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## COMMISSION STAFF WORKING DOCUMENT

**Analysis by the Commission services of the budgetary situation in Spain following the adoption of the COUNCIL RECOMMENDATION to Spain of 21 June 2013 with a view to bringing an end to the situation of an excessive government deficit and the COUNCIL DECISION of 12 July 2016 establishing that no effective action has been taken by Spain in response to the Council Recommendation of 21 June 2013**

*Accompanying the document*

**Recommendation for a**

**COUNCIL DECISION**

**giving notice to Spain to take measures for the deficit reduction judged necessary in order to remedy the situation of excessive deficit**

{COM(2016) 518 final}

## 1. INTRODUCTION

On 27 April 2009, the Council decided, in accordance with Article 104(6) of the Treaty establishing the European Community (TEC) that an excessive deficit existed in Spain and in accordance with Article 104(7) TEC issued a recommendation to correct it by 2012. Since then the Council issued three new recommendations to Spain on the basis of Article 126(7) of the Treaty on the Functioning of the European Union (TFEU), on 2 December 2009, 10 July 2012 and 21 June 2013, extending the deadline for correcting the excessive deficit to 2013, 2014 and 2016 respectively, as the Council considered that Spain had taken effective action, but unexpected adverse economic events with major unfavourable consequences for government finances had occurred.<sup>1</sup>

Specifically, on 21 June 2013, in order to bring the general government deficit below 3% of GDP in a credible and sustainable manner, Spain was recommended to reach a headline deficit target of 6.5% of GDP in 2013, 5.8% of GDP in 2014, 4.2% of GDP in 2015, and 2.8% of GDP in 2016, which was consistent with an improvement of the structural balance of 1.1%, 0.8%, 0.8%, and 1.2% of GDP in the years 2013-2016 respectively based on the Commission 2013 spring forecast extended to 2016. To achieve this improvement, additional fiscal policy measures of 2%, 1% and 1.5% of GDP in 2014, 2015 and 2016, respectively were deemed necessary.

For 2014, the general government deficit was notified in spring 2015 at 5.8% of GDP, just reaching the intermediate deficit target set by the Council for that year. However, in autumn 2015 it was revised up to 5.9% of GDP, marginally above the EDP target, on account of a downward revision in the underlying GDP figure (i.e. resulting in a denominator effect). On 31 March 2016, the Spanish authorities notified to Eurostat a deficit outcome for 2015 of 5.2% of GDP, later revised to 5.1% of GDP, which is almost 1% of GDP above the EDP headline target for that year. Moreover, the change in the structural balance in 2015 and cumulated over 2013-15 have fallen short of the targets set out in the June 2013 Council Recommendation, when measured both in adjusted and unadjusted terms. The fiscal effort based on the bottom-up method in 2015 and cumulated throughout 2013-15 were also well below what was deemed necessary to comply with the Council Recommendation of 21 June 2013.

On 12 July 2016, following a Commission's recommendation in compliance with Article 126(8) TFEU, the Council adopted a decision establishing that no effective action had been taken by Spain in response to the 2013 Council Recommendation.<sup>2</sup> In compliance with Article 126(9), within two months from the Council decision establishing non effective action the Council shall give notice to the country on a new deadline for the correction of the excessive deficit with a specified adjustment path.<sup>3</sup>

This document proposes a new deadline for the correction of the excessive deficit and an adjustment path that could ensure a durable correction of the excessive deficit. To this end, sections 2 and 3 present the recent macro-economic and budgetary developments and outlook

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<sup>1</sup> All documents related to the excessive deficit procedure of Spain can be found at:

[http://ec.europa.eu/economy\\_finance/economic\\_governance/sgp/deficit/countries/spain\\_en.htm](http://ec.europa.eu/economy_finance/economic_governance/sgp/deficit/countries/spain_en.htm) .

