

October 2009

# conjoncture flash

## Contained decline in GDP during the 2<sup>nd</sup> quarter

The recession in the Luxembourg economy, which started in mid-2008, seems to be coming to an end. While a recovery is expected for the 2<sup>nd</sup> half-year, this will be from a very low starting point and the economy has a long way to go before it reaches activity and employment levels seen before the crisis.

### Activity stabilises

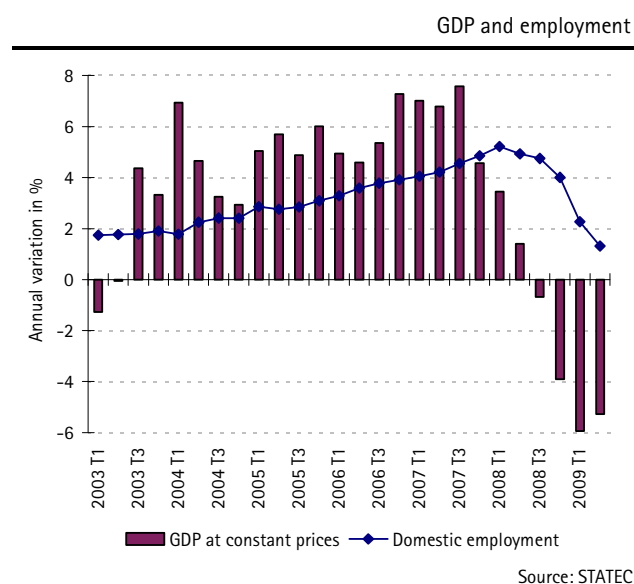
Luxembourg GDP fell slightly during the 2<sup>nd</sup> quarter of 2009 – down 0.3% compared to the 1<sup>st</sup> quarter (based on seasonally adjusted figures). The overall trend is a stabilisation in economic activity or, expressed differently, an end to the decline in activity, particularly in the two most affected sectors (finance and manufacturing). The two previous quarters saw much more marked falls, down 2.9% and 1.7% respectively.

Economic activity experienced a change in dynamics over the 2<sup>nd</sup> quarter. The financial sector again made a positive contribution to growth, after falling sharply in the 1<sup>st</sup> quarter. However, other services (i.e. trade, hotel and catering, transport and communications, property, and business services), which had stood up well in the 1<sup>st</sup> quarter of 2009, fell back significantly. Manufacturing also recovered during the 2<sup>nd</sup> quarter (up 2.6% over the quarter), which may mean that the decline in activity has bottomed out and that the destocking trend which started in late 2008 is coming to an end. Opinion surveys for July to September also point to renewed growth in industrial output for the 3<sup>rd</sup> quarter. In contrast, added value in construction has continued to shrink at the same level as in the 1<sup>st</sup> quarter. While output bounced back in July (see next page), opinions in the construction sector on activity levels in the 3<sup>rd</sup> quarter again deteriorated.

### Recovery in sight

As the Luxembourg economy is highly dependent on foreign trade, the improvement in international growth prospects for the 3<sup>rd</sup> quarter is naturally an encouraging sign. In the quarterly profile, Luxembourg GDP seems likely to return to positive growth levels (as a quarterly variation) during the 2<sup>nd</sup> half and a recovery is in sight.

