

# conjoncture flash

March 2009

Monthly publication of the state of the Luxembourg economy

## Growth for 2009 revised downwards

With business cycle indicators for the 4<sup>th</sup> quarter of 2008 and the 1<sup>st</sup> quarter of 2009 sliding much faster than expected, international institutions have radically revised growth forecasts downwards for Europe in 2009. STATEC, which is to publish its latest macroeconomic forecasts in May, has already predicted a recession in the Luxembourg economy in 2009 in an intermediary forecast.

## External demand much lower than expected

Most of the hypotheses underlying STATEC's autumn forecasts, which posited GDP growth of 0.5% for 2009, have proven overly optimistic.

Whereas the consensus forecast up until November 2008 was that GDP in the eurozone would stagnate in 2009, the scenario is now much more downbeat: since the end of January 2009, the European Commission and the IMF are predicting that GDP will fall by about 2% in the eurozone in 2009. In 2010, activity is expected to increase very slightly (+0.4%) and a real upswing is not expected until 2011.

These less favourable forecasts at European level will automatically affect those of Luxembourg, given its openness to international and European trade in particular. The fall in external demand for exports of Luxembourg goods and services (financial and other) is much sharper than expected and this, combined with the larger shrinkage in the financial markets – with leading stock market indices losing 15–20% of their value since the start of the year – will weigh heavily on exports.

However, low demand worldwide should mean less inflation than previously expected. The hypothesis regarding oil prices has been revised downwards and the European monetary stimulus provided through continuing interest rate cuts should be more substantial.

From a purely national perspective, STATEC has integrated the latest changes in the government's budgetary policy into this intermediary forecast – at least those measures that have been formally announced and can be quantified.

Macroeconomic forecasts 2008–2010

	2008	2009	2010
Trend in % (unless otherwise specified)			
GDP (in vol.)	0.7	-1.8	2.1
Total domestic employment <sup>1</sup>	4.9	1.4	0.6
Unemployment rate <sup>2</sup>	4.2	5.5	6.0
Consumer price index (NCPI)	3.4	0.2	1.7
Average nominal wage costs <sup>1</sup>	2.6	1.6	1.4

<sup>1</sup> National accounts concept

<sup>2</sup> Harmonised, i.e. on the basis of the ILO concept, in % of the working population

Source: STATEC (March 2009 forecast)

In particular, public investment for 2009 and 2010 has been significantly revised upwards compared to the autumn forecasts, as have welfare benefits for 2010, albeit to a lesser extent.

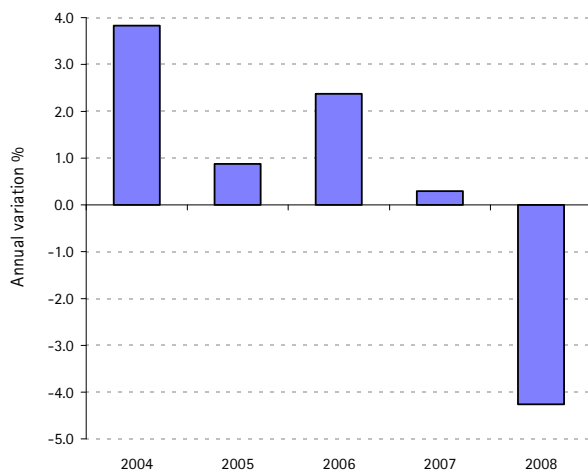
## GDP set to slump in 2009

The forecasts were adjusted based on these new hypotheses (see table opposite). Luxembourg GDP is expected to shrink by almost 2% in 2009 while growth forecasts for 2010 have only been marginally revised downwards (2.1%). National demand is expected to hold up relatively well in 2009 but is expected to suffer the effect of external demand in 2010: continuing falls in the labour market, with the unemployment rate set to climb to 6% of the working population by 2010, will have a particularly negative effect on household consumption. Inflation, which will suffer in 2009 from the effects of the high oil prices in 2008, will be limited to just 0.2% before bouncing back to the relatively low level of 1.7% in 2010. Finally, the downturn in the economic climate will also certainly affect public receipts.

