

Austria's economy set to grow by close to 3% in 2018

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Economic growth in Austria peaked at the end of 2017. The first half of 2018 saw a gradual return to average growth. According to the most recent figures of the OeNB's Economic Indicator of September 2018, this trend is set to continue in the second half of the year. Based on its quarterly forecasting exercise, the Oesterreichische Nationalbank (OeNB) expects real GDP in Austria to rise by 0.6% in the third quarter and by 0.5% in the fourth quarter of 2018 (quarter on quarter; adjusted for seasonal and working-day effects), and thus to remain above the long-term average growth rate of 0.4% until year-end. Thanks to particularly strong growth early in the year, the predicted growth rate for 2018 as a whole is 2.8%, slightly higher than in 2017. External economic uncertainties such as the further course of international trade conflicts and the Brexit negotiations represent a downside risk to the present forecast.

Inflation is expected to remain on a steady course over the next few years. The OeNB forecasts a HICP inflation rate of 2.2% for both 2018 and 2019, followed by a slight decline to 2.0% in 2020. The fact that inflation is set to remain above 2% for the time being can be attributed mainly to favorable economic trends and robust growth in unit labor costs. HICP inflation is not expected to slow until 2020, when crude oil prices are likely to decline. Falling rates of inflation in the energy products market are expected to be largely balanced out by rising inflation rates in the services sector over the forecast horizon. As a result, core inflation (excluding energy and food) is projected to rise from 2.0% in 2018 to 2.3% in 2019 and level off at 2.2% in 2020.

1 Austria's economy maintains growth momentum in first half of 2018

Austria's economy continued to grow strongly in the first half of 2018. According to the most recent national accounts data, real GDP growth stood at 0.8% in the first quarter and 0.6% in the second quarter of the year (quarter on quarter; in real terms, trend-cycle component adjusted for seasonal and working-day effects) and thus remained above the long-term average of 0.4%. However, the growth momentum has slowed slightly from the peak recorded in the fourth quarter of 2017 (0.9%).

The main driver of growth was domestic economic activity. Household consumption went up by 0.5% (quarter on quarter) in each of the first two quarters of 2018, while businesses stepped up their investment spending by approximately 1% in each quarter. Somewhat unexpectedly, both investment in construction and investment in plant and equipment accelerated slightly from the second half of 2017. Despite challenging and uncertain external conditions, Austrian exports of goods and services were up by 1.1% in the first and second quarter of 2018, putting export growth slightly above import growth.

On the output side, the industrial sector recorded the greatest momentum: With average growth rates of 1¼% in the first two quarters, gross value added in industry was nearly twice as high as in the economy as a whole. The services sector continues along a steady path, with growth rates of about 0.5%.

In the most recent data published by Statistics Austria, historical national accounts data have been revised, in some cases substantially. The new data now indicate stronger momentum in 2016, at the beginning of the current cycle;

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Table 1.1

National accounts data for Austria as of September 25, 2018

	GDP	Private consumption	Government consumption	Gross fixed capital formation	Of which: Construction investment	Residential construction investment	Nonresidential construction investment	Investment in plant and equipment
<i>Change on previous period in %</i>								
Q1 17	+0.7	+0.3	+0.4	+1.3	+0.9	+1.0	+0.8	+2.1
Q2 17	+0.6	+0.4	+0.2	+0.8	+0.5	+1.0	+0.3	+1.1
Q3 17	+0.7	+0.5	+0.1	+0.7	+0.6	+0.7	+0.5	+0.6
Q4 17	+0.9	+0.5	0.0	+0.7	+0.7	+0.7	+0.7	+0.6
Q1 18	+0.8	+0.5	+0.2	+1.0	+0.8	+0.8	+0.8	+1.3
Q2 18	+0.6	+0.5	+0.5	+1.0	+0.7	+0.8	+0.7	+1.7
2014	+0.7	+0.2	+0.9	-0.2	+0.5	-0.1	+0.9	-1.4
2015	+1.1	+0.4	+0.8	+2.1	-0.3	+0.8	-1.0	+4.2
2016	+2.0	+1.4	+1.7	+4.2	+0.5	+2.4	-0.8	+9.7
2017	+2.7	+1.7	+1.5	+3.8	+3.2	+3.3	+3.1	+4.8

Data revised since July 30, 2018*Percentage points*

Q3 17	-0.1	0.0	0.0	-0.7	0.3	0.3	0.3	-2.2
Q4 17	0.0	0.0	-0.1	-0.5	0.2	0.2	0.1	-1.6
Q1 18	0.0	0.1	0.1	-0.3	0.1	0.2	0.0	-0.6
Q2 18	-0.1	0.0	0.2	-0.1	0.2	0.4	0.0	0.0
2014	-0.2	-0.1	-0.1	0.4	0.3	0.3	0.4	0.4
2015	0.1	-0.1	-0.5	1.1	-1.1	0.4	-2.2	2.8
2016	0.5	-0.1	-0.3	0.4	-0.8	1.6	-2.4	1.1
2017	-0.3	0.1	0.3	-1.1	1.0	1.2	0.9	-4.1

Source: WIFO, OeNB calculations.

