

Research Update

Economic Analysis and Research Department
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Editorial

by Peter Mooslechner
 Director of the Economic Analysis and Research Department

The Crisis 3.0?

On August 9, 2007, in an unusual move, the Eurosystem provided additional liquidity to the banking system to counteract evolving tensions in the money markets. Today, three years after this visible start of the financial crisis, the good news is mainly that there is no longer only bad news. About a year ago, almost all economies worldwide, and the European economy in particular, were in free fall, and nobody really knew where all this would lead to in the end. Meanwhile, the situation has at least stabilized since the second half of 2009 and the world economy returned to a growth rate of about 4% in 2010.

Does this mean that the crisis is over now? Unfortunately, it seems that we are rather in year 4 of the crisis than in year 1 after the crisis. First of all, we should be precise about the type of crisis we are talking about. The key characteristic of this particular crisis – let's call it "Crisis 3.0" – is that it comes in many different shapes and sizes, ranging from financial distress to severe recession and pressure on public finances, and these are not only concurrent, but also mutually reinforcing phenomena.

Looking back, the financial crisis has triggered a global economic crisis, and the policy measures launched to counteract both crises fueled a sovereign debt crisis; now, negative real developments and public finances are again negatively affecting the financial situation. Breaking this vicious circle is obviously the main objective of the wide range of policy measures, including quite unconventional ones, we have seen in the course of the crisis and we are still in to some extent.

But the longer different aspects of the crisis are lasting and the more stable the real economy tends to look, the greater becomes the need to tackle the longer-term issues raised by the crisis, thereby drawing on the lessons learned. Apparently, fundamental structural changes seem to be necessary in many areas; at least four tasks are of utmost importance:

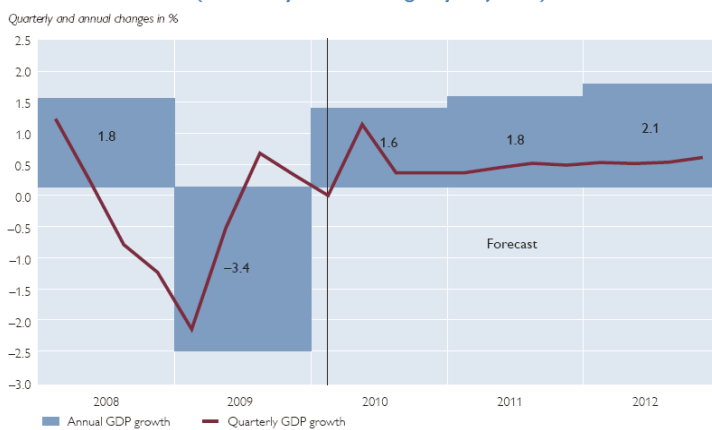
- stabilizing, restructuring and re-regulating the financial system;
- stabilizing public finances and bringing them back on a sustainable path;
- reducing structural imbalances worldwide and within the euro area in particular;
- and, perhaps most importantly, restoring a sustainable and satisfactorily dynamic growth path for the European economy.

These are major tasks lying before us, even more so as central banks will have to play an increased role. Therefore, let's hope that it will be a calm summer that allows us to enjoy some relaxing days of vacation and refill our batteries to tackle the demanding issues ahead.

Subdued Economic Recovery given Necessary Fiscal Consolidation Economic Outlook for Austria from 2010 to 2012 (June 2010)

According to the OeNB's June 2010 economic outlook, GDP is projected to grow by 1.6% in Austria in 2010, after having contracted by 3.4% in 2009. The outlook is even brighter for the years ahead, with a significant acceleration of growth projected for 2011 (1.8%) and especially for 2012 (2.1%). Thus, the economic outlook has improved by 0.4 percentage points for 2010, and by 0.2 percentage points for 2011 over the December 2009 projections, largely thanks to a more rapid recovery of world trade.

Growth of Real GDP (Seasonally and Working Day-Adjusted)



The OeNB expects the annual growth rate of Austrian exports to accelerate to 4.6% in 2010, which is still moderate compared with previous recovery episodes. Looking ahead, export growth is, however, projected to reach 5.4% in 2011 and 6.1% in 2012. By mid-2010, gross fixed capital formation will have moved back into growth territory, yet the annual growth rate for 2010 is expected to remain negative at 4.5%. The growth

outlook further ahead, while positive again at 1.5% (2011) and 2.9% (2012), is nonetheless significantly short of historical averages. Private consumption is projected to grow by 1.1% in 2010. In 2011 and 2012, private consumption growth is expected to be dampened given the restrictive public spending policies underlying the projections. The saving ratio is projected to decline to 10.1% in 2010 and to broadly remain at this level in the following two years. The *unemployment rate* will continue to increase slightly to 5.0% in 2010 and to inch up to 5.1% in 2011, where it will remain also in 2012. *HICP inflation* should come to 1.7%, compared with an exceptionally low rate of 0.4% in 2009. Following unchanged inflation in 2011, a marginal increase to 1.8% is forecast for 2012.

In 2010, the *deficit* will climb to 4.5% of GDP and will subsequently start to shrink in 2011 (4.2%) and 2012 (3.9%) following the more restrictive spending policies the government is expected to embrace. General *government debt* is projected to jump from 66.5% at the end of 2009 to close to 73% of GDP in 2012. In line with Eurosystem rules, these projections reflect only fiscal policy measures that have already been enacted, or that parliamentary adoption of which is only a matter of time. In addition to the baseline projections, the OeNB has also estimated an *economic outlook scenario* which is based on the assumption of compliance with the fiscal consolidation path laid down in Austria's stability program. This scenario yields somewhat lower figures for GDP growth than the baseline scenario, namely 1.7% in the next two years.

