COMMISSION OF THE EUROPEAN COMMUNITIES

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Recommendation for a

COUNCIL RECOMMENDATION TO AUSTRIA

with a view to bringing an end to the situation of an excessive government deficit

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 104(7) thereof;

Having regard to the recommendation from the Commission;

Whereas:

(1) According to Article 104 of the Treaty Member States shall avoid excessive government deficits.

(2) The Stability and Growth Pact is based on the objective of sound government finances as a means of strengthening the conditions for price stability and for strong sustainable growth conducive to employment creation.

(3) The 2005 reform of the Stability and Growth Pact sought to strengthen its effectiveness and economic underpinnings as well as to safeguard the sustainability of the public finances in the long run. It aimed at ensuring that in particular the economic and budgetary background was taken into account fully in all steps in the EDP. In this way, the Stability and Growth Pact provides the framework supporting government policies for a prompt return to sound budgetary positions taking account of the economic situation.

(4) The Council has decided on [2 December 2009], in accordance with Article 104(6), that an excessive deficit exists in Austria.

(5) In accordance with Article 104(7) of the Treaty and Article 3 of Council Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure[1] (which is part of the Stability and Growth Pact), the Council is also required to make recommendations to the Member State concerned with a view to bringing the situation of excessive deficit to an end within a given period. The recommendation has to establish a deadline of six months at the most for effective action to be taken by the Member State concerned to correct the excessive deficit as well as a deadline for the correction of the excessive deficit, which should be completed in the year following its identification unless there are special circumstances. In deciding whether special circumstances exist, "relevant factors" as clarified in Article 2(3) of Regulation (EC) No 1467/97 should be taken into account. Furthermore, in a recommendation to correct an excessive deficit the Council should

[1] OJ L 209, 2.8.1997, p. 6.

request the achievement of a minimum annual improvement in the structural balance, i.e. the cyclically-adjusted balance excluding one-off and other temporary measures, of at least 0.5% of GDP as a benchmark.

(6) Special circumstances, which are relevant for the greater flexibility in the application of the EDP introduced with the 2005 reform of the Stability and Growth Pact, are deemed to exist in the case of Austria. In particular, the economy faces a severe economic downturn in the sense of the Treaty and the Stability and Growth Pact. According to the Commission services' 2009 autumn forecast, real GDP in Austria is projected to contract sharply in the year 2009 by -3.7%. The downturn reflects the abrupt decline in private investment and foreign trade in the export-oriented manufacturing sector as a consequence of the global financial and economic crisis. Economic activity is projected to pick up gradually in 2010, when real GDP growth projected to grow by 0.7%. The existence of special circumstances authorises the Council to allow the correction of the excessive deficit in a medium-term framework.

(7) According to October 2009 EDP notification, the general government deficit in Austria is planned to reach 3.9% of GDP in 2009 taking into account the economic downturn and the fiscal impact of the economic recovery plan fleshed out in the April 2009 update of the stability programme. The Commission services' autumn 2009 forecast projects that the government deficit is expected to deteriorate by almost 4 percentage points in 2009, to 4.3% of GDP. Taking into account the fiscal measures adopted in the current year, the deficit would widen to 5.5% of GDP in 2010 and 5.3% in 2011 on a no-policy change basis. This assumption takes into account that, according to government plans, a large part of the measures of extraordinary nature linked to the crisis in line with the European Economic Recovery Plan will be maintained in 2010 and 2011. Benefitting from a close to balance budgetary position in 2008, Austria adopted appropriate additional fiscal stimulus measures reaching 1½% of GDP in 2009 and ½% of GDP in 2010. The major part of the recovery measures will be permanent (85%) as e.g. income tax cuts, social contribution rate reduction and a reduction in VAT rate for pharmaceuticals. The temporary measures include labour market measures (short-time work), a regional economic stimulus package and vouchers for renovation of buildings with a view to energy conservation.

(8) Considering the special circumstances and the EERP framework, an average annual structural budgetary adjustment is recommended. The required adjustment should take into account the fiscal room for manoeuvre which is assessed on the basis of all factors relevant for achieving the fiscal policy objectives, starting with the level of the general government deficit and gross debt as well as other indicators, such as the current account position, the level of contingent liabilities of the financial sector, interest payments, risk premia and the expected change in age-related expenditure in the medium term. In calculating the average annual adjustment, the 2011 deficit in the Commission services' autumn 2009 forecast is taken as the starting point. The total structural adjustment needed to reach the nominal deficit target of 3% by the deadline is then calculated by assuming a gradual closure of the output gap by 2015.

(9) Against this background, it is appropriate to consider the correction of the excessive deficit in a medium-term framework with a deadline for the correction of 2013. In particular, in view of the absence of major economic imbalances, a credible and sustainable adjustment path would require the Austrian authorities to implement the fiscal measures in 2010 as envisaged; ensure an average annual structural adjustment

of ¾% of GDP over the period 2011-2013, which should also contribute to bringing the government gross debt ratio back on a declining path that approaches the reference value at a satisfactory pace by restoring an adequate level of the primary surplus and specify the measures that are necessary to achieve the correction of the excessive deficit by 2013 cyclical conditions permitting and accelerate the reduction of the deficit if economic or budgetary conditions turn out better than currently expected.

(10) General government gross debt has been above the 60% of GDP reference value since 2008 and, according to the EDP notification of October 2009, is planned to stand at 68.2% of GDP in 2009. According to the Commission services' autumn 2009 forecast, the debt ratio is expected to stand at 69.1% of GDP in 2009 and to rise further to 77% in 2011 on a no-policy change assumption. According to the April 2009 update of the stability programme, the debt ratio is projected to rise from 73% in 2010 to almost 80% of GDP in 2013. Rapid budgetary consolidation is therefore also necessary with a view to bringing the government gross debt ratio on a declining path that approaches the 60% of GDP reference value at a satisfactory pace. Therefore, the Austrian authorities should seize any opportunity beyond the structural budgetary adjustment, to accelerate the reduction of the gross debt ratio back towards the reference value.

