FISKALRAT
Austria

FISCAL RULES COMPLIANCE REPORT 2016–2021 (MAY 2017) – SUMMARY

Broad compliance with fiscal rules in 2016 despite rising deficit; further compliance will require further efforts

In 2016, **Austria's general government**[1] **deficit ratio rose** to 1.6% of GDP, i.e. to a level slightly above the government's fall 2016 forecast (2015: 1.1% of GDP). However, Austria still **complied with the relevant fiscal rules in nominal and real terms** (Maastricht deficit rule, debt rule and expenditure rule in real terms) – with the exception of the structural deficit rule, with which it failed to fully comply. Austria **missed** the medium-term objective (MTO) of achieving a **structurally balanced budget** of -0.5% of GDP by **0.1 percentage point,** even if a **temporary allowance granted under the "unusual event" clause** (regarding net extra costs originating directly from refugee migration and counter-terrorism measures, totaling some 0.4% of GDP) is taken into account. While this shortfall was within the normal margin of tolerance of 0.25 percentage points, this margin of tolerance does not apply, as interpreted by the European Commission, when the flexibility clause is invoked. The Fiscal Advisory Council considers such an interpretation of the Stability and Growth Pact to lack economic substance.

The **stability program update submitted by the Austrian government** in April 2017 envisages **broad compliance with the structural budget rules** of the EU-wide fiscal framework **from 2017 to 2021** subject to the application of the flexibility clause. At the same time, Austria is expected to **fail to comply with** the **expenditure rule** limiting the growth of public spending – among other things due to discretionary revenue shortfalls, which drive up spending under the expenditure rule. In contrast, Austria **generously complies with all fiscal rules** the nonfulfillment of which can **trigger an excessive deficit procedure** (Maastricht deficit rule of no more than 3% of GDP; reduction of the debt ratio).

Compared with the government's stability program update, the **Fiscal Advisory Council's spring forecast** sees **a somewhat stronger reduction of the deficit in 2017** but **a slight increase in 2018** (Maastricht deficit 2017: 0.9% of GDP; 2018: 1.0% of GDP). This increase is expected despite signs of **robust economic activity** in both 2017 and 2018 and even though **interest expenditure** on government debt is set to **decline** by a considerable amount (Fiscal Advisory Council estimate: –EUR 1.2 billion) following the rollover of debt to lower-yielding instruments. However, in the absence of a **federal fiscal framework** update for 2018, which is a key pillar for assessing the fiscal outlook at the federal level, the picture is not complete. The Fiscal Advisory Council's spring forecast for 2018 yields a **"significant" breach of the spending rule**[2] and a **slight deviation from the structural budget objective (subject to application of the unusual event clause)**. Austria is expected to run a **structural deficit** of 0.7% of GDP in 2017 and 0.9% of GDP in 2018 when the "unusual event" provisions for net extra costs originating from refugee migration and counter-terrorism measures are not used, versus 0.3% of GDP in 2017 and 0.6% of GDP in 2018 when the "unusual event" provisions are used. Regarding the **primary surplus,** the Fiscal Advisory Council expects a ratio of 1.0% of GDP for 2017 and 0.7% of GDP for 2018.

The spring forecast of the Fiscal Advisory Council would imply that in the spring of 2019 the European Commission may use the **early warning mechanism** under the **preventive arm of the SGP** ("significant deviation procedure") for 2018, given that from today's perspective both the structural deficit and the government spending increase exceed the respective reference values. In 2018 public spending will be driven up by a number of **investment initiatives** adopted by the government (such as the expansion of

---

1 Central, state and local governments and social security funds as defined in the European System of Accounts (ESA 2010).

2 This assessment is based on a comparatively low reference value in 2017 for public spending growth given the deviation from the MTO (0.7% in real terms) as well as a relatively sharp increase in net spending in 2018 (2.2% in real terms compared with 2017, reflecting higher discretionary spending and revenue shortfalls).

broadband infrastructure, a municipal investment program, a set of measures to boost business start-ups and the development of railroad infrastructure; adding up to additional spending of EUR 0.6 billion). At the same time the tax intake is affected by a range of measures including **cuts of nonwage labor costs** (decrease in contributions to the family burden equalization fund, creating additional revenue shortfalls of EUR 0.5 billion) as well as **one-off** revenue-related **developments** (payments under the revenue sharing framework related to the bank tax frontloaded to 2017). Moreover, the **Austrian government's work program for 2017–2018 released in January 2017** specifies a number of measures – including **bonus payments for hiring eligible individuals** (equivalent to 50% of nonwage labor costs for new hires during the first three years) and the **50+ employment initiative at the municipality level for 20.000** long-term unemployed – without having identified relevant cost-offsetting measures. In its forecast, the Fiscal Advisory Council assumes that the discretionary spending plans of the government will increase the budget deficit by 0.2% of GDP in 2017 and by another 0.5% in 2018.

