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Assessment of the 2018 Stability Programme for

Austria

(Note prepared by DG ECFIN staff)

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1. INTRODUCTION

On 21 March 2018, Austria submitted its 2018 Stability Programme (hereafter called Stability Programme), covering the period 2017-2022 together with the updated Draft Budgetary Plan 2018 in one single document.[1] The parliament adopted the programme on 19 April 2018. The programme is based on the Federal Budgetary Framework Law 2018 to 2021 (BFRG), which sets legally binding expenditure ceilings for the next four years, for the federal government's five main spending categories.

Austria is currently subject to the preventive arm of the the Stability and Growth Pact (SGP) and should preserve a sound fiscal position which ensures compliance with the Medium-Term Budgetary Objective (MTO). As the debt ratio was 81.3% of GDP in 2013 (the year in which Austria corrected its excessive deficit), exceeding the 60% of GDP reference value, Austria is also subject to the debt reduction benchmark during the three years following the correction of the excessive deficit. In this period it should ensure sufficient progress towards compliance with the debt reduction benchmark. After the transition period, as of 2017, Austria is expected to comply with the debt reduction benchmark.This document complements the Country Report published on 7 March 2018 and updates it with the information included in the Stability Programme.

Section 2 presents the macroeconomic outlook underlying the Stability Programme and provides an assessment based on the Commission 2018 spring forecast. The following section presents the recent and planned budgetary developments, according to the Stability Programme. In particular, it includes an overview on the medium term budgetary plans, an assessment of the measures underpinning the Stability Programme and a risk analysis of the budgetary plans based on Commission forecast. Section 4 assesses compliance with the rules of the SGP, including on the basis of the Commission forecast. Section 5 provides an overview on long term sustainability risks and Section 6 on recent developments and plans regarding the fiscal framework. Section 7 provides a summary.

2. MACROECONOMIC DEVELOPMENTS

The macroeconomic scenario of the Stability Programme assumes GDP growth to peak at 3.2% in 2018 and subsequently gradually slow down, reaching 1.5% in 2022. Domestic demand is expected to be the key driver of growth, with robust private consumption mildly fading after reaching a peak in 2018, as well as strong but decreasing investment growth. Net external trade is projected to contribute positively to GDP growth in the coming years with exports growing noticeably stronger than imports in 2018 and 2019, and at a similar pace from 2020 till 2022.

These projections are more favourable than those presented in the 2017 Stability Programme (which projected GDP growth at 1.8% in 2018 and 1.7% in 2019) and are in line with the macroeconomic scenario underlying the assessment of the 2018 updated DBP. For 2018, the improved outlook is driven by a stronger than expected increase of GDP in 2017, as well as stronger private consumption and net contribution of trade in 2018. For 2019-2022, while keeping the same trend, the gradual slowdown of the economy starts from higher levels than reported in the 2017 Stability Programme, given the significantly higher expected levels for real GDP growth and its components in 2018. Private consumption is expected to ease only

[1] The English translation of the Stability Programme was submitted on 24 April.

slowly, while investment and the net contribution of trade to GDP growth are projected to decline more rapidly.

The output gaps as recalculated by the Commission based on the information in the Programme, following the commonly agreed methodology, suggest an improvement of the cyclical position in 2017, almost closing the gap. The recalculated output gap is set to turn positive over 2018-2021, widening until 2019 and subsequently narrowing to finally turn negative in 2022. Over 2018-2019, the output gap profile is largely consistent but somewhat more favourable than the Commission 2018 spring forecast.

The real GDP growth projections for 2018 are more favourable than the Commission 2018 spring forecast, as the Commission expects weaker dynamics in private consumption and exports, while projecting higher investments and a slightly more pronounced impact of net exports. The Commission forecast also assumes somewhat lower but comparable wage growth in 2018 and 2019, and lower employment growth in 2018. For 2018, headline HICP inflation as projected by the Commission is above the levels reported in the 2018 Stability Programme. Overall, the 2018 Austrian Stability Programme is based on favourable macroeconomic assumptions in 2018 and on plausible assumptions thereafter.

Table 1: Comparison of macroeconomic developments and forecasts

	2017		2018		2019		2020	2021	2022
	COM	SP	COM	SP	COM	SP	SP	SP	SP
Real GDP (% change)	2.9	2.9	2.8	3.2	2.2	2.2	1.9	1.6	1.5
Private consumption (% change)	1.4	1.4	1.6	1.8	1.4	1.6	1.6	1.4	1.4
Gross fixed capital formation (% change)	4.8	4.8	3.7	3.5	2.4	2.5	2.1	1.8	1.7
Exports of goods and services (% change)	5.7	5.7	5.2	5.5	4.3	4.5	3.8	3.4	3.2
Imports of goods and services (% change)	5.4	5.4	3.9	4.6	3.4	3.8	3.7	3.3	3.1
Contributions to real GDP growth:									
- Final domestic demand	2.1	2.1	2.0	2.0	1.5	1.7	1.5	1.4	1.3
- Change in inventories	0.4	0.5	0.0	0.5	0.0	0.0	0.1	0.0	0.0
- Net exports	0.4	0.4	0.8	0.6	0.6	0.5	0.2	0.2	0.2
Output gap[1]	-0.2	-0.3	0.6	0.7	0.7	0.9	0.5	0.1	-0.3
Employment (% change)[2]	1.7	1.7	1.5	1.7	1.2	1.1	1.3	1.3	1.0
Unemployment rate (%)	5.5	5.5	5.2	5.2	5.0	5.0	5.0	5.1	5.1
Labour productivity (% change)[2]	1.2	1.2	1.3	1.4	1.0	1.1	0.5	0.6	0.9
HICP inflation (%)[3]	2.2	2.1	2.1	1.9	1.9	1.9	1.9	1.9	1.9
GDP deflator (% change)	1.5	1.5	1.7	1.7	1.7	1.8	1.8	1.9	1.9
Comp. of employees (per head, % change)[2]	1.6	1.8	2.5	2.6	2.5	2.7	2.2	2.2	2.2
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	1.9	2.1	2.0	2.3	2.2	2.6			

Note:

[1]In % of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

[2]The SP figures were provided by the Austrian authorities and are in line with the Commission definition of persons employed. They differ from the figures in the SP, which correspond to the national definition.

[3]The inflation presented in the SP represents the national CPI.

Source :

Commission 2018 spring forecast (COM); Stability Programme (SP).

