Executive summary

Analysis of general government national accounts in 2012

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Macroeconomic framework

In 2012 the Portuguese economy shrank by 3.2%, twice the rate of the previous year and more than initially forecasted. This development was driven by the decline of the positive contribution of net foreign demand and by the more significant negative contribution of domestic demand. The external imbalance adjustment process continued at a stronger pace than expected, leading to a net lending position of the Portuguese economy vis-à-vis the rest of the world, mainly due to the fall in domestic demand, as well as to gains in the market share of exports.

Performance of macroeconomic forecasts

The official macroeconomic forecasts for 2012, both of the Ministry of Finance and the international organisations that provide financial assistance to Portugal, proved to be optimistic in a number of components of significant relevance to the budgetary outturn, in particular as regards employment, GDP, implicit prices and the economic progression over the year.

General government balances

The preliminary estimate of the Portuguese statistical authority (INE) suggests that general government's borrowing requirements rose in 2012 to 10.6 billion euros, equal to 6.4% of GDP. The 2 p.p. of GDP deterioration compared to 2011 results from the dissipation of the effects of temporary measures taken in 2011 and of special factors which had an impacting on expenditure in 2012 In particular, this was the case of the reclassification of capital expenditure transactions which had been previously classified as financial transactions. Adjusting for these effects the deficit stood at 9,800 million euros (M€), or 5.9% of GDP, which is an improvement of 1.3 p.p. of GDP (2,500 M€) in regard to the comparable figure for 2011. The frequent use of temporary measures, which involve large sums, as well as their variability tend to reduce the information the overall balance change can provide about consolidation efforts.

According to the information available, the structural deficit, net of the impact of special factors on expenditure, stood at 4.3% of GDP in 2012, improving by 2 p.p. of GDP compared to 2011. The improvement in the primary structural balance, net of special factors, will have been 2.4 p.p. of GDP compared to 2011. This improvement stems entirely from the spending cuts. As stated in the body of the report these figures may be revised.

In non-adjusted terms the budget deficit was 1.9 p.p. of GDP above the forecasts in the budgetary planning documents (BSD/2011, SB/2012 and BSD/2012). This unfavourable bias was due entirely to revenue, as expenditure fell below the level forecasted in those documents. Adjusting for the reclassified capital transfers, the gap was approximately 1 p.p. of GDP.

Revenue

In adjusted terms general government revenue fell when compared to 2011, and accounted for 40.7% of GDP in 2012. This change is explained above all by the decline in tax revenue, although it was mitigated by the increase in "sales and other current revenues" and by capital revenue. This situation arose despite the increase in taxation, mainly due to the change in the structure of VAT rates. Although the decline in tax revenues was partially due to the harsher than expected economic environment, the magnitude of the bias raises doubts on the reasonableness of initial estimates of the impact of the tax measures set out in the State Budget of 2012 (SB/2012).

Contrary to the assumptions made in various budgetary planning documents published by the Ministry of Finance, the tax burden as a percentage of output fell in 2012, totalling 32.1% of GDP (non-adjusted values).

Expenditure

From 2010 to 2012, the largest annual fall in the adjusted expenditure-to-GDP ratio occurred in 2012. In this period, public expenditure was reduced by 7,035 M€, which represents a decrease of 2.1 p.p. of GDP compared to 2010. This was the result of a sharp fall in primary expenditure (3.6 p.p. of GDP), which was partially offset by the increase in interest charges (1.6 p.p. of GDP). As in 2011, all components of primary expenditure fell in 2012, in nominal terms, with cuts in compensation of employees making the largest contribution to the fiscal consolidation. Over half of the correction of 2012 was concentrated in the final quarter of the year.

Social security funds

The budgetary position of the social security funds subsector has deteriorated considerably in the last two years. Despite the introduction of a number of fiscal consolidation measures since 2010, their impact on expenditure was offset by the substantial rise in the cost of unemployment benefits and pensions (up by 489 M€ and 496 M€, respectively). The growth of revenue did not match the pace of growth in expenditure, consequently reducing the system's balance.

Regional and local governments

During the period 2010-2012 the improvement of the local and regional governments' fiscal imbalances contributed to the general government fiscal adjustment. The local governments' budgetary surpluses in the last two years were a decisive factor in that adjustment. Local debt (according to the Maastricht definition) also decreased.

The two regional governments signed economic and financial assistance agreements with the Central Government. The downward trend in the regional government deficit, interrupted in 2011, was resumed in 2012. The Azores regional government approached a balanced budget, while the Madeira regional government, in the first year of its adjustment program, initiated its imbalance correction process. Regional public debt (Maastricht definition) continued its trend upwards, although at a slower rate.

Public debt

In 2012 general government gross public debt, according to the Maastricht definition, reached 204,500 M€ (123.6% of GDP), which represents a substantial rise of 19,200 M€ (15.3 p.p. of GDP) compared to 2011. There was also a considerable increase in the interest due on debt, reaching 7,600 M€ (4.4% of GDP) in 2012.

In 2012 the increase in debt was much higher than the (non-adjusted) deficit of 10,600 M€, reflecting deficit-debt adjustments of 8,900 M€, due mainly to transactions stemming from the banking sector recapitalisation process and debt settlement operations, particularly concerning the National Health Service.