Recovery of the Austrian Economy Continues

Economic Outlook for Austria from 2010 to 2012 (December 2010)

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1 Summary: Robust Growth Despite Fiscal Consolidation

In the December 2010 economic outlook, the Oesterreichische Nationalbank (OeNB) expects the Austrian economy to grow by 1.9% in 2010, after it had contracted by 3.7% in 2009. Growth will pick up further in 2011 and 2012, reaching 2.1% and 2.3% respectively. The prospects for growth are now better than expected in the OeNB's economic outlook of June 2010, despite the fiscal consolidation measures that have been adopted in the meantime. On average, the annual growth outlook has been revised upwards by ¼ percentage point p. a. The recovery is being driven mainly by exports. Domestic demand remains subdued, not least on account of the budgetary consolidation measures adopted by the Austrian government. The proposed increases in taxes will temporarily push inflation up to 2.2%. The budget deficit will rise to 4.1% of GDP in 2010, but the favorable growth prospects and the fiscal consolidation measures will bring it down again, to below the 3% mark by 2012.

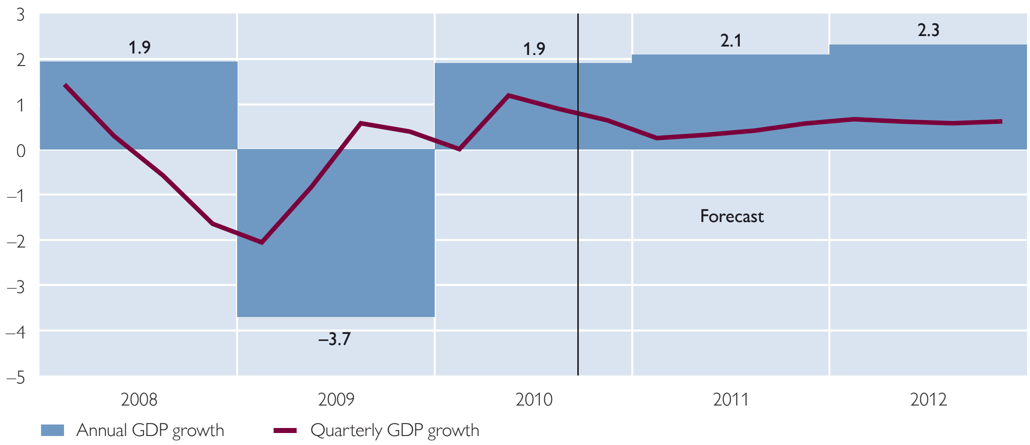
The global economic upturn will continue over the forecasting horizon, but the downturn in the inventory cycle, the expiry of fiscal stimuli and the simultaneous onset of intensified efforts to consolidate the budget will make it lose momentum in the next few months. Moreover, the pace of the recovery will vary, which holds true of both global economic activity in general and that in Europe in particular. The increase in heterogeneity of developments across the globe means that Austria's growth prospects remain subject to high macroeconomic risks from abroad.

The main drivers of economic activity in Austria are the global recovery

Chart 1

Real GDP Growth (Seasonally and Working Day-Adjusted)

Quarterly and annual changes in %



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and, above all, robust economic growth in Germany, Austria's main trading partner. Although, given the above-average importance of trade in machinery and transport equipment, Austria's export industry was affected particularly severely by the crisis in worldwide trade, it was able also to benefit significantly from the current recovery. As a whole, exports in goods and services are thus expected to expand by 10½% in real terms in 2010. In the next few years, however, the upturn will slow down in parallel to the more moderate evolution of global trade, returning to the pre-crisis level of around 7%.

Domestic demand, by contrast, is developing far less dynamically. Given the decline in capacity utilization recorded in the course of the crisis, it was only towards the middle of 2010 that the growth of investment in plant and equipment returned to positive territory, thus far later than in previous periods of upswing. Capacity-enhancing investment in plant and equipment is not to be expected before 2011 and 2012. The outlook for construction investment remains subdued across the whole forecasting horizon. In 2010 as a whole, gross fixed capital formation will continue to decline. Companies' investment activity will not increase until 2011 and 2012, and the pace of expansion will remain slow.

Given the weakness of developments in real wages and salaries, households' expenditure on consumption continued to be subdued in 2010, despite the recovery in business activity. Although households' various kinds of income (compensation of employees, investment income, income from self-employment and operating surpluses) will again rise more markedly in the next two years, the fiscal consolidation measures will impose a burden on their real disposable income, and thus consumer spending. All in all, these measures will reduce private consumption by ¼ to ½ of a percentage point in both 2011 and 2012, so that consumption growth will range between 1% and 1½%.

Given the scale of the slump in business activity, the impact of the economic and financial crisis on the Austrian labor market has been relatively limited. The unemployment rate (Eurostat definition) has risen from 3.8% in 2008 to 4.8% in 2009. And, in the current upswing, the labor market developments are again proving to be a pleasant surprise. The pick-up in economic activity in the course of the year to date has already led to a significant expansion of employment, so that the total number of employed in 2010 as a whole is expected to rise by 35,000, a trend that should continue over the next two years. On account of the clearly procyclical behavior of the labor supply, however, the unemployment rate will decline only slightly to 4.3%.

HICP inflation will amount to 1.7% in 2010, and will rise to 2.2% in 2011. That increase is due primarily to the measures announced within the scope of the fiscal consolidation package, which will have the effect of raising HICP inflation by 0.4 percentage points in 2011.

With the support of the recovery in business activity and assuming that the fiscal consolidation package will be implemented as planned, the general government budget balance will decline to –2.6% of GDP by 2012.

Table 1

OeNB December 2010 Outlook for Austria – Key Results[1]

	2009	2010	2011	2012
Economic activity	*Annual change in % (real)*			
Gross domestic product	–3.7	+1.9	+2.1	+2.3
Private consumption	+1.1	+1.0	+1.0	+1.3
Government consumption	+0.4	+0.3	+0.3	+0.3
Gross fixed capital formation	–9.1	–3.3	+2.1	+3.0
Exports of goods and services	–13.6	+10.4	+7.3	+6.9
Imports of goods and services	–12.5	+6.8	+6.0	+6.2
	% of nominal GDP			
Current account balance	+2.9	+2.5	+3.4	+4.5
Contribution to real GDP growth	*Percentage points of GDP*			
Private consumption	+0.6	+0.5	+0.6	+0.7
Government consumption	+0.1	+0.1	+0.1	+0.1
Gross fixed capital formation	–2.0	–0.7	+0.4	+0.6
Domestic demand (excluding changes in inventories)	–1.3	–0.1	+1.0	+1.3
Net exports	–1.5	+2.2	+1.2	+1.0
Changes in inventories (including statistical discrepancy)	–0.9	–0.2	–0.1	+0.0
Prices	*Annual change in %*			
Harmonised Index of Consumer Prices (HICP)	+0.4	+1.7	+2.2	+1.8
Private consumption expenditure (PCE) deflator	–0.7	+1.7	+2.1	+1.9
GDP deflator	+1.0	+1.6	+1.8	+1.6
Unit labor costs in the total economy	+4.9	+0.1	+1.1	+0.7
Compensation per employee (at current prices)	+1.9	+1.1	+2.3	+2.2
Productivity (whole economy)	–2.8	+1.0	+1.2	+1.5
Compensation per employee (real)	+2.6	–0.5	+0.2	+0.3
Import prices	–1.3	+3.2	+2.4	+1.6
Export prices	–1.5	+1.4	+2.7	+1.8
Terms of trade	–0.2	–1.8	+0.3	+0.1
Income and savings				
Real disposable household income	–0.1	+0.7	+0.7	+1.4
	% of nominal disposable household income			
Saving ratio	11.0	10.9	10.5	10.5
Labor market	*Annual change in %*			
Payroll employment	–1.0	+0.8	+1.1	+0.9
	% of labor supply			
Unemployment rate (Eurostat definition)	4.8	4.5	4.4	4.3
Budget	*% of nominal GDP*			
Budget balance (Maastricht definition)	–3.5	–4.1	–3.0	–2.6
Government debt	67.5	69.6	70.4	70.6

Source: 2009: Eurostat. Statistics Austria; 2010 to 2012: OeNB December 2010 outlook.

[1] The outlook was drawn up on the basis of seasonally adjusted and working-day adjusted national accounts data. Therefore. the historical values for 2009 may deviate from the nonadjusted data released by Statistics Austria.

2 Technical Assumptions

This forecast for Austria is the contribution of the OeNB to the December 2010 Eurosystem staff macroeconomic projections. The forecasting horizon extends from the fourth quarter of 2010 to the fourth quarter of 2012. All assumptions with respect to how the global economy will develop, as well as the technical assumptions relating to interest rates, exchange rates and crude oil prices, take developments up to and including November 15, 2010, into account. The forecast was prepared on the basis of the OeNB's quarterly macroeconomic model, using seasonally and working day-adjusted national accounts data computed by the Austrian Institute for Economic Research (WIFO), which were fully available up to the second quarter of 2010, as the key source of data. The data for the third quarter are based on GDP flash estimates, which cover only part of the aggregates in the national accounts, however. The short-term interest rates used for the forecasting horizon are based on market expectations for the three-month EURIBOR, namely 0.8% in 2010, 1.4% in 2011 and 1.7% in 2012. Long-term interest rates reflect market expectations for ten-year government bonds, and have been set at 3.2% (2010), 3.4% (2011) and 3.7% (2012). The exchange rate of the euro vis-à-vis the U.S. dollar is assumed to remain at USD 1.39. The projected trend in crude oil prices is based on futures prices. The oil price assumed for 2010 is USD 79.5 per barrel of Brent, while those for 2011 and 2012 are set at USD 88.6 and USD 90.7, respectively. The prices of commodities excluding energy are also based on futures prices over the forecasting horizon.

