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**Exports and Investment Adding
Momentum to Cyclical Activity
Economic Outlook for 2006 and 2007**

June 2006

Exports and Investment Adding Momentum to Cyclical Activity

Economic Outlook for 2006 and 2007

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Economic Outlook for 2006 and 2007: Exports and Investment Adding Momentum to Cyclical Activity

Driven by exports and investment, demand and output in Austria are growing by 2.6 percent in volume in 2006, the highest rate since 2000. By contrast, the momentum of private consumption remains subdued, despite the boost to net incomes from the tax reform. The jump in oil prices is hardly giving rise to second-round effects via wage increases, thereby holding back inflation, but also real income gains. In 2007, the one-off effects from Germany will turn negative, slowing GDP growth in Austria to 2.1 percent.

For 2006, WIFO expects real GDP to rise by 2.6 percent, an upward revision from the projection of last March by 0.2 percentage points. The more optimistic assessment is motivated by the performance of exports and investment which both have gained momentum this year.

Exports of goods in 2006 are expected to advance by 8 percent in volume, fuelled by strong global activity and a high degree of price competitiveness. In east-central Europe and in Asia, economic growth is somewhat stronger still than expected, and the re-cycling of oil revenues is boosting imports of Russia and the OPEC countries.

The positive sentiment in the business sector is becoming clearly reflected in higher investment plans. According to the latest WIFO investment survey, manufacturers intend to spend 15 percent more than last year on new capital, an increase almost twice as high as that sampled last autumn. Indeed, manufacturing industry, benefiting from strong gains in exports and corporate earnings, is in a particularly favourable situation, whereas investment for the economy as a whole will post a significantly smaller increase. This seems to be confirmed by the rather cautious responses in the investment survey conducted by the Austrian Economic Chamber.

Private consumption has so far not picked up substantially. While employment growth is strengthening private disposable income, real earnings per capita

advance at a modest pace. With the household saving ratio broadly unchanged, private consumption will grow by nearly 2 percent in real terms this year.

In 2006, the Austrian economy stands to benefit from purchases in Germany carried forward ahead of the increase in the standard VAT rate. The corresponding negative echo-effect will dampen activity in 2007, suggesting a slowdown in Austrian GDP growth to an annual rate of 2.1 percent.

The cyclical revival this year is raising overall employment by a strong 40,000 or 1.3 percent. Demand for new labour is likely to extend to full-time workers, as suggested by the substantial increase in male jobs and jobs in typical full-time branches like manufacturing and construction. The number of unemployed, down by 11,000 from last year mainly on account of more people being enrolled in job training, should rebound in 2007 as funds for active labour market policy are planned to be cut. The total of jobseekers, including people undergoing training, will stay broadly constant this year and next. Therefore, the cyclical strengthening, while sufficient for the absorption of the substantial additional labour supply, will not make significant inroads into the existing stock of unemployment.

Headline inflation will remain relatively low, at a projected 1¼ percent in 2006 and 2007. The hike in oil prices has so far had only little inflationary impact: second-round effects via stronger wage increases are reined back by the persistent high unemployment and employees' implicit weak bargaining position. Even for goods and services of high energy intensity, indirect price effects have been limited. A key price-dampening factor is the rise in low-cost imports of manufactures. The rise of China and other transition economies has thus two contradictory effects: on the one hand it is a main driver of higher energy and commodity prices, but it puts downward pressure on import prices of manufactures, on the other.

The general government deficit turned out lower in 2005 than expected, mainly due to higher receipts from corporate tax. In the current year, the budget will be burdened by the revenue shortfalls from the 2005 tax reform and its lagged impact on profit taxes. Higher outlays for active labour market policy and research act as additional drag. The general government deficit for 2006 is expected at 1.7 percent of GDP, slightly higher than last year. Since no Federal budget draft has yet been

submitted for 2007, the assessment of further fiscal developments is necessarily vague. A "package" of measures in support of medium-sized enterprises, worth € 200 million, has been finalised; while it will take effect in 2007, its budgetary impact will largely show up only in the subsequent years. The more favourable business conditions will probably lead to a lower budget deficit in 2007, provided that a restrictive stance is applied to government spending and the second stage of the administrative reform is implemented without delay.

