Eurogroup

Brussels, 23 November 2020
(OR. en)

EG 29/20
ADD 1

EUROGROUP 29
ECOFIN 1053
UEM 378

COVER NOTE

From:	Secretary-General of the European Commission, signed by Ms Martine DEPREZ, Director
date of receipt:	18 November 2020
To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union
No. Cion doc.:	SWD(2020) 855 final
Subject:	COMMISSION STAFF WORKING DOCUMENT Analysis of the Draft Budgetary Plan of Spain Accompanying the document COMMISSION OPINION on the Draft Budgetary Plan of Spain
Enclosed:	SWD(2020) 855 final

Delegations will find attached document SWD(2020) 855 final.

EUROPEAN
COMMISSION

Brussels, 18.11.2020
SWD(2020) 855 final

COMMISSION STAFF WORKING DOCUMENT

Analysis of the Draft Budgetary Plan of Spain

Accompanying the document

COMMISSION OPINION

on the Draft Budgetary Plan of Spain

{C(2020) 8505 final}

EN EN

Table of Contents

EXECUTIVE SUMMARY

- Economic activity is set to contract sharply in 2020 and to rebound only partially in 2021. GDP will fall in 2020 by 11.2% according to the Draft Budgetary Plan and by 12.4% according to the Commission autumn forecast. For 2021, the Draft Budgetary Plan projects GDP to expand by 9.8%, boosted by the inclusion of expenditure funded by the Recovery and Resilience Facility of 2.2% of GDP. The Commission forecast, which does not include such expenditure given its insufficient specification in the Draft Budgetary Plan but reflects the progressive tightening of containment measures since the end of the summer, projects GDP to grow by 5.4% in 2021.
- The general government budget balance will worsen distinctly in 2020 and improve moderately in 2021 on the back of the economic recovery. In the Draft Budgetary Plan, the headline government deficit is expected to increase sharply in 2020 to 11.3% of GDP, before narrowing to 7.7% of GDP in 2021. According to the Commission 2020 autumn forecast, Spain is projected to have a higher deficit, 12.2% and 9.6% of GDP in 2020 and 2021 respectively, also due the less favourable economic projections. For the time being, since the submission of the Recovery and Resilience Facility and subsequent approval are only expected to take place in 2021, the Commission forecast includes only 0.5% of GDP pre-financing of Recovery and Resilience Facility grants in the budgetary projections for 2021 and treats them as a financial transaction with no impact on the budget balance, but with a public debt-reducing impact.
- The fiscal response focused on addressing the COVID-19 pandemic and mitigating the economic and social impact of the containment measures. The Draft Budgetary Plan reports deficit-increasing measures adopted in 2020 to fight the pandemic and to assuage its adverse socio-economic effects, amounting to 5.5% of GDP. They include extra spending on health care, support to workers and firms to stem the fall of employment and income support to vulnerable groups. Liquidity measures and provision of public guarantees to companies to help them cope with the fall in revenues amount to about 14.4% of GDP and do not entail immediate budgetary impact. Overall, the measures taken by Spain in 2020 were in line with the guidelines of the Commission Communication of 30 March 2020 on a coordinated economic response to the COVID-19 outbreak.
- The improvement of the fiscal balance in 2021 mainly reflects the economic recovery and the unwinding of past emergency measures. The planned impact of discretionary measures in 2021 amount to -4.6% of GDP, with the phasing out of support measures and the implementation of a new tax package. Insufficient details in the Draft Budgetary Plan did not allow to take into account in the Commission forecasts some of the new tax measures and spending plans that have been subsequently (after the cut-off date of the Commission forecast) proposed in some more details by the government in the 2021 draft budget law.

- Public debt will increase markedly. Public debt stood at 95.5% of GDP at end of 2019. On 20 May 2020, the Commission prepared a report under Article 126(3) TFEU analysing whether Spain is compliant with the deficit and debt criteria of the Treaty. Overall, the analysis suggests that both criteria as defined in the Treaty and in Regulation (EC) No 1467/1997 are not fulfilled. In light of the exceptional uncertainty created by the outbreak of COVID-19 and its extraordinary macroeconomic and fiscal impact, including for designing a credible path for fiscal policy, which will have to remain supportive in 2021, the Commission considered that a decision on whether to place Member States under the Excessive Deficit Procedure should not be taken.
- According to the Draft Budgetary Plan, the public debt-to-GDP ratio is planned to rise to 118.8% of GDP in 2020, before declining to 117.4% in 2021. In its autumn forecast, the Commission projects it to reach 120.3% and 122% of GDP in 2020 and 2021, respectively.
- Overall, most of the measures in the Draft Budgetary Plan of Spain are supporting economic activity against the background of considerable uncertainty. At the same time, it would be useful to regularly review the effectiveness of the support measures and stand ready to adapt them as necessary to changing circumstances. Moreover, given the level of Spain's government debt and high sustainability challenges in the medium term before the outbreak of the Covid-19 pandemic, it is important for Spain to ensure that, when taking supportive budgetary measures, fiscal sustainability in the medium term is preserved

1. INTRODUCTION

This document assesses the economic and budgetary projections contained in the 2021 Draft Budgetary Plan of Spain (hereafter called the DBP), which was submitted for 2021 on 15 October in compliance with Regulation (EU) No 473/2013. It was submitted without a draft budget bill being sent in parallel to the parliament. The latter was submitted only two weeks later after a period of continued budget negotiations.

