IP/99/67

Brussels, 3 February 1999

Commission assesses the Portuguese stability programme

The European Commission made a recommendation to the Council of Ministers on the Portuguese stability programme. The recommendation was made in accordance with the new reinforced procedures of the Stability and Growth Pact for the monitoring of the economic and budgetary policies of the countries of the European Union (EU). The Portuguese stability programme covers the period 1999-2002 and projects a decline in the general government deficit ratio to 0.8% of GDP and in the gross debt ratio to 53.2% of GDP by the end of the period of the programme. The Commission concludes that, in absolute terms, the envisaged medium-term target is in line with the Stability and Growth Pact requirements. The Commission considers, however, that in structural (cyclically adjusted) terms, the medium term objective is not sufficiently close to the level which would provide security against the deficit breaching 3% of GDP in the face of normal cyclical variations. In view of the current high level of economic activity in Portugal a more rapid decline in the deficit ratio could be accomplished. The Commission believes that the structural measures announced in the programme appropriate and in line with the Broad Economic Policy Guidelines agreed at the Cardiff European Council. On the basis of the Commission's recommendation, the Council is expected to adopt a formal opinion on the Portuguese programme on 8 February 1999.

The Commission recommendation is adopted on the initiative of President Santer and Yves-Thibault de Silguy, the Commissioner responsible for economic and monetary affairs, as part of the procedures in the Stability and Growth Pact for surveillance and co-ordination of national economic and budgetary policies at the level of the EU.

The Stability and Growth Pact, agreed by the Amsterdam European Council in June 1997, requires countries participating in the Euro-zone to present stability programmes to the Council and the Commission. These programmes aim to demonstrate how countries intend to meet the objectives of the Pact and in particular the medium-term goal of a budget close to balance or in surplus. The Commission's analysis considers, in particular, whether the medium term budgetary target provides a sufficient margin for normal cyclical fluctuations without exceeding the reference value of a deficit of 3% of GDP. The programmes cover the current year and at least three future years (the Portuguese programme covers the period 1999-2002).

The Commission's main conclusions are the following:

- the programme is based on a plausible macroeconomic scenario which assumes GDP growth will decelerate from its current high rate towards growth close to trend during the latter part of period covered by the programme; however, the positive effects of EMU could lead to higher growth and faster catching-up of the Portuguese economy in which case inflationary developments would have to be closely monitored;
- the programme builds on the budgetary consolidation achieved in recent years: the deficit fell from 6.1 % in 1993 to 2.3 % in 1998 while the gross debt ratio declined from 63.1 % in 1993 to 58 % of GDP in 1998. Regrettably, despite high output growth and a substantial fall in interest payments, progress in budgetary consolidation stalled in 1998;
- the programme envisages a further reduction of the deficit ratio to 0.8% of GDP by 2002 which will be achieved primarily through an increase in the revenue-to-GDP ratio; this increase will be due mainly to a welcome continued effort to enhance the efficiency of the tax administration rather than to discretionary tax increases;
- the reduction in the expenditure-to-GDP ratio will be comparatively small and can be attributed primarily to a continued decline in interest payments; areas of expenditure increases will be, in particular, the investment in infrastructure and in the upgrading of the country's human capital;
- a stronger emphasis on current expenditure restraint in the overall consolidation strategy would have been desirable; in this respect the programme announces a variety of welcome measures aimed at improving expenditure control;
- in nominal terms the envisaged medium-term deficit target is consistent with the Stability and Growth Pact;
- however, the target only constitutes a minimum position which does not incorporate any additional safety margin to provide for unforeseen shocks in economic activity or in government finances; moreover, in view of the current high level of economic activity in Portugal a more rapid decline in the deficit ratio could be accomplished;
- the planned budgetary and structural reform measures outlined in the programme appear appropriate. Their expeditious and effective implementation will be essential for the achievement of the goals set in the stability programme.

Key figures of the Portuguese stability programme

	1999	2000	2001	2002
Real GDP growth rate (annual % change)	3.5	3.2	3.2	3.3
General government budget deficit (%of GDP)	2.0	1.5	1.2	0.8
Government debt (%of GDP)	56.8	55.8	54.7	53.2
Inflation (Consumption Deflator)	2.0	2.0	2.0	2.0
Employment growth (annual % change)	0.7	0.5	0.6	0.7

Source: Stability Programme for Portugal (1999-2002).