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STABILITY AND GROWTH PROGRAMME

1999-2002

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1. INTRODUCTION

As one of the eleven Member States of the European Union (EU) that will adopt the euro on 1 January 1999, Portugal is hereby submitting to the EU Council and to the European Commission its stability programme for the period 1999-2002, in accordance with Council Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies.

Following the period of preparation and organisation provided for in the Treaty on European Union, the Union will have a common currency, the euro. The sharing of sovereignty in monetary matters and the setting-up of supranational institutions responsible for formulating and managing monetary policy are major developments in the process of constructing a prosperous and democratic Europe. The introduction of the euro also represents a decisive step in consolidating the single market. Indeed, it constitutes a unique historic event with wide-ranging implications for the future and welfare of Europe. From the Madrid European Council, which chose the euro as the name for the common currency, to the special Council meetings held last May, the Governments of the EU Member States demonstrated a unique political resolve to build economic and monetary union, a process that was crowned with success.

The Portuguese Government reaffirms the undertakings which it entered into in the context of the establishment of the single currency and which are consistent with the final objective of real convergence of the Portuguese economy, notably as regards the safeguarding of macroeconomic stability and the strengthening of the sustainability of public finances. This economic policy stance, which has proved to be the right one for pursuing the objectives of job creation and strengthening of social cohesion, has been broadly endorsed in Portugal, as demonstrated by the votes of congratulation by a large majority in the Parliament regarding Portugal's participation in economic and monetary union.

Portugal's participation in the euro has profound implications for Portuguese society and economy. The new economic and monetary arrangements will be more conducive to productive investment and employment. In view of the increased uncertainty in the international economy, it has become more urgent to preserve the framework of macroeconomic stability by continuing to pursue the gradual process of budgetary consolidation and reduction in the size of the public debt as a share of gross domestic product.

The objectives of budgetary consolidation are reflected in a downward trend in the overall general government deficit, which in the final year of this programme will be close to the level necessary to ensure that, in the event of an economic recession, Portugal will not have an excessive deficit. The necessary financial stringency will be achieved by the new mechanisms for monitoring and controlling the financial situation of the subsectors of general government. A continuing reduction in public debt as a percentage of GDP will be instrumental in this process of gradual budgetary consolidation. Total primary expenditure as envisaged in this programme is the basic benchmark for the preparation of annual budgets, ensuring that the objective set for the overall general government deficit will be pursued. The redirection of expenditure towards social objectives will continue and expenditure on investment in projects essential to the development of the country must be accorded priority. Portugal, which is the country with the lowest income per capita of the eleven countries making up the euro zone, will have to pursue the public investment policy that is absolutely necessary to the process of structural convergence.

The restructuring of the tax system with a view to improving equity and reinforcing the fight against tax evasion and avoidance is the main objective on the revenue side. The Government has already approved the General Tax Law, which restructures the tax system and incorporates a social contract with taxpayers. As regards the property tax, a new legal framework will be proposed involving a revamping of the tax arrangements for the municipal tax and for inheritance and gift tax and the abolition of the municipal tax on real estate sales (SISA). The arrangements for taxing property will be comprehensive, encompassing all economic events, the rules on incidence, and demarcation of the tax base.

The strengthening of the sustainability of public finances and the success of Portugal's participation in the euro will benefit from measures that will be taken in the field of human resources, boosting productivity in the health and social security fields.

Improving manpower competencies is of fundamental importance for the future of competitiveness and productivity of the Portuguese economy. A major drive will be launched to improve the quality of apprenticeship programmes, to implement the programme for developing and expanding pre-school education, to improve basic education (ensuring the effective respect of compulsory schooling of nine years), to consolidate vocational training at the level of secondary education, and to strengthen cooperation between the education system and the system of vocational training.

