

## ■ 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 framework 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 (+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

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## 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 <sup>1)</sup> , 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 <sup>2)</sup>	+ 4.6	+10.6	+ 4.9	+ 7.0	+ 6.5
Construction	- 1.6	+ 4.1	+ 1.2	+ 1.0	+ 1.5
Exports of goods <sup>3)</sup>					
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 <sup>3)</sup>					
Volume	+ 9.4	+ 7.1	+ 5.2	+ 7.5	+ 6.5
Value	+10.9	+ 6.6	+ 5.5	+ 9.1	+ 7.6
Trade balance <sup>3)</sup>	(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 <sup>4)</sup>	(%) 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 <sup>5)</sup>	(%) 4.4	4.7	4.4	4.2	4.1
Percent of dependent labour force <sup>6)</sup>	(%) 7.1	7.2	6.7	6.3	5.9
Dependent employment <sup>7)</sup>	+ 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

<sup>1)</sup> Value added, including mining and quarrying. - <sup>2)</sup> Including other products. - <sup>3)</sup> According to Statistics Austria. - <sup>4)</sup> 10-year central government bonds (benchmark). - <sup>5)</sup> According to Eurostat. - <sup>6)</sup> According to Labour Market Service. - <sup>7)</sup> Excluding parental leave and military service.

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 normally 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 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 would be extremely difficult to assess at present, partly because this will obviously depend on for how long these measures were to be maintained.

Cut-off date: 5 April 2000.



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