

EWALD WALTERSKIRCHEN

TEMPORARY SLOWDOWN IN ECONOMIC GROWTH

ECONOMIC OUTLOOK FOR 2001 AND 2002

The slackening of the business cycle in the USA and the consequences of the rise in oil prices are set to dampen economic growth in the months to come. Following the strong cyclical upturn in 2000 (+3.3 percent), demand and output in Austria are expected to expand by a more moderate 2.6 percent in 2001, before re-gaining momentum in 2002. The somewhat slower pace of activity will still allow unemployment to decline further. Inflation is also likely to abate markedly, if the most recent moves to a downward trend in both oil prices and the dollar exchange rate are confirmed.

All staff members of the Austrian Institute of Economic Research contribute to the Economic Outlook. E-mail address: Ewald.Walterskirchen@wifo.ac.at • Cut-off date: 19 December, 2000

The strong upturn in the Austrian business cycle is being held back after only one year by the effects of higher oil prices and a weakening of demand and output in the USA. Domestic activity attained a peak last summer, but has clearly lost strength since. Gross Domestic Product (GDP) in the third quarter 2000 grew by just over 2 percent year-on-year, following a rate of 4 percent growth in the first six months. The income transfer towards oil producing countries has taken its toll on private consumption as well as on business investment.

Activity in the USA is increasingly reacting to higher energy costs and to monetary restriction. The "landing" of the economy after the extended boom could be less "soft" than expected so far. A slowdown in economic growth in 2001 should also be expected in Europe, where the recovery started only in 1999-2000. Oil prices, though expected to soften, may still exceed their 1999 level by some 50 percent.

Owing to the less favourable international environment, economic growth in Austria is projected to decelerate from 3.3 percent (2000) to 2.6 percent in 2001. The expected weakening of export and investment demand may slow manufacturing output growth from 6½ to 4½ percent.

By 2002, the slowdown in the international business cycle should be overcome as a result of a more expansionary stance of monetary and fiscal policy in the USA. In the EU, and in Austria, growth should pick up again somewhat.

Economic developments are also reflected in public finances. Thus, cyclical strength in 2000 contributed significantly towards the lowering of the government deficit. Expenditure restraint is obviously more effective when revenues from taxes and social contributions grow comfortably, the number of unemployed falls and the social insurance funds swing to financial surplus.

For 2000, the general government deficit is estimated at a ratio of 1.4 percent of GDP; abstracting from the one-off effect of the sale of UMTS licenses, the deficit ratio is 1.8 percent. Thus, despite major tax cuts and raises in family benefits taking effect, the deficit has been kept lower than in 1999 (2.1 percent), largely due to increases in consumption taxes and other public charges.

In 2001, a number of fiscal consolidation measures taken should cut the deficit in half. In particular, increases in a number of taxes and the shifting "off budget" of some responsibilities of the state governments should make for a reduction in the general government deficit to 0.8 percent of GDP. The downward revision of GDP growth may be of little impact for the budgetary outturn, as crucial component variables, such as compensation of employees as the major tax base, or the number of registered unemployed, remain virtually unchanged.

Table 1: Main results

		1997	1998	1999	2000	2001	2002
		Percentage changes from previous year					
GDP							
Volume		+ 1.3	+ 3.3	+ 2.8	+ 3.3	+ 2.6	+ 2.8
Value		+ 2.6	+ 4.0	+ 3.7	+ 4.6	+ 4.1	+ 4.1
Manufacturing ¹ , volume		+ 4.2	+ 4.4	+ 2.4	+ 6.5	+ 4.5	+ 5.0
Private consumption expenditure, volume		+ 1.4	+ 2.9	+ 2.3	+ 2.7	+ 2.0	+ 2.3
Gross fixed investment, volume		+ 1.0	+ 2.7	+ 3.2	+ 3.7	+ 2.3	+ 3.1
Machinery and equipment ²		+ 5.4	+ 5.2	+ 4.6	+ 6.0	+ 4.0	+ 5.0
Construction		- 2.0	+ 0.9	+ 2.2	+ 2.0	+ 1.0	+ 1.5
Exports of goods ³							
Volume		+ 16.5	+ 8.1	+ 7.7	+ 12.0	+ 7.0	+ 8.0
Value		+ 16.8	+ 8.4	+ 7.0	+ 15.9	+ 9.7	+ 10.7
Imports of goods ³							
Volume		+ 9.4	+ 7.1	+ 6.9	+ 7.0	+ 6.0	+ 7.0
Value		+ 10.9	+ 6.6	+ 6.7	+ 13.4	+ 8.1	+ 9.7
Current balance	billion ATS	- 79.2	- 64.5	- 75.1	- 84.7	- 69.7	- 60.8
	billion EUR			- 5.5	- 6.2	- 5.1	- 4.4
	as a percentage of GDP	- 3.2	- 2.5	- 2.8	- 3.0	- 2.4	- 2.0
Long-term interest rate ⁴	in percent	5.7	4.7	4.7	5.6	5.3	5.2
Consumer prices		+ 1.3	+ 0.9	+ 0.6	+ 2.4	+ 1.5	+ 1.3
Unemployment rate	percent of total labour force ⁵	4.4	4.5	3.8	3.3	3.2	3.2
	percent of dependent labour force ⁶	7.1	7.2	6.7	5.9	5.3	5.2
Dependent employment ⁷		+ 0.4	+ 1.0	+ 1.2	+ 1.0	+ 0.8	+ 0.9
General government financial balance	as a percentage of GDP	- 1.7	- 2.3	- 2.1	- 1.4	- 0.8	± 0.0

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.