On 20 March 2020, the Commission adopted a Communication on the activation of the general escape clause of the Stability and Growth Pact and on 23 March 2020 the Ministers of Finance of the EU Member States agreed with the Commission assessment. The clause facilitates the coordination of budgetary policies in times of severe economic downturn. As indicated in the Annual Sustainable Growth Strategy 2021[1] and as communicated in the letter of 19 September 2020 from the Commission to the EU Ministers of Finance[2], the activation of the general escape clause allows for a temporary departure from the adjustment path towards the medium-term budgetary objective of each Member State, which should continue to provide targeted and

[1] Communication from the Commission on Annual Sustainable Growth Strategy 2021, Brussels, 17.9.2020, COM(2020) 575 final.

[2] https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/stability-and-growth-pact/annual-draft-budgetary-plans-dbps-euro-area-countries/draft-budgetary-plans-2021_en

temporary fiscal support in 2021, provided that this does not endanger fiscal sustainability in the medium term. The general escape clause does not suspend the procedures of the Stability and Growth Pact. It allows Member States to depart from the budgetary requirements that would normally apply while enabling the Commission and the Council to undertake the necessary policy coordination measures within the framework of the Pact.

Public finances in 2021 are also expected to be influenced by the proposed establishment of the Recovery and Resilience Facility (RRF), alongside the proposal for the reinforced long-term budget of the EU for 2021-2027. RRF is envisaged to provide a total envelope of EUR 672.5 billion in loans and non-repayable financial support (grants) to support the implementation of investments and reforms in the EU Member States. The budgetary projections in the 2021 DBP of Spain are based on a macroeconomic scenario that takes into account the economic impact of a significant policy package for 2021 of EUR 27.4 billion to be funded mainly by the Recovery and Resilience Facility.

On 20 May 2020, the Commission issued a report under Article 126(3) TFEU, as Spain's general government deficit in 2020 was planned to exceed the 3% of GDP Treaty reference value and Spain did not make sufficient progress towards compliance with the debt reduction benchmark in 2019. The report concluded that, after the assessment of all relevant factors, the deficit criterion was not fulfilled and that the debt criterion was not complied with. In light of the exceptional uncertainty created by the outbreak of COVID-19 and its extraordinary macroeconomic and fiscal impact, including for designing a credible path for fiscal policy, which will have to remain supportive in 2021, the Commission considered that a decision on whether to place Member States under the Excessive Deficit Procedure should not be taken.

As the debt ratio was 97.4% of GDP at the end of 2018 (the year in which Spain corrected its excessive deficit), exceeding the 60% of GDP reference value, during the three years following the correction of the excessive deficit (i.e. 2019-21) Spain is subject to the transitional arrangements to make sufficient progress towards compliance with the debt reduction benchmark. Following the end of the transition period, Spain is subject to the debt reduction benchmark.

2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

The lock-down measures put in place in Spain in response to the COVID-19 pandemic resulted in an unprecedented contraction in activity in the first half of 2020 (-22.1% compared to the end of 2019). The easing of containment measures allowed economic activity to resume over the summer, but the pace of recovery gradually declined as the resurgence of numerous outbreaks in August prompted the progressive adoption by the Spanish authorities of social distancing measures. The 2021 DBP forecasts a GDP contraction of 11.2% in 2020, which embeds a 2-percentage-point downward revision to GDP growth compared to the 2020 Stability Programme for Spain. For 2021, budgetary projections are based on projected GDP growth of 9.8%. This implies a 3-percentage-point upward revision to economic growth compared to the Stability Programme, which is mainly due to the incorporation in the DBP of the policy package expected to be funded by the Recovery and Resilience Facility. The DBP also provides a baseline scenario in which this policy package is not included. In that case, GDP would expand by 7.2% in 2021, which implies an upward revision by 0.4 percentage points compared to the 2020 Stability Programme for Spain. The macroeconomic and fiscal outlook continue to be affected by high uncertainty due to the COVID-19 pandemic.

As from the third quarter of 2020, the DBP projects a continuous recovery path, which will be mainly supported by a rebound in domestic demand, while net external contribution will be positive in 2021, after a sizeable negative contribution in 2020. Consumer spending is expected to be supported by the unwinding of the sizeable increase in household savings. The DBP projects a decrease in the savings rate, assuming that uncertainty gradually dissipates over 2021, along with mobility restrictions. In this setup, investment is also projected to rebound strongly. Exports are also set to expand at a high rate, in line with a higher world trade forecast and supported by a progressive recovery of international tourism.

