



Independent Authority
for Fiscal Responsibility

Report on the General Government draft budgets and main budgetary lines: Draft State General Budget 2016

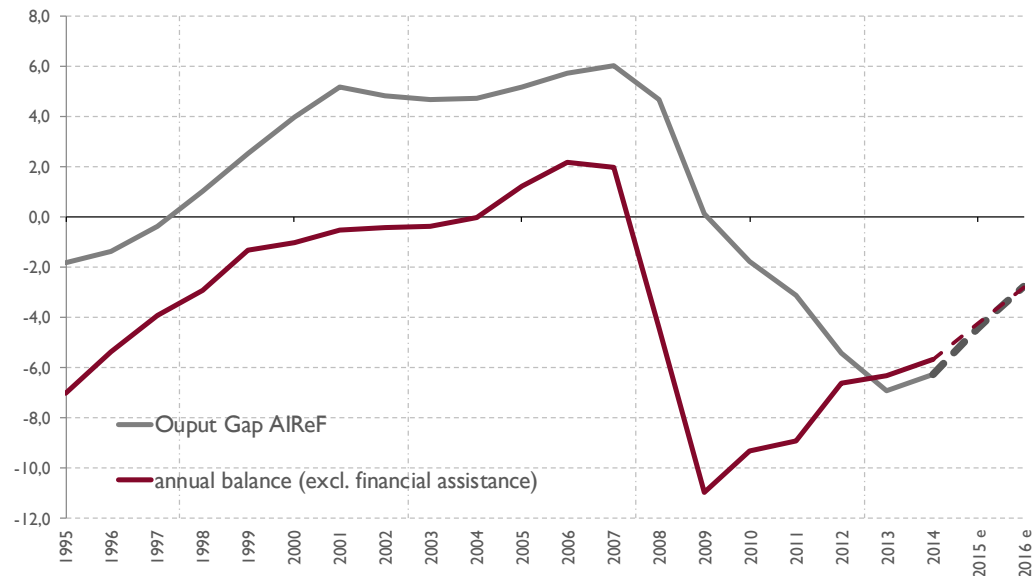
Contents

1. Macroeconomic context
2. Budget stability target
3. Government debt target
4. Expenditure rule
5. AIReF's recommendations

1. Macroeconomic context

The cyclical upturn makes it easier to achieve very demanding deficit targets....

Graph I. Spanish economy output gap and annual balance for General Government sector (excl. financial assistance to banks)



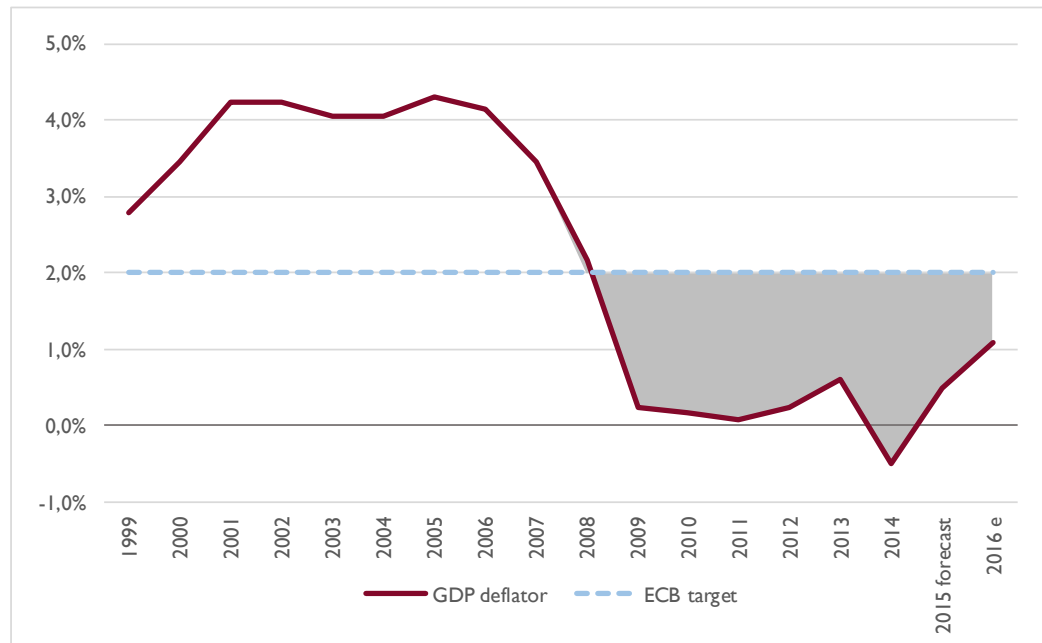
Source: IGAE and AIReF

Deficit reduction 1.5% of GDP in 2015 and 1.4% in 2016.

