

(How) has EMU affected fiscal policy in Austria?

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Since Austria joined the euro area, national budgetary policy has been influenced by EU fiscal rules to a significant extent. Above all, EU fiscal targets were key drivers behind the major consolidation episodes: consolidations either aimed at bringing the headline deficit ratio below 3% of GDP or at moving the structural budget balance closer to the medium-term objective. At the same time, the structure of expenditure and revenue continues to be under full national responsibility. While the revenue structure remained relatively stable over the last 20 years, we observe relatively strong shifts in the expenditure structure towards social transfers in kind.

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With Austria having joined the European Union (EU) in 1995 and having been a first-round member of European Economic and Monetary Union (EMU), since 1999, Austria's fiscal policy has become firmly embedded in the evolving European fiscal framework. This has meant a substantial regime shift for fiscal policymakers.

In the decades preceding EU accession, Austria's budget policymaking had already undergone several regime changes. In the 1960s, Austria's budget policy, precisely the federal government's budget policy, used to be aimed at maintaining a balanced budget. The primary role of government at that time was that of allocating resources to secure the provision of services of general economic interest and to make sure that the essential needs of society would be met. In the 1970s, the advent of the welfare state was accompanied by expansionary budget policies (the so-called Austro-Keynesian model). Ultimately, the development of the welfare state and the stabilization function that fiscal policy assumed on top of its allocation function went hand in hand with permanent budget deficits. The cumulative deficits caused the public debt ratio to soar in the second half of the 1970s, with interest payments spiraling in tandem. This triggered a debate about the necessity of upper limits for budget deficits, based on the Seidl formula.² While successive governments indeed adopted consolidation packages whenever the budget deficit exceeded the Seidl threshold by a certain margin, primary surpluses remained out of reach. Another regime shift in the mid-1980s, finally, implied the de facto departure from the Austro-Keynesian course and a partial move to supply-side economics (see Bartel, 1995).³

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² According to the so-called Seidl formula – based on the theoretical model of Domar (1944) – Austria would have to target a federal government deficit of 2½% of GDP on average to stabilize the debt ratio at 33.3% of GDP given annual nominal GDP growth rates of 7% (see Katterl and Köhler-Töglhofer, 2005).

³ Income as well as corporate taxation were reformed with the aim of strengthening the allocative function and departing from strictly distributional objectives. Among other things, the government reduced the marginal income tax rate from 62% to 50% with the aim of creating stronger incentives to work. The corporate taxation reform introduced a comparatively low proportional tax rate for corporations while expanding the tax base as well as a proportional tax on residential taxpayers' capital income that is withheld at source and treated as a final tax. This comprehensive tax reform was a response to the opening up of the economy and the free movement of capital and labor as well as to the growing locational competition.

The regime shift related to EU/EMU membership ensued from the requirement to comply with the convergence criteria defined by the Maastricht Treaty by 1997. Among the five criteria for nominal convergence there were two fiscal criteria, which requested first and foremost a general government budget deficit that must not exceed 3% of GDP, and second a debt-to-GDP ratio of below 60% of GDP, or – if above 60% of GDP – a debt ratio diminishing and approaching the debt limit at a satisfactory pace. These criteria still form the core of the Stability and Growth Pact (SGP), which was adopted in 1997 in anticipation of the need to help sustain sound fiscal policies beyond the date of accession to the euro area. The SGP defines fiscal rules for all EU countries and can lead to sanctions for euro area member states like Austria. Over time, these criteria have been specified and augmented by country-specific medium-term objectives, requiring balanced budget positions (in structural terms).

Box 1

European fiscal rules in a nutshell

The current set of EU fiscal rules has three pillars indicating whether there are consolidation needs: (i) the 3% of GDP upper limit for the headline deficit, (ii) the requirement of the debt ratio being either below 60% of GDP or sufficiently diminishing, and (iii) the country-specific medium-term targets (MTO) for the structural balance (cyclically adjusted balanced budgets, net of one-off and temporary measures), which currently stands at –0.5% of GDP for Austria. The first two anchors form the corrective arm of the SGP, while the latter is at the core of the preventive arm. If a country does not achieve all these targets, it has to adopt adequate fiscal adjustment measures. The indicators used to assess the adequacy of the consolidation are (a) the change in the structural balance and (b) expenditure growth adjusted for the impact of discretionary revenue measures (for details, see Prammer and Reiss, 2016, 2018). Both consolidation requirements and sanctions tend to be stricter in the corrective arm of the SGP. At the same time, the corrective arm is also much more procyclical, i.e. tends to ask for higher consolidation in economically bad times.

One of the main functions of budgetary and tax policy – in addition to allocation and distribution – is to stabilize the business cycle. In the euro area, monetary policy is expected to be the core instrument of aggregate stabilization policies, at least as long as countercyclical monetary policy is consistent with the ECB's main objective to achieve price stability. At the same time, national fiscal policies are responsible for smoothing country-specific business cycles, through automatic stabilizers and discretionary countercyclical policies.

