

Press information of the Fiscal Advisory Council of September 28, 2018

High fiscal forecasting performance of Austrian Fiscal Advisory Council

The assessment of fiscal forecasts made by the Austrian finance ministry, the European Commission and the Fiscal Advisory Council revealed that the forecast errors for the fiscal indicators for Austria (budget deficit, structural budget deficit, government revenue and expenditure) were clustered closely together. The Fiscal Advisory Council overestimated the general government deficit (in percent of GDP) during the review period (2014 to 2017) by around 0.4% on average for the current year and the subsequent year, as did the finance ministry and the European Commission (Hauth et al., 2018)¹. By international standards, forecast errors of this magnitude can be considered as very low. According to estimates of the European Commission (Fioramanti et al., 2016)², forecast errors were higher in almost all EU countries for the period between 1969 and 2014, coming to around 1% of GDP or more.

Fiscal forecasts for Austria (finance ministry, European Commission and Fiscal Advisory Council) were found to be **biased** in the same direction, **primarily** because the cyclical **upswing** at the end of the review period (2014 to 2017) turned out to be **stronger than anticipated**. In addition, **cautious planning** of government bodies and strict budget execution might have contributed to an unduly pessimistic assessment of fiscal indicators. In the Fiscal Advisory Council's budget forecasts, the share of fundamental and discretionary errors (own estimation errors) in the forecast bias³ came to 32%, while cyclical errors (errors in WIFO's macroeconomic forecasts that were copied by the Fiscal Advisory Council) came to 47%, and basis errors (revisions of actual outcomes by Statistics Austria) to 21%.

The **fiscal forecasts of the Fiscal Advisory Council**, like those of the **finance ministry**, are based on **macroeconomic forecasts provided by the Austrian Institute of Economic Research (WIFO)**. The fiscal forecasts of the European Commission are based on the Commission's **own** economic outlook. Having mapped fiscal forecast errors to the underlying reasons, we found macroeconomic forecasts to be particularly relevant for the forecasts of revenue intake. Looking ahead, the quality of fiscal forecasts for Austria could be improved above all with measures to reduce the forecast bias for **GDP components on the income side** of the national accounts (above all compensation of employees).

The **Fiscal Advisory Council's average forecasting performance** in the forecasting rounds from fall 2014 to fall 2017 for the years t and $t+1$ corresponded roughly to that of the finance ministry and the European Commission, with forecasts for **short forecasting horizons** (forecasts for the current year t) qualifying as **unbiased** and the forecast bias being smaller than that in forecasts made by the finance ministry and the European Commission. The **period under review** included all available forecasts produced so far by the Fiscal Advisory Council, thus covering (the maximum number of) 12 data points.

The mean forecast errors for the **budget deficit** and the **structural budget deficit** in the forecasts of the Fiscal Advisory Council, the finance ministry and the European Commission were found to be similarly high in the period under review (2014 to 2017) (bias and MAE⁴ of some 0.4% to 0.5% of GDP). For both fiscal indicators, the forecast errors **mainly** reflect the uncertainty surrounding forecasts of **government**

1 Hauth, E., J. Holler and P. Schuster. 2018. Fiscal forecasting performance of the Austrian Fiscal Advisory Council (see www.fiskalrat.at/en for more information).

2 Fioramanti, M., L. González Cabanillas, B. Roelstraete and S.A. Ferrandis Vallterra. 2016. European Commission's Forecasts Accuracy Revisited. European Economy Discussion Paper 27.

3 The mean error (bias) serves as an indicator for systematic distortions, indicating whether budget forecasts have tended to be either too optimistic or too pessimistic on average, with overestimations and underestimations setting each other off.

4 The mean absolute forecast error (MAE) is an indicator for forecast precision (average sum of all absolute forecast errors). Overestimations and underestimations do not offset one another in this error measure.

revenue and expenditure. The **forecast errors** for **acyclical government revenue and expenditure** (i.e. budget positions that do not rise and fall in line with economic conditions) may reflect **conceptual weaknesses** of the cyclical adjustment methods used in the fiscal rule monitoring process as well as mis-estimations of the budgetary impact of economic policy measures. However, these aspects have not been addressed in the corresponding paper.

Given the precision of fiscal forecasts made by the Fiscal Advisory Council, the finance ministry and the European Commission, the **structural budget deficit** in Austria seems to be **sufficiently predictable** and **adequate** for **use as fiscal rules** for Austria.

