Oesterreichische Nationalbank

Eurosystem

Speeches by President Adolf Wala and Governor Klaus Liebscher

at the General Meeting
of the Oesterreichische Nationalbank
on May 15, 2003

Speech by President Adolf Wala

The Euro – New Notes and Coins Well Received

Following the smooth introduction of euro banknotes and coins, Austrians have shown a positive attitude toward the new currency. The high quality of the euro cash was a key reason the general public adopted the new money, *as its distinctive security features make the euro one of the most counterfeit-proof currencies in the world.*

Much of the credit goes to the Oesterreichische Nationalbank's competence center for payment means and transactions, comprising, inter alia, the printing works OeBS, or Oesterreichische Banknoten- und Sicherheitsdruck GmbH, and Münze Österreich AG. These companies' know-how, which is held in high esteem internationally, guaranteed that the high quality and security requirements for the new currency were fulfilled efficiently.

However, it is taking longer than expected for people's feel for the value of the new currency to fully develop. Therefore, the OeNB has continued its efforts to inform the public and thus help improve people's understanding of the euro's value. These efforts are considerably facilitated by the public's high rating for the central bank and its competence in fulfilling its responsibilities. *The consistently high degree of trust the public has exhibited in the OeNB as an institution is a sound basis for the OeNB to continue its successful activities within the Eurosystem* (see chart 1).

International and Austrian Economic Developments

The global economic environment was a very difficult one in 2002. After having gained substantial momentum at the beginning of 2002, economic growth lost more and more ground as the year went on (see chart 2). Against the background of growing geopolitical tension, the protracted uncertainty of consumers and the corporate sector alongside investor pessimism acted as dampers on economic activity. The slide on international stock markets is remarkable not just for its intensity, but above all for its duration (see chart 3).

The U.S. economy bolstered international business activity, with U.S. monetary and fiscal policy stimulating growth perceptibly. However, as apprehension increased given the threat of war in Iraq and heavy losses on the stock market, growth decelerated toward the end of the review year. In Japan growth impulses also faltered, and serious structural problems, above all in the banking industry, continue to plague the Japanese economy.

Nor did Europe's economy succeed in getting off the ground in the year under review. Indeed, the euro area posted the weakest economic growth (0.8%) since 1993 (see chart 4). Anemic domestic demand was the root cause of the economic weakness. With uncertainty and risks mounting, consumer confidence deteriorated (see chart 5). Listless business activity burdened government budgets and pushed up unemployment.

Hence, economic policymakers faced a great challenge. The Eurosystem's monetary policy remained solidly oriented on its price stability objective. *In view of the moderation of pressure on prices, the Governing Council of the ECB lowered interest rates in December 2002 and again in March 2003 to a historic low* (see chart 31). The pronounced gain in the value of the euro by nearly one fifth against the U.S. dollar in the course of 2002 reduced the inflationary pressure of the surge in oil prices (see charts 30 and 6). In 2002, inflation lessened to 2.2%, a rate the higher price of services kept slightly above the medium-term goal.

Considering the slack in economic growth, fiscal policymakers let the automatic stabilizers take effect. Some countries with minimal room for maneuver, however, failed to abide by the provisions of the Stability and Growth Pact.

Overall, the economic fundamentals are not so unfavorable as to prevent Europe from returning to a growth path. In addition to high international competitiveness and good labor productivity, the *historically low level of interest rates* and ample liquidity provide for advantageous financing conditions.

Overcoming the economic doldrums thus hinges on resolving the geopolitical tensions and restoring business and consumer confidence. Moreover, economic policymakers are called on to make sure any recovery is a lasting one. Above all, the *process of structural adjustment* must be continued. Structural change must be based solidly on social policy consensus, though, and must not be at the expense of social welfare, because the public would not accept a European economic model that advocates completely unrestrained competition.

Although *Austria* could not disengage itself from the international trend of business activity, its *GDP nevertheless advanced by 1%, which is above the euro area average* (see chart 7). However, never before has economic growth in Austria been so sluggish three years in a row. Consumer spending remained hesitant, and business investment plummeted. *Exports were the mainstay of growth in Austria, with demand from Eastern Europe, where GDP growth was more animated, providing crucial impulses.* Austria's international competitiveness improved once again in terms of relative unit labor cost, enabling exporters to gain market share.

The labor market did not remain unaffected by the tepid economy either. Nonetheless, the *unemployment rate* was low compared to jobless figures in other euro area countries; *only Luxembourg and the Netherlands recorded lower rates. Austria's moderate wage policy also made the country one of the euro area's best performers on price stability, putting it in third place behind Germany and Belgium.* While actual inflation declined, perceived inflation rose throughout the year, in some instances quite perceptibly (see chart 8). As consumers focused on the euro changeover, they were probably also especially attentive to price changes.

Economic stagnation also burdened government budgets. However, having implemented rigorous austerity measures in recent years and having reduced its budget deficit to 0.6% of GDP, Austria ranks among the euro area countries which have some fiscal policy room for maneuver (see chart 9).

In the long run, Austria will remain an attractive business location only if it has a reliable economic policy framework in which social welfare and a broad consensus about economic policy are priorities. These prerequisites are especially important if Austria is to *benefit fully from the steady progress of European integration. Social welfare was the fundamental quality that made Austria not just one of the world's wealthiest, but also one of the world's most livable countries!*

Financial Statements 2002

I will restrict my presentation of the Financial Statements for 2002 to the main changes from the economic perspective in the balance sheet and the profit and loss account. The

Annual Report 2002 contains more detailed notes.

Under the accounting and valuation rules of the European System of Central Banks, all balance sheet items have been valued at market prices since 1999. Unrealized valuation gains cannot be disbursed; much rather, they must be recorded in revaluation accounts, which are used to reverse valuation losses that may arise in future years. *In 2002 the appreciation of the euro resulted in a substantial decline of nearly EUR 1 billion in Eurosystem revaluation reserves. As this example patently shows, annual profits are subject to large fluctuations in an environment of volatile financial markets,* and it takes adequate reserves to hedge against these risks.

At EUR 1.51 billion, the profit before taxes for the business year 2002 was only EUR 127 billion lower than the 2001 result (see chart 10).

This is the *fourth-best result in the history of the Oesterreichische Nationalbank,* and it was achieved under extremely difficult economic conditions as a result of an investment policy that has consistently proved highly successful also by comparison to the policy other ESCB national central banks have pursued. Realized gains arising from gold, foreign currency and security transactions were instrumental in bringing about this result. Equity earnings and transfers from provisions to cover foreign currency depreciation and price losses on securities also contributed to high profit.

In recent years, the OeNB reduced its gold holdings by more than half and substantially decreased its foreign currency portfolio. This investment strategy was especially successful because it was implemented at the right time, did not burden markets and proceeded smoothly. However, the scope for realizing exchange rate and price gains is limited, so that realistically, much lower profits will have to be expected for the future. In addition, high volatility on financial markets may contribute to substantial fluctuations of profits.

The individual items of the *balance sheet* developed as follows:

On the *assets* side, *sales of gold to the Bank for International Settlements (BIS)* further reduced gold holdings by 30 tons in 2002 (see chart 11), with price gains of EUR 237.4 million realized on the sales. The OeNB's *gold holdings total 317 tons with a market value of approximately EUR 3.3 billion.* The OeNB made full use of the scope for gold sales provided under the central bank agreement concluded to stabilize the gold market and the value of gold holdings, which is in effect until 2004.

On the topic of gold policy, I would like to draw your attention to the fact that monetary policy exigencies and profit considerations have induced the OeNB to steadily shed gold holdings since the beginning of the 1990s. Gold sales under this heading proceed smoothly and do not destabilize the gold market. Moreover, the OeNB began to invest its gold reserves for profit earlier than many other central banks. This means that the OeNB's gold holdings are not simply held in vaults where they do not bear interest; 77% of the gold is in fact invested via interest-bearing forward and swap transactions.

Foreign currency claims on euro area residents and non-euro area residents contracted by EUR 5.3 billion from 2001 to EUR 9.8 billion. This marked decline reflects foreign currency sales, but also valuation losses of foreign currency against the appreciated euro.

Turning to *liabilities* (see chart 12), *Eurosystem revaluation reserves fell by more than 35% to EUR 1.6 billion,* mainly on account of valuation losses of foreign currencies against the euro. In line with provisions, the *reserve fund for exchange risks,* which was funded up to the end of 1998 and which serves to cover unrealized foreign currency losses, *was reduced to EUR 1.5 billion by the release of EUR 306.3 million.*

In addition, on the basis of risk model calculations, *EUR 9 million had to be allocated to provisions for exchange rate risks for the first time.* This was the amount by which the Eurosystem revaluation accounts and the reserve fund for exchange rate risks fell short of offsetting the established exchange rate risk. The risk of a drop in securities prices can be hedged with the *reserve for nondomestic and price risks.* Risk calculations based on models for exchange rate and interest rate risk resulted in a total reserve requirement of EUR 1.1 billion. On balance, *EUR 53 million were transferred from the reserve for nondomestic and price risks to cover the risk of losses.*

The following main changes in income and expenses in the *profit and loss account* occurred in 2002 (see chart 13):

At EUR 1.8 billion, *total net income* is 8.2% lower than in 2001. Interest income is one of the main sources of central bank profit. *Net interest income* diminished by *EUR 279 million* or nearly 32% to *EUR 594 million,* chiefly as a consequence of the pronounced decline in interest rates, but also because Austrian banks took less recourse to central bank refinancing.

Realized gains from financial operations (gold, foreign exchange and security transactions) represent a further important source of central bank profit. Despite the prevailing difficult market conditions, these transactions produced net income of *EUR 849 million.*

The *use of derivatives ensures the success of the OeNB's investment strategy* for gold and foreign exchange holdings. Moreover, appropriate risk management methods are applied to hedge market and credit risk. Overall, these management techniques, which are advanced by Eurosystem standards, accounted for a *substantial share of profit.*

Futhermore, at *EUR 243 million net income from equity shares and participating interests expanded nearly fivefold* from 2001. *Profit disbursements by Münze Österreich AG represented the lion's share,* as this subsidiary partly made early dividend payments for the especially favorable financial year 2002, in which the need for the launch stock of euro coins raised profits. In addition to the dividends of the OeNB's subsidiaries, the profit disbursed by the ECB augmented income from equity shares and participating interests.

Finally, *other income* amounted to *EUR 84 million,* most of which stems from schilling banknotes which are no longer expected to be returned.

