

■ BUDGETARY AND LABOUR MARKET POLICIES FACING MAJOR CHALLENGES DESPITE FASTER GROWTH

ECONOMIC OUTLOOK FOR 1999 TO 2001

WIFO is upholding its projections for real GDP growth of 2.2 percent in 1999 and 2.8 percent in 2000. A first outlook into 2001 suggests demand and output may continue rising at an above-average pace of 2¾ percent. Unabated strength of domestic demand should be accompanied by livelier exports and industrial activity. Price stability is set to remain high. The crucial challenges for economic policy will be public sector borrowing and unemployment: on both accounts, the government will, from today's perspective, fail to meet its own targets.

The present business cycle projections are the first ones to be based upon the new System of National Accounts ESA 1995. This implies a number of conceptual changes, and the new set of data established by STATÖ, the Statistics Austria, is not yet complete. On the new data base, real GDP in the third quarter 1999 rose by around 3 percent from the year-earlier level. For the whole of 1999, WIFO maintains its projection of 2.2 percent, unchanged since last March.

In the first half of 1999, growth was driven almost entirely by domestic demand. A favourable employment trend, rising incomes and continued price stability strongly boosted private consumer spending. As from mid-year, lively consumer demand has been supplemented by a recovery of exports and industrial activity. Manufacturing output, having receded in the first semester, advanced by approximately 4 percent year-on-year in the third quarter.

In 2000, the Austrian economy should benefit from an improvement in international framework conditions: business activity, while remaining firm in the USA, is set to gain momentum in Europe, due to a weak Euro as well as to domestic demand strength (notably in France, Spain and some of the smaller EU countries). In Germany, however, recovery remains subdued under the impact of a

restrictive policy stance. Trading partners in Eastern Europe are gradually ridding themselves of restraining forces on economic activity.

Austrian exports are benefiting not only from an accelerating expansion of foreign markets, but also from sizeable gains in competitiveness owing to substantial advances in productivity and pronounced wage moderation. Strong growth of merchandise exports (+7 percent in volume) is giving momentum also to manufacturing output (+4.3 percent) and investment in machinery and equipment (+7 percent). These estimates are confirmed by the very high level of business confidence, as sampled in the WIFO business survey.

In 2000, private consumption will receive additional stimulus. Although gains in gross wages per capita will be squeezed by modest wage settlements, a generous tax reform and yet another raise in family benefits will make for a marked increase in net household income from employment and transfers (+2¾ percent adjusted for inflation). This will give strong upward drift to retail sales, and to consumer spending altogether. In 2001, consumer demand may move ahead at a slower pace, assuming a resumption of budgetary consolidation efforts. Construction activity is expected to remain lagging behind the overall trend in domestic demand, it being dragged down by a decline in residential building.

Government policy should take the opportunity offered by favourable prospects for economic growth to address the key problem areas, i.e., to strive for consolidation of government households, and for a reduction in unemployment. Cuts in private income and business taxes by some ATS 20 billion in the context of the tax reform 2000 will put heavy strain on public finances. With no Federal budget draft for 2000 having yet been submitted, the Minister of Finance has been led to cut Ministries' uncommitted spending by a total of about ATS 20 billion. Incorporating this move, the present projections arrive at a total net government borrowing of 2.2 percent of GDP for 2000, and of 1.9 percent for 2001. EMU obligations and, even more, the need to create scope for the operation of automatic fiscal stabilisers in adverse cyclical periods require therefore further action of budgetary retrenchment.

