

PRESS RELEASE
03/12/2020

AIReF ESTIMATES A DEFICIT OF THE REGIONS OF 0.8% OF GDP IN 2021 AND WARNS OF THE RISK OF A WIDER GAP AS FROM 2022

- The Regions will have less revenue in 2022 and 2023 as a result of the impact of the negative settlements of the financing system, the lower amount of funds linked to the Recovery Plan and the absence of extraordinary transfers from the State
- This situation might also be compounded by the consolidation of a significant part of the expenditure incurred in 2020 and 2021
- AIReF estimates that the Regions' revenue will remain stable in 2021 and that expenditure will grow by 2%, although some regional budgets include a higher growth in expenditure without detailing it.
- Although the Regions' debt will stand at around 26% of GDP in 2021, 1.4 points lower than the expected ratio in 2020, AIReF warns that it will still be 1.6 points higher than the level recorded in 2019
- It recommends the Regions to incorporate information on the measures underpinning their expenditure forecasts and adapt their actions to the development of the pandemic so as to avoid structural increases in expenditure.
- It highlights the need to start drawing up the rebalancing plans required by the Organic Law on Budgetary Stability and Financial Sustainability and calls for a medium-term national fiscal strategy that will realistically and credibly ensure financial sustainability.
- Local Governments (LGs) will close 2021 with a deficit of 0.1 points of GDP, after being close to budgetary balance in 2020 and recording years of surpluses
- The City Councils of Barcelona, Palma, Bilbao, Valladolid, Gijón and l'Hospitalet de Llobregat and the 3 Provincial (Foral) Councils will already record a deficit in 2020

The Independent Authority for Fiscal Responsibility (AIReF) today presented the Report on the Main Lines of the 2021 Budgets of the Autonomous Regions, in which it estimates that the sub-sector will close 2021 with a deficit of 0.8% of GDP, up from the 0.6% which it is likely to record in 2020. In the report, AIReF also warns of possible imbalances that may occur in the budgetary balance of the Regions from 2022 as a result of the impact of the negative settlements of the Regional Financing System (RFS), the lower amount of funds linked to the Recovery, Transformation and Resilience Plan (RTRP) and the



absence of extraordinary transfers from the State. This situation might be compounded by the consolidation of a significant part of the expenditure incurred in 2020 and 2021.

AIReF's deficit estimate for 2021 is more positive than that forecast in the Budgetary Plan, which puts the reference rate of the regional deficit at 1.1%. The difference mainly results from the assumptions on the level of consolidation of the expenditure associated with the health crisis as AIReF considers that, given its temporary nature and the evolution of the pandemic forecast in its central scenario, part of this expenditure would not be repeated in 2021. For the individual analysis, AIReF has assumed that the extraordinary transfer from the State to reduce the Regions' deficit would account for 1.1% of regional GDP for each one. Under this criterion, nine Regions could close 2021 with a deficit below the reference value, four with a deficit similar to -1.1% while another four would record a higher deficit.

| CC.AA. | AIReF's forecasted deficit in 2020 | AIReF's forecasted deficit in 2022 |
|-------------------|---|---|
| Andalusia | -0,1% | -0,9% |
| Aragon | -0,7% | -1,1% |
| Asturias | -0,2% | -0,7% |
| Balearic Islands | -0,2% | -0,5% |
| Canary Islands | 0,5% | 0,4% |
| Cantabria | -0,6% | -1,1% |
| Castile and Leon | -0,5% | -1,1% |
| Castile-La Mancha | -0,5% | -1,4% |
| Catalonia | -0,5% | -0,5% |
| Extremadura | -0,3% | -1,4% |
| Galicia | -0,2% | -0,4% |
| Madrid | -0,2% | -0,3% |
| Murcia | -1,3% | -1,7% |
| Navarre | -2,4% | -1,1% |
| Basque Country | -2,0% | -0,9% |
| Rioja | -2,4% | -1,1% |
| Valencia | -1,6% | -2,3% |
| TOTAL | -0,60% | -0,80% |

AIReF estimates that regional revenue in 2021 will remain stable compared with 2020 and that expenditure will grow overall by 2%, without including the revenue linked to the Recovery Plan. However, part of the regional draft budgets and main budgetary lines forecast growth in expenditure higher than that forecast by AIReF, without specific information on the impact and nature of the measures underpinning this increase. Full implementation of these appropriations would raise the deficit. In the event that this increase eventually materialises, AIReF considers



that it might be structural and would not, in theory, be permanently funded, thus increasing the structural deficit that existed prior to the crisis.

With regard to the funds linked to the RTRP, AIReF estimates that these funds would raise the growth in expenditure to 11% and in revenue to 10%, which should increase their weight in GDP to 18% and 17.2%, respectively. However, the effect in terms of the deficit would be neutral.