In 2002, restrictions in government expenditure (pension reform, civil service payroll) will increasingly be felt. Thus, general government finances should for the first time be in balance, unless overall business conditions turn out substantially worse than presently expected (e.g., "hard landing" in the USA).

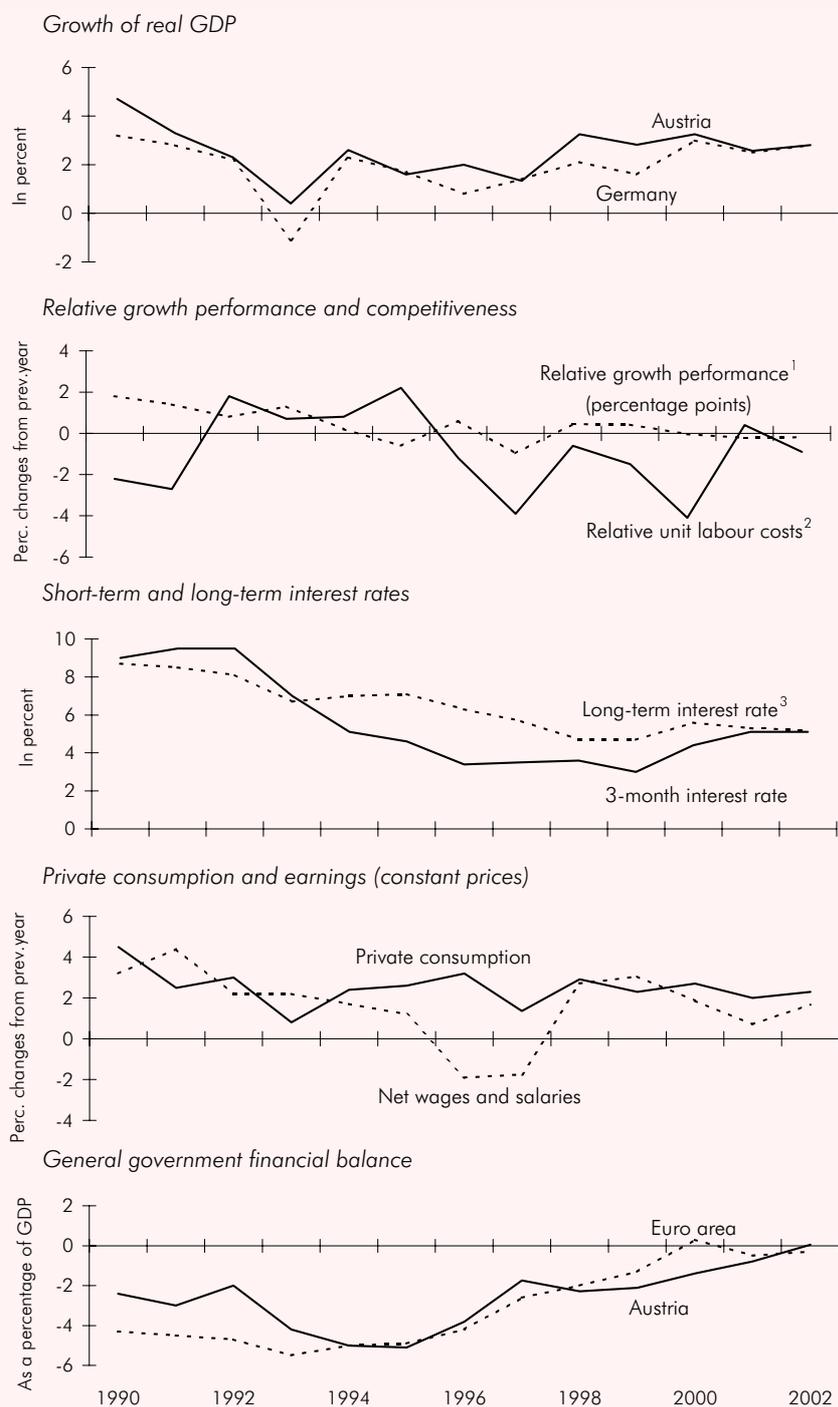
Unlike in 2000, the fiscal stance in 2001 should have a dampening impact on household net incomes. Higher taxes and public charges and weakening cyclical activity will squeeze disposable income. The but modest gain in net real income from employment and social transfers (+ $\frac{3}{4}$ percent) reduces the scope for higher consumption. Households will be able to raise their spending by the projected 2 percent (in volume) only by accepting a significant decline in the saving ratio.

Inflation has peaked in November 2000 at an annual rate of 3.1 percent. Since the inflationary impact of energy prices is going to fade and even be reversed in a year-on-year comparison, the annual average rate of inflation is set to abate to 1.5 percent in 2001 and 1.3 percent in 2002. In 2000, the oil price hike has added almost 1 percentage point to headline inflation. Conducive to a deceleration of price rises from now on should not only be a weakening of oil prices, but also an expected strengthening in the euro exchange rate. As from June 2001, the impact of higher consumption taxes on the annual inflation rate (0.5 percentage point) will disappear. Further exonerating effects are expected from cuts in electricity and telephone charges, as well as from housing rents and seasonal goods prices. However, due to high energy costs being passed onto goods and services produced downstream, core inflation (excluding food and energy items) will go up from 1.8 to 2.3 percent in 2001, before subsiding in 2002.

