Conselho das Finanças Públicas
Portuguese Public Finance Council

Analysis of 2016-2020 Stability Programme

Portuguese Public Finance Council Report

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The Portuguese Public Finance Council is an independent body, set up by article 3 of Law no. 22/2011 of 20 May that introduced the 5th amendment to the Budgetary Framework Law (Law no. 91/2001 of 20 August, republished by Law no. 37/2013 of 14 June).

The decision to set up the Council was taken following the publishing of the final report of the Taskforce to the European Council on economic governance in Europe, and became a reality in October 2010 after agreement was reached between the Socialist Party (PS), in Government, and the Social Democratic Party (PSD). The final version of its Statutes was approved by Law no. 54/2011 of 19 October.

The Council began its work in February 2012 and its mission is to conduct an independent assessment of the consistency, compliance with the stated objectives and the sustainability of public finances, while promoting fiscal transparency, so as to contribute to the quality of democracy and of political economic decisions and so strengthen the State's financial credibility.

This Opinion uses the information available up to 7 May 2016.

In the publications section at www.cfp.pt, a spreadsheet containing all the figures used to build the charts and tables in this Report is available for download.

Contents

List of Charts

List of Tables

List of Boxes

OVERVIEW

This Report complements the Opinion of the Portuguese Public Finance Council (CFP) on the macroeconomic forecasts underlying the Stability Programme 2016-2020 (SP/2016). It looks at the fiscal strategy analysis therein and gauges its consistency with the rules laid down in national and European legislation.

As for the macroeconomic scenario the said Opinion highlighted important risks in two main areas: the assumptions relating to the external framework and the lack of economic grounds to justify the investment and export dynamism that are the mainstay of economic growth over the Programme's time horizon. However, the Opinion admitted that this shortcoming could be overcome through a more detailed link between the macroeconomic scenario and the other economic policy instruments provided for in the Stability Programme itself or in the National Reforms Programme (NRP), both of which relate to the 2016/2020 period.

In regard to the forecasts relating to the external setting, the latest information has confirmed the concerns expressed in the CFP's Opinion. These do not relate only to the arithmetic estimate of external demand based on international forecasts or to the observation of exports, but also to other important matters, such as the structure of Portuguese exported goods which requires consideration to be given not only to the estimated growth in major clients' imports, but also to the more or less intensive mix of Portuguese exports.

This reinforces another concern which is critically important in an economy that has a high degree of external indebtedness and as such is highly vulnerable to the borrowing terms it faces. This gives rise to an asymmetry which should be borne in mind. If the international climate proves to be more favourable than the projections made at the national level, it would improve the terms of access to finance; if the opposite situation arises, the Portuguese economy's performance will once again fall short of expectations. This will lead to harsher terms which could frustrate any recovery strategy until normal borrowing conditions are achieved.

SP/2016 justifies the investment dynamics forecast by the decision to bring forward the implementation of the European Structural and Investment Funds (ESIF) and the need for resident companies to respond to global demand. It is important to note, especially for any demonstration purposes, that the investment leveraged by the ESIF is already reflected in the statistical series used to devise the no-policy-change scenario. The aforesaid uncertainties as to the changes in the external climate are a risk that companies will have to take into account when planning their investment decisions.

As for articulation with other economic policy documents, the medium-term projections still do not include programmes that are sufficiently detailed in terms of the staggering of their respective costs and expected results, which are essential grounds for any monitoring and assessment. It would be important to clarify how the measures designed to enhance domestic demand and to strengthen supply's competitiveness complement each other over time and by nature. In addition, they need to be integrated in an institutional model that ensures they are consistent with the optimal use of resources that a good economic management requires.

In this regard it should be stressed that neither of these programmes (SP and NRP) contains any reference to the implementation of the new Budgetary Framework Law and the General Government Accounting Standardisation System. These are two important shortcomings, precisely because that implementation is the indispensable basis for the aforesaid consistency.

As for fiscal policy, SP/2016 renews the commitment to see the budget deficit and the public debt ration follow a downward path. Thus, a budget surplus of 0.4% of GDP is expected to be achieved in 2020, i.e. a 3.4 p.p. cumulative improvement over the position in 2015 (net of the impact of one-offs). Given that part of this improvement stems from the impact of the expected improvement in the economic environment, the structural adjustment forecast for the same period falls to 1.7 p.p. of GDP. Net of the impact of interest, which is expected to fall, the cumulative improvement in the primary structural balance from 2015 to 2020 is equal to 0.9 p.p. of GDP.

The projected path for the balance would allow the Excessive Deficit Procedure to come to an end in 2016, which will be followed by the preventive arm of the Stability and Growth Pact. However, according to the available information, the programmed structural balance development does not match that laid down in the Stability and Growth Pact, since i) it does not foresee the medium-term objective being achieved within SP/2016's time horizon; ii) it does not ensure compliance with the minimum annual structural adjustment in any of the years covered by the programme. While the path forecast for public debt, which points to a 18.7 p.p. of GDP decrease in the debt ratio from 2015 to 2020, complies with the Stability and Growth Pact rules. The projected economic growth and primary surpluses for this period explain most of that improvement.

Expenditure will be largely responsible for the forecast 3.4 p.p. of GDP decrease in the adjusted budget balance from 2015 to 2020, since the relative weight of revenue in GDP will fall. In absolute terms, at current prices, the cumulative improvement of 6,200 million euros in the adjusted budget balance will be achieved through a 12,700 M€ increase in revenue and a € 6,500 M€ increase in expenditure.

The projected improvement in the balance for the 2016 to 2020 period totals 5,249 M€ (accounting for 2.8 p.p. of GDP). In order to achieve this decrease SB/2016 includes fiscal policy measures. Given the Ministry of Finance's no-policy-change scenario which takes as its starting point the State Budget for 2016 (net of 2015 carry-over effects), SP/2016 incorporates the direct budget impact of a series of policy measures to be taken from 2017 to 2020, that total 2,412 M€ in cumulative terms and at current prices (1.2 p.p. of GDP). These measures are concentrated in 2017 (1,490 M€ or 0.8% of GDP). The improvement in the balance is also based on a significant effect arising from the dynamics inherent in the macro-fiscal no-policy change scenario (1,964 M€, equal to 1.1 p.p. of GDP).

The fiscal policy measures are more concentrated on the expenditure side (1,370 M€ in cumulative terms at current prices). However, in 2017 and 2018 the relative weight of the revenue side policy measures will exceed the net direct effect of the measures relating to expenditure. In cumulative terms, tax measures represent around two-thirds of the sum forecast for the measures relating to revenue as a whole. However, over a half of the additional 704 M€ the MF expects to receive from 2017 to 2020 from indirect taxes has yet to be specified (390 M€).

An important part of the expenditure side measures is dependent upon efficiency gains which, for now, are not sufficiently explained. Less than a third of the volume of savings forecast by the MF on the expenditure side is duly specified, while the remainder (69%), which refers to the expected decrease in intermediate consumption, investment and "other current expenditure" and amounts to 1,775 M€ at current prices, is not. According to the MF the efficiency gains will arise from the on-going Expenditure Review. Thus, the State Budget must define on an annual basis specific measures that will ensure the stated objectives are achieved and the outturn risk is mitigated.

Therefore, the path shown in SP/2016 carries a number of risks, namely:

- The macroeconomic scenario over the entire time horizon, especially in regard to the projected annual growth rates for exports and investment.
- The risks inherent in SB/2016, which was the starting point for the projections. In particular the risks relating to the macroeconomic scenario on which the document is based; the development of social transfers; and the failure to include costs resulting from proposed legislative changes that are in an advanced stage or, alternatively, the defining of compensatory measures that will offset their fiscal impact.
- The asymmetry in the specification of policy measures. According to the CFP classification, while all the measures that will have a negative impact on the budget balance are fully specified, over half the measures that will have a positive impact on the balance (budget consolidation measures) are not properly specified.
- The public debt path is subject to the risks referred to previously and the making of the early loan repayments and the use of Central Government deposits. These debt management decisions to be taken by the MF depend, to a large extent, on factors that are not directly controlled by the MF, such as the interest rates on new issues, the refunding of credit granted and the terms of sale for assets.

As regards the Multiannual Budgetary Planning Framework (MBPF), SP/2016 predicts a significant downwards revision. The correction is justified as it involves stricter limits than those defined in SB/16. However, it is important that the new limits be respected in subsequent periods, in accordance with the law, and put an end to the previous practice of revising all budgetary planning documents without stating the grounds for the changes.

1 INTRODUCTION

This Report analyses the Stability Programme for 2016-2020 pursuant to article 7 of the Portuguese Public Finance Council's (CFP) Statutes, specifically in regard to the preparation of reports on the Stability Programme and other procedures within the European regulatory framework of the Stability and Growth Pact, as well as the Multiannual Budgetary Planning Framework. The CFP's analysis of the macroeconomic scenario underlying this Stability Programme is set out in CFP Opinion nº 2/2016.

This Report is divided into four chapters. The first is the introduction and covers the analysis goals and the document structure. The second chapter provides an assessment of the fiscal adjustment and of compliance with the rules applying to Portugal over the 2016-2020 period. The third chapter analyses whether the no-policy change scenarios and the scenario described in the Stability Programme are consistent bearing in mind the fiscal policy measures reported to the CFP; it reviews public debt developments and identifies risks underlying the projections in the Stability Programme. The fourth and final chapter looks at the Multiannual Budgetary Planning Framework published in the Stability Programme for 2016-2020 (SP/2016).

In order to provide a better evaluation of the fiscal consolidation effort, the general government budget aggregates were adjusted for the impact of temporary measures, one-off measures and other special factors. These adjustments differ from those that underpin the accounts published by the Ministry of Finance in SP/2016.

This report has benefitted from the additional information and clarifications provided by Ministry of Finance (MF) bodies, namely the Planning, Strategy and International Relations Office (GPEARI), the Directorate-General for Budget (DGO), and the Treasury and Public Debt Management Agency (IGCP) and Social Security. The CFP is grateful for all input received.

2 ASSESSMENT OF THE FISCAL ADJUSTMENT AND COMPLIANCE WITH THE RULES FROM 2016 TO 2020

According to SP/2016 from 2017 onwards Portuguese public finances will be assessed under the preventive arm of the Stability and Growth Pact (SGP).[1] The main budget rules applying under these circumstances are recalled here. In addition to maintaining the fiscal balance below 3% of GDP, Portugal will have to ensure the structural balance converges to the MTO which was recently revised to + 0.25% of GDP. Until the MTO is reached, and since Portugal's debt exceeds 60% of GDP, the minimum annual adjustment (annual improvement in the structural balance) must be greater than 0.5 p.p. of GDP, should observable GDP growth be greater than potential output growth and the output gap fall within the range [-1,5, 1,5]. With the end of the Excessive Deficit Procedure (EDP), a three-year transition period begins until the excess debt correction rule of 5% per year kicks in. Over that period (2017-19), Portugal must make sufficient progress to decrease the debt ratio. Progress will be assessed annually, both ex-ante and ex-post, in comparison with the minimum linear structural adjustment (MLSA), that takes the effect of the economic cycle and the benchmark for the debt reduction into consideration.

The figures analysed in this chapter are net of temporary measures, one-off measures and special factors which are identified in Table 7 attached.

2.1 FISCAL BALANCES

SP/2016 restates the commitment to reduce budget deficit and estimates a figure of below 3% of GDP this year and a surplus in 2020. The general government budget deficit should fall from 4.4% in 2015 to 2.2% of GDP in 2016, the correction of the excessive deficit situation being thus achieved one year after the deadline set in Council Recommendation of 14 Julye 2015.[2,3] From 2017 to 2020, the MF predicts an average annual improvement of 0.6 p.p. in the fiscal balance. The final year of the projection is expected to see a surplus of 0.4% of GDP.

Net of the effect of one-offs, the improvement in the fiscal balance should reach 3.4 p.p. of GDP over the five-year period 2016-2020, benefitting from favourable changes in the economy. The said improvement should benefit from a positive contribution of the economic cycle of 1.7 p.p. of GDP (0.6 p.p. of which in 2016) and the ability to produce structural primary surpluses over the projection time frame (a cumulative improvement of 1.1 p.p.), as well as a decrease in the relative weight of public debt interest (down 0.8 p.p.).

[1] The end of the EDP and the exit from the corrective arm of the SGP are dependent on whether the Council of the European Union considers the budget deficit to be sustainable.

[2] The Council of the European Union will shortly conduct an assessment of compliance with the recommendations under article 126 (6) of the Treaty on the Functioning of the European Union.

[3] Net of the effect of the Banif resolution, which accounted for a 1.4% of GDP increase in the deficit in 2015, the decrease would be 0.8 p.p. of GDP in 2016, rather than 2.2 p.p.

