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COMMISSION STAFF WORKING DOCUMENT

Analysis of the draft budgetary plan of Austria

Accompanying the document

COMMISSION OPINION

on the draft budgetary plan of Austria

{C(2017) 8010 final}

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COMMISSION OPINION

on the draft budgetary plan of Austria

1. INTRODUCTION

Austria submitted its Draft Budgetary Plan (DBP) for 2018 on 17 October 2017 in compliance with Regulation (EU) No 473/2013 of the Two-Pack. Given the caretaker nature of the government in place on 17 October 2017, the budgetary projections for 2017 and 2018 in the DBP are based on unchanged policies and include only measures that have been adopted before the national elections of 15 October 2017. Austria is subject to the preventive arm of the Pact and should ensure sufficient progress towards its medium term budgetary objective (MTO). As the debt ratio was 81.0% of GDP in 2013 (the year in which Austria corrected its excessive deficit), exceeding the 60% of GDP reference value, Austria was also subject to the transitional arrangements as regards compliance with the debt reduction benchmark during the three years following the correction of the excessive deficit. In this period it needed to ensure sufficient progress towards compliance with the debt reduction benchmark. Following the end of the transition period, Austria is subject to the debt reduction benchmark.

Section 2 of this document presents the macroeconomic outlook underlying the Draft Budgetary Plan and provides an assessment based on the Commission 2017 autumn forecast. The following section presents the recent and planned fiscal developments, according to the Draft Budgetary Plan, including an analysis of risks to their achievement based on the Commission 2017 autumn forecast. In particular, it also includes an assessment of the measures underpinning the Draft Budgetary Plan. Section 4 assesses the recent and planned fiscal developments in 2017-2018 (also taking into account the risks to their achievement) against the obligations stemming from the Stability and Growth Pact. Section 5 provides an analysis on the composition of public finances and on fiscal-structural reforms in response to the latest country-specific recommendations adopted by the Council on 11 July 2017. Section 6 summarises the main conclusions of the present document.

2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

The macroeconomic scenario underlying the DBP projects GDP growth to accelerate from 1.5% in 2016 to 2.8% in 2017, and then to stabilise at 2.8% in 2018. This represents a significantly more positive assessment of GDP growth in both 2017 and 2018 compared to the 2017 Stability Programme, which expected an increase of 2.0% in 2017 and of 1.8% in 2018. The DBP growth projection is broadly in line with the Commission 2017 autumn forecast for the year 2017 of 2.6% and slightly more optimistic for 2018, where the Commission expects a deceleration of GDP growth to 2.4%. Compared to the DBP, the Commission expects weaker

Table 1. Comparison of macroeconomic developments and forecasts

	2016	2017			2018		
	COM	SP	DBP	COM	SP	DBP	COM
Real GDP (% change)	1.5	2.0	2.8	2.6	1.8	2.8	2.4
Private consumption (% change)	1.5	1.3	1.5	1.4	1.2	1.7	1.5
Gross fixed capital formation (% change)	3.7	2.6	4.2	3.9	2.4	3.0	2.7
Exports of goods and services (% change)	1.9	3.6	5.5	5.3	3.4	4.8	4.5
Imports of goods and services (% change)	3.1	3.3	5.1	4.3	3.0	3.9	3.3
Contributions to real GDP growth:							
- Final domestic demand	2.0	1.5	2.0	1.9	1.4	1.8	1.6
- Change in inventories	0.0	0.2	0.4	0.0	0.0	0.4	0.0
- Net exports	-0.5	0.3	0.4	0.7	0.3	0.6	0.8
Output gap[1]	-1.0	-0.4	0.0	-0.2	0.0	0.7	0.1
Employment (% change)[2]	1.2	1.3	1.5	1.5	1.1	1.5	1.3
Unemployment rate (%)	6.0	5.9	5.6	5.6	5.9	5.4	5.5
Labour productivity (% change)[2]	0.2	0.6	1.3	1.1	0.7	1.2	1.1
HICP inflation (%)[3]	1.0	1.8	1.9	2.0	1.7	1.8	1.6
GDP deflator (% change)	1.1	1.4	1.9	1.8	1.5	2.0	1.6
Comp. of employees (per head, % change)[2]	2.4	1.9	2.3	2.3	2.0	2.7	2.3
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	2.1	1.6	2.7	2.0	1.6	2.9	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.