3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS

3.1. DEFICIT DEVELOPMENTS IN YEAR 2017 AND 2018

In 2017, the general government headline deficit improved markedly, standing at 0.7% of GDP, compared to the projection of the 2017 Stability Programme (1.0% of GDP) While both the expenditure and the revenue ratio have been revised downwards with respect to the 2017 Stability Programme, expenditures decreased stronger (49.3% compared to 50.6% of GDP). On the back of stronger GDP developments (2.9% compared to 2.0% year over year), this is mainly the result of lower expenditures for social benefits in light of positive labour market developments as well as lower interest expenditures as well as stronger than expected real GDP growth (2.9% compared to 2.0% of GDP). On the revenue side, strong employment and payroll developments increased the taxable base of personal income taxes and social security contributions. However, despite strong private consumption, revenues from indirect taxes have increased at a pace slower than expected based on the evolution of these tax bases due to cuts in employers' contributions to the Family Equalisation Fund.

In 2018, the Stability Programme projects the headline deficit to narrow further to 0.4% of GDP, which halves the projection of both the 2017 Stability Programme and the no-policy-change DBP. As compared to the 2017 Stability Programme, this narrowing is mainly due to significant upward revisions of projected nominal GDP growth (4.9% compared to 3.3%) as well as downward revised projections of social benefits due expected improvements on the labour market (unemployment rate projection decreased from 5.9% to 5.2%). However, when comparing the no-policy-change DBP to the 2018 Stability Programme, part of the reduced expenditure projection for 2018 is also due to the fact that several deficit-increasing policy measures implemented by the previous government have been suspended or reduced when the new government took office (e.g., Employment Bonus, Investment Premiums, Municipal Investment Programme), allowing for the restrictive budgetary path the Stability Programme relies on.

3.2. MEDIUM-TERM STRATEGY AND TARGETS

The stated objective of the Stability Programme is to achieve and retain a fiscal position that is compliant with national commitments as well as the provisions of the SGP, which includes meeting the MTO of -0.5% of GDP both in 2018 and 2019. Public expenditure shall grow less than nominal GDP growth, while budgetary leeways provided e.g., by the restructuring of the banking sector, shall be used to finance tax reliefs aimed at lowering the tax ratio to 40% of GDP. The targeted budgetary path of the Stability Programme is to improve the headline deficit from 0.7% of GDP in 2017 to a balanced position in 2019 and budgetary surplus of 0.4% of GDP by the end of the programme period. As a result, the time profile of the adjustment in the headline balance is frontloaded with higher fiscal efforts in the first two years until a balanced position is reached and lower efforts when entering into surplus . According to the authorities, this would allow the structural balance to meet the MTO from 2019 onwards, reaching a balanced position as of 2021.

Table 2: Composition of the budgetary adjustment

(% of GDP)	2017	2018		2019		2020	2021	2022	Change: 2017-2022
	COM	COM	SP	COM	SP	SP	SP	SP	SP
Revenue	**48.4**	**48.0**	**48.1**	**47.8**	**47.8**	**47.7**	**47.4**	**47.3**	**-1.3**
of which:									
- Taxes on production and imports	14.1	13.9	13.8	13.8	13.6	13.5	13.3	13.2	-0.9
- Current taxes on income, wealth, etc.	13.0	13.1	13.2	13.2	13.2	13.2	13.1	13.2	0.1
- Social contributions	15.2	15.1	15.0	15.0	15.0	14.9	14.9	14.9	-0.3
- Other (residual)	6.1	5.9	6.2	5.8	6.1	6.1	6.1	6.1	-0.3
Expenditure	**49.1**	**48.5**	**48.5**	**47.9**	**47.8**	**47.6**	**47.2**	**46.9**	**-2.4**
of which:									
- Primary expenditure	47.2	46.9	47.0	46.4	46.4	46.2	45.9	45.7	-1.8
of which:									
Compensation of employees	10.6	10.4	10.4	10.4	10.4	10.3	10.3	10.2	-0.3
Intermediate consumption	6.1	6.0	6.1	5.8	6.0	6.0	5.9	5.9	-0.4
Social payments	22.2	22.0	22.2	21.8	22.0	21.9	21.9	21.9	-0.6
Subsidies	1.4	1.5	1.5	1.5	1.5	1.4	1.3	1.3	-0.1
Gross fixed capital formation	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	0.1
Other (residual)	3.8	4.0	3.8	4.0	3.6	3.6	3.4	3.4	-0.3
- Interest expenditure	1.8	1.6	1.6	1.5	1.5	1.4	1.3	1.2	-0.6
General government balance (GGB)	**-0.7**	**-0.5**	**-0.4**	**-0.2**	**0.0**	**0.1**	**0.2**	**0.4**	**1.1**
Primary balance	**1.1**	**1.2**	**1.2**	**1.3**	**1.5**	**1.5**	**1.5**	**1.6**	**0.5**
One-off and other temporary measures	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
GGB excl. one-offs	**-0.7**	**-0.5**	**-0.4**	**-0.2**	**0.0**	**0.1**	**0.2**	**0.4**	**1.1**
Output gap[1]	-0.2	0.6	0.7	0.7	0.9	0.5	0.1	-0.3	0.0
Cyclically-adjusted balance[1]	-0.6	-0.8	-0.8	-0.6	-0.5	-0.2	0.2	0.6	1.1
Structural balance[2]	**-0.6**	**-0.8**	**-0.8**	**-0.6**	**-0.5**	**-0.2**	**0.2**	**0.6**	**1.1**
Structural primary balance[2]	1.2	0.8	0.7	0.9	1.0	1.2	1.5	1.8	**0.5**

Notes:

[1]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission on the basis of the programme scenario using the commonly agreed methodology.