The national employment plan adopted by the Portuguese Government set as its main objectives improvement in basic and vocational skills with a view to promoting lifelong training and a strengthening of the role of active employment policies in fostering employability. These hinges on the ability to obtain and hold on to a job, which basically depends on the ability to renew knowledge, competencies, motivation and skills continuously. Measures will thus be taken (i) to reinforce education and initial high-quality training, (ii) to facilitate the transition from education and training to employment and to improve the social and economic integration of young people, and (iii) to foster manpower skills, thereby increasing individuals' adaptability and initiative.

In the health sector, the Government will adopt measures for a gradual but far-reaching reform of the national health service. In the interests of a structural, consensual and sustainable reform, the broad lines of this approach will be the following: (i) improvement in health by facilitating access to health care; (ii) improvement in the effectiveness and efficiency of health services; (iii) speeding-up of the health-promotion and sickness-prevention programmes via a network of primary care; (iv) improvement in the functioning of the health services by introducing new management models that will ensure greater independence and accountability; (v) effective decentralisation of the management of the national health service; and (vi) review of the role of the State in the health sector.

The Government presented to Parliament a draft framework law on social security setting out the priority objectives for the system. These include: improving the conditions of social protection and the system’s equity; improving management effectiveness and efficiency; and adopting measures to ensure the financial sustainability of the system. The financing of pensions will be adjusted and improved, making it possible to preserve social protection without increasing significantly the burden of taxpayers.

In formulating the macroeconomic projections, a cautious attitude was adopted in relation to the growth rate of GDP, and this has been and will continue to be a feature of budget exercises. The average growth rate of GDP in the programme period will be close to the growth potential and to the average recorded over the last five years. The assumptions for external developments correspond to the most recent forecasts made by the European Commission and the OECD.

In the event of deterioration in public finances, the national authorities undertake to adopt measures necessary to remedy the situation immediately in order to attain the objectives laid down for the overall deficit.

The present programme has been sent to the Portuguese Parliament and to the Economic and Social Council.

2. RECENT DEVELOPMENTS IN THE PORTUGUESE ECONOMY

Over the last three years the Portuguese economy has experienced sustained, non-inflationary growth. In 1998 the growth in gross domestic product is expected to be around 4% as a result of favourable trend in domestic demand and buoyant tourism.

The reduction in inflationary expectations, the significant decline in interest rates to the lowest levels recorded in the European Union and the stability of the escudo strengthened confidence of the private sector and gave further impetus to the dynamism of economic activity. The international financial crises had a modest impact on activity even though the stock exchanges experienced some periods of fluctuation and increased volatility.

During this period of growth, the output gap narrowed and the rate of unemployment declined from a high of 7.3% in 1996 to an average level of 4.8% in the first three quarters of 1998. The employment trend was actually very positive and the rates of unemployment fell significantly to levels close to the lowest recorded in the previous economic cycle. In the third quarter of this year, the unemployment rate stood at 4.7%, while the rate of unemployment among young people declined to 10%.

In a situation of currency stability, the reduction in unit labour costs, which reflected wage restraint and higher labour productivity, enabled Portuguese exports to remain competitive.

3. MACROECONOMIC PROJECTIONS FOR 1999-2002

3.1. External environment

The recent medium-term projections by the European Commission and the OECD, which were used in the current projections, point to relatively modest growth prospects for world output and trade given the present uncertainty regarding the repercussions of the recent international financial crises.

However, the growth prospects for the European Union economy, and in particular the euro zone, remain positive, making for an external environment favourable to growth in the Portuguese economy.

In line with the most recent projections, the main external variables determining the macroeconomic scenario underlying the stability programme assume the following evolution:

(i) growth of export markets averaging around 6.7% a year during the four-year period 1999-2002, i.e. lower than the annual average in the last two years (1997 and 1998);

(ii) maintenance of inflation rates within the European Union at below 2% on average;

(iii) recovery as of 1999 in the oil price and in non-energy commodity prices, in US dollars;

(iv) slight decline in international interest rates in 1999 and increase as of 2000, although rates will remain at historically low levels.