The slower pace of output growth will make for somewhat smaller gains in the number of jobs (projected at +24,000) in 2001. Given the new regulations concerning health insurance contributions of non-working spouses (without children), part of the people concerned may seek part-time employment (paid above the contribution threshold). Unemployment is set to recede further, if somewhat more slowly than in 2000. The jobless rate for 2001, on national definitions, is projected at 5.3 percent of the dependent labour force. More than in the past years, the jobs newly created are likely to be filled by people from the unemployment register, as the "hidden reserve" of the labour force be-

comes progressively exhausted. In addition, the ability and willingness to work of people registered as unemployed are now being scrutinised more closely, and benefits are being denied more often than before.

Figure 1: Demand and output



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).

The favourable business cycle in 2000 has made not only for a decline in unemployment, but also for lower government deficits. The general government budget balance is estimated at –1.4 percent of GDP, excluding the one-time revenues from UMTS license sales at –1.8 percent.

**Stronger efforts at
budgetary
consolidation**

Cyclical developments in 2001 will make a smaller contribution to fiscal consolidation than in the past year. In addition, the central government household will be burdened by a further ATS 7 billion subsidy for the Federal railways. However, the increase in taxes and other public charges as well as the shifting "off budget" of some responsibilities of the state government will allow the general government deficit to shrink to $\frac{3}{4}$ percent of GDP.

In 2002, the effect of spending restraints in the areas of social retirement benefits and the public sector wage bill will be increasingly felt. The reform of the pension system is expected to reduce expenditure by more than ATS 10 billion as early as 2002. Salaries of civil servants will be raised by no more than 0.8 percent, the number of civil service jobs will be cut, in part by means of outsourcing of tasks. General government finances may well be in balance in 2002, as a central government deficit of $\frac{1}{4}$ percent of GDP should be offset by an aggregate small surplus in state and local governments' and municipalities' households. This favourable budgetary perspective hinges on the assumption that general cyclical developments will not deviate importantly from present expectations (in particular the one for a "soft landing" of the U.S. economy).

The stance of fiscal restraint could dampen GDP growth in the short run, by an estimated $\frac{1}{4}$ percentage point each in 2001 and 2002¹. In the longer term, positive supply side effects may be expected from a balanced government budget, as business and consumers will anticipate tax cuts rather than further increases.

General government net borrowing in 2000 amounts to 1.4 percent of GDP. In 2001, the consolidation measures taken will cut the deficit ratio in half, and in 2002 a "zero deficit" may be attained.

Table 2: Key policy indicators

		1997	1998	1999	2000	2001	2002
<i>Fiscal policy</i>							
Central government net balance	billion ATS	- 67.7	- 77.1	- 64.8	- 60.0	- 45.0	- 23.0
	as a percentage of GDP	- 2.7	- 2.9	- 2.4	- 2.1	- 1.5	- 0.7
General government financial balance	as a percentage of GDP	- 1.7	- 2.3	- 2.1	- 1.4	- 0.8	± 0.0
General government primary balance	as a percentage of GDP	2.1	1.5	1.4	2.1	2.7	3.4
In percent							
<i>Monetary policy</i>							
3-month interest rate		3.5	3.6	3.0	4.4	5.1	5.1
Long-term interest rate ¹		5.7	4.7	4.7	5.6	5.3	5.2
Percentage changes from previous year							
<i>Effective exchange rate</i>							
Nominal		- 1.7	+ 2.8	+ 1.5	- 2.0	+ 1.8	+ 0.9
Real		- 4.6	+ 0.3	- 1.1	- 2.5	+ 0.8	± 0.0

¹ 10-year central government bonds (benchmark).

The rate of inflation in the euro area has risen markedly, from 1.2 percent in 1999 to 2.4 percent in 2000, under the impact of higher oil prices and the appreciation of the dollar. This prompted the European Central Bank (ECB) to raise interest rates; since October 1999, key rates have been increased by $2\frac{1}{4}$ percentage points. Unlike in the USA, short-term rates in the euro area are still slightly below long-term rates.

For the year to come, signs are for a decline in oil prices (from \$ 30 to \$ 26 per barrel, as assumed for the purpose of the projections) and a recovery of the euro exchange rate. Therefore, the inflation rate in the euro area may remain broadly flat or edge down, despite higher costs feeding in part into output prices.

In such a scenario, a further increase in interest rates by the ECB would not seem necessary. This is confirmed by the Bank's most recent decisions: at its meetings last November and December, the ECB Council kept the minimum rate for refinancing operations constant at 4.75 percent. The ECB motivated these decisions by arguing that the trend expansion of the money supply M3 had become flatter, and that core inflation was low². In November, headline inflation in the euro area ran at an annual rate of 2.9 percent, core inflation stood at 1.5 percent.

No further interest rate hikes

¹ See Breuss, F., "Fiskalpolitische Disziplinierung durch den Stabilitäts- und Wachstumspakt: Österreich auf dem Weg zum Nulldefizit – Eine Modellanalyse", in Neck, R., Holzmann, R., Schneider, F. (Ed.), Staats-schulden am Ende? Ursachen, Wirkungen und Zukunftsperspektiven, Manz, Vienna, 2000.

² European Central Bank, Monthly Bulletin, November 2000.

