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DECEMBER 2004 UPDATE OF THE STABILITY PROGRAMME OF SPAIN (2004-2008)

AN ASSESSMENT

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SUMMARY AND CONCLUSIONS[1]

Spain submitted its sixth updated stability programme, covering the period 2004-2008, on 23 December 2004. The information provided in the updated programme complies with the data requirements of the revised code of conduct on the content and format of stability and convergence programmes[2]. However, the updated programme was presented three weeks after the 1 December.

The programme projects GDP growth of 2.6% of GDP in 2004, 2.9% in 2005 and 3.0% thereafter. These are relatively favourable projections for 2005 and 2006 as compared with the Commission services autumn 2004 forecast, which predicts growth at 2.6% and 2.7% respectively. For the outer years of the programme, growth also seems on the high side compared to estimates of trend GDP growth. The macroeconomic scenario in the update projects buoyant domestic demand coupled with a sizeable but narrowing negative contribution to GDP growth of net external demand. The programme's GDP deflator projections are plausible. The update also includes a "moderate growth" scenario, which projects annual GDP growth of 0.5 percentage points lower than in the reference scenario. While the reference scenario seems on the high side, the moderate growth scenario is considered to be on the low side.

The budgetary strategy of the Spanish authorities is summarised in the programme by the statement that "the general principle guiding fiscal policy is that of budgetary stability over the full economic cycle". This general principle could imply the occurrence of budget deficits, in the event of a cyclical slowdown. In this line, the update provides a brief description of the upcoming reform of the General Law on Budgetary Stability that will redefine the concept of stability in terms of the full length of the business cycle. For 2004, a deficit outcome of 0.8% of GDP is estimated. This is due to one-off accounting adjustments consisting of the reclassification into the general government sector of RTVE (the public broadcasting company), as requested by Eurostat, with an impact on the deficit of 0.1% of GDP, and the assumption of RENFE's (the railway network company) debt, decided by the new government in office since April 2004, with an impact of 0.7% of GDP in the 2004 deficit.

Over the period 2005-2008, the update targets small, but rising surpluses; from 0.1% of GDP to 0.4% of GDP at the end of the projection period. Since interest payments are expected to decrease only slightly over the programme period (from 2.1% of GDP in 2005 to 1.9% in 2008), the primary surplus is projected to remain fairly stable (from 2.2% of GDP in 2005 to 2.3% in 2008). While the targets for the general government balance are broadly the same as in the previous update, the targeted primary surpluses are slightly less ambitious (by around 0.3 percentage points of GDP). Based on trend GDP

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[1] This technical analysis, which is based on information available up to 9 February 2005 accompanies the recommendation by the Commission for a Council opinion on the update of the stability programme, which the College adopted on 16 February 2005. It has been carried out by the staff of and under the responsibility of the Directorate-General for Economic and Financial Affairs of the European Commission. Comments should be sent to Javier Yaniz-Igal (e-mail: Javier-Yaniz-Igal@cec.eu.int)

[2] *Revised Opinion of the Economic and Financial Committee on the content and format of the stability and convergence programmes*, document EFC/ECFIN/404/01-Rev 1 of 27.6.2001 endorsed by the Ecofin Council on 10.7.2001.

calculated by the Commission services from the projected growth rates in the update, and after netting out the effect of the 2004 one-off accounting adjustments, the cyclically-adjusted budget balance remains at between 0.2% and 0.5% of GDP throughout the programme period.

The risks attached to the budgetary targets seem broadly balanced. In particular, while the budgetary projections are built upon somewhat favourable growth assumptions, the size of the consolidation envisaged for the entire period is prudent and the update confirms the commitment of the current government to budgetary stability.

In view of this risk assessment, the budgetary stance in the programme is sufficient to maintain the Stability and Growth Pact's medium-term objective of a position of close-to-balance throughout the period. It also provides a sufficient safety margin against breaching the 3% of GDP deficit threshold with normal macroeconomic fluctuations in each year.

According to the update, the debt ratio will decline steadily from 49% in 2004 to 40% in 2008, well below the 60% of GDP reference value. The pace of debt reduction is plausible compared with the Commission services autumn 2004 forecast. The main contribution to debt reduction stems from sustained primary surpluses. A persistent debt-increasing stock-flow adjustment, which adds around 0.7 percentage point to the debt ratio annually is not explained in the programme.

The programme reviews the government's structural reform programme which focuses on increasing productivity growth and strengthening social cohesion. Specifically, it aims to enhance productivity through increased expenditure on R&D, innovation, education and infrastructure. The programme also outlines measures to promote job creation and participation as well as to reduce labour market segmentation. The government plans a reform and simplification of personal and corporate income taxes, starting already this year, but the programme provides no details on this. The aim of this reform is to enhance the neutrality and efficiency of the tax system. In addition, the government wants to take steps towards a better match between contributory efforts and pension benefits while raising the lowest pensions. However, the impact of this potential reform on public finances in the long term, remains unclear.

Spain appears to be in a relatively favourable position with regard to the long-term sustainability of the public finances, despite the projected budgetary cost of an ageing population. Reforms aimed at enhancing long-term sustainability are geared towards increasing labour market participation, maintaining a sound budgetary position which enables debt reduction, and making a more sustainable pension system that would reduce the budgetary impact of ageing. The strategy outlined in the programme is mainly based on the budgetary effects of the reforms, notably the "Pacto de Toledo", and the planned debt reduction enabled by the target of sustaining budgetary surpluses. However, recommendations agreed within the "Pacto de Toledo", especially the reform of the public pension system as also recommended in the broad economic policy guidelines, have not yet been fully translated into a reform agenda. Resolutely implementing such measures would prevent the emergence of unsustainable trends in public finances in the long run, hence contributing to the achievement of sustainability of the public finances over the long-run.

Overall, the economic policies outlined in the update are partly consistent with the country-specific broad economic policy guidelines in the area of public finances. In particular, as regards the recommended reform of the public pension system to ensure the long-term viability of the system, the reform agenda to align contributions and benefits more closely is not yet defined.

In view of the above assessment, it would be appropriate for Spain to prevent the emergence of unsustainable trends in public finances in the long run, in particular through a major reform of the pension system.