Expenses declined by EUR 32 million or 11% *to EUR 255 million* from 2001. This drop may largely be attributed to two factors: Administrative expenses were lower because there were fewer activities in connection with the introduction of euro notes and coins, and the expenditure for the purchase of euro banknotes fell to nearly half the 2001 level. Staff cost edged up, chiefly because of the boost in salaries in line with collective wage agreements.

I would like to also point out that since the beginning of 2000 the

OeNB's pension reserve has in effect represented a closed system applicable to staff employed before May 1, 1998, as staff recruited after this deadline will receive pensions under a separate, new plan (see chart 14). As a consequence, pension payments no longer affect operating profit before taxes.

Staff was increased by 41 staff members to 984 (see chart 15).

On the basis of the operating profit before taxes of EUR 1,515 million, the central government receives corporate income tax of EUR 515 million and a 90% profit share of EUR 900 million after taxes (see chart 16). *The central government receives a total of 93.4%, i.e. EUR 1,415 million, of the 2002 operating profit.* The central government's profit share is only less than one tenth lower in 2002 than in 2001, making this amount the third-largest transfer of profit to government in the OeNB's history. The size of the operating profit is remarkable considering the very difficult economic environment in which it was made and by comparison to other Eurosystem central banks. All in all, the OeNB has transferred to government 0.7% of GDP annually, or a total EUR 5.7 billion, since the beginning of Stage Three of EMU in the form of corporate income tax and profit! In addition, from its remaining profit, the OeNB provided EUR 284 million for research grants.

The profit for the year 2002 comes to EUR 100.1 million. The following proposal is made to the General Meeting for the appropriation of profit: to use *EUR 1.2 million* to pay the *maximum dividend of 10%* on the OeNB's capital stock of EUR 12 million, to allocate *EUR 70.3 million* to the OeNB *Anniversary Fund for the Promotion of Scientific Research and Teaching,* and to allocate an additional *EUR 4.2 million* to the Leopold Collection on the basis of the promotion contract concluded between the *Leopold Museum Private Foundation* and the OeNB in 1994. Moreover, *EUR 24.2 million* are to be allocated to the reserves of the *OeNB Anniversary Fund,* the first allocation since its foundation in 1966. The income from the investment of these funds shall be available for grants every year on a lasting basis. The remainder of the profit, *EUR 0.2 million,* is to be carried forward as *retained profit.*

The OeNB in the Eurosystem – A Customer-Oriented Enterprise

As the OeNB substantially streamlined its corporate structures at an early point in time, it had a good starting position for cooperation within the ESCB from the very outset. On this basis, the Oesterreichische Nationalbank has achieved high esteem within the Eurosystem since the start of EMU and has implemented the milestones up to and including the introduction of euro notes and coins in an exemplary fashion.

With the framework for the Eurosystem as its point of reference, the OeNB adapted its medium-term strategic orientation in the review year. *Fulfillment of the ESCB mandate – maintaining price stability and ensuring financial stability – is the centerpiece of the corporate strategy* (see chart 17). For the OeNB, the *crucial prerequisites* for carrying out this task from the entrepreneurial perspective are *customer orientation and efficient performance* (see chart 18). To this end, all business sectors continuously accord customer orientation and the optimization of work processes a high priority.

The OeNB has defined its core business areas on the basis of the mandate of the ESCB (see chart 19). This chart patently shows that the *tasks and responsibilities of the national central banks in the Eurosystem have increased in number and have become more demanding.* In addition to the new tasks related to its role in the monetary policymaking process, the OeNB also assumed further responsibilities in the areas *risk assessment and payment systems oversight* following the restructuring of financial system supervision. The OeNB made great strides in all business areas in the year under review, as reflected by the professional logistical and public relations support for the introduction of the euro banknotes and coins, the involvement in the new financial market supervision system, and the introduction of e-business and teleworking models. Allow me to cite two examples of business areas in which the public's attention is focused time and again on the OeNB's obligations.

One of the ESCB's core activities under Article 105 of the Treaty is the *management of official foreign reserves,* with the ESCB being independent and free of instructions under Article 108 of the Treaty in carrying out the tasks and duties conferred upon it. Thus, since the beginning of monetary union the OeNB's reserves have been part of the Eurosystem's reserve assets. Accordingly, the Eurosystem alone decides how high the level of reserves is to be in line with monetary policy requirements. Of course, the optimum volume and the role of reserve assets may be discussed within the framework of the Eurosystem, but the financial market turbulence of recent years and the protracted economic sluggishness have clearly shown that the credibility of monetary policy and the trust in a currency are also determined to a substantial degree by the level of reserve assets.

Income from the investment of official foreign reserves accrues overwhelmingly to the Austrian government, with the exception of a small portion required to secure the OeNB's financial independence according to the provisions of the Treaty. *In its foreign reserve management, the OeNB has demonstrated not just a consistently high degree of efficiency, but has also made full use of its scope for investment. Accordingly, since 1999 the reserve assets have been reduced in a deliberate fashion and at the end of 2002 were roughly equal to the Eurosystem average measured as a percentage of GDP* (see chart 20). The strategy of *reducing net foreign currency reserves by nearly one third* produced considerable profit from price gains that represented a major portion of the high profit transfers to government in the past few years (see chart 21). *The size of Austria's reserve assets is also appropriate in an international comparison:* Austria accounts for a much smaller share of world reserve assets than would correspond to its share of world GDP or world trade (see chart 22).

According to Article 105 of the Treaty, *a further core business area consists in promoting the smooth operation of payment systems.* As efficient and secure payment systems are a key factor in financial stability, the ECB and the BIS call for national central banks to play an active and committed role in this area. *The quality of means of payment along with the security and efficiency of payment operations are the two principal aspects of efficient payment systems. Hence,* ever since the preparations for monetary union began, the OeNB has set great store by *developing its competence center for payment means and transactions* (see chart 23). The production of payment means and the settlement of payments are handled by subsidiaries of the OeNB to ensure that these services are provided in the most efficient manner possible. This approach has been validated by the smooth changeover to euro cash and the growing international demand for products and services of the OeNB's subsidiaries (see chart 24).

The printing works OeBS, Münze Österreich AG and the smart card and identity systems producer AUSTRIA CARD Gesellschaft m.b.H. not only *provided crucial services for the Oesterreichische Nationalbank* in 2002, but also added substantially to the OeNB's profit, and GELDSERVICE AUSTRIA G.m.b.H. (GSA) enabled the entire banking sector to save costs. Moreover, the *repositioning of Austrian Payment Systems Services (APSS) GmbH* represented a *further step toward improving the efficiency of payment processing,* which is also in the overall economic interest. In the long run, one aspect of payment systems is of overriding importance from the monetary policy standpoint: Only those who have the proper know-how about all payment means and services from banknotes to cards to e-money will be well equipped to master the future!

As the core activities reserve asset management and payment means and services indicate, the *OeNB attaches great importance to utility for the user and to efficiency in implementing its mandate.* As a result, the OeNB is one of the most streamlined and efficient of the Eurosystem central banks. *The OeNB has an excellent position in the Eurosystem in terms of operating profit* (see chart 25), *productivity* (see chart 26) and *staff size* (see chart 27) *as well as staff and administrative expenses* (see chart 28).

The staff and management of the Oesterreichische Nationalbank have fulfilled their manifold tasks, which range from cooperation within the ESCB to the implementation of monetary policy to the production of state-of-the-art secure means of payment, with enormous expertise and enthusiasm. I should like to thank the OeNB's staff for its performance and the staff council for its support. The Governing Board of the OeNB has handled its tasks in the ESCB very well indeed.

I would like to thank the members of the General Council for having supported the principal adjustments and the comprehensive projects, and for having provided for a positive and cooperative climate.

Thank you for your attention. I give the floor to Governor Liebscher for his statement.

Speech by Governor Klaus Liebscher

Continued Price Stability and Successful Launch of Euro Banknotes and Coins in 2002

The outstanding event of the 2002 business year was certainly the *smooth introduction of euro banknotes and coins* in Austria and eleven other Member States of the European Union. Orchestrating the changeover from the schilling to the euro, the OeNB successfully managed one of the largest organizational, logistical and public-relations challenges in its history. What is more, the street debut of the euro marked the completion of a long process of monetary integration in Europe and made *monetary union a tangible reality* for many European citizens.

In the meantime, the *euro* has established itself on the international financial markets as a *sound global and anchor currency* next to the U.S. dollar. Moreover, the common currency was *very well received* by some 300 million Europeans as their new *cash,* which they have been readily using as their means of payment in daily transactions. Consumers' feel for euro prices is continually improving, and the gap between subjectively felt and statistically measured inflation, which was a matter for debate in the euro area and also in Austria in the beginning, has nearly closed.

Last year's *price developments* lend substance to this observation. In *Austria,* inflation averaged a mere 1.7% in 2002, which is more than half a percentage point below the price increase recorded in the year prior to the euro cash changeover. Moreover, in the fourth year of monetary union, with an average HICP inflation of 2.2%, *price stability* and thus purchasing power were once again *maintained* in the *euro area* – amid difficult economic framework conditions, yet thanks to the circumspect monetary policy of the Governing Council of the ECB. The *independence of the Eurosystem,* its *decentralized* and hence *efficient structure* as well as its *tried and true monetary policy strategy,* which the Governing Council confirmed on May 8, 2003, have *contributed substantially to maintaining price stability* since the beginning of monetary union.

With inflationary expectations trending downwards, the Governing Council cut the *key interest rate* from 4.75% to 3.25% already in 2001, to further trim it in December 2002 to 2.75%. In early March 2003, it decided to reduce the key interest rate to 2.50%. The euro area key interest rates have thus reached a *very low level,* both in nominal and real terms. On May 8, 2003, the Governing Council reconfirmed that this interest rate level was in line with the maintenance of price stability in the medium term. From a monetary perspective, conditions are therefore favorable for economic growth.

However, the evaluation of future economic developments remains subject to *relatively high forecast risks,* inter alia with respect to the accumulation of macroeconomic imbalances outside the euro area, uncertainty about the restructuring needs in the euro area corporate sector or SARS, which has been spreading, in particular in Asia. While the end of military action in Iraq translates into a reduction of important economic downside risks, it is still relatively difficult to assess how the other factors mentioned above may come to bear on economic developments in the euro area.

In the light of these developments, we continue to *expect a gradual strengthening of real GDP growth to start later in 2003 and to gather more pace in the course of next year.* Diminishing geopolitical uncertainties, rebounding global demand, decreasing financial market volatility and the concomitant recovery on equity markets, the prospect of a further drop in inflation and the resulting increase in real disposable income as well as the low interest rate level support this expectation.

