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**IMF Executive Board Concludes 2018 Article IV Consultation with Austria**

On September 10, 2018, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation1 with Austria.

Austria is a rich, equitable and stable country. The social safety net is ample; thus, poverty and income inequality are low, contributing to strong social cohesion and security.

The economic recovery is strong and broad-based. Following several years of slow growth, Austria's output picked up markedly in 2017, and through early-2018. Output expanded by 3 percent in 2017, boosted by income tax cuts passed in 2016, higher public spending on refugees and a recovery in private investment in 2017, laying the foundation for a sustained robust expansion. Consumer and business confidence indicators have surpassed levels observed before the GFC and credit growth has recovered. Employment growth has accelerated, and unemployment has begun declining recently. Inflation is running slightly higher than in peers, albeit close to the ECB Euro Area target. Financial sector buffers have strengthened. Debt has declined by 5 percentage points of GDP to 78.5 percent in the year to end-2017. The near-term outlook is for strong growth in 2018, at 3 percent, and a gradual return to a potential growth of about 1¾ percent over the medium-term. Risks to the baseline are mainly external, however, their impact would likely be limited.

1 Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

**Executive Board Assessment**[2]

Executive Directors welcomed Austria's robust and broad-based economic growth on the back of sound domestic policies and a favorable external environment. Together with strong business confidence, this has contributed to job creation and a decline in unemployment. Looking ahead, Directors encouraged the authorities to take advantage of the favorable position to step up structural reforms to raise growth potential through inclusive policies. This will help preserve Austria's important achievements in income equality and social cohesion.

Directors commended the authorities for persevering with fiscal consolidation and maintaining public debt on a downward path. They observed that, while the short-term fiscal outlook is favorable, long-term sustainability will require further structural reforms. With spending pressures likely to rise from population aging, it will be important to specify and prioritize reforms that enhance the sustainability of the pension system and generate cost savings in healthcare and subsidies spending. Adjustments in fiscal relations between federal and subnational governments could be necessary to ensure the success of such reforms. Directors emphasized that the authorities' envisaged fiscal consolidation should aim to remain equitable and growth-friendly.

Directors welcomed the progress in reducing banking system vulnerabilities through improved capitalization and asset quality, as well as a further strengthening of Austrian banks' foreign subsidiaries' funding base. While risks have subsided, Directors recommended remaining vigilant and further increasing banks' capital buffers. They also underlined the need to continue efforts to improve cost efficiency to enhance long-term profitability, in particular of smaller banks.

Directors agreed that real estate related risks to financial stability remain contained at present,but urged the authorities to continue to closely monitor house price developments and variable rate and foreign currency denominated housing loan exposures, in order to identify early any household balance sheet strains. They welcomed the recently established legal basis for targeted real estate specific macroprudential tools. While the use of the new macroprudential instruments does not appear necessary at this time, Directors underscored the need to continue to provide clear guidance to banks to maintain sustainable lending standards. It will also be important to continue to bolster the AML/CFT framework.

Directors welcomed the supply-side measures that the authorities are undertaking. They underlined that raising potential growth and lowering structural unemployment require strengthening competition and implementing proactive policies to enhance education outcomes, address skills mismatches, promote labor participation of women and the elderly, and integrate

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

foreign nationals into the labor market. Directors noted that structural and fiscal measures could raise labor demand, including by shifting the tax mix away from labor and ensuring an adequate level of public investment.

It is expected that the next Article IV consultation with Austria will be held on the standard 12-month cycle.

## Austria: Selected Economic Indicators, 2015–23

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|---|---|---|
| | | | | Projections | | | | | |
| NATIONAL ACCOUNTS | | | | | | | | | |
| Real GDP (expenditure) | 1.1 | 1.5 | 3.0 | 3.0 | 2.2 | 1.6 | 1.5 | 1.5 | 1.5 |
| Domestic demand | 1.1 | 2.1 | 2.8 | 2.9 | 2.2 | 1.6 | 1.6 | 1.4 | 1.6 |
| Consumption | 0.8 | 1.7 | 1.3 | 2.1 | 2.0 | 1.5 | 1.6 | 1.7 | 1.6 |
| Private | 0.5 | 1.5 | 1.4 | 2.3 | 2.3 | 1.6 | 1.6 | 1.9 | 1.7 |
| Public | 1.5 | 2.1 | 0.9 | 1.5 | 1.3 | 1.2 | 1.4 | 1.0 | 1.4 |
| Gross fixed capital formation | 1.2 | 3.7 | 4.9 | 4.2 | 3.0 | 2.1 | 1.7 | 1.5 | 1.5 |
| Private | 1.0 | 3.7 | 5.2 | 4.5 | 3.1 | 2.1 | 1.6 | 1.5 | 1.5 |
| Public | 2.4 | 3.2 | 2.6 | 2.2 | 1.9 | 2.4 | 2.0 | 1.9 | 1.6 |
| GNFS exports | 3.1 | 1.9 | 5.6 | 4.1 | 2.6 | 2.6 | 2.3 | 2.4 | 2.3 |
| GNFS imports | 3.1 | 3.1 | 5.7 | 3.5 | 2.7 | 2.8 | 2.6 | 2.6 | 2.4 |
| Contribution to GDP (percentage points) | | | | | | | | | |
| Final domestic demand | 0.8 | 2.0 | 2.0 | 2.5 | 2.1 | 1.6 | 1.5 | 1.5 | 1.5 |
| Net exports | 0.1 | -0.6 | 0.1 | 0.4 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Inventories and statistical discrepancy | 0.1 | 0.0 | 0.9 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Investment (% GDP) | 23.6 | 24.1 | 25.1 | 25.6 | 25.9 | 25.7 | 25.7 | 25.5 | 25.4 |
| Public | 4.3 | 3.8 | 3.9 | 3.9 | 3.9 | 3.9 | 3.9 | 3.9 | 3.9 |
| Private | 19.3 | 20.3 | 21.2 | 21.7 | 22.0 | 21.8 | 21.8 | 21.6 | 21.5 |
| Gross national savings (% GDP) | 25.5 | 26.2 | 27.0 | 27.7 | 27.9 | 27.9 | 27.8 | 27.6 | 27.6 |
| Public | 3.2 | 2.2 | 3.2 | 3.8 | 3.9 | 4.1 | 4.0 | 3.8 | 3.6 |
| Private | 22.3 | 24.0 | 23.8 | 24.0 | 24.1 | 23.8 | 23.8 | 23.8 | 23.9 |
| Potential output | 1.4 | 1.4 | 1.6 | 1.8 | 1.8 | 1.7 | 1.7 | 1.7 | 1.7 |
| Output gap (% potential GDP) | -1.6 | -1.6 | -0.2 | 1.0 | 1.4 | 1.2 | 0.9 | 0.7 | 0.5 |
| LABOR MARKET | | | | | | | | | |
| Labor force | 1.0 | 2.0 | 0.4 | 1.1 | 1.0 | 0.9 | 0.8 | 0.8 | 0.7 |
| Employment | 0.9 | 1.7 | 1.0 | 1.0 | 1.1 | 1.0 | 0.8 | 0.7 | 0.7 |
| Wages (hourly) | 3.2 | 0.5 | 4.0 | 4.5 | 3.2 | 2.6 | 2.6 | 2.7 | 2.7 |
| Unemployment rate (% labor force) | | | | | | | | | |
| EU harmonized rate | 5.7 | 6.0 | 5.5 | 5.2 | 5.1 | 5.0 | 5.0 | 5.1 | 5.1 |
| National definition | 9.1 | 9.1 | 8.5 | 8.1 | 7.9 | 7.8 | 7.7 | 7.7 | 7.6 |
| PRICES | | | | | | | | | |
| Consumer prices (avg) | 0.8 | 1.0 | 2.2 | 2.0 | 2.1 | 2.1 | 2.1 | 2.1 | 2.0 |
| Consumer prices (eop) | 1.0 | 1.5 | 2.3 | 1.9 | 2.1 | 2.1 | 2.1 | 2.1 | 2.0 |
| Core CPI (eop) | 1.9 | 1.6 | 2.2 | 1.7 | 2.1 | 2.1 | 2.1 | 2.1 | 2.0 |
| GDP deflator | 2.3 | 1.1 | 1.6 | 1.8 | 1.8 | 2.1 | 2.2 | 2.1 | 2.1 |
| MACRO-FINANCIAL | | | | | | | | | |
| Broad money | 4.3 | 5.5 | 4.2 | 4.8 | 4.2 | 3.9 | 3.8 | 3.6 | 3.6 |
| Credit to the private sector | 1.8 | 1.3 | 2.5 | 2.9 | 2.2 | 2.4 | 2.6 | 2.6 | 2.6 |
| Corporations | -0.2 | -1.5 | 0.6 | 1.0 | 0.5 | 1.2 | 1.5 | 1.6 | 1.6 |
| Households | 3.9 | 4.1 | 4.1 | 4.5 | 3.7 | 3.4 | 3.4 | 3.4 | 3.4 |
| GENERAL GOVERNMENT FINANCES (% GDP) | | | | | | | | | |
| Revenue | 49.9 | 49.0 | 48.3 | 48.2 | 48.1 | 48.0 | 48.0 | 48.0 | 48.0 |
| Expenditure | 51.0 | 50.6 | 49.0 | 48.4 | 48.1 | 47.8 | 47.8 | 48.0 | 48.2 |
| Net lending/borrowing | -1.0 | -1.6 | -0.7 | -0.2 | 0.0 | 0.1 | 0.1 | -0.1 | -0.3 |
| Structural balance | 0.5 | -0.6 | -0.6 | -0.7 | -0.8 | -0.5 | -0.4 | -0.5 | -0.6 |
| Structural primary balance | 2.8 | 1.5 | 1.2 | 0.9 | 0.7 | 0.9 | 0.9 | 0.8 | 0.6 |
| Gross debt | 84.3 | 83.6 | 78.5 | 74.2 | 70.9 | 67.8 | 65.0 | 62.8 | 60.9 |
| BALANCE OF PAYMENTS | | | | | | | | | |
| Current account (% GDP) | 1.9 | 2.1 | 1.9 | 2.1 | 2.1 | 2.1 | 2.1 | 2.2 | 2.2 |
| Export volume (goods and services) | 3.1 | 1.9 | 5.6 | 4.1 | 2.6 | 2.6 | 2.3 | 2.4 | 2.3 |
| Import volume (goods and services) | 3.1 | 3.1 | 5.7 | 3.5 | 2.7 | 2.8 | 2.6 | 2.6 | 2.4 |
| Int'l investment position, net (% GDP) | 2.5 | 5.7 | 6.0 | 7.8 | 9.5 | 11.2 | 12.9 | 14.6 | 16.2 |
| MEMORANDUM ITEMS | | | | | | | | | |
| Nominal GDP (bn €) | 344 | 353 | 370 | 387 | 403 | 417 | 433 | 449 | 465 |
| Population (million) | 8.6 | 8.7 | 8.8 | 8.9 | 9.0 | 9.0 | 9.1 | 9.1 | 9.2 |
| GDP per capita ($) | 44,297 | 44,733 | 47,357 | 52,297 | 53,761 | 55,957 | 57,915 | 60,064 | 62,075 |
| US$/€ (rate; annual avg) | 1.1 | 1.1 | 1.1 | ... | ... | ... | ... | ... | ... |
| Real effective exchange rate | -4.0 | 1.2 | 2.0 | 0.9 | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 |

Sources: Authorities' data and IMF staff estimates and projections.

INTERNATIONAL MONETARY FUND

# AUSTRIA

## STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION

August 23, 2018

## KEY ISSUES

**Context:** Living standards in Austria are high, and income inequality and poverty low. The economy has picked up markedly, accelerating to 3 percent in 2017, and 3.1 percent (y/y) in 2018: Q1. This provides an opportunity to implement reforms to raise the economy's potential output, reduce unemployment further, and ensure long-term fiscal sustainability. Also, further strengthening the financial system would guard against a less benign global financial environment.

**Outlook and risks:** After another strong performance in 2018, growth is projected to gradually slow, before settling at its medium-term potential rate of 1¾ percent. Inflation has risen to about 2 percent. Unemployment is declining but remains above pre-Global Financial Crisis (GFC) levels. Key risks arise from a possible retreat from cross-border integration, and slower growth in other advanced economies and emerging markets. A potential reduction of efforts to integrate immigrants could diminish their contribution to the economy and increase welfare spending.

**Preserving long-term fiscal sustainability:** Public debt has been declining since 2016, and gradual fiscal consolidation has resumed, maintaining public debt on a downward path. But in the medium- to longer-run, fiscal pressures arising from population aging will increasingly strain public finances. To preserve and expand fiscal space, the current window of opportunity should be used to put in place efficiency-boosting expenditure reforms, in particular in the health sector and in subsidies. More broadly, structural reforms could help raise Austria's growth potential.

**Reducing unemployment:** Lowering unemployment sustainably to pre-GFC levels requires additional measures, including strengthening the education system; special efforts to integrate foreign nationals into the labor market; and structural and fiscal policy measures to raise labor demand. These would also boost potential growth.

**Further strengthening the financial system:** The financial system is stable, and large banks' capital levels have risen, reducing the gap with peers and reaching levels targeted in the bank sustainability package. While further raising capital levels is warranted, focus should shift to boosting cost efficiency, where progress has been slow. Risks in the real estate market are currently limited but warrant continued monitoring.

Approved By
**Mahmood Pradhan (EUR) and Yan Sun (SPR)**

Discussions for the 2018 Article IV consultation were held in Vienna during June 14–25, 2018. The mission comprised Mr. Dorsey (head), Ms. Karpowicz, and Mr. Pitt (all EUR), and Mr. Hukka (FIN). Messrs. Smith and Park (both EUR) assisted from headquarters. Mr. Just (OED) joined the discussions.

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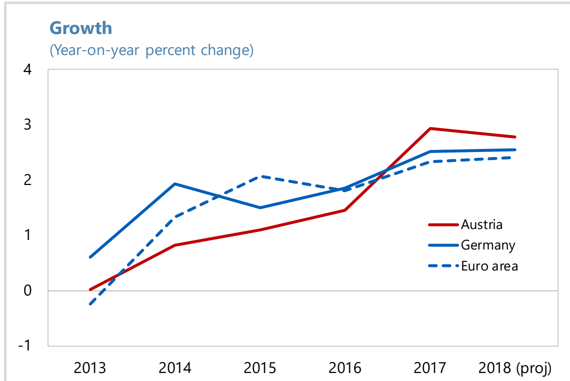
# RECENT DEVELOPMENTS

1. **The Austrian economy is robust.** After several years of slow growth, output accelerated markedly in 2016/17, the public debt-to-GDP ratio has begun to fall, unemployment has declined, and the financial sector has been strengthened.

2. **Growth has picked up markedly and has been broad-based.** GDP expanded by 3 percent in 2017, and by 3.1 percent (y/y) in 2018: Q1, boosted by income tax cuts in 2016, higher public spending on refugees and a recovery in private investment in 2017, laying the foundation for continued robust expansion. A favorable external environment contributed to strong net exports as growth in Europe accelerated more broadly. Consumer and business confidence indicators have surpassed levels observed before the GFC. Employment growth has accelerated, catching up with the rising labor supply from migration and higher labor force participation. As a result, unemployment has begun to decline recently, to 7.7 percent in May.[1] At 2.1 percent y/y in May, inflation has decelerated slightly from its peak in 2017: H2.



Sources: National authorities; and IMF staff estimates.

3. **The fiscal outturn in 2017 was better than expected.** The structural deficit stood at 0.6 percent of GDP, lower than anticipated in the budget (0.8 percent), and the headline deficit was 0.7 percent of GDP against the budgeted 1.2 percent, largely due to the higher-than-anticipated economic growth, but also due to savings on interest payments. Public debt fell by 5 percentage points, to 78.5 percent of GDP, supported by the strong growth and asset recoveries of intervened banks.

4. **The financial system is stronger and better capitalized than in recent years.** Large banks' capital levels have been increased, and risks have been reduced. Profitability has risen, largely due to reduced risk provisions, while banks have continued their cost-cutting efforts. The supervisory framework has been strengthened, including through the creation of a legal basis for using real-estate specific macroprudential measures.

5. **Refugee inflows remain low.** Arrivals of refugees have slowed sharply since 2015, and processing of asylum applications is catching up. Significant challenges remain in integrating accepted asylum seekers into the labor market, such as language barriers and low skills. At the same time, the new government is tightening acceptance criteria, and is considering curtailing asylum seekers'—both in process and recognized—access to social benefits.

[1] National measure, based on registered unemployment. The EU harmonized rate remains low compared to peers, at 4.9 percent in April, ¾ percentage point lower than a year before.

**6. The external position remains broadly in line with fundamentals and desirable policies** (Annex I). Using the External Balance Assessment estimates, at 2 percent of GDP in cyclically-adjusted terms the current account balance was close to the estimated norm of 1.8 percent of GDP in 2017. Model-based estimates suggest that the real effective exchange rate (REER) was modestly overvalued by about 7½–10¼ percent. However, these estimates do not consider the economy's cyclical position. Moreover, the unexplained residual is large. Therefore, staff analysis suggests an indicative REER gap of -1.2 percent which is assessed as broadly consistent with fundamentals.

**7. Political situation.** In early parliamentary elections in October 2017, the center-right Austrian People's Party, under its new leader Sebastian Kurz won the most seats. It has formed a coalition government with the far-right Freedom Party. The new government is broadly continuing and, in some areas, accelerating economic reforms that its predecessor has initiated, but has scaled back some labor market measures, notably subsidies for new private sector employment and public-sector jobs for older long-term unemployed.

# OUTLOOK AND RISKS

## A. Outlook

**8. Growth momentum remains strong in the near term, but output is forecast to converge toward its potential level in the medium term.** In 2018, GDP growth is projected to remain strong, at 3 percent, as accelerating consumption and net exports more than offset the declining contribution of investment. This will open a positive output gap, and growth in 2019–23 is then projected to slow gradually, before settling at its potential rate of about 1¾ percent beyond the projection horizon. This is slightly higher than previously estimated, on account of a pick-up in investment, somewhat faster TFP growth, and higher labor force participation. With the output gap mildly positive, inflation is expected to run slightly above 2 percent in the medium term.

## B. Risks

**9. Risks to the outlook are largely external and would likely have a limited impact if they were to materialize** (Annex II). Key risks are:

- ***Retreat from cross-border integration.*** Increasingly inward-oriented economic policies in some trading partners and reduced international policy coordination and collaboration would leave Austria, a very open economy, vulnerable directly and indirectly through export, FDI, and confidence channels.

- ***Structurally weak growth in advanced economies and emerging markets.*** This would make fiscal consolidation and debt reduction more difficult. Also, a deceleration in Central, Eastern, and Southeastern European (CESEE) countries, which take 21 percent of Austria's exports and with which its banks have extensive financial relations, could affect financial system stability directly and the economy more broadly.

- ***Integration of immigrants.*** If efforts to integrate immigrants were unsuccessful, this could reduce their contribution to the economy, slowing growth and increasing welfare spending.

However, with 70 percent of Austria's exports going to the European Union (EU), where the European Single Market provides a stable framework, the impact of these risks is contained. Also, stronger capital buffers and declining financial sector exposure to CESEE, by divestments as well as the shift of Bank Austria's CESEE operations to its parent bank in Italy (Unicredit), are containing vulnerabilities.

**10. Austria's direct financial exposure to developments in Italy is limited, but indirect adverse effects cannot be ruled out.** Austrian bank's exposure to Italy is small (about 1.3 percent of total foreign claims). Also, the strengthening of capital levels, adequate and stable liquidity, and limited reliance on wholesale funding would provide a buffer. However, confidence effects could be important.

