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Draft Federal Budget 2007-08: Matching Consolidation With New Spending Priorities

The draft federal budget for 2007-08 represents a compromise between the conflicting challenges which fiscal policy in Austria continues to face. For the sake of greater emphasis on forward-looking priorities such as education, research, science, infrastructure and social protection, the general government deficit will be reduced more slowly than warranted by the strength of cyclical activity. The benign economic situation at the same time offers a window of opportunity for the implementation of pending reform projects in the public sector (concerning the allocation of responsibilities between different government levels, public administration and notably the budget legislation process), with the aim of gaining budgetary room for manoeuvre to reinforce spending in the new priority areas. In addition, lasting cuts in government spending should pave the way to a comprehensive reduction of the overall tax burden towards the end of the current legislation period. As a result, the government plans should allow the public claim on resources to decline, both at the federal and the general government level.

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Fiscal policy continues to be faced with conflicting challenges. On the one hand, the additional revenues and the expenditure savings resulting from the persistently strong business activity should be used to consolidate government households. The "preventive arm" of the European Stability and Growth Pact requires member states to reduce their structural government deficits by at least 0.5 percent of GDP per year in economically "good times". A pointedly expansionary stance of fiscal policy would thus be inappropriate at the current juncture. On the other hand, the Austrian situation is still characterised by certain lags in a number of areas that are crucial for future long-term growth (notably in education, research and innovation as well as infrastructure), as has been extensively highlighted by WIFO in its White Paper for Growth and Employment. Catching up on these lags requires not only structural adjustment in institutional setups, but also stronger financial involvement by public authorities.

It is against this background of cyclical conditions and the long-term growth potential that the first budget of the new federal government should be assessed, which the Minister of Finance presented at the end of March 2007 and Parliament adopted in May. As a "twin budget" it covers the years 2007 and 2008 and replaces the statutory provisional budget for 2007. The draft federal budget 2007-08 represents a compromise between the conflicting claims on fiscal policy referred to above. It combines a slower pace of consolidation than warranted by the favourable business situation with a moderate increase in expenditure in the areas of education, research, science, infrastructure and social protection.

Although the general government deficit is on a downward trend, it remains relatively high considering the strength of economic activity and is reduced in relatively small steps. At the same time, the emphasis put on forward-looking expenditure is insufficient in 2007 and 2008 and ought to be reinforced in the medium term. In order to create the necessary budgetary leeway to this end, reform efforts towards greater efficiency in public sector management should themselves be strengthened, notably the key projects of streamlining the allocation of responsibilities between different government levels, the public administration and notably the process of federal budgetary legislation (see box "reform projects for greater efficiency of public sector activities"). The benign framework conditions and the implicit economic and political opportunities offered by the current business situation should be used for the implementation of the major pending structural reforms in the public sector.

The Federal Budget – An Overview

Preliminary Budgetary Outturn for 2006

According to the preliminary outturn for 2006, revenues of the general budget amounted to € 66.1 billion and expenditure to € 70.52 billion. Thereby, the budget targets were exceeded by € 5.75 billion for revenues and by € 4.36 billion for expenditure. Instead of the targeted € 5.81 billion (2.3 percent of GDP), the federal deficit in administrative terms could be limited to € 4.42 billion or 1.7 percent of GDP. Likewise, the deficit in the Maastricht definition turned out lower at € 3.78 billion (1.5 percent of GDP) compared with a projected € 5.59 billion (2.2 percent of GDP) in the draft federal budget for 2006. The primary surplus of the federal government rose to € 3.54 billion (1.4 percent of GDP), markedly above the target of € 1.3 billion or 0.5 percent of GDP.

A large part of the excess expenditure and revenue stems from financial flows recorded in chapter 58 (financing transactions, currency swaps, i.e., the federal debt management) and essentially represents only an increase in gross flows leaving the net balance unaffected. The management of financial reserves also plays a role, with a net increase of about € 300 million. Allowing for these effects, the expenditure overrun is reduced to € 900 million and the excess revenue to € 2.3 billion.

The expenditure side reflects the impact of higher personnel outlays, including for teachers employed by the Länder, since the federal budget for 2006, due to its early drafting date, did not provide for the latest wage agreement for the public sector, an effect only partly offset by lower-than-budgeted retirement expenditure. Further increases were caused by higher interest payments and additional labour market policy measures in the context of the government's "employment campaign". A small part of the expenditure overrun could be neutralised by € 200 million or 3 percent of discretionary spending commitments being retained.

The revenue side benefited notably from the remarkably strong tax intake exceeding the budget projections by nearly € 2.1 billion in gross and € 1.6 billion in net terms. Extra revenues also originated from asset sales, public lease and corporate dividends (from ÖIAG-the public manufacturing companies holding, electricity companies and Oesterreichische Nationalbank). The cyclically-induced revenue boom has thus been the key factor for the decline in the deficit, both at the federal and the general government level.

Draft federal budget 2007

The draft federal budget 2007 provides, in its general part, for a decline in revenues by € 65.71 million (–0,6 percent) and expenditure by € 69.57 million (–1,3 percent), compared with the preliminary outturn 2006. From the draft budget 2006, expenditure is set to rise by 5.2 percent and revenue by 8.9 percent. The federal deficit, in administrative terms, is planned to narrow to € 3.86 billion (1.4 percent of GDP), in Maastricht terms to € 3.55 billion or 1.3 percent of GDP. The primary surplus is set to increase slightly to € 3.57 billion or 1.3 percent of GDP.

Draft federal budget 2008

According to the draft federal budget for 2008, revenue will increase to a total € 66.91 billion (+1.8 percent) and expenditure to € 69.87 billion (+0.4 percent). The administrative deficit is to decline further to € 2.96 billion (1.1 percent of GDP), the Maastricht-Deficit to € 3.28 billion (1.2 percent of GDP). The federal primary surplus is projected to rise to € 4.28 billion or 1.5 percent of GDP.

Austria's fiscal policy in an international context

The declared aim of the government is to achieve permanent ("structural") savings on the expenditure side, with a view not only to create fiscal leeway for reducing the deficit and for growth-enhancing investment, but also to enable comprehensive tax cuts at the end of the current legislation period. Together, these measures are intended to reduce the weight of the public sector in the economy, thereby continuing the trend of the last years (see Table 1), when both expenditure and revenue of the general government (federal, Länder and community level) declined as a share of GDP. By 2008, the expenditure ratio should edge down by 0.8 percentage point vis-à-vis 2006, to 48.3 percent of GDP, whereas the revenue ratio is planned to moderate by 0.5 percentage point to 47.4 percent of GDP. The consolidation of the general government budget, in Table 1 illustrated by the Maastricht balance, is thus brought about predominantly by expenditure-reducing measures. As shown by the trend in the tax ratio, also revenues from taxes and social security contributions are to grow less than GDP, leading to a tax burden that is 0.3 percentage point lower in 2008 than in 2006[1]. Unlike in recent years, however, the current high rate of economic growth allows the government ratios to decline even with nominal increases in budgetary resources.

Table 1: Government ratios in Austria

	2000	2001	2002	2003	2004	2005	2006	2007	2008
				As a percentage of GDP					
Expenditure ratio	51.4	50.8	50.7	51.1	50.3	49.9	49.1	48.6	48.3
Revenue ratio	49.8	50.7	50.0	49.3	49.0	48.3	47.9	47.6	47.4
Maastricht balance	– 1.5	0.0	– 0.5	– 1.6	– 1.2	– 1.5	– 1.1	– 0.9	– 0.7
Tax burden	42.9	44.8	43.8	43.2	42.9	42.1	41.8	41.6	41.5

Source: Federal Ministry of Finance, Federal Budget Law 2007-08, Background document and annexes.