3.2. Macroeconomic scenario

In addition to the external determinants, the reference macroeconomic scenario involves a series of assumptions relating to the Portuguese economy, notably the following:

(i) wage developments consistent with price stability and with the principle of sharing out productivity gains;

(ii) continuation of public investment at a level close to nominal GDP growth.

These assumptions are compatible with fulfilment of the objective of a gradual and sustained reduction in the budget deficit and consolidation of public finances, compatible with the objectives of job creation and improved employability, within the context of the employment action plan, investment promotion and further development of social policies.

The main results of the macroeconomic scenario are set out below:

Table 1. Main economic indicators (1997-2002)

	1997	1998	1999(1)	2000	2001	2002	1999-2002
	(Real growth rate as %)						
GDP	3.8	4.2	3.5	3.2	3.2	3.3	3.3
Private consumption	2.8	3.6	3.3	2.8	2.8	3.2	3.0
Public consumption	1.9	2.7	2.0	1.0	1.1	0.5	1.2
GFCF	13.0	8.0	6.0	6.0	6.2	6.7	6.2
Domestic demand	4.8	4.5	3.7	3.3	3.4	3.6	3.5
Exports	8.4	10.8	7.1	6.8	6.8	7.1	7.0
Imports	10.8	10.5	7.2	6.5	6.6	7.3	6.9
GDP deflator (% change)	2.7	2.7	2.3	2.3	2.3	2.3	2.3
Private consumption deflator (% change)	2.3	2.6	2.0	2.0	2.0	2.0	2.0
Total employment (% change)	1.9	2.6	0.7	0.5	0.6	0.7	0.6

(1) The forecast growth is in the 3.5-4.0% range: for reasons of caution, the lower limit has been taken.

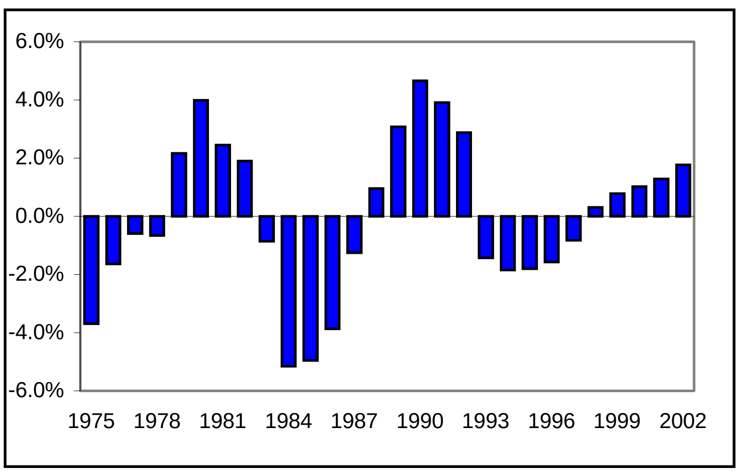
On the above assumptions, the Portuguese economy will continue to follow a growth trajectory higher than that forecast for the EU as a whole (some 0.7 percentage point on average in the period 1999-2002), although this will be lower than during the expansionary phase of the present economic cycle. The economy is expected to grow by 3.3% on average in the period 1999-2002.

In the light of export market developments, exports are projected to grow at a slower rate than in recent years although market shares will increase. The moderate rise in wages and the maintenance of productivity gains will strengthen the competitiveness of Portuguese firms.

During the forecasting period, the output gap is positive but lower than in the expansionary phases of the previous cycle.

Inflation remains stable as a result of the moderate growth in international commodity prices, continuing low levels of inflation in the European Union and moderate increases in unit labour costs.

Figure 1. Output gap*



* $\left(\frac{\text{GDP} - \text{potential GDP}}{\text{potential GDP}}\right) \times 100$; potential GDP was calculated using the Hodrick-Prescott filter.