[2]The DBP 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 DBP, which correspond to the national definition.

[3]The inflation presented in the SP and the DBP represent the national CPI.

Source:

Stability Programme 2017 (SP); Draft Budgetary Plan for 2018 (DBP); Commission 2017 autumn forecast (COM); Commission calculations

growth of private consumption and of gross fixed capital formation in 2018. Both the DBP and the Commission 2017 autumn forecast expect GDP growth in 2018 to be mainly driven by domestic demand. Similarly, both the DBP and the Commission forecast project inflation in Austria to remain above the euro area average, as inflation in the services sector continues to be strong.

The DBP's macroeconomic assumptions are plausible until 2017 and favourable thereafter. Both the DBP and the Commission forecast expect a more substantial contribution of net exports to economic growth compared to the projections of the Stability Programme due to improved expectations relating to the external environment. Based on the strong economic outlook, both the DBP and the Commission forecast expect strong employment growth and a consequently falling unemployment rate.

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

The DBP for 2018 submitted by Austria is based on the macroeconomic forecast published by the Austrian Institute of Economic Research (WIFO) on 29 September 2017. WIFO is a non-profit association under Austrian law, recognised for high-quality economic research and realistic and unbiased forecasts. 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.

3. RECENT AND PLANNED FISCAL DEVELOPMENTS

3.1. Deficit developments

The DBP projects the general government headline balance at -0.9% of GDP in 2017, revising slightly upwards the projections of the Stability Programme (-1.0% of GDP) due to higher expected revenues. The Commission 2017 autumn forecast expects the 2017 headline balance at -1.0% of GDP. The difference from the DBP projections is due to slightly more conservative assumptions on interest expenditure and on collected revenues. In particular, revenues from taxes on production and imports and social security contributions are expected to be slightly lower in the Commission 2017 autumn forecast compared to the DBP, also due to small differences in the projected private consumption and employment growth.

In 2018, the DBP expects the headline deficit to marginally narrow to -0.8% of GDP, confirming the target of the Stability Programme. Compared to the Stability Programme, both revenue and expenditure projections have been revised upwards, due to the brighter macroeconomic outlook and additional spending measures. The Commission 2017 autumn forecast expects the headline balance at -0.9% of GDP in 2018, with the difference from the DBP projections being largely due to base effects. Compared to the DBP, both revenue and expenditure are expected to develop somewhat less dynamically, due to more conservative macroeconomic projections and weaker projected growth in compensation of employees and social payments, respectively.

The main risks to the DBP budgetary projections relate to the favourable economic outlook underlying the revenue forecasts. In addition, some of the recently implemented policy measures, such as the "employment bonus" and the "action 20 000", could result in higher costs than currently estimated. Furthermore, as future tax cuts have been often mentioned during the electoral campaign, the possibility that the new government will implement an expansionary fiscal policy represents an additional risk for budgetary projections.

Euro area sovereign bond yields remain at historically low levels, with 10-year rates in Austria currently standing at 0.5[1]. As a consequence, total interest payments by the general government have continued to decrease as a share of GDP. Based on the information included in the Draft Budgetary Plan, interest expenditure in Austria is expected to fall from 2.1% of GDP in 2016 to 1.8% in 2017 and is projected to decrease further next year, to 1.6% of GDP, well below the 2.7% recorded back in 2012 at the peak of the euro area sovereign debt crisis. The picture stemming from Austria's plans is broadly confirmed by the Commission forecast.

[1] 10-year bond yields as of 6 November 2017. Source: Bloomberg.

