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Deficient Demand

No signs are currently visible of a cyclical recovery in Europe. Survey results for Austria as for the whole EU suggest business conditions being fragile, with no upward tendency. After the end of military operations in Iraq, oil prices have receded and share prices surged. The reaction of the business sector and of consumers is still uncertain.

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Business activity in Europe continues to be sluggish. Demand is lacking from the business sector as well as from households and the government sector. The repeated interest rate cuts were just enough to keep business sentiment stable. A cyclical upturn is still not in sight. Demand impulse in the USA is largely confined to additional military expenditure from which Europe benefits little. The marked rise in the euro exchange rate is beginning to undermine international price competitiveness of the euro area. Economic policy in the EU is invariably geared towards its long-term budgetary, inflation and labour supply targets.

Real GDP of the euro area rose by 1.3 percent year-on-year in the fourth quarter 2002, according to preliminary estimates. The seasonally-adjusted increase from the previous quarter narrowed to 0.1 percent, as both exports and investment stagnated. Only private consumption provided modest, but positive contributions to growth, despite the generally low level of confidence.

The end of the war in Iraq has lifted major political uncertainties, giving rise to lower oil prices and a recovery of stock market values. However, because of persistent economic risks and weak aggregate demand, signs of stronger activity keep lacking even after military operations have ended.

Current developments in Austria are similar to those in the euro area overall. GDP in the fourth quarter 2002 grew by 1.1 percent year-on-year, but edged down by 0.1 percent from the previous period. Results from the latest business cycle survey do not point to an imminent improvement. Sentiment in the manufacturing sector is volatile, with no clear upward trend. While export orders were rated somewhat higher in the second quarter, expectations for production and business conditions were taken down.

Strikes in the context of the envisaged pension reform are leading to temporary production shortfalls in May. They may, however, be largely offset in the following weeks in view of the poor utilisation of capacities (except in transport, education and the media).

The cyclical weakness weighed on labour demand in 2002 and early 2003. In April, however, the number of actively employed increased by about 8,000 year-on-year, mainly due to favourable developments in seasonal activities (tourism, construction), whereas manufacturing recorded further job losses. The number of unemployed did not exceed the year-earlier level in April, owing to more people being enrolled in training activities (+10,000) or claiming advance payments on their retirement benefits, as well as lively demand for seasonal workers.

The sluggish activity has a beneficial impact on the current account. Imports fell markedly as a consequence of notably the slump in investment. For the first time since 1991, the current account moved into surplus in 2002, with the positive trend continuing into early 2003.

Price developments are also reflecting the cyclical weakness. In March, consumer price inflation stood at an annual rate of 1.8 percent, broadly the same rate as for the last six months. The price-dampening effect of the rising euro exchange rate was reinforced in April by falling oil prices.