MARKUS MARTERBAUER

UPSWING BOOSTS MANUFACTURING OUTPUT AND EMPLOYMENT

ECONOMIC OUTLOOK FOR 1998 AND 1999

Economic activity in Austria will expand by 2¾ percent in 1998 and 3 percent in 1999. The main forces driving the economy are the solid expansion in merchandise exports and the revival in investment and consumer expenditures. Employment is growing rapidly and is expected to reach a new record high. Unemployment persists, however, at a high level.

In 1997, Austria's economy expanded by 2½ percent in real terms, with the main impetus stemming from the surge in merchandise exports. The framework conditions for the export sector remain favorable: stable exchange rates, low nominal interest rates, a less restrictive fiscal policy and lower oil prices suggest an acceleration in economic growth in western Europe. Foreign demand from East-Central Europe will remain buoyant, partly because the countries in this region are relaxing import restrictions. The decrease in relative unit labor costs (in a common currency), which will total 10 percent over the period from 1995 to 1999, will improve the price-determined competitiveness of Austria's exporters and facilitate further gains in market shares. The volume of merchandise exports is projected to rise by 10 percent in 1998 and by 8½ percent in 1999.

Given the strong linkage between exports and imports and the rebound in domestic demand, the volume of imports is also projected to expand at a lively pace. As a result of the deep drop in crude oil prices, import prices will remain stable, however, providing a welcome relief to the trade account. More favorable framework conditions in the tourism sector and a slowdown in the growth of spending by Austrians abroad will help to stabilize the tourism balance; a surplus of ATS 17 billion is expected for 1998. The deficit in the current account is likely to drop by more than ATS 10 billion to some ATS 36 billion.

The surge in merchandise exports and the revival of domestic demand will boost output in manufacturing by 5 percent in 1998. Demand for products of the basic goods industry and of technical manufacturing will continue to be lively; as order stocks in the consumer goods industry also improve, the number of jobs in the whole