With cyclical prospects for 2001 more favourable than for the USA, the ECB may not follow early moves by the U.S. Federal Reserve to cut interest rates. However, the leveling-off of inflation leaves the ECB scope for counter-action, should business activity recede beyond expectations.

In November, the ECB intervened in foreign exchange markets in support of the euro. Since a lower euro exchange rate exerts upward pressure on import prices, the ECB is seeking to reduce this potential inflation risk. In the eyes of the ECB, any advantages the export industries may obtain from a low euro exchange rate are but a transitory phenomenon that would soon be neutralised by the implicit rise in import prices.

In December, the euro staged a significant recovery vis-à-vis the dollar. The relative performance of stock markets, real interest rates and growth, as well as the expected weakening of net capital outflows to the USA all suggest that this recovery will continue in 2001. Yet, there is no reliable "forecasting" of exchange rates.

Since last autumn, signs of a slowdown of global activity have become more frequent³. The high oil prices and the restrictive stance of monetary policy are dampening demand and output growth in the industrialised world.

The OECD has now revised upwards its estimate for the restrictive effect of the oil price hike ($-1\frac{1}{2}$ percentage point of GDP growth). While WIFO assumes that oil prices will come down to \$ 26 per barrel on annual average 2001, this would still represent a 50 percent increase over 1999.

Already in its autumn projections three months ago, WIFO was sceptical about the economic outlook for the USA. The inverted yield structure prevailing since last spring suggested an imminent weakening of activity⁴. This is now being increasingly confirmed by recent data: GDP growth in the USA fell below 3 percent in the third quarter 2000, with adverse reports becoming more frequent in the following period. The signs of cyclical fatigue are confirmed by the downward trend in share prices.

In the USA, the restrictive effects of monetary policy are being amplified by real income losses from higher oil prices. GDP growth in 2001 is thus projected to abate to 2 to $2\frac{1}{2}$ percent. Economic policy is expected to counter-act timely, by lowering interest rates, and by a more expansionary fiscal stance (tax cut). In this way, the slowdown under way since mid-2000 should be overcome quickly, and by 2002, growth should rebound to nearly 3 percent on annual average.

In the EU, consumer sentiment has clearly turned less sanguine in the wake of the steep rise in oil prices. The large shift in real income towards the oil producing countries is undermining the propensity to consume. This income loss will be overcome more easily, the sooner exports towards these countries pick up.

The experience of the 1970s shows that the restrictive effects of an oil price hike may be masked for some time by an inventory build-up for energy-intensive commodities (non-ferrous metals, steel, paper, etc.). It is only when this stock cycle has run its course that the full impact of the oil price shock and the subsequent monetary policy response become apparent. GDP growth in the euro area may therefore slow from 3.3 percent in 2000 to 2.8 percent in 2001.

In Germany, the Ifo Institute's business climate index has been heading downwards for the last five months. GDP growth of 2.8 percent in the 3rd quarter has been below expectations. Construction investment dropped significantly (-5 percent), while private consumption remained subdued. Overall economic growth is likely to slow from 3 percent annual average to $2\frac{1}{2}$ percent in 2001. The slackening of demand will be cushioned by an expansionary fiscal stance (tax cut).

First signs of slackening in the international business cycle

³ See Marterbauer, M., "Dämpfung des Wachstums der Weltwirtschaft im Jahr 2001", WIFO-Monatsberichte, 2000, 73(12).

⁴ See Walterskirchen, E., "Economic Outlook for 2000 and 2001: Higher Oil Prices and Fiscal Consolidation Dampen Economic Growth", Austrian Economic Quarterly, 2000, 5(4) ; on the impact of an inverted interest rate structure see also Estrella, A., Mishkin, F.S., "The Yield Curve as a Predictor of U.S. Recessions", Federal Reserve Bank of New York, Current Issues in Economics and Finance, 1996, 2(7).

Table 3: World economy

	1997	1998	1999	2000	2001	2002	
	Percentage changes from previous year						
<i>Real GDP</i>							
Total OECD	+ 3.1	+ 2.3	+ 2.6	+ 3.5	+ 2.3	+ 2.5	
USA	+ 4.4	+ 4.4	+ 4.2	+ 5.0	+ 2.3	+ 2.8	
Japan	+ 1.6	- 2.5	+ 0.2	+ 1.0	+ 1.5	+ 1.0	
EU	+ 2.5	+ 2.8	+ 2.4	+ 3.3	+ 2.8	+ 3.0	
Euro area	+ 2.3	+ 2.8	+ 2.4	+ 3.3	+ 2.8	+ 3.0	
Germany	+ 1.4	+ 2.1	+ 1.6	+ 3.0	+ 2.5	+ 2.8	
Central Eastern Europe ¹	+ 5.0	+ 3.5	+ 3.3	+ 4.2	+ 4.0	+ 4.3	
<i>World trade, volume</i>							
OECD exports	+ 10.0	+ 5.6	+ 5.8	+ 13.0	+ 8.0	+ 8.5	
OECD exports	+ 10.7	+ 5.6	+ 5.0	+ 13.0	+ 7.0	+ 8.0	
Intra-OECD trade	+ 11.3	+ 8.3	+ 7.5	+ 12.3	+ 6.5	+ 8.0	
<i>Market growth²</i>							
Market growth ²	+ 10.9	+ 11.7	+ 6.3	+ 12.0	+ 7.0	+ 7.5	
<i>Primary commodity prices, in USD</i>							
HWWA index, total, 1990 = 100	- 2.0	- 23.0	+ 13.0	+ 44.0	- 9.0	- 2.0	
Excluding energy	+ 1.0	- 13.0	- 8.0	+ 3.0	+ 1.0	+ 2.0	
<i>Crude oil prices</i>							
Average import price (cif) for OECD countries	USD per barrel	19.1	12.6	17.3	30.0	26.0	25.0
Exchange rate	USD per ECU or EUR	1.134	1.121	1.067	0.92	1.00	1.10

