

conjoncture flash

June 2009

Monthly publication of the state of the Luxembourg economy

Price rises in raw materials

After growing strongly in recent years and literally taking off during the 1st half of 2008, prices of raw materials fell sharply thereafter. Since March, however, they seem to be climbing back upwards.

Good or bad news?

Prices of raw materials rose rapidly in early 2008. Oil prices were the reason most often cited for rising inflation in 2008. However, the explosion in prices affected all raw materials (fossil, mineral and agricultural).

From August 2008 on, these prices fell rapidly¹, falling back at the end of the year to levels not seen since 2007. Up to March 2009, prices stabilised somewhat, with the price per barrel of oil holding firm at around USD 50. From mid-March on, prices of raw materials started to climb back up. Further, the return of investors to these markets coincided almost simultaneously with the recovery observed in the equity markets.

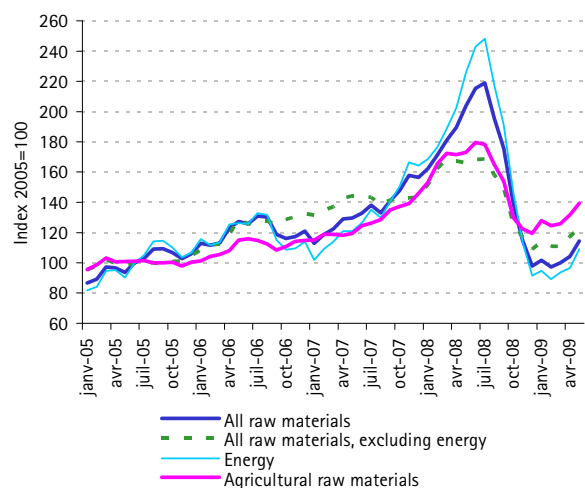
This rise in the prices of raw materials is therefore both good and bad news. It could be interpreted as a sign of recovery, i.e. a rise in expected demand and therefore more sustained global activity. At the same time, it sends out a negative signal in terms of consumption: in the current crisis, falling inflation – and its positive effect on purchasing power – was one of the rare things sustaining growth. The fact that inflation has been so low in recent months is due simply to falling prices in raw materials, mainly oil, compared to 2008 prices.

What will be the effects in Luxembourg?

The consequences of recently observed trends in the costs of raw materials relate mainly to industrial prices and consumer prices.

Industrial output prices rose strongly for 4 years in Luxembourg (up 8.5% per year from 2004 to 2007), mainly due to iron and steel products, with metal prices rising. These prices have fallen since the 3rd quarter of 2008 (except for machinery and equipment, and drink and tobacco). In April 2009, they fell about 12% compared to their peak in August 2008.

Trends in raw material prices



Source: IMF – Primary Commodity Prices (latest data: May 2009)

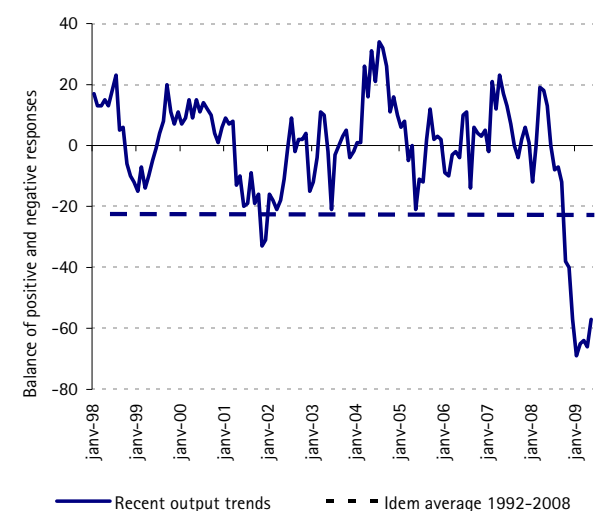
These prices are expected to stabilise over the coming months and then recover, by how much which will depend on trends observed in raw materials.

For consumer prices, as previously mentioned, the downward trend was felt mostly in oil prices (fuel, heating oil, etc.). Food prices, on the other hand, are not falling as yet, but they have more or less stabilised in recent months. They had grown strongly in 2007 and 2008, mainly due to rising cereal prices. This at least was the argument advanced by distributors to justify price rises for products such as bread, flour, pasta products, dairy products or meat. As prices of primary agricultural products had largely fallen back between mid-2008 and early 2009 (cereal prices lost 20–50% depending on type over this period), the price of foodstuffs is expected to fall in the coming months – unless distorted by competition – naturally in proportion to the content of raw materials in the final product.

¹ For more information on this, see "Prices of raw materials fall", Note de Conjoncture No. 2-08, pp. 49–54, STATEC, November 2008.

