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 **ÖSTERREICHISCHES INSTITUT FÜR
WIRTSCHAFTSFORSCHUNG**

**Economic Growth Remaining
Subdued**

Economic Outlook for 2003 and 2004

March 2003

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Austrian Institute of Economic Research

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Economic Growth Remaining Subdued

Economic Outlook for 2003 and 2004

For the third year in a row, the Austrian economy will grow by only around 1 percent in 2003. Adding to the persistent weakness of domestic demand are the economic repercussions of geo-political instability. For 2004, uncertainties are particularly large, with growth projected to stay below average (1.7 percent). Weak overall economic conditions will lead to a further rise in unemployment and a widening budget deficit.

The Austrian economy grew by 1 percent in real terms in 2002, a rate close to what WIFO had expected as early as December 2001 (1.2 percent). Yet, in the third and fourth quarter, GDP remained flat on a seasonally adjusted basis, with stagnation likely to continue this year. The main reasons are the consequences of geo-political instability for the economy as well as continued sluggishness of domestic demand. GDP growth in 2003 is currently expected at 1.1 percent, remaining close to a modest 1 percent for the third consecutive year. Such an extended period of weak activity has not been observed to date.

Prospects for 2004 are necessarily vague at this stage, given the great uncertainty surrounding geo-political developments and the reaction of economic policy. At present, growth is projected at 1.7 percent, remaining again clearly below the long-term trend. Both in 2003 and 2004, the pace of expansion would thereby correspond to the euro area average. A cyclical upswing in Europe appears unlikely, unless world-wide uncertainty subsides and commodity prices ease markedly. Underlying the present projection are the external assumptions of a reference price of 29 \$ per barrel for crude oil in 2003 and of 23 \$ per barrel in 2004, and an exchange rate of 1.08 \$ per euro.

The real-effective appreciation of the euro is holding back the rise in Austrian exports. Merchandise exports are seen rising by 4.3 percent in volume this year, and by 7.5 percent in 2004. As in the past two years, however, and despite the weak interna-

tional environment, exports will stay the main driving force of Austrian economic growth. The weak momentum of foreign demand is dampening investment in the export-oriented business sector. Spending on machinery, vehicles, electronic equipment and software may pick up by an inflation-adjusted 3 percent this year, after having fallen by a cumulated 13 percent since 2000. Towards the end of the year, some positive effects may be expected from spending being carried forward in view of the temporary investment premium expiring. A genuine cyclical recovery of investment may set in by 2004, with expenditure on new equipment projected to gain 5.5 percent. Growth of manufacturing output, expected at 1.8 percent in volume in 2003 and 3 percent in 2004, will also be constrained by weak demand. This will not suffice as to prevent further substantial job losses in industry.

Domestic demand developments remain below the long-term average. After a decline in 2001 and 2002, a slight pick-up may be expected for the current year. Spending of private households is held back by the unsatisfactory labour market situation and the modest gains in net incomes. Nevertheless, private consumption is set to increase by nearly 1½ percent, while public consumption will remain flat. Construction investment in civil engineering is benefiting from higher spending on road and railroad infrastructure, whereas the building sector lacks stimulus.

Consumer price increases are slightly gaining momentum, with the rate of inflation projected at 1.9 percent. Upward pressure is being exerted both by energy and services prices, notably related to housing, but also by industrial manufactures prices. Next year, inflation should moderate to a rate around 1½ percent. The appreciation of the euro is dampening the rise of import prices, and unit labour costs should be of stabilising influence.

Slow economic growth has pushed up the number of unemployed by a cumulated 38,000 in 2001 and 2002. The negative trend is unlikely to reverse during the forecast period. In 2003, the number of actively employed will fall again slightly, with job losses being concentrated in manufacturing, construction and trade. The public sector is planning further cuts in personnel. Unemployment is likely to increase by 8,000 people to a level of 240,000 on annual average 2003, yielding a jobless rate of 7 percent of the dependent labour force (national definition) or 4.2 percent of the total labour force (Eurostat concept). While in 2004 employment may pick up somewhat, unem-

ployment is unlikely to decline, as both the initial steps towards the abolition of early retirement and the expected large inflow of foreign workers will add to labour supply.

