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WIRTSCHAFTSFORSCHUNG**

**Cyclical Upturn Gaining Full
Momentum – Solid Growth
Also in 2007**

Economic Outlook for 2006 and 2007

October 2006

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Economic Outlook for 2006 and 2007

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Economic Outlook for 2006 and 2007: Cyclical Upturn Gaining Full Momentum – Solid Growth Also in 2007

As from the second semester 2005, favourable business conditions worldwide have set in motion a cyclical upswing in Austria, which has been gaining strength in the current year. Demand incentives have been transmitted from exports to domestic investment, thereby fostering the sustainability of the upturn. Slackening external demand, partly related to one-off factors in Germany, will slow the overall pace of growth in 2007, although internal demand will benefit from a revival of private consumption.

WIFO at present sees the short-term economic outlook for Austria markedly more positive than at the time of its last forecast at the end of June. For 2006, GDP growth is revised upwards by ½ percentage point to a rate of 3.1 percent, the projection for 2007 is for a rate of 2.5 percent. In both years, growth would thereby remain above the euro area average. Domestic business fixed investment has picked up much more strongly than expected three months ago, with a likely increase by 5 percent in volume for the year as a whole. Demand is lively for both machinery and equipment as well as for new structures. Lively investment is set to extend into 2007, albeit at a somewhat slower pace of 4 percent.

Goods exports, the principal driver of the upswing, are gaining 10 percent in volume in 2006. Part of the momentum is due to purchases carried forward in Germany ahead of the VAT increase at the beginning of 2007. The expected jump in car purchases in Germany will give a boost also to domestic suppliers to the German motor car industry. Correspondingly, 2007 will see a slump in demand and, more generally, global demand will slacken. Austrian exports will therefore post more moderate gains of less than 7 percent in volume.

Private consumption in Austria, while rising markedly faster (at 1.9 percent in volume) than on average during the last few years, is trailing other demand components. Growth in 2007, although edging up to 2.1 percent, will still be weaker than in earlier

periods of cyclical upswing, since household disposable income will increase only moderately, despite gains in employment.

In the wake of the cyclical revival, the number of people in dependent active employment is rising substantially this year, by 46,000 or 1.5 percent. In manufacturing, the downward trend of the past years is coming to a halt, and the construction sector is adding importantly to its workforce. Employment creation is increasingly extending to full-time jobs. The number of registered unemployed is falling by 11,000 this year, to a total 242,000. This mirrors the rebound in economic activity, but also the efforts to enrol more people in job training. Although growth is set to abate, unemployment is expected to remain flat in 2007. The jobless rate, on national definitions, is receding to 6.9 percent of the dependent labour force this year and to 6.8 percent in 2007.

Despite the important price increases for energy and other commodities in the last few years, second-round inflationary effects are still largely absent. The below-average pace of growth so far and the subdued labour market situation have prevented a more noticeable pass-through of the oil price jump to the consumer price index. For 2006, WIFO expects an average inflation rate of 1.6 percent, edging up to 1.7 percent in 2007. Although improved business conditions in the euro area will add to inflation, the impact of higher energy prices is expected to ebb in 2007.

Because of some lags in the impact of the 2005 tax reform, the general government deficit is going up from 1.5 percent of GDP in 2005 to 1.6 percent this year. Only in 2007 will the rebound in domestic demand reduce the deficit to 1.3 percent of nominal GDP.

Vienna, 6 October 2006

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Projections - September 2006