<sup>2</sup> <http://data.consilium.europa.eu/doc/document/ST-10793-2016-INIT/en/pdf>

<sup>3</sup> In addition to the requirements of EDP recommendations under Article 126(7), the Council decision to give notice under Article 126(9) shall not only set the new budgetary targets but also "indicate measures conducive to the achievement of those targets" according to Article (5)1 of Council Regulation No 1467/1997.

for 2016-2018, respectively. Section 4 presents a proposal for a new fiscal adjustment path. Section 5 reviews recent developments in Spain's fiscal framework. The last section concludes.

## **2. RECENT MACRO-ECONOMIC DEVELOPMENTS AND OUTLOOK FOR 2016-2018**

**Real GDP expanded by 3.2% in 2015.** This was driven by strong private and public consumption and buoyant investment, especially in equipment. In nominal terms, GDP grew by 3.8%.

**Growth is projected to remain strong in 2016.** The Commission has updated its 2016 spring forecast with information available until 19 July 2016. The update includes, among others, the quarterly national accounts for the first quarter of 2016. On this basis, the real growth forecast for this year has been revised upwards by 0.3 pps. of GDP compared to spring, to 2.9%, due to stronger than projected private and public consumption in the first quarter of the year, which more than offset weaker-than expected but still strong investment. The anticipated strength of private consumption can be explained by strong job creation and low oil prices. At the same time, investment, despite moderating, is still predicted to show robust growth, especially in equipment but also in residential construction. Exports have been revised downwards more than imports, bringing the contribution of the external sector to growth down to -0.4 pps. of GDP, 0.1 p.p. less than in Spring. However, the current account balance is expected to remain in surplus. Although growth is forecast to moderate during the second half of this year, it is still projected to remain robust. Nevertheless, and despite the upward revision to real GDP growth in 2016, nominal growth is projected to be 3.4%, almost 0.2 pps. of GDP lower than anticipated in the Commission spring forecast. The GDP deflator is now expected to be 0.5% in 2016, whereas HICP inflation is expected to be -0.3% this year, a downward revision of 0.2 pps. compared to spring.

**In 2017, real GDP is projected to decelerate, but still record a robust 2.3% expansion.** This is 0.2 pps. of GDP less than in the Commission spring forecast. The composition of growth is predicted to change somewhat with respect to 2016, with private consumption moderating on the back of lower job creation. Nevertheless, employment growth is still expected to remain strong. At the same time, investment is forecast to pick up slightly, mostly due to accelerating construction investment, especially residential, as the housing market bottoms out and financial conditions remain favourable. Investment in equipment is set to decelerate somewhat on account of greater uncertainty. Both exports and imports are also forecast to accelerate, allowing Spain to still maintain a current account surplus. Inflation is predicted to recover gradually over 2017 on the back of higher oil prices, and a slightly lower euro towards the dollar, with nominal GDP growth reaching 3.6% in 2017, 0.3 pps. less than expected in spring.

**Growth is projected to ease further in 2018 to 2.1%.** Private consumption is expected to decelerate further, despite declining but still strong job creation, as residential investment increases and households start increasing their level of precautionary savings. Investment is expected to increase slightly with dwellings being its most dynamic component, and the contribution of the external sector becomes positive, mainly due to the deceleration of imports. Inflation is projected to remain just slightly beyond its level in 2016, at 1.4%, as a stronger euro more than offsets rising oil prices. Nominal growth is projected to reach 3.6, same as in 2017.

As Spain enters its 3<sup>rd</sup> year of expansion in 2016, the output gap is projected to start gradually closing. It is forecast to reach a value of -1.7% and -0.2% of GDP in 2016 and 2017, respectively, and eventually turn positive in 2018, when it is expected to reach 0.9% of GDP.

There are, however, downside risks to the growth forecast, especially as from 2017, related among others, to the outcome of the referendum in the United Kingdom on the membership of the European Union, which has increased uncertainty, with potential negative implications for trade and domestic demand.

