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GROWTH TO SLACKEN IN 1999 – TAX REFORM TO BOOST DOMESTIC DEMAND IN 2000

ECONOMIC OUTLOOK FOR 1999 AND 2000

Economic growth in Austria is expected to slip by 1 percentage point to 2.2 percent as a result of the sluggishness of the world economy. Private consumption, benefiting from the gains in purchasing power, will buoy economic activity in 1999 and, more strongly, in the year 2000.

The year 1999 is likely to see a weakening of economic growth by 1 percentage point to 2.2 percent. The crises in Asia, Russia, and Latin America have dampened the expansion of the world economy and render the present forecasts highly uncertain.

Exports, which have long been the mainstay of the upswing, are expected to grow only modestly, given the adverse conditions in foreign markets. Particularly hard hit will be sales to emerging markets afflicted by the financial turmoil. In the current year, weak foreign demand will have a negative impact not only on Austrian exports but also on capital outlays of those enterprises operating in international markets.

Economic activity in Austria continues to be supported by strong consumer spending which benefits from high real income gains. Real net wages and salaries are forecast to expand by 2¾ percent in the current year and by 3¼ percent in the year 2000, with part of the gains due to the "family package" and the tax reform 2000. The growth in real income will not only bolster consumer spending but also boost the savings ratio.

Thus, the effects of the sluggishness of the world economy are being partially offset by a revival of domestic demand. If, however, new crises were to develop or present risks to materialise, a new setback in the manufacturing sector would also shake consumer confidence.

On the downside, the costs of the tax reform and of the "family package" will burden the Federal budget in the year 2000. An increase in the general government deficit to 2½ percent of GDP seems likely, unless strict discipline is applied to gov-

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Table 1: Main results

		1996	1997	1998	1999	2000
		Percentage changes from previous year				
GDP						
Volume		+ 2.0	+ 2.5	+ 3.3	+ 2.2	+ 2.6
Value		+ 3.7	+ 4.1	+ 4.3	+ 3.2	+ 3.9
Manufacturing[1], volume		+ 1.2	+ 5.0	+ 5.0	+ 2.5	+ 3.8
Private consumption, volume		+ 2.0	+ 0.7	+ 1.7	+ 2.0	+ 2.4
Gross fixed investment, volume		+ 2.5	+ 2.8	+ 4.9	+ 3.1	+ 3.6
Machinery and equipment		+ 3.3	+ 5.0	+ 7.7	+ 5.0	+ 6.5
Construction		+ 2.4	+ 1.3	+ 3.0	+ 1.5	+ 1.0
Exports of goods[2]						
Volume		+ 5.4	+15.6	+ 7.1	+ 4.5	+ 6.5
Value		+ 5.5	+16.8	+ 7.1	+ 4.5	+ 7.4
Imports of goods[2]						
Volume		+ 6.1	+ 9.4	+ 8.4	+ 5.0	+ 6.5
Value		+ 6.7	+10.9	+ 6.8	+ 4.5	+ 7.4
Trade balance[2 3]	billion ATS	–100.6	–75.2	–78.4	–81.7	–87.8
	billion euro				– 5.9	– 6.4
Current balance[3]	billion ATS	– 52.3	–61.4	–51.6	–47.0	–46.6
	billion euro				– 3.4	– 3.4
	as a percentage of GDP	– 2.2	– 2.4	– 2.0	– 1.7	– 1.7
Long-term interest rate[4]	in percent	6.3	5.7	4.7	4.2	4.5
Consumer prices		+ 1.9	+ 1.3	+ 0.9	+ 0.7	+ 1.3
Unemployment rate						
percent of total labour force[5]		4.3	4.4	4.5	4.4	4.2
percent of dependent labour force[6]		7.0	7.1	7.2	7.1	6.9
Dependent employment[7]		– 0.6	+ 0.4	+ 1.0	+ 0.6	+ 1.0

[1] Value added, including mining and quarrying. – [2] According to Austrian Central Statistical Office. – [3] 1998: WIFO estimates. – [4] 10-year central government bonds (benchmark). – [5] According to Eurostat. – [6] According to Labour Market Service. – [7] Excluding parental leave and military service.

ernment expenditures. The goal of reducing the deficit of the public households to 1.4 percent of GDP by the year 2002 is only feasible if this condition is met.