Unlike the forecast underpinning the DBP, in line with its no-policy change assumption the Commission forecast includes no expenditure related to the Recovery and Resilience Facility, as the corresponding measures were not sufficiently specified at the cut-off date of the forecast. The Commission's projection also incorporates the recent worsening in the evolution of the pandemic. According to the Commission autumn 2020 forecast, GDP is projected to decline by 12.4% in 2020, before rebounding by around 5½% in 2021. While consumer spending is expected to be supported by pent-up demand unleashed progressively throughout 2021, increased restrictions in the last quarter of 2020 to contain the resurgence of infections are expected to weigh on consumer and business confidence and delay domestic demand strengthening over 2021. Restrictions adopted in several European countries will contribute to a weaker export recovery.

In its opinion on 6 October 2020[3], the Independent Authority for Fiscal Responsibility (AIReF) considered the government's projections for 2021 plausible under the assumptions that the containment measures to control the pandemic are effective and the implementation of the stimulus package is fast and efficient. AIReF also warned about risks associated to the extreme uncertainty regarding the future evolution of the pandemic.

[3] Available at: https://www.airef.es/en/cover-page/airef-endorses-the-macroeconomic-scenario-but-warns-of-the-risks-associated-to-the-context-of-extreme-uncertainty/

Table 1. Comparison of macroeconomic developments and forecasts

	2019	2020			2021		
	COM	SP	DBP	COM	SP	DBP	COM
Real GDP (% change)	2.0	-9.2	-11.2	-12.4	6.8	9.8	5.4
Private consumption (% change)	0.9	-8.8	-12.6	-14.6	4.7	10.7	4.5
Gross fixed capital formation (% change)	2.7	-25.5	-18.3	-17.3	16.7	15.0	3.8
Exports of goods and services (% change)	2.3	-27.1	-22.7	-22.1	11.6	18.0	14.2
Imports of goods and services (% change)	0.7	-31.0	-20.0	-18.9	9.3	17.1	9.4
Contributions to real GDP growth:							
- Final domestic demand	1.5	-9.7	-9.7	-10.7	5.8	9.3	3.7
- Change in inventories	-0.1	0.0	0.0	-0.1	0.0	0.0	0.0
- Net exports	0.6	0.5	-1.5	-1.7	1.0	0.5	1.6
Output gap[1]	2.3	-6.5	-10.8	-10.2	-1.6	-3.7	-6.0
Employment (% change)	2.2	n.a.	-8.4	-4.1	n.a.	7.2	-0.8
Unemployment rate (%)	14.1	19.0	17.1	16.7	17.2	16.3	17.9
Labour productivity (% change)	-0.3	n.a.	-3.1	-4.1	n.a.	2.5	1.8
HICP inflation (%)	0.8	n.a.	n.a.	-0.2	n.a.	n.a.	0.9
GDP deflator (% change)	1.4	-1.0	0.0	0.7	1.8	0.9	1.1
Comp. of employees (per head, % change)	2.1	2.0	2.3	1.9	2.0	0.4	0.0
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	2.5	n.a.	1.4	2.2	1.8	1.1	2.9

Note:

[1]In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

Source:

Stability Programme 2020 (SP); Draft Budgetary Plan for 2021 (DBP); Commission 2020 autumn forecast (COM); Commission calculations

3. RECENT AND PLANNED FISCAL DEVELOPMENTS

On 20 July 2020 the Council addressed recommendations to Spain in the context of the European Semester. In the area of public finances and in line with the general escape clause, the Council recommended Spain to take all necessary measures to effectively address the pandemic, sustain the economy and support the ensuing recovery and, when economic conditions allow, to pursue fiscal policies aimed at achieving prudent medium-term fiscal positions and ensuring debt sustainability, while enhancing investment.

3.1. Deficit developments

The DBP projects a headline deficit of 11.3% of GDP in 2020. This projection implies an upward revision of 1 percentage point with respect to the 2020 Stability Programme and reflects a combination of a sharper GDP contraction than expected in the spring and an extension of measures to counteract the economic fall-out from the pandemic.

In turn, the Commission 2020 autumn forecast projects the deficit to reach 12.2% of GDP in 2020, reflecting both a more pronounced economic downturn and slightly less resilient tax revenues. The latter is reflected by the fact that the revenue-to-GDP ratio is 0.6 percentage points higher in the DBP, with all of the difference stemming from taxes on production and imports and income taxes. As a result, the deterioration in the structural balance estimated by the Commission is slightly larger than the recalculated structural balance[4] based on data in the Plan. In any case, similarly to the macroeconomic forecasts, any budgetary projections in the current circumstances are subject to a high degree of uncertainty.

