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Analysis of the 2016 Draft Budgetary Plan of AUSTRIA

Accompanying the document

COMMISSION OPINION

on the Draft Budgetary Plan of AUSTRIA

{C(2015) 8111 final}

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1. INTRODUCTION

Austria submitted its Draft Budgetary Plan (DBP) for 2016 on 15 October 2015 in compliance with Regulation (EU) No 473/2013 of the Two-Pack. Austria is subject to the preventive arm of the Pact and should preserve a sound fiscal position which ensures compliance with the medium-term budgetary objective (MTO).

As the debt ratio was 80.9% of GDP in 2013 (the year in which Austria corrected its excessive deficit), during the three years following the correction of the excessive deficit Austria is also subject to the transitional debt rule. In this period it should ensure sufficient progress towards compliance.

Section 2 of this document presents the macroeconomic outlook underlying the DBP and provides an assessment based on the Commission Forecast. The following section presents the recent and planned fiscal developments, according to the DBP, including an analysis of risks to their achievement based on the Commission 2015 autumn forecast. In particular, it also includes an assessment of the measures underpinning the DBP. Section 4 assesses the recent and planned fiscal developments in 2015-2016 (also taking into account the risks to their achievement) against the obligations stemming from the Stability and Growth Pact (SGP). Section 5 provides an analysis of implementation of reforms in the area of fiscal governance in response to the latest country-specific recommendations adopted by the Council on 14 July 2015, including those to reduce the tax wedge. Section 6 concludes.

2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

The macroeconomic scenario underlying the DBP projects GDP to increase from 0.4% in 2014 to 0.7% in 2015 and 1.4% in 2016. For 2015 this constitutes a slightly better assessment of GDP growth compared to this year's stability programme which expected an increase of 0.5%. With this projection the DBP is broadly in line with the Commission 2015 autumn forecast which sets GDP growth in 2015 0.1% lower and in 2016 0.1% higher than the DBP. Compared to the DBP the Commission expects in 2016 a weaker increase in private consumption following the income tax reform, but a stronger pick up in investments driven by needs for replacement of equipment and housing demand. In 2016 GDP growth is expected to be mainly driven by domestic demand with net exports contributing to a much lesser extent. The DBP projects inflation at 1.1% in 2015 and at 1.7% in 2016 which is in both years 0.2% less than in the Stability programme (2015/16: 1.3%/1.9%). The Commission 2015 autumn forecast expects inflation to be in 2015 even lower at 0.9% and in 2016 marginally higher at 1.8% compared to the DBP.

Table 1. Comparison of macroeconomic developments and forecasts

	2014	2015			2016		
	COM	SP	DBP	COM	SP	DBP	COM
Real GDP (% change)	0.4	0.5	0.7	0.6	1.4	1.4	1.5
Private consumption (% change)	0.0	0.4	0.4	0.3	1.4	1.3	1.0
Gross fixed capital formation (% change)	-0.2	1.0	0.4	-0.1	2.0	1.5	2.6
Exports of goods and services (% change)	2.1	2.0	2.5	1.2	3.2	3.6	3.7
Imports of goods and services (% change)	1.3	2.3	2.3	1.0	3.7	3.4	3.6
Contributions to real GDP growth:							
- Final domestic demand	0.1	0.7	0.5	0.3	1.3	1.1	1.2
- Change in inventories	-0.3	-0.1	0.1	0.1	0.2	0.0	0.0
- Net exports	0.5	-0.1	0.2	0.2	-0.1	0.3	0.3
Output gap[1]	-0.9	-1.4	-1.3	-1.2	-1.0	-0.8	-0.6
Employment (% change)	0.9	0.6	0.9	0.7	0.8	1.0	0.8
Unemployment rate (%)	5.6	5.3	5.8	6.1	5.3	6.0	6.1
Labour productivity (% change)	-0.5	-0.1	-0.2	-0.1	0.6	0.4	0.7
HICP inflation (%)	1.5	1.3	1.1	0.9	1.9	1.7	1.8
GDP deflator (% change)	1.6	1.4	1.6	1.5	1.7	1.7	1.5
Comp. of employees (per head, % change)	1.7	1.6	1.9	1.8	2.0	1.8	1.8
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	2.0	1.4	1.4	2.5	1.0	1.4	2.6

Note:

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

Source:

Stability Programme 2015 (SP); Draft Budgetary Plan for 2016 (DBP); Commission 2015 autumn forecast (COM); Commission calculations

The macroeconomic outlook of the DBP is based on plausible macroeconomic assumptions. Both the DBP and the Commission forecast expect a small but positive contribution of net exports to economic growth which in the Stability Programme was projected to be slightly negative. Although both assessments expect an increase in employment, they also both expect an increase in the unemployment rate. The main reason for this is that economic growth is not sufficient to have a major positive impact on the labour market which will experience an increase in labour supply due to the expected inflow of immigrants.