Table 2: Government ratios in a European comparison

	Expenditure ratio			Revenue ratio			Tax burden		
	2000	2005	2008	2000	2005	2008	2000	2005	2008
				As a percentage of GDP					
EU 27	*.*	*46.9*	*45.7*	*.*	*44.5*	*44.7*	*40.7*	*39.6*	*40.1*
EU 15	45.0	47.2	46.1	45.9	44.9	45.2	41.2	40.0	40.7
Belgium	49.0	52.2	48.5	49.1	49.9	48.2	45.2	45.5	44.4
Germany	45.1	46.8	43.7	46.4	43.5	43.4	42.3	39.1	39.5
Greece	51.1	47.1	45.2	47.1	41.6	42.5	37.9	34.4	34.2
Spain	39.0	38.2	38.5	38.1	39.3	39.7	33.9	35.6	36.7
France	51.6	53.6	52.7	50.2	50.7	50.8	44.1	43.8	44.1
Ireland	31.6	34.4	35.5	36.2	35.5	36.4	31.7	30.8	32.3
Italy	46.2	48.2	48.3	45.3	44.0	46.1	41.8	40.6	42.9
Luxembourg	37.6	42.8	38.0	43.6	42.6	38.6	39.2	38.6	34.5
The Netherlands	44.2	45.4	46.2	46.1	45.2	46.3	39.9	38.2	39.7
Austria	51.3	49.8	47.9	49.8	48.2	47.1	42.9	42.2	41.2
Portugal	43.1	47.5	45.5	40.2	41.4	42.3	34.3	34.9	36.0
Finland	48.3	50.3	47.3	55.2	53.0	50.9	47.4	44.1	43.5
Denmark	53.5	52.6	49.6	55.8	57.2	53.1	49.4	50.3	48.1
Sweden	57.1	56.3	52.5	60.9	58.4	54.9	52.7	50.7	48.1
UK	36.8	43.7	44.3	40.7	40.6	41.9	37.5	37.2	38.5
Bulgaria	.	39.5	37.6	.	41.4	39.6	36.2	34.1	33.2
Czech Republic	41.8	44.0	43.0	38.1	40.4	39.4	33.9	36.4	34.3
Estonia	36.5	33.2	32.4	36.2	35.5	35.9	31.3	30.9	31.6
Cyprus	37.0	43.6	43.9	34.7	41.2	42.6	30.0	35.6	37.3
Latvia	37.3	35.5	36.4	34.6	35.2	36.5	29.5	29.0	29.2
Lithuania	39.1	33.6	36.0	35.9	33.1	34.9	30.2	28.9	30.6
Hungary	46.5	50.0	49.0	43.6	42.2	44.1	38.5	37.4	37.9
Malta	41.0	46.0	43.4	34.9	42.9	41.9	28.2	34.5	34.7
Poland	41.1	43.4	41.4	38.0	39.0	38.0	32.6	32.8	32.4
Romania	48.4	33.7	34.2	43.8	32.4	31.0	35.0	27.9	26.6
Slovenia	48.2	47.0	44.4	44.3	45.6	42.9	38.6	40.2	37.9
Slovakia	51.7	38.1	35.6	39.8	35.2	32.8	32.9	31.8	29.0

Source: European Commission, Spring 2007 Forecast.

This effect of growth differentials needs to be considered also when comparing government ratios across Europe (Table 2). While the ratios of government expenditure, revenue and taxes in Austria all remain above the (likewise declining) averages for both the EU 27 and the EU 15, the positive gap continues to narrow until 2008. The trend across Europe is one of marked decline, particularly in countries like the Scandinavian with high government ratios. In some countries, however, the ratios are heading up, such as in catching-up economies like Ireland or several of the new EU member states, but also in Italy and the UK. Overall, therefore, government ratios in the EU are gradually converging. Apart from Italy ratios are on a downward trend in all of Austria's neighbouring countries.

[1] The draft federal budget 2007-08 does not yet incorporate the phasing out of the inheritance tax and the gift tax. The direct impact on the overall tax ratio is only marginal, due to the small yield of these taxes. Secondary effects on the yields from other taxes may nevertheless have a small dampening impact on the tax ratio (*Berghuber – Picek – Schratzenstaller*, 2007).

Glossary of Terms

Administrative balance (net balance): revenue minus expenditure; equivalent to current net borrowing.

General household: juxtaposition of revenue and expenditure; the balance is equivalent to the administrative balance (net balance).

Balancing household: juxtaposition of revenue from newly incurred debt (administrative gross deficit) and expenditure on debt redemption; the balance is equivalent to the net balance (with reverse sign).

GDP-relevant balance: Net balance, adjusted for asset-related transactions (e.g. revenues or outlays from real estate sales or purchases) as well as increase or liquidation of reserves.

Gross tax revenue: Revenue from entirely federal or shared federal taxes before transfers to federal government funds, Länder, communities and EU.

Transitory items: Reimbursements and transfers between government institutions including corporate-like establishments; they do not affect the budget balance, as deducted from both expenditure and revenue.

Overall household: consists of general and balancing household; balance always zero, as the general household surplus/deficit is always offset by a deficit/surplus of equal size in the balancing household.

Maastricht-balance: Net balance adjusted (according to ESA 95 definitions) for items that, while associated with revenue and expenditure, do not affect the budgetary situation from the macro-economic perspective (e.g. when the origin of payments dates from an earlier or later period, or when payments correspond to claims or liabilities of the same amount); it is the reference item for the obligations deriving from the European Stability and Growth Pact.

Net tax revenue: Revenue from entirely federal or shared federal taxes (gross tax revenue) net of transfers to federal government funds, Länder, communities and EU.

Primary balance: Revenue minus expenditure net of interest payments on public debt.

Reserves: Amounts not spent during a fiscal year and therefore disposable for the following year.

Swap-transactions: "Contracts whereby the parties mutually agree to honour the obligations from equal liabilities during a certain period at the conditions defined ex-ante" (ESA '95).

Source: *Federal Ministry of Finance* (2004), *Staatsschuldenausschuss* (Public Debt Committee) (2004), *Statistics Austria* (2002).

The federal budget from 2000 to 2008

Table 3 shows the development of key features of the Austrian federal budget from 2000 to 2008. After a marked expansion between 2005 and 2006 of both revenue (from € 61.5 billion by 7.5 percent to € 66.1 billion) and expenditure (from € 66 billion by 6.8 percent to € 70.5 billion), comparatively small changes are planned for 2007 and 2008. The draft budget for 2007 foresees a slight decline in revenue and expenditure, by 0.6 percent and 1.3 percent, respectively, followed by a modest increase in revenue by 1.8 percent and expenditure by 0.4 percent in 2008. Compared with the draft budget 2006, the draft for 2007 nevertheless implies a significant rise in expenditure by 5.2 percent and revenues even by 8.9 percent[2].

In this way, plans for 2008 imply a reduction of the federal revenue ratio by 1.8 percentage points vis-à-vis 2006, to 24 percent of GDP, and of the expenditure

[2] As a consequence of the substantial increase in recorded gross flows between the draft and the final 2006 budget, already referred to above, it is deemed appropriate to compare the draft 2007 with the draft 2006 in order to abstract from the distortion largely related to federal debt management. On the other hand it seems less meaningful to use projections (notably for the Maastricht deficit) when ex-post data are already available. Moreover, using both series for a comparison would be extremely cumbersome. The present analysis therefore refers to the final figures for 2006, unless otherwise stated. Against this background, a reduction in the overall budget volume is what should a priori be expected for the draft 2007 federal budget.

ratio by 2.4 percentage points to 25.1 percent of GDP. The result is a cut in the federal deficit in administrative terms by almost € 1.5 billion between 2006 and 2008 to a total € 2.96 billion, while the Maastricht deficit is reduced by only € 0.5 billion to a nominal € 3.28 billion. The increase in *gross* tax revenues by 4.6 percent and 4.3 percent in 2007 and 2008, respectively, while lower than the +5.7 percent recorded in 2006, is still significantly above the average for the period from 2000 to 2008 of 3.4 percent. The growth of *net* tax revenues of the federal government[3] of 4.3 percent for each year is closer to the longer-term average of 3.7 percent.

Reform Projects for Greater Efficiency of Public Sector Activities

The federal government has declared reforms to modernise the public sector with a view to enhance effectiveness and efficiency of government action to be key elements of its programme (*Federal Ministry of Finance,* 2007A). It thereby follows up on several initiatives kicked off or implemented during the last years (Austrian Convent, administrative reform packages I and II, four-party agreement on reform of budgetary legislation) to carry them further in the current legislation period. The major components of these structural reforms designed to achieve greater efficiency in the allocation of government resources are a constitutional and administrative reform as well as a reform of budgetary legislation.

