

A slow recovery from recession

The main scenario adopted by STATEC forecasts slack growth in the euro zone in 2014, leading to a 1.2% rise in GDP in volume, assuming that the financial crisis will continue to subside with no major upsets.

Luxembourg GDP growth in volume is expected to reach 2.0% in 2013 and 2.7% in 2014, mostly thanks to exports. Domestic demand will remain constrained for various reasons:

- private consumption will remain lacklustre, due to sluggish growth in real wages and rising unemployment;
- some physical investment components are showing signs of flagging.

On the labour market, another slight rise in unemployment is expected in 2014 (reaching an annual average of 7.2%), whereas employment growth is set to peak at 1.7%, with most momentum coming from non-market services or those with little exposure to international competition.

Assuming oil prices remain stable, STATEC anticipates average annual inflation of 1.5% in 2014 (NCPI) (compared to 1.7% in 2013). Nominal wage growth (per capita) is expected to be in line with the sliding wage scale (up 2.5%), as the economic situation does not favour any recovery in wages, excluding the automatic wage indexation system.

The forecasts for the public finances are identical to those of the Note au Formateur, drawn up by the Forecasting Committee with the help of STATEC. Thus, in 2013, public receipts are expected to rise by 4.8% and expenditure by 4.0%. This means that the balance of public finances would be -0.2% of GDP, a slight improvement on 2012 (balance at -0.6%). If policy remains unchanged, the balance will be -0.4% in 2014.

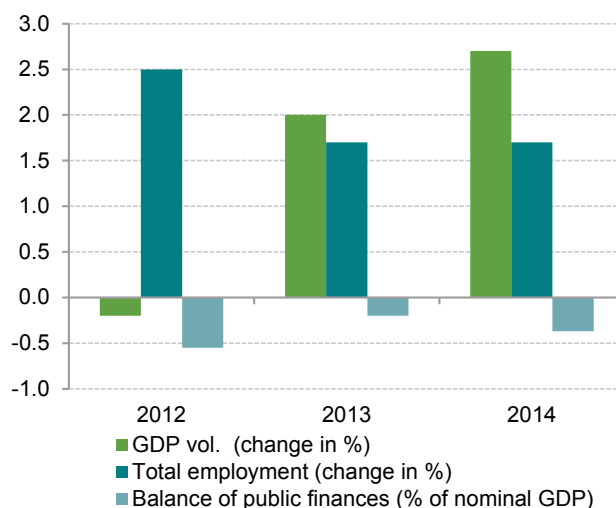
International and domestic risks

Underlying this forecast negative risks are not negligible. It should be mentioned the usual reservations, taking origin in the crisis in the euro zone, which seems likely to re-emerge at any time, but also the dangers of a new budget crisis in the U.S. or unanticipated slowdown in emerging countries.

Some also put forward the "positive" that the recovery, once in place, could strengthen more than expected, building on a virtuous spiral, thanks to a boost of confidence related to the successful implementation of banking union in Europe, in particular, and restart bank lending, following.

Another downside risk, domestic, is formed by the introduction of automatic exchange of financial assets held by non-residents. To assess this risk, STATEC performed simulations

Macro-economic forecasts



Source: STATEC (NDC forecasts 2-2013)

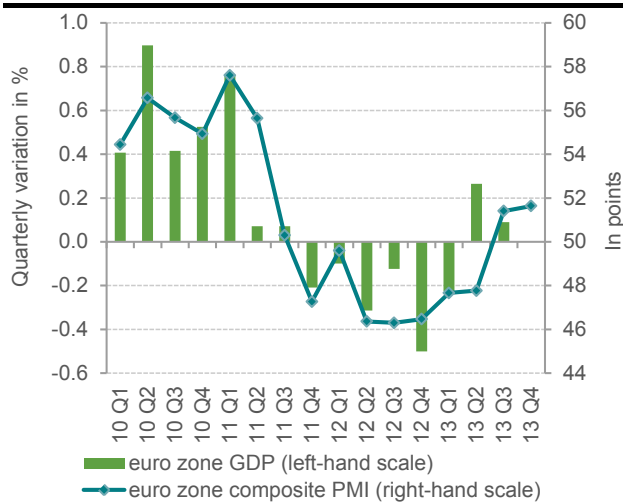
on the assumption that funds under management in the private banking sector will fall by EUR 5 to 15 billion and that profitability in the sector will deteriorate. These calculations give an approximation of the extent of the negative impact on nominal added value in the financial sector (about 5%), GDP in volume (about 1%), total employment (up to 2,000 people) and public finances (balance between -0.2 and -0.3 percentage points). The simulations were carried out on the basis of all things being equal, excluding the possibility that exiting funds could be offset by inflows of new capital or rising stock markets.

