Conselho das Finanças Públicas
Portuguese Public Finance Council

Analysis of the Fiscal Strategy Document 2014-2018

Report by the Portuguese Public Finance Council

No. 3/2014

May 2014

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. 22/2001 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 report was drawn up on the basis of the information available up to 19th May 2014.

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

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OVERVIEW AND CONCLUSIONS

The 2014-2018 Fiscal Strategy Document (FSD/2014) will probably be the last of these series of publications, which throughout the Economic and Financial Assistance Programme (EFAP) replaced the Stability Programmes required under the Stability and Growth Pact. This gives a special importance to the strategy it sets for the coming years because such strategy must ensure that the economy enters into a stable growth and financially sustainable path, in line with the confidence return by the public in general and national and foreign investors in particular.

The macroeconomic scenario adopted in the FSD/2014 foresees economic developments that meet these criteria as it is based on sustained external balance and moderate economic growth, as a result of the recovery in investment, productivity and employment, framed by fiscal stability and public finance sustainability goals in accordance with European rules.

Progress of this type was made possible by the tough adjustment programme that provided a return to external balance equilibrium and the conditions to achieve a budget primary surplus in 2014. However, the confirmation of this scenario in the medium/long run requires a deep change in the behaviour of the Portuguese economy by re-entering a growing environment based on normal financing terms. Such a change will not depend solely on fiscal policy measures for 2014/15. On the one hand, to ensure a sustainable path for public debt, a significant primary structural balance must be maintained far beyond that time span, even if the economic recovery proves to be more favourable in the medium and long run than forecasted in the FSD/2014. On the other hand, growth recovery without losing the external balance surplus calls for a macroeconomic strategy that must be explicit and sufficiently detailed so as to provide economic agents with the guidance needed to align their behaviour with the strategy proposed by the Government.

A programme such as the FSD (and the following Stability Programme) should be capable of establishing this commitment for the fiscal policy strategy and the corresponding framework, in line with the vision of the Government proposing it. To that end it must be explicit, both as regards the strategy goals pursued and the measures required to achieve them, which should be defined for the entire period covered by the programme. The possibility of an annual update of these documents has normally allowed each revision to ignore the forecasts and even the measures published the year before. This practice prevented the documents from being seen as a governance commitment and an effective anchor for economic agents' expectations. Updating the strategy over time is inevitable but abiding by it requires regular monitoring of the outturn of the planned measures over the entire programme period, an assessment of their results and, whenever necessary, the disclosure of the reasons behind any amendments to or rejection of them. In addition it requires that any alternative strategies comply with identical transparency criteria.

These documents should comprise a no policy change macroeconomic scenario, as a basis for adopting the measures and for assessing their expected impacts. This item, while mandatory by current European regulation, is not included in the FSD, therefore hindering a proper evaluation and monitoring of the proposed measures.

Equally important is the need to rethink the legal procedures which allow a new law to amend, as often as the parliamentary majority requires, the measures it defined as strategic or binding for a number of years. This is, for instance, the case with the Multiannual Budgetary Programming Framework (MBPF) whose "binding" multiannual limits are amended as often as the laws that set them (or even on the basis of a mere Government announcement to Parliament). Clearly the intention here is not to curb the Parliament's or the Executive's powers, but rather to stress that the credibility and effectiveness of the legislature's decisions depend on its ability to respect them.

Setting and meeting spending limits is essential in order to ensure the stability and sustainability of public finances. This is especially the case when the country has exhausted the options of public debt and tax burden growth and has to rely on quality private investment, headed to the tradable sectors and increased productivity, to fulfil the strategy that the FSD/2014 properly proposes. Spending limits are also required as a basis for enabling the autonomy and accountability of public services management, leading to efficiency gains and the elimination of incrementalism (positive or negative) that have featured Portuguese fiscal policy. To that end, setting expenditure limits calls for a precautionary reserve appropriation whose eventual use is subject to a clear explanation of the underlying reasons, and must not result in an automatic increase of the limits set for the following years, calling instead for measures to correct it.

In view of these principles the Portuguese Public Finance Council considers that there are aspects of the FSD/2014 that should be valued and vulnerabilities worthy of mention. The document identifies risks (concerning both the central macroeconomic scenario and the management of fiscal variables), reports on the long-term demographic scenarios and possible fiscal impacts and lists the reforms undertaken and under way which the Government believes to be most pertinent to improve the quality of public finances.

As stated above, the fiscal goals set out in the FSD/2014 are suitable considering the state of public finances and the economy. The need to pursue fiscal consolidation and continue to improve the outturns achieved over the period of the financial assistance programme is undeniable. When analysing the FSD/2013, the CFP considered as appropriate the assumption of public debt sustainability as a top priority of fiscal policy (Report no. 3/2013), given the cost of debt and the stable confidence restoration on the Portuguese economy that would emerge from that priority. Any one of these factors supposes the commitment to a clear and long-lasting fiscal consolidation strategy.

The goals published in the FSD/2014 are in line with current fiscal discipline rules. In effect they point to a general government deficit in 2015 below the 3% of GDP limit, which will allow the Excessive Deficit Procedure (EDP) to come to an end. After that year the document forecasts that the convergence trend to the Medium Term Objective (MTO) — currently set at a structural balance of -0.5% of GDP — will reached the target in 2017 and will surpass it in 2018. The substantial decrease in the planned deficit will allow a sharp decline in the general government debt ratio over the five-year period under review, thus complying with the transitional rule for the debt reduction over the first three years following the end of the EDP. Maintaining the structural deficit equal to the MTO beyond 2018 will make it possible to reduce public debt annually at the rate required by the debt rule that requires a decrease of the debt ratio in excess of the 60% of GDP benchmark.

In the long run, the update of the demographic scenarios reported in the FSD/2014 corroborates and underlines the priority of public debt sustainability. From 2013 to 2060, resident population is expected to fall by 22% and the dependency ratio to rise from 30% to 65%. An ageing population is a source of difficulties but it should also be regarded as a challenge for new economic policies. In fact, the demographic prospects call attention to the undeniable need for policies that increase productivity and act as a stimulus to a high rate of activity and high employment across all population segments, regardless of gender, age or academic qualifications. They also stress the importance of active reemployment policies. Such policies would offset the budgetary pressure from an ageing population, minimising the budget consolidation effort required to achieve the primary surpluses needed to comply with the structural balance rule.

The FSD/2014 consolidation measures identified to implement in 2014 and 2015 are very diverse and appear to be dictated by the need to achieve budget outcomes, albeit long lasting, rather than to propose the structural revision of the budget process and the reform of public services provided by the general government. On a positive note, the FSD/2014 sets out the consolidation measures to be included in the SB/2015, which brings credibility to the targets set for that year. However, there is still a need to include them in a well-defined medium and long-term strategy which, among other things, would gain from devising a governance model that clearly defines for each measure elements such as who is responsible for what and when, the scheduling of the necessary management or legislative acts, how the coordinators and implementers of the measures should interact, and the self-assessment process that will expedite the timely correction of any deviations. It is equally important to provide regular information that allows for external monitoring of the outturn of the various measures. In addition, the relative weight of the unspecified measures (0.7% of GDP in 2014 and 0.3% in the next year) is a risk that should be noted.

For the period from 2016 to 2018, the FSD does not describe the additional measures needed to meet the targets set therein. Although less detail is to be expected compared to the 2015 measures, the FSD/2014 should explain the direction and overall amount of the revenue and expenditure measures that are inherent in the macroeconomic scenario and the budgetary planning framework.

The period over which the European Structural and Investment Funds will be applied includes the entire period covered by the FSD/2014. However the document does not specify the link between the fund application strategy and the fiscal strategy. No mention is made of the conclusions of a possible analysis on the consistency of, on the one hand, the national public contribution rates agreed with the EU and, on the other, the macroeconomic scenario, the fiscal targets and the levels of public investment set out in the FSD. The credibility of the FSD would be significantly enhanced by the clarification of these matters, as well as of the foreseeable impact of the "Portugal 2020" Partnership Agreement implementation on the qualitative nature of the budget programmes measures and their annual financial planning.

1 INTRODUCTION

This report analyses the 2014-2018 Fiscal Strategy Document, in compliance with the requirements of article 7 of CFP's statutes, in particular the submission of reports on the Stability and Growth Programme and other procedures within the regulatory framework of the European Stability and Growth Pact, as well as the Multi-annual Budgetary Planning Framework.

This report is structured into five chapters. The first is introductory and describes the aims of the analysis and the structure of the document and informs whether public bodies are fulfilling their information duties. The second chapter provides a brief analysis of the budget developments in the general government sector in 2013, the basis for the FSD/2014. The third chapter assesses the macroeconomic scenario and its risks. The fourth sets out to gauge compliance with fiscal rules based on the forecasts published in the FSD, and summarises the series of European rules applying to Portugal during the period covered by the FSD/2014, which includes not only the corrective arm of the Stability and Growth Pact (currently in force), but also the preventative arm. The fifth chapter analyses the budget forecasts and in particular the composition of the fiscal adjustment, the forecast fiscal consolidation measures and the major risks. Finally the Annex brings together a series of quantitative data processed by the CFP and which is used for the analysis undertaken in the earlier chapters.

In order to better assess the fiscal consolidation effort, the general government budget aggregates were adjusted for the effects of temporary measures, one-off measures and other special factors. Note that these adjustments differ from those underlying the forecasts published in the FSD/2014 Report, and the differences are shown in the sections where analysis are conducted.

The FSD that is the subject-matter of this report was published by the Ministry of Finance (MF) on 30th April 2014. After that date some rectifications were made to numerical data. Readers should be aware that this analysis is based on the tables attached to the original publication and takes into account the amendments in the errata published by the MF on 9th May. However, the baseline information is not consistent with the errata to the annex to the FSD/2014 published on 9th May.

This report also benefitted from additional information and explanations provided by departments of the Ministry of Finance, namely the Planning, Strategy, Evaluation and International Relations Office (GPEARI) and the Directorate-General for Budget (DGO). However, not all the information requested was available when this report was published.

2 BUDGET OUTTURN IN 2013

Summary: *In 2013 the general government fiscal deficit was lower than forecast in the amending state budgets but above the original target. The fiscal adjustment (measured by the change in the primary structural balance net of special factors) was 0.9 p.p. of GDP. Although most of the consolidation effort in 2010-13 took place on the expenditure side, in 2013 there was a change in the adjustment profile, as the improvement was due entirely to revenue, contrary to the FSD/2012 forecasts. An analysis of the budget developments in the general government sector in 2013 is provided in Report no. 2/2014. This chapter provides a summary of that analysis, complemented by indicators calculated on a structural basis.*

In 2013 the general government fiscal deficit was less than shown in the amending state budgets but it was above the original target. The deficit totalled 8122 M€, accounting for 4.9% of GDP. This outcome compares favourably with the revised goal published in the first and second amendments to the SB/2013 (5.5% and 5.9% of GDP, respectively), but exceeds the initial goal of 4.5% of GDP. Net of temporary measures and special factors, the fiscal deficit stood at 5.3% of GDP in 2013, which reflects an improvement of 0.7 p.p. over 2012.[1] However this improvement was the least significant of the last three years (1150 M€). The adjusted primary deficit fell to 1.0% of GDP, which is slightly better than the figure recorded in 2008.

The fall in the fiscal deficit in 2013 was due to the favourable performance of revenue, which more than offset the increase in expenditure. Adjusted general government revenue was up by 6.1% compared to 2012. Tax revenue accounted for four fifths of that increase, as a result of the increased tax burden, which totalled 34.7% of GDP, in non-adjusted terms. Adjusted expenditure rose 3.8%, and this increase was strongly influenced by the impact of the restoring of holiday and Christmas bonuses to civil servants and pensioners, which was not fully offset by fiscal consolidation measures on the expenditure side.

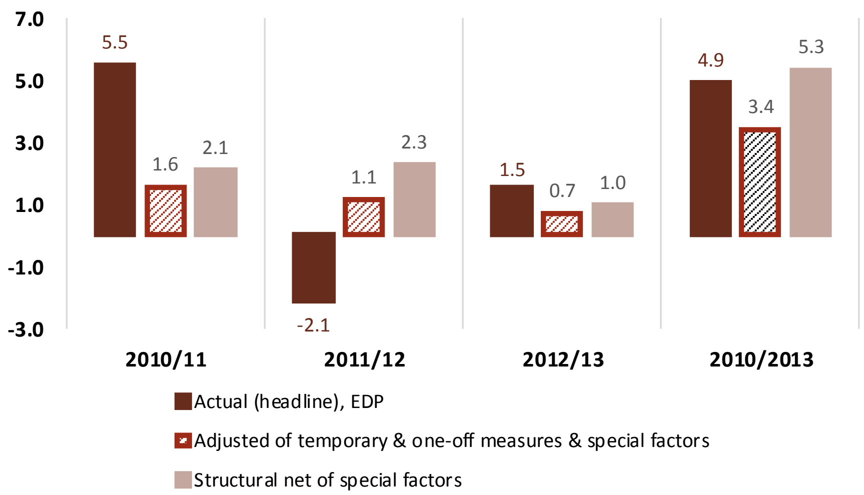
The central government subsector's contribution was essential to the decrease in the deficit. This subsector's deficit fell by 1.1 p.p. of GDP and therefore more than offset the decrease in the social security surplus (0.1 p.p. of GDP) and the local and regional government subsector surplus (0.3 p.p. of GDP). Note that the contribution of social security would have been more negative if this subsector had not benefitted from a higher extraordinary SB transfer than in 2012.

Although less unfavourable than initial forecasts the economic setting continued to have a negative impact on deficit reduction. According to the latest output gap estimate available from the MF, last years deterioration had a negative impact on the fiscal deficit reduction of 0.3 p.p. of GDP (compared to a year-on-year effect of 1.1 p.p. of GDP in 2012). In 2013 the Portuguese economy saw its volume shrink for the third consecutive year, although to a lesser extent. However, it should be noted that the actual decline in output (-

[1] In 2013 the adjustment factors related to two temporary measures: spending on the Banif recapitalisation operation (700 M€) and revenue from the ESSD - Extraordinary system for settlement of tax debts and social security debts (1280 M€).

1.4%), while greater than the initial SB estimates (-1.0%), was less than the revised forecast in the FSD/2013 (-2.3%) due to private consumption and investment being less unfavourable than expected and to a larger rise in exports.

Chart 1 – Change in fiscal balances (p.p. of GDP)



Source: INE and Ministry of Finance. CFP calculations.

The structural deficit, estimated on the basis of the information available, improved and totalled 2.8% of GDP. Net of the impact of special factors, this outcome represents an improvement of 1.0 p.p. of GDP compared to 2012 (1.4 p.p. of GDP including the impact of special factors).[2] This outcome reflects a structural correction greater than that implicit in the ECOFIN Council Recommendation of June 2013 with a view to bringing an end to the situation of excessive government deficit in Portugal.[3] Over 2010-13 the structural balance net of special factors recorded an improvement of 5.3 p.p. Taking into account the estimate for 2013, an additional correction of 2.3 p.p. of GDP is still required to achieve the medium-term objective.[4]

In 2013 the primary structural balance net of special factors improved by 0.9 p.p. of GDP. The change in this balance is normally used to assess the fiscal consolidation effort, given that, to a large extent, the interest payments are predetermined by the debt stock and cost, *i.e.*, by factors beyond the control of the budgetary authority in the year in question. In 2013, the budgetary adjustment – as measured by this indicator – was 0.9 p.p. of GDP. This change compares with 3.3 p.p. of GDP and 2.6 p.p. of GDP in 2011 and 2012, respectively.

[2] Due to a baseline effect stemming from a capital transfer to Sagestamo - Sociedade Gestora de Participações Sociais Imobiliárias, SA, following the conversion of loans granted by Parpública into equity, which was classified as a special factor in 2012.

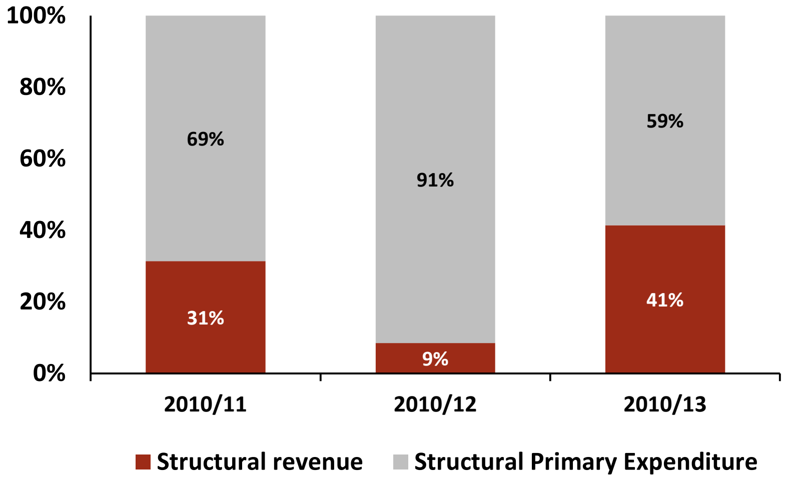
[3] Under that recommendation: "1) Portugal should bring an end to the present excessive deficit situation by 2015; (2) the Portuguese authorities should bring the headline deficit targets to 5,5 % of GDP in 2013, 4,0 % of GDP in 2014 and 2,5 % of GDP in 2015, which is consistent with an improvement in the structural balance of 0,6 % of GDP in 2013, 1,4 % of GDP in 2014 and 0,5 % of GDP in 2015, based on the Commission services' May 2013 update of the economic outlook for Portugal."

[4] The Stability and Growth Pact states that the structural balance shall converge with the Medium-Term Objective(MTO), set at -0,5% of GDP. According to FSD/2014, the MTO should be achieved in 2017.

Thus, since the beginning of the EFAP, the cumulative adjustment amounted to 6.8 p.p. of GDP (see Table 5).

Throughout 2010-13, most of the consolidation effort came from the expenditure side. Primary structural expenditure net of special factors fell 4.0 p.p. of GDP over the period, and accounted for 59% of the adjustment achieved from 2010 to 2013.[5] The increase in structural revenue net of special factors (2.8 p.p. of GDP) accounted for the remaining 41% of the adjustment achieved over the three-year period.

Chart 2 – Breakdown of the budgetary adjustment effort



Source: INE and Ministry of Finance. CFP calculations. | Note: the budgetary adjustment is evaluated on the basis of the primary structural balance net of special factors.

In 2013 there was a change in the adjustment profile which was entirely due to revenue, contrary to expectations set out in the FSD/2012. The restoring of the holiday and Christmas bonuses in 2013 already mentioned and the increase in taxation changed the composition of the adjustment. Up to 2012 the expenditure's contribution represented around 90% of the total effort, mainly due to the decline in compensation of employees. The relevance of measuring the composition of the budgetary adjustment by the change in the primary structural balance (which excludes interest) is justified by the fact that from 2010-13, interest payments rose by 2,2 B€. If the structural balance were used to measure the composition of the adjustment over those three years the effort on the revenue side (53%) would be greater than that of the expenditure side (47%).