3 Diverging Growth Rates Characterize Global Economic Outlook

Thanks both to huge monetary and fiscal policy support measures and to robust business activity in emerging Asia, the world economy's recovery from the global economic and financial crisis since mid-2009 has been faster than expected. The economic upswing across the globe will continue over the forecasting horizon, although the dynamic growth recorded in past quarters will no longer be equaled. The downturn in the inventory cycle, the expiry of fiscal policy stimuli and the simultaneous intensification of endeavors to consolidate the budgets will cause the pace of the upturn in worldwide economic activity and trade to decline in the next few months. Global economic growth will fall from 4.7% in 2010 to some 4% per annum in both 2011 and 2012, while the rate of increase in global trade will drop from 11½% to around 7½%.

The rather favorable outlook for the global economy should not, however, cause the fact to be overlooked that, given the heterogeneity of developments across the globe, the risks involved remain high. The pace of recovery varies, a fact that holds true both for global economic activity in general and for Europe in particular. At the global level, the dynamism of emerging economies in Asia and Latin America stands in contrast to the many impediments to growth in the industrialized countries. Whereas emerging countries like China tend to face the risk of a possible overheating of the economy, growth in many industrialized countries is curbed by problems on financial and real estate markets, by high government debt and by labor market tensions. In Europe, some countries are feeling the impact of the debt crisis and suffer from inadequate competitiveness, while other countries – with Germany topping the list – are enjoying surprisingly high growth rates and robust developments in the labor market. The diversity of economic developments across the globe is also reflected in imbalances on global markets for goods and foreign exchange, without any sign of these imbalances being dismantled within the period under review.

After the strong recovery recorded in the first half of 2010, the outlook for the *U.S. economy* has recently deteriorated again. The necessity for households to save more, losses in asset prices and ongoing difficulties in the U.S. real estate market are proving to be a sustained burden on private consumption. The savings ratio has risen from around 2% in 2007 to currently just under 6%, and is likely to remain at that level across the whole forecasting horizon. Yet another exacerbating factor is the tight situation on the job market. The unemployment rate will reach just under 10% in 2010, a level last recorded at the beginning of the 1980s. Moreover, the now more than 1½ years of persistently high unemployment rates, the above-average proportion of long-term unemployed and the reduced mobility of labor as a consequence of lower real estate prices are all giving rise to vocal fears about a long-term increase in structural unemployment. It was against this background that the U.S. administration adopted a new fiscal stimulus package in the second half of 2010, while the Federal Reserve System (Fed) decided to prolong its purchases of securities (to pursue what is known as "quantitative easing two"). Despite these economic policy stimuli, the annual growth rate in the U.S. economy is likely in the foreseeable future to remain below the long-term average and will probably amount to around 2½% in the period from 2010 to 2012.

In the course of the unprecedented upswing recorded over the past few years, the People's Republic of *China* has replaced not only Japan as the world's second largest economy, but also Germany as the largest exporting country. The dynamism of the Chinese economy was left virtually untouched by the financial crisis. After 9% in 2009, economic growth will again pick up to 10% in 2010. Rising real estate prices, high demand for credit and an investment-to-GDP ratio of almost 50% are indications of a bubble forming on the markets for real estate and capital goods. The government is endeavoring to counter a possible overheating of the economy. To this end, it put in place, inter alia, measures to curb credit growth and has allowed the renminbi yuan to appreciate vis-à-vis the U.S. dollar, but the dampening effect of these measures on growth in China will only be limited. Real GDP will increase by 9% per annum in 2011 and 2012, and the growth expected for India, the second large emerging economy in Asia, is expected to be only moderately less dynamic. The Indian economy is oriented to the domestic market far more strongly than China, so that net exports do not contribute sizeably to growth. With growth rates of 8%, India will continue to be a promising, rapidly expanding market in the period under review.

At the beginning of the year, *Japan* was able to benefit particularly markedly from dynamic demand in neighboring Asian countries. In view of the declining momentum of global trade and the expiry of economic stimulus packages, the growth of the Japanese economy will slow down perceptibly towards the end of 2010. Moreover, the fact that the external value of the yen, which has continued to rise despite the foreign exchange interventions undertaken by the Japanese central bank, will be a burden for the export industry in forthcoming quarters. Public sector debt has increased further as a result of the financial crisis and now already amounts to around 200% of GDP. However, households' high propensity to save has thus far prevented this from having any impact on credit assessments by financial markets. Economic growth will amount to 3½% in 2010 and subsequently decline to 1½% in both 2011 and 2012.

Table 2

Underlying Global Economic Conditions

	2009	2010	2011	2012
	Annual change in % (real)			
Gross domestic product				
World GDP growth outside the euro area	–0.2	+5.3	+4.3	+4.7
U.S.A.	–2.6	+2.7	+2.4	+2.7
Japan	–5.3	+3.6	+1.3	+1.7
Asia excluding Japan	+5.6	+9.1	+7.2	+7.7
Latin America	–1.7	+5.9	+3.7	+3.9
United Kingdom	–5.0	+1.7	+1.8	+1.9
New EU Member States[1]	–2.9	+1.7	+2.9	+3.9
Switzerland	–1.9	+2.6	+1.9	+2.3
Euro area[2]	–4.1	+1.6 to +1.8	+0.7 to +2.1	+0.6 to +2.8
World trade (imports of goods and services)				
World economy	–11.2	+11.7	+7.2	+7.5
Non-euro area countries	–11.1	+13.6	+8.2	+8.3
Real growth of euro area export markets	–11.6	+11.3	+7.2	+7.2
Real growth of Austrian export markets	–11.9	+10.9	+6.7	+6.4
Prices				
Oil price in USD/barrel (Brent)	61.9	79.5	88.6	90.7
Three-month interest rate in %	1.2	0.8	1.4	1.7
Long-term interest rate in %	3.9	3.2	3.4	3.7
USD/EUR exchange rate	1.39	1.33	1.39	1.39
Nominal effective exchange rate (euro area index)	111.70	105.02	105.88	105.88

Source: Eurosystem.

[1] *Member States that joined the EU in 2004 and 2007 and have not yet introduced the euro: Czech Republic, Hungary, Poland, Romania, Bulgaria, Estonia, Latvia, Lithuania.*

[2] *2010 to 2012: Results of the Eurosystem's December 2010 projections. The ECB presents the result in ranges based upon average differences between actual outcomes and previous projections.*

As holds true for the global economy, the picture presented by economic developments in *Europe* is likewise highly disparate. In northern countries with a strong orientation towards exports, such as Finland, Sweden, the Netherlands and Germany, economic recovery is making rapid progress. Growth in the United Kingdom and France, by contrast, will be only modest on account of both the fiscal consolidation efforts and subdued domestic demand. The economic upswing expected for Italy will be even weaker, given the country's persistent lack of competitiveness. In addition, not only a number of countries in the southern periphery, such as Greece, Portugal and Spain, but also Ireland are deeply embroiled in the debt crisis and suffer under the consequences of the bursting of real estate bubbles.

The positive development in Europe that is most significant has indisputably taken place in *Germany*. Although the above-average weight of the intermediate and capital goods sectors there caused Austria's most important trading partner to be hit hard by the crisis in global trade, that weight also worked to Germany's benefit during the recovery. In the second quarter of 2010, for instance, the growth rate in Germany reached a historic (quarter-on-quarter) high of 2.3%. In line with the declining momentum of global trade, the third quarter of 2010 saw economic growth slow down (to 0.7%) as expected, but the German economy will continue to expand at above-average rates in both 2011 and 2012, namely by around 2% per annum. The output gap will have been closed by the turn of the year 2011/12 – far faster than had still been expected in the preceding forecast – with Germany profiting from the unexpectedly robust development of its labor market. The labor market reforms of past years, the possibilities offered by short-time working arrangements and the impact of the lack of skilled labor during the last boom period all contributed to firms laying off fewer staff than would have been expected in a slump as deep as the current one. The hoarding of labor played a major role in the upkeep of production capacities and enabled German companies to respond rapidly and in a timely manner to the rebound in world trade. Germany had moreover generated a current account surplus in the last few years and, even in the crisis, its public sector debt rose only moderately. There was no bubble in the real estate sector. Nor is it likely over the medium term that Germany will have lower growth rates as a consequence of the crisis because there is no need for any sectoral reallocations that have in the past often had longer-lasting dampening effects on growth in the wake of real estate and financial crises.

In contrast to the situation not only in Germany, but also in Sweden, Finland, the Netherlands and Austria, the consequences of the financial crisis will continue to be felt for a longer period in the countries in the *southern periphery,* as well as in Ireland. The painful process of dismantling macroeconomic imbalances, the restoration of price competitiveness and sectoral reallocation will dampen growth prospects throughout the period under review. The magnitude of the sectoral reallocations necessary can be seen from current developments in *Ireland.* Many years of boom activity in the real estate market had pushed the share of real estate investment in real GDP up to 14% in 2006. After the real estate bubble had burst, that share dropped to 4½% at the end of 2009 and will decline further to around 2% by 2012. Last but not least, real estate loan defaults were such a severe drain on the financial sector that it took government support measures and international assistance to prevent a financial meltdown. The government debt-to-GDP ratio rose from 25% in 2007 to just under 100% in 2010. Similar developments were observed in Greece and Portugal – although they differed in magnitude – as well as, to a lesser degree, in Spain. All in all, the euro area as whole will start out on a path of moderate growth in the period under review.

