

## ■ FEW SIGNS OF BUSINESS CYCLE RECOVERY

*The weakness of domestic demand in Austria and in major trading partner countries is shaping current economic developments. Hopes for a pick-up of activity are based upon a speedier recovery in the USA which is, however, subject to considerable risks. In Austria, equipment investment and imports are receding, and industrial output is slightly below the year-earlier level. Retail sales are almost flat, while exports are rising moderately and a tentative recovery of construction activity has become visible in civil engineering. The adverse trend in overall demand is mirrored by a marked decline in employment, higher unemployment and a fall in tax revenues.*

Current cyclical indicators do not point to an imminent upturn in business activity. While output expectations of manufacturing firms have stabilised, actual output in summer fell short even of the low level recorded one year ago, the production index adjusted for calendar effects edging down by ½ percent in the third quarter. Weak demand is being reflected also in firms' low inclination to invest in new production facilities. Capacity utilisation in manufacturing is currently below the long-term average; firms intend to cut down on investment spending, according to the WIFO survey, and imports of capital goods are declining sharply.

The unfavourable economic situation is shaped by weak demand from major foreign trading partners and a persistent sluggishness of domestic demand. While lively demand from East-Central Europe and South-East Asia is the driver of overall export growth (by about 3 percent in value in the first nine months) deliveries to EU markets are barely higher than a year ago. Signs of a cyclical recovery are currently missing in the euro area. GDP grew by only 0.5 percent in the first half of 2002, and the rate should hardly exceed 1 percent in the second semester. Private consumption expenditure, when adjusted for inflation, is only marginally higher than last year, while investment spending is significantly lower. Policy is giving no expansionary incentives, and the hopes for a cyclical upturn rest solely on a strengthening of activity in the USA.

The US economy, due to lively domestic demand and an expansionary stance of fiscal and monetary policy, is growing notably more strongly than Europe (by 1 percent from the previous period and 3¼ percent year-on-year in the third quarter). Nevertheless, the upturn is subject to risks that mainly relate to private

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consumption. Positive developments are recorded for investment, notably as regards expenditure on business equipment and software.

In Austria, weak domestic demand is largely responsible for the overall cyclical sluggishness. Retail sales are depressed by the stagnation in employees' net earnings and transfer income as well as the precarious labour market situation. In the third quarter, sales rose by only 1.3 percent from the low level one year ago, remaining flat in seasonally adjusted terms. Demand for durable consumer goods continues to be particularly weak, notably for motor cars. Figures for the construction sector suggest a tentative recovery in civil engineering, while residential building is still suffering from deficient demand. Lacklustre overall demand is also mirrored by the slide in imports (by a nominal 4 percent from January to August, according to foreign trade statistics; by 2 percent between January and September on payments data). This is the main reason for the current account deficit having disappeared.

The unfavourable business cycle tendency is having negative repercussions in two crucial economic policy areas – the labour market and public finances:

- Employment is following a clear downward trend, with the number of dependent employees (excluding people in statutory military service and recipients of child-care benefits) falling by 20,300 and the jobless figure rising by 12,200 year-on-year. Increasingly, employment problems are spreading from manufacturing and construction to the service sector. As a consequence, female employment has also begun to fall significantly.
- Government gross tax revenues from January to November were 2.6 percent lower than one year ago. For December, against the background of a high year-earlier level, a further decline should be expected. Likewise, on the back of a weak labour market, social security contribution yields are lower than expected, while unemployment-related spending by the Federal government is rising substantially.

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