

■ Global and European setting

■ World economic activity

Slight increase in global growth in the third quarter of 2013

In the third quarter of 2013, growth in the global economy looks set to have improved slightly on the moderate expansion rate recorded in the spring. In the emerging market economies (EMEs) in particular, the pace of growth appears to have picked up slightly in the summer owing, above all, to faster growth in China and some central and east European countries. In other EMEs, however, the rate of growth remained modest, partly as a result of serious structural problems and, in some cases, turbulence on the financial markets in some EMEs with high current account deficits. The catalyst for this turbulence was the US Federal Reserve's announcement at the end of May that it would wind down, or "taper", its strong monetary expansion.

In the industrial countries, the momentum which gave the economy a lift in the spring continued after mid-year. The United States and the United Kingdom maintained virtually the same pace of expansion. By contrast, the Japanese economy, which had recorded robust growth in the first half of the year – not least because of extensive monetary and fiscal stimulus measures – and the euro area fell short of their prior-quarter results. Aggregated real gross domestic product (GDP) across the United States, Japan, the United Kingdom and the euro area rose by ½% after seasonal adjustment and by just over 1% on the year.

Global industrial activity rose slightly over the summer, with seasonally-adjusted global industrial output up by ¾% on average over the July-August period, compared with ½% period-on-period growth in the second quarter. Although this is still a modest increase when measured against the average annual growth rate of just under 4½% during the 2003 to 2007 recovery cycle, it should be noted that the trend growth rate appears to have slowed

considerably since the beginning of the global financial and economic crisis. The world trade volume likewise grew by ¾% in the July-August period compared with spring. Some observers have recently pointed out that the ratio of trade growth to global GDP growth is extremely low by historical standards. However, taking a closer look and accounting for conceptual differences reveals that the decline in income elasticities in world trade over the last few years is significantly smaller than is sometimes argued (see the box on pages 13 to 17).

In the current quarter, global economic growth is likely to continue at more or less the same pace as in the second and third quarters of 2013. The budget dispute in the United States, which was not settled until mid-October and which led to a two-week federal government shutdown and other expenditure cuts, will be only a minor drag on the country's economic output and will have a negligible global impact, judging from experience of a similar escalation in the mid-1990s. It should also be noted that the US Federal Reserve has so far not altered its highly expansionary monetary policy course. Furthermore, there have been no disruptions emanating from the crude oil markets recently, which is, in part, attributable to the relatively mild hurricane season in the Gulf of Mexico.

The disappointing growth in the emerging markets since the beginning of the year, as well as the associated deterioration in the short-term economic outlook in these countries, have prompted the IMF to once again trim its global economic outlook vis-à-vis its interim forecast from early July by ¼ percentage point to 2.9% for 2013 and 3.6% for 2014. The revisions were particularly pronounced for India, Mexico, Russia and (for 2014) Brazil. The forecast for China was likewise revised downwards to 7.6% for 2013 and 7.3% for 2014. In addition, the IMF has reduced distinctly its medium-term growth projections for the EMEs. It

Moderate expansionary course probably maintained in last quarter

IMF revises global growth forecast further downwards

cut its forecast for 2018 to 5.5%, down from 6.2% in its April 2013 estimate. The downward revision is due to a particularly significant correction of 1½ percentage points in the case of China, reducing its growth forecast to 7.0%. The projection for the group of industrial countries remains unchanged from the July interim forecast at 1.2% for this year and 2.0% for 2014. The forecasts for global trade growth were revised downwards to 2.9% and 4.9% respectively. Moreover, the IMF believes that downside risks to the growth outlook still dominate.

Stabilisation of commodity prices

Movements in the international commodity markets also mirrored the relatively modest pace of global growth which continued in the third quarter. Following a sharp fall in the spring, the price of industrial commodities did level off in the current quarter. Although average prices for food, beverages and tobacco once again fell substantially over the summer months compared with the previous period, the figures for this commodity class have budged downwards only slightly since August. By contrast, the price of Brent crude oil has largely recovered from its second-quarter decline. This was driven to a large extent by the marked production shortages in some countries. At the same time, concerns over a potential escalation of military conflict in the Middle East have caused a temporary, yet considerable, increase in spot prices in particular, which, in turn, has led to forward discounts to rise perceptibly for a period of time. The most recent price of a barrel of Brent crude oil on the spot market was US\$107, compared with an average of US\$109¼ over the summer months.

Consumer price inflation remains subdued

The increase in crude oil prices has temporarily pushed up consumer prices again in industrial countries. However, annual percentage growth of the relevant aggregate index already peaked in July at +1.7%. By September, year-on-year inflation had fallen back to +1.2%, primarily because prices had risen so strongly over the same period in 2012. Excluding food and energy from the basket of consumer goods, con-

Global industrial output and world trade

2008 = 100, seasonally adjusted, quarterly, log scale



Source: Centraal Planbureau. ¹ OECD excluding Chile, the Czech Republic, Hungary, Israel, Mexico, Poland, South Korea and Turkey but including Cyprus and Malta.
 Deutsche Bundesbank

sumer prices rose relatively steadily, albeit in a subdued manner. Core inflation likewise stood at +1.2% at the end of the third quarter, marginally lower than three months previously (+1.3% in June) or the September 2012 rate (+1.4%). Overall, there does not appear to be any immediate risk of deflation in the advanced economies.

