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COVID-19 and Beyond.** An Assessment
at the Turn of the Year 2020-21

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Austrian economic policy in 2020 was largely dominated by the fight against the COVID-19 pandemic. As a result, the implementation of the new government programme presented at the beginning of the year took a back seat, as did the solution of a number of structural problems facing the Austrian economy. This article summarises the main lines of economic development in 2020, focuses on the government's main economic policy measures and discusses the issues and necessary reform steps to be taken in 2021, such as climate policy or the long-term consolidation of public budgets. The references refer to in-depth WIFO research on the respective topics.

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In 2020, the COVID-19 crisis overshadowed all other economic policy challenges. At the beginning of 2021, it is still unclear whether and when economic policy can begin to come to terms with the crisis and return to those issues that had to be put on hold because of the COVID-19 pandemic, but which are highly important for the long-term development of the Austrian economy. The

initial situation for reforms deteriorated significantly due to the fiscal and real economic effects of the COVID-19 crisis, but the challenges remained the same.

This article looks back on the past year, gives an assessment of developments in 2020 and discusses the economic challenges for 2021.

1. Retrospect: economic development in the year 2020

Until the diagnosis of the first COVID-19 case in Austria at the end of February 2020, there seemed to be an inconspicuous economic development, in particular a slight weakening of the economy.

1.1 The environment of European economic policy

At the beginning of 2020, a **weak phase in world trade** had a dampening effect on the economy in Austria, which was essentially

supported by consumption. The WIFO forecast assumed that Austria's export dynamics would reach their lowest point around the middle of 2020 (Glocker, 2020, p. 28).

The European Central Bank (ECB) had sent signals towards a "normalisation" of monetary policy until mid-2019 by reducing its monthly bond purchases. However, due to the slight downturn in the second half of 2019, the expansionary course was resumed,

the continuation of which was expected for 2020.

In autumn 2019, the European Commission launched plans for a "Green Deal". The political debate revolved around the chances of realising this ambitious project. Negotiations on the new Multiannual Financial Framework 2021-2027 were underway but not yet far advanced¹. The Commission also initiated a discussion on a medium-term change of the fiscal rules.

This rather low-key development among Europe's major economic policy players changed within a few weeks after the rapid spread of the COVID-19 pandemic in Europe.

The **European Central Bank** reacted quickly to the COVID-19 crisis². This was especially true for the PEPP (**Pandemic Emergency Purchase Programme**), which was announced on 18 March 2020 in the amount of 750 billion €. The programme led to a calming of the financial markets in the euro area and has ensured a reduction in interest rates on government bonds of the euro countries. It was increased first in June and then in December to a total of 1,850 billion € and extended until March 2022.

After prolonged negotiations, the EU responded to the COVID-19 crisis with a fiscal package that is historic in its scale and design. In November 2020, the Council of the European Union and the European Parliament agreed on a **recovery package to address the consequences of the COVID-19 pandemic (NextGenerationEU)**, which is linked to the Multiannual Financial Framework 2021-2027. This European recovery plan has a total volume of just over 1.8 trillion €, of which 1.074 trillion € is allocated to the Multiannual Financial Framework and 750 billion € to the COVID-19 recovery package NextGenerationEU. The package will initially be financed by the EU taking on debt. 390 billion € will go to EU member countries as non-repayable grants and another 360 billion € as loans to be serviced by the countries concerned.

The development plan sets clear priorities in the areas of climate protection and digitalisation. Thus, 30 percent of the expenditures are to be used for climate protection. In the most significant instrument of the recovery package, the Resilience and Recovery Facility (RRF) with a volume of 672.5 billion €, the climate target is even 37 percent; 20 percent of the funds from the RRF are to flow into the digital transformation. The agreement also contains a timetable for the introduction of innovative own resources to service the jointly contracted debt. To

¹ An agreement on this in the European Council was finally reached in July 2020.

finance the **Multiannual Financial Framework**, the existing sources of own resources will be supplemented from 2021 by a system based on a country's non-recyclable plastic waste.

The supranational programmes will support the member countries considerably in their own efforts to combat the crisis. Admittedly, the programmes only have a longer-term effect because the EU funds can only flow from 2021 onwards and funds from the reconstruction package are to be drawn down until the end of 2023.

In the attempts to support the member countries, the European Commission's lack of **decision-making competence in health policy** became apparent. In the hectic search for scarce products such as protective mouth-nose masks or protective suits, there was not only a lack of cooperation among the member countries; rather, they sometimes behaved in a protectionist and nationalistic manner (Wolfmayr, 2020). Internal EU coordination of travel restrictions also failed. Towards the end of the year, however, the Commission succeeded in achieving a coordinated approach to the procurement of vaccines, so that the EU's market power could be played out in contract negotiations with international pharmaceutical companies. However, given the difficulties around the actual delivery of the vaccines, this has yet to prove itself.

1.2 Austria at the start of 2020: the ambitions of a new government programme

On 10 January 2020, when SARS-CoV-2 infections did not yet seem to be a European problem, the newly sworn-in federal government presented its government programme (*Federal Chancellery*, 2020).

The basic **fiscal policy plans** (*Federal Chancellery*, 2020, p. 76ff) were formulated as a reduction of the tax ratio towards 40 percent of GDP, a reduction of the debt ratio towards 60 percent of GDP and a balanced budget over the economic cycle. Considerable relief in the area of wage and income tax was provided with a concrete timetable from 2021. For example, a reduction of corporate income tax to 21 percent and the introduction of a loss carryback for firms who determine their taxes on a cash-base were announced without any further deadline.

In the **environmental field**, the government committed itself to an eco-social tax reform "with steering effects to successfully combat climate change", whereby some smaller measures were announced as a "first step" for 2020. For 2022, an "effective pricing of climate-damaging emissions" was promised

² For an overview see <https://www.ecb.europa.eu/press/key/date/2020/html/ecb.sp200624-d102335222.en.html>.

The EU and ECB provided massive monetary and fiscal stimuli to combat the looming COVID-19 economic crisis.

The new coalition government set programmatic priorities in environmental and financial policy at the beginning of 2020. However, the policy soon came under pressure from the COVID-19 pandemic.

within the framework of a revenue-neutral eco-social tax reform.

The environmental policy part of the programme (*Federal Chancellery, 2020, p. 100ff*) is also ambitious beyond the tax policy. Announced were the achievement of Austria's climate neutrality by 2040, considerable investments for building renovation, a phase-out plan for the use of fossil fuels in space heating (1 million roofs with photovoltaics), a "Green Deal" for Austria's economy, a technology offensive, the introduction of an Austria Ticket for public transport and investments of 1 billion € each in local and regional transport.

Finally, the government programme announced some of the frequently called for "structural reforms": these include a new financial equalisation system and a new framework of competences between the federal government and the Länder to achieve the climate targets (*Federal Chancellery, 2020, p. 11f*), the identification of "deregulation potential in the administration" (p. 14) or a federal funding strategy involving the regional authorities (p. 17).

The question of the **financial viability** of the programme's **projects** was intensively discussed, because even before the outbreak of the COVID-19 crisis it was unclear how the many plans could be realised at the same time, especially the tax relief, the balancing

of the state budget and the planned investment projects.

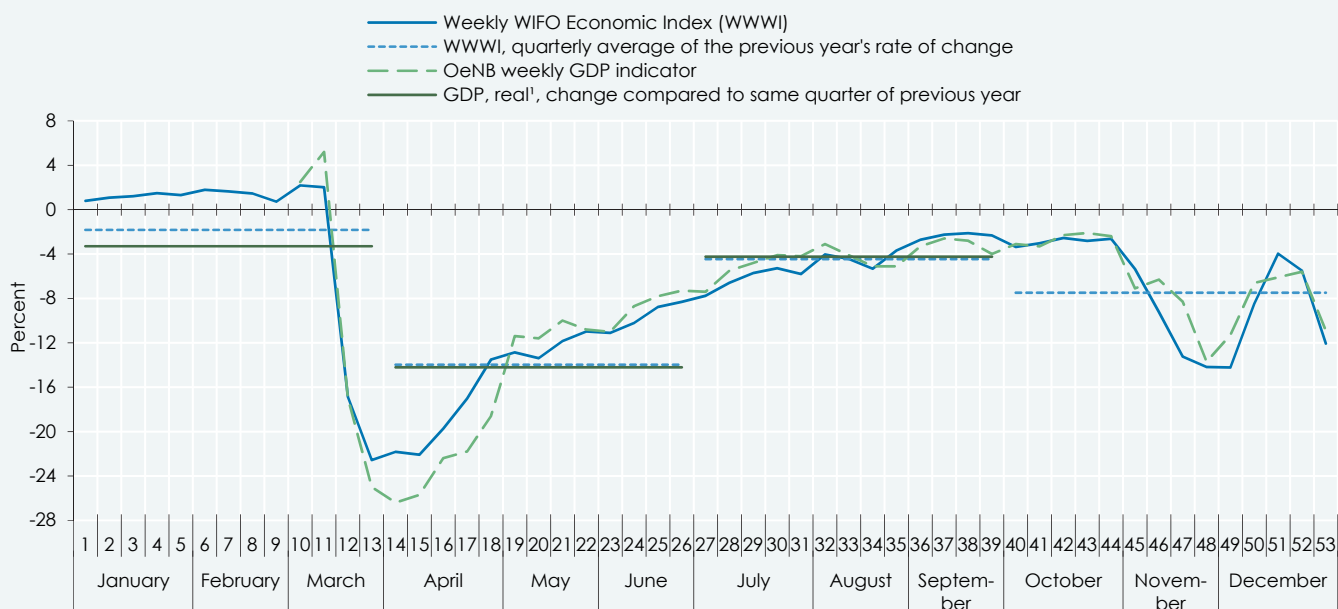
Due to the onset of the COVID-19 pandemic, which began to tie up resources in March 2020, the new government had barely two months to organise its work and initiate concrete processes to deal with the numerous projects. Nevertheless, other economic topics were also on the agenda in the further course of 2020: a care reform process was initiated, a reform of the "Hacklerpension" was discussed, the topics of a shortage of skilled workers and a reduction in working hours were repeatedly touched upon, and finally smaller parts of an eco-social tax reform were also initiated.