[2]Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

Source:

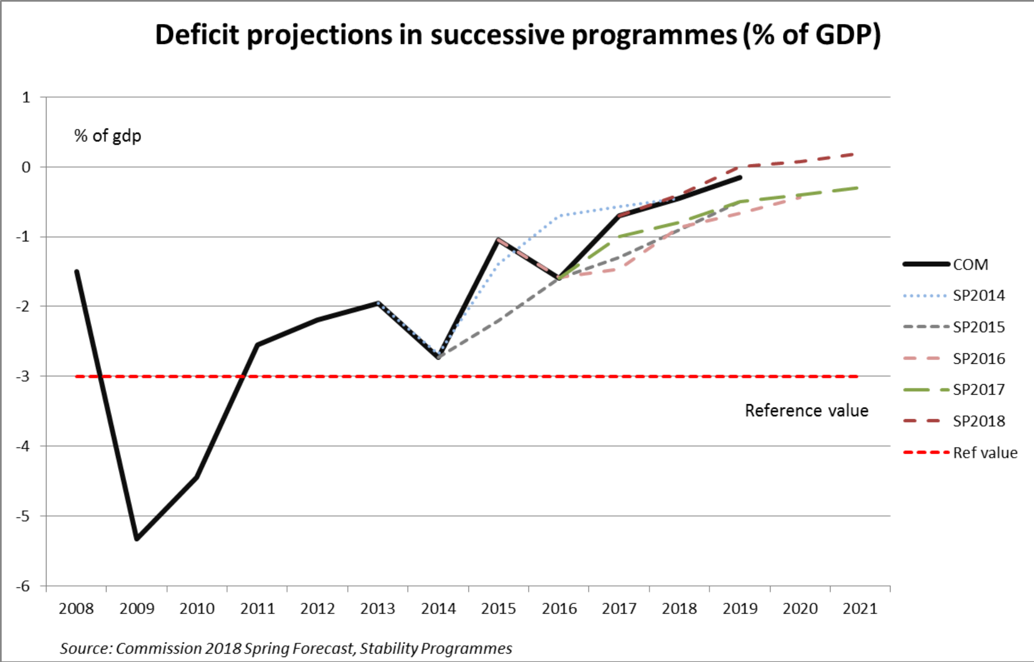
Stability Programme (SP); Commission 2018 spring forecasts (COM); Commission calculations.

The projected improvement of the headline deficit to 0.4% of GDP in 2018 benefits from a strong macroeconomic environment with public expenditures decreasing more than revenues.[2] The affected spending categories are the compensation of employees as well as interest expenditures, which are expected to decline by 0.2 percentage point of GDP, respectively. Interest payments benefit from declining public debt, which is in turn affected by the sale of assets of former state-owned banks as well as historically low average interest rates. While the budgetary share of other categories remains constant, subsidies increase by 0.1% of GDP due to several discretionary measures implemented by the previous government (e.g., Employment Bonus, Investment Premiums). Government revenues are expected to decline by

[2] Due to the fact that Eurostat validated outturn data were not yet available at the time of the submission of the Stability Programme, the 2017 data reported in the Programme do not fully match the 2017 data reported in Table 2.

0.3 percentage point of GDP. While revenues from taxes on income and wealth are projected to increase following the positive development on the labour market, social security contributions are expected to decline by 0.2 percentage point of GDP. Despite strong private consumption, revenues from indirect taxes are expected to decrease by 0.3 percentage point of GDP, which is the result of an additional cut in employers' contributions to the Family Burden Equalisation Fund (*Familienlastenausgleichsfonds*)[3] as well as the reduced stability fee for banks.

Figure 1: Government balance projections in successive programmes (% of GDP)



The general government headline deficit in 2018 is due to the deficit of the central government and somewhat mitigated by a surplus of 0.1% of GDP generated by the Federal States excluding Vienna. Municipal budgets including Vienna are expected to be balanced. Social security funds are projected to achieve a surplus of 0.1% of GDP due to the continuous positive development on the labour market, which generates higher mandatory social contributions.

While the improvement of the headline balance is borne by the positive macroeconomic environment as well as the suspension of several procyclical discretionary measures implemented by the previous government (e.g., Employment Bonus)[4], the (recalculated) structural balance[5] is projected to deteriorate to from -0.6% of GDP in 2017 to -0.8% of GDP in 2018.

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[3] The Family Burden Equalisation Fund (*Familienlastenausgleichsfonds*) provides financial support to families, including child allowances. Employer contributions to the fund were reduced by 0.4 percenateg point in 2017, and by additional 0.2 percentage point from 2018.

[4] The no-policy-change DBP, which assumed the full budgetary impact of the expansionary policy measures, projected the headline balance to stand at -0.9 of GDP in 2018.

[5] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology.

The Commission 2018 spring forecast is largely in line with the projections referred to in the Stability Programme.

In 2019, the Stability Programme projects a balanced budget position, which is the result of an even stronger decline in government expenditure as a percentage of GDP by 0.7 percentage point. Social payments are projected to decline by 0.2 percentage point, which is mainly due to decreasing expenditures for unemployment benefits as well as lower subsidy requirements for (or: out-of-the-budget funding of) the statutory pension system. In addition, intermediate consumption is expected to decrease as a percentage of GDP by 0.1 point and interest expenditure is expected to decrease further by 0.1 percentage point. Revenues are expected to decrease by 0.3 percentage point, which is again the result of reduced non-wage contributions by employers as well as the reduced stability fee for banks, that dampen revenues from indirect taxes. Despite the positive macroeconomic outlook, revenues from taxes on income and wealth are expected to remain constant as a percentage of GDP. While being positively affected by the positive labour market development, the announced implementation of a new family tax credit (Family Bonus plus) is expected to have a net budgetary impact of about EUR 1.3 billion.

Thanks to the considerable improvement of the headline balance by 0.4 percentage point to a zero deficit, the (recalculated) structural balance is expected to improve to -0.5% of GDP in 2019. The Commission 2018 spring forecast is largely in line with the projections referred to in the Stability Programme.

Over the rest of the programme period, the Stability Programme expects the headline balance to continuously improve from the balanced position in 2019 to a surplus of 0.4% of GDP in 2022. Revenues are forecast to continue declining in small increments by 0.5 percentage point overall, reaching 47.3% in 2022, while expenditure is projected to decline by almost one percentage point, reaching 46.9% of GDP. The Stability Programme explains the favourable projections pointing to the restrictive expenditure path based on structural consolidation measures. Following the projected evolution of the headline balance, the Stability Programme expects the (recalculated) structural balance to progressively improve from -0.5% of GDP in 2019 to 0.4% of GDP in 2022..

3.3. MEASURES UNDERPINNING THE PROGRAMME

Main budgetary measures

Revenue
2018
• Second reduction of employer contribution to the Family Burden Equalisation Fund (-0.1% of GDP)
2019
• Introduction of Family Bonus plus (net effect -0.2% of GDP)
2020
• Introduction of Family Bonus plus (net effect -0.1% of GDP)

• Planned tax reform (-0.3% of GDP)
• Planned tax reform (-0.2% of GDP)
Note: The budgetary impact in the table is the impact reported in the Stability Programme, i.e. by the national authorities. A positive sign implies that revenue / expenditure increases as a consequence of this measure.