***Authorities' Views***

**11. The authorities broadly concurred with staff's assessment of the outlook.** However, the Ministry of Finance considered the economy's medium-term potential growth rate to be higher, at about 2¼ percent, and also saw room for higher growth in 2018. With regard to risks, the authorities emphasized that Austria was dependent on open access to markets, and were concerned about potential disruptions to trade, including through sanctions. They also stressed the potentially adverse impact on confidence, which could have wider repercussions on investment and the financial sector. The authorities also pointed to increasing environmental risks arising from climate change, which already had an impact on their tourism industry. With regard to migration, they agreed that integrating immigrants into the labor market was key to domestic security and prosperity. They pointed to some successes in their integration programs but noted that challenges remained large.

# POLICIES

*The overall outlook is robust. Creating fiscal space to prepare for rising costs of an aging population in the longer term requires structural reforms. While unemployment is falling, labor market policies require attention. Financial stability risks, including from housing market developments, appear contained, but banks' cost cutting efforts need to continue.*

## A. Fiscal Policy and Reforms

**12. The current strong economic environment offers an opportunity to fortify the economy's foundations further.** Priorities include (i) creating fiscal space to accommodate the cost of an ageing society, and (ii) boosting the economy's growth potential. Both are interrelated, and require a package of measures that, in combination, can ease long-term fiscal pressures and raise growth while protecting Austria's strong welfare state.

**13. The authorities intend to achieve a structural surplus over the medium term, and a significant reduction in expenditure and revenue as a share of GDP** (Box 1). The 2018/19 budget aims to achieve overall balance by 2019, and the authorities' Stability Program envisages small surpluses thereafter, based on spending reductions across the board, even as revenue is projected to decline.

### Box 1. Stability Program

*In May, the authorities passed a budget for 2018 and 2019 at the same time, since the new government took office only in December 2017, too late to draft a budget for the whole of 2018.*

**The new government's medium-term fiscal plans are ambitious.** Key goals are a faster reduction of public debt than previously envisaged, and a reduction of the tax and contributions burden 'toward 40 percent'. After relatively modest measures in 2018/19, the authorities are planning a comprehensive tax reform for 2020.

**Revenue** is projected to decline by 1¼ percentage points over the next five years, on account of a reduction in indirect tax revenue (largely other than VAT), social security contributions, and other revenue. Specific measures include a reduction of unemployment insurance contributions for low-income earners, a reduction of VAT on overnight stays, and an increase in income tax relief for families with children. Further measures planned from 2020 onward aim to reduce the tax burden on low incomes, as well as on corporates.

**Expenditure** is set to decline by 2.4 percentage points of GDP. Savings are envisaged across the board, largely through efficiency gains in the public administration (including in the health system), avoidance of overbudgeting, cuts in personnel costs, and lower spending on social benefits, due to strong performance of the economy. Also, some recently-introduced labor market programs have been discontinued, and transfer payments abroad may be cut. Spending on IT infrastructure, and on R&D is set to rise, and overall public investment to remain broadly constant as a percentage of GDP.

**The structural balance** would reach Austria's medium-term objective (MTO) of -0.5 percent of GDP in 2019 (and balance in nominal terms), after widening slightly in 2018.[1/] By 2022, with the output gap closed, the nominal and structural balance would reach a surplus of 0.4 percent of GDP.

**Public debt** would, as a result, decline by more than 15 percentage points of GDP over five years, approaching the 60 percent mark established in the Maastricht Treaty. This is a faster debt reduction path than envisaged by the previous government, which anticipated a reduction by about 10 percentage points of GDP over the same time horizon.

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[1/] The structural balance is -0.1 percent of GDP in 2017 and -0.5 percent in 2018 if spending on refugees and anti-terrorism measures are excluded.

**14. The authorities' medium-term plans are difficult to achieve without deeper structural reforms.** Over the medium- to longer-term, significant savings potential exists, especially in the areas of healthcare and subsidies, but a concerted effort of the federal government and states is needed to realize it. This would likely need to include further adjustments in the fiscal relations between the federal and subnational governments. The current federal fiscal framework, which sets revenue sharing and spending parameters through 2022, envisages some steps toward achieving greater spending efficiency in healthcare through benchmarking, cost reduction, and spending reviews (see Country Report 17/26 (2/2/17)). Moreover, in a new initiative, the government intends to reduce the number of insurance bodies. But these measures are only beginning to unfold, and their impact on costs is uncertain. Similarly, the authorities' plan to cut subsidies is welcome, but without a further reform of fiscal federal relations the effect may be limited.[2] Lastly, over the medium term, demography-related spending needs will begin to rise gradually, putting additional pressure on other spending areas, if targeted savings are to be achieved.

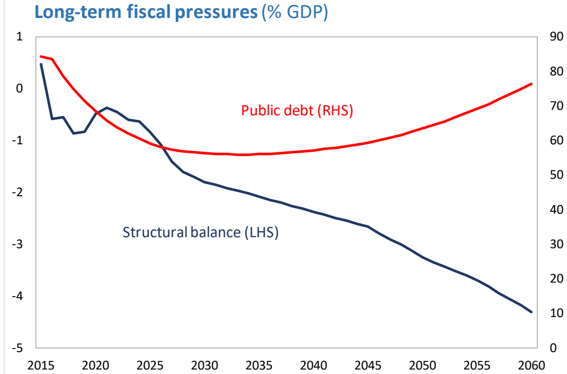
**Medium-Term Fiscal Policy (% GDP)**

| | 2017 | 2018 | 2019 | 2022 | Δppts |
|---|---|---|---|---|---|
| | Act. | | Proj. | | 2022-17 |
| **Authorities' plan** | | | | | |
| Revenue | 48.3 | 47.9 | 47.6 | 47.1 | -1.2 |
| Expenditure | 49.0 | 48.3 | 47.6 | 46.7 | -2.3 |
| Net lending/borrowing | -0.7 | -0.4 | 0.0 | 0.4 | 1.1 |
| Structural balance | -0.6 | -0.8 | -0.5 | 0.4 | 1.0 |
| Gross debt (Maastricht def.) | 78.6 | 74.5 | 70.9 | 62.2 | -16.4 |
| **Staff projections** | | | | | |
| Revenue | 48.3 | 48.2 | 48.1 | 48.0 | -0.4 |
| Expenditure | 49.0 | 48.4 | 48.1 | 48.0 | -1.0 |
| Net lending/borrowing | -0.7 | -0.2 | 0.0 | -0.1 | 0.6 |
| Structural balance | -0.6 | -0.7 | -0.8 | -0.5 | 0.1 |
| Gross debt (Maastricht def.) | 78.5 | 74.2 | 70.9 | 62.8 | -15.7 |

Sources: Statistik Austria, and authorities' and IMF staff projections.

**15. Staff projections are more conservative than the authorities'.** This is largely because most of the planned savings—notably improvements in administrative efficiency—are difficult to quantify.[3] Also, the envisaged reduction in personnel costs will be difficult to achieve in the short run, especially as additional positions are created in the area of police and internal security. Staff project revenue to remain broadly constant in the medium term, as the impact of planned reductions in VAT on overnight stays is small. Nonetheless, even under the staff's scenario, the structural balance would decline to -½ percent of GDP by 2020, and the nominal balance would be zero, before widening again in the outer years as demography-related spending picks up gradually. Public debt would continue to decline, to 61 percent of GDP by 2023 (see Annex III).

**Long-term fiscal pressures** (% GDP)




Source: IMF staff projections.

[2] Despite a small cut in federal subsidies, the authorities project a slight increase in subsidies (from 1.4 percent of GDP in 2017 to 1.5 percent in 2018/19) for the consolidated general government.

[3] A strengthening of tax revenue on account of better administration in 2016 to compensate for income tax cuts, as envisaged in the 2016 budget, has only partially materialized. Also, reduction of overbudgeting does not necessarily lead to lower expenditure, only a reduction of the headroom built into the budget.

**16. Time is ripe for implementing efficiency-raising reforms.** Rebuilding fiscal buffers and further lowering public debt are key for ensuring long-term fiscal sustainability. Therefore, Austria's MTO of a structural balance of -0.5 percent of GDP remains appropriate, while a more specific fiscal program would provide greater confidence that it can be achieved. Moreover, structural fiscal reforms that ensure government spending on a sustainable footing as the population ages are important. Overall, the savings potential from such reforms could be in the range of 2½–3 percent of GDP (see Country Report 17/26 (2/2/17)). As indicated above, this likely requires additional reforms in fiscal federal relations, including stronger incentives for cost savings in the health system. Also, further reforms to the pension system could ease future fiscal pressures. Since reforms in these areas would likely need to be implemented over time, the current window of opportunity—as the economy performs strongly and before ageing costs rise significantly—should be used to tackle them.

**17. In designing reforms, including a tax reform, equity considerations will need to be taken into account.** Austria's income inequality and its poverty rates are relatively low, an achievement that should be preserved, though trade-offs between equity and incentives need to be carefully weighed. In this regard, the reduction in social security contributions for low-income earners is a step in the right direction (including to help their employment prospects). Further steps to lower the tax wedge on low incomes should follow, which could be financed by higher taxation of environmental pollution and wealth. On the other hand, the increase in the family bonus set for 2019 does not support families with incomes below the threshold at which income taxes are due.

***Authorities' Views***

**18. The authorities acknowledged the challenge of reducing revenue and the deficit simultaneously but were confident that this was feasible.** They emphasized the need to accelerate debt reduction toward the Maastricht target of 60 percent of GDP to rebuild fiscal buffers. They pointed out that, with strong growth in 2017 and 2018, tax and social security contributions were already approaching the 40 percent target. With regard to expenditure savings, they considered that high output growth would automatically lead to a reduction in the expenditure-to-GDP ratio. Combined with the already-announced measures, this would reduce spending sufficiently to limit the need for additional cuts.

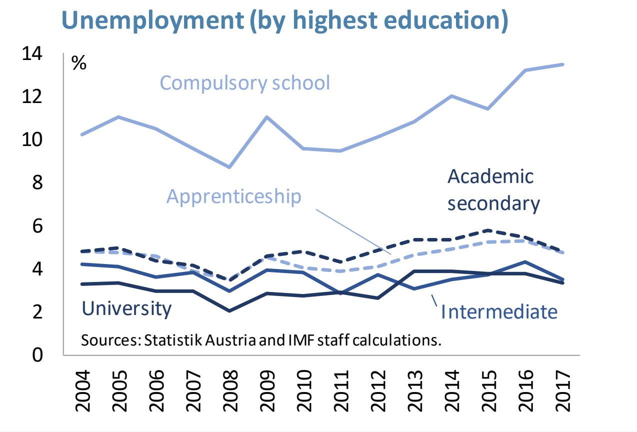
## B. Reducing Unemployment

**19. While employment has increased steadily over the past several years, so has the labor force.** Rising labor force participation among women and the elderly, and immigration, have led to an increase in the labor force by 6.2 percent between 2011 and 2017, and a change in its composition: the share of non-Austrian citizens rose from 11.5 to 16.2 percent.[4] Though employment increased by 5.1 percent, unemployment rose slightly, from 4.9 percent in 2012 to 5.3 percent in 2018: Q1 (EU harmonized rate).

[4] Since 2004, most foreign nationals in Austria are from the recent EU accession states and third countries.

**20. Going forward, labor force growth is projected to slow gradually.** The recently arrived (and accepted) refugees are only gradually entering the labor market and new immigration has slowed, though labor force participation of Austrian women and elderly workers is expected to edge up further.[5] On the employment side, above-potential growth in the next few years should generate employment growth outpacing that of the labor force, and lower unemployment further.

**21. The recent drop in unemployment is welcome, but challenges remain** (Annex V). Driving down unemployment sustainably to levels in the years before the GFC requires proactive policies to increase employability, as well as measures to strengthen labor demand.



Sources: Statistik Austria and IMF staff calculations.

- *Improving education.* Unemployment is highest among those with only compulsory schooling. Strengthening education would help employability and prepare workers for jobs that increasingly demand higher (though not necessarily only academic) skills. In this regard, the recent increase up to the age of 18 of compulsory schooling or training and the training guarantee for people under 25 are positive steps. Austria's strong and institutionally deep-rooted dual-education apprenticeship system is well-placed to boost skills.

- *Integrating foreigners (including accepted refugees) into the labor market.* Foreign-born residents—an increasing share of the labor force—frequently have lower levels of education and training than Austrians, but even at the same level of education, their unemployment rates are higher. Therefore, additional efforts need to be made to address the specific hurdles that non-Austrians face, including acquiring recognized qualifications and language skills.

- *Active labor market policies.* Active labor market polices can help target specific segments of the workforce. Elderly workers, whose labor force participation is rising, face increasing unemployment rates and, once unemployed, have significant difficulties in finding a job. In this context, the government's decision to discontinue targeted support through secondary labor market for over 50-year-old long-term unemployed will likely have adverse effects on this age group. However, costs and benefits of such schemes need to be carefully weighed.

- *Boosting labor demand.* Measures along the lines of those previously recommended by staff (see Country Report 17/26 (2/2/17)), including policies to strengthen innovation and competition by lowering barriers to entrepreneurship, a shift in the tax mix away from labor, and higher public investment would raise private investment and productivity, and with them potential output and employment. In some of these areas, planned steps are promising, such as better support for

[5] The increase in the pension age for women from 60 to 65 years will kick in only in 2024–33.

start-ups, more financing for R&D, a strengthening of the education system and its better integration with the economy, and increasing flexibility in working hours.

***Authorities' Views***

**22. The authorities agreed that tackling unemployment remained a challenge.** They concurred with staff that improving the education system was critical to improve employability as well as address labor shortages in higher-skilled segments of the labor market. They pointed out that high unemployment among foreign nationals occurred partially because they were more often employed in seasonal activities (e.g., in the tourism industry or construction), but also acknowledged that lack of skills could play a role. With regard to targeted support for elderly workers, they considered that providing subsidized employment (including in the public sector) would be inefficient and crowd out the regular labor market. They thought that supporting continuous training and education for workers was more effective in reducing unemployment for the elderly.

## C. Consolidating Financial Stability

**23. Austria's banking system as a whole is well-capitalized, but additional buffers would be welcome as insurance against large adverse events.** The sector-wide capital adequacy ratio stood at 18.2 percent at end-2017, and the CET-1 ratio was 14.6 percent. Large banks have narrowed the gap between their capital levels and those of peers, and have met targets under the authorities' bank sustainability package introduced in 2012, although some continue to maintain relatively modest buffers above the regulatory minimum requirements.[6] The thirteen largest banks are also set to meet the systemic risk capital buffer of up to 2 percent, which is to be fully phased in during 2019. Banks' dependence on wholesale funding is low, and all Austrian banks also meet the recently fully phased-in liquidity coverage ratio (LCR), with a weighted average of 145 percent at the unconsolidated level.[7] Profits have risen further in 2017, largely because of reduced risk provisioning, as nonperforming loans (NPLs) declined (adding to the case for additional capital buffers).[8, 9] However, cost reduction is progressing only slowly and the low-interest environment continues to put pressure on profits.

**24. Risks to banks' portfolios have been reduced.** Domestic household foreign currency loans have declined significantly, to less than 15 percent of total loans as of December 2017, and the share of variable rate loans in new household loans has fallen to a little over half. Moreover, the shift of

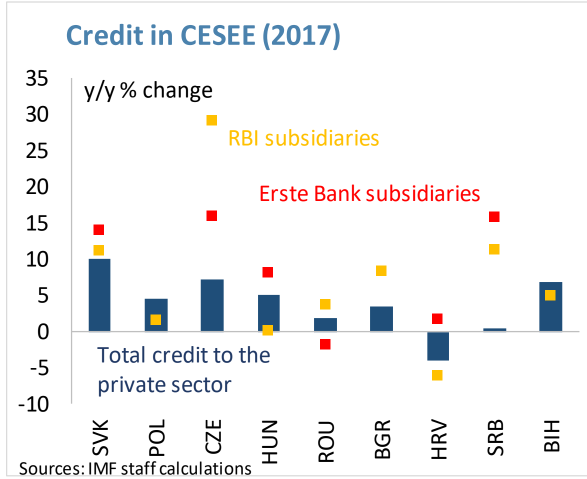
[6] Austrian banks' relatively high risk-weighted assets density will limit the impact from the recently finalized Basel III capital framework, which establishes additional safeguards to the use of internal models to calculate capital requirements.

[7] The full LCR minimum requirement of 100 percent, measured as high-quality liquid assets to stressed net outflows arising over a period of 30 days, was fully phased in by 2018.

[8] The NPL ratio stood at 3.4 percent at end-2017; domestically it was 2.4 percent, while in CESEE there was significant heterogeneity, in part on account of unresolved regulatory issues.

[9] Despite reduced provisioning, Austrian banks' consolidated coverage ratio of 63.8 percent remains among the highest in the EU (50.7 percent).

Bank Austria's CESEE operations to Unicredit in Italy has significantly reduced the direct exposure of the Austrian banking system to CESEE. Austrian banks' subsidiaries in CESEE have further strengthened their funding base, with the loan-to-deposit ratio declining to 79 percent, from over 100 percent in 2011. This also implies that Austrian banks' strategic retrenchment from CESEE countries has not had negative spillovers in the area: with few exceptions, which can be explained by lingering political uncertainties about the treatment of legacy foreign exchange mortgage loans as well as regulatory risks, growth rates of credit issued by them are comparable to—and are in most cases higher than—overall credit growth in these countries.




**25. Credit extension in Austria has recovered from post-crisis lows.** Nominal credit to the private sector grew 3.7 percent (y/y) in February 2018, broadly unchanged from a year earlier, even though the economy accelerated. Both credit to nonfinancial corporations (+5.7 percent) and credit to households (+3.5 percent) have accelerated, but indebtedness remains below peers' levels.[10] Growth in residential real estate loans (+4.8 percent) has remained broadly stable around the growth in house prices.

**26. The regulatory and supervisory frameworks have been strengthened.** The authorities updated their supervisory guidance in 2017. With improved capitalization, a stable funding base in CESEE subsidiaries, and the development of recovery and resolution plans, the focus has now shifted to strengthening the business models of major internationally active banks. This includes rationalization, cost cutting, and IT investments, as well as further strengthening of capital—where increased profit-sharing pressures have led to some loss in momentum. Also, the legal basis for using targeted real-estate macroprudential tools (loan-to-value caps, debt-service-to-income limits, term restrictions, debt-to-income ceilings and minimum amortization requirements) has been established, and the authorities are collecting additional data to improve their analysis of the real estate market and its interaction with the financial system, including early identification of any household balance sheet strains.[11]

**27. Banks should take advantage of the current benign macroeconomic environment to buttress profitability and safeguard internal capital-generating capacity.** This would also underpin business investment and the potential of the economy. While the recent rise in profits is welcome, a significant part of these gains stems from one-off factors (reduced risk provisioning). Large banks need to continue implementing their adjustment plans, and raise further capital to

[10] Stock-based measures, which also reflect exchange rate changes, indicate broadly stagnating credit to nonfinancial corporations, and growth of 3.8 percent to households.

[11] The new tools provide a more targeted complement to the already available counter-cyclical capital buffer intended to counteract risks arising from the credit cycle (currently set at zero percent of risk weighted assets).

bolster cushions above regulatory limits, including by limiting dividend payouts. As net interest income remains constrained in the low interest rate environment, this involves efforts to reduce structural costs (which may also involve investments in efficiency-enhancing infrastructure), refocusing on core activities, and withdrawing from non-profitable and high-risk activities and locations.[12] For smaller banks, reducing costs, including through accelerating the development of digital banking and increasing fee-based activities to offset shrinking interest rate margins, are crucial. Supervisory and regulatory authorities need to ensure that banks further raise capitalization levels, continue to reduce vulnerabilities, and implement their cost-cutting plans.