38th Economics Conference of the Oesterreichische Nationalbank “Central Banking after the Crisis: Responsibilities, Strategies, Instruments”

Central banks throughout the world have been playing a pivotal role in combating the economic and financial crisis over the past three years. The crisis has transformed our understanding of both the importance and responsibilities of central banks and the strategies and instruments they employ. The OeNB's 38th Economics Conference of May 31 and June 1, 2010 explored „Central Banking after the Crisis: Responsibilities, Strategies, Instruments,“ bringing together distinguished national and international experts and practitioners from the world of politics, business,

finance as well as academia to draw first central banking policy lessons from the crisis. In his opening statement, OeNB Governor Ewald Nowotny stressed central banks' enormous responsibility – and challenge – in pursuing a sustainable monetary policy and safeguarding financial stability. Austria's Federal Chancellor Werner Faymann talked about the challenges that might arise in the aftermath of the crisis. During the *Kamingespräch*, Austrian Vice Chancellor and Federal Minister of Finance Josef Pröll explained his view of current economic and fiscal policies, pointing out that the crisis primarily

highlighted a credibility problem of economic policy.

Session 1 of the conference dealt with the question of whether and how the role of central banks as financial crisis managers is compatible with their political independence and what kind of interaction might occur between the two spheres. For a start, ECB President Jean-Claude Trichet explained the measures the ECB had taken in connection with the current financial market tensions. Economic historian Michael Bordo (Rutgers University) explored the interplay between financial and economic crises on the one hand and central bank independence on the other. During the subsequent panel, chaired by Ernest Gnan (OeNB), Martin Cihak (IMF) and Petra Geraats (University of Cambridge) explored whether the goals of monetary and financial stability are complementary or might sometimes be contradictory. OeNB Vice Governor Wolfgang Duchatczek chaired the second session, during which Stefan Gerlach (University of Frankfurt) presented his views on the question of whether, and how, central banking will change after the crisis. In the subsequent

panel, Anne C. Sibert (Birkbeck College, University of London) and Wolfgang Münchau (Financial Times) discussed the possibly higher risks nonconventional monetary policy measures might entail for the balance sheets and the profitability of central banks. The second conference day focused on new financial market issues raised by the crisis. In the beginning, Giovanni Carosio (Banca d'Italia) and Elena Carletti (European University Institute, Florence) discussed the challenges to be addressed from the implementation of a new European macroprudential supervision mechanism. In the final panel chaired by Peter Mooslechner (OeNB), Urs Birchler (University of Zurich) and Alessandro Profumo (UniCredit Group) discussed the question of how to best deal with very large financial institutions during a crisis.

This year's winners of the Klaus Liebscher Award are Zeno Enders (University of Bonn), Philipp Jung (University of Mannheim) and Gernot Müller (University of Bonn) for their joint paper „Has the Euro Changed the Business Cycle?“.

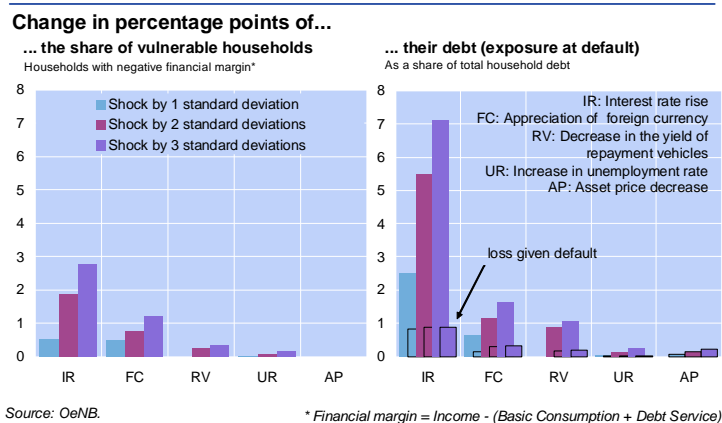
Stress Testing Austrian Households

The sharp increase in household debt over the past decades has raised questions about the sustainability of this debt and about possible risks for the banking sector. As the U.S. subprime crisis and its repercussions recently demonstrated, even a relatively small number of indebted households can produce heavy turmoil if the sustainability of their debt is in question.

The scope of aggregate data for analyzing these risks to financial stability is very limited, because it is neither possible to differentiate between households that hold debt and those that do not, nor is it possible to combine the data on household debt with data on their assets in a reasonable way. Therefore, many authorities concerned with financial stability are increasingly using microdata to analyze such types of financial stability risks. Combining different microdata sources, we assess financial stability risks arising from indebted households in Austria.

We define a financial margin for indebted households and find that around 9.2% to 15.6% of those are vulnerable, i.e. they have a negative financial margin. Under the assumption that all households with a negative financial margin have a probability of default of

1, the EAD (Exposure at Default) is 14.3%, LGD_1 (Loss Given Default - considering only real estate wealth to cover debt) is 2.6% and LGD_2 is 2.1% (Loss Given Default - considering real estate and financial wealth) of total household debt. We stress the indebted households' finances by assuming different types of shock scenarios: changes in interest rates, unemployment rate, asset prices, exchange rates and repayment vehicle yields (see chart below).