Vienna, 28 June 2006.

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Projections - June 2006

Main results

Percentage changes from previous year

		2002	2003	2004	2005	2006	2007
GDP							
Volume		+ 1.0	+ 1.4	+ 2.4	+ 1.8	+ 2.6	+ 2.1
Value		+ 2.2	+ 2.8	+ 4.4	+ 3.8	+ 4.4	+ 3.9
Manufacturing¹, volume		+ 0.4	- 0.1	+ 4.6	+ 3.1	+ 5.5	+ 4.5
Wholesale and retail trade, volume		+ 2.0	+ 0.3	+ 1.9	+ 0.4	+ 1.9	+ 2.0
Private consumption expenditure, volume		+ 0.3	+ 1.6	+ 0.8	+ 1.4	+ 1.9	+ 2.0
Gross fixed investment, volume		- 5.0	+ 6.1	+ 0.6	+ 1.6	+ 3.6	+ 3.3
Machinery and equipment ²		- 8.2	+ 7.7	+ 0.8	+ 1.4	+ 5.0	+ 5.0
Construction		- 2.3	+ 4.8	+ 0.5	+ 1.8	+ 2.5	+ 2.0
Exports of goods³							
Volume		+ 4.3	+ 2.6	+ 12.9	+ 4.0	+ 8.0	+ 5.7
Value		+ 4.2	+ 1.9	+ 13.9	+ 5.4	+ 10.7	+ 6.8
Imports of goods³							
Volume		+ 0.3	+ 6.5	+ 11.4	+ 2.9	+ 6.9	+ 6.0
Value		- 2.0	+ 5.0	+ 12.5	+ 5.9	+ 10.5	+ 7.3
Current balance	€ bn	+ 0.75	- 0.48	+ 0.36	+ 3.01	+ 3.02	+ 2.40
	as a percentage of GDP	+ 0.3	- 0.2	+ 0.2	+ 1.2	+ 1.2	+ 0.9
Long-term interest rate⁴	percent	5.0	4.2	4.2	3.4	4.1	4.3
Consumer prices		+ 1.8	+ 1.3	+ 2.1	+ 2.3	+ 1.7	+ 1.8
Unemployment rate							
Eurostat definition ⁵	percent	4.2	4.3	4.8	5.2	5.0	5.1
National definition ⁶	percent	6.9	7.0	7.1	7.3	6.9	7.0
Persons in active dependent employment⁷		- 0.5	+ 0.2	+ 0.7	+ 1.0	+ 1.3	+ 1.1
General government financial balance							
according to Maastricht definition							
as a percentage of GDP		- 0.5	- 1.5	- 1.1	- 1.5	- 1.7	- 1.3

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 Labour Force Survey. ⁶ According to Labour Market Service, percent of total labour force excluding self employed. ⁷ Excluding parental leave, military service, and unemployed persons in training.

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Key policy indicators

	2002	2003	2004	2005	2006	2007
Fiscal policy						
	As a percentage of GDP					
General government financial balance						
according to Maastricht definition	- 0.5	- 1.5	- 1.1	- 1.5	- 1.7	- 1.3
according to National accounts	- 0.7	- 1.7	- 1.2	- 1.6	- 1.8	- 1.4
General government primary balance	+ 2.6	+ 1.4	+ 1.7	+ 1.2	+ 1.1	+ 1.4
Monetary policy						
	Percent					
3-month interest rate	3.3	2.3	2.1	2.2	3.0	3.3
Long-term interest rate ¹	5.0	4.2	4.2	3.4	4.1	4.3
	Percentage changes from previous year					
Effective exchange rate						
Nominal	+ 1.3	+ 3.8	+ 1.2	- 0.6	± 0.0	- 0.1
Real	+ 0.6	+ 2.8	+ 0.9	- 0.7	- 0.7	- 0.8

¹ 10-year central government bonds (benchmark).