Box 1: The macro economic forecast underpinning the budget in Austria

The DBP for 2016 submitted by Austria states that the DBP is based on the macroeconomic forecast published by the Austrian Institute of Economic Research (WIFO) on 29 September 2015.

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.

WIFO was founded in 1927 and benefits from a reputation as one of Austria's prominent policy oriented economic research institutes. Its analytical infrastructure and staff allow it to carry out research in a broad range of economic issues. WIFO is recognised for high-quality economic research and realistic and unbiased forecasts. It is also charged with compiling the quarterly national accounts and the business/investment surveys.

WIFO is a non-profit association under Austrian law. The 16 member Governing Board (Vorstand) and the 33 member Supervisory Council (Kuratorium) comprise representatives of various NGO's, financial institutions, including the Austrian National Bank, businesses, business associations, the academia as well as the central and regional government. Representatives of the central as well as the regional government occupy 1 seat each on the Governing Board and 1 respectively 2 seats each on the Supervisory Council.

The Scientific Advisory Board comprising 16 renowned scholars ensures the strong integration of the Institute in the international scientific community and promotes knowledge transfer of research content and methods. The board also acts as an external quality control mechanism for WIFO's activities.

3. RECENT AND PLANNED FISCAL DEVELOPMENTS

3.1. Deficit developments

The DBP plans a decrease of the general government deficit to 1.9% of GDP in 2015, by 0.3% of GDP lower than the forecast of the spring Stability Programme. The DBP explains the difference by the projected increase in revenue growth, especially concerning income taxes and taxes on wealth. In fact, in 2015 nominal revenues performed remarkably well, and outpaced GDP growth. This generated a revenue-to-GDP ratio markedly higher when compared to the projections of the Stability Programme and the Commission spring forecast. On the expenditure side, the better than expected increase in employment allowed for higher contributions and less expenditure for public pension funds, that together with unexpected savings in intermediate consumption more than offset the additional spending for labour market measures related to rising unemployment and refugee-related expenditures. As a consequence, the DBP prospects a slightly lower expenditure-to-GDP ratio than the SP. The Commission autumn forecast projects similar developments, but remains slightly more conservative on the revenue side.

According to the DBP, the general government deficit is forecast to decrease to 1.4% of GDP in 2016. This estimate is by 0.2% lower than the forecast of the Stability Programme. This is driven by higher revenue projections, due to better performance of 2015, and by lower costs of rescuing operations in the banking sector, and in particular the phasing out of the costs related to the winding down of financial defeasance structures classified inside the general government (KA Finanz and HETA). While the DBP does not provide an explicit explanation for other differences, this appears to be also due to lower expenditure for intermediate consumption and social payments, which more than offset the additional expenditures for refugees in 2016.

The Commission 2016 autumn forecast expects the headline deficit at 1.6% of GDP, 0.2% higher than planned by the DBP and in line with the Stability Programme. This is mainly due to a slightly more conservative estimate of the measures aimed to finance the tax relief in 2016, which affects particularly the revenue side. In fact, by combating tax fraud in the framework of the tax reform the DBP plans to raise additional revenue from taxes on production and income taxes, leading to higher revenue-to-GDP ratio when compared to the Commission forecast. The difference in the expenditure ratio between the DBP and the Commission autumn forecast is due to the fact that Commission forecast projects higher unemployment levels, which corresponds to an increase in social payments.

