RECOMMENDATIONS BY THE FISCAL ADVISORY COUNCIL ON AUSTRIA'S BUDGET POLICY FOR 2023

Be ambitious in reducing budget deficits

Background: Austria has been running high annual budget deficits since 2000, due to necessary support measures during the COVID-19 pandemic and following the sharp rise in prices. Austria's Federal Ministry of Finance envisages continuous budget deficits also for the next three years, even though crisis-related measures are being phased out, the economic environment is expected to be favorable and labor market developments have been robust. The Ministry of Finance thus pursues an expansionary fiscal policy that goes beyond its cyclical stabilization function, as the high level of public spending cannot be justified by cyclical reasons. The Ministry of Finance also plans for significant structural budget deficits over the entire budgeting horizon. The projected decline in Austria's debt-to-GDP ratio is largely attributable to high nominal GDP growth and, thus, to high inflation. The continuous budget deficits will prevent faster debt reduction.

Recommendations:

- There is currently no need to use budgetary resources to support economic development in Austria. The Fiscal Advisory Council therefore recommends that the federal government implement an ambitious budget path to ensure the swift reduction of the debt-to-GDP ratio. Moreover, the coordination of monetary and fiscal policies should be improved.
- With temporary crisis-related measures being phased out, a rapid return to the medium-term objective (MTO) of balanced budgetary positions should be aimed for.
- Economic policy measures other than future-oriented investments should be financed through current budgets.

Create budgetary scope for addressing fiscal risks and medium-term challenges

Background: Austria's debt-to-GDP ratio increased significantly from 70.6% of GDP in 2019 to 78.4% in 2022 as a result of the latest multiple crises and the related government support measures. This rise was accompanied by a relative deterioration in Austria's credit rating, which contributed to higher spreads between Austrian and German government bonds and drove up financing costs. In addition, urgent climate action investments, climate-related budgetary risks, progressing demographic change and a further rise in interest expenditure will weigh heavily on public finances.

Recommendations:

- Priority should be given to the sustained reduction of government debt in order to regain the fiscal space needed to combat potential future crises and address the host of economic, health, climate and social policy challenges.
- The continuous rise in government spending on long-term care, which has demographic reasons, should be addressed by improving the organization of long-term care services (e.g. better coordination between local, regional and federal authorities) and implementing a sustainable financing model.
- There must not be any ad hoc legal interventions in the pension system that would endanger its sustainability and, thus, the sustainability of Austria's public finances.

Use new revenue sharing agreement to raise cost efficiency especially in health care

Background: Given the prolongation of the Revenue Sharing Act (Finanzausgleichsgesetz – FAG) 2017–2021 by two years, necessary reforms aimed to simplify the complex financing structure of federal, regional and local governments and social security funds have been postponed yet again. While regional governments cover the cost of inpatient treatment (including hospitals' outpatient departments), social security funds finance outpatient treatment by registered doctors. Steps taken to prepare a federal state reform, a reform of the property tax and efficiency-increasing measures for government functions have not yet yielded any results. In future, government spending on long-term care and health care is bound to rise significantly as demographic changes, climate change and medical technology advance. Health care costs are already elevated and will continue to rise, given that the health level of Austrians aged 65+ is below average by European standards (source: Eurostat, EU-SILC). Since access to studies at public medical universities in Austria was restricted in the 2005/06 academic year, the number of medical graduates has decreased significantly (Austrian Court of Audit, 2021).

Recommendations:

- Revenue sharing must contribute to making the organization and financing of health care more efficient. For instance, funding will have to be merged and the management and planning of all health care should be well coordinated and binding.
- Measures should be taken to strengthen public health, with a focus on disease prevention and health promotion, in order to reduce both the related fiscal pressure and the burden on Austria's health care infrastructure. In this context, the Court of Audit's recommendations for disease prevention and health promotion as well as Statistics Austria's evaluation of the fit2work project should be taken into consideration (e.g. ensuring sustainable financing for effective projects in priority action areas).
- To ensure the provision of health care in Austria, access to medical universities must be realigned with demand for health care in the various medical disciplines, and action must be taken to reduce the high share of medical graduates that do not work in their profession, neither in Austria nor abroad. Adequate framework conditions must be implemented to ensure that doctors are willing to work in public health care.
- Moreover, the revenue sharing negotiations have the potential to increase efficiency in a number of other areas apart from health care (see recommendations of December 2022).

Swiftly implement climate action and boldly expand related measures to reduce additional spending in the long term

Background: The Environment Agency Austria (2023) found that Austria is set to miss the EU-wide emission targets by a significant margin given the scope of climate protection measures adopted so far. Austria will not manage to reduce its greenhouse gas emissions by 48% by 2030 against 2005 levels, as required, even if it implements measures that have already been envisaged. This means that high costs must be expected for purchasing emission certificates or paying penalties. Moreover, climate change entails further budgetary risks (investment costs, follow-up costs in health care, economic consequences of extreme weather events, etc.).

Recommendations:

- To proceed toward achieving national and international climate targets, Austria needs to adopt a comprehensive set of measures and create the necessary legal basis. As a case in point, the Climate Protection Act, the Energy Efficiency Act and the Renewable Heat Act must be passed without delay.

- The draft national energy and climate plan, which Austria must submit to the European Commission by end-June 2023, must contain all measures that have already been taken to ensure clarity in assessing any need for additional action.