This characteristically heterogeneous pattern is also to be found in *Central, Eastern and Southeastern Europe* (CESEE), countries that are of major importance to Austria. These countries were affected by the crisis to differing degrees, depending on the importance of the export industry, the proportion of foreign currency loans, the size of the current account deficit and the level of government debt. While some countries, such as Hungary, Ukraine and Romania, were dependent on international rescue programs of the IMF and the EU, Poland was the only country in the EU to record positive growth rates in 2009. All in all, the in some cases high macroeconomic imbalances in this region have led to significantly sharper economic downturns than in the emerging countries of Asia and Latin America. On average, the recovery expected for the Member States that joined the EU in 2004 and 2007 will only be modest. Growth there will gradually pick up from 2% to 4% in the period from 2010 to 2012. While Poland will enjoy persistently strong economic growth across the whole forecasting horizon and the Czech Republic will be able to recover from the economic crisis relatively quickly, growth in both Hungary and Romania will remain clearly below average in 2010 and will accelerate more noticeably only towards the end of the period under review.

4 Austria: Exports Return to Pre-Crisis Levels in the End of 2011

The global economic and financial crisis affected Austrian industry, above all, through a marked slump in exports that began in the second half of 2008. In 2009 alone, goods exports decreased by 20% in nominal terms, with a particularly sharp drop of just under 25% being recorded in exports of machinery and transport equipment. The recovery in global trade that commenced in the second half of 2009 triggered a revitalization of Austrian export activity. The steep downturn in the first two quarters caused real exports of goods and services to decline by 11.9% in 2009 as a whole. The recovery of exports accelerated in the course of 2010, with a real quarter-on-quarter increase of 5.2% being recorded in the second quarter of the year. Although exports expanded somewhat less strongly in the third quarter of 2010, the growth rates remain above average. For the fourth quarter of 2010, the results of the OeNB's export indicator point towards a fluctuation around the levels of average growth. In 2010 as a whole, exports are expected to increase by 10.4% in real terms.

Austria's export industry has thus recovered from the direct effects of the crisis, but growth rates as high as those currently recorded in Germany cannot be expected in Austrian foreign trade. This is due to differences in both the regional and the sectoral structure of the two countries' exports. German companies play a dominant role on global markets in the mechanical engineering sector, which is highly sensitive to cyclical fluctuations, and in the field of road vehicles. Moreover, the dynamically growing markets in Asia are of greater significance for German exporters than for their Austrian competitors. German exporters are thus less dependent than their Austrian counter-

Table 3

Growth and Price Developments in Austria's Foreign Trade

	2009	2010	2011	2012
	Annual change in %			
Exports				
Competitor prices in Austria's export markets	–3.6	+4.8	+1.9	+1.7
Export deflator	–1.5	+1.4	+2.7	+1.8
Changes in price competitiveness	–2.1	+3.4	–0.8	–0.1
Import demand in Austria's export markets (real)	–11.9	+10.9	+6.7	+6.4
Austrian exports of goods and services (real)	–13.6	+10.4	+7.3	+6.9
Market share	–1.8	–0.5	+0.6	+0.6
Imports				
International competitor prices in the Austrian market	–3.3	+3.7	+2.1	+1.7
Import deflator	–1.3	+3.2	+2.4	+1.6
Austrian imports of goods and services (real)	–12.5	+6.8	+6.0	+6.2
Terms of trade	–0.2	–1.8	+0.3	+0.1
	Percentage points of real GDP			
Contribution of net exports to GDP growth	–1.5	+2.2	+1.2	+1.0

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook, Eurosystem.

Table 4

Austria's Current Account

	2009	2010	2011	2012
	% of nominal GDP			
Balance of trade	3.9	3.9	4.4	5.4
Balance on goods	–0.9	–1.1	–0.7	–0.2
Balance on services	4.7	4.9	5.2	5.6
Balance on income	–0.3	–0.5	–0.4	–0.3
Balance on current transfers	–0.6	–0.8	–0.6	–0.6
Current account	2.9	2.5	3.4	4.5

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook.

parts on the only sluggish process of recovery in both industrialized economies and the CESEE countries.

A slightly less dynamic development of exports must be expected for 2011 and 2012. The already visible slowdown in the recovery of global business activity will have an impact on external trade; Austrian exports will rise by some 7% in both of the forthcoming years.

Austria's current account has improved steadily since the mid-1990s. 2008 saw a record surplus of 4.9% of GDP. Although plunging demand for exports during the crisis led to a deterioration of the balance on current account, it remained in positive territory and will again more or less reach its pre-crisis level by 2012.

5 Sluggish Domestic Demand

5.1 Divergent Developments in Investment Activity

The (export-oriented) manufacturing industry was hit particularly hard by the crisis. Output in this sector (NACE C) declined by 12.6% in 2009. The

Table 5

Investment Activity in Austria

	2009	2010	2011	2012
	Annual change in %			
Total gross fixed capital formation (real)	–9.1	–3.3	+2.1	+3.0
of which: Investment in plant and equipment (real)	*–10.8*	*–3.5*	*+3.4*	*+4.6*
Residential construction investment (real)	*–4.1*	*–2.8*	*+0.5*	*+1.6*
Nonresidential construction investment and other investment	*–5.0*	*–3.0*	*+1.4*	*+2.0*
Government investment (real)	*–0.1*	*–1.0*	*–1.5*	*–1.5*
Private investment (real)	*–9.6*	*–3.5*	*+2.3*	*+3.3*
	Contribution to total gross fixed capital formation growth in percentage points			
Investment in plant and equipment (real)	–4.4	–1.4	+1.4	+1.9
Residential construction investment (real)	–0.8	–0.6	+0.1	+0.3
Nonresidential construction investment and other investment	–1.9	–1.2	+0.6	+0.8
Government investment (real)	+0.0	–0.1	–0.1	–0.1
Private investment (real)	–9.1	–3.3	+2.2	+3.1
	Contribution to real GDP growth in percentage points			
Inventory changes (real)	–0.8	+0.6	+0.1	+0.0

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook.

resulting excess capacity, together with uncertain prospects and tighter financing conditions, caused companies to cut back their investment activity considerably. As from mid-2008, *investment in plant and equipment* declined for seven successive quarters, by 15% in all. On account of booming exports, the second quarter of 2010 again saw a first, albeit weak, increase in such investment. In view of stabilizing sales expectations, companies are likely to increase their capacity-enhancing investment in the next few quarters.

The prospects for construction investment, by contrast, are less favorable. Data on the building permits issued allows a stabilization of *residential construction* at a low level to be expected for 2011, but clear signs of a recovery in this sector are still missing. The *civil engineering* sector is profiting from ongoing public sector infrastructure investment, but the relatively stable volume thereof does not give rise to any additional growth stimuli. This is exacerbated by the fact that the financial crisis has left local authorities in a highly precarious financial situation, so that they are reducing their investment activity.

Total *gross fixed capital formation* again rose on a quarterly basis in the third quarter, for the first time since 2009. Viewed over the entire year, however, capital expenditure will continue to decline. A return to positive annual growth rates can only be expected for 2011.

5.2 Consolidation Package Curbs Consumption

As a consequence of high wage settlements, the income tax reform, very low inflation and, last but not least, the car-scrapping premium, consumer spending remained relatively stable despite falling employment levels and rose by 1.1% in real terms in the crisis year of 2009. The sustained growth of consumption was also facilitated by a decline in the savings ratio, which fell from 11.7% in 2008 to 11.0% in 2009. These supporting factors disappeared in the course of 2010, so that (at +1.0%) the increase in consumer spending remained modest despite the recovery in business activity.

Table 6

Determinants of Nominal Household Income in Austria

	2009	2010	2011	2012
	Annual change in %			
Employees	–1.0	+0.8	+1.1	+0.9
Wages per employee	+1.9	+1.1	+2.3	+2.2
Compensation of employees	+1.0	+1.9	+3.4	+3.1
Property income	–29.0	–4.2	+5.2	+6.6
Mixed income and operating surplus, net	–2.3	+1.5	+3.3	+4.1
	Contribution to disposable household income growth in percentage points			
Compensation of employees	+0.8	+1.6	+2.8	+2.6
Property income	–3.9	–0.4	+0.5	+0.6
Mixed income and operating surplus, net	–0.5	+0.3	+0.6	+0.8
Net transfers minus direct taxes[1]	+2.9	+0.8	–1.1	–0.7
Disposable household income (nominal)	–0.8	+2.3	+2.8	+3.3

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook.

[1] Negative values indicate an increase in (negative) net transfers minus direct taxes, positive values indicate a decrease.

Table 7

Private Consumption in Austria

	2009	2010	2011	2012
	Annual change in %			
Disposable household income (nominal)	–0.8	+2.3	+2.8	+3.3
Private consumption expenditure (PCE) deflator	–0.7	+1.7	+2.1	+1.9
Disposable household income (real)	–0.1	+0.7	+0.7	+1.4
Private consumption (real)	+1.1	+1.0	+1.0	+1.3
	% of nominal disposable household income			
Saving ratio	11.0	10.9	10.5	10.5

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook.

