

October 2007

conjoncture flash

Slowdown beginning in the eurozone

Most leading business cycle indicators for the eurozone peaked in May or June 2007. They have since fallen, hinting at an economic slowdown in late 2007 or early 2008.

Depression in the middle of summer...

From the summer on, all leading indicators fell for the eurozone and the United States alike. The downturn was confirmed by data released in September.

Manufacturing activity is slowing down. The PMI index¹ (purchasing managers' index for the eurozone) for the manufacturing sector fell from 54.3 to 53.2 points in September, reaching its lowest point in two years. Indicators for new and pending orders in particular were down. Although the slowdown was observed throughout the eurozone, France and Spain have been hit the hardest.

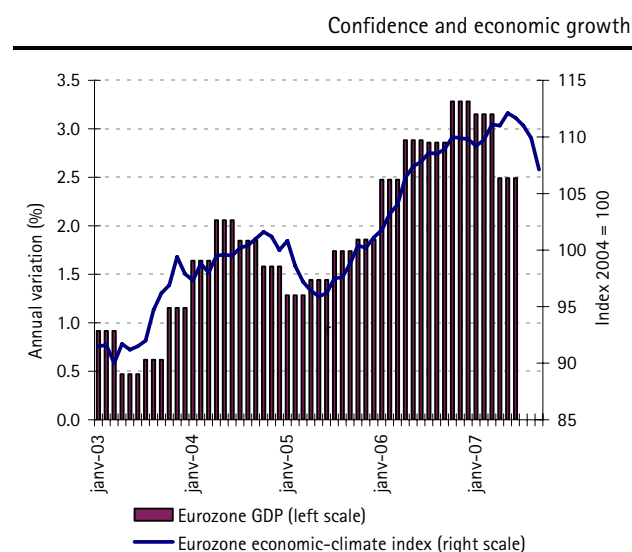
The PMI index for the services sector in the eurozone fell from 57.4 in August to 54.7 in September, affected by increasing pessimism on current and new activity. This time, it was Germany that bore the brunt of the slump, but figures for France were also down.

The economic climate indicator for the eurozone drawn up by the European Commission fell sharply between August and September 2007. This index provides an overview of surveys conducted on business leaders (in manufacturing, construction, retail trade and services) and households (consumer confidence survey). Given the dramatic fall in September, it is difficult not to make a connection with the financial turbulence of the summer, when the large equity markets² fell by about 10% between mid-July and mid-August. However, there may also have been other contributing factors: including in particular, the strong appreciation of the euro since mid-August (crossing the threshold of USD 1.40 to one euro on 20 September), confirmation of the slowdown in the United States, the delayed effects of successive interest rate hikes on household purchasing power, and rising oil prices (Brent crude rose from USD 67 to USD 77 between 20 August and 20 September and was close to USD 90 in the final days).

... that will affect growth in late 2007

A break in the downward trend of leading indicators,

Monthly publication of the state of the Luxembourg economy



Sources: Eurostat, European Commission

cannot, however, be excluded at a later date. The ZEW indices³, which, after falling significantly in August and September, did not see any further correction in expectations for October⁴. This may be linked to the easing off in the financial markets in September and it will be interesting to see if the other indicators react similarly in October.

Regardless, these indicators have been significantly corrected over recent months, which should affect GDP data for the eurozone, given the close correlation between these two types of variables (see graph). Economic growth may be spared in the third quarter, but a slowdown thereafter seems inevitable.

¹ Source: NTC Research

² Dow Jones Industrial Average for the United States, Eurostoxx50 for the eurozone and Nikkei for Japan.

³ Source: Zentrum für Europäische Wirtschaftsforschung. The ZEW indices reflect the sentiment of about 350 German institutional investors and business analysts on the current situation and outlook for Germany, the eurozone and the United States.

⁴ This was the only leading indicator available for October at the time of printing.

