

# ENDORSEMENT OF MACROECONOMIC FORECASTS OF BUDGETARY PLAN OF KINGDOM OF SPAIN FOR 2024

43/23



Independent Authority  
*for* Fiscal Responsibility



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

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# ENDORSEMENT OF MACROECONOMIC FORECASTS OF BUDGETARY PLAN OF KINGDOM OF SPAIN FOR 2024

**The Independent Authority for Fiscal Responsibility, AAI (AIReF) has received the Government's request to report on the macroeconomic scenario that accompanies the Budgetary Plan for 2024, which must be published and submitted to the European Commission no later than October 15<sup>th</sup>.** Article 14 of Organic Law 6/2013, of November 14<sup>th</sup>, on the Creation of AIReF, establishes that the General Government sub-sectors must request that this institution issue a report on the macroeconomic forecasts that are incorporated in the draft budgets or the Stability Programme Update (SPU), indicating whether these forecasts are endorsed.

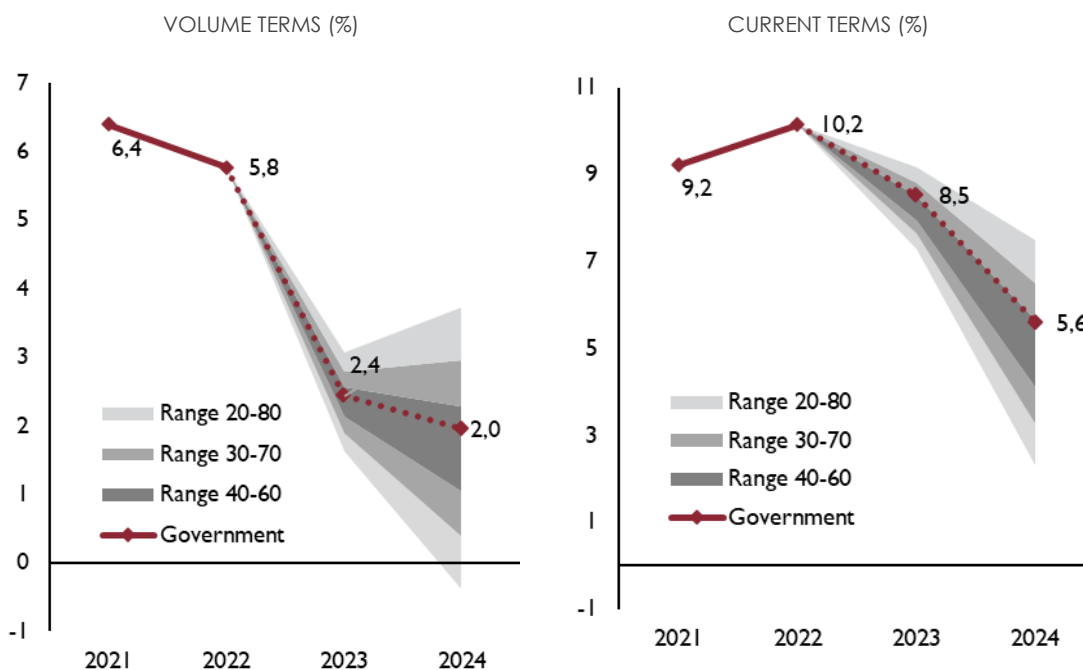
**The purpose of this report is to verify that the budgetary projections on revenue and expenditure contained in the Budgetary Plan are underpinned by reasonable macroeconomic forecasts, given the uncertainty that exists at this time in both the national and international contexts.** To this end, an assessment is made of not only the real growth and expenditure, but also of the macroeconomic aggregates in nominal terms, given the high correlation between tax revenue and the evolution of different components of GDP in current terms and of some spending items, such as pensions, which are indexed to inflation.

**AIReF endorses the macroeconomic scenario that accompanies the Budgetary Plan for 2024.** The Government's scenario forecasts real GDP growth of 2.4% in 2023 and 2% in 2024, which stand within the central range of the probability intervals prepared by AIReF based on its own forecast scenarios. As regards domestic prices, the Government's scenario maintains high growth rates of the GDP deflator in both 2023 and 2024 (of 5.9% and 3.6% in 2023 and 2024, respectively), compared with the 5.8% and 3.2% forecast by AIReF. This means, in nominal terms, that the Government's forecasts stand within the central range of the intervals estimated by AIReF, albeit closer to the upper limit, thus denoting the existence of potential downside risks (Figure 1).