**28. Real estate-related risks to financial stability are contained at present** (Annex V). There is currently no need to formally activate the new macroprudential tools, notwithstanding some limited loosening in banks' lending standards. Furthermore, the associated reporting requirements allowing full evaluation of risks and potential policy effects are expected to become effective only in 2019. That said, the authorities need to remain vigilant and be prepared to take preemptive action to head off stability risks if needed. At the current juncture, consideration should be given to providing clearer guidance to banks on sustainable lending standards, including by quantifying specific loan-to-value, debt-to-income and debt-service-to-income limits.

**29. The Single Resolution Board and the FMA are in the process of issuing binding targets for bail-in-able debt (MREL) for most of the banks under their remit and will complete this process in 2019.** The case for MREL in excess of minimum capital requirements is weaker for small deposit-taking banks (such as Austria's local and regional banks) that have traditionally steered clear of debt markets. For such banks—which are mostly under the purview of national regulators—the expectation should be liquidation rather than resolution in case of difficulties, with no recourse to state aid.

**30. A stronger Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) framework will help Austria sustain its position as a financial center.** The authorities need to continue strengthening their AML/CFT regime in line with their action plan adopted in response to the 2016 Financial Action Task Force (FATF) Mutual Evaluation Report. Several Action Plan items have already been addressed by legislative measures over the course of the last two years. These improvements were acknowledged by the FATF in the first follow-up report in December 2017. Austria should further enhance the effectiveness of the AML/CFT framework by improving investigation and prosecution of money laundering and the use of financial intelligence. As a next step Austria should implement the 5th EU AML Directive. This will further improve Austria's AML/CFT with a view to the current AML/CFT risk landscape (anonymity of virtual currencies and the lack of transparency of beneficial ownership and high-risk countries).

[12] A new module in OeNB 2017 stress tests showed that under baseline normal economic conditions, the low interest rates could reduce Austrian banks' operating profits by 7 percent in the next three years, primarily driven by replacement of maturing long-term fixed rate assets with lower interest assets. At the same time, the positive effect of rising interest rates on net interest income would also be at least partially offset by higher credit risk costs.

***Authorities' Views***[13]

**31. The authorities agreed that banks needed to reinforce their efforts to sustainably raise profitability and continue to improve capitalization.** They were confident that banks would be able to make the needed adjustments, but cautioned that costs could initially rise as investments, especially in IT, were needed to increase efficiency, and staff reductions were also costly. They were of the view that a further strengthening of capital buffers in large banks was desirable, in particular in the current high-growth environment.

**32. The national supervisory authorities shared staff's assessment that real estate-related risks were limited at this time, notwithstanding some loosening in lending standards.** They thought that the European Systemic Risk Board's (ESRB) 2016 warning on medium-term residential real estate vulnerabilities did not sufficiently take into account initial conditions but focused only on changes, and also didn't consider country-specific features of the Austrian housing markets, including a low level of home ownership. They indicated that in some banks mortgage lending practices were riskier than they deemed appropriate and have conducted targeted dialogue with those banks. Also, they pointed out that the mortgage-related data they were currently gathering were only covering part of the sector and that comprehensive monitoring would be possible only from 2019 on.

**33. The government emphasized that they were strongly committed to strengthen their AML/CFT framework.** They explained that in the 2017 follow-up report of the FATF, several of Austria's ratings had improved. They had increased supervisory resources, and recently established a register of beneficial ownership. Going forward, the authorities are preparing to implement the European Union's 5th AML directive, including through improving coordination and information sharing among agencies.

# STAFF APPRAISAL

**34. The economy is robust, and Austria's economic foundations are strong.** Growth has risen markedly, driven by investment, rising labor supply, and net exports. The public debt-to-GDP ratio has continued to fall, unemployment has declined, and the financial sector has been strengthened. The external position remains broadly in line with fundamentals and desirable policies.

**35. The overall outlook is solid, but potential growth remains constrained.** In 2018, GDP growth is projected to remain strong at 3 percent as investment growth and public consumption taper off, but private consumption and net exports accelerate. With the output gap turning positive, growth would then gradually slow, before settling at its potential rate of about 1¾ percent. Inflation should run slightly above 2 percent in the medium term. As employment grows faster than the labor force, unemployment would gradually decline.

[13] Staff from the ECB's Single Supervisory Mechanism participated in a conference call on Austria's systemically significant banks.

**36. Risks arise largely from external factors, but their impact is likely limited overall.** A retreat from cross-border integration, or slow growth in other advanced economies and emerging markets, would lower Austria's performance, largely through confidence, trade and financial channels. However, the European Single Market provides a stable framework, and declining bank exposure to CESEE is containing vulnerabilities. Domestically, if efforts to integrate immigrants were unsuccessful, this could reduce their contribution to the economy.

**37. The short-term fiscal outlook is favorable, but long-term sustainability requires structural reforms.** Debt is set to decline further throughout the medium term. The authorities' planned fiscal consolidation is ambitious and welcome, but the measures needed to achieve it are not fully identified. Priority should be given to structural fiscal reforms that enhance the efficiency of public expenditure and the sustainability of the pension system to create fiscal space to absorb rising spending needs as the population ages. To this end, the current window of opportunity should be used to put in place efficiency-boosting expenditure reforms, in particular in the health sector and in subsidies. To be successful, many of these reforms require adjustments in fiscal relations between the federal and subnational governments. Also, further reforms to the pension system could also ease future fiscal pressures. The potential for savings is significant, and, in combination with growth-raising reforms, would ensure long-term fiscal sustainability.

**38. In designing reforms, including a tax reform, equity considerations will need to be taken into account.** Austria's strong welfare state efficiently achieves relatively low levels of income inequality and poverty rates. While trade-offs between equity and incentives need to be carefully weighed, a rebalancing of the tax burden and expenditure cuts need to be designed with a view to preserving Austria's social achievements.

**39. Reducing unemployment durably requires proactive policies.** While the strong economy has already led to some decline in unemployment, reducing it durably to pre-GFC levels requires additional measures. These include (i) improving education outcomes; (ii) special efforts to supporting the integration of foreigners into the labor market; (iii) targeted active labor market policies where needed; and (iv) structural measures to raise labor demand (and potential growth), shifting the tax mix away from labor, and raising public investment, as previously recommended by staff. Several initiatives by the authorities, including lengthening the duration of compulsory schooling and training guarantees are steps in the right direction.

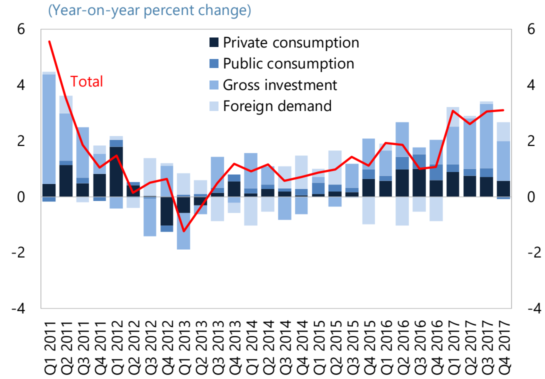
**40. Consolidating financial stability requires that banks continue to implement adjustment plans to cut costs and raise further capital.** While large banks' capitalization has improved in recent years, creating further buffers to prepare for a less benign environment is important. To ensure sustainable profitability and capital-generating capacity, banks now need to focus on strengthening their business models, largely through rationalization, cost cutting, and IT investments. Also, dividend payouts should be consistent with adequate earnings retention. The regulatory and supervisory authorities need to ensure that banks implement measures to these ends. Financial stability risks from the real estate markets remain limited but warrant continued close monitoring. While use of formal macroprudential instruments does not appear necessary at this time, the authorities should not shy away from targeted proactive steps—which could include quantified supervisory guidance—to maintain sustainable lending standards. To preserve Austria's position as a financial center, the authorities will also need to continue bolstering the AML/CFT framework, notably by improving the investigation and prosecution of money laundering and the use of financial intelligence and implement the recently-issued 5th EU AML Directive.

**41. It is recommended that the next Article IV consultation be held on the standard 12-month cycle.**

## Figure 1. Austria: Real Sector Developments

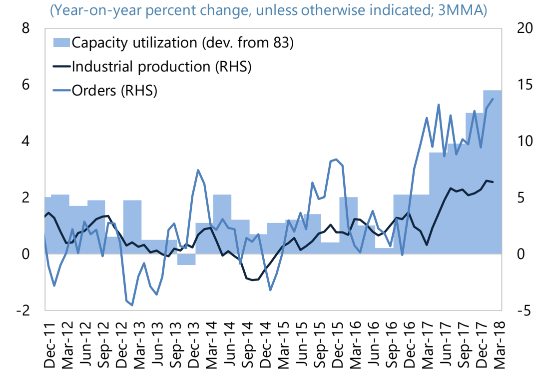
*GDP growth has picked up ...*

**Contribution to Real GDP**
(Year-on-year percent change)



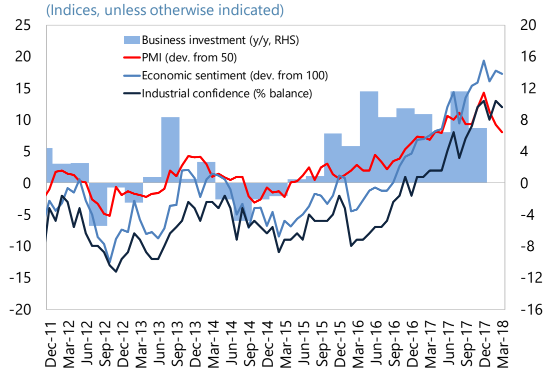

*... with production indicators rising strongly.*

**Production**
(Year-on-year percent change, unless otherwise indicated; 3MMA)



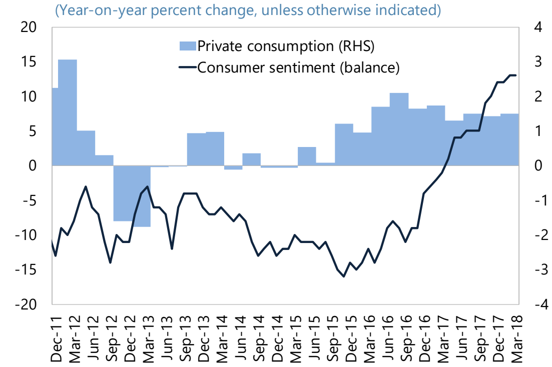

*Investment and business indicators have also risen sharply ...*

**Investment**
(Indices, unless otherwise indicated)



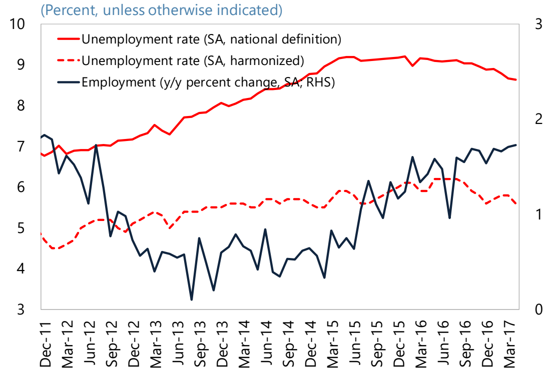

*... as have consumption and consumer confidence ...*

**Consumption**
(Year-on-year percent change, unless otherwise indicated)



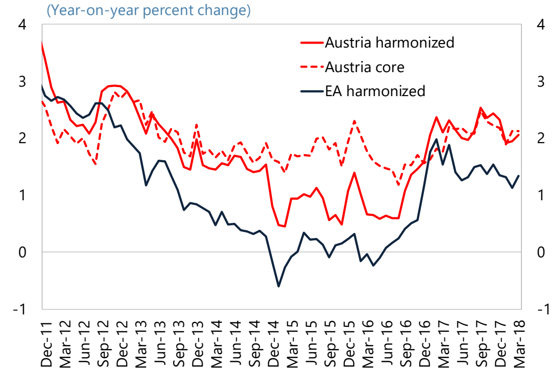

*... as employment is starting to decline.*

**Labor Market**
(Percent, unless otherwise indicated)




*At the same time, inflation has stabilized.*

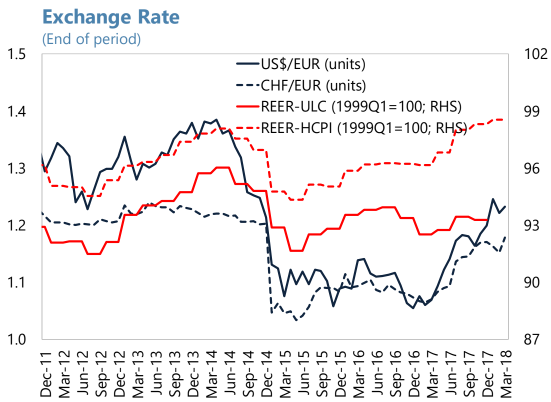
**Consumer Price Index**
(Year-on-year percent change)



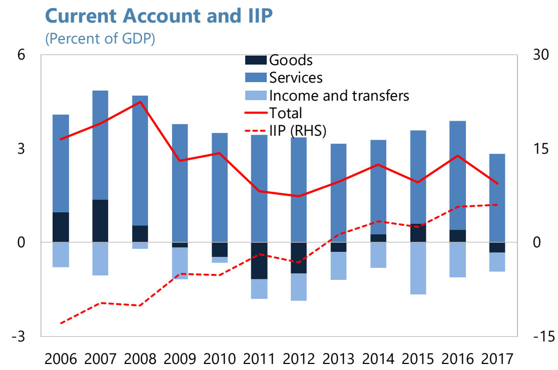

Sources: Haver; Oesterreichische Nationalbank (OeNB); and IMF staff estimates.

## Figure 2. Austria: External and Fiscal Developments

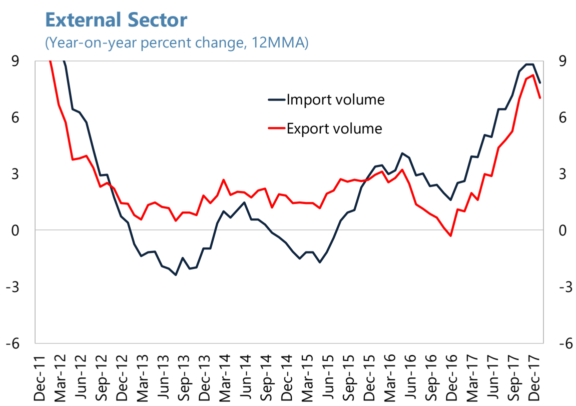
*The real exchange rate has remained broadly stable …*



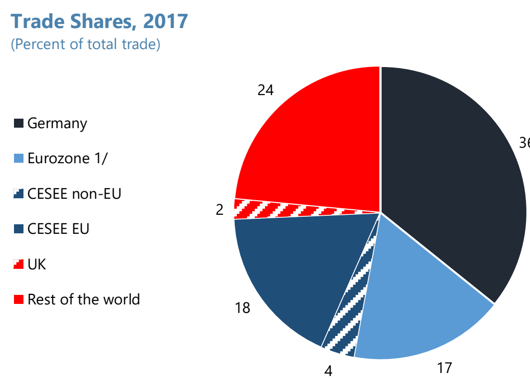

*… and the current account is in small surplus.*



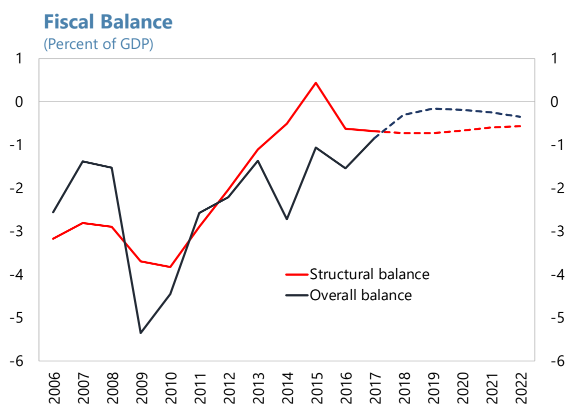

*Trade growth has accelerated strongly.*



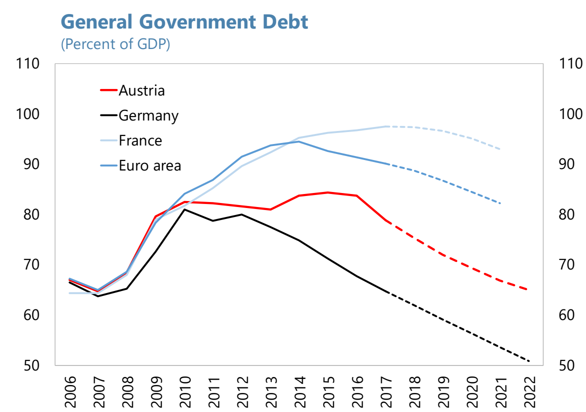

*Most trade is with the EU.*




*Fiscal consolidation has resumed …*




*… and is set to significantly reduce debt.*

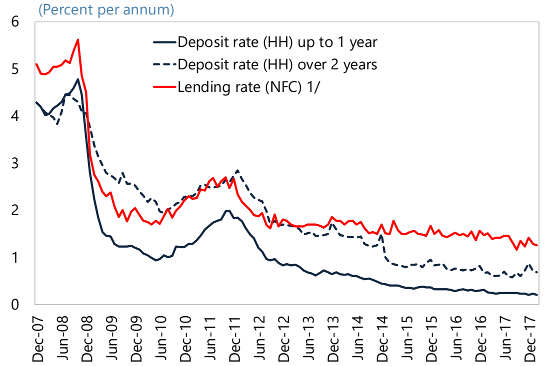



Sources: Haver; OeNB; IMF, Direction of Trade database; and IMF staff estimates.
[1/] Excluding Germany and CESEE euro area countries.

