MACRO RESEARCH - PORTUGAL
NOTE: STATE BUDGET FOR 2018
13TH OCTOBER 2017

State Budget 2018: Fiscal spending based on (cyclical) economic growth, no structural changes in expenditure

- The Portuguese state will increase its spending by € 2.5 billion in comparison to last year. An unexpected strong economic recovery (estimated 2.2% GDP growth in 2018) allows the state to implement more generous measures, costs will partly be reflected in the budget 2019 and 2020.
- The comparably smooth consensus finding betweeen the government and its partners represents a checkpoint for the ongoing, still long-lasting economic recovery path of Portugal. The government however fails to address structural changes on the expenditure side.
- The government estimates a debt/GDP ratio of 123.5% and a state deficit of 1 % by the end of 2018, being in line with EU budget rules as well as meeting its Growth and Stability Programm projections.
- The absolute value of debt will continue to rise, expected to exceed € 246 billion by the end of 2018 (€ 20 billion more than in 2014), the structural deficit is also likely to worsen in the following years (IMF estimates).

Government implements positive measures of net € 841 million

- Minimum level of existence will be lifted from currently € 8500 to € 8847 annually. The second and third tax level will be unfolded, creating two new lines (largest benficiaries: household with monthly income between € 2300 and €2600)[1]. The IRS surcharge will be removed.
  Estimated Cost: total € 380 million, of which € 230 million in 2018
- Pensions will be adjusted for inflation next year, ensuring a minimum adjustment level of 6 € for pensions revised last year and 10 € for the remaining.
  Estimated Cost: € 154 million
- Thawing of careers in the public sector will be implemented and concluded within the coming two years (consecutively in four momentums)
  Estimated Cost: total € 600 million by 2020

Economic Growth allows for spending to increase while reducing state deficit

Each percentage point of growth is estimated to decrease the state deficit by 0.4 percentage points – implying a spending cushion of € 1.5 billion for 2018 (0.8 pp of GDP).

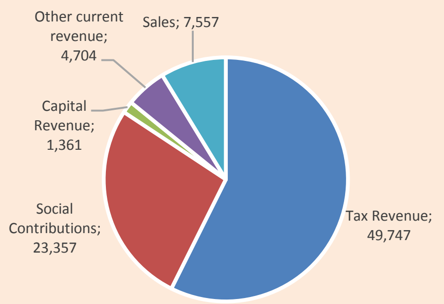
Following (also cyclical) income sources will support public spending next year:

- Dividend payments from Banco de Portugal will increase by € 148 million in comparison to last year (total 527 million)
- Interest payments are expected to decrease by € 443 million due to lower yields on sovereign debt and ongoing advanced repayments of IMF loans
- Nominal freezing of intermediate consumption (€ 300 million, around the same volume as last year)
- Results of the expenditure review exercise (€ 287 million)

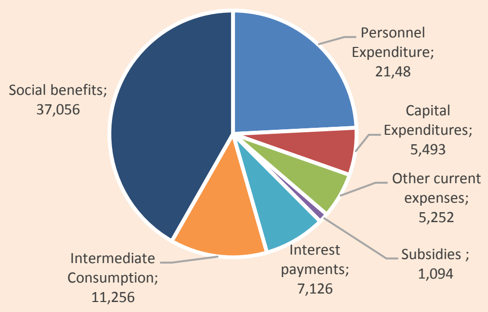
Public investment remains subdued, public staff costs are only reduced in terms of %GDP

- Public investment (gross fixed capital information) is expected to increase by € 1.3 billion in comparison to last year (€ 4.5 billion for 2018), corresponding to 2.3% of GDP – still one of the lowest public investment shares of GDP for the last two decades.
- Salaries and social benefits represent two thirds of spending. Both spending blocks have declined in terms of % GDP, staff costs have increased nominally.
- Taxation and social contribution will remain the largest sources of revenue. Nominal tax revenue is estimated to increase by € 1.184 billion. Social contributions will be benefiting from the increase in employment (estimated unemployment rate of 8.6% in 2018).

State Revenue 2018



State Expenditure 2018



Source: Expresso, 14.10.2017. Values in € billions

[1] Following EY estimations, by order of Diário de Notícias, 13.10.2017

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