

REPORT ON BUDGETARY EXECUTION, PUBLIC DEBT AND THE EXPENDITURE RULE 2020

REPORT 3/20





Autoridad Independiente
de Responsabilidad Fiscal

The mission of AIReF, the Independent Authority for Fiscal Responsibility, is to ensure strict compliance with the principles of budgetary stability and financial sustainability contained in article 135 of the Spanish Constitution.

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EXECUTIVE SUMMARY

The purpose of this report is to analyse the budgetary execution, public debt and expenditure rule of the different Public Administrations (PAs) in 2020. AIReF had previously analysed the situation of the PAs in the context of the current COVID-19 crisis in the Report on the Stability Programme Update (SPU) 2020, published in May. However, this is the first time since the beginning of the crisis that this institution has given its opinion on the situation of each of the Regions and Local Governments (LGs) subject to individual monitoring.

On this occasion, AIReF is updating its macroeconomic and fiscal forecasts in a context that is still highly uncertain, both in the healthcare field and in the economic and fiscal spheres. Although the hardest part of the health crisis has been overcome and the de-escalation of the lockdown has been completed with the end of the state of alarm, the health crisis still persists with strong uncertainty about its future development and its repercussions on economic activity and the activity of the PAs. For this reason, it is not possible to resume AIReF's traditional approach of assessing the probability of compliance with the targets, therefore the analysis framework initiated in the previous report with two alternative scenarios is maintained. These scenarios offer an overview of the main variables which, in the current context, are still difficult to quantify, but help to identify the channels of transmission of the crisis, which is essential for designing measures and strategies.

For this report, AIReF has considered the data published on the economic situation, the budgetary execution of almost the entire first half of the year, the new measures approved by the governments, the information provided by each of the administrations and the data sent by the Ministerio de Hacienda (Ministry of Finance) with a bearing not only on the result of the Administración Central (Central Government - CG), but also on that of the rest of the sub-sectors.

How has the macroeconomic scenario evolved?

AIReF has updated the macroeconomic scenario for the period 2020-2021 published in May. In line with many other national and international institutions and organisations, AIReF has lowered its estimates for the contraction of economic activity in 2020 to a fall in GDP of between -10.1% and -12.4%, depending on the duration of the pandemic, compared to the previously estimated -8.9 and -11.7%. This revision is mainly due to the greater contraction of GDP estimated for the second quarter of 2020, due to the adverse evolution of some activities of high importance in Spain's productive structure, which continue to be very negatively affected by social distancing measures and the decline in international tourism flows.

An incomplete and moderate recovery is expected in 2021. The need for social distancing measures to remain in place until an effective drug or vaccine is available, together with other factors such as the predominance in the productive structure of activities with greater social interaction, the seasonality of employment and a business demography with a greater number of small and medium-sized enterprises that are more vulnerable to financing difficulties, mean that a moderate recovery can be expected. And all this in a context where the pandemic is still spreading globally, which will undoubtedly affect the speed of global recovery. At the national level, the scenario of continuous outbreaks may end up affecting the confidence of families and companies, hindering the reactivation of consumption and employment.

How has AIReF changed its budgetary scenarios?

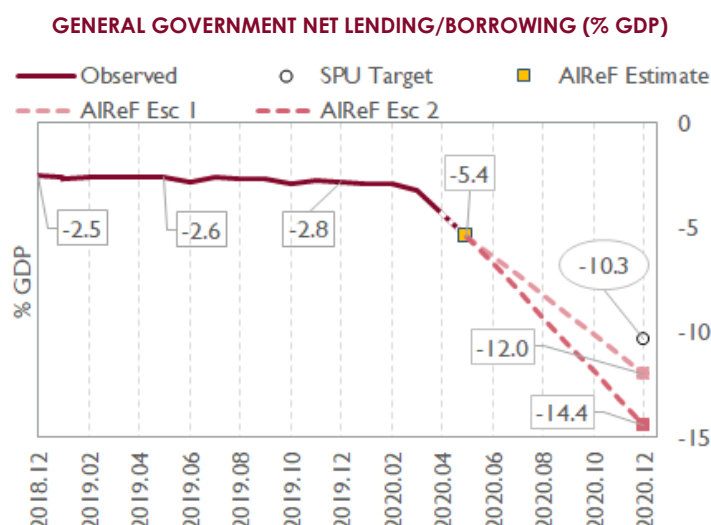
AIReF estimates a PA deficit of 11.9% for 2020, which could reach 14.4% if the most adverse scenario materialises. With respect to the previous report, AIReF has increased its deficit estimate by 1% in Scenario 1, mainly due to new measures approved by governments, and, to a lesser extent, to the revision of macroeconomic forecasts. The revision is smaller in the more adverse scenario, 0.6% of GDP, and is essentially due to the new measures.

Since the publication of the previous report, governments have continued to approve new measures or extend existing ones to mitigate the effects of the COVID-19 crisis, resulting in a deficit increase of 0.8% or 0.6% of GDP depending on the scenario. These measures include the central government's approval of the Minimum Living Income, the extension of the validity of ERTes (Expediente de Regulación Temporal de Empleo - Temporary Redundancy Plans) and the extension and reformulation of benefits for the self-employed. Likewise, the territorial administrations have also adopted new measures and the estimate of the impact of the crisis on health expenditure has been updated.

The revised macroeconomic scenario entails a further deterioration of the deficit by 0.2% of GDP in scenario 1. On the one hand, the lower projected GDP implies an increase of the deficit's weight over GDP by 0.1 % due to the reduction of the denominator. On the other hand, revenue projections have been revised downwards in line with the new scenario and with the collection data known to date, while the forecast of a further fall in employment has meant that unemployment expenditure has been revised upwards. In scenario 2, the downward revision of GDP has a composition with varying effects on fiscal variables, so there is no increase in the deficit despite lower projected growth.

PA revenue will be 40.3% of GDP in 2020 if either scenario materialises. This is an upward revision compared to the previous report because, according to the information published by the Intervención General de la Administración del Estado (General Intervention Board of the State Administration - IGAE), the exemption from social contributions granted by ERTes and for the self-employed are not considered to be lower revenue in the National Accounts (NA), but rather higher expenditure on subsidies. Excluding this accounting effect, revenue has been revised downwards by 0.2% of GDP in scenario 1 since the last report, while it remains unchanged in scenario 2. Personal Income Tax (PIT) collection is performing better than expected, but it does not offset the downward revision in VAT, Corporate Income Tax (CIT) and Special Taxes resulting from the published performance data and the incorporation of the review of the macroeconomic scenario.

Meanwhile, PA expenditure will reach 52.2% of GDP in scenario 1, rising to 54.8% in scenario 2. In addition to the aforementioned effect of accounting for exemptions from social security contributions as expenditure on subsidies, the new measures approved and the increase in the estimate of the impact of COVID-19 on health expenditure in the Regions have also raised the expenditure forecast.



What changes have occurred at the sub-sector level?

The distribution of the impact of the COVID-19 crisis by sub-sectors has changed substantially since the publication of the previous report, with the CG assuming part of the deterioration suffered by other sub-sectors by means of transfers. On the one hand, the Government has approved additional transfers to the Fondos de la Seguridad Social (Social Security Funds - SSF) in the amount of €15.7 billion. On the other hand, it has also approved the COVID-19 Fund for Regions in the amount of € 16 billion.

Thus, AIReF estimates an increase in the CG deficit of between 3.2% and 2.7% to reach 7.7% in scenario 1 and 8.3% in scenario 2, mainly as a result of transfers and, to a lesser extent, the downward revision of tax revenue. For its part, the deficit of the SSF, despite the transfers already approved, will be between -3.9% and -5.1% of GDP, also reflecting the impact of the new measures approved. The Regions' deficit estimate has also been reduced, although to a lesser extent than the new transfers due to the higher estimated health expenditure and the new measures approved.

NET LENDING/BORROWING BY SUB-SECTORS (%GDP)

	2019	Scenario 1		Scenario 2	
		SPU Report	Current	SPU Report	Current
APs	-2.8	-10.9	-11.9	-13.8	-14.4
CG	-1.3	-4.5	-7.7	-5.6	-8.3
FSS	-1.3	-5.0	-3.9	-6.1	-5.1
Regions	-0.5	-1.5	-0.4	-2.0	-0.9
LGs	0.3	0.0	0.0	-0.1	-0.2

What are the implications from the point of view of sustainability?

The update of the macroeconomic and fiscal forecasts does not substantially change the conclusions of the previous report on the sustainability of public

finances. AIReF predicts a 22.1-27.7% increase in the debt-to-GDP ratio in 2020. This means the debt-to-GDP ratio will be between 117.6 and 123.2% GDP in 2020. The primary deficit will be the factor that contributes most to this increase. Although current economic prospects are surrounded by an unprecedented uncertainty, its high impact on debt level is certain. The COVID-19 crisis will cause a sharp and, in principle, temporary, increase in the public deficit, which in turn will lead to a permanent increase in the debt-to-GDP ratio. The starting fiscal position represents an added difficulty due to facing the challenges posed by the crisis. AIReF simulations indicate that even assuming an annual reduction in the public deficit of 0.5% of GDP from the projected level in 2021, it will take at least two decades to return to the debt level of 95.5% recorded at the end of 2019, and that, in contrast to AIReF's pre-crisis scenarios where the 60% level was reached around 2035, this will no longer be achieved before 2050.

What does AIReF recommend in this context?

At present, the fiscal framework applicable to the Public Administrations is not clear. The targets approved prior to the COVID-19 crisis have been far exceeded by the current situation. Furthermore, with a view to the next financial year, the PAs do not have realistic targets consistent with the new situation in order to be able to draw up their budgets for 2021 and their multi-year scenarios. There is also uncertainty about the consequences of non-compliance with the fiscal rules both in 2019 and in the current year.

Although the escape clause has been activated at European level, the government has not declared the exceptional situation provided for in our budgetary stability regulations, which would also entail the obligation to draw up a rebalancing plan to ensure the sustainability of public finances.

To address the current lack of definition of the fiscal framework, AIReF recommends that the Government:

- Clarify the fiscal framework applicable to each of the PAs as soon as possible and in particular with a view to drawing up the Budgetary Plan and the budgets of each administration, which means activating the exceptionality clause, clarifying the consequences of non-compliance with the fiscal rules and establishing a new stability and debt path.
- Establish a medium-term national fiscal strategy that provides fiscal guidance and realistically and credibly ensures the financial sustainability of the PAs.

Furthermore, AIReF also recommends:

- To explore, within the framework of the medium-term fiscal strategy, the implementation of the proposals made by AIReF in the Spending Review

studies, both those already carried out and those to be presented in the near future.

1. INTRODUCTION

According to AIReF's mandate, it must prepare a report on compliance with the stability and debt targets and the expenditure rule for the current year by July 15. Organic Law 6/2013 creating AIReF entrusts this institution with the continuous evaluation of the budgetary cycle and public debt with the ability to prepare a report, at any time, on the desirability of activating the measures provided for in the Organic Law on Budgetary Stability and Financial Sustainability (LOEPySF). In addition to this general authorisation, AIReF is obliged to give its opinion on whether all the Public Administrations (Pas) are complying with the budgetary stability and public debt targets for the current year, as well as with the expenditure rule, before 15 July each year.

However, the 2020 targets have been eclipsed by the crisis. This year, the legal mandate to assess compliance with the current targets has been altered by the exceptional situation resulting from the pandemic. On the one hand, the targets for 2020 of all the General Government (GG) sector and of each of the sub-sectors, approved last February, have become irrelevant due to the magnitude and severity of the pandemic, although formally they are still in force. Furthermore, there are no individual targets for the Regions, as the distribution of the sub-sector's target has been interrupted by the state of alarm declared due to the pandemic.

For this reason, AIReF shifts the focus of the analysis from calculating the likelihood of compliance to evaluating deficit and debt forecasts, also adapting its analysis framework. The magnitude of the crisis caused by the pandemic has led AIReF to adapt its analysis framework. In line with the guidance initiated in the report on the SPU 2020-2021, the high uncertainty has made it advisable to replace the confidence intervals with analysis based on two scenarios, which are determined by the evolution of the pandemic and the pace of economic recovery.

2. PURPOSE AND SCOPE

The purpose of this report is to analyse the stability and debt forecasts for 2020 for PAs, updating the pronouncement made in the previous report on the SPU published in May. As a consequence of the exceptional current context, the monitoring of a target that is not going to be complied with, as acknowledged by the Government in the Stability Programme Update 2020 - 2021, loses its meaning. Therefore, AIReF adapts the content of this report to the new reality and focuses its analysis on the production of deficit and public debt forecasts at the end of the year, using the approach initiated in AIReF's report on the SPU 2020-2021, published in May, which is now being updated.

AIReF updates both macroeconomic and fiscal forecasts with respect to those presented in the last report. The analysis incorporates the new information published to date on both the macroeconomic and fiscal climate, in addition to the impact of the new measures approved to tackle the crisis caused by COVID-19.

The analysis is carried out for all sub-sectors, with an individual analysis by Regions and the main Local Governments (LGs), and is completed with the overview of the PA sector. In particular, AIReF has analysed:

- The *Administración Central* (Central Government - CG) sub-sector.
- The *Fondos de la Seguridad Social* (Social Security Funds - SSF) sub-sector.
- The regional sub-sector and each Region.
- The Local Government (LG) sub-sector.
- In addition to the LG sub-sector, the 24 large local corporations that have already been analysed in previous reports were evaluated individually: the 16 city councils with over 250,000 inhabitants, the Provincial Councils of Barcelona, Valencia and Seville, the Island Councils of Tenerife and Mallorca, and the Provincial Councils of Guipúzcoa, Vizcaya and Álava.

On the other hand, moving forward in the assessment of local sustainability, the 26 city councils with medium-term sustainability risks, identified at the beginning of the budgetary cycle, have been analysed according to the methodology followed in previous reports.

The analysis by sub-sector is completed with an overview of the situation for the GG sector.

The subject of the report has been particularly conditioned by the uncertainty stemming from the evolution of the pandemic. In addition to other limitations common to previous reports, such as the lack of budgets in national accounting terms or the lack of comprehensive, up-to-date information on the impact of the main contingent liabilities that could affect the deficit for the year, the uncertainty surrounding the COVID-19 crisis especially conditions AIReF's pronouncement, whose estimates will have to be treated with greater caution than usual and will be subject to continuous revision in accordance with the data that become available.

2.1. National fiscal framework

At present, the fiscal framework applicable to the Public Administrations is not clear. Although the LOEPySF is in force, the exceptional situation resulting from the pandemic has altered the targets and the enforceability of the consequences resulting from non-compliance with these. This leads to a situation of uncertainty as to which targets are applicable and what the consequences of non-compliance are.

On the one hand, the PAs do not have targets to be able to draw up their budgets for 2021 as well as their multi-year scenarios, which should be prepared in the last quarter of the year. Although the stability and public debt targets for 2020 and for the period 2021-2023, approved last February for the GG sector and each of the sub-sectors, are in force, they have clearly been eclipsed by the crisis resulting from COVID-19. In addition, individual targets have not been approved by the Government for the Regions, since the distribution of the sub-sector target has been interrupted by the pandemic.

On the other hand, there is uncertainty about the consequences of non-compliance with the fiscal rules. According to the publication, on May 29, of the *Ministerio de Hacienda* (Ministry of Finance - MINHAC) report on the degree of compliance with article 17.3 of the LOEPySF¹, there are PAs that have failed to comply with the fiscal rules in 2019. Some of these administrations are working to present an Economic-Financial Plan (EFP) for

¹ [Report on the degree of compliance with the fiscal rules 2019 \(art. 17.3 LOEPySF\)](#)

2020-2021. Currently, this uncertainty about the consequences of non-compliance could apply to the 2020 financial year.

The LOEPySF contains tools to resolve the uncertainty about the fiscal framework caused by the current pandemic. The LOEPySF foresees the possibility that when certain exceptional circumstances occur (natural disasters, serious economic recessions and extraordinary emergencies beyond the control of the PAs) an "escape clause" is activated to put fiscal rules on hold with the requirement that rebalancing plans be drawn up that incorporate a new path of medium-term deficit and debt targets.

The Central Government is responsible for initiating the procedure, as well as for coordinating the actions of all administrations in the area of budgetary stability. The Central Government is responsible for the effective implementation of the principle of budgetary stability, in line with the principles derived from European fiscal regulations. In fact, in accordance with art. 11.3 of the LOEPySF, it is the government that initiates the procedure for applying the escape clause envisaged for the CG and the Regions. In addition, the Central Government is also responsible for coordinating action on stability between the different levels of administration, which in this context would mean clarifying the fiscal framework of the LCs, for which the LOEPySF does not provide for any exceptionality, and ensuring that the rebalancing plans drawn up by each administration are part of a common strategy.

Uncertainty about the European response to the crisis makes it difficult to establish national strategies. Currently, European institutions have implemented various actions to alleviate the effects of the COVID-19 crisis. However, within the framework of the negotiation of the European Union's multiannual financial framework, initiatives have been proposed that would have a strong impact, both in terms of their characteristics and amount, on the activity of Spanish public administrations. Among these initiatives, the Recovery Fund proposed by the European Commission (Next Generation EU) stands out for its fiscal and economic implications.

Furthermore, the European fiscal framework is not without uncertainty. The European Union has activated the escape clause of the Stability and Growth Pact, allowing temporary deviations from fiscal targets this year. Also, unlike Spain, there are 19 countries in the European Union that have activated their national escape clauses. However, it remains to be seen when we will return to the framework of rules and, above all, under what circumstances, since we cannot forget that the European institutions had begun a process of reviewing the fiscal governance framework, which will have to be resumed at some point.

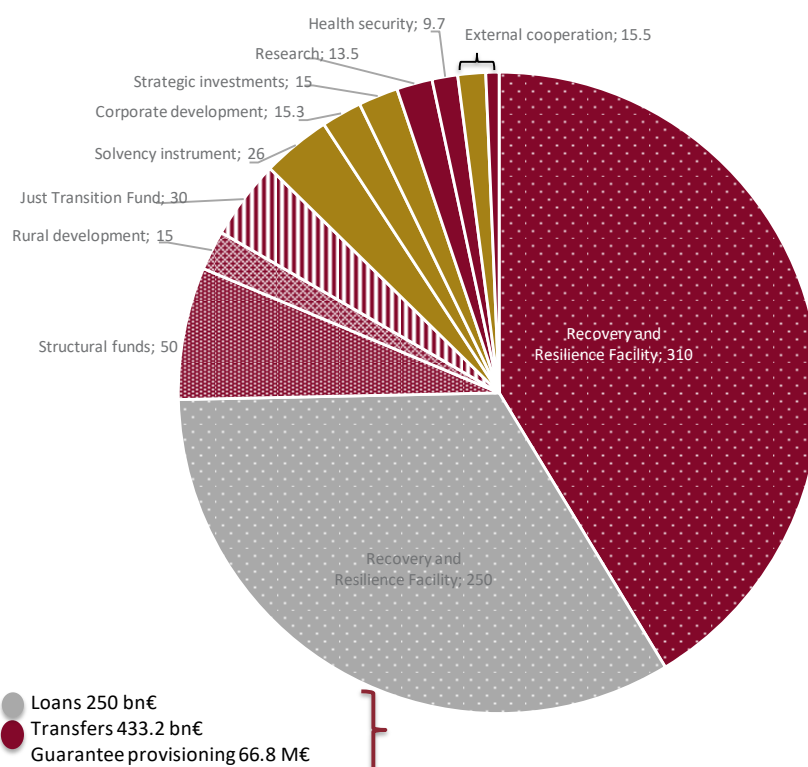
BOX 1. EUROPEAN COMMISSION PROPOSAL FOR THE RECOVERY FUND (NEXT GENERATION EU)

The EC proposal is for a programme of up to €750 billion (in 2018 prices), with expenditure committed over four years (2021-24) and aimed at relaunching activity in the short term, promoting the green and digital transition, as well as sustainable and inclusive growth. To finance it, the Commission, on behalf of the Union, would issue debt, for which it would have to increase the budget's own resources ceiling temporarily and exceptionally.

Key aspects of this Plan, such as the final size, the composition between loans and transfers and the distribution by country, are still pending negotiation.

EUROPEAN COMMISSION PROPOSAL FOR THE RECOVERY FUND (*)

(BILLION EUROS 2018)



Source: Own calculations with data from the European Commission.

(*) On top of these amounts, an additional 5 billion would be added to the structural funds and 5 billion to the solvency fund if there is agreement, both figures under the multiannual financial framework in force (2014-20).

The most relevant instrument is the Recovery and Resilience Facility, with an allocation of €560 billion (distributed between loans and transfers). This facility will support Member States to invest and implement reforms essential for sustainable recovery in accordance with the multiannual national Recovery and Resilience Plans that they will have to design. Possible areas of support

include labour markets, social security, health, education, environment, property, public administration and the judicial system.

Other instruments include increased structural funds, rural development and just green transition, promotion of business development, strategic autonomy, business solvency, research and investment in health security.

3. UPDATE TO THE MACROECONOMIC SCENARIO

AIReF has updated the macroeconomic scenario for the period 2020-2021 which it published in the report on the assessment of the Stability Programme in May. The COVID-19 pandemic has raised uncertainty about the economic outlook, both for the Spanish economy and globally. The difficulties in projecting the evolution of the pandemic and the containment measures, the lack of previous references and models to project how agents will respond to this situation and the complexity of measuring the impact of the numerous measures that governments and monetary authorities have implemented to mitigate the economic impact make it difficult to make forecasts. In this context, many institutions have developed alternative forecasting scenarios, contingent on the duration and intensity of the pandemic.

The two scenarios presented are conditioned by assumptions about the duration of the pandemic and the intensity of recovery. In its report on the Government's Stability Programme, AIReF also approached its analysis by drawing up two forecasting scenarios conditioned, firstly, by the duration of the pandemic and, secondly, by the Spanish economy's ability to recover. Both elements are closely related in these scenarios as it is considered that the longer the duration of the disease, the greater the possibility that the Spanish economy will experience structural damage. The update of these scenarios also incorporates the effects of the economic policy measures adopted to date.

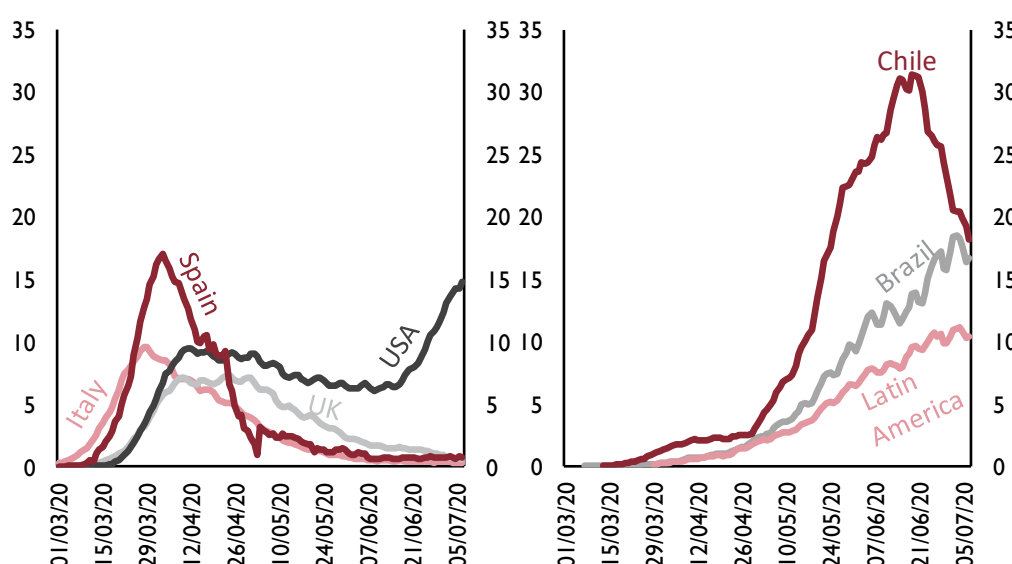
3.1. The external environment of the Spanish economy

The main source of uncertainty is still linked to the evolution of the pandemic, which has continued to spread globally, although its epicentre has moved

from Asia to Europe and then to America. In particular, after the period of slowdown in economic activity in many European countries between March and May, most countries have entered a new phase of recovery of mobility and reopening of economic activity. However, new episodes of infection have been frequent and have required the introduction of local restrictions on mobility.

Every day a new peak is reached in the total number of new cases and some countries have reintroduced restrictions on mobility. In the United States there has been an increase in the rate of new cases since mid-June and they also continue to accelerate in Latin American countries or in India (Figure 1). In some countries such as Australia or Israel, restrictions similar to those imposed in March are being reinstated.

FIGURE 1. DAILY VARIATION IN THE NUMBER OF PEOPLE AFFECTED BY COVID-19 PER 100.000 INHABITANTS



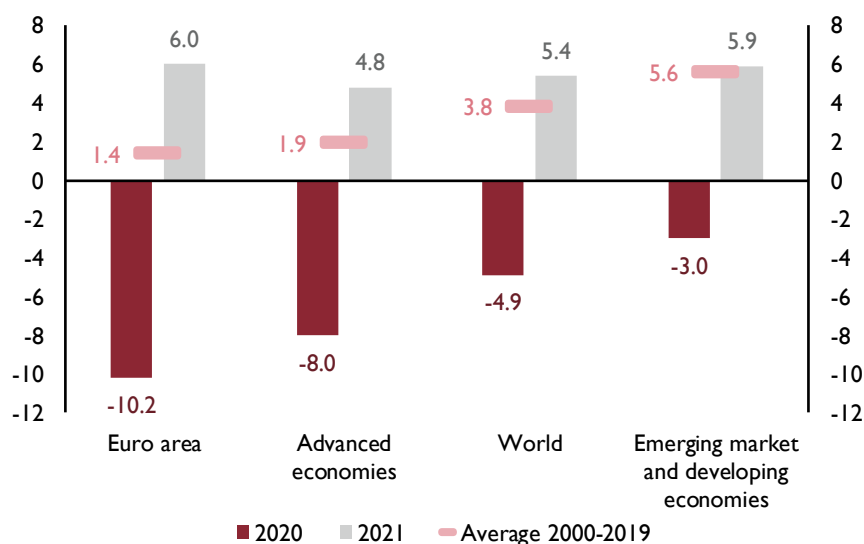
Source: Johns Hopkins University, CSSE. To 5 July 2020

In this context, most international institutions and organisations have revised growth forecasts downward. The forecasts reflect the severe and extraordinary economic impact of the pandemic, which has caused an unprecedented crisis of a more global and synchronised nature than those recorded in recent history. For example, the most recent IMF forecasts (see Figure 2) project very strong GDP declines in 2020 in the different geographical areas, including in the emerging economies as a whole (which had grown at an average of almost 6% over the last two decades).

The fall in activity is particularly intense in the euro area. The ECB, for its part, projects a fall in GDP of 8.7% in 2020 for the whole of the euro area - a rate

similar to that expected by the European Commission - in a scenario that assumes the possibility of localised outbreaks of the disease. This fall would rise to 12.6 % if the severity of these outbreaks were to make stricter containment measures necessary.

FIGURE 2. GROWTH FORECASTS FOR DIFFERENT GEOGRAPHICAL AREAS AND HISTORICAL AVERAGE



Source: IMF

The global and synchronised nature of the crisis leads to expectations of extraordinary setbacks in world trade in goods and especially in tourism-related activities. The World Trade Organization and the World Tourism Organization present very adverse scenarios for the evolution of both variables, and especially for tourism flows, given that restrictions on the international mobility of travellers such as restrictions on international flights or the obligation to undertake quarantine periods still persist (figures 3 and 4).

FIGURE 3. SCENARIOS FOR THE EVOLUTION OF EUROPEAN GOODS IMPORTS. VOLUME INDEX (2005=100)

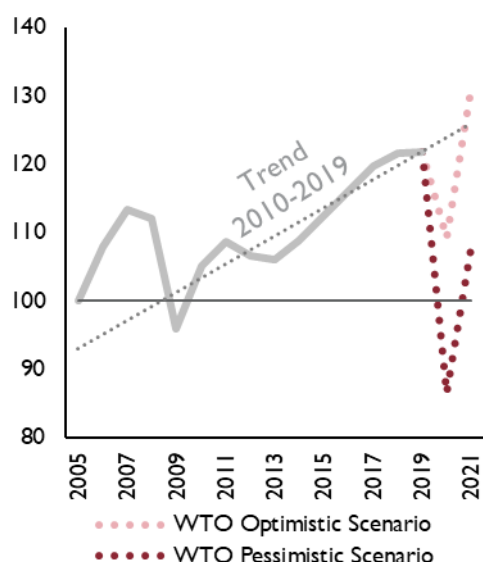
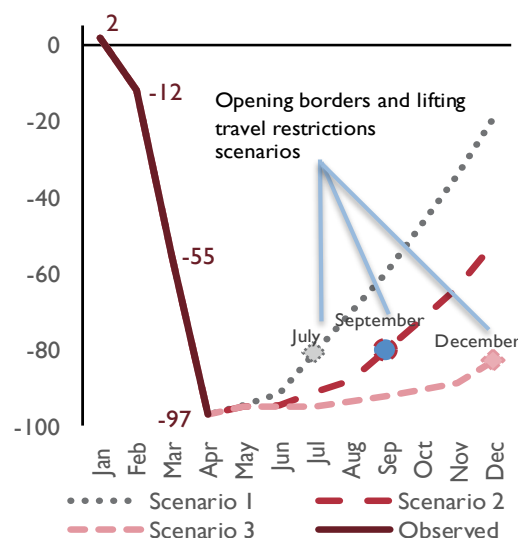


FIGURE 4. SCENARIOS OF EVOLUTION OF WORLD INTERNATIONAL TOURISM FLOWS



Sources: World Trade Organization and World Tourism Organization.

Financial conditions improved in a context where accommodative monetary policy measures were intensified. Since April monetary policy measures have been intensified, particularly in the eurozone, with an expansion of asset purchase programmes and credit facilitation measures. The size of the ECB balance sheet is currently around 53% of eurozone GDP (compared to 33% for the Federal Reserve). In this context of expansive monetary policies, financial markets have generally seen upward trends, following the sharp deterioration observed in mid-February. The stock market indices have had an upward trend on almost all the world's stock markets. The easing of financial tensions has also been reflected in the sovereign debt markets, reducing the yield spreads of eurozone countries' securities compared to the German curve.

3.2. Recent evolution of the Spanish economy

Although the information available is still partial and incomplete, the most recent indicators for the Spanish economy point to a gradual recovery in activity, as the process of de-escalation advances. Most indicators show that the volume of activity reached record lows in April, when non-essential activities were restricted. Specifically, the service sector activity index contracted by 42% in year-on-year terms in April, private car registrations were virtually nil that same month and overnight stays in hotels and the number of foreign tourists stood at zero in April and May. Subsequently, as the de-escalation of mobility and activity restrictions has progressed, a recovery has

begun which has gained strength, as shown by the purchasing managers' indices (PMI) or the EC's economic climate indicator (Figures 5 and 6).

FIGURE 5. PMI SERVICES INDEX
(SEASONALLY ADJUSTED. <50
EQUIVALENT TO CONTRACTION//>50
EQUIVALENT TO EXPANSION)

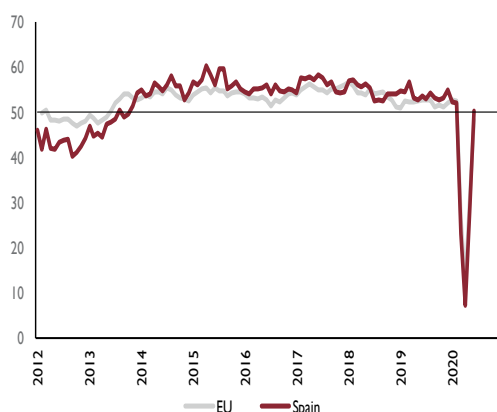
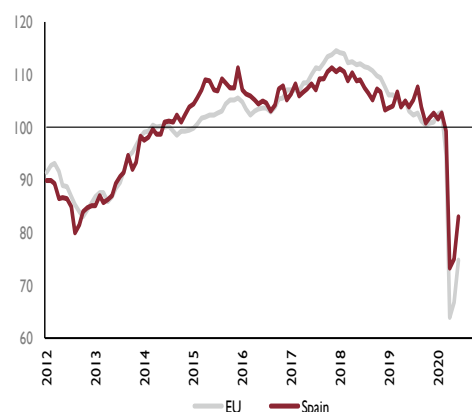


FIGURE 6. ECONOMIC CLIMATE INDICATOR
(AVERAGE INDEX=100)



Fuente: IHS Markit and European Commission

Quantitative indicators also point to a revival in activity. For example, the contraction in electricity consumption in the peninsular electricity system was more than 27% compared to the same period the previous year and in the first week of July it was at a similar level to that of previous years (not corrected for temperature) (see figure 7). Similarly, according to BBVA's figures, weekly credit card spending fell by 60% in year-on-year terms at the beginning of April, coinciding with the most restrictive phase of confinement, while in the last week of June the fall moderated to -2% in year-on-year terms. Significant rebounds were also seen in May retail sales and June car registrations.