Table 2. Composition of the budgetary adjustment

(% of GDP)	2016	2017			2018			Change: 2016-2018
	COM	SP	DBP	COM	SP	DBP	COM	DBP
Revenue	**49.1**	**49.5**	**48.7**	**48.8**	**49.4**	**48.1**	**48.3**	**-1.0**
of which:								
- Taxes on production and imports	14.4	14.5	14.2	14.1	14.2	13.8	13.7	-0.6
- Current taxes on income, wealth, etc.	13.0	13.3	13.1	13.2	13.5	13.1	13.2	0.1
- Capital taxes	0.0	0.2	0.2	0.0	0.2	0.2	0.0	0.2
- Social contributions	15.3	15.4	15.2	15.2	15.4	15.1	15.1	-0.2
- Other (residual)	6.4	6.1	6.0	6.3	6.1	5.9	6.2	-0.5
Expenditure	**50.7**	**50.6**	**49.6**	**49.8**	**50.3**	**48.9**	**49.2**	**-1.8**
of which:								
- Primary expenditure	48.6	48.6	47.7	47.9	48.5	47.3	47.5	-1.3
of which:								
Compensation of employees	10.7	10.7	10.5	10.6	10.6	10.4	10.4	-0.3
Intermediate consumption	6.4	6.4	6.3	6.3	6.4	6.1	6.2	-0.3
Social payments	23.1	23.2	22.6	22.7	23.3	22.4	22.4	-0.7
Subsidies	1.4	1.4	1.5	1.5	1.4	1.6	1.6	0.2
Gross fixed capital formation	3.0	3.0	3.0	3.0	3.0	3.0	3.0	0.0
Other (residual)	4.0	3.9	3.8	4.0	3.8	3.8	3.9	-0.2
- Interest expenditure	2.1	2.0	1.8	1.9	1.8	1.6	1.7	-0.5
General government balance (GGB)	**-1.6**	**-1.0**	**-0.9**	**-1.0**	**-0.8**	**-0.8**	**-0.9**	**0.9**
Primary balance	**0.5**	**0.9**	**0.9**	**0.9**	**1.0**	**0.8**	**0.8**	**0.4**
One-off and other temporary measures	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.1
GGB excl. one-offs	**-1.6**	**-1.0**	**-0.8**	**-1.0**	**-0.8**	**-0.8**	**-0.9**	**0.8**
Output gap[1]	-1.0	-0.4	0.0	-0.2	0.0	0.7	0.1	1.7
Cyclically-adjusted balance[1]	-1.1	-0.8	-0.9	-0.9	-0.8	-1.2	-1.0	-0.1
Structural balance (SB)[2]	**-1.0**	**-0.8**	**-0.8**	**-0.9**	**-0.8**	**-1.2**	**-1.0**	**-0.2**
Structural primary balance[2]	1.1	1.2	1.0	1.0	1.0	0.4	0.8	-0.7

Notes:

[1]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the DBP/programme as recalculated by Commission on the basis of the DBP/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 2017 (SP); Draft Budgetary Plan for 2018 (DBP); Commission 2017 autumn forecast (COM); Commission calculations

Based on the information provided in the DBP, the structural balance[2] is expected to improve from -1.0% of GDP in 2016 to -0.8% of GDP in 2017, thanks to the improving headline balance. In 2018, the (recalculated) structural balance is expected to deteriorate to -1.2% of GDP, as the projected improvement in the headline balance is small compared to the improvement of the economic cycle. The Commission 2017 autumn forecast projects the structural balance at -0.9% of GDP in 2017 and -1.0% of GDP in 2018. The different headline balance projections and the narrower estimated output gap in 2018 drive the difference from the DBP (recalculated) structural balance.

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

Against the background of falling interest expenditure, the projected improvement and deterioration in the structural balance in 2017 and 2018 (+0.2% of GDP and -0.4%, respectively) are accompanied by a slight and a larger deterioration in the structural primary balance (-0.1% of GDP and -0.6%, respectively).

The headline deficit projected by the DBP is driven both in 2017 and 2018 by the deficit of the central government (-0.9% of GDP in both years), while federal states and municipalities are expected to have balanced accounts and social security funds to produce a small surplus in both years. The DBP does not specify the expected contributions of the different government subsectors to the structural balance. The national fiscal rules embedded in the 2012 Austrian Stability Pact require Austria to achieve a structural balance of -0.45% of GDP from 2017 onwards, with the upward limit set at -0.35% of GDP for the federal government (including social security funds) and -0.1% of GDP for federal states and municipalities.

The projected (recalculated) structural balance in 2017 might comply with the national structural target, if the same allowance for exceptional events granted by the Commission is considered. In 2018, the projected (recalculated) structural balance appears to fall short of the national structural target, even after considering the same allowance granted by the Commission. In May 2017, the national Fiscal Council produced an assessment on all national fiscal rules for the period 2012-2015, based on the projections of the Stability Programme. The assessment concluded that the national fiscal rules had been respected by the federal states and the municipalities during that period.