For 2021, the DBP projects a deficit of 7.7% of GDP. This is based on a macroeconomic scenario including the impact of a 2.2% of GDP policy package expected to be funded by the Recovery and Resilience Facility and REACT-EU (see Section 2). However, the revenue/expenditure projections in the DBP include only the fiscal impact of the assumed stronger economic growth resulting from expenditure under the Recovery and Resilience Facility and REACT-EU, not the aforementioned grants and expenditure themselves. The improvement with respect to 2020 is explained by the expected strong economic rebound and the phasing out of the temporary emergency measures implemented to contain the economic effects of the pandemic and the inclusion of a number of revenue measures (See Section 4). The DBP projects the re-calculated structural balance to deteriorate by a further ½ percentage points in 2021. However, a mechanical reading of traditional indicators is not well suited at the current juncture to assessing the fiscal stance. The introduction and subsequent withdrawal of sizeable temporary emergency measures distort the picture, as the corresponding changes in the level of public spending from one year to the next affect the indicators used to assess the fiscal stance. Excluding the temporary emergency measures from the calculation of the fiscal stance indicators provides a more representative assessment of the underlying fiscal support to economic activity.[5] Nevertheless, spending plans for 2021 as set out in the DBP indicate a continuation of the underlying expenditure trend above potential GDP growth. These trends, which require close monitoring, are most visible in intermediate consumption, compensation of employees and social transfers and are accentuated by the decision to revalue contributory old-age pensions by expected inflation (0.9%), non-contributory pensions by 1.8% and to increase compensation of employees by 3%, partly reflecting a pay rise of 0.9%.

The Commission 2020 autumn forecast projects a higher headline deficit, of 9.6% of GDP in 2021. This mainly reflects significantly lower economic growth projections in the Commission forecast. The revenue-to-GDP ratio in 2021 is slightly lower in the Commission forecast, which is explained by a lower starting position in 2020. The difference actually narrows slightly in 2021 as the Commission forecast expects social security contributions to grow somewhat more strongly than what is assumed in the DBP and it does not include as steep a decline in the category other revenues as the latter. This more than offsets stronger growth in taxes on production and imports in the DBP, reflecting the inclusion of more revenues from revenue-increasing discretionary measures.

[4] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology. The estimates of the structural budget balance are affected by high uncertainty due to the economic consequences of the COVID-19 pandemic.

[5] The measure of the output gap is complicated in the face of a sharp economic turnaround and very high level of economic uncertainty.

Since the submission of the Recovery and Resilience Plans and their subsequent approval are expected to take place only in 2021, the Commission 2020 autumn forecast assumes in the budgetary projections for 2021 a 10% pre-financing of Recovery and Resilience Facility grants[6], which in the case of Spain is equivalent to EUR 6.4 billion (or 0.5% of GDP) in 2021, and treats it as a financial transaction with no impact on the budget balance, but with a government debt-reducing impact.

On the expenditure side, in line with its no-policy change assumption, the Commission forecast includes no expenditure related to the Recovery and Resilience Facility, as these measures were not sufficiently detailed in the Draft Budgetary Plans.[7] As a consequence of significantly stronger economic growth in 2021, the expenditure-to-GDP ratio declines more sharply in the projections in the DBP. Adjusting for this denominator effect, the two forecasts are rather similar, with the Commission forecast expecting slightly lower interest expenditure.

The main risk to the budgetary targets for 2021 stem primarily from the high uncertainty associated with the macroeconomic scenario. As in other countries, the government has provided public guarantees to sustain economic activity and sectors particularly hit by the pandemic. Should these guarantees be called, this will be reflected in public debt and deficits in the future.

---

[6] The amount of pre-financing is based on the Council Presidency compromise proposal for the RRF regulation (11538/20) of 7 October 2020, on which the Council Presidency obtained a mandate for conducting the negotiations with the European Parliament.

[7] The treatment of the Recovery and Resilience Facility (RRF) in the Commission's 2020 autumn forecast is explained in detail in Box I.4.3 of the European Commission's Economic Forecast Autumn 2020 (https://ec.europa.eu/info/sites/info/files/economy-finance/ip136_en.pdf). The forecast only incorporates those measures that are credibly announced and sufficiently detailed in the Draft Budgetary Plans, irrespective of whether they are planned to be part of Recovery and Resilience Plans. No financing from the RRF has been included on the revenue side of the budgetary projections. Only the pre-financing of RRF grants is included in the forecast for 2021. The assumptions on expenditure measures linked to the RRF in the Commission forecast are without prejudice to the assessment of the Recovery and Resilience Plans.