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World economy

Percentage changes from previous year

	2002	2003	2004	2005	2006	2007
Real GDP						
World	+ 3.0	+ 4.1	+ 5.1	+ 4.5	+ 4.6	+ 4.4
Total OECD	+ 1.4	+ 2.0	+ 3.3	+ 2.7	+ 3.0	+ 2.8
USA	+ 1.6	+ 2.7	+ 4.2	+ 3.5	+ 3.3	+ 3.0
Japan	+ 0.1	+ 1.8	+ 2.3	+ 2.6	+ 2.8	+ 2.5
EU 25	+ 1.2	+ 1.2	+ 2.4	+ 1.6	+ 2.2	+ 2.0
EU 15	+ 1.1	+ 1.0	+ 2.3	+ 1.5	+ 2.1	+ 1.9
Euro area	+ 0.9	+ 0.7	+ 2.1	+ 1.3	+ 2.1	+ 1.9
Germany	+ 0.1	- 0.2	+ 1.6	+ 1.0	+ 1.9	+ 1.2
New members ¹	+ 2.5	+ 3.9	+ 5.2	+ 4.4	+ 4.7	+ 4.8
China	+ 9.1	+ 10.0	+ 10.1	+ 9.9	+ 9.5	+ 9.0
World trade, volume	+ 3.5	+ 5.1	+ 10.0	+ 7.0	+ 8.5	+ 8.0
Market growth²	+ 2.0	+ 5.6	+ 9.1	+ 6.8	+ 7.8	+ 5.5
Primary commodity prices						
HWWA Index, total	- 5	- 4	+ 18	+ 29	+ 30	+ 2
Excluding energy	- 6	- 6	+ 18	+ 6	+ 20	+ 6
Crude oil prices						
Average import price (cif) for OECD countries	24.1	28.4	36.3	50.3	68.0	68.0
Exchange rate						
USD per euro	0.945	1.131	1.243	1.245	1.25	1.25

¹ Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, Slovenia.

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

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Projections - June 2006

Private consumption, income and prices

	2002	2003	2004	2005	2006	2007
	Percentage changes from previous year, volume					
Private consumption expenditure	+ 0.3	+ 1.6	+ 0.8	+ 1.4	+ 1.9	+ 2.0
Durables	+ 0.3	+ 3.2	+ 0.6	+ 1.7	+ 2.4	+ 2.2
Non-durables and services	+ 0.3	+ 1.5	+ 0.8	+ 1.4	+ 1.8	+ 2.0
Household disposable income	+ 0.7	+ 2.3	+ 1.2	+ 1.9	+ 2.0	+ 2.0
Household saving ratio						
As a percentage of disposable income	7.7	8.6	9.0	9.3	9.4	9.5
	Percentage changes from previous year					
Direct lending to domestic non-banks¹	+ 1.2	+ 1.6	+ 5.0	+ 4.7	+ 5.4	+ 5.0
	Percentage changes from previous year					
Inflation rate						
National	1.8	1.3	2.1	2.3	1.7	1.8
Harmonised	1.7	1.3	2.0	2.1	1.9	1.9
Core inflation ²	2.0	1.3	1.6	1.5	1.6	1.9

¹ End of period.

² Excluding unprocessed food (meat, fish, fruits, vegetables) and energy items.

Productivity

Percentage changes from previous year

	2002	2003	2004	2005	2006	2007
Total economy						
Real GDP	+ 1.0	+ 1.4	+ 2.4	+ 1.8	+ 2.6	+ 2.1
Employment ¹	- 0.1	+ 0.1	- 0.0	+ 0.9	+ 1.1	+ 0.9
Productivity (GDP per employment)	+ 1.1	+ 1.3	+ 2.5	+ 0.9	+ 1.4	+ 1.2
Manufacturing						
Production ²	+ 0.4	- 0.0	+ 4.7	+ 3.2	+ 5.5	+ 4.5
Employees ³	- 2.5	- 1.7	- 0.6	- 0.9	- 0.2	- 0.5
Productivity per hour	+ 3.5	+ 1.3	+ 4.5	+ 4.7	+ 5.3	+ 5.0
Working hours per day per employee ⁴	- 0.5	+ 0.3	+ 0.8	- 0.6	+ 0.4	± 0.0

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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Earnings and international competitiveness