Constitutional and administrative reform

A commission of six experts has been entrusted to elaborate proposals in several stages for constitutional and administrative reform. In a first step, proposals for a reform of the electoral system have been submitted which meanwhile have been put into practice. Measures for a reorganisation of school administration and of administrative jurisdiction may be expected shortly. For the autumn of 2007, a set of measures for a re-allocation of government responsibilities between the territorial authorities has been announced.

Reform of budgetary legislation

The plans for a reform of federal budgetary legislation consist of two stages:

The first stage implies essentially the introduction of a medium-term budgetary framework covering the next four years with an annual update rolled over. federal expenditure will be regrouped into five categories: research and education; social affairs, health and labour; security and legal affairs; economy and infrastructure; interest payments. With the exception of selected cyclically-sensitive spending categories (intra-governmental financial redistribution, statutory retirement and unemployment insurance) that are subject to variable ceilings, binding ceilings will be defined for all other expenditures. Flexibility for the use of funds will be enhanced by the possibility of transferring resources to the subsequent fiscal year. Implementation of the first reform stage, originally foreseen for 2007, is now envisaged for 2009.

The second stage consists of the introduction of a performance-oriented budgeting approach as from 2013 (originally targeted for 2011). The allocation of resources within the framework of global budget, will be linked directly to clearly defined services to be produced. The impact orientation also includes the aspect of gender equality through the activities of the public sector ("gender budgeting"). First steps towards gender budgeting have been taken as from the draft budget 2005, with an analysis of a selected budget item from a gender perspective in each government department. Although this approach is carried further in the draft budget 2007-08 in the context of the explanatory notes (*Federal Ministry of Finance,* 2007B), the analysis generally does not dig very deep. In the preparations for the implementation of the impact-oriented budgeting, to take place between 2009 and the actual introduction in 2013, due attention ought to be given to the gender budgeting aspect as an integral part of the new approach.

No substantial savings should be expected in the short run from the implementation of these reform projects. In the longer term, however, they may contribute importantly towards raising the quality of public finances, also facilitating savings in expenditure. In this regard it will be paramount to avoid a narrow focus on single measures in isolation, notably in the context of the constitutional and administrative reform. What is required is rather a comprehensive approach, starting from a fundamental re-assessment on the role of government and the allocation of tasks to the different territorial levels (federal, Länder and local). Nor should a discussion of the fiscal relations between the different government levels be excluded, as it currently appears to be the case. Indeed, possible options should be explored for disentangling inter-governmental transfers and for strengthening the tax autonomy at the sub-national level. Even if a number of crucial issues still need to be clarified in detail (see *Schratzenstaller,* 2006), the reform of federal budgetary legislation should now be implemented without delay. It would be desirable also to extend such reform to the other territorial authorities, notably the Länder.

Federal expenditure adjusted for transitory items are planned at € 68.84 billion for 2007, down by 0.9 percent from last year, before rising by 0.7 percent to a total

[3] In order to derive net tax revenues, the revenue shares of the other territorial authorities and transfers to off-budget funds (e.g., the family burden-sharing fund) as well as to the European Union are deducted from gross tax revenues.

€ 69.31 billion in 2008 (Table 4). The adjusted revenues edge down by 0.1 percent from last year in 2007 to € 64.98 billion, rebounding by 2.1 percent to € 66.35 billion in 2008.

Table 3: The Federal budget – an overview

	2000	2005	2006	2006	2007	2008	2005-06	2006-07	2007-08	2000-2008
	Outturn		Draft budget	Preliminary outturn	Draft budget			Change		Change p.a.
	Million €						In percent			
Revenue	55,393	61,493	60,351	66,103	65,712	66,909	+ 7.5	– 0.6	+ 1.8	+ 2.4
Expenditure	58,247	66,041	66,161	70,519	69,574	69,869	+ 6.8	– 1.3	+ 0.4	+ 2.3
Administrative balance	– 2,853	– 4,548	– 5,810	– 4,416	– 3,862	– 2,960				
Maastricht balance	– 3,365	– 4,480	– 5,587	– 3,783	– 3,553	– 3,283				
Tax revenues gross	50,387	57,156	58,316	60,398	63,183	65,880	+ 5.7	+ 4.6	+ 4.3	+ 3.4
Tax revenues net	33,041	38,038	38,902	40,454	42,205	44,039	+ 6.4	+ 4.3	+ 4.3	+ 3.7
	As a percentage of GDP									
Revenue	26.3	25.1	23.7	25.8	24.5	24.0				
Expenditure	27.7	26.9	26.0	27.5	26.0	25.1				
Administrative balance	– 1.4	– 1.9	– 2.3	– 1.7	– 1.4	– 1.1				
Maastricht balance	– 1.6	– 1.8	– 2.2	– 1.5	– 1.3	– 1.2				
Tax revenues gross	23.9	23.3	22.9	23.6	23.5	23.5				
Tax revenues net	15.7	15.5	15.3	15.8	15.7	15.7				

Source: Federal Ministry of Finance.

Table 4: Federal expenditure and revenue, adjusted

	2000	2005	2006	2006	2007	2008
	Outturn		Draft budget	Preliminary outturn	Draft budget	
	Million €					
Expenditure general budget	58,247	66,041	66,172	70,519	69,574	69,869
– Transitory items	– 978	– 846	– 949	– 1,070	– 736	– 564
Expenditure, adjusted	57,269	65,195	65,223	69,449	68,838	69,305
Revenue general budget	55,393	61,493	60,360	66,103	65,712	66,909
– Transitory items	– 978	– 846	– 949	– 1,070	– 736	– 564
Revenue, adjusted	54,416	60,646	59,411	65,032	64,976	66,346
Administrative balance	– 2,853	– 4,548	– 5,812	– 4,416	– 3,862	– 2,960

Source: Federal Ministry of Finance, WIFO calculations.

The primary balance, i.e., the nominal balance in each period adjusted for interest payments, is (together with GDP growth and the level of interest rates) the crucial variable for the development of the debt ratio and thus an indicator of the sustainability of fiscal policy (Table 5). The primary surplus, at € 3.57 billion or 1.3 percent of GDP in 2007, is set to remain close to the year-earlier level (€ 3.54 billion or 1.4 percent of GDP) and rise to € 4.28 billion or 1.5 percent of GDP in 2008. The falling trend observed between 2001 and 2004 has thereby been reversed since 2005. The government debt-to-GDP ratio has been steadily falling from 65.5 percent in 2000 to a projected 59.2 percent by 2008.

Debt service payments are set to decline from € 7.95 billion in 2006 to € 7.43 billion in 2007 and eventually to € 7.24 billion in 2008 (Table 5). Notably for 2008, the figure is subject to some uncertainty on account of interest rate developments, although federal interest payments are rather inelastic with regard to short-term interest variations, due to the very high share of fixed-interest-rate debt. Lower interest payments and the planned significant increase in the liquidation of reserves will contribute towards a decline in the administrative deficit in 2007 and 2008, although the GDP-relevant deficit – an indicator of the impact of the federal deficit on aggregate demand – will even edge up slightly, from nearly € 4 billion in 2006 to € 4.24 billion in 2007. In 2008, the GDP-relevant deficit is expected to narrow to € 3.24 billion.

Table 5: The administrative federal budget balance by components

	2000	2005	2006	2006	2007	2008
	Outturn		Draft budget	Preliminary outturn	Draft budget	
	Million €					
Balance of current transactions	+ 3,610	+ 1,481	+ 358	+ 2,214	+ 1,627	+ 2,807
Investment and real estate acquisitions	+ 11	– 164	– 142	– 42	– 104	– 107
Capital transfers, net	– 5,669	– 5,758	– 6,057	– 6,151	– 5,759	– 5,943
GDP-relevant balance	– 2,048	– 4,440	– 5,842	– 3,979	– 4,235	– 3,244
Balance of asset transactions	– 525	+ 171	– 84	– 144	– 173	– 197
Change in reserves, net	– 280	– 279	+ 114	– 294	+ 547	+ 481
Administrative balance	– 2,853	– 4,548	– 5,812	– 4,416	– 3,862	– 2,960
Interest(net of currency swaps)	+ 7,938	+ 7,592	+ 7,109	+ 7,952	+ 7,429	+ 7,243
Primary balance	+ 5,085	+ 3,044	+ 1,297	+ 3,536	+ 3,567	+ 4,283

Source: Federal Ministry of Finance, WIFO calculations.