Main results

Percentage changes from previous year

		2002	2003	2004	2005	2006	2007
GDP							
Volume		+ 0.9	+ 1.1	+ 2.4	+ 2.0	+ 3.1	+ 2.5
Value		+ 2.3	+ 2.4	+ 4.2	+ 3.9	+ 4.7	+ 4.2
Manufacturing¹, volume		+ 0.4	+ 0.1	+ 2.4	+ 2.4	+ 6.7	+ 5.0
Wholesale and retail trade, volume		+ 2.3	+ 0.5	+ 1.3	+ 0.3	+ 1.7	+ 2.1
Private consumption expenditure, volume		+ 0.1	+ 1.3	+ 1.9	+ 1.7	+ 1.9	+ 2.1
Gross fixed investment, volume		- 6.0	+ 5.9	+ 0.6	+ 0.3	+ 5.0	+ 4.0
Machinery and equipment ²		- 7.9	+ 6.8	- 0.7	+ 0.1	+ 7.0	+ 5.5
Construction		- 4.5	+ 5.1	+ 1.6	+ 0.4	+ 3.5	+ 2.7
Exports of goods³							
Volume		+ 4.8	+ 2.6	+ 12.9	+ 2.2	+ 10.1	+ 6.8
Value		+ 4.2	+ 1.9	+ 13.9	+ 5.4	+ 12.9	+ 7.9
Imports of goods³							
Volume		- 0.1	+ 6.5	+ 11.4	+ 2.3	+ 8.0	+ 7.0
Value		- 2.0	+ 5.0	+ 12.5	+ 5.9	+ 11.8	+ 8.3
Current balance	€ bn	+ 0.75	- 0.48	+ 0.36	+ 3.01	+ 3.25	+ 3.18
	as a percentage of GDP	+ 0.3	- 0.2	+ 0.2	+ 1.2	+ 1.3	+ 1.2
Long-term interest rate⁴	percent	5.0	4.2	4.2	3.4	3.8	4.2
Consumer prices		+ 1.8	+ 1.3	+ 2.1	+ 2.3	+ 1.6	+ 1.7
Unemployment rate							
Eurostat definition ⁵	percent	4.2	4.3	4.8	5.2	5.0	5.0
National definition ⁶	percent	6.9	7.0	7.1	7.3	6.9	6.8
Persons in active dependent employment⁷		- 0.5	+ 0.2	+ 0.7	+ 1.0	+ 1.5	+ 1.2
General government financial balance							
according to Maastricht definition							
as a percentage of GDP		- 0.5	- 1.6	- 1.2	- 1.5	- 1.6	- 1.3

¹ Value added, including mining and quarrying. ² Including other products. ³ According to Statistics Austria.

⁴ 10-year central government bonds (benchmark). ⁵ According to Eurostat Labour Force Survey. ⁶ According to Labour Market Service, percent of total labour force excluding self employed. ⁷ Excluding parental leave, military service, and unemployed persons in training.

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Projections - September 2006

Key policy indicators

	2002	2003	2004	2005	2006	2007
<i>Fiscal policy</i>						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 0.5	- 1.6	- 1.2	- 1.5	- 1.6	- 1.3
according to National accounts	- 0.7	- 1.7	- 1.3	- 1.6	- 1.7	- 1.4
General government primary balance	+ 2.6	+ 1.3	+ 1.6	+ 1.3	+ 1.2	+ 1.4
<i>Monetary policy</i>						
	Percent					
3-month interest rate	3.3	2.3	2.1	2.2	3.1	3.8
Long-term interest rate ¹	5.0	4.2	4.2	3.4	3.8	4.2
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 1.3	+ 3.8	+ 1.2	- 0.6	+ 0.2	± 0.0
Real	+ 0.6	+ 2.8	+ 0.9	- 0.7	- 0.7	- 1.0

¹ 10-year central government bonds (benchmark).

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Projections - September 2006

World economy

Percentage changes from previous year

	2002	2003	2004	2005	2006	2007
Real GDP						
World	+ 3.1	+ 4.1	+ 5.3	+ 4.9	+ 5.0	+ 4.5
Total OECD	+ 1.6	+ 2.0	+ 3.2	+ 2.6	+ 3.0	+ 2.5
USA	+ 1.6	+ 2.5	+ 3.9	+ 3.2	+ 3.3	+ 2.5
Japan	+ 0.1	+ 1.8	+ 2.3	+ 2.6	+ 2.8	+ 2.5
EU 25	+ 1.2	+ 1.3	+ 2.4	+ 1.6	+ 2.7	+ 2.4
EU 15	+ 1.1	+ 1.1	+ 2.2	+ 1.5	+ 2.6	+ 2.3
Euro area	+ 0.9	+ 0.8	+ 1.9	+ 1.4	+ 2.6	+ 2.3
Germany	± 0.0	- 0.2	+ 1.2	+ 0.9	+ 2.4	+ 1.7
New members ¹	+ 2.5	+ 3.8	+ 5.1	+ 4.4	+ 5.2	+ 5.0
China	+ 9.1	+ 10.0	+ 10.1	+ 10.2	+ 10.0	+ 9.5
World trade, volume	+ 3.5	+ 5.0	+ 10.0	+ 7.1	+ 8.5	+ 7.5
Market growth²	+ 2.0	+ 5.6	+ 9.1	+ 6.8	+ 9.0	+ 6.0
Primary commodity prices						
HWWA Index, total	- 5	- 4	+ 18	+ 29	+ 27	+ 0
Excluding energy	- 6	- 6	+ 18	+ 6	+ 22	+ 1
Crude oil prices						
Average import price (cif) for OECD countries	24.1	28.4	36.3	50.3	65.0	65.0
Exchange rate						
USD per euro	0.945	1.131	1.243	1.245	1.25	1.25

