August 2008

conjoncture flash

Monthly publication of the state of the Luxembourg economy

A change of cycle for European property

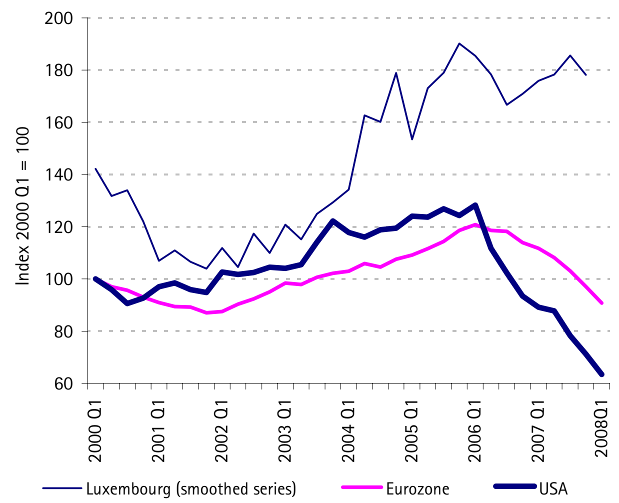
The residential property sector went through a bullish cycle for about 10 years (1997-2007) throughout the eurozone, more specifically in Western Europe, with the notable exception of Germany. Since 2006-2007, however, indicators of activity and related price indicators have started to level out in some countries (France, Italy, Finland and Norway among others) and even fall in others (Spain, Ireland and the United Kingdom). This trend is set to continue in the years ahead.

Downturn less sharp than in the United States

The expected downturn in the European property market, which has already partly begun, is not comparable to that experienced by the United States over the last 2 years. Apart from the United Kingdom, Ireland and Spain, which experienced extremely strong price rises from the late 90s on, a soft landing of the property market rather than a sharp drop is expected for most European countries. There are several reasons for this, mainly linked to better solvency among European borrowers: the criteria for granting mortgages are stricter than in the US and there is a higher proportion of fixed-rate mortgages (and capped variable-rate mortgages).

Sale prices, except in the three above-mentioned countries, are currently slowing down rather than falling but a price drop over the medium term (i.e. over 1 to 4 years) cannot be excluded. This reduced tension on prices is set to slow down new investments, as shown in the drop in the number of planning permissions granted (see graph), inducing potential buyers to postpone buying property. Furthermore, lending conditions have tightened slightly and rising interest rates are having a restrictive effect – these have been rising since early 2006 in the eurozone, with the most recent hike of 25 basis points in July 2008. Several countries have already experienced a rise in the numbers of properties available and a drop in mortgage lending. Rising inflation, which has a negative effect on household purchasing power, has also meant that private individuals are reallocating part of their budget to consumption instead of investments. In addition to this, rising energy prices should see buyers withdrawing from investing in properties at a distance from urban centres (or from public transport infrastructures) and from properties with low energy efficiency (as is sometimes the case with older properties).

Planning permissions granted (residential sector)



Sources: Eurostat, STATEC

No clear reversal as yet in Luxembourg

For its part, Luxembourg seems to be withstanding this cyclical downturn. The number of planning permissions granted in the residential sector has not yet suffered any dramatic decline and mortgage lending is holding up, although the trend in recent quarters points to a slowdown. According to a survey by the Observatoire de l'Habitat[1] (based on announced prices), at the end of the 1st quarter of 2008, asking prices for houses had stabilised and those for apartments were continuing to rise (by 4.5% over one year[2]).

[1] http://www.logement.lu/habitat.html

[2] Observatoire de l'Habitat makes mention of a rise of only 1.2% over one year for apartments, offset by the consumer price index (which rose 3.3% over the same period).