Because of the requirements of the European Stability and Growth Pact, the general government balance in the Maastricht definition is of particular relevance (Table 6). According to the latest update of the Austrian Stability Programme of March 2007, the Länder and local communities are supposed to achieve on aggregate a surplus of 0.4 percent of GDP in 2007 and of 0.5 percent of GDP in 2008. At the same time, the social security finances are expected to be in balance, unlike in the last few years. The achievement of these targets will likely be facilitated on the one hand by the cyclical upturn and, on the other, by the increase in health insurance contributions by 0.15 percentage point announced in the government programme and probably taking effect in 2008.

Table 6: General government balance in the Maastricht definition

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
	As a percentage of GDP										
Government authority											
General government	– 1.47	+ 0.04	– 0.49	– 1.62	– 1.20	– 1.58	– 1.12	– 0.9	– 0.7	– 0.2	+ 0.4
Federal government	– 1.60	– 0.67	– 1.07	– 1.87	– 1.40	– 1.83	– 1.48	– 1.3	– 1.2	– 0.7	– 0.1
Länder (excluding Vienna)	+ 0.20	+ 0.46	+ 0.35	+ 0.16	+ 0.14	+ 0.11	+ 0.25	+ 0.2	+ 0.3	+ 0.3	+ 0.3
Municipalities (including Vienna))	+ 0.04	+ 0.26	+ 0.25	+ 0.17	+ 0.16	+ 0.20	+ 0.15	+ 0.2	+ 0.2	+ 0.2	+ 0.2
Länder and municipalities	+ 0.24	+ 0.72	+ 0.60	+ 0.33	+ 0.30	+ 0.31	+ 0.40	+ 0.4	+ 0.5	+ 0.5	+ 0.5
Social security bodies	– 0.11	– 0.00	– 0.01	– 0.08	– 0.09	– 0.06	– 0.04	± 0.0	± 0.0	± 0.0	± 0.0

Source: Statistics Austria, Federal Ministry of Finance. As from 2007 according to the Austrian Stability Programme 2006 to 2010. + . . . surplus, –. . . deficit.

According to the updated Stability Programme, the general government deficit shall be cut to 0.9 percent and 0.7 percent of GDP in 2007 and 2008, respectively, with the federal government running deficits of 1.3 percent (2007) and 1.2 percent of GDP (2008) and Länder and communities in overall surplus as referred to above. Given the latest upward revision of the projection for nominal GDP growth and the high tax intake during the early months of 2007, these targets are likely to be slightly exceeded. In its short-term projections of June 2007, WIFO expects a general government deficit on Maastricht definitions of 0.7 percent of GDP for 2007 and 0.6 percent for 2008. For 2009, the Stability Programme cites a planned deficit of 0.2 percent of GDP and for 2010 a surplus equivalent to 0.4 percent of GDP. From today's perspective, these targets appear ambitious, but they should be achieved if the public sector reforms referred to earlier are implemented rigorously.

According to the economic forecast by the European Commission of last spring, the Maastricht deficit projected for Austria[4] of 0.8 percent of GDP for 2008 is somewhat

[4] The international comparison in this context has been based upon the spring 2007 forecast by the European Commission. For this reason, the Austrian deficit according to Maastricht definitions is reported higher in the present instance than elsewhere throughout this article.

below the EU average. However, in cyclical boom periods governments should strive for significant budgetary surpluses, as demonstrated by the Scandinavian countries. Nevertheless, Austria should be able to reduce the stock of government debt to 59.2 percent of GDP by 2008, slightly below the average for the EU 15 of 59.9 percent of GDP. While over the same period some other smaller countries like Finland or the Netherlands consolidate their budgets more forcefully, larger countries such as Germany and the UK increased their debt levels due to a cyclical downturn or to structural weaknesses, as notably in the case of Germany.

Table 7: Maastricht budget balances and debt levels of EU member states

	Maastricht balance			Gross debt		
	2000	2005	2008	2000	2005	2008
	As a percentage of GDP					
EU 27	*+ 0.7*	*– 2.4*	*– 1.0*	*61.8*	*62.9*	*58.4*
EU 15	+ 0.9	– 2.3	– 0.9	63.1	64.4	59.9
Belgium	+ 0.1	– 2.3	– 0.2	107.7	93.2	82.6
Germany	+ 1.3	– 3.2	– 0.3	59.7	67.9	63.6
Greece	– 4.0	– 5.5	– 2.7	110.2	107.5	97.6
Spain	– 0.9	+ 1.1	+ 1.2	59.2	43.2	34.6
France	– 1.5	– 3.0	– 1.9	56.7	66.2	61.9
Ireland	+ 4.6	+ 1.0	+ 1.0	37.8	27.4	21.7
Italy	– 0.8	– 4.2	– 2.2	109.1	106.2	103.1
Luxembourg	+ 6.0	– 0.3	+ 0.6	6.4	6.1	6.1
The Netherlands	+ 2.0	– 0.3	+ 0.0	53.8	52.7	45.9
Austria	– 1.5	– 1.6	– 0.8	65.5	63.5	59.2
Portugal	– 2.9	– 6.1	– 3.2	50.4	63.5	65.8
Finland	+ 6.9	+ 2.7	+ 3.6	43.8	41.4	35.2
Denmark	+ 2.3	+ 4.7	+ 3.6	51.6	36.3	20.0
Sweden	+ 3.8	+ 2.1	+ 2.4	50.0	51.6	38.6
UK	+ 4.0	– 3.1	– 2.4	40.2	42.1	45.2
Bulgaria	– 0.5	+ 1.9	+ 2.0	73.7	29.2	18.9
Czech Republic	– 3.7	– 3.5	– 3.6	18.9	31.3	31.9
Estonia	– 0.2	+ 2.3	+ 3.5	4.9	4.5	2.3
Cyprus	– 2.3	– 2.3	– 1.4	58.5	69.7	54.8
Latvia	– 2.8	– 0.2	+ 0.1	11.8	12.3	6.5
Lithuania	– 3.2	– 0.5	– 1.0	23.5	18.4	19.8
Hungary	– 2.9	– 7.8	– 4.9	53.2	60.5	71.5
Malta	– 6.2	– 3.1	– 1.6	54.5	73.4	64.6
Poland	– 3.0	– 4.3	– 3.3	37.4	49.1	49.9
Romania	– 4.6	– 1.4	– 3.2	19.8	15.6	13.6
Slovenia	– 3.9	– 1.5	– 1.5	26.9	28.2	27.3
Slovakia	– 11.8	– 2.8	– 2.8	48.9	35.2	31.8

Source: European Commission, Spring 2007 Forecast.

Trends in the composition of expenditure

General tendencies

The composition of federal expenditure by economic categories has changed somewhat since the year 2000 (Table 8). In a longer-term perspective, transfer expenditure are posting above-average gains, rising by 3.5 percent p.a. since the beginning of the decade. Whereas in 2000 transfers accounted for 35.6 percent of federal government spending, their share is expected to reach 38.6 percent by 2008.

Within the category of federal government transfers, family-related outlays have risen fastest at 5 percent per year since 2000 (Table 9), due to the repeated increase of existing benefits and the introduction of new ones. Additional measures are foreseen also by the draft federal budget for 2007-08. Thus, the monthly assessment base for the level of child-raising allowances in the retirement insurance will be raised in 2007 retroactively as from 2006; and in 2008, the supplement for the third child to the family benefit will be increased. The flexibility introduced for the child-care benefit and the increase in the ceiling for the means test applied to this benefit will further add to expenditure. Nevertheless, the increase in family-related spending will decelerate due to the moderate rise in the standard family benefit. The fund for the compensation of family-related financial burdens ("*Familienlastenausgleichsfonds*") is projected to remain in deficit in 2007 and 2008, albeit narrowing over time. While the negative gap reached a peak of € 674 million in 2005, it diminished to € 466 million in 2006 and is set to abate further to € 419 million in 2007 and € 369 million in 2008.