Manufacturing

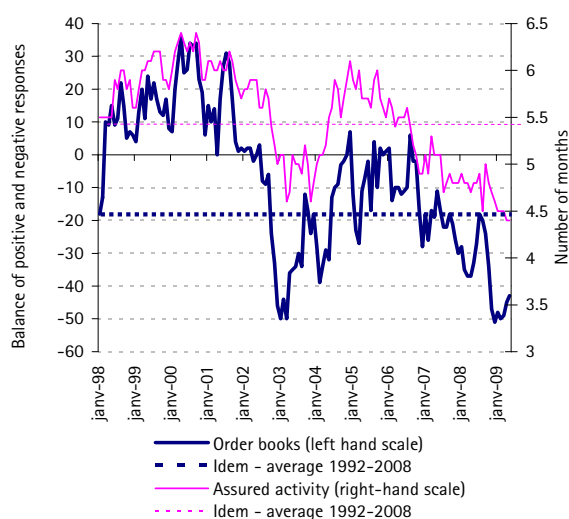
Economic survey on manufacturing



Source: STATEC (activity survey)

Construction

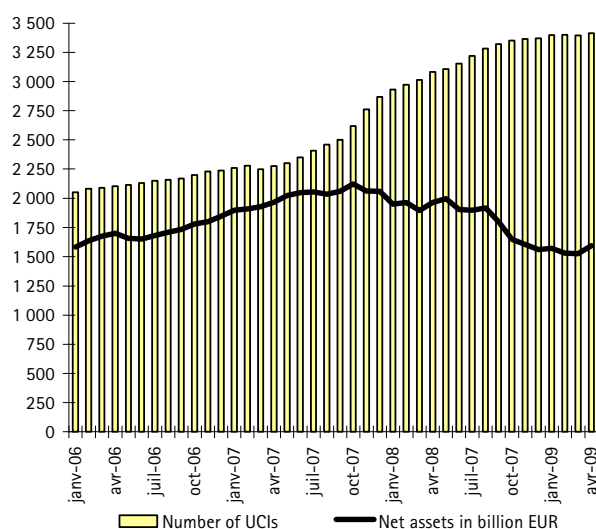
Economic survey on construction



Source: STATEC (activity survey)

Financial sector

Number of UCIs and net assets



Source: CSSF

Has the low point been reached?

Manufacturers' feelings about recent output trends show a recovery compared to the May 2009 survey. A similar trend is observed as regards future output and order books.

However, the average improvement observed using these indicators remains modest and above all it comes from historically low levels. According to activity surveys, industrial output for the 1st quarter was down some 25% compared to the results for early 2008. According to businesses, an almost identical drop is to be expected over the 2nd quarter, which means output levels will stabilise.

Astonishingly, businesses proved much more optimistic in May as regards employment trends, but this remains to be confirmed

Falling activity but less than elsewhere in Europe

Construction businesses' opinions on activity and orders improved in May. Part of this rise, however, was due to seasonal phenomena, there being more construction activity from the Spring onwards. Assured activity expressed in terms of months – at 4.4 months – remains historically low (the long-term average is about 5.5 months).

Output fell more than 1% year-on-year during the 1st quarter and a similar fall is expected during the 2nd quarter. The fall is most noticeable in structural building work, with specialised work continuing to rise. However, compared internationally, Luxembourg is faring rather well: output in the construction sector throughout the eurozone fell by close to 10% over one year during the 1st quarter of 2009.

A more serene environment

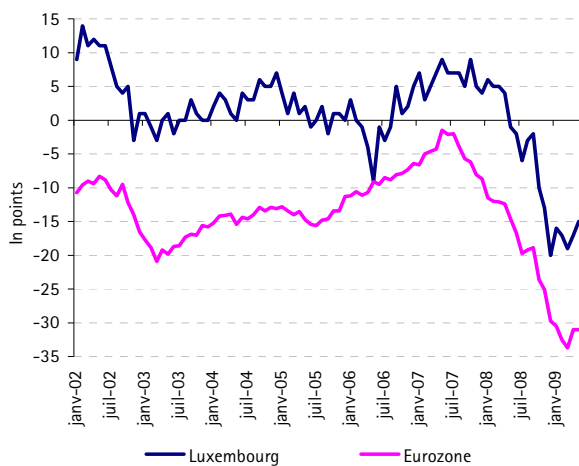
Net UCI assets grew again in April 2009, mainly due to rising markets. Of the EUR 67 billion in additional assets, approximately EUR 60 billion is due solely to market movements. The difference, which represents net capital investment, amounts to some EUR 7 billion for this month, the best performance since July 2008.

Favourable trends in the equity markets in May, with gains of between 15 and 25% on the major leading indices (DJ Eurostoxx50, Dow Jones US, Nikkei), should again boost upcoming UCI results.