## Monthly publication of the state of the Luxembourg economy

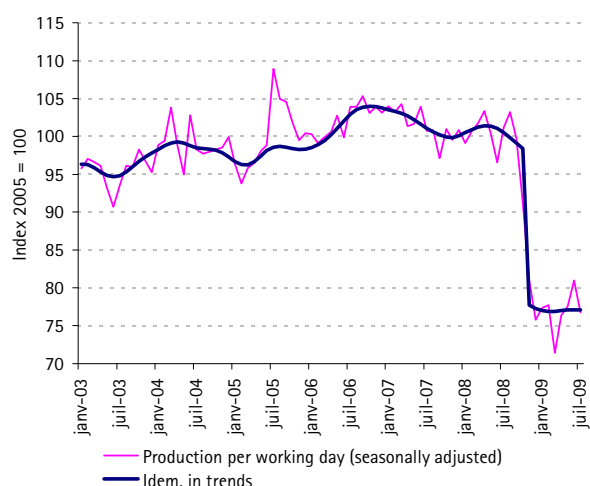


This favourable trend, however, should not lead us to be overly optimistic. From a purely mechanical point of view, it is much easier to accelerate from a position where activity has slowed significantly but it may take time for the economy to get back up to cruising speed or, in economic terms, its potential growth rate. Given the current state of affairs, growth levels should be looked at carefully alongside quarterly growth rates. Over the 1<sup>st</sup> half of 2009, GDP in terms of volume fell over 5% compared to the start of 2008, a record counter-performance that shows the seriousness of the situation. The forecasts from STATEC for 2009 predict a 4% fall in GDP, implying that activity levels for the next two quarters (Q3 and Q4) will be lower than for the 2<sup>nd</sup> half of 2008. With labour productivity remaining unchanged, this means that downward pressure on employment will continue to be felt throughout the second half of 2009 and probably into 2010 as well.

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L U X E M B O U R G

## Manufacturing

Trends in industrial output



Source: STATEC (Manufacturing activity survey)

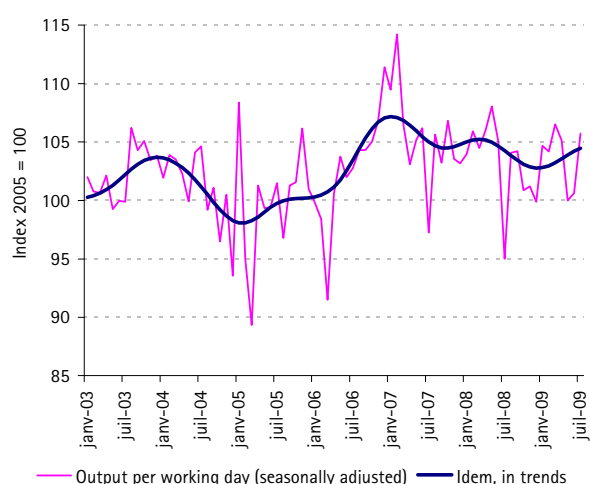
## Disappointing output levels in July

Industrial output based on seasonally adjusted figures fell 5% over one month in July. This is disappointing for at least two reasons: firstly, other eurozone countries posted rises during July. Secondly, it falls short of what was predicted by opinion surveys, which posited a favourable trend from July to September.

However, caution is advisable when it comes to interpreting this negative figure. In the first instance, it may yet be revised. In the eurozone for example, results were significantly revised upward – by 0.9% in June (instead of the 0.2% drop predicted in the previous estimate) and by 0.2% in July (instead of the predicted fall of 0.3%). Moreover, the fall in July in Luxembourg is mostly due to a marked decline in the production of capital goods, while related orders rose significantly, pointing to a recovery in the short term.

## Construction

Trends in output in the construction sector



Source: STATEC (Construction activity survey)

## A nice surprise

With a rise of about 5% compared to June (seasonally adjusted), output in the construction sector picked up significantly in July. This rise was surprising, given that nothing in the opinion surveys carried out over the summer suggested this trend. On the contrary, business owners' opinions were markedly negative between July and September.

However, the positive result for July does not point to any overall trend. Closer reading reveals that a number of large companies saw increased activity in July, mainly for civil engineering works. It remains to be seen whether this recovery, which may be linked to economic support packages, will last.

