Global Economy Continues to Recover in a Fragile Environment

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U.S. economic growth has been gaining momentum, with the annualized growth rate of real GDP reaching 3.1% in the fourth quarter of 2010. Factoring in this good performance, the IMF has revised upward its economic outlook for 2011 by 0.7 percentage points to 3.0%. At the same time, the labor market has been slow to improve, and housing markets are still adjusting; hence the contribution of labor and housing to economic growth has been rather moderate.

Furthermore, the devastating earthquake in Japan hit the economy at a time when the recovery of economic activity was still fragile. Judging from previous experience with earthquakes, international organizations expect the setback in Japanese growth to be temporary, however. The growth effect might swing back into positive territory as reconstruction efforts accelerate in the second half of 2011. Given the limited openness of the Japanese economy, the repercussions on the world economy are likely to remain subdued. The Bank of Japan (BoJ) moved to support the economy by providing ample liquidity and expanding its purchases of securities from the private sector. The G-7 economies joined forces to intervene against the strong appreciation of the Japanese yen in the days following the earthquake.

The year 2010 saw China emerge as the second-largest economy worldwide behind the United States, measured at current GDP prices. The IMF expects the Chinese economy to grow by 9.6% in 2011. The Chinese central bank responded by raising minimum reserve requirements a few times and by increasing its key monetary policy rates three times to keep the economy from overshooting. The renminbi has appreciated by close to 4% since China returned to a more flexible exchange rate arrangement in 2010.

Euro area real GDP grew by just 0.3% quarterly in the fourth quarter of 2010. Euro area-wide unemployment reached 9.9% in January 2011, just 0.2 percentage points short of the 12-year peak recorded in October 2010. ECB staff projections for GDP growth in 2011 are within a range of 1.3% and 2.1%. Reflecting commodity price increases, the annual growth rate of HICP inflation has been trending upward since mid-2010, standing at 2.4% in February 2011. While the economic recovery implied a reversal of public debt dynamics in most euro area countries, the high debt levels of some euro area countries continued to cause turbulence. Exacerbated by the downgrading of ratings for Greece Portugal and Spain, the spreads payable on sovereign bonds issued by peripheral European countries remained elevated. In the spirit of European solidarity, a permanent crisis mechanism – the European Stability Mechanism – has been established in the euro area, which will become operational in mid-2013.

The gradual economic recovery in Central, Eastern and Southeastern European (CESEE) EU Member States continued in the second half of 2010. The business cycles of the countries in the area reconverged somewhat, and domestic demand gained momentum as a driver of growth. These developments were underpinned by a stabilization of current account balances, following a significant recovery of those positions during the recent years of subdued economic growth. Rising food prices and tax increases in a number of countries stoked inflation in recent months, prompting a number of central banks to raise their key monetary policy rates, thereby initiating a reversal from the broadly accommodative stance adopted in the period of crisis.

The Austrian economy, finally, is in very good shape notwithstanding a number of risk factors. The key engine of growth has been the manufacturing industry, which has begun to invest again given strong export growth, whereas the construction sector continues to contract. The OeNB's short-term economic indicator results point to above-average growth in the first half of 2011. These developments will, in turn, continue to improve labor market conditions, which are already favorable. The surge in energy and commodity prices has caused inflation to rise strongly lately; the rate hit 3.1% in February 2011.

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1 Robust World Economic Growth; Effects of Earthquake in Japan Difficult to Estimate, but Geographically Limited

1.1 U.S. Economic Revival Accelerates

U.S. economic growth has been gaining momentum. The annualized growth rate of real GDP reached 3.1% in the fourth quarter of 2010, largely bolstered by household consumption, as in previous quarters. At the same time, the contribution of net exports to growth turned positive again in 2010, reflecting a sharp decline in imports, which had been rebounding strongly. In the first half of 2010, the United States had been benefiting broadly from Chinese export subsidies, which expired at the end of July 2010. A large share of these imports from China was used to restock, thus driving large-scale inventory accumulation. In other words, the decline in U.S. imports and the destocking dynamics in the fourth quarter of 2010 constitute market adjustments.

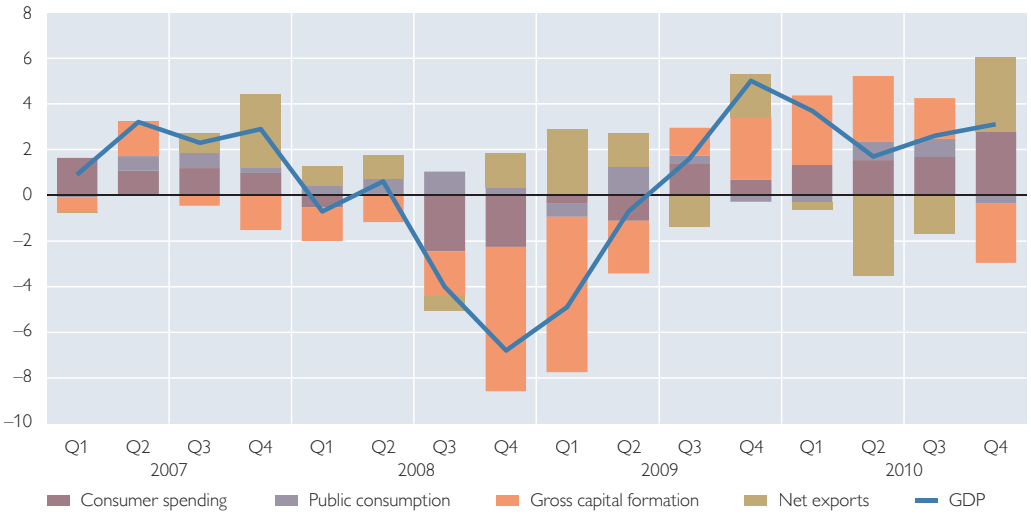
The by now relatively broad-based U.S. growth patterns are likely to be robust. The major leading indicators – such as the Purchasing Managers' Index, retail sales or the Conference Board Consumer Confidence Index – signal rising growth dynamics. The IMF revised upward its growth outlook for 2011 by 0.7 percentage points to 3.0% and expects economic activity to expand by 2.7% in 2012. The Federal Reserve System (Fed) projects growth for 2011 to be within a range of 3.4% to 3.9%, coupled with moderate inflation rates ranging from 1.3% to 1.7%.