From today's perspective, on the assumption of a euro which gains on the U.S. dollar and thus has a dampening effect on inflation via imports, of a forecast for subdued economic growth, of declining oil prices after the war in Iraq and moderate wage settlements, *inflation* in the euro area is set to *fall below 2% over the medium term.*

The Governing Council of the ECB will monitor the future developments very closely with a view to safeguarding price stability in the euro area.

Stability Policy and Structural Reforms Aimed at Raising International Competitiveness Are to Continue

For the euro area to be able to fully utilize the economic potential of the stability-oriented monetary policy, we also need an *economic policy aimed at safeguarding stability in the long run.* This is to ensure that the *euro area* continues to *withstand stiffer global competition* and thus to *sustain growth and employment.* All of this was even more relevant in the light of a *global environment* where a recovery was farther down the horizon, the volatility on financial markets was on the rise and business and consumer confidence were slipping. Stability-oriented policy must meet these challenges at all levels.

Evaluating euro area *fiscal-policy developments* since the inception of monetary union, we see that the *Stability and Growth Pact* produced favorable effects early on. As a case in point, the aggregate fiscal balance of the *euro area countries* was close to balance in 2000 for the first time in decades. In the same vein, *Austria* registered a balanced budget in 2001 and *clearly met the provisions laid down in the Stability and Growth Pact* also in 2002, when most other euro area countries failed to attain the targets set forth in their stability programs and the average budget deficit in the euro area had climbed from 1.6% of GDP in 2001 to 2.2%. Unfortunately, *some EU Member States* have not scaled back their budget deficits swiftly and in due time while economic conditions were still favorable, so that these countries are now – certainly also owing to the current economic slowdown – posting deficit ratios *precariously close to or already above the 3% reference value.*

With players on international financial markets taking cues from the Stability and Growth Pact, the *euro area ministers of finance* agreed on *adequate fiscal consolidation measures* in October 2002. Accordingly, those Member States which already record a deficit ratio of close to or above 3% of GDP are to pursue a *growth-promoting consolidation path* in line with the Stability and Growth Pact. *The euro area countries will have to comply strictly with the Treaty and the Stability and Growth Pact, the institutional framework for monetary union, also in the future.* Therefore, the excessive deficit procedures recently initiated against some euro area countries in line with the relevant provisions of the Treaty *have strengthened the credibility of the Stability and Growth Pact.* Now more than ever, prudence dictates that fiscal policies be geared towards stability and public finance positions be sound, not least because of the demographic developments in the euro area.

Furthermore, *structural reforms on the labor, goods and financial markets* that have already been launched must be pursued resolutely to make the euro area more flexible and resilient to external shocks and to increase potential output, which will *improve growth and employment prospects* and foster consumer and investor confidence.

Austria cannot ignore these European objectives and challenges. In the face of the third consecutive year of difficult framework conditions, our country has shown a *sound economic performance* and has fared well by EU standards in meeting the key macroeconomic targets. As a case in point, Austria partly ranks among the better, i.e. above-average, performers in the EU in terms of inflation, unemployment ratio, budget deficit and current account. Even with regard to economic growth, Austrian businesses managed to compensate for some of the marked weakness evident in Austria's traditional export markets Germany, Italy and Switzerland by means of a timely and vigorous expansion into Central and Eastern Europe. On balance, a moderate wage policy and further productivity increases likewise strengthened the competitiveness of our enterprises on world markets.

However, tax distortions and other disincentives still exist in Austria and they have to be eliminated. A *tax reform* as envisaged by the government must by all means tie in with the target of a balanced budget in line with the Stability and Growth Pact. Over the medium term, the *share of investment in government expenditures* should trend upwards, while the *general government tax-to-GDP ratio* should at the same time be scaled back. The future drag on budgets from ongoing population aging must be cushioned in time through *sustainable reforms of pension and health-care systems.* Other areas in need of reform are *fiscal sharing* and *public administration.* Turning to *structural reforms,* allow me to point out, for instance, the need for a further liberalization of the labor markets, store closing hours, the cutting of red tape and incentives for innovation, research and development as well as education and training. All told, amid keener global competition, Austrian stakeholders *face the tall order of preserving Austria's high attractiveness as a business location through necessary strategic reform measures.*

EU Enlargement – The Next Milestone in European Integration

After the successful implementation of monetary union, the EU is now setting its sights on the *next milestone of integration:* its *enlargement by ten new Member States.* The signing of the Accession Treaty in April 2003 and its subsequent ratification will pave the way for the accession countries to *join the EU in early May 2004.*

This visionary and mutually beneficial integration project, which follows on the heels of previous milestones of European integration, marks the end of the division of Europe after World War II.

The prospective EU members have made *impressive progress in economic transition and catching up* in the past decade, which reflects well on their level of integration. This said, *the per-capita GDP* of the acceding countries *nevertheless* still accounts for *only about half of the euro area average* adjusted for different price levels.

So, the upcoming *integration* of the acceding countries into the EU will be a *challenge* both for the current and the future Member States. From a global perspective, however, no other regional group of countries has matched the successful track record of the acceding countries in the past decade. This is clearly hope-inspiring. Given its well-established trade relations in this region and its well-timed move into these growth markets, *Austria has already benefited significantly* from the economic integration of this region into Europe.

Before the *new Member States can join monetary union,* however, they will participate in the *exchange rate mechanism ERM II* and will have to *strictly and sustainably abide by the legal and economic convergence criteria.* Legal and institutional aspects and the principle of equality of all EU Member States as well as economic considerations underpin the case for gradual monetary integration. After all, *premature adoption of the euro* could result in a disproportionately large burden for the acceding countries, i.e. financial and economic adjustments, and *would thus not be prudent.* In the interest of both the acceding and the euro area countries, the *pace of integration* should therefore *not compromise the quality of this process.*

The Eurosystem central banks, including of course the OeNB, have already established close ties with the central banks of the acceding countries, and the *European System of Central Banks (ESCB)* must follow suit and take preparations regarding its *institutional setup* for the integration of the new EU Member States. To this end, the Governing Council of the ECB adopted a recommendation on the *adjustment of its voting modalities* in line with the Treaty of Nice, which was subsequently endorsed by the European Council in March 2003.

The Euro as a Catalyst for Reform and Integration in Europe

The current *debate about the future constitution and identity of Europe* as well as the exploration of possible limits of the European Union show that we are witnessing an ongoing and important evolutionary process the path of which is to be mapped out by the forward-looking *European Convention.* Following past successes, the *further integration of Europe must* be advanced steadfastly.

The monetary union and the euro have already considerably strengthened the euro area's position in the dynamic process of globalization. In the future, they will continue to *drive reform* and *act as a catalyst for further economic and political integration in Europe. The upcoming enlargement of the European Union,* the next step in the integration process, will not only yield economic advantages, but will also buttress political stability in Europe, sustainably reinforce Europe's global competitiveness and thus, in the long run, significantly contribute to *prosperity, security and peace on our continent.*

Words of Thanks

Striking a similar chord as President Wala, in conclusion, I am pleased to say that the OeNB is in a stellar position not only within the Eurosystem, but – according to survey results – also enjoys very high ratings with regard to confidence, stability and competence in Austria.

Furthermore, it gives my colleagues on the Governing Board of the OeNB and me great satisfaction that in the face of the daunting challenges of the year 2002, we once again managed to produce an operating result in keeping with the resounding successes of the previous two years.

I would like to thank the staff of the Oesterreichische Nationalbank for this success and for their efficiency and commendable effort. Also, I extend my thanks to the President, Vice President and all the members of the General Council for their continuous support and commitment.

Annex[1])

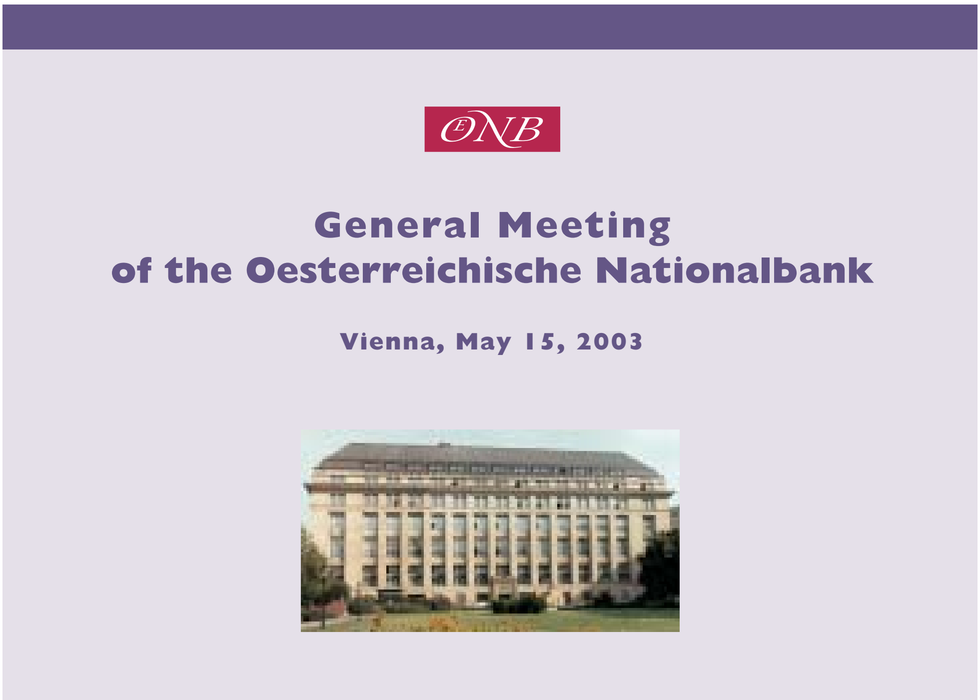
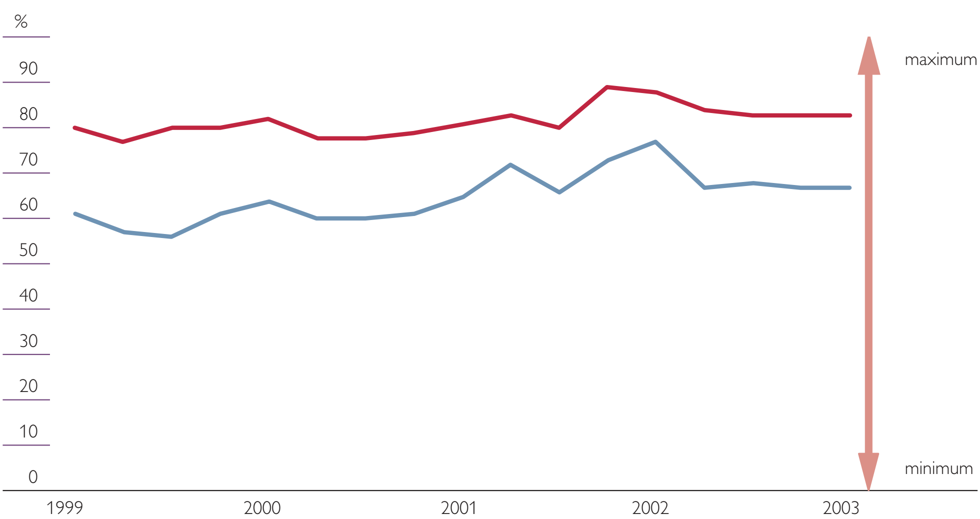