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

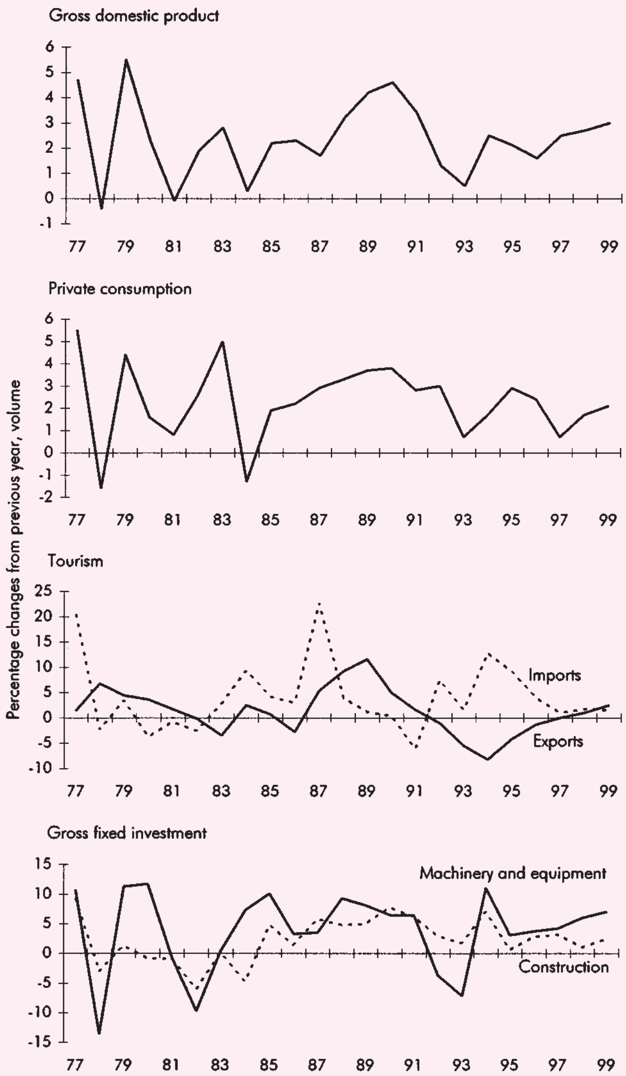
Table 1: Main results

		1995	1996	1997	1998	1999
		Percentage changes from previous year				
GDP						
Volume		+ 2.1	+ 1.6	+ 2.5	+ 2.7	+ 3.0
Value		+ 4.2	+ 3.7	+ 3.9	+ 4.1	+ 4.6
Manufacturing[1], volume		+ 1.0	+ 1.2	+ 4.3	+ 5.0	+ 4.3
Private consumption, volume		+ 2.9	+ 2.4	+ 0.7	+ 1.7	+ 2.1
Gross fixed investment, volume		+ 1.9	+ 2.4	+ 3.6	+ 3.3	+ 4.6
Machinery and equipment		+ 3.1	+ 3.7	+ 4.2	+ 6.0	+ 7.0
Construction		+ 0.6	+ 2.8	+ 3.2	+ 1.0	+ 2.5
Exports of goods[2]						
Volume		+12.1	+ 5.3	+14.9	+10.0	+ 8.5
Value		+13.2	+ 5.5	+16.4	+11.4	+ 9.9
Imports of goods[2]						
Volume		+ 5.7	+ 6.1	+ 7.9	+ 8.0	+ 8.0
Value		+ 6.2	+ 6.7	+ 9.5	+ 8.0	+ 9.6
Trade balance[2]	billion ATS	–88.0	–100.6	–68.1	–49.1	–51.6
Current balance	billion ATS	–47.0	– 43.4	–47.7	–36.0	–37.2
As a percentage of GDP	in percent	– 2.0	– 1.8	– 1.9	– 1.4	– 1.4
Long-term interest rate[3]	in percent	7.1	6.3	5.7	5.2	5.7
Consumer prices		+ 2.2	+ 1.9	+ 1.3	+ 1.2	+ 1.5
Unemployment rate						
Percent of total labor force[4]	in percent	3.9	4.4	4.4	4.5	4.4
Percent of dependent labor force[5]	in percent	6.6	7.0	7.1	7.3	7.1
Dependent employment[6]		+ 0.0	– 0.6	+ 0.4	+ 0.9	+ 1.0

[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 labor exchange statistics. – [6] Excluding parental leave and military service.

Figure 1: Demand and output

Percentage changes from previous year, volume



manufacturing sector will cease to decline for the first time in many years. The rebound in manufacturing output is also expected to boost capital spending on machinery and transport equipment.

In the construction sector, activity in the renovation and modernization business will remain brisk; the extension and improvement of the rail and road system will benefit the engineering sector. Residential construction, however, will experience a marked decline after the buoyancy of the last few years, but commercial construction, in the tourism sector for example, is likely to gain momentum. The total volume of construction put in place will expand by only 1 percent; a slight acceleration is expected for 1999.

Transfer payments as well as after-tax income of private households from wages and salaries declined considerably over the last two years. 1998 and 1999 will see a reversal of this downward trend. Compensation per employee is likely to rise more rapidly in tandem with the pick-up in economic activity; moreover, as fiscal policy turns less restrictive, transfer payments will rise at a more rapid pace, particularly because of the "family package" taking effect in 1999. Higher disposable income of households will revive consumer spending, especially on durable goods. Consumer expenditures are forecast to rise by 1¾ percent and well over 2 percent in real terms in 1998 and 1999.

Provided that the plunge in crude oil prices is more fully passed on to fuel prices at the consumer price level, and that the hike in the value-added tax in Germany does not spill over to Austria, price increases are expected to remain subdued. With inflation rates of 1.2 percent in 1998 and 1.5 percent in 1999, Austria will enjoy price stability.

The strong expansion of output in the goods as well as service producing sectors will boost the demand for labor. In the service sectors, employment – mainly of female workers and of persons in part-time employment – has been on the increase for some time now; in manufacturing, the demand for labor is expected to stop the long-term decline, despite high productivity gains. The number of persons in dependent employment (excluding persons in military service and on parental leave) is forecast to rise by almost

30,000 in 1998 and 1999, respectively. Many women who are currently finding employment have just entered the labor supply. There are several factors raising the labor supply: a cut in the time of eligibility for parental leave assistance, a reduction in the number of persons entering early retirement and the termination of special unemployment assistance. Thus, despite solid employment gains, unemployment is also forecast to rise slightly. In 1998, some 240,000 persons on average will be registered as unemployed with the employment placement service. This implies an unemployment rate of 4.5 percent of the total labor force according to the definitions of the EU Labor Force Survey, and 7.3 percent of the dependent labor force according to the traditional Austrian method of calculation.

Thanks to the consolidation drive of the past years, the financial balance of general government was halved to –2½ percent between 1995 and 1997. The solid income and employment gains expected over the forecasting period will strongly increase revenues from the income tax on wages and salaries and social security contributions. Given the scheduled generous increase in family support measures, the financial balance of general government is likely to improve only slightly to –2¼ percent of GDP (1999).