The signals coming from the U.S. labor market have been mixed lately. The unemployment rate dropped further to 8.9% in February 2011, which means that it has retreated 1.2% from the peak value registered as a result of the recession but that it remains 5 percentage points above the levels observed in the ten years before the economic and financial crisis emerged. At the same time, the number of new jobs has been limited lately. Adjustments in

Chart 1

U.S.A.: Real GDP Growth

Contributions to GDP growth (quarter-on-quarter, seasonally adjusted, annual change in percentage points or in %)



Source: Bureau of Economic Analysis.

the housing markets are ongoing, as reflected by the continued high number of foreclosures and declining house prices. Thus, housing spending is not contributing to economic growth in the United States for the time being.

The inflation rate has been going up visibly lately; in February 2011, it rose by ½ percentage point to 2.1%. This surge primarily reflects developments in global market prices for crude oil and other commodities. The composite index for commodity prices was close to the peak observed in mid-2008. Apart from the global economic revival, the rise in energy prices reflects the current political turbulence in Northern Africa.

The steep upward trend in food commodity prices is attributable to the adverse weather conditions prevailing in 2010 and might, therefore, be reversed soon. Should inflation continue to rise, a turnaround in the Federal Reserve's monetary policy stance might be in the offing. At its meeting on January 25/26, 2011, the last meeting before the editorial deadline for this report, the Fed left the federal funds rate unchanged within a range of 0% to 0.25% and was intending to keep the rate at this level for an extended period. Furthermore, the Fed confirmed that it continued to stand ready to buy Treasury bonds worth USD 600 billion until mid-2011.

1.2 Devastating Earthquake Hits Japan on Top of Already Fragile Economy

An earthquake measuring 9.0 on the Richter scale shook northeast Japan on March 11, 2011, triggering a tsunami and causing severe damage to several nuclear power plants and hitting an economy that was still at a very fragile stage of the business cycle. Government consumption incentives such as premiums for car and flat-screen TV purchases had caused substantial front-loading effects in mid-2010 but by the fourth quarter, when the incentives were phased out, GDP growth had returned to negative territory quarter-on-quarter. In January 2011, the IMF forecast growth for 2011 to be modest at 1.6%.

While only about 6% to 7% of the Japanese population live in the areas afflicted most by the earthquake and the tsunami, and these areas only account for the same percentage of output, the damage to the economy is considered to be massive. Several weeks of recurrent temporary power outages in a larger region that accounts for some 40% of Japanese output contributes to this damage. It will take some time to fully assess the impact of the accidents at the nuclear power plants. However, the negative growth effects stemming from output losses will gradually be offset by the positive effects of reconstruction. Provided that experience with tremors in the past is applicable to this incident, the net economic effect may well be positive after a few months.

The impact on the global economy may well be limited, however, since Japan is a fairly closed economy with a share of no more than 4.5% in world trade. China and the U.S.A. are Japan's main trading partners; the euro area follows with a substantially smaller share. But noticeable effects for the world economy could result from its reliance on important niche products from leading suppliers of automotive and electronic parts in the affected region. These suppliers' failure could disrupt global production chains.

To stabilize financial markets, which became edgy when the earthquake hit, the Bank of Japan provided large-scale liquidity in the days following the tremor and announced that it

would double its securities purchase program from JPY 5,000 billion to JPY 10,000 billion (EUR 87 billion). With key interest rates near zero (ranging from 0.0% to 0.1%) and government debt at over 200% of GDP, Japan's economic policymakers have virtually no scope to stimulate the economy.

Whereas Japanese stock prices plummeted in the days following the earthquake, the Japanese yen appreciated, reaching its highest value against the U.S. dollar since World War II on March 16, 2011. Apparently, insurance companies and investors withdrew funds from abroad to finance reconstruction. To curb the rise of the Japanese yen and the rapid deterioration of Japanese competitiveness in its wake, the G-7 industrial nations pledged a concerted money market intervention, thus bringing down the value of the yen against the world's major currencies and stabilizing it at a level close to that of the months preceding the earthquake.

1.3 China Puts a Lid on Inflation

In 2010, China for the first time took second place in terms of nominal GDP behind the U.S.A. China displaced Japan, which had been the runner-up to U.S. output for decades after stepping into Germany's shoes in 1967. In the fourth quarter of 2010, China's economy grew by 9.8% (annualized). The IMF forecasts growth to continue in the same vein in 2011 and 2012. The impact of the earthquake in Japan on the country's main trading partners is difficult to assess. In the short run, China may benefit by taking up the slack caused by the shortfall in Japanese production. In the medium term, though, disruptions of the production chain may also have negative effects.

Dynamic economic growth in China does present some problems. For example, inflation was running at 4.9% in the first two months of 2011. Fast-paced inflation reflects a rapid rise in politically particularly sensitive food prices as well as energy and other commodity prices. However, core inflation is also elevated.

China has already raised its minimum reserve rate several times and boosted key interest rates three times, most recently by 25 basis points in February 2011, to counteract an overheating of the economy. The speed of the appreciation of the Chinese renminbi against the U.S. dollar has also gained momentum. Since the fixed peg was loosened in June 2010, the value of the renminbi has risen by nearly 4%.