Table 1 – Budget indicators

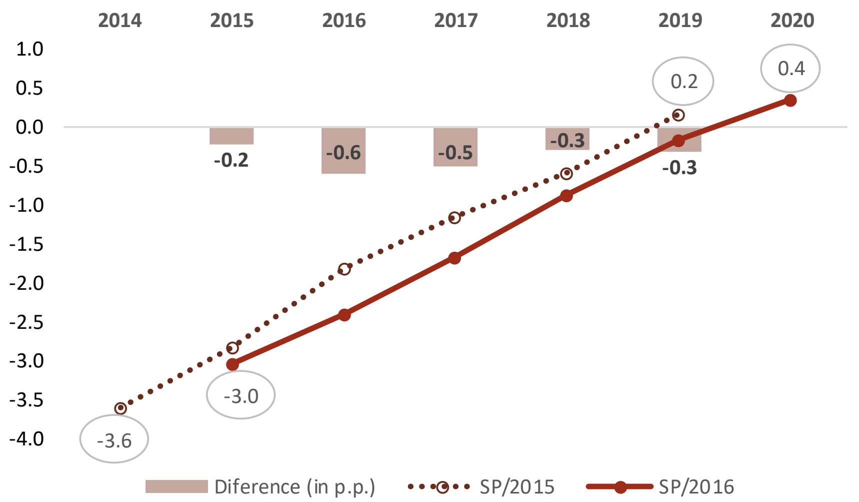
Budget balance:	% of GDP							Change (p.p. of GDP)							
	2014	2015	2016	2017	2018	2019	2020	2015	2016	2017	2018	2019	2020	2010-15	2015-20
Primary	-2.3	0.2	2.2	2.8	3.2	3.8	4.2	2.4	2.1	0.6	0.4	0.6	0.3	8.4	4.0
Actual (headline)	-7.2	-4.4	-2.2	-1.4	-0.9	-0.1	0.4	2.8	2.2	0.8	0.5	0.7	0.5	6.8	4.8
Adjusted of temporary & one-off measures & special factors	-3.6	-3.0	-2.4	-1.7	-0.9	-0.1	0.4	0.6	0.6	0.7	0.8	0.7	0.5	5.5	3.4
Cyclically adjusted	-5.3	-3.2	-1.5	-1.1	-0.8	-0.4	-0.1	2.1	1.7	0.4	0.3	0.4	0.3	7.6	3.0
Structural net of special factors	-1.7	-1.8	-1.7	-1.3	-0.8	-0.4	-0.1	-0.1	0.1	0.4	0.5	0.4	0.3	6.3	1.7
Structural primary net of special factors	3.2	2.8	2.7	2.9	3.3	3.6	3.7	-0.5	-0.1	0.2	0.4	0.3	0.1	8.0	0.9
memo items															
temporary measures & special factors	-3.6	-1.4	0.2	0.3	0.0	0.0	0.0	2.2	1.6	0.0	-0.3	0.0	0.0	1.3	1.4
output gap*	-3.8	-2.4	-1.3	-0.6	-0.1	0.5	1.0	1.4	1.1	0.7	0.6	0.6	0.5	-1.6	3.4
cyclical component	-1.9	-1.2	-0.7	-0.3	0.0	0.3	0.5	0.7	0.6	0.3	0.3	0.3	0.3	-0.8	1.7
interest payments	4.9	4.6	4.4	4.2	4.1	4.0	3.8	-0.3	-0.2	-0.2	-0.1	-0.1	-0.2	1.6	-0.8

Source: INE, MF. CFP calculations. Notes: * as a percentage of potential output. The cyclical component was calculated using the Community method of semi-elasticities based on the MF output gap; (i) the temporary and one-off measures are detailed in Table 7 attached; (ii) due to rounding the changes may not match the differences in the percentage GDP figures.

Compared to SP/2015 the goal of achieving a budget surplus has been postponed for one year and the annual objectives are less demanding. SP/2016 foresees a continuous improvement in the adjusted balance until a 0.4% of GDP surplus is achieved at the end of the projection time frame. A comparison with SP/2015 shows that the annual objectives for the fiscal balance up to 2019 are less demanding, particularly in the first two years, and that difference cannot be attributed solely to the 0.2 p.p. of GDP deviation in 2015 against the earlier forecast.

Chart 1 – Adjusted GG balance projected in the 2015 and 2016 Stability Programmes

(% and p.p. of GDP)



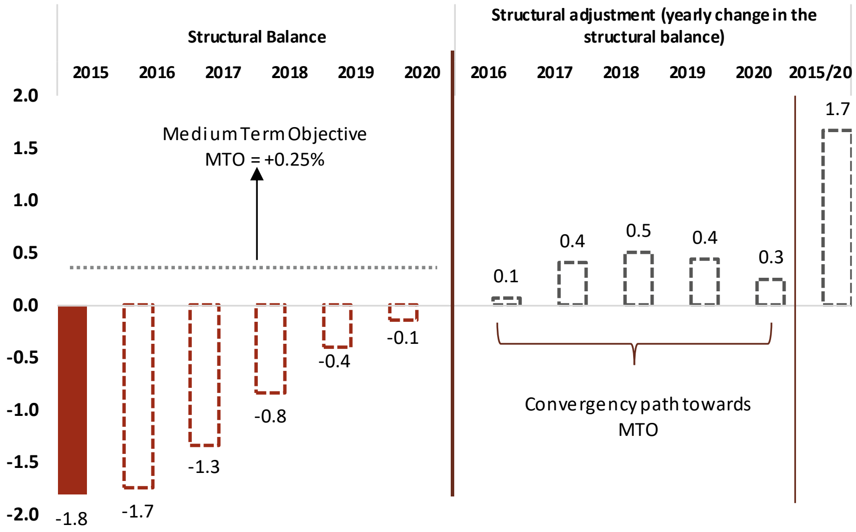
Source: INE and Ministry of Finance. CFP calculations. Note: The temporary and one-off measures are detailed in Table 7 attached.

Having reached a surplus position in 2015, the primary balance should improve up to 2020. Except for the impact of temporary measures, an increase of 2.6 p.p. of GDP in the primary surplus is forecast over the five-year period covered by SP/2016. From 2016 to 2019 an average annual improvement of 0.6 p.p. is projected, followed by 0.3 p.p. in 2020. The achieving of this positive change in the primary balance will determine whether the downward path in the public debt ratio forecast by the MF is reached.

2.2 FISCAL ADJUSTMENT AND FISCAL POLICY STANCE

The structural balance is expected to improve slightly in 2016, following the 0.1 p.p. of GDP deterioration in 2015. Both years should record an unfavourable change in structural primary balance and a decrease in the relative weight of interest. But, whereas in 2015 the favourable change in interest (-0.3 p.p. of GDP) only softens the impact of that deterioration on the structural fiscal balance (-0.5 p.p.), it is estimated that in 2016 the reduced weight of interest (-0.2 p.p.) more than offsets the expected weakening in that balance (-0.1 p.p.). In this way the structural deficit should fall by 0.1 p.p. in 2016 to stand at 1.7% of GDP.

Chart 2 – Compliance with the structural balance rule (% and p.p. of GDP)



Source: INE and Ministry of Finance. CFP calculations. | Note: Structural values are net of the economic cycle and of temporary and one-off measures. (See Table 7 attached).

The budgetary effort underlying SP/2016 will only ensure compliance with the minimal structural adjustment required by the Budgetary Framework Law (BFL) in 2018.[4] Despite the MF projection pointing to a cumulative decrease of 1.7 p.p. of GDP in the structural balance from 2016 to 2020 (except for 2018), the forecast decrease in the nominal deficit relies on an annual improvement in the structural balance that is below the level laid down in the BFL general rule (an annual improvement of 0.5 p.p. of GDP taking into account the position in the economic cycle). Even if the planned path does not ensure full compliance with the national rule, the target of -0.5% of GDP set in the BFL will be achieved in 2019.[5]

[4] Pursuant to Law no. 41/2014 of 10 July.

[5] As follows from the reasoning given in the CFP's Opinion regarding the 8th amendment to the Budgetary Framework Law, of May 2014, the provisions of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG) were not fully transposed into domestic law. In effect the TSCG requires the general government budget to be balanced or in surplus, and that rule shall be deemed to be respected « if the annual structural balance of the general government is at its country-specific medium-term objective as defined in the revised Stability and Growth Pact with a lower limit of a structural deficit of 0.5 % of the gross domestic product at market prices». The wording of article 12-C (3) of the Budgetary Framework Law lays down the «objective of achieving a structural deficit limit of 0.5 %», in other words it matches the medium-term objective to the minimum

The planned development of the structural balance does not match the requirements of the Stability and Growth Pact insomuch as: i) it does not forecast the achieving of the medium-term objective within SP/2016's time horizon, and ii) it does not comply with the minimum annual structural adjustment in any of the years covered by the Programme. The structural adjustment of 0.1 p.p. of GDP forecast for 2016 is below that stated in Council Recommendation of 14 Julye 2015, which set that Portugal should take measures to achieve a fiscal adjustment of 0.6 p.p. of GDP, so as to meet the MTO in 2016 (at that time it was -0.5% of GDP).[6] As for the other years under review, and according to the macroeconomic forecast in SP/2016, the minimum annual structural adjustment under the preventive arm of the SGP is equal to 0.6 p.p. of GDP.[7] In addition SP/2016 does not forecast achieving this minimum adjustment from 2017-2020[8] nor the new figure for the medium-term objective (a structural surplus of 0.25% of GDP). Between the end of 2015 and 2020 the programme predicts an improvement in the structural balance of around 1.7 p.p. of GDP,[9] which implies the adjustment effort will continue beyond the time horizon covered by SP/2016.[10] If the aforesaid minimum annual structural adjustment were achieved, a structural balance would be achieved in 2018 and the MTO in 2019 (see Box 1 for details on the new MTO value).

In 2016 fiscal policy should retain a non-restrictive stance. In 2015 the fiscal policy stance took on an expansionist turn and was pro-cyclical to the extent that the deterioration in the structural primary balance (down 0.5 p.p. of GDP) occurred within an improved economic environment (a positive change in the output gap of 1.4 p.p. of GDP).[11] This year fiscal policy will not be restrictive, bearing in mind that a 0.1 p.p. of GDP decline in the structural primary balance is forecast.

amount defined in the TSCG when, under the terms of the Stability and Growth Pact, that objective may correspond to a balanced structural balance or one in surplus, that is a zero or positive balance.

[6] A possible deviation of 0.5 p.p. of GDP in 2016 could be deemed negligible. In effect in the European Commission's assessment report on the draft budget plan for 2016 it was stated that a deviation in 2016 would not be deemed significant if the structural adjustment was between 0.1 p.p. of GDP and 0.2 p.p. of GDP.

[7] Based on the matrix published in Communication from the Commission COM (2015) 12, of 13 January, in Portugal's case, in the time horizon covered by SP/2016 the minimum adjustment must be over 0.5 p.p. of GDP since the country's public debt exceeds 60% of GDP and the output gap is in the range -1.5% to 1.5% of GDP. The EC has expressed the opinion that an adjustment of over 0.5 p.p. means a minimum adjustment of 0.6 p.p. of GDP.

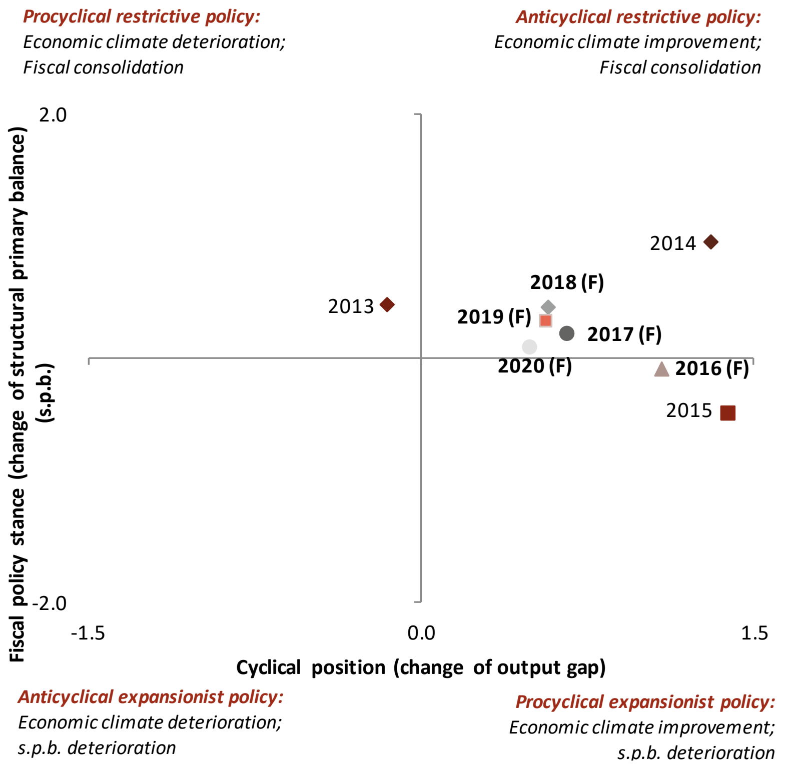
[8] In 2018 the deviation should prove to be negligible since it is estimated that in that year the structural adjustment will be 0.5 p.p. of GDP.