The Austrian authorities indicated in the 2017 Stability Programme that the budgetary impact of the additional costs related to the exceptional inflow of refugees and the terrorist threat is significant and should be considered as an unusual event outside the control of the government, as defined in Article 5.1 and Article 6.3 of Regulation (EC) No 1466/97. More specifically, this expenditure in 2017 was estimated at 0.47% of GDP concerning refugees and 0.05% of GDP concerning security costs. In relation to this, Austria requested a temporary deviation from the adjustment path towards the MTO of 0.01% of GDP in 2017, corresponding to the expected increase in security costs from 2016.

In the present DBP the government has revised slightly those projections for costs related to the exceptional inflow of refugees, that are currently estimated at 0.50% of GDP in 2017.

The Commission provisionally assessed Austria to be eligible for an allowance of 0.02% of GDP in 2017 in relation to the incremental costs considered by the Commission to have a clear and direct link to refugee inflows and security. The carry-forward effect of these costs in 2018 is estimated at 0.02% of GDP. The Commission will make a final assessment, including on the eligible amounts, in spring 2018 on the basis of observed data as provided by the authorities.

3.2. Debt developments

According to the DBP, government debt is set to decline significantly from 83.6% of GDP to 78.3% of GDP in 2017. The decline is driven by a large disposal of earnings from the wind-down of the bad bank HETA, which were used to reduce governmnent debt (1.2% of GDP), and a base effect from pre-payments related to the same bad bank HETA that temporarily

Table 3. Debt developments

(% of GDP)	2016	2017			2018		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio[1]	**83.6**	**80.8**	**78.3**	**78.6**	**78.5**	**75.2**	**76.2**
Change in the ratio	-0.8	-2.8	-5.3	-4.9	-2.3	-3.1	-2.4
Contributions[2]:							
1. Primary balance	**-0.5**	**-0.9**	**-0.9**	**-0.9**	**-1.0**	**-0.8**	**-0.8**
2. "Snow-ball" effect	**0.0**	**-0.7**	**-1.9**	**-1.6**	**-0.8**	**-1.9**	**-1.3**
Of which:							
Interest expenditure	2.1	1.9	1.8	1.9	1.8	1.6	1.7
Growth effect	-1.2	-1.6	-2.2	-2.1	-1.4	-2.1	-1.8
Inflation effect	-0.9	-1.0	-1.5	-1.4	-1.2	-1.5	-1.2
3. Stock-flow adjustment	**-0.3**	**-1.1**	**-2.4**	**-2.4**	**-0.5**	**-0.3**	**-0.3**
Of which:							
Cash/accruals difference							
Net accumulation of financial							
of which privatisation proceeds							
Valuation 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:

Stability Programme 2017 (SP); Draft Budgetary Plan for 2018 (DBP); Commission 2017 autumn forecast (COM); Commission calculations

increased debt in 2016 (1.0% of GDP). Together with the sale of impaired assets from the other bad banks included into government accounts (KA Finanz and Immigon), these transactions generated a large negative stock-flow adjustment (-2.4% of GDP). In 2018, government debt is expected to decline further to 75.2% of GDP, supported again by the divestment of impaired assets from bad banks included into government accounts (0.3% of GDP). Both in 2017 and 2018, the decline of government debt projected by the DBP is also supported by the declining interest expenditure, the contribution of the primary balance and the strong nominal GDP growth (denominator effect). Based on the Commission 2017 autumn forecast, government debt is expected to follow similar dynamics, declining to 78.6% of GDP in 2017 and to 76.2% of GDP in 2018. The decline is slower compared to the DBP projections, due to the slightly more conservative projections of the primary balance, interest expenditure and nominal GDP growth.