## Figure 3. Austria: Credit and Housing

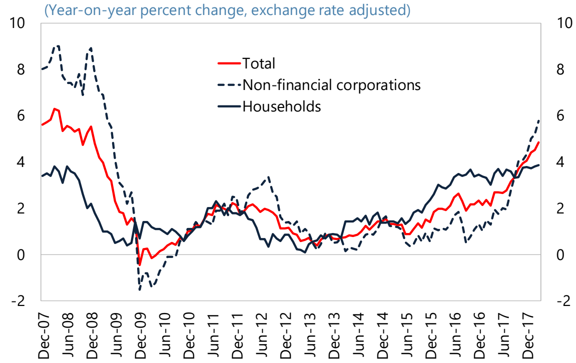
*Interest rates have edged down further …*

### Interest Rates
(Percent per annum)



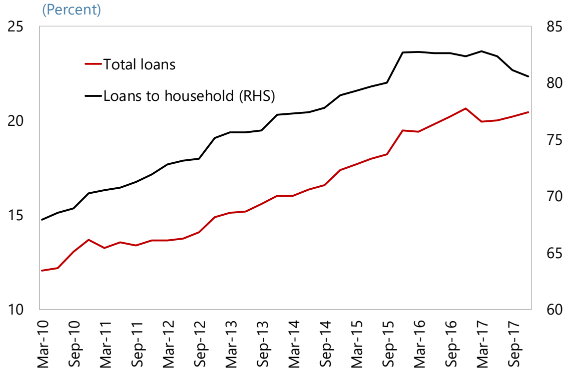

*… and credit has picked up.*

### Credit to the Private Sector
(Year-on-year percent change, exchange rate adjusted)



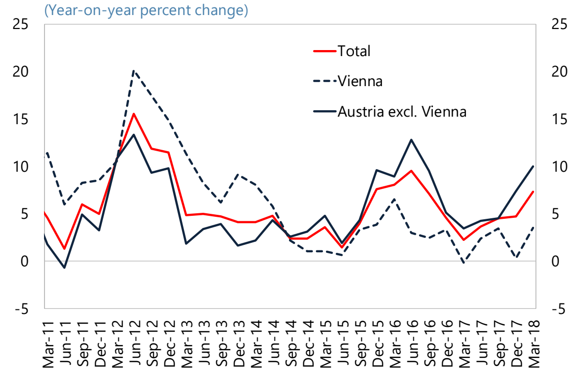

*Real estate loans have continued to grow …*

### Residential Real Estate Loans
(Percent)



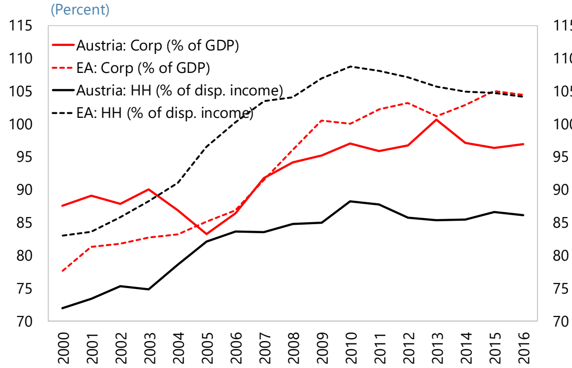

*… as house prices have resumed their rise.*

### House Prices
(Year-on-year percent change)



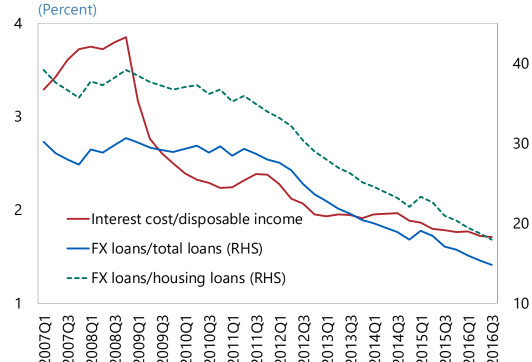

*However, debt levels remain below those of EA peers …*

### Corporate and Household Debt
(Percent)




*…and debt service as well as risk indicators have declined.*

### Households' Debt Service
(Percent)



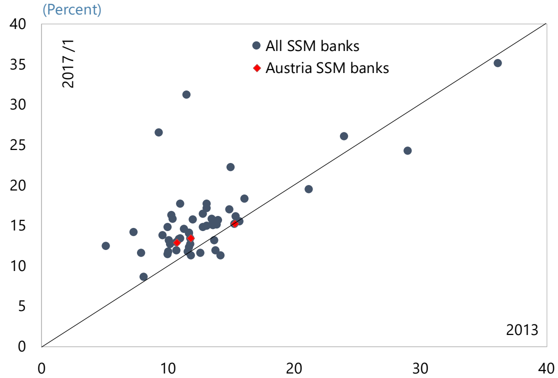

Sources: Haver; OeNB; and IMF staff estimates.

1/ Up to one-year fixed rate for new loans over 1 million euros to non-financial corporations.

## Figure 4. Austria: Banking Sector

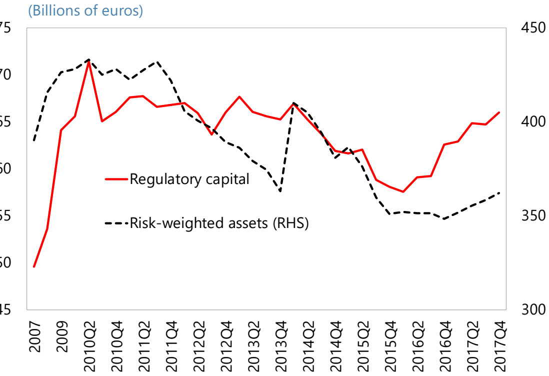
*Austrian banks' have improved their capital ratios …*

**Euro Area SSM Banks: Tier 1 Capital Ratio**
(Percent)



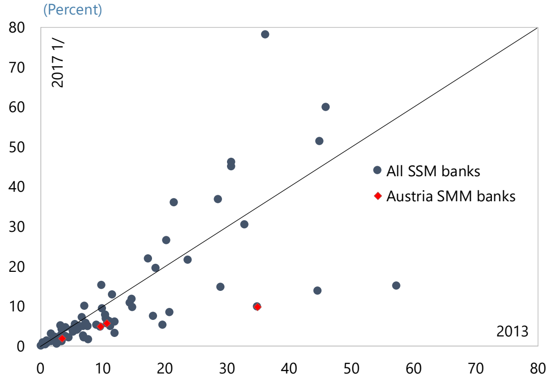

*… with RWA declining and capital broadly constant.*

**Austrian Banks: Capital and Risk-Weighted Assets**
(Billions of euros)



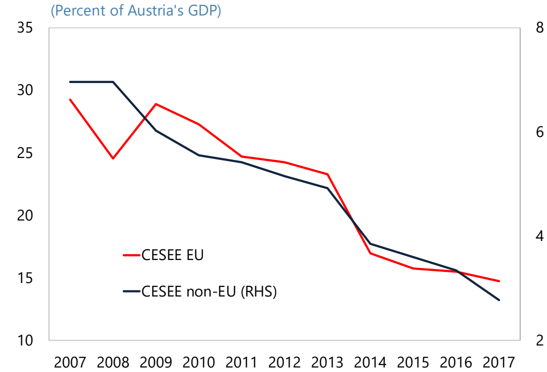

*NPLs have declined as well …*

**Euro Area SSM Banks: NPLs to Gross Loans**
(Percent)



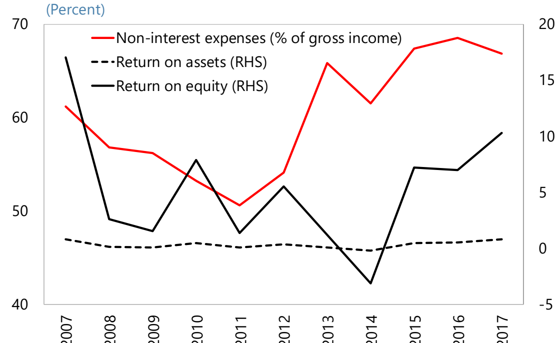

*… and to CESEE has declined.*

**CESEE Exposures**
(Percent of Austria's GDP)



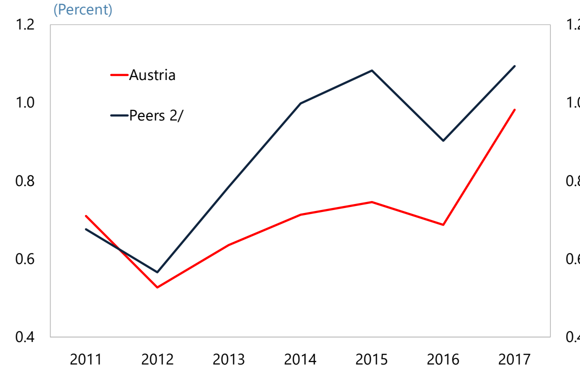

*Profitability has recently risen but costs remain high …*

**Austrian Banks: Profitability**
(Percent)




*Nonetheless, valuations have risen as well.*

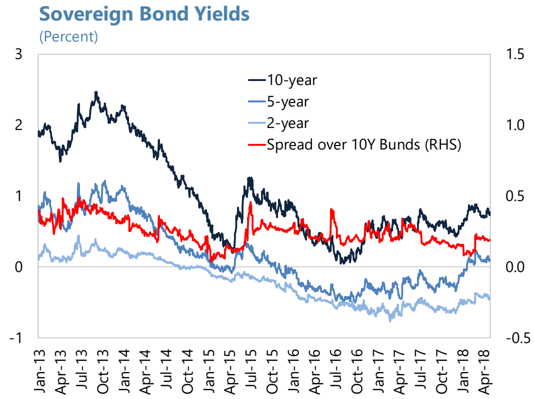
**Price to Book Ratio**
(Percent)



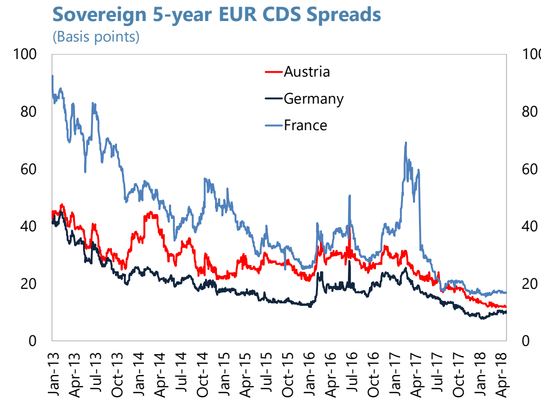

Sources: Bloomberg; SNL; Haver; IMF, Financial Soundness Indicators; and IMF staff estimates.
[1/] 2017 data used when available; otherwise 2016.
[2/] Italy, Hungary, Spain, Belgium, Germany, Sweden and France.

## Figure 5. Austria: Financial Markets

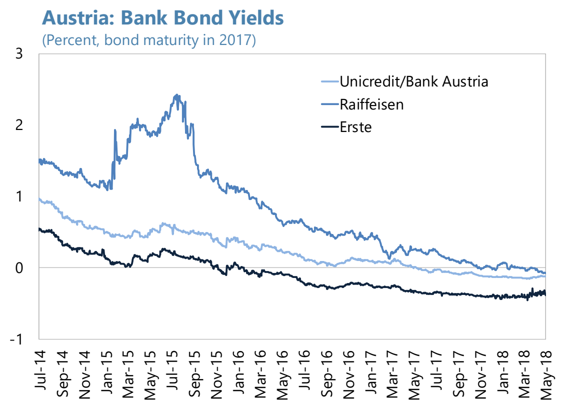
*Borrowing costs remain low …*



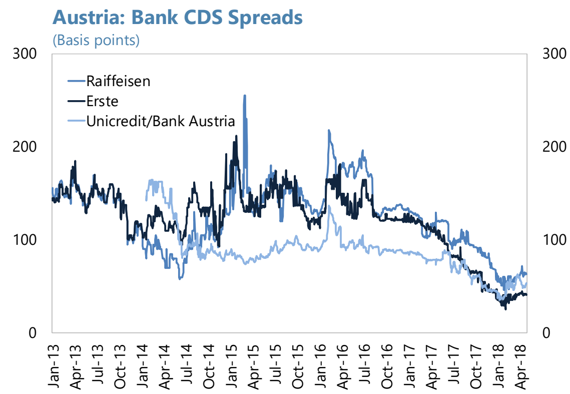

*… while risk perceptions have edged down.*



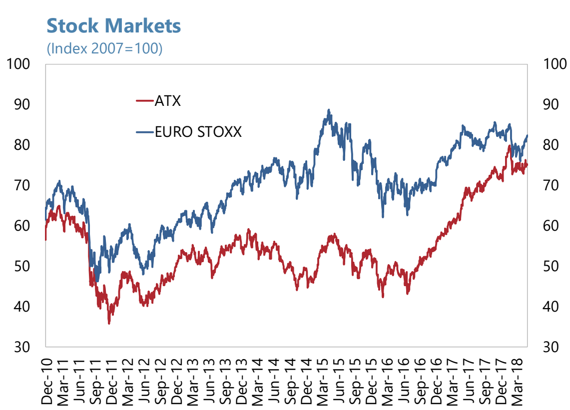

*Bank bond yields have also declined …*



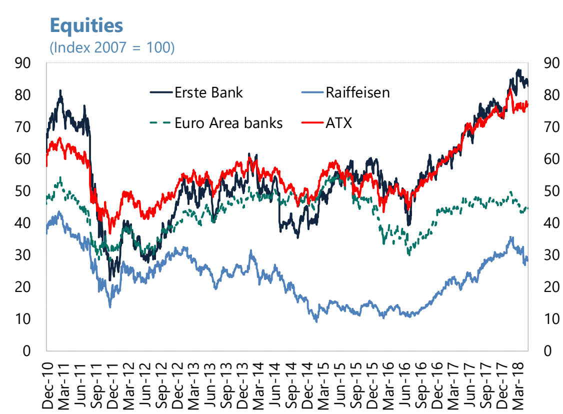

*… and differences in risk perceptions have narrowed.*




*The stock market has recently caught up …*




*… even as some bank equities remain lagging.*




Sources: Bloomberg; DataInsight; and IMF staff estimates.

## Table 1. Austria: Main Economic Indicators, 2015–23

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|---|---|---|
| | | | | Projections | | | | | |
| **NATIONAL ACCOUNTS** | | | | | | | | | |
| Real GDP (expenditure) | 1.1 | 1.5 | 3.0 | 3.0 | 2.2 | 1.6 | 1.5 | 1.5 | 1.5 |
| Domestic demand | 1.1 | 2.1 | 2.8 | 2.9 | 2.2 | 1.6 | 1.6 | 1.4 | 1.6 |
| Consumption | 0.8 | 1.7 | 1.3 | 2.1 | 2.0 | 1.5 | 1.6 | 1.7 | 1.6 |
| Private | 0.5 | 1.5 | 1.4 | 2.3 | 2.3 | 1.6 | 1.6 | 1.9 | 1.7 |
| Public | 1.5 | 2.1 | 0.9 | 1.5 | 1.3 | 1.2 | 1.4 | 1.0 | 1.4 |
| Gross fixed capital formation | 1.2 | 3.7 | 4.9 | 4.2 | 3.0 | 2.1 | 1.7 | 1.5 | 1.5 |
| Private | 1.0 | 3.7 | 5.2 | 4.5 | 3.1 | 2.1 | 1.6 | 1.5 | 1.5 |
| Public | 2.4 | 3.2 | 2.6 | 2.2 | 1.9 | 2.4 | 2.0 | 1.9 | 1.6 |
| GNFS exports | 3.1 | 1.9 | 5.6 | 4.1 | 2.6 | 2.6 | 2.3 | 2.4 | 2.3 |
| GNFS imports | 3.1 | 3.1 | 5.7 | 3.5 | 2.7 | 2.8 | 2.6 | 2.6 | 2.4 |
| Contribution to GDP (percentage points) | | | | | | | | | |
| Final domestic demand | 0.8 | 2.0 | 2.0 | 2.5 | 2.1 | 1.6 | 1.5 | 1.5 | 1.5 |
| Net exports | 0.1 | -0.6 | 0.1 | 0.4 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Inventories and statistical discrepanc | 0.1 | 0.0 | 0.9 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Investment (% GDP) | 23.6 | 24.1 | 25.1 | 25.6 | 25.9 | 25.7 | 25.7 | 25.5 | 25.4 |
| Public | 4.3 | 3.8 | 3.9 | 3.9 | 3.9 | 3.9 | 3.9 | 3.9 | 3.9 |
| Private | 19.3 | 20.3 | 21.2 | 21.7 | 22.0 | 21.8 | 21.8 | 21.6 | 21.5 |
| Gross national savings (% GDP) | 25.5 | 26.2 | 27.0 | 27.7 | 27.9 | 27.9 | 27.8 | 27.6 | 27.6 |
| Public | 3.2 | 2.2 | 3.2 | 3.8 | 3.9 | 4.1 | 4.0 | 3.8 | 3.6 |
| Private | 22.3 | 24.0 | 23.8 | 24.0 | 24.1 | 23.8 | 23.8 | 23.8 | 23.9 |
| Potential output | 1.4 | 1.4 | 1.6 | 1.8 | 1.8 | 1.7 | 1.7 | 1.7 | 1.7 |
| Output gap (% potential GDP) | -1.6 | -1.6 | -0.2 | 1.0 | 1.4 | 1.2 | 0.9 | 0.7 | 0.5 |
| **LABOR MARKET** | | | | | | | | | |
| Labor force | 1.0 | 2.0 | 0.4 | 1.1 | 1.0 | 0.9 | 0.8 | 0.8 | 0.7 |
| Employment | 0.9 | 1.7 | 1.0 | 1.0 | 1.1 | 1.0 | 0.8 | 0.7 | 0.7 |
| Wages (hourly) | 3.2 | 0.5 | 4.0 | 4.5 | 3.2 | 2.6 | 2.6 | 2.7 | 2.7 |
| Unemployment rate (% labor force) | | | | | | | | | |
| EU harmonized rate | 5.7 | 6.0 | 5.5 | 5.2 | 5.1 | 5.0 | 5.0 | 5.1 | 5.1 |
| National definition | 9.1 | 9.1 | 8.5 | 8.1 | 7.9 | 7.8 | 7.7 | 7.7 | 7.6 |
| **PRICES** | | | | | | | | | |
| Consumer prices (avg) | 0.8 | 1.0 | 2.2 | 2.0 | 2.1 | 2.1 | 2.1 | 2.1 | 2.0 |
| Consumer prices (eop) | 1.0 | 1.5 | 2.3 | 1.9 | 2.1 | 2.1 | 2.1 | 2.1 | 2.0 |
| Core CPI (eop) | 1.9 | 1.6 | 2.2 | 1.7 | 2.1 | 2.1 | 2.1 | 2.1 | 2.0 |
| GDP deflator | 2.3 | 1.1 | 1.6 | 1.8 | 1.8 | 2.1 | 2.2 | 2.1 | 2.1 |
| **MACRO-FINANCIAL** | | | | | | | | | |
| Broad money | 4.3 | 5.5 | 4.2 | 4.8 | 4.2 | 3.9 | 3.8 | 3.6 | 3.6 |
| Credit to the private sector | 1.8 | 1.3 | 2.5 | 2.9 | 2.2 | 2.4 | 2.6 | 2.6 | 2.6 |
| Corporations | -0.2 | -1.5 | 0.6 | 1.0 | 0.5 | 1.2 | 1.5 | 1.6 | 1.6 |
| Households | 3.9 | 4.1 | 4.1 | 4.5 | 3.7 | 3.4 | 3.4 | 3.4 | 3.4 |
| **GENERAL GOVERNMENT FINANCES (% GDP)** | | | | | | | | | |
| Revenue | 49.9 | 49.0 | 48.3 | 48.2 | 48.1 | 48.0 | 48.0 | 48.0 | 48.0 |
| Expenditure | 51.0 | 50.6 | 49.0 | 48.4 | 48.1 | 47.8 | 47.8 | 48.0 | 48.2 |
| Net lending/borrowing | -1.0 | -1.6 | -0.7 | -0.2 | 0.0 | 0.1 | 0.1 | -0.1 | -0.3 |
| Structural balance | 0.5 | -0.6 | -0.6 | -0.7 | -0.8 | -0.5 | -0.4 | -0.5 | -0.6 |
| Structural primary balance | 2.8 | 1.5 | 1.2 | 0.9 | 0.7 | 0.9 | 0.9 | 0.8 | 0.6 |
| Gross debt | 84.3 | 83.6 | 78.5 | 74.2 | 70.9 | 67.8 | 65.0 | 62.8 | 60.9 |
| **BALANCE OF PAYMENTS** | | | | | | | | | |
| Current account (% GDP) | 1.9 | 2.1 | 1.9 | 2.1 | 2.1 | 2.1 | 2.1 | 2.2 | 2.2 |
| Export volume (goods and services) | 3.1 | 1.9 | 5.6 | 4.1 | 2.6 | 2.6 | 2.3 | 2.4 | 2.3 |
| Import volume (goods and services) | 3.1 | 3.1 | 5.7 | 3.5 | 2.7 | 2.8 | 2.6 | 2.6 | 2.4 |
| Int'l investment position, net (% GDP) | 2.5 | 5.7 | 6.0 | 7.8 | 9.5 | 11.2 | 12.9 | 14.6 | 16.2 |
| **MEMORANDUM ITEMS** | | | | | | | | | |
| Nominal GDP (bn €) | 344 | 353 | 370 | 387 | 403 | 417 | 433 | 449 | 465 |
| Population (million) | 8.6 | 8.7 | 8.8 | 8.9 | 9.0 | 9.0 | 9.1 | 9.1 | 9.2 |
| GDP per capita ($) | 44,297 | 44,733 | 47,357 | 52,297 | 53,761 | 55,957 | 57,915 | 60,064 | 62,075 |
| US$/€ (rate; annual avg) | 1.11 | 1.11 | 1.13 | … | … | … | … | … | … |
| Real effective exchange rate | -4.0 | 1.2 | 2.0 | 0.9 | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 |

Sources: Authorities' data and IMF staff estimates and projections.