Table 2. Composition of the budgetary adjustment

(% of GDP)	2014	2015			2016			Change: 2014-2016
	COM	SP	DBP	COM	SP	DBP	COM	DBP
Revenue	**50.0**	**49.9**	***50.1***	**50.2**	**49.5**	***49.7***	**49.7**	**-0.3**
of which:								
- Taxes on production and imports	14.4	14.5	*14.4*	14.4	14.8	*14.8*	14.7	0.4
- Current taxes on income, wealth, etc.	13.7	13.8	*14.0*	14.0	13.0	*13.1*	13.0	-0.6
- Capital taxes	0.1	0.2	*0.1*	0.1	0.2	*0.2*	0.1	0.1
- Social contributions	15.4	15.5	*15.5*	15.5	15.6	*15.5*	15.6	0.1
- Other (residual)	6.3	5.9	*6.1*	6.3	5.9	*6.1*	6.2	-0.2
Expenditure	**52.7**	**52.1**	**52.0**	**52.1**	**51.2**	**51.1**	**51.2**	**-1.6**
of which:								
- Primary expenditure	50.2	49.8	49.6	49.7	49.0	48.9	49.0	-1.3
of which:								
Compensation of employees	10.6	10.7	10.6	10.6	10.5	10.5	10.5	-0.1
Intermediate consumption	6.4	6.5	6.3	6.3	6.4	6.2	6.2	-0.2
Social payments	23.3	23.8	23.6	23.6	23.8	23.6	23.7	0.3
Subsidies	1.4	1.5	1.5	1.4	1.4	1.4	1.4	0.0
Gross fixed capital formation	3.0	2.9	3.0	3.0	2.9	2.9	2.9	-0.1
Other (residual)	5.6	4.4	4.6	4.8	4.0	4.3	4.3	-1.3
- Interest expenditure	2.5	2.3	2.4	2.4	2.2	2.2	2.2	-0.3
General government balance (GGB)	**-2.7**	**-2.2**	**-1.9**	**-1.9**	**-1.6**	**-1.4**	**-1.6**	**1.3**
Primary balance	**-0.2**	**0.1**	**0.5**	**0.5**	**0.5**	**0.8**	**0.7**	**1.0**
One-off and other temporary measures	-1.5	-0.5	-0.6	-0.6	-0.2	-0.3	-0.2	1.2
GGB excl. one-offs	**-1.2**	**-1.7**	**-1.3**	**-1.3**	**-1.4**	**-1.1**	**-1.4**	**0.1**
Output gap[1]	-0.9	-1.4	-1.3	-1.2	-1.0	-0.8	-0.6	0.4
Cyclically-adjusted balance[1]	-2.2	-1.4	-1.2	-1.2	-1.0	-0.9	-1.2	1.1
Structural balance (SB)[2]	**-0.7**	**-0.9**	**-0.6**	**-0.6**	**-0.8**	**-0.6**	**-1.0**	**-0.1**
Structural primary balance[2]	1.8	1.4	1.8	1.8	1.4	1.6	1.2	-0.4

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 2015 (SP); Draft Budgetary Plan for 2016 (DBP); Commission 2015 autumn forecast (COM); Commission calculations

The main uncertainty in both the DBP and the Commission forecast is related to the effect of the tax reform and counterbalancing measures. Since the tax relief will amount to approximately 1.2% of GDP in 2016, a shortfall in the effectiveness of the financing measures could have a significant impact on the headline deficit. In this sense, the Commission followed a slightly more cautious approach, especially on the revenue side. On the other hand, it should be taken into account that in the past both the authorities' and the Commission forecast proved to be overly conservative as to the revenue performance.

An additional risk is connected to the financial sector, and concerns in particular the protracted costs of winding-down financial institutions, which represented one of the main drivers of Austria's headline deficit in recent years.

As to the DBP forecast, the recalculated structural balance[1] is planned to remain stable in 2015 and to decrease by 0.1% of GDP in 2016, reaching -0.6% of GDP in level terms. In 2016, the Commission autumn forecast projects a higher structural deficit. This is due to three main factors: the refugee-related costs are not considered as one-offs and thus are included in the structural balance; some measures aimed at financing the tax reform are expected to have a lower effect; the output gap is projected to be slightly lower in absolute terms when compared to the DBP, due to a difference in the estimation of the potential GDP.

Box 2: Impact of the current low interest rate environment on compliance with the SGP

Identifying an interest rate windfall/shortfall for 2016

Sovereign bond yields have fallen sharply since end-2013 and reached historical lows in the first half of 2015, before increasing somewhat during the summer months. However, yields in Austria still remain well below their long-term averages of 4.26%, with 10-year rates standing at 1.49%. As a result of lower interest rates, total interest payments by the general government have also decreased over the last few years. Interest expenditure in Austria is expected to fall from 2.72% of GDP in 2012 to 2.40% in 2015, and is projected to further decrease next year, reaching 2.20% of GDP, based on the information provided in the DBP. This outcome is in line with Commission autumn forecasts, assuming further easing of implicit interest rates on government debt.

Prospects and vulnerability

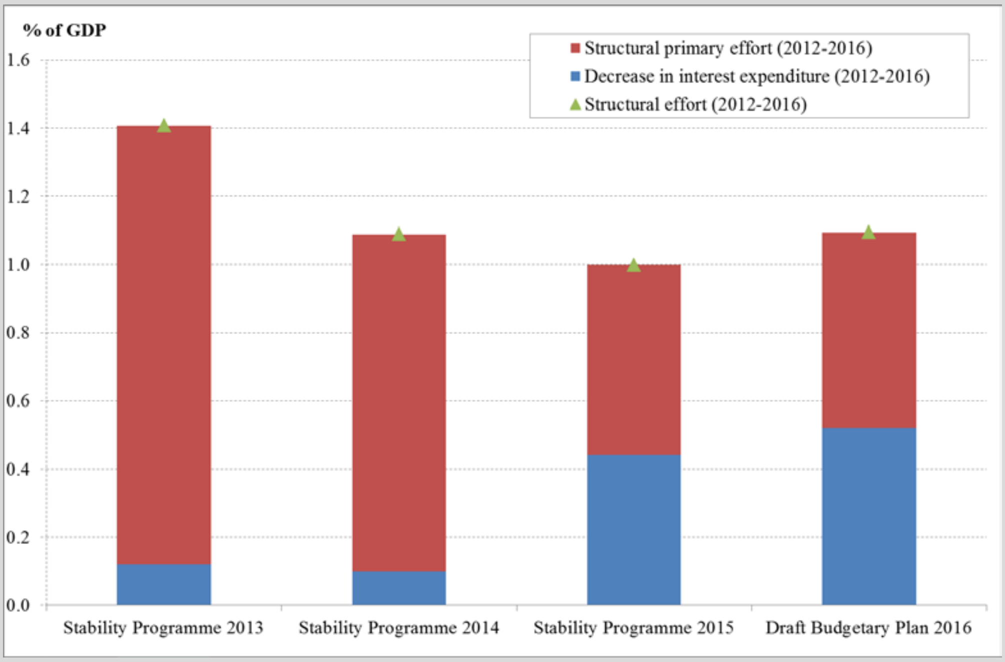
By assuming that in Austria around 10% of consolidated debt falls due every year as it was for the last ten years, the share of outstanding debt to be renewed over 2016-2018 is about 30%. This means that Austria would significantly benefit from a protracted low interest environment, while at the same time being sensitive to a significant increase in interest rates.