Manufacturing

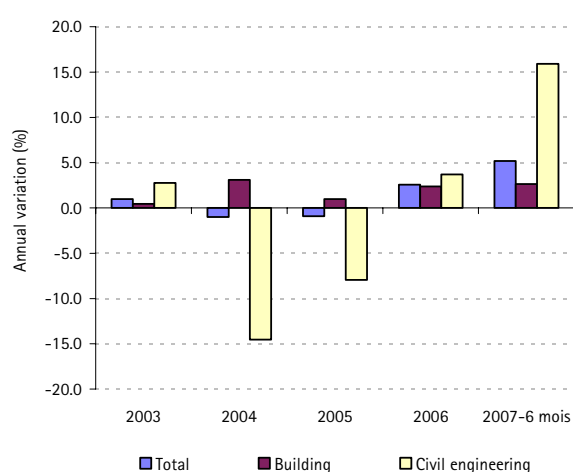
Industrial production per working day



Source: STATEC

Construction

Construction industry production per working day



Source: STATEC

Financial sector (1)

Profit and loss accounts

	September 2006	September 2007	Variation
	In millions of EUR		As a %
Interest margin ¹	3 192	3 723	16.6
Income from commission	2 677	2 970	11.0
Other net income	1 829	647	-64.6
Banking income	7 698	7 340	-4.7
Personnel expenses	1 517	1 682	10.9
Other overhead expenses	1 255	1 393	11.0
Overhead expenses	2 772	3 074	10.9
Earnings before provisions	4 926	4 265	-13.4

Source: CSSF (provisional results)

¹ Including dividends received on subsidiaries

Iron and steel drive production figures

During the first half of 2007, manufacturing output per working day in Luxembourg grew by 2.0% compared to the same period in 2006, at a rate of expansion slightly below that for the year as a whole (+2.3%) Apart from iron and steel, output rose a mere 1%

The iron and steel industry has driven most of the industrial expansion over the last two years, buoyed in particular by development in emerging countries.

Production of consumer goods has slowed significantly since 2006 while energy output and distribution fell in the first half of 2007.

Civil engineering makes a comeback

During the first half of 2007, construction output per working day (based on the volume of hours worked) rose by a little over 5% over one year. This relatively high pace of growth owes much to an extremely dynamic 1st quarter (+11% compared to last year), largely due to favourable climatic conditions.

Construction activity had already accelerated significantly and steadily since mid-2006, coinciding with the return to favour of civil engineering, which had slumped considerably over the two previous years.

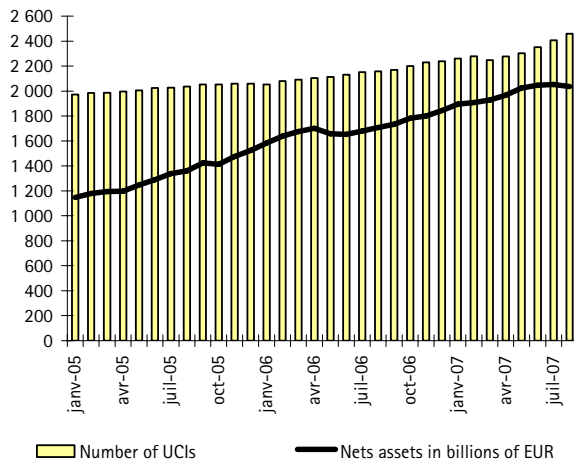
Banking activity holds its own in the 3rd quarter

According to provisional data released by the Commission de Surveillance du Secteur Financier, income before provisions in the banking sector was valued at EUR 4,265 billion as of 30 September 2007, a drop of 13.4% over one year. Setting aside exceptional income for 2006, performance was up 6.1% over one year, down on the position at the end of the 2nd quarter.

The CSSF is, however, reassuring with regard to the difficulties that have recently troubled the stock markets. "Recent tension observed on the financial markets following the downturn in certain segments of the subprime market in the United States have had relatively limited effects on the profits of Luxembourg banks. This is hardly surprising, given that the main activities carried out on the financial markets are private banking and UCI management. Luxembourg banks have little involvement in investment banking, which is particularly hard hit by this tension."

Financial sector (2)