Table 1.2

National accounts data for Austria as of September 25, 2018

	Investment in transport equipment	Machinery investment	Exports	Imports	Domestic demand (excluding changes in inventories)	Net exports	Changes in inventories	Statistical discrepancy
<i>Change on previous period in %</i>				<i>Contribution to GDP growth in percentage points</i>				
Q1 17	+5.4	+0.9	+1.6	+1.6	+0.6	+0.1	-0.1	+0.1
Q2 17	+2.8	+0.4	+1.3	+1.3	+0.4	0.0	+0.2	0.0
Q3 17	+0.4	+0.6	+1.3	+0.7	+0.4	+0.3	0.0	0.0
Q4 17	-2.2	+1.6	+1.6	+0.7	+0.4	+0.5	0.0	0.0
Q1 18	+0.1	+1.8	+1.1	+0.9	+0.5	+0.2	+0.2	-0.1
Q2 18	+4.1	+0.9	+1.1	+1.1	+0.6	+0.1	-0.1	0.0
2014	-7.0	+0.6	+3.0	+2.6	+0.3	+0.3	0.0	+0.1
2015	-0.8	+6.2	+3.5	+3.2	+0.8	+0.3	0.0	0.0
2016	+18.9	+6.8	+3.0	+3.7	+2.1	-0.2	+0.1	+0.1
2017	+11.1	+2.6	+4.6	+4.5	+2.0	+0.2	+0.3	+0.2

Data revised since July 30, 2018*Percentage points*

Q3 17	-1.3	-2.5	0.1	0.0	-0.1	0.1	-0.1	0.0
Q4 17	-3.5	-0.8	0.1	0.0	-0.1	0.1	0.0	0.0
Q1 18	-1.0	-0.4	0.1	0.1	0.0	0.0	0.0	-0.1
Q2 18	3.6	-1.2	0.2	0.2	0.0	0.0	-0.1	0.0
2014	-0.2	0.5	-0.1	-0.2	0.0	0.1	-0.2	-0.1
2015	-0.3	4.1	0.5	0.2	0.1	0.2	-0.2	0.0
2016	4.9	-0.1	0.6	0.1	0.0	0.3	0.0	0.2
2017	4.6	-7.0	-0.7	-0.6	-0.1	-0.1	-0.1	-0.1

Source: WIFO, OeNB calculations.

against this higher baseline, the growth momentum weakened in 2017. Real GDP growth for 2016 was revised upward by 0.5 percentage points, to 2.0%, whereas the figure for 2017 was revised downward by 0.3 percentage points, to 2.7% (or 2.6% in non-seasonally adjusted terms). This revision primarily results from changes in estimates of export and investment activity, which now records stronger growth at the beginning of the current economic cycle in 2016 but weaker growth in 2017. The pattern is even more pronounced for investment in plant and equipment, where there have also been significant internal shifts between transport equipment and machinery. In contrast, the figures for residential construction investment have been raised substantially for both years and now reflect stronger growth than those for the wider economy in both 2016 and 2017.

2 Strong export growth despite challenging environment

Austria's exporters faced increasingly challenging conditions in the first half of 2018. Trade policy conflicts and economic turmoil in emerging economies weighed on the global economy. In Europe, concerns about Italy's future economic and budget policy strategies and the further course of the Brexit negotiations have been mounting. At the same time, the euro area posted disappointing growth figures at the beginning of the year, not least in key export markets such as Germany, France and Italy.

Against this backdrop, Austria has posted strong export growth so far this year, with nominal goods exports up by 5.8% in the first six months of 2018. The breakdown of Austrian exports by region shows that this is a broad-based trend: Austria's businesses have been able to sell more goods to all key export markets with the exception of France and Russia in the year to date. Trade with Central, Eastern and Southeastern Europe (CESEE) performed particularly well. Austrian goods

exports to CESEE expanded by 10% in the first half of the year, twice as much as other exports, which went up by 5%. Although only 18% of goods exports went to the CESEE-8² countries, they accounted for 28% of Austria's entire export growth. Exports to Germany saw slightly above-average growth of 6.3%.

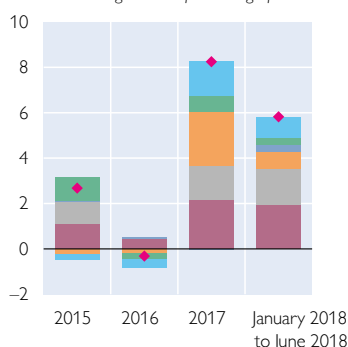
It is not possible to draw firm conclusions about future export trends from the leading indicators currently available. The most recent figures of the OeNB's Export Indicator, which is based on truck mileage data, suggest that export growth over the summer was roughly in line with the average for the first half of 2018. Indications about the further course of the year are contradictory, which is likely to reflect uncertainties in the external environment.