Budgetary adjustment (at national level and within the European Union) will make for a continuation of low long-term interest rates conducive to private investment. The approach adopted for stepping up public investment underscores the importance of endowing the country with the needed physical capital to undertake essential reforms on the labour market and on goods and services markets, thereby enabling the Portuguese economy better to adjust to any asymmetric shocks.

4. MAIN FISCAL POLICY MEASURES

4.1. Measures to improve tax efficiency

The Government has drawn up a strategic framework for IT systems and technological infrastructures in the tax and customs fields which aims, among other things, at boosting efficiency within the tax administration, namely in tax collection and the fight against tax evasion and avoidance, while at the same time considerably improving the standard of service rendered by the tax administration to taxpayers.

In pursuit of the above objectives, the following measures in particular will be implemented in the course of the programme:

- Continuation of tax reform, through measures widening the tax base, the ongoing drive to stamp out tax evasion and avoidance, more accurate determination of the tax base, and reform and modernisation of taxation (namely, the creation of a single tax on wealth).
- A single register of taxpayers will be created in the form of a system of current accounts for each taxpayer.
- The systems for managing and controlling all legal proceedings in the tax field will be streamlined, in particular those relating to enforced tax collection.
- New integrated systems of support for tax inspection, covering the whole range of tax auditing procedures, will be adopted.[1]
- The IT network for the tax and customs administrations will be completed.

4.2. Measures for controlling budget expenditure

During the period covered by the stability programme, implementation of a number of political and administrative measures and other initiatives will continue with the aim of ensuring tighter control and more efficient utilisation of financial resources.

The Government will approve shortly a draft law on budgetary discipline which will incorporate into Portuguese law the foundations underpinning the stability culture and the principles on which the Stability and Growth Pact is based. The new law will lay down the general principles for financial coordination within the public sector, rationalising and harmonising the budgetary and financial decisions and policies implemented by the

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[1] The operations of UCLEFA (Coordination Unit for the Fight against Tax and Customs-Duty Avoidance), which groups together representatives of the different branches of the administration with a view to facilitating information exchange and concerted action, will at the same time be developed.

different branches of the administration whilst ensuring that the obligations deriving from participation in economic and monetary union are fulfilled. It will also establish the general rules and principles to be followed by the different branches of the administration with regard to the preparation, presentation and approval of budgets and accounts, the financial outlays, and budgetary control and accountability. The appropriation of revenues will be made subject to precise, strict rules and the principle of universality will prevail as a rule. The principle of treasury centralisation will be applied at the level of central government and the social security system, on the one hand, and at the level of the autonomous regions and municipalities, on the other. The strict rules necessary for achieving budgetary balance and the limits on the recourse to credit by the autonomous funds and services will be tightened.

The Government is finalising a multiannual programme for current expenditure for the period 1999-2002 with the aim of making all public spending conditional on compliance with the criteria of economy, efficiency and effectiveness. Stricter discipline in the administration of public funds will bring about a significant reduction in current expenditure over the period in question, thereby helping to keep the country on the path of budgetary consolidation.

In the field of budgetary management, the reform of the administration of State finances will continue and will be more thoroughly pursued in the years ahead, with the resulting increase in administrative productivity and gains flowing from application of the treasury centralisation principle to public payments and receipts.

The new Official Plan of Public Accounts will be gradually applied throughout the civil service. Public accounts will incorporate budgetary, capital and analytical accounting methods under the Plan, which is to be applied throughout all central, regional and local government departments, the social security system and other entities which are funded mainly through transfers from the State budget, thereby ensuring that accounting rules are standardised and public funds more tightly controlled.

The Plan will therefore enable financial control to be tightened, accounting systems and principles to be standardised, the accounting data to be produced which are necessary for obtaining the main aggregates of the national accounts, multiannual budgeting to be made more reliable, and strategic decisions to be taken.