1.3 The COVID-19 pandemic and the general economic development in Austria

The Austrian federal government reacted to the rapidly spreading pandemic from the end of February 2020 with a far-reaching catalogue of measures, which led to an almost **complete "lockdown" in mid-March**, especially in the services sector. Industry was only indirectly or less severely affected by this lockdown, but suffered from delays in the supply chains in the first months of 2020 because inputs from China, other Asian countries and later also from Italy did not arrive on time. This was compounded by difficulties in the sales markets and restrictions in transport and travel, also within Europe.

Figure 1: **Weekly key figures of economic activity**

2020



Source: WIFO, OeNB, Statistics Austria. – ¹ Seasonally and working-day adjusted according to Eurostat.

The lockdown in mid-March 2020 triggered the worst economic crisis of the post-war period so far.

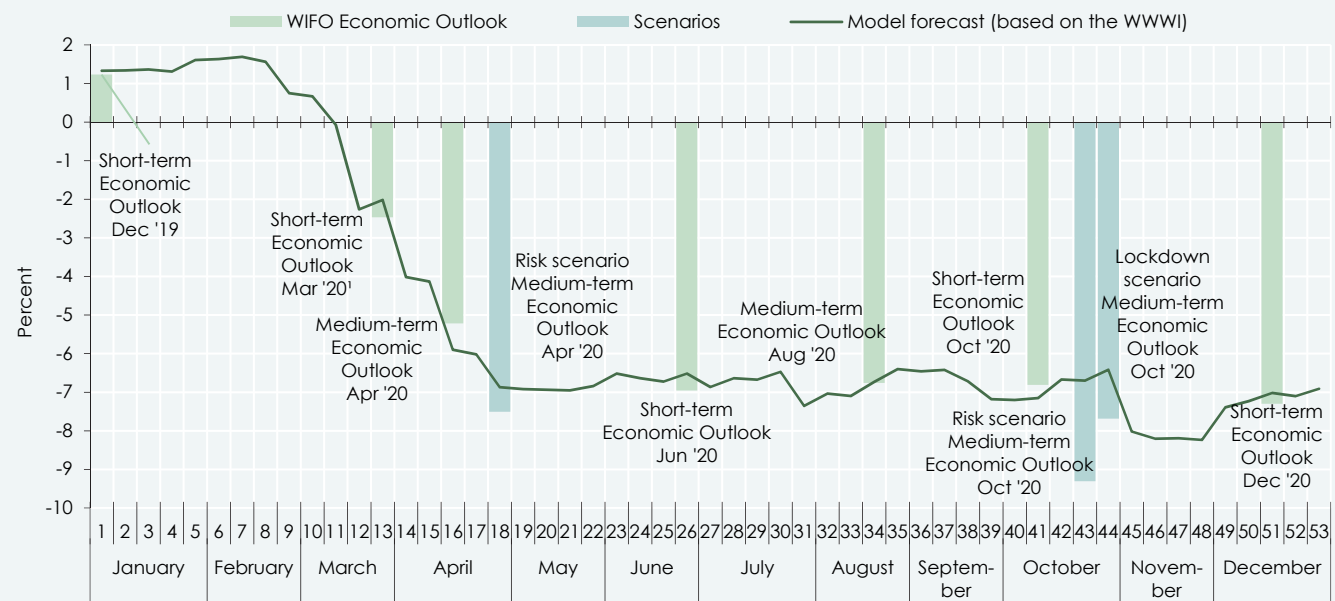
This was followed by a recession that was unprecedented for the post-war period in terms of the speed and depth of the slump. The dramatically fluctuating level of economic activity in the course of 2020 can be seen in the **WIFO Weekly Economic Index – WWWI** (Figure 1; *Bilek-Steindl et al., 2020*). It measures the real economic activity of the Austrian economy on the basis of 14 weekly, seven monthly and one quarterly indicator.

The economic development in 2020 reflected the events of the infection and the political reactions to it: the dramatic economic slump at the end of March was followed by a strong rebound from the second half of April onwards, which was caused by shops opening again and thus the revival of consumption. From May onwards, a phase of slower but steady recovery began, which continued throughout the summer, thanks in part to brisk demand in summer tourism. Despite a clear increase in the number of infections in early autumn, the economy developed relatively favourably until the end of October, although value added remained consistently below the previous

year's level. Politicians reacted to the strong increase in COVID-19 cases only at the beginning of November with an initially partial and two weeks later tightened lockdown. Accordingly, economic activity again plummeted rapidly from the second week of November, although not as deeply as in the spring. The "hard" lockdown from 17 November was reflected in the indicators, as was the recovery after the partial easing from the second week of December (Figure 1). The lockdown in the last week of the year again led to a significant decline in economic activity.

The historically unique recession posed special challenges for economic research. Due to the volatile epidemiological situation, there was a **need for forecasts of economic development** at very short intervals. The expectations could not be met with the traditional instruments: neither were the necessary data bases for a forecast available, nor were there and are there reliable empirical values on how economic subjects behave under completely changed boundary conditions.

Figure 2: GDP growth forecasts and scenarios



Source: WIFO. WWWI . . . Weekly WIFO Economic Index. – ¹ An economic scenario for 2020 was published in March 2020.

Conventional economic forecasts reached their limits, and WIFO replaced and supplemented them with alternative scenarios.

WIFO therefore partially replaced its usual short- and medium-term forecasts with scenarios, or supplemented forecasts with **alternative scenarios** based on different assumptions about the development of infection figures and the measures derived from them³. As the pandemic progressed, the

forecasts had to be adapted several times, with the outlook for economic growth in 2020 becoming increasingly gloomy, with the exception of a brief brightening in the summer (Figure 2)⁴. The main reason for this was a deterioration in the health situation in

³ Alternative scenarios for the economic cycle in 2021 were also calculated in December 2020.

⁴ For the end-of-year forecast of the economy in 2020 based on conventional macroeconomic indicators, see *Schiman* (2021).

autumn, which had not been expected to this extent at the beginning of the summer.

Even if an end to the recession cannot yet be predicted precisely at the turn of the year 2020-21, some general characteristics of the crisis are already certain. Since it was caused by a health threat situation and the necessary policy responses to it, it is **not comparable to any conventional recession**, especially not to the financial market and economic crisis of 2008-09. The economic slump caused by the COVID-19 crisis is expected to be deeper and shorter than that of the financial market and economic crisis. Economic policy measures alone can mitigate the crisis, but not bring it to a sustainable end. This will only be possible when the health threat is permanently overcome through vaccinations or therapies.

The specifics of the COVID-19 recession can also be seen in terms of the **sectors affected**. While the financial market and economic

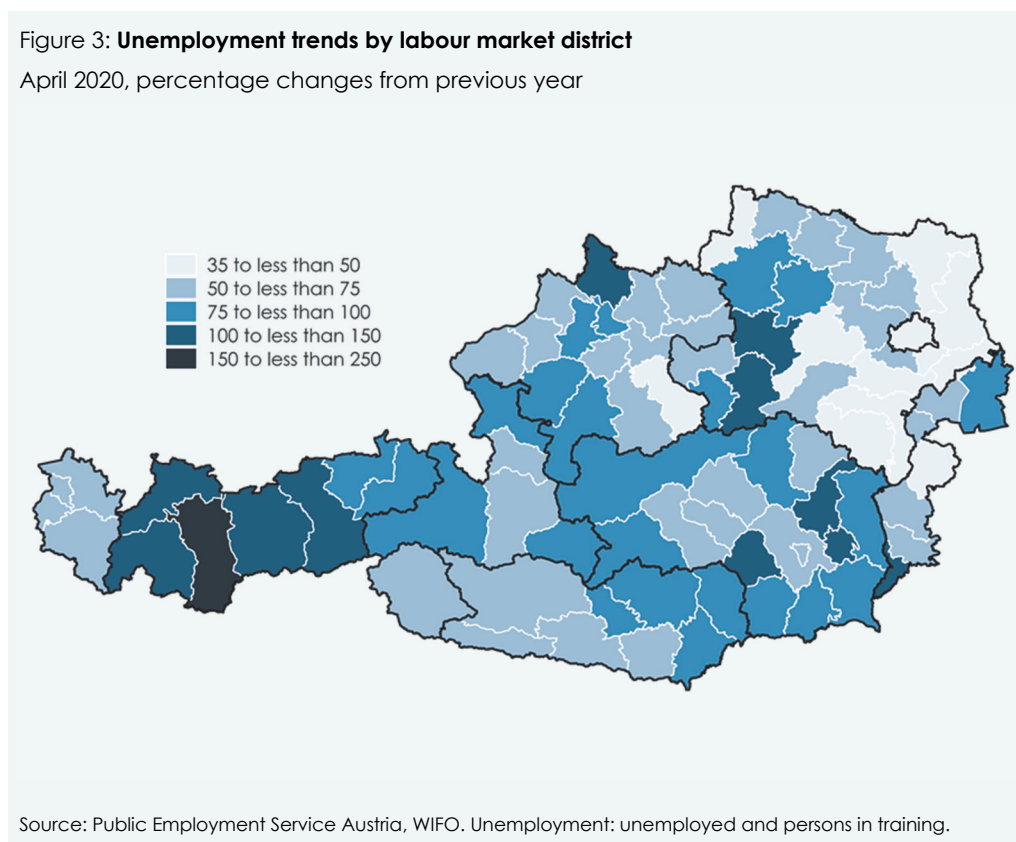
crisis had hit industry particularly hard, in 2020 the sharpest declines in gross value added were observed in services (including arts, entertainment and recreation; see e.g. *Pitlik – Fritz – Streicher, 2020*) and in accommodation and food services. The most severe dislocations are in tourism. A decline of –7.7 percent is expected for manufacturing (including mining)⁵, while tourism, for example, had to contend with declines in overnight stays of up to 40 percent – based on 2020 as a whole.