In this context, AIReF warns of the risk of lower availability of revenue for the Regions in 2022 and 2023 as a result of the impact of the negative settlements of the Regional Financing System (RFS), the lower amount of funds linked to the RTRP and the absence of extraordinary transfers from the State. This situation might be compounded by the consolidation of a significant part of the expenditure incurred in 2020 and 2021.

AIReF forecasts that debt will stand at around 26% of GDP in 2021, 1.4 percentage points of GDP lower than the ratio expected in 2020. This level would still be 1.6 points higher than that recorded in 2019. The increase will be uneven. Valencia, the Balearic Islands and Murcia would be the territories that would record the largest increases in their debt in 2021 compared with 2019, from previous levels that were already high. In 2021, no Region will meet the 13% reference limit, although the Canary Islands, Madrid and the Basque Country would be closer to the legal reference rate.

In 2022 and 2023, the excess deficit forecast in 2021 in some Regions and the settlement of the 2020 instalment payments will result in new borrowing needs. Under a scenario of annual correction of the deficit by 0.25 points of GDP from 2023 for each Region until budgetary balance is achieved, AIReF estimates that returning to the debt level of 23.7% of GDP recorded at the end of 2019 will require at least a decade. In contrast with the scenarios projected by AIReF prior to the crisis, in which the level of 13% of GDP would be reached in around 2035, this limit is not forecast to be reached prior to 2049, even if the budgetary balance of the sub-sector as a whole is maintained.

In this context, AIReF recommends that the Regions should incorporate information on the specific measures underpinning the expenditure forecast, identifying their possible sources of financing and their nature (temporary or permanent) and assessing their additional economic impact in 2021 on the level forecast at the end of 2020 and, as the case may be, in the following years. It also suggested to the Regions that they should adapt their actions to the development of the pandemic, avoiding structural expenditure increases that are not accompanied by the corresponding structural financing.

In addition, it recommends beginning work on drawing up the Rebalancing Plan provided for in the Organic Law on Budgetary Stability and Financial Stability. It also reiterates the outstanding recommendation of establishing a medium-term national fiscal strategy that will act as fiscal guidance and will realistically and credibly ensure the financial sustainability of General Government.

Local Governments

AIReF has also presented the Supplementary Report on the Individual Evaluation of the Main Lines of the 2021 Budgets of the Local Governments, in which the expected results of the 24 large local governments confirm the forecasts of the 5 November report on the local sub-sector as a whole. In that report, AIReF estimated that Local Governments might close 2021 with a



deficit of 0.1 points of GDP, after recording close to budgetary balance in 2020. Within the group of large local governments, the City Councils of Barcelona, Palma, Bilbao, Valladolid, Gijón and l'Hospitalet de Llobregat and the 3 Provincial (Foral) Councils will close 2020 with a deficit. In 2021, the City Councils of Barcelona, Bilbao and Vigo and the 3 Provincial (Foral) Councils will also post a deficit, while the rest will record lower surpluses.

AIReF continues to estimate that in 2021 the application of savings from previous years to local expenditure might amount to 0.1 points of GDP, with the effect of the RTRP on the balance being neutral. The large local governments with very healthy positions and accumulated savings are those which, to a greater extent, can apply surpluses to expenditure after the suspension of the fiscal rules. In fact, the cash surpluses accumulated by this group account for 20% of the total sub-sector.

The possible consolidation in the first half of 2021 of discretionary measures relating to the health crisis might amount to over 0.1 points of GDP in the sub-sector. The group of large local governments have adopted expenditure measures as a result of COVID-19 accounting for almost 2% of their expenditure in 2020. In fact, the large local governments are the ones that have had to face the most expenditure given the intensity of the pandemic in the municipalities with the highest population densities.

In addition to the effects of the pandemic, the sharp growth in expenditure in 2019 has been decisive in the performance of the sub-sector and the group of large local governments in 2020 and 2021. In 2020, the effect of the pandemic on the large local governments will mean that computable expenditure will rise by almost 5% compared with 2019, when it grew by more than 4%.

AIReF therefore recommends that the large local governments incorporate information on the specific measures underpinning the expenditure forecast financed with accumulated surpluses, the need for such measures, as well as their economic impact and whether or not they will be consolidated in the future, avoiding structural increases in expenditure. It also suggests starting work on drawing up medium-term plans to guide their annual policies towards safeguarding sustainability in line with the medium-term fiscal strategy of the General Government.

In addition, the report continues the analysis of medium-term sustainability risks. The 26 Local Governments with sustainability risks selected for evaluation are the same as in the previous cycle. However, given the data provided, Rota has been removed from the evaluation for providing information that guarantees it. In addition, the City Council of Granada will be removed from the analysis in the future as a result of the improvement recorded over recent years. The risk situation of all the selected councils remains the same, with the exception of Alcorcón and La Línea de la Concepción, where it has worsened, and Arcos de la Frontera, Gandía and San Andrés del Rabanedo, where it has improved.