Although the interest rate shock has the strongest impact of all tested scenarios, the risk that households bear is particularly high for those with foreign currency loans and bullet loans; since these loans are often a combination of the two, the resulting risks are multiplied. All in all, the potential loan losses for banks resulting from shocks to Austrian households do not compromise financial stability as a whole. The risk that households bear is particularly high for those with foreign currency loans and bullet loans; since these loans are often a combination of the two, the resulting risks are multiplied.

However, the fact that around 10% of indebted households may have problems and need to reduce

expenses to be able to service their debt if a shock occurs is worrisome. Also, it should be noted that this analysis does not include consumption credit debtors, who – even if the amount of their debt is, on average and in total, much smaller and therefore does not pose a threat to financial stability at all – are not as well off as indebted homeowners and may suffer more under their debt servicing duties.

Albacete, N. and P. Fessler. 2010. Stress Testing Austrian Households. In: Financial Stability Report 19. OeNB. June.

Bank of England Chief Economists' Meeting on „State-of-the-Art Modelling for Central Banks”

Contribution by Peter Mooslechner „A Crisis with Fundamental Effects. Diversity of Perspectives and Pluralism of Models as Challenges for Economic Policymaking”

This year's traditional Bank of England Chief Economists' Meeting in May 2010 dealt with the broad and highly relevant policy issue of „State-of-the-Art Modelling for Central Banks“ – obviously one of the challenges to be addressed in the aftermath of the recent financial crisis. Keynote speakers were Nouriel Roubini (New York University), Andrew W. Lo (MIT) and Alan Kirman (Université Aix-en-Provence).

The contributions by central bank economists included Peter Mooslechner's talk on the impact of the financial crisis on economic policymaking and research inside and outside central banks. Starting with a short discussion about the widespread failure to see the crisis coming („How did economists get it so wrong?” (Paul Krugman)) and about whether this might have to do with the inherent structure of prevalent economic reasoning, Mooslechner argued that the Great Moderation had been accompanied by an unusual „Great Consensus” in policymaking and economics. This convergence of opinions, however, came at a cost. In fact, it had left policymakers „with a disturbing inflexibility when in a very short period of time the economic environment shifted from the Great Moderation to a

global financial crisis and recession.”

Against this backdrop, the case for more pluralism in economic analysis, modelling and policy advice gained considerably in importance. In particular, a more pluralistic approach in various areas, including goals, instruments, models, economic policy rules and the general framework of central bank research seems to be warranted or even unavoidable. The new macroprudential responsibilities, the unconventional monetary policy measures taken and the need for more „unconventional elements” in economics and finance have created important new challenges for central banks and are very likely to stay with us for a very long time. Such a more pluralistic approach can be expected to be beneficial in an environment of persistently higher uncertainty, even if it will make decision making more complex and demanding. In the long run, however, „it may turn out to be much more valuable than concentrating all efforts on a single paradigm or on one methodological framework, in particular in an environment characterized by volatility, unexpected shocks, suboptimal equilibria and new types of policy challenges.”

6th OeNB-Brussels Economic Round-Table: Crisis Managed, Lessons Learned? New Ideas to Improve European Economic Governance

On Thursday, 6th May 2010, the Representative office of the OeNB in Brussels organised its 6th Economic Round-Table under the title “*Crisis managed, lessons learned? New ideas to improve European Economic Governance*”. As Peter Mooslechner, Director of the OeNB’s Economic Analysis and Research Department, who chaired the Round-Table stated at the beginning, the discussion was highly topical: at the very same day, the European Council was busy drafting its support package for Greece and the European Commission was working on its communication on reinforcing economic policy coordination in the EU, to be published the week after.

Evelyn Regner, MEP (ALDE/AT), presented survey results from Austria on the question who was responsible for the crisis and what should be done to

prevent a similar event for the future: the majority of Austrians thinks the originators of the crisis are not the same people who will pay for it and the EU should regulate financial markets more effectively. Daniel Gros, Director at CEPS, criticized the EU for not having a Plan B in case of a sovereign debt crisis and proposed a European Stability Funds which should orderly unwind the debt of defaulting member states. The Funds should be guided by automatic rules to avoid political deals or lengthy discussions, e.g. when determining the haircut on government bonds. Peter Weiss, DG Ecfm, focussed on the debt dynamics in EU member states. As hardly one member state had adhered to the principle of countercyclical budgeting so far, the Commission was ready to ask for more surveillance powers within the preventive arm of the Stability and Growth Pact.

The Analysis of Statistical Data on Credit Extension and the Results of Surveys on Credit Conditions (Bank Lending Survey and a Survey among Austrian Firms) Do Not Deliver any Clear Indication of a Credit Crunch in Austria

The annual growth rate of MFI-loans extended to non-financial corporations (NFCs) in Austria declined markedly since the beginning of 2009. Starting with December 2009 the annual growth rate of loans to NFCs has been negative for the first time in the present credit cycle. Since then the annual growth rate of loans to NFCs stabilized at levels close to -2%. In contrast, the annual growth rate of loans to private households has been on a declining path since the beginning of 2005. This trend steepened from mid 2008 on but in fall 2009 the growth rates stabilized at levels slightly above 0% and have rebounded somewhat since then to levels around 1%. Thus, again in contrast to loans to NFCs, the loan growth to private households already seems to have reached its turning point in the last quarter of 2009, but growth rates are still low compared to the historical development.