Furthermore, the total amount of bank balances finally stabilised in April, after falling for 5 consecutive months.

Consumption

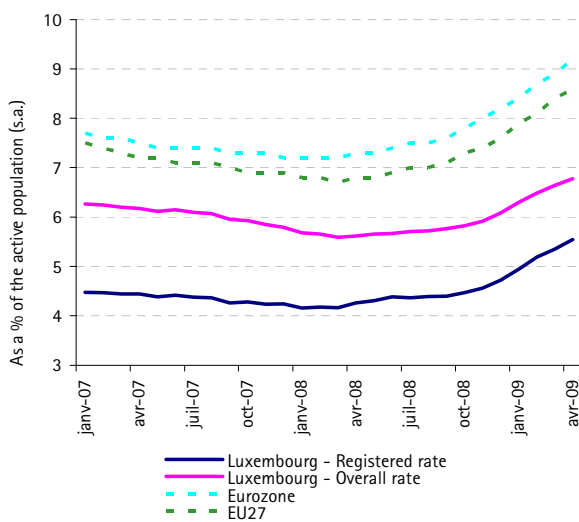
Consumer confidence



Sources: BCL, EUROSTAT (seasonally adjusted data)

Labour market

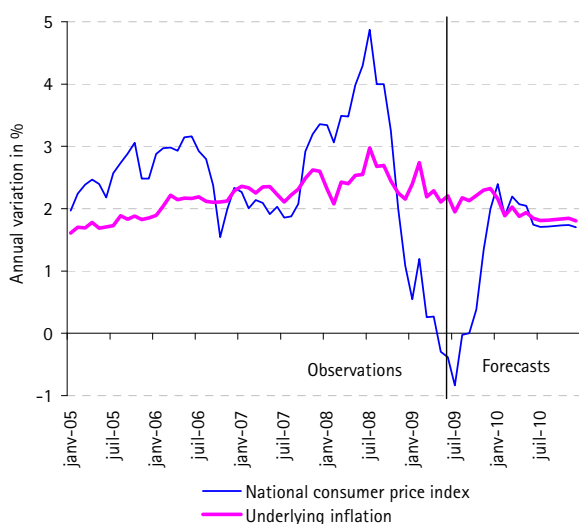
Unemployment rates in Luxembourg and Europe



* s.a. = seasonally adjusted Sources: Eurostat, ADEM, STATEC

Inflation - wages

Inflation: Observations and Forecasts



Source: STATEC

Confidence grows

Consumer confidence in Luxembourg bounced back in May 2009. This was linked in part to generally improving economic prospects but more so to more optimistic expectations with regard to unemployment. This is the first time in nine months that consumers expect unemployment to improve (NB: this data is seasonally adjusted). However, nothing points to a fall in the unemployment rate in the coming months as it is in an upward phase (see below). However, this downturn may mean a relative improvement, i.e. unemployment may rise less rapidly.

In May, consumers also had a less negative view of the general economic situation in the near future, although not of their own personal financial situation.

European unemployment up

Throughout the eurozone, the unemployment rate has shown a significant upward trend in recent months: 9.2% in April 2009 compared to some 7% a year ago. In Luxembourg, the rate reached 5.7% in May 2009 (6.9% if people in job schemes are also taken into account), as against 4.3% (and 5.7%) this time last year.

Unemployment is therefore continuing to accelerate and is expected to rise even more in the coming months, at national, European and international level. The current economic crisis is international and all countries, regardless of their structural difficulties, are affected.

The countries currently most affected by the deteriorating labour market are Denmark, Spain and Ireland – in Ireland the unemployment rate has risen from 5.2% to 11.1% in the space of a single year. In contrast, Belgium, Germany, the Netherlands and Austria seem less affected for the moment.

Negative inflation for mid 2009

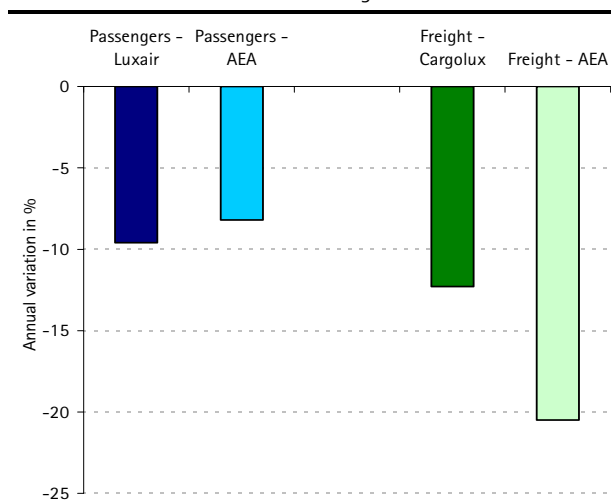
In May 2009, the inflation rate was negative for the first time since the eighties (down 0.3% on an annual basis).