- The steering effects of higher energy prices should be used and reflected in designing regulation plans and calculating compensation payments.

- Purchases of emission certificates and penalty payments may become necessary and further climate-related costs will weigh on the budget. The necessary quantities of budgetary resources will have to be allocated to urgent climate investments considering cost efficiency. In addition, the necessary legal and administrative framework for absorbing public funds will have to be created.

- When choosing appropriate measures to achieve the additional greenhouse gas reduction needed, the cost efficiency of the various available technologies must be taken into account. Regulatory policymaking and awareness-raising measures that do not have a strong impact on the budget should be given priority, giving due consideration to the related adjustment costs for parties concerned. As regards subsidization strategies, care must be taken to avoid deadweight losses.

- It will take additional public and private sector investment in cost-efficient and effective emission reduction (e.g. in building renovation, restructuring mobility systems), and there is also a need for the respective legal frameworks to be put in place. However, the public sector should also focus on expanding public seed investments and complementary investments (e.g. in network infrastructure).

- With regard to the distribution of costs within Austria, a solution will have to be found in the revenue sharing negotiations. Ultimately, adequate involvement of the European institutions will need to be ensured as well.

Phase out broad temporary anti-inflationary measures and ensure that any future support measures effectively target the intended social groups

Background: The fiscal impact resulting from inflation relief measures was EUR 7.3 billion in 2022. The Fiscal Advisory Council expects the volume of these measures to rise to EUR 11.7 billion in 2023, above all due to the new support measures for businesses adopted at end-2022. Essentially, the temporary inflation relief measures have to be seen as stopgap measures, however. For households, they serve to secure real purchasing power until wage increases and social benefits are adjusted to inflation. Following pronounced losses in real wages in 2022, average wage-based incomes per capita have been going up more strongly than consumer prices in 2023, thus eliminating the need for broad-based support measures. Manifest poverty is on the rise in Austria, however, as has been confirmed by empirical evidence. For businesses, the support measures are intended to ensure competitiveness, which is threatened by high energy prices. With energy prices currently on the decline and businesses adjusting to the new market conditions, the need to support Austrian companies is diminishing as well. Moreover, support measures that are not well targeted might spur inflation.

Recommendations:

- Temporary anti-inflationary measures must be phased out consistently. Moreover, no new broad-based support measures should be adopted, and newly envisaged measures should be reconsidered before adoption.

- New support measures should strictly target only vulnerable groups (persons on unemployment benefits, long-term unemployment assistance, social assistance and means-tested top-up benefits). To be able to plan such measures, it is important to build a household income data base. Preparations for such a data base are well advanced and should be followed by rapid implementation. If necessary, greater care must be taken to ensure that benefits are readily available and can be easily obtained.

- Furthermore, to actively fight poverty in Austria, the level of social transfers should be reviewed to ensure that income from transfers maintains its real purchasing power. Temporary support is needed to safeguard the real value of unemployment benefits until collectively agreed wage increases will be reflected in the level of unemployment benefits. In this context, it is key to keep persons on long-term unemployment assistance away from manifest poverty.
- The set of measures adopted by the federal government (anti-inflationary measures for families) is in line with the aim of fighting poverty risk, in particular of groups exposed to inflation. Whether this leads to a sustainable reduction of poverty in Austria remains to be seen.

Align domestic fiscal rules with EU rules as soon as possible and ensure that they support governance

Background: In the face of multiple crises and in line with the approach taken at EU level, Austria activated the "general escape clause," which allows for a temporary coordinated and orderly deviation from structural budget requirements. Accordingly, the evaluation of compliance with national fiscal rules under the Austrian Stability Pact (ÖStP) 2012 – and thus the determination of any breaches that would entail financial sanctions – was suspended for the years from 2020 to 2023. Once the general escape clause will be deactivated as of end-2023, relevant EU and national rules will become applicable again, pending the implementation of the legislative package reforming the EU's Stability and Growth Pact (SGP), which is currently under discussion. On the basis of the ÖStP 2012, structural improvements or structural budget surpluses should be projected in the 2024 budget for the regional government of Vorarlberg and the municipalities of Tyrol and Vorarlberg, provided that a positive change in the output gap is expected at the time of budget preparation.

Recommendations:

- Once the EU's SGP legislative package has been finalized, immediate consideration must be given to its implementation in Austria in order to establish a consistent and effective fiscal framework coordinating all levels of government. Providing a simplified set of rules and improved governance instruments, this fiscal framework should support the return to sound budgetary and debt paths for all levels of government.
- For the transition period (especially for 2024) between the deactivation of the general escape clause and the entry into force of the new EU fiscal framework, it must be examined whether the necessary, cyclically appropriate reduction of excessive control account deficits as of end-2019 is expedient or whether alternative procedures would be more appropriate.
- Debt reduction paths should take into account the new debt levels and debt composition resulting from the multiple crises.
- Compliance with the general government debt rule under the EU's SGP should not obscure the need for action at the subsectoral level in Austria. While compliance with the general government debt rule laid down in the SGP automatically means that Austria fulfills the debt criterion under Article 10(7) ÖStP 2012, the parties to the ÖStP 2012 should avoid relying on the fulfillment of the SGP requirements alone as this undermines the intention of Austria's fiscal framework of defining subsectoral contributions or budget requirements and requiring compliance therewith.