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## Manufacturing

Industrial output per working day



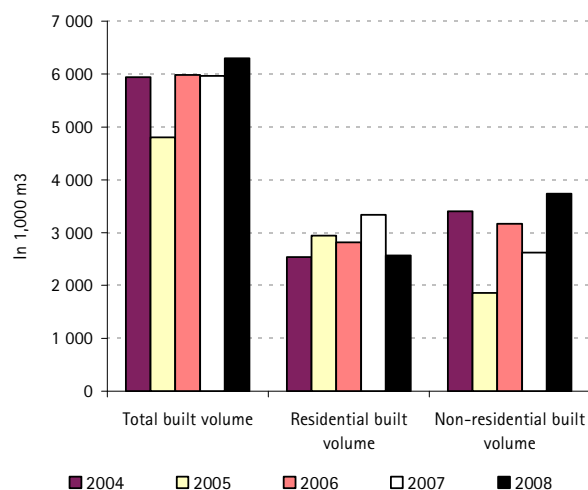
Source: STATEC

## A dispirited end to 2008

Industrial output in Luxembourg fell sharply over 2008 as a whole. With figures down by over 4% compared to 2007, Luxembourg has put in the worst performance in the eurozone, in what was a difficult year for all Member States (down approximately 2%). The 4th quarter, in particular, which saw demand for industrial products collapse rapidly, meant that annual results were cut back significantly. Here again, Luxembourg performed poorly compared to other European countries: output fell by 17% compared to the 4th quarter of 2007 (only Spain managed to perform almost as badly), compared to a downturn of just 9% in the eurozone as a whole. Germany, where industry performed very well in 2007, had to content itself with stagnant output in 2008 and was not able to avoid the downward trend in the 4th quarter (down 7.6%). Luxembourg suffered badly from the slump in iron and steel production, which was greater than 40% over one year in the 4th quarter.

## Construction

Planning permissions at the end of Q4



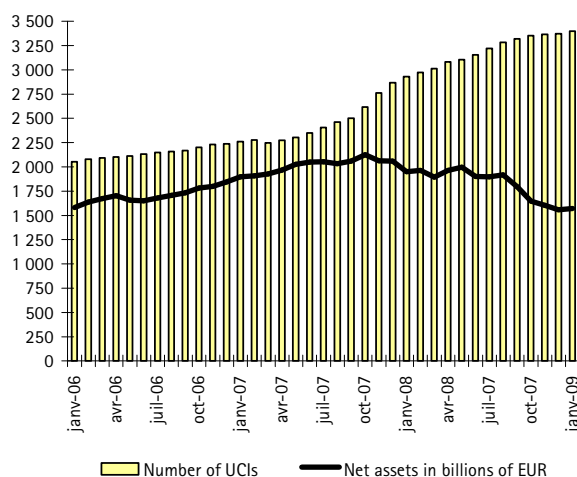
Source: STATEC

## Fewer housing units granted planning permission in 2008

The relative volume of projects granted planning permission rose more than 5% over 2008 as a whole. This positive result was mostly linked to the rise in non-residential projects (up 42% over 2008 as a whole), a trend observed since the start of the year that continued into the 4th quarter. These non-residential construction projects are expected to fall back later, given the economic situation (which does not favour investment) but should help sustain the construction sector over 2009 as a whole. On the other hand, housing construction is set to moderate and residential projects granted planning permission have fallen off significantly (down 23%). The number of housing units granted planning permission amounted to around 4,000 in 2008, well below the average of almost 4,700 units over the three previous years.

## Financial sector

Number of UCIs and net assets



Source: CSSF

## Respite for UCIs in January

Overall net assets of Luxembourg UCIs grew by 0.8% over one month in January (over one year, however, they fell by 20%). This brings an end to a downward trend lasting 4 consecutive months (September to December 2008), when falling values in financial securities combined with large-scale withdrawals of capital.

However, Luxembourg UCIs are not out of the woods yet, given that the leading indices in the main stock markets fell by over 5% in February 2009. However, since 10 March, these indices have recovered significantly, gaining 10-15% in the space of two weeks, a trend which provides some measure of comfort in the current economic situation.