Public debt increased up to 129.0% of GDP (213,6 B€), a ratio higher than forecast in all the budgetary planning documents.[6] As in previous years, the increase in public debt in 2013 (8,8 B€) was once again higher than the budget deficit, but the differential was the lowest for the last four years (649 M€, corresponding to the stock-flow adjustment).

[5] The contributions of primary current expenditure and capital expenditure were 2.3 and 1.7 p.p. of GDP, respectively.

[6] Net of central government deposits (17,3 B€) public debt totalled 118.5% of GDP.

3 MACROECONOMIC SCENARIO

Summary: *The macroeconomic scenario described in the FSD/2014 is in line with the forecasts of international organisations, appearing to be balanced and reasonably prudent. However it should be linked to a more complete set of measures combining economic recovery, external balance and fiscal consolidation so as to ensure the desired trend, within the time frame of the document. In particular, from 2016 onwards, almost two-thirds of the recovery in economic growth is a result of growth in domestic demand, mainly investment, accompanied by sustained positive trade account balances. This trend is consistent with the economic policy strategy goals, but the FSD/2014 should be more specific about the means and measures to be taken to ensure the stable achievement of these outcomes, both in terms of fiscal policy and economy, with which it interacts.*

The macroeconomic scenario described appears to be balanced and reasonably prudent, free of apparent bias, although comprising risks that should be taken into account. Overall the data presented are in line with the latest OECD, European Commission, IMF and Bank of Portugal forecasts, although there are some differences as regards the breakdown of GDP, as well as a net external borrowing capacity more favourable than that foreseen by the international organisations, although lower than the Bank of Portugal projection.

Table 1 – Macroeconomic forecasts for the Portuguese economy

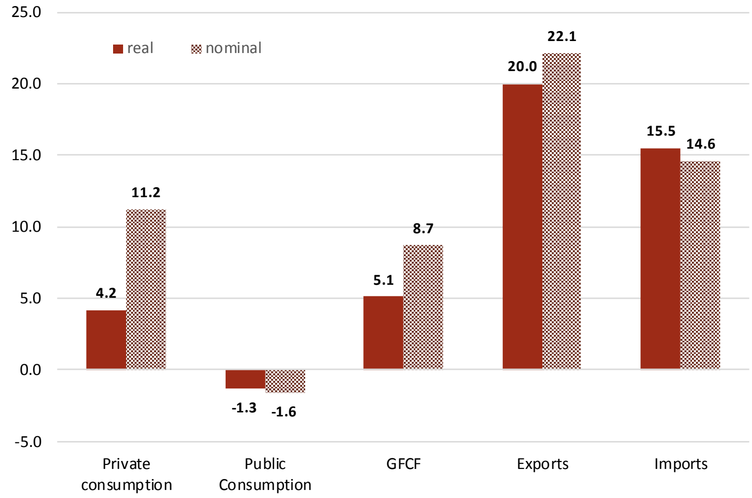
	2013	2014				2015				2016				2017			2018	
	INE	FSD	BdP (1)	EC/IMF (2)(3)	OECD (4)	FSD	BdP (1)	EC/IMF (2)(3)	OECD (4)	FSD	BdP (1)	EC (2)	IMF (3)	FSD	EC (2)	FMI (3)	FSD	IMF (3)
Real GDP	**-1.4**	**1.2**	**1.2**	**1.2**	**1.2**	**1.5**	**1.4**	**1.5**	**1.5**	**1.7**	**1.7**	**1.7**	**1.7**	**1.8**	**1.8**	**1.8**	**1.8**	**1.8**
Private consumption	-1.7	0.7	1.3	0.7	0.7	0.8	1.1	0.7	0.8	0.8	1.2	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Public Consumption	-1.8	-1.6	-0.9	-1.6	-1.6	-1.5	-0.5	-1.5	-1.5	-0.8	0.3	-0.2	1.2	-0.3	-0.3	1.1	-0.1	0.8
Gross Fixed-Capital Formation (GFCF)	-6.6	3.3	1.8	3.1	3.3	3.8	4.4	3.8	3.8	4.0	4.5	4.0	4.0	4.4	4.4	4.3	3.8	3.8
Exports (goods and services)	6.1	5.7	5.3	5.5	5.7	5.7	5.1	5.5	5.7	5.3	5.4	5.3	5.3	5.0	5.0	5.0	5.0	5.0
Imports (goods and services)	2.8	4.1	5.4	4.0	4.1	4.2	4.7	4.0	4.2	4.3	5.1	4.3	4.3	4.3	4.3	4.2	4.2	4.2
Contributions to change in GDP																		
Domestic demand (p.p.)	-2.7	0.5	1.2	0.6	0.6	0.8	1.2	0.8	0.8	1.1	1.5	1.1	1.2	1.3	1.2	1.4	1.3	1.4
Net exports of goods and services (p.p.)	1.3	0.7	0.0	0.6	0.6	0.7	0.2	0.7	0.7	0.6	0.1	0.5	0.5	0.5	0.5	0.4	0.6	0.5
Prices																		
Inflation rate	0.4	0.4	0.5	0.7	0.4	1.1	1.0	1.2	1.1	1.5	1.1	1.5	1.5	1.5	1.5	1.5	1.5	1.5
GDP Deflator	1.7	0.7	:	0.8	0.7	0.9	:	1.0	0.9	1.7	:	1.7	1.7	1.8	1.8	1.8	1.8	1.8
Labour market																		
Unemployment rate	16,3	15.4	:	15.7	15.4	14.8	:	15.0	14.8	14.2	:	14.5	14.5	13.8	14.0	14.0	13.2	13.4
Employment growth	-2.6	0.9	:	0.7	0.9	0.8	:	0.7	0.8	0.7	:	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Current account (inc. capital transfers)	2.0	2.9	3.3	2.4	2.7	3.4	3.7	2.9	3.1	3.6	4.2	3.0	3.2	3.6	3.5	3.5	3.8	3.8
International environment																		
Growth of relevant foreign markets	-0.6	3.9	3.7	:	3.9	4.5	4.8	:	5.5	4.9	5.3	:	:	5.0	:	:	5.2	:
Oil prices (Brent, USD/barrel)	108.6	104.2	107.6	:	107.6	97.9	102.4	:	102.9	93.0	97.8	:	:	90.0	:	:	88.1	:
Short-term interest rate (annual average)	0.2	0.4	0.3	:	:	0.4	0.4	:	:	0.4	0.7	:	:	0.4	:	:	0.4	:
EUR/USD exchange rate (annual average)	1.33	1.37	1.37	:	:	1.39	1.37	:	:	1.41	1.37	:	:	1.43	:	:	1.45	:
Memo items:																		
GDP at current market prices	165.7	168.9	:	169.0	:	172.9	:	173.2	:	178.8	:	179.1	179.0	185.4	185.6	185.5	192.2	192.3

Sources: FSD - Ministry of Finance; (1) Bank of Portugal – Economic Bulletin, Spring 2014 (forecasts published on 26th March); (2) European Commission - The Economic Adjustment Programme for Portugal Eleventh Review, April 2014; (3) International Monetary Fund, IMF Country Report No. 14/102, April 1, 2014; (4) OECD Economic Outlook - May 6, 2014 | Notes: in 2014 the contribution of domestic demand to GDP growth as forecast in FSD/2014 was corrected by the CFP in light of the explanation given in the Document. The CFP calculated the value of nominal GDP attributed to the EC on the basis of the figures referred to in the document (GDP growth rate in value).

From 2016 onwards, almost two-thirds of the recovery in economic growth is a result of growth in domestic demand, although the goods and services account balance is expected to remain positive over the entire period. This forecast is consistent with the economic policy goals and, since the beginning of the adjustment process, the performance of the external sector has dampened the effect of the recessive impact of the decline in domestic demand, and reduced the persistent trade deficit, even leading to its reversal in 2013. However, completing and consolidating the adjustment supposes a return to growth in domestic demand, in particular investment, as well as private consumption and the decline in public consumption will have to slowdown. Such a change, as foreseen in the macroeconomic scenario set out in the FSD, represents a fundamental change in the Portuguese economy's performance, which will not happen spontaneously nor will it depend solely upon the fiscal measures stated for 2014/2015.

Chart 3 – Cumulative change in the components of implicit Aggregate Demand from 2014-2018

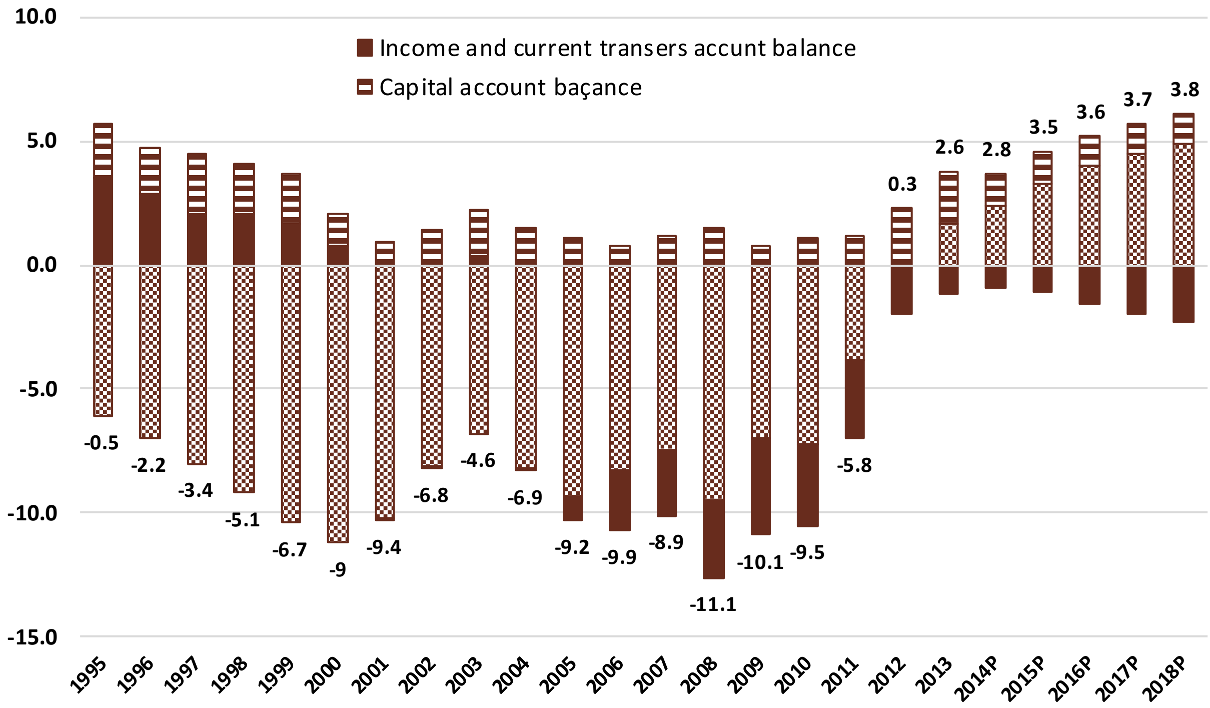
(thousands of M€)



Source: Ministry of Finance.

The forecast of continued external borrowing capacity stems from the surplus on the goods and services account and the capital account. Such a change implies an important structural change in the Portuguese economy, historically characterised by persistently high borrowing requirements, which had risen sharply in the period before the financial crisis. The FSD/2014 presents a scenario in which that correction is achieved via a consistent increase in the trade account surplus and regular positive capital account balances.

Chart 4 – Net external borrowing requirement (-) / capacity (+) (as % of GDP)



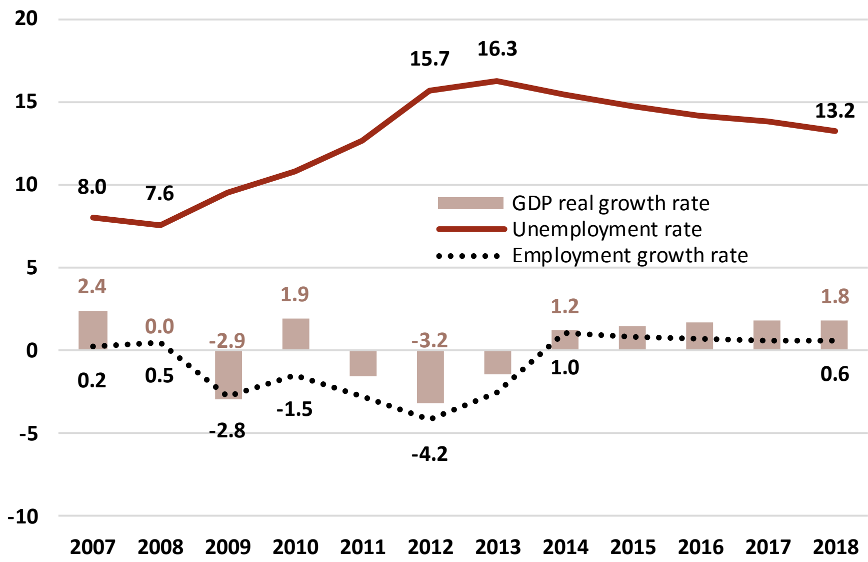
Sources: Bank of Portugal and Ministry of Finance

However, there is not enough information supporting investment growth and the improvement of the external balance, once private and public consumption restriction slows down. This lack of information hinders the transparency of the published fiscal exercise, restricts its role as a guide to internal and external economic agents' expectations and implicitly stresses the risks and uncertainties underlying the forecasting exercise.

In particular, the trend forecast for investment involves a strong recovery, which assumes focus on the external market, and important changes to companies' financial structure and sources of finance. Given the Portuguese economy's structural problems, largely associated with the quantity and quality of Gross Fixed Capital Formation, such a turnaround implies the setting out of a coherent and transparent economic and financial strategy in order to redirect investment and attract the funds required to finance it. Such details would also allow regular monitoring of the outturn of the forecast measures and, when necessary, their timely correction. As the CFP has stressed, all this calls for better and more explicit integration of the FSD and the fiscal strategy contained therein with the programmes relating to the restructuring of the economy and the financial sector.

In regard to employment the FSD estimates a very moderate growth, resulting in the persistence of high rates of unemployment, although in decline. In the light of the latest available data, in particular the number of jobs created in 2013, this estimation seems to be prudent with a 3.1 p.p. drop in unemployment up to 2018. Prudence in this matter is appropriate for two reasons. First of all, it should be borne in mind we are dealing with a fiscal strategy that does not have leeway to correct optimistic forecasts. In addition, it is consistent with the scenario regarding investment and the trade account, which assumes that an increase in labour productivity is a factor in the economy's competitiveness.

Chart 5 – Growth in GDP, Employment and Unemployment (%)



Source: INE and Ministry of Finance. CFP calculations | Note: The INE introduced a new methodology in the Employment Survey in the first quarter of 2011. The results are not comparable with those generated by the previous methodology.

In short, the macroeconomic scenario underlying the FSD is prudent, if the strategy on which it is based materialises. However, such strategy should be specified, not only to evaluate the quality of the exercise, but in particular to transform it into the strategic tool that it should be, ridding it of the vices of the former Stability Programmes that never performed this role. To this end the strategy has to be stated and must be sufficiently detailed, so as to become a governance commitment and an effective guide to economic agents' expectations.

4 FISCAL RULES

Summary: *The fiscal rules applying to Portugal over the period covered by the FSD/2014 are met. The MF predicts the excessive deficit situation will be corrected in 2015 and the rule governing the minimum structural adjustment required to converge with the medium-term objective (MTO) will be met in 2017. In the transition period following the excessive deficit correction, the applicable rule to reduce debt in excess of the benchmark is also met. As for the Multi-annual Budgetary Planning Framework, the FSD/2014 again stresses the need to revise the spending limit for 2014-17 upwards, which shows the fragility of this expenditure rule. Compliance with the expenditure rule, under which spending growth in a given year is contingent upon the development of potential output, cannot be assessed on the basis of the information available.*

4.1 SUMMARY OF APPLICABLE FISCAL RULES

The fiscal rules that Portugal has to comply with within the European framework are relatively numerous and complex. The rules govern the levels and paths of the budget balance and public debt, as well as a subset of primary expenditure net of discretionary measures[7] in terms of revenue. The rules cover both observed amounts and structural indicators, taking into account the influence of the economic cycle on the changes in public finance. There are a number of exceptions that must be considered when applying these rules. Note that since part of the European and national regulations is based on non-observable variables, such as the output gap and the structural balance, it gives rise to revisions of those estimates over time and calls for careful assessment of compliance. In addition to these rules national legislation also sets a multi-annual limit for expenditure financed by general revenue (MBPF).[8]

From the set of European rules, the following are of particular note:

- An excessive deficit situation is deemed to exist if the benchmarks of 3% of GDP for the observed fiscal deficit or 60% of GDP for the observed Maastricht debt are exceeded;
- The defining of a medium-term objective (MTO) for the budget balance, in structural terms, that takes into account a safety margin regarding the 3% deficit ratio vis-à-vis the GDP;
- The defining of a minimum annual adjustment until the MTO has been achieved (convergence path) and a correction mechanism whenever there is a significant deviation from that path and from the achieved MTO;
- The defining of a rule for correcting the debt in excess of the benchmark and, for countries which in 2011 were under an excessive deficit procedure (EDP), a transition period of three years following the excessive deficit correction during which specific conditions apply;

[7] The expression “discretionary measures” is used in this report in line with European regulations, and refers to occasional measures aimed at compliance with the existing economic governance rules.

[8] Budgetary Framework Law approved by Law no. 91/2001 of 20th August, as amended by Organic Law no. 2/2002 of 28th August and by Laws no. 23/2003 of 2nd July and no. 48/2004 of 24th August, no. 48/2010 of 19th October, no. 22/2011 of 20th May, no. 52/2011 of 13th October and no. 37/2013 of 14th June.

— The defining of a benchmark for a subset of primary expenditure (which excludes the spending associated with Community funds and non-discretionary changes to unemployment benefit expenditure) in line with the medium-term growth rate of potential output (or lower in the case of countries whose debt exceeds the benchmark).

There is some overlapping in the rules, particularly among those relating to the MTO and the reduction in the excess debt, since the definition of the MTO takes into account the budget balance required to stabilise debt and an additional effort to ensure its convergence with the 60% of GDP benchmark.

Up to 2015, Portugal will be evaluated under the corrective arm of the Stability and Growth Pact. Compliance with the ECOFIN Council Recommendation of 18 June 2013 requires that Portugal's excessive deficit will be corrected to levels below the 3% of GDP threshold in 2015. If the target set in that recommendation is met it will lead to the closure of the Excessive Deficit Procedure that was opened in 2009.

Therefore, from 2016 onwards it is to be expected that Portugal's public finances will be assessed under the preventative arm of the Stability and Growth Pact, which in addition to maintaining the budget balance below 3% of GDP, requires compliance with the structural balance adjustment path until the MTO, currently set at -0.5% of GDP.[9] The benchmark for the annual adjustment until the MTO is reached should be 0.5% of GDP. Achieving the MTO reference value should allow for:

— A safety margin in regard to the 3% budget deficit limit;
— A sustainable public debt path that takes into account the economic and fiscal impact of an ageing population;
— Fiscal space to meet the needs of public investment.