1.4 The special impact of tourism

The varying impact of individual sectors was also accompanied by **regional differences** in the effects of the crisis. In the early phase of the first lockdown, WIFO estimated the relative impact of the economy by province⁶ (*Bachtrögler et al., 2020*) based on an analysis of 88 ÖNACE divisions and on assumptions about how the lockdown would affect the different sectors⁷.

Figure 3: **Unemployment trends by labour market district**

April 2020, percentage changes from previous year



Source: Public Employment Service Austria, WIFO. Unemployment: unemployed and persons in training.

At the beginning of April 2020, Upper and Lower Austria had the lowest share of employed persons in economically strongly or very strongly affected sectors. In Tyrol and

Salzburg – both federal provinces with an economic structure largely determined by tourism – this share was the highest.

⁵ For a detailed description of affectedness by sector, see *Schiman (2021)*.

⁶ See for an interactive map with continuously updated data on the individual Länder <https://corona.wifo.ac.at/arbeitslosigkeit/2020-11/AT>.

⁷ The sectors classified as "very severely" affected were those that could not continue their business

activities due to the measures or could only do so to a significantly limited extent and for which it seemed unlikely that they would be able to make up for the loss of revenue. Further criteria for the classification were a decline in export and consumer demand as well as supply-side restrictions due to the interruption or delay of supply chains.

The economic crisis affects different sectors and regions to varying degrees. Tourism proved to be a particular problem area.

Despite the massive use of short-time work, the labour market entered a severe crisis; the number of unemployed reached a peak of 522,253 persons at times.

The important role of tourism can also be seen in Public Employment Service Austria (AMS) data on the small-scale development of unemployment (Figure 3). Regional differences were most evident in the phase of the complete lockdown in spring 2020.

WIFO therefore presented several detailed analyses on the specific situation in tourism⁸. After years of almost steady growth in demand, the Austrian **tourism industry** was **hit particularly hard** by the COVID-19 crisis. Both the various travel warnings and the reduced willingness to travel led to a drastic decline in travel activity. Added to this were the supply-side restrictions in the course of the various lockdown phases.

While the increase in domestic demand was still able to dampen the losses in summer 2020, the outlook for the current winter season is gloomy overall, both because of the new lockdown at the beginning of 2021 and because a compensation of the loss of foreign demand by domestic tourism in winter is not to be expected.

In the calendar year 2020, the number of overnight stays is expected to have been around 37 percent lower than in the previous year. Assuming that numerous countries will only lift their travel warnings for Austria in the course of spring, tourism demand will recover only very slowly in 2021; in the winter season 2020-21, the decline in overnight stays will reach around 70 percent. Only in early summer should the recovery in tourism accelerate and be completed towards the end of 2021. In this scenario, the number of overnight stays in 2021 will increase by only about 11 percent compared to the previous year. A "normal year" in tourism can be assumed again in 2022 at the earliest, if the economic crisis can also be overcome by then. In city tourism, market conditions are likely to normalise even later due to the high dependence on long-distance markets.

For these reasons, the situation of the tourism industry has been a particular focus of **economic policy discussions** on the type, scope and duration of state support. Examples of this kind raise the fundamental question of how long public subsidies can be disbursed or whether and to what extent company closures must also be accepted in order to shake out the market.

1.5 Consequences of the COVID-19 crisis for the labour market and social affairs

The COVID-19 economic crisis was of historic significance for the Austrian labour market.

⁸ A summarising account can be found in *Fritz – Ehn-Fragner* (2020).

⁹ See also *Bock-Schappelwein – Huemer – Hyll* (2020A), *Bock-Schappelwein et al.* (2020A).

¹⁰ According to the umbrella organisation of the social insurance institutions, excluding persons in valid

The lockdown in mid-March 2020 caused the highest **decline in dependent employment** in almost 70 years within a few days⁹, whereby the extensive use of COVID-19 short-time work prevented an even greater reduction in employment. Nevertheless, unemployment reached a new high.

At the end of 2020, the consequences for dependent employment were still noticeable: while active dependent employment¹⁰ had fallen by 4.9 percent year-on-year in March 2020 (April 5.0 percent), the level of employment at the end of December was 3.3 percent below the level of the previous year. The number of workers registered for short-time work, after peaking in May with over 1.3 million cases, fell to 133,000¹¹ by the beginning of November and increased to 417,113 by the end of the year as a result of the second lockdown.

After a drastic **rise** between mid-March and mid-April 2020, **unemployment** fell gradually until the end of September and rose again from mid-October, partly due to the end of the summer season in tourism. At the end of December, unemployment was 109,887 or 31.4 percent above the previous year's level, including people in training 113,047 or 27.7 percent above.

The increase in the number of **long-term unemployed** is particularly serious. At the end of December, 166,868 people in Austria had been unemployed for more than a year – apart from short interruptions. This corresponds to an increase of about one third compared to the previous year. 32 percent of all unemployed persons and persons in training were long-term unemployed at the end of 2020. For many who had already been unemployed (for longer) before the COVID-19 crisis, the chances of finding a job fell even further.

In the wake of the financial market and economic crisis of 2008-09, unemployment had already become entrenched. The base unemployment rate also increased during the economic recovery after the end of the crisis. The growing number of older people and people with health problems are particularly at risk of **unemployment becoming entrenched**. These groups find it difficult to return to employment after a job loss.

By **economic sector**, at the beginning of the crisis in March 2020, accommodation and food services, other economic services (such as labour leasing) and construction recorded the largest employment losses (*Bock-Schappelwein – Huemer – Hyll*,

employment contract receiving child care benefit or being in military service.

¹¹ <https://www.bmwfj.gv.at/Services/News/Aktuelle-Arbeitsmarktzahlen.html>.

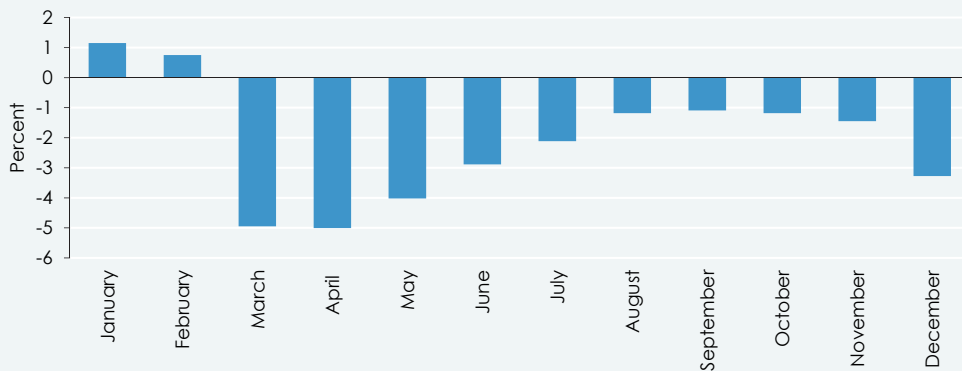
2020A). From April onwards, the contact-intensive sectors of arts, entertainment and recreation as well as personal services also recorded sensitive losses (Bock-Schappelwein et al., 2020B). With the exception of

construction, employment did not reach the previous year's level in any of the mentioned sectors until autumn. At the end of the year, the situation in the contact-intensive sectors worsened again with the second lockdown.

Particular problems arose in the sectors affected by closures. The typical problem groups in the labour market also suffer considerably from the COVID-19 crisis.

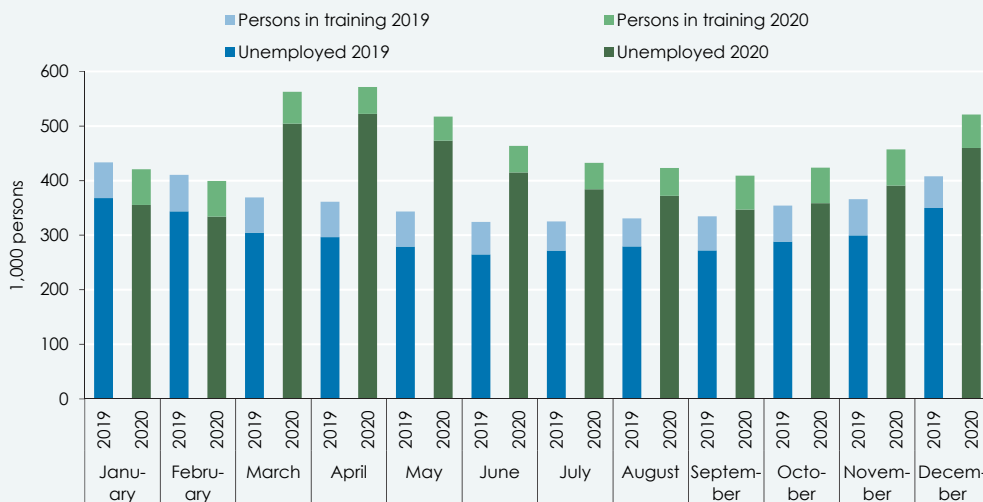
Figure 4: **Development of dependent employment**

2020, change from previous year



Source: Federation of Austrian Social Security Institutions, WIFO.