2 Euro Area Economy Remains on a Growth Path

2.1 Exports and Private Consumption Are Mainstay of Growth in the Fourth Quarter of 2010

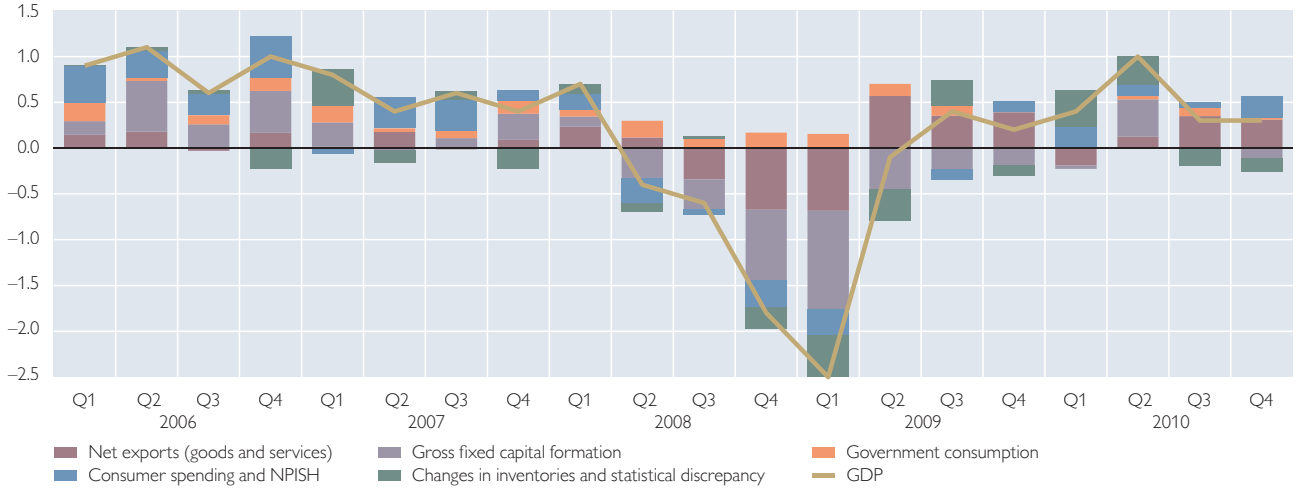
After experiencing robust growth in the first half of 2010, the euro area saw economic momentum weakening somewhat in the second half of the year. GDP growth came to just 0.3% quarter-on-quarter in the fourth quarter of 2010. For 2010 as a whole, economic growth ran to 1.7%. Net exports and consumer spending made positive contributions to growth in the fourth quarter of 2010, with consumer spending largely making up for the losses it had suffered during the recession. Inventory changes and gross fixed capital formation provided slightly negative contributions to growth in the second half of 2010.

The business cycle pattern of the euro area at the end of 2010 was mainly influenced by the economic developments in Germany. The German economy expanded by only 0.4% in the fourth quarter of 2010 after having posted above-average growth in the

Chart 2

Components of Real GDP Growth in the Euro Area

Contributions to GDP growth (quarter-on-quarter, seasonally adjusted) in percentage points, GDP growth in %



Source: Eurostat.

second and third quarters. Growth rates were moderate in France, Spain and Italy as well. Greece and Portugal posted negative growth rates, as private consumption contracted sharply in the wake of substantial consolidation measures.

2.2 GDP Growth Expected to Be Stable in 2011 and 2012

Economic growth is expected to rise to 0.5% in the first quarter of 2011. The sustained global recovery boosts the export sector, and high business confidence as well as an expansive monetary policy support investment. Capacity utilization is also increasing at a constant rate; in the first quarter of 2011, it was only marginally below its long-term average. Confidence indicators signal a positive attitude as well. The Purchasing Managers' Index for industry, for example, which generally is a reliable leading indicator of quarterly GDP performance, posted a ten-year high in February 2011.

The improved outlook for the world economy and for domestic demand prompted upward revisions of key forecasts. ECB experts anticipate GDP growth to range between 1.3% and 2.1% in the euro area in 2011. This corresponds well with the most recent estimates of the European Commission (+1.6%). For 2012, ECB experts expect a growth rate of between 0.8% and 2.8%. The worldwide recovery, expansionary monetary policy and ongoing financial system stabilization measures will continue to support the euro area economy. The upswing will increasingly become self-supporting on the back of the gradual improvement of consumer spending. However, indispensable budget consolidation will act as a damper on the upturn.

2.3 Marginal Decline in Unemployment on the Horizon

Seasonally adjusted unemployment fell slightly to 9.9% in the euro area in January 2011, after the unemployment rate had stabilized at 10.0% in the preceding months. According to first estimates by Eurostat, employment figures also augmented, and employment growth accelerated. The European Commission does not expect the un-

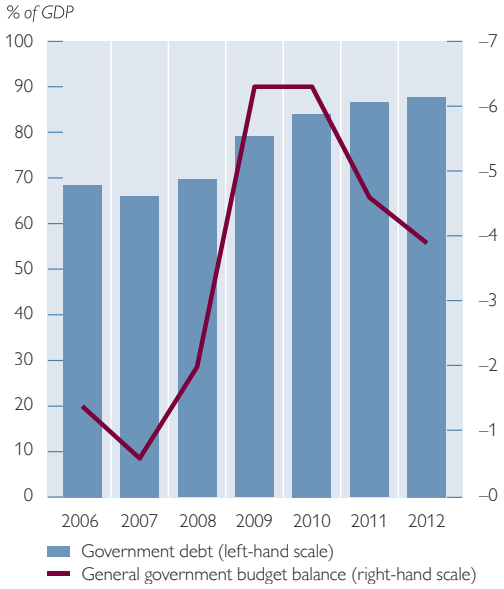
employment rate to decline noticeably until 2012 (to 9.6%).

2.4 Trend Reversal of Budget Developments Initiated, Debt Crisis Continues in Some Euro Area Countries

In 2010, the euro area deficit ratio remained unchanged against the year before at 6.3% of GDP. But a trend reversal is in the offing in most euro area countries, given the continued economic recovery and resolute budget consolidation measures. The average euro area deficit ratio is anticipated to shrink to 4.6% in 2011. Nevertheless, the individual euro area countries' fiscal positions are very heterogeneous and depend significantly on the extent of the macroeconomic imbalances in the respective countries before the financial crisis hit. Ireland, for example, had tipped into a deep recession following the bursting of a real estate bubble in 2008 that severely hit the country's oversized banking sector. Government support measures, in turn, caused public debt to explode. Ireland's public debt burgeoned to 97% of GDP by the end of 2010, and in 2011, the deficit ratio will probably run to 10.3% of GDP. Countries such as Germany, Finland and Luxembourg, by contrast, will be able to slash their deficits to below 3% of GDP as early as in 2011.