3.3. Measures underpinning the draft budgetary plan

As Austria presented a no-policy-change DBP, the budgetary projections assume unchanged policies and are not underpinned by additional measures. Nevertheless, the DBP reports several measures implemented since the submission of the Stability Programme. Although the individual budgetary effect of each measure is not reported, the measures are all deficit-increasing, with an estimated total budgetary impact of 0.1% of GDP in 2017 as reported in the DBP. In 2018, although no estimates are presented, the costs will likely be higher than in 2017, as several measures will take effect only from next year. No financing is currently envisaged, but the DBP reports that the measures will be financed by the incoming government within the next medium-term expenditure framework. The measures are aimed at supporting the labour market, fostering the integration of refugees and strenghtening research and development as well as investment and education. The policy measure with the likely highest budgetary impact is the so-called "employment bonus", reimbursing half of employer social security contributions for newly hired employees during their first three years, under certain conditions (see box 3). The reported measures are expected to have an overall positive effect on economic growth in the short and the medium term, although they significantly increase government spending both in 2017 and 2018. The DBP does not report significant one-off measures over 2017-2018.

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 debt reduction benchmark.

Box 2. 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 that Austria take action in 2017 and 2018 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 recalled 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 autumn 2017 forecast that Austria will be closer to its MTO in 2017 and in line with the arrangements in place for updating the fiscal requirements contained in the country-specific recommendations,[3] the nominal growth rate of net primary government expenditure should not exceed 2.6%, corresponding to an improvement in the structural balance by 0.1% of GDP.

[3] These arrangements, known as the 'unfreezing' principle, are referred to in the Opinion of the Economic and Financial Committee of the Council on "Improving the predictability and transparency of the SGP: A stronger focus on the expenditure benchmark in the preventive arm", of 29 November 2016, and have been specified further in subsequent discussions with the Member States.

4.1. Compliance with the debt criterion

As its public debt exceeds the 60% of GDP reference value of the Treaty, Austria needs to comply with the debt reduction benchmark.

The DBP does not include sufficient information to assess compliance with the debt reduction benchmark in 2017 and 2018. According to the Commission 2017 autumn forecast, Austria is expected to meet the debt reduction benchmark both in 2017 and 2018, as its debt-to-GDP ratio is expected to be below the debt benchmark on a no-policy-change basis, with a gap to the debt benchmark of -4.0% of GDP in 2017 and -3.7% of GDP in 2018.

Table 4. Compliance with the debt criterion*

	2016	2017			2018		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio	83.6	80.8	78.3	78.6	78.5	75.2	76.2
Gap to the debt benchmark [1,2]		-3.1	n.a.	-4.0	-3.1	n.a.	-3.7
Structural adjustment [3]	-0.7	0.2	0.2	0.1	0.0	-0.4	-0.1
To be compared to:							
Required adjustment [4]	-1.1	n.r.	n.r.	n.r.	n.r.	n.r.	n.r.

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 2017 (SP); Draft Budgetary Plan for 2018 (DBP); Commission 2017 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 required adjustment path towards the MTO

In 2015, Austria was granted a temporary deviation from the adjustment path towards the MTO amounting to 0.09% of GDP in relation to the exceptional inflow of refugees. In 2016, an additional temporary deviation of 0.25% of GDP was granted in relation to the exceptional inflow of refugees and 0.04% of GDP for additional security measures related to the terrorist

Table 5: Compliance with the requirements of the preventive arm

(% of GDP)	2016	2017		2018	
Initial position[1]					
Medium-term objective (MTO)	-0.5	-0.5		-0.5	
Structural balance[2] (COM)	-1.0	-0.9		-1.0	
Structural balance based on freezing (COM)	-0.9	-0.9		-	
Position vis-a -vis the MTO[3]	At or above the MTO	Not at MTO		Not at MTO	
(% of GDP)	**2016**	**2017**		**2018**	
	COM	**DBP**	**COM**	**DBP**	**COM**
Structural balance pillar					
Required adjustment[4]	0.0	0.4		0.4	
Required adjustment corrected[5]	-0.9	0.0		0.1	
Change in structural balance[6]	-0.8	0.2	0.1	-0.4	-0.1
One-year deviation from the required adjustment [7]	0.1	0.2	0.2	-0.4	-0.2
Two-year average deviation from the required adjustment [7]	0.5	0.1	0.1	-0.1	0.0
Expenditure benchmark pillar					
Applicable reference rate[8]	2.9	1.1		2.6	
One-year deviation adjusted for one-offs [9]	-0.4	-0.3	-0.3	-0.7	-0.4
Two-year average deviation adjusted for one-offs [9]	0.0	-0.4	-0.3	-0.5	-0.3
PER MEMORIAM: One-year deviation [10]	-0.1	-0.2	-0.2	-0.7	-0.4
PER MEMORIAM: Two-year average deviation [10]	-0.1	-0.2	-0.2	-0.5	-0.3
Conclusion					
Conclusion over one year	Overall assessment	Overall assessment	Overall assessment	Overall assessment	Overall assessment
Conclusion over two years	Compliance	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 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 2016) was carried out on the basis of Commission 2017 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, 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.

