



**Conselho das
Finanças
Públicas**

**GENERAL
GOVERNMENT
BUDGET OUTTURN
IN 2022
EXECUTIVE
SUMMARY**

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EXECUTIVE SUMMARY

Balances, adjustment and fiscal policy stance in 2022

In the context of economic activity surpassing pre-pandemic levels, the General Government (GG) continued in 2022 to correct its fiscal imbalance. In fact, in the last two years the budget balance showed a cumulative improvement of 5.4 p.p. of GDP, approaching a balanced position similar to that of 2019.

In 2022, the budget deficit fell by 2.5 p.p. of GDP to 0.4% of GDP, extending the safety margin from the 3% of GDP limit in the Treaty on the Functioning of the European Union. This budget outturn was better than predicted by the government in the budget programming documents (deficit of 1.9% of GDP). This better result benefited from important gains in tax revenue resulting from the automatic reaction of VAT to the rise in the prices of goods and services accompanied by the non-updating of the PIT brackets in line with inflation. CFP's estimate points out that the non-updating of the PIT brackets in line with inflation has benefited the revenue from this tax by 0.2% of GDP. On the expenditure side, the salary update applied to the civil service (0.9%), well below inflation, favoured a partial and restrained reaction of public expenditure, whose main components, not subject to automatic indexation, reduced their ratio to GDP. At the same time, the withdrawal of a large part of the pandemic crisis response measures has helped to offset the budgetary cost of the new measures aimed at mitigating the effects of the geopolitical shock and the economic and social impact caused by rising prices. In contrast, financial support to corporations in a restructuring process penalized the balance by 0.6% of GDP, aggravated by the impact, albeit smaller, of a one-off measure (0.1% of GDP). The primary balance, which excludes interest, returned to a surplus position reaching 1.6% of GDP.

In the second year of implementation of the Recovery and Resilience Plan (RRP), the 2022 execution approached 800 M€ (0.3% of GDP), less than a quarter of what was foreseen in the SB/2022. The public investment financed by the RRP amounted to 290 M€ of the 1216 M€ foreseen in the SB/2022 (execution degree of 24%). This proved insufficient to boost public investment to cope with the depreciation of the GGs' capital stock, which has been eroding for more than a decade.

Removing the impact of one-off measures, which do not lead to a sustained change in the fiscal position, the decrease in the deficit (3.0 p.p. of GDP) continued to be supported by favourable economic developments (2.4 p.p. of GDP) and a reduction in interest charges (0.4 p.p. of GDP). The remaining part, which is theoretically attributed to government action, as assessed by the change in the structural primary balance, contributed to the improvement of the fiscal situation by 0.1 p.p. of GDP. Adding to this apparently restrictive effect the expansionary fiscal impulse of 0.3 p.p. of GDP conferred by the RRP on economic activity in 2022, it can be concluded that the budgetary execution of the general government has boosted economic activity by 0.2 p.p. of GDP. This result reflects an expansionary stance of fiscal policy, with the inclusion of the RRP.

In line with these developments, adjusting the effect of the business cycle, convergence towards the medium-term objective is estimated to have continued in 2022. In that year, the structural balance will have stood at -1.1% of GDP, an improvement of 0.5 p.p. of GDP compared to the previous year, mainly explained by the decrease in interest charges.

Revenue and expenditure in 2022

Public revenue grew by 10.2% in 2022, slightly below that recorded for nominal GDP (11.4%), implying that the revenue to GDP ratio stood at 44.4%, 0.5 p.p., lower than that observed in the previous year. In absolute terms, GG's revenue increased by 9818 million €, driven exclusively by tax and contributory revenue. Direct taxes, which increased by 24.1%, accounted for more than half of the growth in GG tax revenue, highlighting the strong recovery in CIT revenue after two years of consecutive declines due to the pandemic context. Indirect taxes grew by 11.8%, reflecting the robust performance of nominal private consumption (12.5%). Effective social contributions grew by 10.3%, reflecting the positive dynamics in the labour market. The growth of tax revenue, especially direct taxes at a faster pace than nominal GDP, raised the tax burden to 36.2% of GDP, a new all-time record. In this regard, it is also worth noting the increase in the weight of the PIT and CIT in their respective tax bases. The share of VAT revenue on nominal private consumption also increased in the year under review. In contrast, non-tax and non-contributory revenue decreased by 8.4% in 2022, penalized by the evolution of "other current revenue" and capital revenue. This behaviour showed the sharp decrease in revenue from the European Union, to finance measures in the context of the COVID-19 pandemic as well as the base effect of the repayment of the prepaid margin on loans received in the context of the

Financial Assistance Programme. Adjusting for this one-off transaction, the capital revenue to GDP ratio would increase by 0.1 p.p.