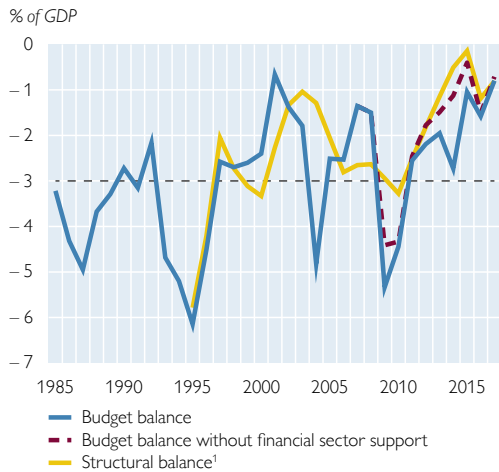
Two decades after the introduction of the euro, the question arises as to whether or to what extent the commitment to respect this European framework has limited Austria's "discretionary fiscal policy space." Put differently: Has fiscal policy in Austria become more or less procyclical or countercyclical since EU/EMU accession? Have the rules hampered policymakers in pursuing distributional and/or allocative goals?

Accordingly, the first section of this article focuses on the impact the European fiscal framework had on the concrete fiscal outcomes in the last two decades and, in particular, on the question whether the fiscal stance has been appropriate over the last 2½ decades. As the SGP does not contain any requirements for the size, structure or composition of national public revenues or expenditures, the second

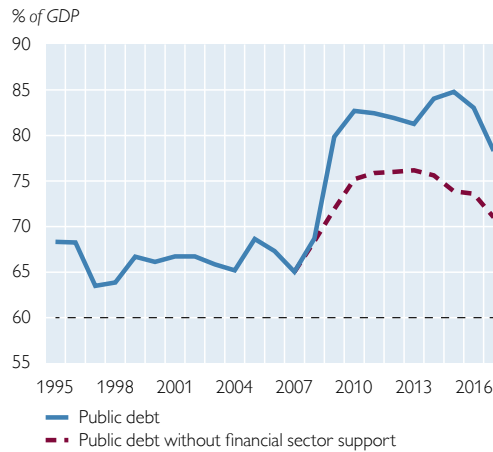
Chart 1

Developments of budget balance and public debt

Budget balance



Public debt



Source: Eurostat, European Commission, OeNB.

¹ Cyclically adjusted balance according to the European Commission minus one-offs according to authors' estimates (see footnote 5).

section is devoted to the development of the revenue and expenditure structure of the general government sector. Section 3 concludes.

1 Austria's fiscal stance and compliance with EMU fiscal rules⁴

According to the most recent data, the general government's deficit ratio has occasionally been above the 3% threshold, while the debt ratio has always been above 60% of GDP (chart 1).

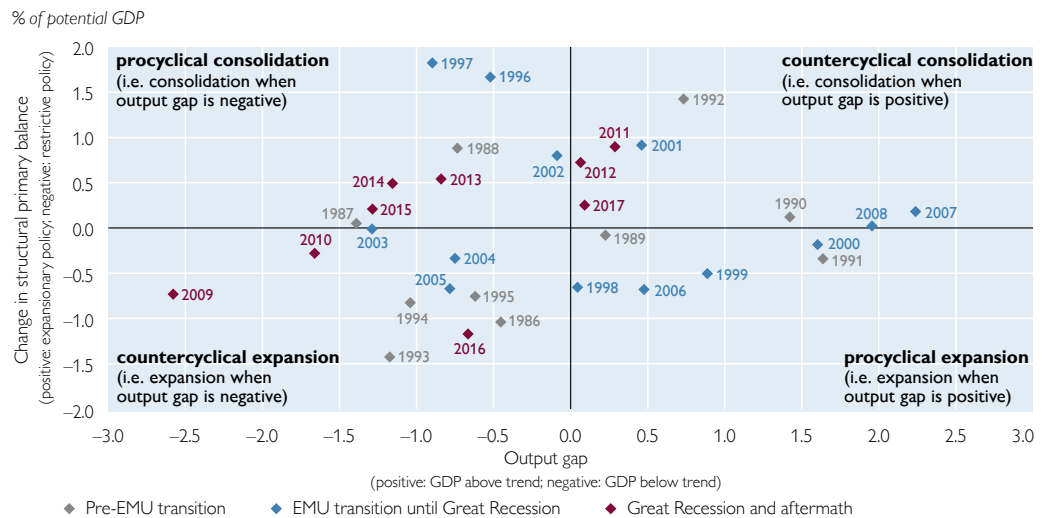
Chart 2 plots the evolution of Austria's fiscal stance (proxied by the change in the structural primary balance⁵) in relation to its position in the economic cycle (proxied by the output gap). The change in the structural primary balance can be considered as an indicator of whether discretionary fiscal policy is contractionary (expansionary) – related to the output gap.⁶ It signals whether the fiscal stance in a certain year/period is appropriate for the current position in the business cycle, i.e. whether discretionary fiscal policy is smoothing economic activity or even amplifying shocks. Ideally, fiscal policy should be restrictive when both output level and growth are above trend, it should be expansionary when both output level and growth are below trend, and it should be passive otherwise. Chart 2 shows that in Austria episodes of active fiscal policymaking (changes in the structural primary

⁴ Please note that the analysis is based on most recent fiscal data and might differ from first ex post released data. Differences are explained in box 2.