In accordance with most international forecasting institutions, WIFO expects an acceleration in economic growth to 2.6 percent in the year 2000. In this scenario, which at present is the most likely, the economic slump which began in the middle of 1998 proves to be only temporary. This forecast is based on the expectation that the weakness in exports will be gradually overcome and that low interest rates will boost domestic demand. The international risks which might justify a more pessimistic scenario remain substantial, however.

Economic growth in Austria will probably not be strong enough to significantly reduce the unemployment rate. As the rise in the unemployment rate in 1998 was only due to special factors (parental leave regulations and the like), a slight decline from 4.5 percent in 1998 to 4.2 percent in 2000 can be expected; this moderation corresponds to a marked expansion in employment resulting from the advance in labour-intensive domestic demand.

The medium-term employment goal of the National Action Plan (1997-2002: +100,000 jobs) will be attained. The envisaged cut in the unemployment rate to 3.5 percent by the year 2002 seems only feasible if economic growth holds up, and if the high number of temporary lay-offs can be reduced.

Inflation does not present a problem for policy-makers for the foreseeable future. Thanks to lower prices of crude oil and the abolishment of monopolies in the public service sector, inflation is subdued and has reached a record low since 1955. This provides the European Central Bank enough leeway for easing monetary policy in the case of a serious economic setback.

THE WORLD ECONOMY IN THE GRIP OF THE FINANCIAL AND CURRENCY CRISES

The economic and currency crises in several emerging markets markedly weakened the growth of the global economy in 1998. Contrary to expectations, Europe suffered more from this turmoil than did the USA. The outlook for the international economy is characterised by unusually high uncertainty and risks.

The development of the world economy in 1998 was determined by the economic and currency crises in Asia, Russia, and Brazil. The economic slump in many emerging markets had an increasingly negative impact on economic activity in the industrialised countries. Surprisingly, the U.S. economy was only moderately affected by these developments and, thanks to a robust domestic demand, has until recently achieved high growth rates. Europe, however, recorded a marked slowdown in economic activity; in Japan, the recession deepened.

Many observers had feared that the economy of the USA, after having passed through a phase of speculative bubbles, was on the brink of a deep recession. Given the instability of the world economy, expectations were that such a slump in the USA would trigger a recession in the global economy.

Such a pessimistic scenario still cannot yet be excluded; a more probable outlook is for the U.S. economy to slow down to a growth rate of 3 percent in 1999. At present, there are no indications of inflationary tendencies, a real estate boom, nor signs of overheating in the U.S. economy, developments which would require abrupt corrective measures. Only the stock market shows signs of an excessively high level (relative to profit expectations) and a need for contractionary policies; it is unwarranted, however, to conclude that a recession is unavoidable[1].

[1] See Institut für Weltwirtschaft, Kieler Kurzberichte, 1999, (2).

Figure 1: Indicators of economic performance

[1] Vis-à-vis the euro zone. – [2] Manufacturing; in a common currency vis-à-vis trading partners. – [3] 10-year central government bonds (benchmark). – [4] Excluding parental leave and military service.

Even in 1999, the Asian crisis countries remain mired in a recession, despite bright spots in some sectors; in Japan, which experienced a decline in real GDP of 2.8 percent in 1998, the end of deflation is not in sight. In Latin America, stabilisation was achieved only at the cost of a deep recession, and in Russia neither the political crisis nor the debt problems have been solved. Thus, the risks have reached a level which far exceeds that of comparable forecasting situations. For example, the growth projections of Germany's economic institutes range from 1.4 percent to 2.8 percent.