Chart 1

Public Confidence in the OeNB



confidence (left scale)
efficiency (right scale)

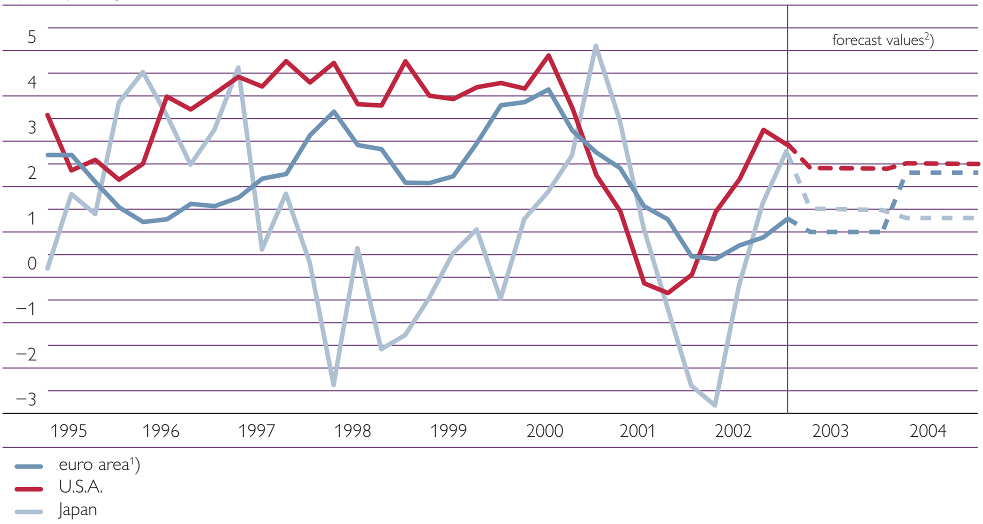
Source: IFES.

1 *Editorial close: May 8, 2003.*

Chart 2

Real GDP

quarterly change annualized in %



Source: Eurostat.

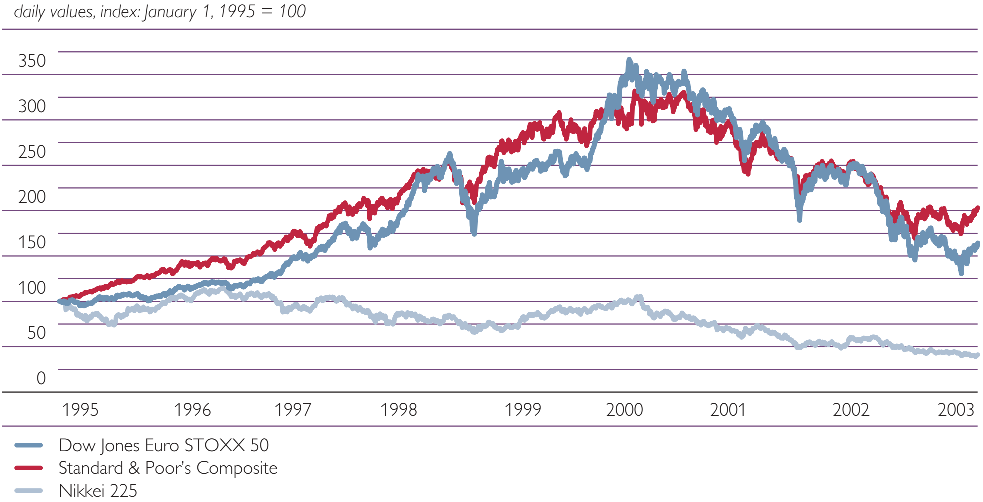
1) EU-11 and Greece until December 31, 2000/EU-12 from January 1, 2001.

2) Spring Forecast of the European Commission.

Chart 3

Stock Markets

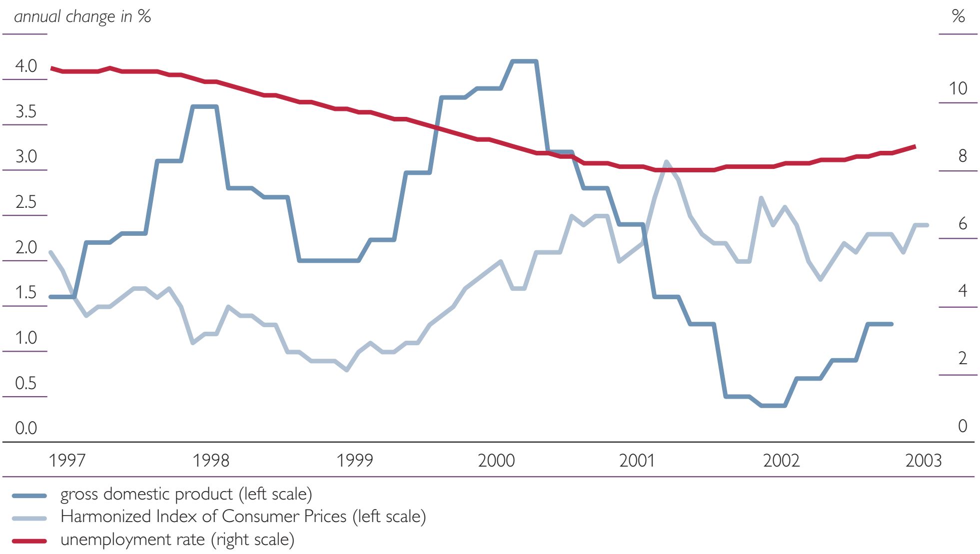
daily values, index: January 1, 1995 = 100



Source: Datastream.

Chart 4

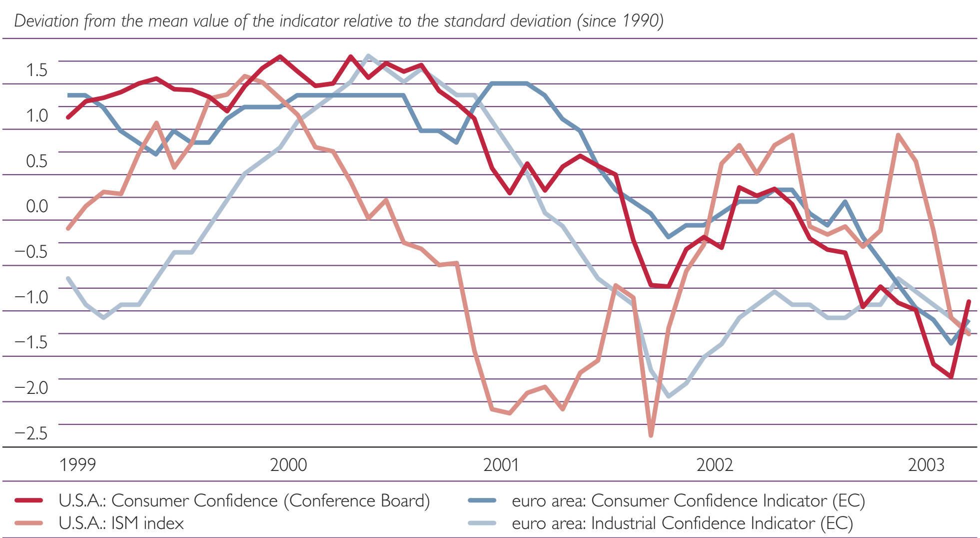
Euro Area – Economic Indicators



Source: Eurostat.

Chart 5

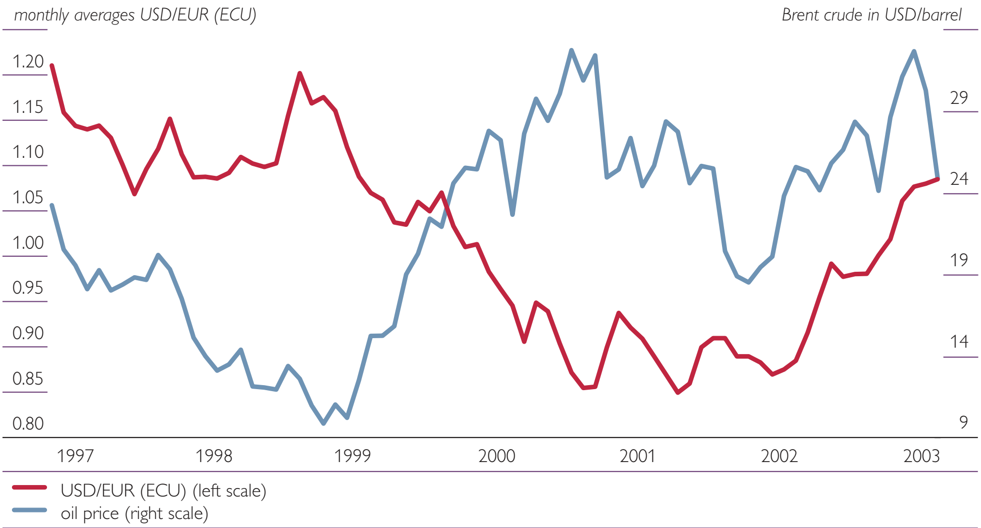
Confidence Indicators – U.S.A. and Euro Area



Source: Datastream, OeNB.

