

## I

*(Resolutions, recommendations and opinions)*

## OPINIONS

## COUNCIL

## COUNCIL OPINION

**of 4 March 2008**

**on the updated stability programme of Austria, 2007-2010**

(2008/C 74/01)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies <sup>(1)</sup>, and in particular Article 5(3) thereof,

Having regard to the recommendation of the Commission,

After consulting the Economic and Financial Committee,

HAS DELIVERED THIS OPINION:

- (1) On 4 March 2008, the Council examined the updated stability programme of Austria, which covers the period 2007 to 2010.
- (2) Over the last few years, Austria has experienced robust economic growth, surpassing that of other euro area countries on average. With private consumption being sluggish, the main contributions to growth came from net exports and investment. Continued wage moderation helped to maintain price stability while boosting external competitiveness.

The Austrian labour market has been performing well, with the unemployment rate being one of the lowest in the EU and the overall employment rate higher than the 70 % targeted by the Lisbon strategy. However, the employment rate of older workers remains well below the EU average. With public debt in excess of 60 % of GDP, the general government deficit has been declining since 2005, but the achievement of a balanced budget has been repeatedly postponed. Lasting consolidation of public finances will hinge also on an overhaul of fiscal relations between different government levels as the present ones are overly complicated and lack transparency.

<sup>(1)</sup> OJ L 209, 2.8.1997, p. 1. Regulation as amended by Regulation (EC) No 1055/2005 (OJ L 174, 7.7.2005, p. 1). The documents referred to in this text can be found at the following website:  
[http://ec.europa.eu/economy\\_finance/about/activities/sgp/main\\_en.htm](http://ec.europa.eu/economy_finance/about/activities/sgp/main_en.htm)

- (3) The macroeconomic scenario underlying the programme envisages that real GDP growth will decelerate from 3,4 % in 2007 to 2,5 % on average over the rest of the programme period. Assessed against currently available information <sup>(1)</sup>, this scenario appears to be based on plausible growth assumptions. Given the latest developments in food and oil prices, inflation could turn out somewhat higher than projected in the programme, but the continued wage moderation should contribute towards maintaining high degree of competitiveness.
- (4) For 2007, the general government deficit is estimated at 0,7 % of GDP in the most recent update of the stability programme, against a target of 0,9 % of GDP set in the previous update. This improvement over the target results mainly from the better-than-expected cyclical developments, with revenue exceeding the budgetary plans and offsetting slightly higher-than-planned expenditure growth. In particular, proceeds from wage and corporate tax as well as capital yields taxes gave rise to the higher-than-planned revenue. The Council notes that, overall, budgetary implementation in 2007 could be considered broadly consistent also with the April 2007 Eurogroup orientations for budgetary policies.
- (5) The main goal of the medium-term budgetary strategy is to reach the medium-term objective (MTO) — a balanced position in structural terms (i.e. in cyclically-adjusted terms net of one-off and other temporary measures) — by 2010. The headline general government balance is planned to swing from a deficit of 0,7 % of GDP in 2007 to a 0,4 % of GDP surplus in 2010, with a back-loaded adjustment. The primary surplus is expected to improve somewhat less — by 0,9 percentage points of GDP — during the period. The structural deficit, calculated according to the commonly agreed methodology, will narrow by about 1 percentage point of GDP between 2007 and 2010 <sup>(2)</sup>. The consolidation relies largely on expenditure cuts, with restraint in social spending and gains from administrative reforms being the main factors. Compared with the previous programme, which envisaged that the MTO would be nearly reached in 2009, the new update slightly backloads the planned adjustment despite a more favourable growth performance in 2007. Government gross debt, estimated at just below the 60 % of GDP Treaty reference value in 2007, is projected to further decline by 4,5 percentage points over the programme period.
- (6) The risks to the budgetary projections in the programme appear broadly balanced for 2008, but for 2009 and 2010 the budgetary outcomes could be worse than projected, despite plausible macroeconomic assumptions. In particular, the programme does not provide sufficient information about the measures that are necessary to underpin the significant expenditure restraint envisaged in the last two years of the programme, although savings on unemployment benefits and on pensions, as a result of the 2004 pension reform, should contribute to the decline in the expenditure *ratio*. It is also not clear how the expenditure targets allow for the planned additional spending on education, R & D and infrastructure over the programme period, while the expected efficiency gains in public administration remain uncertain.

Finally, the programme announces tax cuts for 2010 without making any provision for financing them. The risks to the projected evolution of the debt *ratio* appear to be broadly balanced, with on the one hand potentially higher-than-targeted deficits endangering adherence to the adjustment path presented in the programme, but on the other hand, nominal GDP possibly turning out higher than foreseen.