FIGURE 7. ELECTRICITY DEMAND. PENINSULAR ELECTRIC SYSTEM (GWH). NOT CORRECTED FOR TEMPERATURE

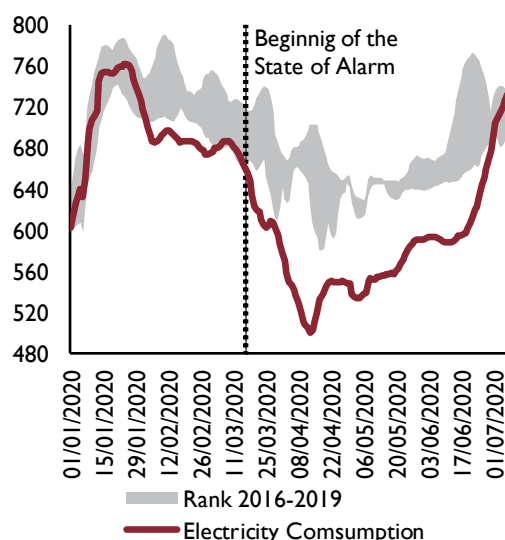
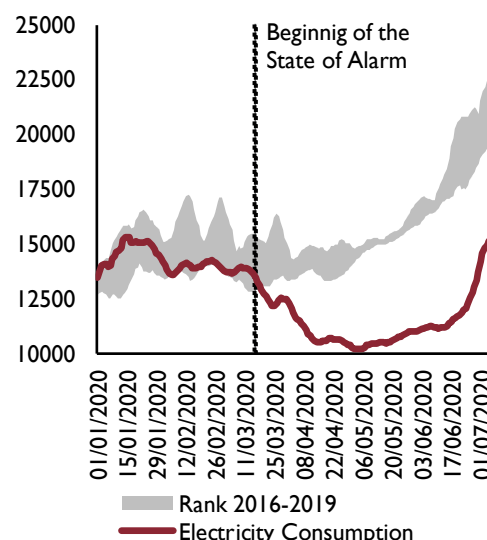


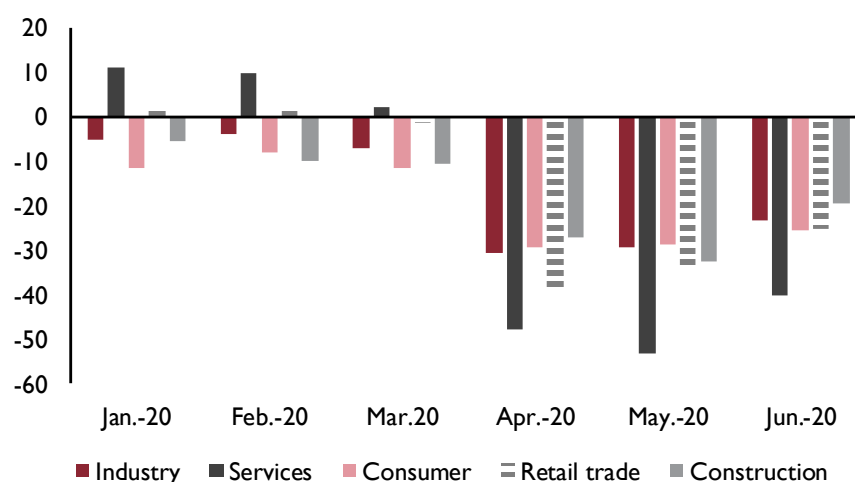
FIGURE 8. ELECTRICITY DEMAND. BALEARIC ELECTRIC SYSTEM (MWH). NOT CORRECTED FOR TEMPERATURE



Source: Red Eléctrica Española and AIReF's calculations.

In general, activity was lower than in the previous year, with significant differences by area and sector. Nevertheless, the high growth rates seen in some high-frequency indicators should be interpreted with caution given the depth of the contraction observed in the preceding months. In general, the indicators suggest that, despite the notable recovery at the end of June, activity levels were still much lower than usual at this time of year and that the recovery has been very uneven by sector (see figure 9) and by Region, depending on the productive structure and the degree of sectoral specialisation of each one.

FIGURE 9. EVOLUTION OF THE ECONOMIC SENTIMENT INDICATOR BY SECTOR

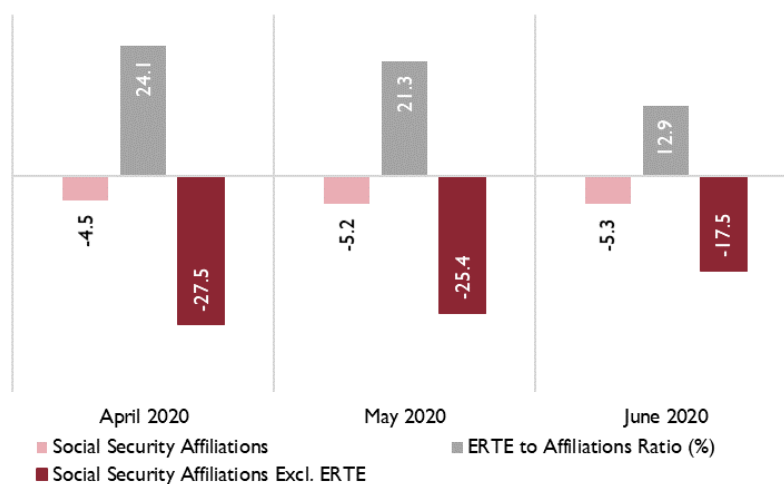


Source: European Commission.

The number of contributors has risen from the lows at the end of March but remains well below the levels recorded in the previous year. In the same vein, employment shows an upward trend from the lows at the end of March, although in year-on-year terms its decline is still intense. At the end of June (29 June), the number of contributors was 700,000 less than in mid-March, 5.3% less than in June of the previous year. The year-on-year drop amounts to 17.5% if workers under Expedientes de Regulación Temporal de Empleo (Temporary Redundancy Schemes - ERTes) are discounted (figure 10).

The reincorporation of workers under ERTes is progressing well, although in some sectors and communities the number of people affected remains high. By the end of June more than 1.5 million of the workers who were under ERTes at the end of April (around 3.4 million) had started working again. The number of ERTes as a percentage of the number of contributors fell from 24.1% in April to 12.9% in June. Even so, at the end of June, 41% of the workers in industry who were affected by an ERTE at the end of April were still in that situation. These percentages amount to 53% in services - 97% in accommodation services and 51% in food - and are somewhat lower in construction (34% of those affected in April) (figure 11).

FIGURE 10. EVOLUTION OF SOCIAL SECURITY AFFILIATIONS AND OF THE NUMBER OF WORKERS UNDER AN ERTE



Source: Ministerio de Inclusión, Seguridad Social y Migraciones (Ministry of Inclusion, Social Security and Migration). AIRcF's calculations.

FIGURE 11. RETURN TO WORK OF WORKERS UNDER AN ERTE BY SECTOR

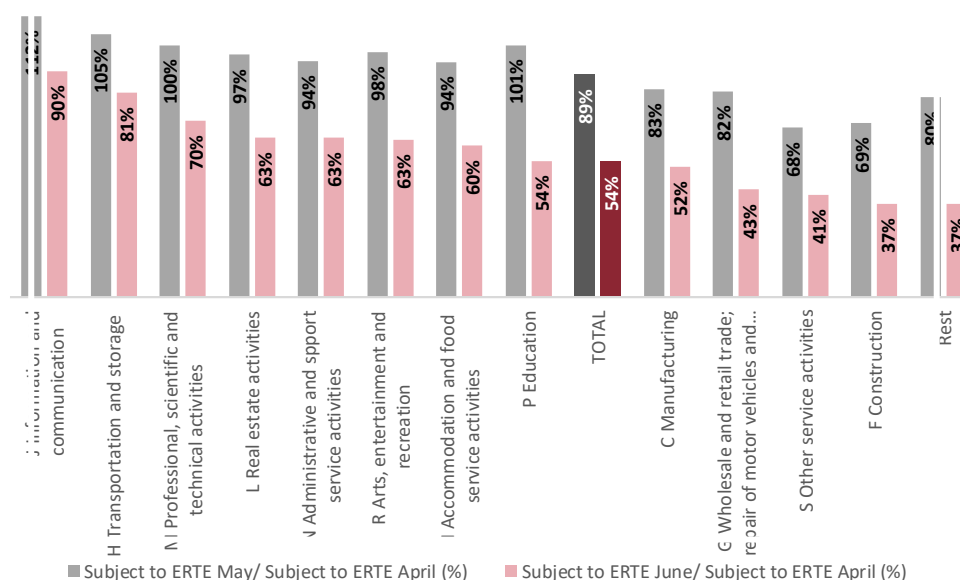
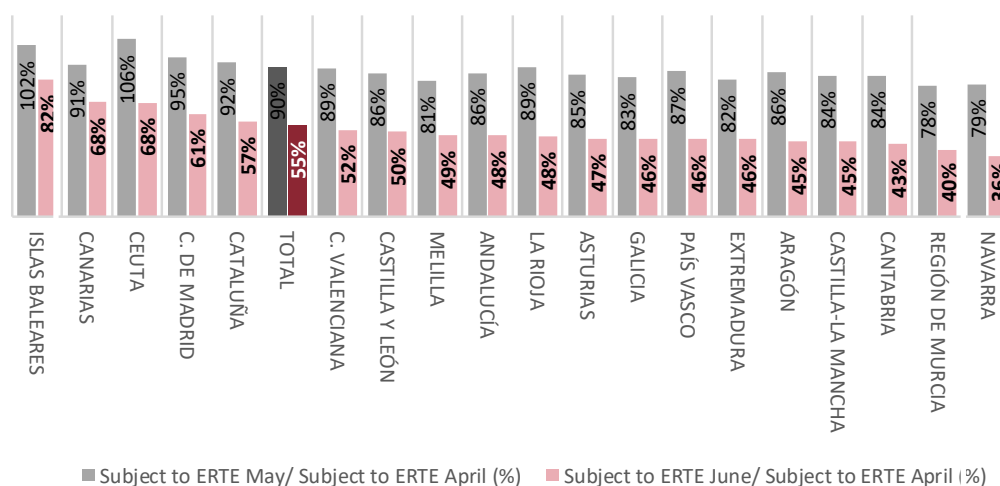


FIGURE 12. RETURN TO WORK OF WORKERS UNDER ERTE BY REGION



Source: Ministerio de Inclusión, Seguridad Social y Migraciones. AIReF's calculations.

3.3. Update to AIReF's Macroeconomic Scenarios

In May, AIReF developed two scenarios conditioned, first, on assumptions about the duration of the pandemic and the speed of recovery.

- In a first scenario, based on simulation models of the number of people affected by the disease, it was hypothesised that by mid-May the epidemiological results would allow restrictions to begin to be relaxed. From that moment on, activity would gradually return to normal.

- In a second, more adverse scenario, it was assumed that there would be a generalised outbreak of the disease that would force measures of confinement and restriction of economic activities to be reintroduced for an additional month in the second half of the year. In this second scenario, it was also considered that the longer duration of the pandemic would lead to greater financial difficulties for companies and households and lower growth in world trade. These developments are implemented in forecasting models through an additional shock to employment, investment and exports.

In both scenarios, it was assumed that tourism-related activities would maintain lower activity levels than usual throughout 2020.

The update of the scenarios presented takes into account the information regarding the evolution of the pandemic, the economic information that has been received, as well as the economic policy measures approved. With regard to the evolution of the pandemic in Spain, the success of the strict measures to contain COVID-19 allowed the transition to a *new normality* to begin at the start of May. The different Regions have been approaching this new normality at an uneven pace, with a gradual lifting of restrictions on mobility and economic activity, which culminated on 21 June with the non-extension of the state of alarm. However, there are still some restrictions that particularly affect activities that involve greater social interaction (e.g. capacity restrictions and restrictions on international mobility). In addition, there have been several local outbreaks in recent days, which have forced the reintroduction of restrictions.

This process of transition is being reflected in a more gradual normalisation of activity than was incorporated in the previous scenarios, which justifies the downward revision of the projections for 2020. The return to normal levels of activity is particularly slow in some social consumption activities and in those related to international tourism, which are highly important for the Spanish economy and where signs of recovery are practically non-existent. Therefore, rather than a different diagnosis on the speed of recovery, it is precisely the fact that the fall in the second quarter has been greater than initially estimated that has led to a downward revision of expected growth in 2020 in both scenarios.

At present, AIRcF's estimates point to a 10.1% drop in GDP in 2020, which could be as high as 12.4% in a scenario with a second peak requiring widespread confinement. These estimates represent a downward revision compared to previous estimates of 8.9% and 11.7%, respectively (see Table 1).

An incomplete recovery is still projected for 2021, with GDP increasing by 5.1% in the first scenario and 5.8% in the second. This represents a marginal revision of the forecast for that year, compared to previous estimates of 4.6% and 5.8%.

TABLE 1. FORECASTING SCENARIOS WITH AND WITHOUT SECOND PEAK

		Stability Programme Update 2020-2021									
MACROECONOMIC SCENARIO		Scenario 1		Scenario 2		Government		Scenario 1		Scenario 2	
VOLUME	2019	2020	2021	2020	2021	2020	2021	2020	2021	2020	2021
GDP (% Y-o-Y. Unless otherwise stated)	2.0	-8.9	4.6	-11.7	5.8	-9.2	6.8	-10.1	5.2	-12.4	5.8
Consumption (contribution to GDP growth)	1.1	-4.2	1.7	-6.0	2.1	-6.5	2.1	-5.5	3.3	-6.6	3.1
Private consumption	1.1	-9.0	3.7	-13.0	5.3	-8.8	4.7	-11.6	6.6	-14.0	6.7
Public consumption	2.3	5.4	-1.8	7.7	-3.4	2.5	1.8	6.4	-1.8	7.9	-2.8
GFCF in Equipment	3.0	-36.2	18.5	-45.2	22.0	-37.0	32.5	-37.7	18.4	-43.9	17.8
GFCF in Construction and Intellectual Property	1.2	-18.7	10.7	-31.1	16.5	-25.0	12.5	-18.7	11.3	-30.6	16.2
Domestic Demand (contribution to GDP growth)	1.5	-9.1	3.8	-13.2	4.7	-9.7	5.8	-10.5	5.5	-13.6	5.5
Exports	2.6	-30.3	15.9	-35.7	13.1	-27.1	11.6	-29.2	15.2	-36.8	12.8
Imports	1.2	-34.3	15.4	-44.3	11.4	-31.0	9.3	-33.2	18.8	-44.0	14.5
External Demand (contribution to GDP growth)	0.5	0.2	0.7	1.5	1.0	0.5	1.0	0.5	-0.2	1.3	0.3
PRICES	2019	2020	2021	2020	2021	2020	2021	2022	2023	2024	2025
GDP deflator	1.6	0.0	0.4	-0.5	0.5	-1.0	1.8	0.4	0.8	0.2	0.6
Private consumption deflator	1.2	-1.9	1.0	-2.4	1.0	-1.5	1.7	-0.2	1.0	-0.8	0.8
NOMINAL	2019	2020	2021	2020	2021	2020	2021	2022	2023	2024	2025
GDP	3.6	-8.9	5.0	-12.1	6.3	-10.1	8.7	-9.7	6.0	-12.2	6.4
Gross Operating Surplus	3.0	-7.6	6.7	-10.7	9.0	0.0	0.0	-9.2	7.7	-11.3	9.5
Net Taxes on rodution and imports	0.9	-10.7	4.7	-14.5	4.8	0.0	0.0	-10.7	4.7	-14.5	4.8
Household savings rate (%GDI)	7.9	9.5	9.2	11.6	9.4	0.0	0.0	11.0	8.4	12.2	8.9
Net Lending/Borrowing (% of GDP)	2.3	3.2	3.0	4.9	5.2	1.8	1.8	2.7	1.8	3.6	3.6
Current Operations vs RoW	-2.0	-2.8	-2.6	-4.4	-4.8	-1.4	-1.5	-2.2	-1.5	-3.2	-3.2
EMPLOE	2019	2020	2021	2020	2021	2020	2021	2022	2023	2024	2025
Compensation of Employees	4.7	-9.5	3.4	-13.0	3.9	2.0	1.0	-9.7	4.5	-12.5	4.3
FTEE	2.1	-9.7	2.6	-12.9	3.1	0.0	0.0	-10.7	4.2	-12.8	4.6
Compensation per employee (Thousands of €, Y-o-Y)	2.2	0.1	0.7	0.1	0.7	2.0	1.0	1.2	0.2	0.4	-0.3
Productivity per Employee	-0.1	0.9	1.9	1.4	2.6	0.5	1.0	0.7	0.9	0.5	1.1
Unit Labour Costs (ULC)	2.3	-0.7	-1.2	-1.3	-1.8	1.5	0.0	0.5	-0.7	-0.1	-1.4

Source: *Instituto Nacional de Estadística* (National Statistics Institute - INE), Ministerio de Asuntos Económicos y Transformación Digital (Ministry of Economic Affairs and Digital Transformation) and AIReF.

The expected fall in 2020 is in line with other organisations' forecasts and places the Spanish economy among those most affected by the economic crisis. This fact mainly reflects the intensity of the health crisis, which led to the introduction of very severe mobility restriction measures, as well as a productive specialisation where activities requiring greater social interaction have a high participation.

Except of public consumption, in 2020 all of demand-side components are expected to decline harshly. The decline in private consumption is noteworthy because of the increase in forced savings during the period of confinement and precautionary savings in view of the deterioration in confidence and employment prospects. Business investment is also falling sharply in a context of high uncertainty about demand prospects and liquidity difficulties. For its part, the expansion of public consumption reflects the increase in purchases of healthcare materials and expenditure on personnel to deal with the pandemic. Exports are also expected to fall sharply in a context of falling world trade and international tourism, while imports will contract, reflecting the drop in domestic demand.

Employment will also fall sharply in 2020. Employment in terms of full-time equivalent jobs (which approximates the employment in hours estimated by

the INE) would register a fall of 10.7% in the first scenario and 12.8% in the second, leading to notable growth in productivity per full-time equivalent job in both scenarios.

Inflation and deflators are revised upward, although they maintain very moderate rates. With regard to prices, the expected growth of product deflators and private consumption has been revised upwards, due both to the assumption of higher oil prices with respect to May, and to the downward resistance that inflation is showing in a context of strong monetary expansion (Box 2 presents AIReF's most recent estimates on the impact of the rise in the minimum wage in 2019).

BOX 2. IMPACT OF THE MINIMUM WAGE

AIReF has carried out an initial ex-post evaluation of the increase in the minimum wage in force since January 2019. This was an unprecedented increase, as it raised the minimum wage by 22% and affected more than one million workers. About 7.1% of employed workers² were being paid less at the time the proposal was approved.



Most of the studies conducted to date take an aggregate approach. **AIReF, however, adopts a quasi-microeconomic approach** by combining anonymised individual data from the 2018 Continuous Working Life Sample (CWLS) with very detailed aggregated information on Social Security affiliations from 2015 to 2019. When the 2019 CWLS is available, it will be possible to refine the analysis to overcome some of its limitations, discussed below.

The detail of the methodology followed by AIReF in this first study is available on AIReF's website. In summary, from these CWLS data, firstly, an indicator is constructed that tries to determine, for each group of workers, to what extent

the increase in the minimum wage affects them. It is an **incidence indicator** that not only quantifies the percentage of workers *directly* affected by the rise in different subgroups, but also weights it by the distance between the new threshold and the individual's contribution base. Secondly, with the monthly series - from January 2015 to December 2019 - of affiliates to the general regime, provided by the *Tesorería General de la Seguridad Social* (General Treasury of Social Security), the aim is to **quantify the incidence of this measure in the affiliations for 2019**. Various robustness analyses were carried out to check the soundness of the results.

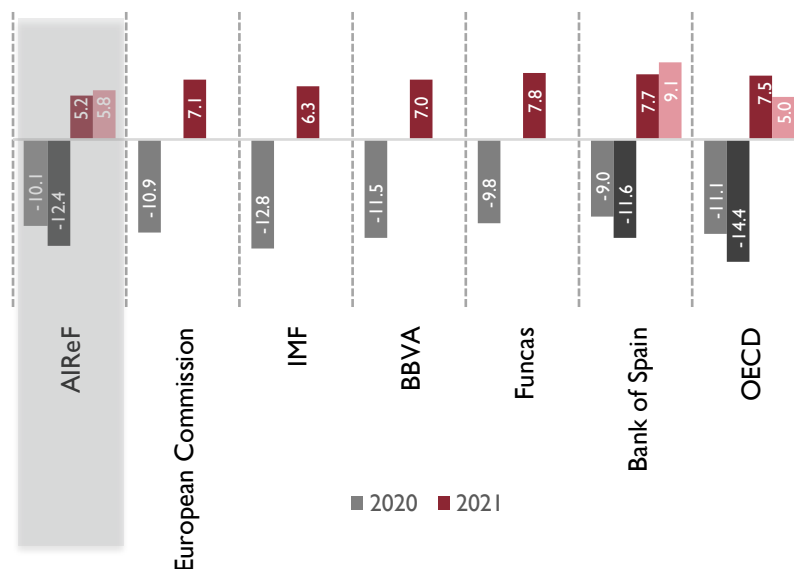
The analysis carried out shows that the rise in the minimum wage in 2019, with the data available for the year as a whole, had a negative effect on affiliation, which represented a reduction of between 0.13 and 0.23 percentage points in its growth rate, resulting in a loss of between 19,000 and 33,000 contributors in 2019.

This effect would have been unevenly distributed by groups, with young people and regions with lower wages bearing a greater weight of this cost. The different impact would only be given by the differences in the potential impact indicator in the different groups, since in this first study no additional analysis of the heterogeneity of the effect by socio-demographic characteristics has been carried out. On the other hand, these estimates do not incorporate possible indirect effects associated with the fact that the increase in the wages of some workers may have some impact on their consumption that may cushion the estimated drop in employment to a certain extent. The CWLS for 2019 will allow the analysis to be completed.

A moderate and incomplete recovery is expected for 2021. There were hardly any revisions to the 2021 forecast in the report on the Stability Programme. AIReF was one of the least optimistic institutions regarding the speed of recovery for 2021 and, in general, as shown in figure 13, this assessment has not changed. In addition to the temporary characteristics that make a more dynamic recovery more difficult (distancing measures, capacity reduction, sanitation, etc.), there are structural characteristics (high participation in the production structure of activities with greater social interaction, seasonality of employment and business demographics with a higher participation of small and medium-sized enterprises that are more vulnerable to financing difficulties), and all this in a context where the pandemic is still spreading globally, which will undoubtedly affect the speed of global recovery. At the national level, the scenario of continuous outbreaks may end up affecting the confidence of families and companies, hindering the reactivation of

consumption and employment. All these elements mean that both scenarios project a less rapid recovery than that envisaged by other institutions.

FIGURE 13. COMPARISON OF FORECASTS OF DIFFERENT ORGANISMS



Source: IMF, BBVA Research, Funcas, Banco de España, OECD

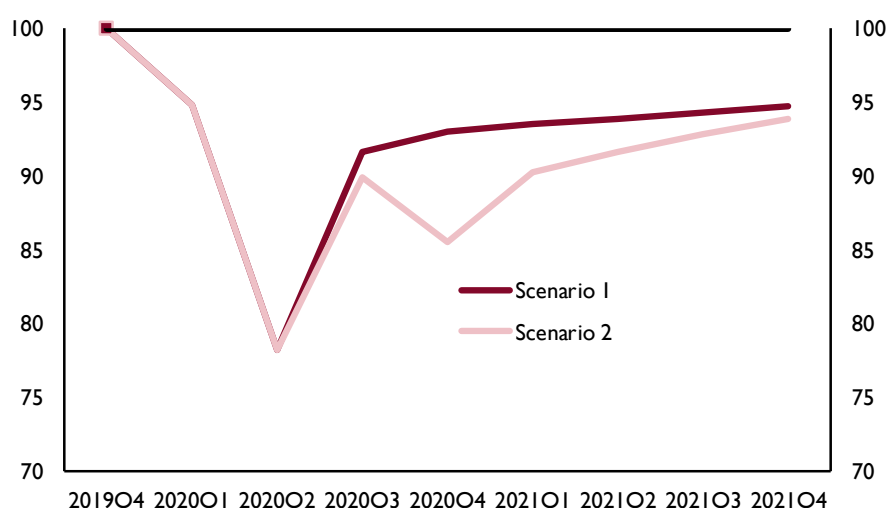
In addition, there is considerable uncertainty about future consumption and employment behaviour, which play a central role in determining the speed of recovery. Faced with the possibility of rapid materialisation of curbed consumption capacity during the period of confinement, the experience of economies that emerged from confinement earlier, such as China, calls for a degree of caution: consumption of durable goods and services in these countries is showing a slow recovery, which is due both to the persistence of social distancing measures and to precautionary savings in the face of high uncertainty.

However, employment growth in 2021 has been revised upwards from the May scenarios. This reflects the possibility that the extension of ERTes, insofar as it allows workers' return to work to be better matched to recovery, will have a favourable effect on confidence and employment.

With regard to the quarterly profile, after the 5.2% drop in GDP in the first quarter of the year, it is estimated that the magnitude of the drop in the second quarter worsened to an inter-quarterly rate of -17.5%. These estimates are in line with the *Banco de España's* most recent forecasts, which are in a range of between -16% and -21% or the FUNCAS estimate which estimates a fall of -18% quarter-on-quarter for the second quarter. As of the third quarter, AIRcF's scenarios project a strong rebound as activity returns to normal levels. This

upturn does not prevent the level of GDP from remaining more than 5% below that observed before the pandemic in both scenarios at the end of 2021, a circumstance common to the forecast scenarios of other institutions and which gives an idea of the magnitude of this crisis. Overall, the recovery of 2019 GDP levels is not expected to occur until 2022.

FIGURE 14. QUARTERLY PATH OF GDP EVOLUTION. INDEX 2019Q4=100



Source: AIReF's calculations

The most important downside risk around these scenarios is associated with the possibility of structural damage to the economy linked to the emergence of solvency problems for Spanish companies and families. The financial vulnerability of Spanish families, which has been highlighted by various surveys, constitutes another risk element around the recovery of consumption and employment². Likewise, until a treatment or vaccine for the coronavirus is discovered, the Spanish economy will be more exposed to possible outbreaks given the high proportion of employment in activities that require high social interaction (OECD, 2020)³

On the contrary, these forecasts have not taken into account the positive impact that may result from the European Recovery Plan currently being negotiated. On May 27 the Commission published its proposal to create a recovery fund for Europe linked to the multiannual financial framework for

² According to the EU-SILC survey, in 2018, 36% of Spanish households stated that they could not afford an unexpected expenditure of 700 euros, a percentage slightly above the European average (32%). The ECB Household Finance Survey suggests that Spanish families only have enough savings to replace almost two months of income. This would allow them to cover five months of basic needs, compared to 7-8 months for Italian, French or German households. See Maria Demertzis, Marta Domínguez-Jiménez and Annamaria Lusardi, The financial fragility of European households in the time of COVID-19, Bruegel policy contribution 15, 2020.

³ OCDE (2020). Facing the jobs crisis OECD Employment Outlook 2020

2021-27. Although key aspects of this Plan are still under negotiation, such as size and distribution by country (see Box 1), if approved it would represent a significant step forward in the European response to the health crisis, which has so far taken the form of three instruments: the new European Financial Stability Facility loan line, the pan-European guarantee programme for the European Investment Bank and the SURE programme comprising Commission loans to Member States to finance expenditure on employment protection schemes. As it is geared to boosting investment, its impact on growth and public accounts could potentially be high.

4. ANALYSIS OF BUDGETARY STABILITY AND THE EXPENDITURE RULE

4.1. General Government Sector

AIReF has revised the fiscal forecasts for 2020 and estimates that the public deficit will be 11.9% of GDP, which could reach 14.4% in the event of the most adverse scenario. Two and a half months have passed since its last pronouncement in the SPU 2020 report, and during this time the adverse forecasts of economic developments and their consequent effect on public revenue and expenditure have been confirmed. However, slight deviations from the scenarios outlined in May, which have been updated in this report, have been detected and are mainly due to three factors.

First, the latest published data has been incorporated, changing the starting point with respect to the previous report. This report includes: the latest data published by the IGAE in national accounting terms (May for the State, April for the CG, SSF and Regions and first quarter for the LGs), the budgetary execution of the different sub-sectors (*Administración General del Estado* - General State Administration, Social Security System, State Public Employment Service - SEPE, *Fondo de Garantía Salarial* (Wage Guarantee Fund – FOGASA) and Regions) for the month of May, monthly information on tax collection from the *Agencia Estatal de la Administración Tributaria* (State Tax Administration Agency – AEAT), also for May, and the pension payroll (eSTADISS database) and unemployment benefits statistics. In addition, a press release confirmed the forecast for the 2019 personal income tax campaign in which a positive contribution to the evolution of the tax was expected.

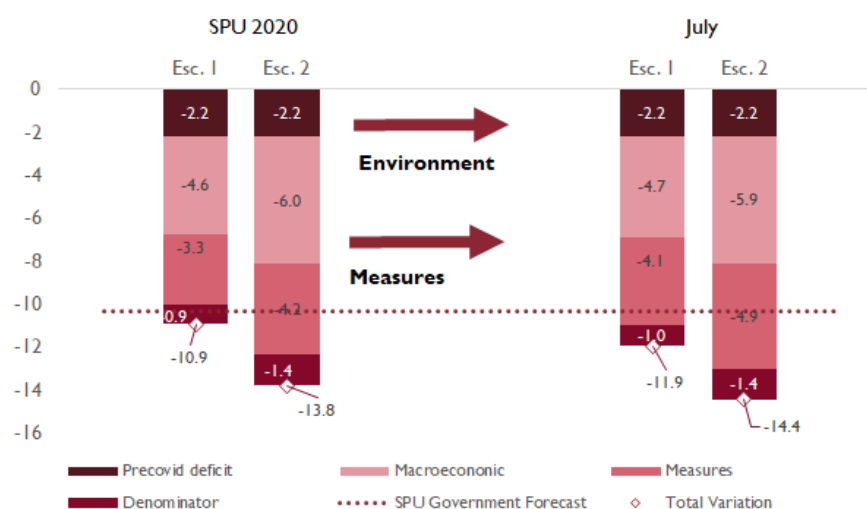
Secondly, for the unknown part of the remainder of the year, the update of the two macroeconomic scenarios projected by AIReF has been incorporated. The models for revenue and expenditure forecasting for unemployment benefits incorporate the new assumptions on the evolution of macroeconomic variables, wages, employment, consumption, gross

operating surplus, etc., with unequal changes between scenarios. In addition, not all macroeconomic components change in the same direction or intensity, resulting in an uneven revision of estimates at year-end.

Finally, the effect known to date of the measures resulting from the pandemic has been incorporated and an estimate of the new measures approved in the last two months has been included. Since the beginning of May, new measures have been approved to contain the effect of the pandemic on households and businesses or those already known have been extended, so the impact of the measures has been completely updated.

As a result of this update the public deficit has worsened by 1% in Scenario 1 and by 0.6% in Scenario 2. Most of the change is explained by the updated impact of the measures, which justify an increase in the deficit of 0.8% in the first scenario and 0.7% in the second. The rest is explained by the new macroeconomic forecasts and the incorporation of known information that worsens the deficit of scenario 1 by 0.2%, without affecting the second scenario.

FIGURE 15. UPDATE OF GENERAL GOVERNMENT NET LENDING/BORROWING AIReF (%PIB)



AIReF estimates that revenue in 2020 will stand at 40.3% of GDP in both scenarios. Although with respect to what was foreseen in the report on the SPU the weight of revenue increases by between 0.8% and 1%, this difference is mainly justified by a change in the criterion for recording exemptions from social contributions in the accounts. In the previous report, the exemptions from contributions resulting from ERTes and the benefit for cessation of activity had been considered as a reduction in the amount of contributions recorded in the national accounts. However, in the published data they have been treated as subsidies, i.e. they have been recorded as expenditure under the heading of subsidies and not as lower revenue under the heading of social contributions. This change implies a greater weight of revenue, and in turn,

and for the same amount, a greater weight of expenditure, so that the net effect on the deficit is zero. Likewise, with respect to scenario 2, the better macroeconomic prospects in the evolution of employment and wages would explain a residual increase in the weight of revenue with respect to the previous report.

Expenditure is expected to rise to between 52.2% and 54.8% of GDP according to AIRcF's estimates, increasing 1.8 and 1.6% compared to the forecasts of the report on the SPU. A part of this change, 0.7% in scenario 1 and 0.8% in scenario 2, is due to the aforementioned change in the way exemptions are recorded in the accounts. The rest is basically explained by the incorporation of the impact of the new measures or the extension of the previous measures.

