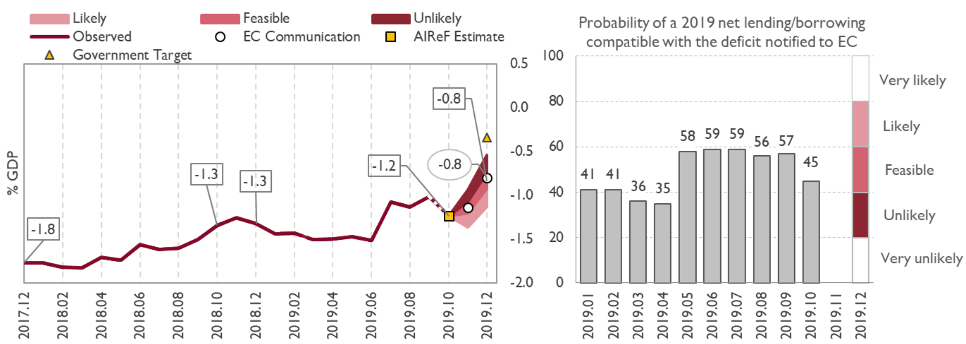
05 December 2019

Monthly monitoring of the stability target

B. Central Government (CG) October 2019

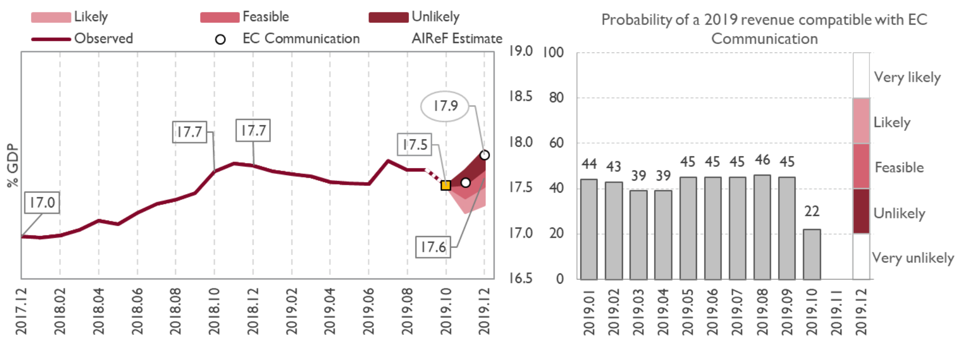
FIGURE 1. NET LENDING/BORROWING



(*) The second deficit and debt notification, sent to the European Commission on September 30 included a forecast for 2019 that reflected a deficit of 0.8% of GDP for the Central Government.

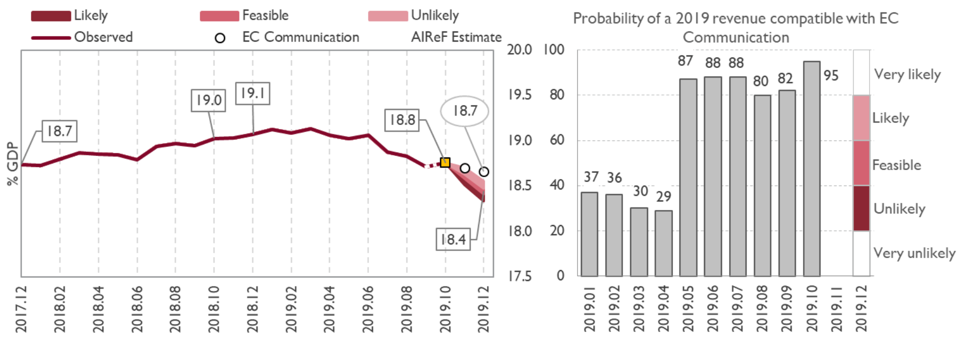
- Compliance with the deficit notified to the European Commission (EC) (*) of 0.8% GDP is considered feasible, introducing significant changes since the last report mainly on the revenue side.
- In 12-month accumulated terms the deficit-to-GDP ratio decreases by 0.1% in September compared with the end of 2018 to 1.2%. This reduction is primarily explained by a higher containment of expenditure than the loss of revenue.