[1] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission on the basis of the information provided in the Draft Budgetary Plan, using the commonly agreed methodology.

Consequences for public finances

Comparing the interest expenditure projections across different vintages of Stability and Convergence Programmes and the DBP sheds more light on the interest windfall since the fall in interest rates (see Chart)[2].

Structural effort and decrease in interest expenditures between 2012 and 2016 based on government plans



Source: Stability programmes, Draft Budgetary Plan 2016 and AMECO

Comparing the interest expenditure projections across different vintages of Austria's Stability Programme and the DBP sheds more light on the (unexpected) interest windfall since the decline in interest rates. In the 2013 Stability Programme, decreasing interest expenditure was expected to contribute 0.1% of GDP to the planned 2012-2016 fiscal consolidation effort. In subsequent programmes, the contribution of declining interest expenditure over 2012-2016 grew gradually, to 0.5% of GDP taking into account the outturn data and projections of the 2016 DBP. The difference with the 2013 Stability Programme could be seen as a benchmark to approximate the size of the interest windfall. The decline in interest expenditure was generally offset by a decline in the structural primary effort. Therefore, the planned and projected change in the structural balance over the period of 2012 and 2016 based on the DBP is lower than planned in 2013 and remained stable compared to the Stabilityy Programmes of 2014 and 2015.

The interest windfall has partly been used for the reduction of the structural balance until 2015, while in 2016 lower interest expenditure is expected to reduce the impact of the

[2] Note that, while it is likely that revisions in the interest expenditure projections across different vintages primarily reflect changes in interest rates, other factors such as debt dynamics, the maturity profile of debt and statistical reclassifications (e.g. the switchover to the ESA 2010 standard of national accounts) may also have played a role.

forthcoming tax relief on the deficit. At the same time, the low interest rate environment has facilitated sizable bank support measures while reaching the MTO in 2014.

Rather than offset the interest rate windfalls, relatively stable inflation has been supportive of the fiscal adjustment and the reduction of the debt ratio.

3.2. Debt developments

Table 3. Debt developments

(% of GDP)	2014	2015			2016		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio[1]	**84.2**	**86.8**	**86.5**	**86.6**	**85.7**	**85.1**	**85.7**
Change in the ratio	3.4	2.6	2.3	2.4	-1.1	-1.4	-0.9
Contributions[2] :							
1. Primary balance	**0.2**	**-0.1**	**-0.5**	**-0.5**	**-0.5**	**-0.8**	**-0.7**
2. "Snow-ball" effect	**0.9**	**0.7**	**0.4**	**0.6**	**-0.5**	**-0.4**	**-0.2**
Of which:							
Interest expenditure	2.5	2.3	2.4	2.4	2.1	2.2	2.2
Growth effect	-0.3	-0.4	-0.6	-0.5	-1.2	-1.2	-1.2
Inflation effect	-1.3	-1.2	-1.4	-1.2	-1.4	-1.4	-1.2
3. Stock-flow adjustment	**2.3**	**1.9**	**2.3**	**2.2**	**-0.1**	**-0.2**	**0.0**

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

Source:

Stability Programme 2015 (SP); Draft Budgetary Plan for 2016 (DBP); Commission 2015 autumn forecast (COM); Commission calculations

In the DBP, general government debt is expected to increase to 86.5% of GDP in 2015. This is largely explained by a debt-increasing stock-flow adjustment.[3] The increase in the general government debt is slightly lower if compared to the SP projections, mainly because of the improvement in the projected headline balance as to the DBP, which more than offsets the projected increase in the stock-flow adjustment.[4] Also the "snow-ball" effect is lower in the

[3] The substantial stock-flow adjustment arises from the inclusion into the general government debt of impaired assets worth EUR 6.3 billion transferred from Kommunal-kredit Austria AG to the balance sheet of KA Finanz, which was already included under general government accounts following the application of ESA 2010 methodology. ESA2010 methodology prescribes that impaired assets taken over by the national government in the context of the winding down of financial institutions should be accounted as government debt. The difference between the transfer value and the economic value of the assets –i.e. the net loss– figures as headline deficit, while the rest is considered as stock flow adjustment. KA Finanz is the bad bank of Kommunal-kredit, thus assets transferred to KA Finanz are accounted as government debt.