Since spring 2015, Austria's budgetary documents (Stability Programmes and DBPs) did not contain the usual table quantifying in detail the expected budgetary effect of each discretionary measure. However, the current Stability Programme contains the customary table showing the no-policy-change budgetary projections, which allows tracing the expected effect of budgetary measures for different revenue and spending categories.

The measures referred to in the Stability Programme can be classified into three broad categories. Firstly, in order to allow for the restrictive expenditure path underpinning the Programme, several measures adopted under the previous government are discontinued or reduced. This affects procyclical measures such as the Employment bonus and investment premiums for entreprises but also structural measures aimed at integrating long-term unemployed, elderly as well as persons entitled to asylum and subsidiary protection in the labour market.[6] Secondly, the Programme announces a catalogue of further cost-saving measures, including the reduction of over-budgeted positions in the public administration, reduced subsidies and spending for personnel of government-owened entities, less spending in rents as well as the indexation of family allowances for children living in EU or EEA countries as well as Switzerland. According to the Programme, the total budgetary saving of all expenditure cuts described so far amounts to EUR 2.5 billion. Thirdly, the Programme mentiones several discretionary measures of the new government for 2018 and 2019 such as the reduction of contributions to the unemployment insurance for low-income earners, the re-introduction of the super-reduced VAT rate on touristic accomodations as well as the Family bonus plus. The latter provides for a personal income tax relief in the order of EUR 1.5 billion over 2019 and 2020 while abolishing, in turn, the deductibility of child care costs and the existing child allowance. Revenue-side measures with a budgetary impact of at least 0.1% of GDP are described in Table above.
While the Stability Programme includes all measures described above, the Commission 2018 spring forecast includes only those measures referred to in categories one and three that were credibly announced and sufficiently specified. The expenditure cuts described under point two are not suffiently detailed to be included in the Commission forecast.

[6] The discontination or reduction of previously adopted measures is regulated by the Law accompanying the Budget Law 2018-2019 as adopted by the National Council on 19 April 2018. The 2018 Stability Programme does not refer to all of the reduced measures in detail.

3.4. DEBT DEVELOPMENTS

Table 3: Debt developments

(% of GDP)	Average 2012-2016	2017	2018		2019		2020	2021	2022
			COM	SP	COM	SP	SP	SP	SP
Gross debt ratio[1]	**83.1**	**78.4**	**74.8**	**74.5**	**71.7**	**70.9**	**67.7**	**65.0**	**62.2**
Change in the ratio	0.2	-5.1	-3.6	-3.9	-3.1	-3.6	-3.2	-2.7	-2.8
Contributions[2] *:*									
1. Primary balance	**-0.5**	**-1.1**	**-1.2**	**-1.2**	**-1.3**	**-1.5**	**-1.5**	**-1.5**	**-1.6**
2. "Snow-ball" effect	**0.3**	**-1.7**	**-1.8**	**-2.0**	**-1.3**	**-1.4**	**-1.1**	**-1.0**	**-0.9**
Of which:									
Interest expenditure	2.4	1.8	1.6	1.6	1.5	1.5	1.4	1.3	1.2
Growth effect	-0.7	-2.3	-2.1	-2.4	-1.6	-1.5	-1.3	-1.1	-0.9
Inflation effect	-1.5	-1.2	-1.3	-1.3	-1.2	-1.3	-1.3	-1.2	-1.2
3. Stock-flow adjustment	**0.5**	**-2.2**	**-0.7**	**-0.7**	**-0.5**	**-0.7**	**-0.6**	**-0.2**	**-0.2**
Of which:									
Cash/accruals diff.									
Acc. financial assets									
Privatisation									
Val. effect & residual									

Notes:

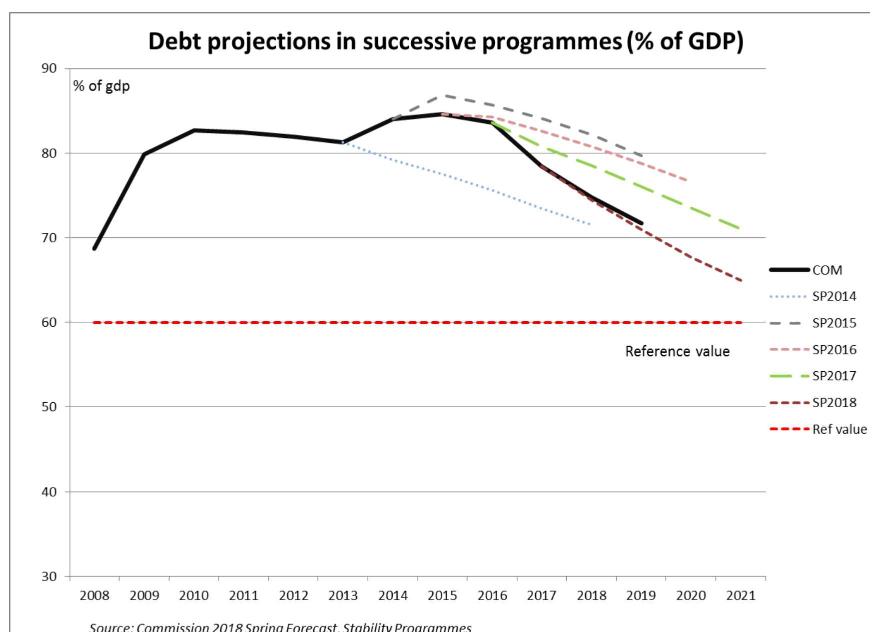
[1] End of period.

[2] The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source :

Commission 2018 spring forecast (COM); Stability Programme (SP), Commission calculations.

Figure 2: Government debt projections in successive programmes (% of GDP)



Following the financial crisis, public support to the banking sector caused government debt to increase substantially, with outstanding liabilities related to bank support amounting to around 10% of GDP at the end of 2016. In particular, three distressed and systemic banks – Kommunalkredit, Volksbanken and Hypo Alpe Adria – have been nationalised or partly nationalised for an orderly wind-down. Liabilities and impaired assets of these banks were subsequently shifted into three bad banks – KA Finanz, Immigon and HETA – and recorded as part of government accounts, causing a step-wise increase in government debt up to 2015. Since then, government debt is on a declining path, supported by the progressive divestment of the impaired assets of the three financial institutions, which is recorded as negative stock-flow adjustment.