The general government account recorded a deficit of € 1.2 billion or 0.6 percent of GDP last year, according to the Ministry of Finance and Statistics Austria. For 2003, no draft Federal budget has yet been submitted. WIFO expects an increase in the overall deficit to some € 2¾ billion or 1.2 percent of GDP, due to the dampening effect of the cycle on tax revenues, the deferred payments for flood relief, and additional outlays such as for family subsidies. Also in 2004, adverse cyclical conditions will leave their mark on the budget in the form of revenue shortfalls and high outlays for unemployment benefits. The general government deficit may amount to 1 percent of GDP.

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Projections - March 2003

Main results

Changes from previous year

		1999	2000	2001	2002	2003	2004
GDP							
Volume		+ 2.7	+ 3.5	+ 0.7	+ 1.0	+ 1.1	+ 1.7
Value		+ 3.4	+ 5.0	+ 2.3	+ 2.3	+ 2.4	+ 3.5
Manufacturing¹, volume		+ 3.0	+ 6.5	+ 1.3	+ 0.2	+ 1.8	+ 3.0
Private consumption expenditure, volume		+ 2.3	+ 3.3	+ 1.5	+ 0.9	+ 1.4	+ 1.9
Gross fixed investment, volume		+ 2.1	+ 5.9	- 2.2	- 4.8	+ 2.0	+ 3.3
Machinery and equipment ²		+ 4.9	+ 11.8	- 2.9	- 8.9	+ 3.0	+ 5.5
Construction		+ 0.0	+ 1.2	- 1.5	- 1.2	+ 1.2	+ 1.5
Exports of goods³							
Volume		+ 7.7	+ 13.1	+ 7.5	+ 5.5	+ 4.3	+ 7.5
Value		+ 7.0	+ 15.6	+ 6.5	+ 4.1	+ 5.3	+ 7.7
Imports of goods³							
Volume		+ 6.9	+ 10.9	+ 5.7	- 0.9	+ 4.6	+ 7.5
Value		+ 6.7	+ 14.7	+ 5.0	- 2.2	+ 6.5	+ 7.0
Current balance	€ bn	- 6.33	- 5.36	- 4.65	- 0.91	- 1.90	- 1.82
As a percentage of GDP	%	- 3.2	- 2.6	- 2.2	- 0.4	- 0.9	- 0.8
Long-term interest rate⁴	%	4.7	5.6	5.1	5.0	3.9	4.0
Consumer prices		+ 0.6	+ 2.3	+ 2.7	+ 1.8	+ 1.9	+ 1.4
Unemployment rate							
Percent of total labour force ⁵	%	3.9	3.7	3.6	4.1	4.2	4.2
Percent of dependent labour force ⁶	%	6.7	5.8	6.1	6.9	7.0	7.0
Dependent employment⁷		+ 1.2	+ 1.0	+ 0.4	- 0.5	- 0.1	+ 0.3
General government financial balance							
according to Maastricht definition							
As a percentage of GDP	%	- 2.3	- 1.5	+ 0.3	- 0.6	- 1.2	- 1.0

¹ Value added, including mining and quarrying. ² Including other products. ³ According to Statistics Austria.

⁴ 10-year central government bonds (benchmark). ⁵ According to Eurostat. ⁶ According to Labour Market Service.

⁷ Excluding parental leave and military service.

