eurostat definition ⁶	percent	3.8	4.8	4.4	4.2	4.6	4.8
Percent of total labour force ⁵	percent	5.3	6.5	6.2	6.0	6.4	6.7
National definition ^{5,7}	percent	5.9	7.2	6.9	6.7	7.1	7.5
Employment rate							
Persons in active employment ^{1,8}	percent	65.7	64.7	65.0	65.9	66.3	66.5
Total employment (Eurostat) ^{6,8}	percent	72.1	71.6	71.7	72.2	72.5	72.6

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

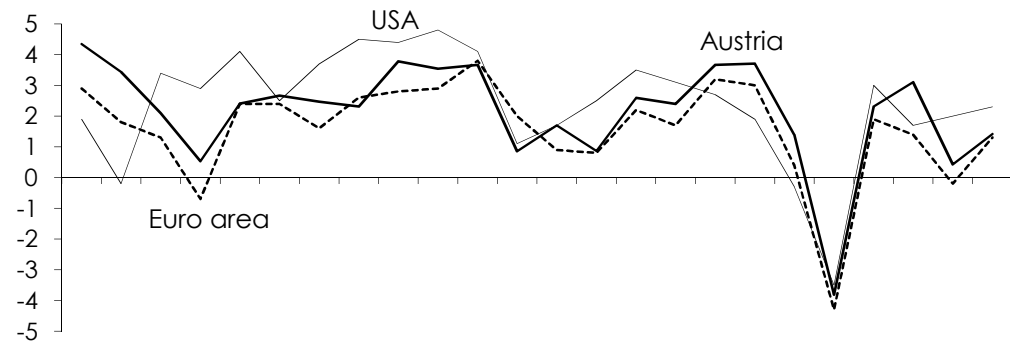
³ According to WIFO. ⁴ Persons in active employment plus unemployment.

⁵ According to Public Employment Service Austria ⁶ According to Eurostat Labour Force Survey.

⁷ Percent of total labour force excl. self-employed. ⁸ Percent of population of working age (15 to 64 years).