Table: Comparison of key macroeconomic and budgetary projections

		2004	2005	2006	2007	2008
Real GDP (% change)	**SP Dec 2004**	**2.6**	**2.9**	**3.0**	**3.0**	**3.0**
	COM Oct 2004	2.6	2.6	2.7	n.a.	n.a.
	SP Jan 2004	*3.0*	*3.0*	*3.0*	*3.0*	*n.a.*
HICP inflation[2] (%)	**SP Dec 2004**	**3.8**	**3.7**	**3.5**	**3.2**	**2.8**
	COM Oct 2004	3.1	2.9	2.5	n.a.	n.a.
	SP Jan 2004	*2.9*	*2.6*	*2.6*	*2.6*	*n.a.*
General government balance (% of GDP)	**SP Dec 2004**	**-0.8**	**0.1**	**0.2**	**0.4**	**0.4**
	COM Oct 2004	-0.6	-0.1	0.0	n.a.	n.a.
	SP Jan 2004	*0.0*	*0.1*	*0.2*	*0.3*	*n.a.*
Primary balance (% of GDP)	**SP Dec 2004**	**1.5**	**2.2**	**2.2**	**2.3**	**2.3**
	COM Oct 2004	1.7	2.1	2.0	n.a.	n.a.
	SP Jan 2004	*2.6*	*2.5*	*2.6*	*2.6*	*n.a.*
Cyclically-adjusted balance (% of GDP)	**SP Dec 2004[1]**	**-0.7**	**0.2**	**0.3**	**0.5**	**0.4**
	COM Oct 2004	-0.7	-0.1	0.0	n.a.	n.a.
	SP Jan 2004[1]	*0.1*	*0.1*	*0.2*	*0.3*	*n.a.*
Government gross debt (% of GDP)	**SP Dec 2004**	**49.1**	**46.7**	**44.3**	**42.0**	**40.0**
	COM Oct 2004	48.2	45.5	42.9	n.a.	n.a.
	SP Jan 2004	*46.6*	*47.7*	*45.7*	*43.8*	*n.a.*

Note:
[1] The commonly agreed methodology based on the production function approach is not yet applied to Spain, pending the resolution of estimation problems. Therefore, cyclically-adjusted balances are calculated by Commission services based on the Hodrick-Prescott filter methodology from the information provided in the programme.
[2] Inflation based on the GDP deflator for the stability programmes.
Sources:
Stability programme (SP); Commission services autumn 2004 economic forecasts (COM); Commission services calculations

1. INTRODUCTION

The sixth update of the Spanish stability programme, covering the period 2004-2008, was approved by the government and submitted on 23 December 2004, three weeks beyond the 1 December deadline set in the code of conduct on the content and format of stability and convergence programmes. The projections provided in the update are consistent with the budgetary targets set in the 2005 Budget Law as approved by the Parliament.

The programme complies with the data requirements of the code of conduct. However, inflation in terms of the HICP measure are missing and no long-term projections are provided. According to the update, it would not appear convenient to provide the outdated available projections when the EPC is expected to produce new ones by mid-2005. In addition, the programme does not give quantitative information on particular budgetary operations in 2004, such as the assumption of the railway network company's (RENFE) debt, the reclassification of RTVE (the public broadcasting company) into the general government sector and other accounting adjustments.

2. MACROECONOMIC DEVELOPMENTS

The programme's estimate of GDP growth is 2.6% in 2004, which is in line with the Commission services autumn 2004 forecast. The underlying external assumptions to the macroeconomic scenario in the update are also consistent with those in the Commission services forecast. According to them, world GDP growth is foreseen to decelerate whereas oil prices are expected to go up. As for the euro area, interest rates are projected to slightly increase.

The programme presents along the programme period somewhat favourable GDP growth projections. Specifically, in 2005 and 2006, GDP growth is estimated at 2.9% and 3.0%, respectively, compared with Commission services forecast of 2.6% and 2.7% for the same years. The programme projects employment growth at or just above 2% in each year, while the unemployment rate decreases from 10.9% in 2004 to 9.6% in 2008. On this basis, compared to the Commission services autumn 2004 forecast, the macroeconomic scenario depicted in the programme appears somewhat favourable.

Table 1: Comparison of macroeconomic developments and forecasts

	2004		2005		2006		2007	2008
	COM	SP	COM	SP	COM	SP	SP	SP
Real GDP (% change)	2.6	2.6	2.6	2.9	2.7	3.0	3.0	3.0
Contributions:								
- Final domestic demand	3.5	4.1	3.4	4.0	3.5	3.7	3.5	3.5
- Change in inventories	0.1	0.2	0.1	0.0	0.1	0.0	0.0	0.0
- External balance on g&s	-1.1	-1.5	-1.0	-1.0	-0.9	-0.7	-0.5	-0.4
Employment (% change)	1.9	2.1	1.9	2.1	1.8	2.2	2.1	2.0
Unemployment rate (%)	11.1	10.9	10.8	10.4	10.6	10.1	9.8	9.6
HICP inflation (%)	3.1		2.9		2.5			
GDP deflator (% change)	3.8	3.8	3.6	3.7	3.4	3.5	3.2	2.8
Current account (% of GDP)	-4.2	-4.8	-4.8	-5.3	-5.0	-5.5	-5.6	-5.7
Sources: *Commission services autumn 2004 economic forecasts (COM); stability programme update (SP)*								

Where the composition of growth is concerned, the update predicts growth to be driven by domestic demand, especially private consumption and residential construction, while the external contribution to growth is negative – but declining - throughout the period. For 2004, the programme estimates the negative contribution of the external side at 1½ percentage points, which reflects an even more unbalanced growth path than in the Commission services autumn 2004 forecast (-1.1 percentage points); however, in view of more recent information, both the update and the Commission services forecast seem to underestimate the size of the negative external contribution of the external sector (estimated now to attain almost -2 percentage points of GDP). According to the programme, a rebalancing of growth composition is projected from 2005 to 2008, when the contribution from the external sector is expected to fall from -1.0% of GDP to -0.4%. In particular, for 2005 and 2006, the programme's figures are broadly in line with those in the Commission services autumn 2004 forecast (-1.0% and -0.9% respectively). Nevertheless, as for 2004, such projections may be underestimating the negative contribution of the external side to Spanish GDP growth.

The negative contributions to GDP growth of the external sector presented in the update are mirrored by a steady deterioration of net borrowing vis-à-vis the rest of the world, from 3.6% of GDP in 2004 to 4.8% of GDP in 2008. These figures, together with those for net lending/net borrowing for the general government sector, allow calculating the net borrowing requirements for the private sector. Specifically, between 2004 and 2006, the update shows a more acute deterioration of private balances than in the Commission services autumn 2004 forecast. Such a worsening would be consistent not only with the deterioration of the external sector, but also with the expected recovery of business investment.

Table 2: Sources of potential output growth

	2004		2005		2006		2007	2008
	COM	SP[3]	COM	SP[3]	COM	SP[3]	SP[3]	SP[3]
Potential GDP growth[1]	3.1	3.2	3.1	3.2	2.9	3.2	2.7	2.5
Contributions:								
- Labour	1.8	1.8	1.7	1.8	1.6	1.7	1.3	1.1
- Capital accumulation	1.3	1.3	1.3	1.4	1.3	1.4	1.4	1.4
- TFP	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Output gap[1,2,4]	-	-	-	-	-	-	-	-

Notes:
[1]based on the production function method for calculating potential output growth
[2]in percent of potential GDP
[3]Commission services calculations on the basis of the information in the stability programme update (SP)
[4]The commonly agreed methodology based on the production function approach is not yet applied to Spain, pending the resolution of estimation problems. Therefore, cyclically-adjusted balances are calculated based on the Hodrick-Prescott (HP) filter methodology. That is why output gaps based on potential GDP growth are not shown in the table.