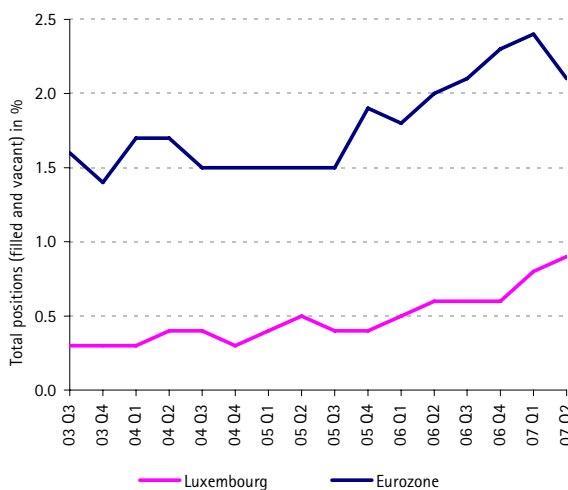
Total UCIs and net assets



Source: CSSF

Labour market

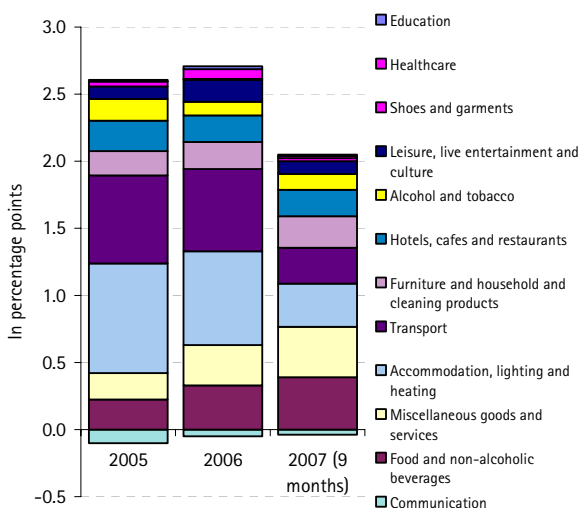
Rate of job positions left vacant



Sources: Eurostat, ADEM-IGSS-STATEC

Wage inflation

Contribution to the progression of the IPCN index



Sources: STATEC

UCIs affected by financial turbulence

The 10% growth in Luxembourg UCI net assets between December 2006 and January 2007 was brought to a halt by the financial turbulence over the summer. July registered only slight growth of 0.3%, while in August growth fell by 0.9%.

Fluctuations in net assets are caused by two variables: net capital investment (issues less repurchases) and variations directly due to trends in the financial markets. Each time the stock market trends fall for a prolonged period, like in February-March 2005, May-June 2006 or July-August 2007, UCI assets are affected directly and indirectly because there is less inflow of new capital (this was nil in August 2007).

Job vacancy rate up in Luxembourg

The job vacancy rate is the proportion of vacancies (newly created jobs, unfilled vacancies or vacancies arising in the short term that the employer is actively seeking and will continue to seek to fill by sourcing workers from outside the business, and that the employer intends to fill immediately or in the near future) to total jobs (occupied or vacant).

The job vacancy rate in the EU fell from 2.2% in the first quarter of 2007 (when it appears to have peaked) to 2.1% in the second quarter, corresponding to the slowdown in employment growth (1.5% in the second quarter of 2007 as against 1.8% a year ago). In Luxembourg, the job vacancy rate rose from 0.8% to 0.9% over the same period.

Luxembourg is currently experiencing very dynamic employment growth (4.2% in the second quarter of 2007).

Employment growth is particularly high (1.9%) in the financial sector and business services.

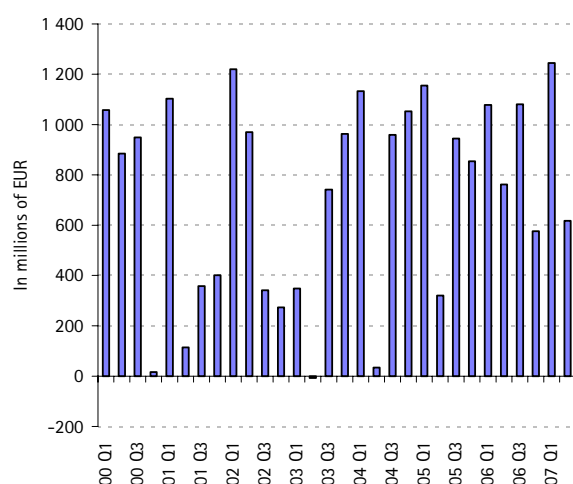
Food price tensions

Food and non-alcoholic beverages accounted for most of the inflation (0.39 % points out of 2.0%) witnessed in the first nine months of 2007. Prices for these goods rose 2.9% on average in early 2007, as against 2.2% per annum on average over the last ten years.