Percentage changes from previous year

	2002	2003	2004	2005	2006	2007
Gross earnings per employee ¹	+ 2.2	+ 1.9	+ 2.0	+ 2.4	+ 2.8	+ 2.5
Gross real earnings per employee ¹	+ 1.2	+ 0.4	+ 0.0	+ 0.4	+ 1.1	+ 0.7
Net real earnings per employee ¹	+ 1.0	+ 0.1	+ 0.3	+ 1.0	+ 0.7	+ 0.4
<i>Total economy</i>						
Unit labour costs	+ 1.0	+ 0.6	- 0.3	+ 1.5	+ 1.4	+ 1.3
<i>Manufacturing</i>						
Unit labour costs	- 0.3	- 0.1	- 3.5	- 1.2	- 2.4	- 2.2
Relative unit labour costs²						
Vis-à-vis trading partners	- 0.7	+ 2.7	- 0.7	- 0.5	- 1.4	- 1.5
Vis-à-vis Germany	- 1.5	+ 1.5	+ 0.4	+ 2.3	+ 0.1	- 0.2
Effective exchange rate - manufactures						
Nominal	+ 1.2	+ 3.7	+ 1.2	- 0.5	± 0.0	- 0.1
Real	+ 0.8	+ 2.9	+ 1.0	- 0.5	- 0.5	- 0.8

¹ Employees according to National Accounts definition.

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

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Labour market

Changes from previous year (1,000^s)

		2002	2003	2004	2005	2006	2007
Demand for labour							
Persons in active employment ¹		- 11.6	+ 8.5	+ 25.1	+ 37.2	+ 45.5	+ 39.5
Employees ²		- 15.0	+ 5.5	+ 21.1	+ 31.9	+ 40.0	+ 34.0
<i>Percentage changes from previous year</i>		- 0.5	+ 0.2	+ 0.7	+ 1.0	+ 1.3	+ 1.1
Nationals		- 20.1	- 10.4	+ 9.2	+ 20.0	+ 24.0	+ 20.0
Foreign workers		+ 5.1	+ 15.9	+ 11.9	+ 11.9	+ 16.0	+ 14.0
Self-employed ³		+ 3.4	+ 3.0	+ 4.0	+ 5.3	+ 5.5	+ 5.5
Labour supply							
Population of working age	(15 to 64 years)	+ 42.9	+ 37.7	+ 34.4	+ 15.6	+ 6.1	+ 20.2
	(15 to 59 years)	+ 13.4	+ 21.2	+ 35.6	+ 48.5	+ 37.7	+ 24.9
Labour force ⁴		+ 17.0	+ 16.1	+ 28.9	+ 45.9	+ 34.5	+ 47.5
Surplus of labour							
Registered unemployed ⁵		+ 28.5	+ 7.7	+ 3.8	+ 8.8	- 11.0	+ 8.0
	1,000 ^s	232.4	240.1	243.9	252.7	241.7	249.7
Unemployment rate							
Eurostat definition ⁶	percent	4.2	4.3	4.8	5.2	5.0	5.1
Percent of total labour force ⁵	percent	6.2	6.3	6.4	6.5	6.2	6.3
National definition ^{5,7}	percent	6.9	7.0	7.1	7.3	6.9	7.0
Employment rate							
Persons in active employment ^{1,8}	percent	62.5	62.2	62.3	62.8	63.5	64.0
Total employment (Eurostat) ^{6,8,9}	percent	-	-	67.8	68.6	68.9	69.2

¹ Excluding parental leave, military service, and unemployed persons in training. ² According to Federation of Austrian Social Security Institutions. ³ According to WIFO. ⁴ Economically active employment plus unemployment.

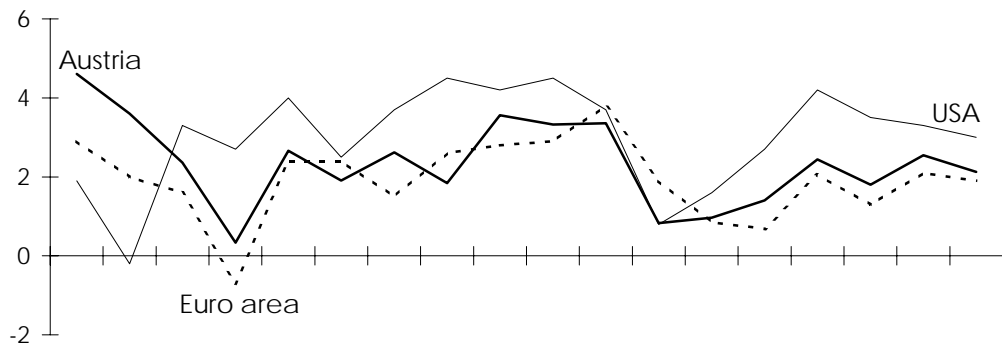
⁵ According to Labour Market Service. ⁶ According to Eurostat Labour Force Survey.

