

The recessionary trend is confirmed

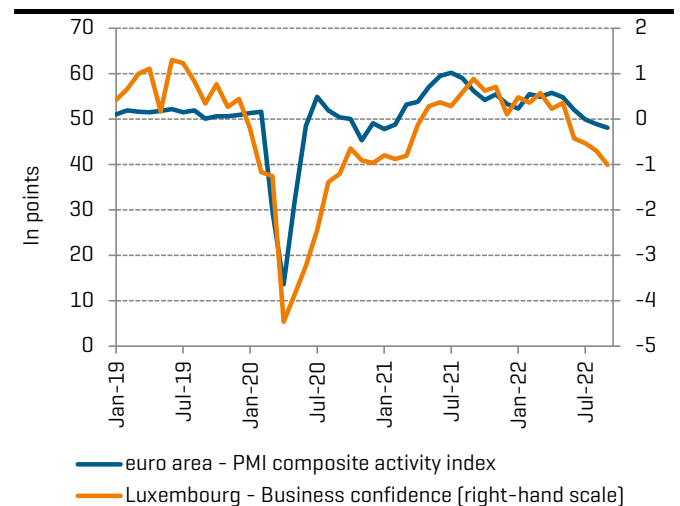
The economic situation in Europe continues to deteriorate as we move into autumn, suggesting the possibility of a recession. While business activity in the euro area, which benefited from the lifting of restrictions, remained resilient in the second quarter, it fell in Luxembourg.

Business survey results for the euro area continued to deteriorate in September. The composite PMI (Purchasing Managers' Index) suggests that both industry and service activities have been contracting since July, pointing to a decline in euro area GDP of around 0.1% quarter-on-quarter in Q3. Moreover, unless economic activity rebounds in the next few months, the downturn will be even more pronounced in the fourth quarter, which would mean that the euro area has entered a recession.

Consumer sentiment dropped to its lowest level on record in September, both for the euro area as a whole and in Luxembourg. Household opinions declined the most with regard to their personal financial situation (recent and anticipated). These concerns are directly linked to the inflation situation and in particular to the rise in energy prices, which was exacerbated by the consequences of the war in Ukraine. Companies are also affected by rising energy prices when they are unable to price these increases into their products, which means that they have to cut their margins. Plans to support the household and business purchasing power have, of course, been put in place in most European countries with the aim of mitigating the effects of this energy shock, but these measures have not been able to fully offset the impact. This situation has led to a surge in demands for higher wages in recent months, in a climate of varying degrees of conflict, depending on the Member State.

Although fiscal policy took a more expansive turn in this context, monetary policy instead opted for the restrictive path. Beyond a slow normalisation, the ECB's interest rate hikes have been very rapid and very sharp (50 basis points in July and then an unprecedented 75 points in September). This significant tightening of European monetary policy is not taking place in a context of economic overheating in Europe, but in a context of price increases that are largely due to external factors. This will weigh on the financing capacity of households and companies and add to the recessionary dynamic by having only an indirect effect on energy prices (via a fall in European demand). And while oil prices and (to a greater extent) gas prices have resumed a downward trend on the markets in recent weeks, there are many other factors behind this trend.