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Projections - March 2003

Key policy indicators

	1999	2000	2001	2002	2003	2004
Fiscal policy						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 2.3	- 1.5	+ 0.3	- 0.6	- 1.2	- 1.0
according to National accounts	- 2.4	- 1.6	+ 0.0	- 0.8	- 1.3	- 1.1
General government primary balance						
	+ 1.4	+ 2.2	+ 3.8	+ 2.8	+ 2.2	+ 2.2
Monetary policy						
	In percent					
3-month interest rate	3.0	4.4	4.3	3.3	2.2	2.6
Long-term interest rate ¹	4.7	5.6	5.1	5.0	3.9	4.0
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 1.5	- 2.5	+ 1.0	+ 1.4	+ 2.2	+ 0.4
Real	- 1.1	- 3.5	+ 0.1	+ 0.6	+ 1.8	+ 0.2

¹ 10-year central government bonds (benchmark).

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Projections - March 2003

World economy

Percentage changes from previous year

	1999	2000	2001	2002	2003	2004	
Real GDP							
Total OECD	+ 3.2	+ 3.8	+ 0.8	+ 1.3	+ 1.5	+ 2.1	
USA	+ 4.1	+ 3.8	+ 0.3	+ 2.4	+ 2.3	+ 2.8	
Japan	+ 0.1	+ 2.8	+ 0.4	+ 0.3	+ 0.8	+ 1.3	
EU	+ 2.8	+ 3.5	+ 1.5	+ 0.9	+ 1.2	+ 1.8	
Euro area	+ 2.8	+ 3.5	+ 1.4	+ 0.8	+ 1.1	+ 1.8	
Germany	+ 2.0	+ 2.9	+ 0.6	+ 0.2	+ 0.5	+ 1.5	
Central Eastern Europe ¹	+ 3.2	+ 3.9	+ 2.3	+ 1.5	+ 2.5	+ 3.3	
World trade, volume							
World trade, volume	+ 6.0	+ 12.7	± 0.0	+ 2.5	+ 5.5	+ 6.3	
OECD exports	+ 5.7	+ 12.0	- 0.4	+ 1.0	+ 4.8	+ 6.0	
Intra-OECD trade	+ 7.8	+ 11.4	- 0.9	± 0.0	+ 3.5	+ 5.5	
Market growth²							
Market growth ²	+ 7.4	+ 12.8	+ 2.2	+ 1.0	+ 4.3	+ 6.5	
Primary commodity prices							
HWWA Index, total	+ 12.0	+ 32.0	- 11.0	+ 1.0	+ 13.0	- 15.0	
Excluding energy	- 8.0	+ 1.0	- 7.0	± 0.0	+ 5.0	- 3.0	
Crude oil prices							
Average import price (cif) for OECD countries	USD/barrel	17.3	28.0	23.5	24.5	29.0	23.0
Exchange rate							
USD per euro		1.067	0.924	0.896	0.945	1.08	1.08

¹ Poland, Slovak Republic, Slovenia, Czech Republic, and Hungary.

² Real import growth of trading partners weighted by Austrian export shares.

Private consumption, income and prices

	1999	2000	2001	2002	2003	2004
	Percentage changes from previous year, volume					
Private consumption expenditure	+ 2.3	+ 3.3	+ 1.5	+ 0.9	+ 1.4	+ 1.9
Durables	+ 7.3	+ 3.8	+ 2.0	- 0.2	+ 1.8	+ 3.1
Non-durables and services	+ 1.6	+ 3.2	+ 1.4	+ 1.1	+ 1.3	+ 1.7
Household disposable income	+ 2.3	+ 3.1	+ 0.4	+ 1.0	+ 1.3	+ 1.8
Household saving ratio						
As a percentage of disposable income	8.5	8.3	7.4	7.5	7.5	7.7
	Percentage changes from previous year					
Direct lending to domestic non-banks¹	+ 5.2	+ 6.7	+ 3.5	+ 2.8	+ 2.4	+ 2.5
Inflation rate				In percent		
National	0.6	2.3	2.7	1.8	1.9	1.4
Harmonised	0.5	2.0	2.3	1.7	2.0	1.4
Core inflation ²	0.7	0.9	2.3	2.0	2.2	1.7