Chart 3

Fiscal Developments in the Euro Area



Source: European Commission, forecasts for 2010 to 2012.

After Greece had been granted bilateral bridge loans in May 2010, other countries with budget problems were also given the option of extending the time they needed to put their finances in order. Therefore, Ireland accepted a bailout package in November 2010 under a financial safety net that the European Union and the IMF had conceived in fall 2010 to run for three years. The emergency funding of EUR 85 billion for Ireland will be financed jointly by the IMF, the newly founded European Financial Stability Facility (EFSF) and the newly founded European Financial Stabilisation Mechanism (EFSM).

In addition to Ireland and Greece, Portugal also moved into the focus of attention at the end of 2010 and beginning of 2011. While Portugal was one of the few euro area countries that had not experienced a banking crisis, it had come under pressure, much like Greece had, because of its high government debt and weak competitive position. Public attention was also focused on Spain, whose government debt at 65% of GDP continues to be just above the level prescribed by the Maastricht Treaty but whose banking sector has to cope with the effects of a real estate bubble.

Neither the first successful programs to consolidate government budgets nor the rapid implementation of newly established funding facilities were able to put financial markets at ease for any length of time. Exacer-

bated by the downgrading of ratings for Greece, Portugal and Spain, the risk premia on sovereign bonds issued by peripheral European countries remained high. To ensure sustained capacity for action, the European Council decided on March 24 and 25, 2011, to establish a permanent European Stability Mechanism (ESM) with subscribed capital of EUR 700 billion, which will take effect from 2013, and the euro area countries along with six other EU Member States adopted a competitiveness pact called the "Pact for the Euro," under which the participating countries undertake to implement concrete national commitments every year to foster competitiveness, promote employment, contribute further to the sustainability of public finances and reinforce financial stability.

2.5 Higher Commodity Prices Push Up Inflation

The rate of HICP inflation in the euro area rose steadily from 1.6% (mid-2010) to 2.4% (February 2011). Around the turn of the year, higher prices for unprocessed foods and energy fueled inflation in particular. Core inflation (HICP excluding energy and unprocessed foods) came to just 1.1% in February 2011. As the rise in food prices had its roots in unfavorable weather conditions in 2010, a change in this trend is to be expected soon. Thus, ECB staff projections show inflation remaining at 2.0% to 2.6% in 2011 and to sink to a rate between 1.0% and 2.4% in 2012. The uncertainty surrounding the development of oil and energy prices represents a significant upside risk to this forecast. More recently, uncertainties linked to the political upheavals in northern Africa have once again caused the oil price to rise markedly. It is also unclear whether the impact of the earthquake in Japan will prompt a fundamental change in energy policy and will thus lead to a negative supply shock in the medium term. Medium- to long-term inflation expectations remain anchored at a level that is in line with the Eurosystem's objective of keeping inflation below but close to 2% in the medium term.

2.6 Phase of Rising Interest Rates Begins

Since the press conference following the first ECB Governing Council meeting of 2011, at which the prospect of an increase in interest rates was held out, interest rate expectations have been on the rise. At the end of March 2011, markets were expecting the Euro OverNight Index Average (EONIA) to climb back to the key interest rate level of 1% by May 2011 and to continue its ascent to reach about 1.7% in February 2012; the current level is at 0.7%. The expectation of a boost in interest rates immediately fed into money market rates, causing them to rise.

Long-term rates in the euro area steadily increased from a low of 2.8% in August 2010 to roughly 4.0% at the end of March 2011. The uptrend partly reflects the improvement in business conditions and partly the development of risk premia, which have jumped since October 2010 when the financial markets began to question some highly indebted countries' solvency. European solidarity with countries experiencing financial difficulties will be decisive for the further development of long-term interest rates. Agreement on the details of the ESM at the end of March 2011 was a decisive step in support of common initiatives.

3 Economic Developments in Central, Eastern and Southeastern Europe

3.1 Gradual Economic Recovery Continues

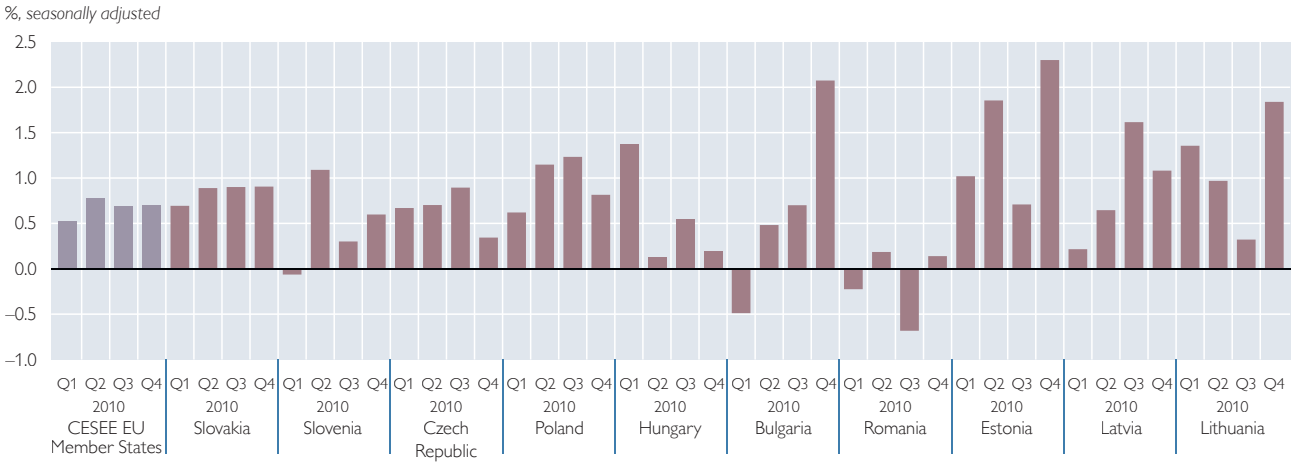
After the 2009 crisis, Central, Eastern and Southeastern Europe (CESEE) saw a gradual economic recovery in 2010, with quarter-on-quarter economic growth averaging a robust 0.7% in the third and fourth quarters. This is still just around half the growth rate recorded in the years immediately preceding the crisis, but the economic upswing then had taken place in a particularly favorable environment.