BUSINESS SURVEYS - EURO AREA



Sources: S&P Global, STATEC

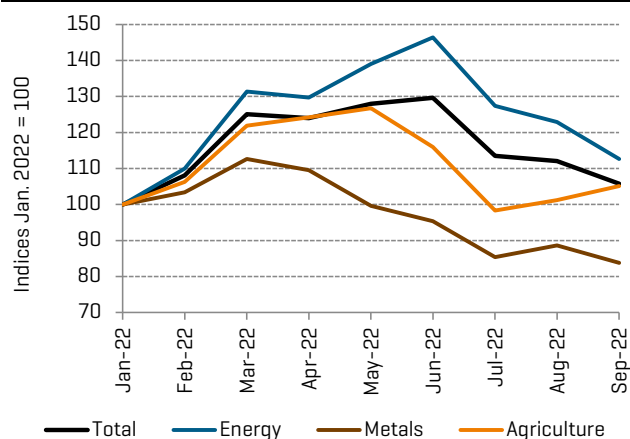
Decline in Luxembourg's GDP in Q2

Luxembourg's GDP fell by 0.5% quarter-on-quarter in Q2 of 2022 (after an increase of 0.7% in Q1). The most negative contributions were seen in the industry and construction sectors, which had performed relatively well in the first quarter. The financial sector held up better (+2.4% quarter-on-quarter compared with a drop of almost 4% in Q1), but the sector's value added in volume terms remains below the levels reached at the end of 2021, which reflects in particular the deterioration of the stock market environment. Household consumption fell in Q2 (-0.4% quarter-on-quarter), as did investment (-5.4%, mainly due to lower construction volumes). Based on these results, growth for 2022 - assuming that GDP stabilises at its Q2 level over the rest of the year - is estimated at 1.6%.

This decline in GDP contrasts with the 0.7% increase recorded in the euro area in Q2. However, it is important to bear in mind that the lifting of health restrictions has particularly boosted the activity of countries with a significant number of tourists (as shown by the excellent results of France, Spain and Italy, in particular), which is not the case for the economy of the Grand Duchy.

International

EVOLUTION OF COMMODITY PRICES



Source: Macrobond

Note: The "Metals" series is the weighted average of the precious and non-precious metal price indices based on the weights published by S&P.

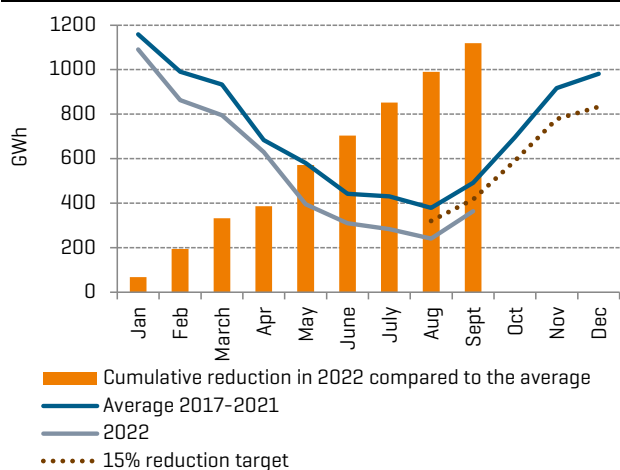
Commodity prices are falling

Following an upward movement after the invasion of Ukraine in February 2022, since the summer a combination of factors has led to a downward trend in commodity prices. These factors include rising storage costs, the appreciation of the dollar, and, more generally, a decline in demand in expectation of an economic recession. The magnitude of the price decline is not uniform across the different commodities.

Energy prices remain above their pre-war levels, reflecting energy supply uncertainties in Europe. Agricultural commodity prices have risen slightly since summer due to high fertiliser costs, which have been impacted by the war, bad weather and a delayed effect of rising energy costs. Metal prices, however, are lower than before the war. This is due to the strength of the dollar and the slowdown in global economic growth.

Energy

GAS CONSUMPTION IN LUXEMBOURG



Source: Eurostat

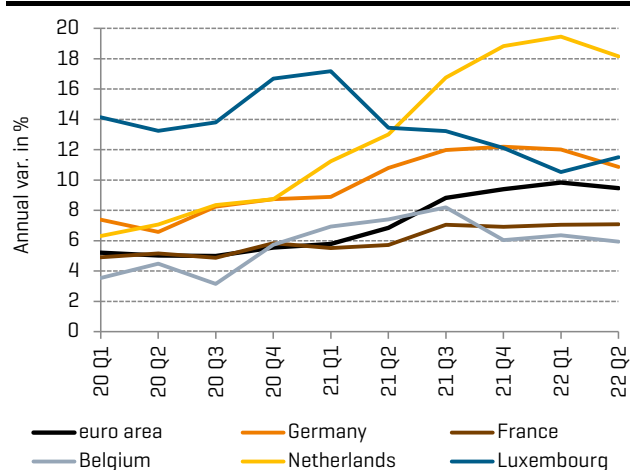
Sharp decrease in gas consumption

Luxembourg consumed about 20% less gas from January to September than it did on average over the last five years. One third of this reduction is due to the closure of a glass industry plant and the replacement of a furnace that was reaching the end of its life. Another third is accounted for by around 20 energy-intensive companies, where a decline in industrial production can be observed since June. This development could reflect a loss of competitiveness following the surge in gas prices through August. The remaining third is attributable to lower gas use for heating: the number of heating degree days was 5% lower than the average over the previous five years.