## Table 2. Austria: Fiscal Accounts, 2015–23

(In percent of GDP, unless otherwise indicated)

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|---|---|---|
| | | | | Projections | | | | | |
| **GENERAL GOVERNMENT OPERATIONS** | | | | | | | | | |
| **Revenue** | **49.9** | **49.0** | **48.3** | **48.2** | **48.1** | **48.0** | **48.0** | **48.0** | **48.0** |
| Tax revenue | 28.6 | 27.5 | 27.2 | 27.2 | 27.1 | 27.1 | 27.0 | 27.1 | 27.1 |
| Direct taxes | 14.1 | 12.9 | 12.9 | 13.0 | 13.0 | 13.1 | 13.1 | 13.1 | 13.1 |
| *Of which:* Personal income tax | 10.7 | 9.4 | 9.4 | 9.5 | 9.5 | 9.5 | 9.5 | 9.5 | 9.5 |
| Corporate income tax | 2.3 | 2.4 | 2.4 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 |
| Indirect taxes | 14.5 | 14.6 | 14.3 | 14.1 | 14.0 | 14.0 | 13.9 | 13.9 | 13.9 |
| *Of which:* VAT | 7.6 | 7.7 | 7.5 | 7.5 | 7.4 | 7.4 | 7.4 | 7.4 | 7.4 |
| Social contributions | 15.1 | 15.3 | 15.1 | 15.1 | 15.1 | 15.1 | 15.1 | 15.1 | 15.1 |
| Other current revenue | 6.2 | 6.2 | 6.0 | 6.0 | 5.9 | 5.8 | 5.8 | 5.8 | 5.8 |
| **Expenditure** | **51.0** | **50.6** | **49.0** | **48.4** | **48.1** | **47.8** | **47.8** | **48.0** | **48.2** |
| Expense | 48.0 | 47.6 | 46.0 | 45.4 | 45.0 | 44.8 | 44.8 | 45.0 | 45.2 |
| Compensation of employees | 10.7 | 10.7 | 10.6 | 10.5 | 10.5 | 10.5 | 10.4 | 10.4 | 10.5 |
| Goods and services | 6.4 | 6.4 | 6.1 | 6.0 | 5.9 | 5.9 | 5.9 | 6.0 | 6.1 |
| Social benefits | 22.8 | 22.9 | 22.2 | 21.9 | 21.9 | 21.9 | 22.0 | 22.2 | 22.3 |
| Other current transfers | 2.7 | 2.8 | 2.5 | 2.5 | 2.4 | 2.4 | 2.4 | 2.5 | 2.5 |
| Capital transfers | 1.3 | 0.8 | 0.8 | 0.9 | 0.8 | 0.9 | 0.9 | 0.8 | 0.8 |
| Interest | 2.3 | 2.1 | 1.8 | 1.6 | 1.5 | 1.4 | 1.3 | 1.2 | 1.2 |
| Subsidies | 1.3 | 1.4 | 1.4 | 1.5 | 1.5 | 1.5 | 1.4 | 1.3 | 1.3 |
| Other | 0.5 | 0.5 | 0.5 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 | 0.5 |
| Acquisition of nonfinancial assets | 3.0 | 3.0 | 3.0 | 3.0 | 3.0 | 3.0 | 3.1 | 3.1 | 3.1 |
| *Of which:* Gross fixed capital formation | 3.0 | 3.0 | 3.0 | 3.0 | 3.0 | 3.0 | 3.1 | 3.1 | 3.1 |
| Operating balance | 1.9 | 1.4 | 2.3 | 2.9 | 3.0 | 3.2 | 3.2 | 3.0 | 2.8 |
| Primary balance | 1.3 | 0.5 | 1.1 | 1.4 | 1.5 | 1.6 | 1.5 | 1.2 | 0.9 |
| **Net lending/borrowing** | **-1.0** | **-1.6** | **-0.7** | **-0.2** | **0.0** | **0.1** | **0.1** | **-0.1** | **-0.3** |
| **GENERAL GOVERNMENT BALANCE SHEET** | | | | | | | | | |
| Financial liabilities | 108 | 108 | 101 | 96 | 92 | 88 | 84 | 82 | 79 |
| Gross debt | 95 | 96 | 89 | 84 | 80 | 77 | 74 | 71 | 69 |
| Other | 12 | 12 | 12 | 12 | 11 | 11 | 11 | 10 | 10 |
| Financial assets | 50 | 50 | 47 | 45 | 43 | 42 | 40 | 39 | 37 |
| Net financial worth | -57 | -59 | -54 | -51 | -49 | -46 | -44 | -43 | -42 |
| Net debt | 69 | 70 | 66 | 62 | 60 | 57 | 54 | 52 | 51 |
| **Gross debt (Maastricht def.)** | **84.3** | **83.6** | **78.5** | **74.2** | **70.9** | **67.8** | **65.0** | **62.8** | **60.9** |
| Guarantees | 23.1 | 20.5 | 16.6 | 15.8 | 15.2 | 14.7 | 14.2 | 13.7 | 13 |
| **MEMORANDUM ITEMS** | | | | | | | | | |
| Cyclically adjusted balance | -0.1 | -0.7 | -0.6 | -0.7 | -0.8 | -0.5 | -0.4 | -0.5 | -0.6 |
| Structural balance 1/ | 0.5 | -0.6 | -0.6 | -0.7 | -0.8 | -0.5 | -0.4 | -0.5 | -0.6 |
| Structural primary balance 1/ | 2.8 | 1.5 | 1.2 | 0.9 | 0.7 | 0.9 | 0.9 | 0.8 | 0.6 |
| Change in real revenue (percent) | 3.3 | -0.3 | 0.8 | 2.6 | 1.4 | 1.3 | 1.5 | 1.5 | 1.6 |
| Change in real primary expenditure (percent) | 0.0 | 1.3 | -0.5 | 2.0 | 1.3 | 1.2 | 1.8 | 2.2 | 2.1 |
| Nominal GDP (bn €) | 344 | 353 | 370 | 387 | 403 | 417 | 433 | 449 | 465 |

Sources: Authorities' data and IMF staff estimates and projections.

1/ One-off measures as defined in the Austrian Stability Program.

## Table 3. Austria: Balance of Payments, 2015–23

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|---|---|---|
| | | | | Projections | | | | | |
| **BALANCE OF PAYMENTS** | | | | | | | | | |
| **Current account** | **1.9** | **2.1** | **1.9** | **2.1** | **2.1** | **2.1** | **2.1** | **2.2** | **2.2** |
| Balance on goods and services | 3.6 | 3.2 | 2.5 | 2.9 | 2.7 | 2.9 | 2.9 | 3.0 | 3.0 |
| Exports of goods and services | 52.8 | 52.2 | 53.5 | 54.9 | 56.1 | 56.4 | 56.7 | 57.1 | 57.4 |
| Exports of goods | 37.4 | 36.5 | 37.5 | 38.6 | 39.6 | 39.7 | 39.9 | 40.0 | 40.1 |
| Exports of services | 15.5 | 15.7 | 15.9 | 16.2 | 16.6 | 16.8 | 16.9 | 17.1 | 17.3 |
| Imports of goods and services | 49.2 | 48.9 | 51.0 | 52.0 | 53.4 | 53.6 | 53.8 | 54.1 | 54.4 |
| Imports of goods | 36.8 | 36.4 | 37.9 | 38.5 | 39.6 | 39.6 | 39.7 | 39.9 | 40.0 |
| Imports of services | 12.5 | 12.5 | 13.1 | 13.5 | 13.8 | 14.0 | 14.1 | 14.2 | 14.4 |
| Primary income, net | -0.7 | -0.1 | 0.2 | 0.2 | 0.3 | 0.3 | 0.3 | 0.2 | 0.2 |
| Secondary income, net | -0.9 | -1.0 | -0.8 | -0.9 | -0.9 | -1.0 | -1.0 | -1.0 | -1.0 |
| **Capital account** | **-0.5** | **-0.2** | **-0.1** | **-0.1** | **-0.1** | **-0.1** | **-0.1** | **-0.1** | **-0.1** |
| **Financial account** | **1.2** | **2.8** | **2.4** | **2.1** | **2.0** | **2.1** | **2.1** | **2.1** | **2.1** |
| Direct investment, net | 1.7 | 0.4 | 0.4 | 0.9 | 1.4 | 2.0 | 2.0 | 2.0 | 2.0 |
| Direct investment abroad, net | -0.6 | -7.4 | 3.7 | 3.7 | 3.7 | 3.7 | 3.7 | 3.7 | 3.7 |
| Direct investment in Austria, net | -2.3 | -7.8 | 3.3 | 2.8 | 2.3 | 1.7 | 1.7 | 1.7 | 1.7 |
| Portfolio investment, net | 4.1 | 6.7 | 5.2 | 3.6 | 3.0 | 2.5 | 2.5 | 2.6 | 2.5 |
| Financial derivatives, net | -0.2 | -0.1 | -0.2 | -0.2 | -0.2 | -0.2 | -0.2 | -0.2 | -0.2 |
| Other investment, net | -4.2 | -4.2 | -2.2 | -2.2 | -2.2 | -2.2 | -2.2 | -2.2 | -2.2 |
| Reserve assets | -0.1 | 0.1 | -0.8 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Errors and omissions, net | -0.2 | 0.9 | 0.7 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **BALANCE SHEET** | | | | | | | | | |
| **Int'l investment position, net** | **2.5** | **5.7** | **6.0** | **7.8** | **9.5** | **11.2** | **12.9** | **14.6** | **16.2** |
| Assets | 254 | 241 | 232 | 227 | 223 | 220 | 217 | 214 | 212 |
| Liabilities | 251 | 236 | 226 | 219 | 213 | 209 | 204 | 200 | 195 |
| Direct investment | 13 | 13 | 11 | 11 | 12 | 14 | 15 | 17 | 18 |
| Assets | 88 | 80 | 79 | 79 | 79 | 80 | 81 | 82 | 83 |
| Liabilities | 75 | 67 | 68 | 67 | 67 | 66 | 66 | 65 | 64 |
| Portfolio investment | -31 | -25 | -19 | -15 | -11 | -8 | -5 | -3 | 0 |
| Financial derivatives | 0 | 0 | 0 | 0 | 0 | 0 | -1 | -1 | -1 |
| Other investment | 15 | 11 | 9 | 6 | 4 | 2 | -1 | -3 | -5 |
| Reserve assets | 6 | 6 | 5 | 5 | 4 | 4 | 4 | 4 | 4 |
| **MEMORANDUM ITEMS** | | | | | | | | | |
| Export value (goods and services) | 2.4 | 1.3 | 7.2 | 7.5 | 6.3 | 4.3 | 4.2 | 4.3 | 4.2 |
| Import value (goods and services) | 1.7 | 1.9 | 9.0 | 6.9 | 6.8 | 4.0 | 4.1 | 4.2 | 4.2 |
| Nominal GDP (bn €) | 344 | 353 | 370 | 387 | 403 | 417 | 433 | 449 | 465 |

Sources: Authorities' data and IMF staff estimates and projections.

## Table 4. Austria: Financial Soundness Indicators, 2013–17

| | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|
| **FINANCIAL SOUNDNESS INDICATORS** | (In percent, unless otherwise inidcated) | | | | |
| **Capital adequacy** | | | | | |
| Regulatory capital/risk-weighted assets 1/ | 18.0 | 16.3 | 16.5 | 18.0 | 18.2 |
| Regulatory Tier 1 capital/risk-weighted assets 1/ | 13.7 | 12.3 | 13.2 | 14.5 | 15.0 |
| Capital/assets 2/ | 8.0 | 6.8 | 7.4 | 7.3 | 7.5 |
| Large exposures/capital 2/ | 52.6 | 70.5 | 59.2 | 60.7 | 51.2 |
| Nonperforming loans net of provisions/capital 2/ 3/ | 5.8 | 13.8 | 13.2 | 11.2 | 10.9 |
| FX NOP/capital | 0.2 | 0.7 | 0.2 | 1.0 | 0.1 |
| **Liquidity and debt 2/** | | | | | |
| Liquid assets/ST liabilities | 69 | 67 | 68 | 67 | 66 |
| Liquid assets/total assets | 24 | 23 | 25 | 25 | 24 |
| Debt/equity | 117 | 112 | 108 | 106 | 102 |
| **Asset quality** | | | | | |
| Loans to residents/gross loans | 70 | 70 | 74 | 75 | 76 |
| Loans to nonfinancial corporations | 20 | 20 | 21 | 21 | 22 |
| Loans to deposit takers | 23 | 20 | 20 | 19 | 18 |
| Loans to other domestic sectors | 20 | 21 | 22 | 24 | 24 |
| Other | 8 | 9 | 11 | 11 | 12 |
| Loans to nonresidents/gross loans | 30 | 30 | 26 | 25 | 24 |
| NPLs/gross loans 2/ 3/ | 2.9 | 3.5 | 3.4 | 2.7 | 2.4 |
| FX loans/total loans | 19 | 19 | 15 | 14 | 11 |
| **Geographic distribution 2/ 4/** | | | | | |
| Domestic economy/gross loans | 70 | 70 | 74 | 75 | 76 |
| Advanced economies/gross loans | 15 | 16 | 14 | 15 | 13 |
| Emerging markets/gross loans | 15 | 14 | 12 | 10 | 10 |
| *Of which:* | | | | | |
| CEE | 12.3 | 10.7 | 9.6 | 8.2 | 8.5 |
| CIS | 2.1 | 2.0 | 1.5 | 0.8 | 0.7 |
| **Earnings, expenses, and profitability** | | | | | |
| Spread (reference lending rate to deposit rate; bps) 2/ | 181 | 196 | 193 | 190 | 179 |
| Net interest income/gross income 1/ | 66 | 59 | 59 | 59 | 59 |
| Trading income/total income 2/ | 2.6 | 1.8 | 2.5 | 1.7 | 1.7 |
| Non-interest expenses/gross income 1/ | 96.5 | 77.3 | 69.6 | 74.8 | 67.1 |
| Personnel expenses/non-interest expenses 2/ | 50.7 | 53.1 | 50.2 | 49.9 | 46.9 |
| Return on assets 1/ | 0.1 | -0.2 | 0.5 | 0.5 | 0.8 |
| Return on equity 1/ | 1.2 | -3.2 | 7.2 | 7.0 | 10.3 |
| Earnings/equity 1/ | 12.6 | 11.0 | 11.1 | 10.6 | 12.1 |
| **Households 2/** | | | | | |
| Household debt/GDP | 51 | 52 | 53 | 53 | 51 |
| Residential real estate loans/total loans | 16.0 | 17.4 | 19.5 | 20.6 | 20.4 |
| Residential real estate prices (% change) | 4.1 | 2.4 | 7.6 | 4.6 | 4.7 |
| **Structural indicators 2/** | | | | | |
| Assets/GDP | 86 | 90 | 90 | 89 | 93 |
| Assets/total financial system assets | 23 | 25 | 26 | 28 | 30 |
| **MEMORANDUM ITEMS** | (In units indicated) | | | | |
| Total assets/liabilities (% GDP) 1/ | 282 | 263 | 248 | 238 | 221 |
| Credit to domestic non-bank private sector (% GDP) | 89 | 85 | 84 | 83 | 81 |
| Percent change (y/y) | -0.2 | -2.0 | 1.8 | 1.3 | 2.5 |
| Corporations | -0.4 | -5.0 | -0.2 | -1.5 | 0.6 |
| Households 5/ | 0.0 | 1.4 | 3.9 | 4.1 | 4.1 |
| Nominal GDP (bn €) | 324 | 333 | 344 | 353 | 370 |

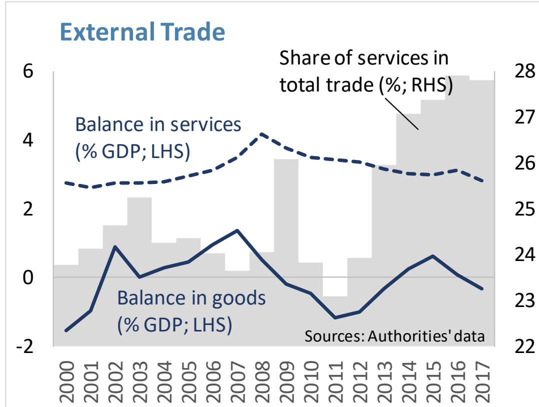
Sources: Authorities, and IMF staff estimates and projections.

1/ Domestically controlled, cross-border and cross sector consolidation basis.
2/ Domestic consolidation basis.
3/ From 2014, NPLs are reported on a borrower instead of single loan basis.
4/ Includes loans to financial institutions.
5/ Exludes shares and other equity.

# Annex I. External Sector Assessment

*Austria's external position remains broadly in line with fundamentals and desirable policies. The current account gap is near zero, while the REER is modestly overvalued.*

**External position.** Austria's external position has strengthened considerably in recent years, with the international investment position (IIP) moving from -21 percent of GDP in 2001 to a moderate 6 percent in 2017, as the current account moved into surplus in 2002. This shift took place as goods exports rose faster than imports as Austria became more closely integrated into European value chains after entry into the EU in 1995. This moved trade in goods closer to balance. At the same time, trade in services, in which Austria has traditionally a surplus (based largely on tourism) became more important in overall trade. Going forward, the current account is expected to remain broadly unchanged. Regarding financial flows, Austrian banks sharply reduced their reliance on foreign wholesale financing (and exposure to CESEEs), with the decline in foreign liabilities exceeding the decline in assets as deposits rebounded both at home and in CESEEs. This has led to a decline in banks' gross external assets from a peak of over 100 percent of GDP in 2008 to about 62 percent of GDP in 2017. The transfer of Bank Austria's CESEE operations to Unicredit, its Italian parent, has further contributed to the reduction of the banking system's asset and liability position in the order of 30 percent of GDP.




**External Balance Assessment**

| Methodology | Total Gap (%) | Policy Gaps (%): Total | Fiscal balance | Health exp. | Reserves | Private credit | Capital controls | Real i-rate | Residual (%) |
|---|---|---|---|---|---|---|---|---|---|
| Current account | 0.1 | 0.9 | 0.6 | -0.3 | -0.2 | 0.9 | -0.1 | … | -0.8 |
| REER (index) 1/ | 7.4 | 2.6 | … | 2.5 | -0.1 | -0.2 | 0.0 | 0.4 | 4.8 |
| REER (level) 2/ | 10.3 | 3.8 | … | 3.5 | -0.1 | -0.2 | 0.0 | 0.5 | 6.6 |

Sources: Authorities' data
1/ Considers the REER CPI index in each country, and thus does not explain inter-country variations.
2/ Takes into account differences in real PPP exchange rates across countries.