**Table 1: recent macroeconomic developments and outlook**

	2015	2016		2017		2018
		Spring forecast	Updated spring forecast	Spring forecast	Updated spring forecast	Updated spring forecast
Real GDP (% change)	3,2	2,6	2,9	2,5	2,3	2,1
Private consumption (% change)	3,1	3,0	3,3	2,3	2,3	1,3
Gross fixed capital formation (% change)	6,4	4,7	3,6	5,0	4,0	4,2
Exports of goods and services (% change)	5,4	4,5	2,8	5,2	4,6	4,2
Imports of goods and services (% change)	7,5	5,8	4,3	5,8	5,4	3,9
<i>Contributions to real GDP growth:</i>						
- Final domestic demand	3,6	2,9	3,0	2,6	2,3	1,9
- Change in inventories	0,1	0,0	0,2	0,0	0,0	0,0
- Net exports	-0,5	-0,3	-0,4	-0,1	0,0	0,2
Output gap <sup>1</sup>	-4,0	-1,5	-1,7	0,3	-0,2	0,9
Employment (% change)	2,9	2,5	2,6	2,2	2,2	1,7
Unemployment rate (%)	22,1	20,0	19,9	18,1	18,1	16,6
Labour productivity (% change)	0,2	0,1	0,3	0,5	0,3	0,4
HICP inflation (%)	-0,6	-0,1	-0,3	1,4	1,5	1,4
GDP deflator (% change)	0,6	0,9	0,5	1,4	1,3	1,5
Comp. of employees (per head, % change)	0,5	0,8	1,0	1,0	1,1	1,6
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	2,1	2,3	2,3	2,1	2,0	2,0
Note:						
<sup>1</sup> In % of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.						
<i>Source :</i>						
<i>Updated Commission 2016 spring forecast (COM).</i>						

### 3. RECENT BUDGETARY DEVELOPMENTS AND OUTLOOK FOR 2016-2018

On the fiscal side, the updated Commission 2016 spring forecast factors in the latest budget execution data, which refers to the first-quarter (for the general government), to the first four months of the year (for the central, regional and social security government subsectors) and until May regarding the *Estado*, which is part of central government.<sup>4</sup>

The updated spring forecast projects the general government deficit to continue to narrow and to reach 4.6% of GDP in 2016. This is 0.7 pp of GDP higher than in the Commission 2016 spring forecast, with differences stemming mostly from a downward revision of expected income tax revenues. The latter owes partly to a more negative valuation

<sup>4</sup>

See

<http://www.igae.pap.minhap.gob.es/sitios/igae/es-ES/ContabilidadNacional/infadmPublicas/Paginas/administracionespublicas.aspx>

of the effects of the personal income tax reform, but is mainly explained by changes made to the legal framework governing corporate income tax instalment payments (*pagos fraccionados*), in force since January 2016. These are expected to lead to a reduction of corporate taxes paid throughout the year, which would be compensated by higher payments in the final tax settlement to be made in the following year. This measure amounts to EUR 6 bn (0.5% of GDP) in the updated spring forecast and qualifies as a one-off according to the Commission.<sup>5</sup> It therefore leads to a worsening of revenues in 2016 but to an improvement by the same amount in 2017.

**The reduction of the deficit in 2016 relative to 2015 continues to rely to a large extent on the positive macroeconomic outlook**, which supports tax revenues and keeps social transfers in check. Moreover, previous improvements in financing conditions and the stabilising public debt ratio imply that interest expenditure is likely to continue to fall. As in the spring forecast, the projected improvement in the deficit for 2016 is also the result of saving measures at central and regional government level put in place by the caretaker government in response to the Commission Recommendation of March 2016. The 2016 Stability Programme targeted savings from the new measures at central and regional level in the amount of around 0.4% of GDP, including cuts in budgetary appropriations (EUR 3.5 billion) and savings from the implementation at regional level of a new expenditure rule on pharmaceutical and healthcare spending (EUR 420 million). Based on the available information on the response of regional governments to the Ministry of Finance's call for spending cuts (through *acuerdos de no disponibilidad*) and the degree of adherence to the new healthcare and pharmaceutical spending rule, the updated Commission 2016 spring forecast incorporates a deficit-reducing impact of about 0.2% of GDP from these savings mostly driven by the central government, which are not expected to remain in place in 2017. This is around 0.1% of GDP lower than in spring.