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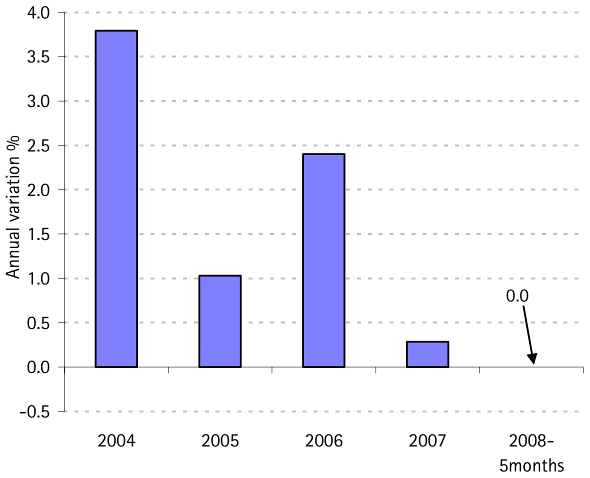
Manufacturing

Manufacturing output per working day



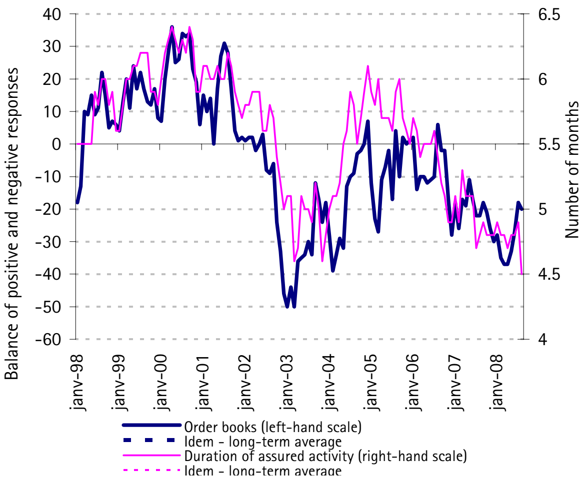
Source: STATEC activity survey

Contrasting results during the 1st half-year

Industrial output in Luxembourg during the 1st half-year of 2008 is set to equal that of last year. The situation improved somewhat during the 2nd quarter (up approximately 2% over one year, with provisional data for June), mainly due to increased output in consumer goods and energy output and distribution. Iron and steel production also recovered, ending up with an increase of almost 2% for the first 5 months of the year. However, several industrial sectors have been lagging behind in 2008, such as food (down 2% over the same period), beverages and tobacco (down 5%), textiles and clothing (down 2%), woodwork (down 16%), paper and cardboard – printing and publishing (down 7%), processing of plastics (down 15%), glass (down 8%) and transport equipment (down 6%).
Manufacturers' opinions (see last month's Conjoncture Flash) point to a more difficult 3rd quarter, marked notably by a significant slump in orders.

Construction

Economic survey on construction



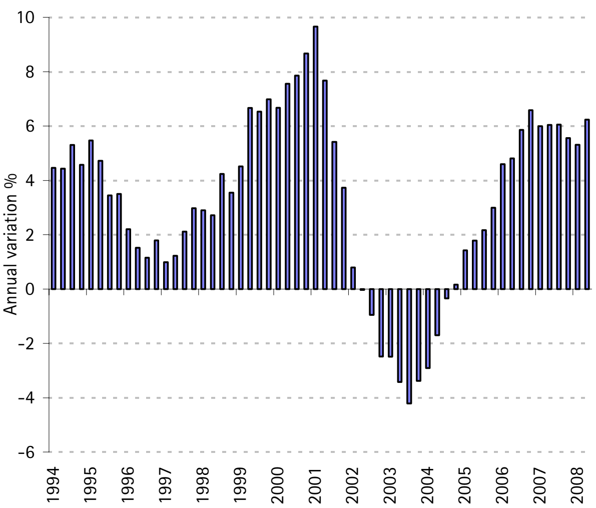
Source: STATEC

Mixed opinions for the 3rd quarter

Directors of construction companies surveyed as part of the regular economic surveys showed signs of uneasiness during the 2nd quarter. Results from surveys carried out in July and August 2008 provide a more mixed picture, although the general trend remains quite downbeat. On the plus side, opinions on the status of order books improved significantly in July and feelings about recent output trends were only slightly affected by the falling orders seen in previous months. On the other hand, assured activity expressed in terms of months fell to a low of 4.5 months in August, excluding seasonal factors, the long-term average being 5.5 months.
Moreover, the number of business owners who estimate that there is insufficient demand has risen sharply since June, reaching 31% in August 2008, as against 15% in August 2007.