[4] The higher stock-flow adjustment is caused by an advance payment of EUR 1.2 billion for a settlement between the Austrian government and Bavaria regarding Hypo-Alpe-Adria-Bank/HETA Asset Resolution, which following the methodology previously mentioned has an effect on debt but not on headline deficit.

DBP than in the SP, given the higher GDP growth and higher inflation projections in the DBP. Furthermore, the higher debt ratio projected by the DBP only slightly increases interest expenditure, given that only the negative net value of the impaired assets of financial institutions included in the government accounts is financed through the issuance of government debt.

Given its slightly stronger "snow-ball" effect coming from lower projections for nominal GDP growth, the Commission autumn forecast projects a moderately higher debt-to-GDP ratio than the DBP for 2015.

After peaking in 2015, the gross debt ratio is expected to decrease in 2016 to 85.1% of GDP, as to the DBP forecast. This is mainly due to the reduced deficit and the progressive disposal of financial defeasance structures included in government accounts. The DBP forecast represents an improvement of 0.6% of GDP with respect to the SP forecast, mainly driven by the different headline balance projections. DBP forecast of the gross debt ratio is by 0.6% of GDP lower also with respect to the Commission autumn forecast, since the Commission does not take into account the debt reducing stock-flow adjustment, that the DBP reports but does not explain. The difference is also due to a lower projected primary balance as to the Commission autumn forecast.

3.3. Measures underpinning the Draft Budgetary Plan

Similarly to the 2015 Stability Programme, the 2015 DBP does not include the usual table quantifying in detail the effect of the discretionary measures underlying the programme. This is to the detriment of the readability and transparency of the budgetary plan.

Nevertheless, quantitative effects of the major policy strategy reported by the DBP – i.e. the adopted tax reform – were described in the 2015 Stability Programme and reported as to their main lines in the DBP. Both the SP and DBP present the reform as fully self-financed, while the SP also describes the counter-financing measures that are expected to assure the budget neutrality. Nevertheless, by considering each measure individually, the Commission estimates that the reform could increase the headline deficit by about 0.3% of GDP. The reform is discussed in more detail in box 4.

An additional measure having relevant budgetary impacts is the amount of EUR 700 million budgeted as a one-off expenditure for any additional costs related to the winding down of financial institutions and to any further recapitalization of banks in 2016. This amount represents a precautionary buffer and does not relate to any particular rescuing operation foreseen to be conducted by the general government in connection with the financial sector developments. The DBP does not provide a clear description of how such amount was estimated, but the inclusion of a buffer for financial rescuing operations seems in itself justified given the various bank resolution processes which are presently ongoing, and the existence of several still pending legal disputes.

The DBP also describes several measures adopted to face the increase in the number of asylum seekers in 2016, and the corresponding budgetary costs. In 2016, the additional refugee-related costs when compared to 2015 sum up to EUR 500 million. The quality of information on refugee related costs is fairly detailed and clearly outlines the additional expenditures related to the unexpected inflows of asylum seekers. The DBP explains additional costs for 2016 in terms of four factors:

1. Increased number of persons requiring public assistance –passing from 27,000 in 2014 to a projection of 61,000 in 2016.

2. Increased individual entitlements. The DBP provides a table showing the evolution of costs per each refugee from 2014 to 2016 (which comprehend costs for food and shelter, language courses, counselling, clothing, recreation and health).

3. A fund of EUR 70 million created by the Federal Government and a second fund of 75 million reallocated by the Ministry of Finance in order to foster the integration of refugees in the labour market.

4. The DBP also mentions further costs for the construction of additional "first-stop" centres and for transportation of people, but does not specify the precise amounts.

The total refugee-related cost estimated by the DBP amounts to 0.35% of GDP in 2016, which is coherent with the details provided when assuming reasonable amounts for the construction of additional "first-stop" centres and for the transportation of people (point 4). Compared to 2015, the DBP points to an increase in refugee-related costs of 0.16% of GDP in 2016. No reference to EU funds targeted to financing the additional inflows of asylum seekers appears in the DBP. The increase in the refugee related costs is considered as one-off expenditure in the DBP which is not in line with the Commission's guidelines.

4. Compliance with the provisions of the Stability and Growth Pact

Austria is subject to the preventive arm of the Pact and should ensure sufficient progress towards its MTO. Box 2 reports the latest country specific recommendations in the area of public finances. Austria is also subject to the transitional debt rule.