¹ End of period.² Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

Productivity

Percentage changes from previous year

	1999	2000	2001	2002	2003	2004
Total economy						
Real GDP	+ 2.7	+ 3.5	+ 0.7	+ 1.0	+ 1.1	+ 1.7
Employment ¹	+ 1.4	+ 0.8	+ 0.7	- 0.4	+ 0.1	+ 0.4
Full-time equivalent	+ 1.3	+ 0.9	+ 0.5	- 0.6	- 0.2	+ 0.2
Productivity (GDP per employment)	+ 1.3	+ 2.8	+ 0.0	+ 1.4	+ 1.0	+ 1.4
Full-time equivalent	+ 1.5	+ 2.6	+ 0.2	+ 1.6	+ 1.3	+ 1.5
Manufacturing						
Production ²	+ 3.1	+ 6.5	+ 1.2	+ 0.1	+ 1.8	+ 3.0
Employees ³	- 0.7	+ 0.0	+ 0.2	- 2.5	- 1.9	- 1.0
Productivity per hour	+ 4.5	+ 6.6	+ 1.4	+ 3.6	+ 4.0	+ 4.1
Working hours per day per employee	- 0.6	- 0.1	- 0.4	- 0.9	- 0.2	- 0.1

¹ Dependent and self-employed according to National Accounts definition.

² Value added, volume.

³ According to Federation of Austrian Social Security Institutions.

⁴ According to 'Konjunkturerhebung' of Statistics Austria.

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Projections - March 2003

Earnings and international competitiveness

Percentage changes from previous year

	1999	2000	2001	2002	2003	2004
Gross earnings per employee ¹	+ 1.8	+ 2.5	+ 1.4	+ 2.2	+ 2.0	+ 2.4
Full-time equivalent	+ 2.2	+ 2.7	+ 1.7	+ 2.6	+ 2.3	+ 2.7
Gross real earnings per employee ¹	+ 1.0	+ 0.9	- 0.6	+ 0.3	+ 0.1	+ 1.0
Net real earnings per employee ¹	+ 0.5	+ 1.5	- 1.0	- 0.5	- 0.4	+ 0.4
Net wages and salaries	+ 3.7	+ 4.5	+ 1.9	+ 1.9	+ 2.1	+ 2.1
<i>Total economy</i>						
Unit labour costs	+ 0.4	- 0.5	+ 1.4	+ 0.7	+ 1.0	+ 1.0
<i>Manufacturing</i>						
Unit labour costs	- 1.2	- 4.5	+ 1.8	- 0.2	- 1.2	- 1.1
Relative unit labour costs ²						
Vis-à-vis trading partners	- 2.1	- 5.4	- 0.2	- 1.1	- 0.2	- 1.8
Vis-à-vis Germany	- 0.8	- 1.8	+ 0.3	- 1.2	- 1.3	- 1.7
Effective exchange rate - manufactures						
Nominal	+ 0.6	- 2.7	+ 0.9	+ 1.3	+ 2.0	+ 0.3
Real	- 1.3	- 3.4	+ 0.3	+ 0.8	+ 1.8	+ 0.2

¹ Employees according to National Accounts definition.

² In a common currency; minus sign indicates improvement of competitiveness.