[9] In the five-year period from 2010-2015 the improvement in the structural balance was 6.3 p.p. of GDP.

[10] The SP/2016 report states that the projection time frame already reflects convergence to the new MTO figure.

[11] Due to the uncertainty surrounding the potential output estimate, the normal practice is to use the change in the output gap to identify any economic improvement or deterioration.

Chart 3 – Fiscal policy and cyclical position from 2013-2020



Source: INE and MF. CFP calculations. | Notes: (i) The fiscal policy stance is assessed by the change in the structural primary balance; (ii) The cyclical position of the economy is evaluated by the change in the output gap, which is given by the difference between observed GDP and potential GDP growth rates.

From 2017 onwards the fiscal policy stance will become restrictive and counter cyclical. In fact the MF estimates an improvement in the structural primary balance of 1.0 p.p. of GDP over the four-year period 2017-2020, towards the MTO. Such improvement should arise within the context of an economic recovery, in so far as the output gap is expected to decrease over the projection time horizon and become positive in 2019.[12]

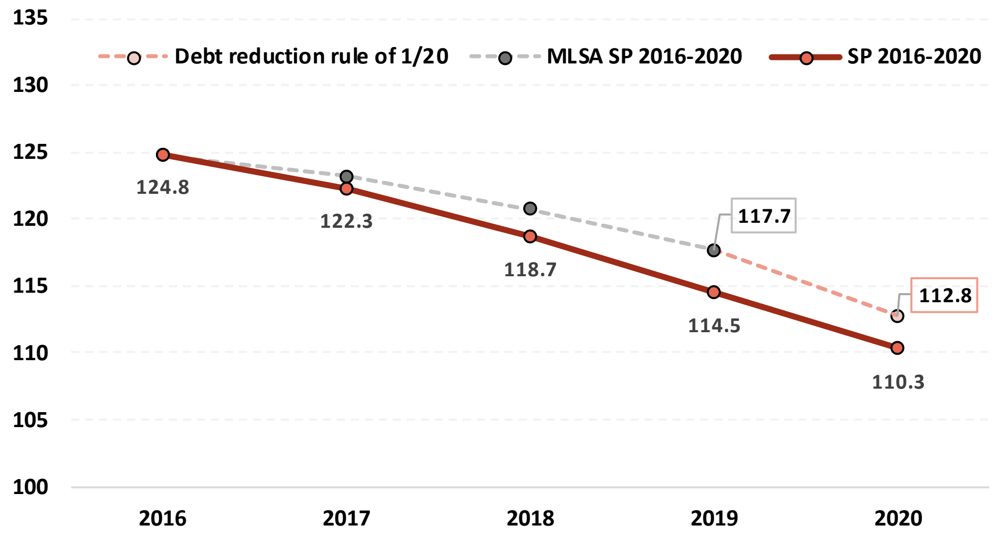
2.3 PUBLIC DEBT

The public debt path shown in SP/2016 surpasses the minimum requirements for public debt reduction applying to Portugal. Assuming that Portugal will exit the EDP on the basis of the general government account figures for 2016, according to the European rules the three following years will be a *transition period*. During this period the debt ratio forecast in SP/2016 complies with the required minimum (*Minimum Linear Structural Adjustment* — MLSA). From the beginning of 2020 the debt reduction rule calling for a one-twentieth decrease per year shall apply, and that is also met in the MF projections. When

[12] A positive output gap means that the level of output generated by the economy exceeds its potential. For further details on the output gap and potential output concepts see Glossary of Public Finance Terms.

ascertaining the MLSA,[13] the CFP calculations were based on the structural balance for 2016 and the nominal GDP path forecast in SP/2016, as well as on the assumption of nominal growth in the economy and in the stock-flow adjustments in 2021 being equal to the MF forecast for 2020.[14,15]

Chart 4 – Public debt developments (as % of GDP)



Source: MF. CFP calculations.

During the transition period the debt ratio projected in SP/2016 is always lower than in the MLSA. The table below compares the debt developments forecast in SP/2016 with the debt which would arise if the minimum linear structural adjustment were made over the transition period. In line with the MLSA, at the end of the transition period (i.e. 2019) the debt ratio to be achieved would be less than 117.7% of GDP. The SP/2016 projection for the debt path produces a lower figure (114.5% of GDP), ensuring compliance with the rules applying to Portugal during the 2017-2019 transition period.

[13] During the three-year transition period, up to the application of the rule calling for an annual 5% decrease in the debt differential, Member States are required to reduce public debt so as to meet at least one of three criteria: retrospective, prospective and cyclically-adjusted. All these criteria assume a linear adjustment over three years. The magnitude of the required adjustment is proportional to the deviation from the estimated debt path in the absence of the adjustment relating to the benchmark (that is, maintaining the structural balance at the same level than the year the excessive deficit procedure was closed). For further details on calculating the MLSA see: Analysis of the 2014-2018 Fiscal Strategy Document.

[14] This result complies with the least restrictive criterion under these conditions: the prospective criterion.

[15] The MF forecasts indicate that the structural balance will be – 0.3% and debt will stand at 114.5% of GDP in 2019.

Table 2 – Compliance with public debt rule (% of GDP)

Year	SP/2016 Public Debt	MLSA Benchmark for Debt
2016	124.8	124.8
2017	122.3	123.2
2018	118.7	120.7
2019	114.5	117.7
2020	110.3	114.9

Source: MF. CFP calculations.

Box 1 – MTO: revisions, convergence path and flexibility

MTO: revisions and convergence path

The Stability and Growth Pact (SGP) was adopted in 1997 to clarify Member States duty to avoid excessive budget deficits, as laid down in article 126 of the current Treaty on the Functioning of the European Union. It is based on «the objective of sound government finances as a means of strengthening the conditions for price stability and for strong sustainable growth conducive to employment creation». In the original wording the Member States agreed to meet the «medium-term objective of budgetary positions of close to balance or in surplus »[1] This wording is based on the notion that maintaining budgetary positions of close to balance or in surplus will allow Member States to deal with normal cyclical fluctuations while keeping the budget deficit within the 3% of GDP reference value. In other words, the SGP was based on the premise that a balanced or in surplus budget would provide sufficient fiscal leeway to counteract the normal cyclical fluctuations without incurring an excessive deficit as a result.[2]

The countries' practical commitment to this objective was limited and demonstrated that convergence towards this objective was difficult to monitor. Varied criticism built up as to the excessively simplistic nature of the SGP initial approach, which did not take sufficient account of economic cycle conditions. Therefore, under the 2005 revision and later the 2011 one, the Medium-term Objective and the respective convergence path became based on the structural balance concept.

Article 2-A of the current wording of Regulation (EC) nº 1466/97[3] states that each Member State shall have a differentiated Medium-term Objective (MTO) for its specific public finances that may diverge from the requirement for a budgetary position close to balance or in surplus. As is also expressed in the respective Code of Good Practice, **the MTO pursues a triple aim**:

i. **Providing a safety margin with respect to the 3% of GDP deficit limit.** That safety margin takes into account past output volatility and the budgetary sensitivity to output fluctuations which gives rise to a "minimum reference value". In the Portuguese case this value is currently 1.6% of GDP (See *Vade Mecum on the Stability and Growth Pact*).
ii. **Ensuring rapid progress towards public finance sustainability.** The MTO calculation shall ensure convergence of the debt ratio on the 60% of GDP reference value taking into account the economic and budgetary impact of an ageing population. That requires taking into consideration the fiscal balance that stabilises the debt at the 60% of GDP reference value, calling for an extra effort from those countries that find themselves over the limit, as well as a pre-funding adjustment required to respond to the current value (actuarial concept) of the future increase in public expenditure relating to ageing.
iii. **Taking (i) and (ii) into account, allowing room for budgetary manoeuvre in particular taking into account the needs for public investment.**

The MTO must be set within the variation interval between -1% of GDP of the structural balance and a structural balance in a balanced position or in surplus. The lower limit is -0.5% of GDP for States which signed the Treaty on Stability, Coordination and Governance (TSCG).[4] The Signatories to that Treaty, including Portugal, committed themselves to ensuring "a rapid convergence towards the respective medium-term objectives."

The medium-term budgetary objectives are revised every three years.[5] The revision generally takes place following publication of the European Commission's Sustainability Report which, in turn, is based on the latest update of budgetary costs relating to ageing. The MTO calculation formula, adopted under the SGP Code of Good Practice[6] represents the said aims and determines the minimum MTO value. It requires calculating the greater of three possible lower limits, namely:

$$\mathrm{MTO}^{\min} = \max\left\{\mathrm{MTO}^{\mathrm{VMR}}, \mathrm{MTO}^{\mathrm{ILD}}, \mathrm{MTO}_{\mathrm{Euro/TECG}}\right\}$$

Where the first term is the minimum reference value; the second, the sustainability component or rapid progress towards public finance sustainability; and the third and final term is the aforesaid general limit of -1% of GDP (-0.5% for TECG signatories). The second component which takes into account the implicit liabilities and debt (ILD) is calculated as follows:

$$\mathrm{MTO}^{\mathrm{ILD}} = \text{Balance debt-stabilizing}_{(60\%\text{of GDP})} + \alpha * \text{Ageing costs} + \text{Effort debt-reduction}$$

Where: the first term is the budgetary balance that would stabilise the debt ratio at 60% of GDP [equal to output between 60% and the nominal growth forecast up to 2060 as calculated by the Ageing Working Group (AWG)]; the second term is the budgetary adjustment that would cover an agreed fraction of the present value of the increase in age-related expenditure, when α = 33%; and the third term represents a supplementary debt-reduction effort specific to countries with a gross debt ratio above 60% of GDP. This last term follows a linear function that requires a supplementary effort of 0.2% of GDP whenever debt reaches 60% of GDP and a supplementary effort of 1.4% of GDP whenever the ratio reaches 110% of GDP (this effort is equal to the outcome of the following operation: 0.024*Debt – 1.24).

In 2016 the MTO was updated according to the regular three-yearly revision. In the Portuguese case, since the previous MTO update there was an increase in the public debt ratio, which led to the minimum MTO value being revised upwards so as to ensure rapid progress towards public finance sustainability. As a result the MTO defined by the Portuguese Government in this Stability Programme is more demanding than previous figures. Thus the MTO went from a structural budgetary deficit of 0.5% of GDP to a structural budgetary surplus of 0.25% of GDP.

Flexibility within SGP rules

The SGP states that each Member State shall implement a minimum annual adjustment until the respective MTO is achieved. Generally this minimum adjustment corresponds to an annual improvement in the structural balance of 0.5 p.p. of GDP, and the effort is modulated according to the economic cycle conditions, the debt ratio and the sustainability risk. Once the MTO is achieved, the quantification of the structural balance continues to be important to the monitoring of the public finance position. In this way whenever a deviation from the MTO (or compared to the respective convergence path) is deemed significant the correction mechanism is triggered.

The European Commission recently introduced the possibility of the SGP rules being interpreted in a more flexible manner as part of a strategy to boost employment and growth. Communication of 13 January 2015 provided guidelines for making the best use of the flexibility within the existing rules of the SGP, without bringing into question compliance with the said rules. That interpretative Communication was the basis for the "*Commonly agreed position on Flexibility within the Stability and Growth Pact*", which was formally endorsed by ECOFIN on 12 February 2016.

The Commission has designed a matrix that specifies the annual fiscal adjustment towards the MTO required under the preventive arm of the Pact taking into account the economic conditions and the sustainability of Member States' public finances, and which clarifies how the annual effort should be modulated. Therefore the matrix calls for a greater fiscal effort from countries whose debt ratio is over 60% of GDP and which are experiencing more favourable economic times, and calls for a smaller effort from countries with a debt ratio below 60% of GDP and experiencing less favourable economic times. The economic conditions are measured by the real GDP growth rate and the output gap.[7]

According to the path foreseen in SP/2016, Portugal should cease to fall under the preventive arm from 2017 onwards. Given the macroeconomic scenario in SP/2016, the matrix calls for an annual minimum adjustment of 0.6 p.p. of GDP, since the country has a public debt ratio of over 60% and because it is forecast that over the time frame covered by SP/2016 the output gap will be in the interval from -1.5% of GDP and 1.5% of GDP which corresponds to "normal times".