## Services

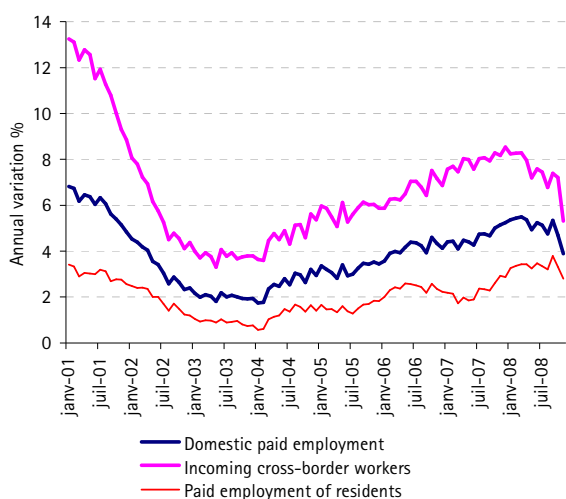
Services – turnover in value

SECTOR	2008	2008 Q3	2008 Q4
Annual variation %			
Hotel and catering	4.1	2.0	2.3
Transport and communications	7.7	9.9	7.3
Real estate, rentals and services provided to businesses	2.8	2.7	-1.9
Real estate activities	-18.2	-7.7	-21.2
Rentals without operator	6.3	4.0	3.8
R&D	4.9	7.9	0.0
Services provided mainly to businesses	10.8	6.0	2.9
Legal, accounting and management consultancy	11.0	10.1	0.4
Architecture and engineering activities	16.4	5.7	12.8
Control and technical analysis activities	5.3	6.4	6.5
Advertising	8.6	11.5	2.6
Selection and provision of personnel	-0.8	1.3	-11.0
Surveys and security	13.8	18.9	19.0
Cleaning activities	8.9	6.1	13.1
Misc. services provided mainly to businesses	9.6	-1.7	1.7

Sources: Administration de l'enregistrement, STATEC

## Labour market

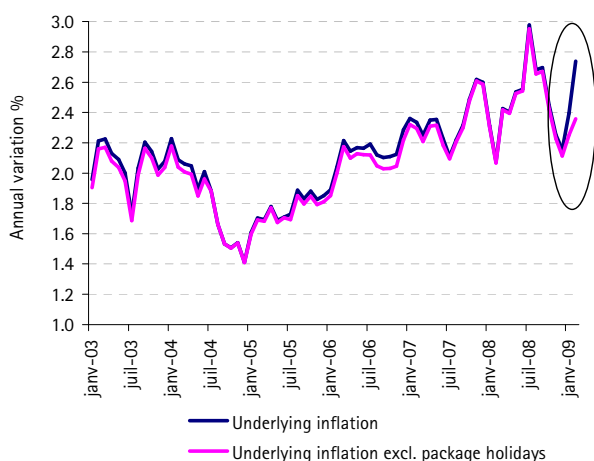
Trends in paid employment in Luxembourg



Source: IGSS

## Inflation – wages

Underlying inflation



Source: STATEC

## A less buoyant climate for services

In the main, turnover data for service companies (excluding the financial sector) fell during the 4th quarter of 2008.

While companies in the hotel and catering sector and in transport and communications seem to have stood up well overall, other sectors had a more difficult end to the year. The main activities affected by the economic downturn in the last quarter of 2008 included real estate and services provided mainly to businesses. In the latter sector, two types of activity headed up this decline: legal, accounting and management consultancy activities (whose business depends largely on the financial sector), and companies involved in the selection and provision of personnel (including temporary employment companies in particular).

## Sharp slowdown in paid employment in late 2008

According to the latest IGSS figures, employment slowed significantly in late 2008. Domestic paid employment fell from some 5.5% in early 2008 to about 5% at the end of the third quarter. While cross-border employment was already slowing down at the start of the year, paid employment of residents remained more or less stable over this period (at approximately 3.5%).

The data for October and particularly for November show that the slowdown is even more significant. Growth in domestic paid employment lost one percentage point in November compared to October and rose by 'only' 3.9% (5.3% for cross-border employment, 2.8% for paid employment of residents). Part of this slowdown is due to the sharp falls in temporary employment (down 16.3% in November): apart from temporary workers, paid employment rose by 4.5% in November, compared to a little over 5.0% in the previous months.

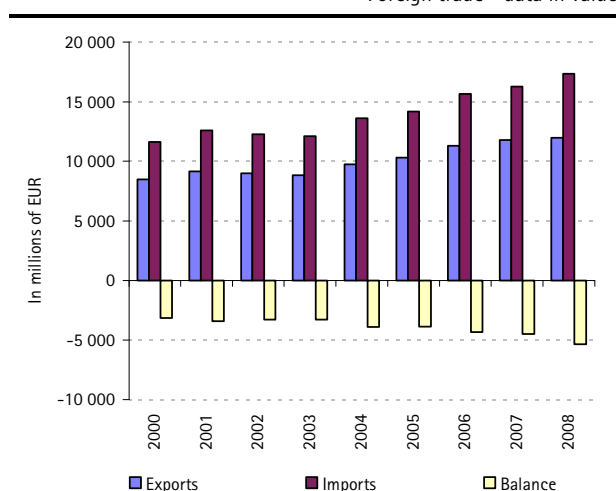
## A technical rise in underlying inflation

Underlying inflation, a sub-series of the general index which excludes oil and other goods whose prices are determined on the international markets, slowed down progressively over the 2nd half-year of 2008, slipping from 3.0% in July to 2.2% in December. This trend is in line with a gloomier international economic environment.