Based on the resolution plans of the Financial Market Authority, the Stability Programme expects negative stock-flow adjustments for these banks over the entire programme horizon, contributing to the fast reduction of government debt from 78.4% of GDP in 2017 to 65.0% of GDP in 2022. Based on the projections of the Stability Programme, this decline also benefits from the contributions of the primary balance, economic growth and inflation. While the contributions of primary balance are expected to increase over time in line with the deficit projections, the contribution of economic growth is expected to be strong in 2018 and declining afterwards. The positive effect of inflation is expected to remain broadly constant over the Programme period, while the negative contribution of interest payments is expected to decrease over time.

The Commission 2018 spring forecast assumes similar trends, but expects an overall slower decline in government debt in both years. In 2018, this is the result of different underlying growth projections. In 2019, this is due to different assumptions of the stock-flow adjustment as well as a more conservative assumptions regarding the primary balance.[7]

3.5. RISK ASSESSMENT

The budgetary targets of the Stability Programme are subject to several risks. The macroeconomic scenario for 2018 underpinning the Stability Programme is favourable. In particular, exports, imports and private consumption are expected to grow somewhat stronger compared to the Commission 2018 spring forecast. Although these components are not the most revenue-intensive, they also contribute to higher projections in employment growth, which is relevant for revenues from taxes on income and wealth.

While the majority of expenditure categories is projected to decrease in terms of GDP ratio by 2022, the decrease is strongest for social spending and interest expenditure, which are expected to decrease by 0.3 and 0.4 percentage point of GDP, respectively.

The Commission 2018 spring forecast has a slightly more conservative perspective on revenues in 2018 and on expenditures in 2019, resulting in higher deficit projections for both years. In particular, while the authorities project a balanced budget position as of 2019, the Commission forecasts a headline deficit of 0.2% of GDP.

There are several uncertainties inherent to the Stability Programme. Firstly, the restrictive expenditure path underlying the projections of the authorities critically depends on the effective implementation of the announced catalogue of cost saving measures. While in the majority of measures this will largely depend on the level of detail with which they will be

[7] Differences in the expected stock-flow adjustment for 2019 are the result of data revisions, which could not been taken into account by the Stability Programme due to its early publication on 21 March, together with the updated DBP. The Commission 2018 spring foreast uses the latest available information.

specified, the indexation of family benefits for children living abroad may not be implementable as it may be incompatibile with EU law. Furthermore, second round effects of several discretionary revenue measures such as the Family bonus plus bear an element of uncertainty, as their budgetary impact and timing is difficult to predict. Thirdly, the government has announced tax refliefs by a comprehensive personal income tax reform aimed at reducing the tax ratio to 40% of GDP as of 2020. The reform is not yet sufficiently specified to estimate the budgetary impact and therefore generates some uncertainty to the revenue side.

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

Austria is subject to the preventive arm of the Pact and also subject to the debt reduction benchmark. Box 1 reports the latest country specific recommendations in the area of public finances.

Box 1. Council Recommendations addressed to Austria

On 11 July 2017, the Council addressed recommendations to Austria in the context of the European Semester. In particular, in the area of public finances the Council recommended to Austria to "pursue its fiscal policy in line with the requirements of the preventive arm of the Stability and Growth Pact, which entails achieving its medium-term budgetary objective in 2018, taking into account the allowance linked to unusual events."

The Council noted that in 2018, based on the Commission 2017 spring forecast, Austria should ensure that the nominal growth rate of net primary government expenditure does not exceed 2.2%, corresponding to an improvement in the structural balance by 0.3 % of GDP. However, in view of the ad hoc forecast underpinning the assessment of the updated DBP in spring 2018, Austria was at its MTO in 2017 and in line with the arrangements in place for updating the fiscal requirements contained in the country-specific recommendations, the nominal growth rate of net primary government expenditure should not exceed 3.3% in 2018, corresponding to an allowed deterioration of the structural balance by 0.2% of GDP.

4.1. Compliance with the debt criterion

Table 5. Compliance with the debt criterion

	2017	2018		2019	
		SP	COM	SP	COM
Gross debt ratio	**78**	**74.5**	**74.8**	**70.9**	**71.7**
Gap to the debt benchmark [1,2]	-5.3	-5.3	-5.2	-5.8	-5.3
Structural adjustment [3]	0.3	-0.3	-0.2	0.3	0.2
To be compared to:					
Required adjustment [4]					

Notes:

[1] Not relevant for Member Sates that were subject to an EDP procedure in November 2011 and for a period of three years following the correction of the excessive deficit.

[2] Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark.

[3] Applicable only during the transition period of three years from the correction of the excessive deficit for EDP that were ongoing in November 2011.

[4] Defines the remaining annual structural adjustment over the transition period which ensures that - if followed – Member State will comply with the debt reduction benchmark at the end of the transition period, assuming that COM (S/CP) budgetary projections for the previous years are achieved.

Source :
Commission 2018 spring forecast (COM); Stability Programme (SP), Commission calculations.

As its public debt exceeds the 60% of GDP reference of the Treaty, Austria needs to comply with the debt reduction benchmark. According to the information provided by the Stability Programme, Austria is expected to comply with the debt reduction benchmark in 2018 and 2019. The debt-to-GDP ratio is expected to be below the debt reduction benchmark with a gap 5.3% and 5.8% of GDP in 2018 and 2019. This result is in line with the Commission 2018 spring forecast, which however projects a smaller gap of 5.2% and 5.3% of GDP for 2018 and 2019, respectively.

4.2. Compliance with the required adjustment path towards the MTO

Assessment of eligibility for the 'unusual events' clause

The 2018 Stability Programme indicates an additonal budgetary impact of the exceptional inflow of refugees in 2017 and provides adequate evidence of the scope and nature of these additional costs. The Programme reports no additional costs for security measures related to the terrorist threat.
Concerning refugee-related costs, the increase recorded in 2017 concerns mainly the category "social payments", which is due to the fact a positive asylum decision has an impact on the

eligibility for social benefits and hence corresponding government spending.[8] As a result, while the number of first time applicants has decreased in 2017, the number of positive asylum decisions has actually increased, leading to increased budgetary costs. This increase is plausible, given the duration of the asylum procdures and the large number of asylum seekers that arrived at the end of 2015. According to the Commission, the eligible additional expenditure in 2017 is estimated at 0.03% of GDP concerning the exceptional inflow of refugees while no additional expenditure is taken into account for security-related measures.
In 2015, Austria was granted a temporary deviation for the exceptional inflow of refugees. In analogy to the implementation of the structural reform and investment clauses, the granted deviations for 2015, 2016 and 2017 are carried forward as an allowed distance from the MTO for a total of three years each by the amounts considered eligible. This is to ensure that Austria benefits from the granted temporary deviations in the same way as countries neither at nor in reach of their MTO.
As regards 2017, the Commission assesses that Austria can benefit from an overall temporary deviation of 0.41% of GDP from its MTO due to the additional expenditure for refugee- and security-related costs. The overall temporary deviation is 0.32% and 0.03% of GDP in 2018 and 2019, respectively.