Table 2. Composition of the budgetary adjustment

(% of GDP)	2019		2020			2021			Change: 2019-2021
	COM	DBP	SP	DBP	COM	SP	DBP	COM	DBP
Revenue	**39.2**	**39.2**	**41.2**	***41.7***	**41.1**	**n.a.**	***40.3***	**40.2**	**1.1**
of which:									
- Taxes on production and	11.5	11.5	11.9	*11.5*	11.1	n.a.	*12.0*	11.1	0.5
- Current taxes on income,	10.4	10.4	11.1	*11.3*	11.0	n.a.	*11.2*	11.0	0.8
- Capital taxes	0.4	0.4	0.5	*0.5*	0.5	n.a.	*0.5*	0.5	0.1
- Social contributions	12.9	12.9	13.5	*14.2*	14.3	n.a.	*13.0*	13.6	0.1
- Other (residual)	4.0	4.0	4.2	*4.2*	4.2	n.a.	*3.6*	4.1	-0.4
Expenditure	**42.1**	**42.1**	**51.5**	**53.0**	**53.3**	**n.a.**	**48.0**	**49.8**	**5.9**
of which:									
- Primary expenditure	39.8	39.8	48.9	50.6	51.0	n.a.	45.8	47.6	6.0
of which:									
Compensation of employees	10.8	10.8	12.7	12.9	12.9	n.a.	12.0	12.5	1.2
Intermediate consumption	5.1	5.1	6.2	6.4	6.4	n.a.	6.1	6.3	1.0
Social payments	18.4	18.4	23.8	24.2	24.3	n.a.	21.4	22.4	3.0
Subsidies	1.0	1.0	1.2	2.0	2.0	n.a.	1.4	1.5	0.4
Gross fixed capital formation	2.1	2.1	2.6	2.5	2.6	n.a.	2.2	2.4	0.1
Other (residual)	2.3	2.3	2.4	2.6	2.7	n.a.	2.7	2.6	0.4
- Interest expenditure	2.3	2.3	2.6	2.3	2.4	n.a.	2.2	2.2	-0.1
General government balance (GGB)	**-2.9**	**-2.9**	**-10.3**	**-11.3**	**-12.2**	**n.a.**	**-7.7**	**-9.6**	**-4.8**
Primary balance	**-0.6**	**-0.6**	**-7.7**	**9.0**	**-9.9**	**n.a.**	**5.5**	**-7.4**	**6.1**
One-off and other temporary measures	-0.2	-0.2	0.0	0.0	-0.2	n.a.	-0.2	0.0	0.0
GGB excl. one-offs	**-2.7**	**-2.7**	**-10.3**	**-11.3**	**-12.0**	**n.a.**	**-7.5**	**-9.5**	**-4.8**
Output gap[1]	2.3	1.3	-6.5	-10.8	-10.2	-1.6	-3.7	-6.0	-5.0
Cyclically-adjusted balance[1]	-4.2	-3.6	-6.4	-4.9	-6.2	0.0	-5.5	-6.0	-1.9
Structural balance (SB)[2]	**-4.0**	**-3.4**	**-6.4**	**-4.9**	**-6.0**	**n.a.**	**-5.3**	**-6.0**	**-1.9**
Structural primary balance[2]	-1.8	-1.2	-3.8	-2.6	-3.6	0.0	-3.1	-3.8	-2.0

Notes:

[1] Output gap (in % of potential GDP) and cyclically-adjusted balance according to the DBP/Programme as recalculated by Commission on the basis of the DBP/Programme scenario using the commonly agreed methodology.

[2] Structural (primary) balance corresponds to cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

Source:

Stability Programme 2020 (SP); Draft Budgetary Plan for 2021 (DBP); Commission 2020 autumn forecast (COM); Commission calculations

3.2. Debt developments

The DBP projects the general government debt-to-GDP ratio to rise by more than 23 percentage points to reach almost 119% of GDP at the end 2020. About three fifths of the increase is due to the snowball effect, in particular the significant drop in nominal GDP, with the large primary deficit explaining the remaining part. For 2021, the DBP projects the debt ratio to decrease by little over 1 percentage point to 117½% of GDP. The still sizeable debt-increasing effect from the primary deficit, combined with a planned debt-increasing stock-flow adjustment, is expected to be offset by the effect resulting from the significant economic rebound. The debt-increasing contribution from interest payments is projected to remain broadly stable with respect to 2020.

The debt projection in the DBP points to a somewhat higher debt ratio than in the Stability Programme in 2020, which in almost equal measure is due to the higher primary deficit and the downward revision to the economic growth.

The Commission 2020 autumn forecast projects a higher debt ratio for both years, with the debt ratio reaching more than 120% of GDP in 2020 and further increasing to about 122% in 2021. This is primarily a result of differences in the economic growth forecast, but also in the primary deficit projections (in itself also largely affected by the different growth forecasts).

Table 3. Debt developments

(% of GDP)	t	2020			2021		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio[1]	**95.5**	**115.5**	**118.8**	**120.3**	**n.a.**	**117.4**	**122.0**
Change in the ratio	-1.9	20.0	23.3	24.8	n.a.	-1.4	1.7
Contributions[2]:							
1. Primary balance	**0.6**	**7.7**	**9.0**	**9.9**	**n.a.**	**5.5**	**7.4**
2. “Snow-ball” effect	**-0.9**	**13.4**	**14.4**	**15.1**	**n.a.**	**-9.3**	**-5.1**
Of which:							
Interest expenditure	2.3	2.6	2.3	2.4	n.a.	2.2	2.2
Real growth effect	-1.8	9.8	12.0	13.4	-7.2	-10.6	-6.0
Inflation effect	-1.3	1.1	0.0	-0.7	-1.9	-0.9	-1.2
3. Stock-flow adjustment	**-1.6**	**-1.0**	**-0.1**	**-0.2**	**n.a.**	**2.5**	**-0.5**

Notes:

[1] End of period.