1. Macroeconomic context

...but the exceptionally low inflation environment is limiting the recovery of government revenue,...

Graph 2. Annual trend for GDP deflator Spain and ECB pricing target

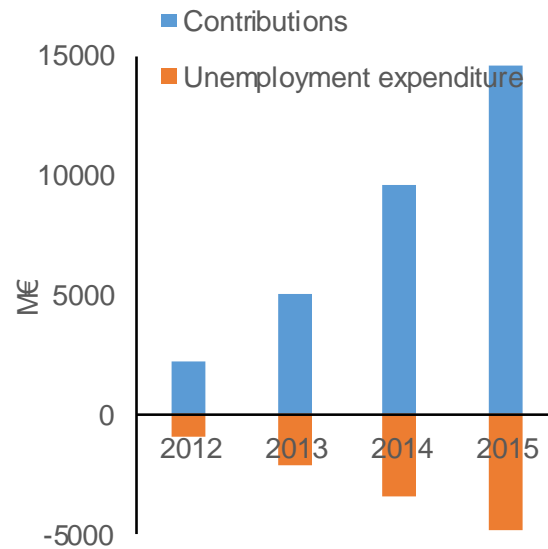
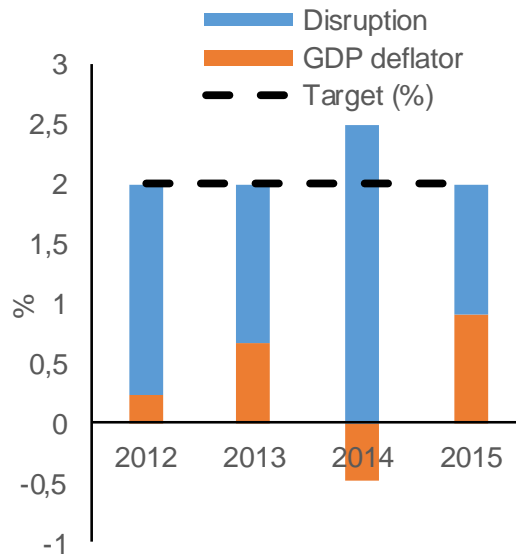


Source: INE, AIReF and FUNCAS

Price trend below the ECB target (2009-2016) accumulates a differential of 12 percentage points in the period.

1. Macroeconomic context

...especially in the case of the Social Security

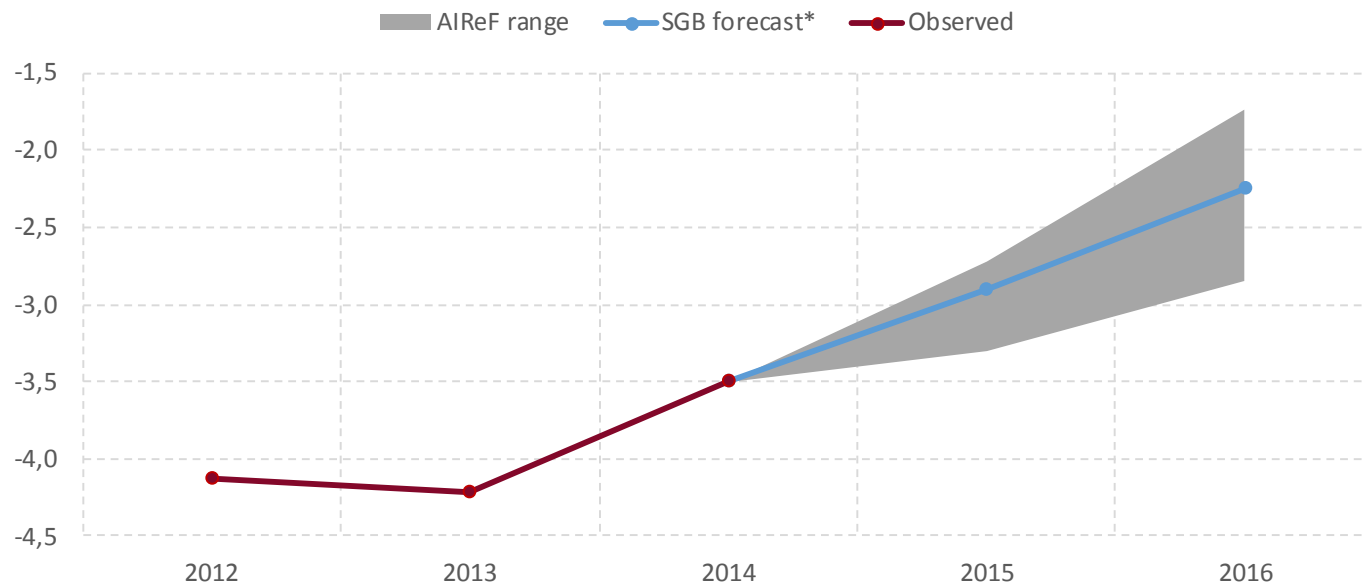


If inflation had developed in line with the ECB target it would have meant almost €15 billion in additional revenue between 2012 and 2015, offset by higher expenditure on unemployment amounting to €5 billion due to the increase in contribution bases.