¹ Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, Slovenia.

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

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Projections - September 2006

Private consumption, income and prices

	2002	2003	2004	2005	2006	2007
	Percentage changes from previous year, volume					
Private consumption expenditure	+ 0.1	+ 1.3	+ 1.9	+ 1.7	+ 1.9	+ 2.1
Durables	+ 2.8	+ 3.1	+ 5.1	+ 2.2	+ 2.1	+ 2.5
Non-durables and services	- 0.3	+ 1.1	+ 1.5	+ 1.6	+ 1.9	+ 2.1
Household disposable income	+ 0.3	+ 2.1	+ 2.0	+ 2.1	+ 2.3	+ 2.1
Household saving ratio						
As a percentage of disposable income	7.6	8.6	8.8	9.1	9.5	9.4
	Percentage changes from previous year					
Direct lending to domestic non-banks¹	+ 1.2	+ 1.6	+ 5.0	+ 4.7	+ 5.8	+ 4.5
	Percentage changes from previous year					
Inflation rate						
National	1.8	1.3	2.1	2.3	1.6	1.7
Harmonised	1.7	1.3	2.0	2.1	1.9	1.9
Core inflation ²	2.0	1.3	1.6	1.5	1.3	1.8

¹ End of period.

² Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

Productivity

Percentage changes from previous year

	2002	2003	2004	2005	2006	2007
Total economy						
Real GDP	+ 0.9	+ 1.1	+ 2.4	+ 2.0	+ 3.1	+ 2.5
Employment ¹	- 0.1	- 0.0	- 0.0	+ 0.5	+ 1.0	+ 0.8
Productivity (GDP per employment)	+ 1.0	+ 1.1	+ 2.5	+ 1.6	+ 2.0	+ 1.7
Manufacturing						
Production ²	+ 0.4	+ 0.1	+ 2.3	+ 2.6	+ 6.7	+ 5.0
Employees ³	- 2.5	- 1.7	- 0.6	- 0.9	± 0.0	- 0.2
Productivity per hour	+ 3.5	+ 1.4	+ 2.0	+ 4.1	+ 6.1	+ 5.2
Working hours per day per employee ⁴	- 0.5	+ 0.3	+ 0.8	- 0.6	+ 0.6	± 0.0

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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Projections - September 2006

Earnings and international competitiveness

Percentage changes from previous year

	2002	2003	2004	2005	2006	2007
Gross earnings per employee ¹	+ 2.2	+ 1.9	+ 1.9	+ 1.7	+ 2.8	+ 2.5
Gross real earnings per employee ¹	+ 1.0	+ 0.3	- 0.0	+ 0.0	+ 1.2	+ 0.8
Net real earnings per employee ¹	+ 0.7	+ 0.0	+ 0.1	+ 1.1	+ 0.6	+ 0.3
<i>Total economy</i>						
Unit labour costs	+ 1.1	+ 0.7	- 0.8	+ 0.2	+ 1.1	+ 0.8
<i>Manufacturing</i>						
Unit labour costs	- 0.6	+ 0.8	- 0.8	- 0.7	- 3.3	- 2.3
Relative unit labour costs ²						
Vis-à-vis trading partners	- 1.1	+ 3.6	+ 2.1	+ 0.1	- 2.3	- 1.6
Vis-à-vis Germany	- 1.9	+ 2.4	+ 3.2	+ 2.9	- 0.8	- 0.3
Effective exchange rate - manufactures						
Nominal	+ 1.2	+ 3.7	+ 1.2	- 0.5	+ 0.2	± 0.0
Real	+ 0.8	+ 2.9	+ 1.0	- 0.5	- 0.6	- 1.0

¹ Employees according to National Accounts definition.

