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# SLOWDOWN IN ECONOMIC GROWTH

## ECONOMIC OUTLOOK FOR 1999 AND 2000

*After the prosperous year of 1998, which saw a growth rate of 3.3 percent, economic expansion in Austria will slow down to 2.4 percent as a result of adverse international conditions. Consumer spending will remain the backbone of the economy. The advance in economic activity is unlikely to be strong enough to significantly lower the unemployment rate.*

1998 was a prosperous year for Austria's economy despite unfavourable external economic conditions. According to recent estimates, real GDP rose by 3.3 percent, the highest growth rate since 1991. Two-digit export gains in the first half of the year, and a steadily rising domestic demand provided the foundation for a remarkable expansion which clearly exceeded the EU average (+3 percent).

In the fall, however, signs of an impending slowdown in manufacturing and in the export sector appeared. The crises in Asia, Russia, and South America as well as the turbulence on the international financial markets acted as a break on the world economy and impaired the performance of Austria's exports as well. The plunge in international raw material prices hit the basic-goods industry particularly hard and worsened business and profits expectations. The pessimistic outlook for the manufacturing sector at the end of the year suggests that the dip in economic activity will extend at least into the first half of 1999.

The deceleration in economic activity resulting from the weakness in merchandise exports is being partially offset by the upturn in consumer spending. In 1998, expenditures of private households (adjusted for price increases) rose by 1.8 percent. In part, the rise in the purchasing power of private households was caused by the same factor which caused the sluggishness in export growth: the deep cut in prices of raw materials, particularly in energy prices.

In 1999, the dynamism of the economy will continue to shift from exports to domestic demand. This assessment is supported by the index of consumer climate, which continuously improved during the last few months owing to the rise in purchasing power, a more favourable employment situation, and lower inflation. Moreover, do-

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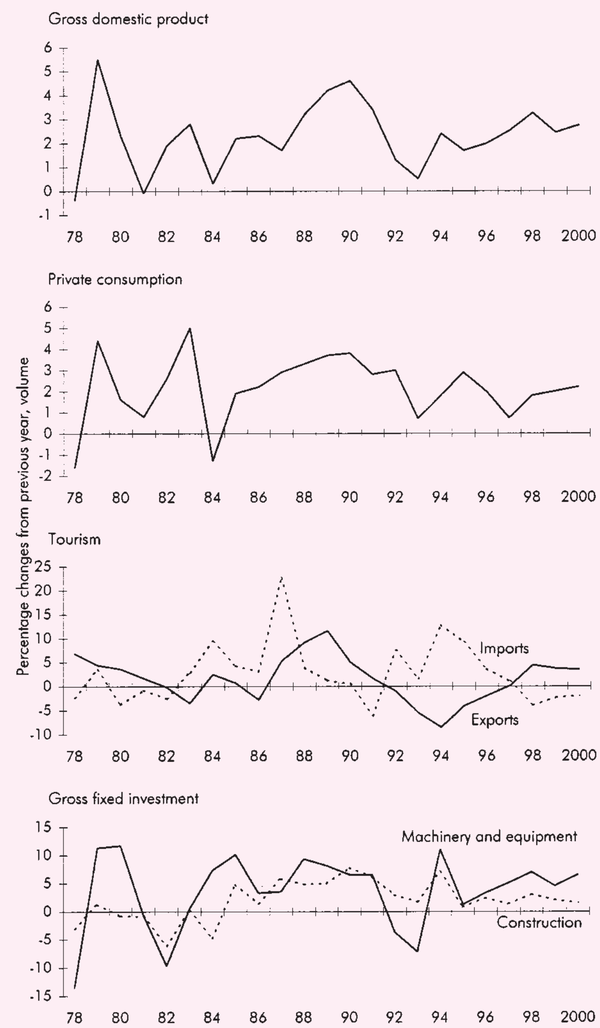
*Table 1: Main results*

