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COMMISSION OPINION

of 22.3.2019

on the updated Draft Budgetary Plan of Luxembourg

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(Only the French text is authentic)

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GENERAL CONSIDERATIONS

1. Regulation (EU) No 473/2013 sets out provisions for enhanced monitoring of budgetary policies in the euro area for ensuring that national budgets are consistent with the economic policy guidance issued in the context of the Stability and Growth Pact (SGP) and the European Semester for economic policy coordination.

2. Article 6 of Regulation (EU) No 473/2013 requires Member States to submit annually to the Commission and to the Eurogroup a Draft Budgetary Plan presenting by 15 October the main aspects of the budgetary situation of the general government and its subsectors for the forthcoming year.

CONSIDERATIONS CONCERNING LUXEMBOURG

3. On 15 October 2018, the caretaker government submitted a Draft Budgetary Plan on the basis of unchanged policies, in compliance with Regulation (EU) No 473/2013, on which the Commission issued an opinion on 21 November 2018[1].

4. On 5 March 2019, the new government, which took office on 5 December 2018, submitted an updated Draft Budgetary Plan for 2019. On that basis, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

5. Luxembourg is subject to the preventive arm of the Stability and Growth Pact and should preserve a sound fiscal position which ensures compliance with its medium-term budgetary objective (MTO) of -0.5% of GDP.

6. According to the Commission ad-hoc forecast[2], real GDP growth is estimated to have reached 3.0% in 2018 and is set to decline to 2.5% in 2019. By contrast, the macroeconomic scenario underpinning the updated Draft Budgetary Plan projects real GDP to grow by 3.0% in both 2018 and 2019. Overall, compared to the Commission ad-hoc forecast the macroeconomic scenario on which the updated Draft Budgetary Plan is based appears plausible for 2018 and favourable for 2019 as the government expects real GDP growth around half a percentage point stronger than in the Commission ad-hoc forecast. Luxembourg complies with the requirement of Regulation EU No 473/2013 since the draft budget is based on independently produced macroeconomic forecasts.

[1] Available at: https://ec.europa.eu/info/sites/info/files/economy-finance/c-2018-8021_lu_en.pdf.

[2] The Commission published its winter 2019 forecast (interim) on 7 February 2019. It only includes projections for GDP growth and inflation. In order to assess the updated Draft Budgetary Plan, the Commission complemented its winter 2019 forecast for Luxembourg by a fully-fledged “ad-hoc” forecast, including in particular projections for the general government balance and the structural balance.

7. The updated Draft Budgetary Plan projects a general government headline budget surplus of 2.6% of GDP in 2018 and of 1.0% of GDP in 2019. For 2018, the updated Draft Budgetary Plan's projection is broadly in line with the Commission ad-hoc forecast, which projects a headline surplus of 2.4% of GDP. For 2019, the Commission ad-hoc forecast projects the headline surplus to reach 1.5% of GDP, which is half a percentage point higher than in the updated Draft Budgetary Plan. The difference is mostly explained by the stronger elasticity of public revenues to GDP growth in the Commission ad-hoc forecast. This more than offsets the less favourable macro-economic scenario of the Commission ad-hoc forecast. The (recalculated) structural balance[3] in the updated Draft Budgetary Plan is expected to increase from 1.7% of GDP in 2017 to 2.6% in 2018 and to decline to 0.9% of GDP in 2019. The Commission ad-hoc forecast foresees the structural surplus to increase to 2.4% of GDP in 2018 and to decline to 1.4% in 2019. In the light of the absence of one-offs and temporary measures, differences are explained by the different evolution in the headline balance between the Commission ad-hoc forecast and the updated Draft Budgetary Plan. The public debt-to-GDP ratio is projected to decrease from a level of 23.0% of GDP in 2017, a level well below the Treaty threshold of 60% and the 30% of GDP threshold set by government, in both the updated Draft Budgetary Plan and the Commission ad-hoc forecast.