ECONOMIC UPSWING IN EUROPE BECOMES MORE BROAD-BASED

Relatively stable exchange rates in the European Monetary System, less restrictive fiscal policies, low nominal interest rates and falling crude oil prices provide favorable conditions for the continuation of the current recovery in Europe. Exports remain the most buoyant component of aggregate demand, but economic activity is increasingly supported by investment and consumer expenditures. Economic growth in the EU will accelerate to almost 3 percent. Unemployment will persist, nonetheless, at a very high level. An unemployment rate of 10¾ percent is forecast for the EU.

Table 2: World economy

		1995	1996	1997	1998	1999
		Percentage changes from previous year				
Real GDP						
Total OECD		+ 2.3	+ 2.6	+ 2.8	+ 2.3	+ 2.5
USA		+ 2.0	+ 2.8	+ 3.8	+ 2.5	+ 2.0
Japan		+ 1.5	+ 3.9	+ 0.9	± 0.0	+ 1.5
EU		+ 2.8	+ 1.9	+ 2.6	+ 2.8	+ 3.0
Germany		+ 1.8	+ 1.4	+ 2.2	+ 2.5	+ 3.0
Eastern Europe		+ 5.4	+ 4.7	+ 4.3	+ 4.5	+ 5.0
World trade, volume		+ 9.5	+ 6.8	+ 9.6	+ 6.6	+ 6.7
OECD exports		+ 8.6	+ 6.3	+10.9	+ 7.3	+ 6.7
Intra-OECD trade		+ 5.5	+ 6.1	+11.1	+ 8.9	+ 7.5
Market growth[1]		+ 6.1	+ 6.2	+ 9.4	+ 8.0	+ 7.5
Primary commodity prices, in US$						
HWWA index, total		+10.0	+ 3.0	– 2.0	– 7.0	+ 4.0
Excluding energy		+11.0	– 9.0	+ 0.0	+ 5.0	± 0.0
Crude oil prices						
Average import price (cif) for OECD countries	US$/barrel	17.2	20.6	19.1	15.5	17.0
Exchange rate	ATS/US$	10.08	10.59	12.20	12.90	12.60

[1] Real import growth of trading partners weighted by Austrian export shares.

The recovery that began in the European Union in the middle of 1996 followed a classical pattern: at first the stimuli came from the strong upturn in export demand. In some economies which benefited from the close linkage to the buoyant North American economies and from favorable exchange rates and other special factors, the recovery became more broad-based as early as 1997. Investment and consumer demand strengthened and boosted growth as well as employment. This pattern does not hold, however, for other European economies; in Germany and France in particular, where disposable income and consumer spending was flat mainly due to public sector consolidation policies, domestic demand remained sluggish. Not until the end of 1997 was there some evidence of a pick-up in investment activity.

The transition from a recovery that is primarily driven by exports to one driven by domestic demand often constitutes a fragile phase of the business cycle. During the period 1994-95 this transition was not successful: the strong upswing stalled after a short time. In 1998, the economic environment seems to be more propitious to economic growth in various ways. In contrast to the mid-1990s, stable exchange rates prevail; moreover, stability is assured for the future, as 11 EU member countries will join the Economic and Monetary Union. Nominal long-term interest rates were on the decline during the last few months in the southern-European countries and to a lesser degree in Germany and France, a consequence of the step-wise transition to the Monetary Union and the capital inflow in the wake of the crisis in Asia. The most restrictive phases of the consolidation drive has come to an end in most EU countries. Crude oil prices have declined by more than one fourth since the end of 1997 (the average price of oil imports to OECD countries is expected to be 15½ $ per barrel), providing an additional stimulus to the economic expansion. Thus, there are several similarities between the current recovery and that of 1986-87, which formed the basis for a long and solid upswing.

Given these favorable conditions, economic growth in the EU is forecast to accelerate from 2.6 percent in 1997 to 2¾ percent in 1998 and to almost 3 percent in 1999. The effects of the turmoil in Asia on the European economy are likely to be very modest. The pick-up in economic activity is expected to contribute to a smooth transition to the European Economic and Monetary Union. The strengthening of economic growth will have a positive impact on the labor market and public sector budgets. The surplus in the current account, at present about 1½ percent, will persist, however, despite the revival of domestic demand.