With an effective decrease in consumption of 36% and 26% for August and September respectively, Luxembourg is on track to meet the European objective of reducing gas consumption by at least 15% between August 2022 and March 2023. Heating accounts for two thirds of gas consumption during the winter. The key factors here will be how severe the winter is and how successful efforts to reduce gas consumption are.

Real estate

SALES PRICES FOR HOUSING



Sources: Eurostat, STATEC

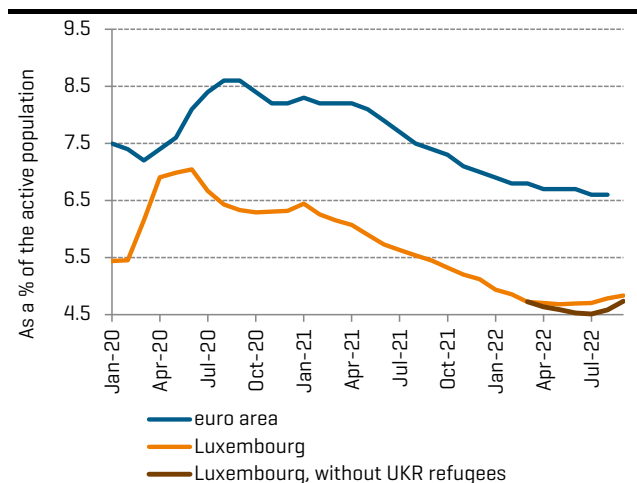
House prices increases are slowing

Selling prices for housing rose by 11.5% year-on-year in the second quarter, compared with 10.3% in the first quarter. However, the fundamental trend continues to be a slowdown, particularly in the case of the prices of existing housing. The number of transactions involving new real estate (where prices are more volatile) is tending to fall, as in previous quarters. The pace of housing price inflation in the euro area seems to have peaked, and the economic context (rising interest rates, high inflation) is likely to lead to a more pronounced slowdown in the coming quarters. The bank credit survey conducted in July shows that demand for home mortgages is declining in Luxembourg and the euro area.

Fixed rates at 10 years or more applied to new mortgages in Luxembourg rose to an average of 2.9% in August (+1.4 percentage point year-on-year). Nevertheless, 30-year fixed rates stabilised at 3.5% in Q3, according to AtHome. Variable rates remained stable at around 1.4% on average in August, but are reported to have risen to 2% at the end of September, following the ECB's key rate hikes.

Labour market 1/2

UNEMPLOYMENT RATE



Sources: ADEM (STATEC calculations), Eurostat, seasonally adjusted figures

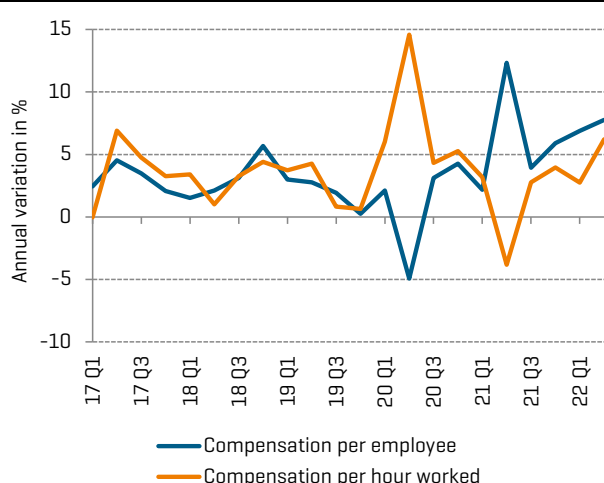
Unemployment rises again

Unemployment is again on the rise in seven of the 19 euro area countries, including Luxembourg. The increase in unemployment is particularly high in Finland and Austria (+1 percentage point since their last low point), as well as in the Netherlands and Belgium (+0.5 percentage points). As unemployment continues to fall in the “heavyweights” (Spain, Italy, Germany), the rate for the euro area as a whole remained stable/decreased slightly, at least through August 2022 [latest data available].

