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Global Economic Boom Gradually Spreading to the Euro Area and to Austria

Economic Outlook for 2004 and 2005

Growth of GDP is set to attain 1.7 percent this year. Notably demand from Germany has picked up significantly over the last few months. Assuming that the moderate recovery in the euro area will continue, growth may accelerate to 2.5 percent next year, providing incentives also for private consumption. Employment will be stimulated by stronger growth. Despite the cyclical recovery, special factors will nevertheless prevent unemployment from falling and drive the government deficit upwards.

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In the first quarter 2004, GDP growth in the euro area (+2 percent in volume year-on-year) and notably in Germany (+1.5 percent) was stronger than expected by most analysts. In Austria, the expansion remained rather modest, at +0.7 percent. Many indicators suggest that the positive trend in the world economy, supported by the boom in China and the upswing in North America, will gradually strengthen the forces of growth also in Europe. The more than three-year-long economic stagnation in the euro area may now have given way to a tentative business cycle recovery. The German export industry will benefit particularly from its close ties with the world economy.

According to the business surveys for Germany, Austria and the euro area at large, manufacturing firms see current business conditions distinctly more positive than one year ago, even if they do not expect a speedy recovery as it was typical for previous cycles. The high euro exchange rate, the price hikes for internationally traded commodities, and particularly the persistent weakness of consumer demand in the euro area hold risks for the further strengthening of business activity.

Due to its close supply relations, Austrian manufacturing industry benefited mainly from the swift revival of German exports. In spring, merchandise exports have probably picked up strongly. For the whole year, volume export growth is expected at 5½ percent, even if the effective appreciation of the euro and a stronger competitive climate in the new EU member states may lead to some losses in foreign market shares. Over the medium term, price competitiveness of Austrian manufacturing industry has significantly improved, as unit labour costs relative to those of the main trading partners have declined by 6 percent since 1999. Manufacturing value added is set to gain 2.8 percent in volume in 2004, clearly more than on average over the last three years. The upward trend in sales expectations and capacity utilisation will also give incentives to investment this year. It has to be noted, however, that for tax reasons investment spending, notably for business vehicles, has been carried forward to an important extent into 2003.

The rise in energy prices has led to substantial terms-of-trade losses, keeping the current account deficit at around € 2 billion. It is also being passed on to the consumer level, where it will boost headline inflation by ¼ percentage point on average in 2004 and 2005 to rates of close to 2 percent, respectively. Growth of real disposable income will thereby be dampened, to a projected rate of 1¼ percent in 2004. For the fourth year in a row, real net income per employee will hardly increase this year. The higher energy costs, while slightly dampening private consumption, will be accommodated mainly by a lower household saving ratio. Only in 2005 will per-capita incomes gain substantially, due to the cuts in direct taxes. This will allow private household spending to revert, for the first time in four years, towards its long-term trend growth of 2½ percent in volume. The household saving ratio is expected to move up to almost 9 percent of disposable income.

Construction, a driver of growth already in 2003, is projected to expand by a further healthy 2½ percent in volume this year. Orders remain on a high level in civil engineering, while demand is set to slacken in the building sector. Rising excess capacity will hold back the creation of new office space, and sluggish demand for housing has led to a fall in building permits for subsidised dwellings by 4,000 or 10 percent in 2003.

Main results

		2000	2001	2002	2003	2004	2005
		Percentage changes from previous year					
GDP							
Volume		+ 3.4	+ 0.8	+ 1.4	+ 0.7	+ 1.7	+ 2.5
Value		+ 4.9	+ 2.8	+ 2.7	+ 2.7	+ 3.1	+ 4.2
Manufacturing[1], volume		+ 6.4	+ 1.5	+ 0.5	– 0.2	+ 2.8	+ 4.0
Whole sale and retail trade, volume		+ 3.7	– 0.0	+ 1.2	+ 1.3	+ 1.4	+ 2.5
Private consumption expenditure, volume		+ 3.3	+ 1.4	+ 0.8	+ 1.2	+ 1.6	+ 2.5
Gross fixed investment, volume		+ 6.2	– 2.3	– 2.8	+ 4.6	+ 3.2	+ 3.7
Machinery and equipment[2]		+ 11.8	– 2.1	– 5.2	+ 6.2	+ 4.0	+ 6.0
Construction		+ 1.9	– 2.5	– 0.7	+ 3.3	+ 2.5	+ 1.7
Exports of goods[3]							
Volume		+ 13.1	+ 7.5	+ 5.2	+ 2.7	+ 5.5	+ 6.8
Value		+ 15.6	+ 6.5	+ 4.2	+ 1.9	+ 6.4	+ 7.3
Imports of goods[3]							
Volume		+ 10.9	+ 5.7	+ 0.8	+ 6.2	+ 3.8	+ 7.1
Value		+ 14.7	+ 5.0	– 2.0	+ 5.0	+ 6.0	+ 7.8
Current balance	billion €	– 5.36	– 4.13	+ 0.36	– 2.04	– 1.80	– 2.02
As a percentage of GDP	%	– 2.6	– 1.9	+ 0.2	– 0.9	– 0.8	– 0.8
Long-term interest rate[4]	%	5.6	5.1	5.0	4.2	4.3	4.5
Consumer prices		+ 2.3	+ 2.7	+ 1.8	+ 1.3	+ 1.9	+ 1.8
Unemployment rate							
Percent of total labour force[5]	%	3.7	3.6	4.3	4.4	4.5	4.4
Percent of dependent labour force[6]	%	5.8	6.1	6.9	7.0	7.1	7.0
Dependent employment[7]		+ 0.9	+ 0.4	– 0.5	+ 0.2	+ 0.6	+ 0.9
General government financial balance according to Maastricht definition							
As a percentage of GDP	%	– 1.5	+ 0.2	– 0.2	– 1.3	– 1.2	– 1.7

[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 Labour Force Survey. – [6] According to Labour Market Service, percent of total labour force excluding self employed. – [7] Excluding parental leave, military service, and unemployed persons in training.

Employment is reacting in the usual way to the recovery of business activity. The number of people in active employment is seen rising by 0.6 percent this year and 0.9 percent in 2005. The increase may now extend also to domestic employees, the number of which has gone down by 30,000 over the last two years. The inflow of foreign labour remains strong. As a consequence of the sizeable increase in labour supply, unemployment will show little reaction to the friendlier business situation, remaining at around 240,000 on annual average 2005.

Likewise, the public sector financial balance will hardly improve, despite the cyclical recovery. The general government deficit in the Maastricht definition is projected at € 3 billion or 1¼ percent of GDP this year, rising to € 4 billion or 1¾ percent of GDP in 2005. The prolongation of tax concessions for investors and rising outlays for social transfers, such as child care and partial retirement benefits, are exerting a drag on the 2004 budget, while in 2005 the sizeable cuts in direct taxes will lead to shortfalls in revenues.