**The updated Commission 2016 spring forecast projects the general government deficit to narrow further to 3.3% of GDP in 2017.** It is also 0.2% of GDP higher than in the spring forecast, reflecting the worse-than-expected starting position and the fact that the savings measures taken in response to the March 2016 Commission Recommendation are not considered to be rolled over to next year. The improvement of the deficit relative to 2016 is again mainly due to the cyclical recovery and the continued decline in interest expenditure. Together with the impact of the 2013 local administration reform and the fact that the repayment of the foregone 2012 Christmas bonus is fading out, expenditure growth is expected to be reined in.

**The updated Commission 2016 spring forecast projects the general government deficit to narrow further to 2.7% of GDP in 2018.** The improvement of the deficit relative to 2017 is again mainly due to the cyclical recovery and the continued decline in interest expenditure and the fact that social transfers continue to grow at a slower pace than nominal GDP.

**In its reasoned request of 13 July, the Spanish government announced its commitment to put in place further deficit-reducing measures.** On the revenue side, amendments to the corporate income tax law, to be adopted as soon as a new government is formed, would allow making up for the loss in revenues expected for 2016 following the changes made to the regulation of instalment payments (*pagos fraccionados*) of the corporate income tax, so as to ensure that corporate income tax revenues in 2016 reach the level expected in the 2016

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<sup>5</sup> The reduction in corporate income tax instalment payments in 2016 create a permanent delay in the payment of taxes, but do not change in the tax rate or tax base, so in a new steady state (starting in 2017) they would not affect revenue from corporate income taxes.

Stability Programme. On the expenditure side, the advancement of the date of closure of the central government's fiscal year, adopted on 14 July, can help contain expenditure developments in the second half of 2016.<sup>6</sup> The updated spring forecast does not include savings from these measures, due to uncertainties surrounding their final specification (in the former) and their estimated impact (in the latter). These measures are subject to considerable implementation risks, in particular with respect to the timely adoption by Parliament of required changes to the corporate income tax law and whether they will be sufficient to offset the expected temporary shortfall in corporate income tax revenues in 2016.

Lastly, according to the updated Commission 2016 spring forecast, the debt ratio is expected to peak at 100.6% of GDP in 2017 before retreating marginally in 2018, thus exceeding the Treaty reference value in all years.

**Table 2: Composition of budgetary adjustment**

(% of GDP)	2015	2016		2017		2018
	Outturn	Spring forecast	Updated spring forecast	Spring forecast	Updated spring forecast	Updated spring forecast
<b>Revenue</b>	<b>38,2</b>	<b>38,2</b>	<b>37,5</b>	<b>38,3</b>	<b>38,2</b>	<b>38,2</b>
<i>of which:</i>						
- Taxes on production and imports	11,7	11,9	11,9	12,0	11,9	11,9
- Current taxes on income, wealth, etc.	10,1	9,9	9,2	10,1	9,9	10,1
- Social contributions	12,2	12,2	12,2	12,1	12,1	12,0
- Other (residual)	4,2	4,1		4,1	4,2	4,2
<b>Expenditure</b>	<b>43,3</b>	<b>42,1</b>	<b>42,1</b>	<b>41,3</b>	<b>41,5</b>	<b>40,9</b>
<i>of which:</i>						
- Primary expenditure	40,3	39,2	39,3	38,7	38,9	38,4
<i>of which:</i>						
Compensation of employees	11,0	10,7	10,8	10,3	10,5	10,4
Intermediate consumption	5,2	4,9	4,9	5,1	5,0	4,9
Social payments	18,4	18,0	18,0	17,6	17,7	17,5
Subsidies	1,2	1,1	1,1	1,1	1,1	1,1
Gross fixed capital formation	2,5	2,3	2,2	2,3	2,3	2,3
Other (residual)	2,1	2,3	2,3	2,2	2,3	2,3
- Interest expenditure	3,1	2,9	2,8	2,7	2,6	2,5
<b>General government balance (GGB)</b>	<b>-5,1</b>	<b>-3,9</b>	<b>-4,6</b>	<b>-3,1</b>	<b>-3,3</b>	<b>-2,7</b>
<b>Primary balance</b>	<b>-2,0</b>	<b>-1,1</b>	<b>-1,8</b>	<b>-0,4</b>	<b>-0,7</b>	<b>-0,2</b>
One-off and other temporary measures	-0,2	0,0	-0,6	0,0	0,0	0,0
<b>GGB excl. one-offs</b>	<b>-4,9</b>	<b>-3,9</b>	<b>-4,0</b>	<b>-3,1</b>	<b>-3,3</b>	<b>-2,7</b>
Output gap (*)	-4,0	-1,5	-1,7	0,3	-0,2	0,9
Cyclically-adjusted balance	-2,9	-3,1	-3,6	-3,2	-3,2	-3,2
<b>Structural balance (SB)</b>	<b>-2,7</b>	<b>-3,1</b>	<b>-3,1</b>	<b>-3,2</b>	<b>-3,2</b>	<b>-3,2</b>