⁵ For the calculation of the structural primary balance, we used output gaps by the European Commission (autumn 2018 data) and a constant budgetary semi-elasticity with respect to the output gap of 0.49 for the whole period. This value corresponds to the one used by the European Commission for the calculation of structural budget balances in the projection rounds of 2013–2014. The semi-elasticity of 0.58 that is currently used by the European Commission would lead to misleading results for the years before and after 2009. Furthermore, the following one-offs have been accounted for: capital transfers in the context of financial sector support from 2009 to 2017 and the reorganization of ÖBB in 2004, small one-off taxes collected in 2012–2014 (tax agreements ...) as well as policy-induced collection peaks in profit-related taxes in 2001 and 2015.

⁶ The output gap measures the deviation of actual output from its trend.

Austria's fiscal stance since 1986



Source: OeNB, European Commission.

balance larger than 0.5 percentage points in absolute terms) primarily coincided with economically bad times. Economically bad times, in turn, have seen both episodes of sizeable consolidations (e.g. in 1996–1997 and 2013–2015) and episodes of large fiscal stimuli (e.g. in 2009–2010).

1.1 Large consolidation necessary for EMU accession

In the decade before EMU accession, Austria's budget balance was on average well above 3% of GDP, peaking in 1995 with a general government balance of –6.1% of GDP (see chart 1). The massive fiscal loosening undertaken in the 1993–1995 period amid slowing growth (chart 1 and countercyclical expansion in chart 2) had been observed with concern by academics (Van der Bellen, 1997) and Austrian policymakers alike as it endangered Austria's EMU accession. Hence, the Austrian government prepared the then largest consolidation package since the end of WW II, including an explicit strategy to bring down the debt ratio (for details see Katterl and Köhler-Töglhofer, 2005). Measures comprised a broadening of the tax base for direct taxes, staff cuts in the public sector, the restructuring of government enterprises to facilitate their reclassification to the private sector, and a package to curb expenditure on pensions.⁷ Moreover, in 1996 the federal government also negotiated a precursor of the today's Austrian Stability Pact with the provinces and the municipalities. Widespread concerns that this procyclical fiscal tightening by almost 4 percentage points might cause an even stronger cyclical bust did not materialize. Real GDP growth and the output gap worsened only slightly compared to the preceding countercyclical expansionary episode in Austria (as shown in chart 2, the output gap deteriorated only slightly in 1997 compared to 1995). Austria even managed to keep GDP growth above the EA-12 average, as the majority of EU Member States willing to participate in EMU had to consolidate as well (Diebalek et al., 2002). The subdued effect of fiscal tightening on the economy might have

⁷ Spending cuts were designed to account for two-thirds of the consolidation success and revenue increases for one-third.

been due to the expectation of positive effects from EMU accession. Another very important reason was that consolidation was, among other things, achieved by massive outsourcing and privatization activities as well as by one-off measures, which did not have an immediate impact on aggregate demand (Prammer, 2009). According to Stübler (2003), outsourcing activities in 1997 – as well as in 2001 – had a quite substantial deficit- and debt-reducing impact in real time, with the outsourcing of the highway authority ASFINAG alone reducing the public debt-to-GDP ratio by about 3 percentage points in 1997 (Prammer, 2009). However, some of these outsourcing activities improved the debt ratio only temporarily (see box 2). While it was widely acknowledged that consolidation was ultimately unavoidable, the timing (cyclical downswing) and size (large) of the consolidation was definitely a response to the fiscal precondition for EMU accession, as being among the initial members of the euro area was considered to be of paramount political importance for Austria (compare Pfaffermayr, 2003; Breuss, 1995; and Breuss et al., 1997).

1.2 Relatively strong variation in fiscal stance before the Great Recession

The years following compliance with the convergence criteria in 1997 and hence EMU accession in 1999 were characterized by euro area-wide fiscal fatigue: In Austria, no new consolidation measures were taken, but temporary consolidation measures were allowed to fade out.⁸ The overall budget deficit remained rather stable despite buoyant economic activity, implying a substantial worsening of the structural balance in 1998 and 1999 (charts 1 and 2). Following the electoral cycle rather than the business cycle, a procyclical tax reform was scheduled for 2000, pushing up the projected deficit ratio even further. However, the resulting path of the deficit would have been at odds with the requirements to achieve a balanced budget in cyclically adjusted terms.⁹ This caused massive criticism from the European Commission (see Katterl and Koehler-Töglhofer, 2005). In response to the criticism and the international request to respect the European fiscal rules, respectively, the government reformulated its fiscal policy strategy and announced its intention to achieve a balanced budget by all means in 2002. Like the 1997–1998 consolidation measures, consolidation again unfolded against the background of a starting slowdown of the economy, caused by the 2000 bust of the “dotcom bubble.” Nevertheless, given the high growth rates in the preceding years, chart 2 displays a countercyclical fiscal consolidation, with a positive but shrinking output gap. The balanced budget target was already met in 2001 according to real-time data (left panel of chart 3 in box 2), albeit with the help of one-off measures (very large revenue derived from income taxes on profits due to changes in tax collection) and further outsourcing measures (whose statistical treatment has since been changed, see box 2). The permanent consolidation measures (such as the increases in excise duty rates and the broadening of the income tax base) helped to keep structural budget deficits broadly stable until 2004.¹⁰ However, consolidation against continued low growth implied fiscal procyclicality in 2002 (chart 2), while fiscal policy was broadly neutral in 2003.