[2] The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source:

Stability Programme 2020 (SP); Draft Budgetary Plan for 2021 (DBP); Commission 2020 autumn forecast (COM); Commission calculations

4. MEASURES UNDERPINNING THE DRAFT BUDGETARY PLAN

The DBP focuses on the policy response undertaken in the context of the COVID-19 outbreak in 2020 and the measures planned to sustain the recovery in 2021. Supportive fiscal measures should be tailored to the specific situation of each Member State, but as a rule, they should be well targeted and temporary. Their use and effectiveness should be regularly reviewed by the national authorities. Depending on the development of the pandemic, emergency fiscal measures should to be adjusted and combined with other measures that improve economic fundamentals, support the green and digital transition and have a positive impact on demand.

4.1. Measures in 2020

The DBP reports discretionary fiscal measures with a direct budgetary impact in 2020 in response to the COVID-19 outbreak and its related economic effects of around EUR 60 billion (about 5.5% of GDP). These consist of expenditure measures totalling EUR 59 billion (5.4% of GDP) and revenue measures costing EUR 1 billion (0.1% of GDP).

Expenditure measures in 2020 include additional spending on health care to cope with the medical emergency, support to workers and firms to safeguard employment, as well as income support to vulnerable groups notably with the creation of a permanent nationwide minimum income scheme since 1 June 2020. Most of the COVID-crisis response measures are set to be discontinued at the end of 2020 (or end of January 2021 for the short time work scheme and similar measures for self-employed and for workers ill with COVID-19). On the revenue side, measures in 2020 include some minor VAT reductions and the possibility to adapt corporate and personal income tax instalment payments to actual tax base. The latter measure is proposed to be extended in the 2021 draft budget law that was submitted to the Parliament on 28 October.

The Commission 2020 autumn forecast has taken on board the measures reported in the DBP, however with a lower estimate of their budgetary impact (at 1.3% of GDP). The Commission forecast considers a large share of the expenditure on short-time work schemes as part of the operation of the automatic stabilisers, whereas the DBP appears to report the gross impact of these schemes. Similarly, some measures reported in the DBP such as the COVID-19 fund for regions, the salary increase in the public sector, and the pension indexation to consumer price index are incorporated implicitly in the Commission's baseline projections.

Beyond the expenditure and revenue measures that have a direct impact on the deficit, the DBP also indicates liquidity support measures in 2020 of EUR 159 billion (14.4% of GDP) of public loan guarantees and some tax deferrals within 2020 (of about EUR 18 billion or 1.6 % of GDP). According to the data from the national development bank (ICO), the take-up of liquidity guarantees is estimated at EUR 79 billion on 15 October 2020.

Overall, the measures taken by Spain in 2020 were in line with the guidelines of the Commission Communication of 13 March 2020 on a coordinated economic response to the COVID-19 outbreak.

Table 4.1.a. Main discretionary measures adopted/announced with budgetary impact reported in the Draft Budgetary Plan

List of measures	Description	ESA Code (Expenditure / Revenue component)	Adoption Status	Budgetary impact (% of GDP - change from previous year)		
					2020	2021
Strengthening the financing of health and research sectors	Increased allocation to health ministry	D1, P2, D63, D62	Approved through Royal Decree Law 7/2020		0.1	-0.1
	Early transfer of money to the regions enabling increased health expenditure	D1, P2, D63, D62	Approved through Royal Decree Law 7/2020		0.3	-0.2
Public service	COVID-19 fund to regions to finance costs related to health, education, compensate for the fall in tax revenues and ensure the provision of essential public services	D1, P2, D63, D62	Approved through Royal Decree Law 22/2020		1.4	-1.3
Income support	Salary increase in the public sector according to the 2018-2020 trade unions agreements	D1	Approved through Resolution of 22 March 2018 and of 19 March 2018		0.3	n.a.
	Pension revalorisation in 2020 and 2021 with CPI of 0.9%	D	Approved through Royal Decree Law 1/2020 and announced in the DBP and to be approved by royal decree law at end-year		0.1	0.1
	Nationwide minimum income scheme	D	Approved through Royal Decree Law 20/2020		0.1	0.1