Financial sector

Trends in employment in banks



Source: BCL

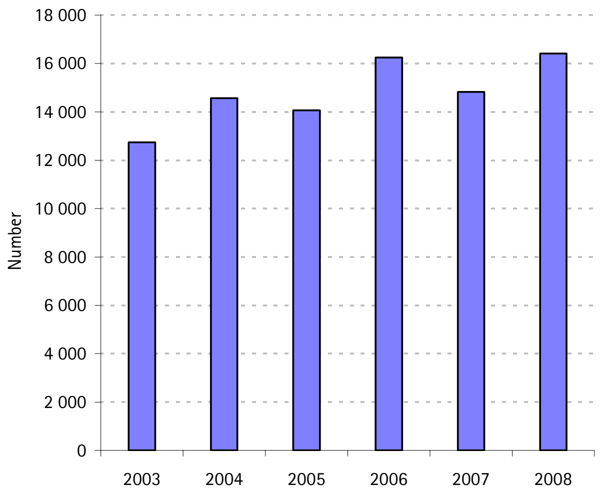
A pleasant surprise for banking employment

Provisional data for banking employment in the 2nd quarter of 2008 showed an increase of 6.2% over one year, a very satisfactory result considering that previous quarters pointed to a slowdown. This recovery was apparently not due to any statistical effect such as a change of scope, and indicates that falling banking results have not yet affected recruitment policies, at least taken on an overall basis.

The CSSF, Luxembourg's financial watchdog, estimated income before provisions for the Luxembourg banking sector at EUR 3.244 billion on 30 June 2008, down 1.8% compared to 30 June 2007. The CSSF believes that this downturn is 'limited' given the current financial context and notes that lending institutions have generally held up well against the downturn in the financial markets.

Consumption

New car registrations at the end of Q2



Source: STATEC

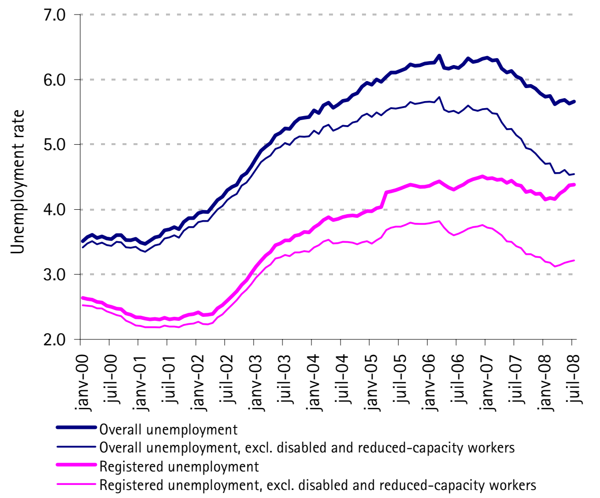
New car registrations recover during the 2nd quarter

After falling 6.5% over one year during the 1st quarter of 2008, new car registrations seem to have recovered, with consumers in Luxembourg returning to the showrooms: registrations rose 10.7% over one year during the 2nd quarter. This recovery translates into a rise of some 2% over the 1st half-year compared to last year.

With this result, Luxembourg's performance is very close to that of Germany (up 3.2%), the Netherlands (up 2.1%) and Austria (up 1.9%) in terms of new car registrations for the first half of 2008. In the eurozone, the 1st half-year was particularly profitable for car sales in Belgium (up 7% over one year), France (up 4%) and Finland (up 13%). On the other hand, several countries witnessed a significant fall in car purchases, particularly Spain (down 18%), Ireland (down 20%) and Italy (down 11%).