Households' various kinds of income (compensation of employees, investment income, income from self-employment and operating surpluses) will again rise more markedly as from 2011, but the fiscal consolidation measures that will take effect in that year (increases in petroleum and tobacco tax, a new tax on airline tickets and cuts in social transfers) will impose a burden on their real disposable income and, later, also on consumer spending. All in all, these measures will reduce consumption growth in both 2011 and 2012 by ¼ to ½ of a percentage point. It is assumed that households will compensate for part of the increased burden by cutting back their savings ratios. The increase in consumer spending in 2011 will be identical to that in 2010, namely 1%, with a slight improvement to 1.3% being expected for 2012.

Box 1

Impact of Fiscal Consolidation

Austria's fiscal position has deteriorated since 2008 as a result of both the effects of automatic stabilizers and the economic stimulus packages. Safeguarding the sustainability of public finances now necessitates extensive consolidation measures.

In spring 2010, the Austrian government decided to lower the spending caps in the federal budget in the period from 2011 to 2014 and confirmed previously announced plans for a slight reduction of public sector jobs. This was already taken into account in the OeNB's forecast of June 2010, in which a very low growth of discretionary expenditure and staffing costs had been taken as given.

In October 2010, the federal government announced a tax reform package that included the following measures: increases in various excise duties (petroleum tax, tobacco tax, etc.), the introduction of a bank tax (together with the elimination of taxes on bank loan contracts), higher pension insurance contributions for farmers and self-employed, and the elimination of income tax exemptions and loopholes (taxation of private foundations, realized gains arising from sales of securities, etc.). At the same time, the government also decided to cut various social transfers.[1]

[1] Other spending cuts are also included in the OeNB's forecast, but they are not considered to be fiscal adjustment measures per se, as they are primarily the result of more favorable macroeconomic conditions. This holds true for, in particular, lower interest payments.

The table below shows the volume of the individual measures and their expected impact on GDP growth, the HICP and the general government budget balance.[2] In the OeNB's view, the fiscal consolidation package will reduce economic growth by 0.3 percentage points in 2011, and by 0.2 percentage points in 2012; at the same time, the increase in excise duties will raise the inflation rate expected for 2011 and 2012 by 0.4 and 0.1 percentage points, respectively. The measures will improve the general government budget balance by 0.6 percentage points in 2011 and by 0.9 percentage points in 2012.[3]

Impact of the Consolidation Package

	Volume		GDP		HICP		Budget balance	
	2011	2012	2011	2012	2011	2012	2011	2012
	% of GDP		*Annual change in %*				*% of GDP*	
Scenario without any consolidation			**+2.4**	**+2.5**	**+1.8**	**+1.7**	**–3.6**	**–3.5**
Consolidation	**0.9**	**1.3**	**–0.3**	**–0.2**	**+0.4**	**+0.1**	**0.6**	**0.9**
Changes in taxation	0.4	0.6	–0.1	–0.1	+0.4	+0.1	0.3	0.4
Petroleum tax[1]	0.2	0.2						
Other excise duties[1]	0.1	0.2						
Bank tax, tax on loan contracts	0.1	0.1						
Cuts in social transfers	0.2	0.2	–0.1	+0.0	+0.0	+0.0	0.1	0.1
Transfers for families	0.1	0.1						
Discretionary spending and staffing costs	0.3	0.6	–0.1	–0.1	+0.0	+0.0	0.2	0.3
OeNB forecast (including consolidation)			**+2.1**	**+2.3**	**+2.2**	**+1.8**	**–3.0**	**–2.6**

Source: OeNB, Ministry of Finance.

[1] Including indirect effects on revenue from value added tax.

[2] The column Volume indicates the revenue increase and/or spending cut that would result if companies and households do not change their behavior. The column Budget balance, by contrast, gives the ex post effect of the respective measure on the general government budget balance. Through the operation of the automatic stabilizers, the negative growth effects of fiscal consolidation measures reduce the tax revenue, and thus also the impact on the fiscal balance. In the case of cuts to the public sector wage bill and/or pension payments, account needs to be taken of the fact that both items entail payments of social security contributions and wage tax. The improvement in the budget balance is thus smaller than the spending cut even if possible effects on the real economy are left unconsidered.

[3] These estimates take account of only short-term demand effects, without any consideration of potential positive medium to long-term effects on confidence, which may – acting through lower interest payments or better expectations – have a favorable impact on growth over the medium to long term.

5.3 Crisis Has No Lasting Impact on Labor Market

Given the scale of the slump in business activity, the impact of the economic and financial crisis on the Austrian labor market has been relatively limited. The number of unemployed rose by just under 50,000 in 2009, pushing the *unemployment rate* (Eurostat definition) up from 3.8% in the preceding year to 4.8%. The effects of the crisis were mitigated in part by a decline in the number of hours worked per employee. In this respect, exceptional provisions, such as short-time work, played an important role in limiting the increase in unemployment. Moreover, the number of individuals undergoing training – persons not deemed to be unemployed – rose by 27,000 in 2009.

The recovery in business activity in the course of 2010 has led to a significant expansion of employment. Most of the growth in employment was accounted for by leased workers (the year-on-year increase in the field of administrative and support services – NACE N – amounted to 26,000 in September 2010) and by the health and social services sectors (NACE Q, where

Table 8

Labor Market Developments in Austria

	2009	2010	2011	2012
	Annual change in %			
Total employment	–0.9	+0.9	+0.9	+0.8
of which: Payroll employment	*–1.0*	*+0.8*	*+1.1*	*+0.9*
Self-employment	*–0.5*	*+1.4*	*+0.1*	*+0.6*
Public sector employment	*+0.2*	*+0.6*	*–0.1*	*–0.1*
Registered unemployment	+16.4	–3.1	–2.1	–0.5
Labor supply	+0.1	+0.6	+0.7	+0.7
	% of labor supply			
Unemployment rate (Eurostat definition)	4.8	4.5	4.4	4.3

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook.

the increase in the number of employed was 22,000). Despite a considerable increase in output (+12.3%, year on year, in August 2010), the manufacturing industry is recruiting hardly any new employees; increased demand for labor there is covered primarily through leased workers. In 2010 as a whole, the number of employed is likely to rise by 35,000 (or 0.9%, year on year), with similar growth rates also being expected for the two subsequent years (0.9% in 2011 and 0.8% in 2012).

Traditionally, there is a highly cyclical pattern to the expansion of the supply of labor. In 2009, for instance, it rose by only 4,000 persons, after having increased by, on average, 35,000 persons per annum between the years 2000 and 2008. The improved labor market prospects will induce some 30,000 persons to enter the Austrian labor market each year from 2010 to 2012. The influx of additional workers from abroad once residents of countries that joined the EU in 2004 gain full access to the labor market in May 2011 is likely to remain small, since free movement is currently already largely given for a number of professions. Demographic developments will have a marginally positive impact on the supply of labor in 2010 and 2011. The effects of the 2003 pension reform have been tempered significantly by what is known as the "heavy-labor pension rule," an exemption that grants workers with above-average years of contributory service early retirement.

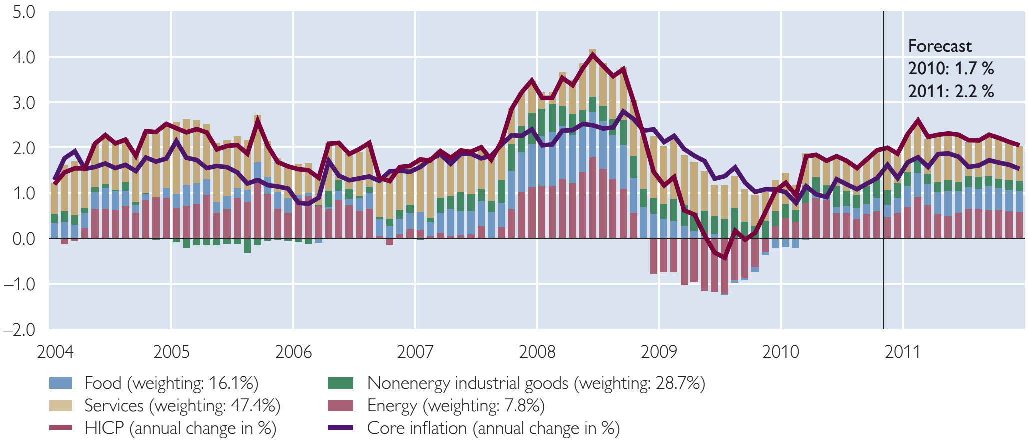
6 Fiscal Consolidation Package and Food Prices Drive Inflation

The crisis year 2009 saw inflation slow down significantly, with the HICP rising by only 0.4%. In the course of the current year to date, the rate of inflation has risen steadily to stand at 1.9% in October. That increase was due, above all, to rising energy and food prices. The upward movement of food prices will continue to pick up over the forecasting horizon. This trend will be fueled by, in particular, processed food prices, which are based on those prevailing on global markets for agricultural commodities. Market expectations indicate that international market prices of agricultural raw materials will rise further in the period from September 2010 to the beginning of 2011, before leveling off by the end of the latter year. In the next few months, the base effect emanating from the earlier sharp decline in food price inflation will moreover also contribute to upward movement of prices in the related sector.

Chart 2

HICP Inflation and Contributions from Subcomponents

Contributions to growth in percentage points *Latest observation: October 2010*



Source: OeNB, Statistics Austria.

The measures announced within the scope of the fiscal consolidation package will raise HICP inflation by 0.4 percentage points in 2011, with the increases in petroleum and tobacco tax accounting for 0.26 and 0.13 percentage points, respectively, and the tax on airline tickets for 0.01 percentage points.