Labour market measures	Increased protection of confined or infected workers	D62	Approved through Royal Decree Law 6/2020		0.1	-0.1
	Social benefits for workers affected by short working time schemes	D62	Approved through Royal Decree Law 8/2020		1.6	-1.4
	Social benefits for self-employed forced out of business or suffering a significant drop in business because of the health emergency	D62	Approved through Royal Decree Law 8/2020, modified through RDL 11/2020		0.5	-0.4
	Suspended social contributions as part of short working time schemes	D39	Approved through Royal Decree Law 8/2020		0.6	-0.5
	Suspended social contributions for those self-employed suffering a significant drop in business because of the health emergency	D39	Approved through Royal Decree Law 8/2020, modified through RDL 11/2020		0.2	-0.2
Tax relief measures	Temporary 0% VAT rate for medical supplies for hospitals and other support measures to ensure corporate viability	D2, D5	Approved through Royal Decree Law 11/2020 and 15/2020		0.1	-0.1
Financing measures	Financial transaction new tax	D.29	Approved by law 5/2020			-0.1
	Digital services tax	D.29	Approved by law 4/2020			-0.1
	Changes in environmental taxation	D.21, D.29	Announced in the DBP for implementation with the 2021 draft budget law			-0.1
	Changes in indirect	D.21	Announced in the DBP for			-0.1

	taxation		implementation with the 2021 draft budget law			
	Anti-fraud measures	D.5, D.21	Announced in the DBP for implementation with the 2021 draft budget law			-0.1
				Total	5.5	-4.6

Table 4.1.b. Guarantees adopted/announced in response to COVID-19 outbreak

List of measures	Description	Adoption Status	Maximum amount of contingent liability* (% of GDP)		Current take-up (actual contingent liability, % of GDP)
Bank guarantees	A guarantee of up to 70% (80% in the case of SMEs) of credit amount	Approved through Royal Decree Law 8/2020		9.0	7.1
Extraordinary insurance coverage	Trade credit line for SMEs and non-listed companies with export activity	Approved through Royal Decree Law 8/2020		0.2	n.a.
Guarantees for vulnerable households	Guarantee covering housing costs for tenants in vulnerable situation because of COVID-19	Approved through Royal Decree Law 11/2020		0.1	n.a.
Guarantees via CERSA	Guarantee covering credit risk of SMEs	Approved through Royal Decree Law 11/2020		0.1	n.a.
Bank guarantees for investments	A guarantee of up to 70% (80% in the case of SMEs) of credit amount	Approved through Royal Decree Law 25/2020		3.6	n.a.
SURE guarantee	New EU instrument for temporary Support to mitigate Unemployment Risks in an Emergency (SURE)	Approved through Royal Decree Law 19/2020		0.2	0
Pan-European Guarantee Fund	New instrument for EIB operations	Approved through Royal Decree Law 21/2020		0.25	0
Solvency fund for	Fund to support the solvency of strategic	Approved through		0.9	n.a.

strategic companies	companies through the granting of participating loans, subordinated debt, subscription of shares or other capital instruments.	Royal Decree Law 25/2020			
			Total	**14.4**	**7.1**

* Any budgetary impact related to expected losses or actual calls should be provided in the standard table **5.1 Description of discretionary measures included in the draft budget** *(see Code of Conduct,* https://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/coc/2014-11-07_two_pack_coc_amended_en.pdf)

4.2. Measures in 2021

For 2021, the DBP presents a set of recovery plans targeted at sectors which are affected the most by the COVID-19 crisis and additional financial transfers to sub-national level of government for coping with the impact of the crisis together with increase in the national expenditure ceilings.

Most of the sectoral plans had not yet been specified in sufficient details to be included in the Commission forecast and in Table 4.1.a. The phasing out of the 2020 measures and the implementation of a new tax package have a deficit-reducing impact of 4.6% of GDP. At the same time, the DBP announces a relinking of pensions to inflation, which may affect fiscal sustainability in the medium term. According to the DBP, this measure is estimated to total 0.1% of GDP. The DBP also includes the full-year impact of the nationwide minimum income scheme, with a similar additional budgetary impact. Insufficient details in the DBP did not allow to take into account in the Commission forecasts some of the new specific spending measures that have been proposed, subsequently to the cut-off date for the Commission forecast, by the government in the 2021 draft budget law.

The Commission 2020 autumn forecast considers about 0.1% of GDP in new revenue measures while the DBP estimates about 0.6 % of GDP. The difference is due to uncertainties surrounding the implementation and the yield of some of the revenue measures (the anti-fraud measures, the financial transaction tax, and the digital services tax) and the fact that some changes in taxation were not specified in sufficient details in the DBP or were not yet considered credibly announced at the cut-off date of the forecast (the single use plastic tax, the green taxation changes, the indirect taxation changes, the direct taxation change, the VAT increase to 21% of sweetened beverages). The 2021 draft budget law submitted to the Parliament on 28 October, after the cut-off date of the Commission's forecast however provided some more details and a credible announcement for the changes in existing taxes.

New revenue measures from the DBP consist of the following:

A. Measures included in the Commission 2020 autumn forecasts (all of which are below 0.1% of GDP in magnitude, unless otherwise stated)

- Creation of a **tax on financial transactions** (EUR 850 million), which levies 0.2% on the value of acquisitions of shares of large Spanish companies. This new tax will enter into force in mid-January. The Commission 2020 autumn forecast factors in a lower yield of revenues (of about EUR 425 million), having considered the amounts collected in other Member States.