2. Budget stability target: Central Government

The 2016 deficit target (2.2% of GDP) is achievable

CENTRAL GOVERNMENT. Annual balance (% GDP)

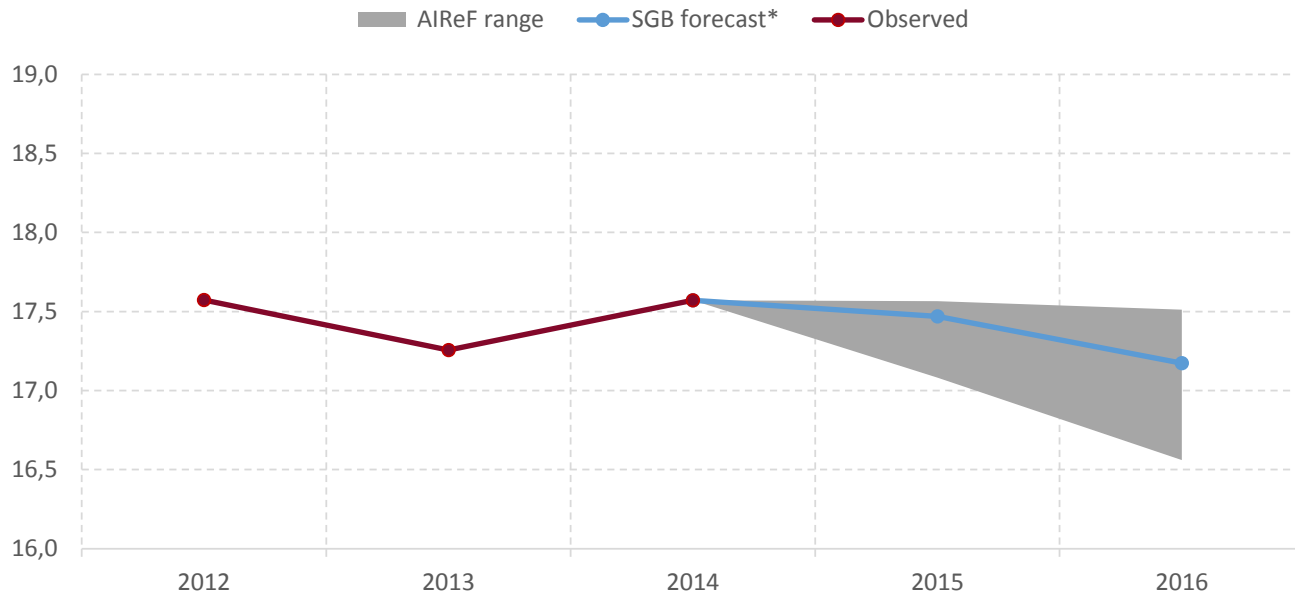


Source: State General Budget (SGB), IGAE and AIReF

2. Budget stability target: Central Government

Growth in revenue seems plausible overall

CENTRAL GOVERNMENT. Non-financial resources (% GDP)