A projection that draws a middle path between the most probable and a crisis scenario would not capture these risks. The present forecast assumes that the crises remain controllable at the political level. Clearly, a more pessimistic scenario is also realistic.

Most international forecasting institutions (IMF, OECD, EU, Institut für Weltwirtschaft and others) view the present slowdown as only a temporary phenomenon and predict a recovery of the global economy in the second half of 1999.

In Europe, the actual economic development as well as the business climate worsened considerably during the course of 1998. The latter was rather due to prices and profits than to the economic performance in real terms. It is to be rated as a positive sign that the business climate did not worsen further during the first months of the year

Table 2: World economy

	1996	1997	1998	1999	2000
	Percentage changes from previous year				
Real GDP					
Total OECD	+ 2.8	+ 2.9	+ 2.3	+ 2.0	+ 2.3
USA	+ 3.4	+ 3.9	+ 3.9	+ 3.0	+ 2.0
Japan	+ 3.9	+ 0.8	– 2.8	– 1.0	+ 1.0
EU	+ 1.8	+ 2.7	+ 2.8	+ 2.0	+ 2.8
Euro area	+ 1.6	+ 2.5	+ 3.0	+ 2.3	+ 2.8
Germany	+ 1.3	+ 2.2	+ 2.8	+ 1.8	+ 2.5
Central Eastern Europe[1]	+ 4.7	+ 5.0	+ 3.3	+ 3.0	+ 3.0
World trade, volume	+ 6.8	+ 9.8	+ 4.3	+ 4.3	+ 5.5
OECD exports	+ 6.3	+11.3	+ 4.0	+ 4.0	+ 5.5
Intra-OECD trade	+ 6.0	+11.5	+ 7.0	+ 4.5	+ 5.5
Market growth[2]	+ 6.2	+ 9.4	+ 6.6	+ 4.3	+ 6.0
Primary commodity prices, in USD					
HWWA index, total, 1990 = 100	+ 4.0	– 1.0	–23.0	– 9.0	+ 4.0
Excluding energy	– 9.0	+ 1.0	–13.0	– 5.0	+ 6.0
Crude oil prices					
Average import price (cif) for OECD countries USD per barrel	20.6	19.1	12.7	11.0	12.0
Exchange rate USD per ECU or euro	1.270	1.134	1.121	1.07	1.09

[1] Poland, Slovakia, Slovenia, Czech Republic, Hungary. – [2] Real import growth of trading partners weighted by Austrian export shares.

but more or less stabilised. Moreover, consumer confidence has continued to improve. In the euro zone, economic growth in 1999 is forecast to be around 2¼ percent; a rate of only 2 percent is expected for the EU (given the economic stagnation in the U.K.). With inflation and interest rates remaining low, domestic demand is forecast to rise substantially and, together with a recovery in exports, to buoy economic growth in the year 2000.

In Germany, economic activity has weakened markedly since the end of the summer. During the first months of 1999 the downward trend in the Ifo business climate index continued. Germany's producers of investment goods have been particularly hard hit by the shortfall in demand in Asia; merchandise exports to these countries plunged by one third. In 1999, the growth rate of Germany's economy is likely to drop to 1¾ percent, somewhat below the growth rate expected for the euro zone.

INTEREST RATE POLICY

Monetary policy is bound to play an important role for the future economic development. During the last few years, the U.S. central bank has operated monetary policy in an exemplary way and can take credit for the excellent performance of the U.S. economy in the 1990s. In 1998, the Federal Reserve Bank reacted to the worldwide turbulence in the financial markets with several swift interest rate cuts; these steps were intended to prop up the economy and to guarantee ample liquidity in the economy.

The present forecast assumes that, in view of the high dynamism of the U.S. economy in the fourth quarter of 1998, the Fed will raise interest rates slightly. The moderate price development does not provide grounds, however, for a pronounced restrictive monetary policy. Given the positive growth differential of the USA vis-à-vis Europe and rising interest rates in the USA, the dollar is likely to strengthen in 1999. A reversal can be expected for the year 2000, because at that time the European economies are forecast to grow faster than the U.S. economy.