The economies of Austria's major trading partners, Germany, Italy and Switzerland, will expand at a slower pace than the EU on average. In East-Central Europe, however, output and demand continue to expand at a brisk pace.

In Germany, the recovery was more sluggish than had been expected by many forecasters. The main factors dampening the upswing were the deep crisis in the construction industry and the persistent stagnation in private consumption. During the last few years, Germany was the only country to record a strong rise in unemployment; the labor market situation continued to worsen even in 1997 when exports boomed. The unemployment rate increased to 9¾ percent. First signs of a revival of investment in machinery and equipment appeared as late as the second half of 1997. The stabilization of the labor market and tax changes (decrease in the Solidarity tax surcharge, increase in the value-added tax as of April 1) might boost private consumption, but even then consumption growth might not exceed 1 percent. If investment activity picks up and the export boom continues, Germany's economy might expand by 2½ percent in 1998.

Given the lira appreciation and the severely restrictive fiscal and monetary polices, Italy recorded an amazingly high growth rate of almost 1½ percent in 1997. It must be noted, however, that the scrapping premium for old automobiles contributed 1 percentage point to the rise in consumer expenditures. The sharp drop in long-term and short-term interest rates in the run-up to European Economic and Monetary Union provided a positive impulse to economic expansion in Italy. With fiscal policy maintaining its restrictive stance, the growth rate in 1998 and 1999 will be at least ½ percentage point below the European average.

The economies of Austria's main trading partners in the EU and of Switzerland are forecast to grow at a below-average rate. The economies of East-Central Europe are likely to continue their rapid expansion. Exports from this region will benefit from the strengthening recovery in western Europe: import restrictions are being relaxed, and the growth potential will rise. In Hungary, the economic expansion is picking up momentum after the stabilization measures of 1996: merchandise imports are forecast to increase by about 15 percent per year. The economies of the Slovak Republic, Poland and Croatia will continue to enjoy strong expansions; in the Czech Republic, a marked pick-up in economic activity is not in sight before 1999.

EXPORT BOOM AND A FALL IN OIL PRICES EASE TRADE ACCOUNT PROBLEMS

High growth in Austria's export markets, favorable exchange rates and strong productivity gains in manufacturing suggest a continuation of the export boom. Import prices are likely to remain unchanged. The trade account is expected to improve markedly.

Thanks to the persistently solid expansion in East-Central Europe and the recovery in the EU, Austrian export markets are projected to expand at a rate of 8 percent per year. As result of the favorable development of exchange rates, high productivity gains and moderate wage increases, relative unit labor costs are expected to decline by 10 percent over the period from 1995 to 1999 and bring about significant gains in market shares. Thus, the boom in merchandise exports is likely to continue: the growth rate of about 10 percent per year is remarkably high, but will fall short of the rate recorded by the Austrian Central Statistical Office for 1997 (+15 percent in real terms).

Significant differences persists between the foreign trade statistics compiled by the Statistical Office and balance of payments statistics of the Austrian National Bank, which recorded an increase in payments for merchandise exports of only 12 percent. The increase in imports (in nominal terms in particular) are forecast to lag behind the surge in exports. This can be attributed primarily to the drop in oil prices. In view of the strong expansion in oil production and the weakness of demand in the industrialized countries, the average OECD import price is forecast to fall from 19 \$ per barrel in 1997 to 15½ \$ in 1998; a slight rise is expected for 1999. The main effect of the decline in oil prices is on inflation. There may also be a positive effect on economic growth, but it is likely to be small, as the intensity of primary energy in output of the OECD countries has been almost halved since the beginning of the 1970s. Given the pick-up in economic activity and the strong link between exports and imports, Austria's merchandise imports are forecast to expand at the lively pace of 8 percent per year.

The favorable export performance as well as the stagnation of import prices in 1998 will provide a marked relief to the trade account; according to the foreign trade statistics, the deficit will decline to ATS 50 billion. If the balance in the account "unclassified goods and services" (according to the balance of payments statistics) is included, the deficit amounts to some ATS 90 billion in each of the years 1996 and 1997; a level of ATS 80 billion is expected for 1998 and 1999, respectively.