Selected emerging market economies

According to data compiled by the National Bureau of Statistics of China, real GDP in China increased year-on-year by 7¾% in the third quarter of 2013, compared with +7½% in the second quarter. On the supply side, industrial output was the main factor behind the slight acceleration of aggregate economic activity. The muted pick-up in external demand in par-

Slightly stronger growth in China

World market prices for crude oil, industrial commodities and food, beverages and tobacco

US dollar basis, 2010 = 100, monthly averages, log scale



Sources: Thomson Reuters and HWWI. • Average of 1 to 8 November or 1 to 13 November 2013 (crude oil). Deutsche Bundesbank

ticular is likely to have contributed to this.¹ Moreover, state investment in infrastructure, which has underpinned GDP growth for some time now, gave a further boost to economic activity. In the medium term, however, the Chinese government hopes that the focus of its growth model will shift to private consumption. Although, at a recent economic conference, political leaders agreed that the market should play a more decisive role in allocating resources, they failed to announce any specific steps towards reform. Consumer price inflation picked up somewhat in recent months, with the annual Consumer Price Index (CPI) reaching 3.1% in September, compared with 2.7% in June. Food prices, in particular, accelerated significantly of late.

Next to Indonesia, India's economy was hit the hardest in recent months by the turbulence which affected the financial markets of many EMEs following the US Federal Reserve's monetary policy announcement at the end of May.

Turbulence on the financial markets is probable cause of real economic slowdown in India.

To ease the downward pressure on the rupee, the Reserve Bank of India initially reacted by introducing liquidity policy measures, only to retract some of them later, instead raising its policy rate. Although the situation on India's financial markets has since eased perceptibly, the real economy still shows visible scars left by the turbulence. GDP growth in India was already on a rather flat expansion path and may well have been dampened even further in the third quarter (national accounts data are not yet available for this period). Consumer price inflation rose slightly from 9.5% in the second quarter to 9.7% in the third, owing in part to the depreciation-related increase in import prices.

The most recent national accounts data available (up to and including the second quarter) suggest that the Brazilian economy has picked up pace again following a protracted lull. This is indicated by seasonally adjusted real GDP growth of 1½% on the quarter. However, it is likely that this is the result of an unusually large number of working days, with the actual pace of growth probably markedly lower. Indicators were mixed for the third quarter. Whilst industrial output fell by a seasonally adjusted 1½% on the quarter, real retail turnover rose by 3¼%. Inflationary pressures eased somewhat in recent months, with CPI inflation dropping from 6.7% in June to 5.9% in September. This was primarily the result of lower food price inflation, while many other components saw a more pronounced increase in prices. Against this background, the central bank continued to tighten monetary policy.

Brazilian spring quarter growth rate probably overstated

Aggregate output in Russia remained listless in the third quarter. According to an initial esti-

¹ Although the Chinese export statistics initially do not appear to show an increase in growth, figures for overall exports for the last few months were not very reliable as some exporters had evidently submitted fraudulent customs declarations to the Chinese authorities. For the most part, the distorted data are mainly on exports to Hong Kong. If trade with Hong Kong is excluded, goods exports (calculated in US dollars) increased 4% year-on-year in the third quarter, compared with +1% in the previous quarter.

The empirical relationship between world trade and global economic output

Concerns about the current lull in the growth of world trade have recently been publicly raised.¹ According to the most recent estimates by the International Monetary Fund (IMF), price-adjusted trade in goods and services is likely to expand by just under 3% this year, thus matching the growth of global real gross domestic product (GDP) weighted by purchasing power parities. Last year, according to the IMF, global trade (+2¾%) actually grew less than economic output (+3¼%).² Given that the ratio of the two percentage changes, known as the income elasticity of trade, is usually around 2, many observers see this as an anomaly. Furthermore, an analysis of the world trade volume over time shows that recent values fall well short of the past trend path.

The empirical relationship between world trade and global economic output can be illustrated by a scatter graph that logs the variables along the axes. The observations for the period 1980 to 2007 can be well approximated by a straight line whose slope corresponds to a simple estimate of the elasticity derived from the linear regression of logged world trade volume on logged

economic output. Using the IMF's preferred measure of output – global GDP based on purchasing power parities – the projected income elasticity of world trade from 1980 to 2007 comes to 1.9. The observations from 2008 to 2013 then in fact deviate significantly from the extrapolated trend path. A regression for this period shows an elasticity of just 1.3.

However, it should be noted that global trade data are calculated by aggregating national variables using their prior-year share of global nominal exports or imports (in US dollars). By contrast, the IMF's preferred measure of global GDP is calculated using weights based on individual economies' contributions to global GDP valued at purchasing power parities.³ If this method is applied, the emerging market economies

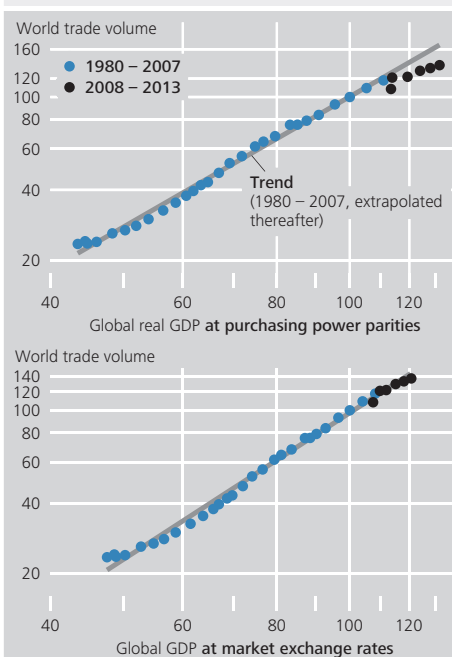
¹ See S Donnan, Trade: Into Uncharted Waters, Financial Times, 25 October 2013, p 9.