According to the commonly agreed position the European Commission may also evaluate Member States' compliance with the rules in a more flexible manner, bearing in mind their right to invoke safeguard clauses. The flexibility consists of authorising a temporary deviation from the MTO if it has been achieved previously or of granting additional time to achieve the MTO, thereby permitting a temporary deviation from the convergence path. The right to invoke the said clauses is dependent upon the following requirements:

- The Member State must be under the preventive arm of the SGP, that is to say, the Excessive Deficit Procedure must already be closed;
- A suitable safety margin is continuously preserved so that the temporary deviation from the MTO or the agreed fiscal adjustment path does not lead to an excess over the 3% of GDP reference value for the deficit. Therefore the

structural balance must never be less than the minimum reference value (which in Portugal's case is equal to 1.6 % of GDP, as mentioned earlier);

- The MTO must be reached within the four-year horizon of the Stability Programme of the year in which the clause is activated, in other words, up to *t*+4; the temporary deviation from the MTO convergence path may not last for more than three years;
- The deviation from the MTO in the year in which the clause is activated (year *t*) may not exceed 1.5% of GDP;
- The temporary deviation may not exceed 0.5% of GDP per year (except when it stems from structural reforms to the pension system that introduce a fully-funded pillar);
- The cumulative temporary deviation which may be permitted under the structural reform and investment clauses (explained below) may not exceed 0.75% of GDP;
- The implementation of the structural reform (or investment) clause is restricted to once per period of adjustment leading to the MTO. This means that a Member State may only invoke the clause a second time after the respective MTO has been met.

Whenever a Member State fulfils these requirements it may invoke the following safeguard clauses:

i) Structural reforms

Pursuant to the current rules of the Pact, Member States covered by the preventive arm of the SGP which implement important structural reforms are allowed to temporarily depart from the MTO convergence path, due to the short-term costs of introducing the reforms. However, that deviation is only allowed under the following conditions (in addition to those referred to above): the reforms in question must have a major positive impact (such as a reform of the pension system), must be fully implemented, and must have long-term positive budgetary effects, namely by strengthening the sustainability of public finances through an increase in revenue or potential output, or a decrease in expenditure. Note that in order to benefit from the structural reforms clause, the Member State has to present a comprehensive and detailed plan of the structural reforms to be implemented in the medium-term.

ii) Investment

Under the preventive arm of the Pact some investments may be deemed equivalent to major structural reforms if it is shown that they are key to achieving and implementing the said reforms. To a large extent eligible investments should benefit from Community co-financing. It should be shown that the investments have a significant net impact on potential growth and public finance sustainability. Therefore, in certain conditions, they may justify a temporary deviation of up to 0.5% of GDP compared to the MTO convergence path. Such a deviation will only be allowed under the following conditions (in addition to those referred to above): when GDP growth is negative or GDP remains well below its potential level (an output gap that is more negative than -1.5% of GDP) and national public investment cannot be replaced by expenditure co-financed by Community funds. Eligible investments are national expenditure on projects co-funded by the EU under the structural and cohesion policy, Trans-European Networks and Connecting Europe Facility, as well as national co-financing of projects also co-financed by the European Strategic Investments Fund (known as the "Juncker Plan").

Following the recent wave of migration, discussions are underway about the introduction of a new safeguard clause relating to the cost of refugee support policies. Whilst the President of the European Commission has recognised that this matter may constitute an "exceptional event", the respective decision will have to be taken on a case by case basis, and countries will have to show that their public accounts were effectively affected by the cost associated with the application of exceptional refugee support policies.

Lastly, under the preventive arm of the Pact the rules do not include detailed provisions on the possibility of the structural reforms or the investment being taken into account at the time it is assessed whether or not the Member State took effective measures regarding the correction of an excessive deficit situation. Even then, the Commission assesses a number of factors, including the outcome of structural reforms in the context of the European Semester, when considering the multiannual path for correcting an excessive deficit situation. An excess deficit versus the reference limit may be deemed exceptional if it arises due to circumstances beyond the Member State's control and has a significant impact on the public finance position or when it is the result of a serious economic recession. If the Member State has taken effective measures and carried out the structural fiscal effort recommended by the Council, it may benefit from a supplementary period in which to correct the nominal excessive deficit without facing financial penalties.

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[1] As per recital nº 2 of Council Regulation (EC) nº 1466/97 of 7 July 1997.

[2] A serious economic recession, then defined as an annual fall of at least 2% of real GDP, could justify the exceptional exceeding of the 3% of GDP limit.

[3] As amended by Regulation (EC) nº 1175/2011 of 16 November.

[4] However, when the public debt ratio is significantly below 60% of GDP and the risks to long-term sustainability of public finances are small, the MTO limit may be a structural deficit of, at most, 1.0% of GDP. The TSCG was signed in Brussels on 2 March 2012 and ratified by Portugal by way of Resolution of the parliament no. 84/2012 (only in Portuguese), approved on 13 April and published on 3 July 2012 (the legislative process may be consulted at the webpage draft resolution no. 30/XII).

[5] Outside of this regular interval, «A Member State's medium-term budgetary objective may be further revised in the event of the implementation of a structural reform with a major impact on the sustainability of public finances». See article 2-A of Regulation (EC) nº 1466/97, as amended by Council Regulation (EC) no. 1055/2005 of 27 June 2005 and by Regulation (EU) no. 1175/2011 of the European Parliament and Council of 16 November.

[6] *Guidelines on the format and content of Stability and Convergence Programmes*, 3 September 2012.

[7] The matrix can be found on page 25 of *Commonly agreed position on Flexibility in the Stability and Growth Pact.*

3 FISCAL PROJECTIONS

The no-policy-change scenario is a starting point for designing a medium-term public finance strategy and so it is fundamental aspect of the Stability Programme. In SP/2016 the MF estimates economic activity will make a positive contribution to the GG account over the projection entire time horizon, in addition to the direct impact of a series of policy measures, which at the end of the time frame of the Programme will total 2,412 M€. However, failure to specify an important part of the fiscal consolidation measures puts the achievement of the published projections at risk. As for the change in public debt, SP/2016 forecasts its GDP ratio to continue along a downward path up to 2020.

3.1 GENERAL GOVERNMENT ACCOUNT

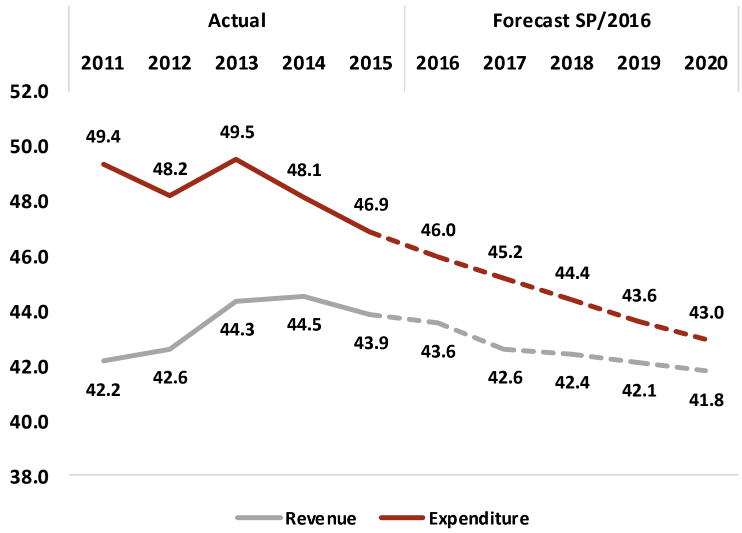
3.1.1 No-policy-change scenario

The MF budget forecasts in SP/2016 take as their reference a no-policy-change scenario.[16] The analysis of revenue and expenditure forecasts incorporated in the no-policy-change scenario is essential to assess the effect of the policy measures contained in the Programme. Since the impacts of the measures are considered differently against the baseline scenario, the SP macro-fiscal forecasts reflect developments in the baseline scenario as well as the impact the new fiscal measures that the MF plans to introduce will have on it. Therefore, any forecasting errors in the baseline scenario are fully transmitted to the macro-fiscal forecast scenario, thus contributing to the reliability of the final result, along with the assessment of the impacts of the new measures.

The direct effect of macroeconomic variables on the no-policy-change scenario can explain the improvement of 1.1 p.p. of GDP (1,964 M€ at current prices) in the fiscal balance up to 2020. Excluding the impact of new measures, the MF predicts that from 2016 to 2020 the expenditure ratio will record a sharper decrease than the revenue ratio. The decline in the revenue and expenditure to GDP ratios would correspond to the projected change in nominal GDP, since both the revenue and expenditure aggregates show nominal increases over the course of the projection time frame. On the revenue side the MF forecasts a fall of 2.1 p.p. of GDP, which is mainly explained by tax revenue (1.5 p.p. of GDP). Except for capital expenditure, all expenditure items would see growth rates greater than or equal to those projected for nominal GDP, and so would contribute to the projected decrease in the relative weight of total expenditure in GDP (down 3.9 p.p.).

[16] The no-policy-change scenario includes the measures of a permanent nature that were in force at the time it was drawn up. It includes the impact of measures impacting after 2016, for which legislation has already been passed.

Chart 5 – Adjusted revenue and expenditure forecasts under a no-policy-change scenario (% of GDP)



Source: INE and MF. CFP calculations. | Note: Revenue and expenditure figures are adjusted for temporary measures, one-off measures and special factors.

Over 80% of the increase in projected revenue can be explained by tax revenue and social contributions revenue, which are dependent upon macroeconomic developments. The increase in tax revenue forecast by the MF will be greater as regards indirect taxes, although growth will be lower than in private consumption. The projection for direct tax revenue is in line with the wage bill and economic activity, except in 2018, where the expected large change is not explained by the respective macroeconomic situation. In this scenario social contributions grow more than the wage bill over the entire period under review, reflecting a variable elasticity over the years (see the Table below). In 2019 also the projected change in this item does not appear to be duly explained by the no-policy-change macroeconomic scenario submitted to the CFP.

Table 3 – Elasticities underlying the SP/2016 projections under a no-policy-change scenario (%)

	2015	2016	2017	2018	2019	2020
Indirect taxes/private consumption elasticity	1.8	1.8	0.2	0.9	0.8	0.8
Direct taxes/compensation of employees elasticity	2.1	-0.7	0.2	1.3	0.8	0.8
Actual social contributions/compensation of employees elasticity	3.4	1.5	1.1	1.3	1.5	1.3
Indirect taxes/GDP elasticity	1.8	1.7	0.2	0.9	0.8	0.8
Direct taxes/GDP elasticity	0.7	-0.5	0.2	1.0	0.7	0.7
Actual social contributions/GDP elasticity	1.2	1.2	0.9	1.0	1.2	1.1

Source: MF and INE. CFP calculations. | Notes: Revenue from taxes and actual social contributions has not been adjusted for policy measures.

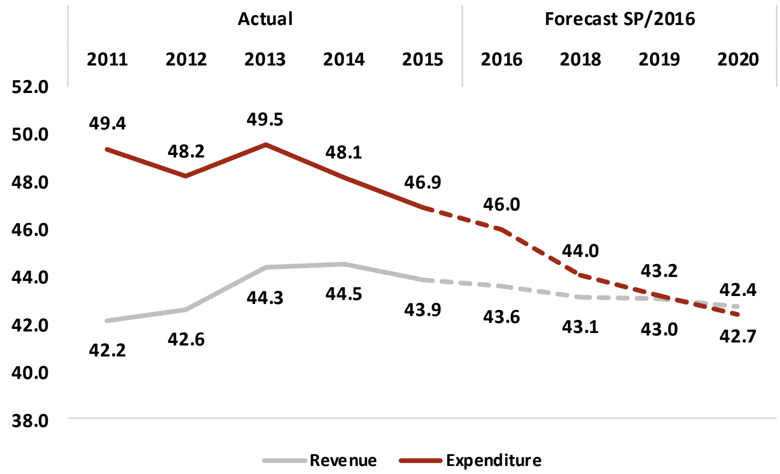
The fall in the expenditure ratio does not lead to a nominal decrease in any of the expenditure items, except subsidies, but rather growth below that of nominal GDP. The nominal increase in expenditure from 2016 to 2020 will essentially result from the projected development in social transfers, expenditure on intermediate consumption and capital expenditure. In the case of social transfers, and according to the MF, the change reflects an improvement in labour market conditions, as well as the restoring of the social transfers indexation rule.[17] However, projected expenditure on social transfers may be underestimated over the course of the projection time frame, taking into account the starting point in 2016. Note that in its analysis of SB/2016 the CFP highlighted the fact that estimated expenditure on social transfers foresaw very small increases compared to 2015, and no measures likely to explain that restraint were provided.[18]

3.1.2 Scenario with measures

3.1.2.1 Revenue and expenditure

Taking into account the effects of the policy measures, SP/2016 points to the relative weight of adjusted public expenditure in GDP being less than adjusted revenue at the end of the projection time frame. The gradual convergence of these two t aggregates over the 2015 to 2020 period will be achieved by a nominal growth in GDP above the nominal increases in revenue and expenditure forecast for each year. The smaller difference between the weights of these (adjusted) aggregates in GDP that result in part from the fiscal consolidation measures, will therefore lead to a balanced position. However, according to the MF projection the change in the relative weight of revenue and expenditure in GDP will be less steep than the one forecast in SP/2015 for the years 2015 to 2019.[19]

Chart 6 – Adjusted revenue and expenditure forecasts, with measures (as % of GDP)



Source: INE and MF. CFP calculations. | Note: The figures are net of temporary and one-off measures and special factors. See Table 7 attached.