Table 3: Productivity

	1995	1996	1997	1998	1999
	Percentage changes from previous year				
Total economy					
Real GDP	+2.1	+1.6	+2.5	+2.7	+3.0
Employment[1]	+0.2	–0.5	+0.4	+0.8	+0.9
Productivity (GDP per employment)	+1.9	+2.1	+2.2	+1.9	+2.0
Manufacturing					
Production[2]		+1.3	+4.3	+5.0	+4.3
Employees		–2.9	–1.4	±0.0	–0.3
Productivity per hour		+4.5	+5.5	+5.0	+4.6
Working hours per day for workers		–0.3	+0.2	±0.0	±0.0

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

DECLINING CURRENT ACCOUNT DEFICIT

The improvement in the merchandise trade account also tends to ease the current account problems. In the 1990s, structural problems in summer tourism, the marked appreciation of the schilling and large net payments to the EU gave rise to a huge deficit. In 1997, the shortfall amounted to almost 2 percent of GDP. For 1998, the outlook is for a reduction in the deficit to about ATS 36 billion or less than 1½ percent of GDP.

The surplus in the tourism balance is expected to stabilize, albeit at the low level achieved in 1997 (¾ percent of GDP). The surplus is now more than ATS 50 billion below the level at the beginning of the 1990s. For the first time in several years, tourism exports are expected to rise slightly (+1 percent in real terms) in 1998, the result of favorable exchange rates and the recovery of the European economies. High quality lodging facilities continue to fare better than private rooms. The development of city tourism is relatively good. The competitive position of Austria's tourism might improve within the Economic and Monetary Union when devaluations of the currencies of important competitors are no longer possible. Tourism imports have also stabilized: after recording hefty increases between 1992 and 1996 (+7 percent in real terms per year), spending by Austrian tourists abroad will rise by only about 1½ percent per year over the forecast period, thanks to the change in foreign exchange rates.

LOW NOMINAL INTEREST RATES

Long-term interest rates have been more or less stable since 1996. The future development of interest rates will be mainly determined by the conditions governing the convergence of short-term interest rates in the countries participating in EMU. The present forecast is based on the assumption of a slight increase in interest rates by 1999. At the beginning of 1999, monetary policy-making will be transferred to the European Central Bank, a change that will impede the comparability of future interest rates with current ones. Owing to the ample inflow of capital in connection with the crisis in South-East Asia, long-term interest rates declined significantly during the last few months. However, cyclical factors might push up interest rates in the bond market over the projection period.

VIGOROUS EXPANSION OF MANUFACTURING OUTPUT

The buoyant growth in merchandise exports is accompanied by a vigorous expansion of manufacturing output, but the growing strength of domestic demand is increasingly contributing to the rise in economic activity. In 1998, output growth in manufacturing (+5 percent) is projected to be strong enough to halt the long-term decline in employment, despite the continuing high productivity gains. The rise in aggregate demand should also boost investment in machinery and equipment.

All cyclical indicators for the goods-producing sector provide positive signals. The financial position of the manufacturing sector has improved markedly since 1997, and so has the price-determined competitive position vis-à-vis the principal trading partners. According to the WIFO business survey from the first quarter of 1998, foreign orders stabilized at a high level; production expectations remained optimistic, especially in the basic goods sector, the chemical industry, and in technical manufacturing. Production expectations of enterprises in consumer goods industries became more optimistic, albeit only relative to the rather gloomy outlook in earlier surveys.

In manufacturing, output rose by more than 4 percent in 1997 on a year-on-year basis. The expansion is likely to accelerate to 5 percent in 1998, encompass more branches and continue at this high rate in 1999. Despite further hefty productivity gains (+5 percent per year), employment in manufacturing is expected to stabilize after a long downward slide. Some branches in technical manufacturing, such as the machinery and metal production industries, have already started hiring new employees.

The vigorous revival in aggregate demand, more optimistic expectations, high profitability and the low cost of outside capital should trigger a pick-up in investment activity. Increasingly investment is undertaken not so much to streamline operations but to expand capacity. The manufacturing sector accounts for about one third of investment in equipment and machinery. In the basic goods sector and in technical manufacturing, where investment activity has been lively since 1996, no change is expected. As the cyclical expansion gains momentum, other sectors, such as small-scale industry and various service branches with low investment activity, should report higher capital outlays. Investment in equipment and machinery, adjusted for price increases, is expected to rise by 6 percent in 1998 and by 7 percent in 1999.

