

Markus Marterbauer

## Economic Recovery Slow in Coming Under Way

**Further developments of the world economy are subject to high risks, in the face of volatile stock markets and a possible war against Iraq. Present cyclical conditions are characterised by a persistent weakness of internal demand, both in Europe at large and in Austria. Opinion surveys among domestic manufacturers do not point to an imminent upturn of activity. The propensity to invest is low, given the under-utilisation of productive capacities and the world-wide uncertainties. Retail sales are flat, whereas construction output is tentatively heading up from its low level. In such circumstances, no improvement on the labour market may as yet be expected.**

All staff members of the Austrian Institute of Economic Research contribute to the Business Cycle Report. • Cut-off date: 5 February 2003 • E-Mail Address: [Markus.Marterbauer@wifo.ac.at](mailto:Markus.Marterbauer@wifo.ac.at)

Current business cycle indicators still do not suggest an upturn of economic activity. Indeed, the results from the WIFO business survey for the first quarter 2003 rather point to a renewed weakening of the business climate, reflecting the considerable uncertainty about global political and economic developments. For the next few months, firms expect but moderate output gains, the seasonally-adjusted balance of optimistic and pessimistic responses having declined from +7.7 to +4.8 percentage points. Scepticism has grown particularly among producers of investment goods.

The picture is confirmed by judgements on capacity utilisation: while edging up to 80.3 percent in the first quarter, it still remains well below its long-term average. This and the general uncertainty about the short-term economic prospects may induce firms to further postpone their investment plans. The WIFO investment survey of November 2002 points to an increase in industrial investment that is, however, entirely due to a few large-scale projects in the automotive industry.

More favourable is the trend of exports. The data, although reaching only as far as October 2002, show that the demand weakness of last summer has been overcome. In September and October, merchandise exports rose by 6½ percent from the year-earlier level. Intra-EU demand has recovered, and deliveries to South-Eastern Europe and South-East Asia picked up strongly.

Exports are also the only major source of growth in the EU and in Germany. Still, the marked appreciation of the euro exchange rate may soon dampen demand from North America and South-East Asia. GDP growth in the euro area is likely to have ground to a halt in the fourth quarter 2002 and the following period, marking another pause in the cyclical recovery. The major cause is the persistent weakness of internal demand. Private investment and public spending are being restrained, and private consumption is growing only slightly, with consumer confidence having fallen sharply between September and January.

Conversely, activity in the USA is mainly driven by domestic demand, while exports are receding. Although growth of private household spending, particularly for durable consumer goods, has decelerated in the fourth quarter 2002, business equipment investment and private construction outlays and, first and foremost, public (military) expenditure have posted strong gains. The USA thus remain the major driving force of the world economy, but the risks remain high: fears about a possible war in Iraq may prompt consumers and investors to restrain spending. Monetary and fiscal policy, on the other hand, are trying to stimulate demand and output.

In Austria, the cyclical low is characterised mainly by weak domestic demand. Retail sales, though up from last year by  $\frac{3}{4}$  percent in volume between January and November, remained flat on a seasonally adjusted basis in the second semester 2002. For the suppliers of durable consumer goods, a slight improvement has become apparent, as witnessed by higher motor car sales in September and October as well as an increase in new car registrations in the fourth quarter.

Output in the construction industry should have passed its trough. Judgements by firms on production and order levels, as expressed in the WIFO business survey, are heading up somewhat. This is confirmed by a slightly better assessment of the business climate among suppliers of construction material. In civil engineering, demand is picking up, while for residential construction it is no longer receding. Firms envisage no further personnel cuts, as the number of employed construction workers fell to 213,000 in December 2002, the lowest level since the mid-1980s.

The persistent decline of imports is also reflecting the weakness of domestic demand. The latter, along with growing tourism, is the main reason for the current account deficit having closed.

Sluggish activity is leaving its marks also on the labour market. In January, the number of actively employed remained at the low level of one year ago. 6,000 more people were unemployed than in early 2002.