| | | 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|---|---|
| | | Percentage changes from previous year | | | | |
| GDP | | | | | | |
| Volume | | + 2.0 | + 2.5 | + 3.3 | + 2.4 | + 2.7 |
| Value | | + 3.7 | + 4.1 | + 4.5 | + 4.1 | + 4.0 |
| Manufacturing[1], volume | | + 1.2 | + 5.0 | + 5.5 | + 3.0 | + 4.0 |
| Private consumption, volume | | + 2.0 | + 0.7 | + 1.8 | + 2.0 | + 2.2 |
| Gross fixed investment, volume | | + 2.5 | + 2.8 | + 4.8 | + 3.2 | + 3.8 |
| Machinery and equipment | | + 3.3 | + 5.0 | + 7.0 | + 4.5 | + 6.5 |
| Construction | | + 2.4 | + 1.3 | + 3.0 | + 2.0 | + 1.5 |
| Exports of goods[2] | | | | | | |
| Volume | | + 5.4 | + 15.6 | + 8.3 | + 5.5 | + 7.0 |
| Value | | + 5.5 | + 16.8 | + 8.3 | + 6.6 | + 8.1 |
| Imports of goods[2] | | | | | | |
| Volume | | + 6.1 | + 9.4 | + 8.2 | + 6.0 | + 7.0 |
| Value | | + 6.7 | + 10.9 | + 7.1 | + 6.0 | + 8.1 |
| Trade balance[2] | billion ATS | –100.6 | – 75.2 | – 72.1 | – 72.2 | – 78.0 |
| Current balance | billion ATS | – 52.3 | – 61.4 | – 53.1 | – 45.4 | – 43.1 |
| | as a percentage of GDP | – 2.2 | – 2.4 | – 2.0 | – 1.7 | – 1.5 |
| Long-term interest rate[3] | in percent | 6.3 | 5.7 | 4.7 | 4.3 | 4.8 |
| Consumer prices | | + 1.9 | + 1.3 | + 0.9 | + 1.0 | + 1.2 |
| Unemployment rate | | | | | | |
| | percent of total labour force[4] | 4.3 | 4.4 | 4.5 | 4.4 | 4.3 |
| | percent of dependent labour force[5] | 7.0 | 7.1 | 7.2 | 7.1 | 6.8 |
| Dependent employment[6] | | – 0.6 | + 0.4 | + 1.0 | + 0.8 | + 0.9 |

[1] Value added, including mining and quarrying. – [2] According to Austrian Central Statistical Office. – [3] 10-year central government bonds (benchmark). – [4] According to Eurostat. – [5] According to labour exchange statistics. – [6] Excluding parental leave and military service.

*Figure 1: Demand and output*

*Percentage changes from previous year, volume*




mestic demand is being buoyed by the persistent decline in interest rates. At the beginning of December 1998, the European central banks cut interest rates with the intention of warding off an economic slump.

Given the deterioration in the international cyclical position, the forecast of economic growth in Austria for 1999 must be revised downwards from 2.8 to 2.4 percent; thus, the growth rate of real GDP is likely to approach the medium-term trend, largely due to the robustness of domestic demand. In view of the favourable economic conditions, of low inflation and interest rates as well as free capacities in particular, the temporary economic weakness triggered by the financial turmoil will probably be overcome in the year 2000.

The dynamism of Austria's economy in the year 1999 will not be strong enough to markedly reduce the unemployment rate. A slight decline from 4.5 to 4.4 percent (7.1 percent according to the traditional Austrian method) seems possible, however, because labour supply will rise at a slower pace than in 1998. Thanks to the vigorous increase in employment-intensive domestic demand, the number of jobs will rise by 24,000 in 1999. Thus, one half of the medium-term goal of the National Action Plan will be attained in the first two years of the five-year schedule. As long as the labour supply is on the rise, however, cutting unemployment will prove quite difficult.

The plunge in international prices of crude oil, food, and manufacturing raw materials continues to dampen inflation. In the year 1998, consumer prices in Austria rose by only 0.9 percent on average. A similar situation is likely to prevail in 1999 and 2000, with the inflation rate only marginally exceeding the mark of 1 percent.

The development of the current account has been dominated by the improvement in the tourism account. Having depressed the balance in the current account for several years, the tourism sector now has a strong positive impact. The timing of the turnaround in the tourism balance indicates that relative prices (exchange rates) do play an important role in directing tourism flows. An important contribution is also being made by structural improvements in Austria's tourism industry. Given favourable conditions, the surplus in the tourism account could improve by as much as ATS 15 billion between 1998 and 2000.

The revision of the growth forecast for 1999 is unlikely to pose additional problems to fiscal policy in Austria, because the changes refer only to exports, but not to domestic demand and the wage bill. The general government deficit in 1999 will amount to about 2 percent of GDP, as scheduled in the Stability Program. The budget situation will remain strained; this is indicated by the development expected for the year 2000: given the technical assumption of a tax reform with a net tax relief of ATS 10 billion, the general government deficit, without recourse to supplemental discretionary measures, is likely to rise to about 2¼ percent of GDP.