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

In 2000, Austrian exporters benefited from the pick-up in global activity and the weakness of the euro. Sales abroad gained strongly, particularly in areas outside the EU (with the exception of the OPEC countries). Data reaching until last August do not yet show a levelling-off of export buoyancy. Goods exports are expected to have gained around 12 percent in volume in 2000, notably more than in 1998 and 1999 (with some 8 percent p.a.). Demand from third countries (USA, developing countries) by far outpaced that from the EU. Thus, exports provided major stimulus to economic growth, particularly in the first half year.

The prospective slowdown of global activity will moderate the advance of Austrian exports to a projected 7 percent in volume in 2001. Besides, competitive advantages deriving from the weakness of the euro should cease to operate, although the latter effect should be felt only with a lag of more than six months. Having dropped markedly in 2000, relative unit labour costs (vis-à-vis main trading partners) in Austrian manufacturing may edge up in 2001.

Due to the rise in oil prices and the weaker euro, merchandise import prices rose by 2 to 3 percentage points more in 2000 than export prices. The terms-of-trade shift in favour of the oil producing countries amounts to some 1 percent of national income. In 2001, with oil prices expected to soften, part of the terms-of-trade loss should be reversed.

The current account has deteriorated markedly in 2000, by ATS 10 billion to an overall deficit of around ATS 85 billion. Energy imports have acted as a major drag. The expected improvement in the terms of trade should enable the high deficit to shrink in 2001.

Unlike in the previous years, the surplus on cross-border tourism services has diminished in 2000. While foreign spending of domestic residents rose broadly in line with the international trend (+5 percent in real terms), the Austrian tourism industry is losing market shares, albeit from a high level. Against the background of lively international demand for travel services, the Austrian suppliers have fared relatively poorly. Overnight stays by foreigners are on a downward trend. Still, foreign earnings have increased by an inflation-adjusted 3 percent, higher spending per customer and day thereby offsetting the fewer stays. In 2001, foreign travel expenditure by Austrians should decelerate, given the smaller gains in private net incomes, such that the tourism balance may improve somewhat.

Exports losing momentum

Table 4: Productivity

	1997	1998	1999	2000	2001	2002
	Percentage changes from previous year					
<i>Total economy</i>						
Real GDP	+ 1.3	+ 3.3	+ 2.8	+ 3.3	+ 2.6	+ 2.8
Employment ¹	+ 0.5	+ 0.8	+ 1.4	+ 1.1	+ 0.9	+ 1.0
Full-time equivalent	+ 0.2	+ 0.2	+ 0.6	+ 0.6	+ 0.6	+ 0.6
Productivity (GDP per employment)	+ 0.8	+ 2.5	+ 1.4	+ 2.2	+ 1.6	+ 1.8
Full-time equivalent	+ 1.2	+ 3.0	+ 2.2	+ 2.6	+ 2.0	+ 2.2
<i>Manufacturing</i>						
Production ²	+ 3.8	+ 3.4	+ 2.3	+ 6.5	+ 4.5	+ 5.0
Employees ³	- 1.4	+ 0.1	- 0.7	+ 0.3	+ 0.1	+ 0.2
Productivity per hour	+ 5.4	+ 3.2	+ 3.6	+ 5.9	+ 4.3	+ 4.8
Working hours per day for employee ⁴	- 0.1	+ 0.1	- 0.6	+ 0.3	+ 0.1	± 0.0

¹ Dependent and self-employed according to National Accounts. – ² Value added. – ³ According to Association of Austrian Social Security Bodies. – ⁴ According to "Konjunkturerhebung" of Statistics Austria.

Preliminary calculations suggest that Austrian GDP rose by 2.1 percent year-on-year in the third quarter 2000, only half the gain recorded in the first six months of the year. The slackening of activity was concentrated in wholesale and retail trade, in construction and in tourism, while production in manufacturing barely lost momentum.

For the whole year 2000, economic growth is estimated at 3.3 percent. The slight downward revision from earlier projections takes account of the stronger-than-anticipated effects of the oil price increase.

In 2001, Austrian GDP growth is projected to decelerate to 2.6 percent, mainly due to the expected weakening of activity abroad. Domestic fiscal tightening may keep the rate of growth $\frac{1}{4}$ percentage point below the EU average. With overall capacity utilisation edging down, output per employee (measured in full-time equivalents) may rise by 2 percent, as compared with $+2\frac{1}{2}$ percent in 2000.

Until last autumn, production in manufacturing has shown little sign of cyclical slackening. In the first nine months 2000, output rose by 7 percent in volume above the year-earlier level.

The strongest output gains were recorded in sectors that already in the past benefited primarily from an oil-price-induced inventory boom: non-ferrous metals, steel, paper, etc. But also suppliers of motor vehicle components and of investment goods were able to raise production further. In the third and fourth quarter, business expectations turned less optimistic, the actual situation and the outlook for production were judged less satisfactory. However, entrepreneurial sentiment weakened less than that of consumers.

