

■ STRONG CYCLICAL UPSWING LEAVES BUDGETARY PROBLEMS UNRESOLVED

ECONOMIC OUTLOOK FOR 2000 AND 2001

Accelerated export growth and solid expansion of domestic demand suggest the Austrian economy will grow by 3.1 percent in volume this year – an upward correction by ¼ percentage point from last December's projections. In 2001, growth may decelerate somewhat (+2.7 percent) under the impact of slackening activity abroad and, more importantly, a stronger demand-restraining impact of domestic budgetary retrenchment. Fiscal policy action, while limiting government net borrowing at a ratio of 2 percent of GDP, will contribute to somewhat stronger inflation. The labour market will benefit from the favourable business cycle trend.

Gross Domestic Product (GDP) in the fourth quarter of 1999 rose by a price-adjusted 3.2 percent above the year-earlier level. The recovery was particularly strong with regard to manufacturing output and investment in machinery and equipment. For the whole of 1999, a rate of growth of 2.2 percent, as has been projected by WIFO since March of last year, has thereby been confirmed.

In 2000, the boom in export industries is set to continue, given the favourable external environment. In the EU, demand and output are expected to increase by 3.2 percent in real terms, interest rates are comparatively low, and exchange rates are beneficial for the euro-zone economies. Moreover, competitiveness of Austrian exporters is boosted by a lower cost burden. Under such conditions, volume exports may advance by some 8 percent, giving strong momentum also to manufacturing output (+5 percent) and to private investment (machinery and equipment +7 percent).

Domestic demand is proving very strong this year. Fiscal policy is still having an altogether expansionary effect which, together with sizeable employment gains, adds substantially to real net disposable income from earnings and social transfers (+2½ percent), to private consumption (+2.7 percent) and to sales turnover

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

Table 1: Main results

		1997	1998	1999	2000	2001
		Percentage changes from previous year				
GDP						
Volume		+ 1.2	+ 2.9	+ 2.2	+ 3.1	+ 2.7
Value		+ 2.8	+ 3.5	+ 2.8	+ 4.6	+ 4.2
Manufacturing ¹ , volume		+ 3.8	+ 3.4	+ 2.0	+ 5.0	+ 4.3
Private consumption expenditure, volume		+ 0.1	+ 1.5	+ 2.4	+ 2.7	+ 2.3
Gross fixed investment, volume		+ 0.8	+ 6.8	+ 2.8	+ 3.6	+ 3.7
Machinery and equipment ²		+ 4.6	+10.6	+ 4.9	+ 7.0	+ 6.5
Construction		- 1.6	+ 4.1	+ 1.2	+ 1.0	+ 1.5
Exports of goods ³						
Volume		+16.5	+ 8.1	+ 5.5	+ 8.0	+ 7.5
Value		+16.8	+ 8.4	+ 5.8	+ 9.1	+ 8.6
Imports of goods ³						
Volume		+ 9.4	+ 7.1	+ 5.2	+ 7.5	+ 6.5
Value		+10.9	+ 6.6	+ 5.5	+ 9.1	+ 7.6
Trade balance ³	billion ATS	-75.2	-67.4	-68.4	-74.9	-71.6
	billion euro			- 5.0	- 5.4	- 5.2
Current balance	billion ATS	-64.1	-56.8	-58.6	-62.6	-57.2
	billion euro			- 4.3	- 4.6	- 4.2
	as a percentage of GDP	- 2.5	- 2.2	- 2.2	- 2.2	- 2.0
Long-term interest rate ⁴	in percent	5.7	4.7	4.7	5.8	5.6
Consumer prices		+ 1.3	+ 0.9	+ 0.6	+ 1.6	+ 1.4
Unemployment rate						
	percent of total labour force ⁵	4.4	4.7	4.4	4.2	4.1
	percent of dependent labour force ⁶	7.1	7.2	6.7	6.3	5.9
Dependent employment ⁷		+ 0.4	+ 1.0	+ 1.2	+ 1.1	+ 1.2
General government financial balance	as a percentage of GDP	- 1.9	- 2.5	- 2.0	- 2.0	- 2.0

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.

(+3.3 percent). Next year, the trend of expansion should flatten somewhat. While higher wage increases and continued strong employment advances may boost disposable income, fiscal policy will probably restrain demand as measures designed to consolidate public finances over the medium term become effective. Growth of the construction sector will clearly lag behind the overall trend, as a result of falling demand for newly built homes and of cuts of public orders to civil engineering.

The current account should stabilise around a deficit of slightly above 2 percent of GDP. The negative balance in merchandise trade should be offset by a surplus on services, even if tourism net earnings may fall short of the more optimistic expectations of last December. The deficit in the income balance (high income of foreign investors from interest, dividends and profits) and in the transfer balance (including net payments to the EU) largely account for Austria's high external deficit.

