

conjoncture flash

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Monthly publication of the state of the Luxembourg economy

Rising pay pressure in Europe

European wages have accelerated significantly since early 2007, in line with stronger economic activity in recent years and falling unemployment. According to provisional data, however, Luxembourg is exercising wage restraint.

Accelerating labour costs in the eurozone

Although labour costs¹ in most European countries have cooled since 2001, pay pressure rose in 2007, more so in the wider European Union than in the eurozone alone. This was mainly due to the phenomenon of more recent Member States catching up.

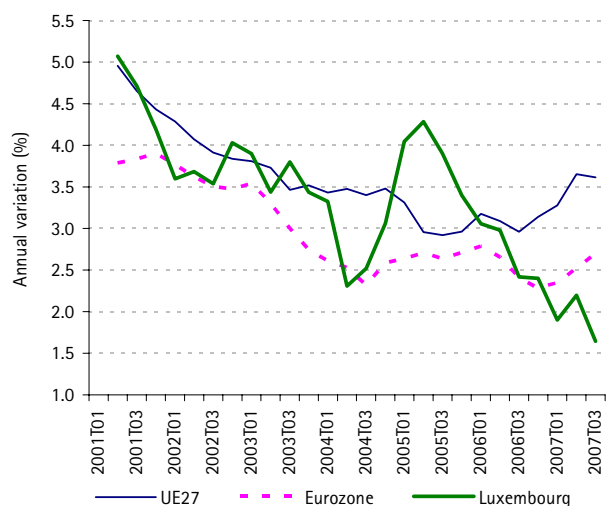
Within the eurozone, wage trends differed significantly from country to country. Most have experienced rising labour costs since 2007, particularly Belgium, Spain, the Netherlands and, to a lesser extent, Austria, Portugal and Finland. The situation is a little different in France, where wages are rising at more or less the same pace as in 2006, and in Germany.

Germany continues to have the most moderate wage growth in Europe, with just 1% nominal growth in 2007 (as against 1.7% in 2006), which, compared to inflation at 2.3%, reveals a drop in household purchasing power in 2007 for the fourth consecutive year. However, wage pressures re-emerged in Germany in early 2008, with pressing wage claims in the metal and transport sectors (which have already been partly accepted) and this may spread to other economic sectors.

Those countries with the most wage pressures, Ireland and Spain (where labour costs grew by over 4% in 2007) are also those with the highest inflation. In their defence, it must be said that economic growth in these countries was also far higher than the eurozone average (at 4.9% and 3.8% respectively in 2007).

In Luxembourg, there is still some evidence of wage restraint, with the labour cost index rising just 1.9% in 2007 (provisional figure).

Trend in hourly labour costs



Source: Eurostat (sliding scales)

Falling unemployment benefits wages

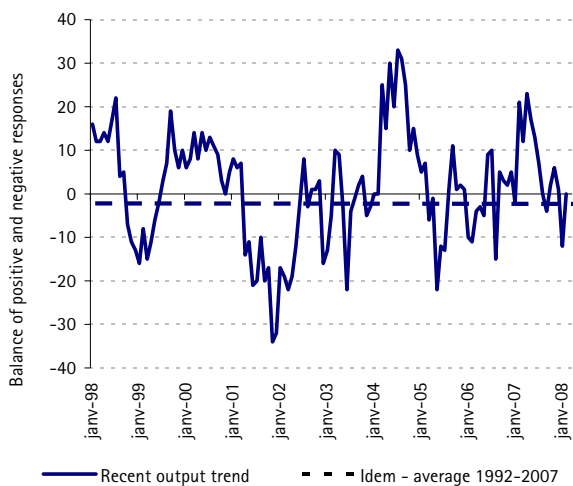
The unemployment rate, which has been falling since mid-2005, continued its downward trend in early 2008, reaching 7.1% in January in the eurozone. Although this fall has been less sharp since the second half of 2007, it is expected to result in additional wage pressure, particularly in sectors experiencing recruitment difficulties (variable from country to country) and/or those least exposed to international competition. The wage contribution (i.e. the share of wages in added value), which has been falling quite markedly since 2004, stands to gain from this.

In the longer term, however, this trend could be reversed if the economic slowdown we are currently witnessing is more marked than expected, thereby changing the balance of power in favour of business leaders in wage negotiations.