Chart 6

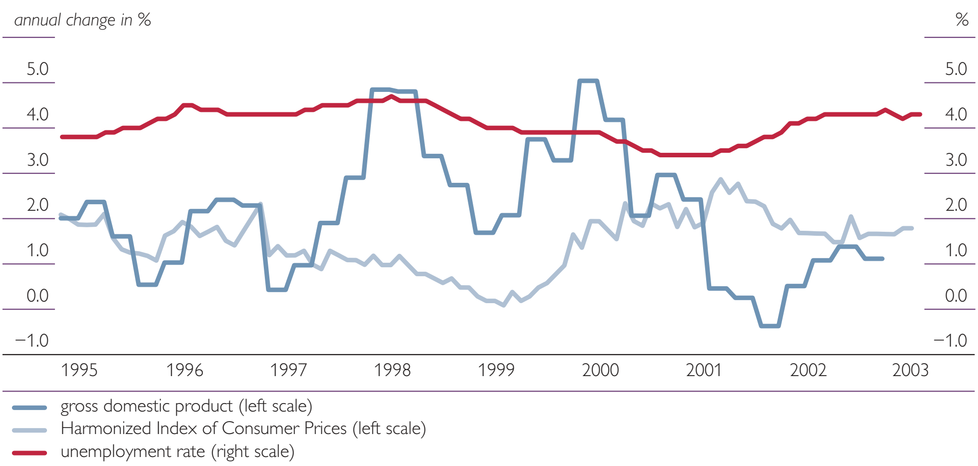
The Oil Price and the USD/EUR Exchange Rate over Time



Source: WIFO, Datastream.

Chart 7

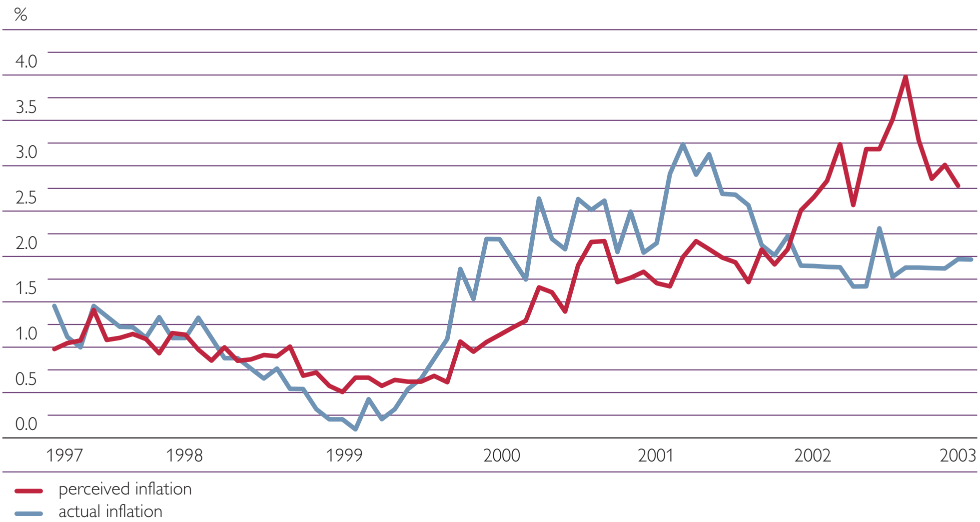
Austria – Economic Indicators



Source: Eurostat, ECB, WIFO.

Chart 8

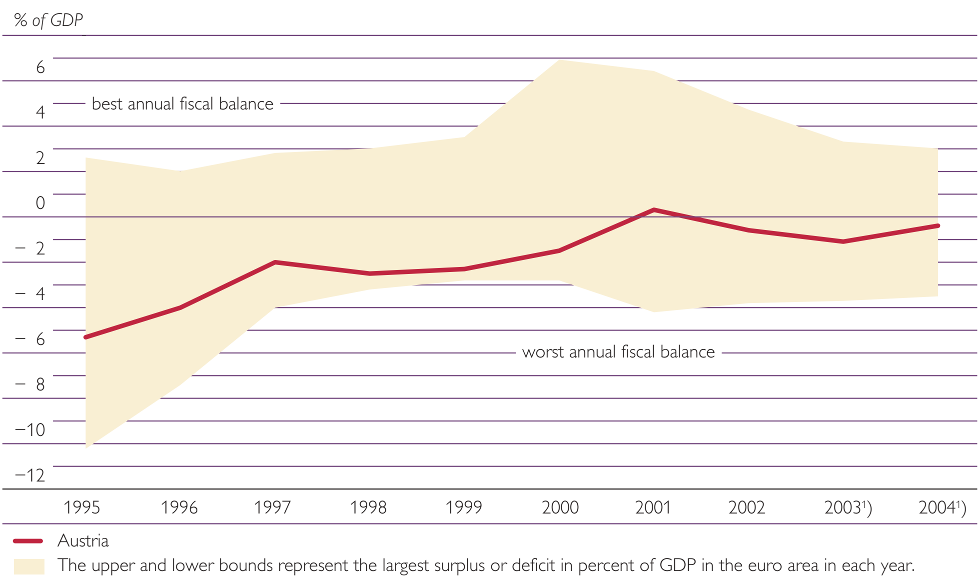
Actual and Perceived Inflation in Austria



Source: Eurostat, OeNB.

Chart 9

Government Net Lending or Net Borrowing in the Euro Area[1])

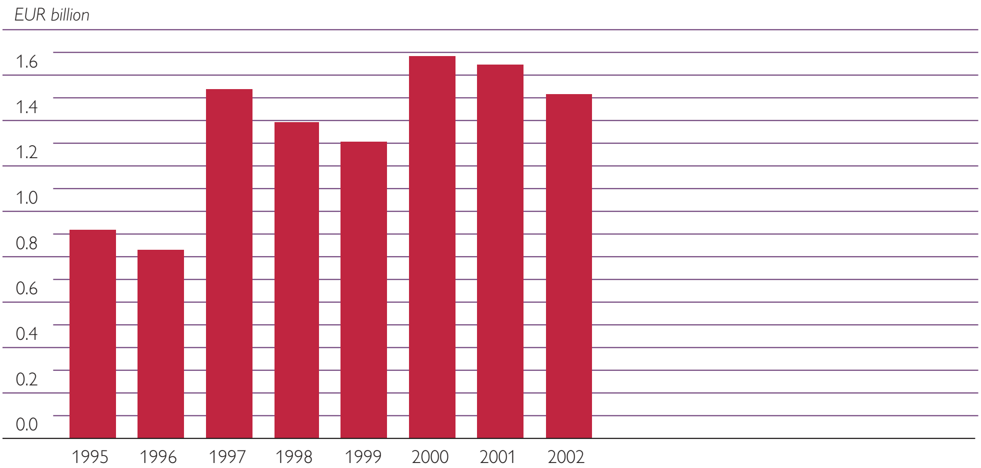


Source: Austria until 2002: Statistics Austria; 2003 to 2004. 2003 to 2004: Spring 2003 forecast of the European Commission; euro area until 1997: Data Pocket Book/Eurostat; from 1998: European Commission.

[1]) Spring Forcast of the European Commission.

Chart 10

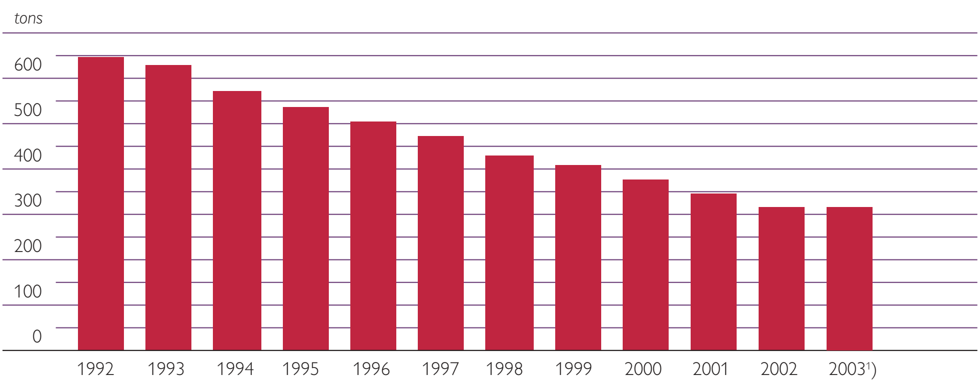
Operating Profit



Source: OeNB.

Chart 11

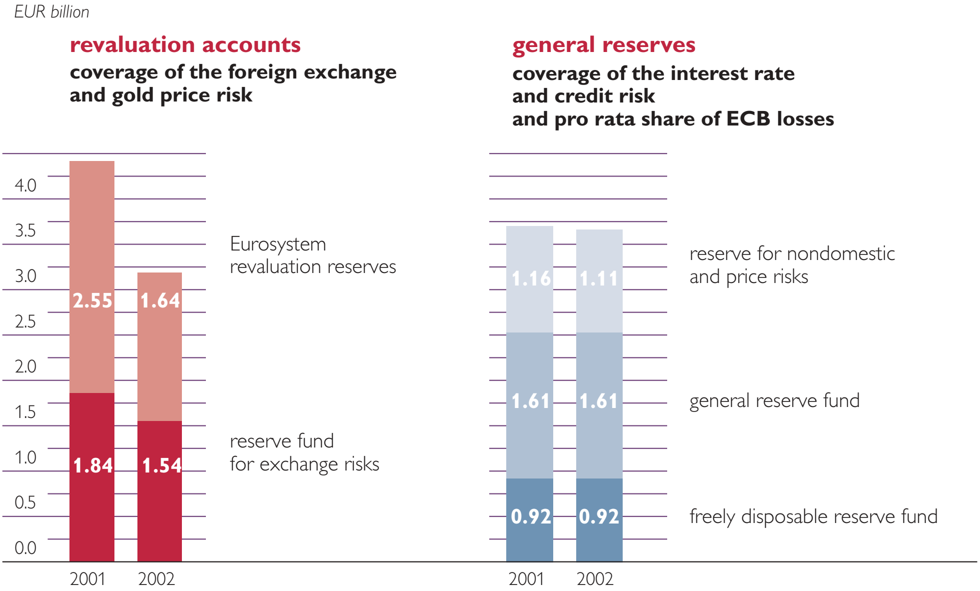
The OeNB's Gold Holdings



Source: OeNB.
[1]) As at the end of April 2003.

Chart 12

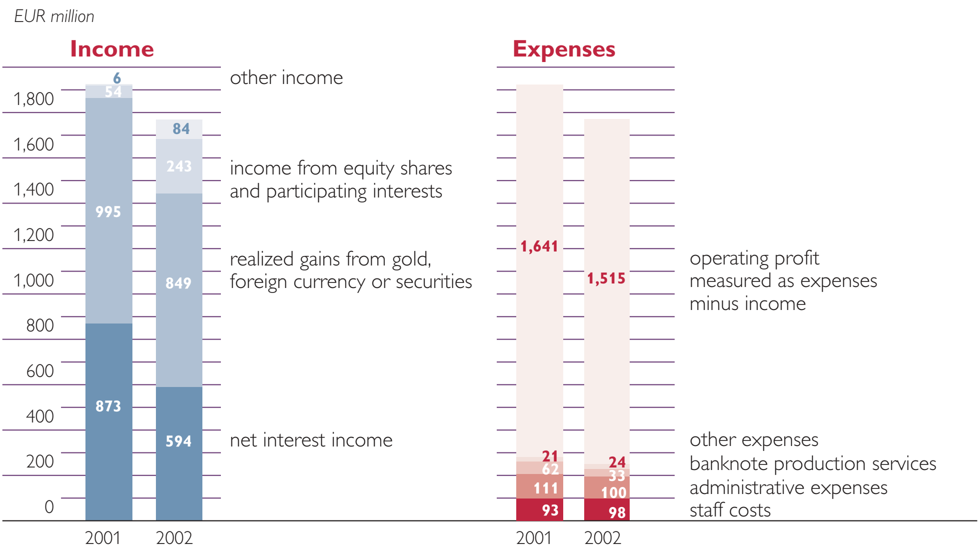
The OeNB's Reserves



Source: OeNB.