- (7) In view of this risk assessment, the budgetary stance in the programme may not be sufficient to ensure that the MTO is achieved by 2010, as envisaged in the programme. However, a sufficient safety margin against breaching the 3 % of GDP deficit threshold with normal macroeconomic fluctuations will be provided throughout the programme period. In 2008, the pace of adjustment towards the MTO implied by the programme is insufficient and should be strengthened significantly to be in line with the Stability and Growth Pact, which stipulates that the annual improvement in the structural balance should be higher than 0,5 % of GDP in good economic times. The Council also

<sup>(1)</sup> The assessment takes into account notably the Commission services' autumn forecast and the Commission assessment of October 2007 implementation report of the national reform programme.

<sup>(2)</sup> If one treated the additional expenditure for military equipment as a one-off measure (which the programme does as reported in the overview table below, even though the Commission services do not), the adjustment in structural deficit would be by 0,2 percentage point lower than if these one-off measures are disregarded.

notes that the pace of adjustment in 2008 is also not consistent with the April 2007 Eurogroup orientations for budgetary policies. After 2008, the planned adjustment should be backed up with specific expenditure-saving measures.

- (8) Austria appears to be at low risk with regard to the sustainability of public finances. The long-term budgetary impact of ageing is lower than the EU average, with pension expenditure projected to decrease as a share of GDP over the long-term. The budgetary position in 2007 as estimated in the programme, which is better than the starting position of the previous programme, contributes to easing the projected long-term budgetary impact of ageing populations. Maintaining high primary surpluses over the medium term, as planned in the programme, would further contribute to limiting risks to the sustainability of public finances.
- (9) The stability programme is fully consistent with the October 2007 implementation report of the national reform programme. Focussing on the measures with a direct budgetary impact, both the stability programme and the implementation report provide for a shift in spending towards growth-orientated categories, such as R & D, infrastructure and education. Likewise, the implementation report contains information on the reforms of the public administration, health care system, as well as on the introduction of a new medium-term budgetary framework, all of which are key elements of the budgetary consolidation path presented in the stability programme.
- (10) The budgetary strategy in the programme is only partly consistent with the country-specific broad economic policy guidelines included in the integrated guidelines and the guidelines for euro area Member States in the area of budgetary policies issued in the context of the Lisbon strategy, as the structural improvement towards the MTO does not appear to be sufficient.
- (11) As regards the data requirements specified in the code of conduct for stability and convergence programmes, the programme provides all required and most of the optional data <sup>(1)</sup>.

The overall conclusion is that in a context of growth remaining close to its potential, the programme envisages slow progress towards the MTO through a relatively back-loaded adjustment that is based on not-fully-specified expenditure restraint. There are risks to the achievement of the budgetary targets after 2008 and the MTO might not be reached by the end of the programme period. The update makes no provision for financing the tax cuts announced for 2010. Government debt is expected to have decreased to just below the 60 % of GDP reference value in 2007 and to continue to decline moderately in future years. In terms of long-term sustainability of public finances, Austria appears to be at low risk.

In view of the above assessment, Austria is invited to take advantage of the slightly lower-than-targeted deficit outcome in 2007 to strengthen the adjustment effort in 2008 as well as to underpin the adjustment planned for the two final years of the programme with specific and sufficient measures, including financing of the envisaged tax reform. In this way, the MTO should be achieved earlier than foreseen in the programme, in particular by more rigorously implementing expenditure restraint and by using any unexpected tax revenues for budgetary consolidation.

The Council also notes that such actions would be consistent with the April 2007 Eurogroup orientations for fiscal policies.

#### Comparison of key macroeconomic and budgetary projections

|                        |              | 2006 | 2007 | 2008 | 2009 | 2010 |
|------------------------|--------------|------|------|------|------|------|
| Real GDP<br>(% change) | SP Nov 2007  | 3,3  | 3,4  | 2,4  | 2,5  | 2,5  |
|                        | COM Nov 2007 | 3,3  | 3,3  | 2,7  | 2,4  | n.a. |
|                        | SP Mar 2007  | 3,1  | 2,7  | 2,3  | 2,5  | 2,6  |

<sup>(1)</sup> In particular, the data on some components of the stock-flow adjustment as well as some items on long-term sustainability are not provided.