⁸ The consolidations in the previous years were partly based on one-off measures and temporary measures, expiring in 1998, such as the temporary abolition of the loss carryover.

⁹ This was later on specified to be achieved in 2002 by all Member States and would have required a yearly adjustment of at least 0.5% of GDP towards the target (see Diebalek et al., 2006).

¹⁰ Moreover, a sweeping pension reform – the biggest in the EU in terms of volume – was announced and implemented in 2003–2004.

The first leg of the 2004–2005 tax reform brought about a slight fiscal expansion amid rebounding growth rates. The general government deficit ratio of more than 4% of GDP in 2004, as displayed in chart 1 according to most recent data, did not give rise to concerns at that time, as it was only 1.5% of GDP according to the first ex post releases (box 2). However, the request for annual structural improvement in the preventive arm of the SGP of at least 0.5% of GDP was not executed.

The lack of enforceability of the SGP, in particular the failure to enforce the corrective arm in the case of Germany and France, ultimately led to its revision in 2005 (see Diebalek et al., 2006). Since then, the preventive arm of the SGP has included explicit country-specific targets for structural budget balances. In general, the adjustment path towards structural balanced budget positions should be aligned with cyclical conditions: while improvements of the structural balance by 0.5% of GDP should be the rule, member states should strive to do more in good times but would be allowed to do less in bad times. In addition, the corrective arm of the SGP specified circumstances allowing for a temporary overrun of deficit targets.

While the first leg of the 2004–2005 tax reform was counter-financed, the second leg of the tax reform – reducing personal income taxes and, above all, corporate income tax rates from 34% to 25% – was clearly at odds with the preventive arm of the SGP. Lack of full counter-financing caused the structural balances to worsen by more than 1/2 percentage point. The fiscal loosening took place against the background of GDP growth above trend, but a still negative output gap. The lagged effects of the tax reform caused the structural budget balance to worsen further in 2006 amid buoyant GDP development, indicated as a procyclical expansion in chart 2. The failure to improve structural fiscal positions during the boom years 2006 and 2007 was more than compensated by high GDP growth, which helped to bring down the overall headline budget deficits to around ½% of GDP in real time (meanwhile revised to about 1½% of GDP). The fact that other euro area countries failed to undertake the necessary structural adjustments during good times as well showed that ownership and enforceability of the preventive arm of the SGP was still weak. In the same way the preventive arm of the SGP had failed to lead to improvements of the structural balance once a nominal balanced budget had been achieved in 2001, the debt rule was sidelined. In fact, public debt in 2005 was higher than in 1995, while it was supposed to be “sufficiently diminishing” according to the Maastricht Treaty.

1.3 Mid-sized stimulus at the beginning of the Great Recession was followed by a long phase of gradual consolidation

The failure to “repair the roof when the sun was shining” took its toll when the economic and financial crisis unfolded from 2008 onward. The government was initially willing to accept deficit ratios above 3% of GDP and implemented a relatively large fiscal stimulus package, comprising an income tax cut, increases to social benefits¹¹ (pensions, family, long-term care) and increases to public investment. While this countercyclical fiscal expansion in 2009 and 2010 (chart 2) seemed justified in light of traditional Keynesian demand policies and also in light of the extraordinarily strong recession, it drove the fiscal deficit well above 3% of GDP in 2009 and 2010.¹²

¹¹ Most of the increases to social benefits were initially deemed to be a response to the high inflation in 2008.

¹² Please note that the first ex post data for 2009 recorded a deficit ratio of only about 3½%, which was later revised upward due to support to the financial sector and reclassifications (each amounting to about 1% of GDP).

Based on its projections for 2009, the European Commission opened an excessive deficit procedure (EDP) against Austria, which was in good company though: all euro area countries except Estonia faced an excessive deficit procedure during/in the aftermath of the economic and financial crisis. Member states essentially got a waiver as regards their fiscal policy in 2009, and euro area countries with medium to good fiscal positions before the crisis (like Austria) were requested to consolidate only from 2011 onward. Austria's first post-crisis consolidation package came into effect in 2011, and involved increases in excise duties, the introduction of a bank levy and capital gains taxation on financial assets as well as cuts to social benefits (including measures curbing early retirement).¹³ This package was successful insofar as it decreased the deficit ratio to below 3% of GDP already in 2011, supported by the comparatively strong cyclical upswing in 2010–2011. Nevertheless, the excessive deficit procedure was not abrogated until 2014, with the European Commission reasoning that it could only be abrogated if compliance with the corrective arm was expected to hold over the forecast horizon. At that time, there was, however, uncertainty about the deficit effects of support to the financial sector (see Prammer and Reiss, 2016). The second post-crisis consolidation package was implemented in early 2012, which was a time when the real economy was cooling down significantly and financial markets were in turmoil. It contained further tax increases as well as a public wage freeze and increases of public pensions far below past inflation. Thus, even though Austria remained subject to an excessive deficit procedure for some years, it managed to fulfil the required fiscal adjustments within the original deadline for correction – unlike several other member states, which were granted extensions, mostly on account of bad economic conditions. Indeed, the consolidations required by the European fiscal framework in this period were heavily criticized and caused intensive political debates among academics and policymakers, going hand in hand with proposals for euro area reforms.¹⁴