A reduction in the Federal government's household deficit in the current year is mainly brought about by a number of one-off measures. In addition, some indirect taxes and public charges will be raised significantly as from next June. It is only as from next year that the necessary consolidation will be supported by more sustained measures. While the targeted deficit reduction in the Federal budget

seems feasible, the government's expectations for surpluses in the households of the Federal states, the municipalities and the social security bodies would appear optimistic in view of shortfalls in tax revenues and financing problems of the health insurance system. In 2001, the fiscal balance as defined by "Maastricht" requirements will be further weakened if the government proceeds as planned with cutting non-wage labour costs. Given such considerations, general government net borrowing is likely to amount to 2 percent of GDP throughout the projection period. The deficit targets laid down in the Stability Programme, i.e., 1.7 percent of GDP in 2000 and 1.5 percent in 2001, will only be met if additional consolidation efforts were undertaken.

Inflation has been accelerating in recent months, mainly as a result of higher energy prices. An upward trend also for other commodities, the effects of a stronger dollar and rising demand and capacity utilisation are increasingly being translated into higher prices for manufactures. In an effort to trim the budget deficit, hikes in indirect taxes and public charges will take effect by mid-2000, which will add 0.3 percentage points to the annual inflation rate, both this year and next. Consumer prices may thus move up by 1.6 percent in 2000 and 1.4 percent in 2001.

The situation on the labour market is set to improve further. Driven by stronger activity, employment is rising at an annual pace of about +35,000, with gains meanwhile extending to full-time workers. Budgetary allocations for active labour market policy are not yet known which complicates projections for the number of unemployed. In case of no decline in the number of people in job training, the average jobless figure for 2001 may for the first time since 1992 fall below 200,000. This would correspond to an unemployment rate of 5.9 percent of the dependent labour force (national definition) or 4.1 percent of the total labour force (EU Labour Force Survey).

Economic growth in Austria is to no significant extent being constrained from the supply side. Lively private investment provides for a steady expansion of overall productive capacities. "Hidden reserves" in labour supply are still substantial, leaving a comfortable margin for additional demand to be met. However, an "active" approach to education as well as labour market policy appears crucial from an overall economic perspective, in order to support the process of structural adjustment.

At the present juncture, the balance of risks to the forecast would appear to be on the upside: recovery in Europe has gained momentum to such extent that growth of demand and output may well outpace the present projections. For 2001, however, the risk may rather be in over-estimating worldwide cyclical strength, since notably a slump in the

Figure 1: Indicators of economic performance



¹ Vis-à-vis the euro area. – ² Manufacturing; in a common currency vis-à-vis trading partners. – ³ 10-year central government bonds (benchmark). – ⁴ Excluding parental leave and military service.

U.S. economy cannot be entirely ruled out. The latter would have negative repercussions also on the Austrian economy, as would have a more restrictive turn in European interest and exchange rate developments. Any impact of the political (and partly also economic) boycott measures recently imposed on Austria are extremely difficult to assess at present, partly because this will obviously depend on for how long these measures were to be maintained.

GROWING MACRO-ECONOMIC IMBALANCES IN THE USA

For the time being, there are no signs for a rapid deceleration of hitherto strong U.S. growth. In 1999, GDP rose by

4.2 percent in volume, showing a renewed pick-up towards the end of the year. Lively internal demand is the major force driving down unemployment – the unemployment rate of 4 percent may be regarded as close to the level of full employment – and being responsible for the healthy state of public finances – a surplus of around 2 percent of GDP is expected for this year.

A significant rise in private consumption expenditure has been brought about by a striking fall in the private household savings ratio to a low of just over 2 percent of disposable income. At the same time, the deficit of the corporate sector rose markedly with the boom in private investment. The mirror image of the large deficit in the private sector financial balance are surpluses of the public

Table 2: World economy

	1997	1998	1999	2000	2001		
	Percentage changes from previous year						
<i>Real GDP</i>							
Total OECD	+ 3.5	+ 2.5	+ 2.7	+ 3.0	+ 2.7		
USA	+ 4.5	+ 4.3	+ 4.2	+ 3.5	+ 2.8		
Japan	+ 1.6	- 2.5	+ 0.3	+ 0.8	+ 1.3		
EU	+ 2.5	+ 2.6	+ 2.2	+ 3.2	+ 3.0		
Euro area	+ 2.3	+ 2.7	+ 2.2	+ 3.2	+ 3.1		
Germany	+ 1.5	+ 2.2	+ 1.5	+ 2.7	+ 2.8		
Central Eastern Europe ¹	+ 5.1	+ 3.4	+ 2.5	+ 3.8	+ 4.5		
<i>World trade, volume</i>	+10.0	+ 5.1	+ 4.5	+ 7.0	+ 6.0		
OECD exports	+11.1	+ 5.4	+ 4.0	+ 6.8	+ 6.5		
Intra-OECD trade	+11.3	+ 7.9	+ 6.0	+ 6.8	+ 6.5		
<i>Market growth²</i>	+ 9.5	+ 9.1	+ 5.0	+ 6.8	+ 6.5		
<i>Primary commodity prices, in USD</i>							
HWWA index, total, 1990 = 100	- 2.0	-23.0	+13.0	+27.0	- 7.0		
Excluding energy	+ 1.0	-13.0	- 8.0	+ 7.0	+ 3.0		
<i>Crude oil prices</i>							
Average import price (cif) for OECD countries	USD per barrel		19.1	12.6	17.3	24.0	21.0
Exchange rate	USD per ECU or euro		1.134	1.121	1.070	1.00	1.08

