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COMMISSION OPINION

on the existence of an excessive deficit in Spain

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THE APPLICATION OF THE STABILITY AND GROWTH PACT IN THE CURRENT CRISIS SITUATION

1. Many EU countries are presently facing general government deficits above the 3% of GDP reference value set in the Treaty. The often strong deterioration in the deficit as well as the debt positions must be seen in the context of the unprecedented global financial crisis and economic downturn. Several factors are at play. First, the economic downturn brings about declining tax revenue and rising social benefit expenditure (e.g. unemployment benefits). Second, recognising that budgetary policies have an important role to play in the current extraordinary economic situation, the Commission called for a fiscal stimulus in its November 2008 European Economic Recovery Plan (EERP), endorsed by the European Council in December. The Plan explicated that the stimulus should be timely, targeted and temporary and differentiated across Member States, with more room for manoeuvre for those Member States that have achieved sustainable public finance positions and improved their competitive positions. The Plan also called for structural reforms that support demand and promote resilience in the short term, while paying special attention to actions in the four priority areas of the Lisbon Strategy. Finally, several countries have taken measures to stabilise the financial sector, some of which impact on the debt position or constitute a risk of higher deficits and debt in the future, although some of the costs of the government support could be recouped in the future.
2. The Stability and Growth Pact requires the Commission to initiate the excessive deficit procedure (EDP) whenever the deficit of a Member State exceeds the 3% of GDP reference value. The amendments to the Stability and Growth Pact in 2005 aimed at ensuring that in particular the economic and budgetary background was taken into account fully in all steps in the EDP. In this way, the Stability and Growth Pact provides the framework supporting government policies for a prompt return to sound budgetary positions taking account of the economic situation, and thereby ensuring long-term sustainability of public finances.

LEGAL BACKGROUND

3. Article 104 of the Treaty lays down an excessive deficit procedure (EDP). This procedure is further specified in Council Regulation (EC) No 1467/97 “on speeding up and clarifying the implementation of the excessive deficit procedure”¹, which is part of the Stability and Growth Pact.

¹ OJ L 209, 2.8.1997, p. 6. Account is also taken of the Opinion of the Economic and Financial Committee on the “Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes”, endorsed by the ECOFIN Council of 11 October 2005, available at http://ec.europa.eu/economy_finance/other_pages/other_pages12638_en.htm.

4. According to Article 104(2) of the Treaty, the Commission has to monitor compliance with budgetary discipline on the basis of two criteria, namely: (a) whether the ratio of the planned or actual government deficit to gross domestic product (GDP) exceeds the reference value of 3% (unless either the ratio has declined substantially and continuously and reached a level that comes close to the reference value; or, alternatively, the excess over the reference value is only exceptional and temporary and the ratio remains close to the reference value); and (b) whether the ratio of government debt to GDP exceeds the reference value of 60% (unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace).
5. Article 104(3) stipulates that, if a Member State does not fulfil the requirements under one or both of these criteria, the Commission has to prepare a report. This report also has to “take into account whether the government deficit exceeds government investment expenditure and take into account all other relevant factors, including the medium-term economic and budgetary position of the Member State”.
6. On the basis of the budgetary data included in the January 2009 update of the stability programme of Spain and taking into account the Commission services’ January 2009 interim forecast, the Commission adopted a report under Article 104(3) for Spain on 18 February 2009².
7. Subsequently, and in accordance with Article 104(4), the Economic and Financial Committee formulated an opinion on the Commission report on 27 February 2009.
8. Article 104(5) of the Treaty requires the Commission to address an opinion to the Council if the Commission considers that an excessive deficit in a Member State exists or may occur. In order to reach a conclusion on whether an excessive deficit exists or may occur, the Commission considers that account should be taken of: (i) the conclusions of its report under Article 104(3) and (ii) the opinion of the Economic and Financial Committee on this report. On the basis of these elements, the Commission has established a number of considerations for Spain.

CONSIDERATIONS CONCERNING SPAIN

9. According to the January 2009 update of the stability programme, Spain's general government deficit is estimated to have reached 3.4% of GDP in 2008, thus exceeding the 3% of GDP reference value. The Commission report under Article 104(3) considered that the deficit was close to the 3% of GDP reference value but that the excess over the reference value cannot be qualified as exceptional within the meaning of the Treaty and the Stability and Growth Pact. In particular, it did not result from an unusual event or a severe economic downturn in 2008. According to the Commission services’ January 2009 interim forecast, real GDP growth in Spain is estimated to have decelerated markedly in 2008 to 1.2%, but the output gap remained positive at 1% of GDP. Furthermore, the excess over the reference value cannot be considered temporary. According to the Commission services’ January 2009 interim forecast, the general government headline deficit will increase to 6.2%

² All EDP-related documents for Spain can be found at the following website:
http://ec.europa.eu/economy_finance/netstartsearch/pdfsearch/pdf.cfm?mode=_m2.

of GDP in 2009, including deficit-increasing one-off measures worth over ½% of GDP. The forecast was based on a projected GDP contraction by 2% as well as on a prudent assessment of both the 2009 Budget Law and the fiscal package announced by the Spanish authorities on 27 November 2008. Based on the customary unchanged policies assumption, the 2010 deficit is projected at 5.7% of GDP. Therefore, the deficit criterion in the Treaty is not fulfilled.

10. General government gross debt remains well below the 60% of GDP reference value and stood at an estimated 39.5% of GDP in 2008 according to the January 2009 stability programme. However, according to the Commission services' January 2009 interim forecast, the general government debt-to-GDP ratio is projected to increase significantly reaching 53% in 2010.
11. In line with the provisions in the Treaty and the Stability and Growth Pact, the Commission also analysed in its report "relevant factors". According to the Stability and Growth Pact, these can only be taken into account in the steps leading to the decision on the existence of an excessive deficit if the deficit satisfies the double condition of closeness and temporariness. In the case of Spain, the double condition is not met. Considered on their own merit, the relevant factors in the current case on balance seem to be relatively favourable.
12. The opinion of the Economic and Financial Committee in accordance with Article 104(4) of the Treaty is consistent with the assessment in the Commission report under Article 104(3).

CONCLUSION

13. The monitoring of the budgetary situation in Spain and, in particular, the examination of the compliance with the criteria laid down in Article 104(2) has led the Commission to prepare a report in accordance with Article 104(3) of the Treaty. The Commission, having taken into account its report and the opinion of the Economic and Financial Committee, is of the opinion that an excessive deficit exists in Spain.