Chart 1

Growth composition of goods exports and imports by regions

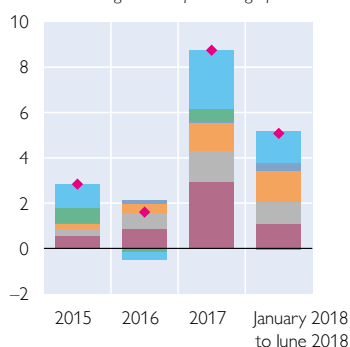
Exports

Annual change in % (in nominal terms); contribution to growth in percentage points



Imports

Annual change in % (in nominal terms); contribution to growth in percentage points



Rest of the world
EU excluding Germany and CESEE-8
CESEE-8
Total

U.S.A.
Euro area excluding Germany and Austria
Germany

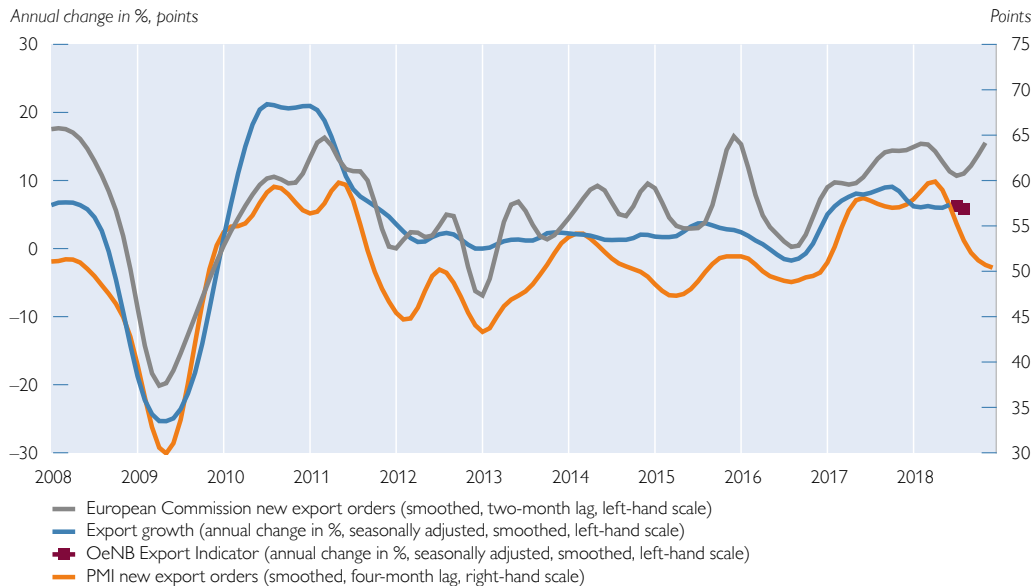
Source: Statistics Austria.

Note: CESEE-8: Bulgaria, Czech Republic, Croatia, Hungary, Poland, Romania, Slovakia, Slovenia.

² Bulgaria, Czech Republic, Croatia, Hungary, Poland, Romania, Slovakia, Slovenia.

Chart 2

OeNB Export Indicator and leading indicators for foreign trade



Source: Statistics Austria, ASFINAG, Bank Austria, OeNB.

While purchasing managers' recent assessment of export order trends was relatively cautious, the data collected by the European Commission on new export orders suggest that export trends are following a steady course or even accelerating slightly. The latent trade conflicts and the ongoing Brexit negotiations give rise to exceptionally high forecast uncertainty.

Growth of goods imports stood at 5.1% in the first six months of the year and thus lagged behind growth of goods exports, unlike in 2017. The weaker growth of goods imports is partly attributable to the fact that imports of vehicles have so far remained roughly at last year's level. This also explains the low growth rate for imports from Germany.

Exports in the services sector expanded by 5.8% over the first six months of 2018, roughly on a par with the goods sector. Business services recorded above-average growth, while transport services grew at a slightly below-average rate. Once again, tourism was the main driver of growth in this sector. The number of overnight stays by visitors from abroad rose by 4.7% in the first seven months of 2018, reaching an all-time high of 70.7 million. Visitors from Germany – by far the most significant country of origin, accounting for approximately 50% of all overnight stays – played a particularly significant part in this good result, with a rise of 6.6%. Overall, tourism services exports were up by 7.1%, which contributed to above-average inflation in this sector.

Thanks to the positive trends in both the goods and the services sector, the current account balance continued to improve. The current account surplus rose by EUR 1.8 billion year on year in the first half of 2018, reaching EUR 6.3 billion, or 3.3% of GDP. The outlook for the second half of the year is favorable. As a result, we expect the current account surplus for 2018 as a whole to exceed last year's figure of 2.0% of GDP.