Before the reform of the EU governance framework in 2011, the fiscal rules had been criticized for having failed to enforce fiscal buffers in good times. To provide a better safety margin to the 3% deficit limit, the preventive arm of the SGP was strengthened by introducing the possibility of sanctions for disrespecting the (adjustment path to) the MTO.

While Austria's 2011–2013 consolidation was induced by the EDP and the corrective arm of the SGP (and to some extent by financial market pressures), the increased importance of the preventive arm of the SGP contributed to a smaller third post-crisis consolidation package in early 2014. These efforts took place against a negative output gap and a euro area-wide bust period (double-dip recession). In 2012, Austria reinforced compliance with the EU rules by adopting an internal Stability Pact with fiscal rules and targets for the different layers of government (federal level, states, municipalities) with the ultimate aim of respecting a national structural balance target of –0.45% of GDP from 2017 onward (for details see Austrian Fiscal Council, 2014). The European Commission, however, asked Austria to intensify its fiscal adjustment to achieve the MTO already in 2015. This continued consolidation process was to a

¹³ Moreover, the comprehensive budget reform that involved the introduction of a medium-term expenditure framework in 2009 as well as changes to the budgeting processes in 2013 (Steger, 2010) might have contributed to the sustained consolidation efforts.

¹⁴ See for instance Truger (2013, 2014), Corsetti et al. (2015), De Grauwe et al. (2013), Bénassy-Quéré et al. (2017), Fatas (2018) and Orphanides (2018).

significant extent based on revenue-side measures such as an increase of excise duties and base-broadening adjustments in the income taxation and taxation of corporations in 2014–2015. After five years of consolidation, the structural budget balance stood relatively close to zero in 2015 – clearly respecting the preventive arm of the SGP. In other words, the breach of the 3% of GDP limit in 2009 had been followed by a comparatively long-lasting consolidation period, whereas the first consolidation episode in 1996–1997 had stopped once the minimum requirements for the headline deficits had been achieved in 1997. Thus, we can conclude that Austrian fiscal policy-makers have indeed responded to the strengthening of the preventive arm of the SGP.

However, once the MTO was achieved, the 2016 income tax reform – considerably decreasing the marginal tax rates for low- and middle-income earners – implied another fiscal loosening in a period when the output gap was still negative but a cyclical upswing emerging. For 2017, chart 2 depicts a broadly neutral fiscal stance against improving cyclical conditions.

Box 2

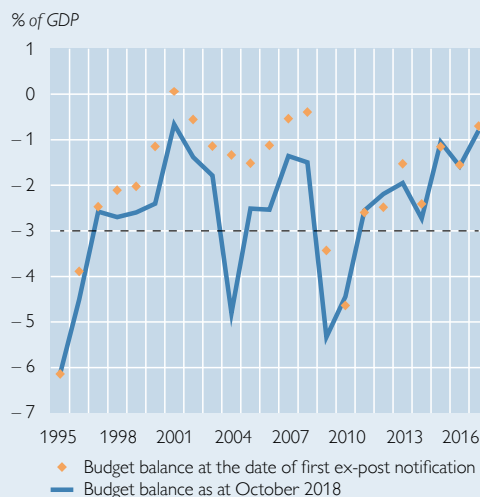
Ex post revisions of budget balance and public debt data

Charts 1 and 2 above are based on the most recent fiscal data available. However, these data have been subject to relatively large revisions. Chart 3 shows that when comparing the first ex post release (currently end of March T+1) to the most recent one (October 2018), deficit ratios from 1998 to 2009 have typically been revised upward by around 1 percentage point. The main revisions were implemented in spring 2011 (implementation of the new Manual on Government Deficit and Debt, see for example p. 12f in Ragacs and Vondra, 2011) and in fall 2014 (switch to the European System of National Accounts 2010, see for example Stübler et al., 2015). They were largely due to rerouted transactions and subsequent reclassifications of state hospitals and ÖBB Infrastruktur. The large upward revision of the 2004 deficit ratio was due to the change in recording of a debt relief and a capital injection to ÖBB before its reorganization. Reclassifications of entities to the government sector (ÖBB Infrastruktur, ÖBB Personenverkehr, KA Finanz, state hospitals, property management vehicles, ...) have also contributed to the large upward revisions in the ratio of government debt to GDP (even though nominal GDP has also been revised upward substantially).