From the end of 2015 to 2020, a cumulative decrease in the weight of revenue in GDP (1.1 p.p.) is projected. The forecasts included in SP/2016 point to an annual decrease in the relative weight of this aggregate's from 43.9% of GDP in 2015 to 42.7% in 2020. This change is fully explained by current revenue (-1.3 p.p.), especially tax and social contributions revenue

[17] Law no. 53-B/2006 of 20 December.

[18] For 2016 the MF forecasts an increase in general government spending on social transfers other than in kind of just 78 M€, while combined CGA and Social Security expenditure should increase by around 513 M€ (CGA 47 M€ and Social Security 466 M€). A deviation in this item in 2016 would have significant repercussions for expenditure over the projection entire time horizon.

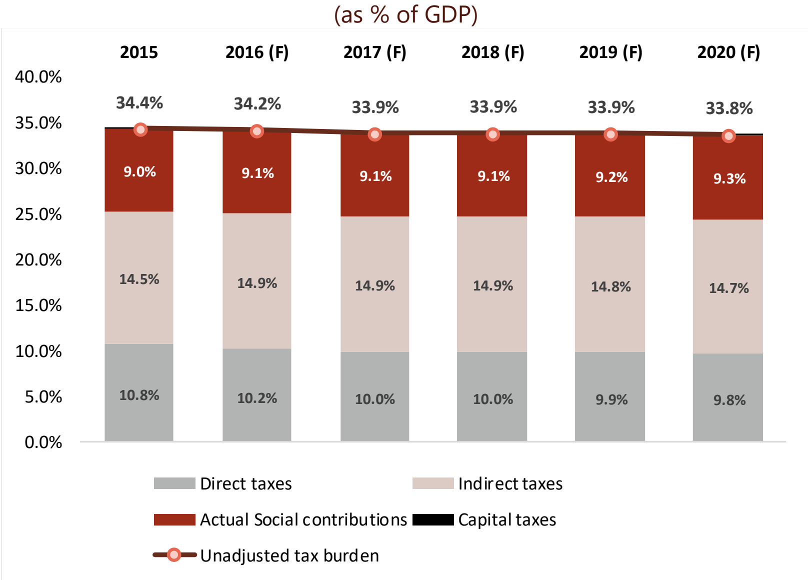
[19] In SP/2015 the expected decrease in expenditure and in revenue was 4.8 p.p. of GDP and 1.8 p.p. of GDP, respectively. These levels compare with the decreases included in SP/2016 of 3.7 p.p. and 0.8 p.p., respectively.

which accounts for 80% of the decrease. To soften the fall the MF foresees a positive change in capital revenue (+0.2 p.p.) which reflects the larger volume of European structural funds intended for public investment.

The SP/2016 projection implies a decrease in the tax burden up to 2020. From the end of 2015 the MF foresees a decline of 0.6 p.p. of GDP in the (unadjusted) tax burden, which could reach 33.8% in 2020. This decline, which will not occur in 2018, is expected to arise in all the remaining years of the projection and be most marked in 2017 (-0.3 p.p.). Direct taxes will contribute fully to the decrease (-1.1 p.p.) mainly as a result of the abolishing of the PIT surcharge. This decrease will be partially offset, on the one hand, by the increase in actual social contributions (+0.3 p.p. of GDP) brought about by the change in the wage bill and the level of employment and, on the other hand, by indirect taxes which reflect not only the growth in VAT (due to the increase in private consumption) and ISP (in line with the progress of domestic demand), but also the effect of so far unspecified tax measures.

Chart 7 – Unadjusted tax burden development

(as % of GDP)



Source: MF. CFP calculations.

On the expenditure side, the MF projections point to a decrease in the relative weight of (adjusted) public expenditure in GDP greater than in the last six years. The MF estimates nominal growth in GDP that more than doubles the nominal increase forecast for expenditure and justifies the fall in the weight of public expenditure in GDP. Therefore, even if in nominal terms the MF projection does not point to a decrease in the level of that aggregate,[20] (adjusted) public expenditure as a percentage of GDP will fall by 4.5 p.p. of GDP up to 2020. The largest decrease (-1.1 p.p. of GDP) will be experienced in 2017 and the MF forecasts that the public expenditure to GDP ratio in 2020 will be at the level recorded in 1997 (42.4% of GDP).

[20] In adjusted terms the nominal cumulative increase in public expenditure forecast in SP/2016 from 2015 to 2019 is 4,993 M€, of which 11 M€ relates to interest charges. Compared to the same period in SP/2015, these figures represent an increase in spending of 3,747 M€ and a decrease in interest of 1,524 M€.

From 2016 to 2020 current primary expenditure will be the major contributor to the decrease in the public expenditure to GDP ratio. All current primary expenditure items will contribute to this decrease. In cumulative terms spending on social transfers (-1.5 p.p. of GDP) and compensation of employees (-1.3 p.p.) will account for around two-thirds of the forecast decrease, while intermediate consumption (-0.5 p.p.) and "other current expenditure" (- 0.2 p.p.) explain the remainder. In annual terms the largest savings will be achieved by social transfers and compensation of employees (on average -0.3 p.p. of GDP per year each), and the latter will total 10% of GDP in 2020, the lowest level since 1995.

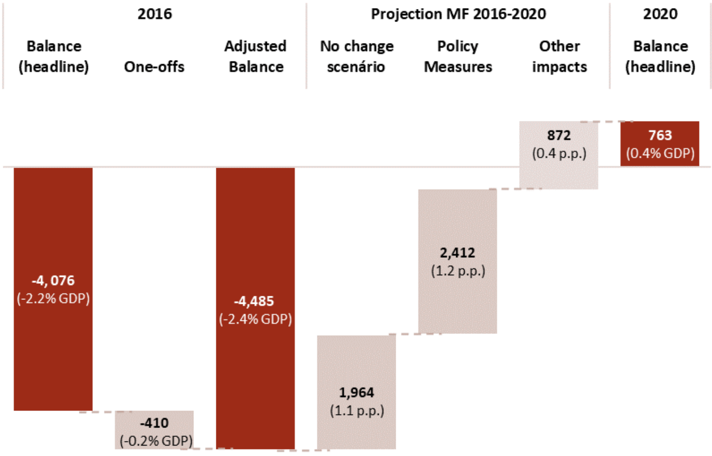
Capital expenditure should not hinder the decrease in public expenditure while expenditure on interest should make a favourable contribution. Although the proposed measures encourage use of European Structural and Investment Funds up to 2020, the MF projection suggests the relative weight of general government investment in GDP will be similar to that recorded in 2015 (2.1%). Therefore, the forecast development in capital expenditure should not affect public spending restraint. Over the projection time frame the MF forecasts a reduction in interest (0.8 p.p. of GDP) that benefits the fiscal imbalance correction. This favourable contribution is contingent on the nominal decrease in public debt (volume effect) resulting from the early repayment of IMF loans which in turn is dependent upon the yield from the sale of financial assets and the repayment of loans made by general government.

3.1.2.2 Fiscal policy measures

The direct effect of policy measures only accounts for around half of the forecast improvement in the fiscal balance from 2016 to 2020. The new policy measures that will be introduced between 2017 and 2020 are listed in Table 8 attached. The achievement of the adjusted overall balance laid down in SP/2016 is dependent upon macroeconomic developments and their impact on the budget variables, as well as on the impact of the new policy measures set out in the Programme. As stated previously, the direct effect of the macroeconomic variables and the pressures upon the budget variables in a no-policy-change scenario accounts for an improvement of 1,964 M€.[21] The policy measures should directly explain an improvement of 2,412 M€, while other effects (that include the effects brought about by the measures on the macroeconomic scenario) explain the remainder (872 M€).

[21] The change in the balance under the no-policy-change scenario reflects not only the improvement in the budget variables linked to the economic cycle, but also the effect of associated fiscal pressures, particularly the developments in Public-Private Partnerships and social transfers.

Chart 8 – From the 2016 deficit to the 2020 surplus (M€)



Source: MF. CFP calculations. | Note: The "No-change Scenario" effect includes the direct effect of the macroeconomic variables and the pressures on the budget variables. "Other impacts" will include secondary effects on the measures. Due to rounding the totals may not necessarily match the sum of the percentage GDP figures.

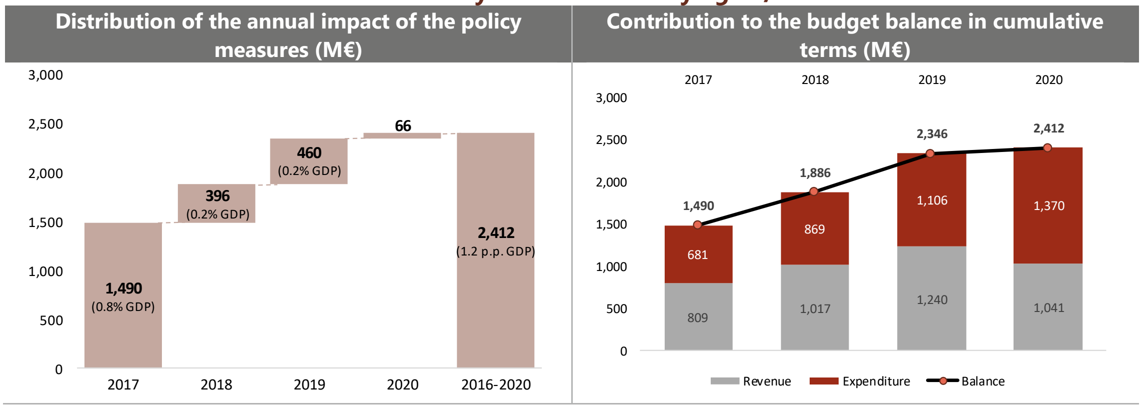
The policy measures forecast for expenditure make the largest contribution to the improvement in the fiscal balance. From 2017 to 2020 the estimated overall net impact of these measures will be 1,370 M€ at current prices. Total measures forecast on the expenditure side amount to 3,752 M€, of which 2,561 M€ come from consolidation measures on the expenditure side, while 1,191 M€ correspond to expenditure growth measures.[22] Most of the contribution of expenditure to consolidation comes from savings in intermediate consumption (1,100 M€) and "other current expenditure" (540 M€), which accommodate the expected increases in compensation of employees (600 M€). For details see Table 8 attached.

Tax measures account for around two-thirds of the sum forecast for revenue as a whole. Over half of the additional 704 M€ that the MF expects to collect from indirect taxes from 2017 to 2020[23] is unspecified (390 M€). The remainder (337 M€) comes from measures aimed at stimulating use of European Structural and Investment Funds, whose impact on capital revenue will be largely directed towards supporting the increase in public investment (See Table 8 attached).

[22] In the policy measure package provided by the MF the cumulative effect of the measures that cause public expenditure to rise between 2017 and 2020 compared to the no-policy-change scenario correspond to: (i) civil service salary measures – productivity bonuses worth 600 M€; (ii) wage complements to low-income families worth 200 M€ and capital expenditure totalling 391 M€, in particular investment resorting to structural funds.

[23] The cumulative total of 704 M€ includes 314 M€ of tax revenue to be obtained by retaining the extraordinary contributions on the banking and energy sectors and on the pharmaceutical industry that are in force in 2016.

Chart 9 – Policy measures underlying SP/2016

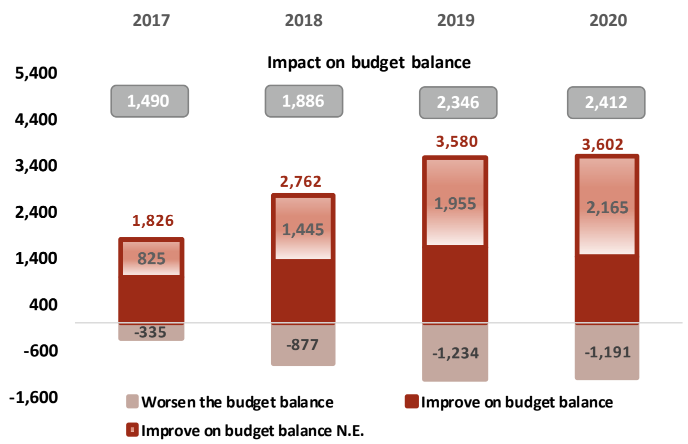


Source: MF. CFP calculations. | Note: The impact of the measures is quantified and classified in Table 8 attached. In the right hand panel the bars represent contributions to the improvement in the balance, both revenue and expenditure.