3 Above-average growth of investment and industrial production

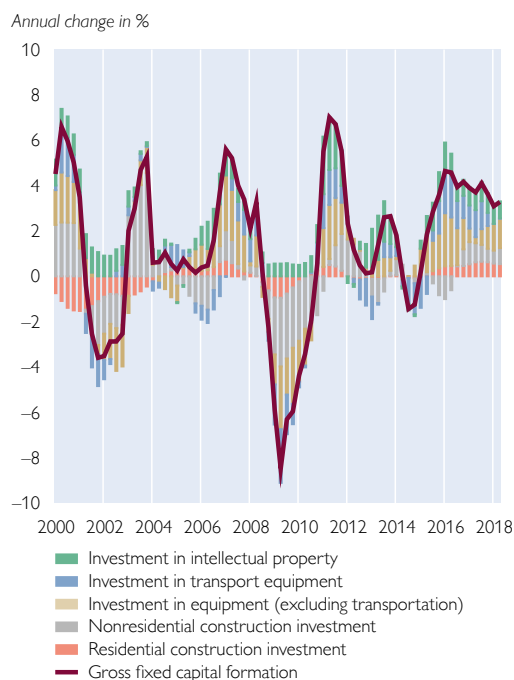
Domestic demand is currently lively and represents a key driver of economic activity, alongside export activity. Consumption and investment are contributing substantially to economic growth in Austria. As of the second quarter of 2018, the current investment cycle is among the longest and strongest of the past two decades, and there is still no end in sight. Businesses' assessment of their own capacity utilization in the third quarter stands at almost 89%, thus remaining above the long-term average and only very slightly below all-time record levels. This suggests a need for additional investment in plant and equipment in the second half of the year. Financing conditions are still favorable, which continues to have a positive impact. However, heightened external risks could curb domestic businesses' propensity to invest. Residential construction investment has returned to an even growth path in recent quarters. National accounts data have posted year-on-year rises of up to more than 3% for six quarters in a row, including the most recent upward revision. The outlook for the next six months remains favorable, as sentiment indicators and hard facts (such as order books and building permits) are both on an upward trajectory. Overall, the investment cycle is expected to level off only gradually.

Robust exports and investment activity are also the drivers of Austrian industry. Measured in terms of gross value added in the national accounts, industrial output has been rising by more than 6% year on year since mid-2017, twice as strongly as Austria's economy as a whole. This is a typical feature of boom periods. Although leading indicators for industry suggest that industrial output has already peaked, growth is still expected to be above average in the second half of the year.

Chart 3

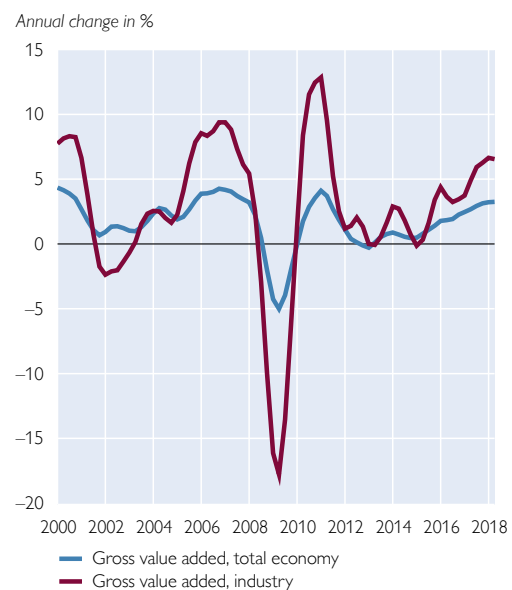
Investment and industry

Investment cycle leveling off only gradually



Source: WIFO.

Robust industrial activity



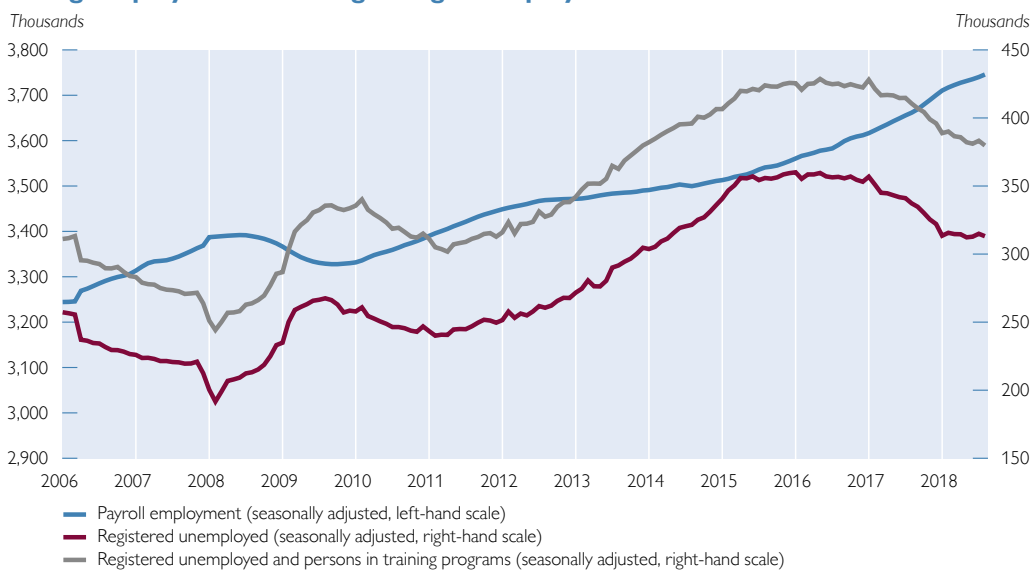
4 Strong rise in employment, but no change in unemployment level in 2018

Households are expected to have scope for additional private consumption in the coming months. Wages settlements are higher than in 2017, pushing up real wages in Austria despite the commodity price-related rise in inflation. Moreover, labor market trends have been very favorable. The number of individuals in payroll employment continued to record a very strong year-on-year rise of nearly 2½% over the summer months. Unlike in the immediate post-crisis years, full-time positions currently account for the entirety of employment growth, while the number of part-time jobs is declining. The rise in employment is especially high in sectors with above-average remuneration, including industry and the information and communication sectors. The sharp increase in the number of registered vacancies indicates that employment growth will remain robust over the next few months. As a result, households' disposable incomes can be expected to rise significantly.