(\*) % of potential GDP

Source: Updated Commission 2016 spring forecast

#### 4. PROPOSED NEW FISCAL ADJUSTMENT PATH

Table 3 summarises the main elements from the updated Commission 2016 spring forecast that underpin the new adjustment path.

**Table 3: Forecast of key macroeconomic and budgetary variables under the baseline scenario**

<sup>6</sup> See Ministerial Decision HAP/1169/2016, of 14 July at <https://www.boe.es/boe/dias/2016/07/16/pdfs/BOE-A-2016-6843.pdf>



		2015	2016	2017	2018
Real GDP growth	%	3,2%	2,9%	2,3%	2,1%
Output gap	%	-4,0%	-1,7%	-0,2%	0,9%
General government balance	%GDP	-5,1%	-4,6%	-3,3%	-2,7%
Structural balance	%GDP	-2,7%	-3,1%	-3,2%	-3,2%
Change in structural balance	pps	-0,9%	-0,4%	-0,1%	0,0%

Source: Updated Commission 2016 spring forecast

**The proposed deadline for correcting the excessive deficit situation notably takes into account the economic conditions together with other relevant factors.** Based on the baseline scenario outlined above, the second-round effects of the additional consolidation efforts required to bring an end to the excessive deficit situation are assessed. Moreover, the design of the new adjustment path for Spain takes account of the fact that the Council decision to give notice is adopted in the second half of the year, which amplifies the fiscal effort it would take to achieve a given annual improvement of the structural balance. Finally, the baseline scenario for the new adjustment path starts with a deterioration of 0.4% of GDP of the structural deficit in 2016, which is at least in part the result of the inflation turning out lower than projected in the scenario underpinning the 2016 budget – an event that is largely outside the control of the government.

**Against this background, it is proposed not to request additional consolidation measures in 2016.** This leads to a headline target for 2016 of 4.6% of GDP, as in the baseline scenario. It implies a 0.4% of GDP deterioration of the structural balance, also as in the baseline scenario.

**An extension of the deadline by two years could be considered appropriate.** Considering that no further structural measures should be requested in 2016, granting Spain one additional year for the correction of its excessive deficit, which is the rule according to Council Regulation (EC) No 1467/97, would require an annual improvement of the structural balance in 2017 of 0.8% of GDP, requiring measures of 0.9% of GDP. Therefore, it seems adequate to extend the deadline for Spain to bring an end to its excessive deficit situation by two years.

**In 2017, in view of the strong cyclical tailwind, the benchmark improvement of the structural balance of at least 0.5% of GDP would bring the general government deficit to 3.1% of GDP.** This requires additional measures of 0.5% of GDP compared to those already included in the updated Commission 2016 spring forecast.