TABLE 2. BREAKDOWN OF THE CHANGE IN % OVER GDP OF THE TWO SCENARIOS

SCENARIO 1						
	Pre-pandemic forecast (1)	2020 COVID Effect			Total COVID effect (2)=(a)+(b)+(c)	Current forecast (3)=(1)-(2)
		Denominator effect (a)	Measures effect (b)	Macro effect (c)		
RESOURCES	39.8	5.1	-0.2	-4.3	0.5	40.3
TAXES	22.7	2.8	-0.2	-3.1	-0.5	22.2
On production	11.6	1.4	-0.1	-1.6	-0.2	11.3
Income type	10.7	1.3	-0.1	-1.5	-0.2	10.5
Capital	0.4	0.1	0.0	0.0	0.0	0.5
CONTRIBUTIONS	13.1	1.7	0.0	-0.9	0.9	13.9
Other resources	4.0	0.5	-0.1	-0.3	0.1	4.1
EMPLOYMENT	41.9	6.1	3.8	0.4	10.3	52.2
Compensation of employees	10.8	1.6	0.2	0.0	1.8	12.6
IC + Social Transfers in kind	7.7	1.1	0.6	0.0	1.7	9.3
Social provisions in cash	16.0	2.3	2.2	0.1	4.7	20.7
Interest	2.0	0.3	0.0	0.2	0.5	2.5
GFCF	2.3	0.3	0.0	0.0	0.3	2.6
Other employment	3.2	0.5	0.7	0.0	1.2	4.4
NET LENDING/BORROWING	-2.2	-1.0	-4.1	-4.7	-9.8	-11.9

SCENARIO 2						
	Pre-pandemic forecast (1)	2020 COVID Effect			Total COVID effect (2)=(a)+(b)+(c)	Current forecast (3)=(1)-(2)
		Denominator effect (a)	Measures effect (b)	Macro effect (c)		
RESOURCES	39.8	6.1	-0.3	-5.2	0.6	40.3
TAXES	22.7	3.4	-0.2	-3.7	-0.6	22.1
On production	11.6	1.7	-0.1	-1.9	-0.3	11.3
Income type	10.7	1.6	-0.1	-1.8	-0.3	10.4
Capital	0.4	0.1	0.0	0.0	0.0	0.5
CONTRIBUTIONS	13.1	2.1	0.0	-1.1	1.0	14.1
Other resources	4.0	0.6	-0.1	-0.4	0.1	4.1
EMPLOYMENT	41.9	7.5	4.6	0.7	12.9	54.8
Compensation of employees	10.8	1.9	0.3	0.0	2.2	13.0
IC + Social Transfers in kind	7.7	1.4	0.8	0.0	2.2	9.9
Social provisions in cash	16.0	2.9	2.6	0.4	5.9	21.9
Interest	2.0	0.4	0.0	0.2	0.6	2.6
GFCF	2.3	0.4	0.0	0.0	0.4	2.7
Other employment	3.2	0.6	0.9	0.1	1.5	4.7
NET LENDING/BORROWING	-2.2	-1.4	-4.9	-5.9	-12.3	-14.4

FIGURE 16. EVOLUTION OF THE GENERAL PUBLIC ADMINISTRATION'S BALANCE

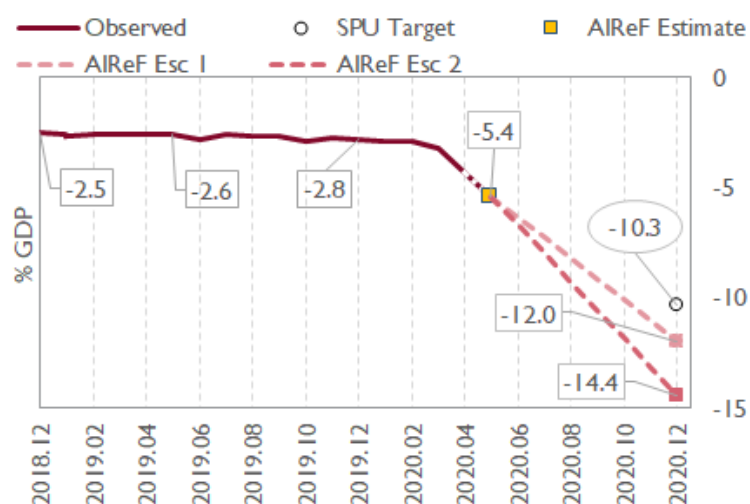


FIGURE 17. EVOLUTION OF THE GENERAL PUBLIC ADMINISTRATION'S REVENUES

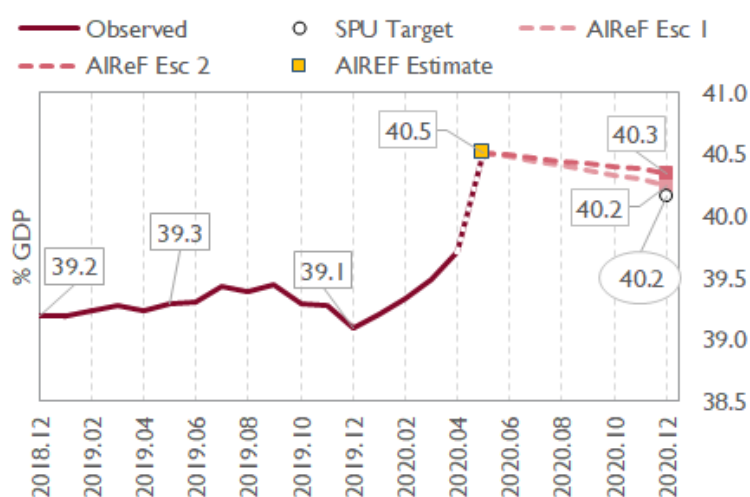
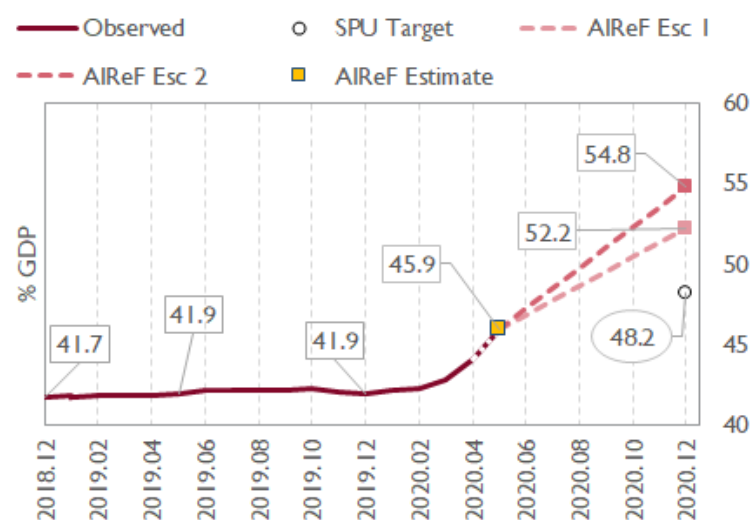


FIGURE 18. EVOLUTION OF THE GENERAL PUBLIC ADMINISTRATION'S EXPENDITURES



4.1.1. Impact of the measures adopted

The measures approved so far cost the public accounts between 4.1% and 4.9% of GDP depending on the scenario. Since the previous report, new measures have been introduced and the impact of previous measures has been updated. As a result of this exercise the deficit has increased by 0.8% in scenario 1 and 0.7% in scenario 2. The main differences with respect to the previous report are the inclusion of the impact of the Minimum Living Income of 1,743 million euros in 2020 and the extension of the ERTes and benefits for cessation of activity, as well as the increase in health expenditure and other measures adopted by the Regions.

TABLE 3. IMPACT OF MEASURES

Impact of measures (+ sign = greater deficit)		AIRcF ESTIMATE - July 2020					
		Scenario 1			Scenario 2		
		Millions	% GDP	Dif. from SPU	Millions	% GDP	Dif. from SPU
Central Government		3,215	0.3	0.0	3,328	0.3	0.0
Expenditure measures		1,754	0.2	0.0	1,754	0.2	0.0
Health expenditure		1,147	0.1	0.0	1,147	0.1	0.0
Other social or economic expenditure		206	0.0	0.0	206	0.0	0.0
RDL measures 17/2020; ACM 09/06/2020; RDL 25/2020		401	0.0	0.0	401	0.0	0.0
Fiscal measures		1,461	0.1	0.0	1,574	0.1	0.0
FSS		32,103	2.9	0.5	36,563	3.3	0.5
Temporary Redundancy Plans (ERTes)	Unemployment benefit	17,673	1.6	0.2	19,777	1.8	0.2
	Contribution exemption	5,346	0.5	-0.1	6,094	0.6	-0.1
Self-employed	Benefit for cessation of activity	4,729	0.4	0.1	5,791	0.5	0.1
	Contribution exemption	1,805	0.2	0.0	2,191	0.2	0.1
Temporary incapacity for work (TIW)		675	0.1	0.0	809	0.1	0.0
Other measures		132	0.0	0.0	158	0.0	0.0
Minimum Living Income		1,743	0.2	0.2	1,743	0.2	0.2
Regions		8,738	0.8	0.2	11,323	1.0	0.1
Region revenue measures (without AGE transfers)		312	0.0	0.0	312	0.0	0.0
Region non-health expenditure measures (without transfers to LGs)		1,415	0.1	0.1	1,415	0.1	0.1
Region health expenditure measures		7,010	0.6	0.1	9,595	0.9	0.1
LGs		2,009	0.2	0.0	2,787	0.3	0.0
LG expenditure measures		996	0.1	0.0	1,291	0.1	0.0
LG revenue measures (without AGE and Region transfers)		1,013	0.1	0.0	1,496	0.1	0.0
TOTAL MEASURES		46,065	4.1	0.8	54,001	4.9	0.7

AIRcF estimates a cost associated with ERTes due to force majeure of between €23,019 and €25,870 M, about €1,600 and €1,000 M higher than estimated in the last report. This amount is between €3,000 and 5,900 M higher than the

€20,110 M envisaged in the SPU. The change in AIReF's estimate is due to three factors, two that reduce expenditure and one that increases it. The two factors that reduce expenditure are the lower number of people affected by ERTes (from an estimated 4M to 3.4M in real terms) and the reduction in the exemption from contributions as the duration of the ERTes is extended. The factor that increases expenditure is the average duration of the situation (from 3.5 months to about 5). The average duration has increased, both because of the assumptions on the duration of the ERTes (the report on the SPU considered that there would be ERTes until the autumn and this report assumes that they will last until the end of the year) and because of the slower speed of recovery in employment compared with the estimate in May. The impact of all these factors produces an increase in benefit expenditure, but some reduction in the cost of exemptions, the first effect being greater than the second. AIReF has drawn up an evolution of people affected by an ERTE by branches of activity, with real data up to the first week of July, and applying assumptions of improved employment thereafter. These assumptions are consistent with the macroeconomic assumptions on job destruction contained in this report. The average benefit is estimated on the basis of unemployment benefit statistics.

BOX 3. ESTIMATE OF THE ECONOMIC IMPACT OF ERTes

In Royal Decree-Law 8/2020 it was accepted that ERTes due to the COVID crisis would be due to force majeure and would be associated with exemptions from contributions of 100% for companies with less than 50 workers and 75% for companies with more than 50 workers. The ERTes would be operational as long as the alarm state was maintained. A total of 3.4M workers were placed under ERTes until the end of April.

With Royal Decree-Law 18/2020 the concept of ERTes was separated from the state of alarm, were prolonged until the end of June and the situation of partial ERTE was established for those companies that began to reincorporate workers. For these cases, a greater exemption is established for those workers who return to work than for those who do not. Additionally, exemptions will be different depending on the size of the company and the month (May and June).

Finally, Royal Decree-Law 24/2020 maintains the differentiation between total and partial ERTE, and accepts that, if there is a relapse in activity, companies that have to put their workers back under an ERTE will benefit from greater exemptions than if they do not need to return to a full ERTE. Again, the exemptions differ depending on the size of the company, the month, the type of ERTE and whether the worker has returned to work or not.

The estimate has changed as data on the evolution of ERTes have been published and as the exemptions from contributions to which one is entitled have been changed according to the month and the situation of the workers. In particular, the average exemption due to ERTes for the first month was about 76%, while the average exemption at the end of September is estimated to be about 35%. This estimate also takes into account the percentage of ERTes that were not due to force majeure (around 10%) and are therefore not entitled to exemption from contributions.

This estimate has been made by distinguishing between activities, and considering a certain evolution for each of them, based on already existing data and the macro assumptions mentioned in this report⁴

The benefit for cessation of activity by self-employed workers and exemption from payment of contributions is valued at between €6,534 and €7,982 million, €1,500 and €2,100 million higher than estimated by AIRcF in May. This new estimate is between €1,700 and €3,200 million more than the €4,748 envisaged in the SPU. The assumptions made by AIRcF regarding the number of workers benefiting (1.4M) and the average benefit have hardly changed from the May estimate, and were in line with those of the SPU. The increase in cost is due to the extension of the term of this benefit. The previous report considered that the benefit would last until the end of June, while Royal Decree-Law 24/2020 extended the duration to the end of September, with certain limitations on the exemption from contributions for workers returning to work. AIRcF considers that 25% of those affected (315,000 workers) will continue to receive the benefit for cessation of activity until the end of September.

AIRcF's estimates of the cost of the Minimum Living Income, approved after the SPU, are in line with those of the Government. This measure, which was not included in the May report, is permanent, resulting in an increase in the structural deficit. The Government has valued the cost of this benefit at € 2,890 million⁶ for a full year (€1,500 million and 850,000 beneficiaries in 2020). AIRcF has used data from the Living Conditions Survey (LCS) for 2018 to estimate the cost of this measure. Based on the result, it has applied data provided by Social Security on the percentage of persons who are excluded by reason of wealth, and based on error correction and rate regression models it estimates that the number of beneficiaries and the cost are in line with those estimated by Social Security. Additionally, AIRcF assumes Social Security's estimates of the cost of the employment incentive (€100 million for a quarter of 2020, €400

⁴ The macro assumptions that determine the cost estimate are mainly the expected recovery in employment and the speed of said recovery. The estimate is adjusted as data on developments are received or any changes are made to these assumptions.

million in 2021) and the reduction in the cost of assimilation of the childcare allowance (€108 million in 2020, prorated to €185 million in 2021. Prorating the cost of the measure by the 7 months that it will be in force in 2020, AIReF estimates an expenditure of €1,743M for 2020.

The assimilation of sick leave or isolation due to COVID-19 as Temporary Incapacity for Work is valued at a cost of between 675 and 809 million, €330 and 400 million higher than that estimated in May, but still lower than estimated in the SPU. The changes in AIReF's estimates are due to Social Security data reporting that the average length of sick leave has been 21 days (instead of the 15 days estimated by AIReF) and that the total number of beneficiaries has been almost 750,000 (220,000 more than estimated in May), indicating that the ratio of sick workers to quarantined persons has been 5.5 instead of the 4 estimated in May (five and a half persons quarantined for each confirmed COVID-19 case)⁷. The total cost is estimated by multiplying new cases and corresponding quarantined persons by the probability of being registered, by the duration of the benefit and by the unit cost of the benefit (75% of the contribution base for private sector members and 100% for public sector members).

With regard to the rest of the approved SSF measures, AIReF estimates their impact at between €132 and 158 million, around €90 million higher than the May estimate. The main difference compared to the previous estimate is the benefit due to cessation of activity for seasonal self-employed workers. In addition, the 50% allowances for permanent, discontinuous tourism-related workers have been extended until the end of the year. The estimate also includes the allowance for temporary workers with contracts lasting more than 2 months who have lost their jobs and the allowance for household employees who have lost their jobs or have been unable to go to work.

The increase in healthcare expenditure caused by COVID-19 is estimated at between 0.7% and 1% of GDP. While expenditure in the CA remains the same as in the previous report, in the Regions it has been revised based on the data provided by the⁵ Regions on the expenditure accrued up to May and other available information. The greater information available regarding the estimate made for the report on the SPU has made it possible to compare the estimates with additional variables, such as total health expenditure up to May, the execution of the main expenditure headings up to April and information on measures provided by the Regions themselves. With the current information, the overall estimate of the previous report has been revised upwards by 0.1%, as well as its distribution by heading.

⁵ The number of cases is obtained from a logistic model and a SIR epidemic model

On the other hand, the Regions have implemented measures and actions in other areas that could lead to an additional 0.2% of deficit. On the expenditure side, the Regions have communicated and assessed measures focused on aid to companies or additional individuals, such as those aimed at strengthening social centres and benefits; actions aimed at alleviating the effects of the crisis on companies and the self-employed; aid to local governments and other affected groups and sectors; as well as measures to strengthen cleaning and the purchase of protective material in public centres.

Most of the measures adopted, except mainly the Minimum Living Income, are of a temporary nature and revert automatically. All measures classified as temporary would lead to a reduction in the following year's deficit as they are not recurrent. This is the case of measures such as the ERTE or the extraordinary benefit for cessation of activity, whose creation regulations already provide for their abolition once the health crisis is over.

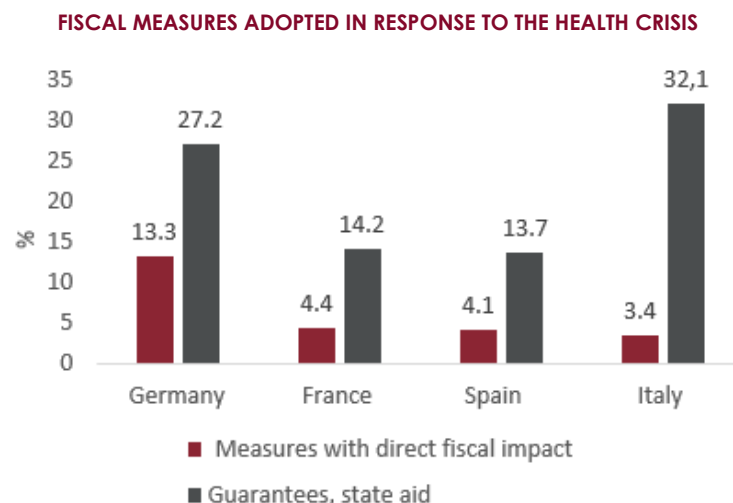
Measures have also been adopted to defer and postpone tax obligations and social contributions. The aim of these measures is to reduce companies' liquidity problems, especially SMEs and the self-employed. Most of these measures will have no impact on revenue for the year as a whole, since the payment of taxes and social contributions is expected before the end of the current financial year. However, these measures introduce an additional element of uncertainty in forecasting revenue to the extent that they alter the monthly revenue profile and there is a risk that some of the revenue may not actually materialise in the year. In fact, the SPU reflects the negative impact on revenue of some of them.

BOX 4. MEASURES ADOPTED AFTER THE 2020-2021 STABILITY PROGRAMME

Various measures have been approved since the publication of the Stability Programme. Some, such as the extension of ERTes or the benefit for cessation of activity for the self-employed, imply the extension of measures that had already been adopted; others, such as the Minimum Living Income, go beyond the predominant fiscal response until now because of their permanent nature. In addition, sectoral support measures involving specific aid to certain areas of economic activity have been adopted and a new line of guarantees has been created to stimulate productive investment.

These additional measures have a direct budgetary impact of around 0.8% of GDP. Moreover, the additional measures to support solvency and business investment amount to a further 4.5% of GDP in aid that does not have a direct short-term impact on the public deficit. Therefore, the direct budgetary impact of all the measures approved so far is estimated to be between 4.1%

and 4.9% of GDP and almost 14% of GDP in guarantees and other instruments that do not contribute to the deficit.



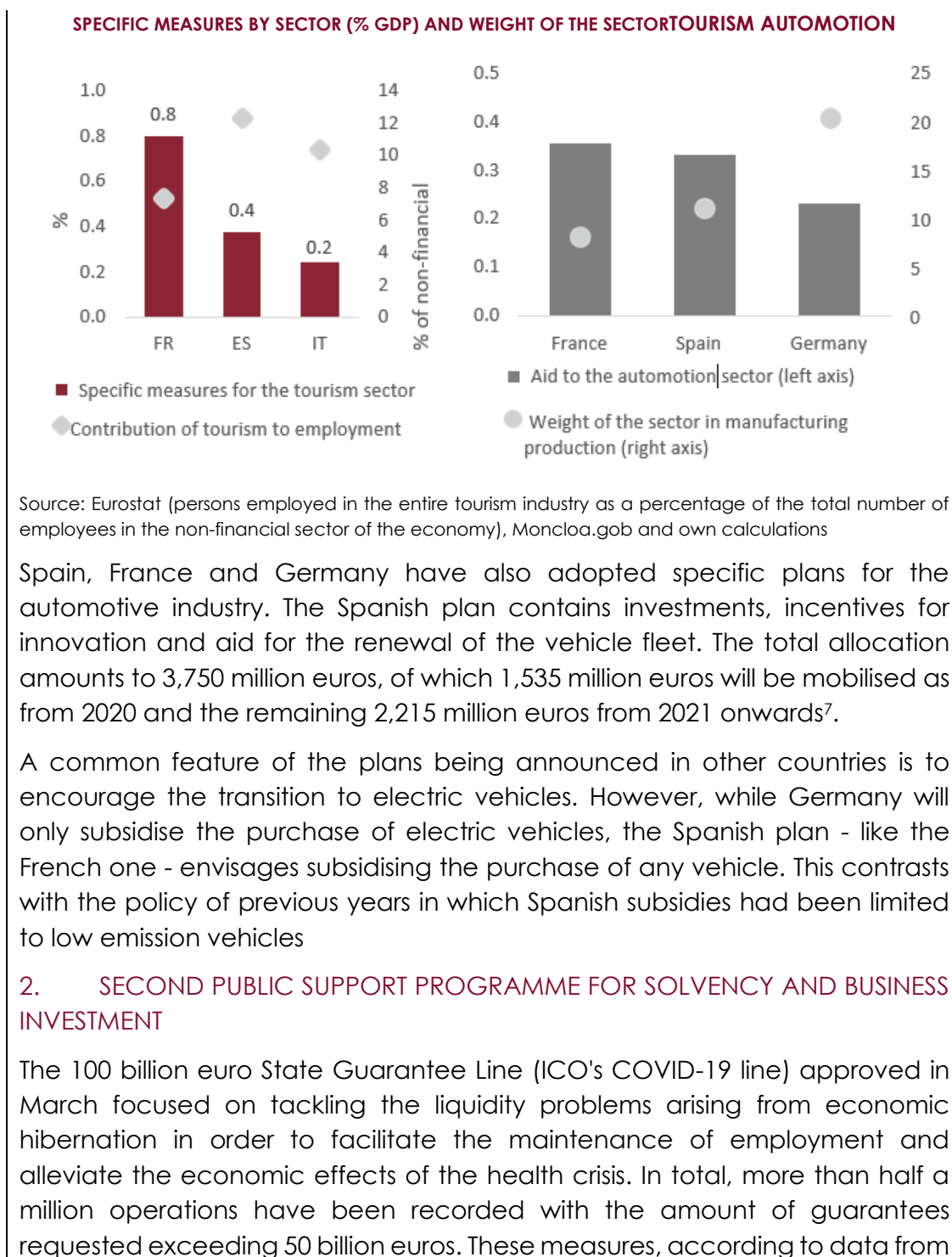
Source: AIReF's calculations based on Stability and Convergence Programme 2020-2023, Bruegel and Moncloa.gob.

1. SECTORAL PLANS: TOURISM and AUTOMOTION

The Tourism Sector Promotion Plan has a total financial allocation of 4,262 million euros for 28 measures divided into five pillars ⁶. The bulk of the financial allocation corresponds to measures that do not have an immediate impact on the deficit, either because they are financial operations (loans through the Fondo Financiero del Estado para la Competitividad Turística - State Financial Fund for Tourism Competitiveness) or because they are contingent liabilities (preferential tranche in ICO's COVID-19 guarantee line of 2.5 billion euros). Specifically, these two types of measures represent slightly over three-quarters of the total Plan.

Other countries in our environment - like France or Italy - have also adopted specific measures for tourism. The composition of the measures in Spain has been more biased towards loans and guarantees, in contrast to France and Italy where the weight of aid with a direct impact on the deficit has been somewhat greater, with measures to boost national tourism demand, for example. In the case of France, the possibility of direct investment in companies in the tourism sector - large or small - that are experiencing difficulties (State aid) has also been approved.

⁶https://www.lamoncloa.gob.es/serviciosdeprensa/notasprensa/industria/Documentos/2020/20062020_PlanTurismo.pdf



⁷https://www.lamoncloa.gob.es/serviciosdeprensa/notasprensa/transportes/Documentos/2020/15062020_PlanAutomocion2.pdf

the Banco de España, have allowed an upturn in new credit to companies of 90%⁸.

The Government has now adopted a second programme to stimulate investment and strengthen solvent companies in strategic sectors whose financial situation may be vulnerable due to COVID-19, especially in the areas of environmental sustainability and digitisation⁹.

This programme consists of two initiatives. On the one hand, a new specific ICO guarantee line has been set up for productive investment for 40 billion euros. On the other hand, a solvency support fund has been created, endowed with 10 billion euros, which will be managed by the Sociedad Estatal de Participaciones Industriales (SEPI). The Fund will invest in those non-financial companies that request it and that are solvent, in addition to being strategic for the productive fabric.

4.2. Revenue forecast

Eliminating the accounting effect of exemptions from social contributions, AIREF maintains the weight of revenue as a percentage of GDP in scenario 1, and improves it by 0.2% compared to scenario 2. The asymmetric behaviour between scenarios is justified by the different intensity of the drop in nominal GDP, as well as by the different behaviour between the components of the macroeconomy. Thus, in scenario 1, revenue decreases with the same intensity as the new nominal GDP forecast, so the larger revenue drop is offset by the denominator effect. In scenario 2, on the other hand, the economic outlook improves compared to the previous forecast, so the denominator effect would explain the increase of 0.1% and the macroeconomic effect would add the second.

TABLE 4. REVENUE AS % OF GDP AIREF

	SPU (1)		Changes (2)		Current forecast (3)=(1)+(2)	
	Scen 1	Scen 2	Scen 1	Scen 2	Scen 1	Scen 2
REVENUE	39.5	39.4	0.8	1.0	40.3	40.3
TAXES	22.3	22.1	-0.1	0.1	22.2	22.1
<i>On production</i>	11.4	11.3	-0.1	-0.1	11.3	11.3
<i>On income</i>	10.4	10.3	0.1	0.1	10.5	10.4
<i>On capital</i>	0.5	0.5	0.0	0.0	0.5	0.5
CONTRIBUTIONS	13.1	13.1	0.8	0.9	13.9	14.1
Other revenue	4.1	4.1	0.0	0.0	4.1	4.1

⁸<https://www.bde.es/f/webbde/GAP/Secciones/SalaPrensa/IntervencionesPublicas/Gobernador/Arc/Fic/hdc230620.pdf>

⁹<https://www.lamoncloa.gob.es/presidente/actividades/Paginas/2020/030720-sanchezpacto.aspx>

With regard to the evolution of revenue from taxes, AIREF maintains a greater drop in revenue than the Government had anticipated in the SPU. The update of the tax trend remains in line with the new macroeconomic forecast of economic activity, with a more intense worsening in the first scenario than in the second. Therefore, while in the first scenario a drop in revenue, in % variation, is expected, some 0.8% higher than that expected in the previous report, in scenario 2 the drop is softened, bringing the fiscal forecasts of the two scenarios closer together.

FIGURE 19. EVOLUTION OF TAX REVENUES. CONTRIBUTION TO CHANGE OF MAIN TAX FIGURES (%VAR.)

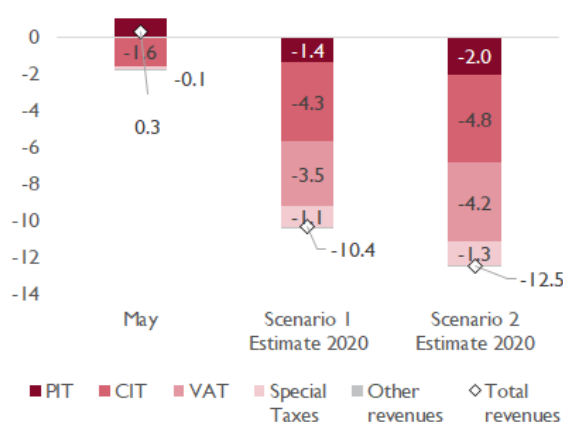
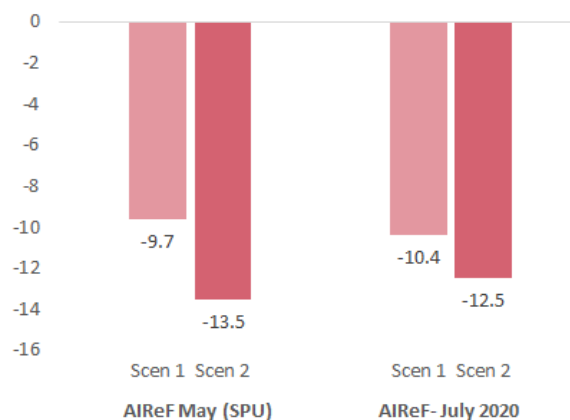


FIGURE 20. UPDATE OF TAX REVENUES IN CASH AIREF FORECAST (%VAR.)



4.2.1. PIT

Personal income tax is the only tax that has been revised upwards from the previous report, although it is still expected that collection will be lower than that presented by the Government in the SPU. In scenario 1 there are two opposing effects. On the one hand, the collection data, adjusted to liquidity measures that are unlikely to have any effect at the end of the year, perform better than expected in the previous report. Furthermore, the positive contribution of the result of the 2019 income campaign to the evolution of the tax is confirmed. However, on the other hand, AIREF expects a slight worsening of compensation of employees, by 0.3%, compared to the macro projection presented in the SPU. The first effect is somewhat stronger than the second, so the expected fall is reduced by 0.2%. On the other hand, in scenario 2 there is an improvement in the macro variable that most affects the tax, compensation of employees, which improves by 0.3% with respect to the SPU, which means that the fall in PIT in this scenario is reduced by almost 1.5%.

FIGURE 21. EVOLUTION OF PIT COMMON TAX REGIME IN NA (%VAR.)

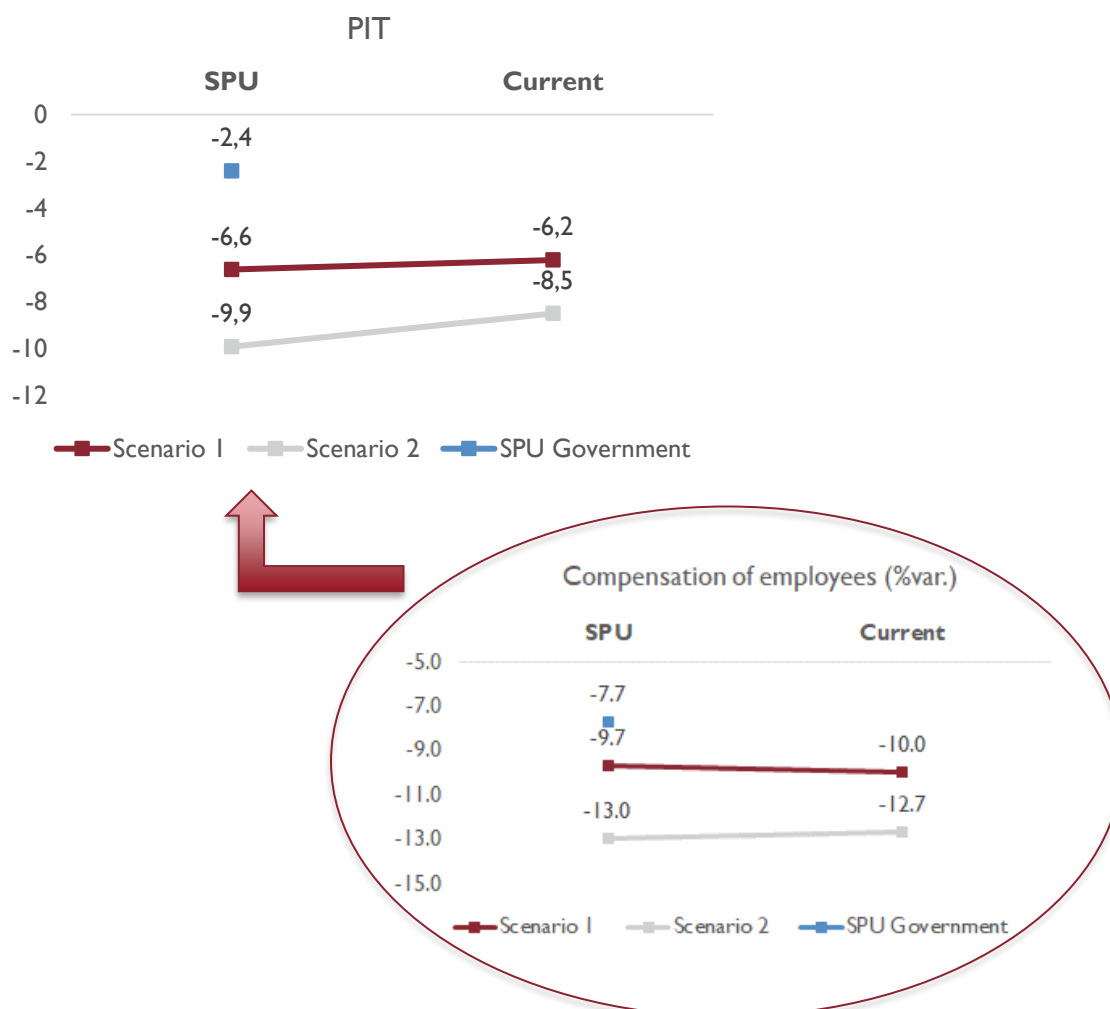
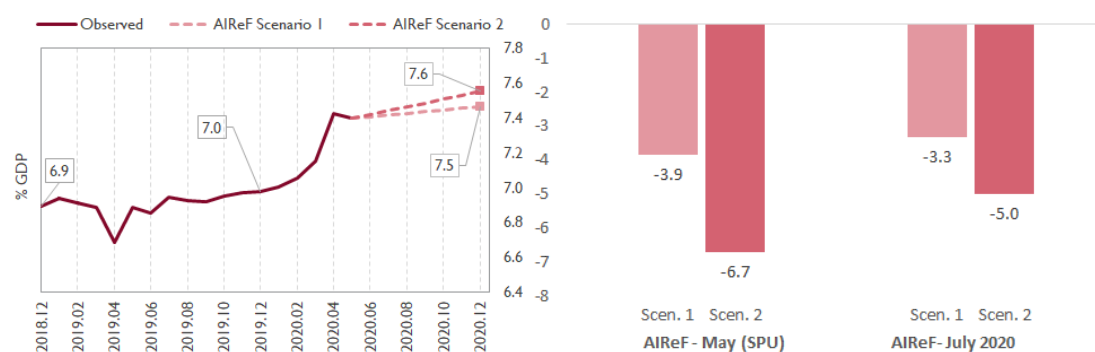


FIGURE 22. EVOLUTION OF PIT IN CASH (%GDP)



4.2.2. Corporate Income Tax

AIReF worsens its Corporate Income Tax forecast, increasing the gap with the Government's forecast in the SPU. The information known to date represents a

small part of the total tax, since the last two instalment payments and the 2019 campaign settlement account for the bulk of its collection. Therefore, almost all the change is due to a worsening of the macroeconomic environment, more so in the case of scenario 1 which increases the drop by more than 4% compared to that predicted by the Government in the SPU. However, in scenario 2, the worsening is milder as it increases by 0.6% due to a scenario closer to that of SPU.