In terms of the structural budget balance and until the MTO is reached, Member-States such as Portugal that have debt levels greater than 60% of GDP must undertake annual adjustments greater than 0.5% of GDP. The adjustment effort required may be greater at times when the economic climate is more favourable and more restricted when the economic climate is unfavourable. Compliance with this rule is assessed taking into account the fiscal stance in structural terms and should be supplemented by an analysis of the rate of growth of expenditure net of discretionary revenue measures. Thus, whilst the MTO is not reached the rate of growth of adjusted expenditure should not exceed the reference rate for medium-term growth in potential GDP.

In terms of public debt, when the Excessive Deficit Procedure ends a transition period of three-years begins until the excess debt correction rule begins to apply at a rate of 5% per year. During this transition period (2016-18) Portugal should make sufficient progress to reduce its debt ratio. Such progress will be assessed annually, both *ex-ante* and

[9] Note that under Community legislation the MTO shall be updated regularly on the basis of commonly agreed methodology, so as to show clearly the risks to public finance stemming from the explicit and implicit liabilities.

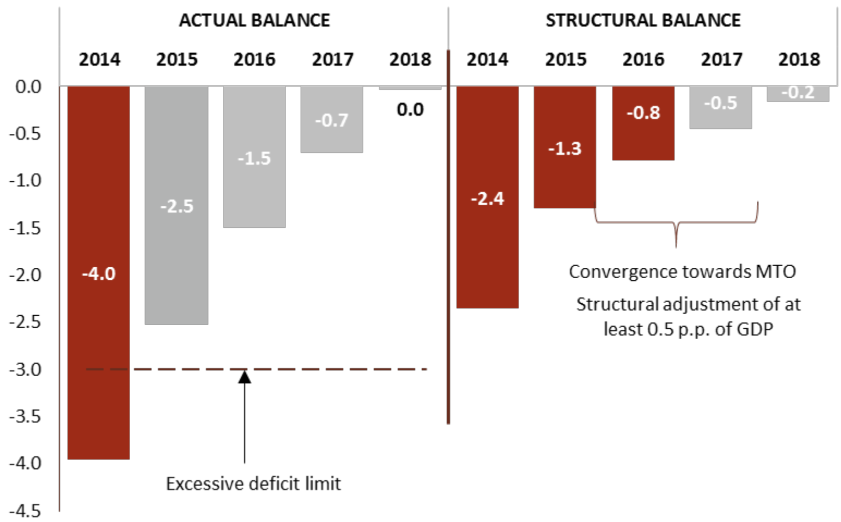
ex-post, in comparison with a minimum linear structural adjustment (MLSA).[10] The path of the minimum linear structural adjustment should take into account the impact of the economic cycle and the debt reduction benchmark (see Box 1). Over this period the following conditions will have to be met simultaneously:

i. The annual structural adjustment must not deviate more than 0.25% of GDP vis-à-vis the linear structural adjustment that ensures compliance with the less demanding debt rule over the transition period;
ii. At any time during the transition period the remaining annual structural adjustment shall not exceed 0.75 % of GDP. This condition does not apply if the former requires an annual effort of over 0.75 % of GDP.

4.2 RULES RELATING TO BUDGET BALANCES

The FSD goals for budget balances meet the Stability and Growth Pact requirements. In terms of the budget balance, Portugal is expected to comply with the Council Recommendation of 18 June 2013 which establishes a decrease in the nominal deficit to 2.5% of GDP in 2015 – enabling the closure of the Excessive Deficit Procedure. The MTO convergence path will also be achieved: the FSD estimates that the structural adjustment in 2016 will be 0.5 p.p. of GDP, in line with the general rule, and the MTO will be met in 2017, which will involve a structural adjustment of 0.3 p.p. of GDP that year (see Table 5).

Chart 6 – Compliance with budget balance rules (% of GDP)



Source: Ministry of Finance. The structural figures shown are net of the impact of the economic cycle and the impact of temporary and one-off measures and special factors.

4.3 EXPENDITURE GROWTH RATE RULE

Compliance with the expenditure rule, under which spending growth in a given year is contingent upon the development of potential output,[11] cannot be assessed on

[10] Minimum Linear Structural Adjustment.
[11] Article 12-C of Law no. 37/2013 of 14th June, which introduces the seventh amendment to the Budgetary Framework Law, approved by Law no. 91/2001 of 20th August, and transposes to Portuguese law Council Directive no. 2011/85/EU of 8 November on the requirements for budgetary frameworks of Member-States.

the basis of the information available. This rule will be applicable once the Excessive Deficit Procedure has come to an end, along with the rule calling for a minimum annual structural adjustment of 0.5 p.p. of GDP. Therefore, compliance with this rule should be assessed in regard to the 2016, and subsequent, budgets. This assessment is performed on the basis of the evaluation of three parameters: (i) relevant expenditure aggregate,[12] (ii) the reference medium-term rate of potential GDP growth and (iii) a convergence margin for those countries that have not yet achieved their MTO. For Portugal the reference medium-term rate of potential GDP growth was set at 0.1%. Until Portugal meets the MTO, the reference rate of expenditure growth should be adjusted by a convergence margin of 1.2%,[13] which gives rise to a reference rate of -1.2%. The FSD/2014 does not provide all the information required to calculate the relevant expenditure aggregate which makes it impossible for the CFP to evaluate whether the expenditure rule will be met.

4.4 RULES RELATING TO PUBLIC DEBT

During the three-year transition period, until the application of the rule which implies a reduction of the debt differential by 5% per year, Member-States are required to undertake a structural balance adjustment that fulfils at least one of the following three criteria: backward looking, forward looking and cyclically adjusted (see Box 1). All the criteria assume a linear adjustment over the three years. The scale of the adjustment required is proportional to the deviation from the estimated debt path in the absence of the adjustment relating to the reference value (that is to say, when maintaining the structural balance unchanged from the level in the year in which the Excessive Deficit Procedure terminated).

The public finance adjustment path foreseen in the FSD/2014 meets the minimum requirements of the debt rules applying to the transition period (2016 -18). The MF forecasts indicate that in 2018 there will be a structural balance of – 0.2% and debt of 116.7% of GDP. According to CFP calculations, taking as a starting point the structural balance in 2015, the nominal GDP path forecast in the FSD/2014, and a potential economic growth of 1% in 2019 and 2020 (in line with MF estimates for medium-term growth in potential output), compliance with the transition period rules will require a structural balance of at least -1.3% and public debt under 119.2% of GDP in 2018.[14] The table below compares the change in debt foreseen in the FSD/2014 with the outcome of the required minimum linear structural adjustment (MLSA) over the transition period.

[12] The relevant expenditure aggregate rule relates to a subset of public expenditure. This excludes the following outlays: interest; those relating to European Union programmes fully covered by EU funds; non-discretionary changes to unemployment benefit spending, and investment expenditure in the current year. However to this subset of expenditure, investment outlays relating to a four-year average, so as to analyse the impact of large scale projects. The source of the information for each variable should be defined in advance in the tables attached to the Stability Programme for *ex-ante* and *ex-post* compliance assessments.

[13] For further information on the reference rate applicable to Portugal see European Commission, 2013, *Vade mecum on Stability and Growth Pact, Occasional Papers 151*

[14] This outcome corresponds to compliance with the least restrictive criterion under these conditions: the backward looking element.

Table 2 – Compliance with budget balance rules (% of GDP)

Year	Debt FSD /2014	Debt with MLSA
2015	128,7	128,7
2016	125,6	126,2
2017	120,7	122,1
2018	116,7	119,2

Source: CFP calculations.

In the three-year transition period the active restriction of fiscal policy in Portugal will be the rule for achieving convergence of the structural balance with the MTO. While compliance with the rule governing the decrease in the public debt ratio over the transition period allows for a structural balance of -1.3% of GDP from 2015 onwards, compliance with the structural balance rule requires that the MTO of -0.5% of GDP be achieved in 2017, which implies a sharper decrease in debt over that period.

Box 1 – Criteria for calculating the minimum linear structural adjustment (MLSA)

The European rules for the public debt path over the transition period establish compliance with a minimum linear structural balance adjustment (MLSA) resulting from the comparison of three elements: backward looking element, forward looking element and the cyclically adjusted element. The minimum structural balance adjustment that fulfils each of them is referred to, respectively, as *BLadj*, *FLadj*, and *CYCLadj*. Only the least demanding criterion is binding and for this reason MLSA is calculated as:

$$MLSA = \min(BLadj, FLadj, CYCLadj)$$

Therefore the values of these parameters correspond to the change in the structural balance that provides for debt's relative weight in GDP equal to the reference value for the various criteria. A brief description is given below of how *BLadj*, *FLadj* and *CYCLadj* are calculated.

Backward looking element:

BLadj is calculated at the end of the transition period, *t*, and corresponds to the minimum linear structural balance adjustment over the three years of the transition period that allows the debt reference value of bb_t to be achieved. This criterion is backward looking to the extent that the reference value takes into account the debt ratios of the three years before the period in which it is calculated.

$$bb_t = 60\% + \frac{0{,}95}{3}(b_{t-1} - 60\%) + \frac{0{,}95^2}{3}(b_{t-2} - 60\%) + \frac{0{,}95^3}{3}(b_{t-3} - 60\%)$$

Forward looking element:

FLadj is calculated at the end of the transition period, *t*, and corresponds to the minimum linear structural balance adjustment over the three years of the transition period that allows the debt reference value of bb_{t+2} to be achieved, assuming the absence of an additional adjustment in *t+1* and *t+2*. This criterion is forward looking to the extent that the reference value is obtained on the basis of the final year of the transition period, *t*, and the two following years, *t+1* and *t+2*.

$$bb_{t+2} = 60\% + \frac{0{,}95}{3}(b_{t+1} - 60\%) + \frac{0{,}95^2}{3}(b_t - 60\%) + \frac{0{,}95^3}{3}(b_{t-1} - 60\%)$$

Cyclically adjusted element:

Finally, *CYCLadj* is calculated at the end of the transition period, *t*, on the basis of the reference value analogous to the backward looking criterion, except that the debt ratio figures, $b_t^{aj.cycle}$, have been adjusted for the economic cycle, as per:

$$b_t^{aj.cycle} = \frac{B_t + \sum_{j=0}^{2} C_{t-j}}{Y_{t-3}\prod_{h=0}^{2}\left(1 + y_{t-h}^{pot}\right)\left(1 + p_{t-h}\right)}$$

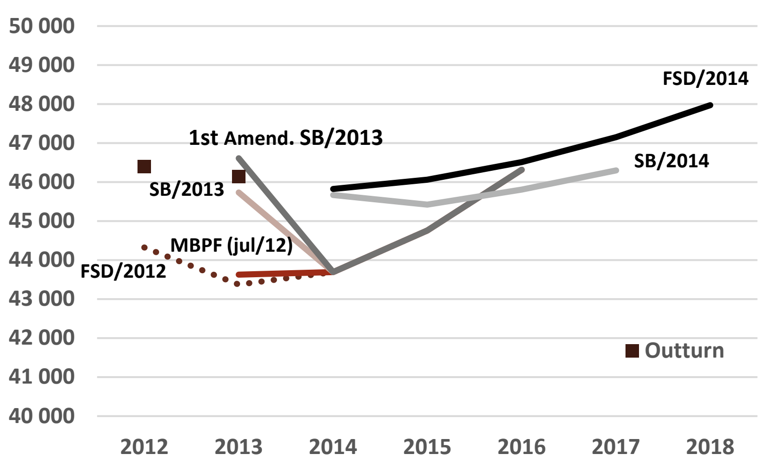
where capital letters are nominal values, *B* is the public debt stock, *Y* is GDP, *C* is the cyclical component of the budget balance, y^{pot} is the growth rate of potential output and *p* is the change in the GDP deflator.

4.5 MULTI-ANNUAL BUDGETARY PLANNING FRAMEWORK

The setting of a multi-annual budgetary planning framework (MBPF) is an important step to create a medium-term anchor for Portuguese public finances. However, the top-down approach in Portugal continues to reveal a planning process far from the purpose the multi-annual spending limits should serve so as to ensure the long run sustainability of public accounts.

The MBPF has not achieved the level of stability that should be inherent in it. This framework sets the ceilings for expenditure planning and outturn in the medium-term. These ceilings correspond to multi-annual limits on central government expenditure financed by general revenue. However, in practice the limits have been changed every year and even more than once in 2013. This is partly due to the apparent contradiction in the Budgetary Framework Law (BFL) which, on the one hand, states that spending limits are binding for four years, and on the other, requires that the MBPF be updated annually for the next four years. Thus, the Government has changed the limits in almost all the budgetary planning documents, impairing the effectiveness of this expenditure control tool.

Chart 7 – Revised multi-annual expenditure limits (M€)



Source: Ministry of Finance. | Note: the figure relating to spending outturn in 2013 is provisional.

The FSD/2014 does not demonstrate the compatibility of the budget goals defined in national accounts with the spending limits set out in the MBPF. Pursuant to article 12-D (4) of the BFL, the MBPF should define the limits for central government spending financed by general revenue, in accordance with goals laid down in the Stability Programme. However, the revised plans for the MBPF set out in the FSD/2014 do not show this compatibility. It is merely stated that the central government expenditure limit is consistent with the medium-term outlook for public finance and with the general government account balance in national accounts, but no other information is provided to support this statement.[15] The revised plans for the MBPF also lack forecasts for general revenue and own revenue of central government bodies and the social security subsector over the following four years. That information should be included in the MBPF in line with the provisions of article 12-D (6) of the BFL.[16]

The CFP recommends that the MBPF provides a breakdown by programme for the whole timeframe, where the figures for t+2 to t+4 are merely indicative. The expenditure limits are broken down by programme only for the first year of the MBPF. In fact under the provisions of the BFL the programme limits are only binding for the following year. However, that provision does not prevent the MBPF from indicating the details per programme for all four years.[17] The inclusion of such details would enhance the transparency of this planning exercise and would also reinforce its credibility. From the public sector management standpoint, in particular to achieve efficiency gains it is essential for the budget programme manager to know the medium-term budget restrictions.

4.5.1 Analysis of outturn from 2012-13

In 2012, expenditure was higher than the limit set in the FSD/2012. In that year central government expenditure financed by general revenue stood at 46 396 M€, exceeding by 571 M€ the limit set out in FSD 2012.[18] This situation is explained mainly by the extraordinary SB transfers made to Social Security (857 M€) and to CGA (220 M€), approved under the 2nd ASB/2012. That additional expenditure was partially offset by savings achieved in the "Public debt management", "Defence" and "Internal security" programmes.

[15] The expenditure that is relevant to fiscal policy supervision and execution is the public expenditure recorded in national accounts. This aggregate is broader than the expenditure financed by general revenue in the central government subsector. National accounts expenditure comprehends all of the general government subsectors and reflects all sources of financing, that is, both own revenue and general revenue from taxation or indebtedness. In addition to this difference, expenditure in national accounts reflects the accrual principle, (i.e. transactions have a different treatment from public accounts) and records specific imputed expenditures with no effect on the balance.
[16] Note that this legal provision was never met in the approved MBPF.
[17] Pursuant to article 12-D (5) of the BFL the following spending limits are also binding: for each programme grouping for year t+2; and for the programmes as a whole for years t+3 and t+4. However, account should also be taken of the exception laid down in paragraph 8 of the same article of the BFL which permits outlays relating to transfers resulting from the application of the autonomous regions and local government laws, transfers to the European Union and the cost of public debt to be subject only to the overall limit.
[18] Note that the budgetary planning framework was submitted for the first time in April 2012, under the FSD and although the reference period was 2013-2016 it also included limits for 2012. The MBPF for 2013 to 2016 was approved by Law no. 28/2012 of 31 July.

Table 3 – Expenditure financed by general revenue from 2012-13 (in M€)

Programme	FSD 2012 (apr/12)	Outturn	FSB 2012 (apr/12)	MFPF (jul/12)	SB 2013 (oct/12)	1st amend. (jul/13)	Estimate (oct/13)	Preliminary Outturn	Change 2012/13
1. SOVEREIGNTY	***4 033***	***3 928***	***3 753***	***4 003***	***4 088***	***4 133***	***4 161***	***4 112***	***184***
Sovereign Bodies	2 827	2 811	2 574	2 824	2 868	2 871	2 871	2 857	46
Governance and Culture	231	203	221	221	222	222	222	206	3
Foreign affairs	305	286	312	312	319	319	306	307	21
Justice	670	628	646	646	679	721	762	743	115
2. SECURITY	***3 480***	***3 249***	***3 503***	***3 503***	***3 670***	***3 669***	***3 475***	***3 513***	***264***
Defense	1 813	1 702	1 778	1 778	1 843	1 842	1 730	1 759	57
Internal Security	1 668	1 547	1 725	1 725	1 827	1 827	1 745	1 754	207
3. SOCIAL	***22 759***	***24 043***	***20 514***	***20 514***	***23 249***	***24 122***	***24 094***	***24 081***	***39***
Health	9 279	9 754	7 546	7 546	7 841	7 913	7 912	7 902	-1 852
Basic and Second. Educ. and Sch. Adm	5 234	5 172	5 077	5 077	5 232	5 475	5 429	5 429	257
Science and Higher Education	1 238	1 244	1 208	1 208	1 305	1 367	1 349	1 356	112
Solidarity and Social Security	7 008	7 872	6 683	6 683	8 871	9 367	9 404	9 393	1 521
4. ECONOMIC	***15 552***	***15 176***	***15 608***	***15 608***	***14 732***	***14 689***	***14 577***	***14 440***	***-736***
Finance and Public Administration	7 623	7 754	7 485	7 485	6 874	7 166	7 286	7 144	-610
Public Debt Management	7 330	6 849	7 551	7 551	7 276	6 941	6 803	6 827	-22
Economy and Employment	174	141	165	165	160	160	125	99	-42
Agriculture, Sea and Environment	425	432	407	407	422	422	363	370	-62
5. TOTAL (1+2+3+4)	**45 825**	**46 396**	**43 377**	**43 628**	**45 737**	**46 613**	**46 306**	**46 147**	**-249**
Memo:									
6. Central Adm. total expenditure	n.d.	58 834	n.d.	n.d.	61 224	62 396	62 245	61 270	
7. Weight , in % [(5)/(6)]	n.d.	78.9	n.d.	n.d.	74.7	74.7	74.4	75.3	

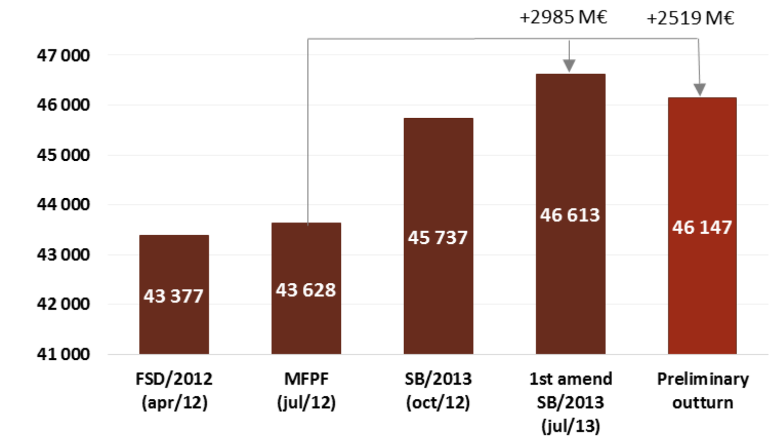
Source: DGO. CFP calculations. | Notes: public accounts figures; the "Health" programme figures for 2012 include overdue NHS payments (1 924 M€, of which 424 M€ were brought forward); for reasons of comparison the structure of the programmes shown in this Table is that which was in effect when SB/2013 and the 1st ASB/2013 were approved. The comparison by programme should take into account that: i) the figures relating to the MF Estimate (published in the SB/2014 report and non-binding) and the 2013 provisional outturn do not exactly match that structure because as a result of Decree-Law no. 119/2013 of 21st August (which approved the new Organic Law of the 19th Government), Employment was incorporated in the "Solidarity, Employment and Social Security" programme and Environment became an autonomous part of the "Environment, Land Management and Energy" programme; ii) the figures are not corrected for changes in expenditure financing sources.