Moreover, in 2010, the economic cycles of the individual CESEE countries began to show signs of reconvergence. A certain degree of heterogeneity remains, however, with developments remaining subdued in Hungary and Romania in particular. In addition, output developments in the Baltic countries continue to display relatively high volatility.

The composition of GDP growth provides another indication of increasing stabilization in CESEE: Although in many countries economic growth continues to rely to a large extent on inventory changes and the external sector, domestic demand has regained its role as a driver of economic growth in at least some CESEE countries in the third and fourth quarters of 2010. This is particularly the case in some Central European countries which weathered the economic downturn relatively well in 2010 and returned to a growth path at an early stage or which – like Poland – did not slip into recession in the first place. Domestic demand was the major growth factor in Slovakia and Poland and showed signs of improvement in other CESEE countries as well. Both investments and private consumption were the key drivers of this recovery in domestic demand. On the one hand, strong export dynamics and industrial production as well as the subsequent increase in capacity utilization may have contributed to this development, on the other hand, the job market situation in the region has stabilized and public sentiment in general is cautiously positive. The European Commission's Economic Sentiment Indicator for the region consequently returned to its long-term average in January 2011.

Chart 4

Quarter-on-Quarter GDP Growth

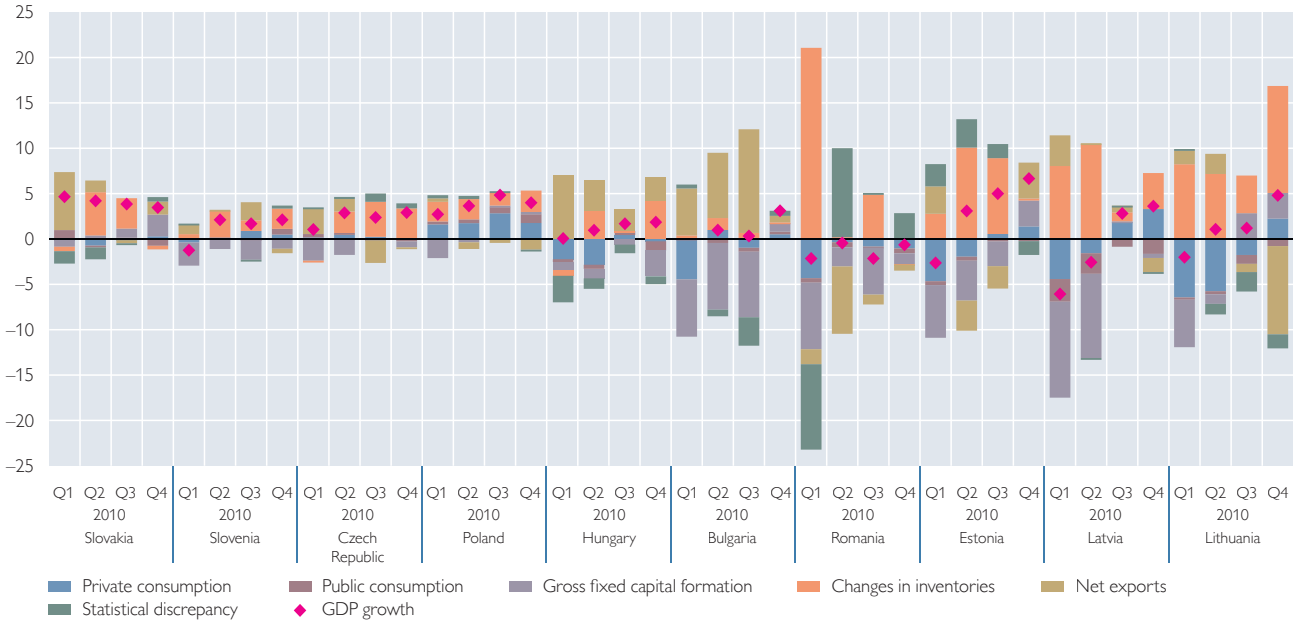


Source: Eurostat.

Chart 5

Year-on-Year GDP Growth

Contributions to GDP growth (against the same quarter of the previous year, not seasonally adjusted) in percentage points, GDP growth in %



Source: Eurostat.

Hesitant lending, the necessity to further reduce household debt, the increased need to consolidate public finances and weak construction activity continue to weigh on the overall recovery, however.

Against this background, the economic outlook for the CESEE region will still be somewhat subdued for 2011. Current forecasts assume an average growth rate of just under 3% for CESEE in 2011, with economic activity expanding again in all the countries of the region (at a rate of between 2% and 4.5%). In 2012, growth will continue to increase slightly to an average rate of between 3.5% and 4%, before stabilizing around an annual 4% in the period from 2013 to 2015. At this rate, the CESEE countries would regain a relatively clear two-percentage point growth edge on the euro area. Following a pronounced slowdown in 2009 and 2010, income convergence with the euro area will thus continue at a stronger pace in the future. The record highs posted in the pre-crisis boom years may well have been a historical exception, however.