- Creation of a **tax on revenues from digital activities** (EUR 968 million), which is levied on the revenues from the provision of online advertisement services, online intermediation services and the sale of user data. This new tax will enter into force in mid-January. The Commission 2020 autumn forecast factors in a slightly lower yield of revenues (of about EUR 800 million), having considered the amounts collected in other Member states.
- **New legislative measures[8] to fight against tax fraud** (EUR 828 million), which consist of publishing the identity of a larger number of tax payers in arrears vis-a-vis the tax authorities, further restricting the use of cash between companies and consumers, prohibiting the use of sales suppression software and strengthening the unit within the tax authority to oversee the tax declarations of high net worth individuals, and reinforcement of the list of tax havens. The Commission 2020 autumn forecast reduces the expected amount of revenue from measures to fight against tax fraud, due to uncertainties surrounding their implementation (EUR 425 million).

B. Measures not included in the Commission 2020 autumn forecasts

- **Increases in direct taxation** without details (estimated budgetary impact in the DBP of EUR 550 million). In the 2021 draft budget, it was then specified that changes will apply in taxing (in part) subsidiaries' dividends and capital gains generated abroad (EUR 473 million) and by increasing the tax rate on large companies' taxable base and in the personal income tax rate for high wage earners and on savings (increase by 3 percentage points for a capital income of more than EUR 200,000 and by 2 percentage points for labour income of more than EUR 300,000) (EUR 144 million). In total, this would yield EUR 617 million, above the initially estimated budgetary impact from the DBP.
- **Increases in indirect taxation** without details (EUR 1509 million or slightly above 0.1% of GDP). In the 2021 draft budget, it was not specified as such.
- **Increase in VAT rate** from 10 % to 21% on sugary and sweetened beverages (EUR 340 million). This was included in the 2021 draft budget with the same estimate of the budgetary impact.
- **Green taxation** without details (EUR 1311 million or around 0.1% of GDP). In the 2021 draft budget, it was specified increases in taxation on diesel oil for non-professional consumers (EUR 450 million) and in taxation on waste (EUR 861 million).
- The creation of the **single use plastic taxation** (EUR 491 million). This new tax needs a new law yet-to-be adopted[9] with all the specificities of the tax parameters (tax base, tax rate etc.).

[8] A draft law was approved at Council of Ministers on 13 of October and submitted to the Parliament.

[9] A draft project of the law was approved at Council of Ministers on 2 of June before public consultation. Public consultation ended on 3 July and the revised draft law has yet to be adopted by Council of Ministers and the Parliament.

In the 2021 draft budget, there are also increases in the insurance premium (with a budgetary impact estimate of EUR 455 million), tax deductions for private pension plans with no impact in 2021 and only in 2022, a one-point rise in the wealth tax for those with more than 10 million euros (although this is difficult to apply because it is transferred to the regional government and therefore was not assigned any budgetary impact estimate), and other measures with a budgetary impact estimate of EUR 225 million in 2021. As these measures were announced after the cut-off date for the Commission forecast, they are not included in the latter's projections.

Some forms of liquidity support will also continue to be provided to hard-hit sectors, notably in the form of guarantees of about 0.4% of GDP for the tourism industry, 0.3% of GDP for the car industry, and 0.9% of GDP for sectors of strategic importance in the short term (such as public health and safety) and medium term (ecological transition, digitalisation, increased productivity and human capital).

The spending plans for 2021 as set out in the DBP indicate a continuation of an underlying expenditure trend above potential GDP growth. These trends, which require close monitoring, are most visible in intermediate consumption, compensation of employees and social transfers and are accentuated by the decision to revalue pensions by inflation and to raise public sector wages. The impact on fiscal sustainability of the (continued) revaluation of pensions by expected inflation and of the increases in public wages deserves close monitoring.

Overall, based on the information presented in the Draft Budgetary Plan and taking into account the Commission 2020 autumn forecast, most of the measures planned by Spain in 2021 are supporting economic activity against the background of considerable uncertainty. Given the level of Spain's government debt and high sustainability challenges in the medium term before the outbreak of the Covid-19 pandemic, it is important for Spain to ensure that, when taking supportive budgetary measures, fiscal sustainability in the medium term is preserved.

At the same time, it would be useful to regularly review the use, effectiveness and adequacy of the support measures and stand ready to adapt them as necessary to changing circumstances. Spain is expected to submit its Recovery and Resilience Plan. The Regulation establishing a Recovery and Resilience Facility will set out how the Commission is to assess that the reforms and investments included in the Recovery and Resilience Plan are coherent with the policy priorities of the Union and the challenges identified in the context of the European Semester. This assessment by the Commission will inform the approval of the Plan by the Council and the information to the European Parliament.

5. ANNEXES

ANNEX 1: Mandatory variables not included in the Draft Budgetary Plan

The DBP does not include several mandatory variables for the basic assumptions including the nominal effective exchange rate, world import volumes (excluding EU) and the statistical discrepancy in sectoral balances.

Not included mandatory variables do not impede the Commission's ability to assess the DBP based on the plan's assumptions.