The public expenditure ratio to GDP decreased by 3 p.p. in 2022, to 44.8% of GDP. This reduction benefited from the denominator effect, as nominal GDP growth (11.4%) was much higher than public expenditure growth, although the latter accelerated from 3.8% in 2021 to 4.4% in 2022. In absolute terms, public expenditure increased 4500 million €, compared to 2021. The decrease in the impact of COVID-19 measures more than offset expenditure due to the adoption of measures to mitigate the geopolitical shock and inflation. Primary current expenditure increased by 3800 million €, practically all of its components recording an increase (except for subsidies, as the result of a strong reduction in COVID-19 measures). Capital expenditure increased by 1.2 bn€, of which 0.8 bn€ due to "other capital expenditures" and 0.4 bn€ in GFCF. GFCF growth was driven by RRP-financed expenditure, although slower than 2021, reducing its share of GDP by 0.1 p.p.. Interest charges decreased in absolute value and as a percentage of GDP for the eighth consecutive year.

Subsectors in 2022

Favourable developments in all subsectors of the GG explained the reduction of the government deficit. Central Government was responsible for almost two-thirds of the improvement in the budget balance by reducing its deficit by 2.9 bn€ (1.6 p.p. of GDP) to 5.2 bn€ (2.2% of GDP). The Social Security Funds reached a surplus of 4.3 bn€ (1.8% of GDP), a new maximum according to data available since the year 2000. This result contributed 0.6 p.p. of GDP to the change in the GG budget balance. Regional and Local Government contributed 0.3 p.p. of GDP to the positive evolution of this indicator, reducing such subsector budgetary imbalance to a close to balance position.

Public debt in 2022

In 2022, the government debt ratio continued on a downward trajectory, falling below the 2019 levels. The decrease of 11.5 p.p. in GDP is explained by a favourable dynamic effect (-10.9 p.p.), particularly influenced by the price effect due to the high inflation registered this year, and the primary balance effect (-1.6 p.p.). The deficit-debt adjustment made an unfavourable contribution (1 p.p.), despite the decrease in cash and deposits. The GGs' debt net of deposits followed the evolution of the public debt ratio, decreasing by 10 p.p. of GDP to 108.1% of GDP.

From a financing point of view, the position supported by the Central Bank stands out, essentially through the Public Sector Purchase Programme and the Pandemic Emergency Purchase Programme, representing 26.2% of the Portuguese public debt stock. The remaining debt held by the resident sector stood at 29.1% of total debt in 2022, while the non-resident sector slightly decreased its position compared to 2021 (falling from 45.2% of total debt in the previous year to 44.7% in 2022).

Comparison with budget programming documents

Nominal growth of public revenue (10.2%) was almost twice the figure anticipated in the State Budget for 2022 [SB/2022]] (5.4%). This deviation amounted to 4664 million €, exclusively due to the favourable developments in tax and contributive revenues (+6767 million €). Comparing public revenue outturn to the MoF estimate for 2022 of October 2022, there was also a positive deviation, although of a smaller magnitude (1330 million €), entirely due to the performance of revenue from taxes and social contributions (+2057 million €). Public expenditure exceeded the SB/2022 forecast by 1196 million €. Primary current expenditure (3152 million €) contributed to this deviation, largely due to the budgetary impact of temporary support measures to mitigate the effects of inflation on corporations and households, which were not foreseen in the SB/2022. These impacted mainly social benefits and allowances, where expenditure was higher than expected by 1690 million € and 561 million €, respectively. In the opposite direction, capital expenditure and interest charges were set below expected in the SB/2022 at 1643 million € and 313 million €, respectively. As to capital expenditure, it is worth mentioning that GFCF was 1416 million € below the initial forecast of the MoF, which was almost double the deviation of 722 million € recorded in 2021. Compared to the MF estimate for 2022 implied in the DSB/2023, public expenditure was lower by 2155 million €, of which 1572 million € in capital expenditure, 373 million € in interest charges and 210 million € in primary current expenditure.