Chart 13

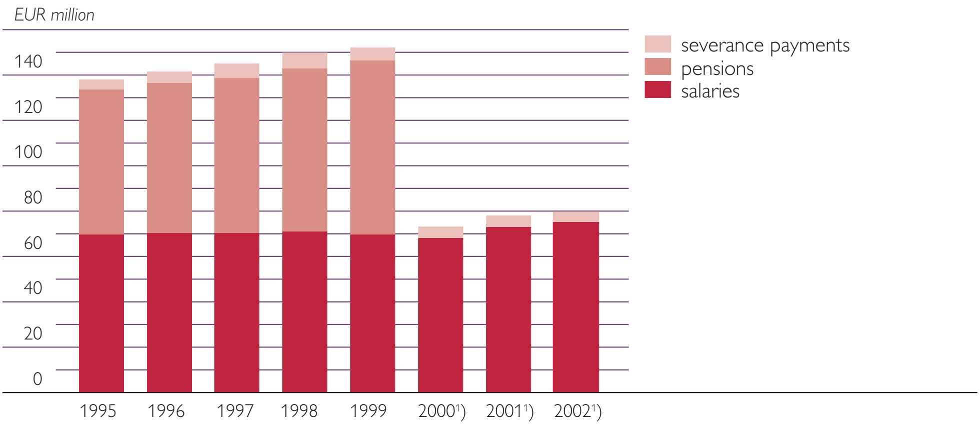
Income and Expenses



Source: OeNB.

Chart 14

The OeNB's Staff Costs

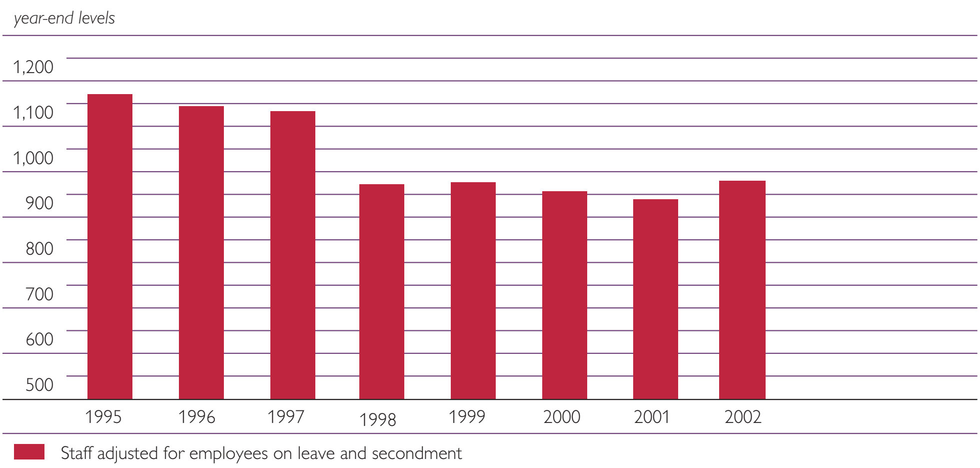


Source: OeNB.

[1]) Starting with the financial statements for 2000 the OeNB has paid retirement benefits out of its pension reserve.

Chart 15

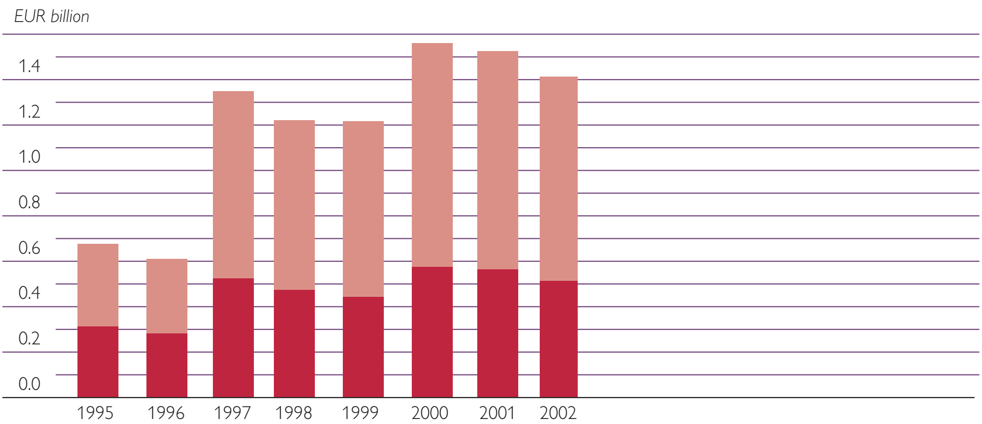
Staff Developments at the OeNB



Source: OeNB.

Chart 16

Central Government's Share of the OeNB's Profit



corporate income tax
central government's share of profit under the provisions of the Nationalbank Act

Source: OeNB.