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Projections - March 2003

Labour market

Changes from previous year (1,000⁵)

		1999	2000	2001	2002	2003	2004
Demand for labour							
Civilian employment ¹		+ 38.2	+ 30.8	+ 15.1	- 11.2	- 1.2	+ 11.5
Dependent employment ^{1,2}		+ 37.2	+ 28.9	+ 13.6	- 14.6	- 4.0	+ 10.0
	<i>Percentage changes from previous year</i>	+ 1.2	+ 1.0	+ 0.4	- 0.5	- 0.1	+ 0.3
Foreign workers		+ 7.8	+ 13.4	+ 9.5	+ 5.1	+ 5.0	+ 6.0
Self-employed ³		+ 1.0	+ 1.9	+ 1.5	+ 3.4	+ 2.8	+ 1.5
Labour supply							
Economically active population	(15-64)	+ 19.8	+ 25.2	+ 28.1	+ 22.9	+ 19.1	+ 1.0
	(15-59)	- 2.6	- 17.5	- 14.2	- 5.5	+ 3.1	+ 3.0
Total labour force ¹		+ 22.2	+ 3.4	+ 24.7	+ 17.3	+ 6.8	+ 11.5
Surplus of labour							
Registered unemployed ⁴		- 16.1	- 27.4	+ 9.6	+ 28.5	+ 8.0	± 0.0
	1,000 ⁵	221.7	194.3	203.9	232.4	240.4	240.4
Unemployment rate							
Percent of total labour force ⁵	%	3.9	3.7	3.6	4.1	4.2	4.2
Percent of total labour force ⁴	%	6.0	5.3	5.5	6.2	6.3	6.3
Percent of dependent labour forc	%	6.7	5.8	6.1	6.9	7.0	7.0
Participation rate^{1,6}							
	%	66.3	66.1	66.2	66.2	66.1	66.3
Employment rate^{1,7}							
	%	62.3	62.5	62.5	62.0	61.8	62.0

¹ Excluding parental leave and military service. ² According to Federation of Austrian Social Security Institutions.

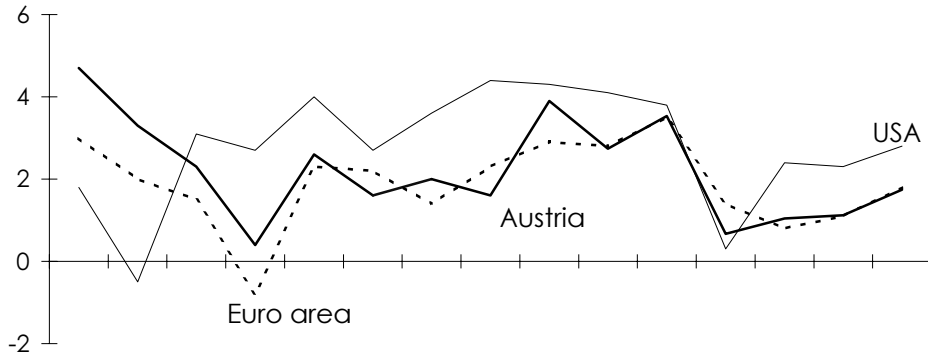
³ According to WIFO. ⁴ According to Labour Market Service. ⁵ According to Eurostat.

⁶ Total labour force as percent of economically active population (aged 15 to 64 years).

⁷ Employment as percent of economically active population (aged 15 to 64 years).