Sources: Commission services autumn 2004 economic forecasts (COM); Commission services calculations

Nominal GDP growth in 2004 is estimated at 6.5% in the update, fully in line with the Commission services autumn 2004 forecast. For 2005 and 2006 the programme projects nominal GDP growth at 6.7% and 6.6%, respectively, around 0.5 percentage points higher than the Commission services autumn 2004 forecast (6.2% in both years). This difference stems mainly from a higher estimate of real GDP growth in the update, whereas he inflation projections (measured by the change in the GDP deflator) in the update are in line with those in the Commission services autumn 2004 forecast: 3.7% and 3.5% for 2005 and 2006, respectively, in the update, compared to 3.6% and 3.4% in the Commission services autumn 2004 forecast. Beyond 2006, the update projects a moderate deceleration of inflation (again on the GDP deflator), from 3.5% in 2006 to 2.8% in 2008, which seems plausible.

It is worth noting that cumulated inflation differentials between Spain and the EU trade partners are dragging competitiveness and might jeopardise sustained growth in the long term. These differentials, coupled with a strong productivity growth slowdown, are behind the above-mentioned deterioration in the external position, which is likely to be maintained in the period covered by the programme.

In addition to the macroeconomic scenario discussed above, the update considers a "moderate growth" scenario, although without providing the full set of macro and budgetary projections. According with the data provided in the update annual GDP will grow by 2.4% in 2005 and 2.5% thereafter. In this alternative scenario, the GDP deflator is projected to increase by slightly less than in the baseline one: 3.5%, 3.4%, 3.0% and 2.7% in 2005, 2006, 2007 and 2008, respectively. Employment is also less dynamic in the moderate growth scenario, growing around 1.6% throughout the programme period. Finally, although the "moderate growth" scenario does not include data on the current account, net borrowing vis-à-vis the rest of the world improves by around 0.4% of GDP, compared with the reference scenario. Growth projections in the Commission services autumn 2004 forecast fall in between the two scenarios sketched in the update. Therefore, while the baseline one can be considered as relatively optimistic, as compared with Commission services autumn 2004 forecast, the moderate growth scenario is on the low side.

3. BUDGETARY IMPLEMENTATION IN 2004

The estimated budgetary outturn for 2004 in the update is broadly in line with the projection in the Commission services autumn 2004 forecast. The current update projects a deficit of 0.8% of GDP, which is close to the corresponding figure in Commission services autumn 2004 forecast of 0.6% of GDP. Total revenues are estimated at 39.9% of GDP, barely changed from the 2003 outturn, while primary expenditure is affected by some one-off accounting adjustments and interest payments decrease by 0.2 percentage points of GDP (to 2.3%). This reduction of interest payments is the result of lower interest rates.

The one-off accounting adjustments consist of the reclassification into the general government sector of RTVE (the public broadcasting company), as requested by Eurostat, and the assumption of RENFE's (the railway network company) debt, decided by the new government in office since April 2004. Although the update does not provide detailed quantitative information on the budgetary impact of these accounting adjustments, it is possible to obtain the corresponding figures on the basis of other official sources. Except for the annual RTVE deficit (at around 0.1% of GDP), the reclassification of RTVE does not affect the general government balance and translates directly into a debt increase by the amount of RTVE's cumulated debt (about € 8,000 million or around 1 percentage point of GDP; see section 5 below on the debt ratio). Conversely, the assumption of RENFE's debt results in higher than initially planned gross fixed capital formation and capital transfers by the general government sector with an impact on the 2004 deficit of 0.7% of GDP. This reclassification neither involves any backward revision nor has carryover effects in the coming years

After netting out these one-off adjustments, which amount to 0.8 percentage points of GDP, the budgetary outturn for 2004 (an estimated deficit of 0.8% of GDP) is practically balanced and fully consistent with the previous update, which targeted a balanced budget.

4. BUDGETARY TARGETS AND THE MEDIUM-TERM PATH OF THE PUBLIC FINANCES

4.1. Evolution of budgetary targets in successive programmes

Table 3 shows that the budgetary targets set in successive programmes have remained broadly unchanged, once the above-mentioned one-off accounting adjustments in 2004 are excluded (related to RENFE's debt assumption and the reclassification of RTVE into the general government sector). The 2005 budget targets a small surplus of 0.1% of GDP. According to the update, this surplus should increase over the programme period to attain 0.4% by 2008. Regarding expenditures, with the exception of 2003, when they turned out to be lower than projected in the 2002 update, the projections in subsequent updates have been revised slightly upwards, although maintaining stable as a percentage of GDP[3]. Although following a slightly increasing path, revenues are also projected to remain broadly stable at around 40% of GDP, somewhat higher than initially projected.

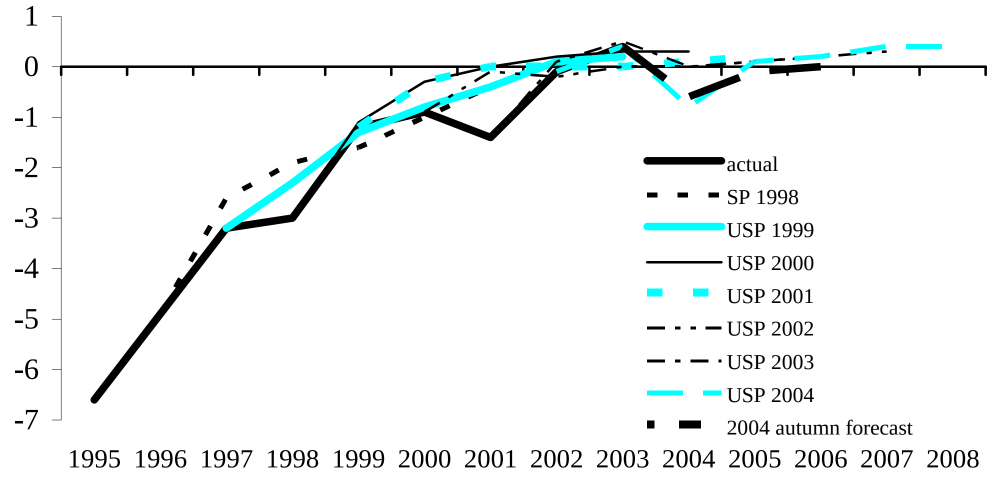
Table 3: Evolution of budgetary targets in successive programmes

		2003	2004	2005	2006	2007	2008
General government balance (% of GDP)	**SP December 2004**	**0.4**	**-0.8**	**0.1**	**0.2**	**0.4**	**0.4**
	SP January 2004	0.5	0.0	0.1	0.2	0.3	
	SP December 2002	*0.0*	*0.0*	*0.1*	*0.2*		
General government expenditure (% of GDP)	**SP December 2004**	**39.6**	**40.6**	**39.8**	**39.8**	**39.8**	**39.8**
	SP January 2004	39.6	40.0	39.9	39.8	39.7	
	SP December 2002	*39.8*	*39.7*	*39.7*	*39.6*		
General government revenues (% of GDP)	**SP December 2004**	**40.0**	**39.9**	**39.9**	**40.0**	**40.1**	**40.2**
	SP January 2004	40.0	40.0	40.0	40.0	40.0	
	SP December 2002	*39.8*	*39.8*	*39.8*	*39.8*		
Real GDP (% change)	**SP December 2004**	**2.5**	**2.6**	**2.9**	**3.0**	**3.0**	**3.0**
	SP January 2004	2.3	3.0	3.0	3.0	3.0	
	SP December 2002	*3.0*	*3.0*	*3.0*	*3.0*		
Sources: *Stability programmes (SP)*							

Figure 1 shows that the budgetary targets set in previous updates have been broadly achieved. It is worth noting that the overachievement of the initial target for 2003 took place in a context of significantly lower real growth than expected in the 2002 update. The strong correlation between the different updates and the actual values seems to confirm the Spanish authorities' commitment to budgetary stability.