In Luxembourg, the increase in unemployment remains limited for the moment (from 4.7% of the active population in April-July to 4.8% in August and September), and the level of unemployment remains historically low. However, the trend is upwards and should become more pronounced over the coming months. In addition, while unemployment stabilised in the spring through the registration of Ukrainian refugees, the rise in the last two months has been mainly due to other categories (in particular young people). Job creation remains strong in Q3 2022 (with employment increasing by 0.6% quarter-on-quarter), but again the trend is towards a slowdown (+0.9% in Q1, +0.8% in Q2).

Labour market 2/2

CHANGE IN COMPENSATION PER EMPLOYEE IN LUXEMBOURG



Source: STATEC – National Accounts

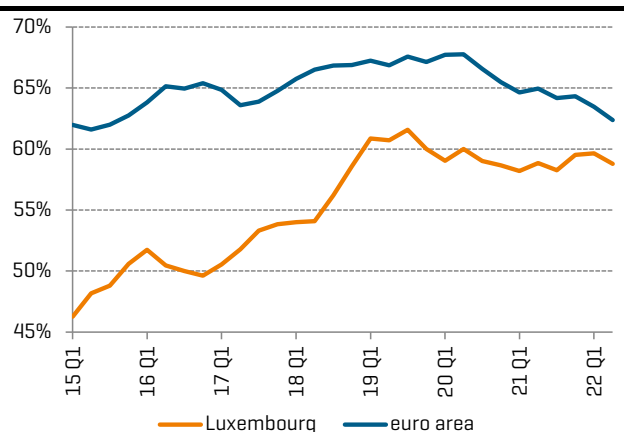
Wages driven by inflation

The compensation per employee [CpE] rose by 7.8% year-on-year in Q2 2022, while the compensation per hour worked [CpHW] rose by 6.2%. These increases were buoyed by inflationary pressures that triggered an index bracket in April 2022, following the one from October 2021.

The compensation per employee and per hour worked differed during the Covid crisis. Measures to protect employment prevented layoffs, while hours worked fell sharply. In addition, composition effects boosted the CpHW, as restrictions (and consequently replacement incomes) were more likely to affect lower wages. While the situation is generally returning to normal, the effects of the crisis persist for the hospitality sector, which was heavily exposed to restrictions in 2021 (the CpE increased by more than 35% in Q2 2022, compared with virtually no change in the CpHW). The main contributors to the increase in CpHW are the financial and transport sectors (due to an increase in bonuses and gratuities in the latter). Compared to the euro area, Luxembourg has a high increase in compensation per employee, notably compared to neighbouring countries (Germany +3.8%; Belgium +6.1% and France +6.7%).

Financial sector

BANK COST-INCOME RATIO



Sources: CSSF, BCE

Income and expense trends are in sync

Bank expenses and income increased by 9.5% in the first half of 2022. Banking income was driven by the rise in interest rates, which supported interest margins, while the increase in expenses was mainly the result of a continuous and significant increase in operating expenses (+10% per year on average since 2018), primarily IT investment expenses, according to the CSSF. Operating expenses are increasing for nearly 80% of banks, and are even higher than personnel expenses at a third of the institutions.

The ratio of expenses to income for banks averages 57% in Luxembourg (it was 60% in the previous three years), compared with 62% in the euro area. Although this ratio has decreased for private banks in Luxembourg, it remains on average higher (median cost-income ratio of 70%) than for universal banks or banks specialising in corporate finance (45%).

Public finances

TAX RECEIPTS [CASH BASIS] AND SOCIAL SECURITY CONTRIBUTIONS

	2022	Evolution	
	9 months	2022/2021	
	In EUR million	In EUR million	In %
Household taxes	5 882	626	11.9
VAT	3 785	339	9.9
Corporate tax	2 404	-11	-0.4
Excise duties	1 268	38	3.1
Subscription tax	983	41	4.3
Others	1 499	75	5.3
Total tax receipts	15 821	1 109	7.5
Social contributions*	4 428	314	7.6

Sources: Tax authorities, IGSS, STATEC

* Data for the first half of the year, calculated according to the ESA2010 national accounts system.