Chart 17

The Hierarchy of OeNB Goals in the Eurosystem

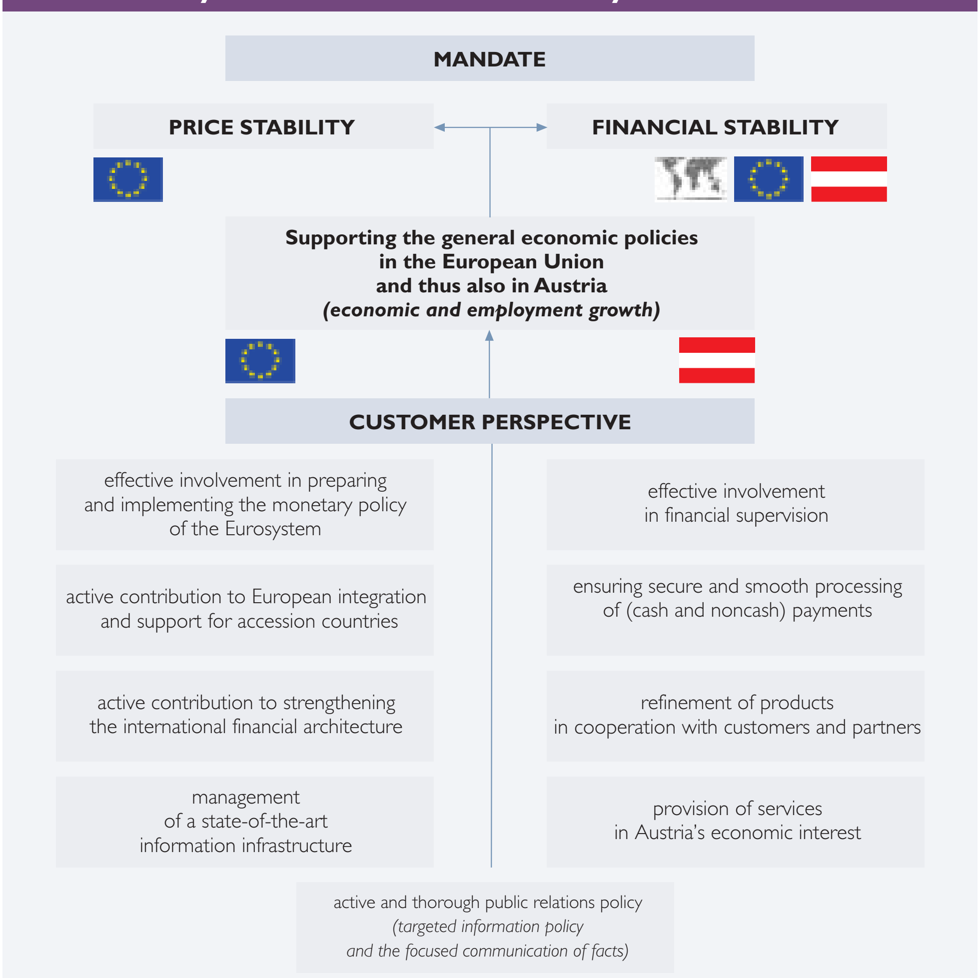


Chart 18

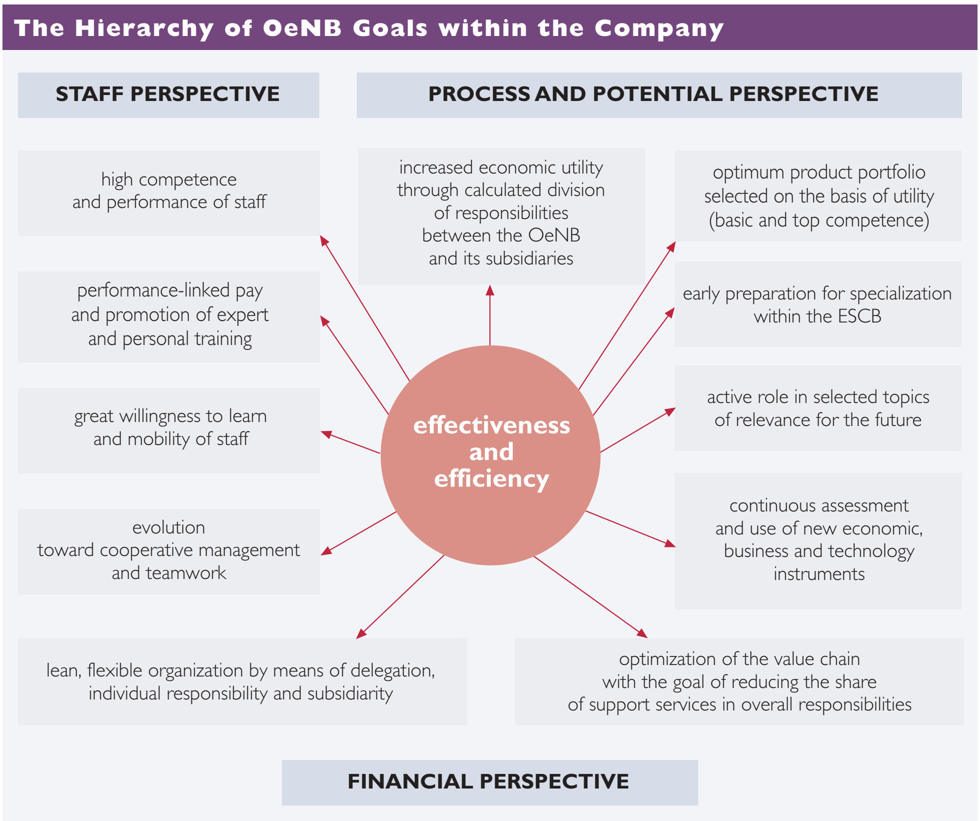


Chart 19

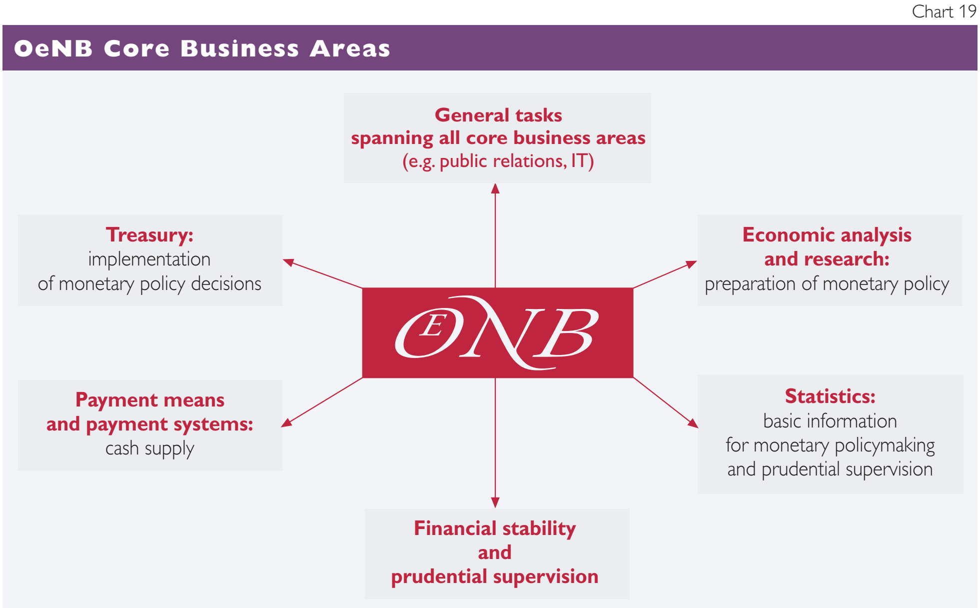
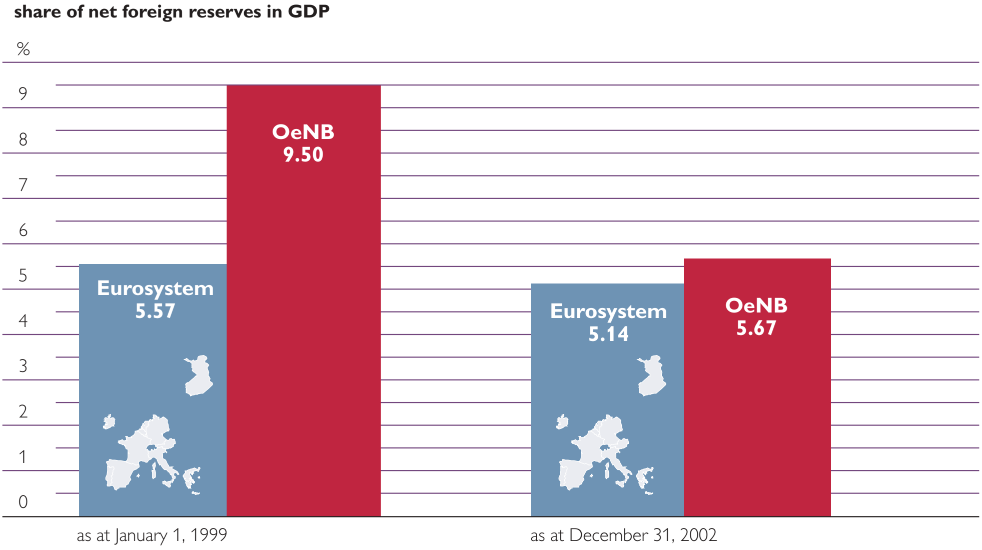


Chart 20

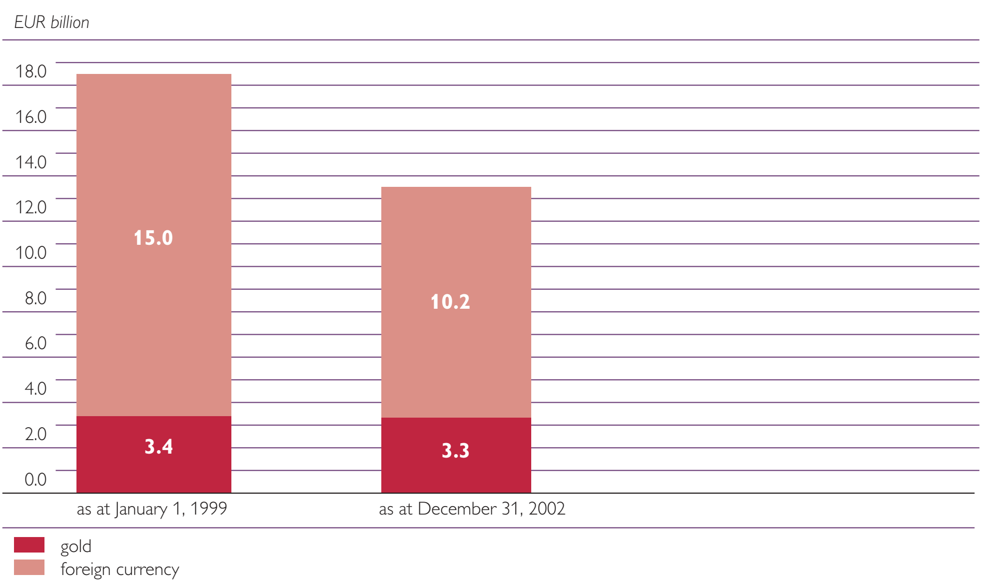
Key Figures – The OeNB Compared to the Eurosystem



Source: OeNB, ECB.

Chart 21

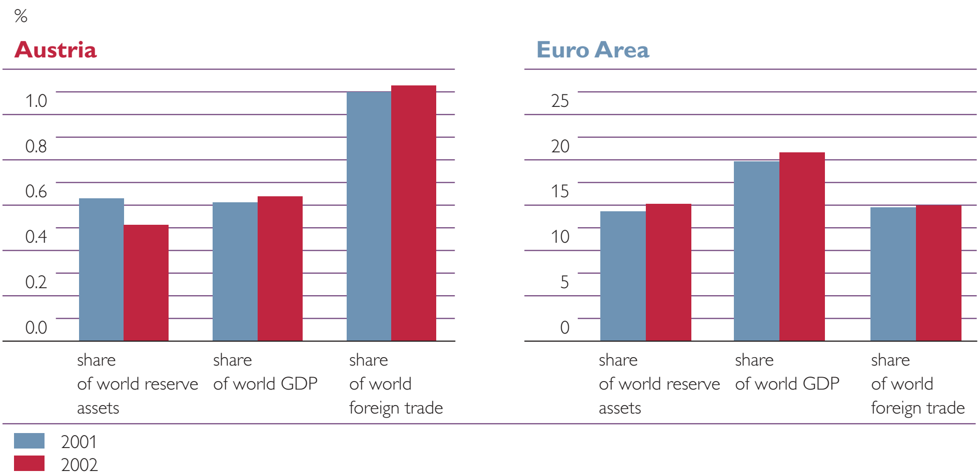
Net Foreign Reserves



Source: OeNB.

Chart 22

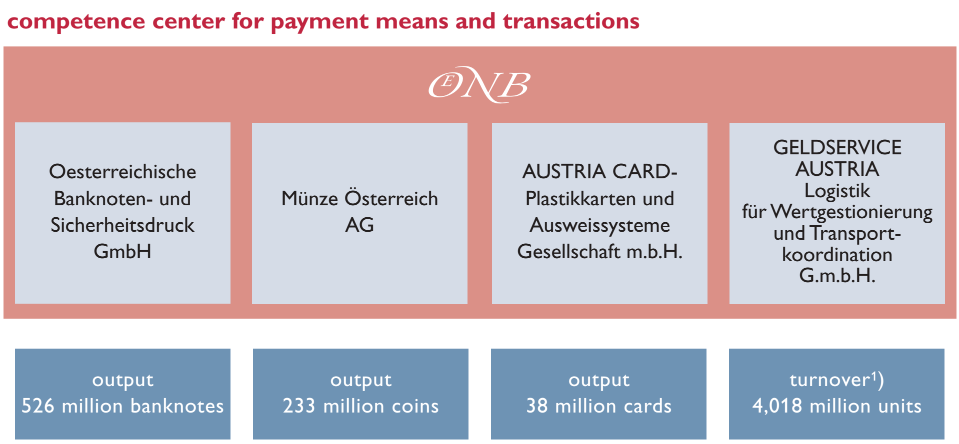
Key Figures – Austria and the Euro Area



Source: IMF, OeNB.

Chart 23

The OeNB and Its Subsidiaries in 2002



Source: OeNB and subsidiaries.

[1]) Coins or banknotes withdrawn or issued.