## SLOWDOWN IN WORLD ECONOMY AND PLUNGE IN COMMODITY PRICES

*The crisis in Asia and the turmoil on the global financial markets have markedly dampened the growth of the world economy in 1998. This development has also had serious consequences on economic activity in Europe through a decline in exports, a drop in prices, and by making investors more cautious. Economic growth in the countries of the European Union will therefore weaken from 3 percent in 1998 to 2¼ percent in 1999, but is expected to accelerate to 2¾ percent in 2000.*

The world economy continues to be characterised by a great deal of uncertainty[1]. The crisis in Asia has proved to be more obdurate than expected, and the Japanese government has failed despite several fiscal programs to overcome the deep confidence crisis affecting investors and consumers. Rescue operations for ailing banks have taken up large government funds. Japan's gross domestic product is likely to shrink by 2½ percent in 1998; there are as yet no concrete signs of the recovery predicted by international institutions for 1999. Some south-east Asian countries may be emerging from the recession, but this is far from certain.

The drop in demand from south-east Asia and Japan in 1998 resulted in a deep drop in prices on international markets. Commodity prices plunged by one fourth on average in 1998; the price collapse engulfed not only crude oil, but also industrial raw materials and food. Latin America was driven into a severe crisis by the drop in prices of raw materials and the high volatility of international capital. Brazil, in particular, suffered from massive capital flight and tried to fight off the capital outflow by high interest rates, a reaction which has paralysed economic activity.

*Table 2: World economy*

| | | 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|---|---|
| | | Percentage changes from previous year | | | | |
| *Real GDP* | | | | | | |
| Total OECD | | + 2.9 | + 3.0 | + 2.0 | + 2.0 | + 2.3 |
| USA | | + 3.4 | + 3.9 | + 3.5 | + 1.8 | + 2.3 |
| Japan | | + 3.9 | + 0.8 | – 2.5 | + 0.8 | + 1.3 |
| EU | | + 1.8 | + 2.7 | + 3.0 | + 2.3 | + 2.8 |
| Euro area | | + 1.6 | + 2.5 | + 3.0 | + 2.5 | + 2.8 |
| Germany | | + 1.3 | + 2.2 | + 2.8 | + 2.0 | + 2.5 |
| Eastern Europe[1] | | + 4.7 | + 5.0 | + 4.3 | + 4.0 | + 4.3 |
| *World trade, volume* | | + 6.8 | + 9.8 | + 4.5 | + 5.3 | + 6.0 |
| OECD exports | | + 6.3 | +11.3 | + 5.0 | + 4.8 | + 6.0 |
| Intra-OECD trade | | + 6.0 | +11.5 | + 7.5 | + 5.5 | + 6.5 |
| *Market growth*[2] | | + 6.2 | + 9.4 | + 7.5 | + 5.5 | + 6.5 |
| *Primary commodity prices, in USD* | | | | | | |
| HWWA index, total | | + 3.0 | – 2.0 | –25.0 | – 4.0 | +11.0 |
| Excluding energy | | – 9.0 | + 0.0 | –13.0 | – 5.0 | + 6.0 |
| *Crude oil prices* | | | | | | |
| Average import price (cif) for OECD countries | USD/barrel | 20.6 | 19.1 | 12.5 | 12.0 | 14.0 |
| *Exchange rate* | ATS/USD | 10.59 | 12.20 | 12.40 | 11.70 | 11.40 |

[1] Czech Republic, Hungary, Slovakia, Slovenia. – [2] Real import growth of trading partners weighted by Austrian export shares.

The crisis in Asia and in Latin America has begun to affect exports and industrial output in the USA. These negative effects, however, were partly offset by extraordinarily vigorous consumer spending. For 1999, a slowdown in economic growth to slightly less than 2 percent is likely, starting in exports and manufacturing output. The marked weakening of the Purchasing Managers' Index (PMI) at the end of the year supports these expectations.

The performance of the European economies has been impaired by a series of financial and currency crises since the beginning of the 1990s. The recession of 1993, exacerbated as it was by a restrictive monetary policy, was followed by the currency crisis of 1995-96, and now by the financial crisis of 1998-99. In such a situation, the challenge posed to economic stabilisation policy consists less in deploying its traditional fiscal instruments than in preventing and containing crises on the liberalised financial and foreign exchange markets. The introduction of the euro on 1 January 1999 and the co-ordinated cut in interest rates by European central banks are important steps in this direction. Without the predetermined schedule for the realisation of the European Monetary Union some European currencies might have been driven into a devaluation spiral during the turmoil of the year 1998.