FIGURE 23. EVOLUTION OF PIT COMMON TAX REGIME IN NA (%VAR.)

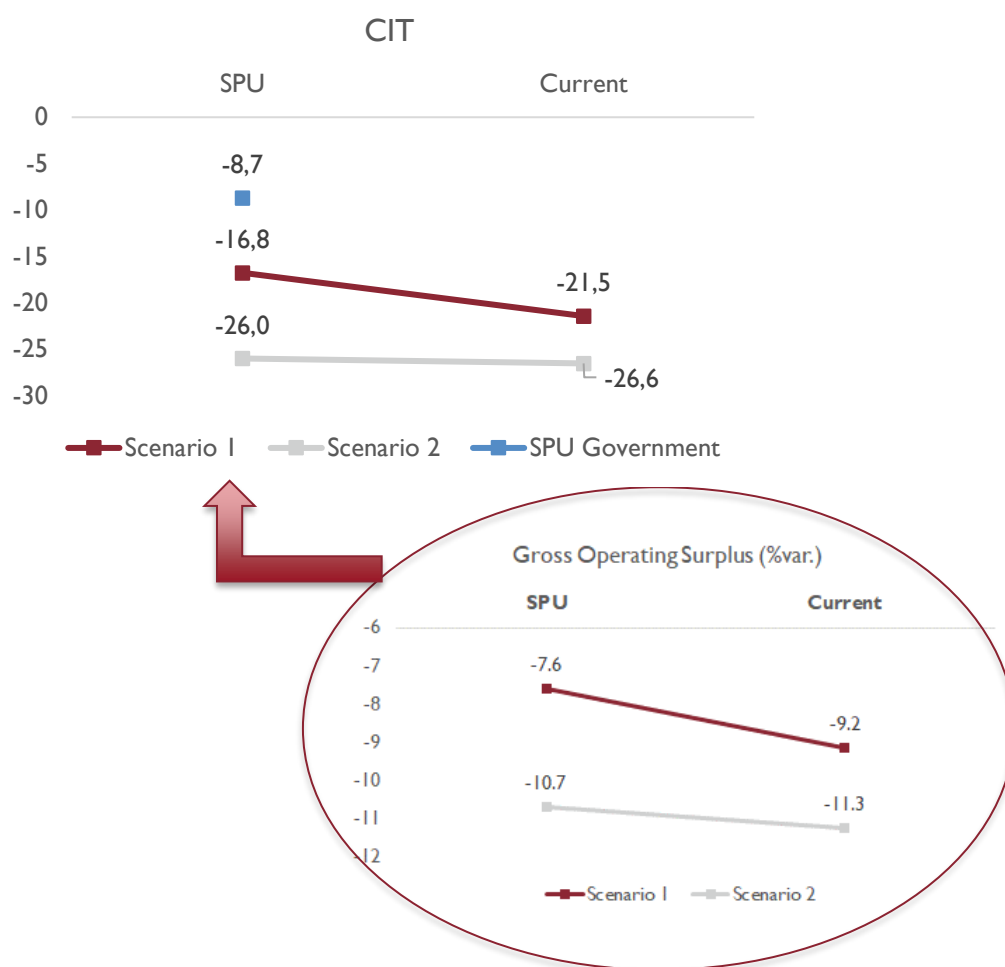
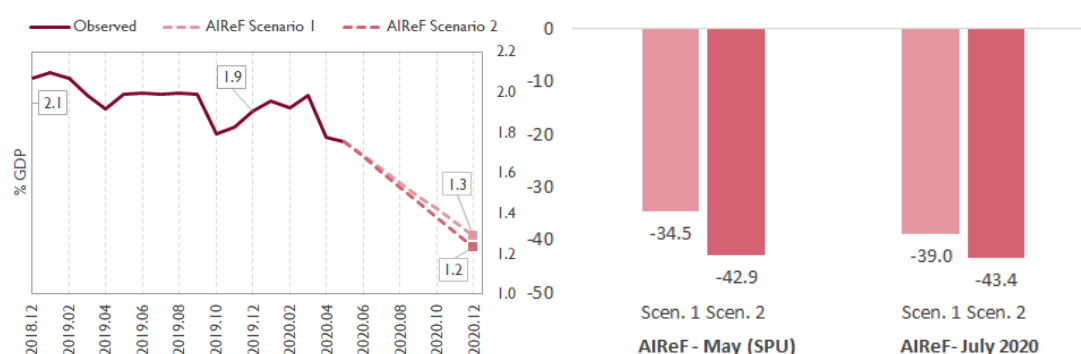


FIGURE 24. EVOLUTION OF CIT IN CASH (%GDP)


4.2.3. VAT

In line with the new domestic demand forecast in nominal terms, AIReF worsens its VAT forecast in its less adverse scenario and improves it in scenario 2. The change in the VAT forecast is marked by the new macro forecast of household consumption and investment in housing, although it has been intensified by the information known to date on collection. The available data reveal a slightly sharper fall than that predicted by AIReF in May, reflecting the strong impact of the economic standstill in the months of confinement, which has led to falls of 32% in April compared to the same month last year and 38% in May in national accounting terms. However, uncertainty remains widespread as the pace of recovery is not yet known.

FIGURE 25. EVOLUTION OF VAT COMMON TAX REGIME IN NA (%VAR.)

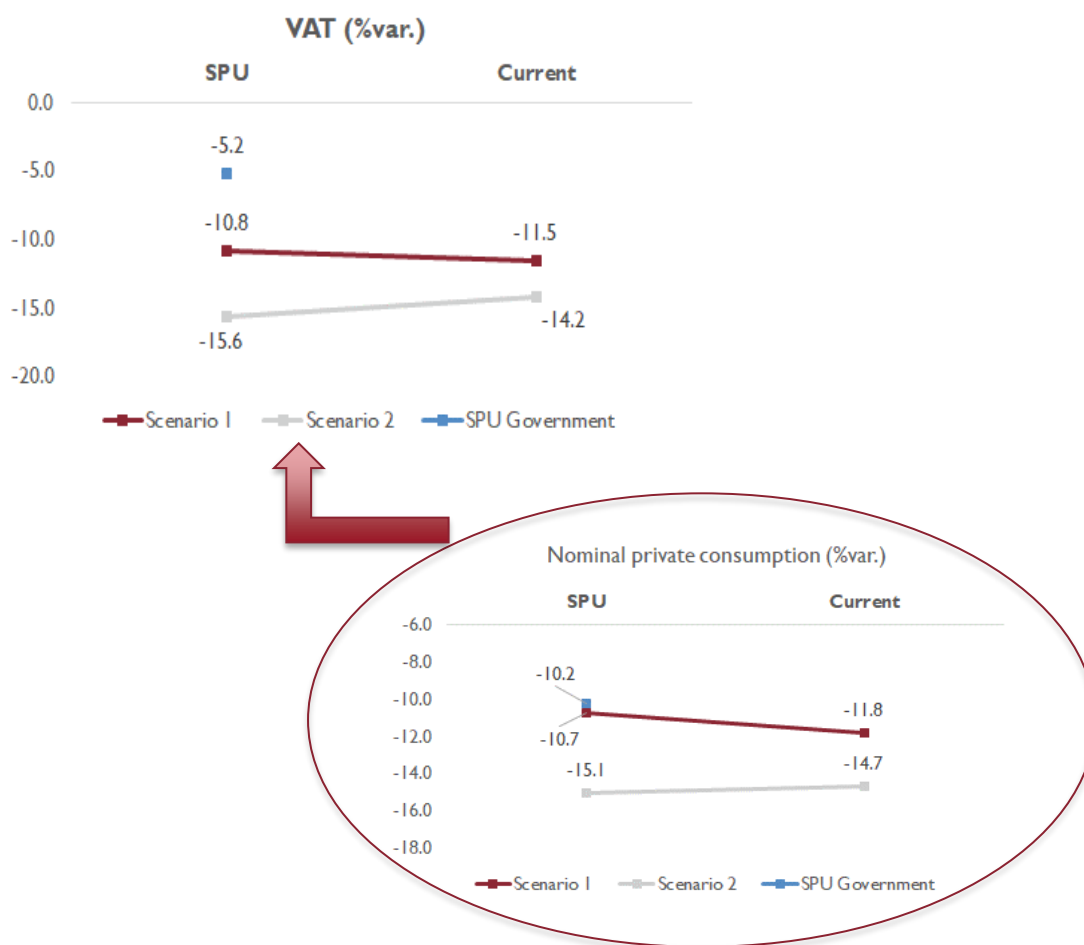
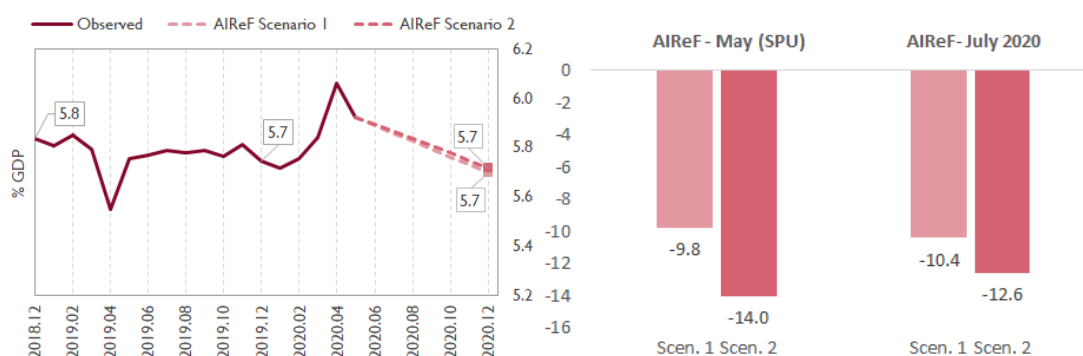


FIGURE 26. EVOLUTION OF VAT IN CASH (%GDP)



4.2.4. Special Taxes

Collection of special taxes has been revised downwards in both Scenario 1 and Scenario 2, but more strongly in the first scenario. Confinement has largely penalised the collection of this type of tax. In particular, the tax on hydrocarbons has been the most affected due to the lack of mobility caused

by the state of alarm. Neither the evolution of collection so far this year nor the update of the forecast of the macroeconomic variable most related to its evolution have seen an improvement, so this type of tax has been revised downwards.

FIGURE 27. EVOLUTION OF SPECIAL TAXES COMMON TAX REGIME IN NA (%VAR.)

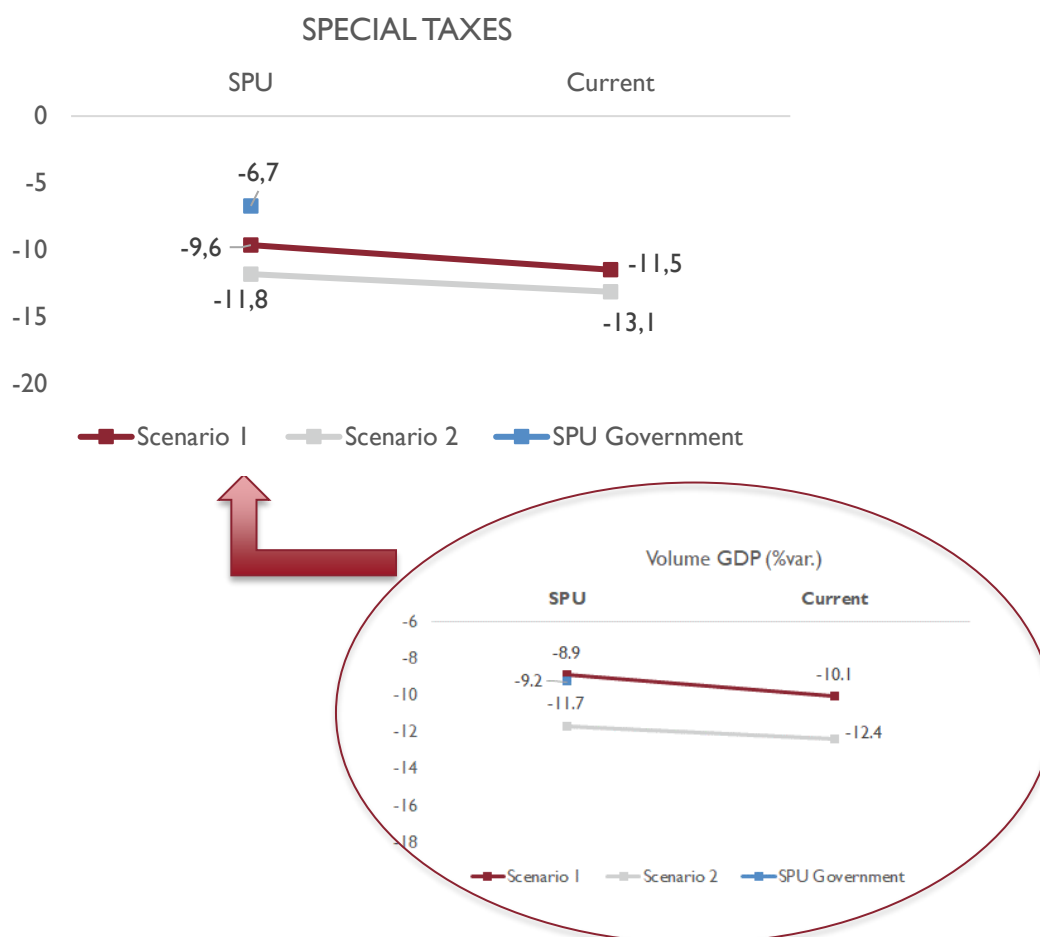
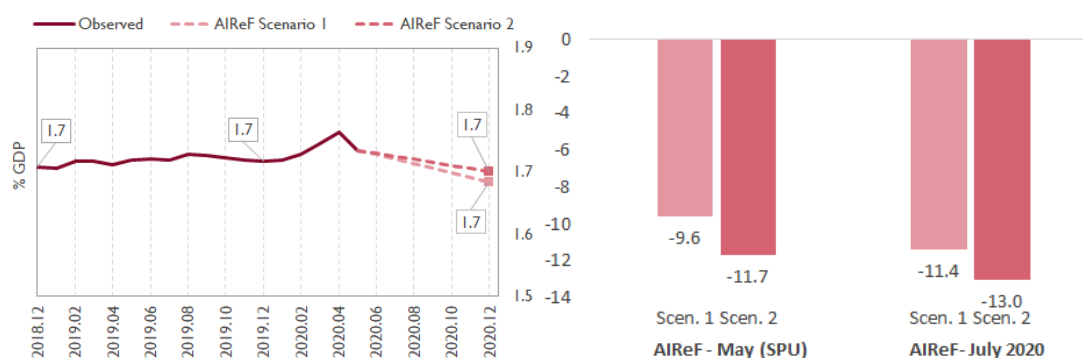


FIGURE 28. EVOLUTION SPECIAL TAXES IN CASH (%GDP)



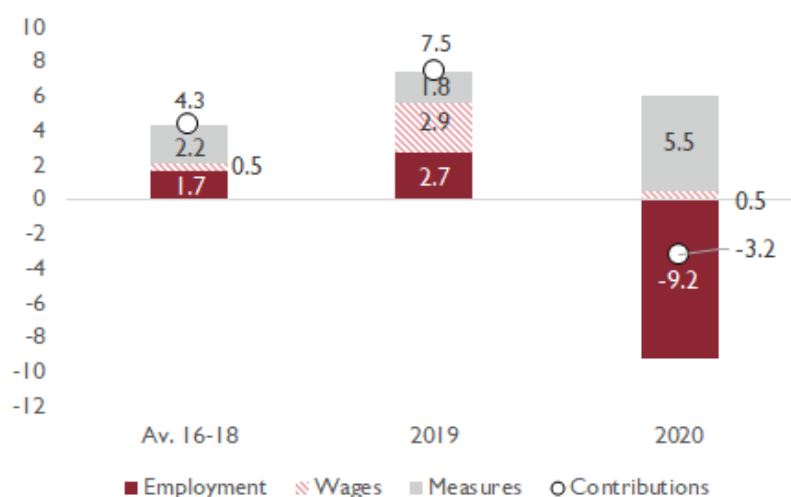
4.2.5. Social security contributions

AIRcF estimates that social security contributions will reach between 13.9% and 14.1% of GDP in 2020, 0.8-0.9% more than the estimate presented in May.

The main reason for these differences is a change in approach to measures involving exemption from contributions, which are now considered to be an increase in subsidy expenditure rather than a reduction in contributions, in line with the approach followed by the IGAE. The difference in impact between the two scenarios is due both to a higher exemption from contributions in scenario 2 and to a macro effect, which reduces contributions in scenario 1.

The determinants of the tax base, wages and employment, have been modified by the new data available, causing contribution revenue to fall in 2020 somewhat more than expected in May for scenario 1 and somewhat less in scenario 2. The influence of employment is key to the decline, as it is mitigated by the measures and, to a lesser extent, by the rise in wages compared to the previous forecast. For 2020, both the measures already approved before the crisis and those aimed at mitigating its effects are included. The former include an increase in contributions for non-professional caregivers, for recipients of the over-52 benefit (which will also affect 2021), a reduction in flat-rate allowances and an increase in the minimum wage approved for 2020. Among the measures approved to deal with the crisis, the measures to exempt companies using ERTes (in different percentages depending on the period, the worker's situation and the size of the company) and self-employed workers affected by the drop in activity from paying contributions are accounted for as an increase in expenditure on subsidies aimed at increasing contributions for the amounts exempted.

FIGURE 29. DECOMPOSITION OF THE GROWTH OF SOCIAL CONTRIBUTIONS



4.2.6. Other revenue

For other revenue, the forecast remains unchanged from the report on the SPU, maintaining a weight of 4.1%, which is in line with the Government's forecast. This revenue includes revenue from sales and property income, with an approximate weight of 3.6% of GDP and other capital revenues for which both the Government and AIReF expect a substantial growth of around 40%, due to the allocation of a higher capital revenue resulting from the reversal due to the end of the concession for the AP-4 and AP-7 highways in the CG for €1,745 million and which will be offset by expenditure on gross fixed capital formation.

4.3. Expenditure forecast

AIReF increases its public expenditure forecast in both scenarios with respect to the report on the SPU, to between 52.2% and 54.8% of GDP. AIReF estimates that expenditure will increase by 1.8% and 1.6% in scenarios 1 and 2, respectively. As regards the breakdown by expenditure heading, the items responsible for this increase are mainly social transfers in cash and subsidies and, to a lesser extent, intermediate consumption.

TABLE 5. EXPENDITURES AS % GDP AIREF

	SPU (1)		Changes (2)		Current forecast (3)=(1)+(2)	
	Scen 1	Scen 2	Scen 1	Scen 2	Scen 1	Scen 2
EXPENDITURE	50.4	53.2	1.8	1.6	52.2	54.8
Compensation of employees	12.5	13.1	0.1	0.0	12.6	13.0
IC + STK acq.mkt	9.1	9.6	0.3	0.3	9.3	9.9
Social benefits in cash	20.1	21.3	0.6	0.5	20.7	21.9
Interest	2.5	2.6	0.0	0.0	2.5	2.6
GFCF	2.7	2.8	-0.1	-0.1	2.6	2.7
Other expenditure	3.6	3.7	0.8	0.9	4.4	4.7
NET LENDING/BORROWING	-10.9	-13.8	-1.0	-0.6	-11.9	-14.4

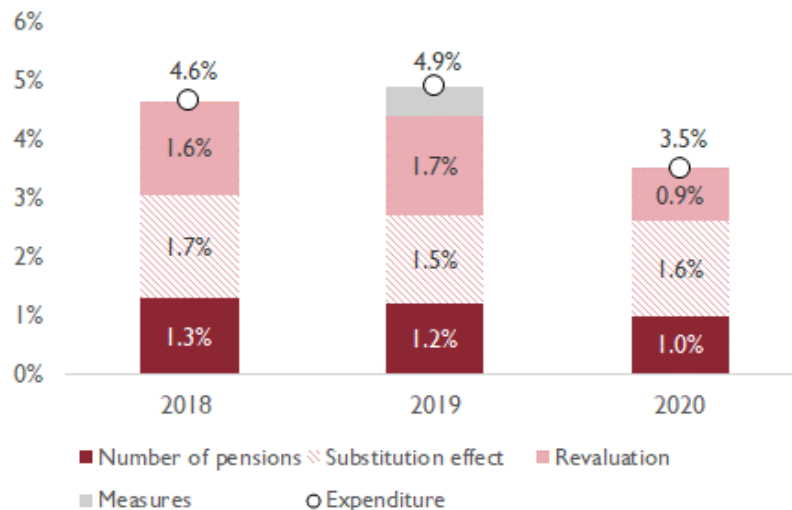
4.3.1. Social Transfers in Cash

AIReF forecasts that social transfers in cash will increase to 20.7% of GDP, or 21.9% of GDP in scenario 2, 0.6% and 0.5% more, respectively, than projected in May, and slightly higher than projected in the Report on the SPU even in scenario 1 (20.6%). The change is mainly due to the higher expenditure estimated for the measures adopted in 2020 due to COVID-19, as well as the approval of the Minimum Living Wage. In particular, the average duration of ERTes and the benefit for cessation of activity has increased from 3.5 months to between 5 and 6 months for ERTes and to more than 4 months for the benefit for cessation of activity. The lower effective number of people who entered ERTes (3.4M instead of the expected 4M) reduces this increase somewhat. This is compounded by a more pronounced denominator effect in Scenario 1 due to the more adverse macro outlook that is now estimated.

AIRcF maintains its estimate of pension expenditure growth of 3.5% for 2020.

With regard to the composition of growth, it is considered that the revaluation was 0.9%, and the hypothesis that the substitution effect will be 1.6% and that the number of pensions will grow by 1% during the year is maintained, despite the fact that growth has been lower in recent months.

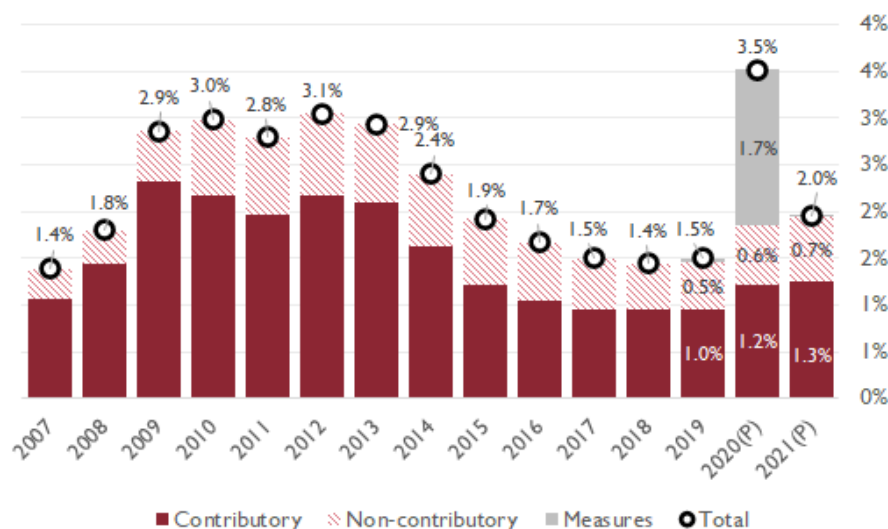
FIGURE 30. PENSION EXPENDITURE GROWTH AIRcF FORECAST



In 2020 unemployment benefits increase from 1.5% GDP to between 3.2% and 4.1% GDP, 0.1% more than the May estimate in both scenarios.

This heading includes the cost of ERTE measures, the payment of unemployment to temporary workers who were not entitled to it and the cost of benefits for household employees. The differences from the May estimate are due to the longer average duration of ERTes and the revision of the macroeconomic forecasts.

FIGURE 31. EVOLUTION OF UNEMPLOYMENT EXPENDITURE AS % DGP. AIRcF FORECAST



For 2020, the rest of the items under the heading are also affected by the extraordinary measures, increasing their weight over GDP compared to the May estimate by 0.3% and 0.4%, up to 2.1% and 2.3%. The differences are due to the increase in the duration of the benefit for cessation of activity, the increase in expenditure for Temporary Incapacity for Work and the inclusion of two new measures: access to the benefit for cessation of activity for temporary self-employed workers and the approval of the Minimum Living Income.

4.3.2. Subsidies

Subsidies are up by 0.8% to 0.9% from our May estimate, almost exclusively due to the change in accounting approach for contribution exemptions. In our May report, these measures were accounted for as a reduction in contributions, and in this report they are accounted for as an increase in subsidies to be used to cover exempted contributions, as published by the IGAE in its latest data. In addition, the granting of aid as a result of the measures adopted due to COVID-19 has led to an increase in subsidies in the CG and regional sub-sectors.

4.3.3. Intermediate consumption

The estimate for intermediate consumption increased by about 0.3% of GDP, centralised in the regional sub-sector. Of this increase, two thirds is due to the reclassification of expenditure from other items to intermediate consumption as a result of new information and one third is due to new expenditure measures related to the pandemic. In this sense, only 0.1% of GDP has contributed to the increase in public expenditure in each of the scenarios considered.

4.3.4. Other expenditure items

The forecast for Gross Fixed Capital Formation has been revised downwards compared to the previous report. This revision is concentrated in the Regions and LGs. In any case, it should be recalled that for 2020 a considerable increase is expected in the Gross Capital Formation item as a result of the reversal of the AP-7 and AP-4 concession in the CG for an amount of 1,745 million euros, although with no impact on the deficit as it leads to an entry in revenue for the same amount.

There is no significant change in the rest of the expenditure items with respect to what was estimated in the previous report on the SPU. The rest of the expenditure headings remain in line with our previous estimates. This is either

because there have been no changes or because the impact of the approval of new measures in recent months has not been sufficiently relevant as a percentage of GDP.

4.4. Analysis by sub-sectors

The fiscal scenario at the sub-sector level has changed with respect to that presented in the report on the SPU. The CG becomes the guarantor of the crisis by assuming part of the expenditure of the other sub-sectors. The pandemic is having a major impact on the public accounts, although the most pronounced effect is occurring in the CG, resulting in a notable increase in the sub-sector's deficit and public debt for 2020.

The CG assumes a part of the deficit deterioration corresponding to the SSF and regional sub-sectors. Thus, AIRcF estimates an increase in the CG deficit of between 3.2% and 2.7% of GDP to reach 7.7% in scenario 1 and 8.3% in scenario 2, mainly as a result of transfers and, to a lesser extent, the downward revision of tax revenue. For its part, the deficit of the SSF, despite the transfers already approved, will be between 3.9% and 5.1% of GDP, also reflecting the impact of the new measures approved. The Regions' deficit estimate has also been reduced, although to a lesser extent than the new transfers due to the higher estimated health expenditure and the new measures approved.

TABLE 6. BREAKDOWN OF NET LENDING/BORROWING BY SUB-SECTORS

SCENARIO 1

	2020					
	Pre-pandemic forecast (1)	COVID effect			Total COVID effect (2) = (a)+(b)+(c)	Actual forecast (3)=(1)-(2)
		Denominator effect (a)	Measures effect (b)	Macro effect (c)		
PAs	-2.2	-1.0	-4.1	-4.7	-9.8	-11.9
CG	-0.9	-0.6	-3.3	-3.0	-6.8	-7.7
FSS	-1.3	-0.3	-1.3	-0.9	-2.5	-3.9
Regions	-0.3	-0.1	0.7	-0.6	-0.1	-0.4
LGs	0.3	0.0	-0.2	-0.2	-0.3	0.0

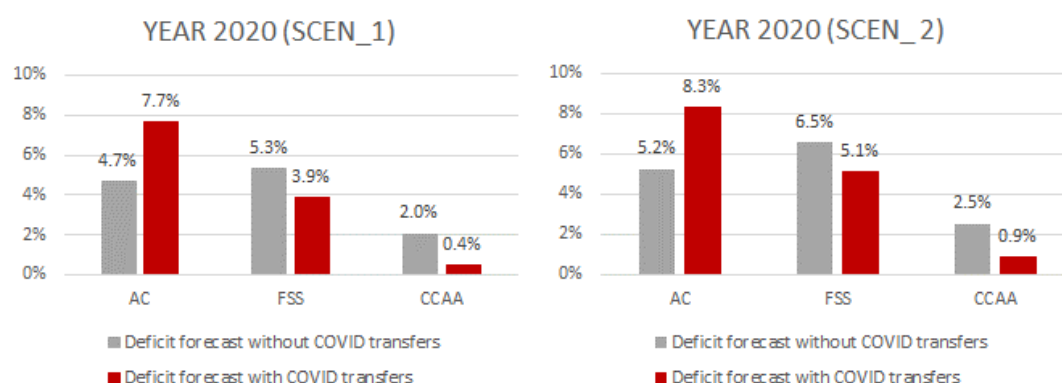
SCENARIO 2

	2020					
	Pre-pandemic forecast (1)	COVID effect			Total COVID effect (2) = (a)+(b)+(c)	Actual forecast (3)=(1)-(2)
		Denominator effect (a)	Measures effect (b)	Macro effect (c)		
PAs	-2.2	-1.4	-4.9	-5.9	-12.3	-14.4
CG	-0.9	-0.7	-3.4	-3.3	-7.4	-8.3
FSS	-1.3	-0.5	-1.8	-1.5	-3.8	-5.1
Regions	-0.3	-0.2	0.5	-0.8	-0.5	-0.9
LGs	0.3	0.0	-0.2	-0.3	-0.5	-0.2

In principle, these transfers would be neutral at the General Government level, although they could lead to changes in the behaviour of individual

administrations due to the increased availability of resources. As they are internal flows, these transfers between sectors impact the deficit by sub-sectors and are offset for the purposes of calculating the deficit and the debt of the PA sector. At the sub-sector level, the reduction in the deficit of the Regions and SSF translates into an increase by the same amount in the CG deficit, putting upward pressure on the level of State debt.

FIGURE 32. DEFICIT OF CG, SSF AND REGIONS WITH AND WITHOUT TRANSFERS FROM CG DUE TO THE COVID-19 CRISIS FOR 2020 (AIReF FORECAST AS. % GDP)



4.5. Central Government

AIReF estimates that the CG deficit could reach 7.7% in 2020 in scenario 1 and worsen to 8.3% in scenario 2, from 1.3% GDP in 2019. The worsening with respect to the previous report is mainly due to expenditure on transfers to other sub-sectors and slightly due to the worsening of the macro environment in the first scenario that becomes a slight improvement in the second scenario.

FIGURE 33. NET LENDING/BORROWING CG FORECAST (%GDP)

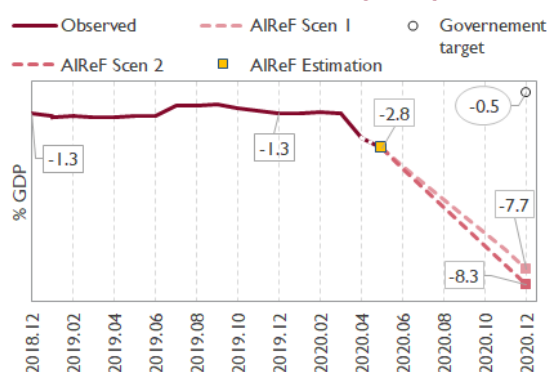
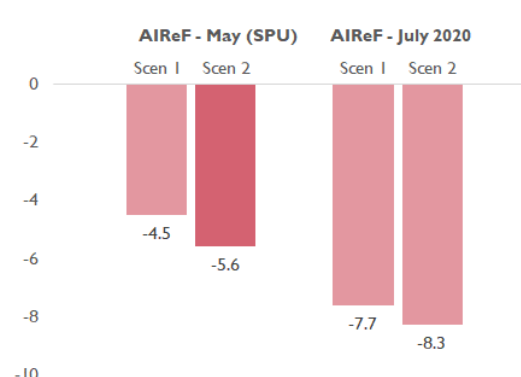


FIGURE 34. UPDATE OF NET LENDING/BORROWING CG FORECAST



4.5.1. Revenue forecast

The reduction in the forecast of tax revenues is offset by the denominator effect of lower GDP, with revenue remaining at the same level relative to GDP in scenario 1 and improving by 0.3% compared to scenario 2, to 16.7% of GDP in both scenarios. The different behaviour between scenarios is explained by the fact that the change in the macroeconomic scenario has been asymmetric, improving the forecast of the macro variables that most affect tax revenues. Thus, the improvement in PIT and VAT with respect to scenario 2 outlined in the previous report leads revenue in the CG to increase its weight over GDP by 0.3%, with this sub-sector assuming all the change in the macroeconomic context by maintaining instalment payments to the Regions and LGs.