**In 2018, a further improvement of the structural balance by 0.5% of GDP would bring the general government deficit to 2.2% of GDP.** This requires additional measures of 0.5% of GDP compared to those already included in the updated Commission 2016 spring forecast. These targets ensure a sufficient margin towards the 3% reference value, enabling Spain to put an end to the situation of an excessive deficit in a durable manner.

**Extending to 2017 the 0.4% of GDP expenditure savings at central and regional government level planned in the 2016 Stability Programme, could, if fully implemented, contribute to the requested effort by 0.4% of GDP.**<sup>7</sup> These savings would need to be complemented with other permanent measures, such as the reduction of the number and scope of tax expenditures, in particular the reduced VAT rates, to achieve the required structural effort. Data show that there is scope for such policy action: the level of indirect taxation and the implicit rate on consumption in Spain remain among the lowest in the EU, at 11.6 % of

<sup>7</sup> To note that half of the 0.4% of GDP savings reported in the 2016 Stability Programme were already included in the updated Commission 2016 spring forecast. However, these savings were not projected to remain in place in 2017.

GDP and 15.2% in 2014, respectively. Moreover, in 2013 (latest available figure), Spain recorded the largest VAT<sup>8</sup> policy gap in the EU (at 53.9 % compared to the EU average of 47.2 %).

**Table 4: Forecast of key macroeconomic and budgetary variables under the EDP scenario.**

		2015	2016	2017	2018
Additional permanent measures	% GDP		0,0%	0,5%	0,5%
Real GDP growth	%	3,2%	2,9%	1,7%	1,5%
Output gap	%	-4,0%	-1,7%	-0,8%	-0,1%
General government balance	%GDP	-5,1%	-4,6%	-3,1%	-2,2%
Structural balance	%GDP	-2,7%	-3,1%	-2,6%	-2,1%
Change in structural balance	pps	-0,9%	-0,4%	0,5%	0,5%

Source: Updated Commission 2016 spring forecast

## 5. Fiscal framework

On 12 July 2016, in the context of the 2016 European Semester, the Council recommended Spain to implement at all government levels the tools set out in its fiscal framework law.

**Spain's fiscal framework does include relevant tools to prevent and correct deviations from fiscal targets.** For example, the 2012 Stability Law introduces an early-warning mechanism so that early corrective action can be taken in the event of an identified risk of non-compliance with deficit, public debt or spending rule targets. If no action is taken, the law foresees corrective and enforcement measures. The experience of the past few years shows that these tools could have been enforced to a greater extent, especially at regional level<sup>9</sup>. Following the March 2016 Commission Recommendation, the Spanish government has enforced some of the corrective provisions in the Stability Law<sup>10</sup> that have so far not been implemented, such as the requirement for non-compliant regional governments to adopt expenditure cuts in budget appropriations. Looking forward, greater automaticity in the application of the preventive and corrective mechanisms provided for in Spain's Stability Law at all government levels could be conducive to a timely and durable correction of Spain's excessive deficit.

**Spain's fiscal framework also includes tools to ensure sustainable expenditure developments.** Specifically, it includes an expenditure rule, whereby the variation in the eligible expenditure of the central, regional and local governments should not exceed the reference rate of medium-term growth of Spain's GDP (set at 1.8% for 2016 by the Ministry of Economy). As the economy is growing above this rate, compliance with this rule can help underpin consolidation by, among other things, avoiding that windfalls are entirely spent. Moreover, the contribution of the Stability Law's spending rule to the sustainability of public finances could be enhanced by clarifying the coverage and definition of the spending categories needed for its computation and, contrary to its implementation in 2016, explicitly calling on the non-compliant public administrations to make up for spending slippages in the year following their occurrence.