² In a common currency; minus sign indicates improvement of competitiveness.

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Projections - September 2006

Labour market

Changes from previous year (1,000^s)

		2002	2003	2004	2005	2006	2007
Demand for labour							
Persons in active employment ¹		- 11.6	+ 8.5	+ 25.1	+ 37.2	+ 51.5	+ 43.5
Employees ²		- 15.0	+ 5.5	+ 21.1	+ 31.9	+ 46.0	+ 38.0
<i>Percentage changes from previous year</i>		- 0.5	+ 0.2	+ 0.7	+ 1.0	+ 1.5	+ 1.2
Nationals		- 20.1	- 10.4	+ 9.2	+ 20.0	+ 30.0	+ 24.0
Foreign workers		+ 5.1	+ 15.9	+ 11.9	+ 11.9	+ 16.0	+ 14.0
Self-employed ³		+ 3.4	+ 3.0	+ 4.0	+ 5.3	+ 5.5	+ 5.5
Labour supply							
Population of working age	(15 to 64 years)	+ 42.9	+ 37.7	+ 34.4	+ 15.6	+ 6.1	+ 20.2
	(15 to 59 years)	+ 13.4	+ 21.2	+ 35.6	+ 48.5	+ 37.7	+ 24.9
Labour force ⁴		+ 17.0	+ 16.1	+ 28.9	+ 45.9	+ 40.5	+ 43.5
Surplus of labour							
Registered unemployed ⁵		+ 28.5	+ 7.7	+ 3.8	+ 8.8	- 11.0	± 0.0
	1,000 ^s	232.4	240.1	243.9	252.7	241.7	241.7
Unemployment rate							
Eurostat definition ⁶	percent	4.2	4.3	4.8	5.2	5.0	5.0
Percent of total labour force ⁵	percent	6.2	6.3	6.4	6.5	6.2	6.1
National definition ^{5,7}	percent	6.9	7.0	7.1	7.3	6.9	6.8
Employment rate							
Persons in active employment ^{1,8}	percent	62.5	62.2	62.3	62.8	63.6	64.2
Total employment (Eurostat) ^{6,8,9}	percent	-	-	67.8	68.6	68.9	69.2

¹ Excluding parental leave, military service, and unemployed persons in training. ² According to Federation of Austrian Social Security Institutions. ³ According to WIFO. ⁴ Economically active employment plus unemployment.

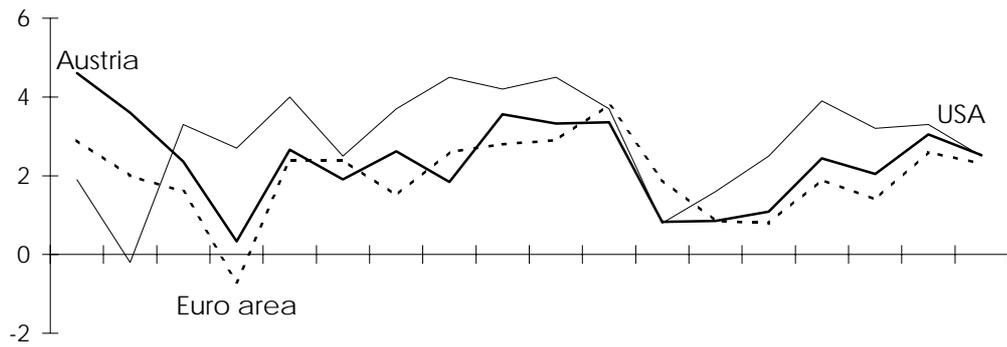
⁵ According to Labour Market Service. ⁶ According to Eurostat Labour Force Survey.

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

⁹ Changed survey method.