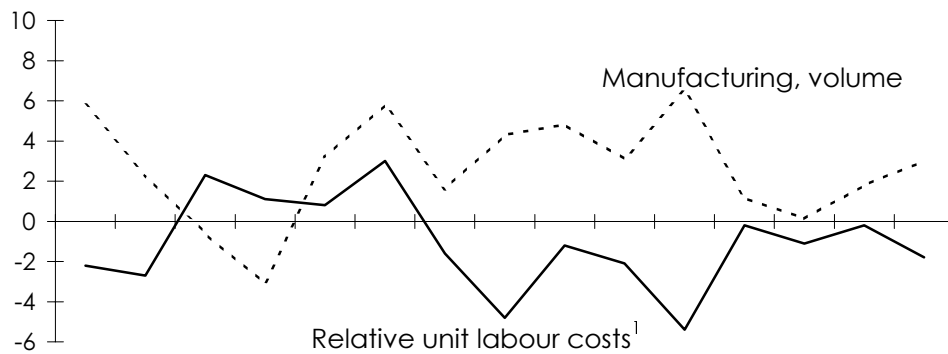
Growth of real GDP

In percent



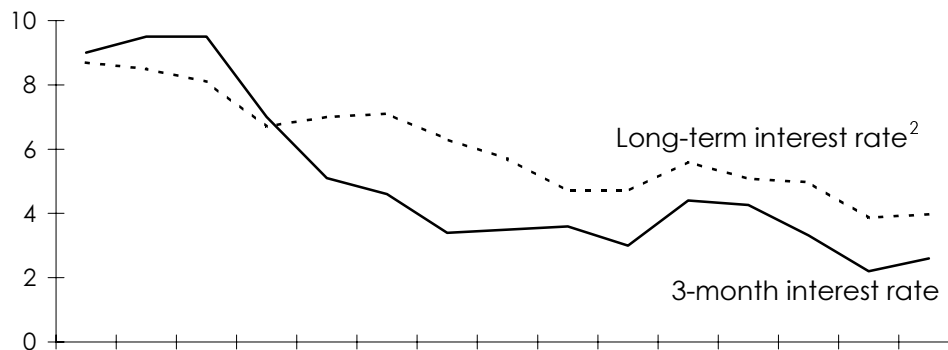
Competitiveness and manufacturing output

Percentage changes over previous year



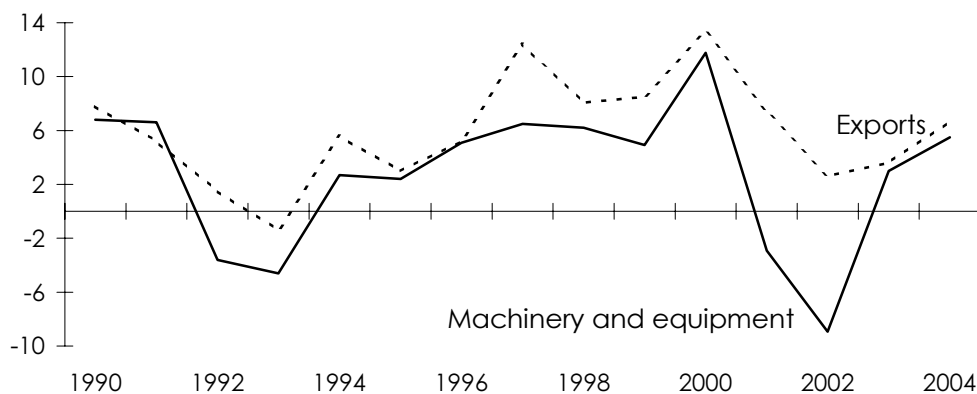
Short-term and long-term interest rates

In percent



Exports and gross fixed investment (constant prices)

Percentage changes over previous year

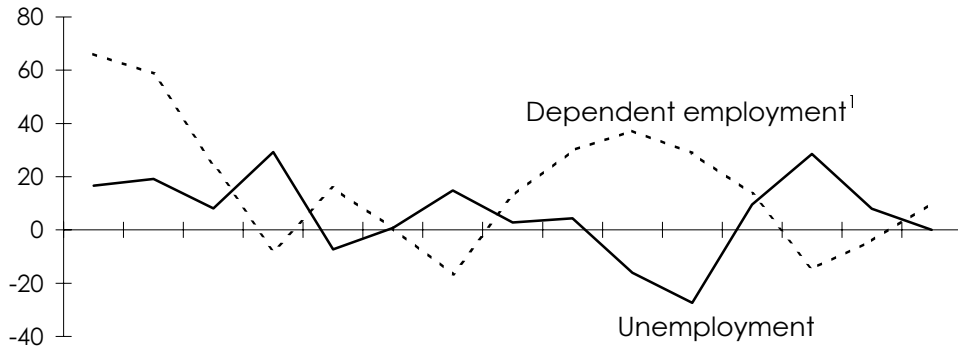


¹ Manufacturing; in a common currency vis-à-vis trading partners.