Good performance of tax receipts

Tax revenues collected by the government in the first three quarters of the year are up 7.5% year-on-year [-1.4% over one quarter]. The projected increase in tax revenue collected over the full year 2022 may be somewhat lower for methodological reasons (lag between collection and the reference period) as well as because the last quarter of 2021 was particularly strong, driven by wage indexation.

Revenues in Q3 2022 were boosted by a rebound in corporate taxes (+6% quarter-on-quarter) and by VAT revenues, which were buoyed by inflation. Social contributions and household taxes were boosted by the April 2022 indexation (+7.6% and +14%, respectively, year-on-year in the first half of 2022). By contrast, subscription tax revenues stagnated in Q2 and Q3 [-8.1% year-on-year in Q3] with the decline in assets under management of investment funds [-6% year-on-year in August]. Excise duties also declined in Q2 and Q3 due to the temporary reduction in autonomous excise duties on gasoline and diesel, and the downward trend in fuel sales.

Trend chart

	Average over the									Same period	
	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	last three months	previous year
	Annual variations in %, except where otherwise indicated										
Activity											
Industrial output per working day, in volume	1.3	2.9	-3.2	-0.6	-1.4	-3.1	0.0	...	...	-1.5	12.0
Construction output per working day, in volume	5.8	5.7	-1.8	-4.2	3.2	-4.9	-2.4	...	...	-1.5	0.1
Turnover by volume of total retail trade	6.7	-6.1	0.2	-6.0	-1.8	-4.2	-0.7	-1.2	...	-2.1	0.2
Prices, wages											
Consumer price index (NCPI)	3.6	6.6	6.1	7.0	6.8	7.4	6.8	6.8	6.9	6.8	2.5
Underlying inflation	1.4	4.2	3.5	4.2	4.5	4.8	4.7	5.1	5.2	5.0	1.3
Oil product index	48.7	51.7	56.9	59.2	49.7	56.3	43.6	36.0	37.4	39.0	30.9
Industrial producer price index	25.7	24.4	24.8	30.3	32.8	30.0	29.6	25.7	...	28.4	11.0
Construction price index ¹	11.6	11.6	11.6	13.9	13.9	13.9	...	...	...	13.9	5.2
Average wage bill, per person (National accounts)	6.9	6.9	6.9	7.8	7.8	7.8	...	...	...	7.8	12.3
Foreign trade											
Exports of goods (volume)	1.7	2.2	-0.5	-8.2	0.8	-2.9	-9.4	...	...	-3.9	10.2
Imports of goods (volume)	4.7	4.5	7.6	6.9	4.2	2.6	4.5	...	...	3.8	14.6
Employment, unemployment											
Domestic number of employees	3.8	3.6	3.7	3.6	3.6	3.5	3.6	3.4	3.2	3.4	3.1
National employment	3.0	2.9	2.8	2.6	2.5	2.5	2.8	2.6	2.5	2.6	2.3
Unemployment rate [% of working population, seas. adj.]	4.9	4.9	4.7	4.7	4.7	4.7	4.7	4.8	4.8	4.8	5.5

Source: STATEC

¹ Estimations based on half-yearly data

Indicators

	Quarterly variation in %					
	2021 Q1	2021 Q2	2021 Q3	2021 Q4	2022 Q1	2022 Q2
Eurozone - real GDP growth (European Commission)	-0.1	2.0	2.3	0.5	0.6	0.8
Luxembourg - real GDP growth (STATEC)	2.0	0.6	-0.3	1.7	0.7	-0.5
	Annual variation in %					
	2018	2019	2020	2021	Forecast 2022	Forecast 2023
Luxembourg - real GDP growth (STATEC)	1.2	2.3	-0.8	5.1	2.0	4.0
GDP at current prices 2021: EUR 72 295 million						
Minimum monthly salary (since 01/04/2022): EUR 2 313.38	Consumer price index [09/2022] - base January 1 st 1948: 963.57					
Current account balance (2022 Q2): EUR 610 million	Half-yearly average of the index linked to base as at January 1 st 1948 [09/2022] : 957.56					
Resident population (01/01/2022): 645 397	Estimated deadline for next salary indexation: 2023 Q1					

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