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

and the foreign sector. The current account deficit has widened considerably with the strength of domestic demand, representing approximately 4 percent of GDP in 2000. The U.S. economy is thus characterised by major macro-economic imbalances which are hardly sustainable over the medium term.

The Federal Reserve is trying to bring these imbalances under control by raising interest rates in a short sequence. Short-term rates have by now come to exceed long-term rates (which are heading down as a consequence of the redemption of public debt). The intention is to counter not only potential inflationary danger in goods markets, but also, and in particular, the excessive rise in stock market values. A possible sharp downward correction of share prices would, however, have adverse effects for consumer and investment demand. WIFO's growth projection for the USA assumes that it will be possible to unwind these imbalances and at the same time avoid slippage into a recession, through active monetary and fiscal management. Under such assumptions, the U.S. economy may expand by 3½ in the current year, and by 2¾ percent in 2001.

Whereas in the USA the 1990s were characterised by the longest economic expansion of the post-war era, Japan has been caught in the longest recession. Over the entire decade, GDP rose by only 12 percent at constant prices, compared with +33 percent for the USA and +18 percent for the EU. During the second half of 1999, activity relapsed into stagnation. Exports are being constrained by a marked appreciation of the yen caused by strong capital inflows. Cuts in bonus payments and the gloomy outlook for employment are dampening private consumption. Yet, survey results appear to indicate a revival in corporate in-

vestment. An early end to the persistent crisis may not be expected under the present framework conditions. By contrast, recovery is making progress in the countries of Southeast Asia which had been most severely affected by the economic and financial crisis of 1997-98. Yet, sluggishness of aggregate demand in Japan is undermining growth in the region as much as the credit restrictions applied by the banking sector suffering from the high number of bad loans.

RECOVERY IN THE EU GAINING MOMENTUM

Results from consumer and business surveys convey a picture of widespread confidence. The strong cyclical upswing in the EU is set to continue, GDP growth in 2000 is expected at a real rate of 3.2 percent. In many EU countries, domestic demand is providing major support, shielding to some extent the recovery against potential external shocks.

The business cycle upswing in the EU has gained significant momentum towards end-1999. GDP in the fourth quarter rose 1 percent on a seasonally adjusted basis vis-à-vis the previous period, and 3 percent from the year-earlier level. For the whole year 1999, the rate of growth was 2.2 percent. Industrial production picked up strongly in recent months, largely driven by the strength of the dollar which stimulated European exports and, as a consequence, private investment. In the majority of the EU countries, however, manufacturers received more orders not only from abroad, but also from domestic customers. Leading indicators point to an unabated upward trend in the near future. According to the regular survey from the European Commission, industrial confidence has further increased in February. Demand and output are gaining most notably in countries with close trade links with the USA and in a group with France as the centre of gravity, where domestic demand has become the major force of recovery. With real GDP growth in 2000 projected at around 3½ percent, France is also the growth engine for the EU as a whole. But also in Italy, where it has been dampened by pronounced fiscal restriction, activity is showing clear signs of picking up and GDP may advance by 2½ percent this year.

The indicator for consumer confidence has risen to a new peak early in the year. A major reason has been the steady improvement in labour markets. Benefiting from stronger activity and intensified efforts of "active" labour market

policy, the seasonally adjusted unemployment rate in the EU subsided to 8.9 percent in the fourth quarter 1999 (down from 9.7 percent a year earlier). Developments have been particularly favourable in France, Sweden, Finland, the Netherlands and Spain.

In 2000, EU GDP is expected to increase by an inflation-adjusted 3.2 percent or more, and the pace should remain lively over the next year. Countries where consumer demand lends firm support to economic activity are likely to fare better than the average. External and policy conditions may become less favourable, however. Slackening demand in the USA would, in the event, also weaken economic growth in Europe, as would adverse developments in interest and exchange rates.