The European Central Bank has decided on a monetary strategy which is compatible with an inflation rate of 2 percent. At present, the rate of inflation is below 1 percent in the euro zone. In the case of an economic recession, the European Central Bank will have to put forward credible arguments that it not only is ready to fight inflation but to counteract recessionary tendencies as well.

SUBSTANTIAL DECLINE IN EXPORTS TO NON-OECD COUNTRIES

The worldwide financial and currency crises have had a particularly strong impact on exports (in addition to the financial institutions). Austria's exports to non-OECD countries, especially to South-East Asia, Russia, the OPEC, and to Eastern Europe have collapsed. Setbacks in trade with the crisis countries were expected, but the extent of the losses surpassed expectations. Exports to Russia, for example, plunged by 60 percent in October and November on a year-on-year basis; exports to South-East Asia dropped by one third.

The moderate international growth forecasts and the persistent pessimistic assessment of foreign orders by enterprises indicate weak export growth in the current year. Merchandise exports should expand by only 4½ percent in 1999 (down from an estimated growth rate for 1998 of 7 percent). A sustained recovery in external economic conditions is unlikely before the year 2000.

The expected improvement in Austria's unit labour costs vis-à-vis the major trade partners suggests slight market share gains in the current and the next year. This comparison considers only the OECD countries, though; the massive devaluations of the emerging markets are not captured in these calculations.

GROWTH IN MANUFACTURING OUTPUT HALVED IN 1999

According to preliminary estimates by WIFO, Austria's economy grew by 3.3 percent in 1998. The expansion was based on the upswing in capital outlays and in private consumption and on the recovery in tourism. The dynamism in exports levelled off, however, with adverse effects

Table 3: Productivity

	1996	1997	1998	1999	2000
	Percentage changes from previous year				
Total economy					
Real GDP	+2.0	+2.5	+3.3	+2.2	+2.6
Employment[1]	–0.6	+0.1	+0.9	+0.6	+0.9
Productivity (GDP per employment)	+2.6	+2.4	+2.3	+1.6	+1.7
Manufacturing					
Production[2]	+1.3	+5.3	+5.1	+2.5	+3.8
Employees	–2.9	–1.4	+0.1	–0.7	–0.3
Productivity per hour	+4.6	+6.6	+4.8	+3.5	+4.5
Working hours per day for employees	–0.3	+0.2	+0.2	–0.3	–0.4

[1] Dependent and self-employed according to National Accounts. – [2] Value added.

Table 4: Private consumption

	1996	1997	1998	1999	2000
	Percentage changes from previous year, volume				
Private consumption	+2.0	+0.7	+1.7	+2.0	+2.4
Durables	+8.1	–3.5	+0.9	+2.5	+3.3
Non-durables and services	+1.1	+1.4	+1.8	+1.9	+2.3
Net wages and salaries	–1.9	–3.1	+1.9	+2.7	+3.2
Household disposable income	–0.2	+0.2	+2.7	+2.3	+2.8
	As a percentage of disposable income				
Household saving ratio	7.8	7.4	8.3	8.5	8.9

on manufacturing output. The sharp drop in prices in the wake of the crisis in Asia had a particularly severe impact on the basic industries (steel, chemical products) and some producers of technical goods (electronics). Demand for vehicles and consumer products remained strong, however.

After a persistent deterioration in the business climate in manufacturing during the second half of 1998, expectations stabilised during the first few months of the current year. A recovery is likely in the second half of 1999, given the upturn in domestic demand in the EU, unless new risks materialise in the emerging markets and impair the business climate. Even so, manufacturing output will expand by only 2½ percent in 1999, at half the rate of 1998.

