

■ MARKED SLOWDOWN OF GROWTH IN EUROPE DAMPENING DOMESTIC BUSINESS ACTIVITY

ECONOMIC OUTLOOK FOR 2001 AND 2002

Economic growth in Austria is set to decelerate from 3.3 percent in 2000 to 1.7 percent this year, and may pick up to slightly above 2 percent in 2002. The slowdown is mainly due to weaker activity in Europe which itself is the consequence of the abrupt cyclical slackening in the USA and of higher energy costs. A further deterioration of business conditions in Europe may not be excluded, given the hesitant reaction of economic policy. Domestic demand in Austria should prove relatively robust, although construction activity is showing clear signs of weakness. The projection for inflation has been revised substantially upwards, both for this year and next (2.6 and 1.9 percent, respectively). The decline in unemployment is coming to a halt.

GDP growth in Austria attained 3.3 percent in 2000, and demand and output remained lively in the first quarter 2001 (+2.4 percent). Since then, however, signs of a slower pace of activity are becoming more frequent.

Business conditions in Europe have weakened markedly over the past few months, and GDP growth in 2001 is unlikely to exceed 1¾ percent. This is the consequence of slower growth in the USA on the one hand, transmitted to Europe via slackening foreign trade and the downturn on financial markets; on the other hand, the persistence of high energy prices is eroding consumer purchasing power. Domestic demand in the EU is therefore hardly able to drive the economy forward. This holds true particularly for Germany, where GDP growth is expected at little above 1 percent this year. Unlike in the USA, economic policy in Europe is taking an ostensibly cautious attitude in the face of the rapidly weakening business cycle: the monetary authorities are being more concerned about still rising inflationary pressure, while fiscal policy maintains its consolidation-oriented stance. The risks of the present projections are therefore biased towards demand in Europe turning out even weaker than assumed.

All staff members of the Austrian Institute of Economic Research contribute to the Economic Outlook.

Slower growth in Europe is being clearly reflected in the more export-oriented sectors of the Austrian economy. Merchandise exports in 2001 may advance at a moderate 4½ percent in volume year-on-year. Manufacturing output is also slowing down considerably, as suggested by second-quarter results from the regular WIFO business survey showing a significant deterioration of the business climate notably for producers of intermediate and investment goods. Overall production of manufactures is expected to rise by only 2¾ percent annual average, following a more than 8 percent increase last year. Along with the slower pace of output and foreign trade, expansion of investment in machinery and equipment, and of wholesale trade will be dampened. While imports are also set to lose momentum, the trade deficit may edge up to ATS 80 billion. The negative gap in the current account may widen to a ratio of 3 percent of GDP.

In Austria, consumption expenditures of private households are stabilising overall demand. On average 2001, they are projected to expand by 1.8 percent at constant prices. Since rising inflation and higher taxes make for a fall in net real incomes from employment and social transfers (-0.5 percent) and in employees' per-capita earnings (-0.8 percent), such increase in consumption would imply a marked decline in savings as percent of private disposable income. For next year, somewhat higher wage settlements are assumed, and newly-introduced social transfers (child care benefits) will further boost disposable income, allowing for a slight acceleration in the growth of consumer spending.

In the construction sector, a sharp drop in the workforce points to weak output prospects (+0.5 percent). Indeed, output is falling in residential construction (due to lack of demand) and in communal civil engineering (in view of budgetary restraint on the Federal states' as well as the municipal level). Nevertheless, construction investment as a ratio of GDP continues to exceed the EU average to a substantial degree.

General government finances will be adversely affected by slower economic growth. Higher inflation, on the other hand, will tend to improve the budget balance, notably from the revenue side. General government net borrowing is projected at 0.5 percent of GDP for the current year. Whether in 2002 the aimed-for balanced budget will actually be achieved will depend on further business cycle developments, but even more on large-scale transfers „off budget“ of public activities (and related expenditures and deficits) that have been initiated, and whether these will be recognised by Eurostat. In the

Main results					
	1998	1999	2000	2001	2002
	Percentage changes from previous year				
GDP					
Volume	+ 3.3	+ 2.8	+ 3.3	+ 1.7	+ 2.2
Value	+ 4.0	+ 3.7	+ 4.5	+ 3.3	+ 4.0
Manufacturing ¹⁾ , volume	+ 4.4	+ 2.4	+ 8.3	+ 2.7	+ 3.5
Private consumption expenditure, volume	+ 2.9	+ 2.3	+ 2.7	+ 1.8	+ 2.0
Gross fixed investment, volume	+ 2.7	+ 3.2	+ 3.4	+ 1.3	+ 2.4
Machinery and equipment ²⁾	+ 5.2	+ 4.6	+ 6.0	+ 2.3	+ 4.0
Construction	+ 0.9	+ 2.2	+ 1.3	+ 0.5	+ 1.0
Exports of goods ³⁾					
Volume	+ 8.1	+ 7.7	+13.0	+ 4.5	+ 5.7
Value	+ 8.4	+ 7.0	+15.6	+ 7.3	+ 8.3
Imports of goods ³⁾					
Volume	+ 7.1	+ 6.9	+ 8.7	+ 4.5	+ 5.0
Value	+ 6.6	+ 6.7	+14.7	+ 7.6	+ 7.6
Current balance (billion ATS)	-64.5	-85.4	-80.9	-85.9	-80.6
(billion Euro)	- 6.2	- 5.9	- 6.2	- 5.9	- 5.9
As a percentage of GDP (%)	- 2.5	- 3.2	- 2.9	- 2.9	- 2.6
Long-term interest rate ⁴⁾ (%)	4.7	4.7	5.6	5.2	5.0
Consumer prices	+ 0.9	+ 0.6	+ 2.3	+ 2.6	+ 1.9
Unemployment rate					
Percent of total labour force ⁵⁾ (%)	4.5	4.0	3.7	3.6	3.6
Percent of dependent labour force ⁶⁾ (%)	7.2	6.7	5.8	5.7	5.7
Dependent employment ⁷⁾	+ 1.0	+ 1.2	+ 1.0	+ 0.4	+ 0.5
General government financial balance					
As a percentage of GDP (%)	- 2.2	- 2.1	- 1.1	- 0.5	± 0.0

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.

event of a stronger-than-expected slump in business activity, budgetary policy should be ready to let automatic stabilisers operate to full effect.

Since inflation proved more persistent during spring than anticipated, the price forecast has to be revised substantially. Higher energy costs and meat prices, as well as rising indirect taxes and public charges have accelerated overall inflation in the first half of this year. The price increases are feeding through to manufactures, transportation services and housing costs and drive up prices there. On annual average, headline inflation may rise to 2.6 percent, before abating to 1.9 percent in 2002, if energy and meat prices level off.

Weaker economic growth is clouding the outlook for the labour market. Employment (excluding people on maternity leave and in compulsory military service) is expected to edge up by only 13,000 (+0.4 percent); the number of unemployed may remain close to 190,000, corresponding to a jobless rate of 3.6 percent of the labour force (EU definition) or 5.7 percent of the dependent labour force (following the conventional national calculation method).

Cut-off date: 28 June 2001.

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