EXPORT-DRIVEN RECOVERY IN GERMANY

In Germany, no substantial recovery of employment has been registered so far. This is also due to the sluggishness of domestic demand which has been suffering from the reunification-related heavy burden, more recently, however, also from fiscal consolidation measures introduced by the Federal government. Exports and industrial output, on the other hand, are gaining upward momentum. New foreign orders to manufacturing industry exceeded the year-earlier level by 17 percent in January. Output is also pointing clearly upwards, with a year-on-year advance of nearly 5 percent in early 2000. Such an increase, while still below average in a European comparison, indicates a significant acceleration of business activity. The marked rise in the Ifo business climate index reflects a substantial improvement in entrepreneurial confidence. GDP in the fourth quarter 1999 rose $2\frac{1}{4}$ percent above the year-earlier level and $\frac{3}{4}$ percent (adjusted for seasonal and calendar variations) from the previous quarter. While the recovery thus keeps lagging behind that in other countries, as has been the case since 1994, it nevertheless appears to rest on a solid base. Owing to strong exports, volume economic growth should rise to a rate of 2.7 percent. In 2001, the carried-forward tax reform will provide additional stimulus, while interest and exchange rate developments as well as the expected slackening of demand in the USA should have some moderating effect.

MARKED RISE IN INTEREST RATES

In mid-March, the European Central Bank raised its key money market rate to $3\frac{1}{2}$ percent. Thereby, short-term interest rates have moved up by a full percentage point since last summer. Short-term real rates, though, have hardly edged up. The rate of inflation in the Euro-area rose to 2 percent in January and February (average 1999

+1.1 percent). While this acceleration has so far been due mainly to the hike in oil prices, a spill-over to the prices of manufactures cannot be ruled out, as firms may take the opportunity of growing demand for raising their profit margins. Underlying the projections is the assumption that, given a still not worrying inflation outlook, interest rates will be raised only slightly between now and the end of 2001. Long-term interest rates have also moved up considerably over the last 15 months. This mirrors developments in both European short-term and U.S. long-term rates.

The Euro has been quoted below parity to a strong dollar in recent weeks. Little will change in this regard in the short run, given the continuing buoyancy of the U.S. economy and the positive differential in real interest rates vis-à-vis Europe. The external weakness of the Euro gave non-negligible support to the recovery of exports and investment in Europe; on the other hand, it has added to the oil-price induced rebound in import prices. Over the longer term, the considerable imbalances in the USA, notably the high current account deficit, should make for a weaker dollar.

EXPORTS BENEFITING FROM RECOVERY IN EUROPE AND HEALTHY COMPETITIVENESS

The strong revival of demand in key trading partner countries is boosting Austrian exports, along with a sustained improvement in cost-competitiveness. Merchandise exports (+8 percent in volume), manufacturing output (+5 percent) and investment in machinery and equipment (+7 percent) are all strongly upward bound.

In parallel with the cyclical recovery in major trading partner countries in Western Europe, exports have gained momentum also in Austria. According to preliminary figures from the statistical office, exports rose by a nominal 10 percent above the year-earlier level in the fourth quarter 1999. Important gains have been reported in particular by manufacturers of investment goods and of chemicals. Price competitiveness of Austrian exporters continues to prove very good. The unit labour cost position vis-à-vis the trading partners has improved by $5\frac{1}{2}$ percent on aggregate since 1995; a further gain by 3 percent is expected for 2000, due to modest wage increases and strong advances in hourly productivity. Moreover, firms are benefiting from sizeable cuts in electricity and telecommunication costs.

Table 3: Earnings and international competitiveness

	1997	1998	1999	2000	2001
	Percentage changes from previous year				
Gross earnings per employee	+0.7	+2.8	+2.0	+1.5	+2.3
Gross real earnings per employee	-1.1	+2.1	+1.3	-0.1	+0.9
Net real earnings per employee	-3.6	+1.6	+1.2	+0.7	+0.4
Net wages and salaries	-0.7	+3.3	+3.8	+4.0	+3.0
Unit labour costs					
Total economy	+0.3	+1.3	+1.7	-0.2	+0.7
Manufacturing	-4.0	-0.7	-0.2	-2.4	-1.5
Relative unit labour costs ¹					
Vis-à-vis trading partners	-3.5	+0.5	-1.5	-3.0	-1.0
Vis-à-vis Germany	+1.3	+1.5	-0.2	-1.5	-1.8
Effective exchange rate – manufactures					
Nominal	-1.8	+0.6	-0.8	-0.9	+0.8
Real	-2.7	-0.0	-1.4	-0.9	+0.4

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

For the current year, export market growth is projected at just below 7 percent. At the same time, Austrian exporters should be able to gain further market shares due to the favourable trend in production costs. Merchandise export volumes may thus rise by 8 percent. In 2001, the pace of export growth is unlikely to slow significantly (+7½ percent).

Higher exports are pulling manufacturing output strongly upwards. Latest results from the quarterly WIFO business survey confirm strong optimism of firms as regards their order situation, the outlook for production, and sales prices over the months to come. Value added in manufacturing may increase by 5 percent in 2000. Under the auspices of excellent sales expectations, a satisfactory profit situation, but at the same time severe competitive pressure, domestic industrial enterprises will be encouraged to timely renewal of their productive capital stock: investment in machinery and equipment is set to expand by 7 percent.