**Current account balance and real exchange rate.** The external balance is assessed to be broadly consistent with medium-term fundamentals and desirable policies. Using the External Balance Assessment estimates, the current account balance in 2017 (2 percent of GDP, cyclically adjusted) was close to the norm (estimated at 1.8 percent of GDP).[1] The policy gap arises from a low budget

[1] The analysis is based on panel regressions of the current account balance and the real effective exchange rate (REER), which are simultaneously determined. The first stage is descriptive and focused on understanding current account and real exchange rate developments. The second stage is oriented toward a normative evaluation, drawing on the regression results to estimate equilibrium values for the current account balance and the REER, deviations ("gaps") of actual current account balances and REER from these equilibrium values, as well as the contributions of "policy gaps" to the overall current account balance and REER gaps.

deficit relative to trading partners—partly counterbalanced by high health expenditure relative to trading partners—and relatively weak credit as a percentage of GDP. However, with the overall gap close to zero, the policy gap is counterbalanced by an unexplained residual. Model-based estimates suggest that the REER was modestly overvalued (around 7½–10¼ percent). However, these estimates do not take into account the cyclical position and the unexplained residual is large, accounting for close to two-thirds of the estimated overvaluation. Therefore, using the current account gap as reference and an estimated semi-elasticity of 0.07 yields an indicative REER gap of -1.2 percent which is assessed as broadly consistent with fundamentals.

**Capital and financial account.** Net direct investment outflows to both CESEE countries and the EU-15, have recovered quickly after the GFC driven by real-sector investment, keeping the FDI position generally in surplus.[2] Net portfolio investment outflows have been strong as well and are expected to remain so, despite the further retrenching of Austrian banks' foreign holdings, and the negative net portfolio investment position is expected to narrow gradually. This will be mirrored by a decline in the net "other investments" position.

**Overall assessment.** Austria's external position is sustainable and broadly in line with fundamentals. The ageing population implies that a build-up of external assets in the next few years is warranted as a buffer for future withdrawals. Policies are broadly appropriate, though raising the efficiency of health expenditures and reforming pensions would open significant savings potential to help ensure fiscal sustainability in the long run.

[2] In 2016, the transfer of CESEE operations of Bank Austria (a subsidiary of Unicredit) to Unicredit in Italy led to the temporary decline in net FDI outflows.

# Annex II. Risk Assessment Matrix[1]

| Source of Risk | Relative Likelihood | Time Horizon | Impact/Policy Response |
|---|---|---|---|
| **Retreat from cross-border integration.** Fraying consensus about the benefits of globalization leads to protectionism and economic isolationism, resulting in reduced global and regional policy and regulatory collaboration with negative consequences for trade, capital and labor flows, sentiment, and growth. | Medium | ST, MT | **Medium.** Austria is a very open economy, with exports comprising over 50 percent of GDP (of which about 70 percent to the EU). A retreat from cross-border integration could reduce exports and potential growth and jeopardize fiscal consolidation. *Policy response:* maintain free movement of goods, services, capital, and labor with key partners as at present. |
| **Policy uncertainty.** Two-sided risks to U.S. growth with uncertainties about the positive short-term impact of the tax bill on growth and the extent of potential medium-term adjustment to offset its fiscal costs; uncertainty associated with negotiating post-Brexit arrangements and NAFTA and associated market fragmentation risks; and evolving political processes, including elections in several large economies, weigh on the whole on global growth. | Medium | ST, MT | **Low.** The effects of Brexit as well as developments in the U.S. are largely indirect (via their impact on Germany and other EU partners) since direct economic relations with the UK are limited. However, a slump in confidence could reduce investment. *Policy response:* implement reforms to boost productivity and potential growth. |
| **Intensification of the risks of fragmentation/security dislocation** in parts of the Middle East, Africa, Asia, and Europe, leading to socio-economic disruptions. | High | ST, MT | **Low.** Increased migrant flows could lead to another wave of refugees entering Austria. Apart from creating political tensions, this would put some strain on public finances in the short term. The contribution of immigrants to the economy will depend on the success of integration policies. *Policy response:* invest in integration of admitted asylum seekers. |
| **Further pressure on traditional bank business models.** Legacy problems, and potential competition from non-banks curtail banks' profitability globally. Loss of confidence if such profitability challenges are not addressed could increase the risk of distress at one or more major banks with possible knock-on effects on the broader financial sector and for sovereign yields in vulnerable economies. Migration of activities outside of the traditional banking sector, including provision of financial services by fintech intermediaries, raises competitive pressures on traditional banks, making risk monitoring and mitigation more difficult. | Medium | MT | **Low.** Confidence in Austria's banks and, more broadly, financial stability could be affected, and financing conditions deteriorate if profitability does not improve, due to materialization of political or regulatory risks in CESEE countries, or increased competition, including from non-banks. However, fintech also represents an opportunity for banks to improve efficiency. Austrian banks have been acquiring fintech companies to this end. Moreover, regulations in Austria are tight, preventing uncontrolled market entry. *Policy response:* further strengthen banks' capital cushions, reinforce efficiency drive. |

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

| | | | |
|---|---|---|---|
| **Structurally weak growth in key advanced economies.** Low productivity growth (U.S., euro area and Japan), high debt, and failure to fully address crisis legacies by undertaking structural reforms amidst persistently low inflation (euro area and Japan) undermine medium-term growth. | High | MT | **Medium.** Austria would be directly affected, if growth in Germany, the rest of the EU, or CESEE were to slow. *Policy response:* accelerate structural and fiscal reforms. Continue close monitoring of banks' profitability and capital levels, and implementation of their adjustment plans. |
| **Cyber-attacks** on interconnected financial systems and broader private and public institutions that trigger systemic financial instability or widely disrupt socio-economic activities. | Medium | ST, MT | **Low.** Austria, like other advanced economies, would be affected negatively. *Policy response:* strengthen domestic defenses including back-up systems and financial cushions and promote international cooperation. |
| **Integration of immigrants.** If efforts to integrate immigrants into the labor market were to be reduced, their productivity could be reduced and welfare dependency rise. | Medium | ST, MT | **Medium.** A potential reduction of efforts to integrate immigrants could reduce their contribution to the economy, slowing growth and increasing welfare spending. *Policy response:* maintain or increase integration efforts. |

# Annex III. Debt Sustainability Analysis

*Austria's debt outlook has improved further. Public debt is sustainable within the medium-term projection horizon, though ageing cost pressures are looming in the longer term. Under the baseline, debt will fall from around 84 percent of GDP at end-2016 to 61 percent of GDP by end-2023. Standardized stress tests indicate that lower growth and a combined macro-fiscal shock could shift the debt-to-GDP ratio upwards, but debt would remain on a downward trajectory. However, in the longer term (starting in the mid-2020s), ageing cost pressures and higher interest rates would reverse the debt path without additional policy measures.*

## Baseline

Under the baseline, fiscal policy is set to return the structural deficit to ½ percent of GDP, Austria's MTO, by 2020.[1] This, as well as the positive effects of the deal with the creditors of HETA, the wind-down unit of the former Hypo Alpe Adria bank, would bring gross public debt to 61 percent of GDP by 2023, almost 18 percentage points down from its 2017 level.[2] Gross financing needs are moderate in the period 2018–23.

The heat map indicates that vulnerabilities remain limited. The declining debt level implies that the impact of potential shocks would not push Austria's debt up—except for a contingent liability shock—over the relevant thresholds. The high share of public debt held by non-residents, and the attendant external financing requirements, are a potential vulnerability, though this is limited by the perception of Austria as a safe haven. However, it could lead to higher volatility in spreads, especially once the European Central Bank's (ECB) asset purchases end, depending on interest rate dynamics outside Austria and residual risks from commercial banks' CESEE exposure.

## Stress Tests

The low-growth scenario assumes that growth is slower by one standard deviation of the historical outturn, implying a reduction by close to 2½ percentage points in 2019–20. However, the debt-to-GDP ratio would increase only marginally and then decline to 68 percent of GDP by 2023. A contingent liability shock of 10 percentage points of GDP would raise public debt to 88 percent of GDP, which would only slowly decline to 81 percent of GDP by 2023. The other standardized macro shocks—the primary balance shock, the real exchange rate shock, and the real interest rate shock—will not lead to significant deviations from the baseline debt path. A combined shock for all variables is driven by assumed lower growth and leads to a similar debt path as in the low-growth scenario.

[1] The structural balance excludes various one-offs, including bank restructuring costs. International experience suggests that the baseline scenario is realistic (Figure 2).

[2] The debt forecast for 2023 is lower than in the 2016 Article IV consultation by almost 7 percentage points (ppts) of GDP on account of a higher nominal GDP during 2017–22, resulting largely from revised real growth projections, and an improved fiscal outlook.

## Figure 1. Austria: Public Sector Debt Sustainability Analysis (DSA) – Risk Assessment

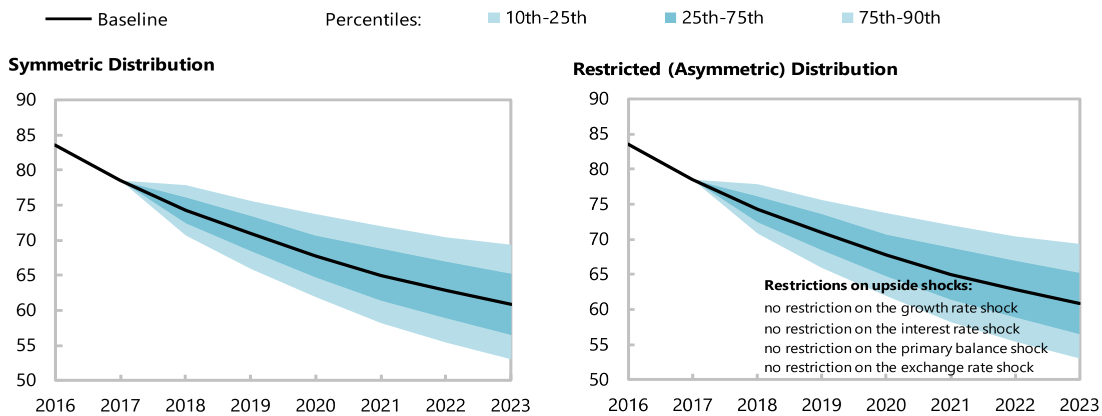
(in percent of GDP unless otherwise indicated)

### Heat Map

| | | | | | |
|---|---|---|---|---|---|
| Debt level 1/ | Real GDP Growth Shock | Primary Balance Shock | Real Interest Rate Shock | Exchange Rate Shock | Contingent Liability shock |
| Gross financing needs 2/ | Real GDP Growth Shock | Primary Balance Shock | Real Interest Rate Shock | Exchange Rate Shock | Contingent Liability Shock |
| Debt profile 3/ | Market Perception | External Financing Requirements | Change in the Share of Short-Term Debt | Public Debt Held by Non-Residents | Foreign Currency Debt |

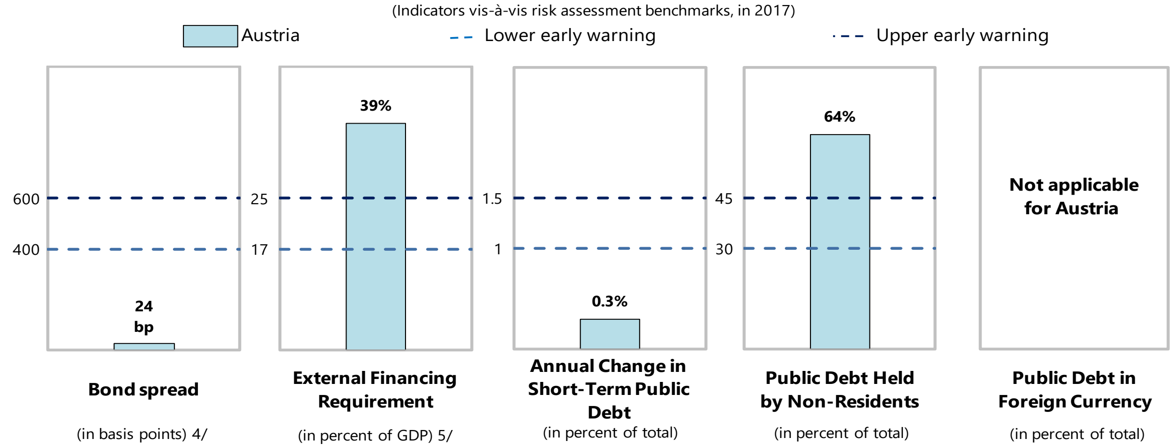
### Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)




### Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2017)




Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 85% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 20% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

400 and 600 basis points for bond spreads; 17 and 25 percent of GDP for external financing requirement; 1 and 1.5 percent for change in the share of short-term debt; 30 and 45 percent for the public debt held by non-residents.

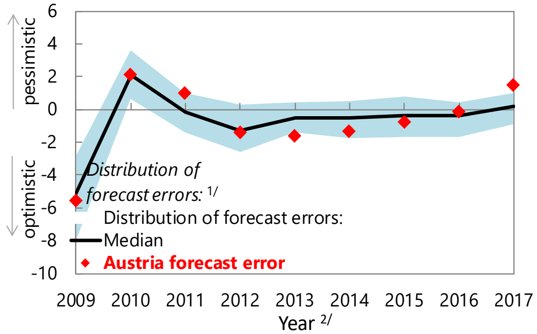
4/ Long-term bond spread over German bonds, an average over the last 3 months, 29-Mar-18 through 27-Jun-18.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

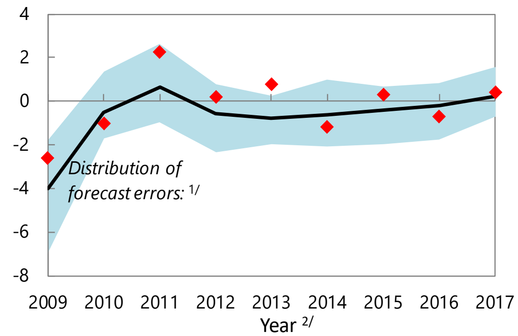
## Figure 2. Austria: Public DSA – Realism of Baseline Assumptions

### Forecast Track Record, versus all countries

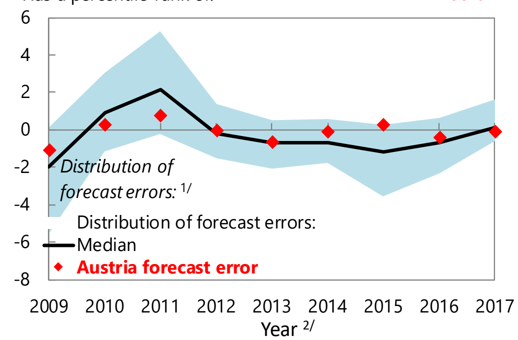
**Real GDP Growth**
(in percent, actual-projection)
Austria median forecast error, 2009-2017: **-0.78**
Has a percentile rank of: **32%**




**Primary Balance**
(in percent of GDP, actual-projection)
Austria median forecast error, 2009-2017: **0.22**
Has a percentile rank of: **79%**

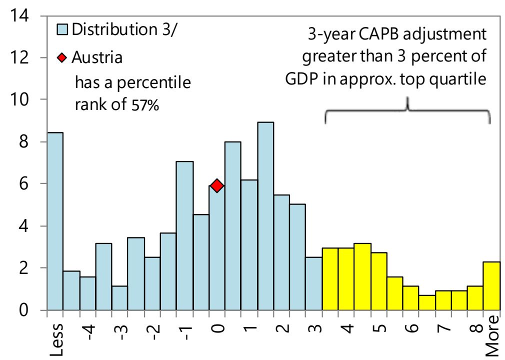



**Inflation (Deflator)**
(in percent, actual-projection)
Austria median forecast error, 2009-2017: **-0.10**
Has a percentile rank of: **66%**

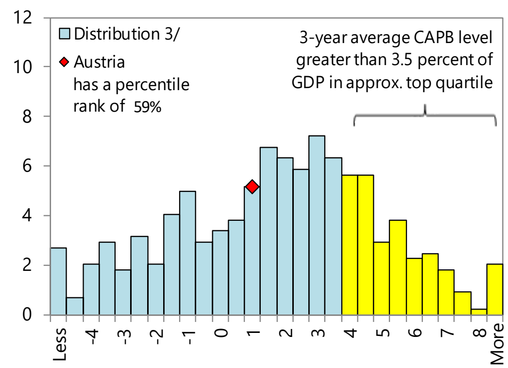



### Assessing the Realism of Projected Fiscal Adjustment

**3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB)**
(Percent of GDP)




**3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)**
(Percent of GDP)




Source : IMF Staff.
1/ Plotted distribution includes all countries, percentile rank refers to all countries.
2/ Projections made in the spring WEO vintage of the preceding year.
3/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

## Figure 3. Austria: Baseline Scenario

(in percent of GDP unless otherwise indicated)

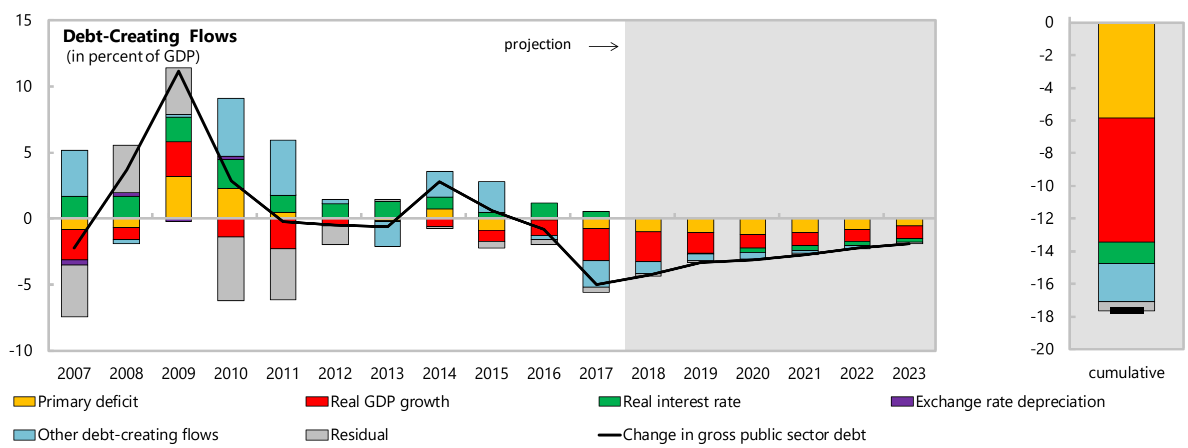
### Debt, Economic and Market Indicators [1]

| | Actual | | | Projections | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2007-2015 [2] | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
| Nominal gross public debt | 78.7 | 83.6 | 78.5 | 74.2 | 70.9 | 67.8 | 65.0 | 62.8 | 60.9 |
| Public gross financing needs | 11.2 | 9.4 | 8.1 | 8.7 | 9.5 | 8.7 | 8.0 | 7.6 | 8.2 |
| Real GDP growth (in percent) | 1.0 | 1.5 | 3.0 | 3.0 | 2.1 | 1.5 | 1.5 | 1.4 | 1.5 |
| Inflation (GDP deflator, in percent) | 1.9 | 1.1 | 1.6 | 1.8 | 1.8 | 2.1 | 2.2 | 2.1 | 2.1 |
| Nominal GDP growth (in percent) | 2.9 | 2.6 | 4.6 | 4.8 | 4.0 | 3.7 | 3.7 | 3.6 | 3.6 |
| Effective interest rate (in percent) [4] | 3.8 | 2.6 | 2.3 | 1.9 | 1.7 | 1.7 | 1.6 | 1.6 | 1.7 |

| As of June 27, 2018 | | |
|---|---|---|
| Sovereign Spreads | | |
| EMBIG (bp) 3/ | | 30 |
| 5Y CDS (bp) | | 15 |
| Ratings | Foreign | Local |
| Moody's | Aa1 | Aa1 |
| S&Ps | AA+ | AA+ |
| Fitch | AA+ | AA+ |

### Contribution to Changes in Public Debt

| | Actual | | | Projections | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2007-2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | cumulative | debt-stabilizing primary balance [9] |
| Change in gross public sector debt | 1.9 | -0.8 | -5.0 | -4.3 | -3.3 | -3.1 | -2.7 | -2.2 | -1.9 | -17.6 | |
| Identified debt-creating flows | 2.7 | -0.4 | -4.7 | -4.1 | -3.2 | -3.1 | -2.7 | -2.3 | -1.8 | -17.1 | |
| Primary deficit | 0.5 | -0.1 | -0.8 | -1.0 | -1.1 | -1.2 | -1.1 | -0.8 | -0.6 | -5.8 | -1.2 |
| Primary (noninterest) revenue and grants | 48.2 | 48.6 | 47.9 | 47.9 | 47.7 | 47.6 | 47.6 | 47.6 | 47.6 | 286.0 | |
| Primary (noninterest) expenditure | 48.7 | 48.5 | 47.2 | 46.8 | 46.6 | 46.4 | 46.5 | 46.8 | 47.0 | 280.1 | |
| Automatic debt dynamics [5] | 0.6 | 0.0 | -1.9 | -2.2 | -1.6 | -1.4 | -1.3 | -1.3 | -1.2 | -8.9 | |
| Interest rate/growth differential [6] | 0.7 | 0.0 | -1.9 | -2.2 | -1.6 | -1.4 | -1.3 | -1.3 | -1.2 | -8.9 | |
| Of which: real interest rate | 1.4 | 1.2 | 0.6 | 0.1 | -0.1 | -0.3 | -0.4 | -0.3 | -0.3 | -1.3 | |
| Of which: real GDP growth | -0.7 | -1.2 | -2.4 | -2.2 | -1.5 | -1.1 | -0.9 | -0.9 | -0.9 | -7.6 | |
| Exchange rate depreciation [7] | 0.0 | 0.0 | 0.0 | ... | ... | ... | ... | ... | ... | ... | |
| Other identified debt-creating flows | 1.6 | -0.3 | -2.0 | -0.9 | -0.5 | -0.5 | -0.2 | -0.2 | 0.0 | -2.3 | |
| General government net privatization proceeds (negative) | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| Contingent liabilities | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| Stock-flow adjustment (incl. asset recovery) | 1.7 | -0.3 | -2.0 | -0.9 | -0.5 | -0.5 | -0.2 | -0.2 | 0.0 | -2.3 | |
| Residual, including asset changes [8] | -0.8 | -0.4 | -0.4 | -0.2 | -0.1 | -0.1 | -0.1 | 0.1 | -0.2 | -0.6 | |




Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as $[(r - \pi(1+g) - g + ae(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as $r - \pi (1+g)$ and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as $ae(1+r)$.