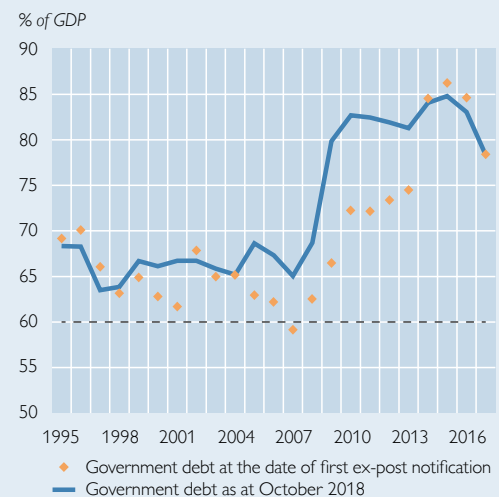
Chart 3

Revisions to fiscal indications

Budget balance



Government debt



Source: Eurostat, Statistics Austria.

2 Shifts in expenditure and (tax) revenue structure since EMU accession

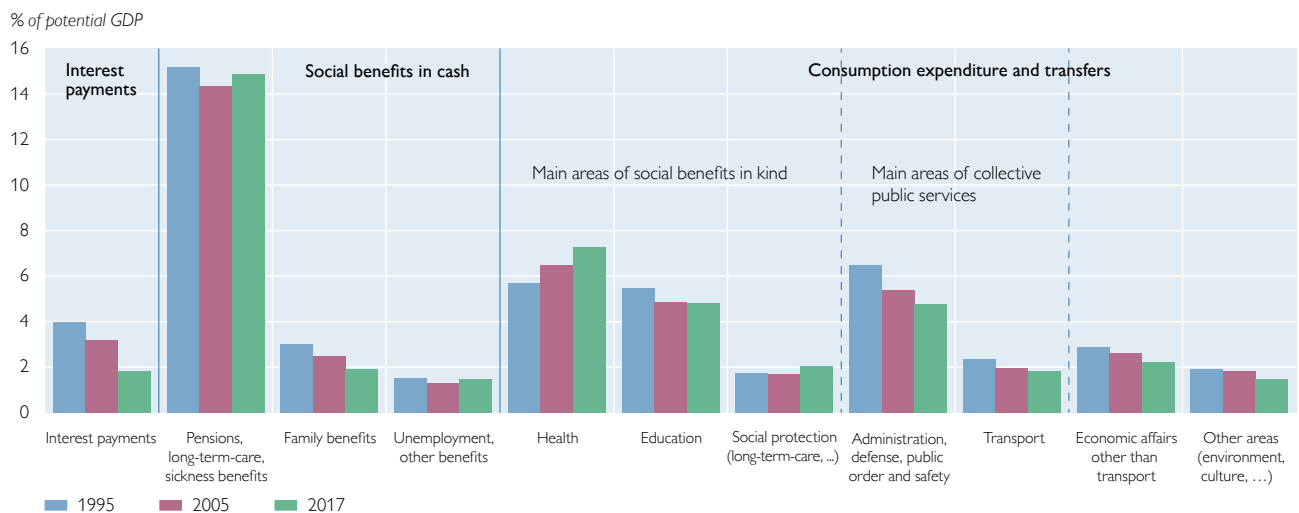
While European fiscal rules bind governments concerning the size of their budget balance and their financial debt, governments are relatively free to choose the size of the government sector and the structure of revenue and expenditure. Distributional goals pursued by the “design” of the tax structure such as the degree of progressivity of personal income tax or the tax treatment of capital etc. are still in the hands of national policymakers. This holds also for allocative goals such as environmental taxation. On the basis of the so-called European Semester, the European Commission and the Council may make (structural policy-induced) recommendations on revenue or expenditure structure in their country-specific recommendations (e.g. to shift taxation from labor income to immovable property), but there are no sanctions in case countries do not follow them (in contrast to recommendations covered by the fiscal rules laid out in the SGP). Thus, the public expenditure and revenue path over the years mirror the political programs of the governments in Austria as well as demographics and economic conditions.

2.1 Expenditure shifted from collective consumption goods to social benefits in kind

Chart 4 shows that there have been sizeable shifts within the structure of total government expenditure:¹⁵

Chart 4

Development of public expenditure since 1995



Source: OeNB, European Commission.

Note: Unemployment benefits have been cyclically adjusted.

¹⁵ Instead of showing expenditure other than interest and social benefits in cash, we show the sum of government consumption and of other transfer payments (subsidies, other current transfers, capital transfers). This means that we replace expenditure on investment by the depreciation of the capital stock (similar to profit and loss accounts by enterprises). Furthermore, this essentially implies that we deduct payments for output sold by government entities (tickets for trains or museums, rental payments to property management vehicles ...). The latter adjustment also removes structural breaks induced by the reclassification of municipal quasi-corporations out of the government sector (in 1997; led to decrease in expenditure and in proceeds from output sold) and of ÖBB Infrastruktur and ÖBB Personenverkehr into the government sector (in 2005; led to increase in expenditure and in proceeds from output sold).