<sup>8</sup> The VAT policy gap is an indicator of the VAT revenue theoretically foregone by applying non-standard rates to some goods and services, expressed as a share of revenues that would be collected if everything was taxed at the standard rate

<sup>9</sup> See section 3.5. on Public Administration, Fiscal Frameworks and Taxation of the 2016 Country Report for Spain at [http://ec.europa.eu/europe2020/pdf/csr2016/cr2016\\_spain\\_en.pdf](http://ec.europa.eu/europe2020/pdf/csr2016/cr2016_spain_en.pdf)

<sup>10</sup> E.g., Art. 25.1a) of Spain's Stability Law.



**The 2016 Country Specific Recommendations also call on Spain to enhance control mechanisms for public procurement and coordination of procurement policies across government levels.** This is against the backdrop of a relatively high number of presumed breaches of EU public procurement legislation brought to the Commission's attention in recent years. Evidence shows that there are disparities in the implementation of public procurement across contracting authorities and entities, and that insufficient ex-ante and ex-post control mechanisms hinder the correct and uniform application of public procurement legislation. Spain stands out for a low publication rate of contract notices compared with other Member States. They represented 1.8 % of GDP in 2014, compared with 4.4 % in the EU, which ranks Spain 23rd out of 28 countries. Similarly, the publication rate in terms of percentage of total expenditure on procurement is only 13.2% compared to an EU average of 26.2%, Spain ranking 22 out of 28 countries. Spain also stands out for a relatively high use of the negotiated procedure without prior publication (10 % of all award notices vs. 5 % in the European Economic Area, ranking 22 out of 31 countries). This translates into limited competition from undertakings from other EU countries and frequently, into direct awards, with implications in terms of higher general government expenditure. The limited use of centralised or joint procurement instruments prevents efficiency gains which would contribute to fiscal savings. The absence of an independent body in charge of ensuring efficiency and legal compliance in public procurement throughout the country hampers the proper implementation of procurement rules and may create opportunities for wrongdoings, both of which have negative impacts on the situation of Spain's public finances.

## 6. CONCLUSIONS

On 12 July 2016, in compliance with Article 126(8) TFEU and following a Commission recommendation, the Council issued a decision establishing that no effective action had been taken by Spain in response to the 2013 Council recommendation. Hence, as prescribed by Article 126(9), the Council upon Commission recommendation, shall give notice to the country to correct its excessive deficit, indicating the adjustment path.

On the basis of the updated Commission 2016 spring forecast, and taking into account that the Council decision to give notice is adopted in the second half of the year, which amplifies the fiscal effort it would take to achieve a given annual improvement of the structural balance, a correction path that envisages no additional measures in 2016 and 0.5% of GDP additional corrective measures in both 2016 and 2017, on top of those already included in the updated 2016 spring forecast, would appear justified. This would lead to a headline deficit of 4.6%, 3.1% and 2.2% of GDP in 2016, 2017 and 2018, respectively and would imply, in turn, a deterioration of the structural adjustment by 0.4% of GDP in 2016 and an improvement by 0.5% of GDP both in 2017 and 2018.

**Annex: forecast of key variables for the computation of the fiscal effort under the baseline scenario**

			2016	2017	2018
<b>Enters top-down</b>	$\alpha$	<i>Structural expenditure (% of potential GDP)</i>	41.08	41.37	41.39
		<i>Potential GDP growth (%)</i>	0.45	0.72	0.90
	$\beta$	<i>Current revenue (national currency)</i>	411.13	434.88	450.87
		<i>Discretionary measures with impact on current revenue (national currency)</i>	-8.04	5.53	0.19
		<i>Nominal GDP growth (%)</i>	3.40	3.63	3.56
	<i>p.m Output gap (% of Pot. Output)</i>	-1.73	-0.23	0.92	
<b>Enters bottom-up</b>		<i>Discretionary measures with impact on total revenue net of one-offs and other temporary measures (national currency)</i>	-2.75	5.52	0.19
		<i>Total expenditure net of one-offs and other temporary measures (national currency)</i>	469.48	480.62	490.70
		<i>Interest expenditure (national currency)</i>	31.47	30.52	29.61
		<i>Total unemployment</i>	4542.96	4136.80	3765.64

*Source: Commission calculations based on updated spring 2016 forecast*