Box 3. Council recommendations addressed to Austria

On 14 July 2015, 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 avoid deviating from the medium-term objective in 2015/2016.

4.1. Compliance with the debt criterion

After correcting its excessive deficit in 2013, Austria is in the transition period as regards the debt criterion for the following three years. This implies that, during this period, it is required to make sufficient progress towards compliance with the debt criterion (as defined by the minimum linear structural adjustment (MLSA) and comply with the debt rule at the end of the transition period.

Besides the moderate GDP growth and the reduction of expenditures for the winding-down of financial institution, the path of Austrian debt is benefiting from the relatively high inflation and low interest rates.

The DBP does not include sufficient information to assess compliance with the transitional debt rule. Based on the Commission autumn forecast, Austria is forecast to achieve a structural adjustment above the required adjustment both in 2015 and 2016 (respectively, 0.1 vs required -0.1and -0.4 vs required -0.5).

Table 4. Compliance with the debt criterion*

	2014	2015			2016		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio	84.2	86.8	86.5	86.6	85.7	85.1	85.7
Gap to the debt benchmark [1,2]							
Structural adjustment [3]	0.6	-0.4	0.0	0.1	0.1	-0.1	-0.4
To be compared to:							
Required adjustment [4]	0.0	-0.3	n.a.	-0.1	-0.3	n.a.	-0.5

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 minimum 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 (SP) budgetary projections for the previous years are achieved.

Source:

Stability Programme 2015 (SP); Draft Budgetary Plan for 2016 (DBP); Commission 2015 autumn forecast (COM); Commission calculations

* An ex-ante assessment of planned compliance with the debt criterion can be based on the DBP only for the concerned countries providing extended data series (i.e. covering years up to t+4) in the DPB on a voluntary basis, as agreed at the EFC-A on 22 September 2014 and reflected in the updated Code of Conduct of the two-pack.

4.2. Compliance with the MTO

In 2015, according to both the information provided in the DBP and the Commission autumn forecast, both the structural balance pillar and the expenditure benchmark point to compliance. Over the years of 2014 and 2015 taken together, the structural balance points to compliance, while the expenditure benchmark points to some deviation (gap of -0.2% of GDP). This calls for an overall assessment. The expenditure benchmark is negatively affected by a significant one-off cost related to the winding-down of financial institutions in 2014. Considering this factor, the structural balance seems to be a better indicator of the fiscal effort at the current juncture. Therefore, the overall assessment at this stage points to compliance. The Commission 2015 autumn forecast provides a near-identical reading. As above, the overall assessment points to compliance as the structural balance is considered to be the more relevant indicator.

For 2016, according to the information provided in the DBP the change in the recalculated structural balance of -0.1% of GDP points to some deviation (gap of -0.2% of GDP) from the required adjustment of 0.1% of GDP. The expenditure benchmark is complied with. This calls for an overall assessment. The compliance of the expenditure benchmark is driven by a strong base effect, caused by the phasing out in 2016 of one-off transactions in relation to the winding down of financial institutions -costs not considered in the structural balance pillar.

Therefore, the overall assessment based on the information provided by the DBP points to some deviation from the MTO in 2016.

As to the Commission autumn forecast, the structural balance is expected to deteriorate by 0.4% of GDP in 2016, resulting in a significant deviation from the required adjustment towards the MTO (gap of -0.6% of GDP). The net expenditure growth rate is expected to be above the benchmark (gap of -0.2% of GDP). While the difference between the two indicators is sizeable, an overall assessment shows that this is mainly due to the above-mentioned one-off transactions connected with year-to-year fluctuations in the cost of winding down financial institutions, which have a positive effect on compliance with the expenditure benchmark but are excluded from the structural balance. Therefore, the overall assessment points to a risk of a significant deviation from the MTO in 2016. Nevertheless, a part of the deviation from the MTO, both on the basis of the structural balance and the expenditure benchmark pillar, is due to an increase in refugee-related spending. If the current estimate of the increase in refugee-related expenditure were excluded, the assessment would point to a risk of some deviation from the MTO in 2016.

Following an overall assessment of the Member State's DBP, with the structural balance as a reference, including an analysis of expenditure net of discretionary revenue measures there is a risk of a significant deviation from the adjustment path towards the MTO in 2016. However, in case the current estimate of the budgetary impact of the exceptional inflow of refugees was excluded from the assessment, the projected deviation would no longer be significant.