The expenditure limit for 2013 was amended three times within fifteen months, which confirms that, in practice, the limit is non-binding. The FSD/2012, published in April 2012, estimated that expenditure financed by general revenue would total 43 377 M€ in 2013. In July 2012, following formal approval of the MBPF for 2013-16, a limit of 43 628 M€ was set for 2013. In October 2012 that limit was revised upwards under the SB/2013 (up 2 109 M€), so as to provide for the partial restoration of the holiday and Christmas bonuses to a part of civil servants and pensioners[19], as well as the extraordinary SB transfer (970 M€) designed to ensure a balanced Social Security System budget balance. In July 2013, under the 1st ASB/2013, the limit was increased once more (up 876 M€), due to the need to make an additional SB transfer to Social Security (500 M€) and also as a result of the complete reversal of the decision to suspend the said bonuses.[20] Thus the limit approved in the 1st ASB/2013 was 3 236 M€ higher than in the FSD/2012. Therefore it may be concluded that the existence of the MBPF does not enforce measures on the expenditure side to offset any deviations from the original plan. This indicates a problem as regards the actual setting of the limits as well as their amendment leading to the ineffectiveness of the tool.

[19] Following Constitutional Court Judgement no. 353/2012 of 5th July.

[20] That reversal was ordered by Constitutional Court Judgement no. 187/2013 of the 5th April 2013. For its part the increase in the SB transfer to Social Security was also intended to offset the effect of the revised macroeconomic scenario on this subsector's account.

Chart 8 – Changes in the 2013 ceilings (in M€)



Source: Ministry of Finance. | Note: the limit set in FSD/2012 was not approved by law, for this reason the total change calculation was based on the MBPF approved in July 2012.

The provisional outturn for 2013 points to an expenditure level below the revised limit set out in the 1st ASB/2013, but 2 519 M€ above the original MBPF. In 2013 the provisional figure for expenditure was higher than the amounts set out in FSD/2012, in the original MBPF and in SB/2013.[21] The revised limit, approved in the 1st ASB/2013 was met as the provisional outturn is 466 M€ lower; the 114 M€ saving on the "Public debt management" programme is of particular note.[22]

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[21] Note that the MBPF was not included in FSD/2013, as the MF held that it was excused from this obligation following the exception provided by the European Commission to Member-States under the financial assistance programme (excused from presenting a Stability Programme).

[22] For information purposes the (provisional) outturn figure for 2013 was 160 M€ below the sum estimated by the MF in the SB/2014 report (see Table 3).

4.5.2 Analysis of MBPF 2014 – 2018

The revised plans for the MBPF set out in the FSD/2014 point to an upward revision of 154 M€ in the 2014 limit.[23] The 2014 limit was set for the first time in Law no. 28/2012 of 31st July at 43 691 M€. In the SB/2014 Law that limit was increased by around 2 000 M€, following the reversal of the measure to suspend bonuses to retired persons and pensioners. The FSD/2014 establishes an updating plan for the MBPF which supposes an upward revision of the 2014 limit (up 154 M€). This higher sum reflects the impact of the approval of the 1st ASB/2014,[24] in particular the rise in spending on CGA pensions and benefits,[25] and the reclassification of the State transfer to the CGA under the "Solidarity, employment and social security" programme, rather than under the "Finance and general government" programme. Note that the revised plans for 2014 require a legislative change since the MBPF was not revised under the ASB/2014.

Table 4 – Limits on expenditure financed by general revenue in 2014 (in M€ and as %)

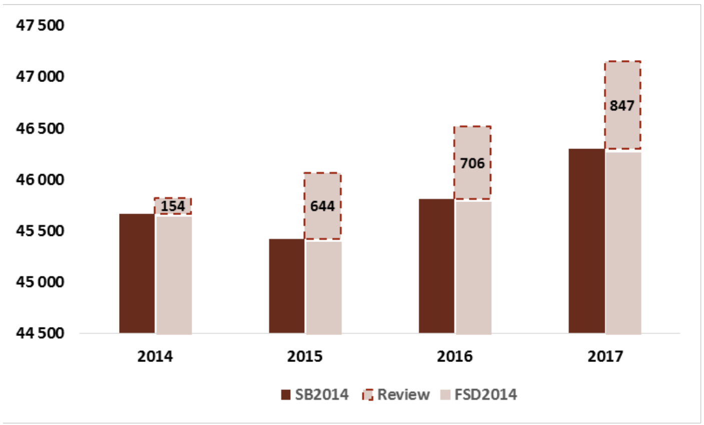
Program	2014			Structure (%)		Diference FSD towards:	
	MFPF (jul/12)	SB 2014 (oct/13)	FSD 2014 (apr/14)	SB 2014	FSD 2014	MFPF	SB 2014
1. SOVEREIGNTY	***3 676***	***4 144***	***4 146***	***9.1***	***9.0***	***470***	***2***
Sovereign Bodies	:	2 975	2 977	6.5	6.5	:	2
Governance and Culture	:	226	226	0.5	0.5	:	0
Foreign affairs	:	285	285	0.6	0.6	:	0
Justice	:	658	658	1.4	1.4	:	0
2. SECURITY	***3 497***	***3 309***	***3 283***	***7.2***	***7.2***	***-214***	***-26***
Defense	:	1 694	1 683	3.7	3.7	:	-11
Internal Security	:	1 615	1 600	3.5	3.5	:	-15
3. SOCIAL	***20 139***	***23 213***	***27 464***	***50.8***	***59.9***	***7 325***	***4 251***
Health	:	7 621	7 621	16.7	16.6	:	0
Basic and Secondary Educ. and School Adm.	:	4 938	4 938	10.8	10.8	:	0
Science and Higher Education	:	1 296	1 296	2.8	2.8	:	0
Solidarity, Employm. and Social Security	:	9 358	13 609	20.5	29.7	:	4 251
4. ECONOMIC	***16 379***	***15 002***	***10 930***	***32.8***	***23.9***	***-5 449***	***-4 073***
Finance and Public Administration	:	7 172	3 099	15.7	6.8	:	-4 073
Public Debt Management	:	7 239	7 239	15.9	15.8	:	0
Economy	:	222	222	0.5	0.5	:	0
Enviroment, P. Territory and Energy	:	41	41	0.1	0.1	:	0
Agriculture and Sea	:	328	328	0.7	0.7	:	0
5. TOTAL (1+2+3+4)	**43 691**	**45 669**	**45 823**	**100.0**	**100.0**	**2 132**	**154**
Memo:							
6. Central Adm. total expenditure	:	60 969	:	:	:	:	:
7. Weight , in % [(5)/(6)]	:	74.9	:	:	:	:	:

Source: DGO. CFP calculations. | Note: public accounts figures; the structure of the programmes presented in this Table is that defined Decree-Law no. 119/2013 of 21st August (which approved the new Organic Law of the 19th Government); From 2014 onwards the transfers to companies in the transport sector to compensate for providing a public service were recorded in the "Economy" programme, whereas in previous years they were recorded under the "Finance and general government" programme; the figures relating to the MBPF approved in July 2012 are identical to those set out in FSD/2012, published in April of that year, and they were not amended in SB/2013, nor in the 1st ASB/2013.

[23] Note that the law establishing the MBPF (Law no. 28/2012 of 31st July), which states that the limits referring to 2014-2016 are merely indicative, has remained unaltered. Article 172 of the SB/2014 Law made a single amendment to Law no. 28/2012 of 31st July, which had approved the MBPF for 2013-16, when it updated the Framework 2014-2017. This provision is in conflict with the provisions of the BFL, a law with added weight. The CFP has already called attention to this loophole in the law and once again recommends the revoking of the provision in question (article 2 (2) of Law no. 28/2012), so as to ensure compliance with the BFL on this matter.
[24] Law no. 13/2014 of 14th March, which did not revise MBPF 2014-18 approved by the SB/2014 Law.
[25] Following Constitutional Court Judgement no. 862/2013 of 19th December that declared the convergence of the civil servant social protection scheme with the general social security scheme to be unconstitutional.

The FSD/2014 also revises the limits set for 2015, 2016 and 2017. If the updating plans are adopted, it will be the second time the limits for those years are revised, the first time was in the SB/2014. The FSD/2014 revises upwards the limits previously set for 2015 (+644 M€), for 2016 (+706 M€) and for 2017 (+847 M€). According to the information provided by the DGO, the revision reflects, among other factors, the impact of the partial restoring of the cut in civil servants' remuneration, forecast in 2015, that will impact on subsequent years and an expected increase in interest payments, partially offset by the downward revision in other costs.[26] The period covered by the new MBPF ends in 2018, the year in which the spending limit rises to 47 974 M€, more 825 M€ that on 2017.

Chart 9 – Changes in MBPF limits (in M€)



Source: Ministry of Finance. CFP calculations.

[26] In reply to a CFP request for clarification DGO stated that the major changes compared to the previous version for 2015 may be explained by the following measures: (i) Restoring of civil servants' wages in 2015, accounting for 20% of the cut recorded in 2014; (ii) Decrease in the transfer to Social Security stemming from a lower level of spending on unemployment benefits, as well as improved performance in social contributions; (iii) Increase in the CGA contribution; (iv) Increase in public debt interest; (v) Increase in Health expenditure, resulting from the payment of previous years' expense and (vi) Savings on compensatory payments under the Economy programme.

5 BUDGETARY PROJECTIONS

Summary*: The budgetary projections for the general government account for 2014-18 reflect the adjustment required to ensure fulfilment of the balance targets set by the ECOFIN Council Recommendation, in order to end the situation of an excessive deficit, and assure compliance with the new European semester rules. Until 2018 the budget consolidation effort will continue to be marked by an adjustment based on the reduction of primary expenditure, notwithstanding the greater contribution now expected from revenue vis-à-vis the previous FSD. Thus, from 2014 to 2018, the relative weight of expenditure in GDP should fall while the relative weight of revenue is expected to remain practically unchanged. In 2014, the FSD estimates an effect of the fiscal consolidation measures less significant than foreseen in the SB/2014, and identifies additional measures for 2015, although no mention is made of their impact over the remainder of the planning period. Changes to the debt ratio are revised upwards compared to the previous FSD. The downward path in the debt ratio over the period covered by the FSD/2014 is based on primary surpluses, continued growth and large scale favourable stock-flow adjustments.*

5.1 FISCAL TRANSPARENCY

For fiscal transparency sake and in line with the guidelines defined at the European level, the FSD/2014 should present projections for general government revenue and expenditure in a non-policy change scenario. Assessing the fiscal strategy to be pursued until 2018 also requires identifying the scale of the adjustment needed to meet the targets set.

The Stability and Growth Pact states that stability programmes must be based on the most probable macro-fiscal scenario or a more prudent one.[27] The Stability Programme and Growth Code of Conduct, approved on 12th September 2012, provides clear guidelines in relation to the format and contents of Stability Programmes. To be precise, information must be provided on the following items:

- Revenue and expenditure ratios and their main components;
- Temporary and one-off measures;
- The expenditure path including detailed information on GFCF;
- The expected growth path of revenue in a non-policy change scenario;
- Quantification of the planned measures;
- Breakdown of the balances by subsector.

Pursuant to article 12-D (1) of the BFL, the MBPF must contain a description of the medium-term policies that impact on general government finances and an assessment of how, given their long-term direct impact, those policies may affect public finance sustainability.

As regards public debt, the Code of Conduct also provides for the supply of information relating to the expected stock-flow adjustments, the revenue arising from privatisations and other financial transactions. The FSD/2014 does not meet any of these requirements, a fact which limits any analysis of the consistency and credibility of the published budgetary projections.

[27] Pursuant to article 3 (2-A) of Council Regulation (EC) No. 1466/97 of 7 July 1997.

5.2 BUDGET BALANCES

The MF projections for 2013-18 forecast a decrease in the general government budget deficit of 4.9 p.p. of GDP. Over half the decrease will arise from the favourable contribution of the economic cycle (2.6 p.p.) and the decline in the relative weight of interest (-0.1 p.p. of GDP), in a period in which the expected impact of temporary measures and one-off transactions will be unfavourable to the tune of 0.3 p.p. of GDP. The budget imbalance correction up to 2018 (i.e. 4.9 p.p. of GDP) is expected to be supported by the ability to generate increasing primary surpluses throughout the projections' time horizon. The reversal of the primary balance position from 2014 onwards will be decisive to achieve the downward public debt ratio path that the MF expects to begin in 2015.

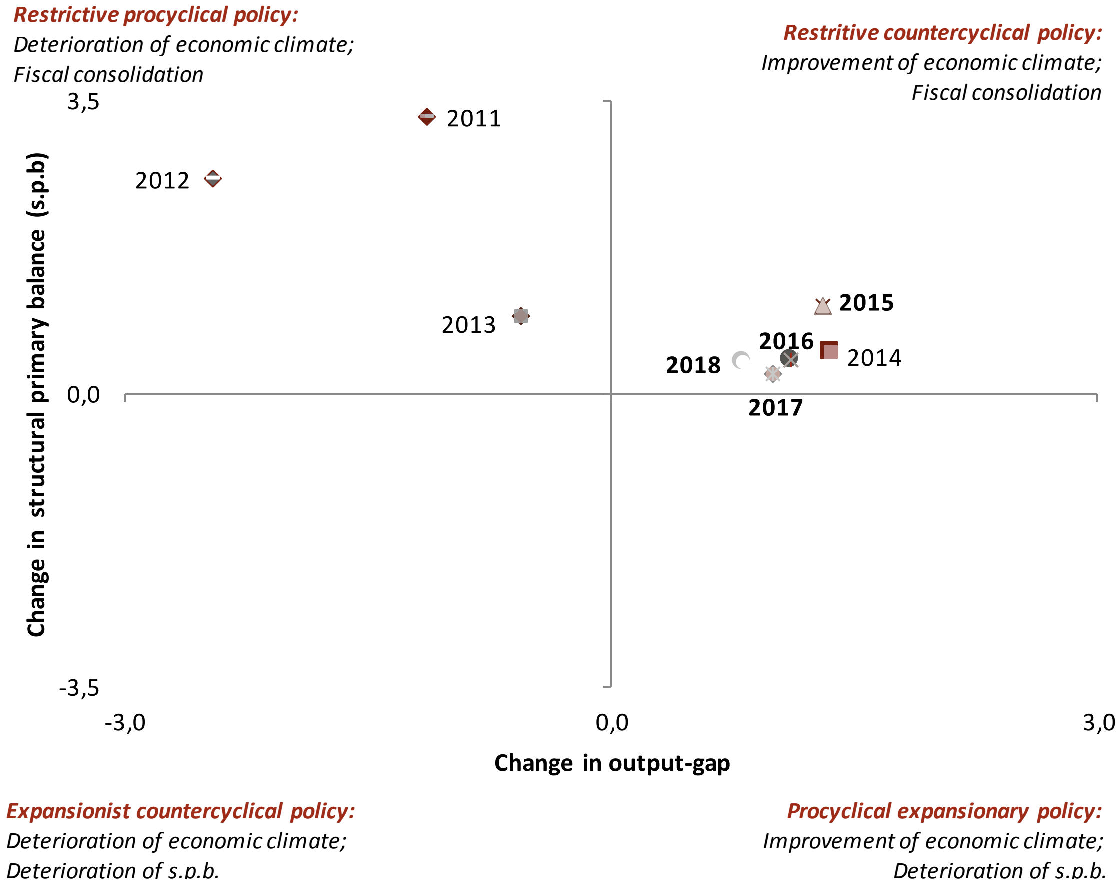
Table 5 – Budget indicators

	% of GDP							Annual change (p.p. of GDP)						
Budget balance	2010	2013	2014	2015	2016	2017	2018	2014	2015	2016	2017	2018	2010-13	2013-18
Primary (EDP)	**-7.0**	**-0.6**	**0.4**	**1.8**	**2.7**	**3.4**	**4.2**	**1.0**	**1.4**	**0.9**	**0.7**	**0.7**	**6.4**	**4.8**
Actual (headline), EDP	**-9.8**	**-4.9**	**-4.0**	**-2.5**	**-1.5**	**-0.7**	**0.0**	**0.9**	**1.4**	**1.0**	**0.8**	**0.7**	**4.9**	**4.9**
Adjusted of temporary & one-off measures	-10.2	-5.3	-4.2	-2.5	-1.5	-0.7	0.0	1.1	1.7	1.0	0.8	0.7	4.9	5.2
Adjusted of temporary & one-off measures & special factors	**-8.7**	**-5.3**	**-4.2**	**-2.5**	**-1.5**	**-0.7**	**0.0**	**1.1**	**1.7**	**1.0**	**0.8**	**0.7**	**3.4**	**5.2**
Cyclically adjusted	-9.3	-2.4	-2.1	-1.3	-0.8	-0.5	-0.2	0.3	0.8	0.5	0.3	0.3	6.8	2.3
Structural	-9.6	-2.8	-2.4	-1.3	-0.8	-0.5	-0.2	0.4	1.1	0.5	0.3	0.3	6.8	2.6
Structural net of special factors	**-8.1**	**-2.8**	**-2.4**	**-1.3**	**-0.8**	**-0.5**	**-0.2**	**0.4**	**1.1**	**0.5**	**0.3**	**0.3**	**5.3**	**2.6**
Structural primary	-6.8	1.5	2.0	3.0	3.4	3.7	4.0	0.5	1.1	0.4	0.2	0.4	8.3	2.6
Structural primary net of special factors	**-5.3**	**1.5**	**2.0**	**3.0**	**3.4**	**3.7**	**4.0**	**0.5**	**1.1**	**0.4**	**0.2**	**0.4**	**6.8**	**2.6**
memo items														
temporary measures	0.3	0.3	0.2	0.0	0.0	0.0	0.0	-0.1	-0.2	0.0	0.0	0.0	0.0	-0.3
special factors	-1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.5	0.0
temporary measures & special factors	-1.1	0.3	0.2	0.0	0.0	0.0	0.0	-0.1	-0.2	0.0	0.0	0.0	1.5	-0.3
output gap*	-1.2	-5.3	-4.0	-2.7	-1.6	-0.6	0.3	1.4	1.3	1.1	1.0	0.8	-4.2	5.6
cyclical component	-0.5	-2.5	-1.8	-1.2	-0.7	-0.3	0.1	0.6	0.6	0.5	0.5	0.4	-1.9	2.6
interest payments (EDP)	2.8	4.3	4.3	4.3	4.2	4.1	4.2	0.1	0.0	-0.1	-0.1	0.1	1.5	-0.1

Source: INE, MF, European Commission. CFP calculations. Note: * as percentage of potential output. The cyclical component was calculated using the Community method of semi-elasticities on the basis of the MF output gap; (i) The temporary and one-off measures and special factors relating to 2010-18 are given in Table 11 in the Annex; For the period 2014-18 the CFP did not include as temporary measures in 2014 the loss of revenue resulting from the investment tax credit nor the impact of compensation under termination by mutual agreement (for which the MF estimates a net impact of 0.3% of GDP). In 2015 revenue from concession agreements expected to be signed that year was not included. (iii) Due to rounding the changes do not necessarily correspond to the differences between the percentage GDP figures.