⁷ Percent of total labour force excl. self-employed. ⁸ Percent of population of working age (15 to 64 years).

⁹ Changed survey method.

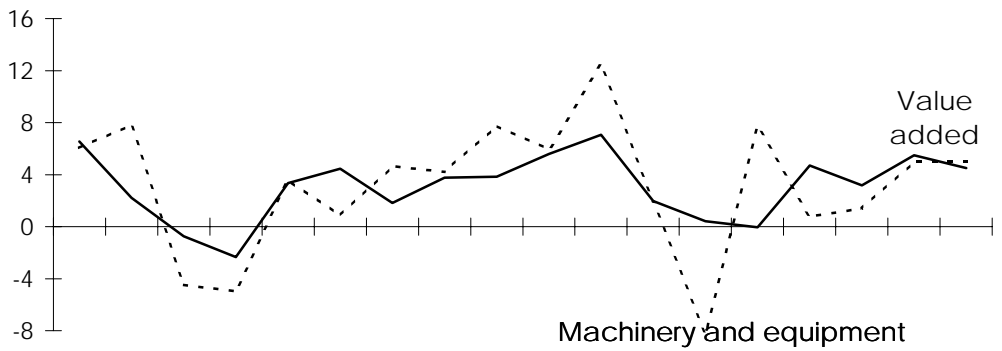
Growth of real GDP

Percent



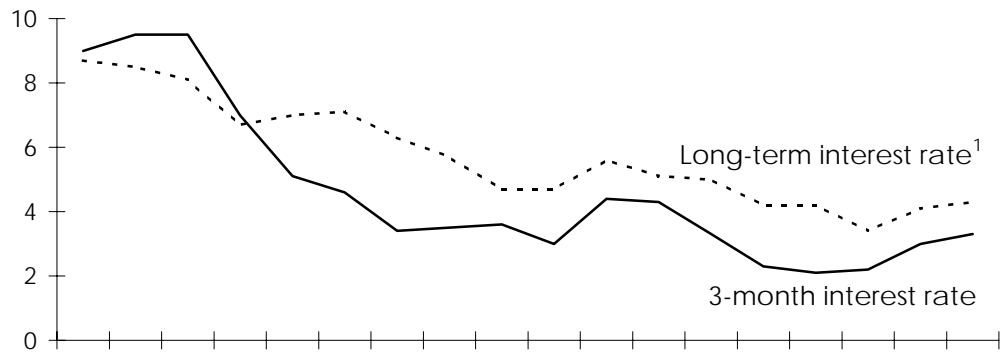
Manufacturing and investment

Percentage changes from previous year, volume



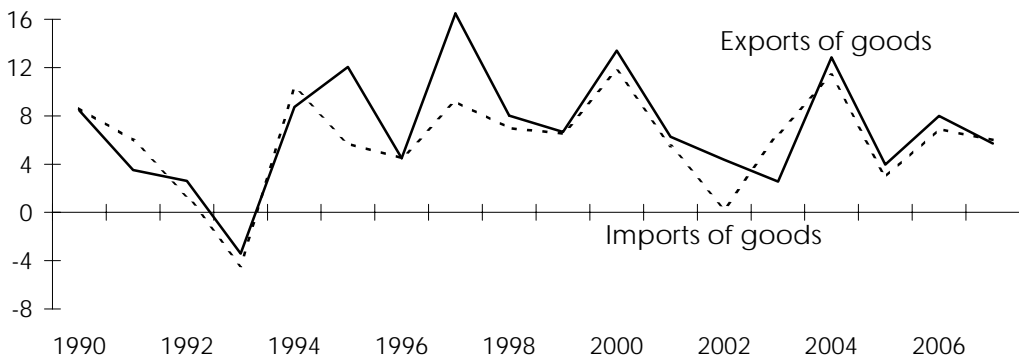
Short-term and long-term interest rates

Percent



Trade

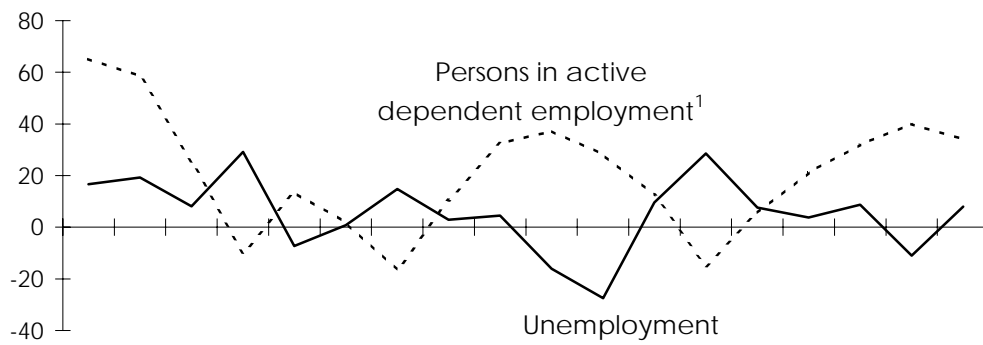
Percentage changes from previous year, volume