Observation of recent figures is vital in order to assess whether the assumptions underlying these simulations are well-founded. When we compare the third and first quarters of 2013, it is clear that quarterly figures on household deposits are indeed down, but this drop is not as yet very significant, just EUR 900 million or 1.5%. Therefore, there is reason to believe that the withdrawals have been at least partially offset by the arrival of new customers. What is more, the rise of some 12% in European stock market indices since March also has helped make up the shortfall.

Thus, STATEC has not as yet significantly reduced its growth scenario for 2014 but, if there are further falls in net assets under management between now and the end of the year, STATEC could be forced to reduce its growth assumptions for the financial sector, with knock-on effects for the economy as a whole.

International

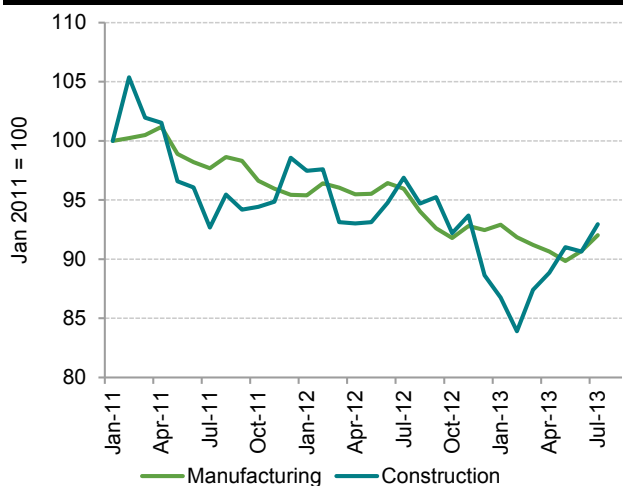
euro zone: GDP and the PMI index



Sources: Eurostat, Markit Economics, STATEC (PMI estimate for Dec 2013)

Manufacturing and Construction

Output per working day



Source: STATEC (seasonally adjusted figures, smoothed over 3 months)

Construction

Building permits - volume of construction projects (at the end of the 1st half of the year)

Source: STATEC

Eurozone: a return of timid growth

After 6 consecutive quarters of recession, the euro zone has finally pulled out of recession, with 0.3% over one quarter in the 2nd quarter of 2013, and then 0.1% in the 3rd quarter. The slower growth in the 3rd quarter demonstrates how unstable this current rally is, in line with confidence indicators, which, although improved since the spring, remained at the end of November 2013 at levels compatible with only weak growth (0.2% growth seems at present to be the most optimistic possibility).

There remain significant gaps between north and south within the euro zone, in terms of growth and even more so in terms of unemployment, but activity is recovering in several countries, including Spain, which exited recession in the 2nd quarter, and Portugal (since the 2nd quarter). At the end of the 3rd quarter, Italy was still in recession but only just, with a 0.1% fall over one quarter.

Output is up but remains low

Manufacturing and construction have entered a recovery phase in terms of output. The most recent output figures (from business surveys carried out in August 2013) confirm this more favourable trend.

This trend was already visible in construction in the 2nd quarter, but it must be remembered that this was due to the fact that activity in the 1st quarter was heavily penalised by particularly unfavourable weather conditions. Therefore, the summer figures show that the rally also had a cyclical element. In manufacturing, the improvement was relatively widespread and mainly linked to computer, electronic and optical products, electrical equipment, the food industry, glass & ceramic manufacturing, and iron & steel.

Despite this recent rally, output levels remained very low at the end of August, particularly in manufacturing.

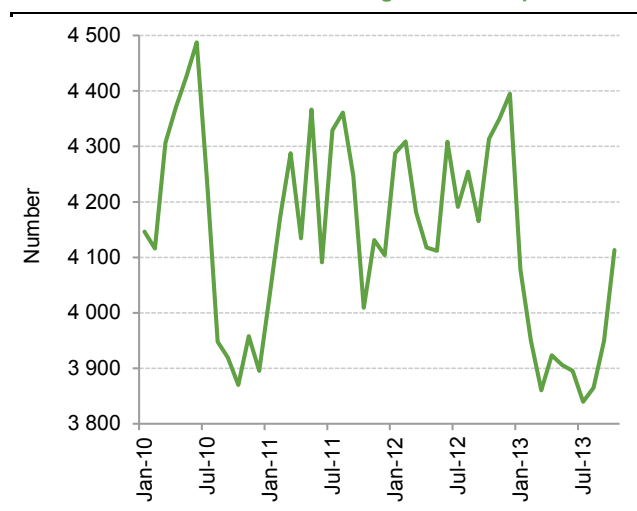
Fewer homes but more building

Building permits granted over the 1st half as a whole sent out a few encouraging signs. After falling significantly last year by 6%, the volume of construction projects relating to these authorisations rose 13% over one year in the first six months of 2013. Most of this rise was due to the non-residential sector, and unfortunately the reverse was true for residential construction (i.e. home-building).