8. In recent years, the national authorities have pursued sound public finances while still increasing public investment, from a level of 3.5% of GDP in 2013 to 4.1% in 2017. The updated Draft Budgetary Plan factors in the decision to increase retroactively from the start of 2019 the minimum social wage through tax credits, which is expected to have an impact on the labour tax wedge. Previously, a reform of the tax code was enacted at the start of 2017, which reduced the progressivity of the tax system for the lower income and introduced two new marginal tax rates for the highest incomes. Finally, the updated Draft Budgetary Plan provides a list of measures adopted or that are to be adopted to ensure an adequate follow-up to the 2018 Country Specific Recommendations.

9. On 13 July 2018, the Council recommended to Luxembourg[4] an increase of the employment rate of older people with a view to improve the long-term sustainability of the pension system. In order to increase the employment rate of older people the Council recommendation suggests enhancing their employment opportunities and employability and to further limit early retirement. In that regard, the updated Draft Budgetary Plan reports on the adopted reform of the long-term care insurance scheme, which entered into effect at the start of 2018, on the new measures to help people in long-term unemployment, which entered into effect in August 2018, and on the reform of early retirement schemes[5]. It also recalls previously reported measures such as the adopted reform of the professional classification scheme for persons with partial incapacity. Nevertheless, in 2018, the working group on pensions mandated

[3] Cyclically-adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology.

[4] Council Recommendation of 13 July 2018 on the 2018 National Reform Programme of Luxembourg and delivering a Council opinion on the 2018 Stability Programme of Luxembourg, OJ C 320, 10.9.2018, p. 68.

[5] Law dated 30 November 2017. A special scheme allowing people to retire from the age of 57 was abrogated in 2018, but its impact on the average effective retirement age and on expenditure is difficult to assess due an easing of restrictions on other kinds of early-retirement schemes.

by the Government concluded that the pension system appears to be not sustainable, amid high uncertainty levels in the long-term projections at unchanged policies.

10. According to the information provided in the updated Draft Budgetgary Plan, Luxembourg is expected to have achieved a (recalculated) structural surplus of 2.6% of GDP in 2018. This is above its MTO of a deficit of 0.5% of GDP[6]. For 2019, based on the information in the updated Draft Budgetary Plan, the (recalculated) structural balance is expected to decline to a surplus of 0.9% of GDP, still above the MTO. The Commission ad-hoc forecast projects the structural balance to reach a surplus of 2.4% of GDP in 2018 and of 1.4% in 2019. Therefore, Luxembourg is assessed to be compliant with the requirements under the preventive arm of the Stability and Growth Pact.

11. Overall, the Commission is of the opinion that the updated Draft Budgetary Plan of Luxembourg is compliant with the provisions of the Stability and Growth Pact. The Commission invites the authorities to implement the 2019 budget.

    The Commission is also of the opinion that Luxembourg has made limited progress with regard to the fiscal dimension of the Council Recommendation of 13 July 2018 in the context of the European Semester and thus invites the authorities to accelerate progress. There is a comprehensive description of progress made with the implementation of the country-specific recommendations in the 2019 Country Report published on 27 February 2019 and the Commission will assess that progress in the context of the country-specific recommendations it will propose in June 2019.

Done at Brussels, 22.3.2019

For the Commission
Pierre MOSCOVICI
Member of the Commission

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[6] MTOs are to be revised every three years. Based on an agreed methodology, the Commission computes a minimum MTO for each country. The minimum MTOs provide a lower bound for the national structural balance targets, which ensure the sustainability of the public finances, including the projected impact of ageing, or rapid progress towards sustainability, while providing a safety margin with respect to the 3% of GDP Treaty reference value. Due to the more favourable estimation of its sustainability components (age-related expenditure, debt) in the 2015 Ageing report, the new minimum MTO for Luxembourg declined significantly, from a structural balance surplus of 0.5% of GDP to a deficit of 1% of GDP. However, given that Luxembourg is bound by the provisions of the Fiscal Compact, a deficit of 0.5% of GDP is considered as a general minimum MTO requirement. With the 2016 Stability Programme Luxembourg decided to revise its MTO from a surplus of 0.5% of GDP to a deficit of 0.5% of GDP for the period 2017-2019.