## Financial sector

Balance sheet at the end of the third quarter

	September 2008	September 2009	Variation in %
	In millions of EUR		In %
Interest margin <sup>1</sup>	4 986	5 066	1.6
Income from commission	2 859	2 436	-14.8
Other net income	-635	646	.
<b>Banking income</b>	<b>7 210</b>	<b>8 148</b>	<b>13.0</b>
Personnel costs	1 874	1 829	-2.4
Other overhead expenses	1 526	1 450	-5.0
<b>Overhead expenses</b>	<b>3 400</b>	<b>3 279</b>	<b>-3.6</b>
<b>Income before provisions</b>	<b>3 810</b>	<b>4 869</b>	<b>27.8</b>

Source: CSSF (provisional results)

<sup>1</sup> Including dividends received from subsidiaries

## Banks benefit from market recovery

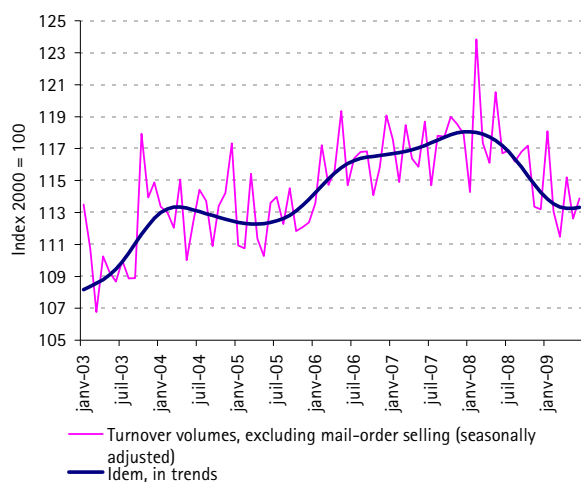
Banks' profit and loss accounts at the end of the 3<sup>rd</sup> quarter show a mixed trend. The interest margin continued to grow in the 3<sup>rd</sup> quarter but confirmed the slowdown noted over the two previous quarters. In contrast, income from commission is still behind 2008 levels, but the fall of 11.5% seen in the 3<sup>rd</sup> quarter was less marked than that noted during the 1st half of 2009 (-16.4%), pointing to a relatively favourable trend.

Most of the rise in banking output (and in income before provisions) still depends on growth in other net income, linked to the positive orientation of the financial markets, which impacts positively on the value of securities held by the banks.

Personnel and other costs were again cut during the 3<sup>rd</sup> quarter.

## Consumption

Trends in turnover in the retail trade



Sources: Administration de l'Enregistrement, STATEC

## Fewer retail sales

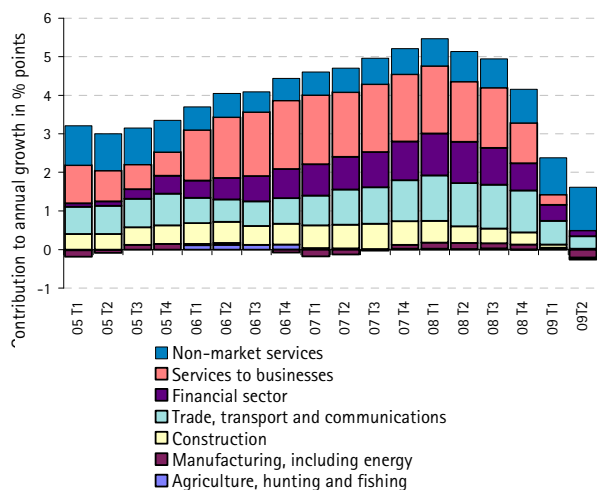
Retail sales have been trending downward since early 2008, falling 3% compared to 2008 over the first 6 months (in volume, seasonally adjusted figures and excluding mail-order sales).

The situation was more or less the same throughout Europe, with sales down 2% over the same period. The countries most affected in the eurozone were Greece (down 14%), Ireland (down 7%), Spain (down 6%), the Netherlands and Finland (both down 4%).

The decline seems to have eased somewhat from the 2<sup>nd</sup> quarter of 2009 on, both in Luxembourg and throughout the eurozone. However, European retail sales estimates point to new falls in July and August, which bodes ill for the upcoming results of companies active in Luxembourg.