[3] Figures for 2004 are affected by the one-off accounting adjustments.

Figure 1: Evolution of targets for the general government balance in successive programmes (% of GDP)



<u>Sources</u>:
Commission services autumn 2004 economic forecasts; stability programmes

4.2. Budgetary targets in the updated programme

The budgetary strategy of the Spanish authorities is summarised in the programme by the statement that "the general principle guiding fiscal policy is that of budgetary stability over the full economic cycle". This general principle could eventually lead to budgetary deficits under certain circumstances (see box 1). However, the update does not target a deficit position over the programme period.

The 2005 Budget Law targets a marginal surplus of 0.1% of GDP, fully in line with the targets for 2005 in previous programmes. Small surpluses are planned for the rest of the programme period (0.2%, 0.4% and 0.4% of GDP for 2006, 2007, 2008 respectively). This is broadly in line with the Commission services autumn 2004 forecast for the public deficit (a deficit of 0.1% of GDP in 2005 and, on a no-policy change basis, a balanced budget for 2006). No significant fiscal efforts appear necessary to attain these targets, since the primary surplus is expected to remain broadly stable at around 2.3% during the programme period. Nevertheless, compared with the previous update, the targeted primary surpluses are slightly less ambitious, by around 0.3 percentage points of GDP annually.

Looking at the breakdown by government subsector, in 2004, the State government is estimated to have registered a deficit of 1.8% of GDP (due not only to the one-off accounting adjustments, but also to a transfer to the Government of Andalusia linked to the recognition of the so-called "historical debt"), while regional and local governments recorded a small surplus. The State deficit is projected to improve to 0.5% of GDP in 2005 and to 0.3% of GDP in both 2006 and 2007. The regional and local governments are expected to record a deficit of 0.1% of GDP in 2005 and 2006, in contrast with the provisions of the General Law on Budgetary Stability (see Box 1). Only in 2007 are regional and local governments expected to return to balance. The social security subsector is envisaged to keep recording high surpluses of around 0.7% of GDP annually, underpinned by buoyant employment creation. No data have been provided in the update for 2008.

Table 5 shows the cyclically-adjusted budget balances (CAB) calculated by Commission services on the basis of trend GDP[4]. The cyclically-adjusted balance deteriorates transitorily in 2004 as a result of the above-mentioned one-off accounting measures. Excluding this effect, the cyclically-adjusted balance remains at around 0.4% of GDP over the programme period, only slightly higher than in the Commission services autumn 2004 forecast. The cyclically-adjusted primary balance is also foreseen to remain largely stable at around 2.3% of GDP during the programme period. Therefore, fiscal policy in Spain can be considered neutral.

Revenues are projected in the update to increase by 0.3% of GDP (from 39.9% in 2004/2005 to 40.2% in 2008) during the programme period. This is broadly in line with the Commission services autumn 2004 forecast, which projects revenues at 40.0% of GDP in 2005 and, on a no-policy change basis, 40.2% of GDP in 2006. The slight increase projected in the update stems from almost all categories of taxes. In fact, only direct tax receipts on households are projected to remain unchanged in terms of GDP. Although showing a slightly upward slope, the revenue path does not depart significantly from that projected in the previous update. The programme does not provide further information about tax measures planned.

Expenditures as a percentage of GDP remain, according to the update, unchanged at 39.8% of GDP between 2005 and 2008 (the 0.8% drop in 2005 is due to the one-off accounting adjustments in 2004 mentioned above). This is slightly below the Commission services autumn 2004 forecast of 40.1% and 40.2% for 2005 and 2006. While **interest payments** are projected to decline by 0.4% of GDP due to debt reduction and interest rate assumptions to end at 1.9% of GDP in 2007/2008, **current primary expenditure** is projected to remain broadly stable during the programme period at close to 40% of GDP. These figures are deemed in the update to be consistent with the announced efforts aiming at promoting education, active labour market policies, social cohesion and productivity enhancing expenditure such as innovation and R&D (see Box 2). However, the programme does not provide the breakdown of such efforts from 2006 onwards. As for capital expenditure, **gross fixed capital formation** is also projected to slightly increase in terms of GDP along the programme period. According to the update they should rise from 3.5% of GDP in 2003 to 3.8% of GDP in 2008. The figure for 2004 is affected by the one-off accounting adjustments.

The risks to the budgetary targets seem broadly balanced. On the one hand, since the budgetary projections in the update are based on somewhat favourable growth assumptions, revenue projections might be on the high side. However, the slight increase foreseen over the programme period does not look particularly demanding. Likewise, the expenditure projections, which merely require a stabilisation of the expenditure ratio from 2005 onwards, appear plausible, especially in view of the slight decline in the interest burden. Furthermore, the Spanish government has a good track record of achieving the budgetary targets (with the exception of 2004, when the estimated deficit reflected the impact of one-off accounting operations). Finally, the projections by sub-sector have been adjusted compared to those in the previous programme, and, in the light of the recent experience, appear more realistic.

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[4] As indicated above, Spain continues to use the HP-filter to derive trend GDP.

Table 4: Composition of the budgetary adjustment

(% of GDP)	2003	2004	2005	2006	2007	2008	Change: 2008-2004
Revenues	40.0	39.9	39.9	40.0	40.1	40.2	**0.3**
of which:							
- Taxes & social security contributions	36.2	36.3	36.4	36.4	36.5	36.6	**0.3**
- Other (residual)	3.8	3.6	3.5	3.6	3.6	3.6	**0.0**
Expenditure	39.6	40.6	39.8	39.8	39.8	39.8	**-0.8**
of which:							
- Primary expenditure	37.1	38.3	37.7	37.8	37.9	37.9	**-0.4**
of which:							
Gross fixed capital formation	3.5	3.7	3.6	3.6	3.7	3.8	**0.1**
Consumption	na	na	na	na	na	na	na
Transfers & subsidies	na	na	na	na	na	na	na
Other (residual)	na	na	na	na	na	na	na
- Interest payments	2.5	2.3	2.1	2.0	1.9	1.9	**-0.4**
Budget balance	**0.4**	**-0.8**	**0.1**	**0.2**	**0.4**	**0.4**	**1.2**
Primary balance	**2.9**	**1.5**	**2.2**	**2.2**	**2.3**	**2.3**	**0.8**
Sources: *Stability programme update; Commission services calculations*							

In view of this risk assessment, the budgetary stance in the programme seems sufficient to maintain the Stability and Growth Pact's medium-term budgetary objective of a budgetary position of close-to-balance throughout the programme period (the deviation in 2004 was due to one-offs). Furthermore, it seems sufficient to provide a safety margin against breaching the 3% of GDP deficit threshold with normal cyclical fluctuations in each year.