CURRENT ACCOUNT MARKED BY DEFICITS IN THE INCOMES AND TRANSFER BALANCES

Despite booming exports, the trade balance is set to slightly weaken this year. The deficit is expected to rise to about ATS 75 billion. Strong demand for consumer and investment goods is boosting imports the same way as are lively exports, which require primary and intermediary inputs from abroad. Moreover, the terms of trade are deteriorating this year as a consequence of higher prices for commodities, notably oil. In the coming year, when import prices are set to rise more slowly, the trade deficit could diminish somewhat.

The rise in the net surplus on cross-border tourism services will likely remain below what had been expected last De-

Table 4: Productivity

	1997	1998	1999	2000	2001
	Percentage changes from previous year				
<i>Total economy</i>					
Real GDP	+1.2	+2.9	+2.2	+3.1	+2.7
Employment ¹	+0.5	+0.9	+1.4	+1.1	+1.1
Productivity (GDP per employment)	+0.7	+1.9	+0.7	+2.0	+1.6
<i>Manufacturing</i>					
Production ²	+3.8	+3.4	+2.0	+5.0	+4.3
Employees	-1.4	+0.1	-0.7	+0.1	±0.0
Productivity per hour	+5.5	+3.2	+3.3	+4.9	+4.3
Working hours per day for employees	-0.1	+0.1	-0.6	±0.0	±0.0

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

ember. Austria will apparently not fully benefit from Europe-wide rising demand for travel and leisure, and will lose market shares. The political sanctions taken by EU member states against the Federal government will lead to adverse economic effects mainly in the tourism industry. In this regard, no conclusive evidence is, however, available as yet, but the amount of earnings foregone will largely depend on how long reservations vis-à-vis Austria as a tourism destination and a host country of international meetings and congresses will be maintained. For the current year, the WIFO projections include rather cautious assumptions on the negative effects which should manifest themselves mainly in foreign visits to the large cities and in congress tourism. Spending by Austrian travellers abroad is expected to fall again slightly on a price-adjusted annual basis. In all, the surplus on tourism services is projected at around ATS 26 billion, up by 1 billion from 1999.

Taken together, the balance of goods and services transactions is close to zero. The deficit in the current account, estimated at around ATS 62 billion or 2.2 percent of GDP for 2000, has its origins in the income and transfer balances: interest and dividend income of foreign investors and earnings from foreign direct investment show up on the negative side of the current account (even if they are not repatriated but re-invested in Austria). The negative balance on cross-border transfers mainly reflects Austria's net contributions to the EU budget.

STRONG GROWTH OF CONSUMPTION, LIVELY RETAIL SALES

Net household incomes from employment and social benefits are posting substantial gains this year, rising by an inflation-adjusted 2½ percent from 1999. While gross real per-capita wages and salaries remain flat, cuts in direct taxes offer some leeway for higher consumption or saving – particularly for the income brackets from ATS 12,000 to 20,000 per month before tax, whose tax burden is being lowered by up to 2 percent. In addition, social transfer

Table 5: Private consumption and earnings

	1997	1998	1999	2000	2001
	Percentage changes from previous year, volume				
Private consumption expenditure	+0.1	+1.5	+2.4	+2.7	+2.3
Durables	-3.5	+1.9	+6.5	+4.5	+2.6
Non-durables and services	+0.7	+1.5	+1.9	+2.4	+2.3
Net wages and salaries	-2.4	+2.6	+3.1	+2.4	+1.6

payments are being raised to a significant extent, i.a., through the "family benefit package", which also benefits low-income groups more than on average. These adjustments to the tax and transfer system, which have taken effect as from 1 January 2000 are also deemed to give over-proportional benefit to people whose propensity to consume is relatively high.

The gains in disposable income are stimulating consumer demand, which is projected to gain 2.7 percent in volume in 2000, the strongest increase in four years. Expenditure on durable consumer goods should continue rising faster than the overall trend. In 2001, the tax-induced stimulus will wear off and fiscal consolidation measures of a more "structural" nature will become effective, thereby constraining the rise in disposable income. On the other hand, some acceleration in gross wage rises and continued robust employment gains may work in the opposite, more expansionary, direction. Net disposable income from employment and transfers may thus grow by 1½ percent in real terms, allowing private consumption to rise by 2¼ percent.

Unlike in Germany, sales turnover in Austria has been rising strongly for some years. This year, value added may gain 3¼ percent, the same rate as recorded in 1999. Retailers are benefiting from lively private consumption, wholesale trade rather from booming exports. The strong momentum is not expected to abate significantly next year.