Annual HICP inflation in 2010 as a whole will amount to 1.7%, while the corresponding rate for 2011 will be in the order of 2.2%. Core inflation (HICP inflation excluding energy and unprocessed food) will rise as well (from 1.1% in 2010 to 1.6% in 2011), but it will remain clearly below HICP inflation. The increase in core inflation

Table 9

Selected Price and Cost Indicators for Austria

	2009	2010	2011	2012
	Annual change in %			
Harmonised Index of Consumer Prices (HICP)	+0.4	+1.7	+2.2	+1.8
HICP energy	–10.4	+7.4	+8.1	+3.0
HICP excluding energy	+1.5	+1.2	+1.7	+1.6
Private consumption expenditure (PCE) deflator	–0.7	+1.7	+2.1	+1.9
Investment deflator	+2.2	+3.0	+1.5	+1.8
Import deflator	–1.3	+3.2	+2.4	+1.6
Export deflator	–1.5	+1.4	+2.7	+1.8
Terms of trade	–0.2	–1.8	+0.3	+0.1
GDP at factor cost deflator	+1.3	+1.5	+1.7	+1.8
Unit labor costs	+4.9	+0.1	+1.1	+0.7
Compensation per employee	+1.9	+1.1	+2.3	+2.2
Labor productivity	–2.8	+1.0	+1.2	+1.5
Collectively agreed wage settlements	+3.4	+1.6	+2.1	+2.2
Profit margins[1]	–3.6	+1.5	+0.6	+1.1

Source: 2009: Eurostat, Statistics Austria; 2010 to 2012: OeNB December 2010 outlook.

[1] *GDP deflator divided by unit labor costs.*

is due to the development of prices in the categories of processed food and services.

Wage developments are not expected to give rise to any noticeable price pressures over the forecasting horizon. The currently available results of the autumn round of wage negotiations indicate that negotiated wages, viewed in terms of the overall economy, are likely to rise by 2.1%. Reductions of overtime, the elimination of flexible wage components and inter-industry shifts caused compensation of employees to increase perceptibly less than the collectively agreed wages in 2009 and 2010, leading to a negative wage drift of 1.5% and 0.5%, respectively. For 2011, the improvement in business activity allows a modest positive wage drift to be expected. In the period under review, companies will be better able again to push through higher prices; together with a favorable development of labor productivity, this will lead to rising profit margins.

7 Downside Risks to Growth Outlook Emanate from Abroad

On the *domestic* side, the risks with respect to *economic growth* are slightly on the upside. In line with Eurosystem rules, this projection is based on the assumption that there will not be any change in policy. This means that only such fiscal policy measures may be considered in the forecast that are already known in sufficient detail at the time it is compiled. In October 2010, the Austrian government announced a fiscal consolidation package (see box 1) that has not yet run through the required process of legislation. Should the announced fiscal consolidation measures be watered down, their inherent effect of curbing growth over the short term would be reduced as well. With respect to domestic demand, a more rapid recovery of, in particular, construction activity cannot be ruled out against the background of rising real estate prices.

The *external* risks surrounding the outlook for economic growth are significantly higher and tilted mainly towards the downside. While it is by no means impossible that the recovery in worldwide economic activity will be stronger than expected in the short term, downside risks predominate over the medium term. The consequences of the debt crisis and the great need across the globe to consolidate public finances could limit economic growth more than expected. Although global imbalances have declined slightly during the crisis, they have not as yet disappeared. In this respect, a risk often discussed is that of economic conflicts emerging that could trigger currency crises and lead to the erection of barriers to international trade. In addition, there are fears of an overheating of the economy in dynamically growing countries like China. Last but not least, further increases in commodity prices constitute a risk for cyclical developments. A renewed surge in commodity prices, in particular in the food sector, is the main upside risk for *inflation*.

8 Revisions to Forecast Driven by Better External Environment and Fiscal Consolidation

The underlying assumptions on the growth of global trade have been revised upward since the OeNB's June 2010 economic outlook. Growth expectations with respect to Austria's export markets for 2011 have been revised upwards by 2 percentage points. Crude oil futures prices have risen by just under USD 5, while the exchange rate of the euro is expected to appreciate both against the U.S. dollar and in nominal effective terms. Long-term

Table 10

Change in the External Economic Conditions since the OeNB June 2010 Outlook

	December 2010			June 2010			Difference		
	2010	2011	2012	2010	2011	2012	2010	2011	2012
	Annual change in %								
Growth of Austria's export markets	+10.9	+6.7	+6.4	+7.4	+4.7	+6.0	+3.5	+2.0	+0.4
Competitor prices in Austria's export markets	+4.8	+1.9	+1.7	+3.9	+2.0	+1.4	+0.9	–0.1	+0.3
Competitor prices in Austria's import markets	+3.7	+2.1	+1.7	+3.1	+1.8	+1.3	+0.6	+0.3	+0.4
	USD per barrel (Brent)								
Oil price	79.5	88.6	90.7	79.5	83.7	86.3	+0.0	+4.9	+4.4
	Annual change in %								
Nominal effective exchange rate (exports)	+2.2	–0.1	+0.0	+2.3	+0.5	+0.0	–0.1	–0.6	+0.0
Nominal effective exchange rate (imports)	+1.5	+0.1	+0.0	+1.4	+0.2	+0.0	+0.1	–0.1	+0.0
	%								
Three-month interest rate	0.8	1.4	1.7	0.8	1.1	1.7	+0.0	+0.3	+0.0
Long-term interest rate	3.2	3.4	3.7	3.4	3.8	4.2	–0.2	–0.4	–0.5
	Annual change in %								
U.S. GDP (real)	+2.7	+2.4	+2.7	+3.1	+2.2	+2.8	–0.4	+0.2	–0.1
	USD/EUR								
USD/EUR exchange rate	1.33	1.39	1.39	1.29	1.26	1.26	+0.04	+0.13	+0.13

Source: Eurosystem.

interest rates are expected to be lower in the years ahead, while short-term rates are expected to be higher. The yield curve is thus likely to become flatter than anticipated as recently as in June 2010.

The effects of the new external assumptions were simulated using the OeNB's macroeconomic model. Table 11 provides detailed reasons for revising the outlook. Apart from the impact of changed external assumptions, they are attributable to the impact of new data and a residual. The influence of new data includes the effects of the revisions of both the historical data already available at the time of the previous economic outlook (i.e. data up to the first quarter of 2010) and the forecasting errors of the previous outlook for the periods now published for the first time (i.e. data for the second and third quarters of 2010). The item Other includes new expert assessments regarding the development of domestic variables, such as government consumption or wage settlements, as well as any changes to the model.

The reason why the economic growth forecast for 2010 is higher than that given in the June 2010 outlook is to be found, first and foremost, in the fact that growth in the second and third quarters of 2010 was stronger than expected, although only slightly so in the second quarter. That higher quarterly growth increases the carry-over effect, and thus also the figure forecast for 2011 by 0.3 percentage points. The more favorable external assumptions raise projected GDP growth by an additional 0.3 percentage points in 2011 and by a further 0.4 percentage points in 2012. The fiscal consolidation mea-

Table 11

Breakdown of Forecast Revisions

	GDP 2010	GDP 2011	GDP 2012	HICP 2010	HICP 2011	HICP 2012
	Annual change in %					
December 2010 outlook	+1.9	+2.1	+2.3	+1.7	+2.2	+1.8
June 2010 outlook	+1.6	+1.8	+2.1	+1.7	+1.7	+1.8
Difference	+0.3	+0.3	+0.2	+0.0	+0.5	+0.0
Due to:	*Percentage points*					
External assumptions	+0.0	+0.3	+0.4	+0.0	+0.0	+0.0
New data	+0.2	+0.3	+0.0	+0.0	+0.1	+0.0
of which: revision of historical data until Q1 10	+0.0	+0.0	x	+0.0	x	x
projection errors for Q2 10 and Q3 10	+0.2	+0.3	x	+0.0	x	x
Other[1]	+0.1	–0.3	–0.2	+0.0	+0.4	+0.0

Source: OeNB December 2010 and June 2010 outlooks.

[1] Different assumptions about trends in domestic variables such as wages, government consumption, effects of tax measures, other changes in assessment and model changes.

sures adopted by the Austrian federal government, by contrast, have the effect of curbing growth by 0.3 percentage points in 2011 and by 0.2 percentage points in 2012 (see figures given for Other in table 11). Upward revision of the inflation forecast for 2011 is due primarily to the effects of the fiscal consolidation package.

Box 2

OeNB-BOFIT Outlook for CESEE Countries: Growth Driven by Net Exports and Restocking, Domestic Demand to Remain Weak[1,2]

Our GDP growth forecast of 1.3% for the CESEE-7[3] region for 2010 remains unchanged compared to our March projections, taking into account major upward (Czech Republic and Hungary) and downward revisions (Bulgaria and Romania) at the country level. Robust growth in Poland and the Czech Republic contrasts with negative GDP growth in Bulgaria and Romania in 2010. Hungary will post modest but positive growth again. Net exports and substantial restocking remain the principal growth drivers. In 2011, investment growth and private consumption will strengthen in all countries, and GDP growth will pick up to 2.8%, implying a marginal downward revision of our March projection of 3.1%. The recovery will continue in 2012, accelerating slightly to 3.4%.