Compliance with the MTO

The MTO for Austria for the period 2017-2019 corresponds to a structural balance of -0.5% of GDP.

In 2017, Austria achieved its MTO corresponding to a structural deficit of 0.5% of GDP within the margin of tolerance.

In 2018, according to the information provided in the Stability Programme, the nominal growth rate of net government expenditure exceeded the applicable reference rate of 3.3% (deviation of -0.3% of GDP), pointing to a risk of some deviation.[9] Similarily, the (recalculated) structural balance is expected to deteriorate by 0.3% of GDP (to -0.8% of GDP), pointing to a risk of some deviation from the required adjustment (deviation of -0.1% of GDP). This calls for an overall assessment. The deviation indicated by the expenditure benchmark is larger than the one indicated by the structural balance. This is due to the fact that the structural balance is supported by declining expenditures for interest, which are excluded from the net government expenditure assessed under the expenditure benchmark. Moreover, differences are based on different underlying estimates of potential growth and revenue shortfalls. While the 10-year average of potential growth underpinning the expenditure benchmark appears more robust, the structural balance benefits from the higher recent estimate of economic potential, although being negatively affected by revenue shortfalls. In consideration of all those factors, the expenditure benchmark appears to more adequately reflect the fiscal effort. Thus, the overall assessment points to a risk of some deviation in 2018.

[8] While an asylum seeker is eligible for the Basic Subsidies Benefit (Grundversorgung), a person granted asylum is eligible for the higher Minimum Income Benefit (bedarfsorientierte Mindestsicherung) and may in addition apply for the housing benefit (Wohnbeihilfe).

[9] As part of the agreement on the EFC Opinion on "Improving the predictability and transparency of the SGP: a stronger focus on the expenditure benchmark in the preventive arm", which was adopted by the EFC on 29 November 2016, the expenditure benchmark, that is the maximum allowable growth rate of expenditure net of discretionary revenue measures, is expressed in nominal terms as from 2018.

Based on the Commission 2018 spring forecast, the expenditure benchmark points to a risk of some deviation both in 2018 and over 2017 and 2018 together, (one-year deviation of -0.4% of GDP and tw-year deviation of -0.1% of GDP), while the structural balance points to compliance. Similarly to the projections of the Stability Programme, the difference between the two indicators is driven by the different assumptions on potential growth, revenue shortfalls as well as declining interest expenditure. Considering those factors, the expenditure benchmark appears to more adequately reflect the fiscal effort. Therefore, the overall assessment based on the Commission 2018 spring forecast points to a risk of some deviation both in 2018 and for 2017 and 2018 together.

In 2019, based on the information provided in the Stability Programme, the nominal growth rate of net government expenditure exceeded the applicable reference rate of 2.9% (deviation of -0.2% of GDP), pointing to a risk of some deviation. The (recalculated) structural balance is expected to improve by 0.3% of GDP , in line with the requirement. The difference between the two indicators rests upon the different reading of economic potential. Taking this into account, the overall assessment points to a risk some deviation in 2019.

Based on the Commission 2018 spring forecast, the expenditure benchmark points to a risk of some deviation over one year (deviation of -0.2% of GDP) and of significant deviation over 2018 and 2019 together (deviation of -0.3% of GDP). The structural balance points to compliance. Again, the structural balance benefits from interest windfalls while the effect of revenue shortfalls and the role of different potential cancel each other out. Taking these aspects into consideration, the overall assessment points to a risk of a significant deviation in 2019, due to the deviation over 2018 and 2019 taken together, based on the expenditure benchmark. At the same time, Austria is projected to be close to its MTO in 2019 (gap of 0.1% of GDP).

Table 6: Compliance with the requirements under the preventive arm

(% of GDP)	2017	2018		2019	
Initial position[1]					
Medium-term objective (MTO)	-0.5	-0.5		-0.5	
Structural balance[2] (COM)	-0.6	-0.8		-0.6	
Structural balance based on freezing (COM)	-0.6	-0.8		-	
Position vis-a -vis the MTO[3]	Not at MTO	At or above the MTO		Not at MTO	
(% of GDP)	**2017**	**2018**		**2019**	
	COM	**SP**	**COM**	**SP**	**COM**
Structural balance pillar					
Required adjustment[4]	0.4	0.0		0.3	
Required adjustment corrected[5]	0.0	-0.2		0.3	
Change in structural balance[6]	0.3	-0.3	-0.2	0.3	0.2
One-year deviation from the required adjustment [7]	0.3	-0.1	0.0	0.1	0.0
Two-year average deviation from the required adjustment [7]	0.2	0.1	0.2	0.0	0.0
Expenditure benchmark pillar					
Applicable reference rate[8]	1.2	3.3		2.9	
One-year deviation adjusted for one-offs[9]	0.3	-0.3	-0.4	-0.2	-0.2
Two-year deviation adjusted for one-offs[9]	-0.1	0.0	-0.1	-0.2	-0.3
PER MEMORIAM: One-year deviation [10]	0.3	-0.3	-0.4	-0.2	-0.2
PER MEMORIAM: Two-year average deviation [10]	0.1	0.0	0.0	-0.2	-0.3

Notes

[1] The most favourable level of the structural balance, measured as a percentage of GDP reached at the end of year t-1, between spring forecast (t-1) and the latest forecast, determines whether there is a need to adjust towards the MTO or not in year t. A margin of 0.25 percentage points (p.p.) is allowed in order to be evaluated as having reached the MTO.

[2] Structural balance = cyclically-adjusted government balance excluding one-off measures.

[3] Based on the relevant structural balance at year t-1.

[4] Based on the position vis-à-vis the MTO, the cyclical position and the debt level (See European Commission: Vade mecum on the Stability and Growth Pact, page 38.).

[5] Required adjustment corrected for the clauses, the possible margin to the MTO and the allowed deviation in case of overachievers.

[6] Change in the structural balance compared to year t-1. Ex post assessment (for 2017) is carried out on the basis of Commission spring forecast 2018.

[7] The difference of the change in the structural balance and the corrected required adjustment.

[8] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A corrected rate applies as long as the country is adjusting towards its MTO, including in year t.