- Due to a strong decline in interest rates, spending on interest payments as a ratio of potential GDP more than halved compared to 1995 (even though the debt ratio has increased substantially). The marked decline in public interest expenditure over the last decade was, however, primarily caused by the Eurosystem's monetary policy after 2008 (especially the reduction of short-term interest rates below zero and the wide range of nonstandard measures).
- Expenditure on social benefits in cash to households have overall increased slightly less than potential GDP. This is mostly due to a falling population share of children, i.e. of potential recipients of family benefits, while cuts to benefits during the consolidations of 1996–1997 and 2011 have been roughly compensated by extraordinarily strong increases in 1999–2000 and 2008–2009. Expenditure increases in the area of pensions have been dampened by increases in the effective retirement age (abolishment and phasing out of early retirement schemes, reform of disability pensions), by various episodes of pension indexation below inflation (especially during the consolidation episodes), and by the cuts of replacement rates induced by the pension reforms of 2003–2005. Pension reforms of the last two decades were dominated by the political intention to ensure the long-term sustainability of the public pay-as-you go system by taking into account actual as well as expected demographic changes in the future.
- Expenditure on social benefits in kind (i.e. government-sponsored services to individual persons) has increased much stronger than potential GDP. This was mainly due to health and social protection (long-term care, youth welfare, and more recently in-kind benefits to refugees ...). Education expenditure increased somewhat less than GDP, which was especially due to primary and secondary schools, while expenditure related to pre-primary education and to universities has increased at a relatively stronger rate.
- Expenditure on collective services has increased at a much slower rate than potential GDP. This is true for administration and security¹⁶ as well as for transportation.
- Other expenditure has also increased much less than potential GDP, even though some specific subitems like subsidies to promote private R&D have increased substantially over the last two decades.

The stronger upward pressure in the area of social benefits in kind as opposed to collective government services is a typical pattern in developed economies. It is not only due to the ageing of society (which puts upward pressure on benefits related to health care and long-term care), but also due to the relatively low technological progress in the area of personal services (also termed “Baumol’s cost disease”).

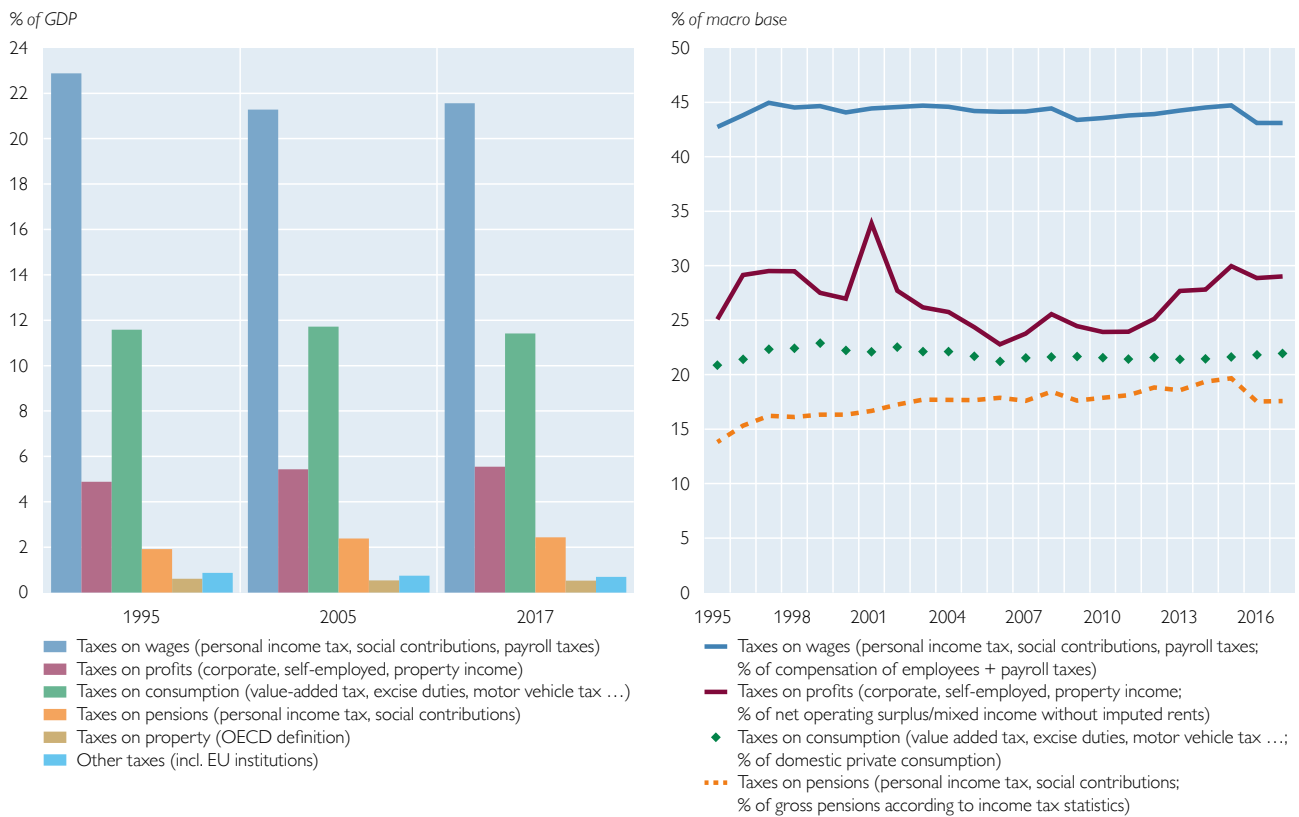
Expenditure growth in both individual and collective government services has been significantly dampened by low increases in agreed wages for government employees in the three major consolidation episodes, with the difference to private sector wage agreements being particularly large in 1996–1997 and in 2011–2013.¹⁷