Source :

Draft Budgetary Plan for 2018 (DBP); Commission 2017 autumn forecast (COM); Commission calculations.

threat. The carry-forward effect of these costs amounts to 0.38% of GDP in 2017 and 0.29% of GDP in 2018.[4]

According to the information provided in the DBP, in 2017 the real growth rate of net primary government expenditure will exceed the applicable expenditure benchmark rate (gap of -0.3% of GDP), pointing to a risk of some deviation. According to the programme, the (recalculated) structural balance is expected to improve by 0.2% of GDP (to -0.8% of GDP), in compliance with the required adjustment (gap of 0.2% of GDP). Over 2016 and 2017 together, the expenditure benchmark points to a risk of significant deviation (gap of -0.4% of GDP), while the (recalculated) structural balance points to compliance (gap of 0.1% of GDP). This calls for an overall assessment. The difference between the two indicators is largely driven by the different underling estimates of potential growth. The expenditure benchmark appears to more adequately reflect the fiscal effort. While the 10-year average of potential growth underpinning the expenditure benchmark appears more robust and thus preferable, there might still be some uncertainty on the actual potential growth underpinning the Austrian economy. The structural balance is flattered by a more favourable reading of economic potential and supported by the declining interest spending, although negatively affected by a small revenue shortfall. After considering all these factors, the overall assessment points to a risk of some deviation in 2017 and of significant deviation for 2016 and 2017 together, based on the expenditure benchmark pillar. This conclusion is confirmed based on the Commission 2017 autumn forecast, and would not change in case the additional budgetary impact of the inflow of refugees and the exceptional security measures in 2017 were excluded from the assessment.

Based on the information provided in the DBP, in 2018 the nominal growth rate of government expenditure, net of discretionary revenue measures and one-offs, will exceed the applicable expenditure benchmark rate (gap of -0.7% of GDP), pointing to a risk of significant deviation.[5] The (recalculated) structural balance is expected to deteriorate by 0.4% of GDP (to -1.2% of GDP), pointing to a risk of some deviation from the recommended structural adjustment (deviation of -0.4% of GDP). This calls for an overall assessment. Similarly to 2017, the structural balance benefits from a more favourable estimate of economic potential and savings in interest expenditure, but is negatively affected by revenue shortfalls. Taking these aspects into consideration, the overall assessment points to a risk of significant deviation in 2018 based on the expenditure benchmark pillar.

Based on the Commission 2017 autumn forecast, in 2018 both the expenditure benchmark and the structural balance point to a risk of some deviation (gap of -0.4% and -0.2% of GDP respectively). Over 2017-2018 together, the expenditure benchmark points to a risk of significant deviation (gap of -0.3% of GDP), while the structural balance points to compliance (no deviation from the required adjustment). Similarly to the projections of the DBP, the difference between the two indicators is driven by the different assumptions on potential growth, with the structural balance being also supported by declining interest expenditure and

[4] In analogy to the implementation of the structural reform clause and the investment clause, temporary deviations granted on behalf of the unusual events clauses are carried forward for a total of three years as an allowed distance from the MTO. This is to ensure that Austria benefits from the granted temporary deviation similarly to countries not yet close to their medium-term budgetary objective.

[5] 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.

negatively affected by revenue shortfalls. Considering all these factors, the expenditure benchmark appears to more adequately reflect the fiscal effort. Therefore, the overall assessment based on the Commission 2017 autumn forecast points to a risk of some deviation in 2018 and of significant deviation for 2017 and 2018 together.