² See IMF, World Economic Outlook: Transitions and Tensions, October 2013, p 2. The data used in the rest of this box are also taken from the IMF's current WEO database for October 2013.

³ See IMF, World Economic Outlook: Transitions and Tensions, October 2013, p 137. To aggregate nominal GDP variables in different currencies, they must first be converted into a common currency using exchange rates. As an alternative to using a market exchange rate, a purchasing power parity exchange rate is often used. This is the rate at which US\$ 1 can buy the same basket of goods in another country as it can in the United States. In terms of purchasing power parities, the currencies of the emerging market economies generally appear to be undervalued at market exchange rates because non-tradable goods are often much cheaper there than in the advanced economies.

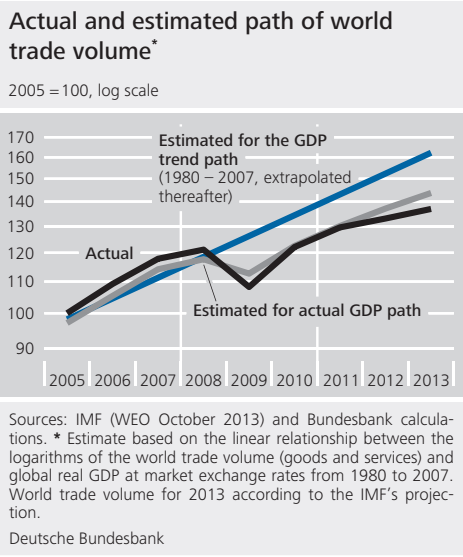
World trade volume and global GDP*

2005 = 100, log scale



Sources: IMF (WEO October 2013) and Bundesbank calculations. * Trade in goods and services. Data for 2013 are IMF projections.

Deutsche Bundesbank



account for a significantly higher share of global GDP than world trade.⁴ As international trade flows are ultimately driven by the purchasing power that actually exists on the markets, and not by fictitious potential consumption abroad as assumed by purchasing power parities, global GDP at market exchange rates is a conceptually better reference variable for world trade.⁵ In view of the large growth gap in recent years between the emerging market economies and the advanced economies, this conceptual difference also has a marked impact on the ratio of world trade to global output. Using GDP at market exchange rates as a reference, only a slight deviation from the relationship that existed from 1980 to 2007 is evident at the current end. According to this calculation, the income elasticity of trade has only fallen from 2.1 to 1.8.⁶

Based on the linear relationship between the log variables, it is also possible to estimate the extent to which the deviation of world trade from its previous trend over time is solely attributable to the change in the pace of global GDP growth (at market exchange rates). To do this, we first calculate the trade volume that would have been

achieved had global economic output continued the expansion path that it followed from 1980 to 2007 and had the relationship between the two variables remained stable. This calculation shows that world trade would have undershot its earlier trend path by 15½% in the current year. If GDP is now assumed to follow its actual path while maintaining the historical relationship, the impact of the economic slowdown can be determined. This indicates that, at the current end, almost three-quarters (just under 11½ percentage points) of the total deviation from the previous trend path is due solely to the deceleration in global growth. Only the remaining gap of just over 4 percentage points may indicate a fall in the dynamics of world trade itself.⁷

It should be borne in mind that the recessionary tendencies seen in some European economies over the last few years probably had more of a dampening effect on world trade than on global GDP. Although the European Union and the United States each accounted for just over one-fifth of (nominal) global GDP at market exchange rates last year, the European Union's share of all

⁴ According to IMF data, half of global GDP calculated at purchasing power parities in 2012 was attributable to the emerging market economies. By contrast, these countries' share of world trade and global GDP is around 38% in each case when calculated from the IMF data at market exchange rates and on a US dollar basis.

⁵ See Kiel Institute for the World Economy, Zu den verschiedenen Methoden bei der Berechnung des Weltbruttoinlandsprodukts, Weltkonjunktur im Frühjahr 2013, p 25.

⁶ Owing to the small number of observations, the estimated elasticity for the later sub-period depends heavily on the precise definition of the period. If 2009 is chosen as the starting point, the elasticity falls to just 2.0. But starting with 2007 lowers the estimated coefficient to 1.7. The constant terms also shift in the estimation. Cointegration tests indicate that the world trade volume and real global GDP at market exchange rates follow the same trend for the entire period (up to the current end). However, if GDP is valued at purchasing power parities, such a trend can no longer be found for the entire period.