In structural terms the improvement in the primary balance will continue to occur under a restrictive fiscal policy, now pursued in an improved economic climate (counter-cycle). From 2011-13 the fiscal policy assumed a restrictive and pro-cyclical nature to the extent that the improvement in the primary structural balance of 6.8 p.p. of GDP occurred at the same time as the deterioration in the economy (a cumulative decrease in real growth in output of 5.9 p.p. of GDP). From 2014 onwards, the FSD budget projection points to the continuity of a restrictive fiscal policy, although in a favourable economic cycle. According to the MF forecasts the increase in the primary structural surplus, from 2013-18 (2.6 p.p. of GDP), will benefit from the economic recovery and growth, which will be essential to achieve the MTO.

Chart 10 – Fiscal stance and cyclical position [2011-2018]



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

The new output gap methodology benefits the structural balance, bringing it closer to the MTO.[28] The figures used in this report are based on the new methodology adopted by the European Commission. The application of the new method to determine the cyclical component of the budget balance points to an improvement in the structural balance compared to that used in the latest budgetary forecast document. Based on information provided by the European Commission, the impact of the new methodology on the output gap for 2013 and 2014 is -1 p.p. and -0.9 p.p., respectively. This change has a favourable impact on the structural balance estimated at 0.5 p.p. of GDP in 2013 and 0.4 p.p. of GDP in 2014, bringing it closer to the MTO.[29] Therefore, from 2013 to 2017 the necessary structural adjustment to achieve the MTO will be 2.3 p.p. of GDP.

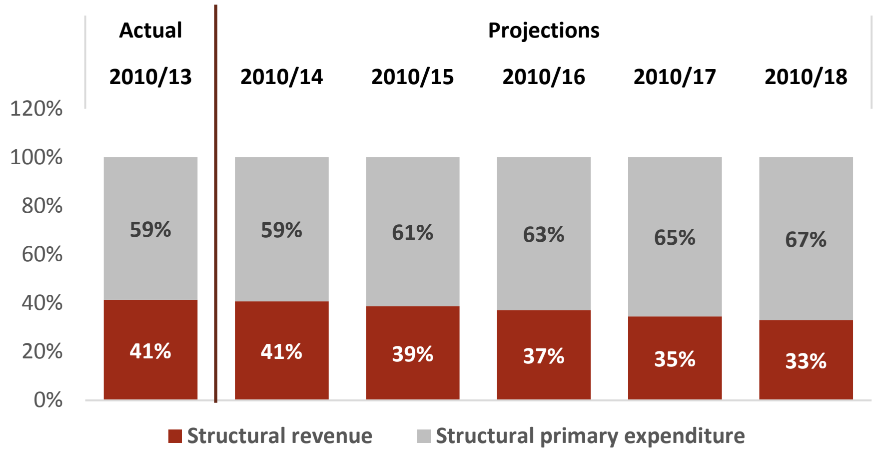
[28] The change in the methodology for calculating the output gap may be found in European Economic Forecast – Spring 2014, Box *I.1: The revised methodology for calculating output gap*. The change stems from the general use of the method to estimate structural unemployment (non-cyclical component of unemployment), a variable that influences the calculation of the potential economic growth rate, and impacts on the calculation of the output gap and the structural balance estimate.

[29] However this change does not impact on the EDP assessment in progress.

5.3 BREAKDOWN OF ADJUSTMENT EFFORT

The MF predicts that two thirds of the fiscal consolidation effort up to 2018 will be explained by the decrease in primary expenditure. The FSD/2014 projection points to a growing contribution from primary expenditure to the decrease in the structural primary deficit. The forecast is for a cumulative contribution from 2014 to 2018 of 9 p.p., going from the 59% recorded up to 2013 to the 67% that is expected up to 2018. The distribution of the effort implicit in the fiscal projections will arise, above all, from the a declining primary current expenditure, in particular from compensation of employees and social transfers, in contrast with the stabilisation of capital expenditure from 2016.

Chart 11 – Fiscal consolidation effort, evaluated in structural terms
Cumulative breakdown of the structural adjustment implicit in the FSD 2014-2018



Source: INE and MF. CFP calculations. | Note: The fiscal consolidation effort corresponds to the improvement in the structural primary balance net of the impact of special factors. The structural figures are net of the effects of the economic cycle and of temporary and one-off measures and special factors.

Once the Excessive Deficit Procedure ends in 2015, achieving the MTO in 2017 will require the definition of discretionary measures that are not identified in the FSD/2014. The fiscal consolidation measures identified and quantified in the FSD/2014 and analysed in detail in the next section, only cover 2014 and 2015, that is to say, until the excessive deficit situation is corrected. Taking as a reference the change in the structural primary balance, which is an indicator of discretionary measures, the FSD/2014 forecast also points to an improvement in that balance of 0.6 p.p. of GDP from 2015-17, resulting essentially from the decrease in primary expenditure (-0.8 p.p. of GDP).

Table 6 – Structural budgetary adjustment indicators (% of GDP)

	Actual		FSD 2014-2018					Annual change p.p. of GDP						
	2010	2013	2014	2015	2016	2017	2018	2014	2015	2016	2017	2018	2013/15	2015/17
Structural Revenue net of S.F.	39.9	42.8	42.9	43.2	43.2	43.0	43.0	0.2	0.3	0.0	-0.2	0.0	0.4	-0.1
Structural Expenditure net of S.F.	48.1	45.5	45.3	44.5	44.0	43.5	43.2	-0.3	-0.8	-0.5	-0.5	-0.3	-1.1	-1.0
Primary Expenditure	45.3	41.3	40.9	40.1	39.8	39.4	39.0	-0.3	-0.8	-0.4	-0.4	-0.4	-1.1	-0.8
Interest paid	2.8	4.3	4.3	4.3	4.2	4.1	4.2	0.1	0.0	-0.1	-0.1	0.1	0.1	-0.2
Structural budget balance net of S.F.	-8.1	-2.8	-2.4	-1.3	-0.8	-0.5	-0.2	0.4	1.1	0.5	0.3	0.3	1.5	0.8
Structural primary balance net of S.F.	-5.3	1.5	2.0	3.0	3.4	3.7	4.0	0.5	1.1	0.4	0.2	0.4	1.6	0.6

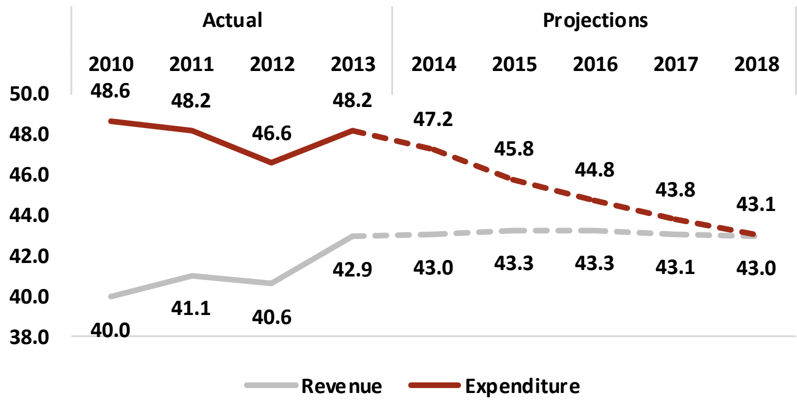
Source: INE and MF. CFP calculations. | Note: see note to Table 5.

5.4 BUDGET AGGREGATES

5.4.1 Revenue and expenditure developments

The fiscal projections underlying the FSD/2014 show an adjustment path which reflects a convergence between the relative weight of revenue and expenditure in GDP, at the end of the forecast time horizon. The MF estimates that a budget balance will be achieved in 2018, as a result of adjusting public expenditure to the expected level of revenue in that year. However, the FSD continues to be insufficiently clear as regards the strategy underlying the adjustment (on both the economic and fiscal terms) and the magnitude of the measures required to achieve the stated targets.

Chart 12 – Adjusted revenue and expenditure forecasts (as % of GDP)



Source: INE and Ministry of Finance. CFP calculations.

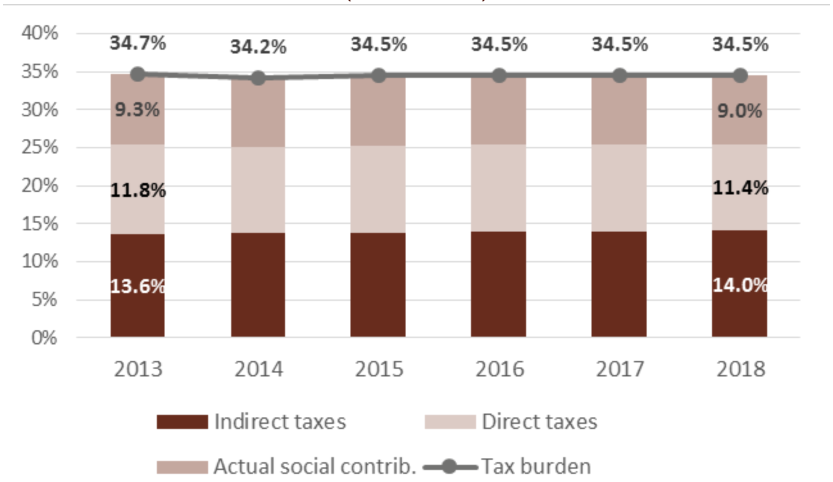
Throughout the time horizon of the FSD/2014 the MF foresees an increase of the revenue-to-GDP ratio by 0.1 p.p. In 2013 total GG revenue accounted for 42.9% of GDP in adjusted terms. The forecasts set out in the FSD/2014 point to progressive increase of this aggregate's weight up to 2016 (43.3%), after which it will fall to 43% of GDP in 2018. Notwithstanding the less expressive increase in the relative weight of total revenue in GDP, a change in the breakdown is expected to occur in 2018 compared to 2013. The 0.1 p.p. of GDP increase will result from a 0.7 p.p. growth in tax revenue, 0.3 p.p. in other revenue and 0.1 p.p. in capital revenue, offset by the decreases in social transfers and the sale of goods and services by -0.8 p.p. and -0.2 p.p. respectively.

Tax revenue will grow at a rate slightly above nominal GDP and is expected to reach 25.5% of GDP in 2018, which contrasts with the 24.8% in 2013. This change is expected to occur over the entire period of the projection, with the exception of 2016, but will be particularly significant in 2014 and 2015. Indirect taxes are the only component of tax revenue that records an increase up to 2017. In this context the MF anticipates its relative weight in GDP to increase by 0.3 p.p. in 2014, 0.2 p.p. in 2015 and 0.1 p.p. in 2017 – the year in which it will reach approximately 14% of GDP. The MF expects a decline in direct taxes of around 0.1 p.p. of GDP in 2014, to a relative weight of 11.3% of GDP, stabilizing in subsequent years at around 11.4%.

The FSD/2014 assumes the retention of high levels of taxation up to 2018. The MF forecasts a decrease in the (non-adjusted) tax burden of 0.5 p.p. of GDP in 2014 (34.2% of

GDP), followed by stabilisation at around 34.5% of GDP in the following years. That stability will be the result of a decrease in the relative weight of actual social contributions (- 0.3 p.p.), offset by the rise in indirect taxes (+ 0.4 p.p.).[30]

Chart 13 – Change in headline tax burden
(as % of GDP)



Source: MF. CFP calculations.

On the expenditure side the MF forecasts a fall of 5.1 p.p. of GDP from 2013 to 2018, with GDP growth more than offsetting the nominal growth in expenditure. Adjusted public spending as a percentage of GDP will fall over the entire time horizon, being particularly sharp in 2015 (-1.4 p.p.) and will then slow down. In 2018 it is expected to total 43.1% of GDP, equal to the 2002 figure. However, the MF only expects a decrease in spending in nominal terms in 2014 and 2015.

From 2013 to 2018 the planned change in expenditure is based essentially on the decrease in primary expenditure. The largest contribution will come from compensation of employees (-2.3 p.p. of GDP), which in 2018 should stand at a record low of 8.5% of GDP.[31] The MF also forecasts a drop in relative weight of social transfers (-2.3 p.p. of GDP). Intermediate consumption will contribute to the drop of expenditure ratio (-0.4 p.p. of GDP), totalling 4.0% in 2018, the lowest level since 1995. Subsidies, other current expenditure and capital expenditure should make only a marginal contribution to the decrease in spending (- 0.1 p.p. of GDP).

The change in interest will make a marginal contribution to the decrease in spending (-0.1 p.p. of GDP). After a strong growth from 2010 to 2012 (from 2.8% to 4.3% of GDP), it is forecasted that interest payments will stabilise from 2013 onwards and there will be a slight fall in 2016. This reflects, in part, the decrease in the forecast medium-term public debt ratio.

[30] Note however that without the impact of the ESSD, direct taxes in 2013 would have a relative weight of 11.4% in GDP, and that is why stabilisation is expected over the period of the projection.
[31] The last figure available in the AMECO database is from 1977 (8.9% of GDP) and the lowest recorded level was in 1979 (8.8% of GDP).

5.4.2 Consistency of fiscal projections

This section of the report analyses the consistency of the fiscal projections for 2014 and 2015 with the impact of the measures set out in the FSD/2014. Note that in the opinion of the MF the effect of the measures identified in the FSD/2014 should always be compared with the previous year's outturn (and not with a non-policy fiscal scenario). The inadequate description of what the FSD deems to be fiscal pressures (increases in outlays and reductions in revenues that are beyond the Government's control) makes a full assessment of the forecasts contained in FSD/2014 impossible. In this respect it is important for the MF to identify the impact of the increase in expenditure associated with the pension systems and the Public-Private Partnerships (PPP).[32] *The fact the measures for the period after 2015 are not specified hinders the transparency and the credibility of the published forecasts as well as the respective assessment.*

The FSD/2014 contains unspecified fiscal consolidation measures. In 2014 they amount to 1 144 M€ (0.7% of GDP) and in 2015 to 517 M€ (0.3% of GDP), which corresponds to around a third of the permanent measures. This sum relates to measures for which no specific information is given regarding their nature and composition, and consequently their impact cannot be assessed. More detailed analysis of the measures published in Fthe SD/2014 can be found in Box 2.

CFP recommends that when the draft SB/2015 is submitted it should include more detailed fiscal consolidation measures. The major measures should be broken down (for example, "other sectorial measures") and accompanied by an operational explanation of how they will be implemented. On the other hand, a governance model should be defined and disclosed for the consolidation measures to be taken that year be defined and disclosed, specifying the following items for each measure: nature, coordinating entity(ies), executing entity(ies), implementation schedule and fiscal impact (identifying the outlay where the respective effect is expected). This procedure would enhance the credibility of fiscal planning and improve monitoring and the possibility of making adjustments over the year.

[32] Although the CFP requested this information from the MF it was not supplied.

Revenue developments

The MF expects that total revenue up to 2018 to be based essentially on an improvement in tax revenue that will offset the forecast drop in the other revenue items. From 2013 to 2018, the MF foresees an increase in tax revenue of around 0.7 p.p. of GDP, which will be more significant in 2014 (0.2 p.p. of GDP) and 2015 (0.3 p.p. of GDP). This change corresponds to an increase of 1 173 M€ and 1 469 M€ in 2014 and 2015, respectively.

The change in indirect taxes revenue is higher than the impact of the consolidation measures set out in the FSD/2014. In 2014 the fiscal consolidation measures set out in the FSD/2014 foresee increments of 0.1% of GDP (170 M€), which clearly show that there must be other, reasonably large factors that justify the predicted change (976 M€), in particular the expected economic recovery (the nominal change in private consumption is estimated at 1.9%). In 2015 the change in indirect taxes revenue (768 M€) is also higher than the consolidation measures amounting to 250 M€ (0.1% of GDP). This increment reflects an increased tax burden, based on the 0.25 p.p. rise in the standard rate of VAT (to be levied on the pension systems), which will have an estimated impact of 150 M€, and on a rise in specific taxes on consumption, corresponding to 100 M€.[33,34] However, this latter measure is not described in detail, which brings added risks and uncertainties to the achievement of the fiscal targets.

The estimated impact of the measures relating to direct taxes is residual when compared with the expected revenue. In 2014 the MF forecasts a 197 M€ rise in direct taxes revenue, which compares with an unfavourable impact of -15 M€ resulting from the measures to be carried out and may reflect a slight improvement in the level of employment (0.9%). Note that the figure of -15 M€ results from an impact of 240 M€, stemming from insufficiently specified measures, being more than offset by an adverse effect of 255 M€, due to the reversal of the transitory measures relating to compensation of employees and social transfers. The following year an increase of 701 M€ (+3.7%) is expected although specified measures only contribute 37 M€. The difference reflects, in part, an improvement in the wage bill which the MF estimates will increase by 1.6% in 2015. As for the remainder, and given the scale of the measures adopted, some uncertainty over the projection for this item is justified. It is also important to state that, according to the information received from the MF, that projection does not reflect possible losses from the CIT reform[35] and the overall impact of the PIT reform still remains to explain.

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[33] The specific taxes on consumption include the Tax on Oil and Energy Products (ISP), the Tax on Alcohol and Alcoholic Beverages (TAAB) and the Tax on Tobacco (TT).

[34] The indirect taxes forecast does not identify the impact of the Green Taxes Reform. The FSD/2014 and the State Reform Guidelines only refer to expectations in economic terms. Note that one of the goals is revenue source diversification, which supposes an increase in revenue from this source.

[35] The CIT Reform Committee held that this could involve, at least in the short run, a negative impact on estimated collected revenue of around 314.1 M€. In this regard it should also be mentioned that a medium-term fiscal strategy should explicitly take into account the Government's economic strategy and the effects of economic policies that have structural aims over the same period, even if the main political driving force is the sectorial ministries, given that permanent changes in the revenue base or in the way goods and services are provided may be at stake. That prospective assessment should be undertaken while maintaining a prudent and transparent analysis of the predictable impact on budget targets.

