

AIReF warns of a 9% expansion in spending by large Local Governments

- Including the positive impact of the 2020 settlement compensation, the surplus forecast is 3% of its revenues.
- In its report of 6 July AIReF recommended the Local Governments (LGs) to avoid increases in expenditure or reductions in revenue that do not have permanent financing, a recommendation that is still valid today.
- Of the 24 large Local Governments, AIReF expects the following to incur a deficit as a result of their management in 2023: the local councils of Madrid, Barcelona, Bilbao, Valladolid and Vigo, the provincial councils of Barcelona and Valencia and the foral councils of Gipuzkoa and Bizkaia.
- For the purposes of the expenditure rule, the group of large LGs expects to increase eligible expenditure by around 9%, following 11% growth in 2022. The growth in eligible expenditure of the group of large LGs at the end of 2023 could raise the 2019 level by almost 35%, which represents an annual average of almost 9% in the period of suspension of the fiscal rules.
- AIReF maintains the sustainability risk rating made in the report on the expected closure of 2022 for the 22 Local Governments analysed, except in the cases of Arcos de la Frontera Town Council, which worsens, San Fernando de Henares, which improves, and Almonte, which is removed from the analysis, as its improvement has been consolidated. Particularly worrying are the situations of the city councils of Jaén and Jerez de la Frontera, where the situation of sustainability risk worsens year by year.

The Local Governments subsector will close the financial year 2023 with a situation close to balance, compared with the surplus of 1% of GDP that was envisaged in the April Report, according to the Report on the budget execution of the LGs published today by the Independent Authority for Fiscal Responsibility (AIReF). If the positive effect in 2023 of the offsetting of the 2020 settlement is excluded from the calculation and, therefore, the management of the Local Governments this year is taken into account, AIReF points out that of the 24 large

Local Governments, it expects the following to incur a deficit resulting from their management in 2023: the local councils of Madrid, Barcelona, Bilbao, Valladolid and Vigo, the provincial councils of Barcelona and Valencia and the foral councils of Gipuzkoa and Bizkaia. The main reason for this development of a greater imbalance is that, for the purposes of the expenditure rule, the group of large Local Governments plan to increase their eligible expenditure by around 9%, after an 11% growth in 2022. AIReF already recommended in its report of 6 July that the Local Governments should avoid increases in expenditure or reductions in revenue that do not have permanent funding.

The Independent Authority for Fiscal Responsibility (AIReF) is legally mandated to report each year on the budget execution, public debt and expenditure rule of the different Public Administrations (PAs). This report is complementary to the one published on 6 July last and includes the individual assessment of the main fiscal indicators that make it possible to anticipate the expected year-end of 2023 for the 24 large Local Governments (LGs) monitored by AIReF, as well as the sustainability assessment of the local councils in which AIReF detected medium-term risks at the start of the current budget cycle.

For the group of large Local Governments AIReF forecasts a surplus of almost 3% of their revenue in 2023, slightly worse than its April estimates. Given the impact on the 2022 and 2023 results of the large Local Governments in common territory of the negative 2020 settlement of the Financing System and its compensation, AIReF includes in this report the estimates of the expected closure in 2023 once the positive effect of the aforementioned settlement has been stripped out, in order to show the results that depend on the management of the Local Government itself, in conditions that are homogeneous with other financial years. Therefore, if the extraordinary compensation for the year for the negative settlement in 2020 is discounted, the group of large LGs would obtain a balance close to equilibrium.

This balance estimated by AIReF for the group of large Local Governments is consistent with the estimates for the whole of the Local Governments sub-sector. The reduction in the surplus of 1% of revenue from the previous report to the current forecast of balance is basically explained by the higher expected expansion of expenditure according to the information provided by the Local Governments and the implementation observed to date. In fact, the large Local Governments' own homogenised forecasts of extraordinary compensations imply a deficit of close to 2% of their revenues, worsening the one reported in April, which was balanced.