Austria's seasonally adjusted unemployment rate (national definition) stood at 7.7% in August, 0.8 percentage points below the August 2017 level. The unemployment rate according to the Eurostat definition was 4.9% in July (down 0.5 percentage points year on year). However, trends in seasonally adjusted employment and unemployment figures over the course of the year indicate that, in keeping with trends in the wider economy, the conjunctural peak on the labor market is already behind us. The seasonally adjusted number of registered unemployed persons has no longer been declining in the year to date, and employment growth has slowed somewhat. The falling number of individuals in training programs is one of the reasons why the high employment momentum has not been accompanied by a further decline in unemployment (see chart 5).

Chart 4

Rising employment and stagnating unemployment levels in the first half of 2018



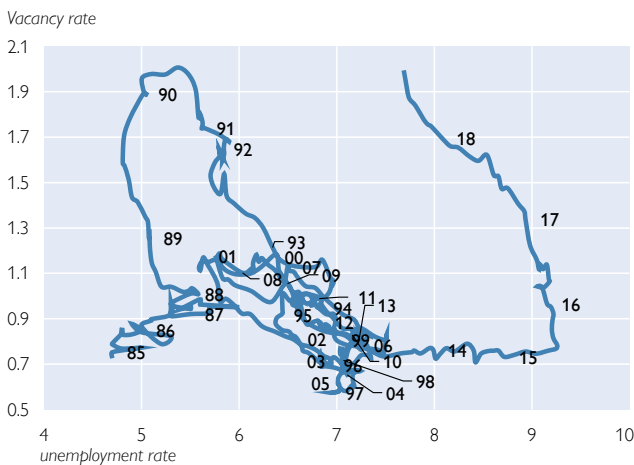
Source: AMS, Main Association of Austrian Social Security Institutions, authors' calculations.

The fact that unemployment remains relatively high despite strong employment growth raises questions to do with matching efficiency and labor shortages on the Austrian labor market. Labor shortage estimates are currently considerably higher than they were in the first half of 2008, toward the end of the last economic boom. In the third quarter of 2018, 18% of industrial companies cited labor shortages as a limiting production factor. Ten years ago, less than 10% identified this as a problem. The number of “shortage occupations” – i.e. those in which the number of job seekers per job vacancy is less than or equal to 1.5 – rose to 86 in August 2018. This figure never exceeded 80 during the previous economic boom. This is especially remarkable given that the unemployment rate is significantly higher today than it was in 2008. Moreover, there are signs of declining matching efficiency

Chart 5

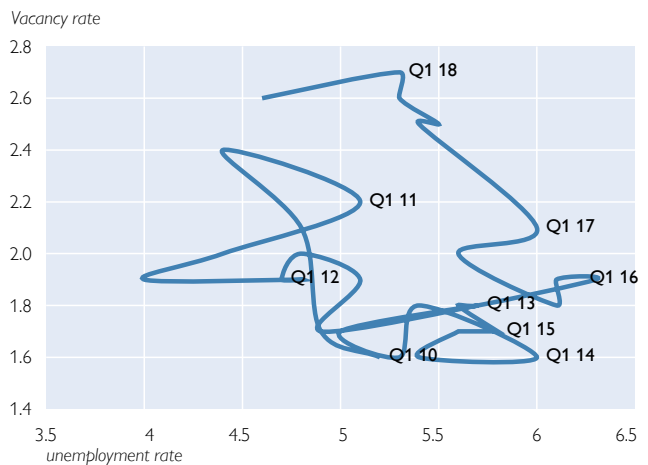
Declining matching efficiency and rising labor shortage

Beveridge curve based on AMS data (January 1985 to July 2018)



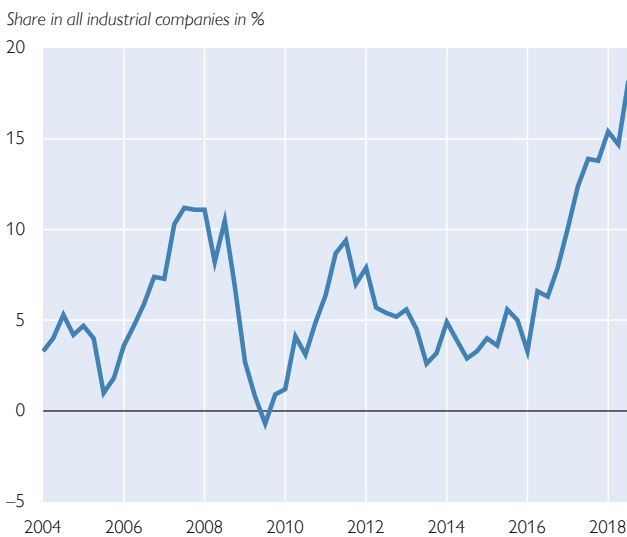
Source: Eurostat.