SLOWDOWN IN INVESTMENT ACTIVITY

So far, the plunge in exports has had only a small impact on investment activity, which remained brisk in the second half of 1998. Apparently, the gloomy prospects for the foreign markets were offset by the more sanguine outlook for the domestic market. Investment in machinery and equipment rose by 7¾ percent in 1998.

In 1999, the expansion in capital outlays will slow down in the wake of reduced profits and the drop in prices. The investment plans in manufacturing (+6.5 percent) indicate a further expansion in 1999, however, unless heightened uncertainty calls for a postponement of projects scheduled to be realised in the current year. The adjustment problems of the year 2000 will trigger substantial investment spending on computer software. The millennium bug, though, is unlikely to cause major disturbances.

Construction activity in 1998 benefited from several special factors: clement winter weather and brisk tax-related renovation and modernisation business. The boom in the renovation and modernisation business will continue into the current year because house owners will move up housing repairs. Starting in the year 2000, maintenance reserves for tenant-occupied houses will no longer be tax-exempt, and a large gap in construction orders will open up: the construction of residential housing will markedly weaken, because demand has fallen off despite generous public subsidies. Civil engineering is recovering gradually from the cuts in public projects; the construction of office buildings appears to be emerging from the recession.

PRIVATE CONSUMPTION PROPS UP ECONOMIC ACTIVITY IN 1999 AND 2000

The rise in the purchasing power of private households will result in a robust expansion of consumer spending. The "family package" and tax cuts will help to buoy real disposable income.

As the negative effects of the fiscal consolidation "packages" vanished, private consumption expanded by a robust 1.7 percent in real terms. Growth in consumer spending is likely to accelerate in 1999 and 2000, because net real wages and salaries (including social transfers) should expand by 2¾ percent in 1999 and by 3¼ percent in 2000, the highest gains for the last seven years.

Low inflation rates, employment gains, and somewhat higher wage settlements are the main components supporting the substantial gains in real income. In contrast to the last few years, the public sector is also generating positive effects: the rise in transfers to families will boost household disposable income by ATS 12 billion; the reform of the income tax schedule will contribute some ATS 17 billion.

Given the strong increase in household income, the expected gains in consumer spending of 2 percent and 2.4 percent, respectively, seem rather modest, but some of the income gains will be absorbed into savings, as the savings ratio, after the hefty decline in 1996-97, reverts to its equilibrium.

Table 5: Earnings and international competitiveness

	1996	1997	1998	1999	2000
	Percentage changes from previous year				
Gross earnings per employee	+1.9	+0.7	+2.6	+2.8	+2.8
Gross real earnings per employee	–1.0	–1.3	+1.7	+2.1	+1.5
Net real earnings per employee	–2.3	–3.8	+1.2	+1.5	+2.4
Net wages and salaries	+0.9	–1.1	+2.9	+3.4	+4.5
Unit labour costs	–0.7	–1.3	+0.2	+1.2	+1.2
Manufacturing	–1.0	–5.0	–3.5	–1.0	–1.4
Relative unit labour costs[1]					
Vis-à-vis trading partners	–2.2	–4.9	–1.4	–1.2	–1.0
Vis-à-vis Germany	–0.6	–0.6	+0.1	–0.3	–0.4
Effective exchange rate – manufactures					
Nominal	–1.2	–1.8	+0.6	–0.3	+0.2
Real	–1.5	–2.6	±0.0	–1.4	–0.3

[1] Manufacturing, in a common currency; minus sign indicates improvement of competitiveness.

RISING TOURISM SURPLUSES

Rising surpluses in tourism characterised the development of the current account. Receipts from tourism (adjusted for price changes) increased steeply because Austria's price-determined competitive position strengthened, and the income situation in Germany, Austria's most important country of origin, improved.

The point of turnaround in the tourism balance indicates that relative prices (foreign exchange rates) are significant. Another crucial factor raising the tourism surplus was the structural improvement of domestic supply. At the same time, Austrians curtailed foreign travel and spending abroad.