Box 1: The reform of the General Law on Budgetary Stability

The new government in office since April 2004 has announced a reform of the General Law on Budgetary Stability, which stipulates that public finances at the local and regional levels should be balanced yearly. The main goal of the reform is the reinterpretation of the concept of budgetary stability throughout the cycle. Accordingly, the economy could register transitory deficits in slowdowns and surpluses in booms. In this respect, the general government account would be balanced in cyclically-adjusted terms. The reform will specify the circumstances in which non-compliance with the stability principle could be permitted. No draft of the reform has been proposed yet.

The current Law gives very limited margin for automatic stabilisers to play a significant role allowing for deficit under restricted circumstances, such as an unexpected external shock. In case of a deficit, the present wording of the Law requires that a three-year correction programme be presented. The reform aims at strengthening the stabilising role of fiscal policy by allowing the free operation of automatic stabilisers over the cycle.

Additionally, the reform aims to enhance the transparency of the public finances, including through higher budgetary information requirements for regional and local governments. The transposition to sub-national governments of the budgetary instruments that have proved so useful at the central government level would be a major step forward to consolidate the already strong commitment of Spain to budgetary stability.

Table 5: Output gaps and cyclically-adjusted (primary) balances (CA(P)B)[4]

	2003		2004		2005		2006		2007	2008	Change: 2008-2004
	COM	SP	COM	SP	COM	SP	COM	SP	SP	SP	SP
Budget balance[2]	0.4	0.4	-0.6	-0.8	-0.1	0.1	0.0	0.2	0.4	0.4	1.2
Output gap[1,3]	0.4	0.2	0.2	-0.2	-0.1	-0.2	-0.2	-0.2	-0.2	-0.1	0.1
CAB[1,2]	0.2	0.3	-0.7	-0.7	-0.1	0.2	0.0	0.3	0.5	0.4	1.1
CAPB[1,2]	2.7	2.8	1.7	1.6	2.1	2.3	2.1	2.3	2.4	2.3	0.7

Notes:
[1]SP (stability programme): Commission services calculations on the basis of the information in the programme
[2]in percent of GDP
[3]in percent of trend GDP
Sources: Commission services autumn 2004 economic forecasts (COM); Commission services calculations

4.3. Sensitivity analysis

Commission services' simulations of the cyclically-adjusted balance under the assumptions of (i) a sustained 0.5 percentage point deviation from the growth targets in the programme over the 2004-2008 period; (ii) trend output based on the HP-filter and (iii) no policy response (notably, the expenditure level is as in the central scenario[5]), reveal that, by 2008, the cyclically-adjusted balance is 0.7 percentage points of GDP below the central scenario. Hence, in the case of persistently lower growth, additional measures (from 0.3 percentage points of GDP in 2005 to 0.6 percentage points in 2008) would be necessary to keep the public finances on the path targeted in the central scenario. Taking into account that the risks associated with the macroeconomic framework of the programme are mainly to the downside, and considering that the Commission services growth projections are between the baseline and the simulated low growth scenario, the achievement of the budgetary targets in the programme would only require a moderate fiscal effort in case of a negative growth surprise of 0.5%.

5. EVOLUTION OF THE DEBT RATIO

Table 6 presents the evolution of the debt-to-GDP ratio and its driving forces. According to the update the debt ratio will decline steadily from 49% in 2004 to 40% in 2008, thus remaining well below the 60% of GDP Treaty reference value. The pace of debt reduction is plausible as compared with the Commission services autumn 2004 forecast.

The contribution of the primary surplus to the change in the debt ratio is above 2 percentage points from 2005 onwards. The interaction between interest payments and nominal growth (so-called snow-ball effect) also serves to reduce the debt ratio over the programme period. These contributions are largely in line with the Commission services' projections. However, the main difference between the debt figures from the update and those from the Commission services autumn 2004 forecast stems from stock-flow adjustments of around 0.7% of GDP annually in the update. The update, however, gives no explicit information about the below-the-line operations that add up to the stock-flow adjustment.

[5] The effect of lower/higher growth on revenues is captured by using the conventional sensitivity parameters adopted in cyclical adjustment procedures.

Table 6: Debt dynamics

	average 2000-2003	2004		2005		2006		2007	2008
	COM	COM	SP	COM	SP	COM	SP	SP	SP
Government gross debt ratio	55.9	48.2	49.1	45.5	46.7	42.9	44.3	42.0	40.0
Change in debt ratio (1 = 2+3+4)	-3.1	-2.5	-1.6	-2.7	-2.4	-2.6	-2.4	-2.3	-2.0
Contributions:									
- **Primary balance** (2)	-2.7	-1.7	-1.5	-2.1	-2.2	-2.0	-2.2	-2.3	-2.3
- **"Snow-ball" effect** (3)	-1.0	-0.7	-0.8	-0.6	-1.0	-0.6	-0.9	-0.7	-0.4
- Interest expenditure	2.9	2.4	2.3	2.2	2.1	2.1	2.0	1.9	1.9
- Real GDP growth	-1.7	-1.2	-1.2	-1.2	-1.3	-1.1	-1.3	-1.3	-1.2
- Inflation (GDP deflator)	-2.3	-1.9	-1.9	-1.7	-1.7	-1.5	-1.6	-1.4	-1.2
- **Stock-flow adjustment** (4)	0.6	0.0	0.7	0.0	0.8	0.0	0.7	0.7	0.7
- Cash/accruals	0.0								
- Accumulation of financial assets	0.6								
of which: Privatisation proceeds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
- Valuation effects & residual adj.	0.0								

Note:
The change in the gross debt ratio can be decomposed as follows:

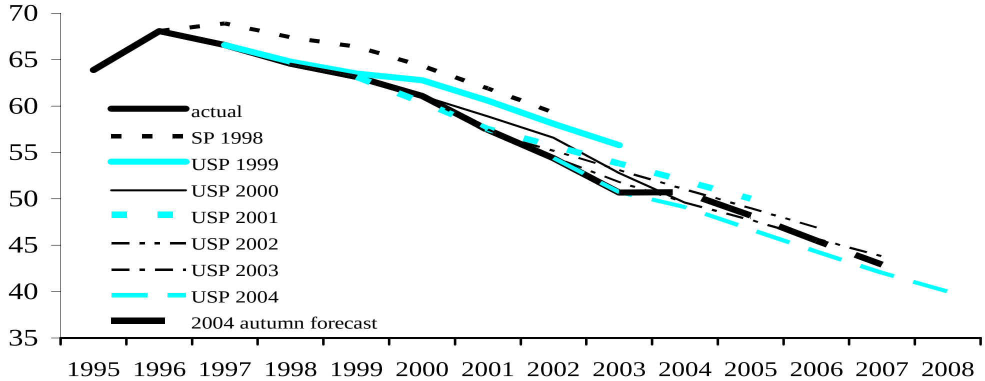
$$\frac{D_t}{Y_t} - \frac{D_{t-1}}{Y_{t-1}} = \frac{PD_t}{Y_t} + \left(\frac{D_{t-1}}{Y_{t-1}} * \frac{i_t - y_t}{1 + y_t} \right) + \frac{SF_t}{Y_t}$$

where t is a time subscript; D, PD, Y and SF are the stock of government debt, the primary deficit, nominal GDP and the stock-flow adjustment respectively, and i and y represent the average cost of debt and nominal GDP growth. The term in parentheses represents the "snow-ball" effect.

