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Statement by Mr. Bevilaqua and Mr. Fuentes on Austria
(Preliminary)
Executive Board Meeting
August 30, 2021

We thank staff for the papers and Mr. Just for the helpful statement. While Austria entered the pandemic with solid macroeconomic fundamentals and a strong fiscal position, the crisis hit the country hard causing a sharp contraction in economic activity in 2020 and early 2021. The widespread impact of the pandemic has been mitigated by the authorities' timely and decisive policy response that resulted in a large deficit and a rise in public debt. While a modest and uneven recovery is expected in 2021, additional measures and reforms are warranted to accelerate the recovery and moderate long-term economic scarring.

Policy support is assessed as well-balanced, yet it must remain flexible as the economy regain its footing. Considering the uncertainty associated with the course of the pandemic, we welcome the extension of the targeted support measures to hard-hit sectors in the revised 2021 budget. Moreover, the authorities' Stability Plan (SP) should provide helpful guidance in the transition from emergency measures to recovery over the near-term. Nonetheless, considering the unprecedented and protracted downturn in key sectors such as tourism and hospitality, rushing into a quick budget adjustment may be premature and could hamper the recovery of hard-hit industries. The fact that authorities continue to see less fiscal space than staff for additional measures could be an exacerbating factor in this regard. *Staff comments are welcome*.

The financial system remained resilient but still marred by low profitability and high exposure to sectors highly impacted by the pandemic. The short-term work scheme (STWS) and public loan guarantees effectively eased pressures on household income and corporate liquidity and allowed the banking system to maintain credit flow. As recovery takes hold, closer monitoring and better targeted support to the corporate sector becomes paramount as solvency risks have increased. Similarly, we concur with staff on the need to remain vigilant about the rising exposure of banks to the hospitality and tourism sectors. In that vein, the failure of two small banks and its potential impact to the overall efficiency of the deposit guarantee scheme (DGS) are causes for concern that underscore the need to reinforce auditing and renew commitment to the implementation of the recommendations presented in the 2020 FSAP. Similarly, closer monitoring and stricter enforcement of prudential guidelines to address risks emanating from the housing sector are warranted as house prices continue to rise.

Deeper structural reforms are needed to raise potential output and mitigate scarring from the pandemic. Potential growth in Austria has weakened during the last two decades and is expected to remain around 2 percent into the medium term. In this context, the combination of job disruption from the pandemic and the protracted decline in total factor productivity could lead to higher structural unemployment and lower human capital accumulation. Higher potential output is critical to improve fiscal sustainability, particularly to lower long-term spending pressures from population aging, where further actions are needed to supplement pension reform and strengthen labor force participation. In addition, measures directed to promote digitalization and foster innovation, particularly among SMEs, are warranted to boost labor demand and facilitate resource reallocation.

With these remarks, we wish the Austrian authorities all success in their future endeavors.