The expected slowdown in export and investment activity will also affect manufacturing output in 2001, whose rate of growth may decline from $6\frac{1}{2}$ to $4\frac{1}{2}$ percent.

Private consumption has provided strong support to economic growth in the first half of 2000, rising 3.6 percent year-on-year. However, in the third quarter, retail sales (excluding motor cars) no longer exceeded the year-earlier level, car sales remained clearly below. A major reason for the stagnation has been the loss in purchasing power of private incomes related to high-flying oil prices. Wholesale trade also slackened considerably during autumn.

On annual average 2000, private consumption expenditure (+2.7 percent) and investment in machinery and equipment (+6 percent) have expanded strongly, though less than earlier expected.

In 2001, the only moderate gains in real net income from employment and social transfers ($+3\frac{1}{4}$ percent) will limit the scope for higher consumption. Unlike in 2000, budgetary policy is having a dampening effect on private net incomes: the increase in taxes and other public charges as well as the but small raise in civil service salaries and pensions ($+1\frac{1}{2}$ percent) are squeezing household purchasing power. In addition, income developments will reflect the slackening business activity. Private consumption is projected to expand by an inflation-adjusted 2 percent, which hinges on the assumption that households will be willing to reduce their current saving. Sluggish car sales, a major factor for the stagnation of demand for consumer durables in 2000, are expected to return to normal level in 2001.

Smaller gains in manufacturing output

Following a strong advance by $6\frac{1}{2}$ percent in 2000, the weaker international environment will lead to a more moderate increase by some $4\frac{1}{2}$ percent in Austrian manufacturing output in 2001.

Slower expansion of domestic demand

Table 5: Private consumption and earnings

	1997	1998	1999	2000	2001	2002
	Percentage changes from previous year, volume					
Private consumption expenditure	+ 1.4	+ 2.9	+ 2.3	+ 2.7	+ 2.0	+ 2.3
Durables	- 1.2	+ 7.0	+ 8.4	± 0.0	+ 1.0	+ 2.0
Non-durables and services	+ 1.7	+ 2.3	+ 1.4	+ 3.1	+ 2.1	+ 2.3
Net wages and salaries	- 1.8	+ 2.7	+ 3.1	+ 1.9	+ 0.7	+ 1.7
	Percentage changes from previous year					
Direct lending to domestic non-banks ¹	+ 3.6	+ 3.7	+ 5.2	+ 7.2	+ 4.4	+ 5.1
	In percent					
Inflation rate						
All items	1.3	0.9	0.6	2.4	1.5	1.3
Core inflation ²	1.1	1.2	0.8	1.8	2.3	1.7

¹ End of period. – ² Excluding food and energy items.

Table 6: Earnings and international competitiveness

	1997	1998	1999	2000	2001	2002
	Percentage changes from previous year					
Gross earnings per employee ¹	+ 0.7	+ 3.0	+ 2.0	+ 2.0	+ 2.7	+ 2.5
Full-time equivalent	+ 1.3	+ 3.6	+ 3.0	+ 2.5	+ 3.1	+ 2.9
Gross real earnings per employee	- 0.8	+ 2.5	+ 1.2	- 0.3	+ 1.2	+ 1.2
Net real earnings per employee	- 2.5	+ 2.3	+ 0.9	+ 0.6	+ 0.4	+ 0.7
Net wages and salaries	- 0.3	+ 3.3	+ 3.7	+ 4.2	+ 2.2	+ 3.0
Unit labour costs						
Total economy	+ 0.2	+ 0.7	+ 0.9	- 0.0	+ 1.2	+ 0.6
Manufacturing	- 4.4	- 1.7	- 0.5	- 3.7	- 1.2	- 1.4
Relative unit labour costs ²						
Vis-à-vis trading partners	- 3.9	- 0.6	- 1.5	- 4.1	+ 0.4	- 0.9
Vis-à-vis Germany	+ 0.8	+ 0.4	- 0.1	- 0.5	- 0.2	- 1.1
Effective exchange rate – manufactures						
Nominal	- 1.8	+ 2.5	+ 0.6	- 2.2	+ 1.4	+ 0.8
Real	- 4.3	+ 0.5	- 1.3	- 2.5	+ 0.5	± 0.0

¹ According to National Accounts. – ² Manufacturing, in a common currency; minus sign indicates improvement of competitiveness.

Investment has been very lively in the first semester 2000, but is losing momentum with the growing uncertainty over the business outlook. The stagnation of imports of investment goods last autumn suggests that investors, too have lost confidence as a result of the oil price increase. Towards the end of the year, the imminent abolition of the fiscal investment premium should have led to some demand for machinery and equipment being carried forward, which would imply a negative overhang for 2001.

Advanced purchases induced by the phasing out of the investment premium should also be expected for the construction sector. Wherever possible, contracted construction services will be invoiced within 2000. Real activity should have benefited from mild weather conditions in the 4th quarter. Overall construction output may grow by 2 and 1 percent, respectively, in 2000 and 2001, still clearly lagging behind overall economic activity. Weak housing demand is bearing down on new-home building, while civil engineering is negatively affected by the restraint in public expenditure. The only dynamic component is private commercial building.

