

Appearance by the President, Cristina Herrero, before the Budget Committee
of the Congress of Deputies

**AIReF IDENTIFIES SIGNIFICANT DEFICIENCIES IN THE
2023 BUDGET AND WARNS OF ITS WEAKNESS AS A
KEY ECONOMIC POLICY INSTRUMENT**

- Cristina Herrero stresses that these deficiencies, observed in previous years, are worsening and detract from the quality of the information in the Budget, undermine its potential as a tool for economic planning and weaken its accountability function
- The deficiencies include underestimation of 2022 revenue, failure to incorporate measures, lack of information on execution of the RTRP and lack of integration in a medium-term fiscal strategy
- AIReF presents a complete macroeconomic scenario up to 2026, which suggests that the economy recovers to pre-pandemic levels of activity in the first quarter of 2024
- AIReF estimates a total General Government (GG) deficit of 3.3% of GDP in 2023, without including the extension of the package of energy measures, after closing 2022 with a deficit of 4.4% of GDP
- In the medium term, the GG deficit stabilises at around 3.2% of GDP and the scope for reduction without additional measures is exhausted
- AIReF warns that the increase in current primary expenditure would be almost 7% if all the measures were extended for 2023, which is clearly above the recommendation made by Brussels to Spain
- Debt will fall by 7.2 points in 2023 compared with 2021, although in the medium term AIReF projects it will stabilise at around 108.5% of GDP
- AIReF makes two new recommendations aimed at properly structuring the budget process and addressing the deficiencies noted in the Budget

The President of the Independent Authority for Fiscal Responsibility (AIReF), Cristina Herrero, appeared today before the Budget Committee of the Congress of Deputies to present the Report on the main budgetary lines and draft budget for 2023. AIReF identifies significant deficiencies in the Budget about which the institution has been warning for some time and which are tending to become budgetary practice.

The President of AIReF stated that the draft budget is the main economic policy instrument of the Government and therefore a fundamental control mechanism at a national level in terms of its design and implementation. However, it has notable

deficiencies that detract from its informative quality and its potential as an economic planning tool. Moreover, the Budget as it is designed weakens its accountability function. According to AIReF, the current uncertainty cannot undermine the purpose of the Budget, which has elements for managing it.

Among the deficiencies, AIReF's President highlighted that the 2023 Budget underestimates the starting point as it is based on revenue forecasts that do not include the most recent information for 2022. In addition, it does not incorporate measures for a potentially large amount that are expected to be adopted, given that the Government itself projects that the economic circumstances that led to them in 2022 will persist in 2023. Furthermore, the measures announced a week later are not incorporated and the Budgetary Plan sent to Brussels incorporates a second scenario with higher revenue and expenditure than the Budget.

Moreover, the Budget still does not provide information on the national accounting of the initial budget, national accounting adjustments and execution of the Recovery, Transformation and Resilience Plan (RTRP). Neither does it resolve the deficiencies generated in the process of endorsement of the macroeconomic outlook by AIReF and it does not form part of a medium-term strategy.

AIReF has warned of these weaknesses on previous occasions through the inclusion of new recommendations and the reiteration and expansion of previous recommendations in the Report on the 2022 Budget (October 2021), and in the endorsement of the macroeconomic forecasts of the 2023 Draft Budget (October 2023). In this context, AIReF considers that these are repeated deficiencies that are tending to become budgetary practice and to worsen, following the unsatisfactory response to the institution's recommendations.

The report presented today by the President in Congress completes the endorsement of the macroeconomic forecasts made on [October 4th](#). The report assesses the 2023 Budget of the Central Government and the Social Security Funds. On October 27th, AIReF will complete its analysis by reporting on the Budgetary Plan sent to Brussels, the main lines of the regional and local government budgets and the individual reports of each region.

Macroeconomic scenario

Regarding the macroeconomic scenario, AIReF reiterates that the nominal growth that accompanies the Budget does not present substantive differences from AIReF's current forecast. However, there are differences in the outlook for real growth and inflation, the composition of real growth and the perception of risks. AIReF has revised its estimate for real growth to 1.5%, while the Government has lowered it to 2.1%. Although the Government has brought its forecasts closer to those of AIReF, they remain in the optimistic part of the confidence interval and above those of most analysts and institutions. At the same time, there has been a general upward revision of inflation forecasts, albeit less intense in the case of the Government, which forecasts a change in the deflator that lies at the lower limit of AIReF's central range.

AIReF continues to identify major risks surrounding the central scenario: the security of gas supply, the tightening of monetary policy, the behaviour of private consumption, the

risks of de-anchoring of inflation expectations and the execution risks of RTRP investments, as AIReF estimates a more gradual and prolonged impact over time than it estimated in May.

In order to help medium-term economic planning, which AIReF considers essential in this uncertain environment and which it repeatedly includes among its recommendations, AIReF presents a complete macroeconomic scenario up to 2026. According to this scenario, the economy would resume a path of recovery in the spring of 2023 and return to pre-pandemic levels of activity in the first quarter of 2024. Specifically, GDP will moderate to 1.5% in 2023, after having grown by 4.4% in 2022. In 2024, it will grow by 2.7%, in 2025 by 1.8% and in 2026 by 1.6%.