In the 2nd quarter in particular, a number of major projects were given the go-ahead, including several administrative buildings in Luxembourg City, commercial buildings and a warehouse in the south of the country.

Consumption

New registrations of private cars



Sources: SNCT, STATEC (seasonally adjusted figures)

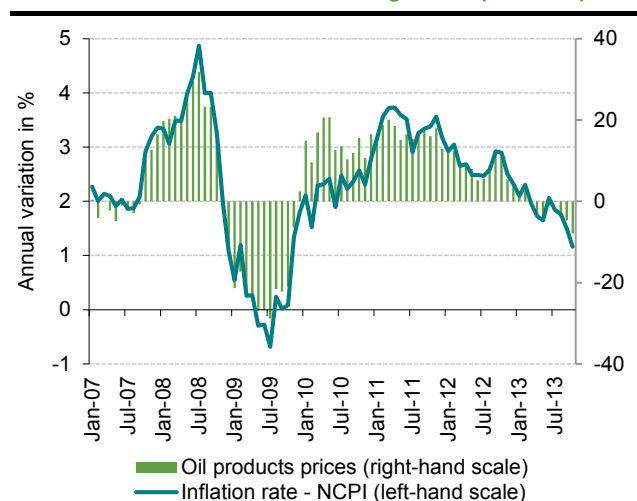
Recent rally in registrations

New registrations of private and mixed-use cars bounced back in September and October. The sharp fall in car sales observed in early 2013 was partly due to a technical effect (linked to the ending of the car scrappage scheme on 1 January, which boosted sales in late 2012), but the fact that they remained at low levels up to August was beginning to become worrying.

Even with these latest figures, the drop in registrations compared to 2012 remains significant, falling some 7% over the first 10 months of the year, a counter-performance very similar to that seen throughout the euro zone over the same period.

Inflation

Inflation in Luxembourg and oil products prices



Source: STATEC

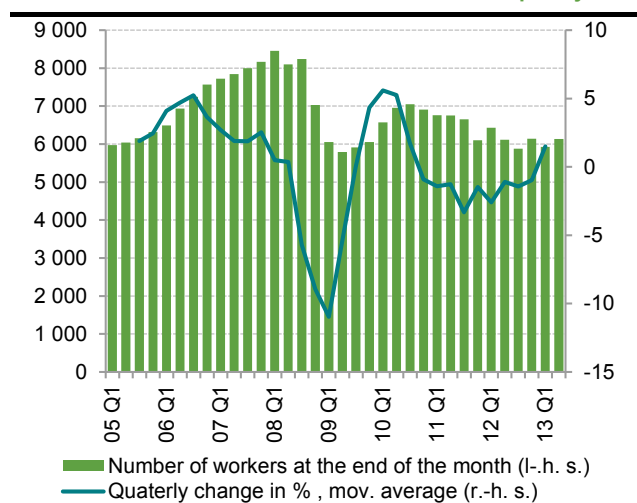
Oil prices have driven inflation below 2%

Inflation fell to 1.2% in October in Luxembourg, the lowest level in four years. It has been slowing since 2011 as a result of the slowdown in oil prices. Over the current year, oil prices have been trending negatively year-on-year, like in 2009.

Thus, over the first 10 months of 2013, diesel, petrol and liquid fuel (heating oil) made the most significant contributions to bringing down the inflation rate. This downward pressure was boosted by the appreciation of the euro against the US dollar, peaking at USD 1.38 in late October. It has fallen back slightly since then, to about USD 1.35 at end-November, due to the ECB's dropping of its main leading rate to 0.25%, the lowest ever recorded.

Labour market

Temporary work



Sources: IGSS, STATEC (seasonally adjusted figures)

A positive signal for temporary employment

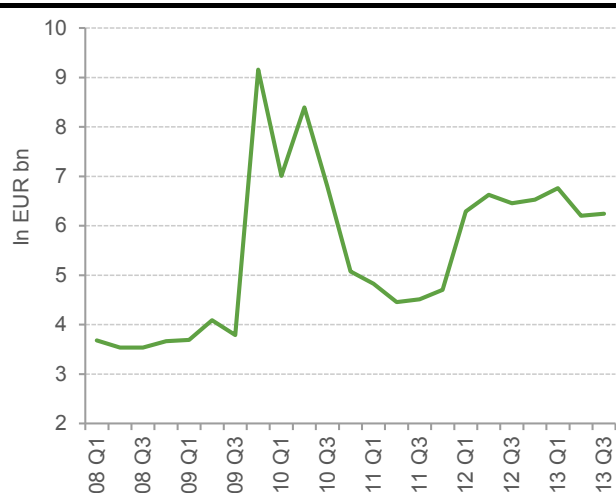
Numbers of temporary workers fell considerably in the past 2 years, particularly from mid-2011 to mid-2012. In early 2013, although there was no clear recovery in temporary employment, a more favourable trend was evident all the same, which is a positive signal for the labour market given that the temporary employment market acts as a precursor for overall employment and unemployment.