Structures and schemes will be set up for assessing the productivity and social usefulness of administrative departments, in order to strengthen management control from a cost-benefit standpoint, in the areas of human resources policy, the modernisation and rationalisation of structures and the streamlining of procedures.

New procedures will be applied to the autonomous funds and services enabling their budgetary situation to be ascertained more quickly and any corrective decisions that may prove necessary to be taken in good time.

If deemed necessary, measures similar to those taken in the past and included in the State budget for 1999 will be kept in force, namely:

- a cut of 2% in nominal terms in the operating expenditure of departments in relation to the estimated outturn for 1998;
- the blocking of 10% of operating expenditure in the case of variable and contingent payments, expenditure on goods and services, other current expenditure and acquisitions of capital goods, and of 5% of operating expenditure in the case of current transfers to autonomous funds and services. Likewise, in the case of capital expenditure, blocking of 6% of the items in Chapter 50 and the items associated with the Military Planning Law;
- current and capital transfers to the autonomous funds and services may also be blocked where it is not necessary;
- the maintenance of the total freeze on staff recruitment, to be waived only in exceptional circumstances decided on a case-by-case basis and where the impact on expenditure is to be offset elsewhere so as to avoid aggravating the budget deficit.

The process of restructuring the state-owned sector will continue, with the aim of putting the state-owned enterprises on a sounder financial footing and boosting their efficiency and effectiveness. Under the privatisation programme, receipts from selling off some of the enterprises that still belong to the public sector will also help to reduce the stock of public debt and hence debt-servicing costs.

The Government will keep up the momentum of its reform of the health service by drawing up a *Health strategy* that will serve as a general reference tool for the health service, guide the actions of the different participants in the process and give concrete expression to the Government's explicit undertaking to put the essential measures of the reform into practice. In particular, a wide-ranging political and social consensus will be developed on a sustainable system for financing health care. The following are some of the measures to be taken: generalised introduction of the National Health Service user's card, which will ensure that health-care services are co-financed precisely by the right subsystem; more widespread use of the new form for medical prescriptions, which will simplify administrative processing, making prescribing practitioners more accountable and enabling costs to be controlled more effectively; strengthening of the role played by the contracting agencies in the regional health administrations, which will contribute to the rationalisation drive and cost control; development of the local health-care systems which are necessary for making health-care delivery more efficient; and, among the new management methods to be tried out, development of an innovative approach to hospital management.

The social security system will pursue its policy of strict budget implementation through a two-pronged attack on benefit fraud and evasion of contributions; this has released additional resources for consolidating new welfare policies without undermining the long-term financial sustainability of the system. The fight against fraud and the evasion of contributions has in recent years enabled the scheme's revenues from contributions to grow at a much faster rate than the total wage bill: 12% in 1997 and 9% in 1998. The stepping-up of checks on payments has yielded substantial savings in the payment of benefits, in particular sickness benefit, with highly positive effects on the overall of current social security expenditure.

The Government has tabled before Parliament a new draft framework law laying down basic rules on solidarity and social security, which pursues two fundamental strategic objectives: boosting the effectiveness of welfare policy and safeguarding the financial sustainability of the social security system. In line with the recommendations set out in the White Paper on social security, the draft law aims to establish, in the context of the system of solidarity and social security, a clear and coherent definition of citizenship welfare protection and employment welfare protection, laying down the necessary legal bases for developing the latter in a three-pillar system. The development of sources of financing, combining the pay-as-you-go and funded systems, is based on principles of diversification and the selective matching of sources of finance will also help to make the social security system more transparent and financially sustainable.