The Federal Government has not only set medium-term targets for fiscal policy, in the Stability Programme, but also for the labour market up to 2002, with the 1997 National Action Plan for Employment. Dependent employment is to be raised by 100,000, the unemployment rate to be lowered to 3½ percent. The projected pick-up in economic growth should make for a strong increase in the number of jobs, allowing the employment target to be reached already by 2001 – if only, however, with regard to the number of employment contracts, and not of full-time equivalents, given the strong expansion of part-time work. The rate of unemployment (EU defini-

Main results

| | | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|----------------|---------------------------------------|-------|-------|-------|-------|
| | | Percentage changes from previous year | | | | |
| GDP | | | | | | |
| Volume | | + 1.2 | + 2.9 | + 2.2 | + 2.8 | + 2.8 |
| Value | | + 2.8 | + 3.5 | + 2.9 | + 3.6 | + 3.9 |
| Manufacturing ¹⁾ , volume | | + 3.8 | + 3.4 | + 2.3 | + 4.3 | + 4.3 |
| Private consumption expenditure, volume | | + 0.1 | + 1.5 | + 2.3 | + 2.7 | + 2.3 |
| Gross fixed investment, volume | | + 0.8 | + 6.8 | + 3.3 | + 3.9 | + 4.2 |
| Machinery and equipment ²⁾ | | + 4.6 | +10.6 | + 6.0 | + 7.0 | + 7.0 |
| Construction | | - 1.6 | + 4.1 | + 1.3 | + 1.5 | + 2.0 |
| Exports of goods ³⁾ | | | | | | |
| Volume | | +16.5 | + 8.1 | + 4.5 | + 7.0 | + 7.0 |
| Value | | +16.8 | + 8.4 | + 4.8 | + 8.1 | + 8.1 |
| Imports of goods ³⁾ | | | | | | |
| Volume | | + 9.4 | + 7.1 | + 6.2 | + 6.5 | + 6.5 |
| Value | | +10.9 | + 6.6 | + 6.7 | + 8.1 | + 7.6 |
| Trade balance ³⁾ | (billion ATS) | -75.2 | -67.4 | -86.8 | -94.0 | -96.7 |
| | (billion Euro) | | | - 6.3 | - 6.8 | - 7.0 |
| Current balance | (billion ATS) | -64.1 | -56.8 | -61.2 | -64.7 | -57.6 |
| | (billion Euro) | | | - 4.4 | - 4.7 | - 4.2 |
| As a percentage of GDP | (%) | - 2.5 | - 2.2 | - 2.3 | - 2.3 | - 2.0 |
| Long-term interest rate ⁴⁾ | (%) | 5.7 | 4.7 | 4.7 | 5.5 | 5.7 |
| Consumer prices | | + 1.3 | + 0.9 | + 0.5 | + 1.1 | + 1.0 |
| Unemployment rate | | | | | | |
| Percent of total labour force ⁵⁾ | (%) | 4.4 | 4.7 | 4.4 | 4.2 | 4.1 |
| Percent of dependent labour force ⁶⁾ | (%) | 7.1 | 7.2 | 6.7 | 6.5 | 6.2 |
| Dependent employment ⁷⁾ | | + 0.4 | + 1.0 | + 1.2 | + 1.0 | + 0.9 |
| General government financial balance | | | | | | |
| As a percentage of GDP | (%) | - 1.9 | - 2.4 | - 2.1 | - 2.2 | - 1.9 |

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

tion) will decline to 4.1 percent of the labour force by 2001, a further fall to 3½ percent in 2002 may be achieved only under the assumption of a further increase in financial resources for active labour market and training measures, and of stronger emphasis being put on the creation of full-time jobs.

The Austrian economy has entered a period of marked upturn, driven by both domestic and export demand. Supply constraints are unlikely to emerge over the projection period, given strong investment activity and considerable labour market reserves (high unemployment and growing labour supply). This is confirmed also by the prospects for sustained price stability – consumer price inflation being expected at an annual rate of only 1.1 percent in 2000. The risks of the present projections are located at the international level. Economic activity in the two most important trading partner countries, Germany and Italy, is distinctly lagging behind that in most other EU countries. In both countries, monetary and fiscal policies have turned restrictive in the early stages of a still hesitant recovery. The situation in the USA is marked by strong macro-economic imbalances in the form of a high current account deficit and an extraordinarily low saving ratio of private households; if the latter were to revert to a normal level, there would be a risk for an abrupt end to the by now over-extended boom period.

Cut-off date: 15 December 1999.