

Report on Initial Budget of General Government 2025

## **AIReF MAINTAINS ITS MACROECONOMIC AND FISCAL FORECAST, BUT WARNS OF RISK OF ECONOMIC UNCERTAINTY**

- The Independent Authority for Fiscal Responsibility (AIReF) maintains its forecast for real GDP growth for 2025 at 2.5%, due to the strength of domestic demand and the recovery of investment, in contrast to other institutions that have recently revised their estimates upwards
- The new forecasts do not incorporate the impact of the trade war or the effects of increased uncertainty. AIReF has calculated that uncertainty could subtract up to 0.5 points from GDP growth in 2025, if not quickly corrected
- At the fiscal level, AIReF incorporates the impact of the latest measures and year-end 2024, and maintains the forecast for the headline deficit at 2.7% of GDP in 2025, or 2.4% excluding the impact of the DANA
- AIReF estimates that primary expenditure net of revenue measures - the new key variable following the entry into force of the European fiscal framework - will grow by 4.6% in 2025, 0.9 points above the expenditure commitment of the Medium-Term Structural-Fiscal Plan (MTP)
- Debt will stand at 100.8% of GDP in 2025, with a slowdown in the rate of reduction, which will fall from 3.3 points to just 1 point
- AIReF recommends guaranteeing compliance with the national and European expenditure rules, publishing monthly figures for primary expenditure net of revenue measures for the purposes of the European expenditure rule and resuming the monthly publication of eligible expenditure for the national expenditure rule

The Independent Fiscal Responsibility Authority published the Report on the Initial Budget of the General Government (GG) 2025 today, in which it updates its macroeconomic and fiscal forecasts. At the macroeconomic level, AIReF maintains GDP growth of 2.5% in 2025, without incorporating the effect of the trade war or the impact of uncertainty. However, it has carried out a separate exercise in which it estimates that this increased uncertainty could subtract up to 0.5 points from GDP this year, if not corrected quickly. At the fiscal level, AIReF incorporates the impact of the measures approved since the last report, including those aimed at mitigating the effects of the Isolated High Altitude Depression (DANA), as well as information on year-end 2024, and maintains the forecast for the headline deficit of the GG at 2.7% of GDP in 2025. In addition, it estimates that primary expenditure net of revenue measures will grow by 4.6% in 2025, 0.9 points above the commitment made in the MTP.

AIReF maintains its forecast for real GDP growth for 2025 at 2.5%, in contrast to other institutions that have recently revised their estimates upwards. As AIReF explains, the absence of revisions is based on the strength of domestic demand projected for 2025, underpinned by growth in employment, the high rates of savings achieved and the improvement in financing conditions. The scenario also incorporates a recovery in business investment which, in the current context of uncertainty, is subject to downside risks. This scenario does not yet incorporate the impact of the trade war unleashed by the United States, the outcome of which is difficult to predict at present. Nor does it incorporate the negative effects associated with the extraordinary increase in uncertainty about trade policy, although AIReF has carried out an exercise in which it estimates that it could subtract up to 0.5 percentage points from the growth of the Spanish economy as early as 2025 if not corrected quickly.

AIReF warns that the downside risks surrounding this growth scenario are high. In this regard, it explains that the uncertainty is reflected in a fall in the stock markets that could slow the recovery of investment. Furthermore, the increase in tariffs fuels expectations of a recession in the United States and may lead to a fragmentation of trade relations with the consequent loss of efficiency at a global level and a redesign of global value chains. According to AIReF, increased defence spending or a shift in German fiscal policy could offset this scenario, but its effects are not expected until 2026.

In terms of prices, AIReF expects the GDP deflator to slow to 2.2%, reflecting the moderation of energy prices and the absence of wage pressures in a context of increased labour supply associated with immigration. Furthermore, the imposition of tariffs by the United States may pose an upside risk to inflation if China diverts its production to European markets. Nominal GDP would grow by 4.8% in 2025, compared with 6.2% in 2024.

### **Budgetary scenario**

AIReF estimates that by 2025 the growth in GG primary expenditure net of revenue measures will be 4.6%, 0.9 points above the commitment contained in the MTP. After closing 2024 with growth of 3.5%, 1.8 points below the MTP forecast, the cumulative growth of net expenditure from 2025 would stand at 8.3%, 0.9 points below the MTP. Unlike in the case of the fiscal balance, the figure for net expenditure in 2024 has not yet been published, so in both cases this is an AIReF forecast subject to a certain degree of uncertainty as no official methodology has been published at either the national or European level.

AIReF's forecast for the GG headline deficit for 2025 stands at 2.7% of GDP, almost 0.3 points less than forecast in November. Excluding the impact of the DANA, the headline deficit would be 2.4% of GDP. Taking into account AIReF's revenue forecast, meeting the net primary expenditure figure in the MTP (3.7% in 2025) would imply a further reduction in the deficit of 0.3 points, to 2.4% of GDP (2.1% excluding the DANA). Furthermore, compliance with the national expenditure rule would lead to a deficit of 2.3% of GDP and growth in primary expenditure net of revenue measures of 3.5%, in line with the commitment contained in the MTP.