Chart 24

The OeNB and Its Subsidiaries

One-stop Shop for Payment Services

banknotes | coins | cards | electronic money

- **research and development**
- **production**
- **distribution and recycling**
- **counterfeit deterrence and information**
- **technology consultancy**

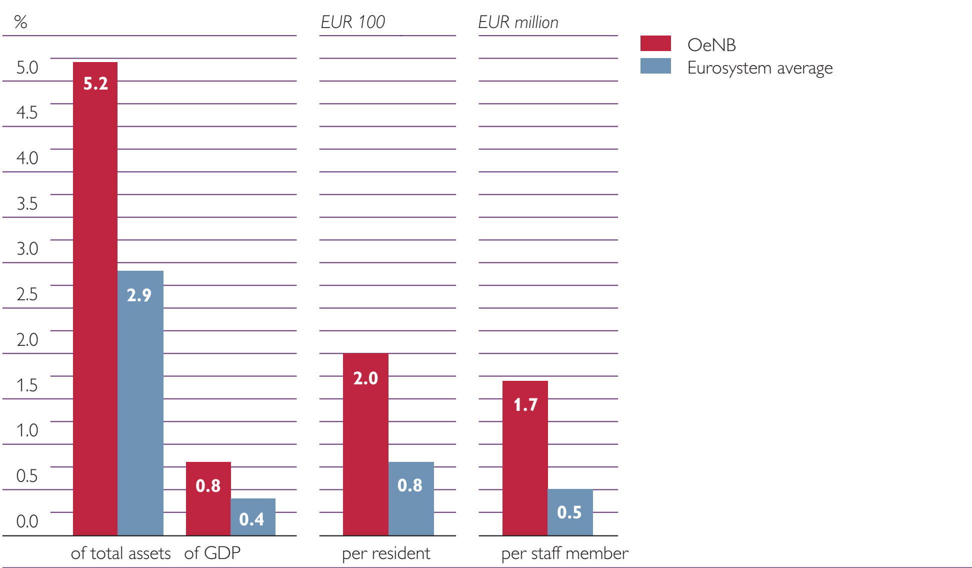
security | quality | efficiency

Source: OeNB and subsidiaries.

Chart 25

Key Figures – The OeNB Compared to the Eurosystem Average

operating profit in 2001

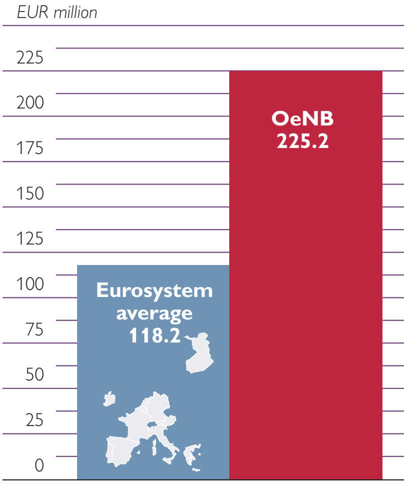


Source: NCBs' annual reports, Eurostat and IMF.

Chart 26

Key Figures – The OeNB Compared to the Eurosystem Average

staff productivity in 2001
GDP per staff member in the euro area countries

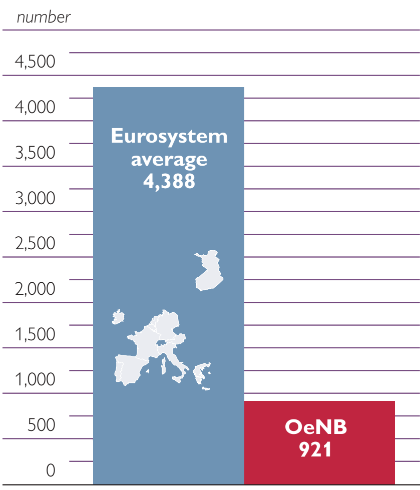


Source: NCBs' annual reports, Eurostat.

Chart 27

Key Figures – The OeNB Compared to the Eurosystem Average

staff size in 2001

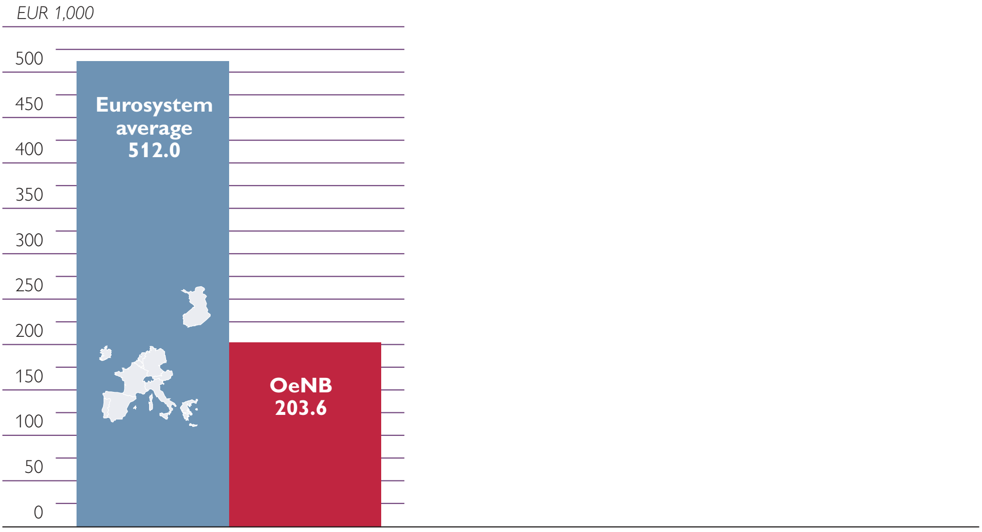


Source: NCBs' annual reports.

Chart 28

Key Figures – The OeNB Compared to the Eurosystem Average

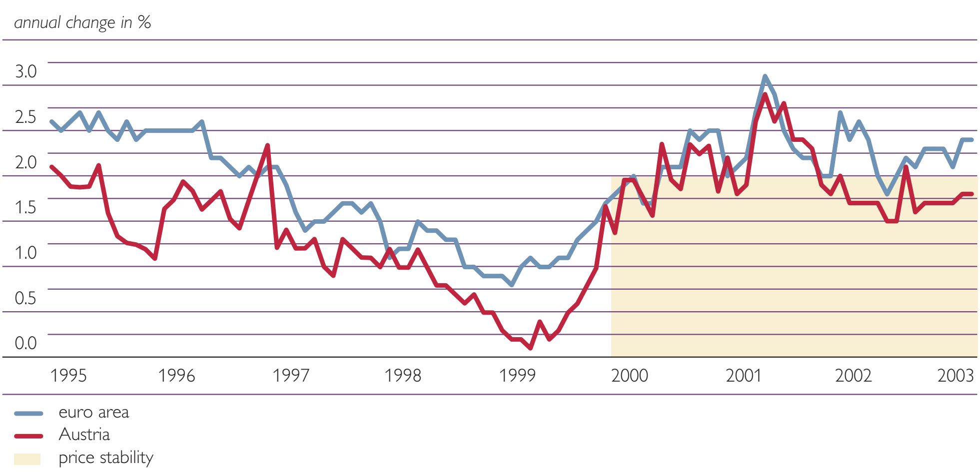
staff and administrative expenses in 2001



Source: NCBs' annual reports.

Chart 29

The Euro Area's Harmonized Consumer Price Index



Source: Eurostat, ECB.

Chart 30

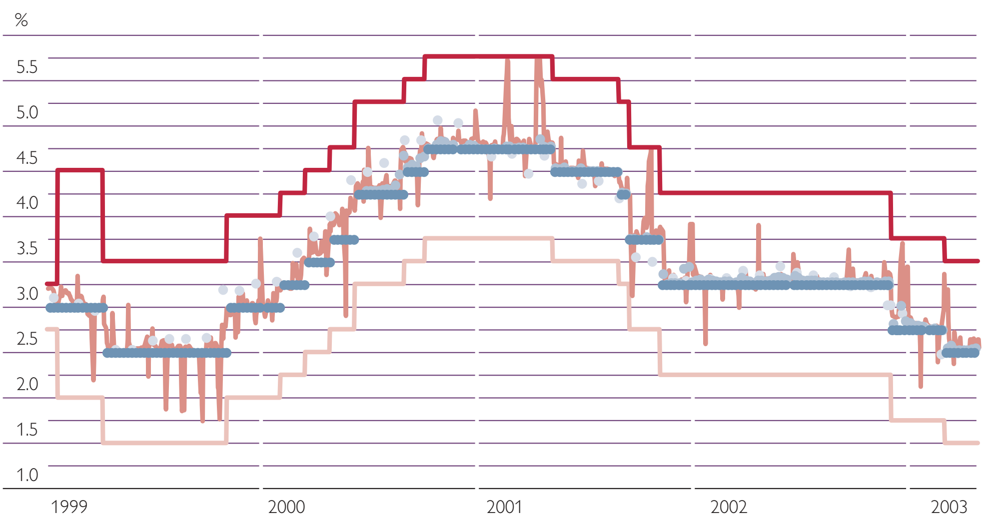
Development of the USD/EUR Exchange Rate and Real-Effective Exchange Rate of the Euro

development of the USD/EUR exchange rate
real-effective exchange rate of the euro[1])

Source: ECB, BIS.
[1]) In CPI terms, rebased.

Chart 31

Interest Rates in the Euro Area[1])

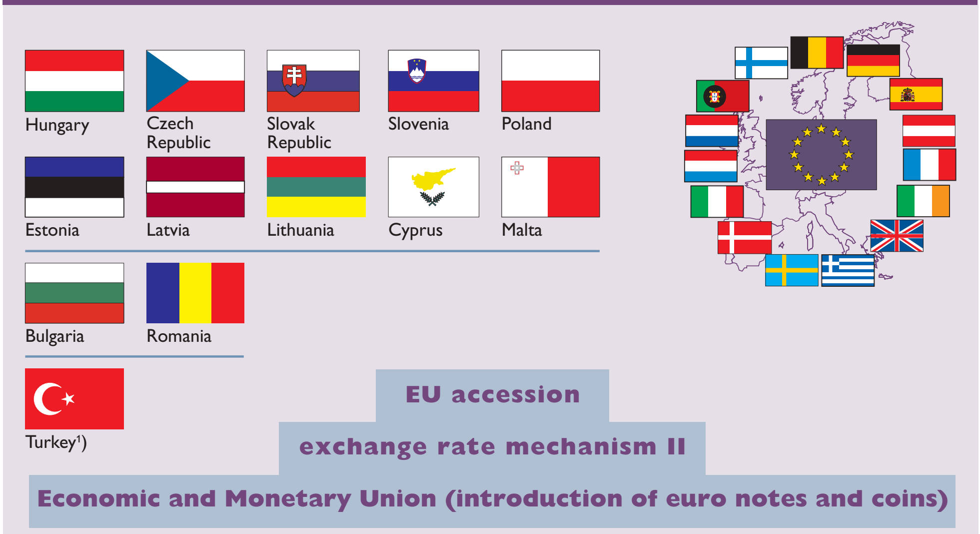


marginal lending facility
EONIA
deposit facility
marginal allotment rate (variable rate tender) in longer-term refinancing operations (LTROs)
marginal allotment rate (variable rate tender) in main refinancing operations (MROs)
allotment rate (fixed rate tender) or minimum bid rate (variable rate tender) in MROs

Source: ECB.
[1]) As of May 2, 2003.

Chart 32

Enlargement of the European Union



[1]) *The European Union has not yet started accession negotiations with Turkey.*