Inflation has reached a peak in November at a rate of 3.1 percent. It will decelerate markedly in the months to come, as the contribution from energy prices (in an annual comparison) fades. The year-to-year rise in energy prices attained a maximum already in the 1st quarter 2000, and has diminished since.

Decelerating inflation

On annual average 2000, headline inflation probably amounted to 2.4 percent. The Harmonised Consumer Price Index (HCPI) shows a lower rate of increase, mainly due to different weights attached to the major components. The inflation rate as measured by the HCPI falls below the EU average.

The projection for 2001 is for a decline of the rate of inflation to 1.5 percent. This is consistent with the slowdown in business activity at home and abroad and the expected softening of oil prices (from \$ 30 to \$ 26 per barrel) coupled with a strengthening of the euro exchange rate. In 2001, a new consumer price index based on an updated weighting scheme will be introduced; according to past experience, the new index will yield a lower rate of inflation than the one used so far.

Inflation should abate to an average rate of 1.5 percent in 2001, as oil prices no longer exert upward pressure. "Core" inflation, however, may keep rising.

Table 7: Labour market

	1997	1998	1999	2000	2001	2002
	Changes from previous year, in 1,000					
<i>Demand for labour</i>						
Civilian employment	+ 8.8	+ 22.1	+ 32.2	+ 27.9	+ 24.5	+ 4.8
Dependent employment ¹	+ 8.3	+ 21.1	+ 31.2	+ 26.0	+ 22.5	+ 2.7
Excluding parental leave and military service	+ 12.8	+ 29.8	+ 37.2	+ 29.0	+ 24.0	+ 29.0
Percentage changes from previous year	+ 0.4	+ 1.0	+ 1.2	+ 1.0	+ 0.8	+ 0.9
Parental leave and military service ¹	- 4.4	- 8.7	- 6.0	- 3.0	- 1.5	- 26.3
Foreign workers	- 1.6	- 0.2	+ 7.8	+ 14.0	+ 17.0	+ 18.0
Self-employed ²	+ 0.5	+ 1.0	+ 1.0	+ 1.9	+ 2.0	+ 2.1
<i>Labour supply</i>						
Economically active population	+ 13.5	+ 11.0	+ 19.8	+ 23.1	+ 20.5	+ 19.5
Total labour force	+ 11.7	+ 26.5	+ 16.2	+ 1.2	+ 7.5	- 1.2
Foreign	- 1.7	+ 0.7	+ 6.6	+ 13.0	+ 14.0	+ 16.0
Migration of nationals	+ 5.4	+ 3.9	+ 3.0	- 1.5	- 1.0	- 2.0
Indigenous	+ 8.0	+ 21.9	+ 6.6	- 10.3	- 5.5	- 15.2
<i>Surplus of labour</i>						
Registered unemployed ³	+ 2.8	+ 4.4	- 16.1	- 26.7	- 17.0	- 6.0
	in 1,000	233.3	237.8	221.7	195.0	178.0
<i>Unemployment rate</i>						
According to Eurostat (percent of total labour force)	4.4	4.5	3.8	3.3	3.2	3.2
According to AMS (percent of total labour force)	6.4	6.5	6.0	5.3	4.8	4.6
According to AMS (percent of dependent labour force)	7.1	7.2	6.7	5.9	5.3	5.2
Participation rate ⁴	67.2	67.6	67.6	67.4	67.3	67.0
Employment rate ⁵	62.9	63.2	63.6	63.8	64.0	63.9

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).

The key factor for the deceleration of inflation will be the waning of the energy price effect which, in 2000, has added almost 1 percentage point to the annual rate. As from June 2001, the effect of higher consumption taxes (+0.5 percentage point in the annual rate) will disappear. In addition, cuts in electricity and telephone charges should have a moderating impact, as well as benign price developments for housing rents and seasonal goods. On the other hand, higher wage settlements will push up services prices, and the pass-through of higher oil prices will be reflected in those of manufactured goods.

The rise in prices of imported goods is estimated at 6 percent for 2000, that of wholesale prices at 4½ percent. Higher energy costs oblige firms to either accept lower profit margins or, market situation permitting, shift them onto sales prices. Because of such shifts, core inflation (excluding food and energy items) is set to accelerate from 1.8 to 2.3 percent in 2001. For 2002, a deceleration of both core inflation and the overall index may be expected.

Higher energy prices are unlikely to be passed on in full onto wages. While effective wages of metal workers, in view of the good export situation, were raised by a strong 3.4 percent, those for other sectors recorded clearly smaller gains (minimum wages for trade workers +2.4 to +3 percent). With regard to budgetary consolidation, wages and salaries in the public sector go up by only 1.5 percent.

Average earnings per full-time employee rose by 2½ percent in 2000, partly due to a cyclically-induced increase in working hours. In 2001, higher wage settlements may lead to a somewhat stronger gain in per-capita earnings of around 3 percent.