The gradual economic recovery in the Central and Eastern European EU Member States continued into the first half of 2010 with highly dissimilar developments in individual countries.

[1] Compiled by the Foreign Research Division, julia.woerz@oenb.at.

[2] The OeNB and the Bank of Finland Institute for Economies in Transition (BOFIT) compile semiannual forecasts of economic developments in selected CESEE countries (Bulgaria, the Czech Republic, Hungary, Poland, Romania, Russia and Croatia). The OeNB is in charge of the projections for the EU Member States as well as Croatia, BOFIT provides the forecast for Russia. The cutoff date for all projections was September 24, 2010 (Croatia: October 5, 2010). The forecasts are based on a broad range of information, including country-specific time series models for Bulgaria, the Czech Republic, Hungary, Poland and Croatia (for technical details, see Crespo Cuaresma, Feldkircher, Slačík and Wörz. 2009. Simple but Effective: The OeNB's Forecasting Model for Selected CESEE Countries. Focus on European Economic Integration Q4/09. 84–95). The forecast for Romania draws on information from various sources and expert judgment (given that the time series are as yet too short to conduct model calculations). The projections for Russia are based on a SVAR model.

[3] Bulgaria, the Czech Republic, Hungary, Latvia, Lithuania, Poland and Romania. Latvia and Lithuania are not covered by our own projections, but are included in the CESEE-7 aggregate based on the most recent IMF projections. As Estonia will become a euro area member at the beginning of 2011, it is no longer covered in the CESEE-7 aggregate.

Apart from Poland, still the region's growth engine, private consumption will remain subdued as a result of the still rather bleak labor market situation and very moderate or – in the public sector often – negative wage growth. Investments are hampered by low credit growth and low levels of capacity utilization. Thus, the replenishment of stocks remains the only positive growth component that adds substantially to the recovery in 2010. Restocking will continue in all countries over the entire projection period. Its substantial positive growth contribution in 2010 will be only temporary and will become negligible in 2011 and 2012.

Leading indicators point toward a continued recovery. Especially the industrial sector has benefited so far from strengthening external demand and restocking. Industrial production, new orders and sales have generally already surpassed their precrisis levels, and capacity utilization is rising steadily from historically low levels. On the other hand, weak private consumption implies a much more protracted recovery in retail trade and the construction sector compared with industry.

The housing boom in many CESEE-7 countries found an abrupt end in the crisis. Credit conditions will remain tight in the near future, and fiscal consolidation needs have already resulted in tax hikes and other restrictive budgetary measures in some countries. As a result, investment is expected to remain well below the longer-term precrisis average over the projection period, which is further reinforced by low capital utilization rates in many countries. EU-funded projects will represent an important component of investment activity, especially so in Hungary, Bulgaria and Poland.

Domestic demand will revive very hesitantly in 2011, again making a positive contribution to the still moderate growth rate of 2.8% in the region. With little room for maneuver, public consumption will remain weak. Investment growth will pick up somewhat as utilization rates increase, backed by large-scale projects cofinanced by the EU as well as by strengthening output growth in the export-oriented industrial sector. Thus, reviving external demand will support investment growth. Export and import growth are expected to be more dynamic, with net exports turning negative again in 2011 in all countries except for Hungary.

The picture will remain largely unchanged in 2012. Domestic demand and investments will gain momentum, but both will remain well below their long-term precrisis average. Import growth is expected to be buoyant. Net exports will again make a negative contribution despite significant export growth. Restocking will not accelerate further in 2012.

The CESEE-7 region will reach its precrisis output level by the end of 2011. However, it should be noted that Poland, the largest economy in the region, did not experience any output loss in 2009. The Czech Republic will recover its precrisis GDP level in 2011, Bulgaria only in 2012, and Hungary and Romania will need more time to recover to their precrisis output levels.

The risks attached to the external environment are rather balanced, given our already cautious assumptions on EU and euro area GDP and import growth. As in our last forecast, uncertainty continues to prevail with respect to changes in investor confidence (i.e. the development of global risk aversion, in particular vis-à-vis emerging economies). Fiscal consolidation poses a considerable downside risk to our forecast for all countries apart from Romania and the Czech Republic, where reforms have already been passed and are thus included in our forecasts. Serious consolidation efforts would further depress nascent domestic demand; in particular, private and public consumption will be directly affected.

CESEE-7: GDP Projections for 2010 to 2012 and Revisions to OeNB March Projections

	Eurostat	OeNB			Change from March	
	2009	2010	2011	2012	2010	2011
	Year-on-year growth in %				*Percentage points*	
CESEE-7	**–3.3**	**1.3**	**2.8**	**3.4**	**–0.0**	**–0.2**
Bulgaria	–5.0	–0.3	2.4	3.2	–0.6	–0.5
Czech Republic	–4.2	2.1	2.4	2.5	0.8	–0.2
Hungary	–6.3	0.8	2.2	3.0	1.0	–0.3
Poland	1.7	3.2	3.7	4.1	0.2	0.3
Romania	–7.1	–2.6	1.5	2.8	–3.4	–1.6

Source: OeNB September 2010 forecast, Eurostat.

BOFIT-OeNB Forecast for Russia: Consumption-Driven Growth to Continue

Russia will exhibit a brisk consumption-driven recovery. For the second half of 2010, growth is expected to be animated, although the exceptionally hot and dry summer will shave a bit off of production volumes. Especially in 2010, growth – materializing at slightly below 5% – is supported by the world market price of oil. Rather weak growth in the first half of 2010 will (as a low base) raise the annual figure for 2011 to over 5.5%, despite a slowdown in early 2011. GDP will reach its pre-recession level of 2008 in mid-2011.

Growth will be driven mainly by private consumption. Real wages are anticipated to grow briskly, and the public sector is assumed to stick to its plan to keep the pension and wage ratio virtually constant. Household propensity to save is not expected to rise from its current level, to which it had already risen during the crisis. Unemployment prospects are relatively uncertain, as employment decreased only by a few percentage points in the recession, thus dampening productivity strongly.

Investments are forecast to revive with a lag, partly because companies have more idle production capacity than before the crisis. In the first half of 2010, investment growth was zero. It is expected to revive in the second half of the year, but tangible investment growth will take off only in 2011. Deleveraging and the adjustment of banks' balance sheets may have run their course, and banks look poised to expand credit prudently soon.

Public consumption is expected to still increase slightly this year due to the remaining anti-crisis measures but to remain unchanged in the period from 2011 to 2012. The public sector is practically free of debt (net), and there is no immediate need to balance public sector finances, although the government and particularly regions and municipalities have scaled down their total real expenditures this year. Significant expenditure cuts are hardly likely, as elections are approaching (Duma elections in December 2011, presidential elections in March 2012).

Despite the rapid growth of world trade, Russia's export volume is expected to grow relatively slowly, as export volumes of crude oil, oil products and gas – accounting for 55% to 58% of Russian exports of goods and services in 2009 and in the first half of 2010 – are forecast to increase very modestly because of slow production growth.

Seasonally adjusted imports in the first quarter of 2010 fell from the preceding quarter, but rose fast in the second quarter. Import growth is expected to decelerate slightly in the third quarter and to fall further from 2011 to 2012, but is still anticipated to come to over 10%. Imports will be driven by consumption growth, and from 2011, by a pickup of investments.

The forecast is based on the view of brisk but somewhat decelerating growth of the world economy and world trade, and a gradually rising world market oil price. The uncertainties surrounding the forecast are exceptionally large. A drop in the oil price could hit the Russian economy strongly, especially now, as the chances for fiscal stimulus are becoming smaller than in 2008, after which the government had spent half of its reserve funds. In the midst of uncertainty, the direction of capital flows may change easily and strongly, backed by large amounts of liquidity both globally and in the Russian banking sector. Still, positive surprises for Russia are also possible in terms of higher energy prices, foreign finance and bank lending growth. The revival of investment in Russia is subject to considerable uncertainty, which from the perspective of private investors is represented by interference by the state, i.e. politicians and officials, in corporate activities, as well as by short-term reactions to problems arising from the recession. Russian companies' inventory building is fraught with abnormal uncertainty; even in less turbulent times, changes in inventories (mostly growth) have had a considerable impact on Russia's GDP growth.

Russia: GDP Projections for 2010 to 2012 and Revisions to BOFIT March Projections

	Rosstat	BOFIT-OeNB			Change from March	
	2009	2010	2011	2012	2010	2011
	Year-on-year growth in %				*Percentage points*	
Russia	–7.9	4.9	5.6	4.7	–0.6	0.6

Source: BOFIT September 2010 forecast, Rosstat.

OeNB Projections for Croatia: Weak Domestic Demand Slows Economic Recovery

Given weak domestic demand, the Croatian economy will continue to contract in 2010. Although the fragile recovery continued in early 2010, the economy still contracted by 2.5% year on year in the first half of 2010 on the back of still depressed domestic demand. The downward trend of the Croatian economy is set to moderate further in the second half of the year, implying a drop of approximately 1.6% in real output for 2010 as a whole and, like in Romania and Bulgaria, a rather sluggish economic recovery.

In particular, private consumption is expected to gain some momentum in the latter half of 2010 following the abolition of the crisis tax in two steps (July and November) and the reduction of the level and number of personal income tax rates as of July 2010. However, the full impact of these measures will materialize only in 2011. Similarly, gross fixed capital formation is seen to have bottomed out in the first half of 2010. The main impetus for recovery in investment activity should come from the private sector following the introduction of the government's three-pillar credit/financing scheme in early 2010, which is aimed at stimulating bank lending to the economy. However, like public consumption, public investment is expected to remain listless in light of increasing fiscal constraints. Against the background of firming export growth and a relatively good tourism season (arrivals were up by 12% year on year in July 2010, while nights spent increased by 5%) as well as the ongoing downward adjustment of imports, net exports are forecast to contribute positively to growth also in the second half of 2010.