Despite the larger contribution of measures on the expenditure side, an important part of them is dependent on efficiency gains whose outcome is uncertain. Less than a third of the volume of savings forecast by the MF (31%) is specified in precise terms.[24] The remainder, over two-thirds (69%), refers to the expected decrease in spending on intermediate consumption, investment and "other current expenditure", totalling 1,775 M€, and is unspecified.

Chart 10 – Cumulative effect of specified and unspecified policy measures

(M€ at current prices)



Source: MF and CFP calculations. | Note: N. E. – Unspecified. For more details on the unspecified measures see Table 8 attached.

The published strategy requires the State Budget to define concrete yearly measures that will ensure the stated objectives are reached and the balance follows the path described in SP/2016. The expected cumulative impact of the unspecified measures varies from 825 M€ in 2017 to 2,165 M€ in 2020, of which two-thirds are concentrated in 2017 and 2018. The credibility of the published strategy implies that the annual budgetary planning documents provide the necessary detail and quantification of the measures concerned. The

[24] The measures refer to the savings to be obtained from (i) interest charges (349 M€), (ii) the application of the civil service personnel rule (277 M€) and (iii) social transfers, particularly in terms of greater control and monitoring of the allocations of other social transfers and the plan to fight fraud and evasion (150 M€).

inadequate specification of the policy measures on which the fiscal strategies and the annual budgets are based have been a recurring failure in Portuguese fiscal policy.

3.1.3 Consistency between scenarios with and without policy measures

The macroeconomic developments and the measures published do not seem sufficient to sustain the improvement presented by the MF at the end of the projection time frame. A comparison of the MF's no-policy-change scenario with the direct cumulative impact of the fiscal policy measures shows that the remaining difference[25] is more concentrated on the revenue side. However, in 2020 that difference is large on both the revenue and expenditure sides, contributing to the decrease in the deficit of 0.4 p.p. of GDP. The improvement forecast in 2020 is explained by revenue (0.3 p.p. of GDP), and reflects an increase of actual social contributions above the forecast change in the respective macroeconomic aggregate. As regards expenditure the 0.1 p.p. of GDP improvement is brought about by the expected development in "other capital expenditure".

Table 4 – Other impacts on the GG account

	2017	2018	2019	2020
Absolute figures (M€)				
Total Revenue	144	269	352	570
Total Expenditure	-90	-77	-10	-302
Budget balance	235	346	362	872
In % of GDP				
Total Revenue	0.1	0.1	0.2	0.3
Total Expenditure	0.0	0.0	0.0	-0.1
Budget balance	0.1	0.2	0.2	0.4

Source: MF. CFP calculations. | Note: The figures were calculated by deducting the effect of the measures from the no-policy-change scenario and working out the difference between that outcome and the SP/2016 projections.

3.2 PUBLIC DEBT DEVELOPMENTS

According to SP/2016 the debt shall continue the downward path that began in 2015. Over the period covered by SP/2016, the MF foresees a decline of 18.7 p.p. of GDP in the debt ratio. Most of this decrease arises in 2016 and the final two years of the projections. The impact of economic growth will provide the largest contribution to the cumulative decrease over the life of the SP, and accounts for around 54% of it, followed by the primary surpluses, which contribute 41% and the stock-flow adjustments which make up the remainder. According to the MF forecast, the contribution to debt growth over the SP/2016 time horizon will come solely from interest (+ 20.5 p.p. of GDP) although the MF predicts that interest expenditure ratio will fall from 4.6% of GDP in 2015 to 3.8% in 2020. This situation reflects a fall in the implicit interest rate of 0.1 p.p. resulting from the combined effect of the early repayment of the IMF loans[26] and the improved State borrowing conditions.

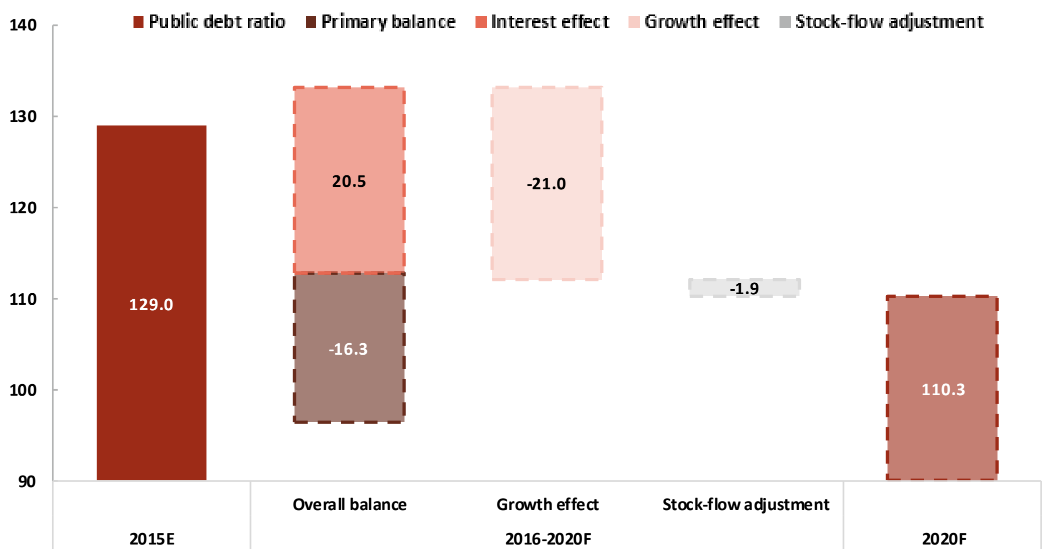
[25] The remaining difference is obtained by deducting the cumulative impact of the fiscal policy measures from the no-policy-change scenario.

[26] Within the SP/2016 time horizon the repayment of the IMF loans under the EFAP will total 8.2 p.p. of GDP.

In contrast to the forecast for the GDP ratio, the MF estimates the public debt stock will grow by 4,500 M€ from the end of 2020 compared to the end of 2015. The MF forecasts that the nominal value of debt will go from 231,300 M€ in 2015 to 235,800 M€ in 2020. This nominal increase only arises in the first three years, and the highest level should be reached in 2018, when total debt will be 236,500 M€ (following an increase of 3,100 M€ in the previous year). In 2019 and 2020 a decrease in public debt stock of 700 M€ is forecast. While the nominal decrease in 2019 involves transactions that have no impact on the balance, 2020 should record a budget surplus.

SP/2016 forecasts the stock-flow adjustments will have a favourable impact of 1.9 p.p. of GDP from 2016-2020. These adjustments reflect: (i) the use of deposits to pay off public debt, (ii) the return on the sale of Novo Banco which will allow the repayment of loans made to the Resolution Fund, (iii) the return on the sale of Oitante, (iv) the CoCos refund and (v) the differences from the change from public accounts to national accounts, which will include the liquidation of Banif, SA.

Chart 11 – Contributions to public debt developments from 2016 to 2020 (as % of GDP)



Source: MF. BoP. CFP calculations.

3.3 FISCAL PROJECTION RISKS

The path published in SP/2016 is based on the fiscal balance forecast in SB/2016 that carries a number of risks. These risks are inherent in the no-policy-change scenario on which the SP/2016 exercise is based. Here attention is drawn to the change in the level of spending on social transfers forecast by the MF for GG as a whole in 2016, which is significantly lower than the budgeted increase in CGA and Social Security expenditure.[27] If some of the risks

[27] For 2016 the MF forecasts an increase in general government spending on social transfers other than in kind of only 78 M€, while total CGA and Social Security expenditure should increase by around 513 M€ (CGA 47 M€ and

should occur, they would make it more difficult to achieve the said path from 2017 to 2020. In addition SP/2016 does not expressly incorporate the costs stemming from the proposed legislative changes that are in an advanced stage, nor the measures capable of offsetting their fiscal impact. Special mention is made of the legislation that would define a 35-hour week as the rule for civil servants, for which the related Bills were approved by Parliament in general terms on 15 January 2016.[28]

The asymmetry in the specification of policy measures that lead to a deterioration in the fiscal balance and those that lead to its improvement puts the strategy published in SP/2016 at risk. In point of fact, according to the CFP classification, while all the measures that will have a negative impact on the fiscal balance are fully specified, over half the measures that will have a positive impact on the balance (fiscal consolidation measures) are not properly specified.

The revenue projection includes unspecified measures the implementation if which could affect the entire macro-fiscal scenario. In addition to revenue being based in annual increases in taxes that have yet to be defined (and which, in cumulative terms, total 390 M€), the revenue developments forecast by the MF at the end of the projection time frame reflects other effects that do not result solely from the economic activity. Furthermore the nature of the measures that will worsen the fiscal position but have not been specified may influence macroeconomic developments and the forecast impact on the budget variables.

The public expenditure path published in SP/2016 is also highly dependent upon a series of unspecified measures. The lack of knowledge about budget consolidation measures, particularly in expenditure fields such as intermediate consumption, investment and "other current expenditure", coupled with uncertainty as to their outcomes, introduces a risk factor in regard to the budget targets to be met. The MF estimates that the impact of these measures as a whole (1,755 M€ at current prices at the end of the time period) accounts for 0.8 p.p. of GDP of the forecast decrease in the public expenditure ratio up to 2020. Past experience of unspecified measures recommends special prudence when planning their outcomes, since their insufficient achievement could jeopardise the adjustment defined in SP/2016.

Thus, the development in the fiscal balance up to 2020 could fall short of that published by the MF. As noted previously, the annual improvement resulting from SP/2016 falls short of the minimum adjustment required by the relevant European and national rules. If the aforesaid risks do arise, they could lead to a significantly biased situation and hinder access to the flexibility underlying the recently announced Programa Nacional de Reformas (see Box 1).

The macroeconomic scenario also carries risks for budgetary planning. In its Opinion on the macroeconomic forecasts underlying SP/2016, the CFP drew attention to the risks linked to those projections, above all as regards the projected annual growth rates for exports and

Social Security 466 M€). A deviation in this account in 2016 will have a non-negligible impact on the expenditure over the entire time frame of the projection.

[28] See Bills no. 7/XIII [PCP], 18/XIII [PEV], 96/XIII [BE] and 97/XIII [PS].

investment. The uncertainty surrounding the Portuguese financial system was another prudence factor highlighted by the CFP. The improvement in the fiscal balance forecast by the MF as a result of macroeconomic developments over the projection period shows how the budgetary targets are sensitive to deviations that may arise between the projections and macroeconomic reality.

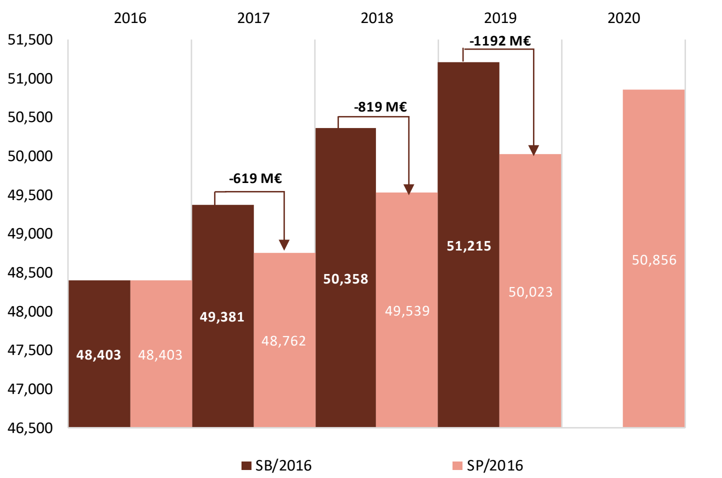
The public debt path is dependent upon the early repayments and the use of Central Government deposits. The MF expects the early repayment of loans to continue in 2016 on the back of the sale of assets in Novo Banco and Oitante and Cocos refunds. These transactions involve the risks linked to the timing and value of the sales. Should those risks occur they could jeopardise the strategy of public debt repayment and the decrease in the public debt ratio to 110.3% of GDP at the end of 2020 shown in SP/2016. The use of Central Government deposits is contingent on debt management circumstances associated with borrowing conditions. Central Government deposits, which amounted to 7.4% of GDP at the end of 2015, are expected to be used intensively over the SP/2016 time horizon and will only account for 4.4% of GDP at the end of 2020.