Sources:
Stability programme update (SP); Commission services autumn 2004 economic forecasts (COM); Commission services calculations

The projected pace of debt reduction does not seem to be subject to sizeable risks. According to the update, even if the alternative "moderate growth" scenario would materialise, the debt ratio would fall to 42.6% by the end of the projection period, i.e. only 2.6 percentage points of GDP higher than in the reference scenario.

Figure 1: Evolution of debt ratio targets in successive programmes (% of GDP)



Sources:
Commission services autumn 2004 economic forecasts; stability programmes

6. STRUCTURAL REFORM AND THE QUALITY OF PUBLIC FINANCES

According to the update, the increase of productivity growth, while enhancing social cohesion, is among the policy priorities of the government.

- Significant budgetary efforts on R&D, innovation, education and infrastructure have been planned in the 2005 Budget Law to enhance productivity (see Box 2).

- The government also aims to maintain sound job creation. The government is committed to carrying out significant efforts so as to reduce segmentation, facilitate job search (through more efficient public employment services) and promote on-the-job training. However, no further details are provided in the update on when or how these measures will be implemented.

- In order to enhance the neutrality of the tax system, the government plans a reform and simplification of personal and corporate income taxes. The government plans to launch the reform already this year, but no further details have been provided in the update. In addition, stricter controls aiming at preventing tax fraud and tax avoidance will be implemented. The government wants to pay special attention to indirect taxation and the construction sector, where fraud seems to be larger. The programme announces the creation of a State Agency for the evaluation of the quality of public services and policies aimed at improving the efficiency and transparency of the public sector.

- Although the update does not give details, it expresses the government's commitment to take steps towards a better match between contributory efforts and pension benefits while raising the lowest pensions. However, the degree of compatibility of this potential reform with the goal of sustainable public finances in the long term remains unclear.

- Finally, the update provides a brief description of the coming reform of the General Law on Budgetary Stability (see Box 1 above) aimed at strengthening the stabilising role of fiscal policy.

Box 2: Productivity-enhancing budgetary measures in 2005

According to the 2005 Budget Law, the productivity-enhancing budgetary measures will concentrate on higher expenditure efforts on R&D, innovation, education and investment in infrastructure. Specifically, the budget encompasses a 25% increase of funds devoted to R&D policies, including an endowment of € 3 billion (about 0.4% of GDP), which will be allocated to research on information technologies (IT). Most of this endowment is meant to translate into loans to selected projects at low or zero interest rates. The government is committed to doubling expenditure on R&D within four years in order to catch up with the euro area average.

The central government aims to increase grants and allowances significantly. Expenditure on education will increase by 6% of GDP in nominal terms with respect to the total amount allocated in the previous year. Most of this increase will translate into more and higher grants. This increase is of the same order of magnitude that the nominal GDP growth in both the update and the Commission services autumn 2004 forecast.

Finally, the budget gives priority to investment in infrastructure, with spending planned to increase by 9.1% in nominal terms. Special attention will be paid to improving terrestrial transport, notably motorways and the promotion of high-speed railway network.

7. THE SUSTAINABILITY OF THE PUBLIC FINANCES

The assessment of the sustainability of Spanish public finances is based on an overall judgement of the results of quantitative indicators and qualitative features. The quantitative indicators project debt developments according to two different scenarios to take into account different budgetary developments over the medium term. The "programme" scenario (baseline) assumes that the medium-term objective set in the programme is actually achieved, while the "2004" scenario assumes that the underlying primary balance remains throughout the programme period at the 2004 level.

The graph below presents gross debt developments according to the two different scenarios. It should be noted that the present update does not include projections of age-related expenditures. The Commission's projections reported here are therefore based on the previous update and are complemented with the harmonised Economic Policy Committee projections. These are subject to considerable uncertainty as a result of the likely changes in demographic scenarios[6]. On this basis, age-related expenditure is foreseen to increase by 6% of GDP between 2009 and 2050. The gross debt ratio is projected to decline steadily over the next 25 years. Thereafter, as the costs of ageing kicks in, gross debt starts to rise but remains below 60% of GDP at the end of the projection period[7].

On the basis of the debt projections, it is possible to calculate a set of sustainability indicators to measure the gap between the current policies and a sustainable one. The S1 indicator shows the permanent change in the primary balance in order to have a debt to GDP ratio in line with the 60% of GDP Treaty reference value in the very long run (year 2050)[8]. S2 shows the gap between the current tax policies and those that would ensure respect of the intertemporal budget constraint given the future impact of ageing on public expenditure, namely the change in the tax ratio that would equate the present discounted value of future primary balances to the current stock of gross debt. According to the latter, in order to tackle the cost of ageing entirely through a budgetary strategy, Spain should raise its tax ratio by about 1.9 percentage points compared with the projected one at the end of the programme period. This would lead to a negative sustainable debt ratio by the middle of the century[9]. The budgetary effort over the first 5 years of the projections (i.e. after the end of the programme period) to respect the intertemporal budget constraint requires a primary surplus of around 4% of GDP on average, 2 percentage points higher than targeted for the last year of the programme period (measured in underlying terms).

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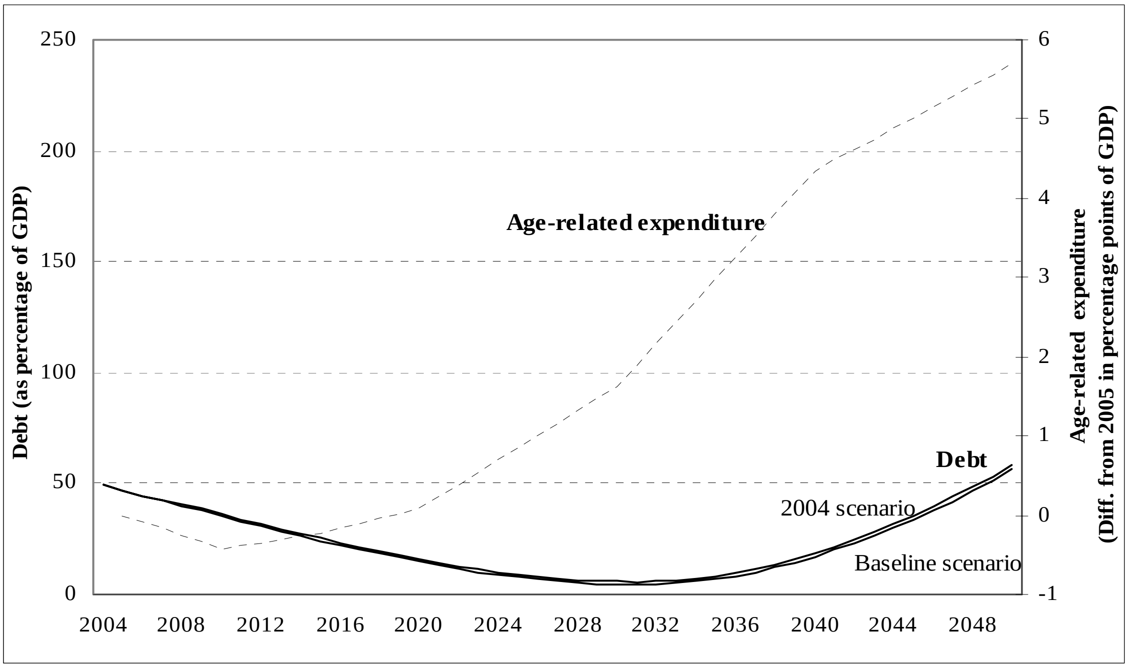
6 The Ageing Working Group and the Economic Policy Committee is currently in the preparatory phase of preparing new budgetary expenditure projections until 2050 on the basis of Eurostat's updated demographic projections. These are expected to be available by mid-2005.