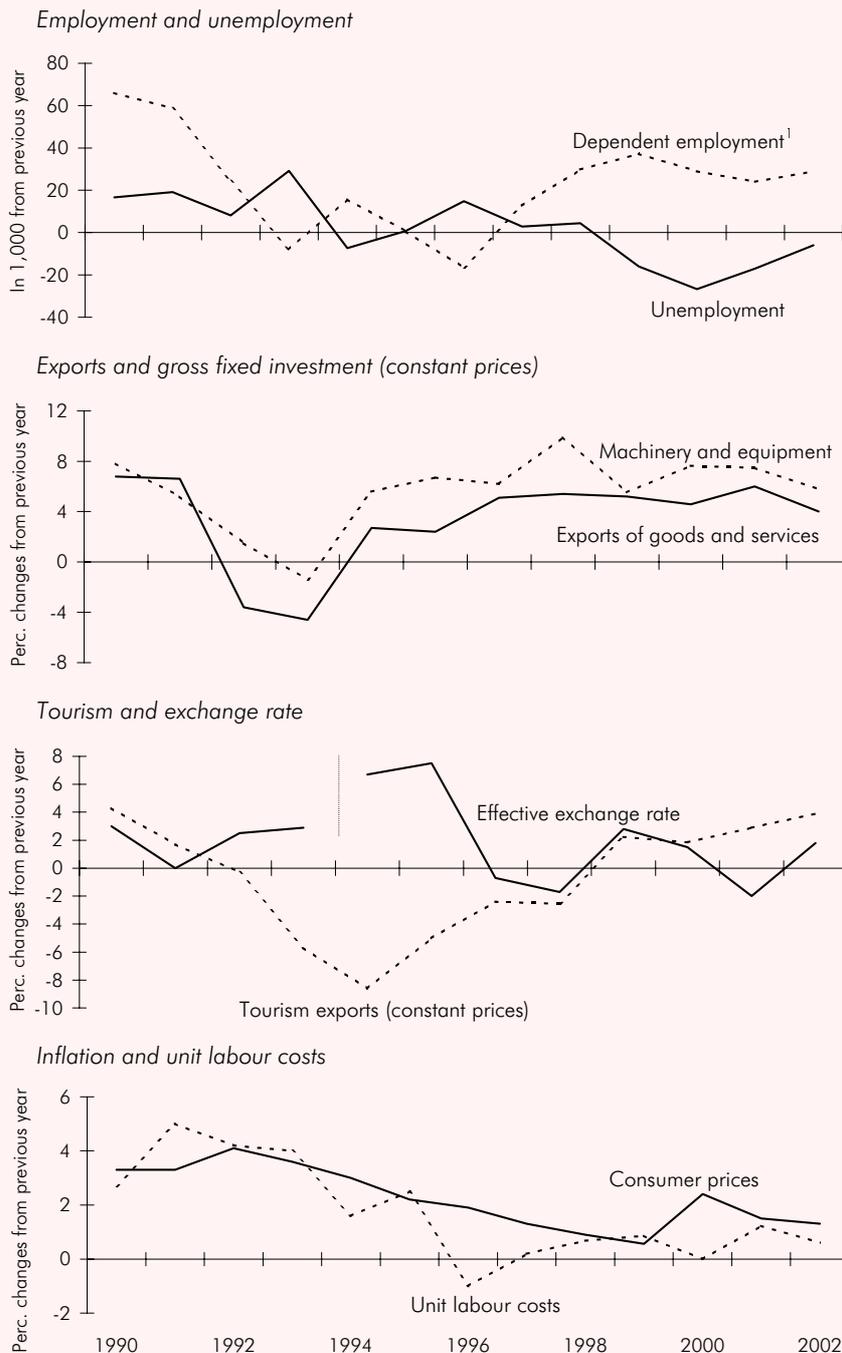
Unemployment to decline further in 2001

Unit labour costs for the whole economy are set to edge up by 1 percent in 2001, having remained stable in the past year. The advance in real incomes (+1 percent) will continue lagging behind the gain in productivity.

Strong economic activity in 2000 is reflected in a marked improvement on the labour market. Since early summer, however, employment growth has slowed. The main reason is a wave of early retirement (particularly of civil servants) in anticipation of new retirement regulations taking effect. The replacement of job leavers is complicated by the financial constraints of the public sector and by labour supply becoming tighter. Employment is receding in construction and the public sector, while rising in manufacturing and, more strongly, in private services. On annual average, the number of jobs went up by 29,000 or 1 percent.

Lively economic growth made for a significant reduction in unemployment in 2000. The decline, accompanied by a more moderate increase in the number of jobs, should be seen in the context of a wave of new entrants into retirement. In 2001, the fall in unemployment should continue at a somewhat slower pace.

Figure 2: Main economic indicators



¹ Excluding parental leave and military service.

Lively activity is also favouring a reduction in unemployment. More than in the last years, the new jobs are being filled by people from the unemployment register, as the "hidden reserve" of the labour force has been depleted to some extent. Roughly half of the reduction in unemployment is accounted for by the age group of 50 years and above, which should be related to the more frequent entries into retirement. In addition, there is evidence to suggest that unemployment benefits are being granted less generously than in the past: the applicants' ability and willingness to work are put to closer scrutiny, and benefits are denied more frequently than before.

With economic growth decelerating, employment gains will also shrink (+0.8 percent on average 2001). Given the new regulations on health insurance contributions for non-working spouses (without children), part of the people concerned may seek part-time jobs paid just above the contribution threshold. Unemployment is likely to fall further, albeit more slowly than in 2000. The average rate of unemployment for 2001 is projected at 5.3 percent (on national definitions). The jobless rate as calculated by Eurostat is more difficult to anticipate. In a first stage, it is extrapolated using the trend for the unemployment rate according to the labour exchange service, before being revised on the basis of the results from the regular labour market survey (Mikrozensus of March). For 2000, the unemployment rate following Eurostat stands at 3.3 percent, which may still be revised.