Figure 5: **Unemployment (including people in training)**



Source: Public Employment Service Austria.

Younger workers (20 to 24 years) were disproportionately affected by the COVID-19 measures. Not only are they relatively often employed in particularly severely affected sectors, but they are also – due to their comparatively short length of service – among the part of the workforce that first loses its job in a crisis. **Young people** up to 19 years of age were particularly affected by the significant decline in the number of holiday jobs offered during the summer (Bock-Schappelwein – Huemer – Hyll, 2020B).

Men lost their jobs with above-average frequency, especially at the beginning of the

crisis (Bock-Schappelwein – Famira-Mühlberger – Mayhuber, 2020). In May and June, men benefitted from the resumption of construction activity. **Women's** job losses, on the other hand, were more concentrated in tourism, which is why they benefitted from the high season in tourism during the summer months. In September, men recorded slightly higher employment losses than women, as they had since the summer, as gains in construction, ICT or public-related services were offset by continued low employment levels in labour leasing and transport. Women, on the other hand,

benefitted somewhat more from increases in public and professional services and ICT.

Blue-collar **workers** lost their jobs disproportionately more often than white-collar workers (including civil servants; *Bock-Schappelwein et al., 2020B*). **Foreign workers**, especially commuters with foreign residence, were more affected than nationals.

The self-employed (especially one-person businesses) are among the most socially affected groups. The gaps in their social protection become clear.

In 2020, the COVID-19 crisis also affected to a large extent **self-employed persons** who work (often as **one-person businesses – EPU**s) in the service sectors that are directly and indirectly particularly burdened by the lockdown. The social protection of this group of people is worse than that of the employed, even though the government is taking countermeasures.

The consequences of the crisis for the self-employed are less evident in employment figures than in **income or turnover losses**, especially in customer-intensive sectors such as catering, personal services, direct sales, leisure, sports, trade, culture and personal care. Based on the sectoral structure of self-employment, WIFO¹² estimates that at least 37 percent of all self-employed persons (34 percent of one-person businesses and 43 percent of self-employed persons employing workers) suffered losses (*Bock-Schappelwein – Mayrhuber, 2020*).

The amount of loss of earnings and the impact of the support measures for the self-employed could not yet be quantified at the end of 2020, as the application deadlines for certain measures (e.g. third tranche of the fixed cost allowance) had not yet expired.

The relative income losses are likely to be generally higher in the case of the self-employed affected by the crisis than for the employed affected, as the replacement rates of the aid measures granted to the self-employed up to the second lockdown were lower than under COVID-19 short-time work. Moreover, the long-term effects of the crisis are particularly important, for example on lifetime earnings and especially on the situation at retirement age. Since COVID-19 assistance, unlike periods of unemployment or short-time work, does not establish partial insurance periods in social insurance, self-employed persons suffer noticeable disadvantages in their pension amount, especially in the case of longer-lasting business closures. A downgrading to the minimum contribution basis also has similar consequences.

The scientific recording of the general **social consequences** of the COVID-19 crisis is only

at the beginning. Initial analyses show that **women** were more affected than men by the newly created challenges in everyday life, such as the need to reconcile home office and home schooling (*Bock-Schappelwein – Famira-Mühlberger – Mayrhuber, 2020*). Women also work more often than men in system-relevant industries, but also more often in industries that were directly affected by lockdowns.

WIFO used microsimulation to examine the effects of the COVID-19 crisis on the **income situation of private households** (*Fink – Moreau – Rocha-Akis, 2020*), but without taking self-employed households into account. The results show a heterogeneous development of disposable household equivalent incomes¹³ according to groups of persons and income classes. For the lowest income quintile, the COVID-19 crisis had the effect of slightly improving incomes, especially since this group includes many people far from the labour force (e.g. pensioners) and the unemployed who had not suffered any loss of income due to COVID-19, but nevertheless benefitted from additional social benefits due to the crisis. However, as income increases, household income losses increase both in absolute and relative terms. However, the measured effects are too small to be reflected in poverty indicators.

Results of this kind require careful interpretation. First, income losses are closely related to crisis-related unemployment. As long as this can be limited by short-time work schemes, too large income losses of a broad stratum of the population can be avoided. This underlines the relevance of short-time work, but also the instability of the economic situation.

Secondly, own information is required to assess the situation of one-person businesses. 50 percent of EPU had to take advantage of subsidies from the hardship fund (*Bock-Schappelwein – Mayrhuber, 2020, p. 220*) – an indication of the precarious situation of this group of people.

In general, there are empirical indications that population strata that were already at risk of poverty before were hit particularly hard by the COVID-19 crisis; beyond that, however, entirely new population strata could slide into **poverty risk**, for example with the EPU (*Heitzmann, 2020*). Reports of people coming to welfare organisations who had never sought help before also point in this direction¹⁴.

¹² The estimates are from August 2020.

¹³ Equivalent household income records the sum of the incomes of the persons living in it for all households, standardised with a needs scale (OECD scale)

according to the structure of the household (size and age of household members).

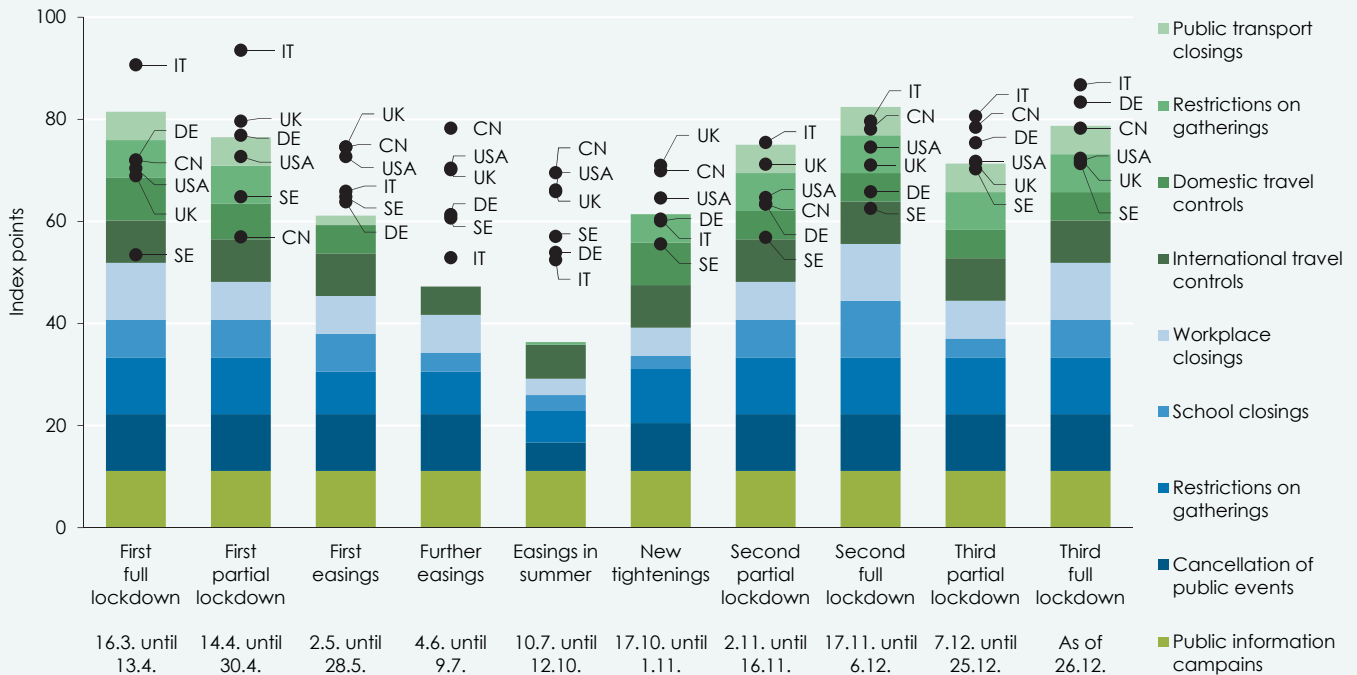
¹⁴ E.g. *Heschl (2020)*.

1.6 Economic policy measures to combat the crisis

While political decisions in March 2020 had clearly given priority to health objectives, economic and health policy aspects were increasingly weighed up as the year progressed due to the worsening economic

situation. This was particularly evident with regard to the situation of tourism businesses, but also to some extent in the case of trade, when towards the end of the year, for example, the need to "save part of the Christmas business" entered into political decision-making processes.

Figure 6: Intensity of lockdown measures in international comparison



Source: Blavatnik School of Government, University of Oxford, WIFO.

As an international comparison of the **intensity of the measures set** shows, in spring 2020 Austria was among those countries that regulated public and economic life the most (Figure 6). From early summer onwards, by contrast, restrictions in Austria were particularly generous, which was also reflected in a relatively favourable development of summer tourism. Even if it seems obvious to cite this as a cause for the strong increase in the incidence of infections in autumn, the descriptive findings alone are not sufficient for scientific proof of this connection. With the gradual tightening introduced from mid-October, Austria again approached the regulatory practice of the comparison countries.

No matter how far-reaching the health policy regulations in Austria may have been, **economic policy** reacted promptly to their economic effects. A complete **overview of the measures taken** is difficult because new measures were repeatedly developed or individual measures were modified in the course of 2020. This also applies to particularly expenditure-intensive areas such as COVID-19 short-time work, which was available in three variants in the course of 2020

and will still be granted in 2021. Figure 7 provides a schematic overview of the different measures.