According to the Bank Lending Survey of the Eurosystem (BLS) the credit standards of loans to NFCs have become tighter in Austria since mid 2007 but have

not been tightened further from Q3 2009 on. The tightening was mostly caused by the perception of risk of banks which represents the cyclical component of credit supply, but less so by the banks’ own balance sheet constraints which would indicate a credit crunch commonly triggered by the banks’ difficulties in their own refinancing. The demand for loans, in contrast, has declined in Austria according to the BLS also in the most recent quarters. The main cause appears to be lower financing needs which are a consequence of a marked decline in corporate investment.

A survey conducted among Austrian firms confirms the finding of the BLS that credit conditions became tighter during the financial crisis up to the end of 2009. Starting with the first quarter of this year the further increase in restrictions on credit conditions eased somewhat, in particular for large firms and for loans with long maturities. Overall, however, credit conditions are still tight and demand for new loans remains subdued.

Workshop on „Macro-Financial Stability in CESEE: Have we Learned all the Lessons?”

On June 21, 2010, the Oesterreichische Nationalbank (OeNB) hosted a workshop on „Macrofinancial Stability in CESEE: Have we Learned all the Lessons?” More than 50 selectively invited participants took part in the event: representatives of commercial banks operating in CESEE, home and host country supervisory authorities, EU institutions and IFIs.

The workshop focused on three issues related to macrofinancial stability in CESEE: (i) recent developments in cross-border lending, including cross-border capital and liquidity allocations; (ii) implications of the credit cycle for banks' business models and credit risk management; (iii) the issue of foreign currency lending in CESEE. Following valuable presentations, each session was characterized by questions & answers and an open and frank discussion of these topics, including of policy suggestions.

OeNB Governor Ewald Nowotny held an introductory statement. He highlighted the factors that led to overheating of domestic demand in general and to excessive credit growth in particular in some countries in the last few years before the crisis. Moreover, he drew lessons from the boom and the crisis in CESEE and addressed current risks and challenges for the banking sectors in CESEE.

Session 1, chaired by Philip Reading (OeNB, Director of Financial Stability and Bank Inspections Department), dealt with cross-border lending and cross-border capital and liquidity allocation. Radovan Jelašić (Governor, National Bank of Serbia) shared the Serbian experience with cross-border bank lending to banks and non-banks against the background of the domestic measures taken by the Serbian authorities. Ralph de Haas (EBRD) presented the results of empirical studies on cross-border bank funding and its impact on the local banking sector. Then, Manfred Wimmer (Erste Group Bank) and John Hollows (KBC Group) presented the views of two

practitioners on capital and liquidity allocation in multinational banks by contrasting the scope for action in boom times and in crisis times.

Session 2 was chaired by Peter Mooslechner (OeNB, Director of Economic Analysis and Research Department) and dealt with boom, bust and credit risk in CESEE under the title: Is the worst yet to come? Henry MacNevin (Moody's) spoke about the prospects of recovery in Emerging Europe, the distribution of bank ratings and the merits of foreign ownership. Piergiorgio Pradelli (Eurobank EFG) highlighted the implications of the crisis for banks' business models in CESEE, stressing the role of the „Vienna Initiative”. Dubravko Mihaljek (BIS) elaborated on banking sector risks in CESEE, distinguishing between challenges (global, regional, country-specific), responses (in the various policy fields) and outlook (short-term, medium-term).

Session 3, chaired by Michael Würz (OeNB, Head of Financial Markets Analysis and Surveillance), focused on „Foreign Currency Lending in CESEE – A Threat to Stability?” It was held in the form of a panel discussion with six panellists: Carlo Vivaldi (UniCredit Bank Austria AG) and Martin Grüll (Raiffeisen International Bank-Holding AG) presented the perspective of parent banks, while Ion Dragulin (National Bank of Romania) shared the view of a local supervisor and the Romanian experience with foreign currency lending. Moreover, Peter Grasmann (DG Ecfm, European Commission), Mark Allen (IMF) and Piroska Nagy (EBRD) presented the perspective of their respective institutions on this issue, with the latter presenting the EBRD's initiative for organic local currency and local capital market development and risk management as an answer to dependence on foreign exchange and foreign savings.

If you are interested in some of these presentations, please do not hesitate to contact us.

OeNB Guest Professor 2010 Peter Howitt: „The Macroeconomics of Self Organising Economies”

On June 14. and 15th 2010 Peter Howitt, Brown University, visited the research division of OeNB and gave a series of lecture on the topic „The Macroeconomics of Self Organising Economies”. The main theme of the lecture was an overview on recent research attempting at new approaches to macroeconomic modelling. The lectures described an approach to macroeconomics that focuses on what Jevons called the mechanism of exchange. The approach starts from the premise that a free market economy depends for its smooth functioning on a self-organizing network of firms that create and operate markets. Collectively, these firms play the part of Walras's auctioneer, matching buyers with sellers and helping the economy to approximate an efficient equilibrium even though no one in the economy understands it. Instead of

using the methods of rational-expectations equilibrium, the approach is based on agent-based computational analysis, an approach that has been used in many disciplines to study large complex systems in which distinct patterns emerge from the interaction of heterogeneous agents with relatively simple behavioural patterns. The first lecture introduced the method by showing how to build a highly stylized artificial economy in which money and markets evolve from purely local interactions. The next two lectures were organized around the substantive themes of inflation and bank regulation, both of which can be studied using a more elaborate version of the artificial economy introduced in the first lecture. Methodological issues raised by the approach were discussed in all three lectures, as well as the related literature on agent-based financial markets.