According to preliminary estimates, the current account recorded a deficit of only ATS 52 billion, around ATS 10 billion less than in 1997. This reduction is mainly due to the improved performance in the tourism account; another factor is the plunge in oil prices, which narrowed the trade deficit. Still, in view of the lower-priced crude oil imports (ATS –3 billion) and the improvement in unit labour costs, the development of the trade balance is disappointing.

The deficit in the current account is forecast to decrease slightly in 1999 and 2000, still due to the improving tourism balance. The bill for crude oil, however, is likely to raise the deficit.

NO RISK OF INFLATION

In 1998, the moderation of inflation was mostly due to the drop in oil prices. The abolishment of monopolies in the public service sector and the deceleration in rent increases played a part as well.

Given the sluggishness of economic activity, price increases will remain subdued in 1999, with a rate of inflation below 1 percent. The turnaround in international crude oil prices and the pick-up in economic activity is expected to raise inflation to 1.3 percent in the year 2000. This forecast is based on the assumption that OPEC will be unsuccessful in raising oil prices.

The exceptionally low inflation rate in the euro zone should provide the European Central Bank enough leeway for easing monetary policy in the case of a serious economic setback.

SLIGHT DECLINE IN UNEMPLOYMENT

While in 1998 unemployment rose as a result of special factors, the number of jobless is forecast to drop slightly in 1999 and 2000. This development corresponds to a marked expansion in employment.

In 1998, the rise in unemployment was due to special factors: shortening of paid parental leave and tightening of criteria for early retirement[2]. Without these special factors, given the expansion in employment and the demographic development, unemployment should have declined in 1998 (by about 5,000 persons).

In the current year, the unemployment rate is forecast to decline slightly, despite the slowdown in economic activity. Unemployment is unlikely to be reduced substantially since the majority of the new jobs created are part-time jobs, while most of the unemployed are seeking full-time jobs.

If the economic forecast for the year 2000 comes true, unemployment will be cut significantly. The unemployment rate is likely to drop below the mark of 7 percent, according to the traditional Austrian method, and to approach the limit of 4 percent, according to the Eurostat method. This improvement will stem partly from various measures within the framework of the National Action Plan, particularly active labour market policies. In view of the great risks surrounding the current economic developments, the expected moderation in unemployment is fraught with great uncertainty.

The envisaged cut in the unemployment rate to 3.5 percent by the year 2002 seems within reach, but only if economic growth holds up, and if the number of temporary lay-offs – a sort of annualised short-term working – can be curtailed.

At the beginning of the current year, employment even in the cyclically sensitive manufacturing sector showed no

[2] See Marterbauer, M., Walterskirchen, E., "Determinants of the Rise of Unemployment in Austria", in this issue.

Table 6: Labour market

	1996	1997	1998	1999	2000
	Changes from previous year, in 1,000				
Demand for labour					
Civilian employment	–23.8	+ 8.8	+22.1	+16.6	+27.9
Dependent employment[1]	–20.9	+ 8.3	+21.1	+15.6	+27.0
Excluding parental leave and military service	–16.5	+12.8	+29.8	+18.0	+29.0
Percentage changes from previous year	– 0.6	+ 0.4	+ 1.0	+ 0.6	+ 1.0
Parental leave and military service[1]	– 4.4	– 4.4	– 8.7	– 2.4	– 2.0
Foreign workers	+ 0.0	– 1.6	– 0.2	+ 0.5	+ 0.7
Self-employed[2]	– 2.9	+ 0.5	+ 1.0	+ 1.0	+ 0.9
Labour supply					
Total labour force	– 9.0	+11.7	+26.5	+16.6	+20.1
Foreign	+ 2.8	– 1.7	+ 0.7	+ 0.3	+ 0.7
Migration of nationals	+ 4.9	+ 5.4	+ 5.5	+ 3.5	+ 2.0
Indigenous	–16.7	+ 8.0	+20.3	+12.8	+17.4
Surplus of labour					
Registered unemployed[3]	+14.8	+ 2.8	+ 4.4	± 0.0	– 7.8
In 1,000	230.5	233.3	237.8	237.8	230.0
Unemployment rate					
percent of total labour force[4]	4.3	4.4	4.5	4.4	4.2
percent of total labour force[3]	6.3	6.4	6.5	6.4	6.2
percent of dependent labour force[3]	7.0	7.1	7.2	7.1	6.9
Participation rate[5]	67.2	67.2	67.6	67.7	67.9
Employment rate[6]	62.9	62.9	63.2	63.4	63.7