Table 5: Compliance with the requirements of the preventive arm

(% of GDP)	2014	2015		2016	
Initial position[1]					
Medium-term objective (MTO)	-0.5	-0.5		-0.5	
Structural balance[2] (COM)	-0.7	-0.6		-1.0	
Structural balance based on freezing (COM)	-0.4	-0.6		-	
Position vis-a -vis the MTO[3]	Not at MTO	At or above the MTO		At or above the MTO	
(% of GDP)	**2014**	**2015**		**2016**	
	COM	**DBP**	**COM**	**DBP**	**COM**
Structural balance pillar					
Required adjustment[4]	0.6	0.0		0.0	
Required adjustment corrected[5]	0.6	-0.1		0.1	
Change in structural balance[6]	0.7	0.0	0.1	-0.1	-0.4
One-year deviation from the required adjustment [7]	0.1	0.0	0.1	-0.2	-0.6
Two-year average deviation from the required adjustment [7]	n.a. (in EDP in 2013)	0.1	0.1	-0.1	-0.2
Expenditure benchmark pillar					
Applicable reference rate[8]	-0.1	1.3		0.8	
One-year deviation [9]	-1.5	1.1	1.0	0.0	-0.2
Two-year average deviation [9]	n.a. (in EDP in 2013)	-0.2	-0.2	0.6	0.4
Conclusion					
Conclusion over one year	Overall assessment	Compliance	Compliance	Overall assessment	Overall assessment
Conclusion over two years	n.a. (in EDP in 2013)	Overall assessment	Overall assessment	Overall assessment	Overall assessment

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 27.).

[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 2014) was carried out on the basis of Commission 2015 spring forecast.

[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 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.

Source :
Draft Budgetary Plan for 2016 (DBP); Commission 2015 autumn forecast (COM); Commission calculations.

5. IMPLEMENTATION OF REFORMS IN THE AREA OF FISCAL GOVERNANCE

In the context of the 2015 European Semester, Austria was issued the recommendation to "(…) Correct the misalignment between the financing and spending responsibilities of the different levels of government"; "Take measures to ensure the long-term sustainability of the pension system, including by earlier harmonisation of the statutory retirement age for men and women and link the statutory retirement age to life expectancy".

As to the long-term sustainability of the pension system, the DBP points out that in mid-July the Parliament adopted the introduction of the part-time pension, aimed at increasing the effective pension age, following the view that elderly workers would be incentivised to continue working part-time instead of retiring early. Also, a semi-annual monitoring on the effects of the pension reform described in the 2015 National reform programme has been established. On the other hand, the DBP does not mention the harmonisation of the statutory retirement age for men and women, nor the linking of the statutory retirement age to life expectancy. Similarly, the misalignment between the financing and spending responsibilities of the different levels of government was not considered in the DBP.

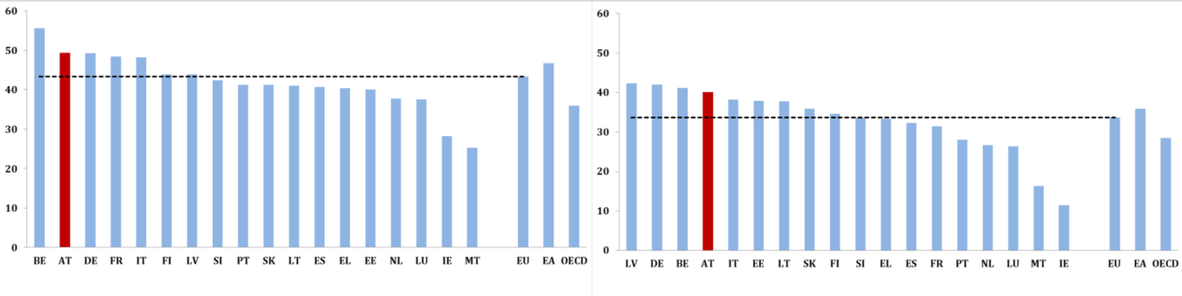
A comprehensive assessment of progress made with the implementation of the CSRs will be made in the 2016 Country Reports and in the context of the CSRs adopted by the Commission in May.

Box 4. Addressing the tax burden on labour in the euro area

The tax burden on labour in the euro area is relatively high, which weighs on economic activity and employment. Against this background, the Eurogroup has expressed a commitment to reduce the tax burden on labour. On 12 September 2015, the Eurogroup agreed to screen euro area Member States' tax burden on labour against the GDP-weighted EU average, relying in the first instance on indicators measuring the tax wedge on labour for a single worker at average wage and a single worker at low wage. It also agreed to relate these numbers to the OECD average for purposes of broader comparability. Furthermore, the Eurogroup expressed its intention to take stock of the state of play in the reduction of the tax burden on labour when discussing the DBPs of euro area Member States.

The tax wedge on labour measures the difference between the total labour costs to employ a worker and the worker’s net earnings. It is made up of personal income taxes and employer and employee social security contributions. The higher the tax wedge, the higher the disincentives to take up work or hire new staff. The graphs below show the tax wedge in Austria for a single worker earning respectively the average wage and a low wage (50% of the average) compared to the EU average.

The tax burden on labour in Austria at the average wage and a low wage (2014)



Notes: Data for Latvia, Lithuania and Malta is for 2013. No recent data is available for Cyprus. EU and EA averages are GDP-weighted. The OECD average is not weighted.