SUBDUED EXPANSION OF CONSTRUCTION ACTIVITY

Construction firms are negatively effected by the continued decline in residential building. Demand for new homes is slack to such extent that there is a large overhang in public financial resources set aside for that purpose. While construction of new dwellings is set to decline further in the years to come, renovation of existing structures is meeting strong demand even after special tax concessions have been phased out. In Vienna, a programme for improving the insulation of social and communal dwellings is making good progress. Demand for new office space is expected to stay lively over the projection period. High corporate earnings and a favourable invest-

ment climate should also stimulate demand for new industrial structures.

Civil engineering companies have generally expressed confidence in responding to the latest WIFO business and investment surveys. Investment in highway and railroad infrastructure should in 2000 maintain the level of last year. As from 2001, public investment outlays may be trimmed for budgetary reasons. Road construction may already be affected this year, other projects risk being delayed. The rise in the highway toll as from 1 January 2001 and the envisaged introduction of road pricing for trucks may over the medium term provide additional resources for maintenance and improvement of the road infrastructure.

Overall construction output is unlikely to expand by more than 1 percent in volume in 2000, with no acceleration being in sight thereafter.

INFLATION ACCELERATING DESPITE PRONOUNCED WAGE MODERATION

Inflation is gaining some momentum. Higher taxes and public charges will add about 0.3 percentage point to the annual inflation rate, both this year and next.

The price projections of last December require substantial correction. First, the hike in oil prices lasted longer than expected, and thereby also the increase in energy costs for the consumer. This adds almost ¼ percentage point to this year's rate of inflation. However, at its last meeting OPEC agreed on an increase in production by around 8 percent, which has already led to a turnaround in spot market prices. In spite of rising demand in the industrialised countries, crude oil prices should come down further over the rest of the year. Underlying the present projections is an average level of 24 \$ per barrel, subsiding to 21 \$ in 2001.

Second, the Federal government envisages, as from mid-year, a notable increase in excises for tobacco, for electricity consumption, in the insurance tax for motor cars, as well as in some other public charges. The aggregate impact on the consumer price index is calculated at +0.6 percentage point as from June, and +0.3 percentage point for the average of 2000. Consumer price inflation will thereby rise to a rate of 1.6 percent.

Wage increases are exerting a marked dampening effect on inflation this year. On the basis of agreements reached in last autumn's wage round, and because of a steady increase in part-time employment, per-capita wages are expected to rise by only 1.5 percent, thus clearly lagging be-

hind overall productivity advances and even slightly behind the rate of inflation. Unit labour costs for the whole economy are seen edging down 0.2 percent. The wage share in national income remains on its downward trend. Given the favourable business cycle prospects, per-capita wages may pick up in 2001 (+2¼ percent), and unit labour costs rise by 0.7 percent. In such a scenario, wage cost developments would once again avoid adding to inflationary pressure.

In 2001, energy prices should contribute to disinflation, as oil prices are set to decline and the ongoing liberalisation of electricity and gas networks will have price-dampening effects. Prices of manufactures, on the other hand, will continue trending upwards, given lively demand and a high degree of utilisation of production capacities. Higher taxes and public charges will again add 0.3 percentage points to the rate of inflation. Assuming no further hikes in administered prices than those decided upon so far, consumer prices are projected to go up by 1.4 percent on annual average.

CRITICAL FRAMEWORK CONDITIONS FOR FISCAL CONSOLIDATION

The impact of the “family benefit package” and the tax reform, as well as the delayed drafting of the annual Federal budget complicate the task of fiscal policy in the current year. For 2001 it is intended to change a great number of one-off measures for a more sustained and coherent consolidation strategy. However, little relief may be expected for the financial situation of the Federal states, the municipalities, public funds and the social security bodies. The general government deficit may represent 2 percent of GDP in both years of the projection period.

The Federal budget draft for 2000 has been submitted to Parliament short time ago. The auspices are for fiscal policy to resume the consolidation strategy which between 1995 and 1997 allowed the general government deficit to fall from 5.1 to 1.9 percent of GDP, but was abandoned thereafter, notably in 1999 and 2000, with tax cuts for households and companies and increases in family benefits. Due to the long time that elapsed between the last Parliamentary elections and the formation of a new government, little room for manoeuvre was left for lasting consolidation measures. The government attempts to contain net borrowing at the Federal level at a ratio of

Table 6: Key policy indicators

	1997	1998	1999	2000	2001
<i>Fiscal policy</i>					
Central government net balance	billion ATS -66.7	-77.2	-64.9	-62.0	-58.5
as a percentage of GDP	- 2.6	- 3.0	- 2.4	- 2.2	- 2.0
General government financial balance	as a percentage of GDP - 1.9	- 2.5	- 2.0	- 2.0	- 2.0
General government primary balance	as a percentage of GDP + 2.0	+ 1.5	+ 1.9	+ 2.0	+ 2.4
In percent					
<i>Monetary policy</i>					
3-month interest rate	3.5	3.6	3.0	4.0	4.3
Long-term interest rate ¹	5.7	4.7	4.7	5.8	5.6
Percentage changes from previous year					
<i>Effective exchange rate</i>					
Nominal	- 2.3	+ 0.6	- 0.7	- 0.9	+ 1.2
Real	- 3.4	- 0.2	- 1.5	- 1.2	+ 0.8

¹ 10-year central government bonds (benchmark).