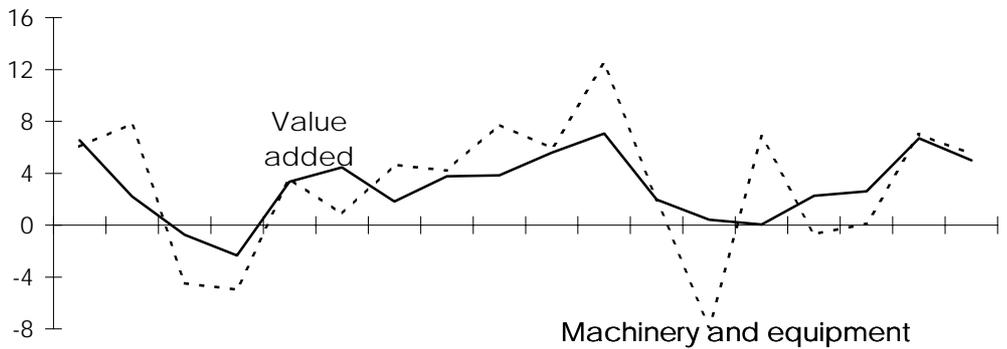
Growth of real GDP

Percent



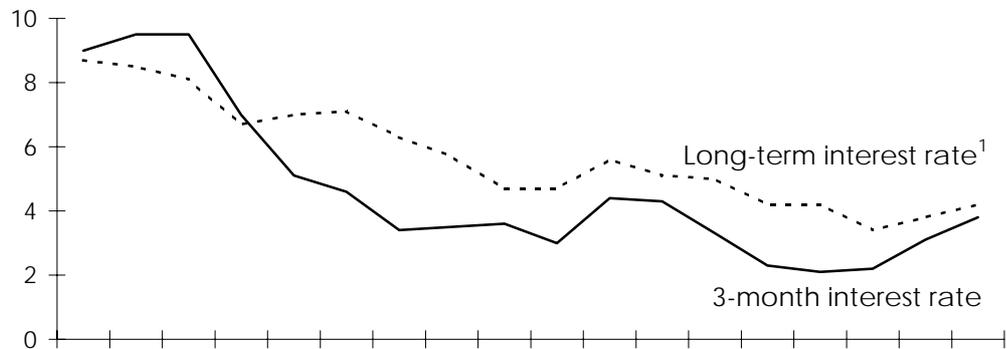
Manufacturing and investment

Percentage changes from previous year, volume



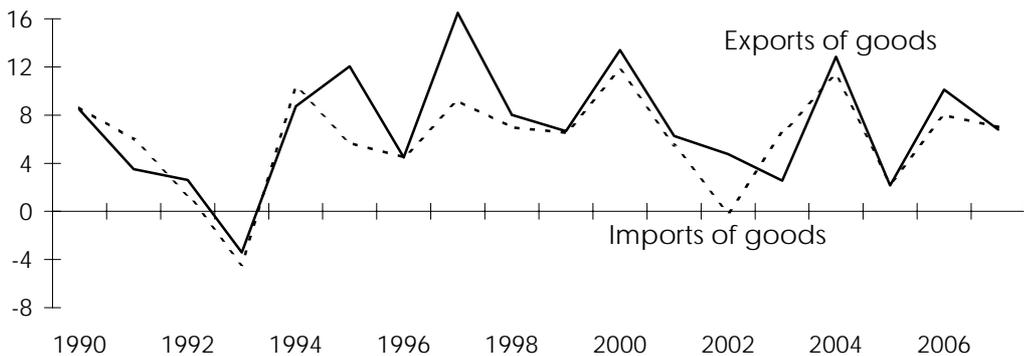
Short-term and long-term interest rates

Percent



Trade

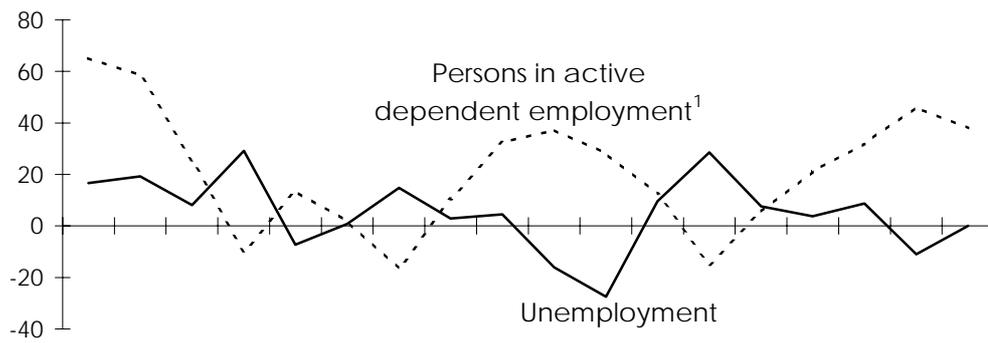
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

