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Export Boom Losing Momentum

Exports of goods as the driver of business activity are losing steam, and the impulse to private consumption from the tax reform has not yet taken full effect. Yet, together with the tax reform, the marked deceleration of inflation is boosting private purchasing power, suggesting more substantial gains in private consumption for the second half of this year. In the last two months, the business surveys for the euro area have also given hope for some strengthening of the current lacklustre business activity. For Austria, the latest survey results do not show a clear trend.

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Whereas exports had sustained GDP growth last year, they have slackened markedly since. In the first five months of 2005, they only rose by 3 percent in nominal terms from last year. The slowdown mirrors the new bout of cyclical weakening abroad and the relatively high euro exchange rate. However, the most recent improvement in business expectations in the euro area, notably in Germany, raises the hopes for a recovery in the second half of the year.

For Austria, the business survey for the manufacturing sector gives no indication for a pick-up in orders and business conditions in the third quarter. Productive capacities are utilised only to an average degree, with more buoyant demand lacking. For the months to come, firms expect but a moderate increase in production.

Firms in the construction sector see their business situation relatively favourable. This holds particularly for civil engineering, where orders have been rising strongly, whereas those for residential building are stagnating.

Retail sales are posting smaller gains than in 2004, despite the boost to net incomes from the tax reform. In the first five months of 2005, volume sales rose by only around 1 percent year-on-year. The uncertain labour market outlook is weighing on household spending. The lagged effects of the tax reform should nevertheless allow private consumption to revive in the second semester, unless further hikes in energy prices squeeze the purchasing power of households.

Inflation has decelerated markedly in the last months. In May and June, headline inflation at 2.3 percent was $\frac{1}{2}$ percentage point lower than in the months before, mainly due to weaker upward pressure on food prices. Nearly half of the annual price increase is accounted for by higher costs for energy and housing.

Unemployment is rising in spite of an overall growing number of jobs. Notwithstanding the moderate pace of economic activity, 29,000 or 0.9 percent more people were in active employment in July than one year ago. The increase is mainly owed to the labour market becoming more flexible. Productivity, i.e., GDP per labour contract, edged up by only about $\frac{1}{2}$ percent in the last few months, due to the higher number of part-time jobs. Around 70 percent of the new jobs were taken up by women.

Even with the substantial number of new jobs being created, the number of people out of work keeps rising. In July, 211,000 job-seekers were registered with the labour market service, 10,000 more than one year ago. The bulk of the unemployed is seeking full-time jobs which, however, are in short supply. Long-term unemployed compete for the scarce full-time jobs with new entrants to the labour market, among

which people from the domestic "hidden reserve" and job-seekers from abroad. In this "competition", the long-term unemployed are at a clear disadvantage. Policy is currently envisaging additional incentives for firms hiring long-term unemployed as well as for people out of work to accept a lower paid job.