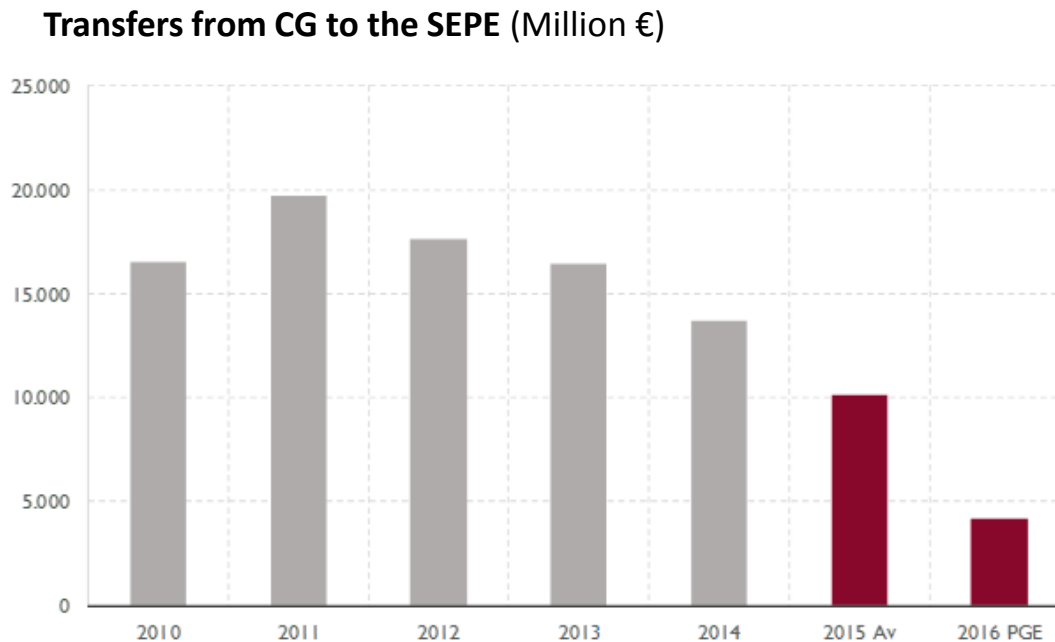


Source: State General Budget (SGB), IGAE and AIReF

The economic recovery is driving higher revenue collection despite the effects of the tax reform.

2. Budget stability target: Central Government

The reduction in expenditure on unemployment allows transfers to the SEPE to be reduced



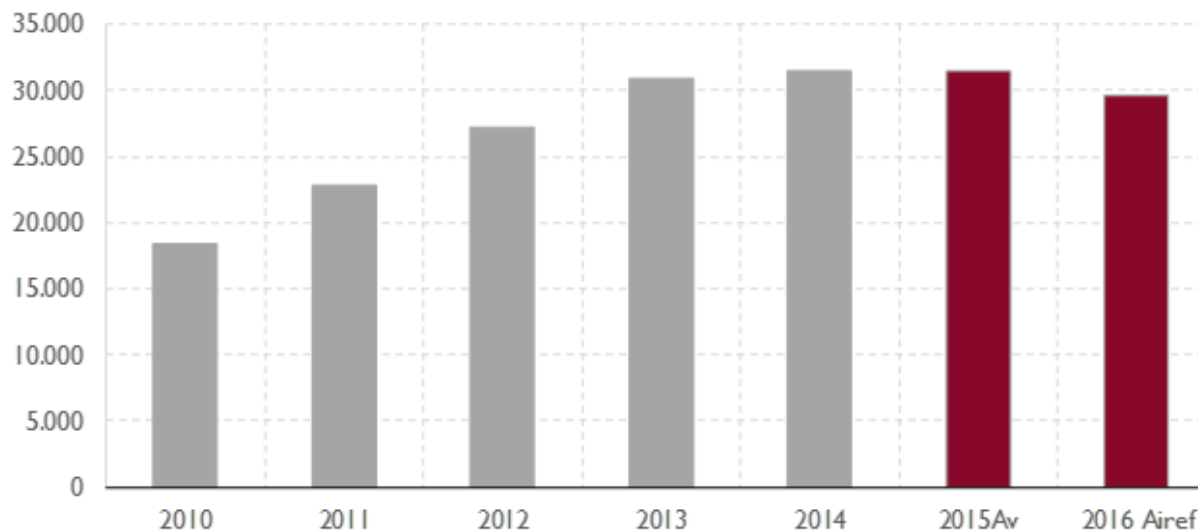
Source: State General Budget (SGB) and IGAE

This decrease is partially offset by the increased funds received by regional and local governments

2. Budget stability target: Central Government

Financial expenses (interest payments) fall 5.9% compared to the 2015 settlement projection in line with AIReF's estimates

Central Government interest payments (Million €)