Fiscal scenario

Against this background, the government deficit will stand at 3.3% in 2023 without including the extension of the package of energy measures, after ending 2022 at 4.4% of GDP. AIReF's forecasts remain 0.6 points below the reference rates set by the Government. In the medium term, AIReF estimates that the GG deficit will stabilise at around 3.2% of GDP, with a slight upturn in 2026 to 3.3% of GDP. According to AIReF, the margin for reducing the deficit without adopting additional measures is exhausted and the gap in the accounts stabilises above the 3% of GDP limit set in the Stability and Growth Pact.

Specifically, AIReF notes that the level of deficit reduction in 2023 will depend on the decision on the extension of the measures. The expected deficit reduction is influenced by several factors such as the reduction in the cost of measures to combat COVID, the revenue measures included in the Budget and the baseline evolution of revenue and expenditure. However, the projected deficit of 3.3% would be increased depending on the horizon and the scope of the extension(s) to be adopted over the year, as well as by new measures.

AIReF also notes that the revenue measures included in the Budget will add 0.2 points to the weight of revenue over GDP in 2023 and warns that the permanent measures entail a structural loss of revenue, while the increases in revenue come from temporary measures.

By GG sub-sector, AIReF forecasts a deficit in 2023 of 3% of GDP for the Central Government, 0.2 points less than in 2022. In this regard, AIReF points out that since the fiscal rules were suspended in 2021, the revenue forecast in the GSB has been below what has actually been collected, a trend that seems to be continuing for 2023. Specifically, AIReF estimates that in 2023 the weight of tax revenue as a percentage of GDP will be 0.5 points higher. The main difference focuses on the year-end 2022 figure. The total weight of Central Government revenue in relation to GDP stabilises until 2023. The non-financial expenditure limit in 2023 consolidates the increase of the last two years and is 1.1% higher than in 2022. AIReF considers a reduction in the weight over GDP of 1.3 points in 2023, excluding the RTRP.

For the Social Security Funds, AIReF estimates a deficit of 0.7% in 2023, 0.2 points higher than in 2022 and in line with the Government's reference rate. The weight of revenue as a proportion of GDP rises by 0.2 points as a result of the increase in

contributions and higher transfers from the State, while the weight of expenditure as a proportion of GDP rises by 0.4 points due to the increase in pensions in line with the CPI.

At her appearance, Cristina Herrero gave an initial overview of the Budgetary Plan, which will be analysed in more detail in the Report of October 27th. The plan presents two scenarios with the same deficit path and without considering the impact of the measures on the macroeconomic scenario. Scenario 2 raises revenue and expenditure by the same amount for both years, although the different assumptions underlying the two scenarios, which are based on the same macroeconomic outlook, are not clear. It does not specify which measures are extended, which might explain the differences from AIReF's forecasts in 2023

CSR and sustainability

According to the Country Specific Recommendation (CSR), Spain should limit the increase in nationally financed current primary public expenditure below medium-term potential growth (ranging from 3.1% to 5.1% depending on the deflator). According to AIReF, the increase in expenditure envisaged in the 2023 GSB would be in the range of compliance with the CSR, but if all the measures were extended for 2023, the current primary expenditure of the GG would be almost 7% per year, which is clearly above the recommendation.

In terms of sustainability, AIReF states that the favourable trend in the denominator of the debt ratio means that it can be expected to fall in the short term. For 2023, AIReF estimates a reduction of 7.2 points of GDP compared with the 2021 level due to the favourable evolution of nominal GDP. However, the pace of this reduction is projected to slow down in the medium term and stabilise at 108.5% of GDP.

Recommendations

In this context, AIReF makes two new recommendations aimed at properly structuring the budget process and addressing the deficiencies noted in the Budget: to restore the central role of the Budget as an instrument of fiscal and economic policy and an element of design, planning, execution, control and supervision of the activity of the public sector; and to incorporate and publish, in any extension of the measures, an evaluation of their effectiveness and efficiency and specify the conditions that trigger their extension or withdrawal with the aim that the measures can be integrated into a realistic and credible medium-term national fiscal strategy.

It also reiterates the recommendation on the need to include information on national accounting adjustments in the Budget; information on those entities which, although not of a public nature, are included for the purposes of ESA 2010 in the Central Government sub-sector and on the balance resulting from the net lending/borrowing of Central Government Bodies; and an initial budget of the CG and SSFs in national accounting terms. AIReF is also keeping alive and repeating its recommendation to establish a medium-term fiscal strategy to provide fiscal guidance and credibly and realistically guarantee sustainability.

These recommendations are in addition to those made in the endorsement of October 4th on the need for the Ministry of Economic Affairs and Digital Transformation to consult AIReF on the Report on the Situation of the Spanish Economy that it draws up and which

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is the basis for setting the budgetary stability and public debt targets, which constitute the first step for preparing the Draft General Government Budget. AIReF also reiterated the need for adequate information on the budgetary and fiscal measures included in the macroeconomic scenario and to regulate the endorsement process through an agreement with the Ministry of Economic Affairs and Digital Transformation.