|  |                             | 2006         | 2007         | 2008         | 2009         | 2010        |
|--|-----------------------------|--------------|--------------|--------------|--------------|-------------|
| HICP inflation (%)   | <b>SP Nov 2007</b>          | <b>1,5</b>   | <b>1,9</b>   | <b>2,0</b>   | <b>2,0</b>   | <b>2,0</b>  |
|  | COM Nov 2007                | 1,7          | 1,9          | 1,9          | 1,8          | n.a.        |
|  | SP Mar 2007                 | 1,5          | 1,6          | 1,7          | 1,7          | 1,8         |
| Output gap <sup>(1)</sup> (% of potential GDP)                   | <b>SP Nov 2007</b>          | <b>- 0,5</b> | <b>0,4</b>   | <b>0,4</b>   | <b>0,5</b>   | <b>0,5</b>  |
|  | COM Nov 2007 <sup>(2)</sup> | - 0,4        | 0,4          | 0,8          | 0,8          | n.a.        |
|  | SP Mar 2007                 | - 0,3        | 0,1          | - 0,1        | 0,1          | 0,3         |
| Net lending/borrowing vis-à-vis the rest of the world (% of GDP) | <b>SP Nov 2007</b>          | <b>3,2</b>   | <b>3,5</b>   | <b>3,7</b>   | <b>3,7</b>   | <b>3,7</b>  |
|  | COM Nov 2007                | 3,3          | 4,6          | 5,2          | 5,3          | n.a.        |
|  | SP Mar 2007                 | n.a.         | n.a.         | n.a.         | n.a.         | n.a.        |
| General government balance (% of GDP)                            | <b>SP Nov 2007</b>          | <b>- 1,4</b> | <b>- 0,7</b> | <b>- 0,6</b> | <b>- 0,2</b> | <b>0,4</b>  |
|  | COM Nov 2007                | - 1,4        | - 0,8        | - 0,7        | - 0,4        | n.a.        |
|  | SP Mar 2007                 | - 1,1        | - 0,9        | - 0,7        | - 0,2        | 0,4         |
| Primary balance (% of GDP)                                       | <b>SP Nov 2007</b>          | <b>1,5</b>   | <b>2,0</b>   | <b>2,1</b>   | <b>2,3</b>   | <b>2,8</b>  |
|  | COM Nov 2007                | 1,4          | 1,7          | 1,8          | 2,0          | n.a.        |
|  | SP Mar 2007                 | 1,9          | 2,0          | 2,1          | 2,6          | 3,1         |
| Cyclically-adjusted balance <sup>(1)</sup> (% of GDP)            | <b>SP Nov 2007</b>          | <b>- 1,2</b> | <b>- 0,9</b> | <b>- 0,8</b> | <b>- 0,4</b> | <b>0,1</b>  |
|  | COM Nov 2007                | - 1,2        | - 1,0        | - 1,0        | - 0,8        | n.a.        |
|  | SP Mar 2007                 | - 1,0        | - 0,9        | - 0,7        | - 0,2        | 0,2         |
| Structural balance <sup>(3)</sup> (% of GDP)                     | <b>SP Nov 2007</b>          | <b>- 1,2</b> | <b>- 0,7</b> | <b>- 0,6</b> | <b>- 0,4</b> | <b>0,1</b>  |
|  | COM Nov 2007                | - 1,2        | - 1,0        | - 1,0        | - 0,8        | n.a.        |
|  | SP Mar 2007                 | - 1,0        | - 0,8        | - 0,4        | - 0,2        | 0,2         |
| Government gross debt (% of GDP)                                 | <b>SP Nov 2007</b>          | <b>61,7</b>  | <b>59,9</b>  | <b>58,4</b>  | <b>57,0</b>  | <b>55,4</b> |
|  | COM Nov 2007                | 61,7         | 60,0         | 58,4         | 57,2         | n.a.        |
|  | SP Mar 2007                 | 62,2         | 61,2         | 59,9         | 58,5         | 56,8        |

## Notes:

(1) Output gaps and cyclically-adjusted balances according to the programmes as recalculated by Commission services on the basis of the information in the programmes.

(2) Based on estimated potential growth of 2,2 % in 2006 and 2,4 % in 2007-2009.

(3) Cyclically-adjusted balance excluding one-off and other temporary measures. According to the most recent programme one-off and other temporary measures are 0,2 % of GDP in 2007 and 2008 and 0,1 % of GDP in 2009; all deficit-increasing (spending on military equipment). There are no one-off and other temporary measures in the Commission services' autumn forecast as the Commission services do not consider this expenditure on military equipment as a one-off.

## Sources:

Stability programme (SP); Commission services' autumn 2007 economic forecasts (COM); Commission services' calculations.