Table 8: Federal government expenditure by economic category, adjusted

	2000	2005	2006	2006	2007	2008	2005-06	2006-07	2007-08	2000-2008
	Outturn		Draft budget	Preliminary outturn	Draft budget			Change		Change p.a.
	Million €						In percent			
Goods and services	16,151	15,380	15,762	16,092	16,998	17,081	+ 4.6	+ 5.6	+ 0.5	+ 0.7
Transfers	20,384	24,912	25,660	25,698	26,214	26,758	+ 3.2	+ 2.0	+ 2.1	+ 3.5
Financing	20,734	24,903	23,800	27,658	25,625	25,466	+ 11.1	− 7.4	− 0.6	+ 2.6
Total	57,269	65,195	65,223	69,449	68,838	69,305	+ 6.5	− 0.9	+ 0.7	+ 2.4
	Percentage shares									
Goods and services	28.2	23.6	24.2	23.2	24.7	24.6				
Transfers	35.6	38.2	39.3	37.0	38.1	38.6				
Financing	36.2	38.2	36.5	39.8	37.2	36.7				
Total	100.0	100.0	100.0	100.0	100.0	100.0				

Source: Federal Ministry of Finance, WIFO calculations.

Table 9: Federal government expenditure on transfers

	2000	2005	2006	2006	2007	2008	2005-06	2006-07	2007-08	2000-2008
	Outturn		Draft budget	Preliminary outturn	Draft budget			Change		Change p.a.
	Million €						In percent			
Retirement insurance	11,901	14,473	15,026	15,121	15,354	15,688	+ 4.5	+ 1.5	+ 2.2	+ 3.5
Federal civil servants	2,525	3,066	3,327	3,229	3,268	3,337	+ 5.3	+ 1.2	+ 2.1	+ 3.5
Reimbursement state teachers	697	931	975	949	958	971	+ 2.0	+ 1.0	+ 1.3	+ 4.2
Postal employees	846	1,124	1,159	1,131	1,135	1,144	+ 0.6	+ 0.4	+ 0.8	+ 3.8
Railway employees	1,695	1,762	1,830	1,742	1,837	1,892	− 1.1	+ 5.4	+ 3.0	+ 1.4
Subsidies to social retirement insurance[1]	6,139	7,590	7,735	8,069	8,156	8,344	+ 6.3	+ 1.1	+ 2.3	+ 3.9
Family support	3,296	4,572	4,528	4,653	4,748	4,855	+ 1.8	+ 2.0	+ 2.2	+ 5.0
Family allowances[2]	2,798	3,021	3,014	3,025	3,041	3,078	+ 0.1	+ 0.5	+ 1.2	+ 1.2
Maternity and child care	421	1,059	1,020	1,191	1,189	1,248	+ 12.5	− 0.2	+ 5.0	+ 14.5
Pension contributions for child care periods	77	492	494	437	518	529	− 11.3	+ 18.7	+ 2.1	+ 27.2
Unemployment benefits	1,859	2,327	2,568	2,328	2,243	2,174	+ 0.1	− 3.7	− 3.1	+ 2.0
Nursing care benefit	1,264	1,421	1,404	1,474	1,533	1,595	+ 3.7	+ 4.0	+ 4.0	+ 2.9
Other	2,063	2,120	2,135	2,123	2,336	2,446	+ 0.1	+ 10.0	+ 4.7	+ 2.2
Total	20,384	24,912	25,660	25,698	26,214	26,758	+ 3.2	+ 2.0	+ 2.1	+ 3.5
	Percentage shares									
Retirement insurance	58.4	58.1	58.6	58.8	58.6	58.6				
Family support	16.2	18.4	17.6	18.1	18.1	18.1				
Unemployment benefits	9.1	9.3	10.0	9.1	8.6	8.1				
Nursing care benefit	6.2	5.7	5.5	5.7	5.8	6.0				
Other	10.1	8.5	8.3	8.3	8.9	9.1				
Total	100.0	100.0	100.0	100.0	100.0	100.0				

Source: Federal Ministry of Finance, WIFO calculations. – [1] including minimum pensions and transfers to the retirement insurers balancing fund. – [2] including child birth and school travel subsidies.

The increase in old-age-related expenditure as well as for unemployment compensation will also slow down. The latter are even foreseen to decline overall according to the 2007-08 budget, with outlays for active labour market policy (primarily vocational education and training, job search, structural adjustment measures as well as wage supplements to facilitate the insertion into the regular job market) to remain constant. Spending on nursing care is likely to rise by 4 percent per year, faster than in the last years because of the ageing of the population.

Thus, the composition of federal transfer spending changes gradually between 2000 and 2008. The share of family-related expenditure is increasing, and also that of nursing care after a fall up to the middle of the decade. The proportion of federal spending on old-age insurance remains high at almost 59 percent.

Federal government retirement expenditure has been rising at 3.5 percent per year in gross terms since 2000. Subsidies to the social old-age insurance have posted above-average increases, at 6.1 percent p.a., as well as the refunds for retirement benefits of teachers employed by the Länder (+4.2 percent p.a.) and the benefits of retired postal workers (+3.8 percent p.a.). Over the same period, federal revenues related to retirement edged up by only 0.6 percent on annual average, such that federal retirement expenditure in net terms went up by 3.9 percent per year.

Table 10: Federal government retirement expenditure

	2000	2005	2006	2006	2007	2008	2005-06	2006-07	2007-08	2000-2008
	Outturn		Draft budget	Prelimi-nary outturn	Draft budget			Change		Change p.a.
			Million €					In percent		
Federal civil servants	2,525	3,066	3,327	3,229	3,268	3,337	+ 5.3	+ 1.2	+ 2.1	+ 3.5
Reimbursement state teachers	697	931	975	949	958	971	+ 2.0	+ 1.0	+ 1.3	+ 4.2
Postal employees	846	1,124	1,159	1,131	1,135	1,144	+ 0.6	+ 0.4	+ 0.8	+ 3.8
Railway employees	1,695	1,762	1,830	1,742	1,837	1,892	– 1.1	+ 5.4	+ 3.0	+ 1.4
Subsidies to social retirement insurance	4,152	6,060	6,187	6,439	6,467	6,673	+ 6.3	+ 0.4	+ 3.2	+ 6.1
Minimum pensions	741	822	841	857	941	952	+ 4.2	+ 9.8	+ 1.2	+ 3.2
Transfers to retirement insurers balancing fund	1,246	708	707	773	748	720	+ 9.2	– 3.2	– 3.9	– 6.6
Total expenditure	11,901	14,473	15,026	15,121	15,354	15,688	+ 4.5	+ 1.5	+ 2.2	+ 3.5
Contributions from federal civil servants	561	544	566	560	558	563	+ 2.8	– 0.3	+ 0.8	+ 0.0
Contributions Art. 13 Pension Act	47	123	132	124	125	126	+ 1.3	+ 0.7	+ 0.7	+ 13.1
Contributions from state teachers	14	36	35	36	38	40	+ 2.1	+ 4.5	+ 4.5	+ 14.2
Contributions postal employees	273	198	185	193	185	176	– 2.5	– 4.6	– 4.6	– 5.3
Contributions railway employees	435	350	388	344	374	376	– 1.7	+ 8.6	+ 0.5	– 1.8
Supplementary contributions railway	50	82	66	91	64	65	+ 11.5	– 29.5	+ 1.2	+ 3.4
other revenue	46	243	145	137	133	130	– 43.7	– 2.5	– 2.4	+ 13.9
Total revenue	1,412	1,576	1,516	1,486	1,477	1,476	– 5.7	– 0.6	– 0.1	+ 0.6
Net expenditure on retirement benefits	10,490	12,897	13,509	13,635	13,877	14,212	+ 5.7	+ 1.8	+ 2.4	+ 3.9

Source: Federal Ministry of Finance, WIFO calculations.

Financing outlays by the federal government are rising by 2.6 percent per year between 2000 and 2008, somewhat faster than federal expenditure overall. Within this category, only transfers to public-sector institutions and to companies exhibit sustained above-average growth and thus an increase in their relative share. This tendency, a consequence of the outsourcing strategy at the federal level, raises the urgency of introducing greater transparency into the financing relations between the federal government and off-budget entities by means of regular reporting ("report on outsourcing") on these entities as to their levels of employment, investment, indebtedness, etc.

After an increase in the share of financing outlays in total federal expenditure to almost 40 percent in 2006, a marked decline is foreseen for 2007 and 2008, to 36.7 percent in the latter year. It is largely driven by the expected reduction in debt interest payments and by the fact that the draft federal budget 2007-08 provides for hardly any addition to financial reserves.