7 It should be recalled that, being a mechanical, partial equilibrium analysis, projections are in some cases bound to show highly accentuated profiles. As a consequence, the projected evolution of debt levels is not a forecast of likely outcomes and should not be taken at face value.

8 The respect of the underlying debt path does not ensure sustainability over an infinite horizon, but only that debt remains below 60% up to 2050. In most cases, this would imply an increasing trend and possible imbalances after the end of the projection period.

9 The debt ratio of almost -70% in 2050 according to the S2 indicator illustrates that the sustainability gap is higher in order to ensure a sustainable evolution of gross debt beyond 2050, compared with the S1 indicator, which illustrates that a lower budgetary strengthening is compatible with the 60% reference value in 2050.

Long-term sustainability: summary results



Sustainability indicators

	S1*	S2**	RPB***
Baseline scenario	-0.1	1.9	4.3
2004 scenario	0.0	1.9	4.3

Notes:
* It indicates the required change in tax revenues as a share of GDP over the projection period that guarantees to reach debt to GDP ratio of 60% of GDP in 2050.
** It indicates the change in tax revenues as a share of GDP that guarantees the respect of the intertemporal budget constraint of the government, i.e., that equates the actualized flow of revenues and expenses over an infinite horizon to the debt as existing at the outset of the projection period; p.m. debt to GDP ratio in 2050: -68.0%
*** Based on S2, the Required Primary Balance (RPB) indicates the average minimum required cyclically adjusted primary balance as a share of GDP *over the first five years* of the projection period that guarantees the respect of the intertemporal budget constraint of the government for this period.

In interpreting these results, several factors must be taken into account.

First, the projected reduction of the gross debt ratio towards levels of 40% seems attainable on the basis of the medium-term budgetary plans.

Second, Spain has been taken for some years significant measures to meet the costs of an ageing population. The strategy is based on several building blocks: i) structural reforms aimed at strengthening the supply-side of the economy (increase participation rates, raise productivity growth), ii) the ongoing development of a multi-pillar pension system[10], and iii) measures aimed at rationalising the use and cost of medicines.

10 The accumulation of reserves in the Social Security Reserve Fund should help in coping with the future cost of ageing. This Fund's reserves consisted almost exclusively (to 95%) of Spanish government bonds and bills in November 2004, which are netted out in the calculation of Maastricht gross debt.

However, given the significant budgetary impact of ageing in Spain, such strategy could not be sufficient to fully ensure the long-run sustainability of public finances. Consequently, as recommended in the Broad Economic Policy Guidelines, it is necessary to complement the initiatives above by taking appropriate steps to implement a major reform of the pension system. The Permanent Commission of the "Pacto de Toledo" regularly reviews progress in the pension system towards financial sustainability. In line with these recommendations, the update acknowledges the need for strengthening the match between pension contributions and benefits. However, the Permanent Commission agrees on broad guidelines, but does not make concrete proposals on measures, such as for instance the number of contributory years, the retirement age and the replacement ratio.

* * *

Annex 1: Summary tables from the stability programme update

Table A 0: Basic assumptions

	2004	2005	2006	2007	2008
Euro area short-term interest rate (annual average)	**2.1**	**2.6**	**3.5**	**-**	**-**
Euro area long-term interest rate (annual average)	**4.2**	**4.6**	**4.8**	**-**	**-**
USA: short-term (3-month money market)	**-**	**-**	**-**	**-**	**-**
USA: long term (10-year government bonds)	**-**	**-**	**-**	**-**	**-**
US$/€ exchange rate (annual average)	**1.23**	**1.24**	**1.24**	**-**	**-**
Nominal effective exchange rate (euro area)	**2.8**	**0.6**	**0.3**		
World GDP growth rate	**-**	**-**	**-**	**-**	**-**
World excluding EU, GDP growth	**5.7**	**4.8**	**4.6**	**-**	**-**
USA GDP growth	4.4	3.0	2.9	**-**	**-**
Japan GDP growth	4.2	2.1	2.3	**-**	**-**
EU GDP growth	**2.5**	**2.3**	**2.4**	**-**	**-**
Growth relevant foreign markets	**-**	**-**	**-**	**-**	**-**
World import volumes, excluding EU	**11.6**	**8.8**	**8.3**	**-**	**-**
World import prices (manufactured goods in USD)	**-**	**-**	**-**	**-**	**-**
Oil prices (Brent USD/barrel)	**39.3**	**45.1**	**40.1**	**-**	**-**
Non-oil commodities prices (in USD)	12.9	-2.9	-0.5	**-**	**-**

Table A 1. Growth and associated factors

	2003	2004	2005	2006	2007	2008
GDP growth at constant market prices (7+8+9)	**2.5**	**2.6**	**2.9**	**3.0**	**3.0**	**3.0**
GDP *level* at current market prices (€ bn.)	**744.8**	**739.2**	**846.3**	**902.5**	**959.3**	**1016.1**
GDP deflator	**4.0**	**3.8**	**3.7**	**3.5**	**3.2**	**2.8**
HICP change	**-**	**-**	**-**	**-**	**-**	**-**
Employment growth [11]	**1.7**	**2.1**	**2.1**	**2.2**	**2.1**	**2.0**
Unemployment rate	11.3	10.9	10.4	10.1	9.8	9.6
Labour productivity growth	0.7	0.5	0.8	0.8	0.9	1.0
Sources of growth: percentage changes at constant prices						
1. Household and NPISHs consumption expenditure	**2.9**	**3.3**	**3.1**	**3.0**	**2.9**	**2.9**
2. Government consumption expenditure	**3.9**	**4.2**	**3.5**	**3.3**	**3.3**	**3.3**
3. Gross fixed capital formation	**3.2**	**4.5**	**5.7**	**4.8**	**4.3**	**4.1**
4. Changes in inventories and net acquisition of valuables [12]	**0.1**	**0.2**	**0.0**	**0.0**	**0.0**	**0.0**
5. Exports of goods and services	**2.6**	**5.1**	**6.4**	**6.8**	**6.9**	**6.9**
6. Imports of goods and services	**4.8**	**8.9**	**8.5**	**7.5**	**7.0**	**6.9**
Contribution to GDP growth						
7. Final domestic demand	**3.3**	**4.1**	**4.0**	**3.7**	**3.5**	**3.5**
8. Change in inventories and net acquisition of valuables	**0.1**	**0.2**	**0.0**	**0.0**	**0.0**	**0.0**
9. External balance of G&S	**-0.8**	**-1.5**	**-1.0**	**-0.7**	**-0.5**	**-0.4**