Of the 24 large Local Governments, AIReF expects the following to run a deficit in 2023 as a result of their management: the local councils of Madrid, Barcelona, Bilbao, Valladolid and Vigo, the provincial councils of Barcelona and Valencia and the foral councils of Gipuzkoa and Bizkaia. AIReF is therefore forecasting deficits in nine large Local Governments (LGs) in 2023 when in April it was only estimating deficits in four. Including the positive impact of the offsetting of the negative settlement, AIReF estimates that the city councils of Barcelona, Bilbao and Valladolid, as well as the foral Councils of Gipuzkoa and Bizkaia will run deficits in 2023.

On the expenditure side, the large Local Governments plan to increase their primary expenditure, net of RTRP (Recovery and Resilience Plan) funding, by more than 4% in 2023, following increases of more than 7% in the previous two years. The overall result is particularly affected by the projected growth of almost 10% in primary expenditure in 2023 for the subgroup of large Provincial Councils.

For the purposes of the expenditure rule, the group of large Local Governments plans to increase eligible expenditure by around 9%, after an 11% increase in 2022. In this respect, the growth forecast for 2023 by the Foral Councils group stands out, at more than 20%, after a 10% increase in 2022, affected by revenue reduction measures. Likewise, the city councils of Las Palmas de Gran Canaria, Córdoba, Vigo, the Provincial Council of Barcelona and the Foral Council of Gipuzkoa estimate changes in eligible expenditure in 2023 of more than 20%. As a result, the growth in eligible expenditure of the group of large LGs at the end of 2023 could be almost 35% higher than in 2019, which represents an annual average of almost 9% in the period of suspension of the tax rules.

In this regard, AIReF already recommended in its report of 6 July that the Local Governments should avoid increases in expenditure or reductions in revenue that do not have permanent financing.

AIReF also recommended that the financial supervisory bodies should verify the correct application of the European System of Accounts criteria in the calculation of the net lending/net borrowing for each year as it has detected that some Local Governments have not correctly included, among other adjustments, those arising from the significant impact of the negative 2020 settlement and the compensation from the State.

City councils with sustainability risks

This report also continues with the monitoring of the 22 city councils in which AIReF identified significant medium-term sustainability problems at the start of the cycle. The 22

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city councils with a population of over 20,000 inhabitants analysed are: Alcorcón, Alboraya/Alboraiá, Algeciras, Almonte, Aranjuez, Arcos de la Frontera, Arganda del Rey, Ayamonte, Barbate, Los Barrios, Caravaca de la Cruz, Gandía, Jaén, Jerez de la Frontera, La Línea de la Concepción, Los Palacios y Villafranca, Navalcarnero, Parla, Puerto Real, San Andrés del Rabanedo, San Fernando de Henares and Totana.

AIReF maintains the sustainability risk rating made in the report on the expected closure of 2022 for all the Local Governments analysed, except in the cases of Arcos de la Frontera Local Council, which worsens, San Fernando de Henares, which improves and Almonte, which leaves the analysis because its improvement has been consolidated. Particularly worrying are the situations of the city councils of Jaén and Jerez de la Frontera, where the sustainability risk situation worsens year by year.

By 2023 AIReF expects all these Local Governments to be in surplus except in the cases of Jaén, Parla, Totana and Arcos de la Frontera local councils where it estimates a deficit.

Because of its negative impact on its return capacity, the increase in the average annual computable expenditure for the period 2019-2022 of more than 10% in the local councils of Totana and Arcos de la Frontera and more than 20% in Algeciras should be highlighted. For this reason AIReF recommends that these local councils limit increases in expenditure or reductions in revenue this year that are not consistent with the commitments made to the Ministry of the Treasury and Public Administration Affairs (MINHAFF) in their adjustment plans.

Likewise, insofar as they are subject to enhanced supervision due to their situation, AIReF also recommends that the Ministry of the Treasury and Public Administration Affairs and their respective financial supervisory bodies should monitor the budget implementation in 2023 in the city councils of Algeciras, Arcos de la Frontera and Totana to detect increases in expenditure or decreases in revenue that are incompatible with the fiscal consolidation commitments made in their adjustment plans.