Olga Radzyner Award 2010 for Scientific Work on European Economic Integration

The Oesterreichische Nationalbank has established an award to commemorate Olga Radzyner, former Head of the Foreign Research Division, who died in a tragic accident in August 1999. The award is bestowed on young economists for excellent research focused on topics of European economic integration and is conferred annually. In 2010, four applicants are eligible to receive a single payment of EUR 3,000 each from an annual total of EUR 12,000.

The submitted work shall be in English or in German, should not exceed approximately 30 pages and shall preferably be in the form of a working paper or a scientific article. The topic of the submitted work should be on European economic integration issues. Authors shall submit the work before their 35th birthday and shall be citizens of any of the following countries: Albania, Belarus, Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Estonia, FYR Macedonia, Hungary, Kosovo, Latvia, Lithuania, Moldova, Montenegro, Poland, Romania, Russia, Serbia, Slovakia, Slovenia and Ukraine. Previous winners of the Olga Radzyner Award, ESCB central bank employees as well as current and former OeNB staff are not eligible. In case of coauthored work, each of the coauthors has to fulfill all the criteria.

The Oesterreichische Nationalbank shall receive the work submitted for this award, by October 4, 2010, and the work shall be sent by electronic mail to eva.gehringer-wasserbauer@oenb.at or in hard copy to the Oesterreichische Nationalbank, Foreign Research Division, Otto Wagner-Platz 3, POB 61, A-1011 Vienna, Austria. To identify their work as a submission, applicants shall mark the envelope with the reference „Olga Radzyner Award”. Apart from the copy of the applicant's birth or citizenship certificate, the author shall provide a brief CV.

For detailed information, please visit our Internet website at <http://ceec.oenb.at> or contact Eva Gehringer-Wasserbauer in the Foreign Research Division of the Oesterreichische Nationalbank either by e-mail (eva.gehringer-wasserbauer@oenb.at) or by phone (+43-1-40420-5205).

Workshop: „Consumer Payment Choice and the Demand for Money”

In cooperation with the Fernando Alvarez (University of Chicago), Francesco Lippi (University of Sassari and Einaudi Institute of Economics and Finance) and the Research Center of the Deutsche Bundesbank, the Oesterreichische Nationalbank organized and hosted a two day workshop on „Consumer Payment Choice and the Demand for Money” (July 1 and 2).

The workshop was motivated by the fact that consumers’ payment behavior and demand for currency has undergone a considerable transformation with the advancement and dissemination of new payment and withdrawal technologies. This development has stimulated an increasing interest among economists, providing new theoretical and empirical insights on how these technological transformations affect money demand and hence monetary policy. Another strand of the literature has concentrated on the choice of payment instruments and on consumer behavior – from the determinants of the adoption of payment cards to the consequences on households’ financial decision making, such as incurring credit card debt. Against this background, the aim of the workshop was to bring together leading scholars who work on this topic, to shape the research agenda and to disseminate new ideas and modelling approaches.

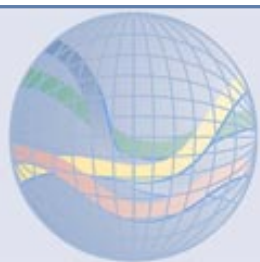
The audience comprised of researchers from several central banks as well as renowned scholars from a variety of countries and the presented papers illustrate the diversity of interests that economist are bringing to the study of this topic, ranging from theoretical models

of money and payments to empirical analyses of trends in consumer payments. Importantly, views from both sides of the Atlantic were presented, providing the basis for a discussion of differences and similarities in payment trends.

The presented papers: (title/presenter)

- How Consumers Pay: Adoption and Use of Payments (Scott Schuh, Federal Reserve Bank of Boston)
- Cash, Debit or Credit: Why, Where and When? - A Canadian Survey (Carlos Arango, Bank of Canada)
- Consumer Choice and Merchant Acceptance of Payment Media (Wilko Bolt, De Nederlandsche Bank)
- Using Cash to Control Expenditures – Implications For Payments, Withdrawal Behavior and Currency Demand (Tobias Schmidt, Deutsche Bundesbank)
- The Impact of the Debit Card on Money Demand (David Bounie, Ecole Nationale Supérieure des Télécommunications)
- Currency Demand with Uncertain Lumpy Purchases (Fernando Alvarez, University of Chicago)
- Rebalancing Frequency and the Welfare Cost of Inflation (Andre Silva, Universidade Nova de Lisboa)
- The Case for a Financial Approach to Money Demand (Xavier Ragot, Banque de France and Paris-Jourdan Sciences Economiques)

The full workshop program can be obtained from beate.hofbauer@oenb.at



FRANZ WENINGER AWARD

Award for master’s and doctoral theses in the field of monetary theory and monetary policy

The Franz Weninger Award is granted at the annual Conference on European Economic Integration (CEEI) of the Oesterreichische Nationalbank (OeNB). The OeNB confers this award every year for outstanding master’s and doctoral theses in the field of monetary theory and monetary policy in commemoration of the late head of the Economic Analysis Division of the OeNB. The Governing Board of the OeNB bestows the Franz Weninger Award on recommendation of a panel of experts.