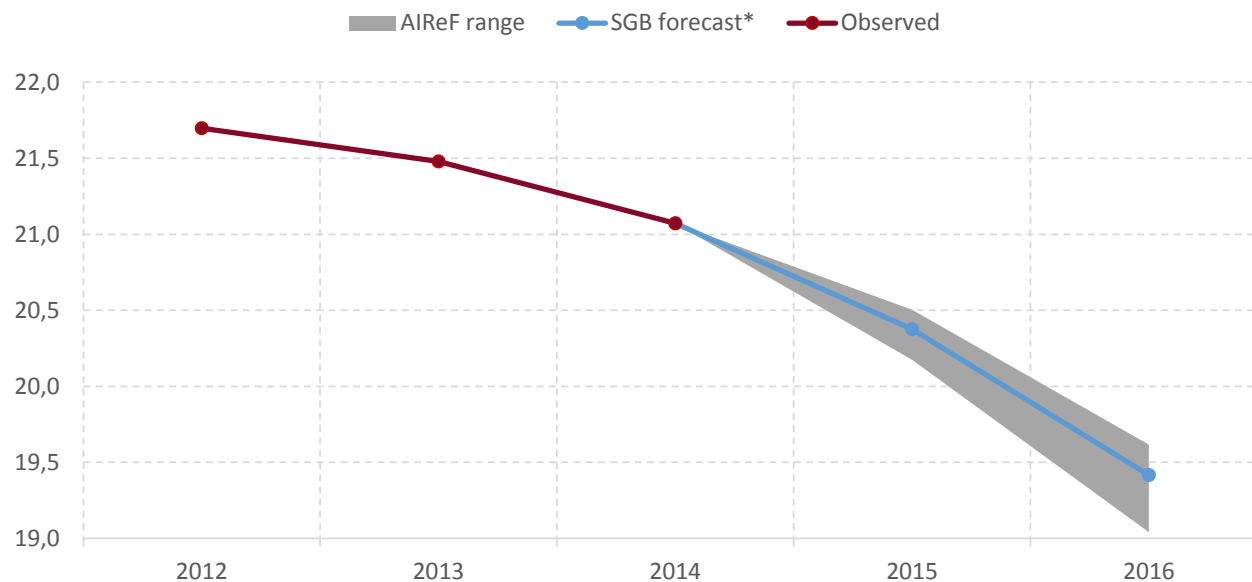


Source: State General Budget (SGB), IGAE and AIReF

2. Budget stability target: Central Government

Implementation of all other expenditure must keep strictly to budget

CENTRAL GOVERNMENT. Non-financial resources (% GDP)



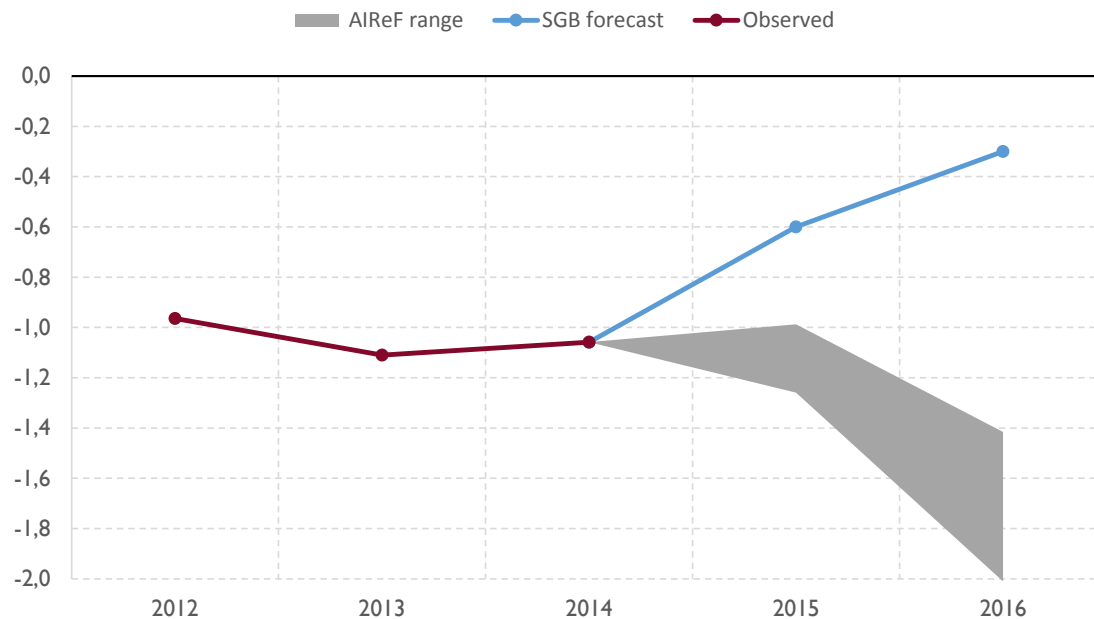
Source: State General Budget (SGB), IGAE and AIReF

All other expenditure (employee compensation, Intermediate consumption and investment) growing in line with GDP.

2. Budget stability target: Social Security Funds

The possibility of non-compliance with the target for 2016 is very high, with a more than 1% GDP deviation.

Social Security Funds (SSF) balance (% GDP)