The scenario set out in the FSD suggests a slight recovery of social contributions revenue in 2014 (20 M€) and 2015 (234 M€). The forecast published in the FSD/2014 includes consolidation measures that have an estimated net impact of 164 M€ and 162 M€ in 2014 and 2015, respectively. In 2014 the increase in the ADSE, ADM and SAD beneficiaries' contribution rates, estimated to be 261 M€, partially offset by the negative impact of the worsening of the earnings reduction (-133 M€), will not be sufficient to produce a significant increase in this item. The social contributions revenue also reflects an expected impact of 31 M€ from Social Security inspections and enforced collection, plus 5 M€ from other measures that cannot be evaluated because no detail is provided. The increase in 2015 (234 M€) reflects the 0.2 p.p. rise in the employees' contribution to social welfare systems (100 M€), as well as the carry-over effect of contributions to health subsystems due to the law coming into force later than originally forecasted (75 M€), plus the 8 M€ increase in ADSE revenue from the restoring of wages. Note also that the annual change in imputed contributions does not always match the forecast for civil servants wages and salaries.[36]

The MF forecast for sales and other revenue points to a rise in 2014 and 2015. For 2014 consolidation measures worth 329 M€ are forecasted, a figure which is higher than the estimated change in this aggregate (212 M€). In this context inflows of 199 M€ are foreseen from the optimisation of the use of European funds in the Employment and Social Security subsectors. Given the scale of the impact of the measure and the lack of details, uncertainty as to its quantification is justified. Mention should also be made of other measures in the SB/2014 to sum of 67 M€, of which there is an unexplained sum of -20 M€ in the FSD. For 2015 of the expected change of 378 M€, only 65 M€ are explained by measures, 50 M€ of which are unspecified.

[36] For example in regard to 2015 the estimated decrease in imputed contributions stands at 6.9%, while civil servants' wages are expected to fall by 3.5%.

Table 7 – Adjusted general government account and fiscal consolidation measures for 2014 and 2015 (M€ and as % of GDP)

	Adjusted figures M€					Measures M€		Measures % of GDP	
	2013	2014	2015	13/14	14/15	2014	2015	2014	2015
Total revenue	**71 130**	**72 711**	**74 831**	**1 580**	**2 121**	**648**	**514**	**0.4**	**0.3**
Current revenue	**69 628**	**71 033**	**73 113**	**1 405**	**2 081**	**648**	**514**	**0.4**	**0.3**
Tax revenue	41 045	42 218	43 687	1 173	1 469	155	287	0.1	0.2
Indirect taxes *	22 213	23 189	23 957	976	768	170	250	0.1	0.1
Direct taxes	18 832	19 029	19 730	197	701	-15	37	0.0	0.0
Social contributions	19 905	19 926	20 159	20	234	164	162	0.1	0.1
of which: actual	15 097	15 481	16 023	384	542	164	162	0.1	0.1
Sales and other current revenue	8 677	8 889	9 267	212	378	329	65	0.2	0.0
Capital transfers received	**1 503**	**1 678**	**1 718**	**175**	**40**	**0**	**0**	**0.0**	**0.0**
Total expenditure	**79 831**	**79 799**	**79 197**	**-32**	**-602**	**-2 778**	**-823**	**-1.6**	**-0.5**
Primary expenditure	**72 767**	**72 475**	**71 716**	**-293**	**-759**	**-2 778**	**-823**	**-1.6**	**-0.5**
Current primary expenditure	69 444	68 770	67 993	-674	-777	-2 466	-798	-1.5	-0.5
Intermediate consumption	7 308	7 746	7 402	438	-343	-460	-537	-0.3	-0.3
Compensation of employees **	17 789	16 370	15 805	-1 419	-565	-1 207	-187	-0.7	-0.1
Social transfers	38 834	38 657	38 751	-177	94	-598	76	-0.4	0.0
Other than in kind	31 229	31 063	31 356	-166	293	-577	289	-0.3	0.2
In kind	7 605	7 594	7 394	-11	-200	-21	-213	0.0	-0.1
Subsidies	1 117	1 201	1 190	84	-11	-153	-99	-0.1	-0.1
Other current expenditure	4 397	4 796	4 845	400	49	-48	-51	0.0	0.0
Capital expenditure	3 324	3 705	3 723	382	18	-311	-24	-0.2	0.0
Interest paid (EDP)	**7 064**	**7 324**	**7 481**	**260**	**157**	**0**	**0**	**0.0**	**0.0**
Balance (EDP)	**-8 701**	**-7 088**	**-4 366**	**1 613**	**2 722**	**3 426**	**1 337**	**2.0**	**0.8**
Primary balance (EDP)	**-1 637**	**236**	**3 115**	**1 873**	**2 880**	**3 426**	**1 337**	**2.0**	**0.8**
GDP at current market prices	**165 666**	**168 906**	**172 935**						

Source: Ministry of Finance. CFP calculations. | Notes: * The makeup from the revenue side measures is different to that published in FSD/2014: in 2015 the sum of 100 M€ relating to "Specific taxes on consumption" was included whereas the MF classified the measures as "Other revenues". ** The figure for compensation of employees does not include the effect of imputed contributions (~28.4% of the amount).

Expenditure developments

The nominal decrease in primary expenditure is substantially less than the impact of the measures presented. Total permanent measures on the expenditure side for 2014 were revised vis-à-vis the SB/2014 figure (going from 3 184 M€ to 2 778 M€). Nonetheless, primary expenditure should fall by just 293 M€, which suggests a significant fiscal pressure. Whereas in 2015, the MF foresees a decline in primary expenditure of 759 M€, which seems to be consistent with the measures amounting to 823 M€.

In 2014 and 2015 overall compensation of employees falls in line with the impact of the measures presented. In 2014, this account will record a fall (-1 419 M€) that corresponds globally to the effect of the measures announced (-1 207 M€, plus the effect of imputed contributions) but is partially offset by employment termination compensations. In 2015 the MF foresees a decrease (-565 M€) in compensation of employees which is explained by the published measures (-187 M€) and by the baseline effect (around 300 M€) associated with the cost of termination of employment compensation in 2014 that will not be repeated in 2015. On the contrary, from 2016 to 2018 the MF estimates an increase in this spending, suggesting that the gradual restoring of the cut in compensation of employees or the unfreezing of promotions will have a fiscal impact that will not be totally offset by a significant medium-term decrease.

A decrease in expenditure on social transfers is only forecasted in 2014. The decrease in spending estimated by the MF (-177 M€) is less than the published total impact of the measures (-598 M€), probably as a result of unspecified fiscal pressures. In 2015, the published value of the measures (76 M€) is consistent with the forecast increase in social transfers (94 M€); this suggests that the increased pension outlays will be offset by a favourable change in the automatic stabilisers (decline in unemployment benefits).

The development in intermediate consumption is less significant than the value of the measures for 2014 and 2015. In 2014 expenditure rises (438 M€), despite the high value of the measures planned for that year (-460 M€). While in 2015, despite the MF foreseeing a cut in expenditure (-343 M€), it will be less than the impact of the measures (-537 M€). Those differences may be due to fiscal pressures (for example, the increase in the cost of PPP) the value of which, although requested, was not provided by the MF.

The increase in subsidies, other current expenditure and capital expenditure does not appear to be consistent with the value of the measures. Together these accounts produce an increase in 2014 and 2015 (865 M€ and 56 M€, respectively) although the MF estimates a substantial set of fiscal consolidation measures to be carried out (-512 M€ and -174 M€). This large disparity should be explained in the FSD/2014.

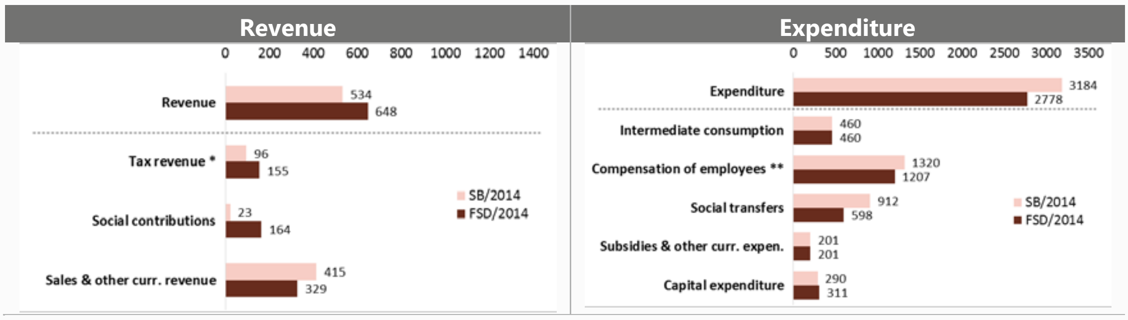
Box 2 – Fiscal consolidation measures

Consolidation measures for 2014

In order to reduce the deficit adjusted for the impact of temporary and one-off measures from 5.3% of GDP in 2013 to 4% in 2014, the Government revised the fiscal consolidation measures to be adopted (estimated at 2.1% of GDP, i.e. 3 558M€) of which 3 426 M€ correspond to permanent measures and 132 M€ to occasional measures. That accounts for a decrease of 0.2 p.p. (343 M€) compared to the figure of 2.3% in the SB/2014 Report. Such decrease is explained by a more favourable starting point of the adjusted deficit (0.5 p.p. of GDP), by the positive impact of the economic outlook (0.8 p.p. of GDP) and by a less negative impact of fiscal pressures (1.1 p.p. of GDP).

The fiscal pressures forecast in the SB/2014 totalled 1% of GDP and have more than doubled in the FSD (2.2 % of GDP). The MF explains this as a consequence of a set of specific effects in 2013 that should not be carried forward into 2014, of new risks revealed by the cumulative budget outturn up to March, namely in terms of Social Security and CGA revenues, and of the effect of the Extraordinary Investment Tax Credit (0.1% of GDP) in 2014 versus 2013. This last fact shows that the foreseeable effects for 2014 were not fully reflected in the original MF forecast.

Chart 14 – Permanent fiscal consolidation measures in 2014 (M€)



Source: Ministry of Finance.

The net impact of the consolidation measures to be carried out on the **revenue** side stands at 648 M€, equal to 18.9%[37] of the total permanent measures planned for 2014. The new estimates reflect an upward revision of the expected impact of the revenue side measures of around 114 M€, due in essence to the increase in the civil servants' health subsystems contribution rates[38] and a smaller decrease in tax revenue stemming from the decision that the measure that provided for the convergence of the CGA pensions calculation formula with the Social Security formula is unconstitutional. The net effect of the measures impacting on the tax and social security contributions revenue should be 155 M€ and 164 M€, respectively.

As regards **direct taxes** not all the consolidation measures are specified. In this context there is an estimated loss of 15 M€ (resulting from measures relating to compensation of employees and social transfers).[39] According to the MF, the projections reflect the unfavourable impact of 0.1 p.p. of the Extraordinary Investment Tax Credit. As per **indirect taxes**, the MF predicts fiscal consolidation measures of 170 M€.

The scenario presented in the FSD/2014 foresees consolidation measures with a net impact of 164 M€ on **contributory revenue**. The upward revision of the revenue in social contributions of 129 M€ compared to the SB/2014 reflects the effects of the increase in the ADSE, ADM and SAD beneficiaries' contribution rates, to offset the effect of the Constitutional Court's (CC) decision that the pensions convergence measure was unconstitutional.[40] Social contribution revenue also reflects an unexpected impact of 31 M€ relating to Social Security inspections and enforced collection and of 5 M€ relating to other measures that cannot be evaluated due to lack of details.[41] Consolidation measures that have significant impact on revenue levels include those relating to other revenue valued at 329 M€.

On the **expenditure** side the impact of the measures was revised downwards to 2 778 M€. The largest adjustment (406 M€) was made to **social transfers** (314 M€), mainly due to the CGA pensions measure proving to be unviable. In December 2013, the CC declared the convergence of CGA and Social Security pensions to be unconstitutional, which had a gross impact of 388 M€. This measure was offset, only partially (67 M€) on the expenditure side by lowering the minimum threshold at which the Extraordinary Solidarity Contribution is payable (which went from 1 350 € to 1 000 €).

In terms of **compensation of employees**, special mention is made of the sharp downward revision in the impact of employment termination (-42 M€) and requalification programmes (-50 M€). It must be stressed that it is not possible to identify the reason for the inadequate application of these measures due to the absence of specified sectorial goals in the SB/2014 and in the FSD/2014. Changes to the draft SB/2014 are also identified that restrict the application of the cut in earnings to the lowest salaries (-21 M€), offset by unspecified **investment** measures (+21 M€).

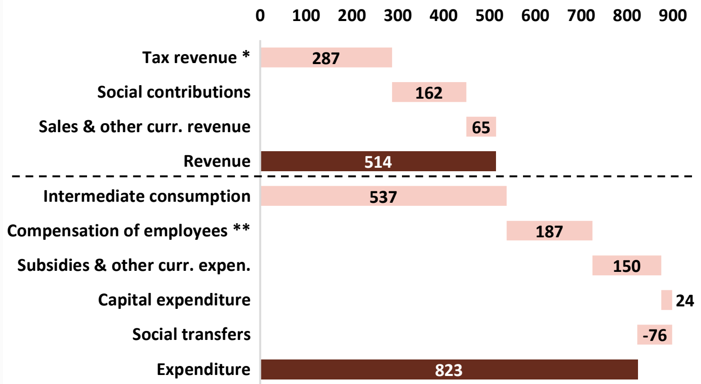
Consolidation measures for 2015

The MF estimates that in 2015 additional fiscal consolidation measures of around 0.8% of GDP (1 378 M€) will be needed.[42] The net impact of consolidation measures to be implemented on the revenue side stands at 514 M€, 38.4% of total permanent measures in 2015. On the expenditure side, measures published amount to 823 M€. Total measures forecast for 2015 (1 378 M€) are a mix of the following impacts: (i) measures agreed under the 11th regular review (1 414 M€); (ii) the net effect of the gradual reversal of the transition measures (-708 M€) and (iii) the introduction of compensatory measures and effects of that reversal (672 M€). The 115 M€ impact on tax and social security contributions revenue stems from the decision to return 20% of the civil service pay cut and the net effect of the measure abolishing the

[37] In SB/2014 this sum totalled 534 M€.
[38] ADSE, SAD and ADM.
[39] In SB/2014 the loss was 74 M€, while in the FSD it is 15 M€.
[40] Note that these beneficiaries' contributions went from 1.5% to 2.25% in 2013, to 2.5% from 1st January 2014 and became 3.5 % from 1st June 2014.
[41] Note that the inspections and compulsory payments are strategies to encourage voluntary compliance with the law, so that non-fulfilment of contributory obligations runs a high risk of detection and penalty. These actions are strategic goals in the inspection and enforced collection fields, rather than fiscal consolidation measures.
[42] Includes 41 M€ of occasional measures.

Extraordinary Solidarity Contribution. Note that the sum of 1 378 M€ includes 41 M€ of occasional measures.

Chart 15 – Permanent fiscal consolidation measures for 2015 (M€)



Source: Ministry of Finance. | Notes: *It was decided to include here 100M€ of "Specific taxes on consumption" in 2015, unlike the MF which classified this measure as "Other revenue". **Does not include the effect of imputed contributions (~28.4% of the amount).

As regards **indirect taxes** the MF fiscal consolidation measures account for 0.2% of GDP (250 M€), corresponding essentially to the 0.25 p.p. rise in the standard VAT rate. As for **direct taxes** the MF reports an impact of 37 M€ (resulting from the reversal of the measures). In this item the overall impact of the PIT reform over the projection time frame is not identified.

The increase in employees' contributions to social welfare systems carries significant weight, accounting for a 19.5% rise in expected revenue in 2015. The FSD/2014 estimates revenue of 100 M€ from **social contributions**, resulting from the 0.2 p.p. increase in the employees' charge in the CGA and Social Security systems. This revenue is intended to offset, in part, the cancelling of the Extraordinary Solidarity Contribution, which has been deducted from pension's expenditure. Still in regard to social contributions, the MF estimates a carry-over effect due to the legislation coming into force later than the date originally foreseen (75 M€).

The consolidation measures relating to **other revenue** stand at 65 M€, of which 50 M€ are not specified. The change in revenue is contingent on the impact of those measures being correctly estimated by the MF, which constitutes an additional risk factor in the public finance consolidation process.

The forecast measures on the **expenditure** side total 823 M€ and are due to policy changes with opposite effects. On the one hand, a 514 M€ increase in spending is expected as a result of the reversal of current measures: the Extraordinary Solidarity Contribution will be replaced by the sustainability contribution (net impact of -289 M€)[43] and the partial reversal of the current pay cut (225 M€). On the other hand, these effects will be more than offset by measures totalling 1 337 M€.

The largest saving comes from the measures with a bearing on **intermediate consumption** where the impact is 537 M€. For Information and Communications Technology (138 M€) there is a strategic plan with 25 specific measures aimed at reducing spending.[44] However, around 400 M€ of the measures lack the operational details required to assess their feasibility: reduced spending on studies, professional opinions and other items (179 M€), the "Get Closer Programme"[45] (30 M€) and other sectorial measures (190 M€).

[43] The result of the abolishing of ESC (-660 M€), partially offset by the sustainability contribution (372 M€). It is assumed that this measure is also recorded as expenditure in the national accounts.
[44] The Overall strategic plan for the rationalisation and cost cutting of General Government ICT began to be implemented in early 2012 and was based on a diagnosis report produced in 2011.
[45] The Council of Ministers Resolution on the "Get Closer" (*Aproximar*) Programme only sets out the general aims.

Social transfers in kind are expected to contribute 213 M€ to the decrease in expenditure, mainly from the health sector. The MF estimates that the largest impact will come from the cut in pharmaceutical expenditure (200 M€). Although the implementation of this measure carries some risk, since it depends upon negotiations with the pharmaceutical industry, such risk is mitigated by a measure of the same scale to be taken on the revenue side if agreement is not reached.

Compensation of employees is expected to fall by 187 M€[46] following the application of new measures (412 M€) that more than offset the reversal of the pay cut (-225 M€). The largest contribution will come from the reduction in staff numbers due to retirement (190 M€). Nonetheless, the implementation of the remaining measures carry some risks: in the case of the employment termination and requalification programmes (123 M€) the impact has been successively revised downwards; in the case of the programme "Aproximar" and other sectorial measures (100 M€), how the savings will be obtained is not specified. Mention must also be made of other measures that may increase fiscal pressure and whose impact is unknown: the introduction of the Single Pay Scale, the revaluation of supplementary earnings and the unfreezing of promotions.

Measures relating to the **subsidies**, **investment** and **other current expenditure** items are worth 174 M€. In the case of subsidies, of special note is the decrease in compensation payments in the State Corporate Sector (85 M€), although it is stated only that the corporations affected belong to the transport sector. The remaining measures (99 M€) are not specified in the FSD.