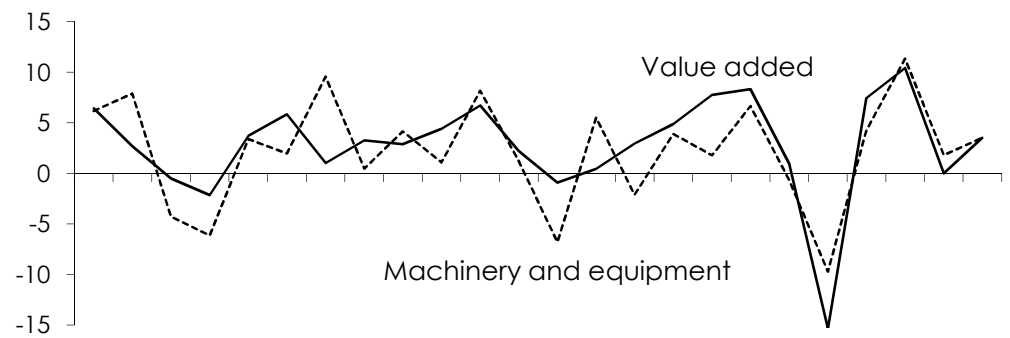
Growth of real GDP

Percent



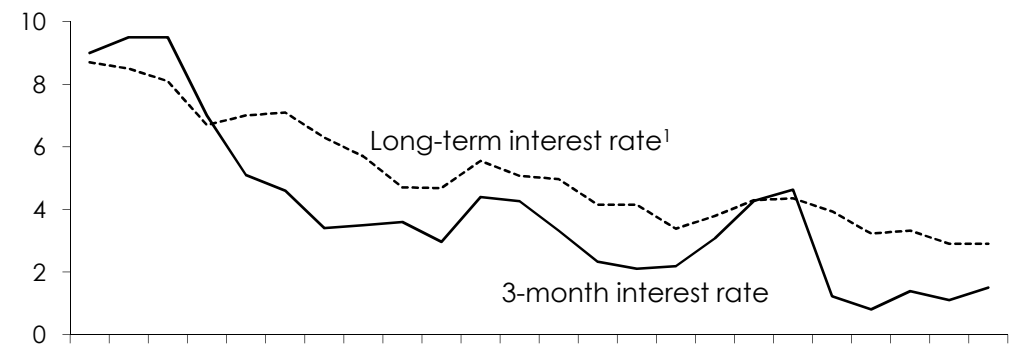
Manufacturing and investment

Percentage changes from previous year, volume



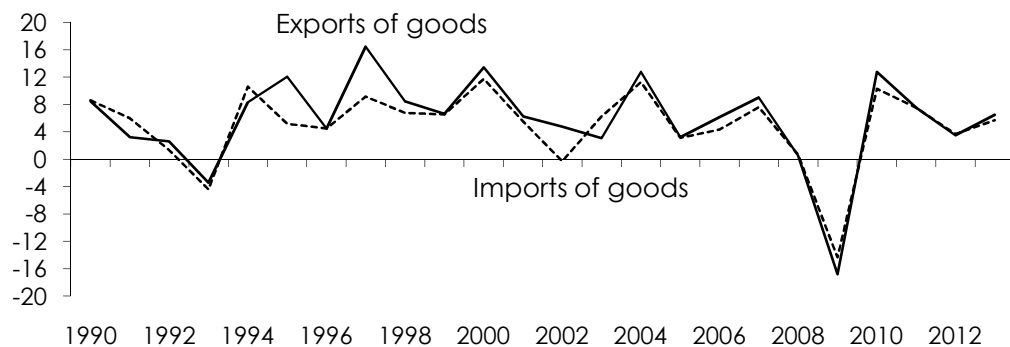
Short-term and long-term interest rates

Percent



Trade

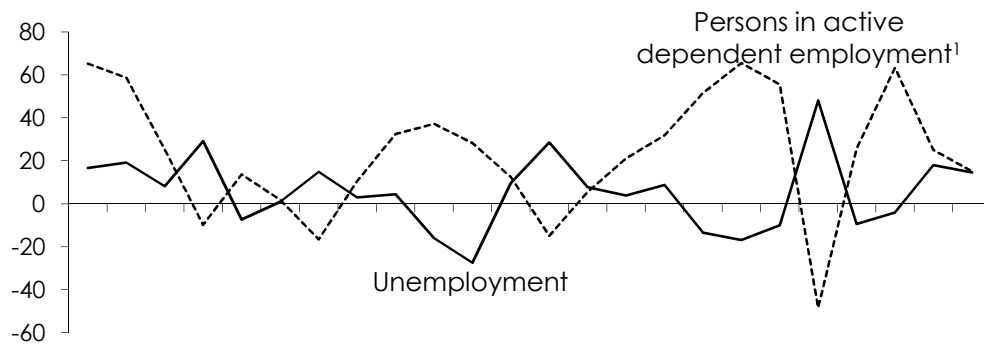
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

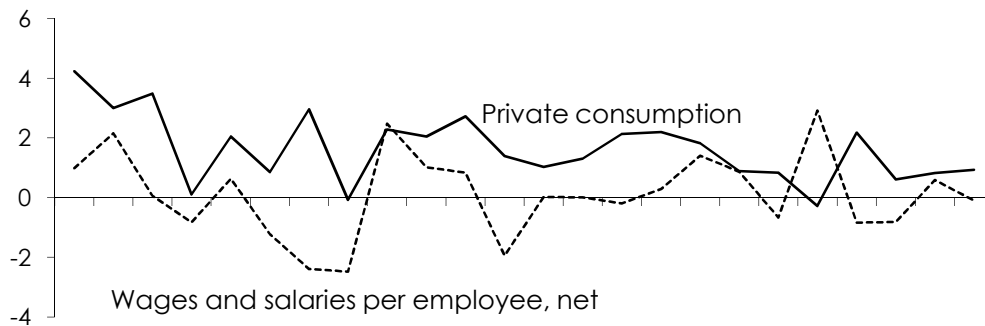
Employment and unemployment

1,000^s from previous year



Consumption and income

Percentage changes from previous year, volume



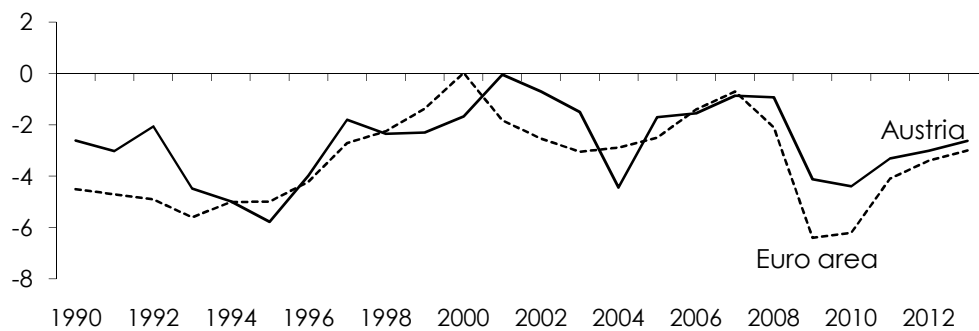
Inflation and unit labour costs

Percentage changes from previous year



General government financial balance

As a percentage of GDP



¹ Excluding parental leave, military service, and unemployed persons in training.