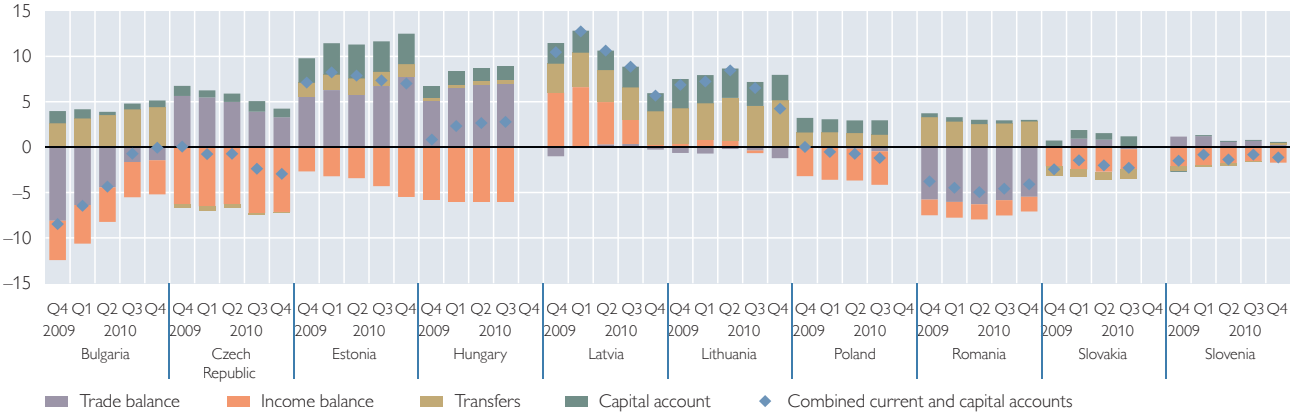
3.2 Current Account Positions Largely Stable after Significant Improvement during the Crisis

The external position of all CESEE EU Member States improved (sometimes significantly) during the crisis. In the wake of accelerating economic activity, current account positions appear to be stabilizing at the moment, which is mainly attributable to two factors: First, domestic demand, which had lately strengthened in some countries, has a dampening effect on trade balances. Second, income accounts deteriorated in many countries, most likely reflecting the renewed repatriation of profits from foreign direct investment enterprises. Hungary, Bulgaria and Romania are the major exceptions from the developments outlined above; in

Chart 6

Current Account Balances in CESEE

% of GDP, moving average over the last four quarters



Source: National central banks.

these countries, the recovery is still slightly more fragile than in the remaining CESEE countries, and the positive effects of the economic slack on the current account positions persist. But these positive effects are likely to fade out in the course of 2011. Current forecasts expect current account balances to deteriorate slightly in all CESEE countries in 2011 – a trend that is likely to continue over the medium term. However, as there are currently no indications of overshooting in lending, wages and public spending (like before the crisis), it is very unlikely that over the next few years, current account gaps will again widen to their extremely high pre-crisis levels.

3.3 Exit from Monetary Easing as Inflation Rates Rise

Inflation rates were rising (clearly, in part) across the entire CESEE region over the past few months. This was mainly attributable to surges in both processed and unprocessed food prices, which together account for almost the entire average rise in inflation in CESEE. In some countries, VAT hikes, which were implemented in a reaction to tight fiscal positions, fueled inflation as well. This effect was most obvious in Romania, where a rise in the major VAT rate from 19% to 24% in the summer of 2010 caused the inflation rate to almost double in the second half of the year. VAT hikes took also place in the Czech Republic at the beginning of 2010 (from 19% to 20%) and in Poland and Slovakia at the beginning of 2011 (from 22% to 23% and from 19% to 20%, respectively). In Slovakia in particular, this rise had a significant effect on the inflation rate as early as in January 2011.

Although core inflation remains clearly below HICP inflation in most countries under consideration, several central banks in the region increased their key interest rates in response to rising price pressures, thereby starting the exit from the broadly accommodative monetary policy stance adopted during the crisis. Narodowy Bank Polsky (NBP), for example, raised its key policy rate by 25 basis points to 3.25% in January 2011, while Magyar Nemzeti Bank (MNB) increased its key interest rate in three steps by 25 basis points each (November and December 2010 and January 2011) to currently 6%. In Poland, CPI inflation came to

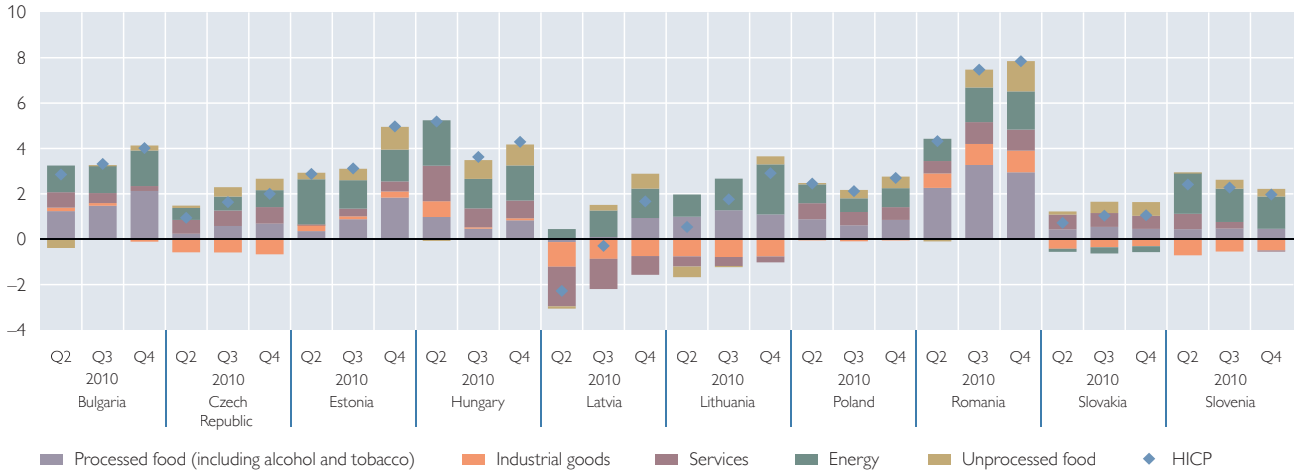
3.6% in February 2011 and was thus clearly above the inflation target of 2.5% (CPI). Given high energy and food prices as well as the VAT hikes mentioned above, Poland is not expected meet its inflation target over the next few months. According to the NBP, accelerating price growth has begun to affect inflation expectations. The situation is similar in Hungary, where the central bank expects to clearly surpass the inflation target (3% CPI inflation) in the next few quarters. Rising food and oil prices as well as the potential pass-through of special sectoral taxes to consumer prices will have a short-term inflationary effect, while on the cost side, moderate wage developments are likely to slow down price growth at least in the short term. Inflation expectations, however, remain at a relatively high level (between 4.0% and 5.5%) and might – together with strengthening consumer demand – slow down the decrease in inflation as soon as the effects of short-term shocks have subsided. In addition, the higher risk premiums on Hungarian financial assets recorded in the period in question may have influenced the interest rate decisions of the MNB.