¹ Hourly labour cost index, working-day adjusted (Source: Eurostat)

Manufacturing

Economic survey on industry



Source: STATEC

Measured optimism in a difficult context

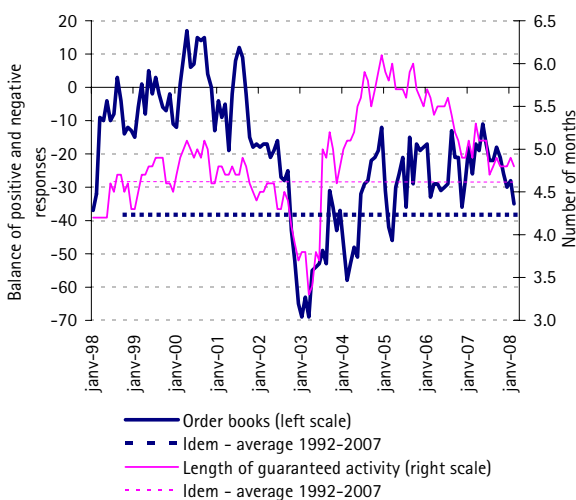
Luxembourg manufacturers' opinions improved slightly in February: opinions on recent output and order books were up, after a very downbeat January.

Globally, opinions are close to their long-term average, moderately upbeat for the 1st quarter of 2008. It must be noted that industrial output in Luxembourg practically stagnated in 2007 (+0.3%).

Despite a recovery in industrial output in the eurozone in January, the trend is downward and opinions on order books (PMI survey) do not point to any rally in the short term. The trend in the United States was also down in early 2008, in terms of both output and new orders.

Construction

Economic survey on construction



Source: STATEC

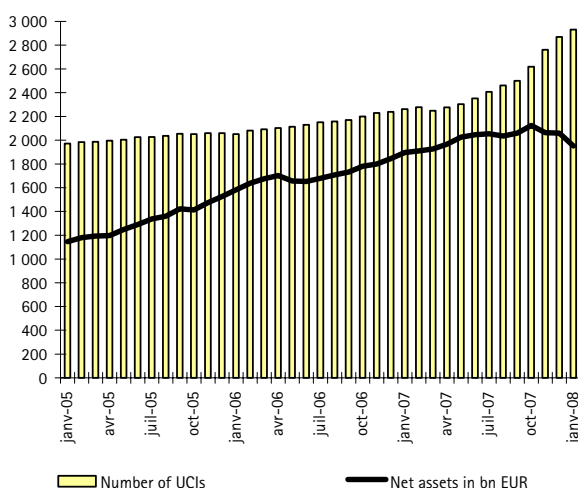
Activity more sluggish in early 2008

Opinions in the construction industry slumped in February (this is a recent trend, orders and activity are holding up) but this is usual at this time of year and it is not completely out of line with historical data. As in the 2nd half of 2007, output is expected to grow slightly in early 2008 and will probably be down on last year's results, given that the first quarter of 2007 was marked by exceptionally high levels of activity.

Output grew in the eurozone in January, but this has now stabilised. After rising sharply from 2005 to 2006, construction activity throughout the eurozone seems to have peaked in 2007. In recent months, output has been down in several countries such as Spain, Ireland, Austria and Germany.

Financial sector

Number of UCIs and net assets



Source: CSSF

A bad start to the year for UCIs

January 2008 proved a disastrous month for Luxembourg UCI results. Net assets fell below the symbolic barrier of EUR 2,000 billion, a level not seen since June 2002 (-5.3% compared to December 2007, representing a drop of some EUR 110 billion).

UCI assets linked solely to the financial markets were a major factor in this negative performance. In parallel, net inflows of capital are down (in other words, there is a net capital outflow), which has exacerbated the downward trend of previous months.

The prospects for the 1st quarter of 2008 as a whole are not particularly encouraging, given recent trends in the financial markets. Prices did stabilise in February, but March was again marked by several extensive downward corrections.