Three one-time prizes of EUR 3,000 each may be conferred for such theses every year. The theses shall be approved by an Austrian university. Approval shall be from the academic year (October 1 – September 30) immediately preceding the submission date. The master’s or doctoral thesis submitted shall be postmarked October 4, 2010, at the latest, must bear the reference „Franz-Weninger-Stipendium/Franz Weninger Award“ and sent to Oesterreichischen Nationalbank, Otto-Wagner-Platz 3, A-1090 Vienna, Austria. For further details please go to [Conditions for Participation](#) on the OeNB webpage (you can also the order these conditions via telephone or e-mail).

OeNB Periodical Publications

http://www.oenb.at/de/geldp_volksw/vowi_pub/volkswirtschaftliche_publicationen.jsp

List of all Publications since 2001 (by staff of the Economic Analysis and Research Section):

http://www.oenb.at/de/img/publications_2010_2_fin_tcm14-189588.pdf



Financial Stability Report 19

From Stormy Expansion to Riding out the Storm: Banking Development in Kazakhstan (Barisitz, Lahnsteiner)

Stress Testing Austrian Households (Albacete, Fessler)

Effects of the Payment Services Act on the Austrian Financial Market (Freitag, Schimka)

Assessing the Relevance of Austrian Investment Companies and Mutual Funds for Financial Stability (Kavan, Sedlacek, Seliger, Ubl)



Focus on European Economic Integration Q2/10

Private Sector Credit in CESEE: Long-Run Relationships and Short-Run Dynamics (Eller, Frömmel, Srzentic)

Real Effects of Crisis Have Reached CESEE Households: Euro Survey Shows Dampened Savings and Changes in Borrowing Behavior (Dvorsky, Scheiber, Stix)

SUERF Conference and Special East Jour Fixe – Contagion and Spillovers – New Insights from the Crisis

66th East Jour Fixe – Kazakhstan – From Star Performance to Crisis Management and Back Again?

Olga Radzyner Award 2010 for Scientific Work on European Economic Integration



Monetary Policy and the Economy Q2/10

Subdued Economic Recovery given Necessary Fiscal Consolidation. Economic Outlook for Austria from 2010 to 2012 (June 2010) (Ragacs, Vondra)

Real Estate Inheritance in Austria (Fessler, Mooslechner, Schürz)

Modeling and Predicting the EUR/USD Exchange Rate: The Role of Nonlinear Adjustments to Purchasing Power Parity (Crespo Cuaresma, Orthofer)

Stock Market Volatility and the Business Cycle (Raunig, Scharler)

Summary of the 38th Economics Conference (Gnan, Kaufmann)



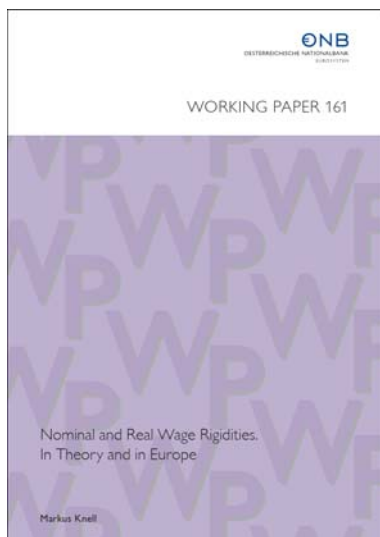
Sustainability Report 2009

Annual Report 2009 including the Intellectual Capital Report and the Environmental Report

In line with the Federal Act on the Oesterreichische Nationalbank, the Annual Report of the OeNB provides information about the monetary policy of the Eurosystem, reviews economic developments and describes the OeNB's tasks and its role in maintaining price and financial stability. Furthermore, it recounts the OeNB's main activities in its core business areas. The OeNB's Financial Statements are a central part of the Annual Report. The Annual Report 2009 also features the OeNB's Intellectual Capital Report and Environmental Statement, which were previously published as separate items of the combined Sustainability Report.

OeNB Working Papers

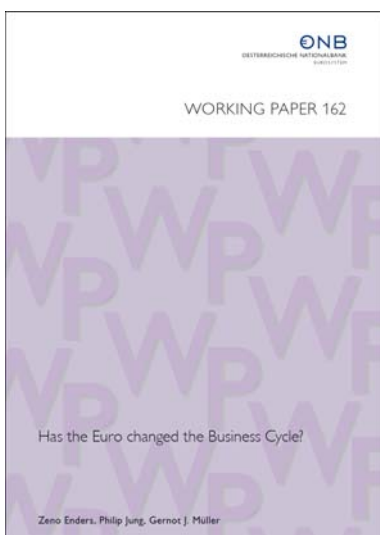
http://www.oenb.at/en/presse_pub/research/020_workingpapers/working_papers_2010.jsp



Nominal and Real Wage Rigidities. In Theory and in Europe

Markus Knell (Working Paper 161)

In this paper the author studies the relation between real wage rigidity (RWR) and nominal price and wage rigidity. He shows that in a standard DSGE model RWR is mainly affected by the interaction of the two nominal rigidities and not by other structural parameters. The degree of RWR is, however, considerably influenced by the modelling assumption about the structure of wage contracts (Calvo vs. Taylor) and about other institutional characteristics of wage-setting. The author uses survey evidence on price and wage-setting for 15 European countries to calculate the degrees of RWR implied by the theoretical model. The average levels of RWR are broadly in line with empirical estimates based on macroeconomic data. In order to be able to also match the observed cross-country variation in RWR it is, however, essential take more institutional details into account.