[1] According to Association of Austrian Social Security Bodies. – [2] According to WIFO. – [3] According to Labour Market Service. – [4] According to Eurostat. – [5] Total labour force as a percentage of active population (aged 15 to 64). – [6] Employment as a percentage of active population (aged 15 to 64).

signs of a downswing. This could be interpreted as evidence that firms view the current downturn as a temporary phenomenon only. In 1999, employment is expected to rise by 18,000 persons, slightly less than in 1998.

TAX REFORM WILL RAISE GENERAL GOVERNMENT DEFICIT IN THE YEAR 2000

The general government deficit fluctuated around 2 percent during the period 1997 to 1999. As a result of the tax reform 2000, an increase to 2½ percent seems likely, unless strict discipline is applied to government spending.

In 1998, the general government deficit rose slightly despite favourable economic conditions. This was due to the termination of telecom license fees (1997) and the shortfall in the taxes on consumption and interest income. Nonetheless, the preliminary budget could be realised, largely as a result of an above-average rise in revenues from income taxes. The provinces and the municipalities recorded a surplus of ½ percent of GDP.

Table 7: Key policy indicators

	1996	1997	1998	1999	2000
	Billion ATS				
Fiscal policy					
Central government net balance	–89.4	–67.2	–67.0	–70.0	–81.0
	As a percentage of GDP				
Central government net balance	– 3.7	– 2.7	– 2.6	– 2.6	– 2.9
General government financial balance	– 3.7	– 1.9	– 2.1	– 2.1	– 2.5
	In percent				
Monetary policy					
3-month interest rate	3.4	3.5	3.6	3.2	3.3
Long-term interest rate[1]	6.3	5.7	4.7	4.2	4.5
Bond yield, average	5.3	4.8	4.4	4.0	4.2
	Percentage changes from previous year				
Effective exchange rate					
Nominal	– 1.5	– 2.3	+ 0.6	– 0.3	+ 0.4
Real	– 2.1	– 3.3	– 0.1	– 1.5	– 0.4

[1] 10-year central government bonds (benchmark).

The slowdown in economic activity in 1999 stems from exports rather than from domestic demand. As the wage bill and retail sales, the main factors determining revenues from the taxes on income and consumption, are likely to rise at a fast pace, the general government deficit will remain unchanged at 2 percent of GDP, despite the additional burden imposed by the first phase of the "family package". Thus, the deficit will remain within the limits of the Stability Pact.

The tax reform will put considerable strains on the Federal budget in 2000; if another consolidation package is to be avoided, strict discipline must be applied to government expenditures. In the absence of a draft budget, the WIFO forecast makes the assumption, in accordance with the political aims of the coalition government, that the net income tax relief will total ATS 17 billion, with about ATS 13 billion scheduled for the year 2000. The tax reform also includes measures to improve Austria as a location of business activity (e.g., tax credits for the training of apprentices and for research). Under these assumptions, the general government deficit can be expected to increase to 2½ percent of GDP, unless discretionary measures are taken on the spending side. Moreover, in the year 2000, the second phase of the "family package" will need to be financed. Thus, fiscal policy will face a particularly difficult task. The envisaged reduction in the deficit of the public households to 1.4 percent of GDP by the year 2002 is feasible only if economic growth holds up, and with strict discipline in public spending.

Cut-off date: 24 March 1999.