FIGURE 35. REVENUES CG FORECAST (%GDP)

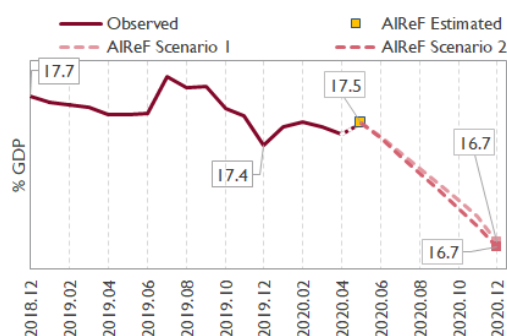
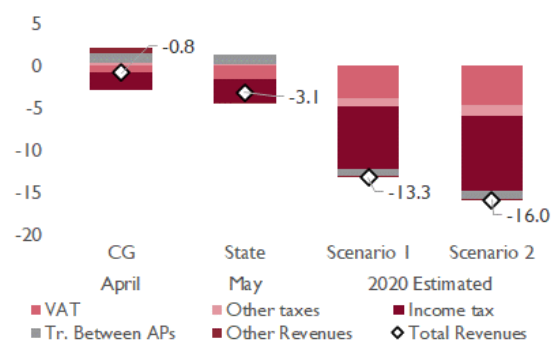
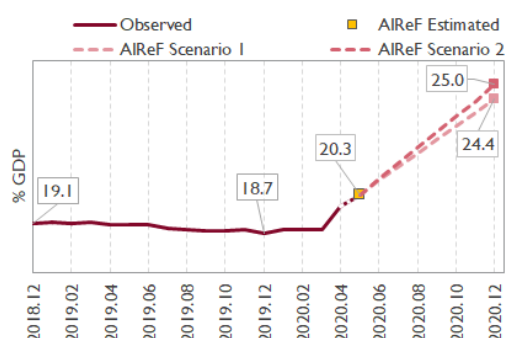
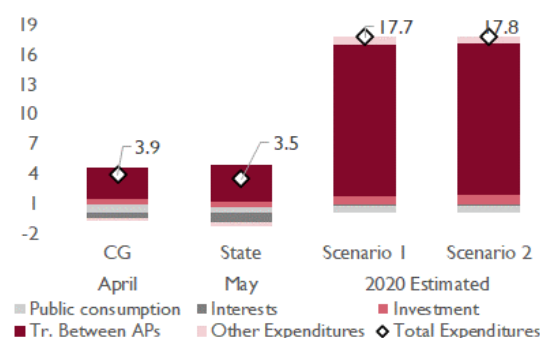


FIGURE 36. CONTRIBUTION TO UPDATE OF REVENUES CG



4.5.2. Expenditure forecast

AIReF forecasts that CG expenditure will grow between 3.2% and 3% of GDP more than estimated in the previous report, to reach between 24.4% and 25% of GDP, mainly due to transfers to other sub-sectors. Since the publication of the Report on the APE, last May, the Government approved measures to tackle the COVID-19 that imply greater expenditure for the CG of some €32.5 billion, of which nearly €32 billion correspond to transfers from the CG to other sub-sectors to alleviate the effects of the pandemic. Previously, at the beginning of the COVID-19 crisis, CG expenditure measures to combat the virus had represented around €3 billion, half of which corresponded to transfers to other sub-sectors. It is precisely the increase in expenditure on transfers between PAs that has led to the deterioration of the CG deficit

FIGURE 37. EXPENDITURES CG FORECAST (%GDP)

FIGURE 38. CONTRIBUTION TO UPDATE OF EXPENDITURES CG


On the one hand, the CG has made new transfers to the SSF for the amount of **€15.7 billion, 1.4% of GDP**. These transfers are to balance the accounts of the SSF due to the effect of COVID-19, for an amount of €14 billion, as well as to finance the Minimum Living Income allowance estimated by AIReF at just over €1.7 billion in 2020. However, the amount of transfers could even increase in order to cover, before the end of the year, the deficit that would remain to be financed according to AIReF's estimates (see Box 5).

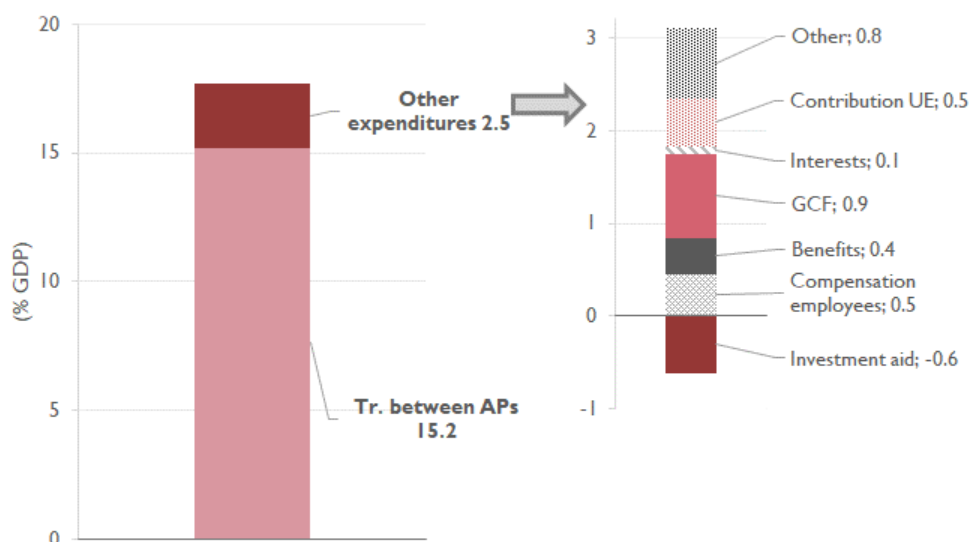
The CG has also made new transfers to the Regions for an amount of more than 16 billion, between 1.4% and 1.5% of GDP. Among the new transfers approved, the COVID-19 Fund for the Regions, amounting to 1€6 billion, of which €50 million are for Ceuta and Melilla, stands out for its quantitative importance.

Other factors contributing to the increase in expenditure compared to the report on the SPU are the increase in subsidies and Spain's commitments to the EU. On the one hand, the Government approved aid to the wine and automotive sector due to the COVID-19 crisis, resulting in an increase in subsidies of nearly €350 million. On the other hand, Spain's commitments to the EU increased by some 500 million, mainly due to the latest changes to the EU budget leading to a higher Spanish contribution in 2020.

In conclusion, CG non-financial expenditure is expected to increase by 17.7% compared to 2019 in scenario 1, with 15% of the growth corresponding to transfers between PAs. According to AIReF's forecasts, transfers between PAs will increase significantly over the year to contribute more than 85% to expenditure growth in 2020. Secondly, it is worth noting the contribution of 0.9% to the increase in expenditure at year-end due to the increase in gross capital formation (GCF) due to the reclassification of two sections of the AP-7 highway

for an amount of €1,745 million, with no impact on the deficit¹⁰. Finally, mention should be made of the impact of the contribution to the EU and of compensation of employees, of 0.5% respectively.

FIGURE 39. CONTRIBUTION TO GROWTH TO EXPENDITURE ITEMS (%)



Moreover, almost all of the increase in expenditure is of a non-recurring nature, which would distort the calculation of the expenditure rule in 2021. Expenditure measures for the COVID-19 crisis alone, including non-recurring transfers to other sub-sectors for 32 billion, and the reversal of the toll roads for €1,745 million would reach almost €35.5 billion in 2020. If other operations of a non-recurring nature estimated for this year are added, such as the expenditure estimated for the cold drop and for the Asset Protection Schemes (APS), the amount could rise to around €38 billion. In years such as the current one in which non-recurring operations represent such a significant amount, it is more necessary to deduct these operations from the starting point in order to calculate the growth of the computable expenditure, otherwise this calculation would be completely distorted and would not reflect the real growth of expenditure.

Finally, it is worth mentioning the increase in the fiscal risk assumed by the CG due to the new granting of guarantees and sureties for €57 billion, in addition to the more than €104 billion contracted as of the date of the Report on the SPU. The provision of guarantees by the CG as a result of the pandemic represents a significant increase in contingent liabilities. In fact, Spain is among the main economies in the Eurozone with the highest use of public guarantees.

¹⁰ The reversion of two sections of the AP-7 and AP-4 highways due to the end of the concession contract has a zero effect in terms of deficit since, as the State did not have to pay anything for these assets, an allocation of the same amount is made to revenue.

The provision of guarantees, although it has no effect on the 2020 deficit, poses a fiscal risk in the future.

4.6. Social Security Funds

The deficit of the SSF increases in 2020 to a range between 3.9% and 5.1% GDP depending on which scenario materialises, an improvement of 1.1% and 1% compared to the previous report. The positive effect on the deficit of CG transfers has been somewhat mitigated by the increased cost of the measures. In addition, there has been an increase in both revenue and expenditure due to the change in accounting for social contribution exemption measures.

SSF contributions have increased their weight over GDP from 12.2 in both scenarios to 13 and 13.1% for scenarios 1 and 2, respectively. This increase is due to certain changes in the macroeconomic scenario (downwards in scenario 1, upwards in scenario 2), but above all to the different approach to accounting for contribution exemption measures in this report.

FIGURE 40. EVOLUTION OF SSF NET LENDING/BORROWING (%GDP)

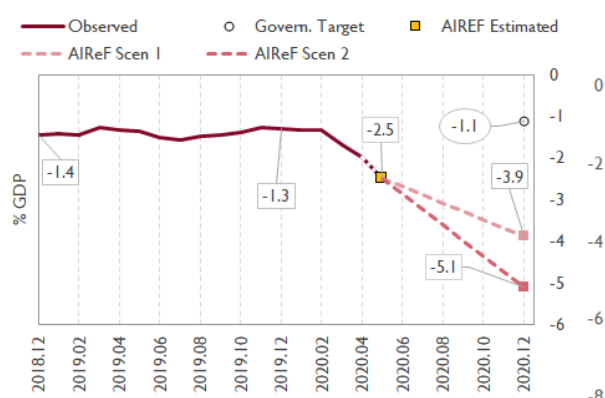


FIGURE 42. EVOLUTION OF SSF REVENUE (%GDP)

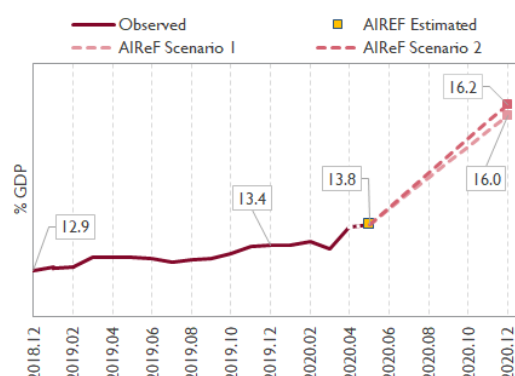


FIGURE 41. UPDATE OF NET LENDING/BORROWING SSF FORECAST

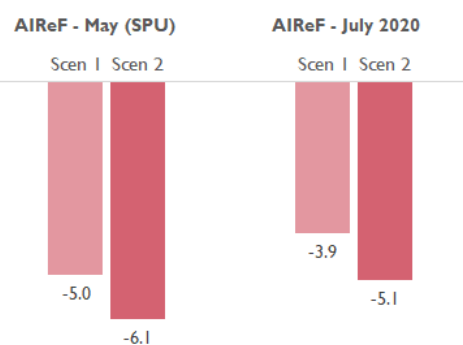


FIGURE 43. CONTRIBUTION TO UPDATE OF REVENUES SSF

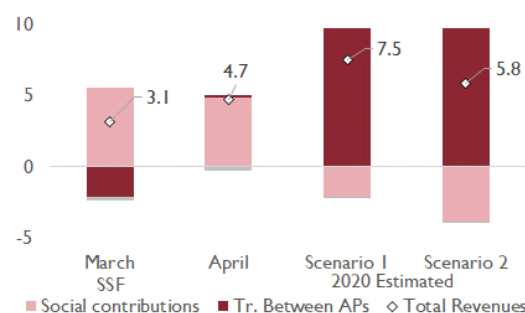
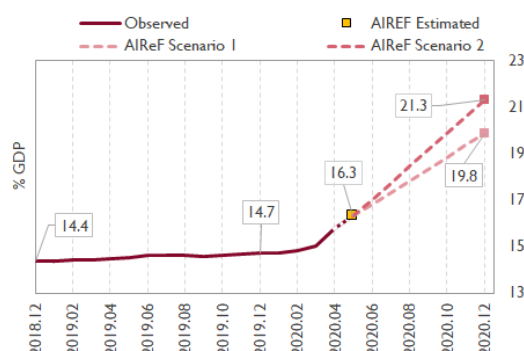
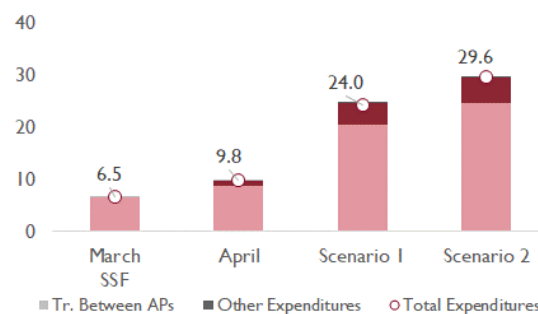
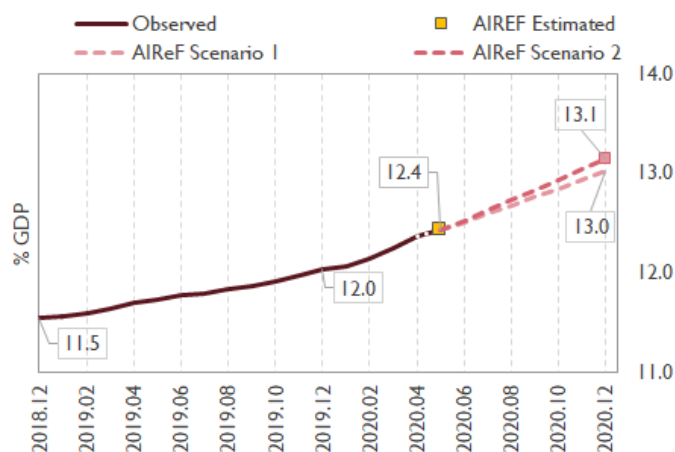


FIGURE 44. EVOLUTION OF SSF EXPENDITURES (%GDP)

FIGURE 45. CONTRIBUTION TO UPDATE OF EXPENDITURES SSF

FIGURE 46. EVOLUTION OF SOCIAL CONTRIBUTION (%GDP)


During the state of alarm caused by the COVID-19 crisis, the Government has approved measures to alleviate the effects of the crisis in the amount of between 2.9% and 3.3% of GDP, 0.5% more than estimated in May in both scenarios¹³. About 0.2% is due to the approval of the Minimum Living Income, and the rest is almost entirely due to the greater average duration of ERTE measures and the benefit for cessation of activity in both scenarios. The increase is mitigated by lower estimates of the cost of contribution exemptions due to lower exemption rates for the following months, but this reduction is barely 0.1% of GDP.

BOX 5. FINANCIAL FLOWS BETWEEN THE CG AND THE SSF

The CG finances a part of the activity carried out by the SSF by making transfers and, where appropriate, by granting loans. The financing approved for 2020 amounts to €61 billion, of which €31 billion are transfers and €30 billion are loans, in both cases doubling the amounts granted in 2019. However, according to the deficit estimated by AIREF for 2020, these amounts are expected to increase further before the end of the year.

1. Transfers.

Initially, transfers from the CG to the SSF were expected to be slightly higher in 2020 than in 2019 (an increase of about 1.5%). These transfers are intended, on the one hand, to finance benefits of a non-contributory nature, including non-contributory disability and retirement pensions, minimum pension supplements and dependency allowances; and, on the other hand, to support budgetary balance.

TRANSFERS FROM CG TO SSF IN 2019 (EXECUTED) AND IN 2020 (AIREF'S FORECAST) BUDGETARY AND NATIONAL ACCOUNTING (Millions of euros)

	BUDGETARY ACCOUNTING					NA	
	2019		2020			2019	2020
	Initial credits	Recognised obligations	Initial credits	COVID changes	Final credits	Executed	AIReF forecast
SSF							
Social Security System (SSS)	14,785	15,484	14,785	14,873	29,658	15,553	31,771
Current transfers	14,768	15,464	14,768	14,873	29,641	15,533	31,751
Non-contributory benefits	13,044	13,123	13,044	371	13,415		238
New MLI non-contributory benefit				500	500		1,743
To support budgetary balance	1,334	1,934	1,334		1,334		
To balance the impact of COVID-19 on accounts			0	14,002	14,002		14,002
Other	390	407	390		390		
Capital transfers	18	20	18		18	20	20
SEPE	55	0	55		55	0	0
FOGASA	91	0	91		91	0	0

However, as a consequence of the COVID-19 crisis, new transfers from the State to the SSF have been approved:

- Extraordinary provision of €14,002 million to balance the impact of COVID-19 on the accounts (Royal Decree-Law 19/2020)

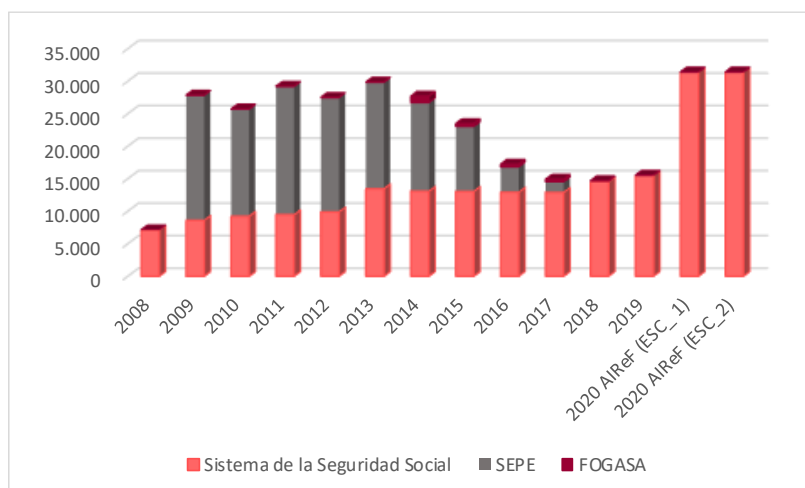
Additional provision of €371 million to finance non-contributory pensions and family protection (Royal Decree-Law 19/2020). Of this amount, only €238 million is taken into account, which is the increase over what was executed in 2019, which is the starting point for AIReF's forecasts for 2020

Extraordinary provision of €500 million to finance the Minimum Living Income (MLI) as a new permanent non-contributory benefit (Royal Decree-Law 20/2020). Although the cost announced by the Government amounts to €1.5 billion for 2020, AIReF estimates that expenditure will reach €1.743 billion this year. (see section 4.1.1).

On the other hand, since the SEPE (*Servicio Público de Empleo Estatal* - State Public Employment Service) and FOGASA (both bodies of the CG but part of the SSF for the purposes of the deficit in the national accounts) did not receive any transfers from the State in 2019, it is expected that they will not receive any in 2020 either. However, given the significant unemployment expenditure expected from the economic crisis and the payment of ERTes, it is foreseeable

that the State, as in previous crises, will assume the financing of SEPE unemployment benefits not covered by social contributions. During the Great Recession, in the period 2009-2012, transfers to the SEPE averaged some €18.2 billion per year, reaching €19.7 billion in 2011

EVOLUTION OF TRANSFERS FROM CG TO THE SSF. NATIONAL ACCOUNTS
(millions of euros)

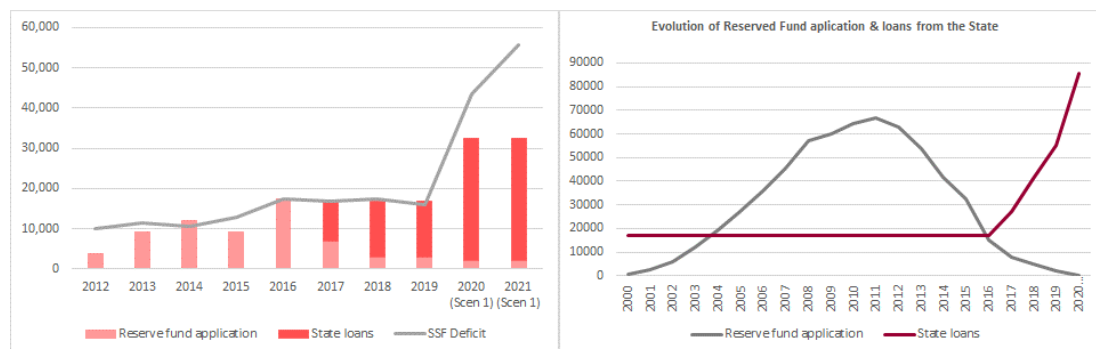


2. Loans

In addition to financing through transfers, the State can also grant loans to the SSF sub-sector to finance its deficit.

In the first decade of the 2000's, the SSF recorded surpluses that made it possible to build up the *Fondo de Reserva de la Seguridad Social* (Social Security Reserve Fund - known as "the pension piggy bank"). The first deficits were recorded in 2010, and from 2012, when these deficits exceeded 10 billion, the Reserve Fund began to be used to finance the deficit caused by contributory pensions. As the Fund has been depleted, the financing of the deficit has been supplemented by loans from the State.

EVOLUTION OF THE RESERVE FUND AND STATE LOANS AND FINANCING OF THE SSF DEFICIT 2019
(DATA EXECUTED) AND 2020 (AIREF'S FORECAST).
(Millions of euros)



This explains why, until 2016, the social security debt remained stable at around €17 billion. In 2020, although a loan equal to that of 2019 was initially planned for €13.8 billion, the COVID-19 crisis led to the additional approval of a new loan for €16.5 billion, increasing the debt in 2020 by €30.3 billion, double that of 2019. This will lead to an increase in debt from €55 billion on 31 December 2019 to over €85 billion by the end of 2020.

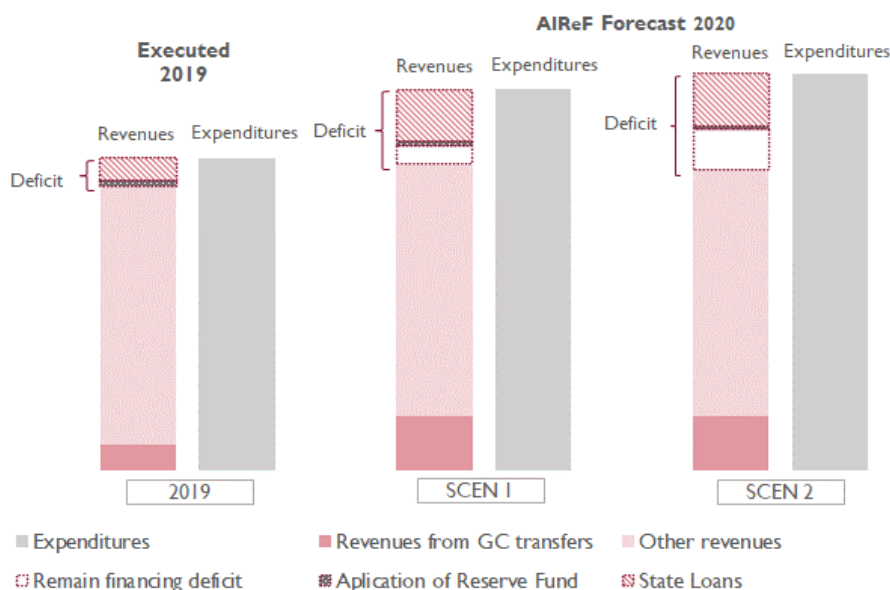
AIReF estimates a deficit for the SSF of between €43.6 and €55.7 billion in 2020. The State has so far granted loans amounting to €30.3 billion. Even if the outstanding balance of the Reserve Fund were to be applied, if the SSF deficit were not reduced by the above-mentioned transfer to the SEPE to finance unemployment, the outstanding part would be between €11 and €23 billion. In the event that the CG does not make a new transfer to the SSF, it would be necessary to grant a new loan for the outstanding amount, which would bring the debt to levels around €100 billion.

FINANCING FROM CG TO SSF IN 2019 (EXECUTED) AND 2020 (AIREF'S FORECAST). NATIONAL ACCOUNTS
(Millions of euros)

SSF	NA		
	2019	2020 (SCEN_1)	2020 (SCEN_2)
1. Revenue	167,035	179,616	176,797
Revenue from AC transfers	15,533	31,771	31,771
Other revenue	151,502	147,845	145,026
2. Expenditure	183,087	223,221	232,552
3. Borrowing requirements (1)-(2)	-16,052	-43,605	-55,755
4. Loans	13,830	30,330	30,330
5. Application of the Fondo de Reserva (*)	2,893	2,150	2,150
6. Difference (3)-(4)-(5)	671	-11,125	-23,275

(*) For 2020, assuming the application of the outstanding balance of the Fondo de Reserva (Reserve Fund)

SSF DEFICIT AND FINANCING. YEAR 2019 AND AIREF's 2020 FORECAST (% GDP)



These measures do not affect the various agents of the SSF in the same way.

By carrying out a simplified analysis, based on the pre-COVID situation of each agent, the impacts are broken down into a denominator effect, a measure effect and a macro effect. Regarding the macro effect, within the SSF, the reduction in cyclical revenue is almost entirely from the SSS, while the increase in cyclical expenditure is almost entirely from the SEPE. Of the projected increase in the SSF deficit (between 2.5% and 3.8% GDP), slightly more than half pertains to the SSS, and the rest to the SEPE. Compared to what was published in May, the distribution has changed mainly due to the increase in the weight of the measures and the transfers from the Central Government.

TABLE 7. NET LENDING/BORROWING OF SOCIAL SECURITY FUNDS BY AGENT (%PIB)

ESCENARIO 1

		2020				
	Pre-pandemic forecast (1)	COVID effect			Total COVID impact (2) = (a)+(b)+(c)	Current forecast (3)=(1)-(2)
		Denominator effect (a)	Measures effect (b)	Macro effect (c)		
SSF	-1.3	-0.3	-1.3	-0.9	-2.5	-3.9
SSS	-1.4	-0.3	0.3	-0.7	-0.6	-2.1
SEPE	0.1	0.0	-1.7	-0.2	-1.9	-1.8

ESCENARIO 2

		2020				
	Pre-pandemic forecast (1)	COVID effect			Total COVID impact (2) = (a)+(b)+(c)	Current forecast (3)=(1)-(2)
		Denominator effect (a)	Measures effect (b)	Macro effect (c)		
SSF	-1.3	-0.5	-1.8	-1.5	-3.8	-5.1
SSS	-1.4	-0.5	0.0	-0.9	-1.4	-2.9
SEPE	0.1	0.0	-1.8	-0.6	-2.4	-2.2

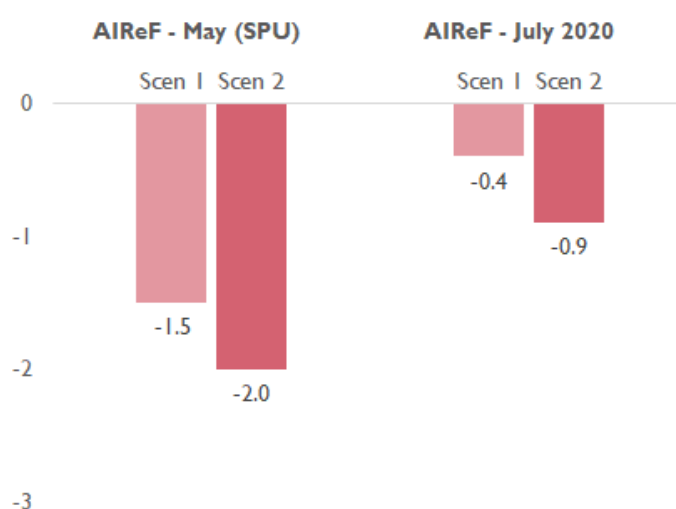
4.7. Regions

4.7.1. Analysis of the sub-sector

AIRcF estimates that the Regions could reach a deficit of between 0.4% and 0.9% of GDP in 2020, once the transfers of the COVID-19 Fund have been incorporated (1.4%/1.5%). As indicated in the May report, the impact of the pandemic on the Regions could be largely cancelled out by the materialisation of the transfers of €16 billion from the fund (€15,950 for the Regions, as €50 million are for Ceuta and Melilla), which was finally approved by Royal Decree-Law 22/2020, provided that the amounts received are used exclusively to cover the higher expenditure and lower revenue resulting from COVID-19. With the incorporation of these funds, the outlook for the sub-sector as expressed in the previous report improves, depending on the scenario, by the 1.4% or 1.5% of GDP represented by transfers. On the contrary, the current information available on health expenditure incurred up to May, the impact

of the measures adopted by the Regions in other areas and the expected loss of revenue, especially in the Regions governed by the provincial regime, has worsened the assessment of the impact of COVID-19 at regional level, which could range from 1.5% to 2% of GDP. In addition, this situation could be worsened by the measures adopted, if necessary, in the field of education for the coming year, unless they are offset by a greater non-execution of other expenditure, and, in the opposite direction, it could be favoured by the implementation of the State's Minimum Living Income (MLI) to the extent that it replaces all or part of the equivalent aid currently regulated in each Region.

FIGURE 47. UPDATE OF NET LENDING/BORROWING SUBSECTOR REGIONS FORECAST (%GDP)



BOX 6. COVID-19 FUND ROYAL DECREE-LAW 22/2020

Main features:

- ✓ **€16,000 M (1.4% of GDP/1.5% of GDP)**
- ✓ **15,950 in favour of the Regions and 50 to Ceuta and Melilla**
- ✓ **Non-repayable and unconditional**
- ✓ **Divided into 4 tranches:**

Tranche 1:

- 6,000 M€
- To pay in July
- Distribution over health and population variables. In the Basque Country and Navarre it is set in the Mixed/Coordinating Commission
- For all the Regions, Ceuta and Melilla

Tranche 2:

- €3,000 M

- To pay in November
- Distribution on health and population variables. In the Basque Country and Navarre it is set in the Mixed/Coordinating Commission
- For all the Regions, Ceuta and Melilla

Tranche 3:

- 2,000 M€
- To pay in September
- Distribution over population aged 3-24 years. In the Basque Country set in the Mixed/Coordinating Commission
- For all the Regions, Ceuta and Melilla

Tranche 4:

- 5,000 M€
- To pay in November
- Distribution over average collection of main regional taxes and transport-related variables (specific amount for Canary Islands, Madrid and Catalonia)
- Only for the Regions under the common tax regime

AIRcF estimates the impact of the pandemic on the regional level at between 1.5% and 2%, increasing the estimate in the May report by 0.3%. The estimate of the impact that COVID-19 may have on the regional accounts for 2020 considers three fundamental elements:

- Health expenditure due to COVID-19 will increase between 0.6% and 0.9% GDP. With current data, AIRcF has increased the preliminary estimate in the May report by a little over 0.1%.
- Measures taken in other areas could have an impact of around 0.2% of GDP.
- An impact of between 0.7% and 0.9% is expected due to the fall in economic activity, 0.2% above the forecast in the previous report.

The projected balance in the sub-sector in 2020 would come from a sharp growth in both revenue, from state transfers, and expenditure, as a result of COVID-19. The pandemic has led to an exceptional increase in expenditure in the Regions, especially in the area of health, which at year-end could be between 8% and 10% above the 2019 level. This, added to the estimated fall in GDP, would increase the weight of expenditure over GDP by between 2.9% and 3.6%. On the other hand, the unconditional transfers received from the

State, both through the Financing System of the Regions under the common tax regime (FSR) and through the COVID-19 Fund, mean that, despite the expected fall in the rest of revenue, an increase in revenue at year-end of between 10% and 8% over the previous year is estimated (between 8% and 7% without counting the negative impact of the Immediate Information System -IIS- in 2019). Thus, revenue would increase by between 3 and 3.3% of GDP (0.2% less when discounting the effect of the IIS of 2019). Without the impact of COVID-19 and the non-repayable funds, the balance that the sub-sector would probably have reached in 2020 would be -0.3% of the currently estimated GDP.