[11] Full-time equivalent, national accounts

[12] Contribution to GDP growth

Table A 2. General government budgetary developments

In % of GDP	2003	2004[13]	2005	2006	2007	2008
Net lending by sub-sectors						
General government	**0.4**	**-0.8**	**0.1**	**0.2**	**0.4**	**0.4**
Central government	**-0.3**	**-1.8**	**-0.5**	**-0.4**	**-0.3**	**-0.3**
State government	**-0.2**	**0.2**	**-0.1**	**-0.1**	**0.0**	**0.0**
Local government	**-0.1**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Social security funds	**1.0**	**0.8**	**0.7**	**0.7**	**0.7**	**0.7**
General government						
Total receipts	**40.0**	**39.9**	**39.9**	**40.0**	**40.1**	**40.2**
Total expenditures	**39.6**	**40.6**	**39.8**	**39.8**	**39.8**	**39.8**
Budget balance	**0.4**	**-0.8 (-0.1)**	**0.1**	**0.2**	**0.4**	**0.4**
Net interest payments	**2.5**	**2.3**	**2.1**	**2.0**	**1.9**	**1.9**
Primary balance [14]	**2.9**	**1.5**	**2.2**	**2.2**	**2.3**	**2.3**
Components of revenues						
Taxes	36.2	36.3	36.4	36.4	36.5	36.6
Social contributions	13.7	13.7	13.7	13.7	13.8	13.8
Interest income	-	-	-	-	-	-
Other	-	-	-	-	-	-
Total receipts	40.0	39.9	39.9	40.0	40.1	40.2
Components of expenditures						
Collective consumption	-	-	-	-	-	-
Social transfers in kind	-	-	-	-	-	-
Social transfers other than in kind	-	-	-	-	-	-
Interest payments	2.5	2.3	2.1	2.0	1.9	1.9
Subsidies	-	-	-	-	-	-
Gross fixed capital formation	3.5	3.7	3.6	3.6	3.7	3.8
Other	-	-	-	-	-	-
Total expenditures	39.6	40.6	39.8	39.8	39.8	39.8

Table A 3. General government debt developments

In % of GDP	2003	2004	2005	2006	2007	2008
Gross debt level	**50.7**	**49.1**	**46.7**	**44.3**	**42.0**	**40.0**
Change in gross debt	**-3.7**	**-1.6**	**-2.5**	**-2.4**	**-2.2**	**-2.1**
Contributions to change in gross debt						
Primary balance	**-2.9**	**-1.5**	**-2.2**	**-2.2**	**-2.3**	**-2.3**
Interest payments	**2.5**	**2.3**	**2.1**	**2.0**	**1.9**	**1.9**
Nominal GDP growth	**-3.4**	**-3.1**	**-3.1**	**-2.9**	**-2.6**	**-2.4**
Other factors influencing the debt ratio	0.1	0.8	0.7	0.7	0.7	0.7
Of which: Privatisation receipts	-	-	-	-	-	-
p.m. implicit interest rate on debt	-	-	-	-	-	-

[13] Figures in parentheses exclude the one-off items in 2004.

[14] Actual balance less net interest payments.

Table A 4. Cyclical developments

In % of GDP	2003	2004[15]	2005	2006	2007	2008
GDP growth at constant prices	**2.5**	**2.6**	**2.9**	**3.0**	**3.0**	**3.0**
Actual balance	**0.4**	**-0.8 (-0.1)**	**0.1**	**0.2**	**0.4**	**0.4**
Interest payments	**2.5**	**2.3**	**2.1**	**2.0**	**1.9**	**1.9**
Trend GDP growth	3.0	3.0	3.0	3.0	2.9	2.9
Output gap	0.2	-0.2	-0.2	-0.2	-0.1	0.0
Cyclical budgetary component	0.1	-0.1	-0.1	-0.1	0.0	0.0
Cyclically-adjusted balance	0.3	-0.7 (0.0)	0.3	0.3	0.4	0.4
Cyclically-adjusted primary balance	2.8	1.6 (2.3)	2.4	2.3	2.3	2.3

Table A 5. Divergence from previous update

In % of GDP	2003	2004	2005	2006	2007
GDP growth					
Previous update	2.3	3.0	3.0	3.0	3.0
Latest update	2.5	2.6	2.9	3.0	3.0
Difference	0.2	-0.4	-0.1	0.0	0.0
Actual budget balance	-	-	-	-	-
Previous update	0.5	0.0	0.1	0.2	0.3
Latest update	0.4	-0.8	0.1	0.2	0.4
Difference	-0.1	-0.8	0.0	0.0	0.1
Gross debt levels	-	-	-	-	-
Previous update	51.8	49.6	47.7	45.7	43.8
Latest update	50.7	49.1	46.7	44.3	42.0
Difference	-1.1	-0.5	-1.0	-1.4	-1.8

Table A 6. Long-term sustainability of public finances

In % of GDP	2000	2005	2010	2020	2030	2040	2050
Total expenditure	-	-	-	-	-	-	-
Old age pensions	-	-	-	-	-	-	-
Health care (including care for elderly)	-	-	-	-	-	-	-
Interest payments	-	-	-	-	-	-	-
Assumptions							
Labour productivity growth	-	-	-	-	-	-	-
Real GDP growth	-	-	-	-	-	-	-
Participation rates males (aged 20-64)	-	-	-	-	-	-	-
Participation rates females (aged 20-64)	-	-	-	-	-	-	-
Total participation rates (aged 20-64)	-	-	-	-	-	-	-
Unemployment rate	-	-	-	-	-	-	-

15 Figures in parentheses exclude the one-off items in 2004.

Annex 2: Indicators of long-term sustainability

Main assumptions - baseline scenario (as % GDP)	2009	2010	2020	2030	2040	2050	changes
Total age-related spending	18.3	18.2	18.7	20.2	22.9	24.3	6.0
Pensions	8.0	8.0	8.5	9.9	12.0	13.0	5.0
Health care	5.8	5.8	6.1	6.5	7.0	7.2	1.4
Education**	3.9	3.8	3.6	3.4	3.6	3.7	-0.2
Unemployment benefits**	0.6	0.6	0.5	0.4	0.4	0.4	-0.2
*Total primary non age-related spending**	19.6						
*Total revenues**	40.2						

* constant

** EPC projections

Results (as % GDP)	2009	2010	2020	2030	2040	2050	changes
Baseline scenario							
Gross debt	37.6	35.2	14.6	4.5	17.0	56.1	18.5
i + 0.5*	37.8	35.5	16.3	7.0	20.7	62.9	25.2
2004 scenario							
Gross debt	38.7	36.2	15.8	5.7	18.6	58.2	19.6
i + 0.5*	38.9	36.6	17.5	8.4	22.6	65.5	26.7

* i + 0.5 represents the evolution of debt under the assumption of the nominal interest rate being 50 basis points higher throughout the projection period.