Table 4: Earnings and international competitiveness

	1995	1996	1997	1998	1999
	Percentage changes from previous year				
Gross earnings per employee	+3.2	+1.7	+1.6	+2.0	+2.7
Gross real earnings per employee	+1.5	–0.8	–0.4	+0.8	+1.2
Net real earnings per employee	+0.5	–2.2	–2.4	+0.4	+0.7
Net wages and salaries	+2.7	+0.9	+0.1	+2.6	+3.3
Unit labor costs					
Total economy	+1.4	–0.5	–0.5	+0.2	+0.7
Manufacturing	–0.6	–1.0	–3.8	–2.5	–1.5
Relative unit labor costs[1]					
Vis-à-vis trading partners	+2.1	–3.0	–4.1	–2.3	–0.9
Vis-à-vis Germany	–0.2	–0.6	±0.0	–0.7	–0.1
Effective exchange rate – manufactures					
Nominal	+3.0	–1.2	–1.8	±0.0	+0.6
Real	+2.6	–1.5	–2.6	–1.1	–0.3

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

LIVELY RENOVATION AND CIVIL ENGINEERING CONSTRUCTION

For the first time in a prolonged period statistics have become available on the volume of construction put in place. These statistics show an increase in value added of 3 percent in real terms for 1997, a much higher rate than estimated at the December forecast. Much of the extra output growth is, however, concentrated in the first quarter of 1997 when construction activity benefited from the clement weather conditions. Turnover stagnated in the following quarters. As result of tax incentives, activity in the renovation and modernization business was brisk. In 1998, this sector should be able to maintain this high level. Residential construction, however, will experience a marked decline, despite an ample flow of public funds. Excess demand in this area has been almost eliminated over the last few years, and the number of construction permits in subsidized residential construction has fallen sharply. The less than optimistic business climate in the construction sector is another piece of evidence for this trend. In Vienna, funds were allocated for several non-residential construction projects (the new museum quarters, the development of the area around the railway station Wien-Mitte).

The situation in civil engineering has improved. The establishment of new public sector entities, new models of financing public investment and revenues from autobahn tolls provide additional public funds for the extension and repair of the railroad and road system. Industrial construction is still down, but should recover as soon as the cyclical upturn picks up momentum. According to business surveys, the tourism industry is set to implement long-delayed investment plans and spend more on construction investment. The total volume of construction put in place will expand only slightly in 1998 (+1 percent), but the outlook is for a modest recovery in 1999.

HIGHER INCOME GAINS WILL STIMULATE CONSUMER SPENDING

After declining for two years, real wages and salaries (on a net basis) will increase again in 1998 and 1999, though only slightly (by about ½ percent per year):

- The growth of wages and salaries is likely to accelerate as the recovery picks up; for the first time since 1995, compensation in the public sector will also record substantial gains. On the other hand, the increasing flexibility on the labor market, particularly with respect to new working time arrangements, will have a dampening effect on wage growth because bonus payments, payments in excess of wage rates set in bargaining agreements and overtime payments are on the decline. The share of wages in GDP continues to fall, despite higher income gains for persons in dependent employment; as is typical for an economic upswing, income from property and entrepreneurship rises twice as fast as compensation for wage earners.
- The federal budget does no longer have a negative impact on transfer payment; at the beginning of 1998, pension payments were increased by 1.3 percent. Disposable income available to wage and salary earners (including retired persons) will again increase substantially in real terms. In 1999, about ½ percentage point of the increase is due to the "family package".

The growth in total disposable income (by 2½ percent per year in real terms) will revive consumer spending, which is expected to increase by 1¾ percent in 1998 and by more than 2 percent in 1999 in real terms. Sales of durable consumer goods are likely to boom again, after the trough in 1997. As a rule, consumers adjust their consumption plans with a certain lag to changes in income. Thus, con-

Table 5: Private consumption

	1995	1996	1997	1998	1999
	Percentage changes from previous year, volumes				
Private consumption	+2.9	+2.4	+0.7	+1.7	+2.1
Durables	+0.9	+8.0	–2.3	+3.5	+3.1
Non-durables and services	+3.2	+1.6	+1.2	+1.4	+1.9
Net wages and salaries	+1.2	–1.6	–1.8	+1.4	+1.8
Household disposable income	+2.9	+0.7	–0.1	+2.5	+2.6
	As a percentage of disposable income				
Household saving ratio	10.2	8.6	7.9	8.6	9.0

sumption growth will lag behind income growth over the next two years, and the saving rate, about 9 percent of disposable income in 1999, will gradually approach the "normal" level. Retail trade is likely to benefit from the rebound in consumer spending and the incipient recovery of the tourism industry. Buoyant exports and the expansion in manufacturing will boost turnover in wholesale trade.