2.2 percent of GDP in 2000 primarily by resorting to cuts in non-committed outlays, to one-time revenues, asset sales, liquidation of reserves and re-allocation of surpluses in public funds. In addition, several indirect taxes will be raised markedly as from mid-year, yielding budget-effective revenues of ATS 6.8 billion.

While the Federal budget target ratio appears possible to meet, the assumption of an aggregate financial surplus of 0.5 percent of GDP for the Federal states (“Länder”), the local communities and the social security system would seem optimistic. Thus, the budget drafts for the “Länder” suggest a substantial fall in expected surpluses, mainly due to revenue shortfalls resulting from the tax reform 2000. Such shortfalls would have to be offset in the process of budget implementation. Moreover, a quick solution would have to be found to compensate for the abolition of the beverages tax, and to cover the prospective deficit in the health insurance system. At the present state of information, WIFO regards a figure of 2 percent of GDP for general government net borrowing requirement as a realistic assumption.

In 2000, the “family benefit package” and the tax reform will boost household net disposable income by ATS 20 billion or more. Lower income brackets will benefit more than proportionally. Opposite, i.e., demand restraining effects will be exerted by cuts in public investment and indirect tax increases in the amount of some ATS 15 billion. Increases in taxes and public charges constitute a relatively heavier burden for the recipients of low incomes. In all, budgetary policy will still have an expansionary effect in 2000.

In 2001, according to the Stability Programme, the Federal government is to reduce its net borrowing to 2 percent of GDP. This will require moving from one-off meas-

ures which characterise the budget draft for 2000, to a more sustained consolidation strategy. The government is considering action in the areas of Federal subsidies to the pension system and of civil service payroll. The “package” of tax increases and higher public charges will take full effect in 2001 and should yield ATS 6 billion in additional revenue. In total, the tax increases will raise public revenues by ATS 13 billion, with further measures still being prepared. The consolidation measures so far decided for 2001 will dampen disposable income and thereby aggregate demand to a greater extent than those taking effect in the current year.

The financial situation of the Federal states and the municipalities – which are negatively affected by the tax cuts as from 1 January 2000, but hardly benefit from the tax increases as from the middle of this year – will not improve significantly in 2001. However, negotiations for a new burden sharing agreement between the territorial authorities offer an opportunity for reform of the allocation of responsibilities and financial resources between the different government levels. Projections for the health insurance system point to a widening financing gap. Moreover, in an effort by the Federal government to cut non-wage labour costs, the employers’ contributions to work accident insurance and to the fund protecting employees’ earnings against the risk of their company becoming insolvent are to be reduced by together 0.6 percentage point, amounting to a total ATS 5 billion, as from 1 January 2001. This will weaken the “Maastricht”-defined public sector balance by nearly 0.2 percent of GDP. Under these conditions, and unless further measures were taken to restrain expenditure or raise revenue for any of the public sector authorities (federation, states, local communities, funds or social security institutions), general government net borrowing would likely remain at an unchanged ratio of 2 percent of GDP in 2001. This would be clearly in excess of the 1.5 percent target foreseen in the Stability Programme. The primary budget balance (i.e., current revenues minus current expenditure excluding interest payments) would yield a surplus of 2½ percent of GDP.

CYCLICAL STRENGTH ALLOWS FURTHER DECLINE IN UNEMPLOYMENT

The labour market situation is improving, as measured by both employment and jobless figures. In 2000, the number of dependent workers and employees (excluding people in military service or on parental leave) is expected to rise by about 34,000 (+1.1 percent) above the year-earlier level, that of people out of work to fall by 10,000. In 2001, assuming lively activity will allow employment to rise by 1.2 percent and sufficient resources will be made