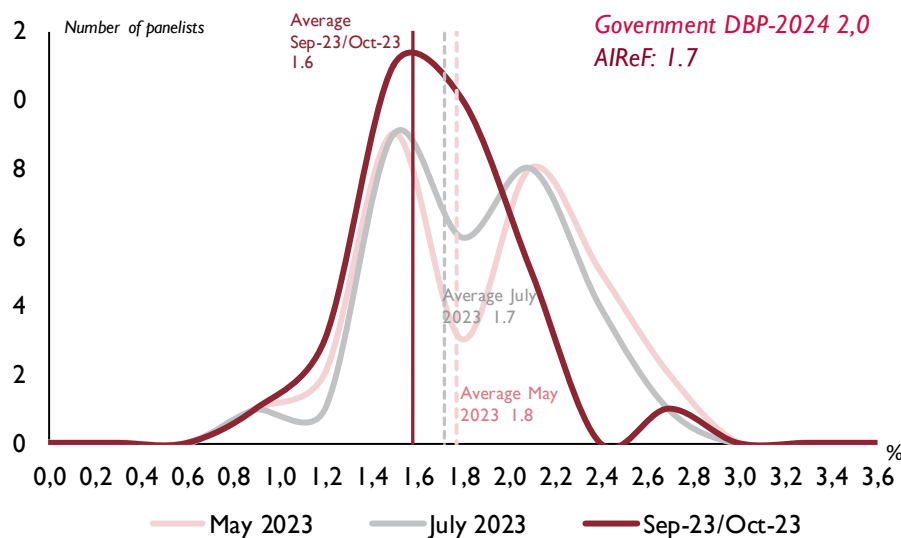
**AIReF considers that downside risks predominate in 2024 regarding the economic growth estimated by the Government.** In particular, the Government's macroeconomic scenario includes a significant acceleration of private consumption (it would grow by 2.5% in 2024 in real terms, compared with 1.5% estimated for 2023), which may be optimistic in a context of waning consumer confidence and the tightening of financing conditions for households.

Furthermore, gross fixed capital formation is expected to rise significantly in 2024 (by 4%), which also entails downside risks given the impact that the tightening of financial conditions may have on business investment against a backdrop of worsening foreign trade and, in particular, of the economies in the euro area, and in demand for residential property. Overall, the growth in national demand expected by the Government for 2024 is optimistic, given the tightening of the financing conditions of the economy, the withdrawal of the measures introduced to mitigate the impact of inflation – most of which are scheduled to be withdrawn in January 2024 – and the worsening of business and household confidence. In this regard, it is key that the investment projects associated with the Recovery, Transformation and Resilience Plan (RTRP), the effect of which on the real economy is subject to significant uncertainty, are suitably rolled out. Furthermore, the Government's scenario forecasts a negative contribution from the foreign sector to growth (-0.2 pp). The real growth forecasts are also higher than the average of the most recent estimates made by the main analysts and international bodies, which also indicates the existence of downside risks in the Government's estimates (see Figure 2).

**FIGURE 1. GROWTH FORECASTS OF GROSS DOMESTIC PRODUCT**



Source: National Statistics Institute, Ministry of Economic Affairs and Digital Transformation and AIRcF.

**FIGURE 2. COMPARISON OF GDP GROWTH FORECASTS IN VOLUME TERMS FOR 2024**


Source: forecast panels and AIReF.

Note: The averages and distributions have been calculated using only those entities that have issued new forecasts in September and up to October 10<sup>th</sup>.

**As regards prices, the Government's scenario points to the persistence of domestic inflationary tensions.** The Government forecasts growth in the GDP deflator of 3.6% in 2024, underpinned by growth in salaries slightly below inflation and in the expansion of business margins. AIReF considers that the rise in domestic prices could be somewhat more moderate than the Government's forecast, due to the slowdown of economic activity and the impact of the rises of the reference interest rates of the European Central Bank and the measures to reduce the liquidity of the economy. Furthermore, the Government's scenario includes an improvement in the real terms of trade of the economy, which is subject to risks, given the tensions that persist in the raw materials markets, particularly the energy markets.

**AIReF stresses the prevailing uncertainty at this time, associated with the geopolitical context.** The persistence of the war in Ukraine, and the break out of war in Israel may lead to a higher increase and greater price volatility of energy raw materials in the coming months regarding the external assumptions under which the Government has prepared its scenario. Furthermore, the weaknesses of China – an economy that has contributed significantly to global growth and the expansion of trade in recent decades – points to downside risks in regard to foreign trade growth, although the direct exposure of Spanish exports to this economy is not high.

### Recommendations

**AIReF issues one new recommendation and reiterates three, of which two are live recommendations.**

### **New recommendations**

Pursuant to Article 15.5 of Organic Law 2/2012, of April 27<sup>th</sup>, on Budgetary Stability and Financial Sustainability (LOEPSF), it falls to the Ministry of Economic Affairs and Digital Transformation to annually draw up the Report on the Situation of the Spanish Economy which, in addition to assessing the expected economic situation for each year that said report refers to, must contain the reference rate for the growth of the Spanish economy for the purposes of the expenditure rule.

This report has not been published to date. On September 25<sup>th</sup>, the Council of Ministers received a report from the Ministry of Economic Affairs and Digital Transformation on the situation of the Spanish economy. In the event that this is the report drawn up according to the provisions of Article 15.5, its content has not yet been published.