[9] Deviation of the growth rate of public expenditure net of discretionary revenue measures, revenue increases mandated by law and one-offs from the applicable reference rate in terms of the effect on the structural balance. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.

[10] Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate in terms of the effect on the structural balance. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.

<u>Source</u> *:*
Stability Programme (SP); Commission 2018 spring forecast (COM); Commission calculations.

5. FISCAL SUSTAINABILITY

Austria does not appear to face fiscal sustainability risks in the short run.[10]
Based on Commission forecasts and a no-fiscal policy change scenario beyond forecasts, government debt, at 78.4% of GDP in 2017, is expected to decrease to 55.1% in 2028, thus falling below the 60% of GDP Treaty threshold as of 2025. Sensitivity analysis shows similar risks.[11] Overall, this highlights low risks for the country from debt sustainability analysis in the medium term. The full implementation of the Stability Programme would put debt on a steeper decreasing path by 2028, falling below the 60% GDP reference value in 2023.
The medium-term fiscal sustainability risk indicator S1 stands at -0.5 percentage points of GDP, thanks to the initial budgetary position (contributing -1.9 percentage points of GDP), thus indicating low risks in the medium term. The full implementation of the Stability Programme would put the sustainability risk indicator S1 even at -2.0 percentage points of GDP. Overall, risks to fiscal sustainability over the medium term are, therefore, low. Fully implementing the fiscal plans in the Stability Programme would further decrease those risks.
The long-term fiscal sustainability risk indicator S2 (which shows the adjustment effort needed to ensure that the debt-to-GDP ratio is not on an ever-increasing path) is at 2.9 percentage points of GDP. In the long term, Austria therefore appears to face medium fiscal sustainability risks, due to the projected ageing costs, which contribute 3.0percentage points of GDP and are primarily related to health and long-term care expenditure. Full implementation of the Programme would nonetheless put the S2 indicator at 2.2 percentage points of GDP, corresponding to a lower long-term risk.

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[10] This conclusion is based on the short-term fiscal sustainability risk indicator S0. See the note to Table 6 for a definition of the indicator.

[11] Sensitivity analysis includes several deterministic debt projections, as well as stochastic projections (see Debt Sustainability Monitor 2017 for more details).

Table 5 . Fiscal Sustainability Assessment
Austria

Time horizon				Commission Scenario		Stability / Convergence Programme Scenario	
Short Term				**LOW risk**			
S0 indicator [1]				0.1			
	Fiscal subindex			0.1	LOW risk		
	Financial & competitiveness subindex			0.1	LOW risk		
Medium Term				**LOW risk**			
DSA [2]				LOW risk			
S1 indicator [3]				-0.5	LOW risk	-2.0	LOW risk
	of which						
		Initial Budgetary Position		-1.9		-2.9	
		Debt Requirement		0.9		0.2	
		Cost of Ageing		0.5		0.7	
		of which					
			Pensions	0.2		0.3	
			Health-care	0.2		0.2	
			Long-term care	0.2		0.2	
			Other	-0.2		0.0	
Long Term				**MEDIUM risk**		**MEDIUM risk**	
S2 indicator [4]				2.9		2.2	
	of which						
		Initial Budgetary Position		-0.1		-1.0	
		Cost of Ageing		3.0		3.2	
		of which					
			Pensions	0.6		0.6	
			Health-care	1.1		1.0	
			Long-term care	1.4		1.4	
			Other	0.0		0.2	

Source: Commission services; 2018 stability/convergence programme.

Note: the 'Commission' scenario depicts the sustainability gap under the assumption that the structural primary balance position evolves according to the Commissions' spring 2018 forecast covering until 2019 included. The 'stability/convergence programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented over the period covered by the programme. Age-related expenditure as given in the 2018 Ageing Report.

[1] The S0 indicator of short term fiscal challenges informs the early detection of fiscal stress associated to fiscal risks within a one-year horizon. To estimate these risks S0 uses a set of fiscal, financial and competitiveness indicators selected and weighted according to their signalling power. S0 is therefore a composite indicator whose methodology is fundamentally different from the S1 and S2 indicators, which quantify fiscal adjustment efforts. The critical threshold for the overall S0 indicator is 0.46. For the fiscal and the financial-competitiveness sub-indexes, thresholds are respectively at 0.36 and 0.49*.

[2] Debt Sustainability Analysis (DSA) is performed around the no fiscal policy change scenario in a manner that tests the response of this scenario to different shocks presented as sensitivity tests and stochastic projections*.

[3] The S1 indicator is a medium-term sustainability gap; it measures the upfront fiscal adjustment effort required to bring the debt-to-GDP ratio to 60 % by 2032. This adjustment effort corresponds to a cumulated improvement in the structural primary balance over the 5 years following the forecast horizon (i.e. from 2020 for Commission scenario and from last available year for the SCP scenario); it must be then sustained, including financing for any additional expenditure until the target date, arising from an ageing population. The critical thresholds for S1 are 0 and 2.5, between which S1 indicates medium risk. If S1 is below 0 or above 2.5, it indicates low or high risk, respectively*.

[4] The S2 indicator is a long-term sustainability gap; it shows the upfront and permanent fiscal adjustment required to stabilise the debt-to-GDP ratio over the infinite horizon, including the costs of ageing. The critical thresholds for S2 are 2 and 6, between which S2 indicates medium risk. If S2 is below 2 or above 6, it indicates low or high risk, respectively*.

* For more information see Fiscal Sustainability Report 2015 and Debt Sustainability Monitor 2017.