4 MULTIANNUAL BUDGETARY PLANNING FRAMEWORK FROM 2016 TO 2020

The BFL provides that the Multiannual Budgetary Planning Framework (MBPF) be updated annually in the State Budget, for the four following years, in keeping with the objectives defined in the Stability Programme. The MBPF limits are binding per programme and per grouping for the first and second years, respectively. However, SP/2016 contains a revision of the limits set last March, without providing any grounds for the change. Despite article 12-D of the BFL requiring the MBPF limits to be set in keeping with the objectives defined in the Stability Programme, the MF still does not provide any evidence of that consistency.

SP/2016 already contains a revision of the MBPF limits approved last March along with the State Budget for 2016 (SB/2016). In effect, Law no. 7-C/2016 (only in Portuguese), of 31 March approved the MBPF for 2016 - 2019, defining the effective Central Government (CG) expenditure limits financed by general revenue.[29] SP/2016 includes a proposed downward revision of those limits for the years following 2016, as well as the limit defined for 2020 (Chart 12). In this case the change, which is significant, can be explained by the fact that SB/16 was not based on the new fiscal strategy that SP/2016 came to define. Since the latter calls for more stringent limits than those defined in SB/16, the correction is justified. However, it is important that the new limits come to be respected in the upcoming periods, pursuant to the law, and thus put an end to the previous practice of revising them in every budgetary planning document without providing grounds for the changes.[30]

Chart 12 – MBPF expenditure limits in SB/2016 and SP/2016 (M€)



Source: Ministry of Finance. CFP calculations.

In earlier versions the MBPF underwent successive changes which led to spending limits that were always higher than the original forecasts. In addition to including more years,

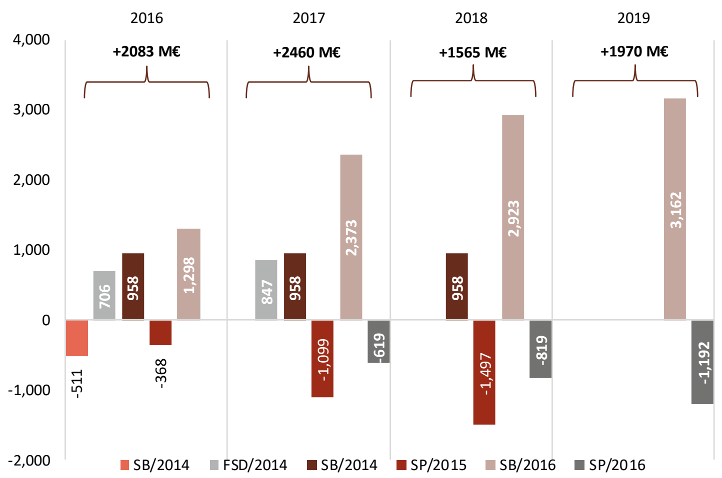
[29] Expenditure financed by taxes. The MBPF does not cover expenditure financed by services' own revenue (for example, fees). See CFP's Glossary of Public Finance Terms.

[30] The MBPF limits per budgetary programme are binding in the first economic year, per programme area (sovereignty, security, social and economic) in the second year and for the budgetary programmes as a whole in the third and fourth years. This does not prevent the publishing of a breakdown per programme for every year. However, SP/2016 only commits itself to the binding breakdown.

as the MBPF has a moving time frame, changes were made to expenditure limits set for the same years under successive MBPFs. For 2016 to 2019 (Chart 12), note the downward revision from SB/2016 to SP/2016 which totals 2,630 M€ between 2017 and 2019, with the largest portion affecting the final year (-1,192 M€). Note also that while the State Budgets, which constitute formal approval of the MBPF, have normally undertaken upward revisions in expenditure limits, the subsequent Stability Programmes have forecast lower limits, as was the case in SP/2015 and SP/2016. However, despite the revisions in opposite directions the limits applied to each year have always been higher than the original forecasts for each of them (Chart 13).[31]

Chart 13 – Change in limits for 2016-2019 compared to the sums originally forecast

(M€)



Source: MF. CFP calculations. | Note: Changes for each budget planning document were calculated vis-à-vis the preceding document.

Despite the 2016 - 2020 downward revision of the path laid down in the latest legislation on the subject (see Chart 12), the limits relating to Central Government (CG) in the MBPF should increase in absolute terms compared to 2015. From 2015 to 2020 the MF forecasts an overall increase of 4,959 M€**.** The largest increase should occur this year (2,506 M€).[32] The proposed MBPF included in SP/2016 does not contemplate in any of these years a decrease in expenditure, in nominal terms, compared to the previous year (Chart 14, left hand panel). However, if the developments forecast by the MF do occur, the expenditure financed by general revenue to GDP ratio should continue to fall, following an increase in 2016 (0.4 p.p. of GDP). From 2015 to 2020 that ratio is expected to fall by 1.8 p.p. of GDP (see Chart 14, right hand panel).

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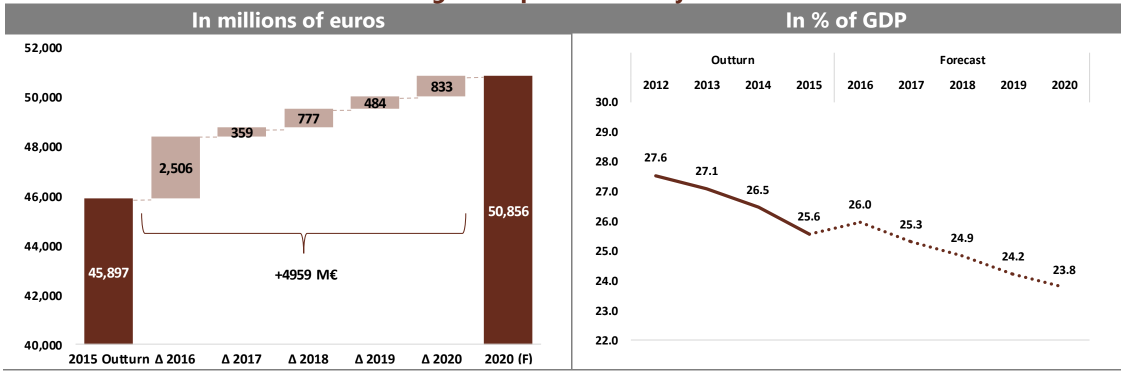
[31] Up to SP/2015 there had only been one downward revision (SB/2014 decreased the limit for 2016 by 511 M€). However in the subsequent (2014) Fiscal Strategy Document (FSD) the forecast was up by 706 M€ compared to SB/2014.

[32] Although net of the impact of reclassifying own revenue allocated to particular services as general revenue in 2016 (964 M€), it would be 1,542 M€, which is still the highest figure over all the years in the period. Most of this increase is brought about by growth in expenditure in economic area budgetary programmes ("Finance and public administration" and "Public debt management"), namely as a result of the full restoring of pay among General Government employees (+447 M€) and the increase in State direct debt costs (interest and other) (see Analysis of the Draft State Budget for 2016).

Chart 14 – Change in expenditure subject to MBPF limits



Source: Ministry of Finance. CFP calculations. | Notes: the figure shown for 2015 is provisional; "Δ" means the forecast change compared to the previous year.

The SP/2016 report does not evidence that the spending limits set out in the MBPF are consistent with the budgetary objectives defined in the national accounts for the SP time horizon. Pursuant to article 12-D (4) of the BFL, the MBPF should set limits for CG spending financed by general revenue, in accordance with the objectives defined in the Stability Programme. Since the MBPF only sets limits from the public accounts standpoint for the CG subsector and it does not include all expenditure, the SP should provide evidence of consistency with the account relating to GG as a whole. However, the SP/2016 report makes no mention of this matter.[33] According to the Ministry of Finance the limits for expenditure financed by general revenue are consistent with the macro-fiscal scenario underlying SP/2016, particularly in regard to the various expenditure aggregates. However, the information provided by the MF at the CFP's request is insufficient to assess in quantitative terms the consistency of the MBPF limits with the budgetary objectives in SP/2016, as required by the BFL.

Lastly, as the CFP has highlighted in the past, the projections for general revenue and own revenue of Central Government bodies and the Social Security subsector for the four following years have still not been published at the same time as the MBPF. The publication of these projections is mandatory under the provisions of article 12-D (6) of the BFL. This legal requirement has never been met.

[33] For 2016, taking into account the additional information provided by the MF, it was possible to gauge this consistency (see the report Analysis of the Draft State Budget for 2016).

ANNEXES

Table 5 – General government adjusted account 2015-2020 (as % of GDP

	2015	2016	2017	2018	2019	2020	Change (p.p.)	
							2015/2020	2016/2020
Total revenue	**43.9**	**43.6**	**43.2**	**43.1**	**43.0**	**42.7**	**-1.1**	**-0.8**
Current revenue	**43.1**	**42.8**	**42.3**	**42.2**	**42.0**	**41.8**	**-1.3**	**-1.0**
Tax revenue	25.4	25.2	24.9	24.9	24.7	24.5	-0.9	-0.7
Indirect taxes	14.5	14.9	14.9	14.9	14.8	14.7	0.2	-0.2
Direct taxes	10.8	10.2	10.0	10.0	9.9	9.8	-1.1	-0.4
Social contributions	11.5	11.5	11.4	11.3	11.3	11.4	-0.2	-0.1
of which: actual soc. contr. received	9.0	9.1	9.1	9.1	9.2	9.3	0.3	0.2
Sales & other current rev.	6.2	6.1	6.0	6.0	6.0	5.9	-0.3	-0.2
Capital transfers received	0.7	0.8	0.9	1.0	1.0	0.9	**0.2**	**0.1**
Total expenditure	46.9	46.0	44.8	44.0	43.2	42.4	**-4.5**	**-3.6**
Primary expenditure	42.3	41.5	40.6	39.9	39.2	38.6	**-3.8**	**-3.0**
Current primary expend.	39.6	39.1	38.1	37.3	36.5	35.9	-3.7	-3.1
Intermediate consumption	5.9	6.2	5.9	5.7	5.5	5.4	-0.5	-0.8
Compensation of employees	11.3	11.1	10.8	10.5	10.2	10.0	-1.3	-1.1
Social transfers	19.2	18.6	18.4	18.2	18.0	17.7	-1.5	-0.9
other than in kind	17.4	16.8	16.6	16.5	16.3	16.1	-1.3	-0.7
Subsidies	0.7	0.8	0.6	0.6	0.6	0.6	0.0	-0.1
Other current expenditure	2.5	2.5	2.4	2.3	2.3	2.3	-0.2	-0.2
Capital expenditure	2.7	2.5	2.5	2.6	2.7	2.6	-0.1	0.2
GFCF	2.1	1.9	2.0	2.0	2.1	2.0	0.0	0.1
Other	0.7	0.5	0.6	0.6	0.6	0.6	-0.1	0.0
Interest paid	**4.6**	**4.4**	**4.2**	**4.1**	**4.0**	**3.8**	**-0.8**	**-0.6**
General government balance	**-3.0**	**-2.4**	**-1.7**	**-0.9**	**-0.1**	**0.4**	**3.4**	**2.8**
Primary balance	1.5	2.0	2.5	3.2	3.8	4.2	2.6	2.2

Source: INE. MF. CFP calculations.