FIGURE 2. NON-FINANCIAL RESOURCES



- AIReF considers it unlikely to comply with the revenue forecasts of 17.9% GDP, at the end of the period, compatible with the 2nd Notification to the EC.
- This lower probability is due primarily to the evolution of the second instalment payment of CIT, which has been much lower than expected, and, to a lesser extent, the revision of the forecasts of special taxes and VAT.
- AIReF estimates that at the end of the year, revenue will stand at 17.6% GDP.

FIGURE 3. NON-FINANCIAL EXPENDITURE



Source: IGAE and AIReF's estimates The AC figure for the current month is estimated based on the data published by the State for this month, through a time-series econometric model.

- AIReF deems it highly likely to comply with the expenditure level of 18.7% GDP that is compatible with the 2nd Notification to the EC.
- In 12-months accumulated terms, expenditure has reduced 0.3% with respect to 2018, a trend that will continue until the end of the year driven by the effect of the Order regulating the budgetary closure of 2019.
- The reduction in expenditure expected in the last months of 2019 is explained by the effect of non-recurrent items recorded in late 2018 that will not be recorded in 2019 or will be recorded in a lesser amount, such as the impact of the DTAs, and by the different pace of execution of such items as contributions to the EU and the rebates of maternity leave.

Assumptions and Notes on Monthly Monitoring

- AIReF's forecasts for non-financial revenue, non-financial expenditure and the fiscal balance are updated monthly, considering the results of its own models for taxes and interest and the national accounting data available up to the current month.

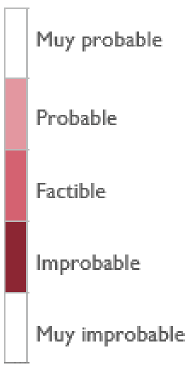
- The figures represent the fiscal balance, revenue and expenditure of the last twelve months accumulated as a percentage of GDP. The expenditure data excludes financial aid. The forecasts are conditioned by the updates continuously carried out by General Intervention Board of the State Administration (IGAE) on the GG Accounts.

- The deficit target of -0.3% GDP was set by the Council of Ministers on 07 July 2017. The first deficit and debt notification, sent to the European Commission on 30 March 2019, included a 2019 deficit forecast that reflects that the deficit foreseen for the CG is greater than the target approved, standing at -1% GDP. Subsequently, the Stability Programme Update sent in April 2019 foresees a deficit for the CG of -0.5% GDP. Finally, the second deficit and debt notification sent to the European Commission on 30 September includes an expected deficit of -0.8%. The analysis of probability is relative to compliance with the forecast of the second notification to the European Commission.

- As there is no official revenue and expenditure path in national accounting terms for the CG, an estimate is made considering that the differences between the cash forecasts for the revenue estimated by AIReF and those forecasted in the draft GSB for 2019, excluding the effect of the measures not in force, are shifted to revenue in national accounting terms and that the expenditure is adjusted as necessary to comply with the deficit notified.

- AIReF's updated forecast and the official forecast of the fiscal balance, revenue and expenditure by month apply the same weights as assigned by the ARIMA Tramo Seats projection to each month for each of these components, considering the effect of both seasonality and series trends.

- Confidence intervals are obtained in two stages. First, a VAR model is estimated for the following variables: (i) sub-sector specific variables, such as expenditure, revenue and government debt-to-GDP ratio; and (ii) common variables referring to the national aggregate: real GDP, GDP deflator and ten-year government bond yields. Second, using projected trajectories for the different variables and the estimated joint distribution of VAR shocks, 15,000 probabilistic scenarios are constructed. The intervals shown have been used to assess the achievement of targets according to the following probabilities:



80-99%: compliance highly likely.

60-79%: compliance likely.

40-59%: compliance feasible.

20-39%: compliance unlikely.

0-19%: compliance highly unlikely.