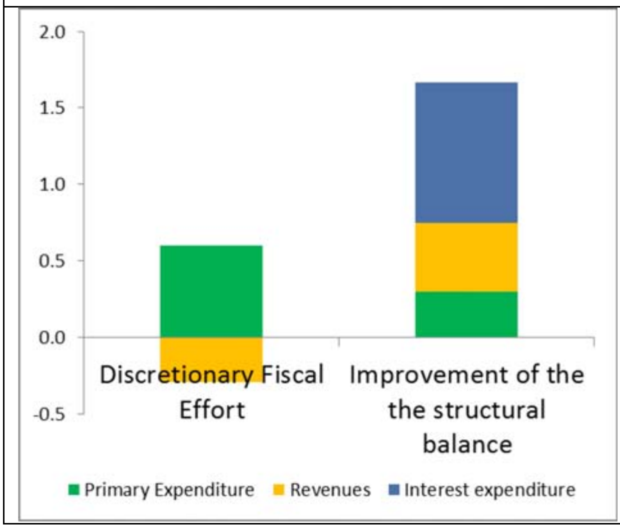
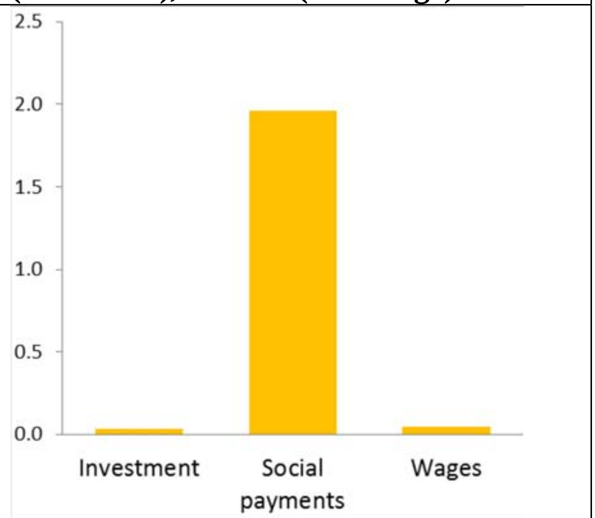
This conclusion would not change in case the carry-over of the additional budgetary impact of the inflow of refugees and the exceptional security measures in 2017 were excluded from the assessment for 2018.

An overall assessment based on the draft budgetary plan and the Commission 2017 autumn forecast, points to a risk of significant deviation from the required adjustment path towards the MTO in 2017 and 2018.

5. Composition of public finances and Implementation of fiscal structural reforms

The nominal adjustment projected by the DBP in 2018 is driven by a stronger decline of expenditure with respect to revenues as a percentage of GDP, with revenues expected to decline by 0.6% of GDP and expenditure by 0.7% of GDP (to 48.1% and 48.9% of GDP in 2018, respectively). Similarly, over 2011-2017 the projected improvement of the structural balance is largely driven by declining expenditure, mainly due to lower interest spending but also linked to a reduction in primary expenditure. Revenue growth played also an important role in supporting the structural balance over 2011-2017, and was so strong to more than offset the impact of legislated tax cuts.

Based on the DBP projections, in 2018 public investment is expected to remain broadly stable at 3% of GDP, which is the same rate observed since 2011. Also expenditure for public wages is expected to remain broadly constant as a percentage of GDP at the same rate observed since 2011, while a strong increase in social payments is expected over 2011-2017.

Graph 1: Composition of the fiscal effort (2011-2017), Austria (% GDP)	**Graph 2: Change in the share in total expenditure of selected expenditure items (2011-2017), Austria (% change)**
	

Source:

Draft Budgetary Plans 2018, European Commission 2017 autumn forecast.

Note:

Graph 1 shows the Discretionary Fiscal Effort (DFE) which combines a top-down approach on the expenditure side with a bottom-up or narrative approach on the revenue side. In a nutshell, the DFE consists of the increase in primary expenditure net of cyclical components relative to economic potential on the one hand, and of discretionary revenue measures on the other hand. See European Commission (2013): Measuring the fiscal effort, Report on Public Finances in EMU, part 3.
http://ec.europa.eu/economy_finance/publications/european_economy/2013/pdf/ee-2013-4.pdf

Overall, Austria's tax structure relies heavily on taxes on labour, with social security contributions and yields from income taxes paid by households representing a relatively high share of total revenues. The DBP presents several measures implemented since the Stability Programme that could contribute to improve the growth-friendliness of the tax system. On the business side, the research bonus for corporations has been increased starting from 2018, while a temporary investment bonus for large companies was implemented in 2017. In addition, the tax on flight tickets is halved from 2018. On the labour side, the "employment bonus" will temporarily reduce employer social security contributions (see box 4).