¹⁶ These developments are especially due to military spending, which has increased much less than the expenditure on police, law courts and prisons.

¹⁷ The focus of this section is more on the structure of expenditure than on its overall size. The slowdown of potential GDP growth (nominal potential GDP growth from 2005 to 2017 has been on average by about ½ percentage points lower than from 1995 to 2005) has contributed substantially to the observed increases in social benefits between 2005 and 2017.

Chart 5

Development of tax revenue since 1995



Source: Eurostat, Statistics Austria, OeNB.

2.2 Tax burden on wages has remained stable, while other implicit tax rates have increased

On the revenue side, the left panel of chart 5 shows that income from employed labor is by far the most important source of tax revenue, followed by consumption, profit income and pension income, while taxes on property (according to the OECD definition) make up for rather little revenue.¹⁸ The right panel of chart 5 shows that the implicit tax rate¹⁹ on wages has remained broadly stable since 1995, while the implicit tax rates on profits, consumption and pensions have all increased somewhat:

- Taxes on wages have remained stable, but they are still very high by international standards (see also European Commission, 2018). After the consolidation package of 1996–1997, episodes of non-indexation of tax brackets have been followed by

¹⁸ Other taxes in the left panel of chart 5 only shows the main components of tax revenue. It leaves out some minor tax items summing up to about 1% to 1½% of GDP (depending on the year) which are only shown in the left panel of chart 5, namely taxes on property according to the OECD definition, import levies, and various taxes paid by enterprises irrespective of their payroll or profits (e.g. bank levy). Furthermore, note that we do not show the developments of non-tax revenue in chart 5. The main non-tax revenue items (proceeds from market and nonmarket output, output for own final use) are implicitly included in chart 4, while the other items (property income, other current and capital transfers received) are relatively small (currently around 1½% of GDP).

¹⁹ As total economy wages have increased less than GDP since 1995 (so taxes on wages have increased less than GDP even though the implicit tax rate staid the same), we divided the major tax revenue categories by the macroeconomic main aggregate closest to the true tax base.

income tax cuts (in 2000, 2004–2005, 2009, 2016), while social contribution and payroll tax rates have remained broadly stable over that time span (see also Reiss and Schuster, 2019).

- Taxes on profits increased at a stronger rate than net operating surplus adjusted for imputed rents (which is a rather crude tax base) as the major corporate income tax cut of 2005 was more than offset by substantial base-broadening measures in the three major consolidation episodes described in section 1 (1996–1997, 2000–2002 and 2011–2015); 2001 and 2015 also saw policy-induced peaks in tax collection.
- Taxes on consumption increased somewhat during the 1996–1997 consolidation and remained stable afterwards. The standard VAT rate remained fixed at 20% throughout the observed time period, while the nominally fixed rates of excise duties (such as energy taxes and the tobacco tax) and the motor vehicle tax have been adjusted upward occasionally (above all during the 2000–2002 and the 2011–2015 consolidation episodes).
- Taxes on pensions increased at a stronger rate than overall pensions due to increases in health insurance contributions (esp. in 2004–2005), relatively large fiscal drag (induced by high growth in average pensions) and cuts to tax credits (largely targeted at pensioners (as part of the consolidation packages of 2000–2002 and 2011–2015).

Overall, the respective composition of implemented fiscal stimulus as well as consolidation packages has contributed to a slight shift in taxation away from employed labor.

3 Conclusions

This essay highlights that, first, the European fiscal framework has had quite a substantial influence on fiscal policymaking in Austria. Second, it shows that Austrian fiscal policymakers have been adhering broadly to the rules-based fiscal policy scheme. Third, it indicates that fiscal policy had to be restrictive in periods when it may have been economically adequate to provide a more expansionary response, implying that the stabilization function in these periods was impaired. In other words, fiscal policy was intensifying rather than smoothing output and employment cycles. Partly this was due to the fact that good times were not used to build up fiscal buffers in order to have more room for fiscal maneuver. Finally, in comparison with the decades before EU/EMU accession, fiscal sustainability considerations have gained greater importance, given the increased importance of debt developments.

As the SGP does not contain any requirements for the level or composition of public revenue or expenditure of EU Member States, fiscal policymakers are still free in pursuing their political priorities. We show that over the last two decades, there were no substantial shifts in the structure of tax revenue, while on the expenditure side there has been a shift from collective services (like administration, security) to social benefits in kind (health, long-term care).

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