Labour market

Unemployment rate in Luxembourg



Sources: STATEC, ADEM

Unemployment continues to rise

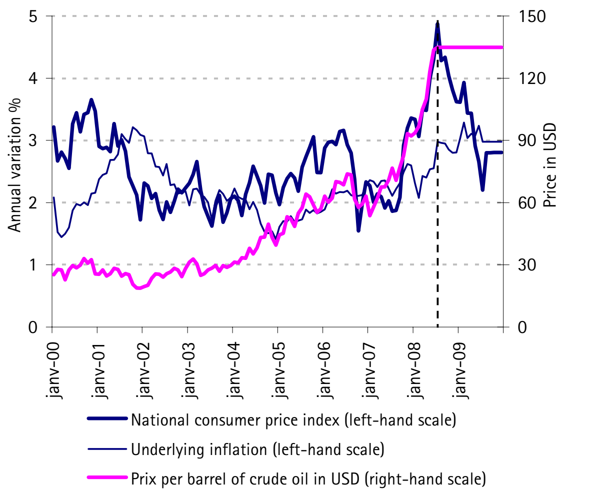
In July 2008, the registered unemployment rate, seasonally adjusted, was 4.4% as against 4.2% in January. The overall unemployment rate, which also takes into account the number of those in job schemes, has gone against the downward trend since April.

This is partly because of the compensatory effect of two phenomena. Firstly, the number of disabled and reduced-capacity workers registered with ADEM continues to grow strongly (up 30% as an annual variation since late 2006). Secondly, the number of workers in job schemes is falling more and more quickly (down 20% in July 2008 as against a drop of 0.4% in January 2007 and a rise of 15% in January).

As the falling numbers of those in job schemes is not taken into account in the registered unemployment rate, the rise in this latter rate is even more significant.

Inflation – wages

Inflation forecasts



Source: STATEC

Inflation forecast: 3.9% in 2008 and 3.0% in 2009

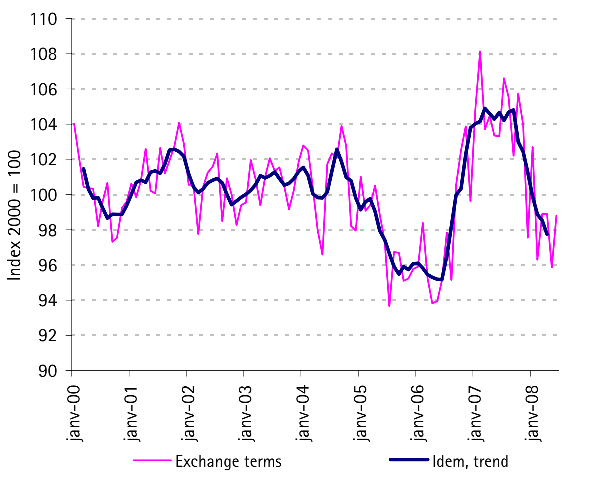
Since the last quarter of 2007, when the inflation rate stood at some 2%, oil prices, combined with other elements such as food prices, pushed inflation up to ever-increasing levels (4.9% in July 2008).

According to the latest forecasts from STATEC, which are based on a price per barrel of USD 135 and an exchange rate of 1.58 USD/EUR, inflation is expected to reach an average of 3.9% in 2008 and 3.0% in 2009.

These forecasts are highly dependent on changes in oil prices, particularly for 2009. If the price per barrel remains at USD 150 over the forecast period, all things being equal elsewhere, the inflation rate should fall from 4.0% in 2008 to 3.2% in 2009. If the price per barrel drops to USD 100, inflation should fall to 3.7% in 2008 and 2.6% in 2009. Therefore, a difference of USD 50 in the price per barrel would have an impact of 0.3 percentage points on the inflation rate in 2008 and 0.6 points in 2009.