In a longer-term perspective, federal government expenditure for the production of public goods and services is losing importance, mainly because of the relative decline in personnel outlays, the largest item in this category. The latter, after sluggish gains in the first half of the decade, nevertheless rebounded strongly in 2006, rising by 4.1 percent from the previous year; more moderate advances are foreseen in the 2007-08 budget[5].

[5] No budgetary provisions have been made for the 2008 wage round.

Table 11: Federal government expenditure for financing purposes

	2000	2005	2006	2006	2007	2008	2005-06	2006-07	2007-08	2000-2008
	Outturn		Draft budget	Prelimi-nary outturn	Draft budget			Change		Change p.a.
	Million €						In percent			
Interest on financial debt[1]	8,773	9,231	9,283	10,897	10,006	9,688	+ 18.1	– 8.2	– 3.2	+ 1.2
Transfers to public authorities	6,503	10,305	9,690	10,283	10,437	10,642	– 0.2	+ 1.5	+ 2.0	+ 6.3
Global amount on universities	.	1,751	1,725	1,779	2,144	2,162	+ 1.6	+ 20.5	+ 0.9	.
Other	6,503	7,753	7,965	8,504	8,293	8,479	+ 9.7	– 2.5	+ 2.2	+ 3.4
Transfers to enterprises	2,277	3,149	3,811	3,932	3,908	3,966	+ 24.9	– 0.6	+ 1.5	+ 7.2
Cost of money transfers, exchange rate losses and reimbursements	652	356	91	552	243	115	+ 55.4	– 56.1	– 52.8	– 19.5
Loans, acquisition of stakes	683	175	131	209	194	219	+ 19.4	– 6.9	+ 12.7	– 13.3
Transfers to reserves	1,209	972	5	1,078	13	9	+ 10.9	– 98.8	– 28.4	– 45.6
Other	638	716	789	707	824	827	– 1.2	+ 16.4	+ 0.4	+ 3.3
Total	20,734	24,903	23,800	27,658	25,625	25,466	+ 11.1	– 7.4	– 0.6	+ 2.6

Source: Federal Ministry of Finance, WIFO calculations. – [1] including currency swaps.

Table 12: Federal government expenditure for the production of goods and services

	2000	2005	2006	2006	2007	2008	2005-06	2006-07	2007-08	2000-2008
	Outturn		Draft budget	Prelimi-nary outturn	Draft budget			Change		Change p.a.
	Million €						In percent			
Personnel outlays	10,896	10,604	10,402	10,948	11,275	11,352	+ 3.2	+ 3.0	+ 0.7	+ 0.5
Federal employees	6,947	6,878	6,856	7,163	7,355	7,381	+ 4.1	+ 2.7	+ 0.4	+ 0.8
Compensation for states teachers	2,802	2,947	2,712	2,985	3,114	3,176	+ 1.3	+ 4.3	+ 2.0	+ 1.6
Postal service	1,148	779	834	800	806	796	+ 2.8	+ 0.8	– 1.4	– 4.5
Current material expenditure	4,673	4,505	5,189	4,924	5,519	5,551	+ 9.3	+ 12.1	+ 0.6	+ 2.2
Investment	528	182	162	144	202	175	– 21.0	+ 40.4	– 13.1	– 12.9
Acquisition of real estate and other claims	54	89	9	76	2	2	– 14.5	– 97.1	+ 0.9	– 33.0
Total	16,151	15,380	15,762	16,092	16,998	17,081	+ 4.6	+ 5.6	+ 0.5	+ 0.7

Source: Federal Ministry of Finance, WIFO calculations.

Expenditure priorities

On the expenditure side, special emphasis has been given to education, research, infrastructure and family-related spending, items considered crucial in the theoretical and empirical literature for the promotion of growth and employment (*Schratzenstaller,* 2007A) which have been given priority by Austrian fiscal policy already in the past years (Table 13; *Federal Ministry of Finance,* 2007A). In all these categories, federal expenditure have been rising above-average over the period from 2000 to 2008.

The strongest increase is observed for federal government outlays for research between 2000 and 2007 and in particular since 2005 (by 8.2 percent per year). As a consequence, their share is following an upward trend, both as percent of total expenditure and of GDP. The funds already allocated in the context of the government's previous "research campaigns" will be reinforced by an additional € 40 million in 2007 and € 80 million in 2008.

The relatively slowest trend increase is recorded for expenditure on education which gained 2.5 percent on annual average. Its share in total federal government expenditure thereby remained constant over the years and fell somewhat in relation to GDP. Growth rates foreseen for 2007 and 2008 in this category are primarily due to the cost implied by the lowering of the pupil/teacher ratio to be implemented in the early grades of compulsory schooling.

Expenditure on infrastructure will increase by an average 3.8 percent p.a. from 2000 until 2008. The jump recorded for 2007 is largely due to the purchase of Eurofighter aircrafts (€ 467 million), as is the subsequent fall in 2008 (with a budgeted outlay for Eurofighter planes of € 250 million). Adjusted for this item, infrastructure spending will be increased by nearly 10 percent in 2007, levelling off in 2008. The longer-term perspective shows an above-average increase, where the share of infrastructure (excluding the Eurofighter purchase) rises as percent of total federal government expenditure between 2000 and 2008, but remains constant in relation to GDP.

Table 13: Priorities for growth in the federal government budget

	2000	2001	2002	2003	2004	2005	2006	2006	2007	2008	2000-2008
	Outturn						Draft budget	Preliminary outturn	Draft budget		Change p.a.
Education (excluding science)											
Million €	5,533	5,733	5,769	5,870	5,902	6,187	6,012	6,401	6,634	6,730	
Change from previous year in percent		+ 3.6	+ 0.6	+ 1.8	+ 0.5	+ 4.8	− 2.8	+ 3.5	+ 3.6	+ 1.4	+ 2.5
Percent of total expenditure	9.5	9.5	9.3	9.6	9.1	9.4	9.1	9.1	9.5	9.6	
Percent of GDP	2.6	2.7	2.6	2.6	2.5	2.5	2.4	2.5	2.5	2.4	
Research[1]											
Million €	1,225	1,351	1,362	1,395	1,462	1,765	1,499	1,891	2,134	.	
Change from previous year in percent		+10.2	+ 0.9	+ 2.4	+ 4.8	+20.7	−15.1	+ 7.1	+12.9	.	+ 8.2
Percent of all Austrian research expenditure	30.4	30.7	29.1	27.7	27.9	29.8	23.6	29.9	31.2	.	
Percent of total expenditure	2.1	2.2	2.2	2.3	2.3	2.7	2.3	2.7	3.1	.	
Percent of GDP	0.6	0.6	0.6	0.6	0.6	0.7	0.6	0.7	0.8	.	
Infrastructure investment[2]											
Million €	3,348	3,388	3,711	3,768	3,845	3,716	3,711	3,871	4,706	4,508	
Change from previous year in percent		+ 1.2	+ 9.5	+ 1.5	+ 2.0	− 3.4	− 0.1	+ 4.2	+21.6	− 4.2	+ 3.8
Percent of total expenditure	5.7	5.6	6.0	6.1	5.9	5.6	5.6	5.5	6.8	6.5	
Percent of GDP	1.6	1.6	1.7	1.7	1.6	1.5	1.5	1.5	1.8	1.6	
Family support											
Million €	4,322	4,494	4,532	4,960	5,477	6,100	5,789	5,892	5,961	6,024	
Change from previous year in percent		+ 4.0	+ 0.8	+ 9.4	+10.4	+11.4	− 5.1	− 3.4	+ 1.2	+ 1.1	+ 4.2
Percent of total expenditure	7.4	7.4	7.3	8.1	8.4	9.2	8.7	8.4	8.6	8.6	
Percent of GDP	2.1	2.1	2.1	2.2	2.3	2.5	2.3	2.3	2.2	2.2	
Total expenditure											
Million €	58,247	60,409	61,818	61,387	64,977	66,041	66,161	70,519	69,574	69,869	
Change from previous year in percent		+ 3.7	+ 2.3	− 0.7	+ 5.8	+ 1.6	+ 0.2	+ 6.8	− 1.3	+ 0.4	+ 2.3
Percent of GDP	27.7	28.0	28.0	27.1	27.6	26.9	26.0	27.5	25.9	25.0	

Source: Federal Ministry of Finance, WIFO calculations. - [1] According to global estimate by Statistics Austria, April 2007; no figure available for 2008, therefore annual average change 2000/2007. - [2] 2007-08: including instalments for the purchase of military aircraft.