⁷ This is less than one standard error of the underlying regression and also includes purely coincidental errors.

imports measured by value amounted to around one-third, while the United States' share was just one-eighth. This is attributable to the close ties between the European economies, due not least to the European single market.⁸ A large part of the statistically recorded foreign trade of the EU countries therefore represents transactions between EU countries (intra-EU trade), while the corresponding flows within the United States are considered domestic trade and are not recorded in the statistics. If intra-EU trade were also considered domestic trade and the international trade weights were adjusted accordingly, a rough calculation of the volume of global imports of goods and services in 2012 and 2013 would result in respective growth rates of 3½% and 3¼% instead of 2½% and 2¾%.⁹

Over and above this purely statistical influence caused by recessions in some European economies, the global cyclical weakness is likely to have strongly slowed world trade growth in recent years. A similar pattern can at least be identified in past economic downturns. For instance, global trade contracted by 2¼% in 1982, while economic output calculated on the basis of market exchange rates still rose by ½%. In 2001 world trade stagnated even though global output increased by 1½%. And in 2009 the slump in the world trade volume (-10½%) exceeded the decline in real GDP (-2%) several times over. At the time, many observers underestimated the cyclical effect on world trade and predicted a merely tentative recovery.¹⁰ In reality, international goods and services flows rebounded to a normal level the very next year. This sensitivity to the economic cycle is often attributed to the fact that demand components with a very high import content, such as inventory changes and investment in machinery and equipment, show sharp cyclical swings.¹¹

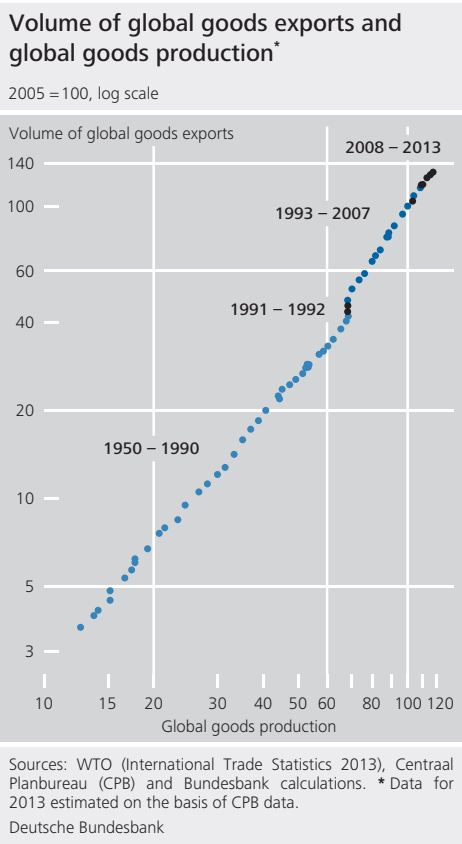
This is ultimately due to the fact that a significant part of the total output produced by the economy and recorded as GDP cannot be traded internationally. This includes buildings, for example, but also many services. It would therefore be more appropriate to consider the volume of world trade in relation to the production of tradables rather than on the basis of aggregate output. However, because such data are not available, an alternative approach is to restrict the measure of world trade volume

8 Conversely, it could also be argued that the plurality of European states inflates the statistically recorded volume of foreign trade flows. For more information on the general impact of an increasing number of countries on the measurement of global trade flows over time, see E Lavallée and V Vicard (2013), *National Borders Matter ... Where One Draws the Lines Too*, *Canadian Journal of Economics*, Vol 46, No 1, pp 135-153.

9 The adjusted shares of global imports attributable to the EU and the USA last year would then be roughly the same. The World Trade Organisation (WTO) comes to a similar conclusion. It estimates that if the European Union were to be treated as a single economic entity, world trade growth would be 3¼% in 2012 rather than 2%. See WTO, *Trade Developments in 2012 and Early 2013*, *World Trade Report 2013*, p 21.

10 In spring 2009, the IMF expected the volume of world trade to increase by ½% in 2010 and global GDP at market exchange rates to concurrently expand by 1%. The OECD assumed that trade would grow by 2%, and even under an optimistic scenario capped the forecast increase at just 5%. However, according to current data, the world trade volume soared by 12¾% in 2010. See IMF, *World Economic Outlook: Crisis and Recovery*, April 2009, p 10; OECD (2009), *The Role of Financial Conditions in Driving Trade*, *Economic Outlook*, No. 85, pp 23-24.

11 Alessandria et al (2010) focus on inventory adjustments, whereas Bussière et al (2013) highlight the importance of the import content of gross fixed capital formation and exports. However, it should be noted that gross fixed capital formation includes, in the form of construction investment, a demand component that has little relevance to foreign trade but which has suffered a particularly pronounced slump in some economies in recent years. In 2012, the ECB likewise linked the slump in world trade to sluggish investment. See G Alessandria, J P Kaboski and V Midrigan (2010), *The Great Trade Collapse of 2008-09: An Inventory Adjustment?*, *IMF Economic Review*, Vol 58, No 2, pp 254-294; M Bussière, G Callegari, F Ghironi, G Sestieri and N Yamano (2013), *Estimating Trade Elasticities: Demand Composition and the Trade Collapse of 2008-2009*, *American Economic Journal: Macroeconomics*, Vol 5, No 3, pp 118-151; and ECB, *Global Trade: Recent Developments and Short-Term Outlook*, *Monthly Bulletin*, December 2012, pp 11-12.



to goods and relate it to the global production of goods.¹² Corresponding time series produced by the WTO go back as far as 1950, which makes it possible to assess whether and to what extent specific influences affect other data releases from 1980 onwards.¹³ For instance, a scatter graph of the log level of the global export volume and output of merchandise shows a fairly close linear relationship from 1993 to 2007, which implies an elasticity of 1.9. In the last few years, world trade appears to have remained somewhat below this trend, although the elasticity has only fallen to 1.8. Between 1950 and 1990, the elasticity of real goods flows to merchandise output was just 1.4. It is striking that at the beginning of the 1990s, however, not only did the elasticity increase, but the relationship between the levels also shifted overall. In mathematical terms, this is because world trade expanded significantly between 1991 and 1993 while the pace of global output

simultaneously faltered.¹⁴ This development might conceivably have been caused largely by the inclusion of transition countries and other emerging market economies in the global economy. However, due to this break, a simple linear regression for the period between 1980 and 2007 would in fact show an elasticity of 2.1.