² 10-year central government bonds (benchmark).

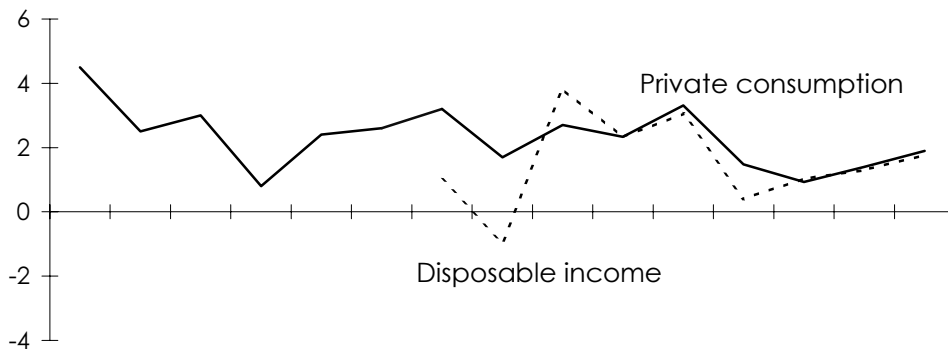
Employment and unemployment

1,000s over previous year



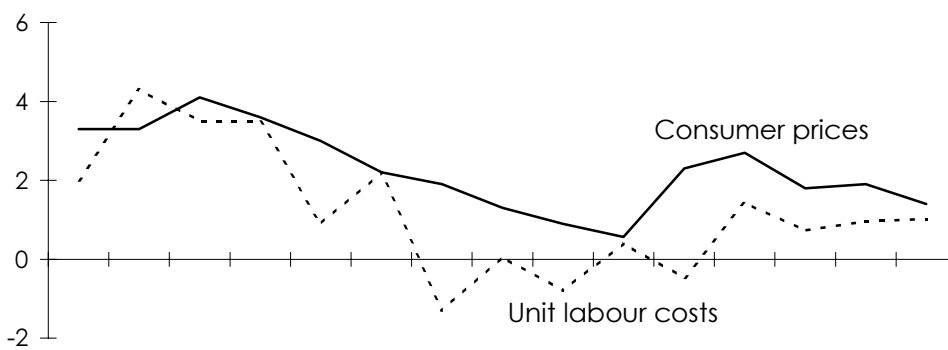
Consumption and income of private households (constant prices)

Percentage changes over previous year



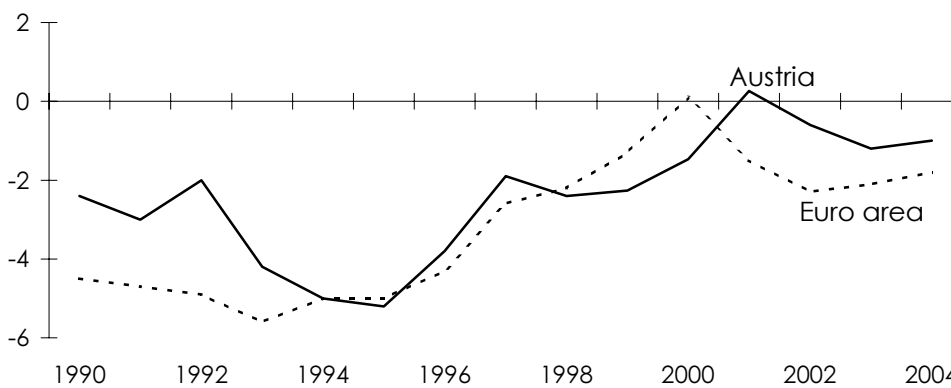
Inflation and unit labour costs

Percentage changes over previous year



General government financial balance

As a percentage of GDP



¹ Excluding parental leave and military service.

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