This negative rate is explained by the sharp drop in oil prices compared to the same period last year (down 26.9%). In fact, although oil prices have risen dramatically in recent months (while prices per barrel of oil remained below USD 50 for the first quarter, it is currently fluctuating around USD 70), they remain well below levels recorded a year ago (USD 123 per barrel in May 2008 and even USD 134 in June).

Given this situation, it would be wrong to talk about a deflationary trend. In fact, as can be seen in the underlying inflation rate (2.1% in Luxembourg), prices for other goods and services continue to rise. According to the latest forecasts from STATEC, the rate will remain negative throughout the summer months, coming back up to 2% at the end of the year.

Transport

Trends in air traffic during the first 4 months of 2009



Source: Association of European Airlines

Air traffic down

According to the data gathered from members of the AEA (Association of European Airlines, which has 34 member companies), early 2009 was marked by a sharp drop in air transport activity.

Passenger traffic lost over 8% over the period between January and April compared to 2008. The impact of the crisis is still being felt in freight volumes. According to the AEA, May 2009 is set to be very difficult but the situation is likely to improve thereafter.

In this difficult economic climate, two large Luxembourg companies have posted contrasting results. Luxair's performance remains slightly below the average for air companies in terms of passenger transport, without drifting too far from the norm. Cargolux, on the other hand, performed well, although also affected by the fall in global trade and freight volumes.

Statistics table

	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-09	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	3.4	-9.7	-17.2	-27.7	-22.1	-22.5	-26.7	...	...	-23.9	-4.3
Construction output per working day, in volume	-0.5	-4.9	-1.8	5.1	1.8	-5.4	0.1	...	...	-1.3	-2.4
Turnover by volume of total trade	71.2	31.9	-12.3	-11.0	-11.9	-15.2	4.2	...	...	-7.2	18.4
Turnover by volume of total retail trade	2.8	-3.9	2.0	-4.1	-1.5	-10.1	...	...	...	-5.1	2.1
Prices, wages											
Consumer price index (IPCN)	4.0	3.3	2.0	1.1	0.5	1.2	0.3	0.3	-0.3	0.1	3.7
Underlying inflation	2.7	2.4	2.3	2.2	2.4	2.7	2.2	2.3	2.1	2.2	2.5
Oil product index	23.3	15.0	-0.9	-12.7	-21.3	-17.3	-22.7	-23.5	-26.9	-24.4	22.5
Industrial producer price index	7.1	32.8	4.1	0.2	2.0	2.2	-1.2	-5.8	...	-1.6	1.6
Construction price index ¹	3.0	3.1	3.1	3.1	3.2	3.2	3.2	...	...	3.3	3.0
Average wage bill, per month, per person	4.7	5.0	3.2	4.0	...	...	...	...	...	4.1	3.3
Foreign trade											
Exports of goods	-0.1	-13.0	-16.5	-24.3	-33.0	-18.6	-13.1	...	...	-21.6	-3.4
Imports of goods	3.0	-5.3	-5.2	-9.6	-12.2	-15.8	-10.2	...	...	-12.7	0.2
Employment, unemployment											
Domestic number of employees	5.3	4.7	3.9	4.0	3.3	2.6	2.7	2.2	1.9	2.3	5.3
National employment	3.5	3.2	2.9	3.2	3.0	1.9	2.0	1.8	1.7	1.8	3.2
Unemployment rate (% of working population, seasonally adjusted)	4.4	4.5	4.6	4.7	4.9	5.2	5.3	5.5	5.7	5.5	4.2

Sources: STATEC

Data grey coloured are estimates

¹Estimations based on half-yearly data

Indicators

	Variation on previous quarter in %					
	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1
Eurozone- Growth in volume of GDP (European Commission)	0.4	0.7	-0.3	-0.4	-1.8	-2.5
Luxembourg - Growth in volume of GDP (STATEC)	0.5	-1.0	0.2	-0.6	-3.6	...
	Annual variation in %					
	2007	2008	Forecast 2009		Forecast 2010	
Luxembourg - Growth in volume of GDP (STATEC)	5.2	-0.9	-4.0		1.0	
GDP at current prices for 2008: EUR 36 662 million	Minimum monthly salary (since 01/03/2009: EUR 1 682.76)					
Consumer price index (May 2009) - base January 1 st 1948: 741.59	Half-yearly average of the index linked to base as at January 1 st 1948: 737.49					
Current account balance (2008 - 4th quarter): EUR 260 million	Resident population (01/01/2009): 493 500					

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