On balance, after taking into account various conceptual discrepancies, the decrease in the income elasticity of world trade in recent years is considerably smaller than some analyses suggest. Global GDP at purchasing power parities is not a suitable measure of economic activity in relation to foreign trade flows. Even if global GDP at market exchange rates is used as a reference variable, the result at the current end is impaired. This is mainly due to the economic problems that European countries, in particular, have experienced in recent years; because the EU accounts for a large share of world trade, the recent problems of the European countries are depressing world trade more than global output. Furthermore, world trade is often disproportionately weak during a global economic downturn. Bearing all this in mind, it appears difficult to draw inferences about possible trend shifts from a snapshot dip in world

¹² The figure given by the WTO for global goods exports in 2012 is US\$ 17,930 billion, while exports of services only amounted to US\$ 4,350 billion. See WTO, World Trade Developments in 2013, International Trade Statistics 2013, p 22 and p 26.

¹³ The data are taken from Table A1a of the International Trade Statistics 2013. The data still outstanding for 2013 are extrapolated on the basis of the year-on-year rates of change of the world trade volume (goods) and global industrial output for the period January to August 2013 according to the CPB.

¹⁴ According to WTO data, global goods exports rose by 4¼% on average between 1991 and 1993, while merchandise output actually fell slightly. CBP data on the level of the relevant variables only go back as far as 1991 but paint a similar picture, according to which international goods trade increased by 4½% on average between 1992 and 1993. However, industrial output only went up by just under 1%; in the advanced economies, it actually contracted by almost 1%.

trade. Ultimately, the past two decades may represent an artificially high benchmark elevated by one-off effects stemming from the integration of a number of transition countries and emerging market economies into the global economy.

In view of strengthening global economic activity, especially in industry, the ratio between the growth rates of world trade and global GDP (at market exchange rates) may well be higher in the next few years than during the past two years.¹⁵ Nonetheless, regarding its pattern over time, the world trade volume is unlikely to return to its previous trend path. However, this is due less to a fundamental impairment of the underlying relationship than to a flattening of the upward curve of global GDP at market exchange rates. In particular, demographic influences are likely to have persistently slowed the pace of expansion of output in

major industrial countries.¹⁶ Recently, there has been growing evidence of a slowdown in potential growth in some emerging market economies, too.

¹⁵ However, the WTO considers it unlikely that this ratio will return to a value of around 2, because many of the forces that drove world trade over recent decades have already exhausted themselves. See WTO, Factors Shaping the Future of World Trade, World Trade Report 2013, pp 55-57.

¹⁶ See, for example, Deutsche Bundesbank, The US economy in the current economic upturn, Monthly Report, April 2013, pp 15-37.

*Sustained
economic lull
in Russia*

mate by the Russian Federal Statistics Service, real GDP grew once again by 1¼% on the year. Russia's economy is mainly suffering from a pronounced investment slump, with gross fixed investment down by 2½% year-on-year in spring and apparently no fundamental improvement over the summer months. The IMF recently called on Russia to take steps to improve its investment climate and encouraged the country to diversify its economic structure to reduce its commodity dependence. Consumer price inflation decreased distinctly in the period under review, with annual inflation falling from 6.9% in June to 6.1% in September.

USA

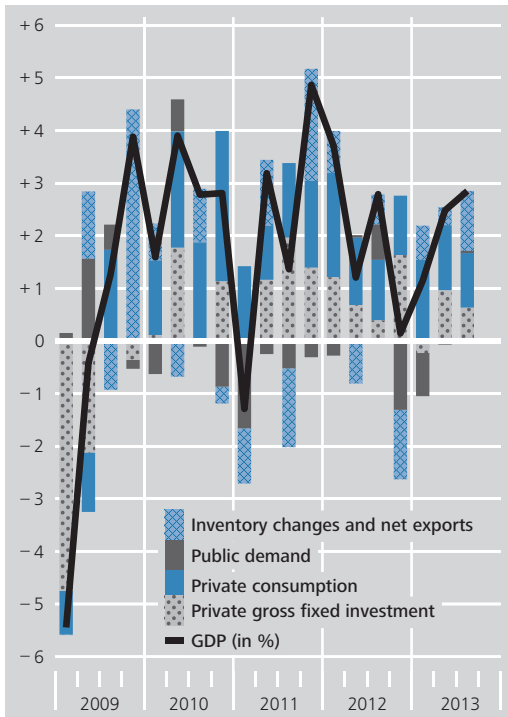
*Aggregate
growth up
slightly*

The US economy picked up pace slightly in the third quarter. Adjusted for price and seasonal effects, GDP increased by ¾% on the quarter, compared with growth of just over ½% in the second quarter. However, in unadjusted terms,

this rise is solely attributable to inventory changes and net exports, meaning that the underlying pace of economic growth was still moderate. The expansion in private consumption, in particular, remained muted. Furthermore, growth in business gross fixed investment slowed significantly, with enterprises even distinctly cutting real spending on equipment. Although private residential construction investment remained strong, leading indicators such as housing starts suggest that this pace is likely to abate in the fourth quarter of 2013 and the first quarter of 2014. However, on an encouraging note, government demand was no longer a drag on aggregate growth. Further federal spending cuts were counterbalanced by an equivalent boost to expenditure at state and municipal level. When compared with experiences from the 1990s, the temporary shut-down of non-essential government services brought about by a budget impasse in October should have only a marginal impact on aggregate growth in the current quarter.