FIGURE 48. AIREF FORECAST 2020. SUB-SECTOR REGIONS. ESTIMATED IMPACT OF COVID-19 ON THE BALANCE (% GDP)

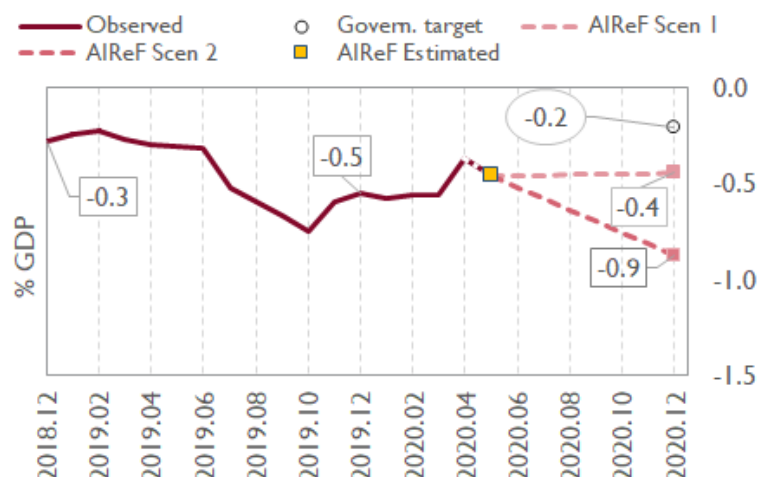


FIGURE 49. AIREF FORECAST 2020. SUB-SECTOR REGIONS. ESTIMATED IMPACT OF COVID-19 ON THE REVENUES. (% GDP)

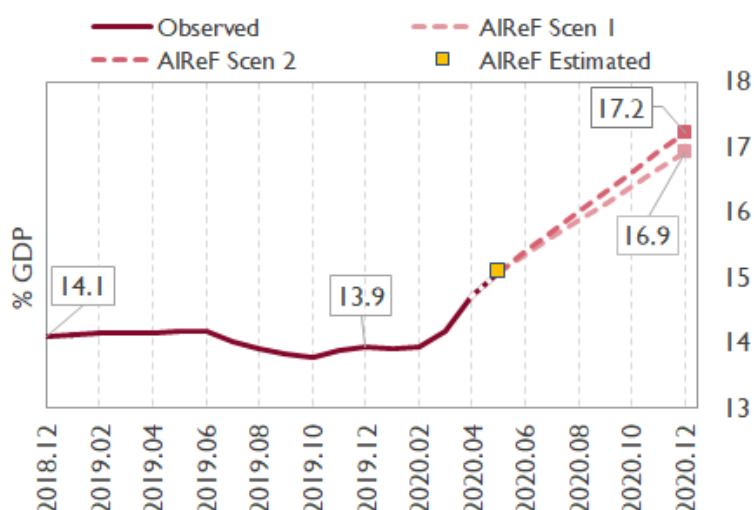
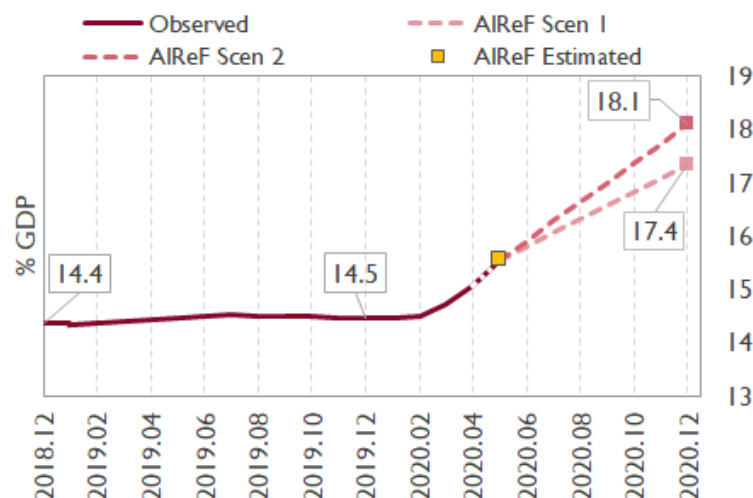


FIGURE 50. AIREF FORECAST 2020. SUB-SECTOR REGIONS. ESTIMATED IMPACT OF COVID-19 ON THE EXPENDITURES (% GDP)



Coverage of expenditure in the first half of the year with the system's resources would be maintained in the second half with the COVID-19 Fund. The instalment payments of the FSR, set by Royal Decree Law 7/2020, have been calculated without considering the expected macroeconomic deterioration and their payment has been anticipated to the months of March and April. A significant part of the 2018 settlement payment has also been anticipated in the first half of the year. This has meant that in the first months of the year the Regions have not seen their balance deteriorate, despite the exceptional increase in expenditure they have had to deal with due to the pandemic and the fall in other revenue in these months. Transfers from the COVID-19 Fund to be paid throughout the second half of the year would allow this situation to continue until the end of the year.

FIGURE 51. CONTRIBUTION TO UPDATE OF REVENUES REGIONS (%VAR)

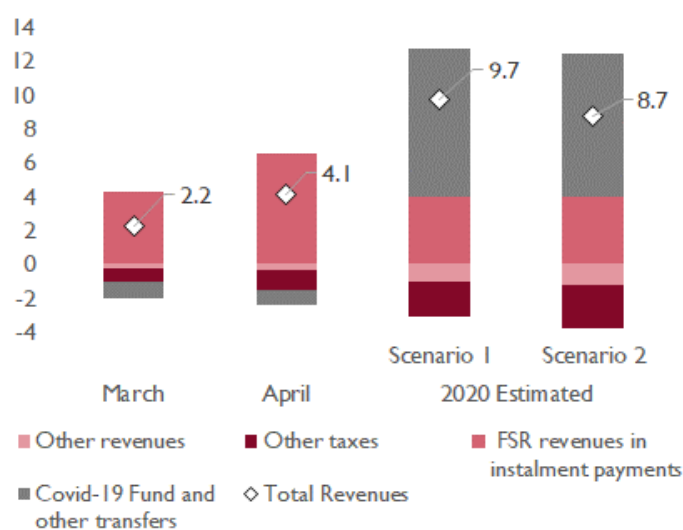
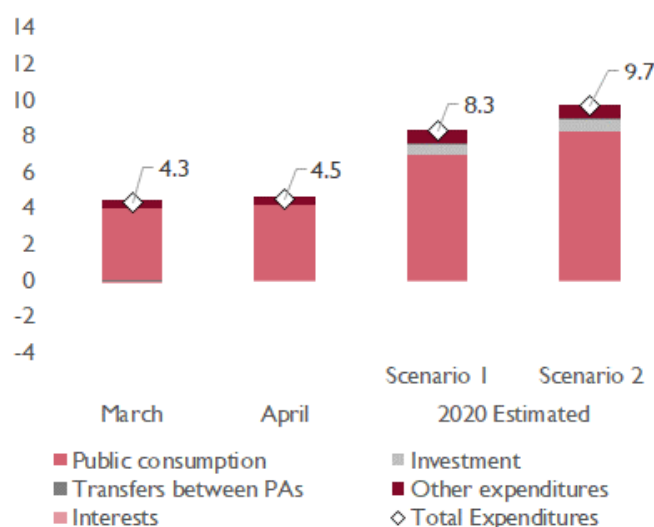


FIGURE 52. CONTRIBUTION TO UPDATE OF EXPENDITURES REGIONS (%VAR)



The significant increase in expenditure that the pandemic is generating at the regional level would place computable expenditure for the purposes of the expenditure rule, largely of a non-recurring nature, well above reference levels. With an estimated growth in current primary expenditure and net payments to the State by the RFS (which constitutes the bulk of computable expenditure in the sub-sector) of between 9% and 10%, a rate of change in computable expenditure along these lines is foreseeable. On the other hand, the fact that it is largely non-recurring may significantly affect the variation in 2021.

However, the uncertainty surrounding the application and measurement of the rule in the current situation makes it impossible to assess it. It is not known how the revenue and expenditure associated with the pandemic will be treated in the Regions, either on a regular or exceptional basis. These uncertainties about the application and measurement of the rule under the current situation prevent an assessment of the final result of the rule in the sub-sector.

In 2020, the impact of the current crisis is expected to be assumed by the CG, and is transferred to the regional sub-sector in the following years. The instalment payments of the regional financing system received by the Regions under the common tax regime, established by Royal Decree Law 7/2020¹¹ were calculated without considering the expected macroeconomic deterioration, i.e. they do not include the expected fall in tax revenue as a result of the pandemic. Additionally, transfers from the COVID-19 Fund could

¹¹ [Royal Decree-Law 7/2020, of 12 March, adopting urgent measures to respond to the economic impact of COVID-19](#)

offset most of the impact of the pandemic in the Regions. In short, in 2020 the CG will assume almost all of the effect of the health crisis.

The expected worsening in the sub-sector in 2021 is accentuated to the same extent that the 2020 year-end forecast improves, and the negative outlook for 2022 is maintained. Regional revenue will be affected by the crisis in 2021 with the updating of the common regime financing system's resources in accordance with the real macroeconomic scenario and the non-repetition of the extraordinary transfers in 2020. Under the current macroeconomic forecasts, the Regions' resources could fall by between 12% and 14% in 2021, incorporating an estimated fall in the common regime system resources of between 9% and 12%. Under these revenue forecasts, despite the negative evolution expected in expenditure as most of the expenditure incurred in 2020 has not been replicated as a result of the pandemic, a significant deterioration in the sub-sector's balance in this financial year is expected, close to 2% of GDP.

In 2022, on the other hand, the Regions under the common regime will have to deal with the final settlement of the financing system. The settlement carried out in 2022 according to the tax revenue collected by the State in 2020 could range from 0.6% to 0.9% of GDP, depending on which scenario materialises. A recovery is only expected in the Regions under the provincial regime from 2021.

4.7.2. Detail of the impact of COVID-19 by health expenditure and other measures

The increase in healthcare expenditure caused by COVID-19 is estimated at between 0.6% and 0.9% of GDP. This element has been revised based on the data provided by the Regions on the expenditure accrued up to May and other available information. The data for May were projected to year-end based on the relative impact of the different Regions, the information provided and the assumptions made in the two scenarios considered. The greater information available regarding the estimate made for the report on the SPU has made it possible to compare the estimates with additional variables, such as total health expenditure up to May, the execution of the main expenditure headings up to April and information on measures provided by the Regions themselves. With the current information, the overall estimate of the previous report has been revised upwards by 0.1%, as well as its distribution by heading, considering a greater impact on intermediate consumption, which include the purchase of health products and materials and hospital expenditure, and less on social transfers in kind which record expenditure on non-hospital pharmacy and health care agreements,

compensation of employees and investment. By agreement of the Council of Ministers of 31 March¹², the State distributed 300 million in funds to the Regions by means of conditional direct transfers to meet these needs.

On the other hand, the Regions have implemented measures and actions in other areas that could lead to an additional 0.2% of deficit. On the expenditure side, the Regions have issued and evaluated measures on aid to companies or individuals, both through the application of funds received from the State for social services, child feeding and housing¹³ (420 million), and additional measures aimed at strengthening social centres and benefits (family financial aid and minimum income), actions aimed at alleviating the effects of the crisis on companies and self-employed workers (direct subsidies and increased resources for guarantee companies to increase guarantee operations); aid to local governments and other affected groups and sectors, such as children's education centres or certain manufacturing centres); as well as measures to strengthen cleaning and the purchase protection materials for public centres. At the same time, savings resulting from the suspension of certain services or the non-implementation of certain expenditure items have been assessed. These include the lower expected expenditure on training for employment as the state funding associated with this expenditure has been suspended.

The educational measures for the next academic year and the effect of the MLI on regional minimum incomes lead to additional uncertainty about the expenditure estimates. Although most Regions have identified residual measures that have been carried out in the educational field, only eight, Principality of Asturias, Balearic Islands, Cantabria, Castile-La Mancha, Madrid, Murcia, Navarre and Valencia, have provided a more or less detailed or extensive forecast of measures to be implemented for the coming academic year, with a greater impact in 2021. On the other hand, except in the case of Aragon and Valencia, the possible effect that the implementation of the recently approved Minimum Living Income (MLI) may have on the regional accounts has not been assessed, and the Regions indicate that it is not yet known whether the legislation governing this aid in each Region will be amended, nor the possible savings that could result from it.

¹² [Council of Ministers of 31 March 2020](#)

¹³ [Royal Decree-Law 7/2020 adopting urgent measures to respond to the economic impact of COVID-19;](#)

[Royal Decree-Law 8/2020, of March 17, on extraordinary urgent measures to deal with the economic and social impact of COVID-19](#)

[Royal Decree-Law 11/2020 adopting supplementary urgent social and economic measures to deal with COVID-19](#)

Revenue measures will have less impact on the deficit increase, around 0.1% GDP. On the revenue side, the Regions' main actions have been aimed at granting tax deferrals, suspension of instalment payments, exemption from rent and free provision of certain services, of which the effect in terms of GDP is estimated to be low. In addition, the State funds allocated to the above-mentioned expenditure and the lower transfers to finance training for employment have been identified, with a negative net amount but less than 0.05% of GDP. Altogether, revenue would drop by almost 0.1% due to these factors.

TABLE 8. ESTIMATED IMPACT OF COVID-19 IN THE REGIONS AS A RESULT OF THE INCREASE IN HEALTHCARE EXPENDITURE AND MEASURES ADOPTED DUE TO THE PANDEMIC. % GDP

Estimated impact of COVID-19 on 2020 expenditure and revenue due to health expenditure and other measures adopted in the Regions (% GDP)	Scenario 1	Scenario 2
EXPENDITURE MEASURES	0.8	1.0
Health expenditure	0.6	0.9
Social services	0.1	0.1
Economic promotion	0.1	0.1
Training for employment	-0.1	-0.1
Education	0.1	0.1
Housing, transportation and others	0.0	0.0
REVENUE MEASURES	-0.1	-0.1
Tax measures	0.0	0.0
Conditional transfers from the AGE	0.0	0.0
Revenue from provision of public services	0.0	0.0
Other revenue measures	0.0	0.0
TOTAL IMPACT ON DEFICIT	-0.8	-1.1

Source: Information from the Regions' and AIRcF's estimates

4.7.3. Detail of the impact of COVID-19 by macroeconomic effect

In the sub-sector the expected fall in economic activity may result in a lower expected collection of between 0.7% and 0.9% GDP in the regional revenues that are not part of the resources of the Regional Financing System (RFS). The main revenue of the Regions under the common regime, derived from the RFS, will not be affected in 2020 by the expected fall in economic activity. However, the rest of revenue items will be significantly affected by the crisis. This impact has been revised since the previous report based on the execution data available to date, the forecasts provided by the Regions on the greater expected expenditure on transport subsidies and the fall in revenue unrelated to the RFS, and the revision of AIRcF's models for forecasting taxes and other regional revenue. From this, on the one hand, the expected fall in the main revenue items of the Regions under the provincial regime is significantly

accentuated (overall, 0.1% of GDP in the sub-sector). On the other hand, the estimated impact on the rest of revenue items increases by a further 0.1%, concentrated in the Tax on Property Transfers and Documented Legal Acts (TPTDLA) and in the revenue from university fees and transport tariffs, where applicable. The impact of COVID-19 on the main revenue items is directly felt in the Regions under the provincial regime in 2020, despite the transfers expected from the COVID-19 Fund, and it is therefore expected that the crisis will have a greater effect in this year and that these Regions' recovery will be faster starting next year.

TABLE 9. ESTIMATED IMPACT OF COVID-19 IN THE REGIONS DUE TO DETERIORATION OF THE MACROECONOMIC SCENARIO % GDP

Estimated macro impact of COVID-19 in 2020 (%GDP)	Scenario 1	Scenario 2
IMPACT ON REVENUE	-0.6	-0.8
TATDLA	-0.2	-0.3
Other taxes (*)	-0.1	-0.2
Sales	-0.1	-0.2
Rest of current expenditure (**)	-0.2	-0.2
Capital expenditure	0.0	0.0
IMPACT ON EXPENDITURE	0.1	0.1
Interest	0.0	0.0
Transport	0.0	0.0
Other current expenditure (***)	0.0	0.0
TOTAL IMPACT ON DEFICIT	-0.7	-0.9

* Includes taxes of the provincial regime of Navarre and the Fiscal Regime of the Canary Islands

** Includes transfers received from the Provincial Councils in the Basque Country

*** Includes the lower transfers to the Island Councils of the Canary Islands due to the Region's drop in revenue

Source: AIReF's estimates and information from the Regions

4.7.4. Individual analysis by Region

Since the last report on the main budgetary lines for 2020, AIReF's forecasts for each Region have varied more in composition than in result, mainly due to the impact of COVID-19 and the State's transfers. AIReF's forecasts for the close of 2020 in each Region have been revised since the reports on the main budgetary lines in December 2019 as from: the published close of 2019, the updating of the instalment payments that will finally be received by the Regions under the common regime and the estimate of the impact of the pandemic on resources to be received from the COVID-19 Fund.

The detail of the estimates for each Region is included in the individual reports that are published jointly. An individual analysis of the expected situation for each Region has been conducted in the reports published at the same time as this one, updating the pronouncement of the report on the main budgetary lines and recording the expected effects of the pandemic and of the transfers associated with it.

At an individual level, the estimated impact of COVID-19 **could vary between 0.8% and 2% of GDP depending on the Region and scenario considered, with a greater impact in the Basque Country and Navarre.** The three fundamental factors that determine the aforementioned estimates have a different weight in each Region:

- In general, the increase in health expenditure resulting from COVID-19, the main element of impact of the pandemic, could vary between Regions and scenarios by between 0.5% and 1.1%.
- The higher expenditure or lower revenue resulting from other measures range from neutral impact to 0.4% of GDP, depending on the information provided by each Region. Thus, several Regions have estimated savings for expenditure items that will not be executed, partly offsetting the expected increase in others. On the other hand, there is a greater impact, except in the Balearic Islands, on the Regions that have provided forecasts on measures in education for the coming academic year: Asturias, Valencia, Castile-La Mancha, Navarre and, to a lesser extent, Murcia, Madrid and Cantabria.
- The fall in revenue due to the crisis could have an impact of between 0.3% and around 1.5% in the Regions under the common regime, which is expected to be much higher in the Regions under the provincial regime.

The transfers that the Regions under the common regime will receive from the COVID-19 Fund range from 1.2% to 1.6% of the estimated regional GDP, except for Castilla-La Mancha, where they could be greater, and for the Regions under the provincial regime that participate directly in the first 3 tranches of the fund, where the transfers could represent close to 1% of GDP. The distribution of the COVID-19 Fund approved by Royal Decree-Law 22/2020¹⁴ has been estimated based on the available or estimated elements which, for each tranche and in accordance with the aforementioned legislation, serve as a basis for the calculation of this distribution. This forecast is generally in line with the estimates made by the Regions themselves.

¹⁴ [Royal Decree-Law 22/2020 regulating the creation of the Fondo COVID-19 and establishing for the rules for its distribution and release](#)

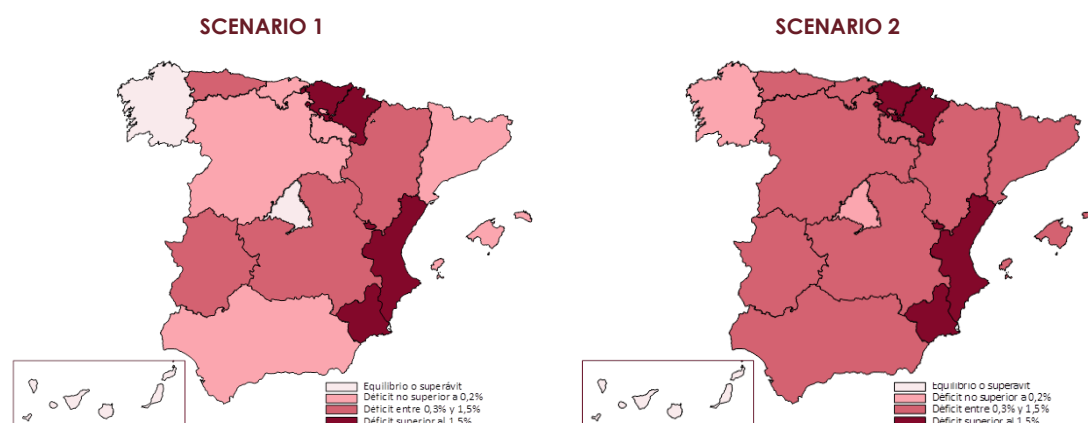
TABLE 10. SUMMARY OF THE CLOSING FORECASTS FOR 2020 BY REGION % GDP

Regions	Budgetary lines forecast (**)	Variation at the close of 2019	Variation in RFS resources	Other non-COVID factors	Forecast without COVID	COVID impact*		Fondo COVID-19		Current forecast	
						Scenario 1	Scenario 2	Scenario 1	Scenario 2	Scenario 1	Scenario 2
AND	0.1	0.0	-0.1	-0.1	-0.2	-1.3	-1.7	1.4	1.4	-0.1	-0.4
ARA	-0.5	-0.2	-0.1	0.0	-0.7	-1.0	-1.3	1.2	1.3	-0.4	-0.7
AST*	-0.1	-0.4	0.0	0.0	-0.4	-1.5	-1.8	1.3	1.3	-0.4	-0.7
BAL*	0.0	0.1	-0.2	0.0	-0.1	-1.5	-2.0	1.4	1.5	-0.2	-0.6
CAN	0.9	0.3	0.0	0.2	1.3	-2.2	-2.6	1.2	1.3	0.4	0.2
CNT*	-0.2	-0.3	0.1	0.0	-0.5	-1.1	-1.4	1.3	1.4	-0.2	-0.5
CYL	-0.1	-0.5	0.0	-0.1	-0.7	-1.1	-1.5	1.6	1.6	-0.2	-0.6
CLM*	-0.7	-0.5	0.1	0.1	-1.0	-1.6	-2.0	2.1	2.1	-0.5	-0.9
CAT	-0.3	0.0	0.0	0.1	-0.1	-1.6	-2.0	1.5	1.6	-0.2	-0.6
EXT	-0.7	-0.2	0.0	0.0	-0.9	-1.1	-1.5	1.5	1.6	-0.5	-0.8
GAL	0.0	-0.1	0.0	0.0	-0.1	-0.9	-1.2	1.2	1.2	0.2	-0.1
MAD*	0.0	-0.1	-0.1	0.0	-0.2	-1.3	-1.6	1.6	1.6	0.1	-0.2
MUR*	-1.4	-0.3	0.0	0.0	-1.7	-1.0	-1.3	1.2	1.2	-1.6	-1.9
NAV*	0.2	0.4	0.0	0.0	0.6	-4.5	-5.6	1.0	1.1	-2.9	-3.9
PVA	0.3	0.3	0.0	-0.1	0.5	-3.2	-4.2	1.1	1.1	-1.6	-2.6
RIO	-0.1	-0.3	0.2	-0.3	-0.5	-1.1	-1.6	1.6	1.7	0.0	-0.4
CVA*	-1.7	-0.3	0.1	0.2	-1.8	-1.8	-2.2	1.4	1.4	-2.1	-2.6
Total Regions	-0.2	-0.1	0.0	0.0	-0.3	-1.5	-2.0	1.4	1.5	-0.4	-0.9

(*) No forecast of possible measures in education for the coming academic year, except in the regions of Asturias, Balearic Islands, Cantabria, Castile-La Mancha, Madrid, Murcia, Navarre and Valencia, nor assessment of the impact of the MLI, except in Aragon and Valencia.

(**) Baseline forecast of the report on the main budgetary lines, calculated based on the 2020 GDP currently estimated.

FIGURE 53. 2020 FORECAST BY REGIONS.



4.8. Local Governments

4.8.1. Local Governments Analysis

With the current data, AIReF confirms its assessment of the LG sub-sector made in May, placing it around balance. With the latest published data, AIReF has updated the expected outcome at the end of 2020 for the LGs as a whole,

under the scenario of limited duration of the pandemic. In the light of these latest available data, corresponding to the execution of the first quarter of 2020, financial information on local debt and deposits for March of this year, and data communicated to AIReF by the large LGs monitored individually and by MINHAC on the estimated closure of 2020, AIReF confirms its forecasts for the local sub-sector to obtain a result around balance. The possibility of a second outbreak in the autumn would worsen AIReF's forecasts for the LGs as a whole by around 0.2% GDP and could lead to a deficit for the first time since 2011.

While AIReF maintains its more optimistic scenario around balance, with the current data it has reduced both its revenue and expenditure estimates. AIReF has revised its forecast for local revenue growth downwards, estimating that, given the current extraordinary situation, it will break its trend of stable growth since 2012, and decrease by more than 3% in 2020 compared to 2019. This expected change in the revenue trend is essentially due to:

- The estimated reduction in tax revenue of the Provincial Councils, as a result of the fall in economic activity caused by the pandemic, as well as the measures adopted by them. This reduction also has an impact on expenditure, as most of it is transferred to the Basque Country.
- The extension over time of the measures adopted by the Regions in the area of exemption and/or suspension of the collection of certain local taxes, with the aim of mitigating the effects of the pandemic on those economic sectors and populations that are most affected.
- The expected decrease in net revenue to be received in 2020 by the LGs through current and capital transfers, mainly as a result of the reduction in the contributions of the Region of the Canary Islands to the Island Councils due to the drop in IGIC (Indirect Canary Islands Tax) revenue, and the decrease in revenue to be received by the LGs through agreements with the Regions.

In terms of GDP, the reduction in revenue projected by AIReF under the two scenarios presented, whether or not the pandemic re-emerges in the autumn on a widespread basis, is similar, given that the greater reduction in revenue estimated in the event of a re-emergence is offset by a greater decline in GDP.

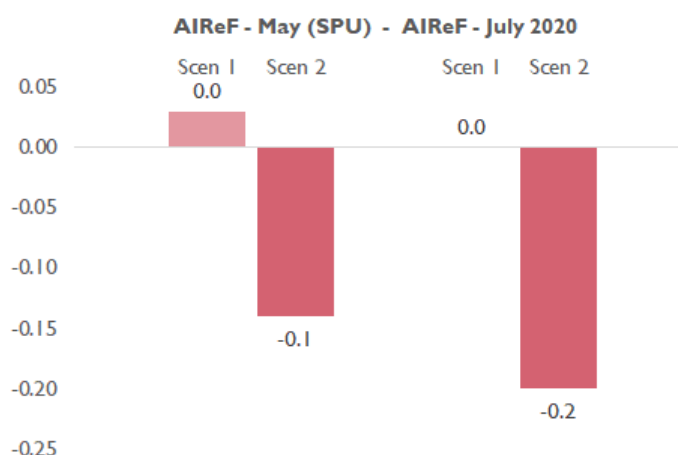
In the same way, AIReF has corrected the expenditure forecast for the local sub-sector downwards, bringing the projected growth to around 2%. This is mostly a consequence of:

- The reduction of the contributions from the Provincial Councils to other PAs due to a drop in their revenue, as indicated.
- The estimate of a significant reduction in investment expenditure this year,

caused both by the need to boost current expenditure, mainly social, given the context generated by the pandemic, and by the failure to approve at this time the necessary annual authorisation required by the stability regulations¹⁵ to carry out expenditure qualified as financially sustainable investments (FSIs) this year, other than those linked to social policies¹⁶, or environmental sustainability.¹⁷

In terms of GDP, AIReF estimates that, in the event of a pandemic outbreak in the autumn, expenditure in the local sub-sector at the end of 2020 would be about 2% higher than it would be in the absence of such an outbreak (see figure 59).

FIGURE 54. UPDATE OF NET LENDING/BORROWING SUBSECTOR REGIONS FORECAST (%GDP)



¹⁵ Sixth additional provision of Organic Law 2/2011, on budgetary stability and financial sustainability on "Special rules for the allocation of the budgetary surplus of local corporations"

¹⁶ Art.3 of the Royal Decree-Law 8/2020, on urgent measures to deal with the extraordinary economic and social impact of COVID-19 and art.20 of the Royal Decree-Law 11/2020 allow the LGs, as a whole, to allocate up to €300 million from the 2019 surplus to finance economic aid and the provision of social services for primary care and dependence in 2020, with each LG that meets the requirements being able to spend a maximum of 20% of the remaining cash surplus at the end of 2019

¹⁷ In addition, Article 6 of Royal Decree Law 23/2020 allows LGs to allocate, in 2020, a maximum of 7% of this surplus from 2019 to investments in pure electric vehicles or those with a ZERO environmental label and in charging infrastructure for the use of the vehicles purchased, provided that they are used to provide public services for the collection, disposal and treatment of waste, public safety and order, civil protection, fire prevention and extinction and passenger transport.

FIGURE 55. CONTRIBUTION TO UPDATE OF REVENUES LOCAL SUBSECTOR (%VAR)

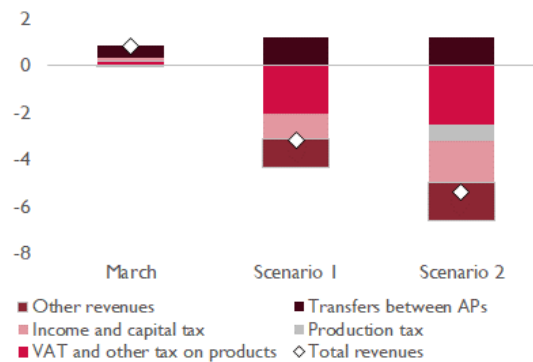
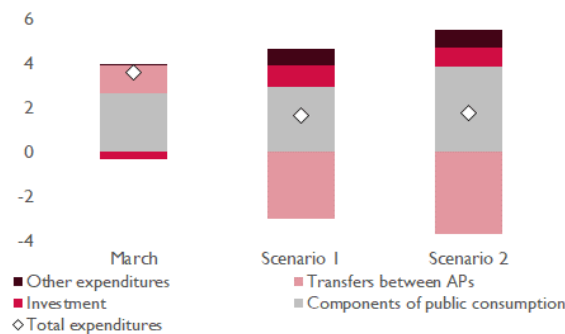


FIGURE 56. CONTRIBUTION TO UPDATE OF EXPENDITURES LOCAL SUBSECTOR (%VAR)



The closing forecasts for 2020 communicated to AIReF by the large LGs confirm this result a diminishing local surplus, mainly due to the crisis caused by COVID-19. The information received by AIReF from the large LGs on the closing estimate for 2020 and the measures adopted have confirmed AIReF's April forecasts of obtaining a local balance in 2020 close to balance, with the possibility of a deficit depending on the extent and economic impact of the pandemic. Together, these 24 large LGs obtained a surplus of over €1.7 billion, representing almost 45% of the overall result. The forecasts for 2020 for these LGs show a net deficit result of more than €70M, which means an approximate 104% reduction in the balance obtained the previous year, mainly as a result of the expansion of current expenditure in social areas and the lower expected revenue, both due to the decrease in revenue resulting from the economic crisis and the adoption of relief measures in the form of exemption and/or suspension of local taxes for the economic sectors and citizens most affected by the pandemic. These results, whose accuracy at the end of the year will depend on the extent and intensity of both the health crisis and the subsequent economic and social crisis, corroborate AIReF's estimates that, in the most favourable scenario, the result of the LGs as a whole will be close to balance at the end of 2020, with a deficit if the pandemic experiences a new widespread outbreak.

FIGURE 57. EVOLUTION OF SUB-SECTOR LG NET LENDING/BORROWING (%GDP)

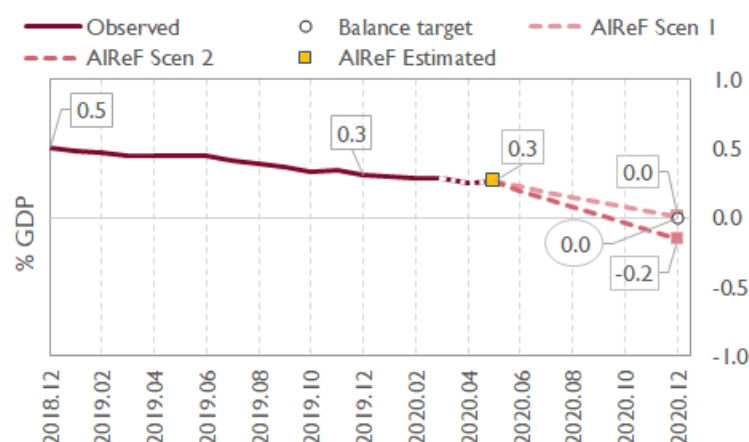


FIGURE 58. EVOLUTION OF SUB-SECTOR LG REVENUES (%GDP)

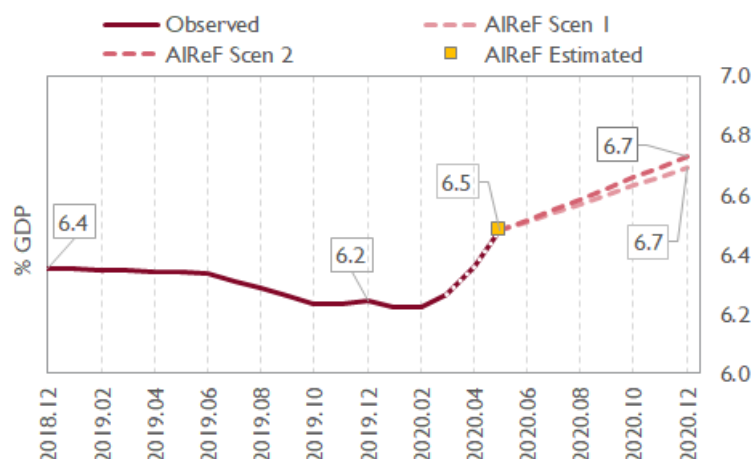
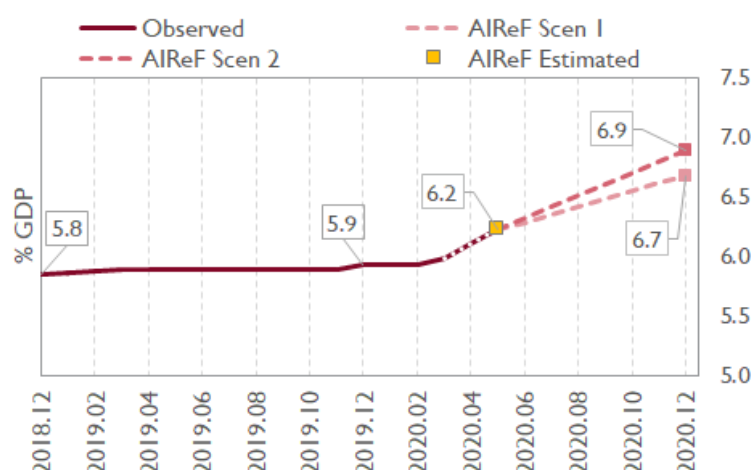


FIGURE 59. EVOLUTION OF SUB-SECTOR LG EXPENDITURES (%GDP)



Given the extraordinary circumstances caused by the pandemic, AIReF estimates that it is time for the LGs to apply the margins generated in previous years from the application of the expenditure rule, provided that their future sustainability is not compromised. Since its inception, AIReF has advocated

the need for the PAs to be subject to the expenditure rule, as an instrument of budgetary discipline that makes it possible, through the containment and streamlining of expenditure, to generate surpluses in times of prosperity, which can serve to alleviate the negative effects on the provision of public services of the reduction of resources needed in times of crisis. Therefore, in view of the repeated demands of the local sub-sector to make this rule more flexible, AIReF has always advocated an update and the need to incorporate a medium-term approach to the rule rather than to make it more flexible. In a context as exceptional as the current one, where the health emergency has given way to an economic and social emergency in which the role of the LGs as the administration closest to the citizen is proving decisive, AIReF has already stated that it is time to be able to apply the savings generated from adherence to the expenditure rule in previous years, as long as no deficit is incurred, given its constitutional requirement, and no recurrent expenditure is generated in future years that could compromise the future sustainability of these administrations. For this reason, AIReF does not assess compliance with the expenditure rule in the local sub-sector in this Report.