6. FISCAL FRAMEWORK

The Stability Programme recalls the national fiscal rules introduced by the Austrian Stability Pact in 2012, but does not provide any assessment of compliance of the budgetary targets with these rules. With respect to the general government, national fiscal rules broadly reflect the provisions of the Pact, and a similar assessment of compliance can be assumed. Regarding subnational levels of government, the Stability Programme does not contain sufficient information to assess compliance of each sublevel with the respective targets for the structural budget, expenditure growth and debt reduction.
The Stability Programme reports on policy measures aimed at improving the quality of public finances in three arreas: administration, intergovernmental fiscal relations as well as harmonisation of budget law. As for the latter, the Programme refers to the harmonisation of accounting standards across subnational levels of government to increase transparency and improve budgetary planning and monitoring. As for intergovernmental fiscal relations, the 2017 financial equalisation law introduced several positive elements in the Austrian fiscal framework, which are likely to contribute to increasing transparency and contain spending at the subnational level. These include a new task orientation of certain spending categories, the benchmarking systems as well as spending reviews. As for the area of public administration, the Programme recalls the stated objective of the government to streamline the organisation of authoritiesas and to strengthen the Austria as a business location also by deregulating services.
The Stability Programme constitutes also the medium-term fiscal plan required under Article 4(1) of Regulation (EU) 473/2013. Nevertheless, it does not include indications on the expected economic returns on non-defence public investment projects that have a significant budgetary impact. This Stability Programme for the period 2017-2022 submitted by Austria states that it is based on the Federal Budgetary Framework Law 2017 to 2020 (BFRG) and the parameters of the Austrian Stability Pact (ÖStP), national accounts data from Statistics Austria (STAT) until 2016, the medium-term economic forecast by the Austrian Institute of Economic Research (WIFO) of March 2017, and calculations and assessments by the Federal Ministry of Finance (BMF).
It is a long-standing practice in Austria that the Ministry of Finance bases its fiscal plans on the macroeconomic forecast that WIFO produces four times a year following an established, pre-announced calendar. The main features of WIFO's forecasts are freely available to the public.

7. SUMMARY

In 2017, Austria achieved its MTO with the applicable margin. In 2018, on the basis of the Stability Programme, Austria is at risk of some deviation from the required adjustment path towards the MTO in 2018. This assessment is confirmed on the basis of the Commission forecast. In 2019, on the basis of the Stability Programme, Austria is at risk of some deviation from the required adjustment path towards the MTO. According to the Commission 2018 spring forecast, based on an overall assessment, there is a risk of significant deviation in 2019, due to the deviation over 2018 and 2019 taken together.

Based on the Stability Programme, Austria is expected to meet the debt reduction benchmark both in 2018 and 2019, which is confirmed by the Comission 2018 spring forecast.

8. ANNEXES

Table I. Macroeconomic indicators

	2000-2004	2005-2009	2010-2014	2015	2016	2017	2018	2019
Core indicators								
GDP growth rate	2.0	1.4	1.3	1.1	1.5	2.9	2.8	2.2
Output gap [1]	0.1	0.4	-0.6	-1.1	-1.1	-0.2	0.6	0.7
HICP (annual % change)	1.8	1.9	2.3	0.8	1.0	2.2	2.1	1.9
Domestic demand (annual % change) [2]	1.3	1.3	0.8	1.1	2.1	2.5	2.0	1.6
Unemployment rate (% of labour force) [3]	4.5	5.0	5.1	5.7	6.0	5.5	5.2	5.0
Gross fixed capital formation (% of GDP)	24.3	22.9	22.5	22.5	23.1	23.5	23.7	23.7
Gross national saving (% of GDP)	25.4	26.8	25.8	25.8	26.2	27.2	27.5	27.8
General Government (% of GDP)								
Net lending (+) or net borrowing (-)	**-2.2**	**-2.6**	**-2.8**	**-1.0**	**-1.6**	**-0.7**	**-0.5**	**-0.2**
Gross debt	**66.1**	**69.9**	**82.5**	**84.6**	**83.6**	**78.4**	**74.8**	**71.7**
Net financial assets	**-36.5**	**-44.2**	**-55.4**	**-56.1**	**-57.2**	**n.a**	**n.a**	**n.a**
Total revenue	49.5	48.3	49.0	49.9	49.0	48.4	48.0	47.8
Total expenditure	51.7	51.0	51.8	51.0	50.6	49.1	48.5	47.9
of which: Interest	3.4	3.1	2.7	2.3	2.1	1.8	1.6	1.5
Corporations (% of GDP)								
Net lending (+) or net borrowing (-)	**-1.6**	**0.0**	**2.3**	**0.5**	**0.9**	**0.7**	**0.6**	**0.4**
Net financial assets; non-financial corporations	**-83.6**	**-79.8**	**-71.8**	**-68.5**	**-66.6**	**n.a**	**n.a**	**n.a**
Net financial assets; financial corporations	**-5.2**	**-2.7**	**1.6**	**-0.9**	**0.5**	**n.a**	**n.a**	**n.a**
Gross capital formation	16.0	15.1	14.6	15.1	15.4	16.2	16.5	16.6
Gross operating surplus	24.9	26.7	24.5	24.2	23.5	24.1	24.4	24.3
Households and NPISH (% of GDP)								
Net lending (+) or net borrowing (-)	**4.5**	**5.5**	**2.7**	**2.1**	**2.8**	**1.9**	**1.8**	**2.0**
Net financial assets	**109.1**	**116.8**	**124.6**	**128.0**	**128.9**	**n.a**	**n.a**	**n.a**
Gross wages and salaries	39.3	38.0	39.0	39.0	39.6	39.3	39.2	39.2
Net property income	9.6	11.1	7.9	7.5	6.1	5.8	5.5	5.4
Current transfers received	22.8	22.4	23.3	23.5	23.6	22.9	22.6	22.3
Gross saving	9.4	10.6	8.3	7.5	8.1	7.5	7.3	7.4
Rest of the world (% of GDP)								
Net lending (+) or net borrowing (-)	**0.6**	**2.9**	**2.3**	**1.6**	**2.1**	**1.9**	**2.0**	**2.2**
Net financial assets	**17.7**	**11.8**	**4.2**	**0.0**	**-2.8**	**n.a**	**n.a**	**n.a**
Net exports of goods and services	2.5	3.8	3.0	3.7	3.4	3.4	3.9	4.4
Net primary income from the rest of the world	-0.6	0.1	0.3	-0.7	-0.1	-0.2	-0.3	-0.3
Net capital transactions	-0.2	-0.1	-0.1	-0.5	-0.2	-0.4	-0.5	-0.5
Tradable sector	46.4	45.5	44.8	44.4	44.0	44.3	n.a	n.a
Non tradable sector	42.9	43.6	44.3	44.8	45.1	44.9	n.a	n.a
of which: Building and construction sector	6.4	6.1	5.7	5.6	5.7	5.8	n.a	n.a
Real effective exchange rate (index, 2000=100)	98.3	100.0	101.2	102.3	103.7	103.6	104.8	104.7
Terms of trade goods and services (index, 2000=100)	103.0	101.3	98.5	99.8	100.3	99.8	99.5	99.3
Market performance of exports (index, 2000=100)	103.4	100.5	100.3	96.5	94.4	95.1	94.6	94.0

Notes:

[1] The output gap constitutes the gap between the actual and potential gross domestic product at 2005 market prices.

[2] The indicator on domestic demand includes stocks.

[3] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.

Source:
AMECO data, Commission 2018 spring forecast