5. PUBLIC FINANCES UP TO 2002

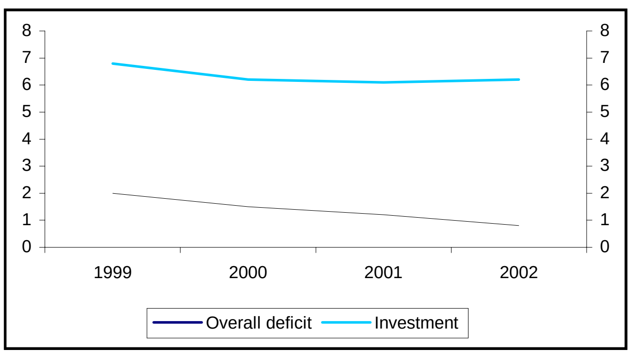
5.1. Overall balance of the general government budget

The strict budgetary stance will keep up the process of gradually reducing the general government deficit, which should amount to 0.8% of gross domestic product in the year 2002. With the deficit being reduced by 1.2 percentage points of GDP, the level of public investment expenditure as a proportion of GDP will remain stable thanks to larger savings on current expenditure, around 0.5 of a percentage point of GDP. The current balance will be in surplus throughout the period covered by the Programme, rising from 1.9% of GDP in 1999 to 2.4% in 2002.

The growth in primary current expenditure can be accounted for mainly by the expenditure of education and health and also by the increase in social security transfers, in particular higher spending on pensions linked to the ageing of the population.

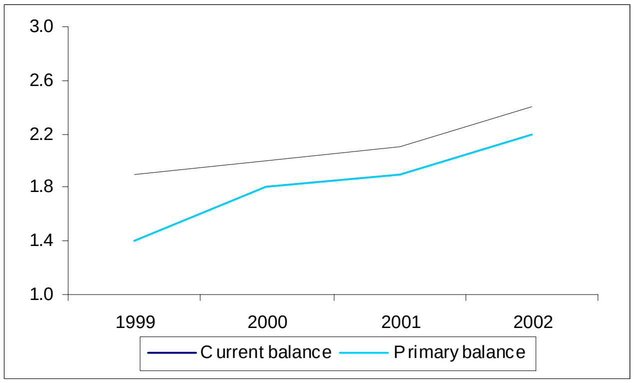
The restraint on other items of (primary) current expenditure is to be achieved through deep cuts in operating expenditure and in spending on subsidies. The policy of selective recruitment will be stepped up, and measures that are expected to have a significant impact on productivity will be put into effect.

Figure 2. Overall government deficit and investment
(% of GDP)



The major investment drive will continue, with capital expenditure exceeding 6% of GDP each year. The golden rule for public finances will thus continue to be observed under the programme. The primary balance will rise from 1.4% of GDP in 1999 to 2.2% in 2002.

Figure 3. General government current balance and primary balance
(% of GDP)



The significant improvements to the IT system and the introduction of new tax inspection procedures, e.g. under the new General Tax Law, will bring sizeable gains in the collection of indirect taxes. On the other hand, the need to use non-renewable resources more efficiently should prompt adjustments to or improvements in the specific taxation of those resources.

Table 2. General government accounts*

(PTE billion)

	1999		2000		2001		2002	
	Value	% of GDP	Value	% of GDP	Value	% of GDP	Value	% of GDP
Current revenue	8456.6	41.7	8981.0	41.9	9523.9	42.1	10 097.9	42.2
Current expenditure	8075.3	39.8	8547.6	39.9	9041.1	40.0	9 517.5	39.8
Current balance	381.3	1.9	433.4	2.0	482.8	2.1	580.4	2.4
Capital revenue	584.4	2.9	581.1	2.7	627.2	2.8	701.0	2.9
Capital expenditure	1372.3	6.8	1337.6	6.2	1373.3	6.1	1 472.6	6.2
Capital balance	-787.9	-3.9	-756.4	-3.5	-746.1	-3.3	-771.6	-3.2
Overall balance	-406.6	-2.0	-323.0	-1.5	-263.3	-1.2	-191.2	-0.8
Interest payments	687.4	3.4	708.1	3.3	704.0	3.1	717.7	3.0
Primary balance	280.7	1.4	385.0	1.8	440.7	1.9	526.5	2.2

* Drawn up in accordance with the European System of Accounts (ESA 79).