Table 6 – General government headline figures, 2015 - 2020 (as % of GDP)

	2015	2016	2017	2018	2019	2020	Change (p.p.)	
							2015/2020	2016/2020
Total revenue	**43.9**	**43.7**	**43.4**	**43.1**	**43.0**	**42.7**	**-1.1**	**-1.0**
Current revenue	**43.1**	**42.8**	**42.3**	**42.2**	**42.0**	**41.8**	**-1.3**	**-1.0**
Tax revenue	25.4	25.2	24.9	24.9	24.7	24.5	-0.9	-0.7
Indirect taxes	14.5	14.9	14.9	14.9	14.8	14.7	0.2	-0.2
Direct taxes	10.8	10.2	10.0	10.0	9.9	9.8	-1.1	-0.4
Social contributions	11.5	11.5	11.4	11.3	11.3	11.4	-0.2	-0.1
of which: actual soc. contr. received	9.0	9.1	9.1	9.1	9.2	9.3	0.3	0.2
Sales & other current rev.	6.2	6.1	6.0	6.0	6.0	5.9	-0.3	-0.2
Capital transfers received	**0.7**	**0.9**	**1.1**	**1.0**	**1.0**	**0.9**	**0.2**	**0.0**
Total expenditure	**48.3**	**45.9**	**44.8**	**44.0**	**43.2**	**42.4**	**-5.9**	**-3.5**
Primary expenditure	**43.7**	**41.5**	**40.6**	**39.9**	**39.2**	**38.6**	**-5.1**	**-2.9**
Current primary expend.	39.6	39.1	38.1	37.3	36.5	35.9	-3.7	-3.2
Intermediate consumption	5.9	6.2	5.9	5.7	5.5	5.4	-0.5	-0.8
Compensation of employees	11.3	11.1	10.8	10.5	10.2	10.0	-1.3	-1.1
Social transfers	19.2	18.6	18.4	18.2	18.0	17.7	-1.5	-0.9
other than in kind	17.4	16.8	16.6	16.5	16.3	16.1	-1.3	-0.7
Subsidies	0.7	0.8	0.6	0.6	0.6	0.6	0.0	-0.1
Other current expenditure	2.5	2.5	2.4	2.3	2.3	2.3	-0.2	-0.3
Capital expenditure	4.1	2.3	2.5	2.6	2.7	2.6	-1.5	0.3
GFCF	2.2	1.9	2.0	2.0	2.1	2.0	-0.1	0.2
Other	1.9	0.5	0.6	0.6	0.6	0.6	-1.4	0.1
Interest paid	**4.6**	**4.4**	**4.2**	**4.1**	**4.0**	**3.8**	**-0.8**	**-0.6**
General government balance	**-4.4**	**-2.2**	**-1.4**	**-0.9**	**-0.1**	**0.4**	**4.8**	**2.5**
Primary balance	0.2	2.2	2.8	3.2	3.8	4.2	4.0	1.9
Public debt	129.0	124.8	122.3	118.7	114.5	110.3	-18.7	-14.5

Source: INE. MF. CFP calculations.

Quadro 7 – Temporary measures, one-off measures and special factors (as % of GDP)

	2011	2012	2013	2014	2015	2016	2017
Temporary measures, one-off measures (impact on balance)	**0.2**	**-0.1**	**0.3**	**-3.6**	**-1.4**	**0.2**	**0.3**
Revenue	**0.5**	**0.3**	**0.8**	**0.0**	**0.0**	**0.1**	**0.2**
Taxes on repatriation of capitals		0.2					
Exceptional Scheme for Settling Tax and Social Security Debts - VAT			0.1				
Exceptional Scheme for Settling Tax and Social Security Debts - Oth. IT.			0.1				
Exceptional Scheme for Settling Tax and Social Security Debts -PIT ; CIT			0.4				
Exceptional Scheme for Settling Tax and Social Security Debts -IMT; IMI			0.0				
Exceptional Scheme for Settling Tax and Social Security Debts - social contributions			0.1				
Surcharge on PIT for 2011 income	0.5	0.1					
BPP guarantee recovery							0.2
Pre-paid Margins						0.1	
Expenditure	**0.3**	**0.3**	**0.4**	**3.6**	**1.4**	**-0.1**	**0.0**
Proceeds from concessions	0.0	-0.2				-0.1	
Capital transfers (Banking sector)	0.3	0.5	0.4	2.9	1.4		
One-off payments to the EU Budget		0.1				0.0	
Debt assumptions of transportation sector				0.7			
Sale of F-16 to Romania						-0.1	0.0
Special Factors (impact on balance)	**-0.3**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Revenue	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Expenditure	**0.3**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Reclassification of PPP into general government	0.1						
Madeira capital transactions (reclass. of Via Madeira)	0.2						
Madeira region debts from programme contracts & football clubs	0.1						
Temporary measures, one-off measures and special factors (impact on balance)	**-0.2**	**-0.1**	**0.3**	**-3.6**	**-1.4**	**0.2**	**0.3**

Source: INE, MF and BdP. CFP calculations. | Note: Due to rounding the totals do not necessarily correspond to the sum of the percentage GDP figures. No temporary measures were considered from 2018 to 2020.

Table 8 – Policy measures, accumulated effect vis-à-vis the scenario of no policy changes (in M€)

Component/measure	2017	2018	2019	2020	Measures Type	Measures situation
Total Revenue	**809**	**1,017**	**1,240**	**1,041**		
Taxes on Production and Imports	**524**	**614**	**704**	**704**		
Extraordinary Contribution on the Banking Sector	210	210	210	210	Improves Balance	S
Extraordinary Contribution on the Energy Sector	90	90	90	90	Improves Balance	S
Contribution on the Pharmaceutical Industry	14	14	14	14	Improves Balance	S
Other taxes	210	300	390	390	Improves Balance	N.S.
Capital transfers received	**285**	**403**	**536**	**337**		
Structural funds	285	403	536	337	Improves Balance	S
Total Expenditure	**-681**	**-869**	**-1,106**	**-1,370**		
Compensation of employees (**)	**-122**	**0**	**123**	**323**		
New civil servants rotation policy (volume)	-122	-200	-277	-277	Improves Balance	S
Salary Measures in the Public Service (Price)	0	200	400	600	Deteriorates Balance	S
Intermediate consumption	**-300**	**-650**	**-980**	**-1,100**		
Nominal freeze of intermediate consumption without PPP	-300	-650	-980	-1,100	Improves Balance	N.S.
Social transfers	**-100**	**50**	**50**	**50**		
Tax credit on families with low-incomes	0	200	200	200	Deteriorates Balance	S
Savings on social transfers	-100	-150	-150	-150	Improves Balance	S
Interest paid	**-186**	**-246**	**-311**	**-349**		
interest Savings	-186	-246	-311	-349	Improves Balance	S
Subsidies	**7**	**-4**	**-37**	**-10**		
Structural funds	7	-4	-37	-10	Improves Balance	S
Other current expenditure	**-180**	**-360**	**-450**	**-540**		
Nominal freeze	-180	-360	-450	-540	Improves Balance	N.S.
Gross Fixed Capital Formation	**145**	**257**	**385**	**209**		
Structural funds	280	392	520	344	Deteriorates Balance	S
Savings in investments	-90	-90	-90	-90	Improves Balance	N.S.
Savings in RPC	-45	-45	-45	-45	Improves Balance	N.S.
Other capital expenditure	**56**	**85**	**114**	**47**		
Structural funds	56	85	114	47	Deteriorates Balance	S
Impact on balance	**1,490**	**1,886**	**2,346**	**2,412**		
Measures that improve the balance | Impact on balance	**1,826**	**2,762**	**3,580**	**3,602**		
Revenue (Increases in revenue)	**809**	**1,017**	**1,240**	**1,041**		
Specified [S]	599	717	850	651		
Non specified [N.S.] *	210	300	390	390		
Expenditure (reductions in expenditure)	**-1,017**	**-1,746**	**-2,340**	**-2,561**		
Specified [S]	-402	-601	-775	-786		
Non specified [N.S.] *	-615	-1,145	-1,565	-1,775		
Measures that worsen the balance | Impact on balance	**-335**	**-877**	**-1,234**	**-1,191**		
Expenditure (increases in expenditure)	**335**	**877**	**1,234**	**1,191**		
Specified [S]	335	877	1,234	1,191		
Non specified [N.S.] *	0	0	0	0		
Impact on balance of non specified measures *	**825**	**1,445**	**1,955**	**2,165**		

Source: MF. CFP Calculations. | Note: Measures were classified by the CFP. [S] Specified; [N.S.] Not Specified. The impact of measures considered in the Taxes on Production and Imports includes 314 M€ in tax revenues by maintaining extraordinary contributions on the banking, energy and pharmaceutical sectors, which we be in force until the end of 2016.

Table 9 – Policy measures, change towards the previous year (in M€)

Component/measure	2017	2018	2019	2020	Measures Type	Measures situation
Total Revenue	**809**	**208**	**223**	**-198**		
Taxes on Production and Imports	**524**	**90**	**90**	**0**		
Contribution on the Banking Sector	210	0	0	0	Improves Balance	S
Extraordinary Contribution on the Energy Sector	90	0	0	0	Improves Balance	S
Contribution on the Pharmaceutical Industry	14	0	0	0	Improves Balance	S
Other taxes	210	90	90	0	Improves Balance	N.S.
Capital transfers received	**285**	**118**	**133**	**-198**		
Structural funds	285	118	133	-198	Improves Balance	S
Total Expenditure	**-681**	**-188**	**-237**	**-264**		
Compensation of employees (**)	**-122**	**122**	**123**	**200**		
New civil servants rotation policy (volume)	-122	-78	-77	0	Improves Balance	S
Salary measures in the Public Service (Price)	0	200	200	200	Deteriorates Balance	S
Intermediate consumption	**-300**	**-350**	**-330**	**-120**		
Nominal freeze of intermediate consumption without PPP	-300	-350	-330	-120	Improves Balance	N.S.
Social transfers	**-100**	**150**	**0**	**0**		
Tax credit on families with low-incomes	0	200	0	0	Deteriorates Balance	S
Savings on social transfers	-100	-50	0	0	Improves Balance	S
Interest paid	**-186**	**-60**	**-65**	**-38**		
interest savings	-186	-60	-65	-38	Improves Balance	S
Subsidies	**7**	**-11**	**-33**	**27**		
Structural funds	7	-11	-33	27	Improves Balance	S
Other current expenditure	**-180**	**-180**	**-90**	**-90**		
Nominal freeze	-180	-180	-90	-90	Improves Balance	N.S.
Gross Fixed Capital Formation	**145**	**112**	**128**	**-176**		
Structural funds	280	112	128	-176	Deteriorates Balance	S
Savings in investments	-90	0	0	0	Improves Balance	N.S.
Savings in RPC	-45	0	0	0	Improves Balance	N.S.
Other capital expenditure	**56**	**29**	**29**	**-67**		
Structural funds	56	29	29	-67	Deteriorates Balance	S
Impact on balance	**1,490**	**396**	**460**	**66**		

Source: MF. CFP Calculations. | Note: Measures were classified by the CFP. [S] Specified; [N.S.] Not Specified. The impact of measures considered in the Taxes on Production and Imports includes 314 M€ in tax revenues by maintaining extraordinary contributions on the banking, energy and pharmaceutical sectors, which we be in force until the end of 2016.

LIST OF ABBREVIATIONS

Abbreviations	Meaning
ADM	Military Health System
ADSE	Civil Servants Health System
AMECO	Annual Macro-Economic Database of the European Commission
ANA	Aeroportos de Portugal, S.A.
ASB	Amending State Budget
BFL	Budgetary Framework Law
BoP	Bank of Portugal
CC	Constitutional Court
CET1	Common Equity Tier
CFP	Portuguese Public Finance Council
CGA	Civil Servants Pension Agency
CIT	Corporate Income Tax
CP	Comboios de Portugal, E.P.E.
CRD IV	Capital Requirements Directive
CRR	Capital Requirements Regulation
CTT	Correios de Portugal S. A
DGO	Direção-Geral do Orçamento (Directorate-General for Budget)
EC	European Commission
ECOFIN	Economic and Financial Affairs Council
EDP	Energias de Portugal, S.A.
EDP	Excessive Deficit Procedure
EFAP	Economic and Financial Assistance Programme
EGREP	EGREP-Entidade Gestora de Reservas Estratégicas de Produtos Petrolíferos, E.P.E.
ESA	European System of National and Regional Accounts
ESC	Extraordinary Solidarity Contribution
ESSD	Extraordinary System for Settling Tax Debts and Social Security Debts
EU	European Union
EUR	Euro
FSD	Fiscal Strategy Document
g	Nominal GDP growth rate
GDP	Gross Domestic Product
GFCF	Gross Fixed Capital Formation
GG	General government
GPEARI	Planning, Strategy, Evaluation and International Relations Office (at the Ministry of Finance)
HCPI	Harmonised Consumer Price Index
ICT	Information and Communications Technology
IMF	International Monetary Fund
IMI	Municipal Property Tax
IMT	Municipal Property Transfer Tax
INE	Statistics Portugal (Portuguese Statistical Authority)
ISP	Tax on Oil and Energy Products
IT	Tax on Tobacco
M€	Million euros
MBPF	Multi-annual Budgetary Planning Framework
MF	Ministry of Finance
MLSA	Minimum Linear Structural Adjustment
MTO	Medium-Term Objective
NHS	National Health Service
NRPC	Non-Reclassified Public Corporations

Abbreviations	Meaning
OECD	Organisation for Economic Co-operation and Development
p.p.	Percentage points
s.p.b.	Structural primary balance
PB	Primary Balance
PIT	Personal Income Tax
PPP	Public-Private Partnerships
r	Implicit interest rate
REN	Redes Energéticas Nacionais, SGPS, S.A.
SAD	Police Force Health System
SB	State Budget
SF	Special factors
SFA	Stock-flow adjustment
STCP	Sociedade de Transportes Coletivos do Porto, SA
Swaps	Swap agreements
TAAB	Tax on Alcohol and Alcoholic Beverages
USD	US Dollar
VAT	Value Added Tax

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