The measures can be structured both temporally and according to their target groups or primary objectives. At the beginning of the first lockdown, emergency measures were primarily intended to prevent excessively high unemployment and **liquidity bottlenecks** threatening the existence of companies affected by plant closures. Particularly important were the introduction of a new **short-time work scheme ("COVID-19 short-time work")**, but also emergency aid for companies (hardship fund and fixed cost subsidy). These instruments were accompanied by far-reaching **guarantees and liabilities for business loans** as well as reductions and **deferrals** of claims for taxes and social security contributions, initially until the end of September 2020. Subsequently, measures were tightened up (fixed cost subsidy) or supplemented for particularly vulnerable target groups, e.g. for the unemployed, families or for NGOs. Some measures were extended (e.g. deferral of tax and contribution debts, second one-time payment for the

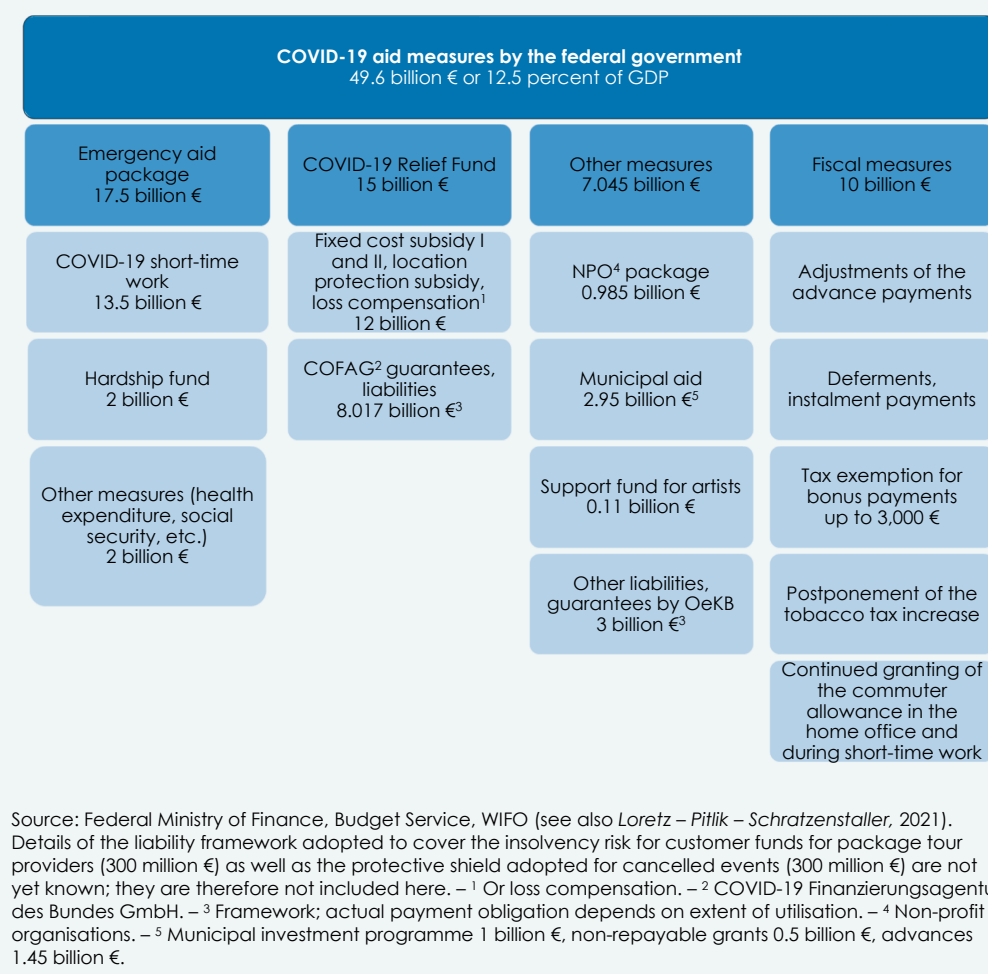
In an international comparison, Austrian policy reacted particularly sharply to the outbreak of the COVID-19 pandemic in spring 2020. In the summer, on the other hand, regulations in Austria were particularly liberal.

Economic policy reacted to the crisis with a comprehensive set of measures; problems emerged in the practical implementation.

unemployed, wage replacement for special care time) and other measures were introduced (turnover replacement for

companies affected by official closures in November and December).

Figure 7: **COVID-19 aid measures at a glance**



The discussion on the various forms of the **fixed cost subsidy** gained particular momentum. It is intended to support companies whose sales have collapsed as a result of COVID-19 measures, either directly (through closures) or indirectly, for a longer period of time by compensating part of their fixed costs through a state subsidy.

The spending programmes were supplemented by **fiscal measures** – beyond the deferral and reduction of taxes and duties. On the one hand, these were aimed at supporting liquidity in certain sectors (e.g. gastronomy and hotel industry, book trade, culture) by temporarily reducing the VAT rate to 5 percent – which was tolerated by the European Commission. On the other hand, the first phase of the wage and income tax reduction already planned by the government was brought forward to January 2020, which involved in particular a reduction of the entry tax rate as well as some accompanying measures for low-income earners. This

was aimed at a general strengthening of purchasing power, with the goal of also providing impulses for consumption. Thus, the COVID-19 aid seamlessly transitioned into an economic stimulus programme.

In connection with the lockdown phases at the end of 2020, various forms of **turnover replacement** were introduced, first a flat-rate replacement of 80 percent of the previous year's turnover for restaurants and tourism businesses, and later – after the lockdown was tightened in mid-November – a turnover replacement differentiated by sector for retailers with replacement rates between 20 percent and 60 percent. After the government had been heavily criticised in spring for delays in the payment of promised support, it was decided in autumn to make a lump-sum payment using the turnover of 2019. Although this allowed for an unbureaucratic processing, it triggered the (in itself justified) criticism of "over-subsidisation"¹⁵, since neither short-time work subsidies nor other

¹⁵ Cf. e.g. *Szigetvari (2020)*.

support payments (e.g. immediate payments, assumption of liability, etc.) nor sales made despite the closure (e.g. through the collection of food) had to be offset against the sales replacement. In this case, the typical regional operating surplus of the previous year could have been used instead of the turnover to calculate the compensation. The turnover replacement expired at the end of 2020; from 2021 onwards, only the fixed cost subsidy and **loss compensation** can be granted.

The municipalities were confronted with a drastic decline in revenues due to the loss of municipal tax revenues and income shares in the course of the tax union. By means of a **municipal investment programme** they received an additional 1 billion € for the co-financing of investments. In addition, non-repayable subsidies of 0.5 billion € (0.4 billion € replacement for revenue shares and 0.1 billion € increase of the structural fund for financially weak municipalities for the year 2021) as well as advances of 1.45 billion €¹⁶ are granted by the federal government to the municipalities.

In addition to the various COVID-19 aid measures, the government put together an **economic stimulus package** in mid-June 2020, which essentially consisted of public investments, primarily in climate protection, as well as an investment premium and some other tax measures to promote investment (declining depreciation) and liquidity support for companies (loss carry back, reduction in value-added tax rates for some industries). In the 2021 federal budget estimate, the COVID-19 aid measures and the economic stimulus package are presented separately, although the two packages of measures cannot be precisely distinguished from each other.

The design and processing of the various aid measures also had an impact on the **economic policy institutions** in Austria. In the first weeks after the lockdown in spring 2020, delays occurred due to massive overloading of the organisations responsible for processing the aid, which led to severe criticism. This affected e.g. the Public Employment Service (AMS), and partly also the banks responsible for emergency aid payments. The disbursement of money from the hardship fund by the Chamber of Commerce was politically controversial. At the beginning of April 2020, the **COVID-19 Finanzierungsagentur des Bundes GmbH (COFAG)** was created and tasked with handling business subsidies.

The COVID-19 crisis resulted in a noticeable **increase in the importance of the social partners**. Not only were they involved in the

design of most of the measures; in important areas, such as COVID-19 short-time work, the design of the instruments was the result of agreement between the social partners. The social partners demonstrated a high degree of responsibility during the crisis. For example, some important wage agreements (e.g. metal industry, trade) were reached in a short period of time.

The longer the crisis lasts, the more the question of **the effectiveness of the economic policy measures** is raised in the political discussion. The package of measures could not yet be comprehensively evaluated by the end of 2020, as important data required for this was missing. However, there is no doubt that the measures already have a great impact due to their scope, especially in comparison with the counterfactual scenario of no state intervention. The social costs in this case would have been dramatically high, considering alone the number of potentially unemployed or the possible insolvencies of companies.

Some attempts at timely economic evaluation of individual measures have been made, however. One example is the brief study jointly prepared by WIFO, IHS and EcoAustria on the **package of measures** presented by the government in **June 2020** (Baumgartner et al., 2020A). The package essentially contained the extension of the fixed cost subsidy, various projects to strengthen private household incomes and to promote investment, as well as some public investments. A smaller part of these measures (a total of 10.3 billion €) could be examined and effects on GDP and unemployment could be demonstrated. If the measures examined had not been implemented, the unemployment rate would have been 0.43 percentage points higher and the value added 0.7 percentage points lower.

A research project by IHS and WIFO is currently investigating the cyclical, fiscal and distributional effects of the most important economic policy measures to cushion the COVID-19 crisis by means of **micro- and macro-simulations** as well as **multi-regional input-output analysis**. Initial results indicate that household disposable incomes were 3.1 billion € higher in total as a result of the support measures than they would have been without them. Real GDP would have been 0.5 to 1 percentage points lower without the measures¹⁷.

An initial assessment of **companies' reactions** to the aid measures was made possible by special surveys conducted as part of the WIFO-Konjunkturtest (business cycle survey)

In the COVID-19 crisis, the role of the social partners gained weight, also through new responsibilities in support measures.

In the second half of 2020, WIFO presented the first studies on the effectiveness of the COVID-19 measures.