PRICE STABILITY PERSISTS

Inflation continues to be very subdued. In 1998, the inflation rate will be 1.2 percent, after 1.3 percent in 1997. Falling unit labor costs, intense competitive pressures and the drop in energy prices are the main factors keeping inflation flat. So far, the plunge in oil prices has not been fully passed on to the consumer price level. It will also be incumbent on consumer advocates to make sure that the hike in the value-added tax as of April 1 in Germany does not spill over to Austria and raise the prices of items such as books and cars. Given strong competitive pressures and stable unit labor costs, inflation will rise only slightly to 1½ percent, in tandem with the economic upswing.

UNEMPLOYMENT RISES DESPITE SOLID EMPLOYMENT GAINS

The tight link between economic growth and the development of employment is again visible in the current upturn: the increase in output boosts employment (excluding persons in military service and on parental leave) by almost 30,000 per year. But, with the labor supply outpacing the expansion in labor demand, unemployment keeps increasing.

The beginning of the current year produced surprisingly good employment data. Most of the employment gains were recorded in the area of producer-oriented services (including workers on loan to other firms) and in health services, and concerned mainly the female workforce. Many employment relations involve part-time work. In manufacturing, the vigorous output expansion is likely to halt the long-term decline in employment. The number of persons in dependent employment (excluding persons in military service and on parental leave) is forecast to rise by 27,000 (+0.9 percent) in 1998 and by 30,000 (+1 percent) in 1999. In the whole economy, productivity is expected to increase by 2 percent, at a rate close to the long-term average.