5.5 PUBLIC DEBT DEVELOPMENTS

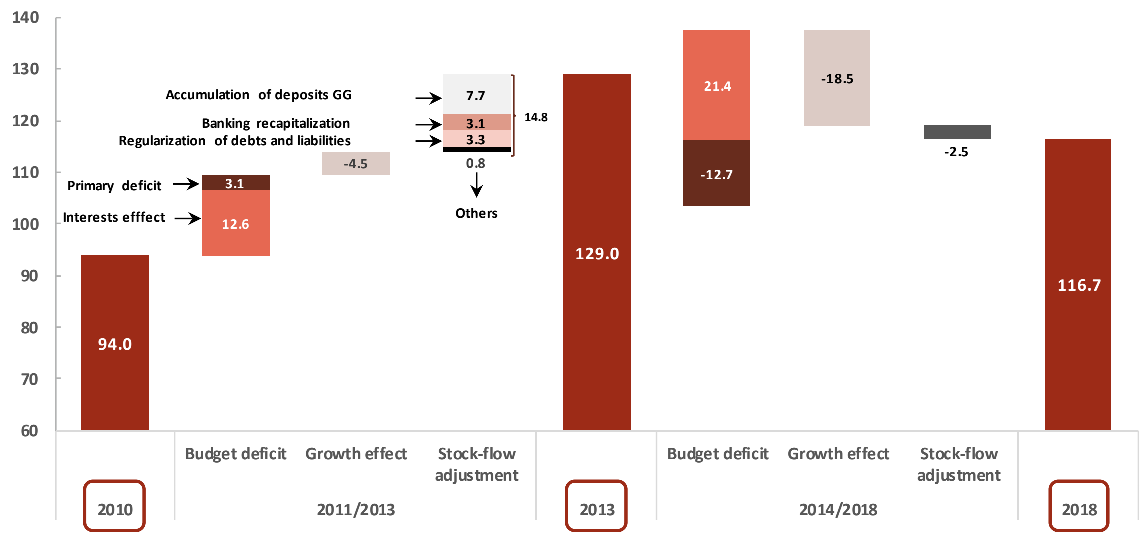
Notwithstanding the publication of an estimate for debt[47] under ESA 2010 in the FSD, the CFP believes there is still uncertainty at the international level as to the application of the ESA 2010 rules that will come into force in September of this year and prudence is recommended when comparing the data forecast in line with this new framework. Therefore they will be evaluated at a later date.

The short and medium-term

The downward path of the debt ratio over the period covered by the FSD/2014 is based on forecast primary surpluses and economic growth. This outlook contrasts sharply with the situation throughout 2010–13, in which there were always primary deficits (a cumulative total of 3.1 p.p. of GDP). Fulfilment of the goals in the FSD/2014 requires a significant fiscal consolidation effort to achieve the primary surpluses indicated therein (a total of 12.7 p.p. of GDP). Note that interest payments is the only item that will worsen the debt ratio over the time horizon of FSD/2014, which will offset around two thirds of the favourable effects expected among the other items that affect debt development[48].

[46] Excluding the impact of imputed contributions on compensation of employees (around 28.4%).
[47] ESA 2010: the next version of the European System of National and Regional Accounts. This system is the methodological framework for computing the accounts of an economy.
[48] The cumulative value of the snowball effect (interest effect + growth effect) contributed to the ratio growth by around 2.9 p.p. of GDP from 2014 to2018.

Chart 16 – Contributions to public debt developments under ESA 95, 2010-2018 (as % of GDP)



Source: INE and Ministry of Finance.

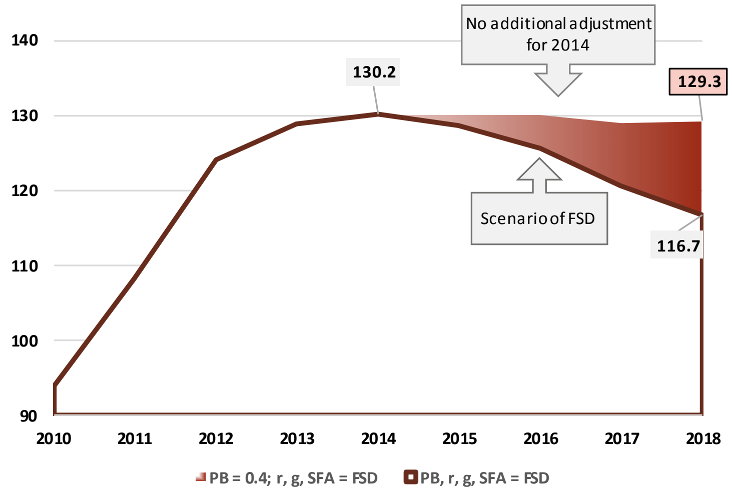
In the FSD/2014 there is no mention of the application of privatization revenues in the repay of debt. Although privatisations that will take place during the period covered by the FSD/2014 are described, the amount that will be used to repay the debt is not stated.[49] For the purposes of transparency, CFP suggests that in future the MF explains the reasons why the amount of revenue from privatisations used to amortise public debt has been practically none.

According to the FSD the stock-flow adjustment for 2014-18 will be significantly lower than in the previous three-year period. In 2014 the stock-flow adjustment will be affected by major contrasting effects. According to the information provided by the MF, in 2014 the increase in debt should reflect borrowing and the taking on debts from NRPC of around 3.1 p.p. of GDP, which should continue to rise until 2016. The MF expects the Social Security Financial Stabilisation Fund to purchase public debt in 2014 to partially offset this effect.

Unless the fiscal consolidation effort continues, it will be impossible to reduce debt and comply with international obligations. If the primary balance remains unchanged at the figure set for 2014 (a surplus of 0.4% of GDP) and considering an implicit interest rate of 4% and the rate of economic growth estimated in the FSD, the debt ratio in 2018 will be practically equal to the figure of 2013 (129.3% of GDP, considering a favourable stock-flow adjustment, or 131.8% of GDP if that effect is not taken into account). However, note that the interest rate assumed herein may not be consistent with a no adjustment scenario that would be penalised by the financial markets.

[49] The financial inflows from the privatisations of CTT and ANA (around 1 500 M€) did not contribute to the decrease in public debt in 2013. The return on these privatisations was only allocated in 2014 by Ministry of Finance Order no. 308/2014 of 8th January (CTT) and by Order no. 358/2014 of 9th January (ANA). FSD/2014 does not state the year in which that revenue will be used to repay debt.

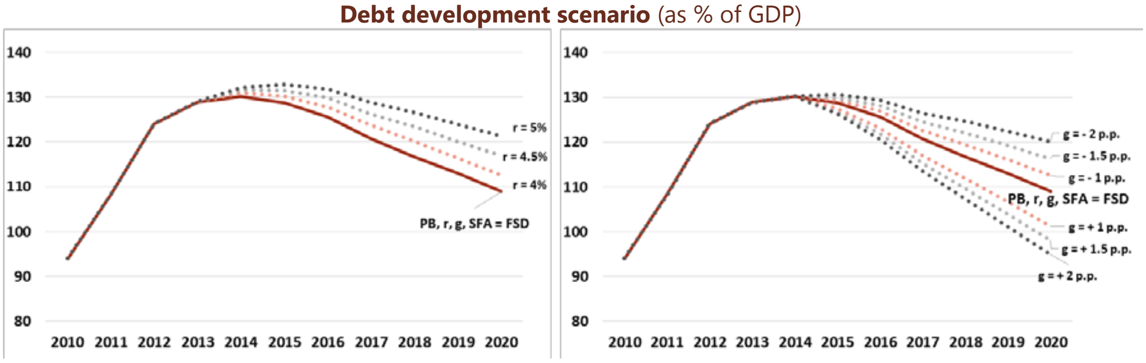
Chart 17 – Sensitivity analysis: scenario of debt development with no additional adjustment vs. 2014
(as % of GDP)



Source: INE, Ministry of Finance. CFP calculations. | Notes: In the scenario of no additional adjustment versus 2014, an interest rate of 4% and the FSD hypotheses for the remaining relevant variables (growth and stock-flow adjustment) were assumed.

The forecast primary surpluses and the achievement of favourable stock-flow adjustments will place the debt ratio on a downward path, even in a more unfavourable macroeconomic climate. Higher interest rates or lower growth than foreseen in the FSD would delay the turnaround in debt ratio, and slow the downward trend, but would not bring it into question in the variants simulated in Chart 18. This conclusion illustrates the importance of achieving the primary surpluses in the period 2014-18.

Chart 18 – Implicit interest rate and growth rate sensitivity analysis
Debt development scenario (as % of GDP)



Source: INE, Ministry of Finance. CFP calculations. | Notes: *PB* stands for primary balance (as % of GDP), *r* the implicit interest rate (as a percentage), *g* nominal GDP growth rate (as a percentage), *SFA* the stock-flow adjustment. In the nominal GDP growth rate sensitivity analysis the scenarios correspond to variations vis à vis the nominal growth forecast in FSD/2014.

The long-term

The FSD/2014 does not provide a long-term debt sustainability analysis. Unlike the FSD/2013, the FSD/2014 does not provide a long-term public debt sustainability analysis which should be accompanied by a suitable analysis of the debt path's sensitivity to the relevant variables. The high levels of public debt and its effects on both public finance and economic activity mean that a decrease in this indicator is a priority for fiscal policy, and a thorough analysis of the risks associated with its progress is justified.

A simulation of the public debt ratio development after 2017 is shown below (assuming the structural balance remains unchanged at the level corresponding to the MTO). When conducting the exercise a nominal interest rate of 4.5% and nominal growth of 3.5% after 2017 were assumed; these values appear to be reasonable given the outlook for long-term growth published by the OECD.[50]

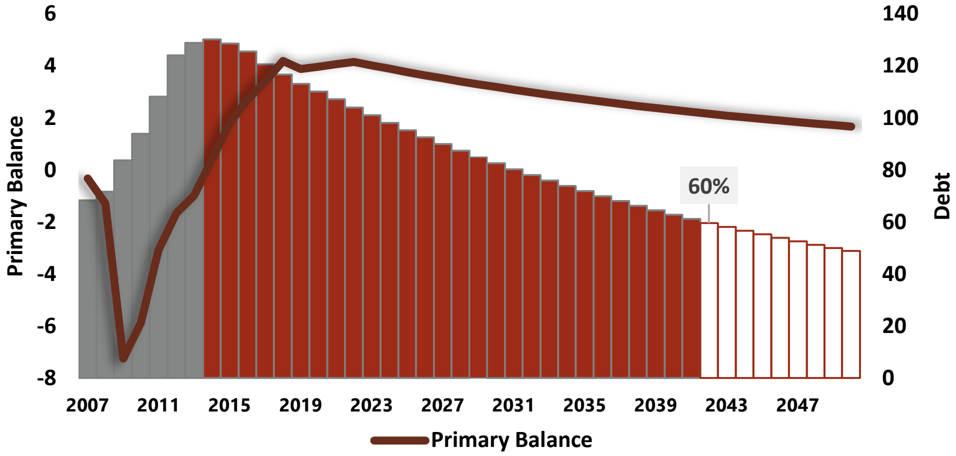
The achievement of the medium-term objective of a structural deficit of 0.5% of GDP will be sufficient to comply with the debt reduction rule. In effect the maintaining of a structural balance of 0.5% after 2017, as required by the Stability and Growth Pact and the Budgetary Treaty, will be sufficient to reduce the debt in excess of the 60% of GDP benchmark at the rate of one twentieth per year (see Chart 19).

Maintaining a budget balance in line with the medium-term objective will depend critically upon the ability to generate significant primary surpluses. The primary surplus required to achieve the MTO will be higher initially, as a result of the interest payments due to the higher debt ratio, and then decrease gradually as the debt ratio falls.[51] Thus, from 2018 to the end of the 2020 decade the required primary surplus will be greater than 4% of GDP, decreasing gradually to 2% of GDP at the end of time frame (2050), which corresponds to an average of 3% of GDP. In this scenario the Budgetary Treaty debt rule is met, and the ratio of 60% of GDP is achieved in 2042. The projected figures would improve if lower interest rates and/or a higher growth rate were assumed. As stressed by the OECD, in the aforementioned study, a successful budget adjustment can bring important benefits in terms of a decrease in the sovereign debt risk premium, as well as the decrease in the country risk on the internal interest rates if that adjustment contributes to the decline in external debt.

[50] In the latest *OECD Economic Outlook*, May 2014, the OECD sets out the long-term outlook that points to real growth in GDP *per capita* within the OECD of around 1.5% per year and a rise in the real long-term interest rate of approximately 1.5 p.p. in the next 4-5 years as the output gap closes and monetary policy rates normalize.

[51] The annual fiscal effort needed to achieve the primary surplus required to comply with the structural balance rule will vary, as a result of fiscal pressures, namely those stemming from the ageing of the population and other contingent liabilities.

Chart 19 – Public debt development in a scenario where MTO is met (as % of GDP)



Source: INE and Ministry of Finance. CFP calculations. | Note: In this projection it is assumed that the interest rate remains at 4.5% and nominal GDP growth at 3.5% from 2022 onwards. Up to 2018 the FSD figures are used, while from 2019 to 2021 a convergence with the long-term figures is assumed. The primary balance from 2007 to 2013 is the adjusted primary balance.

5.6 OTHER BUDGET RISKS

In addition to the risks inherent to the economic context and the outturn of the planned measures, budgetary results are also subject to risks linked to changes of a statistical and/or regulatory nature. These include risks resulting from the reclassifying or changes in the treatment of institutions and transactions that until now have fallen outside the budget scope, as well as possible unfavourable decisions as to the measures currently in force. The incurring of contingent liabilities under guarantees provided and hedging contracts, along with changes in the cost of PPPs, also brings budget outturn risks. Furthermore the new national accounts rules that will come into force next September (ESA 2010) can lead to the incorporation of various Non-Reclassified Public Corporations (NRPC) within general government scope. A strategy that includes, as stated in the FSD/2014, the granting of concessions for public services provided by the NRPC involves reinforcing these corporations' financial soundness, which could have consequences on the public debt level.

The FSD only partially identifies the amounts linked to these risks. Thus, the sums identified in regard to guarantees provided, which total around 9.9% of GDP, only relate to the State subsector, and no mention is made about the amount guaranteed to regional and local government enterprises, nor to the banking sector.[52] In the latter case, in addition, the new Basel III prudence rules regarding the composition of bank equity led to a change in the way deferred taxes are treated. This change in treatment could involve their partial

[52] According to the information received from the MF in reply to a request for clarification, the amount of debt guaranteed by the State to the banks accounts for 9.9% of GDP.

transformation into tax credits, with implications for budget deficits, in terms which are being discussed by the statistical authorities.[53]

Part of the statistical changes referred to include the change to the base and conceptual framework of national accounts (from ESA 95 to ESA 2010). Note that these changes have far wider consequences, some favourable to the budget aggregates, that are also worthy of mention, as, in particular, the case of the revision, likely to be upwards, of the value of nominal GDP and its effects on the deficit and public debt ratios.

5.7 COMPARISON WITH THE FSD/2013

The goals of correcting the excessive deficit and achieving the medium-term objective for the structural balance are the same as in the FSD/2013. The budgetary projection for 2014-18 restates the elimination of the excessive deficit situation in 2015 and the achievement of the MTO in 2017, as required by the aforementioned Council Recommendation and the Stability and Growth Pact.[54] The nominal deficit targets for 2014 and 2015 remain the same as in the previous FSD, although there is a slowdown in the rate of the budget imbalance correction up to 2017. The lower decrease in the deficit reflects the downward revision of the targets for 2016 and 2017, from -1.2% of GDP to -1.5% of GDP and from -0.2% of GDP to -0.7 % of GDP, respectively. In structural terms, from 2013 to 2017 the FSD estimates a structural deficit correction of 2.6 p.p. of GDP compared with 3.1 p.p. of GDP in the previous FSD.[55]

In the updated medium-term forecast the MF expects revenue to make a greater contribution to the budget adjustment. Compared to the previous FSD, the scale of the adjustment to be undertaken on the expenditure side is amended. Thus, for the 2010-17 period, the updating of the projection increases revenue's contribution to the structural adjustment, which is expected to be 15 p.p. higher than projected in the FSD/2013. In the later document, the distribution of the adjustment effort up to 2017 revenue contributed only with 19% and expenditure with 81%.

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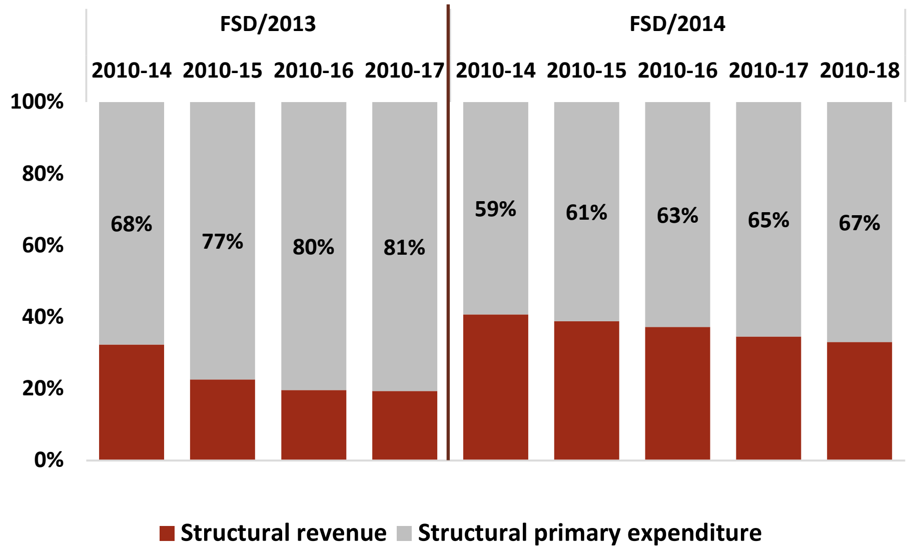
[53] In the report relating to 11th review of the EFAP, the IMF warns of the potential impact on these assets in public accounts: *"Fiscal accounts may also be impacted by possible changes in the treatment of deferred tax assets which are still under consideration and by the statistical treatment of efforts to more efficiently manage the debt overhang of some state-owned enterprises."* (paragraph 34).

[54] Assessment of compliance with fiscal rules and goals is provided in detail in section 4 of this report.

[55] In order to identify the fiscal consolidation effort, the budget aggregates examined in this section are net of the effects of temporary and one-off measures and of special factors. It is stressed that these adjustments differ from those underlying the forecasts published in the FSD/2014 Report. To be precise, the loss of revenue from the investment tax credit and the impact of the compensation payable in regard to termination by mutual agreement (for which the MF estimates a net impact of 0.3% of GDP) were not considered temporary measures in 2014.