Tourism

Arrivals and overnight stays: hotels, hostels, guest houses

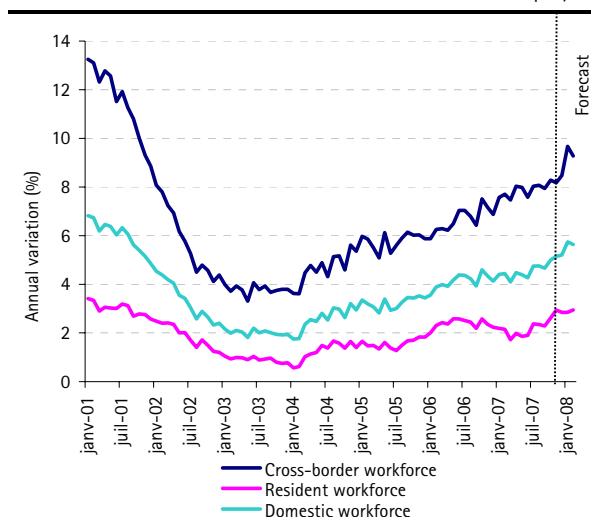
	2006	2007*	2007/06*
	Unit: thousands		Variation (%)
Arrivals			
Entire country	702.4	629.7	4.7
incl.			
Luxembourg City	369	328.5	4.9
Rest of country	333.4	301.2	4.5
Overnight stays			
Entire country	1 361	1 223	4.8
incl.			
Luxembourg City	702.1	635.3	6.8
Rest of country	659.1	587.3	2.8

Source: STATEC

* 10 months

Labour market

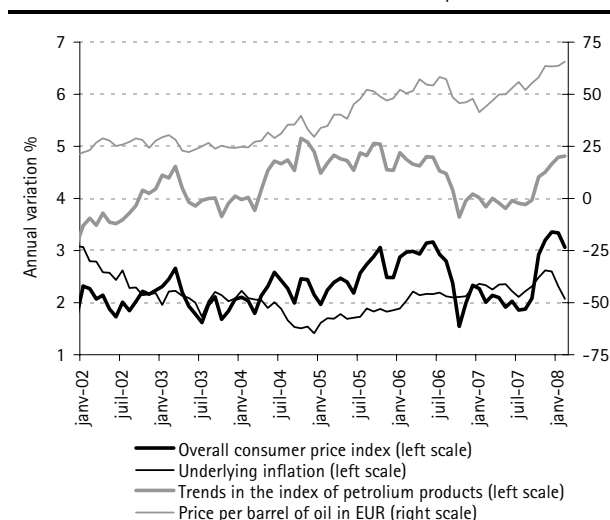
Trends in employment



Source: IGSS

Inflation, wages

Trends in oil prices and inflation



Source: STATEC

A satisfactory 2007

Tourist statistics reveal growth of approximately 5% in 2007, in terms of both arrivals and overnight stays.

This rise in tourism in 2007 was linked both to the favourable economic climate, which generates business tourism, and to the exceptional weather conditions in March and April. For example, overnight stays in March 2007 were up 10% on March 2006. Furthermore, it should be remembered that Luxembourg, together with the Greater Region, was the European Capital of Culture 2007, which had a positive effect on tourism and the hotel industry.

German and British tourists were up (+8% and +6%) but there were slight falls of about 2% among Dutch and French tourists.

Job creations also benefit residents

According to the latest available data, paid employment grew 5.2% in November 2007. This means that the acceleration seen the previous month (rising from 4.7% in September to 5.0% in October) has continued.

While cross-border employment continues to grow strongly (at around 8%), paid employment of residents is rising much faster: from 2.3% in September to 2.6% in October and 2.9% in November. Paid employment of residents has returned to the pace of growth before the slowdown in 2001. Just as with cross-border workers, resident workers are being hired in the financial sector, business services, construction, transport and communications, as well as health and public administration. However, cross-border employment still accounts for approximately 70% of net new jobs created in Luxembourg.

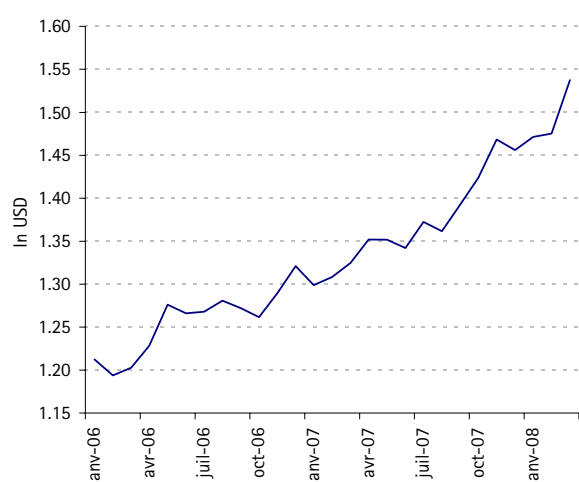
Inflation set to remain high in 2008

Inflation is set to remain high in early 2008, due in particular to a significant statistical effect concerning oil prices. Oil prices dropped in late 2006, reaching a relatively low level in early 2007 (EUR 41 per barrel of Brent in January as against EUR 58 in mid-2006). Inflation therefore slowed down slightly at the end of 2006 and the first three quarters of 2007 (see graph opposite). Although oil prices rose throughout 2007, they remained below 2006 highs until the fourth quarter of 2007.