¹⁶ A chargeback of these advances is foreseen from 2023 at the earliest.

¹⁷ Rocha-Akis, S. (Project Leader), Economic and Fiscal Effects of the COVID-19 Crisis and

Countermeasures. Micro- and macroeconomic analyses (for description see <https://www.wifo.ac.at/www/pubid/66380>).

In the wake of the COVID-19 crisis, it became clear once again that research needs better access to register data.

in the period between April and August 2020. The COVID-19 short-time work was rated as particularly helpful, the fixed cost subsidy had only been used by a minority of companies at the time of the survey. Liquidity support was heavily criticised, yet it obviously played an important role (Hölzl et al., 2020).

The analyses outlined above illustrate a general finding: in order to comprehensively assess the effects of COVID-19 measures – as well as economic policy interventions in general – research requires unrestricted **access to register data (administrative data)** and other statistics. Unfortunately, this has so far only been ensured to an insufficient extent and there is currently more need than ever for action on the part of the responsible bodies.

1.7 The effect on public budgets

The government provided the announced economic policy measures with a partly very generous budget framework¹⁸. As of the end of 2020, the budgeted sub-items for the various COVID-19 aid programmes added up to a good 49.6 billion € (Loretz – Pitlik – Schratzenstaller, 2021), spread over several years. In addition, there are economic stimulus measures amounting to 11.6 billion € for the years 2020 and 2021 (Federal Ministry of Finance, 2020).

The Federal Ministry of Finance publishes the amounts¹⁹ actually disbursed for the individual programmes on a monthly basis in a separate COVID-19 report²⁰. The **degree of utilisation of the sub-budgets** varies considerably between the expenditure categories. The framework of smaller, more social policy-oriented measures was fully utilised, e.g. for the one-off payment for the unemployed or for the child bonus. Other, very highly budgeted measures were only utilised to a small extent. Due to the settlement mode, payments for the COVID-19 short-time work lag significantly behind the approvals; it is to be expected that an extension of short-time work beyond March 2021 can be partly financed from the budget appropriations approved so far.

The fixed cost subsidy was decided in several tranches and can be drawn down until well into 2021. Only a very small part of the

total budget of 12 billion € was used by the end of 2020, and it is unclear whether it will ever be used in full.

The resulting budgetary leeway allows the government a certain flexibility in planning and implementing measures; this is also provided for in the 2021 federal budget.

The budget margins cannot hide the fact that the **effects of the COVID-19 crisis on public budgets** in Austria are dramatic. The consequences of the political announcement at the beginning of the crisis to provide almost unlimited financial resources to cushion the recession ("at any cost") can be illustrated by macroeconomic data. These show a development that is unique in the Second Republic: while in 2019 Austria had still achieved a **Maastricht budget surplus** of +0.7 percent for the public sector as a whole and a public debt of 70.4 percent of GDP, the situation changed dramatically for the following years: for 2020, WIFO expects a **Maastricht deficit** of –10.1 percent and a public debt of 85.7 percent of GDP in its forecast of December 2020. For 2021, depending on the scenario, a budget deficit of between –5.5 percent and –6.2 percent and a **national debt** of between 85.4 percent and 87.7 percent of GDP are assumed (Schiman, 2021).

Due to the low interest rate level and in international comparison, these values are not dramatic. Nevertheless, it is remarkable that this course was taken by a government that had originally set itself the goal of a balanced state budget and a significant reduction in the tax burden, and had laid this down in the government programme.

Whether the actual budgetary development will correspond to the forecasts depends above all on the duration and intensity of the pandemic in 2021. The WIFO forecasts are based on a "no policy change" assumption for the public sector; policy decisions in the future that are relevant for revenues or expenditures cannot be included. The WIFO forecasts are based on the assumption of a waning of the COVID-19 pandemic in 2021, so that health policy no longer has to set any relevant restrictions on economic activities in the second half of the year.

2. Outlook: economic policy in the period after COVID-19

The most urgent policy task for 2021 is to end the health crisis. The longer the pandemic lasts, the longer relief measures have to be

continued, the greater the economic crisis and the burden on public budgets.

¹⁸ There are two important exceptions to this finding: The allocation to short-time work was clearly too low, especially in the initial phase of the crisis, and was therefore increased several times. Similarly, the high take-up of the investment premium quickly led to the need for a top-up.

¹⁹ <https://www.bmf.gv.at/themen/budget/das-budget/budget-2020.html>.

²⁰ A more detailed analysis of these data is given in a separate article in this issue (Loretz – Pitlik – Schratzenstaller, 2021).

In 2021, however, economic policy will not only be able to deal with repairing the damage caused by the COVID-19 crisis. It will also have to address a number of **fundamental problems of the Austrian economy** were masked for months by the COVID-19 pandemic and whose solution was postponed to the future. The list of issues below is therefore similar to the point made in January of the previous year (*Badelt, 2020, p. 12ff*). Essentially it is about

- to become **more involved in Europe** and to solve the **structural problems of Austria's foreign trade**,
- to reduce the uncertainties created by the COVID-19 crisis and to integrate research and technology policy into a field of **coherent measures to strengthen competitiveness**,
- to counteract a number of other **socio-political undesirable developments** in the world of work besides **long-term unemployment**,
- to further develop the existing approaches in **environmental policy** into a **comprehensive process of transformation**,
- to stabilise **public budgets** again and in the process solve **structural problems** that jeopardise the sustainable development of the public sector.

The **ageing of society** and **digitalisation**, two challenges that shape socio-economic change in society in many ways, run through several fields of action.

2.1 Challenges posed by a new international environment

The international environment of the Austrian economy is undergoing profound change. First of all, this affects the **European Union** itself, which not only has to prepare for the post-Brexit period, but also has to deal with a number of new tasks, e.g. the bond issue envisaged in the European Recovery Plan. In **tax policy**, too, important projects must be pursued further, such as the work on effective taxation of the profits of multinational companies in general and of digital companies in particular.

Also of great importance is the work on **innovative own resources** to be introduced in the coming years to finance the EU recovery fund. For example, the European Commission is to present proposals for a CO₂ border adjustment mechanism and a digital tax by June 2021, to be introduced by 2023 at the latest. Also by mid-2021, a system of own resources based on the European Emissions Trading Scheme (EU-ETS) is to be developed. Further new own resources are to be proposed by mid-2024, which could, for example, be based on a taxation of financial transactions or a harmonisation of the corporate tax base. A proposal for the long

overdue revision of the Energy Tax Directive is also to be developed.

Since the formulation of all these issues has repercussions on Austrian policy, it would be in Austria's national interest to play a committed role in dealing with them. This also applies to efforts to reformulate **fiscal rules**, which will gain momentum due to the effects of the COVID-19 crisis.

Global economic developments also harbour uncertainties and new challenges. The COVID-19 crisis strengthened **protectionist tendencies** that had already germinated in the course of the globalisation discussion, as it showed the disadvantages of an international division of labour that ignores supply risks, for example in the provision of medicines or similarly urgently needed products. The supply problems could be eliminated by a reorientation of **European industrial policy**. The attitudes behind this, however, correspond to protectionist tendencies, as they have been strongly propagated above all by the USA. Even if the Biden administration is likely to deviate from Trump's policy in some respects, an extensive liberalisation of trade relations between Europe and the USA cannot be expected.

Uncertainties regarding further **trade conflicts** and the future of the WTO as well as the further implementation of the Brexit exit agreement, which came into force on 1 January 2021, will continue to weigh on the external economic environment.

The Phase I agreement (*FIW, 2020*) between China and the USA harbours the **danger of trade diversion** for the EU and Austria. In general, the EU has not clearly positioned itself in the competition between the USA and China and has not yet developed a stringent counter-position to **China's** growing **power** – see, for example, the "New Silk Road" project or the "Made in China 2025" strategy.

The Austrian economy will have to come to terms with these new conditions in its export behaviour and serve **new markets** more strongly, **also outside Europe**. Specific foreign trade challenges to be mentioned are above all:

- The **structural problems in the export economy** must be solved, e.g. in the automotive industry or the partly very specialised automotive supply industry, which must adapt to the necessary adjustment processes due to **technological change** (e-mobility). The high degree of specialisation in technologically and economically closely intertwined sectors increases cluster risks in the event of an unfavourable development or a shift in demand. A major increase in the importance of electric drives in individual

The COVID-19 crisis pushed important economic policy issues into the background; they urgently need to be addressed in 2021.

In its own interest, Austria should become more involved in the upcoming economic policy discussions at EU level.

The upcoming challenges on the world markets require a reorientation of Austrian export behaviour.

A counter-cyclical expansion of innovation and R&D funding is necessary.

- transport would therefore not only affect individual product lines in the export basket, but the entire Austrian supplier industry as well as large parts of upstream and downstream industries.
- Ensuring the **resilience of international supply and value chains**, guaranteeing security of supply for critical products and reducing dependence on individual suppliers (supplier countries) do not necessarily have to be achieved by shifting back and shortening supply chains through increased domestic or European production. Broader geographic diversification of supply chains or increased warehousing are also possible.

2.2 New impulses for technology and research policy to strengthen the competitiveness of the Austrian economy

The uncertainty caused by the COVID-19 pandemic and the decline in economic activity will dampen productivity growth in the long term due to the curtailment of R&D spending. Based on the forecast of real GDP and labour volume presented in April 2020, WIFO estimates the **slowdown in R&D investment growth** compared to 2019 at just under 5 percentage points (cf. *Reinstaller, 2020*). According to this, R&D spending by the corporate sector would have roughly stagnated for 2020. However, even a slowdown in growth momentum has a negative impact on the productivity path and employment in the corporate sector. As uncertainty increased again towards the end of 2020, a **counter-cyclical expansion of innovation and R&D funding will prove necessary** to rekindle innovation activities, as hardly any more impetus can currently be expected from interest rate cuts either (*Benigno – Fornaro, 2018, Friesenbichler et al., 2020*).