## Labour market

Trends in domestic paid employment by sector



Source: Statec (Quarterly national accounts)

## Employment slows drastically in early 2009

During the second quarter of 2009, domestic paid employment rose just 1.3% on an annual basis, confirming the slowdown noted since 2008.

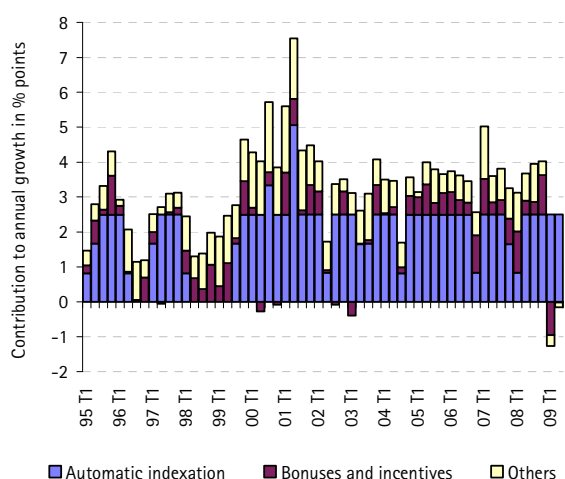
This trend is mainly due to the slowdown in employment in business services (down 0.1% in Q2'09 compared to a rise of 9.4% in the same quarter the previous year) and in the financial sector (up 1.2% against a rise of 8.5% a year ago).

However, most sectors have been affected by the slowdown and employment has slowed everywhere. Manufacturing posted the most significant fall in employment, with a fall of 1.9%, followed by construction (down 0.3%).

It was only in non-market services (public services, education, health and welfare services, domestic services, etc.) that employment performed well, rising 4.9% over one year in the second quarter compared to a rise of 3.5% in Q2'08.

## Inflation - wages

Trends in average wage costs and of its components



Source: IGSS

## Little increase in wages in early 2009

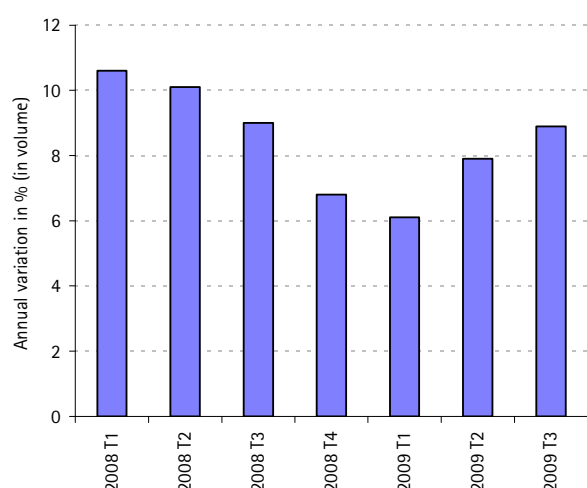
Over the second quarter of 2009, the average wage bill per person rose 0.4% compared to a rise of 2.7% a year ago. Considering that the automatic index-linked pay rises added 2.5% to the wage bill over this period, the trend is even more remarkable as it means that real wage costs have fallen significantly (down 2.1% over the second quarter of 2009).

The slowdown was mostly due to bonuses and gratuities (up 1.2% compared to a rise of 11.4% a year ago), even if the impact is less significant than during the first quarter (down 10.6%).

In terms of sector, the average wage bill per person fell significantly in the financial sector and manufacturing (down 4.4% and 1.5% respectively). In contrast, it rose slightly in construction (up 1.6% after falling 1.1% in the first quarter). As with paid employment (see above), wages in non-market services put in the best performance, rising 3.2% over one year during the second quarter of 2009.

## International

Trends in GDP in China



Source: National Bureau of Statistics of China

## Early recovery in emerging countries

The large emerging countries were not spared from the international crisis but are expected to undergo a much more dynamic recovery than what are termed the "developed" countries. China's growth accelerated again during the 3<sup>rd</sup> quarter (up 8.9% as an annual variation). The rapid recovery of the Chinese economy was made possible by a huge recovery plan, financed by trade surpluses generated in previous years.