Has the Euro changed the Business Cycle?

Zeno Enders, Philip Jung, Gernot J. Müller (Working Paper 162)

In this paper the authors analyze European business cycles before and under EMU. Across the two periods the authors find 1) a significant decline in real exchange rate volatility, 2) significant changes in cross-country correlations, and 3) the volatility of macroeconomic fundamentals largely unchanged. They develop a two-country business cycle model and show that the calibrated model is able to replicate key features of the data prior to and under EMU. The authors find that the euro has a strong bearing on the transmission mechanism as cross-country spillovers increase substantially under EMU. As a result, foreign shocks become more and domestic shocks less important in accounting for the (unchanged) volatility of macroeconomic fundamentals.

External Publications by Staff Members

„What do Russians think about Transition?“

Irina Denisova, Markus Eller, Ekaterina Zhuravskaya; *Economics of Transition* 18(2), February 2010, 249-280

We use data from the 2006 round of the Russian Longitudinal Monitoring Survey to describe perceptions of the Russian population about the transition process and the role of the state compared with that of free markets. We find that about one-half of the Russian population is disappointed with transition and a large majority is in favour of high state regulation and state provision of goods and services. High demand for government regulation and increased state intervention coexists with a low level of trust in government institutions and recognition of high and rising levels of corruption. The findings are consistent with the theory developed by Aghion et al. (2009). In an environment with poor social capital, private business imposes negative externalities on the society and society chooses to demand more state regulation and tolerate corruption to reduce these externalities. We also find that individual perceptions of social capital and corruption co-vary with the demand for regulation, as predicted by the theory.

„No risk and some fun? Trade and wages in the enlarged European Union“

Éva Katalin Polgár and Julia Wörz; *Empirica*, 37, April 2010, 127–163

This paper analyses the relationship between openness to trade and wages at the industry level (15 manufacturing and 6 service industries) in 25 EU countries over the period from 1995 to 2005. By applying a cross-country and industry-specific approach, it is possible to control for unobserved heterogeneity at both country and industry levels. We also differentiate between intra and interindustry trade and we try to assess the relative importance of foreign wages versus domestic productivity developments in an open environment. We find that trade is not an important driver of wages, since the wage response to trade is small. Moreover, in line with the Stolper-Samuelson reasoning, the overall wage impact is always positive if significant in central and eastern Europe, while in western Europe we often observe a negative response, particularly in resource-based industries. Nevertheless, increased trade reinforces the productivity-wage link and weakens the co-movement of wages in eastern Europe, while there is less evidence of a similar wage-disciplining effect of trade in the west.

„Default Rates in the Loan Market for SMEs: Evidence from Slovakia“

Jarko Fidrmuc, Christa Hainz; *Economic Systems* 34(2), June 2010, 133-147

Financial markets in emerging economies are often perceived as more risky than those in developed countries. We investigate whether this is true for loans to SMEs using a unique unbalanced panel of nearly 700 loans made to SMEs in Slovakia between 2000 and 2005. Several probit and panel probit models show that liquidity and profitability factors are important determinants of SME defaults. Moreover, we find that indebtedness significantly increases the probability of default. Liability as proxied by the legal form of SMEs has important incentive effects. Finally, there exist significant differences between sectors. We show that default rates and factors converged to values found in developed financial markets.

„The Impact of the Global Financial Crisis on Business Cycles in the Emerging Economies in Asia“

Jarko Fidrmuc, Iikka Korhonen; *Journal of Asian Economics* 21(3), June 2010, 293-303.

We analyze the transmission of global financial crisis to business cycles in China and India. The pattern of business cycles in emerging Asian economies generally displays a low degree of synchronization with the OECD countries, which is consistent with the decoupling hypothesis. By contrast, however, the current financial crisis has had a significant effect on economic developments in emerging Asian economies. Applying dynamic correlations, we find wide differences for different frequencies of cyclical development. More specifically, at business cycle frequencies, dynamic correlations are typically low or negative, but they are also influenced most by the global financial crisis. Finally, we find a significant link between trade ties and dynamic correlations of GDP growth rates in emerging Asian countries and OECD countries.

„A Monetary Real-Time Conditional Forecast of Euro Area Inflation”

Sylvia Kaufmann and Peter Kugler; *Journal of Forecasting*, Volume 29(4) July 2010, Pages: 388-405

Based on a vector error correction model we produce conditional euro area inflation forecasts. We use real-time data on M3 and HICP, and include real GDP, the 3-month EURIBOR and the 10-year government bond yield as control variables. Real money growth and the term spread enter the system as stationary linear combinations. Missing and outlying values are substituted by model-based estimates using all available data information. In general, the conditional inflation forecasts are consistent with the European Central Bank's assessment of liquidity conditions for future inflation prospects. The evaluation of inflation forecasts under different monetary scenarios reveals the importance of keeping track of money growth rate in particular at the end of 2005.