Family-related expenditures exhibit an increase by 4.2 percent per year over the period from 2000 to 2008. As referred to above, the pace has slowed from the peak recorded in 2005, with their share levelling off both with regard to total expenditure and GDP. The total amount of monetary transfers to families remains nevertheless substantial, notable when compared to the volume of family benefits in kind. Against this background, current efforts are to be welcomed and should be pursued to reinforce transfers in kind by offering more public child-care facilities, thereby allowing people to better reconcile work with family obligations, as has been advocated for some time by institutions like the OECD or the European Commission.

Trends in the level and composition of revenues

Overall tendencies

On average for the period from 2000 to 2008, federal government revenues (net tax and tax-like revenues plus other revenues) went up by 2.5 percent per year (Table 14). Tax-like revenues (+2.9 percent p.a.) and particularly net tax revenues (+3.7 percent p.a.) are gaining importance among total federal revenues – a trend to be welcomed from the point of view of sustainability of the revenue situation. Thus, the share of net tax revenues rises from 60.7 percent of total federal revenues in 2000 to 65 percent according to the draft budget for 2007 and further to 66.4 percent in 2008. Conversely, the share of "other" revenues (i.a., from federal assets and sales) which was almost 25 percent in 2000 is falling to 19.1 percent and 17.6 percent in 2007 and 2008, respectively. Tax-like revenues (mainly unemployment insurance contributions, employers' contributions to the family benefit fund as well as shares of income tax revenues earmarked for the financing of the family benefit fund) maintain a broadly stable share of around 16 percent of total federal revenues in 2007 and 2008.

Table 14: Federal government revenues by economic categories, adjusted

	2000	2005	2006	2006	2007	2008	2005-06	2006-07	2007-08	2000-2008
	Outturn		Draft budget	Preliminary outturn	Draft budget			Change		Change p.a.
			Million €					In percent		
Taxes, net	33,037	38,038	38,902	40,454	42,205	44,039	+ 6.4	+ 4.3	+ 4.3	+ 3.7
Tax-like revenues	8,434	9,437	9,717	9,844	10,329	10,617	+ 4.3	+ 4.9	+ 2.8	+ 2.9
Other	12,945	13,172	10,792	14,734	12,442	11,689	+ 11.9	− 15.6	− 6.0	− 1.3
Total	54,416	60,646	59,411	65,032	64,976	66,346	+ 7.2	− 0.1	+ 2.1	+ 2.5
			Percentage shares							
Taxes, net	60.7	62.7	65.5	62.2	65.0	66.4				
Tax-like revenues	15.5	15.6	16.4	15.1	15.9	16.0				
Other	23.8	21.7	18.2	22.7	19.1	17.6				
Total	100.0	100.0	100.0	100.0	100.0	100.0				

Source: Federal Ministry of Finance, WIFO calculations.

Development of gross tax revenues

Among gross tax revenues of the federal government (exclusive plus shared federal taxes)[6], the decline in importance of taxes on wealth in the longer run is eye-catching. These are essentially the tax on the acquisition of real estate, the inheritance and the gift tax as well as the taxes on capital transactions. From a ratio of 4.1 percent in 1990, their share has fallen to a broadly constant 1.5 percent of total gross taxes since the middle of the nineties. If, after the two recent Constitutional Court rulings on the inheritance and the gift tax (currently accounting for about 0.2 percent of gross tax receipts) the government refrains from a reform of these two taxes in compliance with the constitution, bequests and gifts will no longer be subject to taxation as from July 2008. As a consequence, the weight of wealth-related taxes in Austria would decline further.

Indirect taxes yield revenues which over the longer term have proved rather stable around 50 percent of total gross tax revenues. Within this group, energy-related taxes (mineral oil tax, energy levy) are gaining importance (with a share rising from 4.6 percent of all federal taxes in 1990 to a projected 6.9 percent in 2008). Nevertheless, from a peak of 7.7 percent in 2004, when both mineral oil tax and energy levy were last raised, the share of energy taxes has somewhat declined or stagnated, a tendency set to continue in 2007 and 2008. These figures, however, only include the increase in the mineral oil tax by € 0.01 per litre of petrol (from € 0.417 to € 0.427) and by € 0.03 per litre of diesel (from € 0.302 to € 0.332)as originally planned, but not the additional € 0.02 tax increase for each litre of petrol and diesel decided after the draft budget for 2007-08 had been finalized[7]. The latter measure will slightly increase the share of energy-related taxes in total tax revenues as well as the ratio of total taxes to GDP[8].

At the same time, the share of direct taxes is rising markedly in the longer run. According to the draft federal budget for 2008, it will attain 48.7 percent, compared with a ratio of 42.9 percent in 1990. The main driver is the wage tax whose share has climbed from about one-quarter of gross tax revenues in 1990 to over 30 percent in 2008. Reasons for the increase are the growth of employment (most recently also of

[6] Gross federal tax revenues account for over 90 percent of total tax revenues; the remainder are own taxes levied by the Länder (their revenues being of minor importance, however) and by the local communities.

[7] According to a political agreement between the federal government, the Länder and the communities of early July 2007, the additional revenue received from the raise of the mineral oil tax as from 1 July 2007 are to be used for purposes of climate protection (along the lines of the climate protection strategy).

[8] The additional revenues generated by the mineral oil tax increase, once fully accruing as from 2008, amount to € 370 million per year (some € 120 million in 2007) allowing for the revenue losses from the 50 percent-reduction of the motor vehicle tax. These revenues will be distributed among the territorial authorities according to the shares agreed in the Financial Burden Sharing Act, i.e., € 269 million p.a. for the federal government, € 69 million p.a. for the Länder and € 32 million p.a. for the communities.

full-time employment) in recent years, the effect of fiscal drag exacerbated by the 2004-2005 tax reform, as well as the slightly accelerated momentum of gross wages and salaries. The relative weight of corporate tax, which has been steadily declining from a peak in 2001[9] until 2005, has been heading up since, to a projected 9 percent of total gross tax revenues by 2008. The share of assessed income tax, for its part, is going down in a longer-term perspective, from nearly 8 percent of gross tax revenues in 1990 to an estimated 4.3 percent in 2008, a consequence, i.a., of a number of ad-hoc tax cuts introduced over the last few years[10]. The shift of revenues from from assessed income tax towards corporate tax is probably also related to the fact that the Austrian company tax system is not neutral with regard to the legal status of a company, an effect that has been strengthened by the corporate tax cut of 2005[11].

Underlying the draft federal budget 2007-08 and notably the tax projection upon which it is based is the WIFO forecast of December 2006 establishing growth of nominal GDP (the relevant variable for the development of tax revenues) at 4.4 percent for 2007 and 4 percent for 2008. However, in the light of the most recent WIFO forecast of June 2007 and given the buoyant tax intake over the last months, it is likely that the revenue targets will again be surpassed this year.

This implies that the tax-to-GDP ratio may remain constant or increase slightly, rather than decline as assumed earlier (from 41.8 percent in 2006 to 41.5 percent of GDP in 2008; Table 1). Furthermore, the general government deficit may turn out lower than anticipated in either the government programme of January 2007 (1.1 percent of GDP) or the latest update of the Stability Programme and the draft federal budget (0.9 percent of GDP). The latest WIFO forecast expects the general government deficit to narrow to 0.7 percent of GDP in the current year, under the assumptions of budget execution on the expenditure side according to plans, the rigorous implementation of the major efficiency-enhancing reform projects in the public sector and the achievement of an aggregate budgetary surplus of 0.4 percent of GDP by the Länder and the local communities.