Beveridge curve based on Eurostat data (first quarter of 2010 to second quarter of 2018)



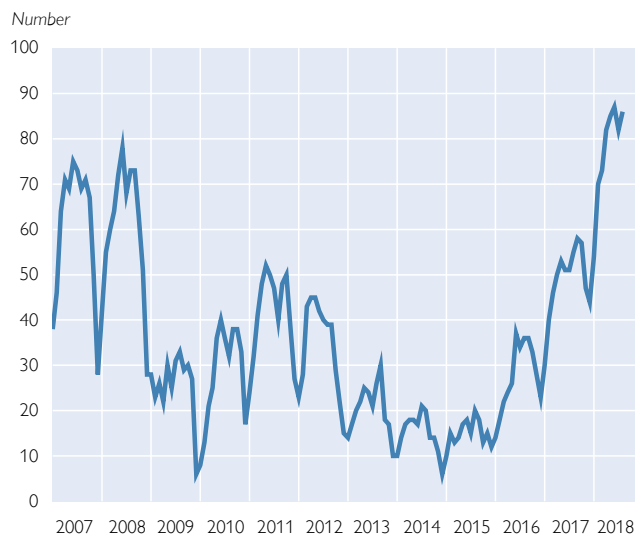
Source: AMS.

Labor shortages as a limiting production factor



Source: Eurostat.

Shortage occupations (NACE four-digit codes)



Source: AMS.

on the Austrian labor market. The Beveridge curve, which charts the negative correlation between the unemployment rate and the vacancy rate, has shifted outward, signaling a deterioration of the job matching process. Although this shift is overstated due to a change in the way vacancies are recorded in AMS (Public Employment Service Austria) data, it is also reflected in Eurostat data, where no such methodological changes have occurred. Improvements in matching can be achieved by means of investment in the education system (in the long term) and training programs (in the short and medium term).

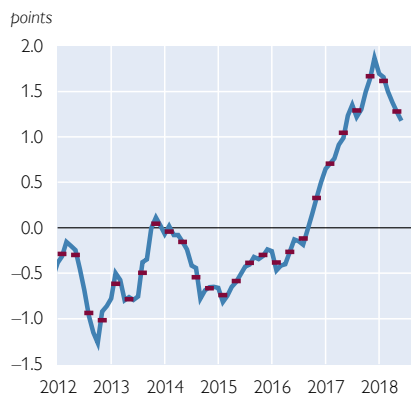
5 Economic indicators stabilizing at a high level

Following record highs at the turn of the year, sentiment indicators and economic indicators for Austria have declined over the course of 2018. The most pronounced correction was recorded by the Purchasing Managers' Index (PMI), which fell from 64.3 points in December 2017 to 56.4 points in August 2018. All index

Chart 6

Confidence indicators for the Austrian economy

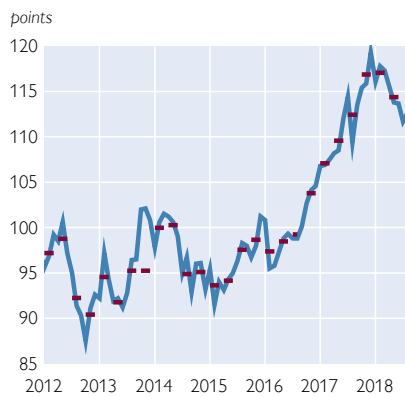
Mean value across the five confidence indicators



Source: Authors' calculations.

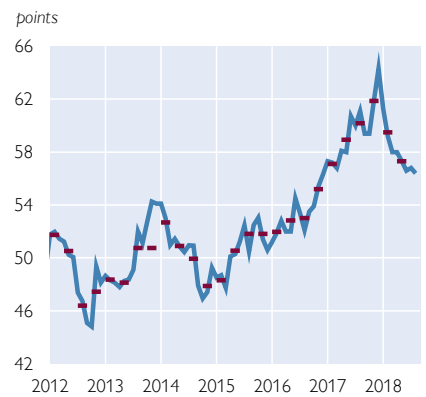
Note: Standardized mean of ESI, PMI, WIFO leading indicator, WIFO economic climate indicator and Bank Austria's economic indicator.

European Sentiment Indicator (ESI), European Commission



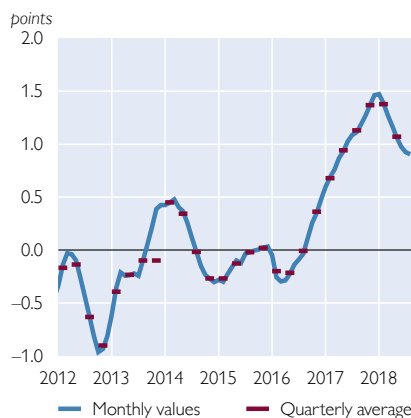
Source: European Commission.