The DBP reports several measures addressing the fiscal-structural part of the country-specific recommendations. Concerning streamlining fiscal relations and responsibilities across the various layers of government, the DBP reports two Parliamentary decisions taken since the Stability Programme. In particular, the autonomy of federal states in setting the rate for the contributions to house subsidies has been ratified, while educational boards were created as a cross-regional inter-governmental authority for education. Common education boards represent a positive step towards harmonising education policies across federal states and streamlining inter-governmental responsibilities in the area of education. Nevertheless, the measure does not affect the general misalignment between managing and funding responsibilities of federal states. The same applies to the increased tax autonomy of federal states, which remains small compared to their spending powers. Several other initiatives included in the 2017 Financial Equalisation Law appear as more promising and deserve a thorough implementation. These include spending reviews, benchmark systems and task-oriented financing at the subnational level as well as a general reform of inter-governmental competencies. Concerning the sustainability of the healthcare system, the DBP reports the ratified plan to expand the provision of primary care, which could contribute to reduce the size of the hospital sector and improve efficiency in the medium term. No new measures are mentioned concerning the sustainability of the pension system.

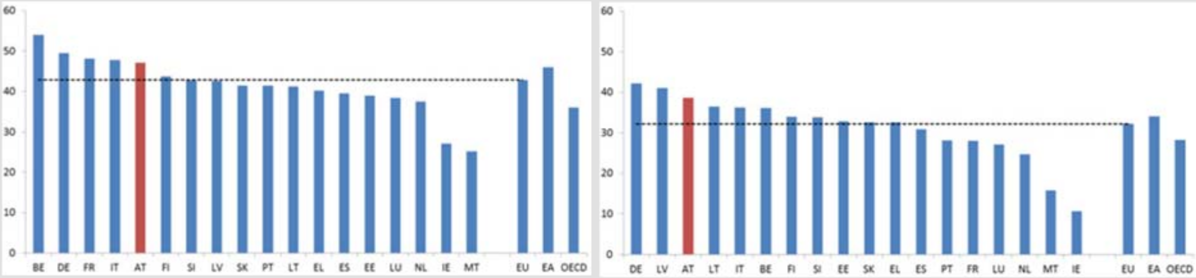
Box 3 – Addressing the tax burden on labour in the euro area

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 benchmark 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.

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 at low wage (2016)



Notes: 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.

Benchmarking 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 2017 European Semester, and in particular in recital 12 of the country-specific recommendations to Austria, it was mentioned that the tax wedge on labour in Austria remains relatively high despite the 2016 tax reform, while more growth-friendly sources of revenue, such as recurrent property taxes, are underutilised.

Austria's Draft Budgetary Plan contains one measure that affects the tax wedge on labour, i.e. the "employment bonus". Half of employer social security contributions for newly hired employees can be reimbursed upon request, during the first three years, starting in July 2017. The "employment bonus" only applies to employees that previously worked in Austria, were registered as unemployed in Austria or graduated from an Austrian university. No financing is envisaged yet, while the overall cost is capped at EUR 2.2 billion up to 2023. Nevertheless, given the projected strong employment growth, it cannot be excluded that costs will exceed estimates in 2017 and 2018, depending on the uptake of the initiative. In the current positive phase of the economic cycle, this measure is expected to have limited impact on growth, and could result in reimbursing social security contributions for workers that would have been hired anyway.

6. OVERALL CONCLUSION

Based on the Commission 2017 autumn forecast, Austria is expected to meet the debt reduction benchmark both in 2017 and 2018

Following an overall assessment of the no-policy-change DBP, the projected structural adjustment points to a risk of significant deviation both in 2017 and 2018. The conclusion is confirmed based on the Commission 2017 autumn forecast, and would not change in case the current estimate of the budgetary impact of the exceptional inflow of refugees and security measures in 2017 is deducted from the assessment.