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

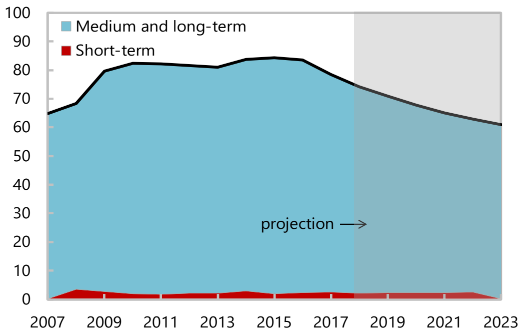
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

## Figure 4. Austria: Public DSA – Composition of Public Debt and Alternative Scenarios

### Composition of Public Debt

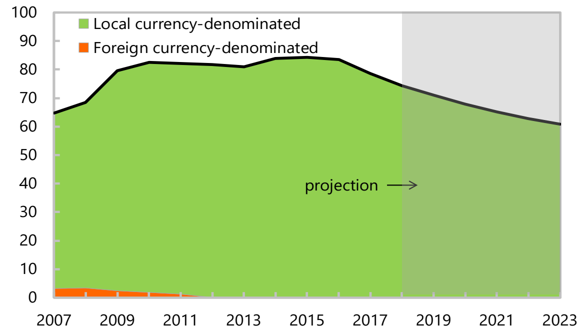
**By Original Maturity**

(in percent of GDP)




**By Currency**

(in percent of GDP)

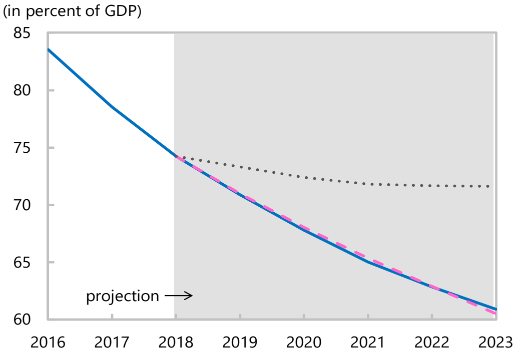



### Alternative Scenarios

Baseline    Historical    Constant Primary Balance

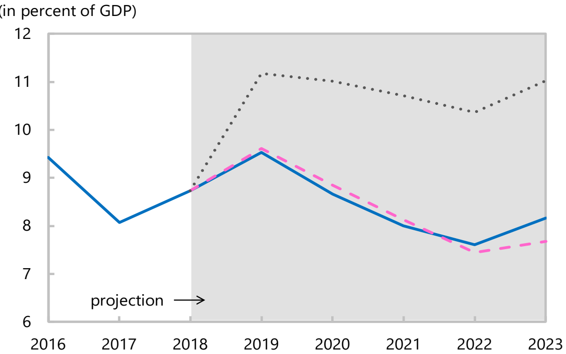
**Gross Nominal Public Debt**

(in percent of GDP)




**Public Gross Financing Needs**

(in percent of GDP)




### Underlying Assumptions

(in percent)

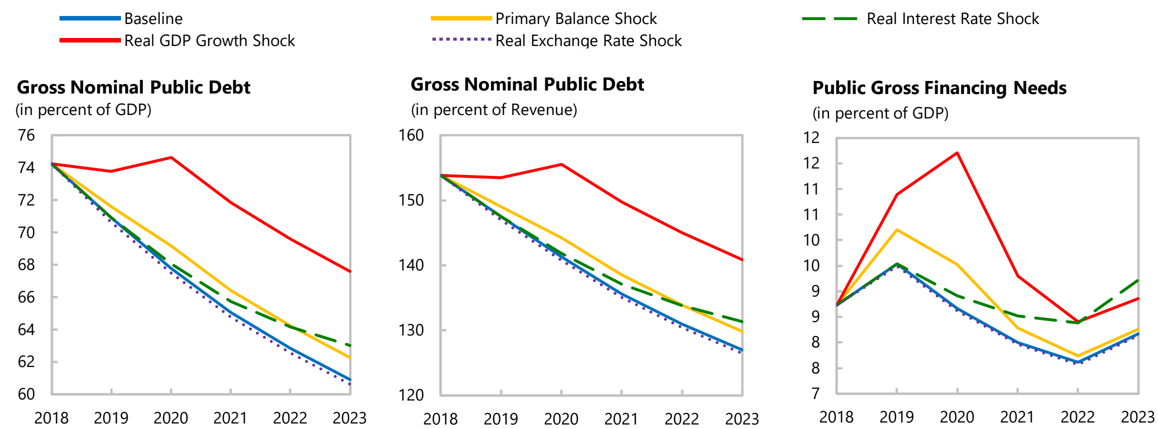
| **Baseline Scenario** | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|
| Real GDP growth | 3.0 | 2.1 | 1.5 | 1.5 | 1.4 | 1.5 |
| Inflation | 1.8 | 1.8 | 2.1 | 2.2 | 2.1 | 2.1 |
| Primary Balance | 1.0 | 1.1 | 1.2 | 1.1 | 0.8 | 0.6 |
| Effective interest rate | 1.9 | 1.7 | 1.7 | 1.6 | 1.6 | 1.7 |
| **Constant Primary Balance Scenario** | | | | | | |
| Real GDP growth | 3.0 | 2.1 | 1.5 | 1.5 | 1.4 | 1.5 |
| Inflation | 1.8 | 1.8 | 2.1 | 2.2 | 2.1 | 2.1 |
| Primary Balance | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 |
| Effective interest rate | 1.9 | 1.7 | 1.7 | 1.6 | 1.6 | 1.7 |

| **Historical Scenario** | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|
| Real GDP growth | 3.0 | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 |
| Inflation | 1.8 | 1.8 | 2.1 | 2.2 | 2.1 | 2.1 |
| Primary Balance | 1.0 | -0.4 | -0.4 | -0.4 | -0.4 | -0.4 |
| Effective interest rate | 1.9 | 1.7 | 1.9 | 2.1 | 2.3 | 2.5 |

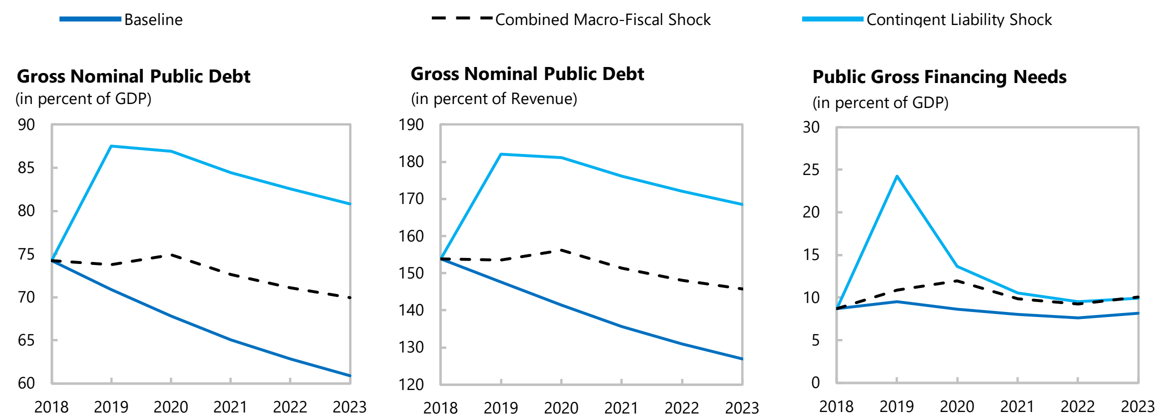
Source: IMF staff.

## Figure 5. Austria: Public DSA – Stress Tests

### Macro-Fiscal Stress Tests




### Additional Stress Tests




### Underlying Assumptions

(in percent)

| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|
| **Primary Balance Shock** | | | | | | |
| Real GDP growth | 3.0 | 2.1 | 1.5 | 1.5 | 1.4 | 1.5 |
| Inflation | 1.8 | 1.8 | 2.1 | 2.2 | 2.1 | 2.1 |
| Primary balance | 1.0 | 0.4 | 0.5 | 1.1 | 0.8 | 0.6 |
| Effective interest rate | 1.9 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 |
| **Real Interest Rate Shock** | | | | | | |
| Real GDP growth | 3.0 | 2.1 | 1.5 | 1.5 | 1.4 | 1.5 |
| Inflation | 1.8 | 1.8 | 2.1 | 2.2 | 2.1 | 2.1 |
| Primary balance | 1.0 | 1.1 | 1.2 | 1.1 | 0.8 | 0.6 |
| Effective interest rate | 1.9 | 1.7 | 2.0 | 2.3 | 2.6 | 2.9 |
| **Combined Shock** | | | | | | |
| Real GDP growth | 3.0 | 0.2 | -0.4 | 1.5 | 1.4 | 1.5 |
| Inflation | 1.8 | 1.3 | 1.6 | 2.2 | 2.1 | 2.1 |
| Primary balance | 1.0 | 0.0 | -1.1 | 1.1 | 0.8 | 0.6 |
| Effective interest rate | 1.9 | 1.7 | 2.1 | 2.4 | 2.7 | 3.0 |

| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|
| **Real GDP Growth Shock** | | | | | | |
| Real GDP growth | 3.0 | 0.2 | -0.4 | 1.5 | 1.4 | 1.5 |
| Inflation | 1.8 | 1.3 | 1.6 | 2.2 | 2.1 | 2.1 |
| Primary balance | 1.0 | 0.0 | -1.1 | 1.1 | 0.8 | 0.6 |
| Effective interest rate | 1.9 | 1.7 | 1.7 | 1.7 | 1.7 | 1.8 |
| **Real Exchange Rate Shock** | | | | | | |
| Real GDP growth | 3.0 | 2.1 | 1.5 | 1.5 | 1.4 | 1.5 |
| Inflation | 1.8 | 2.2 | 2.1 | 2.2 | 2.1 | 2.1 |
| Primary balance | 1.0 | 1.1 | 1.2 | 1.1 | 0.8 | 0.6 |
| Effective interest rate | 1.9 | 1.7 | 1.7 | 1.6 | 1.6 | 1.7 |
| **Contingent Liability Shock** | | | | | | |
| Real GDP growth | 3.0 | 0.2 | -0.4 | 1.5 | 1.4 | 1.5 |
| Inflation | 1.8 | 1.3 | 1.6 | 2.2 | 2.1 | 2.1 |
| Primary balance | 1.0 | -13.3 | 1.2 | 1.1 | 0.8 | 0.6 |
| Effective interest rate | 1.9 | 1.8 | 2.5 | 2.4 | 2.4 | 2.4 |

Source: IMF staff.

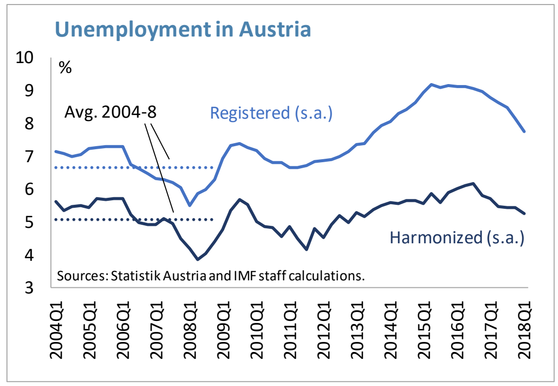
# Annex IV. Authorities' Response to Past IMF Policy Advice

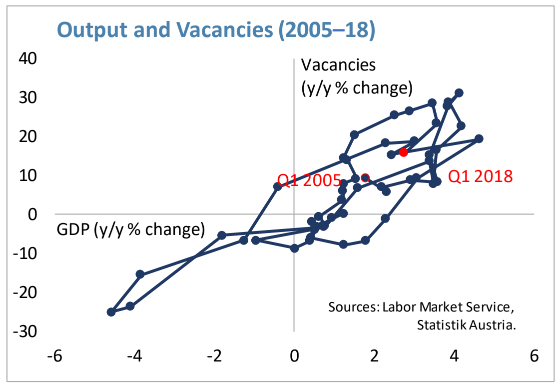
| 2016 Article IV Recommendations | Authorities' Actions |
|---|---|
| | |
| **Fiscal policy I**<br>Resume fiscal consolidation to ensure public debt remains on a declining path. | The authorities envisage a gradual consolidation to reach a structural balance of 0.5 percent of GDP by 2019, and surpluses by 2022. |
| **Fiscal policy II**<br>Broad-based expenditure reforms to realize savings while maintaining quality of public service delivery | A five-year agreement on fiscal federal relations has been reached, which includes efficiency targets and benchmarking. Discussions on further reforms are continuing. |
| **Fiscal policy III**<br>Further reduction of labor tax wedge | The tax code envisages some modest reductions in social security contributions in 2018–19. |
| **Fiscal policy IV**<br>Raise public investment | The authorities' projections imply maintaining public investment at current levels. |
| **Immigration**<br>Rapid integration of accepted asylum seekers | Several initiatives taken, including provision of language classes and a program to identify skills. However, the government is curtailing asylum seekers'—both in process and recognized—access to social benefits |
| **Structural reforms I**<br>Policies to raise TFP growth and labor force participation | A program to support start-ups financially and administratively has been put in place. Fiscal support to encourage work instead of early retirement is in place. Spending on research is being increased, and investment incentives for SMEs provided. A comprehensive overhaul of the education system is beginning to be implemented. |
| **Financial sector I**<br>Continuously assess adequacy of bank capital | The authorities are closely monitoring banks' capital cushions and capital-raising plans. |
| **Financial sector II**<br>Alternative measures to raise capital if banks' plans to raise capital ratios falter. | Not applicable, as banks' plans are still being implemented. |
| **Financial sector III**<br>Proactively mitigate risks related to Swiss franc loans | Banks have been promoting conversion of Swiss franc mortgage loans to euro-denominated loans with gradual amortization. |
| **Financial sector IV**<br>Strengthen preparedness by introducing macroprudential instruments | Legislation has been approved, and the authorities are collecting data. |
| **Financial sector V**<br>Strengthen AML/CFT framework | In progress. The authorities have developed an action plan and are preparing to implement the 5$^{th}$ EU AML Directive. |

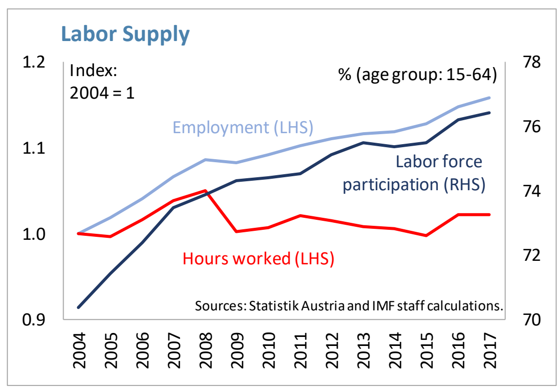
# Annex V. Unemployment and Housing Market Developments

## *Unemployment*

**1. Unemployment has recently declined but remains relatively high by Austrian standards.** While the impact of the GFC has been less severe than elsewhere in Europe, unemployment remains above pre-GFC levels, and well above the low of 2008. With the output gap nearly closed, the question arises how much further unemployment can fall sustainably.




**2. A permanent—or at least long-lasting—increase in equilibrium unemployment could occur for a number of reasons:** (i) a reduction in demand for labor due to lower potential growth or rising unit labor costs; (ii) a reduction in supply of labor but not the labor force because of a higher reservation wage; or (iii) mismatches between demand and supply, e.g., due to skills mismatches or geographical mismatches.

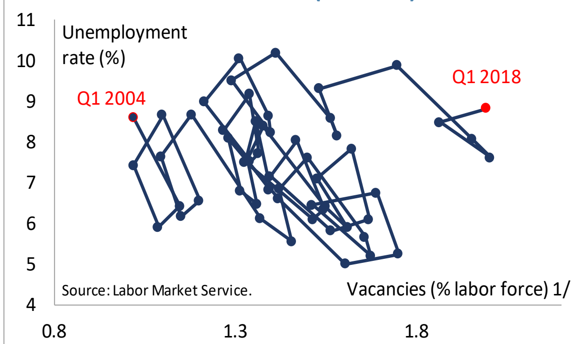
- *Demand for labor is in line with previous upswings*. Unit labor costs have risen relative to peers, implying that competitiveness has been eroded. However, the current account remains positive, and export growth has been solid, suggesting that Austria's level of competitiveness remains solid. Also, the economy is generating vacancies at a similar pace as in previous upswings.

- *Supply of labor is rising* (though hours worked are not), as labor force participation has continued to increase, and immigration continues. Participation rates of women and elderly workers have increased strongly, the latter likely due to tightened rules regarding early retirement, as well as pension reforms that require a higher number of contribution years before a full pension can be drawn. The increase in female labor force participation follows a general trend across European countries and is particularly strong in the age group of 50 to 64 years, representing a catch-up with other European countries. Immigration has also been strong, leading to an expansion of the labor force even as the native working-age population shrinks. Labor force participation has increased also among those with low education even as work has become relatively less worthwhile for them: earnings of workers in the first income quartile have declined significantly relative to unemployment benefits for those with the lowest levels of education, especially for men.[1]

3. **Mismatches have increased nonetheless,** although the labor market appears to operate well overall. They arise in mainly in skills/education and nationality.

