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■ AUSTRIA'S ECONOMY BEFORE THE CRISIS IN RUSSIA

In late summer, activity in the financial markets was overshadowed by the crisis in Russia and the turbulence on the international stock exchanges. The financial outlook was also dimmed by the ongoing Asian crisis. The business climate of the Austrian manufacturing sector was barely impaired, however. Austrian firms took a more pessimistic view of most economic indicators than in spring, but the assessment was about the same as at the beginning of the year.

The upswing of the Austrian economy was only slightly weakened by the Asian crisis in the first half of the year. Exports rose by about one tenth over last year.

The Russian crisis also seems to have affected Austrian exporters only marginally. Austria ships only 1.4 percent of its exports to Russia; during the first quarter of 1998, this share was slightly smaller (1.2 percent). This figure captures, however, only part of the possible impact on Austria's economy. The indirect effects of a demand shortfall on third markets also need to be taken into account; moreover, the danger that the crisis will spread to other countries, mainly via financial markets, cannot yet be ruled out. The consequences of the turbulence on the financial markets for the non-financial sector are difficult to evaluate, given the dominance of psychological and political factors, but are likely to be small for Europe.

Though current perspective is limited, it seems likely that even in the worst case the crisis in Russia will have only moderate impact on the economies of Western Europe and Austria. Japan, however, has been seriously affected by the financial crisis in South-East Asia. The recession has become more severe during the last few months: in the second quarter of 1998, Japan's manufacturing sector produced about 8 percent less than in the same period of the previous year.

The U.S. economy has weakened somewhat, partly as a result of the Asian crisis. Growth in manufacturing output has steadily weakened since the beginning of the year (from +5¾ percent to +3¾ percent in June). So far this is the only area where the expected slowdown of economic growth can be seen.

The European economies have held up rather well in the wake of the crisis on the financial markets. A slight deceleration took place, however, before the summer. In the second quarter, manufacturing output was up by 4 percent com-

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pared with the same quarter of the last year, not quite attaining the rate of growth of the two preceding quarters (+5 percent). Economic activity slowed down especially in the U.K., primarily because of the revaluation of the British pound.

The banking sector has been more strongly affected by the Asian as well as the Russian crises than the export industry, and has been forced to write off part of its outstanding loans. A portion of the loans are covered by government guarantees. At the present time, it is impossible to predict when and to what extent these guarantees will be drawn upon.

Most economic indicators suggest that domestic demand has revived significantly in continental Europe during 1998.

In Austria, firms view the economic situation now somewhat less optimistically than in the spring. The assessment of order stocks and production expectations are at about the same level as in the winter months.

The rise in inventories of finished products indicates that the demand increase has not kept up with the vigorous production gains. The rise in the number of firms expecting a drop in prices reflects the decline in world market

prices of raw materials. In the summer months prices of raw materials were one fifth below the level of the previous year. The steepest decline was registered by crude oil prices (about -30 percent) and industrial raw materials (-15 percent).

Investment and consumption gathered pace in the first half of the year. Retail sales (adjusted for price changes) in the first five months exceeded last year's level by 2½ percent.

The favorable economic situation led to robust growth in employment in the course of 1998. August saw an increase of 31,800 jobs (+1 percent) compared to the same month last year. The small increase in the wage bill as well as in social security contributions indicates that the expansion of employment is concentrated in part-time work. Unemployment remained at a relatively high level, however: the rate of unemployment was 4.5 percent of the total labor force according to the EU definitions, and 5.9 percent of the dependent labor force according to the traditional Austrian method of calculation.

Cut-off date: September 7, 1998.