While the European economies proved to be relatively immune to the adverse effects of the Asian crisis in the first

[1] See Marterbauer, M., "Wachstumsabschwächung stellt internationale Wirtschaftspolitik vor neue Herausforderungen", WIFO-Monatsberichte, 1998, 71(12).

half of 1998, the business climate changed radically in the second half of the year under the impact of the crisis in Russia and the stock market crash. The European banks suffered more severely from the Russian turmoil than from similar earlier events; this experience has probably made them more cautious in extending export loans. The crisis in Russia has not spread to the countries of East-Central Europe, whose economies have become strongly geared to western Europe. The Czech Republic is the only country experiencing a recession.

The general business and order situation in manufacturing in the EU deteriorated markedly in the second half of the year. Capacity utilisation nonetheless increased continuously up to the third quarter. This suggests that the price and earnings situation is more responsible for the depressed business climate than the real sphere.

The development in Germany closely mirrored that of the EU on average. In the third quarter the German economy expanded by a strong 2.8 percent, but the growth in foreign orders and in industrial production slowed during the last few months. The Ifo business climate index has been trending downwards for several months. Reflecting the most recent developments, real GDP is expected to grow by 2.0 to 2.3 percent in 1999.

In view of these favourable economic conditions, such as low inflation and interest rates and free production capacities, the economic sluggishness that has been caused by the turmoil on financial markets should be short-lived and end in the year 2000, provided economic policy reacts in an appropriate manner. The danger of a recession has diminished along with the stabilisation of the international stock markets, but has not been entirely averted. How the problems will be managed in the emerging economies of Asia and South America as well as in Russia remains of great importance for the development of the global economy.

## CO-ORDINATED CUT IN INTEREST RATES

The USA reacted swiftly to the world-wide financial turmoil with several interest rate cuts intended to stimulate the economy and to provide relief to the debtor countries. These measures tend to lower the value of the dollar and thus help the debtor countries to service their dollar debts. Over the last few decades, a rise in the value of the U.S. currency has as a rule triggered financial crises in some debtor countries[2].

After several cuts in interest rates in the USA, the European central banks unexpectedly lowered their interest rates as well in a co-ordinated action to ward off the danger of a recession in Europe.

Along with the flight of international capital into safe havens, the term structure in the EU turned inverse in the fall of 1998, i.e., short-term interest rates rose above long-term rates and thus had a restrictive impact on the economy. The co-ordinated cut in interest rates could help to normalise the term structure.

As of 1 January 1999, the monetary authority in the euro zone shifted to the European Central Bank. The euro zone now has a uniform money market interest rate. As a result of the cut in base interest rates at the beginning of December, the European Central Bank will escape being immediately confronted with the demand for a more expansive monetary policy.

In Austria, short-term interest rates were stable until the co-ordinated monetary operation at the beginning of December; long-term interest rates declined by about ½ percentage point since the summer. Short-term interest rates are likely to remain more or less stable in 1999 and 2000, but long-term rates will probably post a further marked decline in 1999 before rising again with the pick-up of the global economy.

## EXPORTS AFFECTED BY THE WEAKNESS IN THE INTERNATIONAL ECONOMY

While the performance of the Austrian economy was relatively little impaired in the first half of 1998, the number of indicators pointing to a slowdown increased in the second half of the year. Exports and production gains levelled off significantly. The growth rate of merchandise exports (payments for merchandise exports) declined from 12 percent in the first half of 1998 to 7 percent in the third quarter. Exports to south-east Asia, Russia, and the OPEC countries have posted strong losses in recent months.

The increasingly pessimistic assessment of foreign orders by manufacturing firms indicates that export growth will slow down further in 1999. This outlook is consistent with the revision of short-term forecasts in the most important industrial countries, which suggests a slower growth in markets for Austrian exporters. Merchandise exports (adjusted for price changes) are forecast to rise by only 5½ percent in 1999 (following 8.3 percent in 1998). If the instabilities on the international financial markets can be successfully warded off, a recovery of the global economy seems to be within reach; this would open up new opportunities for Austria's export sector.