At present, with a view to the process for the drawing up of the budgets of the different territorial General Government sub-sectors, the only reference that exists is the forecast contained in the 2023-2026 Stability Programme Update at the level of the balance by sub-sector which, for 2024, in the case of the Autonomous Regions (ARs), this corresponds to a situation of budgetary balance and, in the case of the Local Governments (LGs) to a surplus of 0.2% of GDP.

In this regard, the risk exists that the ARs and LGs prepare their budgets with the sole limitation on the balance, but without taking into account that part of the revenue under the financing system they will receive in 2024 is temporary, which would mean they undergo growth in primary spending net of revenue measures, without the RTRP and without REACT, of around 7% and 9% respectively. This very high margin for growth in spending without the existence of the limitation that may derive from the expenditure rule could compromise the fiscal path in the future and mean that spending is strictly contained, which is hard to implement in practice.

### **Accordingly, AIR<sup>e</sup>F issues a new recommendation to the Ministry of Economic Affairs and Digital Transformation:**

- 1. To publish the Report on the Situation of the Spanish Economy provided for in Article 15.5 of Organic Law 2/2012, of April 27<sup>th</sup>, on Budgetary Stability and Financial Sustainability which stipulates the reference rate of the expenditure rule for 2024.**

### **Reiterated recommendations**

The LOEPSF establishes that the Ministry of Economic Affairs and Digital Transformation, in the preparation of its annual Report on the Situation of the Spanish Economy must previously consult the Bank of Spain and take into account the forecasts of the European Central Bank and the European

Commission. However, with regard to the Report on the Endorsement of the General State Budget (GSB) for 2023, published on October 4<sup>th</sup>, 2022, AIReF recommended that the Ministry of Economic Affairs and Digital Transformation should also consult it before issuing the Report on the Situation of the Spanish Economy.

This report contains a multiyear estimate of the economic scenario which serves as the foundation for the preparation of the GSB and which many public authorities take as the starting point for the preparation of their own macroeconomic and budgetary scenarios. Accordingly, AIReF considers that it should be consulted before it is issued given that, subsequently, it has to endorse the macroeconomic scenario when the budgets have already been prepared.

This ministerial department indicted that AIReF cannot report on the Report on the Situation of the Spanish Economy given that this is not provided for in the Organic Law on the Creation of AIReF, however, this may occur by means of a petition made by the ministerial department.

However, AIReF considers that it could voice its opinion on the Report on the Situation of the Spanish Economy by means of issuing an Opinion, which is an option provided for in the law on its creation.

**Accordingly, AIReF reiterates the recommendation made to the Ministry of Economic Affairs and Digital Transformation:**

**2. To previously consult AIReF regarding the Report on the Situation of the Spanish Economy prepared by this ministerial department pursuant to the provisions contained in Article 15.5 of Organic Law 2/2012, of April 27<sup>th</sup>, on Budgetary Stability and Financial Sustainability.**

### **Live recommendations**

In line with the good practices of our peer countries, AIReF considers that it would be advisable to enter into a “memorandum of understanding” in which the deadlines and the content of the exchanges of information required during the endorsement process of the macroeconomic forecasts are agreed. According to the response from the ministerial department, when AIReF issued this recommendation in previous reports, the interaction and flows of information between the different General Government sub-sector and AIReF are thoroughly regulated in a detailed manner in Order HAP/1287/2015, of June 23<sup>rd</sup>, on the performance of the forecasts contained in Article 4.2 of Organic Law 6/2013, of November 14<sup>th</sup>, on the Creation of the Independent Authority for Fiscal Responsibility.

However, according to AIReF, this Order does not contain the specific provisions required to regulate the endorsement process, which constitutes one of the fundamental tasks of its mandate in accordance with prevailing legislation, nor

does it contain sufficient detail about the information required to perform this function in a suitable and transparent fashion.

**Accordingly, as a live recommendation, AIReF reiterates to the Ministry of Economic Affairs and Digital Transformation:**

- 3. That the endorsement process of the macroeconomic forecasts should be regulated by means of an agreement between the parties.**

Given the existing interrelationship between the macroeconomic outlook and the fiscal scenario, AIReF considers that in order to make the endorsement with greater rigour, it would be necessary to be aware of the revenue and expenditure path that accompanies the Government's macroeconomic outlook and have greater detail on the fiscal measures proposed to be included in the budget. Among these, it would be fundamental to have updated information on the level of execution, in national accounting terms, of the projects associated with the Recovery, Transformation and Resilience Plan (RTRP) and of the assumptions included in this regard in the Government's forecast scenario.

**In this regard, as a live recommendation, AIReF reiterates to the Ministries of Economic Affairs and Digital Transformation and of Finance and Civil Service:**

- 4. That they should provide more information on the measures of a budgetary and fiscal nature included in the macroeconomic scenario with a view to enhancing the rigour of the endorsement process.**

The President of AIReF



Cristina Herrero Sánchez