Chart 20 – Fiscal consolidation effort evaluated in structural terms
Cumulative composition of structural adjustment implicit in the FSD/2014 and in the FSD/2013



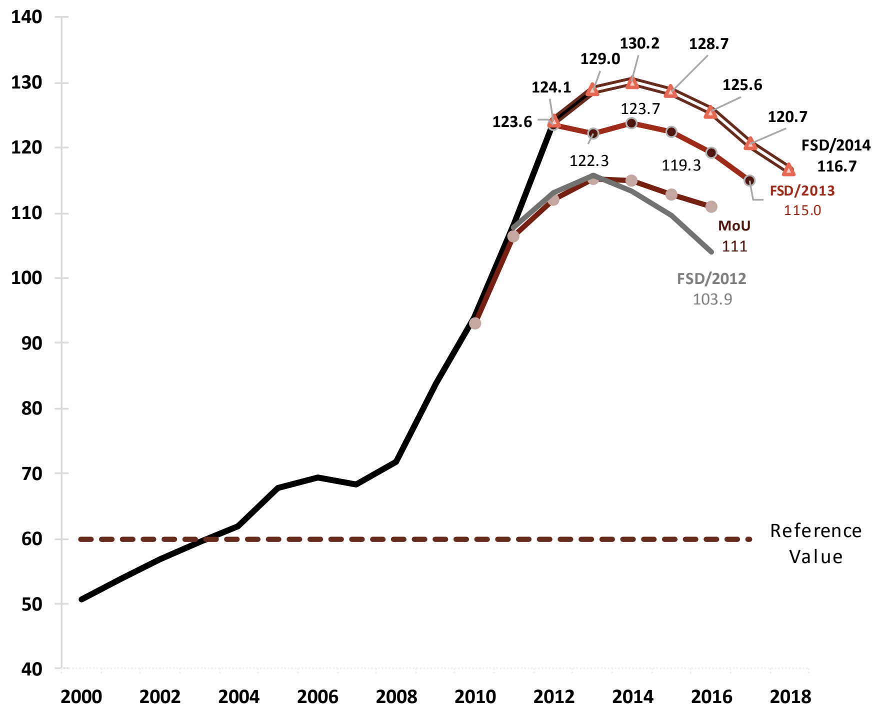
Source: INE and MF. CFP calculations. | Note: The fiscal consolidation effort is the improvement in the structural primary balance net of the impact of special factors. The structural figures are net of the effects of the economic cycle and the impact of temporary and one-off measures and special factors.

In the FSD/2013 total revenue was expected to follow a downward path and to stand at 41.7% of GDP in 2017, while in the FSD/2014 total revenue in the same year is estimated at around 43.1%. This discrepancy can be found mainly in current revenue (1.2 p.p.), in particular in tax revenue, which in the FSD/2013 had a relative weight of 24.7%, while in the FSD /2014 it is 25.4% (+0.7 p.p.). In this context the significant difference stems above all from direct taxes, more precisely from PIT, which should reflect a baseline effect from the fiscal developments in 2013. Note also that social contributions account for 0.3 p.p. of the divergence in the analysis, especially from 2015 onwards, which is justified by the 0.2 p.p. rise in employees' contributions to social welfare systems (price effect) and improved prospects for the labour market (quantity effect).

The fiscal consolidation effort estimated by the MF should continue to be based upon the cut in spending as a percentage of GDP, but at a slower pace than expected in the previous FSD. A year ago expenditure was predicted to reach 41.9% of GDP in 2017, while now the forecast for the same year is 43.8% (i.e. a nominal difference of around 3 700 M€). In 2017, the difference (1.8 p.p. of GDP) is by large justified by subsidies and other current expenditure (1.0 p.p.), a substantial change that is not explained in the FSD/2014. Social transfers and capital expenditure have been revised upwards (both by 0.3 p.p.), and so have, on a lesser scale, intermediate consumption and compensation of employees (both by 0.2 p.p. of GDP). These revisions are offset by a lower forecast for interest outlays (-0.2 p.p. of GDP), reflecting the lower implicit interest rate, given that the amount of debt is higher over the entire time span.

In 2014 the debt ratio shows an upward revision of 6.3 p.p. of GDP compared to the previous FSD. This revision totals 6.2 p.p. of GDP in 2015 and 6.3 p.p. of GDP in 2016. For the three-year period 2014-2016 the revisions are substantial, as the State assumes the debt of the transport corporations for which concessions are to be granted,[56] replacing the bank debt guaranteed by the State. In regard to the year in which the turnaround in debt's upward path takes place under ESA 95, the FSD/2014 is in line with the previous FSD and points to 2015.

Chart 21 – Public debt developments in successive forecasts in budgetary planning documents
(% of GDP)



Source: MF. CFP calculations.

[56] FSD/2014 states that the concession procedures for Carris, STCP and some CP lines are underway or already scheduled.

6 ANNEX

Table 8 – General government non-adjusted account (as % of GDP)

	INE		FSD 2014 - 2018					Annual change p.p. of GDP						
	2010	2013	2014	2015	2016	2017	2018	2014	2015	2016	2017	2018	2010-13	2013-18
Total revenue	**41.6**	**43.7**	**43.2**	**43.3**	**43.3**	**43.1**	**43.0**	**-0.5**	**0.1**	**0.0**	**-0.2**	**0.0**	**2.1**	**-0.7**
Current revenue	**38.8**	**42.8**	**42.1**	**42.3**	**42.3**	**42.1**	**42.0**	**-0.7**	**0.2**	**0.0**	**-0.2**	**0.0**	**4.0**	**-0.8**
Tax revenue	22.1	25.4	25.0	25.3	25.3	25.4	25.5	-0.4	0.3	0.1	0.1	0.1	3.3	0.1
Indirect taxes	13.3	13.6	13.7	13.9	13.9	14.0	14.0	0.1	0.1	0.1	0.1	0.0	0.3	0.4
Direct taxes	8.8	11.8	11.3	11.4	11.4	11.4	11.4	-0.5	0.1	0.0	0.0	0.0	3.0	-0.4
Social contributions	12.3	12.2	11.8	11.7	11.5	11.4	11.2	-0.4	-0.1	-0.1	-0.1	-0.2	-0.1	-1.0
of which: actual	9.1	9.3	9.2	9.3	9.2	9.1	9.0	-0.1	0.1	-0.1	-0.1	-0.1	0.2	-0.3
Sales and other current revenue	4.4	5.2	5.3	5.4	5.4	5.3	5.4	0.1	0.1	0.1	-0.1	0.1	0.9	0.1
Capital transfers received	**2.8**	**0.9**	**1.1**	**1.0**	**1.0**	**1.0**	**1.0**	**0.2**	**-0.1**	**0.0**	**0.0**	**0.0**	**-1.9**	**0.1**
Total expenditure	**51.5**	**48.6**	**47.1**	**45.8**	**44.8**	**43.8**	**43.1**	**-1.5**	**-1.3**	**-1.0**	**-1.0**	**-0.7**	**-2.9**	**-5.6**
Primary expenditure	**48.7**	**44.3**	**42.8**	**41.5**	**40.5**	**39.7**	**38.9**	**-1.5**	**-1.3**	**-0.9**	**-0.9**	**-0.8**	**-4.3**	**-5.5**
Current primary expenditure	42.9	41.9	40.7	39.3	38.5	37.7	37.0	-1.2	-1.4	-0.8	-0.8	-0.7	-1.0	-5.0
Intermediate consumption	5.2	4.4	4.6	4.3	4.3	4.1	4.0	0.2	-0.3	0.1	-0.2	-0.1	-0.8	-0.4
Compensation of employees	12.2	10.7	9.7	9.1	8.8	8.6	8.5	-1.0	-0.6	-0.3	-0.2	-0.1	-1.5	-2.3
Social transfers	22.0	23.4	22.9	22.4	22.0	21.6	21.2	-0.6	-0.5	-0.4	-0.4	-0.4	1.5	-2.3
other than in kind	4.9	4.6	4.5	4.3	4.2	4.0	3.9	-0.1	-0.2	-0.1	-0.1	-0.1	-0.3	-0.7
Subsidies	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.0	0.0	0.0	0.0	0.0	-0.1	0.0
Other current expenditure	2.8	2.7	2.8	2.8	2.6	2.7	2.7	0.2	0.0	-0.2	0.1	0.0	-0.2	0.0
Capital expenditure	5.7	2.4	2.1	2.2	2.0	2.0	1.9	-0.3	0.1	-0.1	-0.1	-0.1	-3.3	-0.5
GFCF	3.8	1.4	1.8	1.7	1.7	1.6	1.6	0.3	0.0	-0.1	-0.1	-0.1	-2.3	0.1
Other capital expenditure	2.0	1.0	0.3	0.4	0.3	0.3	0.3	-0.7	0.1	-0.1	0.0	0.0	-1.0	-0.6
Interest paid (EDP)	**2.8**	**4.3**	**4.3**	**4.3**	**4.2**	**4.1**	**4.2**	**0.1**	**0.0**	**-0.1**	**-0.1**	**0.1**	**1.5**	**-0.1**
General government balance (EDP)	**-9.8**	**-4.9**	**-4.0**	**-2.5**	**-1.5**	**-0.7**	**0.0**	**0.9**	**1.4**	**1.0**	**0.8**	**0.7**	**4.9**	**4.9**
Primary balance (EDP)	-7.0	-0.6	0.4	1.8	2.7	3.4	4.2	1.0	1.4	0.9	0.7	0.7	6.4	4.8
Tax burden	31.3	34.7	34.2	34.5	34.5	34.5	34.5	-0.5	0.4	0.0	0.0	0.0	3.4	-0.2
Current expenditure	45.7	46.2	45.1	43.6	42.7	41.8	41.2	-1.1	-1.4	-0.9	-0.9	-0.7	0.4	-5.0
Public debt	94.0	129.0	130.2	128.7	125.6	120.7	116.7	1.2	-1.5	-3.1	-4.9	-4.0	35.0	-12.3

Source: INE and MF. CFP calculations. | Note: (i) The figures used by the CFP, when analysing FSD/2014, correspond to those published in the Report's tables, duly amended in line with the errata published by the MF on 9th May. However that information is not consistent with the errata given in the Annex published on the same date; (ii) Due to rounding the changes do not necessarily correspond to the differences between the percentage GDP figures.

Table 9 – General government adjusted account (as % of GDP)

	INE		FSD 2014 - 2018					Annual change p.p. of GDP						
	2010	2013	2014	2015	2016	2017	2018	2014	2015	2016	2017	2018	2010-13	2013-18
Total revenue	**40.0**	**42.9**	**43.0**	**43.3**	**43.3**	**43.1**	**43.0**	**0.1**	**0.2**	**0.0**	**-0.2**	**0.0**	**3.0**	**0.1**
Current revenue	**38.8**	**42.0**	**42.1**	**42.3**	**42.3**	**42.1**	**42.0**	**0.0**	**0.2**	**0.0**	**-0.2**	**0.0**	**3.2**	**0.0**
Tax revenue	22.1	24.8	25.0	25.3	25.3	25.4	25.5	0.2	0.3	0.1	0.1	0.1	2.6	0.7
Indirect taxes	13.3	13.4	13.7	13.9	13.9	14.0	14.0	0.3	0.1	0.1	0.1	0.0	0.1	0.6
Direct taxes	8.8	11.4	11.3	11.4	11.4	11.4	11.4	-0.1	0.1	0.0	0.0	0.0	2.6	0.1
Social contributions	12.3	12.0	11.8	11.7	11.5	11.4	11.2	-0.2	-0.1	-0.1	-0.1	-0.2	-0.3	-0.8
of which: actual	9.1	9.1	9.2	9.3	9.2	9.1	9.0	0.1	0.1	-0.1	-0.1	-0.1	0.0	-0.1
Sales and other current revenue	4.4	5.2	5.3	5.4	5.4	5.3	5.4	0.0	0.1	0.1	-0.1	0.1	0.9	0.1
Capital transfers received	**1.2**	**0.9**	**1.0**	**1.0**	**1.0**	**1.0**	**1.0**	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**	**-0.3**	**0.1**
Total expenditure	**48.6**	**48.2**	**47.2**	**45.8**	**44.8**	**43.8**	**43.1**	**-0.9**	**-1.4**	**-1.0**	**-1.0**	**-0.7**	**-0.5**	**-5.1**
Primary expenditure	**45.8**	**43.9**	**42.9**	**41.5**	**40.5**	**39.7**	**38.9**	**-1.0**	**-1.4**	**-0.9**	**-0.9**	**-0.8**	**-1.9**	**-5.1**
Current primary expenditure	42.1	41.9	40.7	39.3	38.5	37.7	37.0	-1.2	-1.4	-0.8	-0.8	-0.7	-0.2	-5.0
Intermediate consumption	4.7	4.4	4.6	4.3	4.3	4.1	4.0	0.2	-0.3	0.1	-0.2	-0.1	-0.3	-0.4
Compensation of employees	12.2	10.7	9.7	9.1	8.8	8.6	8.5	-1.0	-0.6	-0.3	-0.2	-0.1	-1.5	-2.3
Social transfers	21.9	23.4	22.9	22.4	22.0	21.6	21.2	-0.6	-0.5	-0.4	-0.4	-0.4	1.5	-2.3
other than in kind	4.8	4.6	4.5	4.3	4.2	4.0	3.9	-0.1	-0.2	-0.1	-0.1	-0.1	-0.2	-0.7
Subsidies	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.0	0.0	0.0	0.0	0.0	-0.1	0.0
Other current expenditure	2.5	2.7	2.8	2.8	2.6	2.7	2.7	0.2	0.0	-0.2	0.1	0.0	0.1	0.0
Capital expenditure	3.7	2.0	2.2	2.2	2.0	2.0	1.9	0.2	0.0	-0.1	-0.1	-0.1	-1.7	-0.1
GFCF	3.0	1.4	1.8	1.7	1.7	1.6	1.6	0.3	0.0	-0.1	-0.1	-0.1	-1.6	0.1
Other capital expenditure	0.7	0.6	0.4	0.4	0.3	0.3	0.3	-0.2	0.0	-0.1	0.0	0.0	-0.2	-0.2
Interest paid (EDP)	**2.8**	**4.3**	**4.3**	**4.3**	**4.2**	**4.1**	**4.2**	**0.1**	**0.0**	**-0.1**	**-0.1**	**0.1**	**1.5**	**-0.1**
General government balance (EDP)	**-8.7**	**-5.3**	**-4.2**	**-2.5**	**-1.5**	**-0.7**	**0.0**	**1.1**	**1.7**	**1.0**	**0.8**	**0.7**	**3.4**	**5.2**
Primary balance (EDP)	-5.9	-1.0	0.1	1.8	2.7	3.4	4.2	1.1	1.7	0.9	0.7	0.7	4.9	5.1
Tax burden	31.3	33.9	34.2	34.5	34.5	34.5	34.5	0.3	0.4	0.0	0.0	0.0	2.6	0.6
Current expenditure	44.9	46.2	45.1	43.6	42.7	41.8	41.2	-1.1	-1.4	-0.9	-0.9	-0.7	1.3	-5.0
Public debt	94.0	129.0	130.2	128.7	125.6	120.7	116.7	1.2	-1.5	-3.1	-4.9	-4.0	35.0	-12.3

Source: INE and MF. CFP calculations.| Note: (i) The figures are adjusted for the impact of the temporary and one-off measures and special factors shown in Table 11; (ii) Due to rounding the changes do not necessarily correspond to the differences between the percentage GDP figures.

Table 10 – Multi-annual Budgetary Planning Framework [2014-18] (M€)

	PROGRAM	MINISTRY Executor	Proposed Law n.º 178/XII (SB/2014)				FSD 2014-2018				FSD 2014 *vs* PL n.º 178 (SB/2014)							
			2014	2015	2016	2017	2014	2015	2016	2017	2014		2015		2016		2017	
											Δ abs	Δ rel.	Δ abs	Δ rel.	Δ abs	Δ rel.	Δ abs	Δ rel.
SOVEREIGNTY	P001 - Sovereign Bodies	EGE	2 975				2 977				2							
	P002 - Governance and Culture	PCM	226				226				-							
	P005 - Foreign affairs	MNE	285				285				-							
	P008 - Justice	MJ	658				658				-							
	Subtotal		**4 144**	**3 981**			**4 146**	**4 101**			**2**	**0%**	**120**	**3%**				
SECURITY	P006 - Defense	MDN	1 694				1 683				- 11							
	P007 - Internal Security	MAI	1 615				1 600				- 15							
	Subtotal		**3 309**	**3 208**			**3 283**	**3 309**			**- 26**	**-1%**	**101**	**3%**				
SOCIAL	P012 - Health	MS	7 621				7 621				-							
	P013 - Basic and Second. Educ. and Sch. Adm.	ME	4 938				4 938				-							
	P014 - Science and Higher Education	ME	1 296				1 296				-							
	P015 - Solidarity, Employm. and Soc. Security	MSSS	9 358				13 609				4 251							
	Subtotal		**23 213**	**22 853**			**27 464**	**27 310**			**4 251**	**18%**	**4 457**	**20%**				
ECONOMIC	P003 - Finance and Public Administration	MF	7 172				3 099				- 4 073							
	P004 - Public debt management	MF	7 239				7 239				-							
	P009 - Economy	MEE	222				222				-							
	P010 - Enviroment, P. Territory and Energy	MAOTE	41				41				-							
	P011 - Agriculture and Sea	MAM	328				328				-							
	Subtotal		**15 003**	**15 379**			**10 930**	**11 346**			**- 4 073**	**-27%**	**-4 033**	**-26%**				
	Expenditure ceilings financed by general revenues		**45 669**	**45 422**	**45 809**	**46 302**	**45 823**	**46 066**	**46 515**	**47 149**	**154**	**0%**	**644**	**1%**	**706**	**2%**	**847**	**2%**
	% GDP		**27.2**				**27.1**											

Source: MF. CFP calculations.

Table 11 – Temporary measures and special factors (as % of GDP)

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Temporay & one-off measures *(impact on b. balance)*	**0.3**	**3.6**	**0.0**	**0.3**	**0.2**	**0.0**	**0.0**	**0.0**	**0.0**
Revenue	**1.7**	**4.0**	**0.3**	**0.8**	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**
Transfer of pension funds	1.6	3.5	0.1	0.0					
EGREP Dividends					0.0				
Taxes on repatriation of capitals	0.1		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					
PIT sucharge relating to income from 2011		0.5	0.1						
Expenditure	**1.3**	**0.3**	**0.4**	**0.4**	**-0.1**	**0.0**	**0.0**	**0.0**	**0.0**
Proceeds from concessions	-0.1	0.0	-0.2	0.0	-0.1				
Capital transfers (Banking sector)	1.3	0.4	0.5	0.4					
One-off payments to the EU Budget	0.1		0.1						
Special factors *(impact on b. balance)*	**-1.5**	**-0.9**	**-0.5**	**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**	**0.0**	**0.0**
Expenditure	**1.5**	**0.9**	**0.5**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Delivery of submarines	0.5								
Capital transfers (Sagestamo)			0.5						
Reclassification of PPP into general government	0.4	0.1							
Recording of Madeira region debt	0.6								
Madeira capital transactions (SESARAM & reclass. of Via Madeira)		0.3							
Madeira region debts from programme contracts & football clubs		0.1							
Reclassification of support fund to health service		0.3							
Temporay measures, one-off measures and special factors	**-1.1**	**2.8**	**-0.5**	**0.3**	**0.2**	**0.0**	**0.0**	**0.0**	**0.0**

Source: MF. CFP calculations. | Note: Due to rounding the totals do not necessarily correspond to the sum of the percentage GDP figures.

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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