We expect the economy to grow by 1.5% in 2011 and to return to the growth pattern seen before the crisis, with a positive (negative) contribution of domestic demand (net exports). Investment activity is expected to pick up on the back of resuming lending activity and improving consumer and business sentiment. Private consumption should benefit from the tax *relief measures mentioned above and possibly also from incipient improvements in labor market conditions. At the same time, no major stimuli can be expected from public consumption as budget expenditures for 2011 and 2012 are frozen at the level of the revised 2010 budget. Given that general elections will be held in 2011, no substantial progress will be achieved with structural reforms, either. Provided the global environment is supportive, export growth is anticipated to accelerate further in 2011, but will be outpaced by import growth in light of strengthening domestic demand.*

The Croatian economy is forecast to expand by 2.8% in 2012, driven by a further strengthening of domestic demand. In particular, gross fixed capital formation is projected to accelerate on the back of increased FDI inflows ahead of the country's prospective EU entry. Croatia is expected to accede to the EU in 2013 provided membership negotiations are completed on schedule by mid-2011 and the subsequent ratification process in the EU Member States is concluded on time.

Croatia: GDP Projections for 2010 to 2012 and Revisions to OeNB March Projections

	Eurostat	OeNB			Change from March	
	2009	2010	2011	2012	2010	2011
	Year-on-year growth in %				*Percentage points*	
Croatia	–5.8	–1.6	1.5	2.8	–1.5	–0.3

Source: OeNB September 2010 forecast, Eurostat.

Annex: Detailed Result Tables

Table 12

Demand Components (Real Prices)

Chained volume data (reference year = 2000)

	2009	2010	2011	2012	2009	2010	2011	2012
	EUR million				*Annual change in %*			
Private consumption	139,531	140,901	142,362	144,207	+1.1	+1.0	+1.0	+1.3
Government consumption	49,348	49,501	49,645	49,802	+0.4	+0.3	+0.3	+0.3
Gross fixed capital formation	52,229	50,484	51,532	53,100	–9.1	–3.3	+2.1	+3.0
of which: Investment in plant and equipment	*21,020*	*20,276*	*20,973*	*21,947*	*–10.8*	*–3.5*	*+3.4*	*+4.6*
Residential construction investment	*10,435*	*10,139*	*10,191*	*10,355*	*–4.1*	*–2.8*	*+0.5*	*+1.6*
Investment in other construction	*21,336*	*20,695*	*20,994*	*21,424*	*–5.0*	*–3.0*	*+1.4*	*+2.0*
Changes in inventories (including statistical discrepancy)	1,491	891	696	744	×	×	×	×
Domestic demand	242,599	241,778	244,235	247,854	–2.4	–0.3	+1.0	+1.5
Exports of goods and services	132,130	145,871	156,451	167,319	–13.6	+10.4	+7.3	+6.9
Imports of goods and services	118,225	126,245	133,805	142,105	–12.5	+6.8	+6.0	+6.2
Net exports	13,905	19,626	22,646	25,214	×	×	×	×
Gross domestic product	256,504	261,403	266,880	273,067	–3.7	+1.9	+2.1	+2.3

Source: 2009: Eurostat; 2010 to 2012: OeNB June 2010 outlook.

Table 13

Demand Components (Current Prices)

	2009	2010	2011	2012	2009	2010	2011	2012
	EUR million				*Annual change in %*			
Private consumption	148,974	152,936	157,783	162,810	+0.5	+2.7	+3.2	+3.2
Government consumption	54,209	55,402	56,610	57,863	+4.1	+2.2	+2.2	+2.2
Gross fixed capital formation	57,423	57,164	59,245	62,132	–7.1	–0.5	+3.6	+4.9
Changes in inventories (including statistical discrepancy)	1,335	2,622	2,008	1,469	×	×	×	×
Domestic demand	261,941	268,123	275,647	284,274	–1.4	+2.4	+2.8	+3.1
Exports of goods and services	139,904	156,630	172,423	187,664	–14.9	+12.0	+10.1	+8.8
Imports of goods and services	128,612	141,792	153,873	166,069	–13.7	+10.2	+8.5	+7.9
Net exports	11,293	14,837	18,550	21,595	×	×	×	×
Gross domestic product	273,234	282,960	294,197	305,869	–2.8	+3.6	+4.0	+4.0

Source: 2009: Eurostat; 2010 to 2012: OeNB June 2010 outlook.

Table 14

Deflators of Demand Components

	2009	2010	2011	2012	2009	2010	2011	2012
	2000 = 100				*Annual change in %*			
Private consumption	106.8	108.5	110.8	112.9	–0.7	+1.7	+2.1	+1.9
Government consumption	109.8	111.9	114.0	116.2	+3.7	+1.9	+1.9	+1.9
Gross fixed capital formation	110.0	113.2	115.0	117.0	+2.2	+3.0	+1.5	+1.8
Domestic demand (excluding changes in inventories)	108.1	110.2	112.4	114.4	+0.8	+2.0	+1.9	+1.9
Exports of goods and services	105.9	107.3	110.2	112.1	–1.5	+1.4	+2.7	+1.8
Imports of goods and services	108.8	112.3	115.0	116.9	–1.3	+3.2	+2.4	+1.6
Terms of trade	97.3	95.6	95.8	96.0	–0.2	–1.8	+0.3	+0.1
Gross domestic product	106.5	108.2	110.2	112.0	+1.0	+1.6	+1.8	+1.6

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook.

Table 15

Labor Market

	2009	2010	2011	2012	2009	2010	2011	2012
	Thousands				*Annual change in %*			
Total employment	4,079.5	4,114.4	4,149.4	4,183.3	–0.9	+0.9	+0.9	+0.8
of which: Private sector employment	*3,546.9*	*3,578.9*	*3,614.6*	*3,649.2*	*–1.1*	*+0.9*	*+1.0*	*+1.0*
Payroll employment (national accounts definition)	3,499.3	3,527.1	3,564.6	3,596.4	–1.0	+0.8	+1.1	+0.9
	% of labor supply							
Unemployment rate (Eurostat definition)	4.8	4.5	4.4	4.3	×	×	×	×
	EUR per real output unit x 100							
Unit labor costs (whole economy)[1]	63.5	63.6	64.2	64.7	+4.9	+0.1	+1.1	+0.7
	EUR thousand per employee							
Labor productivity (whole economy)[2]	62.9	63.5	64.3	65.3	–2.8	+1.0	+1.2	+1.5
	EUR thousand							
Real compensation per employee[3]	37.4	37.2	37.3	37.4	+2.6	–0.5	+0.2	+0.3
	At current prices in EUR thousand							
Gross compensation per employee	39.9	40.4	41.3	42.2	+1.9	+1.1	+2.3	+2.2
	At current prices in EUR million							
Total gross compensation of employees	139,757	142,444	147,284	151,850	+1.0	+1.9	+3.4	+3.1

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook.

[1] Gross wages divided by real GDP.
[2] Real GDP divided by total employment.
[3] Gross wages per employee divided by the private consumption expenditure (PCE) deflator.

Table 16

Current Account

	2009	2010	2011	2012	2009	2010	2011	2012
	EUR million				*% of nominal GDP*			
Balance of trade	10,521.0	10,979.8	12,981.9	16,494.3	3.9	3.9	4.4	5.4
Balance on goods	–2,328.0	–3,014.8	–2,185.6	–717.6	–0.9	–1.1	–0.7	–0.2
Balance on services	12,849.0	13,994.6	15,167.5	17,211.9	4.7	4.9	5.2	5.6
Balance on income	–823.0	–1,450.3	–1,288.5	–953.7	–0.3	–0.5	–0.4	–0.3
Balance on transfers	–1,722.0	–2,349.3	–1,641.1	–1,708.6	–0.6	–0.8	–0.6	–0.6
Current account	7,976.0	7,180.2	10,052.4	13,832.1	2.9	2.5	3.4	4.5

Source: 2009: Eurostat; 2010 to 2012: OeNB December 2010 outlook.