This points to a fundamental problem for the period after the COVID-19 pandemic is over: Measures by the federal government to ensure liquidity of enterprises and employment should only be understood as bridging and adjustment assistance. Otherwise, there is a danger of the emergence of "**zombie companies**" that will only survive in the longer term with government assistance. Such enterprises draw resources away from healthy parts of the economy and dampen the recovery process and productivity growth. For this reason, too, public funding for basic research and innovation must be expanded and disbursed quickly; in addition, specific funding for investments is necessary to ensure a continuous increase in productivity.

WIFO has also been able to empirically prove that the uncertainty caused by the

²¹ <https://op.europa.eu/en/publication-detail/-/publication/9b64a034-8e58-11e9-9369-01aa75ed71a1>.

²² This primarily addresses low- and medium-skilled workers in occupations with a high proportion of

crisis has a very negative impact on the investment and innovation behaviour of companies and thus on their long-term competitiveness. As several waves of the WIFO-Konjunkturtest (business cycle survey) showed in the course of the crisis, a number of companies intend to postpone or abandon planned investment projects (*Hözl et al., 2020*).

Investment promotion and location policy should therefore be developed into a **coherent strategy between different fields of economic policy** and departments. Export promotion measures should be combined with research promotion as well as with education and location policy approaches. Particular attention should be paid to digitalisation and digital technologies. In practice, this means:

- Digitalisation potentials must be exploited and corresponding deficits eliminated (cf. *Hözl, 2019*).
- Investments in the Austrian ICT infrastructure must be expanded, also via EU programmes. Security concerns and a lack of technological standards, for example, constitute a diffusion barrier for industry 4.0 technologies (*Hözl et al., 2019*)²¹,
- High-risk R&D and innovations – especially those that link different fields of technology and application – are to be promoted.
- Investments in the training of academic and non-academic skilled workers and in increasing the technological competences of employees and pupils must be increased. This includes a re-qualification offensive with a focus on digital skills for people at high risk of unemployment²².
- In addition, location policy is needed to strengthen the competence base. The focus should be on direct investments with potentially high spillover or demonstration effects, which should be flanked by measures to embed companies in the national innovation and production system.

2.3 New focus on the world of work

The COVID-19 crisis caused the most severe problems in the labour market since the post-war period. Experience from past crises suggests that unemployment will remain at higher levels after the crisis ends than before it began. Moreover, the COVID-19 crisis has other effects on the world of work and entails challenges that economic and social policy will have to face in 2021.

The first topic area concerns **long-term unemployment** or, more generally, the solidification of unemployment. On the one hand,

standardised activities or activities that are increasingly supported by the use of AI applications. Therefore, requalification also addresses classic qualified service occupations.

Export promotion must be combined with research promotion and education and regional policy measures; especially with regard to digitalisation.

instruments will be needed to reintegrate the long-term unemployed into the labour market; on the other hand, labour market policy will also have to take **preventive** action: for example, in the area of health policy, through the creation of age-appropriate jobs or incentives that counteract the redundancy of older workers. **Qualification measures** play an important role here, all the more so as Austria still has a considerable **shortage of skilled workers** in some professions. Therefore, it will be necessary, for example, to also provide over 50 year olds with targeted further training in order to equip them with the necessary qualifications for their advanced working age.

The greater the problem of long-term unemployment, the more the need for **direct employment policy** arises, e.g. through **employment projects** with dedicated posts for the reintegration of the long-term unemployed. For some age groups, these projects are of particular relevance: be it for young long-term unemployed in order not to lose the ability to lead an orderly working life; be it for older people in the last years before reaching retirement age. Relevant policy experiments should be tested for their effectiveness instead of discussing measures from an ideological point of view, as was the case with "Action 20,000", for example.

A particular problem area relates to the **future opportunities of young people**. In addition to the general worsening of the labour market situation mentioned in chapter 1.5 (e.g. due to the lack of summer jobs), there was a **shortage of apprenticeship places** in most regions of Austria, which made it difficult for school leavers to access vocational training. Furthermore, children and young people suffered from the **school closures**. These entail high individual and social costs and have a direct (through loss of income) or indirect effect on the further life of those affected. Children at the beginning of formal schooling are likely to be particularly affected, as they need comprehensive support in learning (Bock-Schappelwein – Famira-Mühlberger, 2020). The problem is even more serious for children from educationally disadvantaged families (often with a migration background) who lack the necessary support during the closure phases.

As regular classroom instruction took place on less than half of all school days in 2020, the already existing danger of failing to achieve educational goals, e.g. in writing, reading or mathematics, intensified, especially for these disadvantaged groups (Bock-Schappelwein – Huemer, 2017). This is not only problematic for the further life of those affected, but also for the national economy, which is why it will be important in 2021 to mitigate possible negative long-term consequences of the crisis through **targeted educational offers**.

The **"home office"** system led to challenges of a technical and social nature, raised **labour law issues** revolving around the use of private resources such as computers or mobile phones for official purposes, and created **gender-specific burdens** that carry the seeds of a renaissance of **traditional gender roles**. For example, women are more often exposed to the increased double burden of employment and childcare or home schooling (Mader et al., 2020, Berghammer – Beham-Rabanser, 2020, Berghammer, 2020A, 2020B). Apparently, they also take on the majority of unpaid work during the COVID-19 crisis (Bock-Schappelwein – Famira-Mühlberger – Mayrhuber, 2020).

If home office is also increasingly used after the end of the crisis, this could increase the pressure to face a double burden even when educational institutions are open again. An **emancipatory social policy** aiming at gender equality in working life must increasingly provide incentives to include women in gainful employment, e.g. through the expansion of childcare services or through changes in tax law.

However, the pressure to establish home office workplaces also brought **positive impulses for the digitalisation efforts of companies**. Digital skills and the corresponding technological equipment suddenly came into focus for companies as well as for many workers and families. In this respect, the COVID-19 crisis was also associated with a modernisation push.

Based on the activity profiles of occupations, the **home office potential in Austria** can be calculated. Occupations with a non-manual focus without personal customer contact and with a cognitive routine focus (e.g. office work) are particularly suitable for home office. In 2019, around 45 percent of all dependent employment relationships in Austria are likely to have had home office potential (Bock-Schappelwein – Firgo – Kügler, 2020). This contrasts with actual use: only 22 percent of employees worked from home at least sometimes in 2019. In a European comparison (e.g. Sweden 37 percent), there is thus still room for improvement in Austria – a diagnosis that addresses an important aspect of the **digitalisation strategy in Austria** and should lead to corresponding initiatives (Kügler et al., 2020), admittedly taking into account undesirable socio-political side effects (cf. Bock-Schappelwein – Firgo – Kügler, 2020).

However, the occupations suitable for home office are – depending on the specific bundle of activities – also subject to particular **competitive pressure from "digital migrants"** – i.e. people in low-wage countries who offer such activities via the internet. The COVID-19 crisis could therefore also lead to

Long-term unemployment must be combated through prevention, qualification measures and direct employment policy.

The forms of "home office" that have become popular as a result of the COVID-19 measures are to be shaped with a view to an emancipatory social policy.

Home office can become part of a broader digitalisation strategy; its potential is still partly untapped.

new types of distortions on the labour market (cf. Baldwin, 2019, chapter 5).

2.4 A new start for a comprehensive climate policy

The environment and climate issue took a back seat in 2020 due to the COVID-19 crisis – wrongly so, as the problems have not diminished. Therefore, it is urgent to put a strong focus on a comprehensive climate policy in the upcoming year.