Contributions to quarter-on-quarter growth in real US GDP

In percentage points, seasonally adjusted, in annualised terms



Source: Bureau of Economic Analysis.
 Deutsche Bundesbank

Mixed signals on strength of labour market recovery

Despite rather mixed signals from some economic indicators, the labour market continued to recover in the third quarter. According to company data, only 163,000 new (non-farm) jobs were created on average each month during the third quarter, compared with an average of 195,000 in the first two quarters.² Nonetheless, the unemployment rate, which is based on a separate household survey, decreased from 7.6% in June to 7.2% in September. These conflicting markers are probably one important reason why the Federal Reserve has not yet begun to “taper” its asset purchases. Although the unemployment rate rose slightly in October, this was most likely because federal employees who were temporarily furloughed on account of the budget impasse were thus considered unemployed during the reporting period. These figures, however, are not reflected in company data, which even indicate considerable growth in employment in October (+204,000 jobs), compared with September’s figures. Owing to the unfavourable price devel-

opments during the same period in 2012, CPI inflation weakened by 0.6 percentage point to +1.2% over the summer months. By contrast, core inflation was slightly higher in September (+1.7%) than in June.

Japan

The Japanese economy, which underwent a strong upturn in the first two quarters of 2013, lost some steam in the summer months. In seasonally adjusted terms, real GDP picked up by ½% on the period, compared with growth of 1% in each of the first two quarters. One reason for the lower growth is a fall-off in household consumption following a surge in the first half of the year. Another is that exports fell slightly, while imports continued their sharp climb. Thus, net exports have gone from boosting aggregate growth to dragging it. Although enterprises pushed up gross fixed investment only slightly, in unadjusted terms the slowdown in the pace of destocking boosted growth significantly. This contrasted with an acceleration in government investment and investment in private housing construction. While government investment is likely to be nearing its peak, front-loading of demand in the last quarter of 2013 and the first quarter of 2014 is expected to lend a fresh boost to residential construction in particular. The background to this is the consumption tax hike scheduled for April 2014, which will also apply to corporate property sales. In addition to construction orders, recent new passenger car registration figures indicate that this type of front-loading could be significant over the autumn months. According to Japan’s national accounts, households’ nominal income, which the government and central bank consider to play an important role in leading the economy out of its mild deflation over

Upturn no longer quite as strong

² Prior to the release of the latest figures, average growth in employment was estimated at just 143,000 jobs over the summer months. For more information on the susceptibility to revision of employment figures in the United States, see Deutsche Bundesbank, Need for revision of monthly employment estimates in the US, Monthly Report, April 2011, p 42.

the medium term, trended slightly downwards in summer. The decline in income was more pronounced in price-adjusted terms. Year-on-year CPI inflation was significantly higher in September (+1.1%) than in June (+0.2%), with core inflation (0.0%) emerging from negative territory for the first time since the end of 2008. At 4.0%, the unemployment rate in September was only marginally higher than June's figures.

United Kingdom

Pace of growth unchanged

The pace of economic recovery in the United Kingdom continued unabated in the summer months. According to initial estimates, seasonally adjusted real GDP rose just as sharply period-on-period as in the spring (+3/4%). Growth in the services sector was up marginally and surveys conducted at the beginning of autumn indicated that this growth could continue to gain momentum. Gross value added of the services sector, which accounts for more than three-quarters of aggregate output, exceeded for the first time its previous peak of winter 2008. Construction sector growth was of a similarly high magnitude as in the second quarter. This is all the more remarkable given that the spring figures seemed to be overstated on account of the weather conditions. Energy production, on the other hand, plummeted during the warm and dry summer. However, a further sharp rise in manufacturing more than made up for this fall-off, which meant that the increase in gross value added in the entire production sector (excluding construction) was only somewhat weaker than in spring. On the expenditure side of GDP, the increased upward momentum in real retail sales suggests an upturn in private consumption. The impact of the overall economic recovery, which was quite strong compared with the slow-paced growth in recent years, has spilled over onto the labour market. The standardised unemployment rate reported by the Office for National Statistics fell from 7.8% in the spring to 7.6% in the third quarter. A clearer improvement in the situation

could be seen in the number of recipients of unemployment benefits, which trended downwards sharply up to October. After holding firm at 2.7% in the summer months, HICP inflation dropped to 2.2% in October.

New EU member states

The overall economic upturn in the new EU member states (EU-8),³ which began in spring, has strengthened in the past few months. In most of the countries which published flash estimates, period-on-period real GDP growth ranged from marked to substantial; only in the Czech Republic did it fall. As before, economic activity in the EU-8 is likely to have received a positive impetus from the euro area. Furthermore, domestic demand also seems to have picked up in many countries. However, the labour market situation has remained difficult. The overall unemployment rate in the new EU countries has been stuck at 9.8% since May. Aggregate HICP inflation, which had already reached a multi-year low in the first two quarters of 2013, fell further in the third quarter. The figures ranged in September from -1.3% in Bulgaria and +0.9% in Poland to +1.6% both in Hungary and Croatia. The central banks in Poland, Hungary, Latvia and Romania have used the lower level of inflation to cut interest rates further in the period under review.