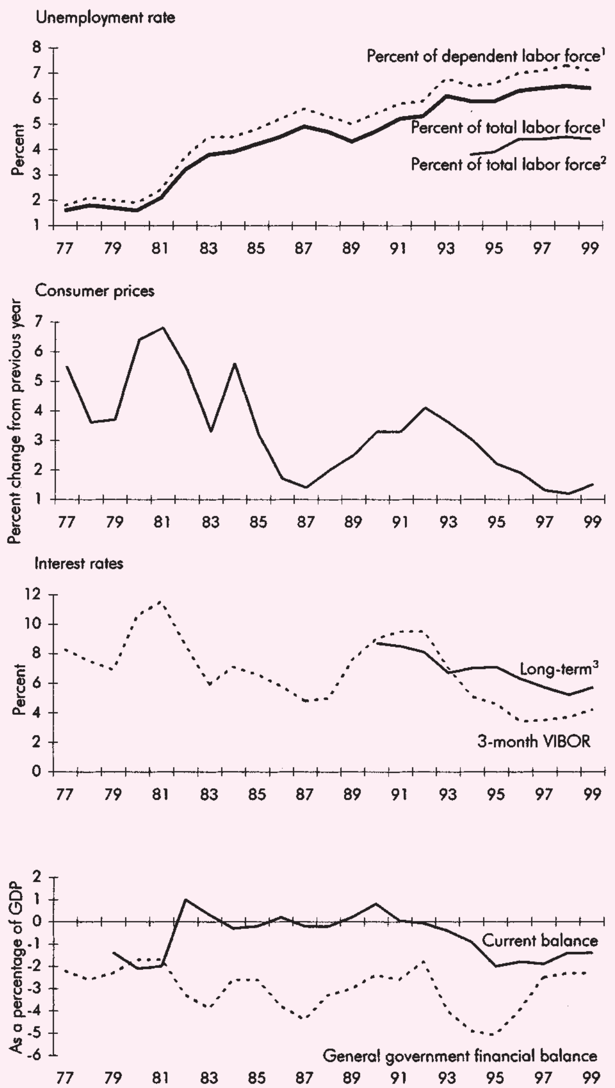
Table 6: Labor market

		1995	1996	1997	1998	1999
		Changes from previous year (in 1,000)				
Demand for labor						
Civilian employment		– 12.3	– 23.8	+ 8.8	+ 15.0	+ 25.0
Dependent employment[1]		– 2.5	– 20.9	+ 8.3	+ 14.0	+ 24.0
Excluding parental leave and military service		+ 0.6	– 16.5	+ 12.8	+ 27.0	+ 30.0
Percentage changes from previous year		+ 0.0	– 0.6	+ 0.4	+ 0.9	+ 1.0
Parental leave and military service[1]		– 3.2	– 4.4	– 4.4	– 13.0	– 6.0
Foreign workers[2]		+ 9.3	+ 0.0	– 1.6	+ 3.0	+ 3.0
Self-employed[3]		– 9.8	– 2.9	+ 0.5	+ 1.0	+ 1.0
Labor supply						
Total labor force		– 11.6	– 9.0	+ 11.7	+ 22.2	+ 20.0
Foreign		+ 8.7	+ 2.8	– 1.7	+ 2.0	+ 3.0
Migration of nationals		+ 5.6	+ 4.9	+ 5.0	+ 3.0	± 0.0
Indigenous		– 25.9	– 16.7	+ 8.4	+ 17.2	+ 17.0
Surplus of labor						
Registered unemployed[4]		+ 0.8	+ 14.8	+ 2.8	+ 7.2	– 5.0
In 1,000		215.7	230.5	233.3	240.5	235.5
Unemployment rate						
Percent of total labor force[5]	in percent	3.9	4.4	4.4	4.5	4.4
Percent of total labor force[4]	in percent	5.9	6.3	6.4	6.5	6.4
Percent of dependent labor force[4]	in percent	6.6	7.0	7.1	7.3	7.1
Participation rate[6]		67.5	67.2	67.2	67.4	67.5
Employment rate[7]		63.5	62.9	62.9	63.0	63.2

[1] According to Hauptverband der österreichischen Sozialversicherungsträger. – [2] Corrected for statistical breaks. – [3] According to WIFO. – [4] According to labor exchange statistics. – [5] According to Eurostat. – [6] Total labor force as a percentage of active population (aged 15 to 64). – [7] According to Hauptverband der österreichischen Sozialversicherungsträger. – [7] Employment as a percentage of active population (aged 15 to 64).

In the past, labor supply has been very responsive to an increase in labor demand. This phenomenon is very pronounced in the current expansion. The marked employment gains in the service sector benefit mostly women who were not part of the labor supply in the recessionary phase of the cycle. Moreover, the cut in the time of eligibility for parental leave assistance to 1½ years has the effect of increasing the supply of female workers. The termination of special unemployment assistance has a similar impact. As a result of these primarily institutional changes, unemployment rises in tandem with employment. In 1998, some 240,000 persons will be registered as unemployed. This implies an unemployment rate of 7.3 percent of the dependent labor force according to the traditional Austrian method of calculation, and of 4.5 percent of the total labor force according to the definitions of the EU Labor Force Survey. The outlook is for a marginal drop in unem-

Figure 2: Main economic indicators



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

ployment in 1999. The measures proposed by the federal government within the "national employment program" may contribute to this development.

PAUSE IN THE BUDGET CONSOLIDATION DRIVE

Comprehensive measures to consolidate the budgets of the public sector have pushed net borrowing from 5 percent of GDP in 1995 to 2½ percent in 1997. This austerity policy was required not only by the rules of the Maastricht Treaty but was also necessary to enlarge the economic and social maneuvering room that had become severely restricted by the steady rise in interest payments. It took the form of tax increases, restraint in the public sector's wage bill and significant cuts in social transfers. The consolidation program strongly dampened the growth in disposable income and private consumption; this effect was mainly felt in 1997. These measures were painful, but qualified Austria for the Economic and Monetary Union.

Table 7: Key policy indicators

	1995	1996	1997	1998	1999
	Billion ATS				
Fiscal policy					
Central government net balance	–117.9	– 89.4	– 67.2	– 67.3	– 70.1
	As a percentage of GDP				
Central government net balance	– 5.1	– 3.7	– 2.7	– 2.6	– 2.6
General government financial balance	– 5.1	– 4.0	– 2.5	– 2.3	– 2.3
	In percent				
Monetary policy					
3-month interest rate (VIBOR)	4.6	3.4	3.5	3.7	4.2
Long-term interest rate[1]	7.1	6.3	5.7	5.2	5.7
Bond yield, average	6.5	5.3	4.8	4.9	5.4
	Percentage changes from previous year				
Effective exchange rate					
Nominal	+ 3.9	– 1.5	– 2.3	– 0.0	+ 0.8
Real	+ 3.2	– 2.1	– 3.3	– 1.3	– 0.2

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

The pick-up in employment and income will now help to improve the financial position of the public sector. Revenues from the income tax on wages and salaries will attain a record level, increasing by 5 percent per year in 1998 and 1999. Social security contributions are expected to grow by 3½ percent. The automatic stabilizers will have the effect of reducing the government deficit and widening the leeway for countercyclical policies. With this in mind, it should be noted that in 1999 the government deficit will not fall any further but level off at 2.3 percent of GDP. The generous measures contained in the "family package" are the main reason for this development. Thus, the maneuvering room for the envisaged tax reform in the year 2000 appears severely restricted.

Cut-off date: April 1, 1998.