According to the Fiscal Advisory Council's spring forecast, the intended budgetary path is set to **deviate from EU requirements under the preventive arm of the SGP** in **2018**, unless government **measures to contain spending growth** become effective in 2018. In the opinion of the Fiscal Advisory Council it would be necessary to include the spending plans outlined in the government's work program for 2017–2018 in the fiscal framework and to make sure that the underlying cost will be compensated fully by offsetting measures – as planned.

Both the stability program update as well as the Fiscal Advisory Council's forecast are based on the WIFO outlook of March 2017 projecting real growth rates of 2.0% for 2017 and 1.8% for 2018. **Forecast risks on the upside** relate to the pace of economic growth and labor market developments. **Downside fiscal risks** include – apart from the climate of **geopolitical uncertainty** combined with rising protectionist sentiment – above all **the impact of commitments that may be made prior to the parliamentary elections scheduled** for October 2017 ("pre-election gifts"). Legislative proposals with medium- to long-term economic and financial consequences **should be adopted only on the basis of impact assessments**.

To ensure compliance with fiscal requirements in years to come, Austria must continue to **implement stability-oriented fiscal policies that are supportive of growth** while **reinforcing structural reform**. The Fiscal Advisory Council supports all initiatives that are expected to support a **sustained growth of potential output** and **employment** (above all structural reforms of the education system, public infrastructure investment as well as measures to reduce the tax burden on labor and ease small business regulations). These measures should be accompanied by **countercyclical fiscal policies** aimed at achieving budget surpluses in economically good times (positive output gap) and budget overspending in economically bad times (negative output gap). With the economy in recovery, there is currently no need for additional fiscal stimulus. At the same time, it would be advisable to support the recovery by ensuring a stable policy framework.

Top priorities include measures to enhance **efficiency**, especially in areas in which **central, regional and local authorities** share responsibilities, such as **education, health care, long-term care, local public transport** as well as the government's objectives of **reallocating intergovernmental functions and raising the effective retirement age**. Continuing with cost containment in **health care and long-term care** agreed in the Fiscal Sharing Agreement of 2017 (limiting additional spending growth in the health care sector to 3.2% by 2021 (starting with 3.6% 2017), and in the long-term care sector to 4.6%) requires efficiency-enhancing measures, such as shifting health services from inpatient to outpatient care, offering more mobile nursing services, reconciling medication across the continuum of care, offering additional measures to harmonize supply structures and quality as well as improving transparency in the field of health and long-term care. With regard to the **education system,** the negotiated reform project designed to strengthening school autonomy by supporting school cluster development and integrated forms of all-day schooling should be implemented without delay. With regard to local public transport, increased cooperation across municipalities and mandatory standardized tenders would be expected to cut costs and improve supply.

It should also be emphasized that **efforts for the fast social integration of people who have been granted asylum in Austria** may reduce the total requirement public spending on integration. These efforts would include, for instance, providing trainings, facilitating access to the labor market, providing increased incentives for integration, implementing uniform standards across all provinces regarding means-tested minimum benefits and integration measures. However, progress in implementing such measures **has been limited so far**.

Moreover, with a view to strengthening the basis for developing Austria's stability program, the Fiscal Advisory Council calls upon the government to enhance its **medium-term strategic budgeting process in the spring** by implementing **revenue and expenditure tracking** and **impact-oriented budget management**. Such information enhances transparency and reinforces the strategic orientation of budgeting. The legal framework for budgeting at the federal government level is currently being evaluated by IMF and OECD staff experts. Medium-term planning ought to focus above all on the **strategic orientation** of economically **significant spending areas**. The current **stability program update** does not provide any **information** on the budgetary impact of **individual spending plans of central, regional and local government authorities and the social security funds**, which ought be quantified in the form of tables (based on ESA 2010). There is also a need for meaningful transition tables between administrative accounts and ESA 2010 data.

The "Fiscal rules compliance report for 2016 to 2021" provides information about **the Austrian government's medium-term budget performance** and about **the general government's level of compliance with EU-wide fiscal rules**. To ensure the best possible assessment of Austria's current fiscal position, the Fiscal Advisory Council produced its **own budget forecasts for 2017 and 2018** and compared the results with the **government's stability program update** of April 2017.