As far as the different subsectors are concerned, the overall central government deficit will continue to decline appreciably to around -1½% of GDP in 2002; the budget for regional and local government will remain close to balance, while the social security system will be put onto a sounder financial footing in order to enable it to cope with future increases in the system's financing requirements due to the ageing of the population.

5.2. Public debt

5.2.1. Recent developments

Portugal's public debt will remain on the downward path it has been following in recent years and will continue to decline as a percentage of GDP. It is expected to fall from 65% in 1996 to 58% by the end of 1998.

Table 3. Public debt

	General government debt		State government debt	
	PTE billion	% of GDP	PTE billion	% of GDP
1996	10 902.7	65.0	10 207.7	61.4
1997	11 016.9	61.5	10 505.5	58.7
1998	11 115.8	58.0	10 785.3	56.3

Source: Ministry of Finance

5.2.2. Projection to 2002

The main assumptions underlying public debt projections are as follows:

- the overall general government deficit will remain on its downward path in line with the objectives of this programme, falling from 2% of GDP in 1999 to 0.8% of GDP in 2002;
- GDP will grow by an average rate of around 5.6% in nominal terms (3.3% in real terms) between 1999 and 2002;
- central government financial assets, net of reimbursements, will amount in 1999 to around PTE 22.8 billion, rising in subsequent years at the same rate as GDP;
- privatisation receipts (some PTE 100 billion) will be used each year from 2000 onwards for the purpose of repaying government debt;
- short-term interest rates will follow the OECD forecasts. The differential between Portugal and Germany's long-term interest rates in the period covered by this programme will correspond to the normal country-risk premium.

Public debt as a percentage of GDP will follow a downward path until 2002. The underlying assumptions that have been adopted and the achievement of fairly substantial primary surpluses during the projection period will contribute to that trend.

Table 4. Public debt projections

	General government debt		State government debt	
	PTE billion	% of GDP	PTE billion	% of GDP
1999	11 527.9	56.8	11 260.1	55.5
2000	11 956.5	55.8	11 673.9	54.5
2001	12 363.7	54.7	12 065.1	53.4
2002	12 709.7	53.2	12 394.1	51.8

Source: Ministry of Finance

5.2.3. Public debt management strategy

Management of the public debt has been geared to the objectives of minimising the impact of interest-rate volatility on debt-servicing costs and increasing the duration and liquidity of the portfolio, thereby reducing its cost and the associated risk. The new debt management strategy takes into account the prospect of early completion of the process of convergence of domestic interest rates on levels similar to those prevailing in the other economies belonging to the euro area, the low levels to which interest rates have fallen and the new financial area that is about to come into operation with the advent of the single currency, in which Portuguese government debt placements will enter into direct competition with issues by the national treasuries of the other participant countries and by large European companies.

In the years ahead, the measures to be taken will be aimed at safeguarding the effectiveness of debt management in a single market, which will be significantly larger than the existing domestic market.

The situation will be kept under close review and any adjustments made necessary by the arrangements and conditions for placing debt in the new euro area will be introduced swiftly so as to ensure the full success of these operations. Measures will also continue to be taken to widen the investor base and increase the maturity and liquidity of government debt.

5.3. Sensitivity of the general government balance and public debt to economic growth and interest rates

To assess the sensitivity of the general government balance and government debt to different economic growth scenarios and also to fluctuations in interest rates, three alternative assumptions have been taken into consideration: two for the GDP growth rate and one for the interest rate.

***Assumption 1**: the real rate of GDP growth is half a percentage point higher, on annual average, than in the reference (central) scenario*

On this assumption, with other things being equal, the general government deficit in 2002, expressed as a percentage of GDP, is 0.5 of a percentage point lower and the public debt ratio 2 percentage points lower than in the reference scenario.