Foreign trade

Exchange terms



Source: STATEC

Exchange terms fall

Exchange terms, which plot unit values for exported goods against those for imported goods, represent a country's purchasing power in terms of imports. In Luxembourg, these significantly improved between mid-2006 and early 2007, due to falling energy prices (on the import side) and higher iron and steel prices (on the export side).

After a period of stabilisation, the exchange terms fell sharply from the 4^{th} quarter of 2007 on, affected by the rapid rise in oil prices. The price per barrel expressed in euro rose some 60% between June 2007 and June 2008, which was not offset by increases in iron and steel prices (Luxembourg's main exports), these last growing by just 20% over the same period.

Statistics table

	Nov-07	dec-07	Jan-08	Feb-08	Mar-08	Apr-08	May-08	Jun-08	Jul-08	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	-1.6	0.4	-4.0	-0.1	-1.2	2.0	3.6	...	...	1.4	1.6
Construction output per working day, in volume	-4.0	-10.3	-5.5	-3.3	0.2	-0.3	3.3	...	...	1.1	4.7
Turnover by volume of total trade	16.1	11.6	15.1	29.2	12.8	12.4	...	...	...	17.4	2.0
Turnover by volume of total retail trade	1.8	-1.2	0.9	5.2	2.4	...	...	...	...	2.9	2.6
Prices, wages											
Consumer price index (IPCN)	3.2	3.4	3.3	3.1	3.5	3.5	4.0	4.3	4.9	4.4	1.9
Underlying inflation	2.6	2.6	2.3	2.1	2.4	2.4	2.5	2.6	3.0	2.7	2.2
Oil prices	12.6	16.5	19.8	20.4	21.0	21.1	25.4	29.6	31.9	29.0	-2.7
Industrial producer price index	5.7	7.4	7.2	6.1	5.1	5.0	7.4	9.4	...	7.3	11.2
Construction price index[1]	3.0	3.0	...	...	...	...	...	...	...	3.0	2.4
Average wage bill, per month, per person	3.8	2.5	2.5	2.4	4.4	4.6	...	...	...	3.8	5.0
Foreign trade											
Exports of goods	-2.4	-3.6	1.1	5.9	-1.2	3.7	-1.1	-2.2	...	0.3	-5.6
Imports of goods	-2.1	-6.9	-2.5	-8.2	-9.1	2.5	-12.7	-7.5	...	-6.8	-0.7
Employment, unemployment											
Domestic number of employees	5.2	5.2	*5.4*	*5.4*	*5.4*	*5.4*	*5.5*	*5.5*	*5.5*	*5.5*	4.5
National employment	2.8	2.7	*3.1*	*2.7*	*2.7*	*2.7*	*3.1*	*3.2*	*3.2*	*3.2*	2.0
Unemployment rate (% of working population, seasonally adjusted)	4.2	4.2	*4.2*	*4.2*	*4.2*	*4.2*	*4.3*	*4.4*	*4.4*	*4.3*	4.4

Sources: STATEC

Data in italic font are estimates

[1]Estimations based on half-yearly data

Indicators

	Variation on previous quarter in %					
	2007 T1	2007 T2	2007 T3	2007 T4	2008 T1	2008 T2 (est.)
Eurozone- Growth in volume of GDP (European Commission)	0.8	0.3	0.6	0.4	0.7	-0.2
	Annual variation in %					
	2006	2007		Forecast 2008		Forecast 2009
Luxembourg - Growth in volume of GDP (STATEC)	6.1	4.5		3.0		4.0

GDP at current prices for 2006: EUR 36 137 million	Minimum monthly salary (since 01/03/2007: EUR 1 609.53)
Consumer price index (July 2008) - base January 1^{st} 1948: 743.77	Half-yearly average of the index linked to base as at January 1^{st} 1948: 740.65
Current account balance (2008 - 1st quarter): EUR 949 million	Resident population (01/01/2008): 484 000 (estimation)

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