In the period under review (2014 to 2017), the **EU's expenditure rule** for Austria appears to have been **largely inadequate** for use as fiscal rules for Austria owing to two effects (varying targets and uncertainty surrounding government expenditure growth): In hindsight, the **varying targets** derived for Austria from the European Commission's forecasts with regard to the expenditure rule appear to have been too restrictive (bias of -0.51; MAE of 0.55 percentage points). Furthermore, the **growth rates of (adjusted, nominal) public expenditure** were **overestimated** (forecasts of the Fiscal Advisory Council: bias of 0.34; MAE of 0.39 percentage points). The expenditure rule in the EU's fiscal framework provides an additional assessment criterion for the cyclical adequacy of the budget path under the preventive arm of the Stability and Growth Pact.

The **preliminary data on actual fiscal outcomes for the past year** (available by March) published by Statistics Austria feed into the assessment of Austria's **compliance with fiscal rules** made first by the European Commission and then by the Ecofin Council. While the ex post revisions of actual outcomes were rather limited for the budget deficit, the preliminary data on **public revenue and expenditure** were found to be fraught with weaknesses. One way to improve the quality of the data that are available by March would be to **bring forward the deadlines by which the subsectoral levels of government and large off-budget units** are required to submit data to Statistics Austria.

To enhance the predictability of the budget and the forecasting performance of the Fiscal Advisory Council, the Fiscal Advisory Council would suggest improving the quality of **economic indicators** that are relevant for policymaking (e.g. for employment growth in general and the government sector), ensuring **quality costing exercises** for major government economic policy measures as well as safeguarding **broad access to official data and information**, subject to compliance with confidentiality requirements.

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Different definitions of subsidies cause big differences in recorded figures on government subsidy spending

Elimination of existing information deficits and improved evaluation could enhance efficiency of subsidies

The application of different national and international definitions of subsidies is the reason why the recorded amounts of subsidies in Austria vary widely (Grossmann, 2018).⁵ Depending on the definitions used, central government subsidies amounted to between EUR 6.9 billion and EUR 15.7 billion in 2016, and subsidies paid out by regional and local governments totaled between EUR 1.4 billion and EUR 7.5 billion. Given the differences in definitions and a lack of comparability (e.g. of subsidy instruments or the sectoral classification of recipients), interpreting data on subsidy levels requires in-depth knowledge and additional information. Greater transparency in the Austrian system of subsidies in terms of objectives, resources and impact could enhance the efficiency of subsidies and prevent instances of multiple subsidies. To this end, the transparency database set up jointly by the central and regional governments could be gradually expanded and the existing instrument of the regulatory impact assessment pursuant to the Federal Budget Act 2013 could be optimized.

The Austrian system of subsidies has repeatedly been presented as a prominent example of an area of joint tasks and expenditure across all levels of government that holds a high potential for enhancing efficiency and cutting costs (see, for instance, Court of Auditors, 2016 and 2015; Pitlik, 2012; or Fiscal Advisory Council, 2018).⁶ This is essentially attributable to the system's **lack of transparency with regard to the objectives, amounts and actual impact of subsidies**, which also impedes a strategic approach to subsidization in Austria that is consistent across all levels of government.

The level of subsidies depends to a large extent on the **choice of subsidy instrument, the design of the tax system** and the type and scope of governmental tasks (outsourced tasks and inherent responsibilities). Figures on subsidy spending are largely determined by the **definitions and sectoral classifications** that are used. As a result, the **recorded amount of central government subsidies** ranged from EUR 6.9 billion (based on the European System of Accounts (ESA) 2010) to EUR 15.7 billion (based on the Federal Budget Act 2013) in **2016**. Under ESA 2010, the scope of subsidy instruments (essentially **direct subsidies** or transfers to the **corporate sector**)⁷ and the classification of significant recipients of subsidies as part of the government sector (e.g. public transport operators) limit the figures recorded for subsidies to third parties. In contrast, under the Federal Budget Act 2013, subsidies comprise primarily indirect subsidies (such as tax breaks like lower tax rates provided by the Value Added Tax Act), which account for around 75% of total subsidies. (In addition, subsidies under the Federal Budget Act 2013 also include benefits for households.) The amount of **regional and local government** subsidies to the corporate sector recorded for **2016** ranges from EUR 1.4 billion (based on the 1997 Budgeting and Accounts Regulation) to EUR 7.5 billion (based on ESA 2010).