Purchasing Managers' Index (PMI)



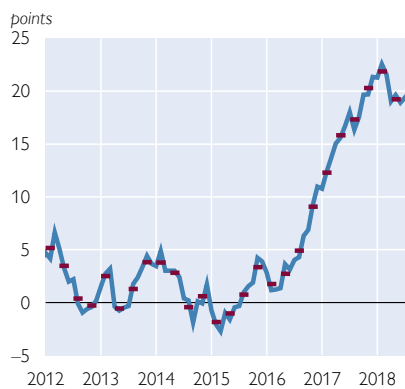
Source: Bank Austria.

WIFO leading indicator



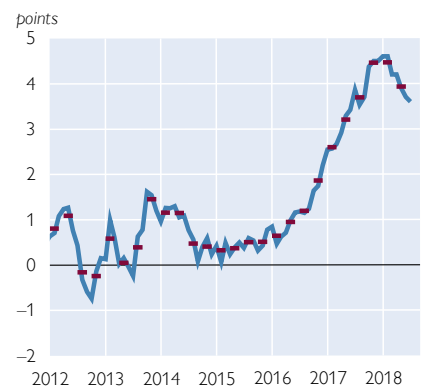
Source: WIFO.

WIFO economic climate indicator



Source: WIFO.

Bank Austria economic indicator



Source: Bank Austria.

subcomponents contributed to this decline, with the assessment of new export orders exhibiting the strongest downward trend. This reflects heightened external uncertainties. The Economic Sentiment Indicator (ESI) charted a similar, albeit less pronounced, course: it fell from 119.3 points in December 2017 to 112.7 points in August 2018. Nevertheless, the PMI and the ESI remain considerably above their long-term averages.

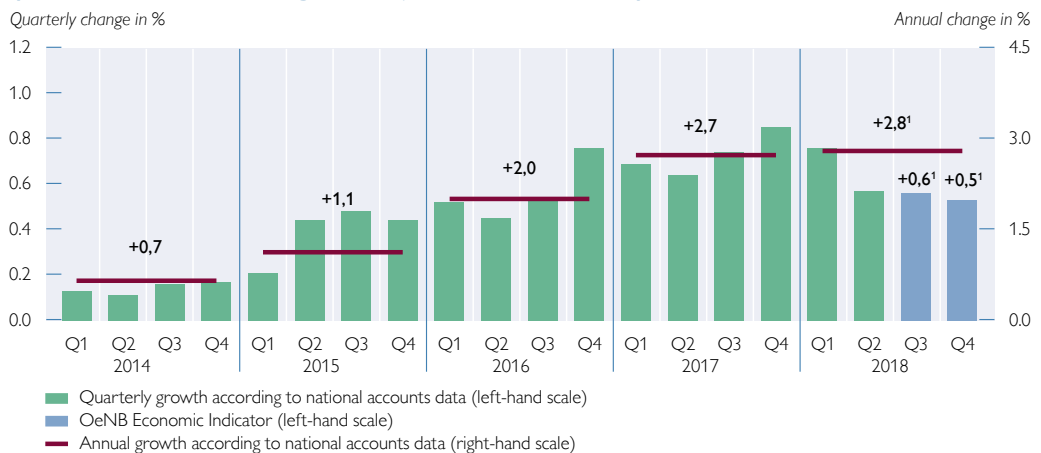
The deterioration of sentiment indicators slowed significantly in mid-2018. In fact, some indicators, including WIFO's economic climate indicator, have recently even recorded slight improvements. Overall, indicators appear to have plateaued at a relatively high level. Lower risks in the external environment have played a role here. Partly because of the tentative deal reached in the trade conflict between the U.S.A. and the EU, the ifo index for Germany has once again improved, and domestic exporters have become somewhat more optimistic about new order trends. Overall, the available leading indicators suggest that the Austrian economy will grow at a slightly above-average pace over the next few months.

6 Austria's economy set to grow by close to 3% in 2018

Based on the available economic indicators, it is likely that the current economic cycle peaked at the turn of 2017/2018. The first half of 2018 saw a gradual return to average growth. According to the most recent results of the OeNB's Economic Indicator of September 2018, this trend is set to continue in the second half of the year. Based on its quarterly forecasting exercise, the OeNB expects real GDP in Austria to rise by 0.6% in the third quarter and by 0.5% in the fourth quarter of 2018 (quarter on quarter; adjusted for seasonal and working-day effects), and thus to remain above the long-term average growth rate of 0.4% until year-end. Thanks to particularly strong growth early in the year, the predicted growth rate for 2018 as a whole is 2.8%, slightly higher than in 2017. External economic uncertainties such as the further course of international trade conflicts and the Brexit negotiations represent a downside risk to the present forecast.

Chart 7

Outlook for Austrian real GDP for the third and fourth quarters of 2018 (seasonally and working-day adjusted trend series)



Source: OeNB Economic Indicator, interim update of September 2018; WIFO.

¹ Forecast.