4.8.2. Individual analysis of the LGs and impact of COVID-19 on the corporations analysed

AIReF assesses the fiscal rules at the end of 2020 in the 50 LGs subject to individual monitoring in the Supplementary report. As in previous reports, AIReF individually monitors the fiscal rules of the 24 large LGs¹⁸, which represent more than 25% of the overall result, as well as 26 entities¹⁹ in which, at the beginning of the budget cycle, it detected medium-term sustainability problems, and whose evaluation requires the combination of structural indicators with the analysis of fiscal rules that must be complied with on an annual basis.

The 2020 closing forecasts made by the group of large LGs show a worsening of the results reported in March, with the possibility of incurring a deficit for the first time since 2012. In AIReF's 2020 Report on the Main Budgetary Lines for 2020, with data projected before the pandemic, the large LGs expected to

¹⁸ The large LGs analysed are: the City Councils of Madrid, Barcelona, Valencia, Sevilla, Zaragoza, Málaga, Murcia, Palma, Las Palmas de Gran Canaria, Bilbao, Alicante, Córdoba, Valladolid, Vigo, Gijón and L'Hospitalet de Llobregat; the Councils of Barcelona, Valencia and Seville; the Island Council of Tenerife; the Island Council of Mallorca; and the Provincial Councils of Álava, Guipuzcoa and Biscay.

¹⁹ The 26 City Councils with a population of over 20,000 inhabitants, selected due to presenting sustainability risks, are: Alcorcón, Alboraya/Alboraya, Algeciras, Almonte, Aranjuez, Arcos de la Frontera, Arganda del Rey, Ayamonte, Barbate, Los Barrios, Caravaca de la Cruz, Gandía, Granada, Isla Cristina, Jaén, Jerez de la Frontera, La Línea de la Concepción, Los Palacios y Villafranca, Navalcamero, Parla, Puerto Real, Rota, San Andrés del Rabanedo, Sanlúcar de Barrameda, Totana and Valdemoro.

increase their lending capacity by 7% by the end of this year. However, with current data, these entities expect to obtain a net deficit equivalent to 0.3% of the group's non-financial revenue. These new estimates include both the economic impact of reduced revenue and increased expenditure arising from the measures and reduction in economic activity caused by the pandemic, the net economic impact of which is forecast at around €1.5 billion, and the effect of economic decisions to increase expenditure not directly related to this extraordinary situation.

TABLE 10 presents the main conclusions of the monitoring of the fiscal rules at the end of 2020 in the large LGs, as well as the results obtained in the last year ended, 2019.

TABLE 10. COMPARISON OF FORECASTS OF COMPLIANCE WITH FISCAL RULES IN 24 LARGE LGs

LOCAL GOVERNMENTS	ECONOMIC FINANCIAL PLAN (EFP), and/or ADJUSTMENT PLAN (AP) APPROVED AND IN FORCE	STABILITY TARGET (ST)		EXPENDITURE RULE (ER)		DEBT-TO-GDP RATIO (DR)
		2019 year-end	2020 Forecast	2019 year-end	2020 Forecast	
MADRID	Failed to comply with ER15 and ER16. After 3 EFPs approved by Plenary session but not by the financial guardianship body, EFP 17-18 was definitively approved on 17 Dec. Failure to comply with ER 19.	✓	✓	✗	✓	31%
BARCELONA	EFP for non-compliance with ER15 approved for 15-16. Reviewed due to prior non-compliance 16. New EFP 16-17. Non-compliance with ER 18, new EFP 19-20.	✓	✗	✓	✓	30%
VALENCIA	Non-compliance with ER17, according to the homogeneous criteria for calculation of the ER of the IGAE guide. An EFP should have been submitted but was not completed. Failure to comply with ER 19.	✓	✓	✗	✗	40%
SEVILLE	EFP for non-compliance with ER18 approved for 19-20.	✓	✓	✓	✓	32%
ZARAGOZA	EFP for non-compliance with ER15 approved for 16-17. Non-compliance with ER17 committed to in the EFP due to time lag.	✓	✓	✓	✗	88%
MALAGA	EFP for non-compliance with ER15 approved for 16-17. Failure to comply with ER 19.	✓	✓	✗	✓	42%
MURCIA	EFP for non-compliance with ST and ER16 approved for 17-18. Failure to comply with ER 19.	✓	✓	✗	✓	84%
PALMA	EFP for non-compliance with ER15 approved for 16-17	✓	✗	✓	✗	44%
LAS PALMAS DE GRAN CANARIA	EFP for non-compliance with ER17 approved for 18-19	✓	✓	✓	✗	0%
BILBAO	EFP approved by approving the 2017 budget with deficit, in non-compliance with the provisions of the LOEPySF. In October 2019, in view of forecast of non-compliance with the ER 2019, approved a new EFP 19-20.	✓	✓	✓	✓	1%
ALICANTE	EFP for non-compliance with ER15 approved for 16-17	✓	✓	✓	✗	7%
CORDOBA	Failure to comply with ER 19.	✓	✓	✗	✗	52%
VALLADOLID		✓	✗	✓	✗	32%
VIGO	EFP for non-compliance with ST and ER 2018 approved for 19-20.	✓	✓	✓	✗	0%
GIJÓN	Did not comply with ER17. Did not approve the EFP in plenary session.	✓	✗	✓	✗	40%
L'HOSPITALET DE LLOBREGAT	EFP for non-compliance with ER 2018 approved for 19-20	✓	✗	✗	✗	29%
Council of BARCELONA	EFP for non-compliance with ER17 approved for 18-19. Failure to comply with ER19.	✗	✓	✗	✓	0%
Council of VALENCIA	EFP for non-compliance with ER15 approved for 16-17. Failure to comply with ER19.	✓	✓	✗	✓	26%
Council of SEVILLE		✓	✓	✓	✓	0%
ISLAND COUNCIL OF TENERIFE		✓	✓	✓	✗	8%
ISLAND COUNCIL OF MALLORCA	EFP for non-compliance with ST and ER16 approved for 18-19	✓	✓	✓	✓	26%
PROVINCIAL COUNCIL OF ARABA/ÁLAVA		✓	✗	✓	✓	73%
PROVINCIAL COUNCIL OF GIPUZKOA		✓	✗	✓	✓	23%
PROVINCIAL COUNCIL OF BIZKAIA		✓	✗	✓	✓	77%

✓ Compliance
✗ Non-compliance

Note: The background colours in the debt column represent the DR range: green if it is <75%, yellow if it is between 75% and 110% and red if it is >110%

Likewise, in the Supplementary report, AIReF continues to monitor the 26 city councils with significant medium- and long-term sustainability problems. In this report, AIReF maintains both the subjective scope of entities in which it detected medium-term sustainability risks at the beginning of the current budgetary cycle, 26 LGs, and the methodology for rating the sustainability risk situation. All analysed City Councils, as well as MINHAC's Information Centre, have complied with the duty to collaborate with AIReF, providing the information needed for the analysis, with the exception of Barbate which has not complied with the duty of cooperation regulated in article 4 of Organic Law 6/2013, on the creation of AIReF, and, for this reason, a warning must be published on this Institution's website.

AIReF maintains the sustainability risk rating of all the entities analysed, except in the cases of the City Council of Arganda del Rey, which improves, and the City Council of Arcos de la Frontera, which worsens. With the latest data available for the end of 2019, AIReF does not change its conclusions with respect to those contained in last year's December Report, in terms of the risk situation rating of 24 of the 26 LGs assessed. Only the City Council of Arganda del Rey improved its rating, going from high to moderate sustainability risk, while, in contrast, the City Council of Arcos de la Frontera worsened its rating, going from moderate to high risk, as its debt-to-GDP ratio worsened and it had a deficit in the last few years that were closed. Although almost all the LGs maintain their medium-term rating, within this category we can see that the position of the City Councils of Jaén, Los Barrios, Algeciras, Aranjuez and Almonte worsens, while that of Jerez de la Frontera, Gandía, Navalcarnero, Los Palacios and Villafranca, San Andrés del Rabanedo, Granada and Sanlúcar de Barrameda improves. Particularly worrying is the situation of the City Council of Jaén which, with a critical risk rating (which means that a return to a sustainable situation is not considered feasible with constant revenue and expenditure policies), continues to worsen its position year after year.

The following table sets out the main conclusions obtained in the sustainability risk rating of the LGs analysed, as well as the results obtained in the last financial year closed in 2019.

TABLE 11. 26 LGS RATING OF THE MEDIUM-TERM SUSTAINABILITY RISK SITUATION

RISK LEVEL	LOCAL GOVERNMENT	Main parameters to qualify the sustainability risk situation			
		(Outstanding debt + Negative treasury remnant)/Current revenue (CR)	APP	Op. balance Current/CR	Lending capacity/CR
Critical	Jaén	554%	598	-22%	-29%
	Jerez de la Frontera	439%	340	-5%	0%
	Parla	1168%	290	-24%	-23%
Very High	Barrios (Los)	630%	123	3%	4%
	Gandia	297%	16	12%	12%
	Totana	370%	103	10%	12%
HIGH	Arcos de la Frontera	109%	503	-11%	-9%
	Ayamonte	102%	418	66%	17%
	Barbate	Non-compliance with the duty to collaborate			
	Navalcarnero	378%	231	-13%	0%
	Palacios y Villafranca (Los)	170%	353	3%	5%
Moderate	Alcorcon	109%	11	18%	20%
	Algeciras	185%	13	0%	0%
	Aranjuez	271%	222	14%	5%
	Arganda del Rey	144%	39	11%	5%
	Línea de la Concepción (La)	215%	29	8%	8%
	San Andrés del Rabanedo	224%	49	15%	15%
Low	Alboraia/Alboraya	136%	27	24%	-4%
	Almonte	115%	287	-11%	-15%
	Caravaca de la Cruz	129%	128	7%	10%
	Granada	85%	165	6%	9%
	Isla Cristina	102%	120	13%	13%
	Puerto Real	161%	185	17%	18%
	Rota	98%	136	6%	6%
	Sanlúcar de Barrameda	124%	37	15%	16%
	Valdemoro	98%	29	27%	29%

	Non-compliance with the duty to collaborate with AIRcF
	The rating of its medium-term sustainability structural situation improves
	The rating of its medium-term sustainability structural situation worsens
	Its position within the sustainability risk situation rating group improves
	Its position within the sustainability risk rating group worsens

In all the LGs analysed, there are significant uncertainties with respect to 2020, as a result of the expected economic impact of the set of measures adopted to mitigate the effects of the pandemic. AIRcF has asked all the LGs analysed for information on the economic impact they expect the measures adopted as a result of the pandemic to have on their accounts, in terms of both revenue and expenditure, as well as the impact of the reduction in revenue due to the fall in economic activity during this extraordinary situation. The difficulty in measuring this impact, as well as the uncertainties about the extent and intensity of the pandemic, and the possible lack of homogeneity in the assumptions used by each of them for the calculation, mean that the data reported do not make it possible to distinguish, when monitoring this year's

fiscal rules, the true impact of COVID-19. Despite these uncertainties, the data provided by all the LGs subject to individual assessment show a total estimated impact, in net terms, of over €1.5 billion euros in the large LGs and €58 million in the group of local corporations with sustainability problems, although with an uneven impact among the LCs analysed. The greater impact of the COVID-19 crisis on the concerted taxes of the Provincial Councils (PCs) (PIT, CIT and ST) than on local taxes (Property Tax, Tax on the Increase in Value of Urban Land, Tax on Mechanical Traction Vehicles, etc.) is significant, which leads to a greater decrease in their revenue, mostly diluted by the lower contributions that, based on this revenue, the PCs make to other PAs. In relative terms of total revenue, the impact of the pandemic on the large LGs in terms of reduced resources is 10% on average, with 2% in the group of LCs with structural sustainability problems. In terms of expenditure, the relative effect of the measures adopted due to COVID-19 is a 1% increase in the large LGs and a 1.4% increase in the LGs with sustainability risk.

5. PUBLIC DEBT

5.1. GENERAL GOVERNMENT SECTOR

5.1.1. Recent evolution and medium-term outlook

The halt in economic activity in the first half of 2020 and the increased borrowing requirements resulting from the COVID-19 crisis have once again brought the debt-to-GDP ratio close to 100%. In the first 4 months of the year, public debt totalled 45.38 billion euros, reaching 1.23 trillion. In the first quarter of 2020, the debt-to-GDP ratio increased by 3.5% compared to the end of the year, therefore it is once again close to 100%.

FIGURE 60. DEBT (% GDP)

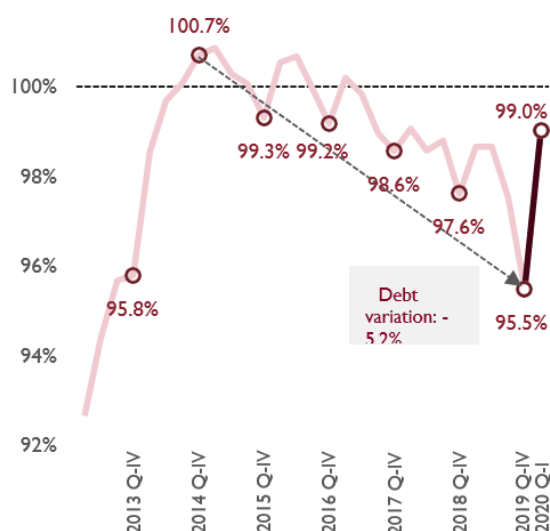
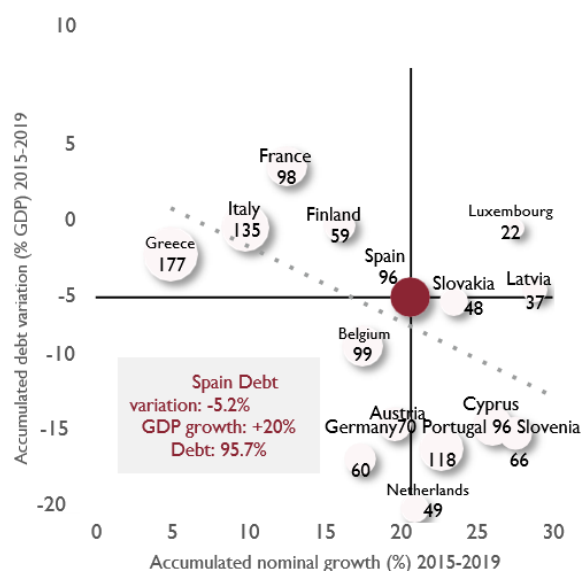


FIGURE 61. VARIATION IN DEBT AND ACCUMULATED GROWTH, EUROZONE COUNTRIES COMPARISON



Note: The size of the circumference corresponds to the debt-to-GDP ratio at the end of 2019

The reduction of the debt-to-GDP ratio in recent years has been very moderate, practically half that required by the LOEPySF²⁰. Economic growth and the continued reduction in the cost of issuing public debt managed to reduce the debt-to-GDP ratio by 5.2% over the last 5 years, compared with an increase of 65% between 2008 and 2014. This decline in the ratio is significantly smaller than in Eurozone countries with high debt and similar cumulative growth. Strict compliance with the LOEPySF requirement would have placed the debt-to-GDP ratio at around 90% of GDP in the most favourable scenario by the end of 2019, generating more fiscal space, although this margin would not have been sufficient to offset the increase in the debt-to GDP ratio forecast for 2020, which is unprecedented in peacetime.

FIGURE 62. VARIATION OF DEBT (%GDP) ACCORDING TO THE REQUIREMENT OF THE LOEPySF

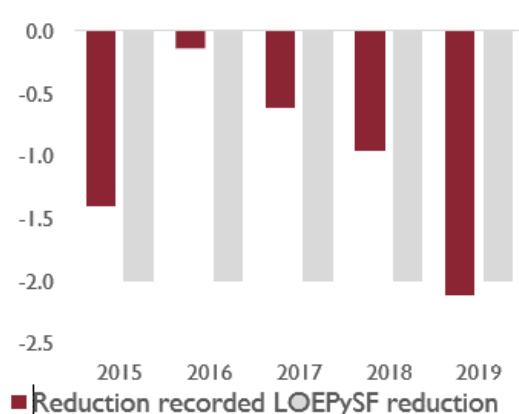
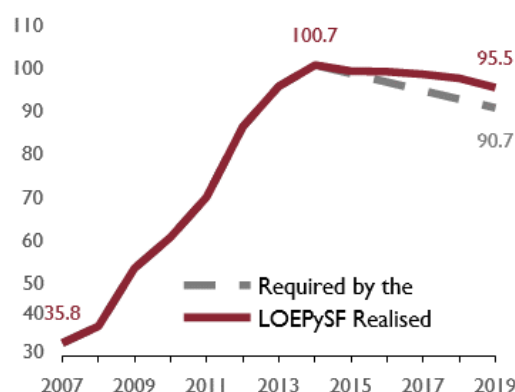
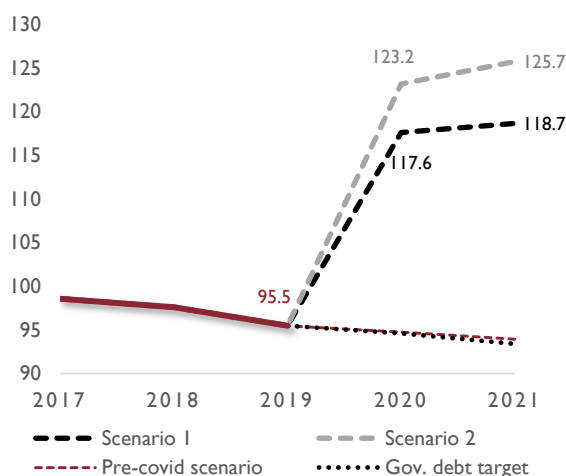


FIGURE 63. DEBT FORECAST (%GDP) ACCORDING TO THE REQUIREMENT OF THE LOEPySF



The macro-fiscal assumptions in AIReF's scenarios project an increase in the debt-to-GDP ratio of between 22.1% and 27.7% in 2020, and 1.1% and 2.5% in 2021. Under the different macro-fiscal scenarios estimated by AIReF the debt-to-GDP ratio would be between 117.6% and 123.2% in 2020 and between 118.7% and 125.7% in 2021, deviating completely from the paths projected at the beginning of the year.

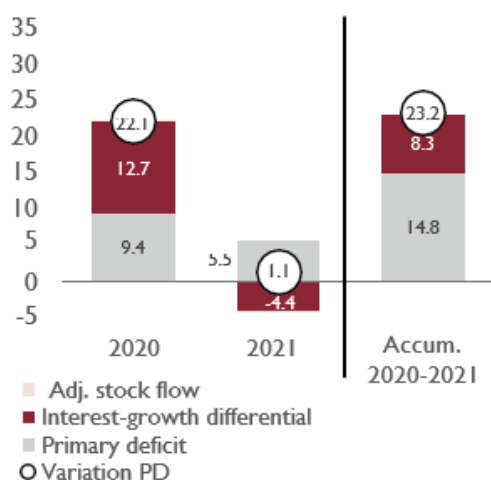
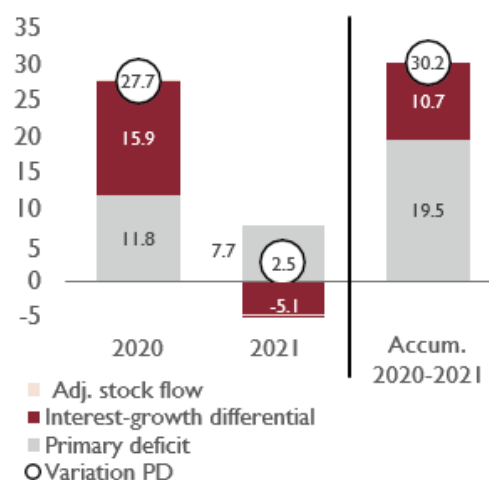
²⁰ The LOEPySF 2/2012, in its first transitional provision (1TP), required a decrease of at least 2% in the public debt-to-GDP ratio starting from the year (between 2012 and 2020) in which real GDP grew at 2% per year or from the year in which the Spanish economy generated net employment with growth of at least 2% per year

FIGURE 64. DEBT PROJECTIONS (%GDP)

FIGURE 65. MACRO-FISCAL ASSUMPTIONS

	Scenarios		
	2020	Pre-covid	
Real GDP	1.6	-10.1	-12.4
Deflator	1.7	0.4	0.2
Nominal GDP	3.3	-9.7	-12.2
Primary deficit	-0.1	-9.4	-11.8
Public deficit	-2.3	-11.9	-14.4

	2021	Pre-covid	
Real GDP	1.5	5.2	5.8
Deflator	1.6	0.8	0.6
Nominal GDP	3.2	6.0	6.4
Primary deficit	-0.1	-5.5	-7.8
Public deficit	-2.1	-8.0	-10.3

In 2020 the combination of a rising public deficit and falling economic growth is likely to be the largest in recent history, both contributing to the escalation of the debt-to-GDP ratio. The accumulation of primary deficits projected for the next two years will be the largest contributor to the increase in public debt (between 14.8% and 19.5% GDP depending on the scenario), while the fall in nominal GDP will significantly increase the debt-to-GDP ratio in 2020 only through the denominator effect. The expected rebound in economic activity and the low interest rate environment will contribute to the reduction of the debt-to-GDP ratio in 2021, but will not be sufficient to offset the projected budgetary imbalance in that year, thus leading to a further increase in the debt-to-GDP ratio, albeit to a much lesser extent than in 2020.

FIGURE 66. CONTRIBUTION TO THE VARIATION OF DEBT (%GDP). SCENARIO 1

FIGURE 67. CONTRIBUTION TO THE VARIATION OF DEBT (%GDP). SCENARIO 2


5.1.2. Compliance with the debt target

TABLE 12. INITIAL TARGETS AND DEBT FORECASTS (EDP AS % GDP)

EDP DEBT TARGETS (% GDP)	Agreement of CM February 2020	2020		
		SPU 2020-2021	AIReF, scenario 1	AIReF, scenario 2
CG and SSF	69.2	..	88.7	92.8
Regions	23.4	..	26.9	28.1
Local Government	2.0	..	2.0	2.3
General Government	94.6	115.5	117.6	123.2

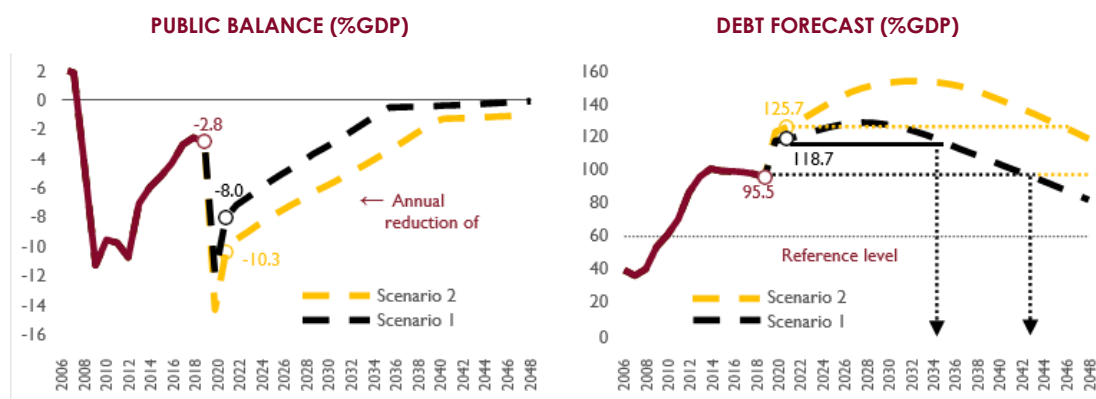
Due to the exceptional situation caused by COVID-19, the General Government will not comply with its debt targets. The public debt targets for the period 2020-2023 for the General Government and each of the sub-sectors were set by the Agreement of the Council of Ministers (ACM) of 11 February 2020. Due to the exceptional situation caused by COVID-19, these targets, in force until the escape clause is activated, became obsolete just one month after their approval. The Stability Programme Update presented by the Government at the end of April already predicted non-compliance of almost 21% of GDP for the public sector as a whole. AIReF's forecasts project non-compliance of between 23% and 28.6%, with the joint debt of the CG and SSF being the main cause of this deviation.

5.1.3. Sustainability analysis

Although the current economic outlook is surrounded by unprecedented uncertainty, its high impact on debt levels is certain. One of the few certain elements in the current context is that the spread of COVID-19 will lead to a sharp, and in principle temporary, increase in the public deficit which will in turn lead to a permanent increase in the public debt-to-GDP ratio. This will be a feature of the new macro-fiscal landscape of all advanced economies, as evidenced by major economic disruptions in the past.

As AIReF's simulations show, the high levels of debt imply that, in the medium term, when the crisis has passed, appropriate consolidation plans will have to be designed. Under a scenario of an annual deficit correction of 0.5% of GDP from 2021 to a primary surplus of 2%, it is estimated that a return to the 95.5% debt level recorded at the end of 2019 will take at least two decades. In contrast to the scenarios projected by AIReF before the crisis, where the level of 60% would be reached around 2035, this limit is not expected to be reached before 2050, even if the budget remains balanced.

FIGURE 68. DEBT PROJECTIONS (% GDP) ASSOCIATED WITH THE ASSUMPTION OF ANNUAL REDUCTION OF THE DEFICIT IN 2021 OF 0.5 POINTS OF GDP

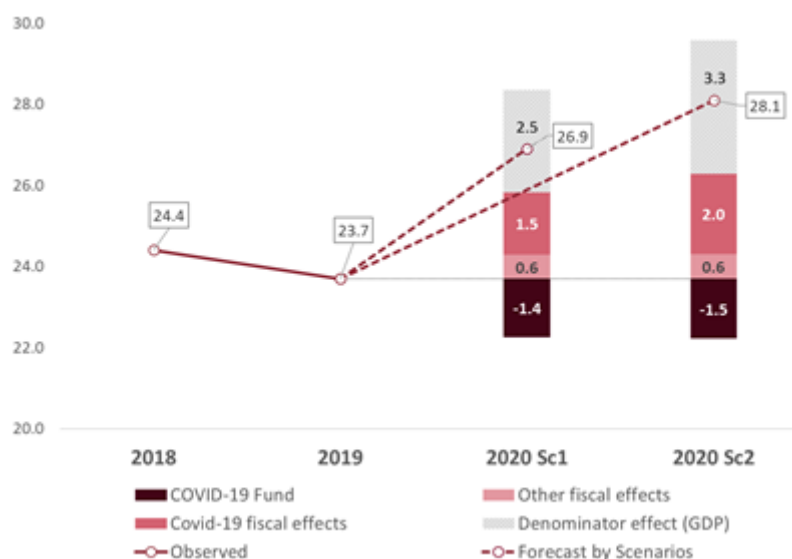


5.2. Regions

AIRcF estimates that in 2020 the regional sub-sector could increase its debt-to-GDP ratio considerably, which could range from 26.9% to 28.1%. Based on a regional 23.7% debt-to-GDP at the end of 2019, this indicator could increase by between 3.2 and 4.4 percentage points.

The main factor explaining this increase is the expected fall in GDP, given that the effects of the pandemic are largely offset by the COVID-19 Fund. The fiscal impact of increased expenditure due to the pandemic and reduced revenue due to the economic crisis could amount to between 1.5% and 2% of GDP overall. There are also additional fiscal effects arising from the need to finance previous deficits and other factors, amounting to around 0.6%. The COVID-19 Fund could largely offset the fiscal effects of the pandemic in 2020, so the main factor explaining the notable increase in the debt-to-GDP ratio this year will not be the increase in the volume of debt but the projected fall in GDP in each of the scenarios, which would cause this indicator to grow by between 2.5 and 3.3 percentage points.

FIGURE 69. EVOLUTION OF DEBT LEVEL OF REGIONS BY SCENARIOS AND EXPLICATIVE FACTORS (%GDP)



The situation may worsen from next year, due to the effects on the debt volume of the fiscal deterioration expected in 2021 and 2022. While the expected recovery in GDP would have a dampening effect on the indicator, the deterioration in the fiscal balance projected for 2021 and 2022 will lead to a considerable increase in the debt volume which will further increase the already high debt-to-GDP ratio.

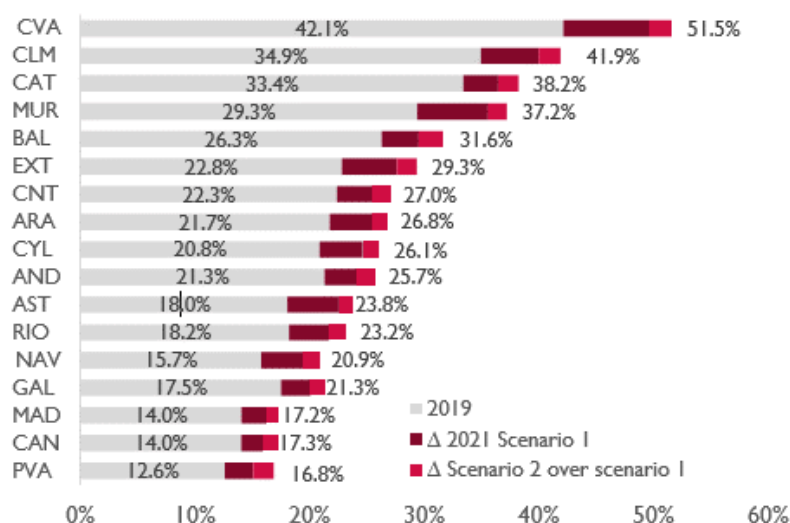
It will be essential to control debt levels given the scenario outlined. In this sense, it should be noted that MINHAC, following AIReF's recommendations, has stated that it is taking into account the excess indebtedness of previous years when calculating the financing resources allocated through mechanisms. AIReF welcomes this and other measures adopted in relation to the monitoring of the Regions' debt as it believes that they will help to control debt levels.

With regard to sustainability, the sharp fall in economic growth together with the deterioration of the fiscal balance caused by the COVID-19 crisis from 2021 onwards will increase the level of financial sustainability risk for the entire regional sub-sector. The deterioration of the fiscal balance projected from 2021 onwards will lead to a considerable increase in the debt volume which, despite the expected recovery in GDP, will lead to a further increase in the debt-to-GDP ratio.

The increase in the debt-to-GDP ratio will be uneven across the different Regions, with Valencia, Murcia and Castile-La Mancha being the territories that will see their debt grow the most over the next two years, from previously very high levels. The macro-fiscal assumptions in the scenarios prepared by AIReF project an increase in the regional debt-to-GDP ratio of between 3%

and 4.2% in 2020, and a further 0.5% and 0.8% in 2021, estimating that the ratio of the regional sub-sector will lie between 26.7% and 27.9% in 2020 and between 27.2% and 28.7% in 2021. The increase in the debt-to-GDP ratio will be uneven across the different Regions, with Valencia (9.4%), Murcia (7.7%) and Castile-La Mancha (6.9%) being the territories that will see their debt grow the most over the next two years.