After two quarters in recession, GDP in Brazil grew almost 2% (quarterly variation) in the 2<sup>nd</sup> quarter and is expected to end 2009 with positive growth. The rise in raw materials from April on was a major factor supporting activity in this country. It was the same for Russia (which has vast oil and gas reserves), which came out of recession during the 3<sup>rd</sup> quarter and where the unemployment rate fell sharply in September.

## Statistics table

	Jan-09	Feb-09	Mar-09	Apr-09	May-09	Jun-09	Jul-09	Aug-09	Aug-09	Average over the last three months	Same period previous year
	Annual variations in %, except where otherwise indicated										
<b>Activity</b>											
Industrial output per working day, in volume	-21.8	-23.6	-28.4	-25.5	-21.9	-15.3	-23.7	...	...	-20.4	-2.4
Construction output per working day, in volume	1.0	-1.0	1.8	-0.8	-6.8	-4.0	10.0	...	...	-0.6	-0.3
Turnover by volume of total retail trade	3.5	-8.7	-5.4	-0.7	-6.4	-2.4	...	...	...	-3.2	0.9
<b>Prices, wages</b>											
Consumer price index (IPCN)	0.5	1.2	0.3	0.3	-0.3	-0.3	-0.7	0.2	0.0	-0.1	4.3
Underlying inflation	2.4	2.7	2.2	2.3	2.1	2.2	2.0	2.1	2.0	2.0	2.8
Oil product index	-21.3	-17.3	-22.7	-23.5	-26.9	-26.7	-28.8	-21.6	-22.2	-24.3	26.1
Industrial producer price index	1.8	1.5	-1.1	-5.8	-7.6	-10.6	-14.5	-14.1	...	-13.1	6.7
Construction price index <sup>1</sup>	2.5	2.5	2.5	1.6	1.6	1.6	...	...	...	1.6	3.1
Average wage bill, per person (National accounts)	0.4	0.4	0.4	0.4	0.4	0.4	...	...	...	0.4	1.6
<b>Foreign trade</b>											
Exports of goods (volume)	-29.7	-26.7	-12.7	-27.9	-20.8	-19.3	-17.1	-10.6	...	-16.1	0.8
Imports of goods (volume)	-18.6	-19.3	-5.5	-21.0	-20.7	-9.2	-21.0	-13.4	...	-14.9	0.9
<b>Employment, unemployment</b>											
Domestic number of employees (IGSS)	3.3	2.6	2.2	1.9	1.6	1.0	0.8	0.8	0.1	0.6	5.1
National employment (IGSS)	2.3	1.8	1.7	1.6	1.5	1.2	1.0	0.8	0.6	0.8	3.3
Unemployment rate (% of working population, seas. adj.)	5.0	5.2	5.4	5.5	5.7	5.8	5.8	5.9	5.8	5.8	4.4

Sources: STATEC

Data grey coloured are estimates

1 Estimations based on half-yearly data

## Indicators

	Variation on previous quarter in %					
	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2
Eurozone- Growth in volume of GDP (European Commission)	0.8	-0.3	-0.4	-1.8	-2.4	-0.2
Luxembourg - Growth in volume of GDP (STATEC)	0.4	-1.0	-0.4	-2.9	-1.7	-0.3
	Annual variation in %					
	2007	2008	Forecast 2009		Forecast 2010	
Luxembourg - Growth in volume of GDP (STATEC)	6.5	0.0	-4.0		1.0	
GDP at current prices for 2008: EUR 39 347 million						
Minimum monthly salary (since 01/03/2009: EUR 1 682.76)						
Consumer price index (September 2009) - base January 1 <sup>st</sup> 1948: 747.11						
Half-yearly average of the index linked to base as at January 1 <sup>st</sup> 1948: 743.43						
Estimated deadline for next salary indexation: [July 2010; November 2010]						
Current account balance (2009 - 2nd quarter): EUR -348 million						
Resident population (01/01/2009): 493 500						

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