7 Austria's inflation rate at 2.3% since June

Austria's HICP inflation rate remained at 2.3% over the last three reporting months. It stood at 1.9% at the beginning of 2018 and then gradually declined to 2.3%, where it remained from June until August 2018. The decline in food price inflation, which was especially pronounced in August (the most recent reporting month), was balanced out by a simultaneous rise in services inflation, resulting in a practically unchanged headline inflation rate. The energy component of HICP inflation, on the other hand, has maintained a relatively steady high level for several months. Core inflation (excluding energy and food) has fluctuated around the 2% mark since the beginning of the year and stood at 1.8% in August 2018.

Overall, Austria's inflation rate in August continued to be somewhat higher than those of the euro area and Germany. The recent fall in inflation in Germany and the euro area meant that Austria's inflation gap vis-à-vis Germany and the euro area widened to 0.4 and 0.3 percentage points, respectively. However, these figures are still significantly lower than in 2017 and early 2018, when Austria's inflation rate doggedly remained more than half a percentage point above that of the euro area.

8 Inflation outlook: slight fall to 2.0% anticipated by 2020

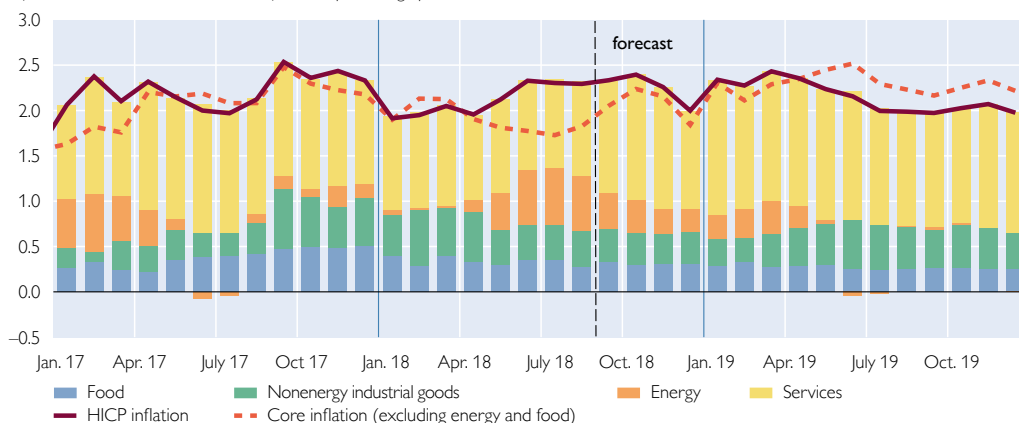
According to the OeNB's September 2018 inflation forecast, HICP inflation will largely follow a steady path until 2019. Thanks to the favorable economic situation and the anticipated surge in unit labor costs, inflation is expected to persist at 2.2% in 2018 and 2019.

The rise of nonenergy industrial goods prices is predicted to remain above average in 2018 and 2019 due to favorable trends in consumer demand and the acceleration of unit labor cost growth. Services inflation is likely to climb significantly over the forecast horizon, primarily as a result of the anticipated rise in labor costs (see chart 8). The HICP inflation rate is predicted to drop to 2.0% only in 2020, on the back of a slight dip in crude oil inflation, a fall in food inflation, and the gradual end of the current economic cycle. Favorable trends in

Chart 8

Contributions to Austrian HICP and core inflation

Inflation rates in %; contributions to inflation in percentage points



Source: Statistics Austria, OeNB.

Forecast: September 2018 to December 2019.

Table 2

Assumptions of the OeNB inflation outlook of September 2018

	Assumptions				Revisions since June 2018		
	2017	2018	2019	2020	2018	2019	2020
					<i>change in %</i>		
Energy and exchange rates							
Crude oil price (EUR/barrel)	48.2	60.7	62.6	60.3	-2.3	0.9	4.0
USD/EUR exchange rate	1.1	1.2	1.1	1.1	-1.7	-3.4	-3.4
Nonenergy commodity prices							
EU producer prices, food	107.2	106.5	109.3	109.7	-0.7	0.6	1.3
World market prices, food	133.5	130.2	133.7	140.9	-5.6	-8.3	-5.0
World market prices, metallic raw materials	122.9	125.3	118.6	123.2	-8.4	-14.2	-14.5
Interest rates							
					<i>in %</i>		
Three-month interest rate	-0.3	-0.3	-0.2	0.0	-0.0	-0.1	-0.2
Ten-year government bond yield	0.6	0.7	0.8	1.0	-0.1	-0.2	-0.3
					<i>change in percentage points</i>		

Source: Eurosystem.

Note: June 2018 (cutoff date for data: May 23, 2018); September 2018 (cutoff date for data: August 23, 2018).

domestic economic factors, including domestic demand and unit labor costs, are expected to cause core inflation (excluding energy and food) to rise to 2.3% by 2019 (see chart 8).

The predicted annual inflation rate for 2018 has remained unchanged since the last forecast, published in June 2018. However, the forecast HICP inflation rates for 2019 and 2020 have been revised upward by 0.2 and 0.1 percentage points, respectively. These upward revisions are based on anticipated rises in producer prices for food and in crude oil prices (see table 2). Services inflation also saw a slight upward revision as unit labor costs increased somewhat more strongly than expected in the last forecast.