Table 7: Labour market

	1997	1998	1999	2000	2001	
	Changes from previous year, in 1,000					
<i>Demand for labour</i>						
Civilian employment	+ 8.8	+22.1	+32.2	+35.0	+36.8	
Dependent employment ¹	+ 8.3	+21.1	+31.2	+33.1	+34.8	
Excluding parental leave and military service	+12.8	+29.8	+37.2	+34.5	+36.0	
Percentage changes from previous year	+ 0.4	+ 1.0	+ 1.2	+ 1.1	+ 1.2	
Parental leave and military service ¹	- 4.4	- 8.7	- 6.0	- 1.4	- 1.2	
Foreign workers	- 1.6	- 0.2	+ 7.8	+ 9.0	+10.0	
Self-employed ²	+ 0.5	+ 1.0	+ 1.0	+ 1.9	+ 2.0	
<i>Labour supply</i>						
Total labour force	+11.7	+26.5	+16.2	+25.0	+25.1	
Foreign	- 1.7	+ 0.7	+ 6.6	+ 7.0	+ 9.0	
Migration of nationals	+ 5.4	+ 3.9	+ 3.0	+ 2.0	+ 1.0	
Indigenous	+ 8.0	+21.9	+ 6.6	+16.0	+15.1	
<i>Surplus of labour</i>						
Registered unemployed ³	+ 2.8	+ 4.4	-16.1	-10.0	-11.7	
	in 1,000	233.3	237.8	221.7	211.7	200.0
<i>Unemployment rate</i>						
According to Eurostat (percent of total labour force)	4.4	4.7	4.4	4.2	4.1	
According to AMS (percent of total labour force)	6.4	6.5	6.0	5.7	5.3	
According to AMS (percent of dependent labour force)	7.1	7.2	6.7	6.3	5.9	
Participation rate ⁴	67.2	67.6	67.7	67.9	68.2	
Employment rate ⁵	62.9	63.2	63.6	64.1	64.6	

¹ According to Association of Austrian Social Security Bodies. – ² According to WIFO. – ³ According to Labour Market Service. – ⁴ Total labour force as a percentage of active population (aged 15 to 64). – ⁵ Employment as a percentage of active population (aged 15 to 64).

available for “active” labour market measures, unemployment may for the first time since 1992 remain below an annual average of 200,000.

The labour market is benefiting from the favourable trend in business activity. Employment is set to post solid gains, now also extending to full-time jobs. Unemployment should stay on a clear downward trend, although the amount of resources available for “active” labour market policy is still uncertain.

While over the last years rising employment was largely confined to part-time workers, an increase also in the number of full-time jobs is expected for 2000: given strong exports and industrial activity, demand for workers and employees in manufacturing has stopped declining. Some key areas in technical manufacturing, such as machine tool and vehicle production, are adding to personnel. At the same time, employment in services remains strongly upward bound, the bulk of the new jobs once again being part-time. When marginal employment (people working very short hours) is included (as does the EU Labour Force Survey, but not the Austrian data collected by the social security agency), the rate of employment growth in Austria is as high as 1.4 percent. Counting this category also for the calculation of the employment ratio,

one arrives at a figure of 70 percent for Austria, which corresponds to the EU medium-term target.

The trend in the number of unemployed depends not only on growth of output and demand for labour, but importantly also on institutional factors. Among the latter, the role of “active” labour market policy measures is crucial. In 1999, almost half of the reduction in unemployment was owed to a reinforcement of training and qualification programmes. How much money will be available for “active” labour market policy in 2000 and 2001, is as yet unclear. It is widely expected that any budgetary cuts will lead

to a lower intensity of measures rather than to a reduction in the number of people enrolled. On the other hand, the raising of the age limit for early retirement will imply an increase in labour supply.

Should the number of unemployed enrolled in active labour market policy not be raised, it will be difficult to meet the target fixed by the EU Employment Guidelines, i.e., an enrolment ratio in training activities of at least one-fifth of the total number of job-seekers.

Cut-off date: 5 April 2000.

49th Euroconstruct Conference: Trends in the European Construction Industry

Vienna , 8th and 9th June 2000

8th June 2000: Changes and Challenges in Housing Policy

- Housing Policy – Expected Changes and Trends
- Reforms in Germany – From Non-profit Organisations to Social Market Strategies
- Consequences of Changes in Housing Policy in the Netherlands
- Changes in Housing Policy in the EU – Suggestions for Austria
- Panel Discussion: The Future of Construction and Housing Construction Financing – Alternative Financial Instruments in the Housing Sector

9th June 2000: European Construction Outlook: 2000-2002

- European Macroeconomic Outlook
- Housing in Europe
- Non-residential Building
- Civil Engineering
- The Construction Sector in Eastern Europe
- European Construction Outlook – Summary
- The Construction Industry in Japan/Asia

Conference Venue

Wirtschaftskammer Österreich – Austrian Economic Chamber • Julius-Raab-Saal • Wiedner Hauptstrasse 63 • 1040 Vienna – Austria

Conference Organisation

WIFO – Austrian Institute of Economic Research
Dr. Margarete Czerny
P.O. Box 91, A-1103 Vienna – Austria

For further information please contact Andrea Luger or Vera Plass • Telephone (+43 1) 798 26 01, ext. 207 or 215 • Fax (+43 1) 798 93 86 • e-mail: Andrea.Luger-Hoefling@wifo.ac.at, Vera.Plass@wifo.ac.at • <http://www.wifo.ac.at>, <http://www.euroconstruct.com>