If oil prices stabilise (to 100 USD per barrel at an exchange rate of 1.5 EUR/USD), the inflation rate will remain high in early 2008 (at about 3.2%) but will fall back below 2.5% by the end of the year.

Foreign trade

Euro-US dollar exchange rate



Source: EUROSTAT

A weakening dollar

The euro was worth about 1.55 US dollars in mid-March, as against 1.20 in March 2007. The single currency has appreciated strongly against the dollar since early February 2008. As the Japanese yen has also gained on the US dollar, it would seem that it is the dollar that is depreciating rather than the euro that is appreciating.

The falling dollar is due to the difficult economic situation in the US, where growth in recent years was funded mainly by public and private debt. The falling trend has been present since 2003, but the pick-up in pace seen in early 2008 is due to recent developments in the current property and financial crisis that is threatening to plunge the world's leading economy into recession. The sharp drop in US interest rates (from 5.25% to 2.25% within 6 months) has also contributed to the currency's depreciation.

Statistics table

	juil-07	août-07	sept-07	oct-07	nov-07	déc-07	janv-08	févr-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	-3.7	-2.5	-5.1	-1.4	-1.4	0.6	...	...	-0.8	2.1
Construction output per working day, in volume	-5.0	0.3	-3.5	-0.8	-3.8	-10.1	...	...	-4.5	3.6
Turnover by volume of total trade	2.4	24.0	4.8	-3.1	-4.2	...	...	...	-1.2	10.9
Turnover by volume of total retail trade	35.2	39.2	13.8	11.0	11.6	...	...	...	19.3	15.8
Prices, wages										
Consumer price index (IPCN)	1.9	1.9	2.1	2.9	3.2	3.4	3.3	3.1	3.3	2.2
Underlying inflation	2.1	2.2	2.3	2.5	2.6	2.6	2.3	2.1	2.3	2.3
Oil prices	-2.3	-3.0	-0.8	10.4	12.6	16.5	19.8	20.4	18.9	-0.6
Industrial producer price index	6.1	8.3	7.3	7.3	6.4	8.1	7.2	...	7.3	10.7
Construction price index ¹	3.1	3.1	3.1	3.0	3.0	3.0	...	...	3.0	2.4
Average wage bill, per month, per person	4.4	3.9	3.2	3.6	3.8	...	...	...	4.2	2.2
Foreign trade										
Exports of goods	2.0	-7.9	-6.3	-3.0	-5.0	-3.6	...	...	-3.9	-5.5
Imports of goods	14.2	14.8	-4.5	1.3	-3.0	-4.6	...	...	-2.1	-0.6
Employment, unemployment										
Domestic number of employees	4.7	4.8	4.7	5.0	5.2	5.2	5.7	5.6	5.5	4.3
National employment	2.2	2.2	2.2	2.5	2.7	2.6	2.6	2.6	2.6	2.1
Unemployment rate (% of working population, seasonally adjusted)	4.4	4.4	4.3	4.3	4.2	4.2	4.2	4.2	4.2	4.5

Sources: STATEC

Data in grey are estimates

¹Estimations based on half-yearly data

Indicators

	Variation on previous quarter in %					
	2006 Q3	2006 Q4	2007 T1	2007 T2	2007 T3	2007 T4
Eurozone- Growth in volume of GDP (European Commission)	0.6	0.8	1.2	0.3	0.7	0.4
	Annual variation in %					
	2005	2006	Forecast 2007		Forecast 2008	
Luxembourg - Growth in volume of GDP (STATEC)	5.0	6.1	5.0		4.0	
GDP at current prices for 2006: EUR 33 852 million	Minimum monthly salary (since 01/03/2008: EUR 1 609.53)					
Consumer price index (February 2008) - base January 1 st 1948: 731.97	Half-yearly average of the index linked to base as at January 1 st 1948: 725.39					
Current account balance (2007 - 3rd quarter): EUR 1 212 million	Resident population (01/01/2007): 476 200 (estimation)					

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