Table 17

Quarterly Outlook Results

	2010	2011	2012	2010				2011				2012			
				Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Prices, wages and costs	*Annual change in %*														
HICP	+1.7	+2.2	+1.8	+1.3	+1.8	+1.7	+1.9	+2.4	+2.3	+2.2	+2.1	+1.8	+1.8	+1.7	+1.7
HICP (excluding energy)	+1.2	+1.7	+1.6	+0.9	+1.1	+1.3	+1.5	+1.7	+1.9	+1.7	+1.6	+1.7	+1.7	+1.6	+1.6
Private consumption expenditure (PCE) deflator	+1.7	+2.1	+1.9	+1.3	+2.0	+1.7	+1.7	+1.8	+1.9	+2.5	+2.3	+2.0	+1.9	+1.8	+1.8
Gross fixed capital formation deflator	+3.0	+1.5	+1.8	+2.7	+3.6	+2.8	+2.8	+1.9	+0.8	+1.7	+1.8	+1.8	+1.7	+1.8	+1.8
GDP deflator	+1.6	+1.8	+1.6	+1.5	+1.8	+2.2	+1.0	+1.4	+1.5	+1.6	+2.8	+2.2	+1.7	+1.4	+1.3
Unit labor costs	+0.1	+1.1	+0.7	+1.3	–0.4	–0.4	–0.2	–0.3	+1.0	+1.8	+1.7	+1.2	+0.7	+0.5	+0.4
Nominal wages per employee	+1.1	+2.3	+2.2	+1.1	+1.0	+1.0	+1.4	+1.7	+2.2	+2.7	+2.7	+2.5	+2.3	+2.0	+1.9
Productivity	+1.0	+1.2	+1.5	–0.2	+1.4	+1.4	+1.6	+1.9	+1.2	+0.9	+0.9	+1.4	+1.6	+1.6	+1.5
Real wages per employee	–0.5	+0.2	+0.3	–0.2	–1.0	–0.7	–0.3	–0.1	+0.3	+0.2	+0.4	+0.5	+0.4	+0.3	+0.1
Import deflator	+3.2	+2.4	+1.6	+1.8	+3.4	+4.1	+3.6	+3.6	+2.7	+1.8	+1.7	+1.6	+1.6	+1.6	+1.6
Export deflator	+1.4	+2.7	+1.8	–1.1	+0.4	+2.9	+3.3	+3.7	+3.4	+1.8	+1.8	+1.8	+1.8	+1.8	+1.7
Terms of trade	–1.8	+0.3	+0.1	–2.8	–2.9	–1.2	–0.3	+0.2	+0.7	+0.0	+0.2	+0.2	+0.1	+0.1	+0.1
Economic activity	*Annual and/or quarterly changes in % (real)*														
GDP	+1.9	+2.1	+2.3	+0.0	+1.2	+0.9	+0.6	+0.3	+0.3	+0.4	+0.6	+0.7	+0.6	+0.6	+0.6
Private consumption	+1.0	+1.0	+1.3	+0.2	+0.2	+0.2	+0.3	+0.3	+0.3	+0.3	+0.3	+0.3	+0.4	+0.4	+0.4
Government consumption	+0.3	+0.3	+0.3	–0.2	–0.1	+0.1	+1.4	–0.5	–0.3	–0.2	+0.0	+0.2	+0.2	+0.2	+0.1
Gross fixed capital formation	–3.3	+2.1	+3.0	–1.8	–0.6	+0.6	+0.5	+0.4	+0.6	+0.8	+0.9	+0.8	+0.7	+0.6	+0.7
Exports	+10.4	+7.3	+6.9	+2.0	+5.2	+3.4	+1.3	+1.1	+1.3	+1.4	+1.7	+1.9	+1.7	+1.8	+1.8
Imports	+6.8	+6.0	+6.2	+2.2	+3.3	+2.6	+1.1	+1.0	+1.3	+1.4	+1.5	+1.6	+1.5	+1.6	+1.6
	Contribution to real GDP growth in percentage points														
Domestic demand	–0.1	+1.0	+1.3	–0.3	+0.0	+0.3	+0.5	+0.1	+0.2	+0.3	+0.3	+0.4	+0.4	+0.4	+0.4
Net exports	+2.2	+1.2	+1.0	+0.0	+1.3	+0.7	+0.2	+0.1	+0.1	+0.2	+0.2	+0.3	+0.3	+0.2	+0.3
Changes in inventories	–0.2	–0.1	+0.0	+0.2	+0.0	+0.0	–0.1	+0.0	+0.0	+0.0	+0.0	+0.0	+0.0	+0.0	+0.0
Labor market	*% of labor supply*														
Unemployment rate (Eurostat definition)	4.5	4.4	4.3	4.5	4.6	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.3	4.3
	Annual and/or quarterly changes in %														
Total employment	+0.9	+0.9	+0.8	+0.3	+0.3	+0.3	+0.3	+0.2	+0.2	+0.2	+0.2	+0.2	+0.2	+0.3	+0.3
of which: Private sector employment	*+0.9*	*+1.0*	*+1.0*	*+0.3*	*+0.3*	*+0.3*	*+0.3*	*+0.2*	*+0.2*	*+0.2*	*+0.2*	*+0.2*	*+0.3*	*+0.3*	*+0.4*
Payroll employment	+0.8	+1.1	+0.9	+0.1	+0.4	+0.4	+0.4	+0.2	+0.2	+0.2	+0.2	+0.2	+0.3	+0.3	+0.3
Additional variables	*Annual and/or quarterly changes in % (real)*														
Real disposable household income	+0.7	+0.7	+1.4	+0.3	+0.2	+0.7	+0.5	–0.3	+0.1	+0.2	+0.2	+0.5	+0.4	+0.4	+0.4
	% of real GDP														
Output gap	–0.4	–0.2	0.2	–1.2	–0.5	–0.1	0.1	–0.1	–0.2	–0.3	–0.2	0.0	0.1	0.2	0.3

Source: OeNB December 2010 outlook (based on seasonally and working-day adjusted data).

Table 18

Comparison of Current Economic Forecasts for Austria

Indicator	OeNB			WIFO		IAS		OECD			IMF		European Commission		
	December 2010			September 2010		September 2010		November 2010			October 2010		November 2010		
	2010	2011	2012	2010	2011	2010	2011	2010	2011	2012	2010	2011	2010	2011	2012
	Annual change in %														
Key results															
GDP (real)	+1.9	+2.1	+2.3	+2.0	+1.9	+1.8	+2.0	+2.0	+2.0	+2.0	+1.6	+1.6	+2.0	+1.7	+2.1
Private consumption (real)	+1.0	+1.0	+1.3	+1.1	+0.8	+1.0	+1.2	+0.9	+1.1	+1.5	×	×	+0.9	+0.8	+0.9
Government consumption (real)	+0.3	+0.3	+0.3	+0.6	–0.3	+0.5	+0.2	+0.8	–0.2	–0.5	×	×	+0.8	+0.0	+0.5
Gross fixed capital formation (real)[1]	–3.3	+2.1	+3.0	–2.5	+2.4	–0.5	+2.1	–2.4	+2.5	+3.2	×	×	–2.6	+2.7	+2.9
Exports (real)	+10.4	+7.3	+6.9	+9.2	+6.2	+9.3	+6.5	+8.1	+7.6	+5.8	×	×	+9.0	+6.3	+6.5
Imports (real)	+6.8	+6.0	+6.2	+7.3	+5.4	+7.7	+5.5	+5.5	+6.6	+5.3	×	×	+6.4	+5.6	+5.5
GDP per employee	+1.0	+1.2	+1.5	+1.1	+1.2	+1.0	+1.1	×	×	×	×	×	+1.3	+1.0	+1.3
GDP deflator	+1.6	+1.8	+1.6	+1.0	+1.7	+1.3	+1.7	+1.5	+1.1	+1.2	×	×	+0.6	+1.6	+1.3
CPI	×	×	×	+1.8	+2.1	+1.7	+1.8	×	×	×	+1.5	+1.7	×	×	×
HICP	+1.7	+2.2	+1.8	+1.8	+2.1	×	×	+1.6	+1.8	+1.9	×	×	+1.7	+2.1	+1.8
Unit labor costs	+0.1	+1.1	+0.7	+0.3	+1.0	×	×	×	×	×	×	×	+0.3	+1.2	+0.8
Payroll employment	+0.9	+0.9	+0.8	+0.8	+0.6	+0.8	+0.9	×	×	×	×	×	+0.7	+0.7	+0.8
	% of labor supply														
Unemployment rate[2]	4.5	4.4	4.3	4.4	4.3	4.4	4.2	4.5	4.4	4.3	4.1	4.2	4.4	4.2	4.0
	% of nominal GDP														
Current account	2.5	3.4	4.5	2.7	3.3	×	×	2.6	3.1	3.8	2.3	2.4	3.0	3.5	4.1
Government surplus/deficit	–4.1	–3.0	–2.6	–4.1	–3.5	–4.3	–3.4	–4.4	–3.4	–3.0	×	×	–4.3	–3.6	–3.3
External assumptions															
Oil price in USD/barrel (Brent)	79.5	88.6	90.7	76.0	80.0	75.0	75.0	80.0	80.0	80.0	76.2	78.8	79.9	88.9	90.8
Short-term interest rate in %	0.8	1.4	1.7	0.8	1.0	0.8	1.2	0.8	1.1	1.8	0.8	1.0	0.8	1.4	1.7
USD/EUR exchange rate	1.33	1.39	1.39	1.30	1.35	1.30	1.27	1.39	1.39	1.39	1.31	1.28	1.33	1.39	1.39
	Annual change in %														
Euro area GDP (real)	+1.6 to +1.8	+0.7 to +2.1	+0.6 to +2.8	+1.8	+1.7	+1.7	+1.6	+1.7	+1.7	+2.0	+1.7	+1.5	+1.7	+1.5	+1.8
U.S. GDP (real)	+2.7	+2.4	+2.7	+2.7	+2.0	+2.7	+2.3	+2.7	+2.2	+3.1	+2.6	+2.3	+2.7	+2.1	+2.5
World GDP (real)	+4.7	+3.8	+4.2	+4.0	+3.5	×	×	×	×	×	+4.8	+4.2	+4.5	+3.9	+4.0
World trade	+11.7	+7.2	+7.5	+18.8	+8.0	+16.5	+5.5	+12.3	+8.3	+8.1	+11.4	+7.0	+12.1	+7.1	+6.9

Source: OeNB, WIFO, IAS, OECD, IMF, European Commission.

[1] For IAS: Gross investment.

[2] Eurostat definition.