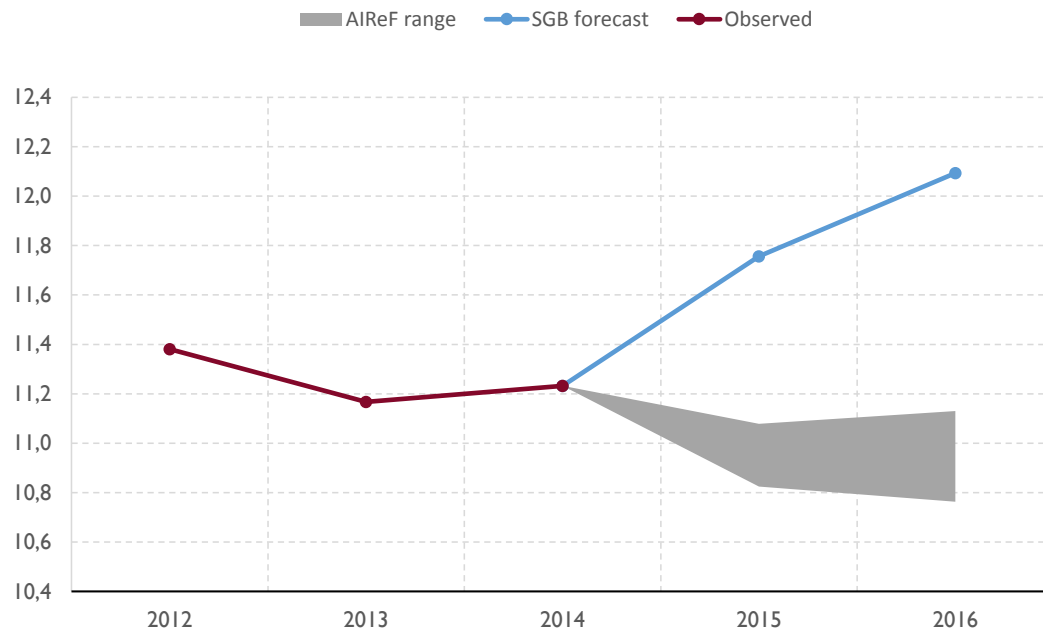


Source: State General Budget (SGB), IGAE and AIReF

2. Budget stability target: Social Security Funds

Revenue is very likely to develop substantially below the forecast

Social Security Contributions (% GDP)



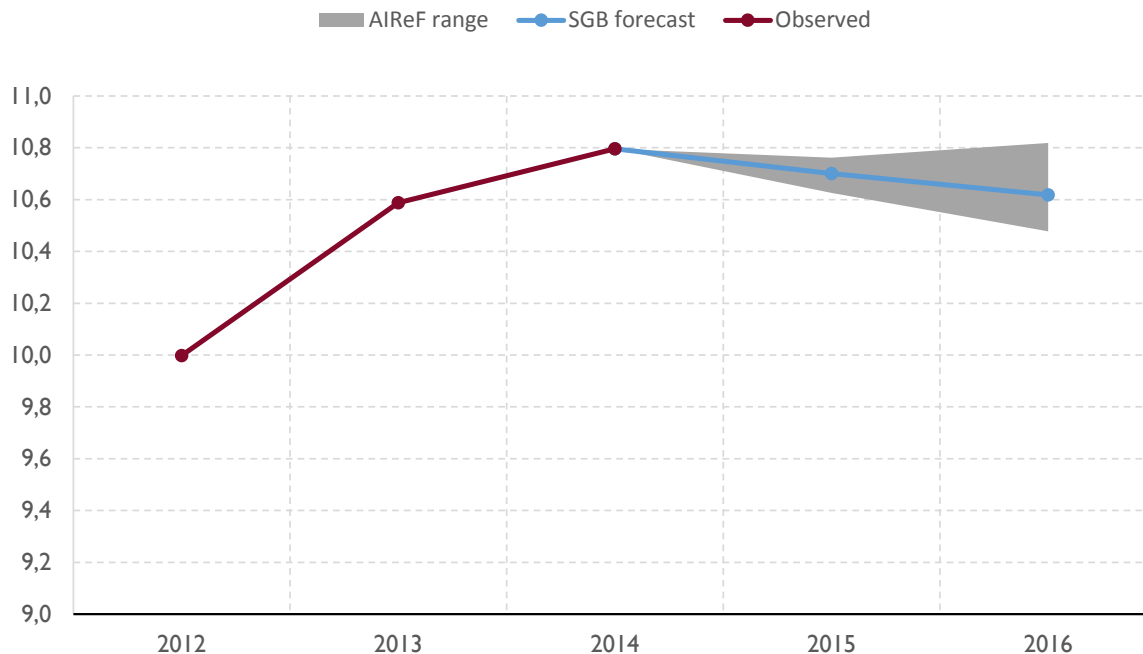
Source: State General Budget (SGB), IGAE and AIReF

Contributions are impacted by the effects of low inflation, low employment and the employment stimulus measures.