Already in 2005 and 2006, actual tax revenues exceeded significantly the budgetary targets, by nearly € 850 million in 2005 and € 2,082 billion gross and 1.6 billion net in 2006. Main contributors to the positive result were excess revenues in corporate tax of € 1.033 billion or more than 27 percent above plans, in VAT of € 771 million or 4 percent, and in wage tax of € 392 million or over 2 percent. Thus, the general government deficit of 1.1 percent of GDP in 2006 was 0.6 percentage point below the target figure included in the draft federal budget for 2006 and the Austrian Stability Programme. The excellent tax intake also compensated the shortfall on the part of Länder and communities which, according to the Maastricht notification of March 2007, reached an actual surplus of 0.4 percent of GDP overall, rather than of 0.6 percent as foreseen by the intra-Austrian Stability Pact.

The swift growth of corporate tax revenues is likely to extend into the current year. Driven primarily by excellent corporate profits, it more than offsets the revenue losses resulting from the cut in the corporate tax rate from 34 percent to 25 percent as from 2005. In addition, positive effects from the latter reform on investment and growth may materialize with a certain time lag. Moreover, the revenue shortfall from the new form of taxation for holding companies (group taxation), also introduced in 2005, has so far proved rather limited, with some € 170 million in 2006. The reasons are that so far only few cross-border holding companies have been established for tax-avoidance purposes, and that any offsetting of domestic losses against foreign earnings within a holding company should play only a minor role in the prevailing profit boom.

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[9] The extraordinarily high corporate tax receipts in 2001, as well as the high yields of assessed income tax are primarily the result of a one-time effect, i.e., the introduction of interest obligation for outstanding tax liabilities.

[10] In particular the introduction and subsequent increase of tax allowances and premia for research and education, tax privileges for undistributed profits and advantages for small-scale self-employed benefiting from simplified accounting obligations.

[11] This is indeed a characteristic feature of the company tax system of all EU member states (*Schratzenstaller,* 2007B).

Table 15: Gross tax revenues by categories

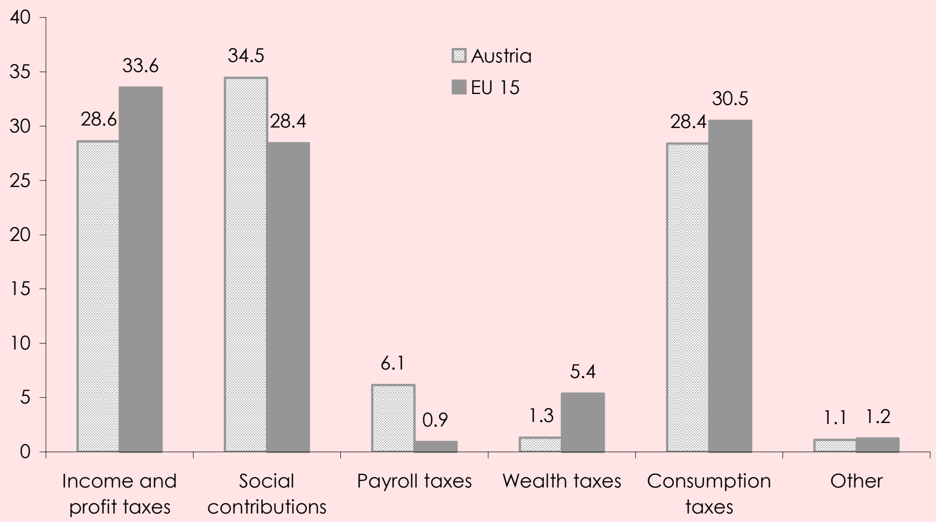
	Total	Income taxes Assessed income tax	Corporate tax	Wage tax	Consumption taxes Total	Energy taxes	Wealth taxes
				In percent			
1990	42.9	7.9	3.2	24.8	50.6	4.6	4.1
1995	46.7	5.8	5.4	28.8	50.8	6.0	1.7
2000	47.1	5.6	7.7	28.7	50.5	6.5	1.4
2001	50.8	7.1	11.1	27.9	47.1	6.5	1.3
2002	48.5	5.7	8.3	29.5	49.3	6.9	1.2
2003	49.5	5.0	8.1	31.7	49.2	7.5	1.3
2004	48.0	5.0	8.0	30.5	50.3	7.7	1.3
2005	46.6	4.4	7.7	29.6	51.7	7.6	1.4
2006	47.1	4.2	8.0	30.0	50.4	7.0	1.5
2007[1]	48.1	4.3	8.7	30.1	49.7	6.9	1.5
2008[1]	48.7	4.3	9.0	30.4	49.2	6.9	1.5

Source: Federal Ministry of Finance, WIFO calculations. – [1] Federal draft budget.

Figure 1 illustrates for the year 2005 the composition of total taxes (taxes accruing to all territorial levels plus social security contributions) in Austria in comparison with the EU-15 average. The most eye-catching difference has become still wider since 2003 (*Schratzenstaller*, 2005), with labour-earnings-related taxes (social security contributions plus all other payroll taxes) claiming a share of 40.6 percent of total taxes in 2005 in Austria compared with 29.3 percent for the EU 15. At the same time, taxes on wealth play only a minor role in Austria, accounting for 1.3 percent of the total, whereas in the EU 15 their share equals 5.4 percent. The share of taxes on income of private households and corporate profits in Austria is 5 percentage points below the EU 15 average, as is – albeit slightly – the financial contributions from taxes on consumption.

Figure 1: Tax structure in Austria compared with the EU 15

2005, share of total tax revenue in percent



Source: OECD, Revenue Statistics 1965-2005, Paris, 2006.

Such revealed imbalance of the Austrian tax structure, which will be further exacerbated by the envisaged increase in health insurance contributions by 0.15 percentage point[12] as from 2008 as well as by the announced expiry of the inheritance

[12] The increase in health insurance contributions as from 2008, with an annual additional yield projected at € 150 million, is supposed to cover half of the expected increase in public health expenditure.

and the gift tax, is considered problematic both from an employment (*Schratzenstaller,* 2006) and an equity perspective[13].

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Draft Federal Budget 2007-08: Matching Consolidation With New Spending Priorities – Summary

Austria's budget policy continues to face challenges that are difficult to reconcile. On the one hand the additional revenues and the expenditure savings in the wake of the economic upswing should be used for the consolidation of the public budgets. On the other, Austria still faces deficits in some areas of key importance for the development of the long-term growth path (in particular education, research and development, infrastructure). The federal budget draft for 2007-08 is a compromise between these conflicting requirements. It combines a slower budget consolidation than the dynamic economic situation would allow with slight increases in spending for education, research, science, infrastructure and social protection.

A precondition for the emphasis put on future-oriented expenditure for the years 2007 and 2008 to be pursued also in the longer term will be to create the necessary budgetary leeway. To this end, it will be essential to step up especially the big reform projects aimed at improving the efficiency of public sector activity itself: constitutional and administrative reform as well as the reform of federal budget legislation. In addition, structural savings on the expenditure side are to enable a substantial tax relief at the end of the legislation period. These measures should reduce government spending ratios both at the federal and the general government level.

Since 2000 there have been slight structural shifts in federal government spending. The share of total expenditure accounted for by transfer expenditure is set to grow over a longer period of time; for 2008, it is estimated at 38.6 percent. The main reason behind the dynamic development of transfer expenditure lies in the marked increase in expenditure on family benefits. The share of expenditure on old age protection, accounting for almost 59 percent of all transfer expenditure, remains constantly high.

Of all federal government revenue items, tax-like receipts as well as the federal government's net revenue from taxes are gaining in significance. This implies that revenue from one-off measures is becoming less important and hence sustainability of the federal government's revenue situation is increasing. Over the long term, the most obvious structural change regarding the federal government's gross tax revenue is the relative loss in importance of wealth taxes: starting from 4.1 percent in 1990, their share in total gross tax revenue has remained stable at a constantly low level of around 1.5 percent since the mid-1990s. At the same time taxes on labour have been gaining in significance in Austria. This imbalance of Austria's tax structure, which is problematic notably from an employment policy, but also from a distribution policy point of view, will be exacerbated by the 0.15 percentage point increase in health insurance contributions to be introduced in 2008 as well as by the announced phasing out of the inheritance and gift tax.

[13] The OECD, in its latest economic survey of Austria, also points to the lop-sided tax structure and its potential problems. The latter are reinforced by the fact that real estate wealth is under-assessed for tax purposes not only in the context of inheritance and gift tax, but also due to deficiencies in the valuation adjustment mechanism.

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