The trend toward some monetary tightening in periods of rising inflation rates can be observed in a number of non-EU CESEE countries. Thus in February 2011, the Central Bank of Russia (CBR) raised several interest rates (e.g. the refinancing rate, by 25 basis points to 8%) as well as the minimum reserve requirements (which it had slightly raised already in January 2011). At the same time, the trading band of the Russian ruble around its central rate against a U.S. dollar-euro currency basket consisting of the U.S. dollar and the euro was widened from RUB 4 to RUB 5. In Serbia, the key interest rate was raised in two steps in January and March 2011, by 50 basis points and 25 basis points, respectively, to 12.25%. Apart from fighting inflation, another objective of these measures may have been to stabilize the Serbian dinar, which had come under pressure over the past months and had to be supported through several interventions.

Chart 7

Inflation Developments in CESEE

Contributions to HICP changes (against the same quarter of the previous year) in percentage points, HICP in %



Source: Eurostat.

The Turkish central bank (TCMB), by contrast, lowered its key interest rate by 25 basis points to 6.25% in January 2011 despite the economic boom, following a reduction by 50 basis points in December 2010. Most likely, this step was aimed at containing (speculative) capital inflows and has to be seen in connection with a rise of several minimum reserve requirements agreed upon a few days after the interest rate reduction. According to the TCMB, this measure absorbed liquidity to the extent of EUR 4.9 billion from the market, which means that overall, these two monetary policy steps resulted in a certain tightening of monetary policy.

4 Austrian Economic Growth Remains Strong in Early 2011

4.1 Economic Growth Reaches 2.1% in 2010

After the severe economic slump in the course of the financial and economic crisis, Austria's economy returned to positive growth in 2010. The main drivers of economic recovery were the rebound of the world economy and in particular the robust economic growth observed in Germany, Austria's main trading partner. In the fourth quarter of 2010, export activity slackened temporarily, but this development did not come as a surprise after the extraordinarily rapid growth rates recorded in previous quarters. The results of the OeNB's export indicator, which is based on truck mileage data provided by ASFINAG, Austria's highway operator, suggest that exports resumed their expansion in January and February 2011. As Japan plays only a minor role as a trading partner to Austria (e.g. accounting for only 0.8% of Austrian goods exports in 2009), the catastrophe in Japan is currently not expected to have direct adverse effects on the Austrian economy.

The dynamic growth in exports was especially beneficial to Austrian industry; by the end of 2010, this sector was able to offset nearly three-quarters of the drop in production by just under 20% brought about by the crisis. Thanks to growth in exports and industrial production, the contractionary phase of the investment cycle also came to an end in mid-2010. Manufacturers reported above-average levels of capacity utilization, and investments in plant and equipment began to climb again for the first time in nearly two years. At the same time, construction invest-

Table 1

Real GDP and Demand Components (in real terms; seasonally and working-day adjusted)

	GDP	Private consumption	Government consumption	Gross fixed capital formation	Exports	Imports	Total domestic demand (excluding inventories)	Net exports	Inventories	Statistical discrepancy
	Change on previous period in %						*Contribution to GDP growth in percentage points*			
Q1 10	0.2	0.2	–3.2	–1.1	3.2	2.4	–0.7	0.5	0.3	0.1
Q2 10	1.0	0.2	0.3	0.3	4.2	3.7	0.2	0.5	0.4	–0.2
Q3 10	1.1	0.2	0.1	1.2	3.2	2.7	0.4	0.5	0.4	–0.1
Q4 10	0.8	0.2	0.3	1.1	1.2	0.8	0.4	0.3	0.4	–0.3
2008	2.2	0.7	3.9	2.8	0.5	–1.7	1.7	1.2	–0.6	–0.1
2009	–3.9	1.2	0.4	–7.9	–15.6	–12.5	–1.0	–2.7	–0.9	0.8
2010	2.1	1.0	–2.4	–1.2	10.6	7.5	–0.2	2.0	0.9	–0.6

Source: WIFO.

ments showed disappointing development, as investments in both residential construction and civil engineering projects continued to fall. Despite positive quarterly growth rates in the last three quarters of 2010, gross fixed capital formation contracted further over the year as a whole. Although consumer spending rose moderately in 2010, domestic demand did not make a positive contribution to economic growth, which was mainly driven by net exports and restocking.

Some special temporary factors which had previously supported growth – such as the buildup of inventories depleted during the crisis and the (now expiring) expansionary fiscal policies introduced in response to the crisis – are currently fading out. This development has been accompanied by additional factors dampening economic growth: The fiscal consolidation measures required in response to the crisis are putting pressure on households' disposable income. Combined with sharp increases in energy and commodity prices, this pressure has weakened private consumption.

However, the growth dynamics underlying the Austrian economy still appear to be robust. The highly favorable situation on the job market is having a positive effect on the household income situation. Employment is once again surging in Austria, which has led to declines in unemployment figures. Both the sharp rise in registered vacancies and the massive decline in the number of planned layoffs suggest that this trend is likely to continue in the coming months. In the near future, positive stimuli can be expected mainly from exports and investments. At the same time, the restocking phase has probably not yet come to an end and will therefore continue to drive growth as well.

Results of the OeNB Economic Indicator of March 2011[1]

The Austrian economy is currently expanding at an above-average rate; this growth is primarily rooted in strong demand from abroad. For the first quarter of 2011, the OeNB's economic indicator points to real GDP growth of 0.6% (seasonally and working-day adjusted; compared to the previous quarter). In the second quarter of 2011, we can expect GDP growth to weaken to 0.5%. In the first and second quarters of 2011, growth will thus come to 3.5% and 3.0%, respectively, on a quarterly basis.