- *Skills.* Demand for highly skilled workers is rising much faster than for those with lower skills. At the same time, the mismatch for highly skilled workers (with a university or post-secondary college degree) has remained broadly unchanged since 2007/08, but at a higher level than for other workers. This suggests that the education system is keeping up with the needs of the labor market. However, with an increasing share of highly-skilled workers in both the workforce and in vacancies, this specialization nonetheless implies that the economy-wide skills mismatch has increased relative to where it would have been without the shift to demand and supply for higher skills. At the other end of the education spectrum, both demand and supply of low-skilled workers have declined significantly, but unemployment has risen. While the mismatch has recently fallen back to pre-GFC levels, it appears that there are still too many workers with only compulsory school education.

**Labor Market Mismatch (2004–18)**

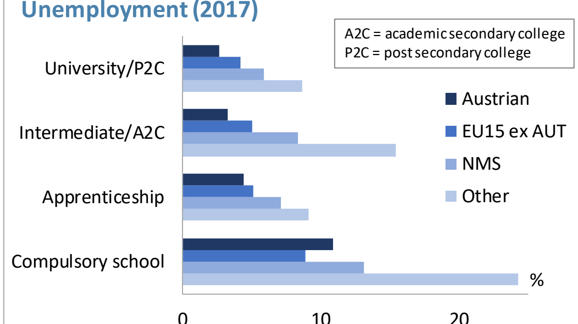



Source: Labor Market Service.

1/ Includes immediately and not immediately available vacancies.

- *Nationality.* With the removal of mobility restrictions on citizens of the EU's New Member States (NMS) in 2011, their number has increased significantly. In addition, geographic proximity (especially for Vienna, the economic hub) makes it also easy for daily or weekly commuters to work in Austria while residing in neighboring countries. At the same time, foreign nationals are much more likely to be unemployed than Austrians. Independent of the level of education, foreign nationals, in particular those from outside the EU, face a higher risk of unemployment than Austrian nationals. To some extent, this is natural: there are language barriers, there may be skills gaps (even if the formal level of education is the same), foreign nationals may have fewer informal connections. Nonetheless, even over time, the difference does not decline significantly—on the contrary, second-generation foreign nationals have the highest unemployment rate—which suggests

**Unemployment (2017)**



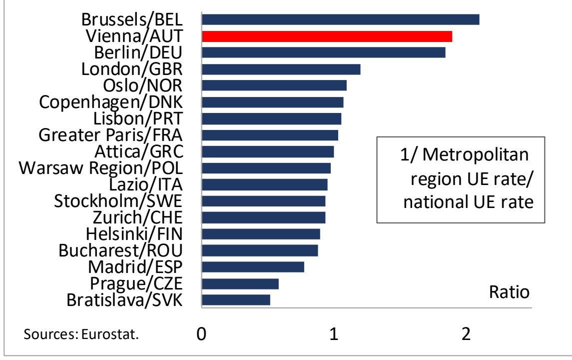

Sources: Statistik Austria and IMF staff calculations.

[1] The reason behind this is a decline in real earnings, not an increase in benefits.

that in some segments of the population, poverty and unemployment may have become entrenched.

- *Vienna*. Labor market mismatches arising from education and/or nationality background can explain some of Vienna's unemployment, which is significantly higher than elsewhere in Austria—unusual compared to other European countries. But unemployment rates in Vienna are higher across all educational levels and nationalities.

Regional Unemployment (2017) 1/



Sources: Eurostat.

### *The Housing Market*

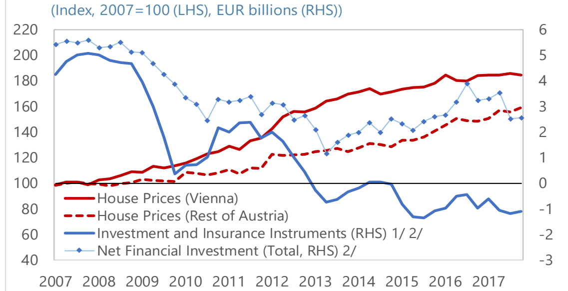
**4. The Austrian housing market has shown a strong trend rise in valuations over the last decade, mainly driven by price increases in Vienna.** Prices stagnated through the mid-2000s but have since outpaced most of Austria's EU peers. In September 2016, the ESRB issued Austria a warning on medium-term residential real estate vulnerabilities because of the robust price and credit growth and the risk of further loosening in credit standards.[2] Recently, price growth moderated to 4.7 percent (y/y) at end-2017, due to a slowdown in Vienna, though prices accelerated in the rest of the country.

Change in Real House Price Index (2007-17)
(Percent)

Sources: OECD; and IMF staff calculations.

**5. While the robust price growth has largely reflected underlying market fundamentals, the nationwide market has recently started to show signs of modest overvaluation.** Housing demand has been buoyed by demographic factors, including the spike in immigration in 2015–16, and low interest rates which also have increased the attractiveness of housing assets as a form of saving. Supply-side constraints, such as land availability, have also played a role, despite some recent pickup in construction activity. The OeNB's fundamentals indicator for residential property prices suggests a modest overvaluation of around

House Prices and Household Net Financial Investment
(Index, 2007=100 (LHS), EUR billions (RHS))



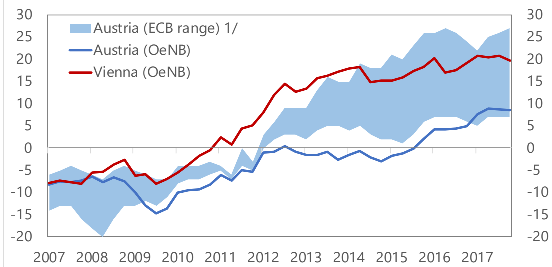
Source: OeNB, IMF Staff calculations.
1/ Total Net Financial Investment Excluding Currency and Transferable Deposits.
2/ One-year moving average.

[2] The ESRB warning was issued to seven other member states after the conclusion of a EU-wide real estate market vulnerability assessment. See ESRB Risk Dashboard, September 16 (Issue17). Indicators used for the assessment refer to the period up to 2016: Q1.

10 percent for Austria in 2017 (and a larger overvaluation for Vienna of about 20 percent), broadly corresponding to a range of ECB indicators as of end-2017.

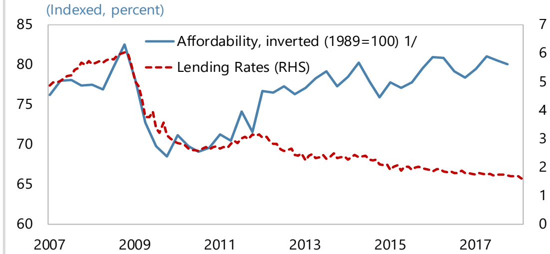
**6. Real estate related financial stability risks are nonetheless contained.** The rise in mortgage debt in Austria has been modest compared to other EU countries experiencing large property price increases, and its share relative to households' incomes has remained stable and among the lowest in the Euro Area. Residential real estate exposures account for only about a fifth of Austrian banks' total loan stock and about 150 percent of consolidated CET-1 capital. Furthermore, the prevalence of rental accommodation (about half and three-quarters of housing nationwide and in Vienna, respectively) shield a large share of the population from adverse price developments.[3] Less than half of homeowners have outstanding mortgages, and they also typically have higher incomes and net wealth relative to the rest of the population.

**Indicators of Over-/Undervaluation (2007-17)**
(Percent)




Source: OeNB; ECB; and IMF staff calculations.
1/ Average of four different valuation methods (price-to-rent ratio, price-to-income ratio, asset pricing approach and a Bayesian estimated inverted demand model).

**Affordability and Mortgage Lending Rates**
(Indexed, percent)




Source: OeNB.
1/ Ratio of hypothetical borrowing capacity, based on disposable household income and interest rate, to property prices. An increase in the inverted index indicates improved affordability.

**7. Some pockets of vulnerability and early signs of increasing risks nonetheless warrant continued close monitoring.** The share of foreign exchange denominated housing loans at around 15 percent remains high relative to Austria peers, although it has declined significantly in recent years.[4] Furthermore, the recent prolonged period of low lending rates saw a significant increase in the share of variable interest rate mortgages, which despite a recent decline still amount to about three-quarters of the total stock. There are also signs of some easing in banks' lending standards, with a rising—albeit still limited—share of relatively high loan-to-value, debt service-to-income, and debt-to-income ratios in new housing loans to households.[5]

**8. Supply side measures could help ease the modest price imbalances over time, while the recently expanded macroprudential toolkit can help prevent a build-up of systemic risks.** Measures to address supply-side constraints could include reviewing zoning regulations and other restrictions on construction. Addressing outdated property tax valuations could help improve

[3] About 57 percent of rental accommodations are publicly supported affordable housing.

[4] About three quarters of the foreign exchange loans are bullet loans linked to repayment vehicles (RPV), and thereby subject to both exchange rate and RPV performance risks. An OeNB/FMA bank survey showed that, at the end of 2016, the estimated funding shortfall of such loans amounted to about a third of the total outstanding volume.

[5] A 2014 OeNB study based on household survey data also suggests that loan-to-value ratios may be higher for households that have the highest debt service burden (nearly 90 percent among households in the 80th percentile of the DSTI ratio), increasing their vulnerability to simultaneous adverse shifts in prices and interest rates.

residential mobility and market efficiency. At the same time, the new real-estate specific macroprudential policy tools provide additional scope for tailored preventive measures to ensure systemic risks arising from the mortgage market remain contained. These are accompanied by new reporting requirements, expected to be introduced in 2019, to facilitate evaluation of risks and impact of potential policy changes. They also complement a 2016 call by the Financial Market Stability Board for the Austrian banks to maintain sustainable lending standards, although the guidance does not specify quantitative limits for the vulnerability ratios.

INTERNATIONAL MONETARY FUND

# AUSTRIA

August 23, 2018

## STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By | European Department

## CONTENTS

# FUND RELATIONS

(As of July 5, 2018)

***Mission:*** Consultation discussions were held in Vienna from June 14–25, 2018. The authorities released the mission's concluding statement, which is available at: http://www.imf.org/en/News/Articles/2018/06/25/mcs6252018-austria-staff-concluding-statement-of-the-2018-article-iv-mission

***Staff team:*** Messrs. Dorsey (head), Pitt, and Ms. Karpowicz (all EUR), and Hukka (FIN). Mr. Just (OED) participated in the discussions.

***Country interlocutors:*** Minister of Finance Loeger, OeNB Governor Nowotny and other senior officials, parliamentarians, and representatives of the social partners, the banking sector, and think tanks.

***Fund relations:*** Austria is on a 12-month consultation cycle. The last consultations were held from December 2–13, 2016 and the staff report is available at: http://www.imf.org/en/Publications/CR/Issues/2017/02/02/Austria-2016-Article-IV-Consultation-Press-Release-and-Staff-Report-for-Austria-44608

**Membership Status:** Joined: August 27, 1948; Article VIII, as of August 1, 1962

| **General Resources Account:** | **SDR Million** | **Percent Quota** |
|---|---|---|
| Quota | 3,932.00 | 100.00 |
| Fund holdings of currency | 3,608.24 | 91.77 |
| Reserve position in Fund | 323.79 | 8.23 |
| Lending to the Fund: | | |
| New Arrangements to Borrow | 192.77 | |

| **SDR Department:** | **SDR Million** | **Percent Allocation** |
|---|---|---|
| Net cumulative allocation | 1,736.31 | 100.00 |
| Holdings | 1,626.71 | 93.69 |

**Outstanding Purchases and Loans:** None

**Latest Financial Arrangements:** None

**Projected Payments to Fund:**

(SDR Million; based on existing use of resources and present holdings of SDRs):

| | Forthcoming | | | | |
|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | 2020 | 2021 |
| Principal | --- | --- | --- | --- | --- |
| Charges/Interest | 0.31 | 0.52 | 1.06 | 1.06 | 1.06 |
| Total | 0.31 | 0.52 | 1.06 | 1.06 | 1.06 |

**Implementation of HIPC Initiative:** Not Applicable

**Exchange System:**

As of January 1, 1999, the currency of Austria is the euro, which floats freely and independently against other currencies. Austria's exchange system is free of restrictions on the making of payments and transfers for current international transactions, with the exception of restrictions notified to the Fund in accordance with decision No.144-(52/51) resulting from UN Security Council Resolutions and EU Council Regulations.

# STATISTICAL ISSUES

1. **Macroeconomic statistics are adequate for surveillance.** Austria subscribed to the Fund's Special Data Dissemination Standard (SDDS) in 1996, and its metadata are available on the Fund's electronic Dissemination Standards Bulletin Board. Austria is availing itself of the SDDS flexibility option on the timeliness of the industrial production index and the merchandise trade data. Austria is currently preparing for SDDS Plus adherence.

2. **The ECB reporting framework is used for monetary statistics and data are reported to the IMF through a "gateway" arrangement with the ECB.** The arrangement provides an efficient transmission of monetary statistics to the IMF and for publication in the IFS and IFS Supplement.

| Austria: Table of Common Indicators (as of July 5, 2018) | | | | | |
|---|---|---|---|---|---|
| | Date of latest observation | Date received | Frequency of data | Frequency of reporting | Frequency of publication |
| Exchange rates | 7/5/18 | 7/5/18 | Daily | Daily | Daily |
| International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1] | May 2018 | 6/6/18 | Monthly | Monthly | Monthly |
| Reserve/Base Money | May 2018 | 6/6/18 | Monthly | Monthly | Monthly |
| Broad Money | May 2018 | 6/6/18 | Monthly | Monthly | Monthly |
| Central Bank Balance Sheet | May 2018 | 6/6/18 | Monthly | Monthly | Monthly |
| Consolidated Balance Sheet of the Banking System | May 2018 | 6/6/18 | Monthly | Monthly | Monthly |
| Interest Rates[2] | 7/5/18 | 7/5/18 | Daily | Daily | Daily |
| Consumer Price Index | May 2018 | 5/18/18 | Monthly | Monthly | Monthly |
| Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4] | 2017 | 3/27/18 | Quarterly | Quarterly | Quarterly |
| Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government | 2017 | 6/15/18 | Quarterly | Quarterly | Quarterly |
| Stocks of Central Government and Central Government-Guaranteed Debt | 2017 | 6/15/18 | Quarterly | Quarterly | Quarterly |
| External Current Account Balance | 2017 | 3/30/18 | Quarterly | Quarterly | Quarterly |
| Exports and Imports of Goods and Services | 2017 | 3/30/18 | Quarterly | Quarterly | Quarterly |
| GDP/GNP | 2018:Q1 | 3/30/18 | Quarterly | Quarterly | Quarterly |
| Gross External Debt[5] | 2017 | 3/30/18 | Quarterly | Quarterly | Quarterly |
| International Investment Position | 2017 | 3/30/18 | Quarterly | Quarterly | Quarterly |

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra-budgetary funds, and social security funds) and state and local governments).
[5] Including currency and maturity composition.

**Statement by Mr. Just, Alternate Executive Director for Austria**
**September 10, 2018**

The Austrian authorities express their appreciation to the mission team for the candid discussions. They welcome staff's excellent understanding of the EU's policy frameworks and overall awareness of Europe's fiscal, financial and supervisory policy discussions which frame the internal Austrian economic policy discourse. The Austrian authorities welcome the staff's high-quality analytical work and its succinct presentation, which may be beneficial to reach a wider audience and to stimulate public debate.

## Economic policy

The Austrian authorities concur with the main messages as well as the economic outlook presented in the staff report. GDP growth is broad-based, consumer confidence and sentiment indicators show high values and order books are well-filled. Recent indicators clearly confirm that strong growth is set to continue also in 2018. This in turn will bolster the achievement of the fiscal target in 2018. Staff forecasts a moderation of growth in 2019 which is in line with Austrian expectations of a maturing cycle. Going forward, the Austrian authorities are confident that private consumption will be supported by increased family benefits coming into effect in 2019 and therefore see the external environment posing the main risks to the outlook, in particular a further increase in protectionism, legal uncertainty stemming from unilateral sanctions against trading partners, an increase in risk averseness in the wake of emerging market jitters.

The authorities concur that supply-side measures are needed to increase potential growth. Since its inauguration on December 12, 2017, Parliament has adopted 75 laws, of which 40 are directly related to improving the supply-side of the economy. As of September 1, 2018, the daily maximum working-time was increased from 10 hours to 12 hours, with longer assessment periods for compensation. SMEs were relieved from approval procedures for production sites or retail outlets, crowdfunding has been broadened and some 2,500 outdated laws were abolished. Going forward, the economic policy priorities for the Austrian authorities are to reduce the high tax burden and to further improve the flexibility of the labor market, which will be achieved by a reform of the unemployment benefit system with the clear objective to strengthen work incentives. As mentioned in the staff report, enhancing the efficiency of the public sector is another priority and first steps are being taken to merge the many health funds in Austria.

## Fiscal policy

The authorities are committed to reduce fiscal revenues towards 40 percent of GDP, while at the same time reaching a positive structural balance in the medium term. The debt-to-GDP level stood at 78.3 percent of GDP at the end of 2017 and is on a clear declining path toward the EU-agreed 60 percent by the end of the medium-term planning horizon. The current economic environment clearly contributes to improving the budget situation, but there are also considerable additional fiscal efforts underway to reduce discretionary spending with procyclical effects.

The authorities agree with staff that the current economic environment is supportive of structural reforms that will boost growth and increase efficiency in various policy areas in the medium and longer term. Most importantly, the Austrian government has put forward a plan to reduce the number of public social security entities from 21 to 5 to save administrative costs and streamline IT-expenses. Moreover, the authorities are aware of demography-related cost pressures stemming from long-term care and are currently working across all levels of government on proposals to secure long-term financing in this policy area. In the context of subsidies, further efforts to achieve better coordination between the different levels of government will help identify savings potential and pave the way for reform options for a future reorientation of fiscal federal relations.

**Financial Sector**

Amidst a benign macroeconomic environment and historically low credit risk costs, Austrian banks recorded their highest post-crisis profits in 2017, marking a recovery to pre-crisis levels. Banks continued to benefit from their activities in Central and Eastern Europe (CESEE), where net results were high due to low provisioning needs as well as the buoyant macroeconomic development. Furthermore, Austrian banks increased their capitalization in 2017, although some momentum was lost compared to previous years due to – among other factors - an increase in dividend payments.

Despite these benign developments, the supervisors have repeatedly recommended especially to significant financial institutions to reinvigorate efforts to increase their capitalization above regulatory limits as the current buoyant economic activity in Austria and CESEE may show signs of excessive credit growth. Furthermore, banks need to improve structural efficiency to foster the sustainability of profits, as a significant part of the recent rise in profits stems from one-off factors, especially reduced risk provisioning. While initially expenses could rise as investments in IT as well as staff reductions are costly, these measures should increase efficiency and reduce the cost-income ratio in the medium term and provide banks with enough room for manoeuvre in potential future downturns.

The Austrian authorities agree with staff that real estate-related risks to financial stability are contained at present, but that caution is warranted. Currently, the authorities see limited risks arising from residential real estate lending, mainly due to the high risk-bearing capacity of both lenders and borrowers. In addition, residential real estate prices and loan growth rates have stabilized. Nonperforming loan ratios have remained low as lending standards have mostly been sustained. However, some challenges for financial stability lie ahead as the share of housing loans in banks` balance sheets is increasing. Thus, the authorities are vigilant to prevent a deterioration of lending standards. The supervisors not only monitor comprehensively lending standards but also engage in a continued dialogue with banks if mortgage lending practices appear to be riskier than deemed appropriate.

The Austrian authorities see a strong and effective Anti-Money Laundering / Combating the Financing of Terrorism (AML/CFT) framework as quintessential to safeguard Austria's role as a regional financial center. Several measures, such as increasing supervisory resources and establishing a register of beneficial ownership, have recently been taken. This resulted in an improvement in several of Austria's ratings in the 2017 follow-up report of the FATF. The implementation of the European Union's 5th AML will further improve Austria's AML/CFT framework.