AIReF estimates that the cost of the measures to mitigate the effects of the DANA in 2025 amounts to 0.3 points of GDP. If added to the 0.4 points of impact in 2024, the total cost amounts to almost 0.7 points for the GG Sector. In addition, the Government has

adopted other measures, such as changes to Corporate Income Tax, the approval of the Complementary Tax to guarantee a minimum global level of taxation, the Tax on the Margin of Interest and Commissions that replaces the Tax on Credit Institutions and the repeal of the Energy Tax. Measures to increase spending have also been adopted, such as a pay rise for military personnel and the extension of public transport subsidies. In net terms, the new measures not associated with the DANA imply a reduction in the deficit of just under 0.1 points in 2025.

In addition, changes in the macroeconomic scenario reduce the deficit by 0.1 points due to improved tax collection, while the incorporation of the latest information available leads to a reduction in the deficit of 0.1 points of GDP compared with November.

In this context, AIReF estimates that the deficit in 2025 will fall by 0.5 points of GDP compared with 2024. On the one hand, the progressive withdrawal of measures to alleviate the effects of the price and energy crisis contributes to a reduction of 0.3 points of GDP in the headline deficit in 2025, while other revenue measures adopted represent an additional reduction of 0.1 points of GDP. The expected reduction in non-recurring operations associated with court rulings will also reduce the deficit by another 0.2 points of GDP. In contrast, the evolution of other revenue and expenditure will imply an increase in the headline deficit of 0.2 points.

### **Sub-sectors**

By sub-sector, AIReF estimates a deficit of 2.2% of GDP for Central Government (CG) in 2025, which represents an increase of 0.2 points with respect to the previous forecast. Excluding the DANA, the deficit would be 2% of GDP. Eligible expenditure for the purposes of the national expenditure rule will grow by 5.2% in 2025, excluding DANA spending, 2 points above the reference rate of 3.2%. AIReF also estimates that the contribution of the CG to the European expenditure rule would result in an increase in primary expenditure net of revenue measures of 3.5% with respect to 2024, slightly below the MTP reference rate. Under AIReF's current revenue scenario, compliance with the expenditure rule in 2025 would improve the deficit by 0.2 points to 2% of GDP.

In the case of the Social Security Funds (SSFs), AIReF increases the deficit estimate of the SSFs by 0.1 points to 0.3% of GDP. Primary expenditure net of revenue measures for the purposes of the European expenditure rule would grow by 4.8% in 2025.

In the case of the Autonomous Regions (ARs), eligible expenditure for the purposes of the national expenditure rule will grow by 5.3% in 2025, 2.1 points above the 3.2% limit. Primary expenditure net of revenue measures, calculated in accordance with the European fiscal framework methodology, will also grow by 5.4%. The deficit of the ARs will increase to 0.5% of GDP, or 0.4% excluding the impact of the DANA, 0.1 points less than forecast in the previous report.

In the case of the Local Governments (LGs), AIReF estimates 2.6% growth in eligible expenditure for the purposes of the national expenditure rule, below the reference rate set at 3.2%. For the purposes of the European expenditure rule, net primary expenditure will grow by 3.8%, slightly above the MTP reference rate. LGs will close 2025 with a surplus of 0.3% of GDP, improving the forecast of the previous report by 0.3 points.

The updated AIReF forecasts project a 1-point decrease in the debt-to-GDP ratio this year, bringing it to 100.8% in 2025, with a slowdown in the pace of debt reduction, from

a fall of 3.3 points to just 1 point. This reduction is consistent with the projections presented by the Government in the MTP, as well as by the European Commission and the International Monetary Fund (IMF), which estimate decreases of 1.1 points, 1 point and 1.6 points respectively. AIReF predicts that the ARs will reduce their level of indebtedness by 1.3 points in 2025, reaching 19.8% of GDP, while LGs will improve their net position due to the increase in deposits and decrease in debt.

### **Recommendations**

According to AIReF forecasts, the growth in primary expenditure net of revenue measures for 2025 for the purposes of the European expenditure rule is above the commitment made in the MTP but within the limit of the annual deviation allowed by European regulations. Furthermore, the European Commission has recently communicated the possibility for Member States to request the activation of the national escape clause, in order to exclude the increase in defence spending of up to 1.5% of GDP from the level recorded in 2021. AIReF also identifies a risk of non-compliance with the national expenditure rule for the Central Government, the Autonomous Regions and four Local Governments. In addition, compliance with this rule would lead to compliance with the European expenditure rule.

In this context, AIReF recommends that the Ministry of Finance monitor budgetary execution and establish the coordination mechanisms necessary to guarantee compliance with the national and European expenditure rules by the GG Sector. It also recommends that the Ministry of Finance publish monthly figures for primary expenditure net of revenue measures for the purposes of the European expenditure rule and resume the monthly publication of eligible expenditure for the national expenditure rule. Along the same lines, it recommends that the ARs and five LGs monitor budgetary execution and periodically update the growth estimates for eligible expenditure. Finally, AIReF recommends signing an agreement with the Ministry of Finance for the provision of the information necessary for the preparation of its reports.