High fiscal forecasting performance of Austrian Fiscal Advisory Council

The assessment of fiscal forecasts made by the Austrian finance ministry, the European Commission and the Fiscal Advisory Council revealed that the forecast errors for the fiscal indicators for Austria (budget deficit, structural budget deficit, government revenue and expenditure) were clustered closely together. The Fiscal Advisory Council overestimated the general government deficit (in percent of GDP) during the review period (2014 to 2017) by around 0.4% on average for the current year and the subsequent year, as did the finance ministry and the European Commission (Hauth et al., 2018)[1]. By international standards, forecast errors of this magnitude can be considered as very low. According to estimates of the European Commission (Fioramanti et al., 2016)[2], forecast errors were higher in almost all EU countries for the period between 1969 and 2014, coming to around 1% of GDP or more.

Fiscal forecasts for **Austria** (finance ministry, European Commission and Fiscal Advisory Council) were found to be **biased** in the same direction, **primarily** because the cyclical **upswing** at the end of the review period (2014 to 2017) turned out to be **stronger than anticipated**. In addition, **cautious planning** of government bodies and strict budget execution might have contributed to an unduly pessimistic assessment of fiscal indicators. In the Fiscal Advisory Council's budget forecasts, the share of fundamental and discretionary errors (own estimation errors) in the forecast bias[3] came to 32%, while cyclical errors (errors in WIFO's macroeconomic forecasts that were copied by the Fiscal Advisory Council) came to 47%, and basis errors (revisions of actual outcomes by Statistics Austria) to 21%.

The **fiscal forecasts of the Fiscal Advisory Council**, like those of the **finance ministry**, are based on **macroeconomic forecasts provided by the Austrian Institute of Economic Research** (WIFO). The fiscal forecasts of the European Commission are based on the Commission's **own** economic outlook. Having mapped fiscal forecast errors to the underlying reasons, we found macroeconomic forecasts to be particularly relevant for the forecasts of revenue intake. Looking ahead, the quality of fiscal forecasts for Austria could be improved above all with measures to reduce the forecast bias for **GDP components on the income side** of the national accounts (above all compensation of employees).

The **Fiscal Advisory Council's** average **forecasting performance** in the forecasting rounds from fall 2014 to fall 2017 for the years t and t+1 corresponded roughly to that of the finance ministry and the European Commission, with forecasts for **short forecasting horizons** (forecasts for the current year t) qualifying as **unbiased** and the forecast bias being smaller than that in forecasts made by the finance ministry and the European Commission. The **period under review** included all available forecasts produced so far by the Fiscal Advisory Council, thus covering (the maximum number of) 12 data points.

The mean forecast errors for the **budget deficit** and the **structural budget deficit** in the forecasts of the Fiscal Advisory Council, the finance ministry and the European Commission were found to be similarly high in the period under review (2014 to 2017) (bias and MAE[4] of some 0.4% to 0.5% of GDP). For both fiscal indicators, the forecast errors **mainly** reflect the uncertainty surrounding forecasts of **government**

1 Hauth, E., J. Holler and P. Schuster. 2018. Fiscal forecasting performance of the Austrian Fiscal Advisory Council (see www.fiskalrat.at/en for more information).

2 Fioramanti, M., L. González Cabanillas, B. Roelstraete and S.A. Ferrandis Vallterra. 2016. European Commission's Forecasts Accuracy Revisited. European Economy Discussion Paper 27.

3 The mean error (bias) serves as an indicator for systematic distortions, indicating whether budget forecasts have tended to be either too optimistic or too pessimistic on average, with overestimations and underestimations setting each other off.

4 The mean absolute forecast error (MAE) is an indicator for forecast precision (average sum of all absolute forecast errors). Overestimations and underestimations do not offset one another in this error measure.

revenue and expenditure. The **forecast errors** for **acyclical government revenue and expenditure** (i.e. budget positions that do not rise and fall in line with economic conditions) may reflect **conceptual weaknesses** of the cyclical adjustment methods used in the fiscal rule monitoring process as well as mis-estimations of the budgetary impact of economic policy measures. However, these aspects have not been addressed in the corresponding paper.

Given the precision of fiscal forecasts made by the Fiscal Advisory Council, the finance ministry and the European Commission, the **structural budget deficit** in Austria seems to be **sufficiently predictable** and **adequate** for **use as fiscal rules** for Austria.

In the period under review (2014 to 2017), the **EU's expenditure rule** for Austria appears to have been **largely inadequate** for use as fiscal rules for Austria owing to two effects (varying targets and uncertainty surrounding government expenditure growth): In hindsight, the **varying targets** derived for Austria from the European Commission's forecasts with regard to the expenditure rule appear to have been too restrictive (bias of –0.51; MAE of 0.55 percentage points). Furthermore, the **growth rates of (adjusted, nominal) public expenditure** were **overestimated** (forecasts of the Fiscal Advisory Council: bias of 0.34; MAE of 0.39 percentage points). The expenditure rule in the EU's fiscal framework provides an additional assessment criterion for the cyclical adequacy of the budget path under the preventive arm of the Stability and Growth Pact.

The **preliminary data on actual fiscal outcomes for the past year** (available by March) published by Statistics Austria feed into the assessment of Austria's **compliance with fiscal rules** made first by the European Commission and then by the Ecofin Council. While the ex post revisions of actual outcomes were rather limited for the budget deficit, the preliminary data on **public revenue and expenditure** were found to be fraught with weaknesses. One way to improve the quality of the data that are available by March would be to **bring forward the deadlines by which the subsectoral levels of government and large off-budget units** are required to submit data to Statistics Austria.

To enhance the predictability of the budget and the forecasting performance of the Fiscal Advisory Council, the Fiscal Advisory Council would suggest improving the quality of **economic indicators** that are relevant for policymaking (e.g. for employment growth in general and the government sector), ensuring **quality costing exercises** for major government economic policy measures as well as safeguarding **broad access to official data and information,** subject to compliance with confidentiality requirements.

Inquiries: Office of the Fiscal Advisory Council, phone: (+43-1) 40420-7471.

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