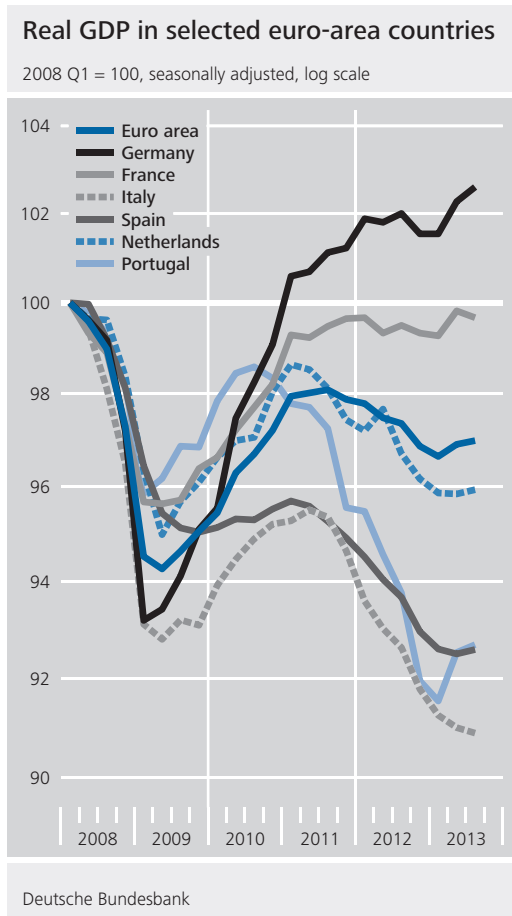
Economic recovery stabilised

Macroeconomic trends in the euro area

The economic upturn in the euro area, which took root in the spring, continued into the second half of the year, albeit with little momentum. After seasonal adjustment, real GDP grew marginally in the summer compared with the second quarter, in which it had risen somewhat more strongly. Despite this, growth was

Marginal GDP growth

³ This group comprises the non-euro-area countries that have joined the EU since 2004 (including the newest member state, Croatia).



still down by ½% on the year and fell 3% short of the level recorded before the financial and economic crisis struck at the beginning of 2008. Broken down by region, growth figures in the third quarter were once again strongly boosted by the German economy, where production expanded by a seasonally adjusted ¼%. Of the remaining 12 countries which have released figures on economic growth in the summer months, Estonia and Finland reported the strongest growth (+1½% compared with the second quarter), followed by Austria, Belgium and Slovakia (+¼% each). GDP in the Netherlands rose slightly. The French economy was not quite able to sustain the distinct rise in output reported in the spring. By contrast, the stabilisation tendencies which were already evident in the spring continued in the majority of peripheral countries. For instance, following nine quarters of recession, the Spanish economy grew again slightly in the quarter under review and real GDP in Portugal rose again, this time by ¼%. The downturn in Italy slowed fur-

ther; only Cyprus recorded a notable decline (-¾%). In Greece, where the Statistical Authority has ceased to publish seasonally adjusted figures until further notice, the economy contracted at an annual rate of 3% after shrinking by 3¾% in spring. In its autumn economic forecast, the European Commission estimated a year-on-year decline of ½% in the economic output of the euro area for 2013 on the whole.

The available indicators suggest that the modest upturn will continue in the final quarter. For instance, purchasing managers' indices for manufacturing and services were again distinctly above the expansion threshold. Furthermore, according to survey results, confidence in the retail, services and industrial sectors has risen considerably in recent months. In September, the industrial indicator exceeded its long-term average for the first time since March of last year, rising further in October. This included, in particular, a strong improvement in companies' output expectations. The growing optimism was reflected in the seasonally adjusted 1% increase in the value of manufacturing orders over the July-August period compared with the second quarter, with orders received from countries outside of the euro area rising particularly sharply.

Economic indicators suggest slight growth in the last quarter

The industrial sector provided no positive impetus in the third quarter. Following considerable growth in spring, output was down ¼% in the summer quarter on the back of a distinct decline in energy production (-1½%). Excluding energy, output remained unchanged from the previous period. While the production of consumer goods fell somewhat, the production of intermediate goods expanded by ¼% while that of capital goods remained unchanged. Capacity utilisation in manufacturing nonetheless continued to rise slightly from July to October, yet still fell short of its long-term average. In the summer months, economic activity was propped up by the construction sector, which had shrunk by 27½% overall between the first quarter of 2007 and the winter quarter of 2013. Construction activity rose period-on-

No impetus in the summer quarter from the industrial sector, but construction activity up sharply again

period by a seasonally adjusted 2¼% in the July-August period following growth of 1¾% in the spring. It is striking that the rise in construction activity after mid-year was broadly based throughout the euro area. However, it is not yet clear whether this indicates an end to the adjustment crisis in the construction sector in some of the peripheral countries.