Source: European Commission Tax and Benefit Indicator database based on OECD data.

This screening is only the first step in the process towards firm, country-specific policy conclusions. The tax burden on labour interacts with a wide variety of other policy elements such as the benefit system and the wage-setting system. A good employment performance indicates that the need to reduce labour taxation may be less urgent while fiscal constraints can dictate that labour tax cuts should be fully offset by other revenue-enhancing or expenditure-reducing measures. In-depth, country-specific analysis is necessary before drawing policy conclusions.

In the context of the 2015 European Semester, Austria was issued the recommendation to "(...) ensure the budget neutrality of the tax reform aimed at reducing the tax burden on labour (...).". Austria's DBP refers to the measures described in the 2015 National Reform Progamme and adopted in mid-July 2015, that affect the tax wedge in the following ways:

- The re-modulation of the tax brackets and of the tax rates. The number of tax brackets will move up from 3 to 6 and the entry tax-rate will be reduced from 36.5% to 25% up to EUR 18000 of annual income. The tax base for the 50% tax rate will be increased from 60000 to 90000 and a temporary 55% tax rate is envisaged for annual income above EUR 1 million.

- The reimbursement of half of social security contributions for very low income earners.

The tax reform was adopted in mid-2015. Overall, the reform will cost EUR 5.2 billion (1.5% of GDP), but the comparison between the no-policy change and the policy change scenarios shows that only EUR 4.1 billion of tax relief will materialize in 2016, of which EUR 3.9 billion for lower wage tax and Eur 200 million for reimbursement of social security contributions.

As to the 2015 SP and DBP, the tax reform is expected to be fully counter-financed and budgetary neutral. The main measures to finance the cost of the reform were specified in the SB, and consist in: i) raising additional resources from fighting tax frauds by introducing compulsory cash registers and providing full access to bank accounts to tax authorities in case of tax audits; ii) increasing the reduced-rates of the VAT tax for certain products from 10% and 12% to 13%; iii) increasing the tax rate on capital income from 25% to 27.5%; iv) raising to 30% the real estate gains tax and widening the tax base from unremunerated real estate transfers; v) introducing a single rate for depreciation of buildings of business property. On the expenditure side the programme reports the aim of achieving savings from reduction in state subsidies and public administration reforms.

As to the yields of the different measures, the amounts specified in the SP are different from those emerging in the DBP from the comparison between the no-policy change and the policy change scenarios, possibly because the SB assumes the full effect of the reform while the DBP only refers to 2016. The DBP does not report a precise estimate of the exact amounts expected by each measure, but this can be reconstructed by comparing the DBP with the document "*Analysis of the tax reform 2015/2016*" prepared by the budget service of the Austrian Parliament. In 2016, the different measures are expected to yield to: i) EUR 1.9 billion from fighting tax fraud; ii) a total of EUR 200 million from the increase of VAT, the introduction of a single depreciation rate for buildings and other changes in tax law; iii) EUR 400 million from the increase of other taxes; iv) EUR 0.9 billion from reduction in administrative spending and subsidies. Furthermore, there is a negative balance of EUR 600 million (0.18% of GDP), which can be considered as implicitly covered by second-round effects of the reform, mentioned in the SP but not in the DBP.

As to the measures aimed at counter-financing the reform, the DBP estimations present several uncertainties and seem to reflect a rather optimistic approach, especially in connection with measures combating tax fraud. Nevertheless, compared to the spring forecast the Commission revises upwards the estimations of the effects of the counter-financing measures, given that additional supported documents were provided and that the DBP itself discounted the effects of some of the measures if compared to the SP –since now only part of the reform was considered as implemented in 2016. In particular, while in spring the commission discounted 50% of the revenues expected from combating tax fraud, the Commission autumn forecast discounts only 20% of the effect, given that the Austrian government provided a comparative study analysing similar measures implemented in countries facing comparable economic conditions. As to the second-round effects of the reform, the Commission maintained its reservation and treated them as an upward risk, given the high uncertainty as to the size and timing of such effects. Overall, the scenario underlying the Commission Autumn forecast, by including only part of the resources to cover the cost of the tax reform, would suggest that the reform could be underfinanced by around 0.3% of GDP.

6. OVERALL CONCLUSION

Based on the Commission 2015 autumn forecast, the structural improvement in both 2015 and 2016 respects the minimum linear structural adjustment required to satisfy the transitional debt rule.

With regard to the adjustment path towards the MTO, the assessment of the DBP points to compliance with the required adjustment towards the MTO in 2015, and to some deviation in 2016. As to the Commission autumn forecast, the overall assessment points to a risk of significant deviation from the MTO in 2016. However, in case the current estimate of the budgetary impact of the exceptional inflow of refugees was excluded from the assessment, the projected deviation would no longer be significant.