International comparisons of national levels of subsidies are usually based on **ESA 2010**. These data suggest that, **compared to other euro area countries**, the level of subsidies granted to the corporate sector in Austria is **average**. According to this data source, Austria's **total government spending on subsidies for the corporate sector** amounted to EUR 14.6 billion in 2016,⁸ with the category “**economic**

5 Grossmann, B. 2018. Subsidies in Austria: definitions, spending levels and suggestions for improving efficiency (available in German only, see www.fiskalrat.at)

6 RH-Bericht Reihe Bund 2015/17 and Reihe Bund 2016/22; Pitlik, H. (2012). Darstellung der Unternehmensförderungen in Österreich und Identifikation von Einsparungshebeln; Fiscal Advisory Council. 2018. Fiscal Rules Compliance Report 2017-2022.

7 The term corporate sector is used in a broad sense (i.e. private sector excluding households).

8 Sum of subsidies (D.3), current international cooperation and miscellaneous current transfers (D.74 and D.75) and capital

affairs” receiving the largest share by far (EUR 5.0 billion), followed by “**social insurance**” and “**human health activities**” (EUR 2.1 billion each). These figures do not include EU subsidies for Austrian manufacturers in the amount of EUR 1.1 billion, which are granted above all to the agricultural sector and constitute only pass-through funds in Member States’ budgets.

Different institutional setups (in addition to some leeway in accounting) make international comparisons difficult. For instance, the level of public subsidies (under ESA 2010) depends on the sector classification of quasi-public organizations (e.g. on whether transport infrastructure operators or healthcare and education providers are considered as part of the government or the private sector). While funding flows between government entities (e.g. central government funds to the Austrian Federal Railways’ infrastructure and passenger subsidiaries (ÖBB Infrastruktur and ÖBB Personenverkehr)) do not constitute subsidies but intergovernmental transfers, financial flows to third parties (e.g. local private railway operators) are recorded as subsidies to the private sector.

Subsidy reports published by the central government and some regional governments contain relevant information, but **no uniform reporting requirements or standards** apply for data coverage and definitions. Harmonizing data coverage and involving all levels of government would help establish a regular **reporting framework**, thereby yielding information that could feed into a shared **database**.

The “**transparency database**,” launched in 2010 on the initiative of the Federal Ministry of Finance, operates on the basis of a very broad definition of subsidies, a number of different objectives as well as individual personal and business data. Designed as a comprehensive information, monitoring and control tool, the database has repeatedly been **criticized** – e.g. by the Court of Auditors and some regional governments – for the way it has been **organized and implemented so far**. For instance, the database so far does not cover important target areas of regional and local government subsidies because the administrative burden of supplying the relevant data is considered to be too high. Furthermore, the information stored in the database (e.g. subsidy amounts) is hardly accessible to the public. The usability of the **transparency database** could be enhanced by its **gradual expansion and the requirement to make the information accessible to the public** (in compliance with data protection law). A first priority could be to **identify multiple subsidies**; for this goal to be achieved, it does not appear to be absolutely necessary to store individual personal and business data.

A more **in-depth policy discussion about the benefits and costs** of individual subsidization measures requires **detailed information about subsidy programs offered by the various levels of government and the EU** (e.g. targets broken down by impact categories, planned and actual budgetary costs, characteristics of recipients like economic sector and company size as well as actual impact), and this information should be open to the public. At present, **exhaustive** (external) **expert evaluations** of individual subsidies (e.g. research grants, financial incentives for households to hire contractors for renovation and upkeep work) are provided only **in some cases** and not always accessible to the public.

The **regulatory impact assessment pursuant to the Federal Budget Act 2013** is a suitable instrument that could also be applied to all significant subsidy measures and programs, even – in a simplified form – to those provided by regional and local governments. Information related to the impact of subsidies (impact targets, measures and indicators) has been an integral part of central government budget estimates since 2013; as a rule, this information is subjected to an ex post review. However, there is a need to improve both **ex ante regulatory impact assessments and ex post evaluations**, e.g. in terms of uniform quality standards, choice of impact indicators and methodological changes in ex post evaluations. Furthermore, the current 5-year deadline for ex post evaluations in general should be reduced in the areas of subsidies. The main results should feed into a publicly accessible **database**.

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