2. Budget stability target: Social Security Funds

Forecasts for expenditure on pensions seem well-assessed

Expenditure on Pensions. (% GDP)



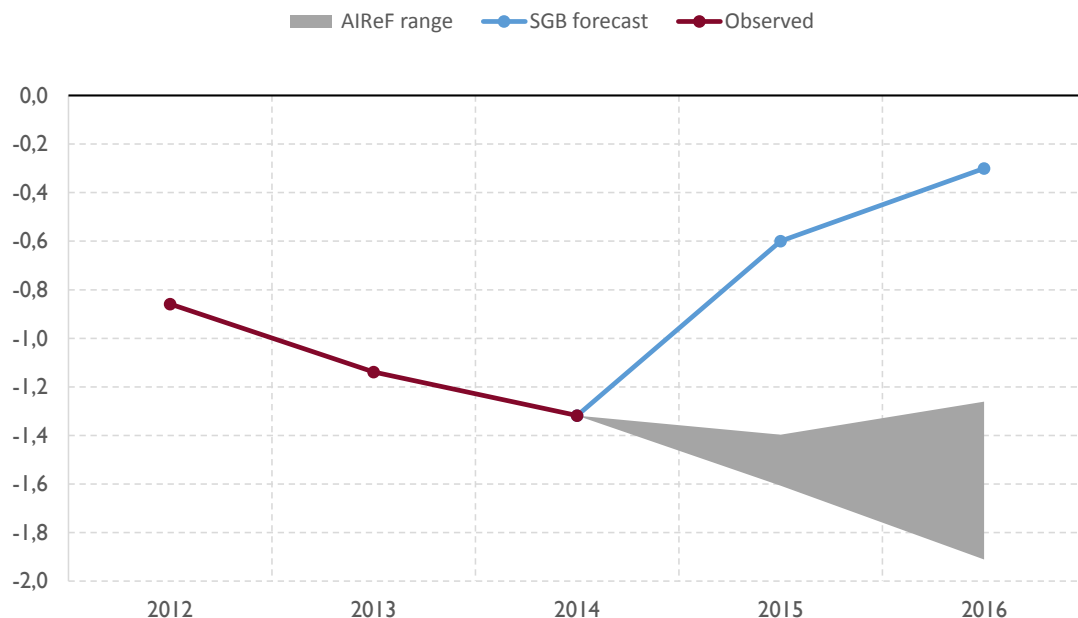
Source: State General Budget (SGB), IGAE and AIReF

Expenditure on pensions continues to grow at close to 3% despite being curbed by the application of the PRI.

2. Budget stability target: Social Security Funds

The Social Security system deficit is stabilising, but...

Social Security System (SSS) balance (% GDP)



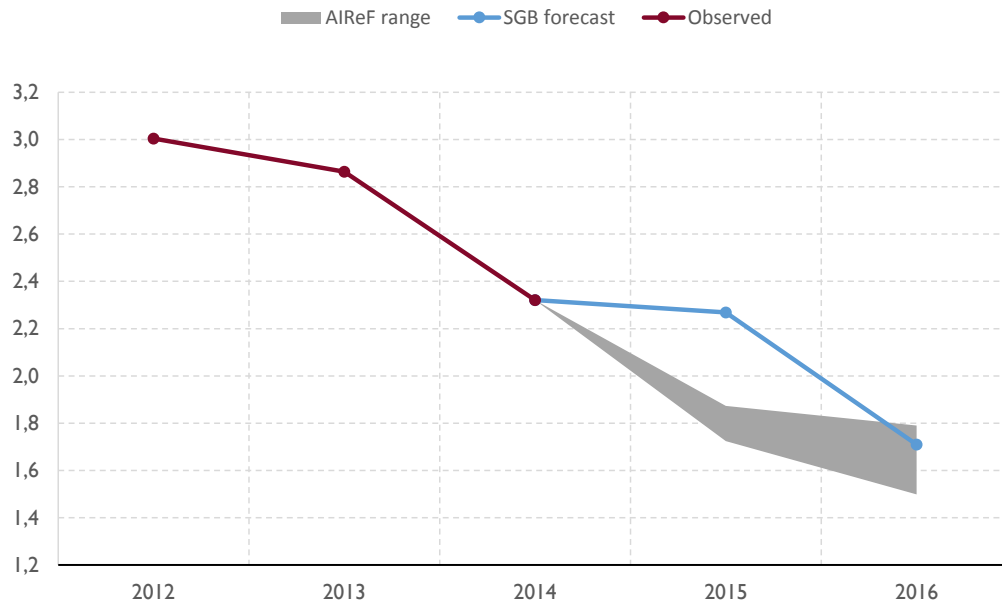
Source: State General Budget (SGB), IGAE and AIReF

It is unlikely that the Social Security System can progress towards budget stability in the next few years.