¹ 10-year central government bonds (benchmark).

Employment and unemployment

1,000^s from previous year



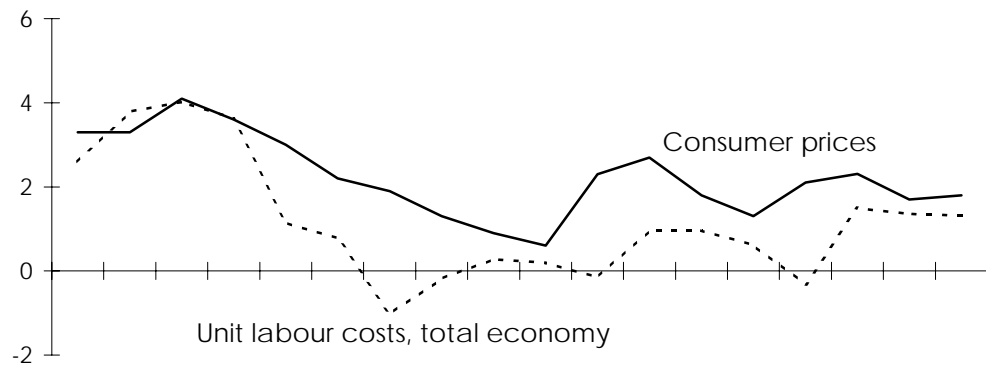
Consumption and income

Percentage changes from previous year, volume



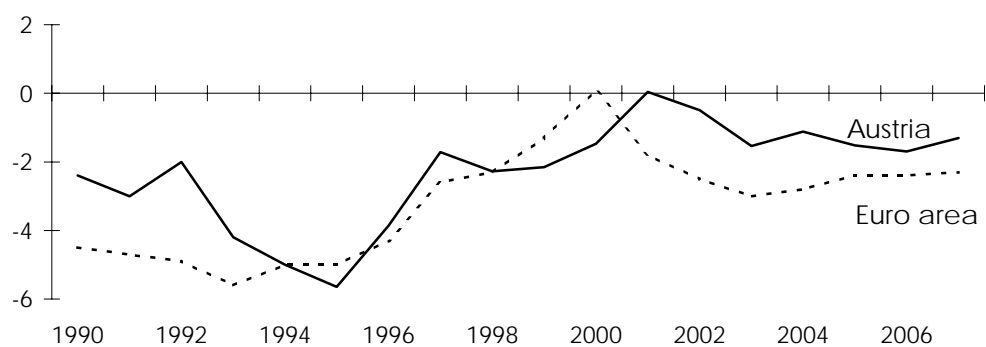
Inflation and unit labour costs

Percentage changes from previous year



General government financial balance

As a percentage of GDP



¹ Excluding parental leave, military service, and unemployed persons in training.

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