Short-Term Outlook for Austria's Real GDP in the First and Second Quarters of 2011 (seasonally and working-day adjusted)

2009				2010				2011	
Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Year-on-year quarterly change in %									
–4.4	–5.4	–3.8	–1.8	0.5	2.3	2.7	3.1	**3.5**	**3.0**
Quarterly change in %									
–2.0	–0.8	0.7	0.4	0.2	1.0	1.1	0.8	**0.6**	**0.5**
Annual change in %									
–3.9				**2.1**					

Source: Results of the OeNB's Economic Indicator of March 2011, Eurostat.

[1] *The next release of the OeNB's Economic Indicator is scheduled for July 2011.*

4.2 New Employment Record Reached in February 2011

Thanks to the favorable development of the economy in recent quarters, the situation on the Austrian labor market has improved markedly. For a full year now, employment growth has been accelerating steadily. According to employment data provided by the Main Association of Austrian Social Security Institutions, payroll employment had risen by 72,100 (year on year) by February 2011, which represents a growth rate of 2.2%. A look at the seasonally adjusted data series indicates a new employment high in February 2011, with employment exceeding the previous record of June 2008 by a full 14,200. The continued surge in the number of registered vacancies also warrants expectations of a further rise in employment over the coming months.

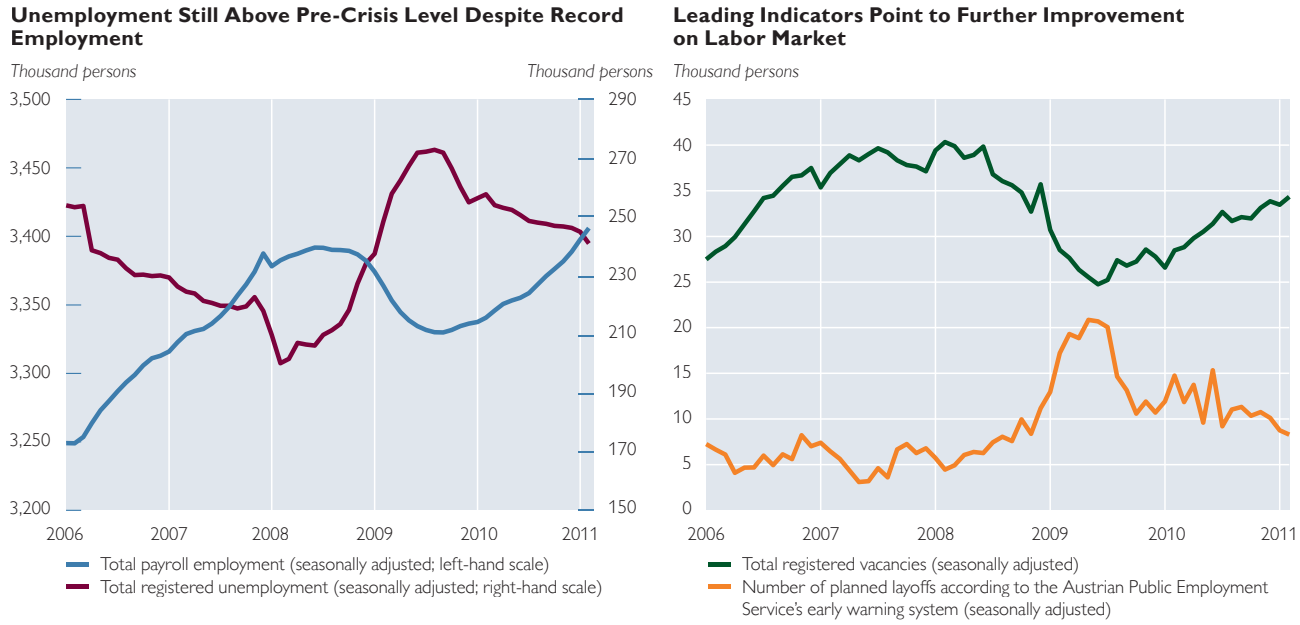
According to the most recent figures available (January 2011), Austria and the Netherlands currently have the lowest unemployment rates (both at 4.3%) in the entire EU, where the overall average is 9.5%. Eurostat has made substantial downward revisions to Austria's unemployment figures for the past months, indicating that the rate of unemployment dropped from 4.8% in the crisis year 2009 to 4.4% in 2010. Considering the depth of the recession, the economic and financial crisis thus left only a faint mark on the Austrian labor market compared to many other countries. Nevertheless, total registered unemployment in February 2010 was still 40,800 higher than the low reached in February 2008, which can be attributed to rapid growth in the labor supply.

4.3 Energy Prices Fueling Inflation

Inflation accelerated steadily in the course of 2010 and reached a new high of 3.1% (HICP inflation rate) in February 2011. This development was primarily caused by the current surge in energy prices, which accounted for approximately one-third of the 0.6 per-

Chart 8

Austrian Labor Market Developing Very Favorably



Source: Public Employment Service Austria, Main Association of Austrian Social Security Institutions, OeNB.

centage point rise in HICP inflation between January and February 2011. At 12.9%, inflation in the energy sector was clearly higher in February 2011 than in the previous month (10.6%). The prices of motor fuels and heating oil shot up due to developments on the crude oil markets. The rise in prices for other fuels (natural gas, solid fuels) was far less pronounced because those prices are not directly affected by changes in crude oil prices. According to the OeNB's projections, the hike in taxes on mineral oils, tobacco and airline tickets introduced in Austria's fiscal consolidation package will boost inflation by 0.4 percentage points in 2011. Food prices are also making a noticeable contribution to inflationary pressure at the moment; in February 2011, their contribution came to 0.7 percentage points. This can largely be put down to rising commodity prices, which have affected the prices of processed foods in Austria. The OeNB has now updated the inflation forecast published at the beginning of March 2011; on the basis of higher assumptions regarding the price of crude oil, the OeNB expects HICP inflation to amount to 2.7% for the year 2011 overall.

At present, the development of wages cannot keep up with inflation. Wages per employee rose by 1.7% in the fourth quarter of 2010. In February 2011, the index of agreed minimum wages also increased by 1.7% year on year. As a result, workers are currently seeing their wages decline noticeably in real terms.