[2] See Schulmeister, S., "Finanzmarktturbulenzen beeinträchtigen internationale Wachstumsdynamik. Mittelfristige Prognose der Weltwirtschaft bis 2002", WIFO-Monatsberichte, 1998, 71(12).

*Table 3: Productivity*

| | 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|---|
| | Percentage changes from previous year | | | | |
| *Total economy* | | | | | |
| Real GDP | +2.0 | +2.5 | +3.3 | +2.4 | +2.7 |
| Employment[1] | –0.6 | +0.1 | +0.9 | +0.7 | +0.8 |
| Productivity (GDP per employment) | +2.6 | +2.4 | +2.3 | +1.7 | +1.9 |
| *Manufacturing* | | | | | |
| Production[2] | +1.3 | +5.3 | +5.5 | +3.0 | +4.0 |
| Employees | –2.9 | –1.4 | +0.5 | –0.7 | –0.3 |
| Productivity per hour | +4.6 | +6.6 | +5.0 | +4.0 | +4.3 |
| Working hours per day for workers | –0.3 | +0.2 | ±0.0 | –0.3 | ±0.0 |

[1] Dependent and self-employed according to National Accounts. – [2] Value added.

## SLUGGISH GROWTH IN MANUFACTURING

Faltering export dynamism has started to leave its mark on manufacturing output. The rate of expansion declined from 9 percent (in nominal terms) in the first half of 1998 to about 5 percent in the months of July and August. The business climate continued to worsen during the fourth quarter. The balance of negative and positive output expectations barely remained in the positive range. Weak foreign demand and pessimistic expectations suggest a further deceleration in 1999. Manufacturing output is forecast to rise by only 3 percent, half the growth rate achieved in 1998. A pickup in manufacturing is likely in the year 2000, however, along with the recovery of the world economy. The downward pressure on prices in the wake of the Asian crisis had the strongest impact on the basic-goods industry (steel, chemical industry) and some branches of technical manufacturing (electronics). Economic activity remained robust in the consumer goods and transport industries, however. Given the strong weight of these industries in Austria's economy, the adverse impact is relatively large. On the other hand, Austria's unit labour costs declined against those of the trading partners. This comparison encompasses only the OECD countries, however, and thus neglects Russia and the countries in south-east Asia, all of which underwent massive currency depreciations.

## INVESTMENT ACTIVITY LOSES MOMENTUM

Gains in sales and high profitability during the last few years resulted in a vigorous expansion of investment in machinery and equipment. In 1999, the expansion in capital outlays will level off in line with the slowdown in merchandise exports and output. Some investment projects scheduled for 1999 will be delayed in view of the higher sales risks in important emerging markets and the instability of the international financial markets.

*Table 4: Private consumption*

| | 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|---|
| | Percentage changes from previous year, volume | | | | |
| Private consumption | +2.0 | +0.7 | +1.8 | +2.0 | +2.2 |
| Durables | +8.1 | –3.5 | +2.0 | +2.5 | +2.9 |
| Non-durables and services | +1.1 | +1.4 | +1.8 | +1.9 | +2.1 |
| Net wages and salaries | –1.9 | –3.1 | +1.8 | +2.5 | +2.9 |
| Household disposable income | –0.2 | +0.2 | +2.6 | +2.5 | +2.8 |
| | As a percentage of disposable income | | | | |
| Household saving ratio | 7.8 | 7.4 | 8.1 | 8.6 | 9.1 |

The rise in construction investment in 1998 was mainly due to special factors: a mild winter and the tax-related surge in the renovation and modernisation business supported a marked expansion in the volume of construction.

The boom in the renovation and modernisation business is likely to continue into 1999, because maintenance projects will be moved up. With the release of accumulated rental reserves coming to an end in the year 2000, a big gap in construction orders will open up. Moreover, construction of residential housing is markedly levelling off. The pent-up demand has vanished, and rents charged for newly let apartments are on the decline. The reduction in residential housing construction to a "normal" level will sharply depress activity in the construction industry in the next years as well. Civil engineering, on the other hand, is emerging from the effects of the budget restrictions imposed over the last few years; the construction of office buildings appears to have bottomed out.