2. Budget stability target: Social Security Funds

...the Central Government's transfer to SEPE is brought into line with forecast needs and its surplus of previous years disappears

Expenditure on Unemployment. (% GDP)



Source: State General Budget (SGB), IGAE and AIReF

Expenditure on unemployment is reduced both because of the improved employment rate and exhaustion of benefit entitlements

2. Budget stability target: Social Security Funds:

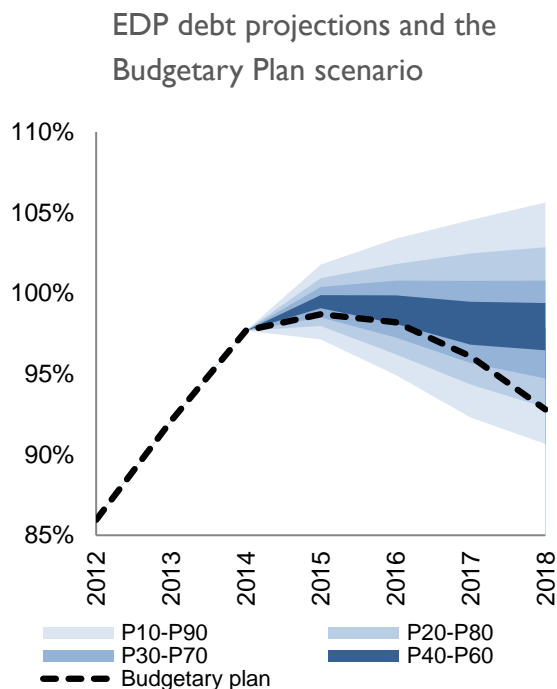
Social Security Funds recommendation

Actions should be taken with the aim of developing Additional Provision Sixty-five in the 2016 Budget Bill and guaranteeing the compatibility between the budget stability targets approved for the Social Security Funds and the funding of the benefits included in the System.

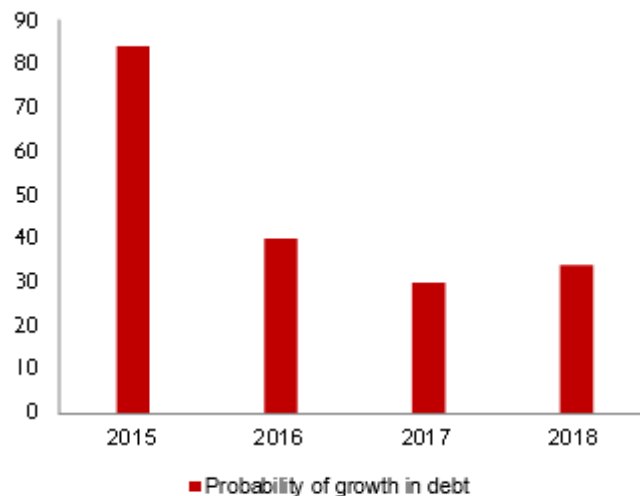
- ❖ The Social Security Funds target will be difficult to achieve.
- ❖ The Social Security system has very few drivers available to it to boost revenue collection in the short-term and its expenditure is determined by legislation
- ❖ The pensions reforms that have been approved (parametric reforms and PRI) are very relevant but their effects are still limited as insufficient time has gone by for their full development.

3. Government debt target

The level of government debt forecast is in line with AIReF's estimates although a gradual downward deviation is observed at the end of the period



Probability associated with growth of government debt compared to its level the previous year



Source: Ministry of Finance & Public Administrations and AIReF



4. Central Government expenditure rule

With the information available in the Draft SGB 2016 a risk of non-compliance with the expenditure rule set at 1.8% is observed for the following reasons:

- The deviations in 2014 (health cent) and 2015 (tax reform) have to be absorbed.
- In 2016 there is once again a negative impact of the tax reform amounting to 0.34% of GDP that will have to be offset with lower spending.
- Additionally, the eligible expenditure for the purposes of the expenditure rule represents less than 50% of the total non-financial uses of the Central Government which includes items for which there is no leeway for action such as pensioners, supplements to minimum benefits and other benefits, or the contribution to the EU budget (10%).
- For these reasons compliance with the expenditure rule for the Central Government in 2016 is more restrictive than compliance with the stability target

5. AIReF's recommendations

Budget stability target

- Actions should be taken with the aim of developing Additional Provision Sixty-five in the 2016 Budget Bill and guaranteeing the compatibility between the budget stability targets approved for the SSF and the funding of the benefits included in the System.

Government debt target

- More complete information should be given in the Draft SGB so that an assessment can be made specifically of compliance with the debt target by the Central Government.

Expenditure rule

- Inclusion in the SGB draft of all the necessary information required to determine the variation in the eligible expenditure in the Central Government. Normative development of the content of article 12 of the LOEPSF.
- Creation of working groups in the CPFF and CNAL to debate and prepare a paper setting out the research done and its conclusions.

Other recommendations

- An initial budget should be drawn up in national accounting terms for the CG and the SSF and forecasts of settlements for the current year for the SSF.
- The SGB should include information on the entities that are not public entities but that are still included for the purposes of ESA 2010 in the CG subsector.
- The SGB should include sufficient information required to make the PRI calculation.



www.airef.es

 [@AIReF_es](https://twitter.com/AIReF_es)