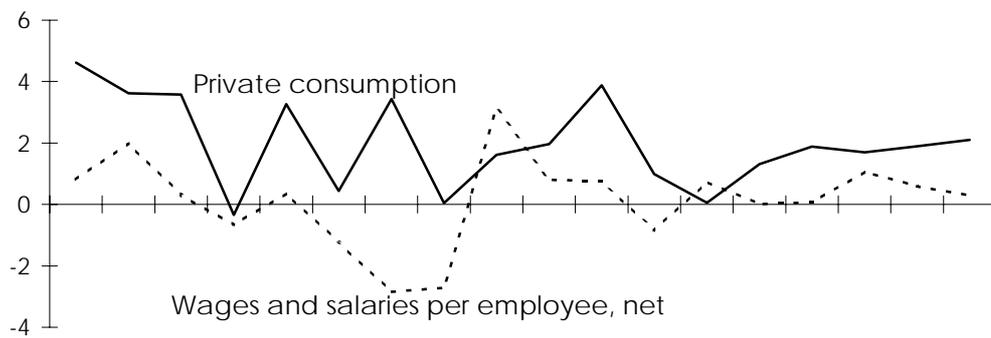
Employment and unemployment

1,000^s from previous year



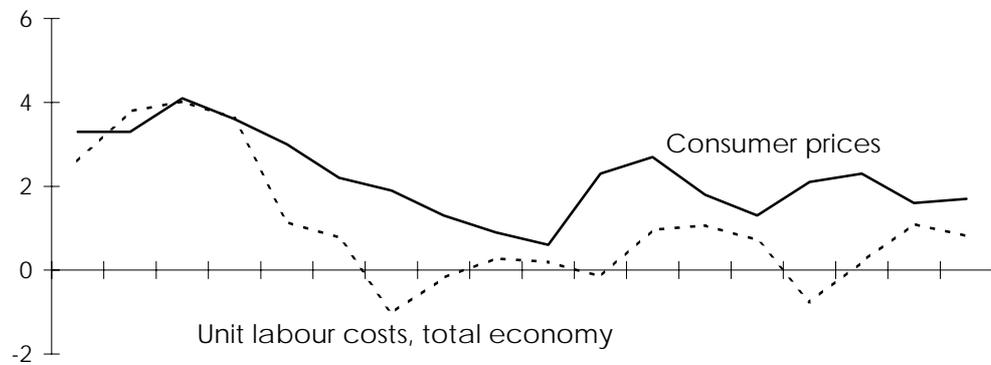
Consumption and income

Percentage changes from previous year, volume



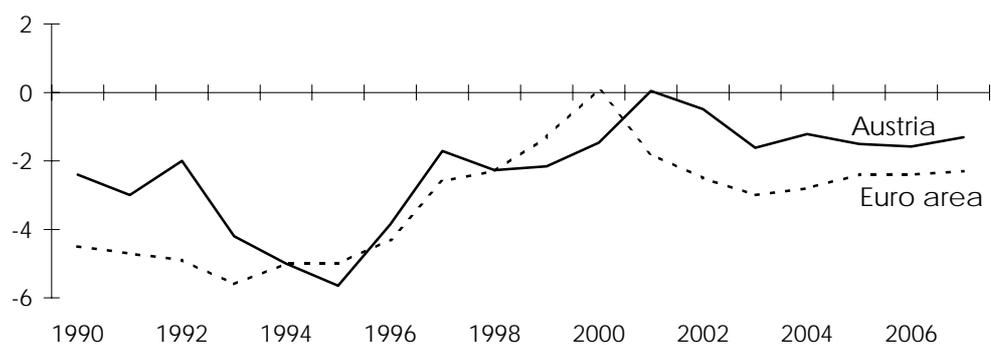
Inflation and unit labour costs

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.

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