## HEFTY CONSUMER DEMAND HELPS TO SUSTAIN CURRENT UPSWING

*In 1999, private consumption will be the mainstay of economic growth. The rise in purchasing power and the gain in consumer confidence suggests a vigorous expansion in consumer expenditures.*

The rise in real disposable income significantly boosted retail sales and private consumption (1.8 percent in real terms) in 1998. The real income gains forecast for 1999 (2½ percent) will provide ample room for the expansion of consumer expenditures in the next year as well. As the savings ratio tends to return to its normal level after the sharp drop in 1995-1997, only part of the additional purchasing power will flow into consumer spending. In contrast to the last few years, the budgets of the public sector will stimulate the economy in 1999: the increase in the salaries of employees in the public sector by 2½ percent, the

*Table 5: Earnings and international competitiveness*

| | 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|---|
| | Percentage changes from previous year | | | | |
| Gross earnings per employee | +1.9 | +0.7 | +2.5 | +2.8 | +2.8 |
| Gross real earnings per employee | –1.0 | –1.3 | +1.6 | +1.8 | +1.6 |
| Net real earnings per employee | –2.3 | –3.8 | +1.1 | +1.2 | +2.3 |
| Net wages and salaries | +0.9 | –1.1 | +2.7 | +3.5 | +4.1 |
| Unit labour costs | | | | | |
| Total economy | –0.7 | –1.3 | +0.1 | +1.1 | +0.9 |
| Manufacturing | –1.0 | –5.0 | –3.1 | –1.3 | –1.4 |
| Relative unit labour costs[1] | | | | | |
| Vis-à-vis trading partners | –2.2 | –4.9 | –1.2 | –0.6 | –1.1 |
| Vis-à-vis Germany | –0.6 | –0.6 | –0.7 | –0.6 | –0.5 |
| Effective exchange rate – manufactures | | | | | |
| Nominal | –1.2 | –1.8 | +0.6 | +0.6 | +0.1 |
| Real | –1.5 | –2.6 | –0.1 | –0.1 | –0.5 |

[1] Manufacturing, in a common currency; minus sign indicates improvement of competitiveness.

"family package" (additional expenditure and tax allowances amounting to ATS 12 billion in 1999 and 2000, respectively), as well as the tax reform of the year 2000 will push up disposable income.

Thus, the dampening effects emanating from foreign trade will be significantly mitigated by a revival of domestic demand. This component of aggregate demand will be buoyed by the gains in purchasing power accruing to private households, a result of declining inflation, rising employment, and higher income growth. A further deterioration in the global economy could, however, adversely affect domestic demand as well.

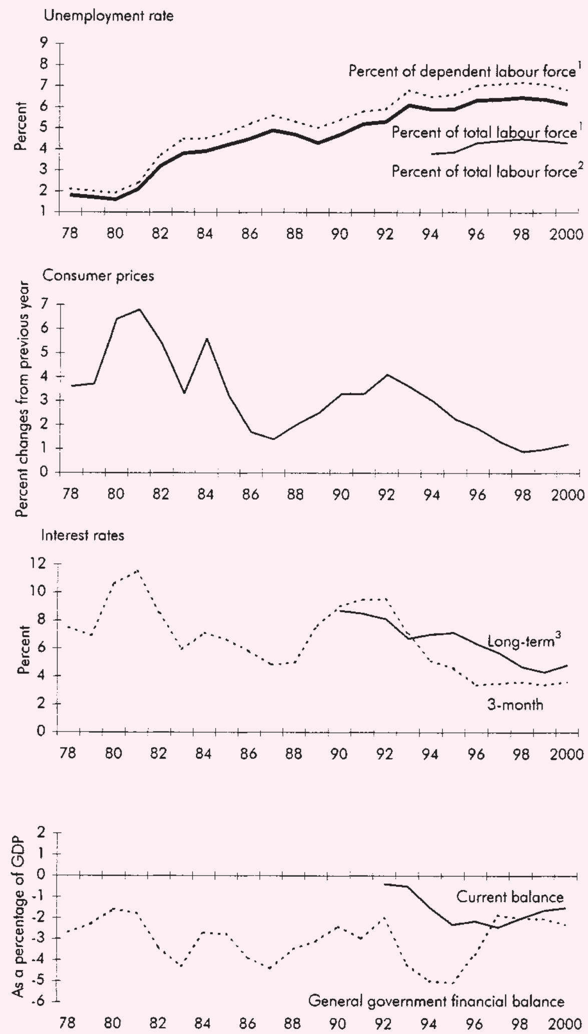
## RISE IN TOURISM SURPLUS IMPROVES CURRENT ACCOUNT

The development of the current account has been dominated by the improvement in the tourism account. Having caused the deterioration in the current account for several years, the tourism sector is now having a strong positive impact. The timing of the turnaround in the tourism balance indicates that relative prices (exchange rates) do play an important role in directing tourism flows. At the same time, the restructuring of tourism supply also plays an important part in boosting the surplus in the tourism account.