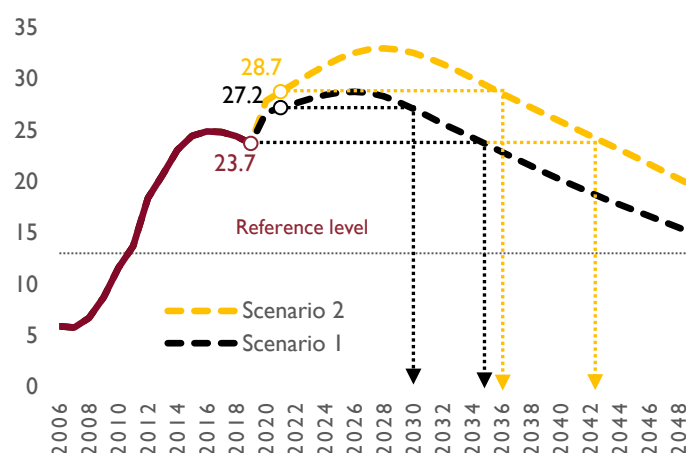
FIGURE 70. DEBT RATIO AS % REGIONAL GDP, 2019-2021 YEARS



The extraordinary financing mechanisms will cover more than 90% of the 2020 debt needs, providing liquidity to the territories at a very low cost and avoiding the payment of higher differentials in the case of the most indebted Regions. Dependence on financing through these mechanisms, already very high for certain Regions (currently accounting for over 70% of the debt of eight Regions, and over 80% for four of them), will continue to grow. Despite the deteriorating outlook for financial sustainability, the rating agencies have not downgraded the rating of the Regions, with the exception of Fitch which has downgraded the rating of the Regions of Cantabria, La Rioja and Madrid from 'BBB' to 'BBB-', although it continues to place their long-term debt in the investment grade category.

A return to the 23.7% debt level recorded at the end of 2019 would take at least a decade under assumptions of a fixed annual correction of the deficit. Under a scenario of an annual deficit correction of 0.25% of GDP from 2021 to achieve budgetary balance, it is estimated that a return to the 23.7% debt level recorded at the end of 2019 will take at least a decade. In contrast to the scenarios projected by AIRcF before the crisis, where the level of 13% would be reached around 2035, this limit is not expected to be reached before 2050 under these assumptions, even if the budget remains balanced in the entire sub-sector.

FIGURE 71. DEBT FORECAST (%GDP) ASSOCIATED WITH 0.25% ANNUAL REDUCTION OF DEFICIT IN 2021 UP TO BUDGETARY BALANCE. REGIONS.



5.3. Local Government

AIReF forecasts that by the end of 2020 the local debt-to-GDP ratio will be around 2%, slightly worsening the 2019 result. The local debt data published by the *Banco de España*, corresponding to the end of 2019, report a reduction last year of nearly €2 billion, placing the local debt-to-GDP ratio at 1.9%. This trend of reducing the LGs' debt level continued during the first quarter of 2020, when the debt-to-GDP ratio of the LGs reached 1.8%. However, the advance data from April of this year, in the midst of the state of alarm, reflect a significant increase in local debt of more than €1.3 billion euros in a single month, which points to a change in the trend of this ratio, as a result of the reduction in the surplus of the local sub-sector as a whole, given the context of the widespread crisis that the pandemic has caused. AIReF estimates that, consistent with the decline in the surplus, local debt will stabilise or increase slightly during 2020, with the latter standing at around 2% of GDP at the end of the year. In the most pessimistic scenario of a widespread resurgence of the pandemic in the autumn, the local debt level, consistent with the projected deficit, would rise further to around 2.3% of GDP.

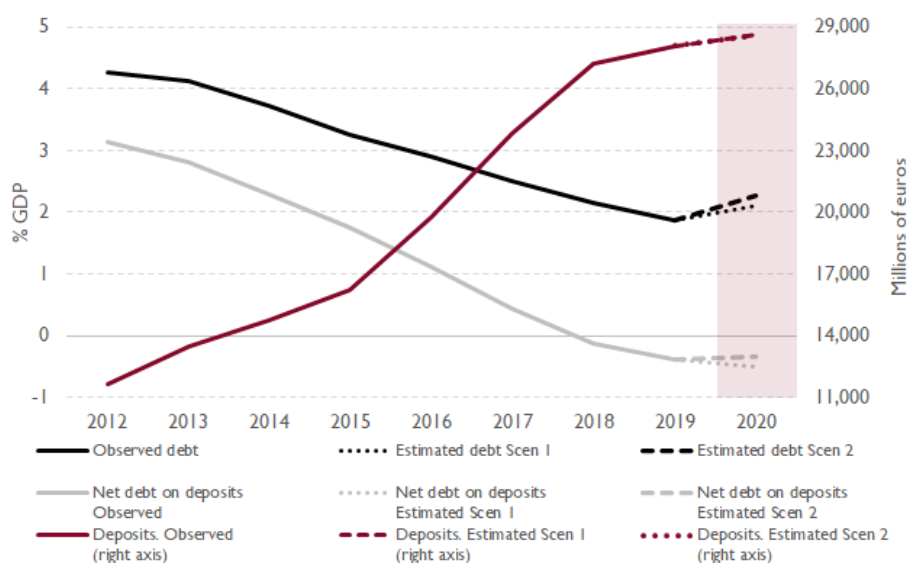
In line with the reduction of the local surplus, AIReF envisages a further mobilisation of the LG deposits in 2020 to meet the expenditure needs generated by the pandemic which will ease throughout the year. As shown in several previous AIReF reports, since the end of 2012, the LGs have been increasing bank deposits, which by the end of 2019 stood at €28.1 billion, almost

€1 billion more than at the end of 2018. As a result, the net debt of liquid financial assets of the LGs became negative in 2018 and has continued in 2019. The extraordinary situation caused by the pandemic has led to a greater mobilisation of local deposits in the first quarter of 2020, in order to meet some

of the extraordinary expenditure arising from the social emergency situation caused by the pandemic, which is why the LGs' bank deposits were reduced in the first quarter of the year by €1.5 billion, a reduction trend that is expected to slow down over the year as the social emergency improves.

Figure 72 shows the evolution of the observed data on debt, deposits and net liability position of the LGs (In % of GDP), from 2012 to 2019, as well as AIREF's closing forecast for 2020 in its two scenarios.

FIGURE 72. EVOLUTION OF THE DEBT AND LIQUID ASSETS LGS SUB-SECTOR 2012-2019 YEARS (%GDP) AND 2020 AIREF ESTIMATES



6. RECOMMENDATIONS

From AIReF's perspective, the current priority is to respond to the crisis, but without losing sight of the medium-term effects of the pandemic. For this reason, this institution made recommendations in the Report on the SPU 2020-2021 last May, aimed at making use of the fiscal margin allowed by the regulations by activating the national escape clause, and at the same time, preparing the exit strategy that requires a Rebalancing Plan, taking into account the EU context.

However, MINHAC deviated from both recommendations, mainly citing the situation of uncertainty in order to delay the activation of the escape clause and the development of the Rebalancing Plan.

AIReF agrees that the severity and depth of the crisis remain uncertain, which makes planning difficult at this time. However, this cannot be an excuse for not carrying out a medium-term strategy and forecasting exercise, without this involving revisions according to the circumstances that materialise.

As a result of the delay in activating the escape clause, there is currently a great deal of uncertainty about which national fiscal framework is applicable, which means that administrations do not know which targets are applicable and what the consequences of non-compliance are:

- the administrations do not have targets for this year or the following years, either because they have been overridden by the crisis, or because they have not been approved as in the case of the individual targets of the Regions,
- where there is uncertainty as to the enforceability of the consequences of non-compliance, both with respect to 2019 and with respect to non-compliance that may occur in 2020.

Likewise, the postponement of these actions has led to the absence of a medium-term national fiscal plan that sets out the Government's strategy for redirecting the public accounts in a joint and coordinated manner. At this time of exceptional crisis, a comprehensive approach with a medium-term horizon is absolutely necessary in order to properly plan and set up a stable and reliable framework for the actors to make their decisions.

This national strategy must be joint and ensure the coherence of all plans, both at administrative, national and European level. In order to ensure its implementation, it should include a tentative timetable for the achievement of milestones and contain a number of flexible elements so that, in a context of uncertainty such as the present one, they can be reviewed in the light of circumstances, which could lead to the extension of the planned measures or, where appropriate, the addition of new ones.

In conclusion, postponing these actions and not using the planned coordination mechanisms, the *Consejo de Política Fiscal y Financiera* (Fiscal and Financial Policy Council - CPFF) and the *Comisión Nacional de la Administración Local* (National Commission for Local Administration - CNAL), until the uncertainty ends would lead to a lack of coordination of the actions of the PAs in fiscal matters. As has been pointed out, the lack of fiscal guidance and a clear and defined fiscal framework means not only that the process of drawing up their budgets for the coming year, which should be completed in the last quarter of the year, is delayed, but also that the necessary medium-term planning is postponed.

For this reason, AIReF recommends that the Government:

- 1. Clarify the fiscal framework applicable to each of the PAs as soon as possible and in particular with a view to drawing up the Budgetary Plan and the budgets of each administration, which means:**
 - 1.1. Activating the exceptionality clause envisaged in article 11.3 of Organic Law 2/2012 on Budgetary Stability and Financial Sustainability, identifying the scope of its effects for the different PAs.**
 - 1.2. Clarifying the consequences of non-compliance with the 2019 fiscal rules and, where appropriate, non-compliance in 2020, consistent with the current situation.**
 - 1.3. Setting stability and debt targets so that the PAs can prepare their budgets for 2021 within multi-year scenarios and facilitate their monitoring by AIReF and the PAs themselves.**
- 2. Establish a medium-term national fiscal strategy that provides fiscal guidance and realistically and credibly ensures the financial sustainability of the PAs. This requires:**
 - **Counting on all levels of the Administration, considering their fiscal realities in terms of resources and competences, to ensure adequate coordination and co-responsibility.**
 - **Considering the levels of public debt and fiscal risks, especially those assumed in managing the COVID-19 crisis.**
 - **Establishing a tentative schedule for achieving milestones.**

- ***Serving as a framework for the PAs' Rebalancing Plans and promoting their coordination with national recovery and resilience plans.***

In these moments of crisis, it is important to prioritise expenditure and redirect it to reforms that have a positive impact on economic recovery and the provision of basic services. In this sense, it would be advisable to take advantage of this opportunity to implement AIReF's proposals resulting from the Spending Review studies, insofar as these may be useful to increase expenditure efficiency, redesign policies that are not working, or replace them with new, more efficient and effective ones.

For this reason, AIReF recommends that the Government:

3. ***Explore, within the framework of the medium-term fiscal strategy, the implementation of the proposals made by AIReF in the Spending Review studies, both those already carried out and those to be presented in the near future.***

AIReF President



Cristina Herrero Sánchez

ANNEX I. EVALUACION MEDIDAS APROBADAS EN RELACIÓN CON EL COVID-19

Central Government revenue measures					
RD Law	Art.	DESCRIPTION OF MEASURE	IMPACT ON DEFICIT	GOVERNMENT ESTIMATE	2020 AIReF ESTIMATE
7	14	Relaxation of requirements regarding tax debt deferral up to a term of 6 months, for those taxpayers with a volume of operations not exceeding 6 million euros in 2019	NO	9	
8	33	Extension of the payment period of tax debts that have already been settled and notified to 30 April and extension of those that have been notified since the entry into force of RD-law to 20 May	NO		
11	41	Suspension of interest payments and amortisations of EMPRENDETUR loans granted by SET	NO	0.74	0.74
11	52	Deferral of debts derived from customs declarations: Deferral of revenue from customs and tax debt corresponding to customs declarations presented up to 30 May 2020, provided that the amount of debt to be deferred is over 100 euros.	NO	2.7	
14	1	Extension of the term for presenting and submitting self-assessments with maturity from the entry into force of the RD Law for taxpayers with a volume of operations not exceeding 600,000 euros in 2019 to 20 May	NO		
15	8	VAT Application of zero rate VAT for medical devices aimed at fighting COVID-19 and whose buyers are Public-Law Entities, clinics or hospital centres	YES	1,022	296
15	9	Corporate Income Tax Extraordinary option for calculating instalment payments during the 2020 financial year on the year's accumulated tax base to taxpayers with a volume of operations not exceeding 6 million euros	YES		450
15	10	PIT and VAT The objective estimation regime for PIT and the simplified and special agriculture regime for VAT can be waived exclusively for 2020	YES	1,130	596
15	11	PIT and VAT Instalment payments in the objective estimation method of PIT and from the quarterly quota of the simplified VAT regime will be reduced proportionately to the number of days of each quarter for which the state of alarm is active	YES		99
15	2nd FP	VAT Reduction of the VAT rate applicable to digital books, newspapers and magazines to 4%	YES	24	20
TOTAL REVENUE MEASURES				2,188	1,461

Central Government expenditure measures					
RD Law	Art	DESCRIPTION OF MEASURE	IMPACT ON DEFICIT	GOVERNMENT ESTIMATE	AIReF's ESTIMATE
Reinforcement measures in the health field					
7	1	Extraordinary credit for the <i>Ministerio de Sanidad</i> (Ministry of Health) to deal with the National Health System's extraordinary expenditure	YES	1,400	1,400
7	2 to 6	Updating Regions' payments to boost the availability of resources to meet the immediate needs of their health systems (1)	YES	2,867	770
8	36	Exceptional labour measures in the field of public entities that are part of the Spanish System of Science, Technology and Innovation	YES	0.77	0.77
8	37	Extraordinary credit in the <i>Ministerio de Ciencia e Innovación</i> (Ministry of Science and Innovation) budget in relation to scientific research on COVID-19. Directed towards Instituto de Salud Carlos III and Consejo Superior de Investigaciones Científicas (Spanish National Research Council - CSIC)	YES	29.65	29.65
11	AP1	Extension of employment contracts signed through public calls for human resources in the field of research and the integration of contracted staff in the National Health System	YES	15.65	15.65
7	ACM 12 March	Extraordinary credit and credit supplements in the <i>Ministerio de Sanidad</i> budget to finance the needs caused by the COVID-19-related public health emergency in Spain	YES	19	19
Support measures for workers, families and vulnerable groups					
7	8 and 9	Credit supplement to finance Regions' social service programmes	YES	25	25
8	1	Credit supplement to finance a <i>Fondo Social Extraordinario</i> (Extraordinary Social Fund) aimed exclusively at dealing with the social consequences of COVID-19	YES	300	300
8	3	LGs' surplus in 2019 may be used for investment expenditure	YES	300	300
8	34	Compensation for the suspension of public contracts as a result of COVID-19	YES	8	8
11	10	Rent aid for tenants of habitual residences who have temporary problems in paying all or part of their rent due to COVID and are vulnerable. Up to €900 a month	YES	300.7	0
11	13	Authorisation to transfer funds to the Regions and Ceuta and Melilla in advance for 2020 and 2021 to execute the 2018-21 State Housing Plan	YES	346.6	0
11		Additional state financial contribution to the 2018-2021 State Housing Plan	YES	100	100
11		Aid programme for victims of gender-based violence, people evicted from their habitual residence, homeless people and other especially vulnerable people	YES	50	50
11	40	Refund on behalf of <i>Instituto Español de Comercio Exterior</i> (Spanish Institute for External Trade - ICEX) of expenditure and granting of aid for cancellation of activities to promote international trade and other international events	YES	12.4	12.4
11	44	Suspension of electricity, natural gas and petroleum products bills during the state of alarm. For the self-employed.	YES	58	58
11	46	Aid to compensate part of DTT costs	YES	15	15
11	AP1	Extension of university contracts	YES	3.4	3.4
11	AP19	Plans to expedite justice in the commercial, contentious and social sphere once the state of alarm has ended	YES	40	40
15	AP1	Extension of predoctoral contracts for research staff	YES	0.4	0.4
15	4th FP	Provisions applicable to certain university loans	YES	1.5	1.5

Expenditure measures (Continued)					
RD Law	Art	DESCRIPTION OF MEASURE	IMPACT ON DEFICIT	GOVERNMENT ESTIMATE	AIReF's ESTIMATE
17	1	Direct grants to <i>Sociedad Reciproca Audiovisual Fianza</i> to boost financing for the cultural sector	YES	17	17
17	3	Extraordinary aid for the performing arts and music	YES	24	24
17	11	Direct grants for owners of cinematographic exhibitions. Extraordinary social fund	YES	13	13
17	12-13	Extraordinary aid system for the Spanish contemporary art and book sector	YES	5	5
19	10	Transfer to Social Security to balance the impact of COVID-19	YES	14,002	14,002
20	32	Transfer to Social Security to finance minimum living income [2]	YES	1,500	1,743
ACM 9 June		Wine sector measures	YES	91	91
ACM 16 June		MOVES II programme for efficient and sustainable mobility	YES	100	100
ACM 16 June		Educa Digital Programme for technological transformation	YES	48	48
22		Fondo COVID-19	YES	16,000	16,000
20/06/2020		Tourism Reactivation Plan (preparation of guides, training and promotion)	YES	62	62
20/06/2020		Tourism Reactivation Plan (tourist equipment and tourist intelligence systems)	YES	20	20
25	10	Tourist Destinations Sustainability Plan (support for investing in improving destinations)	YES	12	12
20/06/2020		12-month extension on paying the mortgage principal on assets in the tourism sector for self-employed people and companies and for operations subscribed before the SoA	NO		
20/06/2020		Moratorium on leasing fees for occasional transport buses in the tourism sector	NO		
25	7	Moratorium on the leasing of real estate related to tourist activity	NO		
25	38	RENOVE Plan 2020	YES	250	250
26	18	Temporary moratorium on payment of the principal in loan contracts instalments, leasing and renting of vehicles dedicated to public transport in financial difficulties due to COVID-19	NO		
26	8th FP	Extension of the Social Bonus to 30 September for the beneficiaries who are due to receive it before that date	NO		
26	9th FP	Extraordinary extension for a maximum of 6 months of leases of habitual residence for those that expire up to 30 September	NO		
26	9th FP	Guaranteed supply of electricity, petroleum products, natural gas and water until 30 September for consumers in their habitual residence	NO		
TOTAL EXPENDITURE MEASURES				38,037	35,535

(1) The SPU's calculation corresponds to the difference between the amount of the updated instalment payments according to collection forecasts at 1 January 2020, as provided in the RDL, and the amount that would be charged in the year in a budgetary extension scenario. The amount estimated by AIReF as a COVID measure is the difference between the updated amount indicated by the RDL and the amount AIReF had estimated in the scenario of estimated revenue before COVID.

(2) AIReF has estimated the annual cost of the benefit, which is around €3 billion. This cost is weighted for the 7 months that the measure will be in force. The Social Security estimates on the cost of employment incentives (included in the MAIN) are introduced and the savings estimated by SS by assimilating the benefit for dependent children under 18 years of age are deducted. In its latest estimate, this resulted in a reduction from an estimated €290M in the MAIN to €108M for 2020. The total cost will be €1,743M.

Central Government liquidity measures					
RD Law	Art	DESCRIPTION OF MEASURE	IMPACT ON DEFICIT	GOVERNMENT ESTIMATE	AIReF's ESTIMATE
7	12 and AP1	200M expansion of ICO's Thomas Cook financing facility to serve all companies established in Spain included in certain economic sectors and of the <i>Ministerio de Industria, Comercio y Turismo</i> (Ministry of Industry, Commerce and Tourism) guarantee regarding 50% of the available credit. Additional 100M ministerial guarantee	NO	200	200
8	29	Line of guarantees from the <i>Ministerio de Asuntos Económicos y Transformación Digital</i> (Ministry of Economic Affairs and Digital Transformation) for companies and the self-employed to mitigate the economic effects of COVID-19	NO	100,000	100,000
8	31	Extraordinary insurance coverage line for exporting SMEs from the <i>Fondo de Reserva de los Riesgos de la Internacionalización</i> (Reserve Fund for Internationalisation)	NO	2,000	2,000
8	35	The <i>Ministerio de Agricultura, Pesca y Alimentación</i> (Ministry of Agriculture, Fisheries and Food - MAPA) will finance the additional cost of the guarantees granted by <i>Sociedad Anónima Estatal de Caución Agraria</i> (State Limited Company for Agrarian Guarantees - SAECA) derived from the extension of the financial credits granted to owners of agricultural holdings affected by the drought of 2017 by up to one year, which will be agreed with the entities	NO	3	3
8	RDL Annex 8	ICO financing for the purchase and leasing of equipment and services for the digitisation of SMEs and remote working solutions (PLAN ACELERA)	NO	200	200
11	9	1,200M ICO guarantee line for State coverage of financing to vulnerable tenants	NO	1,200	1,200
11	AP1	CERSA COVID-19 guarantee line	NO	1,000	1,000
17	1	Lines of financing for companies in the cultural sector	NO	780	780
19	4	Authorisation to grant EC guarantees under the European Instrument for Temporary Support to mitigate unemployment risks in an emergency (SURE instrument)	NO	2,253	2,253
20/06/2020		ICO/AENA guarantees for the tourism sector 2020-2021	NO	3,256	3,256
20/06/2020		FOCIT loans for competitiveness and sustainable transformation of tourism	NO	515	515
25	11	Financing of tourism digitisation, innovation and internationalisation projects	NO	216	216
25	1	Line of guarantees for financing investments of companies and the self-employed	NO	40,000	40,000
25	2	Fund to support the solvency of strategic companies	NO	10,000	10,000
TOTAL LIQUIDITY MEASURES				161,623	161,623

Regions' revenue measures				
AREA	DESCRIPTION	IMPACT ON DEFICIT	REGION'S ESTIMATE	AIReF's ESTIMATE
Tax measures	Tax credits (<i>Juego</i> scheme), elimination of instalment payments in special PIT regimes (Navarra) and IGIC (Canary Islands).	YES	-121	-121
Conditional transfers from the AGE	<i>Fondo Social Extraordinario</i> (Extraordinary Social Fund - € 300M); <i>Fondo Emergencia Sanitaria</i> (Health Emergency Fund - € 300M); Aid for school canteens (€ 25M); <i>Fondo de Vivienda</i> (Housing Fund - € 100M); MOVES Programme (€ 100M). The effect of the reduction in the transfer for job training (€ 1.257M) is calculated, although some Regions have not reported this effect.	YES	92	-438
Revenue related to public services	Free services. Postponement of rent payments. Reductions in fees, rates and public prices, among which AIReF has estimated, in addition to what was communicated by the Regions, an expected drop in university fees.	YES	-203	-203
Other revenue measures	Other measures not included in previous sections	YES	12	12
TOTAL REVENUE MEASURES			-220	-750

Regions' expenditure measures				
AREA	DESCRIPTION	IMPACT ON DEFICIT	REGION'S ESTIMATE	AIReF's ESTIMATE
Health	Recruitment of additional health staff, overtime and salary increases related to COVID-19. Hospital care expenditure, expenditure on pharmaceutical products, medical supplies and other current expenditure. Expenditure on health care agreements. Investments related to the health response to the pandemic.	YES	-	7,010.0 - 9,595.0
Social services	Direct aid to families and intermediate institutions (social centres, local governments, etc.) to alleviate the social effects of the crisis. Social services' increased resource needs managed directly by the Regions. Increase in amounts of guaranteed minimum income in some Regions.	YES	751	751
Economic promotion	Direct aid to companies in various forms (subsidies to SMEs, microSMEs and self-employed people, weekly cheques, compensation for social contributions, etc). Aid to promote recruitment. Reinforcement of mutual guarantee and guarantee companies' resources. Approximately a quarter corresponds to investment aid and other capital expenditure.	YES	1,170	1,170
Education	Measures to adapt teaching to non-contact methods during confinement (purchase of computer equipment and software, aid to homes and institutions). Lower expenditure effects reported by some Regions have been discounted. Only a few Regions have already planned measures for the first months of the next academic year (September-December 2020).	YES	724	724
Training for employment	Cancellation of actions in this matter resulting from the deviation of the transfer for training for employment to the payment of direct benefits. Not all Regions have communicated measures to reduce this expenditure.	YES	-727	-1,257
Housing	Increase in subsidies for rental and rehabilitation of housing.	YES	129	129
Transport	Disinfection and safety preparation of passenger transport means. Other transportation expenditure related to the pandemic. The drop in billing and resulting compensation to transport concessionaires have been considered as impacts.	YES	65	65
Others	Other measures related to COVID-19, including expected savings on certain expenditure items , for which AIReF expects non-execution	YES	208	-79
TOTAL EXPENDITURE MEASURES			2,319	8,512.10 - 11,097.10

Social Security Measures					
RD Law	Art	DESCRIPTION OF MEASURE	IMPACT ON DEFICIT	GOVERNMENT ESTIMATE	AIReF's ESTIMATE
7 and 25	13 and 4th AP	50% allowance of the business contribution to the SS of employees with discontinuous fixed contracts in the tourism, commerce and hospitality sectors linked to tourist activity.	YES	45	26 / 26
7	11	Benefit for temporary incapacity for work assimilated to work accidents for all employed and self-employed workers.	YES	1,355	675 / 809
8 and 24	17 and 9	Benefit for the cessation of activity for self-employed people affected by the state of alarm	YES	3,767	4,729 / 5,791
8 and 24	17 and 8	Exemption from paying contributions for self-employed people affected by the state of alarm	YES	981	1,805 / 2,191
8 and 24	22-25	Contributory unemployment benefit under ERTes linked to COVID-19. Also for discontinuous permanent workers	YES	17,894	17,673 / 19,777
8 and 24	24, 6th AP	Exemption of the company from paying business contributions to SS under the ERTes linked to COVID-19	YES	2,216	5,346 / 6,094
24	10	Extraordinary benefit for cessation of activity for seasonal self-employed workers	YES		52 / 68
		Exemption from contributions for seasonal self-employed workers			19 / 25
24	1st AP	Exemption for companies with total force majeure ERTes from paying business contributions to SS	YES		
11	30-32	Extraordinary allowance for lack of activity for people integrated into the Special System for Household Workers of the GSSR of 70% of the regulatory base	YES	3.15	8 / 12
11	33	Exceptional unemployment benefit for the end of temporary contracts for one month of 80% IPREM	YES	17.6	27 / 27
11	34	6-month moratorium on social contributions for companies and the self-employed	YES	351	
11	35	Deferral of payment of debts to the SS for companies and the self-employed	NO	340	
15	22	Legal situation of unemployment due to the termination of the employment relationship in the trial period occurred during the SoA	YES	42	
15	25	Contributions under situation of inactivity in the Special System for Self-Employed Agricultural Workers established in the GSSR with a reduction of 19.11%	YES	43	
20		Minimum Living Income	YES	1,500	1,743 / 1,743(*)
TOTAL SOCIAL SECURITY MEASURES				28,555	32,103 / 36,563

(*) AIReF has estimated the annual cost of the benefit, which is around €3 billion. This cost is weighted for the 7 months that the measure will be in force. The Social Security estimates on the cost of employment incentives (included in the MAIN) are introduced and the savings estimated by SS by assimilating the benefit for dependent children under 18 years of age are deducted. In its latest estimate, this resulted in a reduction from an estimated € 290M in the MAIN to € 108M by 2020. The total cost will be € 1,743M

ANNEX II. SSF MEASURES

Measure	AIRcF's July assessment	AIRcF's SPU assessment	Government
50% allowance of the business contribution to the SS of employees with discontinuous fixed contracts linked to tourist activity.	<ul style="list-style-type: none"> ✓ Those potentially affected will be employees with a discontinuous fixed contract that are not under an ERTE ✓ The exemption for affected workers will be 50% of the contributions that must be paid by the average CB ✓ Duration: 10 months ✓ Impact: 26 M€ ✓ Affected: 13,500 	<ul style="list-style-type: none"> ✓ Duration: 5 months ✓ Impact: 13 M€ ✓ Affected: 13,500 	<ul style="list-style-type: none"> ✓ 45 M€
Extraordinary benefit for the cessation of activity for self-employed people affected by the state of alarm 70% contribution base	<ul style="list-style-type: none"> ✓ The impact of the crisis on each branch of activity is estimated (double digits) ✓ The average benefit is estimated from the updated CWLS ✓ From July to September, 25% will not return to work ✓ Average duration: 4 months (5 months in scenario 2) ✓ Impact: 4,729/5,791 M€ ✓ Affected: 1.4 M until June, 315 thousand until September 	<ul style="list-style-type: none"> ✓ Duration: 3 months (4 months in scenario 2) ✓ Impact: 3,623/4,270 M€ ✓ Affected: 1.4 M€ 	<ul style="list-style-type: none"> ✓ 3,767 M€ ✓ 1.4 M affected
Exemption from paying contributions for self-employed people affected by the COVID crisis	<ul style="list-style-type: none"> ✓ The exemption will be for total contributions until July ✓ Those who have returned to work will have an exemption of 100% in July, 50% in August and 25% in September ✓ Those who have not returned to work will have an almost total exemption for 3 months from July to September (€30 less per month) ✓ Duration: 6 and a half months (1 more month in scenario 2) ✓ Impact: 1,805/2,191 M€ ✓ Affected: 1.4 M€ 	<ul style="list-style-type: none"> ✓ Duration: 3 months (4 months in scenario 2) ✓ Impact: 1,316/1,552 M€ ✓ Affected: 1.4 M€ 	<ul style="list-style-type: none"> ✓ 981 M€ ✓ 1.4 M affected

Measure	AIRcF's July assessment	AIRcF's SPU assessment	Government
Contributory unemployment benefit in the ERTes linked to COVID-19.	<ul style="list-style-type: none"> ✓ The impact of the crisis on each branch of activity is estimated (double digits) ✓ The average benefit is estimated on the basis of unemployment benefit statistics. ✓ Assumptions are made about the monthly evolution of returning to work ✓ Average duration: 5 months (6 in scenario 2) ✓ Impact: 17,673/19,777 M€ ✓ Affected: 3.4 M€ 	<ul style="list-style-type: none"> ✓ Average duration: 3 and a half months (4 in scenario 2) ✓ Impact: 15,211/17,938 M€ ✓ Affected: 4 M€ 	<ul style="list-style-type: none"> ✓ 17,894 M€ ✓ 4 M affected
Exemption of the company from paying business contributions to SS under the ERTes linked to COVID-19 Variable percentages according to month, company size and employment evolution	<ul style="list-style-type: none"> ✓ Those affected and the duration are the same as in the previous measure ✓ The exemption depends on the month, size of the company and employment situation of contributors under an ERTE ✓ Average duration: 5 months (6 in scenario 2) ✓ Impact: 5,346/6,094 M€ 	<ul style="list-style-type: none"> ✓ Duration: 3 months (4 months in scenario 2) ✓ Impact: 6,203/6,875 M€ ✓ Affected: 3.4 M€ 	<ul style="list-style-type: none"> ✓ 2,216 M€ ✓ 4 M affected

Measure	AIRcF's July assessment	AIRcF's SPU assessment	Government
Benefit for temporary incapacity for work assimilated to occupational accidents For all employed and self-employed workers	<ul style="list-style-type: none"> ✓ Average duration of time off: 21 days ✓ The ratio of confirmed COVID cases to people in quarantine is set at 5.5 ✓ Cases are estimated with a logistic model or an SIR model. ✓ Impact: 675/809 M€ ✓ Affected: 750,000 	<ul style="list-style-type: none"> ✓ Average duration of time off: 15 days ✓ The ratio of confirmed COVID cases to people in quarantine is set at 4 ✓ Affected: 530,000 	<ul style="list-style-type: none"> ✓ 1,355 M€ ✓ 400 thousand affected
Extraordinary allowance for people integrated into the GSSR Special System of Household Employees 70% of the regulatory base	<ul style="list-style-type: none"> ✓ The number of workers affected by the measure is estimated from the affiliation data. ✓ The benefit will be for 70% of the average contribution base of these workers. ✓ Duration: 2 months (3 in scenario 2) ✓ Impact: 8/12 M€ ✓ Affected: 10,000 	<ul style="list-style-type: none"> ✓ There are no changes to this estimate 	<ul style="list-style-type: none"> ✓ 3.15 M€
Exceptional unemployment allowance for the end of a temporary contract for one month 80% IPREM	<ul style="list-style-type: none"> ✓ The number of beneficiaries is estimated from the affiliation data by branch ✓ It is weighted by temporary contracts lasting more than two months and by the percentage of workers not entitled to unemployment benefits ✓ The average benefit is 80% of the IPREM ✓ Duration: 1 month ✓ Impact: 27 M€ ✓ Affected: 64,000 	<ul style="list-style-type: none"> ✓ There are no changes to this estimate 	<ul style="list-style-type: none"> ✓ 17.6 M€ ✓ 462 thousand affected

Measure	AIRcF's July assessment	AIRcF's SPU assessment	Government
Minimum Living Income	<ul style="list-style-type: none"> ✓ The number of beneficiaries by income ratio is estimated from the 2018 LCS ✓ Candidates who do not meet equity requirements are eliminated ✓ The number of beneficiaries for 2019 is estimated by regression. ✓ Impacts of employment incentive and savings for child benefit estimated by the SS are included ✓ 2020 Impact: 1,743 M€ ✓ Affected: 811 thousand 	<ul style="list-style-type: none"> ✓ The measure was not approved when the previous report was published 	<ul style="list-style-type: none"> ✓ € 2,890M (complete annual cost – € 1,500M for 2020. Not including employment incentive and savings for child benefits) ✓ 850 thousand
Benefit for cessation of activity for temporary self-employed workers whose activity has been affected by the crisis 70% contribution base	<ul style="list-style-type: none"> ✓ The difference between the maximum number of affiliates last year and the average number of affiliates for the rest of the year is considered to be affected. ✓ It is considered that the CB will be identical to that of the self-employed total. ✓ Duration: 3 months (4 in scenario 2) ✓ Impact: 52/68 M€ ✓ Affected: 22 thousand 	<ul style="list-style-type: none"> ✓ The measure was not approved when the previous report was published 	
Exemption from paying contributions for temporary self-employed workers whose activity has been affected by the crisis	<ul style="list-style-type: none"> ✓ Those affected and the duration are the same as in the previous measure ✓ Impact: 19 / 25 M€ 	<ul style="list-style-type: none"> ✓ The measure was not approved when the previous report was published 	