(11) The required consolidation efforts should be supported by the recent reform of the budgetary framework law (federal level) comprising a new multi-annual expenditure framework with fixed ceilings (for about 80% of total expenditures) set for four consecutive years on a rolling basis (Federal Budgetary Framework Act – "Bundesfinanzrahmengesetz"). It is expected to prevent pro-cyclical spending and to enhance the effectiveness of the automatic stabilisers. Starting as of 2013, the reform also foresees the introduction of output-based budgeting ("performance budgeting") and the modernisation of the accounting system of the public administration. Despite the overall sound quality of public finances and fiscal rules, there is still room for improvement of Austria's institutional budgetary framework. Austria's federal fiscal relations – governed by the Fiscal Equalisation Act ("Finanzausgleichsgesetz") 2008-2013 and the Domestic Stability Pact 2008 – are rather complex due to overlapping responsibilities, co-administration and co-financing at all three levels of government. Consequently, there is scope for efficiency gains in several areas of public spending, in particular in health care and education.

(12) With regard to the long-term sustainability of public finances, the long-term budgetary impact of ageing in Austria is lower than the EU average, with pension expenditure projected to decrease as a share of GDP over the long-term. The risks from the financial sector stabilisation schemes implemented in response to the crisis could have a potential negative impact on the long-term sustainability of public finances, primarily via their impact on government debt, although some of the cost of the government support could be recouped in the future. Achieving high primary surpluses over the medium term as well as reforms aimed at limiting the increase in age-related expenditure, including by rising the effective retirement age, would help to reduce the risk as defined by the Commission Communication[2] on 'Long-term sustainability of

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[2] Available at: http://ec.europa.eu/economy_finance/publications/publication15996_en.pdf.

public finances for a recovering economy' and endorsed by the ECOFIN Council[3] on 10 November 2009.

(13) Enhanced surveillance under the EDP, which seems necessary also in view of the deadline for the correction of the excessive deficit, will require regular and timely monitoring of the progress made in the implementation of the fiscal consolidation strategy. In this context, a separate chapter in the updates of the Austrian stability programme which will be prepared between 2010 and 2013 could usefully be devoted to this issue.

(14) In general, budgetary consolidation measures should secure a lasting improvement in the general government balance, while being geared towards enhancing the quality of the public finances and reinforcing the growth potential of the economy. In particular, Austria should improve its budgetary framework to strengthen fiscal discipline at all levels of government through enhanced transparency and accountability notably by aligning legislative, administrative and financing responsibilities between the different levels of government and should also spell out specific reforms enhancing potential growth in the areas of the education, R&D and innovation as well as the social security system (health sector). In addition Austria should improve incentives for older workers to continue working by implementing a comprehensive strategy including enhanced job-related training, adaptation of working conditions, and tightening the conditions for early retirement; and improve education outcomes for disadvantaged youth.

(15) In addition, in view of the importance of achieving its medium-term objective (MTO) to provide an adequate safety margin against cyclical downturns and to ensure convergence of the debt ratio towards a prudent level, also taking into account implicit liabilities related to ageing, Austria should also ensure that budgetary consolidation towards the MTO is sustained after the excessive deficit will have been corrected.

HEREBY RECOMMENDS:

(1) Recognising that the Austrian budgetary position in 2009 resulted from measures amounting to 1½% of GDP, which were an appropriate response to the European Economic Recovery Plan, and the free play of automatic stabilisers, the Austrian authorities should implement the fiscal measures in 2010 as envisaged and, starting consolidation in 2011, to put an end to the present excessive deficit situation by 2013.

(2) The Austrian authorities should bring the general government deficit below 3% of GDP in a credible and sustainable manner by taking action in a medium-term framework. Specifically, to this end, the Austrian authorities should:

(a) ensure an average annual structural budgetary adjustment of ¾% of GDP over the period 2011-2013, which should also contribute to bringing the government gross debt ratio back on a declining path that approaches the reference value at a satisfactory pace by restoring an adequate level of the primary surplus;

(b) specify the measures that are necessary to achieve the correction of the excessive deficit by 2013 cyclical conditions permitting and accelerate the

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3 Available at: http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/111025.pdf.

reduction of the deficit if economic or budgetary conditions turn out better than currently expected.

(3) In addition, the Austrian authorities should seize any opportunity beyond the structural adjustment, to accelerate the reduction of the gross debt ratio back towards the reference value.

(4) The Council establishes the deadline of [2 June 2010] for the Austrian government to take effective action to implement the fiscal measures in 2010 as planned and to outline the measures that will be necessary to progress towards the correction of the excessive deficit. The assessment of effective action will take into account economic developments compared to the economic outlook in the Commission services' autumn 2009 forecast.

The Austrian authorities should report on progress made in the implementation of these recommendations in a separate chapter in the updates of the stability programmes which will be prepared between 2010 and 2013.

Furthermore, the Council invites the Austrian authorities to implement reforms with a view to raising potential GDP growth. This includes reforms conducive to enhancing the quality of public finances, in particular by improving its budgetary framework to strengthen fiscal discipline at all levels of government through enhanced transparency and accountability notably by aligning legislative, administrative and financing responsibilities between the different levels of government as well as reforms improving incentives for older workers to continue working by implementing a comprehensive strategy including enhanced job-related training, adaptation of working conditions, and tightening the conditions for early retirement; and improving education outcomes for disadvantaged youth.

This recommendation is addressed to the Republic of Austria.

Done at Brussels,

For the Council
The President