Growth in receipts from tourism accelerated markedly in the summer season of 1998 (from 3¾ percent in 1997 to 6¼ percent). The performance of overnight stays was less favourable, but this indicator provides little information in times of fast structural change in tourism. Moreover, Austrians curtailed foreign travel and spending abroad.

In 1998, the current account is expected to record a deficit of ATS 53 billion, slightly less than in 1997, with the decline mainly due to the upturn in tourism and the plunge in

*Figure 2: Main economic indicators*




[1] According to labour exchange statistics. [2] According to Eurostat. [3] Yield of 10-year central government bonds (benchmark).

oil prices. The surplus in the tourism account is expected to rise from ATS 29 billion to almost ATS 45 billion between 1998 and 2000. The deficit in the current account is likely to shrink by a slightly smaller amount (ATS 10 billion).

## MINIMAL RATE OF INFLATION

The sharp drop in internationally traded commodities such as crude oil, food, and manufacturing raw materials, has further depressed price increases. At present, inflation does not require remedial action, neither in Austria nor in Europe. This has enlarged the manoeuvring room for monetary policy to ward off an economic setback.

According to the HWWA index, international raw material prices (on a dollar basis) in 1998 were one fourth below

*Table 6: Labour market*

| | 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|---|
| | Changes from previous year, in 1,000 | | | | |
| *Demand for labour* | | | | | |
| Civilian employment | –23.8 | + 8.8 | +23.0 | +22.0 | +24.3 |
| Dependent employment[1] | –20.9 | + 8.3 | +22.0 | +21.0 | +23.4 |
| Excluding parental leave and military service | –16.5 | +12.8 | +29.5 | +24.0 | +26.0 |
| *Percentage changes from previous year* | – 0.6 | + 0.4 | + 1.0 | + 0.8 | + 0.9 |
| Parental leave and military service[1] | – 4.4 | – 4.4 | – 7.5 | – 3.0 | – 2.6 |
| Foreign workers | + 0.0 | – 1.6 | – 0.5 | ± 0.0 | + 1.5 |
| Self-employed[2] | – 2.9 | + 0.5 | + 1.0 | + 1.0 | + 0.9 |
| *Labour supply* | | | | | |
| Total labour force | – 9.0 | +11.7 | +28.0 | +20.0 | +16.6 |
| Foreign | + 2.8 | – 1.7 | + 1.0 | ± 0.0 | + 0.7 |
| Migration of nationals | + 4.9 | + 5.4 | + 5.5 | + 3.5 | + 2.0 |
| Indigenous | –16.7 | + 8.0 | +21.5 | +16.5 | +13.9 |
| *Surplus of labour* | | | | | |
| Registered unemployed[3] | +14.8 | + 2.8 | + 5.0 | – 2.0 | – 7.7 |
| In 1,000 | 230.5 | 233.3 | 238.3 | 236.3 | 228.6 |
| Unemployment rate | | | | | |
| percent of total labour force[4] | 4.3 | 4.4 | 4.5 | 4.4 | 4.3 |
| percent of total labour force[3] | 6.3 | 6.4 | 6.5 | 6.4 | 6.1 |
| percent of dependent labour force[3] | 7.0 | 7.1 | 7.2 | 7.1 | 6.8 |
| Participation rate[5] | 67.2 | 67.2 | 67.6 | 67.8 | 68.0 |
| Employment rate[6] | 62.9 | 62.9 | 63.2 | 63.5 | 63.8 |

[1] According to Association of Austrian Social Security Bodies. – [2] According to WIFO. – [3] According to labour exchange statistics. – [4] According to Eurostat. – [5] Total labour force as a percentage of active population (aged 15 to 64). – [6] Employment as a percentage of active population (aged 15 to 64).

the level recorded in 1997. The main reasons were the demand shortfall and the downward pressure on prices in the wake of the Asian crisis. In Austria, the rate of inflation at the consumer level diminished to 0.9 percent.

Price increases are likely to remain subdued in 1999 and 2000, with the rate of inflation barely exceeding the mark of 1 percent. Raw material prices will probably stabilise after the plunge in 1998. The euro is expected to be a strong currency and likely to gain in value against the dollar and thus to dampen possible surges in prices of crude oil and other raw materials.