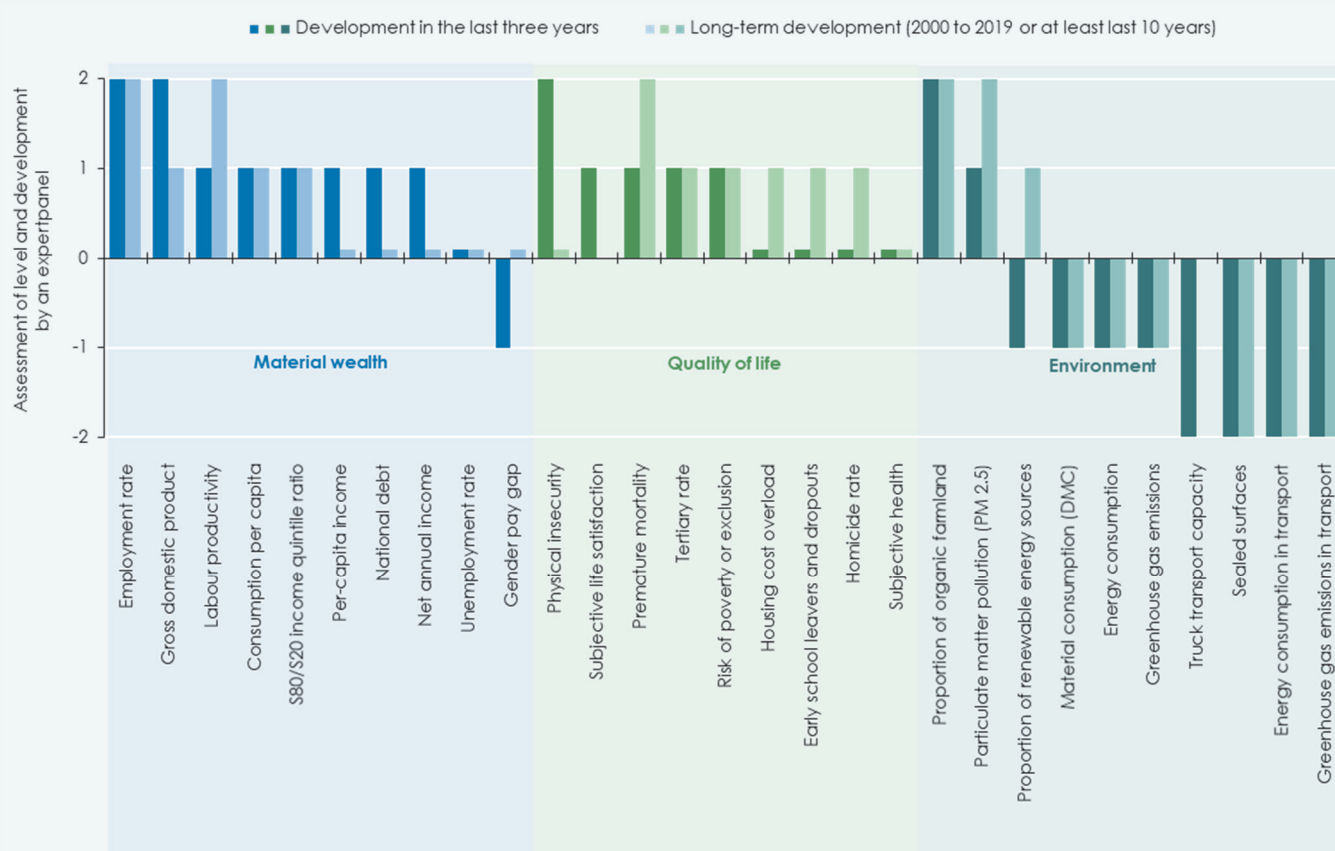
The **initial situation** is critical. The Austrian economy is far from being climate neutral. In 2019, 80.4 million tonnes of **greenhouse gases** were emitted; within 20 years, this value should fall to zero. It is true that the COVID-19 measures reduced production and consumption worldwide, and thus also emissions: in 2020, greenhouse gas emissions

in Austria are also expected to have decreased significantly compared to the previous year (Sinabell – Sommer – Streicher, 2020). However, this effect is not sustainable, as the economic upturn expected for 2021 will again lead to an increase in emissions, as was the case after the financial market and economic crisis of 2008-09 (Köppel et al., 2020).

In an **overall view of the living situation** in Austria, the environmental issue is one of the few factors to be critically assessed, as evidenced e.g. by the indicator set "Wie geht's Österreich" published by Statistics Austria (2020). The set also contains indicators that allow conclusions to be drawn on the causes of greenhouse gas emissions, e.g. on transport, material consumption or soil sealing (Figure 8).

The initial situation of the Austrian economy with regard to greenhouse gas emissions is critical and shows an urgent need for action.

Figure 8: Main results of the indicator set "Wie geht's Österreich" 2020



Source: Statistics Austria (2020, p. 18). Positive values correspond to a favourable rating.

In environmental policy, a comprehensive transformation process of the Austrian economy must be initiated.

At the political level, the initial situation is characterised by an ambitious government programme (cf. chapter 1.2) and by initial priorities in the 2021 budget, which relate to environmentally relevant public investments and the promotion of relevant private investments (investment premium). Building on this, concrete and coordinated activities must now be set up on a broader basis to

initiate a **comprehensive transformation process of the Austrian economy**.

With regard to the market-based steering and incentive effects, the eco-social reorientation of the tax system planned for 2022 by means of introducing a CO₂ price is a key factor. It is important to send out clear **price signals on emissions** and to determine the price development for a longer-term

development path in order to enable companies and households to make corresponding behavioural adjustments that are not detrimental to the competitiveness of the economy. To this end, **fundamental political decisions** are needed, e.g. on the tax bases – including decisions on previous emissions-related taxes – on the level of emissions pricing over time and on the use of the revenues generated by the new taxes. This must be coordinated with the goals for the overall level of the tax burden and for the financing of climate-relevant investments.

Due to the complexity of these issues and the **large number of stakeholders involved**, a **roadmap of the transformation process** has to be designed that also takes into account the institutional specificities of Austria, e.g. the role of the Länder and municipalities, both in terms of responsibilities and in terms of cash flows resulting from fiscal equalisation.

The Länder and municipalities are already implementing a large number of activities that play a decisive role in a transformation process towards sustainability. These include, for example, the planning as well as the expansion of public transport, the promotion of the use of renewable energy sources or forest restoration and afforestation²³. The public sector is also one of the most essential shapers of the transformation process through its own behaviour: the capital stock of the public sector's vehicle fleet, facilities and buildings should be systematically and consistently redesigned towards climate neutrality.

The scope and significance of the transformation process also challenge **empirically oriented research**. While extensive evidence is available on the basic interrelationships surrounding the climate problem, a great deal of research work will have to be done to better substantiate political decisions. This concerns in particular the clarification of (un)intended **effects of environmental policy measures**, e.g. on disadvantaged population groups or competitiveness; the need for restructuring employment or the qualification structure of the labour force will also become apparent. The transformation process should rest on the evidence of an environmental economics research programme.

2.5 New and old challenges for public budgets

The situation of public budgets in 2021 will be significantly determined by the measures taken to overcome the COVID-19 crisis (cf. chapter 1.7). The challenges for economic policy have clearly intensified as a result of the economic crisis.

At first glance, the main issue is how quickly and with what consistency the historically uniquely high Maastricht deficit can and should be brought back to a **balanced budget**. Even if there is no consensus in economics on the necessity of a "zero deficit", there is no doubt that a government financing balance of more than –10 percent of GDP should not be a permanent condition even at the prevailing low interest rate level. It is equally obvious that a deficit cannot be reduced within a few years only by the upswing of the economy if the public sector at the same time takes decisions that lead to an increase in expenditure. The medium-term forecast of WIFO assumes – depending on the further development of the infection, but always under the assumption of "no policy change" – a deficit of between 1.0 and 2.4 percent of GDP for 2025 (*Baumgartner et al., 2020B*).

The situation is similar for **public debt**. The "no policy change" scenario would result in a national debt of between 80.1 and 93.2 percent of GDP in 2025 (*Baumgartner et al., 2020B*). This raises the question of a time horizon for the reduction of public debt, e.g. to the level permitted under the Maastricht criteria.

Even if "growing out" of budget deficits and high debt ratios is made a political maxim, a discussion on future **public spending priorities** would be unavoidable, because both in the context of the COVID-19 crisis and for other reasons there are significant spending needs or at least demands for **additional public spending**.

Many challenges in the wake of the COVID-19 crisis ultimately entail new government spending. This applies, for example, to labour market policy, to research and technology promotion and to many aspects of climate policy; even more so for the latter if the intention is to offset the already slow-growing revenues from a pricing of emissions by reducing other taxes.

In addition, there are other economic and socio-political problems that have been awaiting a solution for a long time. Many of them are related to **demographic change**. These include, in particular, the care problem, but also the question of a justifiable level of public spending on pensions, as well as some aspects of the health care system. To improve competitiveness, investments are needed in research and technology, in the expansion of the infrastructure necessary for digitalisation, and in education, for example

Empirically oriented research on the effects of environmental policy measures should be part of the transformation process.

Fiscal planning for the post-COVID-19 pandemic period needs to begin quickly and should start with priority setting.

Demographic change is causing government expenditure to rise; this must be taken into account in financial planning.

²³ For details, see *Kletzan-Slamnig – Sinabell (2021)*.

to ensure that basic educational goals are achieved and to counteract a shortage of skilled workers.

Of course, the urgency and prioritisation of these expenditure categories is seen differently in different political camps. However, spending in many areas (e.g. pension system) is developing a momentum of its own. Certain issues, such as the care problem, cannot be ignored by politicians. In addition, there is the political goal – also anchored in the government programme – of **reducing the tax ratio**, which is diametrically opposed to the concern of increasing expenditure.

The desired goals of fiscal policy can only be achieved through efficiency increases in the public sector and the necessary structural reforms.

This Gordian knot can only be untied through a discussion of **priorities in government spending** and tasks that also takes into account the unpopular issue of spending cuts in less urgent areas. Spending cuts could lose their political explosive power if efficiency gains can be achieved in the public sector. Such would be achievable not only through the general and often used buzzword of "administrative reform", but also through **structural reforms** that carry inherent incentives for thrift. In the area of federalism, for example, the desired effect could be achieved by merging responsibility for expenditure and revenue, the associated streamlining of tasks and their clearest possible allocation.

The implementation of such structural reforms must overcome political resistance. So far, resistance has been too strong to bring

about actual changes, as can be seen, for example, in the non-implemented reform of the distribution of competences between the regional authorities. Even without a constitutional amendment, however, some improvements could be achieved through a new **financial equalisation system**, which in itself would be up for renegotiation in 2021. Examples of this would be an improved coordination of subsidies, a reform of property tax, a joint approach to care needs planning or a change in municipal financing. Municipal revenues are very cyclical, which means that economic crises have a strong impact on municipal budgets. In the event of external shocks, however, the municipalities are hardly in a position to cope with budget crises on their own. Even if – as politically announced – fiscal equalisation is extended for another year, the time thus gained should therefore be used to negotiate fundamental reforms.

The call for structural reforms in the public sector is a kind of "**ceterum censeo**" of **economic research**. In retrospect, it is clear that this demand has been made very often. However, under the conditions of the initial situation of the public budgets after the COVID-19 crisis, if no structural reforms are implemented, only three ways of rehabilitating the state budget would be conceivable: an increase in taxes, a cancellation or reduction of current expenditures or the acceptance of higher deficits – even in phases of prosperity. All three ways would have to be critically evaluated in terms of their sustainability.

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