Slight increase in domestic demand, but exports weak

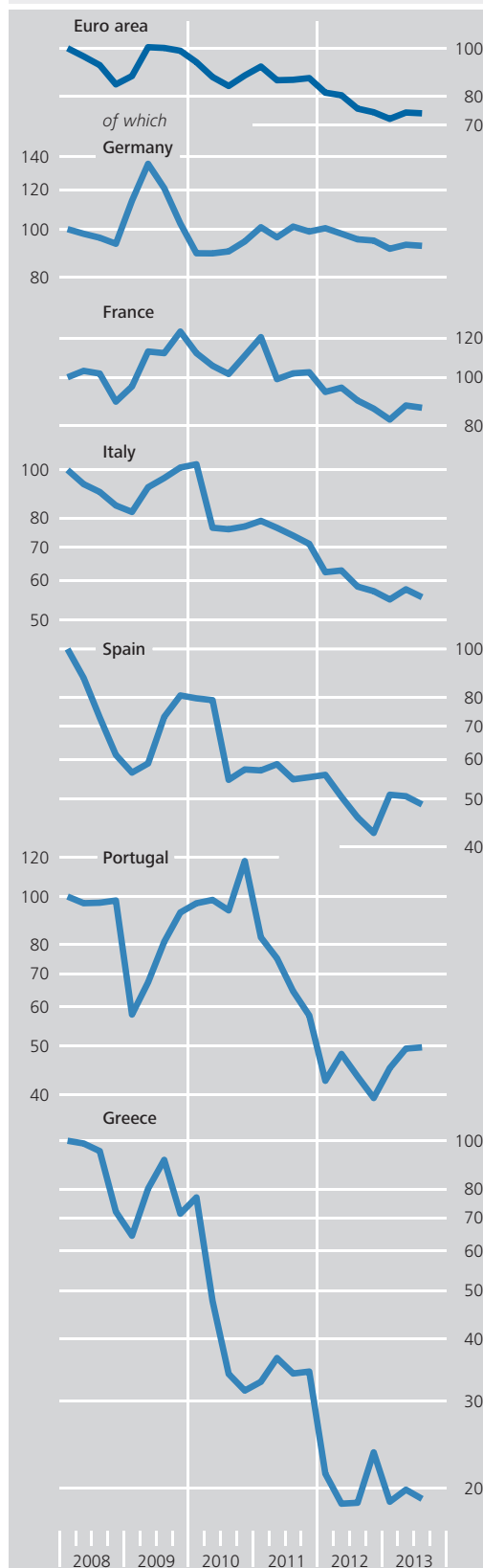
Domestic demand is likely to have once again given a slight boost to the demand side of the economy. The ½% rise in real retail sales from the second to the third quarter points to a moderate increase in private consumption. Furthermore, consumer optimism continued to grow in the summer months. However, the number of new passenger car registrations fell by ½% on the quarter and 2% on the year. Given that the output of machinery and equipment remained unchanged, the strong growth in construction suggests a higher level of gross fixed investment. By contrast, exports are likely to have had a more dampening effect on activity in the third quarter. At all events, nominal exports of goods to non-euro-area countries were down in July-August by a seasonally adjusted 2½% from the second quarter. However, it is important to note that, in terms of the contribution to growth by net exports, goods imports also fell (-¾%).

Situation on the labour market remains poor

Thanks to the economic upturn evident since spring, the increase in the unemployment rate was distinctly lower in the euro area in the second and third quarters of 2013. The seasonally adjusted number of unemployed persons rose considerably more slowly on average over the second and third quarters taken together (+141,000) than in the previous seven quarters of recession (+495,000). The standardised unemployment rate, which stood at 12.1% from April to July, increased to 12.2% in August and remained unchanged in September. In two peripheral countries (Ireland and Portugal), the unemployment rate fell slightly after mid-year. By contrast, unemployment went up slightly in Spain and Greece and considerably in Cyprus and Italy. The Benelux countries and France

New passenger car registrations in the euro area

2008 Q1 = 100, seasonally adjusted, quarterly, log scale



Source: ECB.
 Deutsche Bundesbank

also recorded an increase in unemployment in recent months. The rate also rose somewhat in Austria; however, at 4.9%, it remains the lowest unemployment rate in the euro area. The number of those in work, which declined marginally in spring, is likely to have stabilised in summer.

Subdued upward trend in consumer prices

After seasonal adjustment, euro-area consumer prices were up in the third quarter by 0.5% on the period. The very strong increase, which averaged at an annualised 2%, should be considered in relation to the very low quarterly rate of 0.1% (annualised 0.4%) in the second quarter. Taken together, the two quarters suggest a subdued rise in consumer prices, which can also be seen in the annual HICP inflation rate of 1.3% in the third quarter. The slowing rate of inflation (year-on-year HICP inflation had been as high as 2.5% in summer) is mostly evident in the energy component and in industrial goods. The sideways tendency in crude oil prices and the marked appreciation of the euro are im-

portant factors here. The levelling-off in the trend in services prices, which are mainly determined by domestic economic factors, was less pronounced.

After seasonal adjustment, consumer prices fell unexpectedly sharply in October on the month (-0.2%); annual HICP inflation fell to 0.7% from a September figure of 1.1%. These movements were mainly attributable to a further fall in energy prices due to the euro's appreciation and low crude oil prices as well as the continuing normalisation of food prices, which had risen quite sharply in the first two quarters. The seasonally adjusted slight decline in services prices can be explained by one-off measures such as the abolition of tuition fees in Germany and cheaper telecommunication rates in Italy. On the other hand, the VAT increase in Italy does not yet appear to have fed through to prices. The subdued upward price trend and the correspondingly low annual inflation rates are expected to continue over the next few months.

Surprisingly sharp fall in HICP inflation rate in October