However, in early 2009, this index rose significantly (2.4% in January and even 2.7% in February). The rise was due mainly to methodological changes in how package holidays are treated. Since 1 January 2009, holiday prices are taken on a monthly basis as opposed to twice yearly as was done previously. This means that the seasonal nature of holiday prices is recognised more efficiently. Thus, 0.38 percentage points of the 2.7% in underlying inflation in February are due to this change (February holidays (carnival)).

## Foreign trade

Foreign trade – data in value



Source: STATEC

## Trade deficit rises substantially

In 2008, the foreign trade deficit increased by approximately 20% compared to the previous year, i.e. EUR 5,358 million.

Exports rose 1.7% in value but this was mainly concentrated in EU countries (exports outside the EU fell by 6.7%). Germany was responsible for over half of this increase, notably through price increases in metal products. Imports in value rose 6.6% in 2008, with EU partners contributing significantly, particularly with goods from Belgium, linked to the hikes in oil prices up until the summer of 2008.

Alongside these price effects, 2008 was marked by a fall in trading volume, both for imports and exports (falling for the 2nd consecutive year).

## Statistics table

	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09	Feb-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	-3.4	1.1	2.7	0.8	-9.7	-16.0	-24.5	...	...	-16.6	-0.8
Construction output per working day, in volume	-1.9	-2.8	-4.6	0.3	-5.3	-2.8	4.7	...	...	-1.8	-4.2
Turnover by volume of total trade	70.5	68.9	46.3	71.2	31.9	-18.5	-13.7	...	...	-1.9	7.0
Turnover by volume of total retail trade	-1.4	0.5	-2.5	-1.6	-1.5	-6.4	...	...	...	-2.5	2.7
<b>Prices, wages</b>											
Consumer price index (IPCN)	4.3	4.9	4.0	4.0	3.3	2.0	1.1	0.5	1.2	0.9	3.3
Underlying inflation	2.6	3.0	2.7	2.7	2.4	2.3	2.2	2.4	2.7	2.4	2.3
Oil product index	29.6	31.9	23.3	23.3	15.0	-0.9	-12.7	-21.3	-17.3	-17.2	18.9
Industrial producer price index	9.7	14.5	13.9	12.9	12.5	9.1	4.3	...	...	8.6	6.7
Construction price index <sup>1</sup>	3.1	3.1	3.1	3.2	3.2	3.2	3.3	3.3	3.3	3.3	3.0
Average wage bill, per month, per person	5.3	4.2	2.9	4.7	5.0	3.2	...	...	...	4.3	3.6
<b>Foreign trade</b>											
Exports of goods	-5.5	-0.2	-6.2	-0.1	-13.0	-16.5	-19.1	...	...	-16.1	-2.9
Imports of goods	-11.2	-13.1	-21.4	3.0	-5.3	-5.2	-7.2	...	...	-5.9	-1.1
<b>Employment, unemployment</b>											
Domestic number of employees	5.2	5.1	4.8	5.3	4.7	3.9	3.9	3.1	2.9	3.3	5.4
National employment	3.3	3.2	3.1	3.6	3.2	2.7	2.5	2.3	2.1	2.3	3.1
Unemployment rate (% of working population, seasonally adjusted)	4.4	4.4	4.4	4.4	4.5	4.6	4.8	5.0	5.2	5.0	4.2

Sources: STATEC

Data grey coloured are estimates

<sup>1</sup>Estimations based on half-yearly data

## Indicators

	Variation on previous quarter in %					
	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4
Eurozone- Growth in volume of GDP (European Commission)	0.7	0.4	0.7	-0.2	-0.2	-1.5
Luxembourg - Growth in volume of GDP (STATEC)	0.6	0.9	0.1	1.2	-1.9	...
	Annual variation in %					
	2006	2007	Forecast 2008		Forecast 2009	
Luxembourg - Growth in volume of GDP (STATEC)	6.4	5.2	0.7		-1.8	
GDP at current prices for 2007: EUR 36 409 million	Minimum monthly salary (since 01/01/2009: EUR 1 641.74)					
Consumer price index (February 2009) - base January 1 <sup>st</sup> 1948: 740.36	Half-yearly average of the index linked to base as at January 1 <sup>st</sup> 1948: 739.53					
Current account balance (2008 - 3rd quarter): EUR 348 million	Resident population (01/01/2008): 484 000 (estimation)					

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