The unemployment rate stood at 7.0% of the working population in October 2013, evidence of a certain amount of stabilisation since the summer, after rising sharply in the early part of the year. Domestic employment rose close to 1.8% (on estimate) over one year in the 3rd quarter, very slightly above the two previous quarters (1.6% in Q1 and 1.7% in Q2).

Financial sector

Insurance: income lower since the 2nd quarter

Insurance premium income - quarterly figures



Sources: Commissariat aux Assurances, STATEC (seas. adj. figures)

Over the first 3 quarters of 2013, premiums collected by Luxembourg insurance companies fell very slightly, by 0.15%, compared to last year.

While premiums were still rising in the 1st quarter (based on seasonally adjusted figures), they fell back somewhat after that. This downturn was noted in life insurance (which accounts for 85% of total premiums) and affected both unit-linked and conventional life insurance products. Non-life insurance continued to grow strongly, posting a 10.5% gain on 2012 (over the first three quarters) after climbing some 15% last year. This trend, mainly linked to the boom in international business (excluding marine insurance), has offset the drop in life insurance.

Trend chart

	Feb-13	Mar-13	Apr-13	May-13	Jun-13	Jul-13	Aug-13	Sep-13	Oct-13	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	-4.5	-8.0	-2.4	-4.7	-8.4	-4.7	2.0	...	...	-4.1	-1.5
Construction output per working day, in volume	-10.1	-9.6	2.1	-4.4	-3.7	-4.4	-4.9	...	...	-4.2	5.2
Turnover by volume of total retail trade	-6.2	-3.2	-0.6	-1.8	-3.0	1.3	-0.5	...	...	-0.7	2.6
Prices, wages											
Consumer price index (NCPI)	2.3	2.0	1.7	1.6	2.1	1.8	1.8	1.5	1.2	1.5	2.8
Underlying inflation	2.3	2.2	2.3	2.3	2.4	2.0	2.3	2.1	2.0	2.1	2.1
Oil product index	2.5	-0.6	-3.9	-5.0	-1.0	-0.1	-3.8	-4.7	-7.9	-5.5	10.4
Industrial producer price index	-1.1	-1.5	-2.5	-2.8	-3.3	-3.6	-3.3	-3.3	...	-3.4	0.9
Construction price index ¹	2.2	2.2	1.9	1.9	1.9	...	...	...	...	1.9	2.9
Average wage bill, per person (National accounts)	2.3	2.3	2.7	2.7	2.7	...	...	...	...	2.7	2.3
Foreign trade											
Exports of goods (volume)	-5.5	-10.3	6.6	3.9	-7.1	0.0	-4.2	-3.7	...	-2.6	-4.7
Imports of goods (volume)	8.6	-9.8	10.4	-8.9	-4.2	-6.6	-9.8	-7.1	...	-7.9	4.2
Employment, unemployment											
Domestic number of employees	1.7	1.5	1.4	1.9	1.8	1.8	1.8	1.9	2.0	1.9	2.3
National employment	1.7	1.5	1.6	1.8	1.8	1.7	1.9	1.9	1.9	1.9	2.4
Unemployment rate (% of working population, seas. adj.)	6.6	6.7	6.8	6.9	6.9	7.0	6.9	7.0	7.0	6.9	6.2

Source: STATEC

Data blue coloured are estimates

¹ Estimations based on half-yearly data

Indicators

Variation on previous quarter in %						
	2012 Q2	2012 Q3	2012 Q4	2013 Q1	2013 Q2	2013 Q3
Eurozone- Growth in volume of GDP (European Commission)	-0.3	-0.1	-0.5	-0.2	0.3	0.1
Luxembourg - Growth in volume of GDP (STATEC)	0.5	0.2	1.1	-0.6	1.6	...
Annual variation in %						
	2009	2010	2011	2012	Forecast 2013	Forecast 2014
Luxembourg - Growth in volume of GDP (STATEC)	-5.6	3.1	1.9	-0.2	2.0	2.7
GDP at current prices 2012: EUR 42 917 million						
Minimum monthly salary (since 01/10/2013): EUR 1 921.03						
Current account balance (2013 Q2): EUR 508 million						
Resident population (01/01/2013): 537 039						
Consumer price index (October) - base January 1 st 1948: 823.00						
Half-yearly average of the index linked to base as at January 1 st 1948: 820.24						
Estimated deadline for next salary indexation: October 1 st 2014						

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