Wage costs will exert only slight upward pressures on prices, because the settlements achieved in the overall wage bargaining round fall far short of the relatively high wage gains attained by the metal workers. After several years of stagnation, unit labour costs are forecast to rise by about 1 percent in 1999 and 2000. The projection of the rise in gross earnings per employee of 2.8 percent is in line with the major wage settlements concluded in the fall and need not be revised.

## UNEMPLOYMENT WILL FALL ONLY MARGINALLY IN 1999

In the fall of 1998, the labour market showed no signs of a slowdown in economic activity; the employment expansion continued unabated. The year 1998 saw employment

*Table 7: Key policy indicators*

| | 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|---|
| | Billion ATS | | | | |
| *Fiscal policy* | | | | | |
| Central government net balance | –89.4 | –67.2 | –67.0 | –70.0 | –78.5 |
| | As a percentage of GDP | | | | |
| Central government net balance | – 3.7 | – 2.7 | – 2.5 | – 2.6 | – 2.8 |
| General government financial balance | – 3.7 | – 1.9 | – 2.0 | – 2.0 | – 2.3 |
| | In percent | | | | |
| *Monetary policy* | | | | | |
| 3-month interest rate | 3.4 | 3.5 | 3.6 | 3.4 | 3.6 |
| Long-term interest rate[1] | 6.3 | 5.7 | 4.7 | 4.3 | 4.8 |
| Bond yield, average | 5.3 | 4.8 | 4.4 | 4.2 | 4.6 |
| | Percentage changes from previous year | | | | |
| *Effective exchange rate* | | | | | |
| Nominal | – 1.5 | – 2.3 | + 0.7 | + 1.2 | + 0.3 |
| Real | – 2.1 | – 3.3 | – 0.2 | + 0.2 | – 0.6 |

[1] 10-year central government bonds (benchmark).

gains of 30,000; the corresponding figure for 1999 will be 24,000 because of the slackened pace of economic activity.

According to the March census, the newly created jobs are exclusively part-time jobs. Therefore, the number of unemployed who usually search for full-time jobs did not decline. The majority of the additional part-time jobs were filled by female employees, who had dropped out of the labour market during the years of sluggish growth. Moreover, the shortening of the period during which parental leave benefits can be drawn also boosted the supply of female labour.

*The lively pace of domestic demand has already left a strong mark on the labour market: about 30,000 additional jobs were created in 1998, mainly in the service sector. Another 24,000 jobs are in the offing in 1999. The employment gains have so far been limited to part-time jobs, however, and thus have not lowered the number of unemployed seeking full-time jobs.*

In 1999, the "hidden labour reserves", from which labour was drawn in 1998, will be almost exhausted, and the unemployment rate will drop to 4.4 percent (7.1 percent according to the traditional Austrian method). A contributing factor will be the measures taken in the framework of the National Action Plan. Given the risks surrounding the cyclical development, these forecasts are shrouded in uncertainty.

## GENERAL GOVERNMENT DEFICIT IN 1999 ONLY 2 PERCENT OF GDP DESPITE ECONOMIC SLOWDOWN

The development of the Federal public budget in 1998 proceeded largely according to schedule. The data available at the end of the year indicate that with a ratio of 2.5 percent of GDP the deficit will be slightly below the ratio envisaged in the preliminary budget. The Länder and municipalities are likely to post a surplus of ½ percent of GDP, so that the deficit of all government budgets will attain 2 percent of GDP, slightly less than postulated by the Stability Program (2.2 percent).

The weakening of economic activity in 1999 is unlikely to pose additional problems to fiscal policy in Austria: the revisions in the forecast refer only to exports but not to domestic demand. The forecasts of the wage bill and of the retail sales, which are the central determinants of revenues from income and value added taxes, remain unchanged. In 1999, the general government deficit will amount to 2 percent of GDP, as scheduled in the Stability Program.

The fiscal situation will remain tight; this is indicated by the economic performance expected for the year 2000. The present forecast is based on the technical assumption that a tax reform will be realised with a net tax relief of ATS 10 billion. Under this assumption and without additional discretionary measures, the general government deficit will rise to about 2.3 percent of GDP. If the target of 1.4 percent in the year 2002, as prescribed in the Stability Program, is to be achieved, fiscal policy will need to continue its restrictive course.

Cut-off date: 16 December 1998