„The Role of Credit Aggregates and Asset Prices in the Transmission Mechanism: A Comparison between the Euro Area and the USA”

Sylvia Kaufmann and Maria Teresa Valderrama; *The Manchester School*, Vol 78 No. 4 345–377

We analyse the interaction between credit and asset prices in the transmission of shocks to the real economy using a Markov switching vector autoregression. While we confirm the existence of different regimes, we find no evidence of financial imbalances coming from mutually reinforcing effects of lending and asset prices in the euro area. In the USA, on the contrary, there is some evidence for reinforcing effects between asset prices and lending. Moreover, it turns out that in the USA asset prices are important determinants of GDP, while in the euro area lending is an important determinant of inflation.

„Comment to: The role of monetary aggregates in the policy analysis of the Swiss National Bank, by Jürgen Wolters and Gebhard Kirchgässner”

Sylvia Kaufmann; *Swiss Journal of Economics and Statistics* Vol 146,255-267

„A Systematic Approach to Multi-Period Stress Testing of Portfolio Credit Risk”

Thomas Breuer, Martin Jandačka, Javier Mencía, Martin Summer; *Banco de España*, Working Paper No. 1018, June 2010

We propose a new method for analysing multiperiod stress scenarios for portfolio credit risk more systematically than in the current practice of macro stress testing. Our method quantifies the plausibility of scenarios by considering the distance of the stress scenario from an average scenario. For a given level of plausibility our method searches systematically for the most adverse scenario for the given portfolio. This method therefore gives a formal criterion for judging the plausibility of scenarios and it makes sure that no plausible scenario will be missed. We show how this method can be applied to a range of models already in use among stress testing practitioners. While worst case search requires numerical optimisation we show that for practically relevant cases we can work with reasonably good linear approximations to the portfolio loss function that make the method computationally very efficient and easy to implement. Applying our approach to data from the Spanish loan register and using a portfolio credit risk model we show that, compared to standard stress test procedures, our method identifies more harmful scenarios that are equally plausible.

„Nominal and real wage rigidities. In Theory and in Europe”

Markus Knell; *European Central Bank (ECB) Working Paper No. 1180*, April 2010

In this paper I study the relation between real wage rigidity (RWR) and nominal price and wage rigidity. I show that in a standard DSGE model RWR is mainly affected by the interaction of the two nominal rigidities and not by other structural parameters. The degree of RWR is, however, considerably influenced by the modelling assumption about the structure of wage contracts (Calvo vs. Taylor) and about other institutional characteristics of wage-setting (clustering of contracts, heterogeneous contract length, indexation). I use survey evidence on price- and wage-setting for 15 European countries to calculate the degrees of RWR implied by the theoretical model. The average levels of RWR are broadly in line with empirical estimates based on macroeconomic data. In order to be able to also match the observed cross-country variation in RWR it is, however, essential to move beyond the country-specific durations of price and wages and to take more institutional details into account

Changes in the Austrian structure of wages, 1996–2002: evidence from linked employer-employee data
Wolfgang Pointner, Alfred Stiglbauer; Empirica 37(2), May 2010, 105–125

Analyzing data from the Structure of Earnings Surveys we find that wage dispersion in Austria increased only marginally between 1996 and 2002. There was an increase in the returns to education which accrued only to male workers. The positive effects of tenure and especially of experience on wages decreased over time. We adopt the Machado–Mata (J Appl Econ 20:445–465, 2005) counterfactual decomposition technique which allows to attribute changes in each wage decile to changes in worker and workplace characteristics and into changes in returns to these characteristics. Behind the small net increase in inequality we document a number of interesting gross effects that influence the change in the wage distribution. We find that both composition effects due to gender, education and age and market-driven effects such as changes in returns and changing workplace characteristics contributed to a higher dispersion of wages.

New Conditions to Ensure the Sustainability of Austria’s Public Finances
Bernhard Grossmann; In: Bauer H., H. Pitlik und M. Schratzenstaller (Eds.). Demografischer Strukturwandel als Herausforderung für die öffentlichen Finanzen. Neuer Wissenschaftlicher Verlag

Based on the European Commission’s „S1” sustainability indicator, this contribution investigates Austria’s budget consolidation requirements from three angles: the European Commission’s latest age-related public expenditure projections, the discretionary fiscal policy measures taken to stimulate the economy in response to the global economic crisis, and the crisis-induced output loss.

Upcoming and Recent Events

The following events are organized by the OeNB. Please note that attendance is by invitation only. If you are interested in participating in one or more of the events, please send an e-mail to OeNB.ResearchUpdate@oenb.at

Upcoming	
August 30 – September 3, 2010	OeNB Summer School: Micro Econometrics
November 15–16 2010	OeNB Conference on Eastern European Integration: Catching-Up Strategies after the Crisis
Recent	
June 25, 2010	Friday Seminar held by Christian Ewerhart (University of Zurich): “Repo Markets, Counterparty Risk, and the 2007/2008 Liquidity Crisis”
June 21, 2010	CESEE Workshop: Macro-Financial Stability in CESEE: Have we learned all the lessons?
June 14, 2010	Press conference: Gesamtwirtschaftliche Prognose der OeNB für Österreich 2010 bis 2012 vom Juni 2010

OeNB Courses at the Joint Vienna Institute (JVI)

For further details see: http://www.jvi.org/fileadmin/jvi_files/JVI_Program2010.pdf

September 13–17, 2010	Macro-financial Stability and the Road to the Euro
October 4–8, 2010	Monetary and Financial Statistics Collected and Compiled by the ESCB
October 11–14, 2010	Economic and Monetary Integration in Europe: CIS Related Aspects

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