The fall-off in inflation (down from 2.7% in 2006 to 2.0% for the first nine months of 2007) was mainly due to accommodation, heating and lighting (down 0.4% points) and transport (down 0.3% points). Given the current oil prices (almost USD 80 per barrel in October, up 40% over one year; a 20% increase in the price in EUR) there will be a basic effect on data in late 2007 (the oil price index fell 3% in the fourth quarter of 2006). High inflation during the last quarter of 2007 is to be expected (+2.7% according to the latest forecasts), as is an annual inflation rate of over 2.0% (2.2% according to the latest forecasts).

Foreign trade

Current account surplus



Sources: STATEC, BCL

Current account surplus remains high

According to BCL and STATEC, the current account surplus for the first half of 2007 was settled at EUR 1.86 billion, as against EUR 1.84 billion for the first half of 2006.

Surplus in trade in services grew about 10% over one year, mostly due to the excellent performance in the UCI management sector, which led to a rise in income from financial services of some 15%. The surplus for other service activities was somewhat stagnant, and exports fell slightly (-1%) following the marked decline in activity in IT and information services.

The trade deficit dropped slightly, thanks to clear improvements in terms of trade (+8%) affected by both falling prices for oil products on the import side during the first half and rising prices for iron and steel on the export side. Strengthened by substantial sell-offs of non-monetary gold, this favourable trend more than offset the rising imports of intermediate goods and capital goods.

Statistics table

	Feb-07	Mar-07	Apr-07	May-07	Jun-07	Jul-07	Aug-08	Sep-08	Average over the last three months	Same period previous year
Annual variations in %, except where otherwise indicated										
Activity										
Industrial output per working day, in volume	3.9	2.0	3.7	-0.5	4.7	...	...	...	2.6	1.1
Construction output per working day, in volume	14.1	9.2	4.2	-3.7	0.9	...	...	...	-2.7	2.1
Turnover by volume of total trade	-2.0	1.7	1.1	-1.5	-1.3	...	...	...	-0.6	2.9
Turnover by volume of total retail trade	-0.5	4.5	0.4	-4.4	2.8	...	...	...	-0.5	4.1
Prices, wages										
Consumer price index (IPCN)	2.0	2.1	2.1	1.9	2.0	1.9	1.9	2.1	1.9	2.7
Underlying inflation	2.3	2.3	2.3	2.4	2.2	2.1	2.2	2.3	2.2	2.1
Oil prices	-4.1	0.0	-2.2	-4.9	-1.0	-2.3	-3.0	-0.8	-2.0	9.6
Industrial producer price index	12.2	11.3	13.1	10.0	10.3	6.1	...	...	8.8	9.0
Construction price index ¹	2.8	2.8	3.3	3.3	3.3	...	...	...	3.3	2.9
Average wage bill, per month, per person	5.1	5.8	4.0	6.2	0.7	...	...	...	4.1	3.6
Foreign trade										
Exports of goods	6.2	8.3	7.9	2.5	6.4	8.8	...	...	5.8	10.3
Imports of goods	5.9	6.5	-6.4	9.2	6.4	11.5	...	...	9.0	13.7
Employment, unemployment										
Domestic number of employees	4.4	4.1	4.5	4.4	4.3	4.4	4.4	4.4	4.4	4.2
National employment	2.0	1.7	1.9	1.8	1.8	1.9	1.9	2.0	1.9	2.1
Unemployment rate (% of working population, seasonally adjusted)	4.5	4.4	4.5	4.4	4.5	4.4	4.4	4.3	4.4	4.4

Sources: STATEC

Data in italic font are estimates

¹Estimations based on half-yearly data

Indicators

	Variation on previous quarter in %					
	2007 Q1	2007 Q2	Forecast 2007 Q3		Forecast 2007 Q4	
			Min	Max	Min	Max
Eurozone- Growth in volume of GDP (European Commission)	0.7	0.3	0.3	0.7	0.3	0.7
	Annual variation in %					
	2005	2006	Forecast 2007		Forecast 2008	
Luxembourg - Growth in volume of GDP (STATEC)	5.0	6.1	6.0		5.0	
GDP at current prices for 2006: EUR 33 852 million						
Minimum monthly salary (since 01/01/2007: EUR 1 570.28)						
Consumer price index (September 2007) - base January 1 st 1948: 719.15						
Half-yearly average of the index linked to base as at January 1 st 1948: 715.89						
Current account balance (2007 - 2nd quarter): EUR 618 million						
Resident population (01/01/2007): 476 200 (estimation)						

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