***Assumption 2**: the real rate of GDP growth is half a percentage point lower, on annual average, than in the reference (central) scenario*

On this assumption, with other things being equal, the general government deficit in 2002, expressed as a percentage of GDP, is 0.5 of a percentage point higher and the public debt ratio 2 percentage points higher than in the reference scenario.

Table 5. Three scenarios for public finances

	1999	2000	2001	2002	1999-2002
Central scenario					
GDP (real rate of growth as %)	3.5	3.2	3.2	3.3	3.3
General govt balance (% of GDP)	-2.0	-1.5	-1.2	-0.8	
Public debt (% of GDP)	56.8	55.8	54.7	53.2	
Upper scenario (GDP growth 0.5 of a percentage point higher)					
GDP (real rate of growth as %)	3.8	3.8	3.7	3.8	3.8
General govt balance (% of GDP)	-1.9	-1.3	-0.8	-0.3	
Public debt (% of GDP)	56.6	55.1	53.4	51.1	
Lower scenario (GDP growth 0.5 of a percentage point lower)					
GDP (real rate of growth as %)	3.2	2.7	2.6	2.8	2.8
General govt balance (% of GDP)	-2.1	-1.8	-1.6	-1.3	
Public debt (% of GDP)	57.0	56.5	56.1	55.2	

Figure 4. Overall general government deficit
(Three scenarios)

percent of GDP

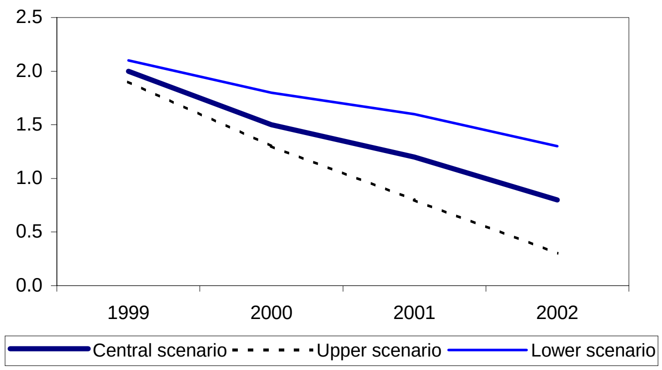
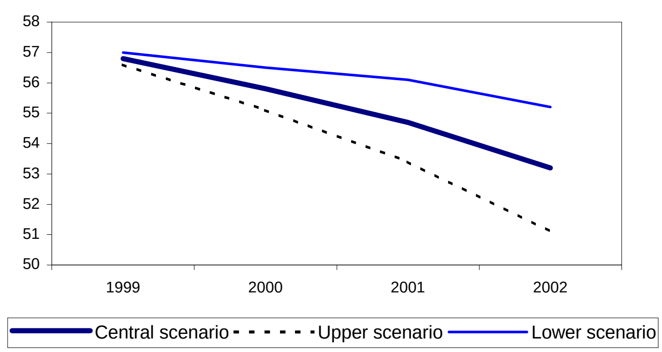


Figure 5. Public debt
(Three scenarios)

percent of GDP



Assumption 3*: interest rates are 1 percentage point higher than in the reference (central) scenario*

In a scenario with higher interest rates, GDP growth will be slightly lower owing to slacker domestic demand. At the end of the programme period, the general government deficit, expressed as a percentage of GDP, is 0.3 of a percentage point higher and the public debt ratio 1.2 percentage points higher.

The impact of a rise in interest rates on government debt is fairly modest, justified by the fact that the bulk of the debt consists of fixed interest-rate borrowings (made in previous years), so that the new interest rates will affect only the servicing costs for new debt issues.

Table 6. Scenario with higher interest rates

Differential in percentage points with respect to the reference scenario

	1999	2000	2001	2002
	Cumulative			
General government deficit (% of GDP)	0.2	0.2	0.3	0.3
General government debt (% of GDP)	0.3	0.6	0.9	1.2