The figures at the cut-off date of this report[1] on the general government sector in National Accounts terms, relating to the first quarter of this year, cover the central government, the regional governments and the Social Security system (see accompanying table). According to that information, the general government sub-sectors together posted a deficit in January-March of 0.5% of GDP, 0.2 pp smaller than in the same period of 2016.

Consolidated general government (excluding local government) revenue increased by 3.4% year-on-year in the first quarter of the year, compared with the decline of 1.2% recorded in the same period of 2016, due to the dynamism of tax revenue and social contributions. The latest data, for May, on revenue from taxes shared by central, regional and local governments show a continuation of that revenue strength at the start of the second quarter. However, it should be noted that part of this strong behaviour of direct tax revenue is due to the base effect associated with the change in regulations on minimum corporate income tax prepayments, effective from October 2016.[2] The new legislation affected payments for the year as a whole, which were thus

1 22 June 2017.

2 Royal Decree-Law 2/2016 of 30 September 2016.

Table 1
DEVELOPMENTS IN GENERAL GOVERNMENT ACCOUNTS (a)

	€m	Year-on-year rate of change			
	2016 Jan-Dec	2016 Jan-Dec	2016 Jan-Mar	2017 Jan-Mar	Official targets 2017
1 Total resources (b)	375,325	1.6	-1.2	3.4	5.6
Taxes on production and imports	104,125	1.6	-0.7	3.8	5.4
Income and wealth taxes	102,775	1.9	-10.3	3.5	7.7
Social contributions	136,047	3.1	1.8	5.2	4.6
Other resources (b)	32,378	-5.1	17.1	-9.4	0.6
2 Total uses (b)	419,510	0.5	-0.6	0.5	2.0
Compensation of employees	99,519	2.0	0.0	1.6	1.9
Other final consumption expenditure (c)	64,557	-1.1	0.7	3.7	-2.1
Social benefits (not in kind)	173,453	2.1	1.5	1.5	2.3
Actual interest paid	30,781	-5.4	-5.8	-9.8	2.7
Subsidies	10,013	-8.9	-38.0	37.2	2.3
Other uses and current transfers (b)	16,005	7.5	-9.8	-24.0	—
Gross capital formation	16,644	-19.6	-9.7	1.4	10.3
Other capital expenditure (b)	8,538	57.2	—	37.4	—

	€m	As a percentage of annual nominal GDP (e)			
Net lending (+) or net borrowing (–)	2016 Jan-Dec	2016 Jan-Dec	2016 Jan-Mar	2017 Jan-Mar	Official targets 2017
3 Consolidated aggregate (3 = 3.1 +3.2 + 3.3)	-57,659	-5.2	-0.8	-0.5	-3.1
3.1 Central government	-30,408	-2.7	-0.8	-0.5	-1.1
3.2 Social Security funds	-18,096	-1.6	0.2	0.1	-1.4
3.3 Regional government	-9,155	-0.8	-0.1	-0.1	-0.6
4 Local government	7,083	0.6	0.1	—	0.0
5 Total general government (5 = 3 + 4)	-50,576	-4.5	-0.7	—	-3.1
Memorandum item					
Aid to financial institutions (d)	-2,389	-0.2	0.0	0.0	—
Public debt (EDP)	1,106,952	99.4	101.2	100.4	98.8

SOURCES: IGAE and Stability Programme (2017-2020).

a The revenue and expenditure data refer to the accounts of the consolidated aggregate including the central government, regional government and Social Security funds. Local government data are therefore not included, because monthly information is not available.
b Consolidated figures for transfers to other general government tiers (local government).
c Includes inputs and market producers' social transfers in kind.
d Capital transfers granted to financial institutions.
e For 2017 the annual nominal GDP envisaged in the Stability Programme (2017-2020) was taken. In the case of debt, GDP at market prices was prepared drawing on the official series of the Quarterly National Accounts published by INE, aggregating the last four quarters for each reference date.

concentrated in the fourth quarter of the year. Hence the positive impact on tax revenue in January-May due to this measure will be gradually mitigated over the course of the year until it is eventually neutralised in the fourth quarter of 2017, when the year-on-year comparison will be homogeneous. Meanwhile, general government (excluding local government) expenditure rose by 0.5% year-on-year to March, compared with a decrease of 0.6% in the same period of 2016. The main items increased moderately, except for the expense of non-wage government consumption, which grew by nearly 4% in the first quarter, while government debt interest payments trended downward more steeply.

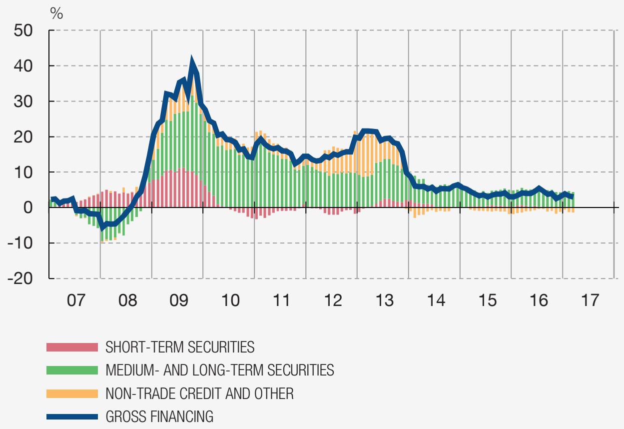
General government debt rose by 1.1 pp of GDP to 100.4% in 2017 Q1, since the expansion of output only partly offset the increase in the debt of the sector (see Charts 1 and 2). However, this increase was largely due to a concentration of debt issuance in the first quarter, which was partially offset in April when, according to the leading indicator of debt, there was net negative issuance. Despite this, the decline in average financing costs meant that the associated debt service burden continued to fall, dropping to 2.8%. The breakdown by instrument shows that the main source of financing for general government in the first quarter of the year continued to be long-term securities. The breakdown by holder shows that the main net purchasers of State government securities in this period were the Banco de España (in the context of the Eurosystem's asset purchase programme) and, to a lesser extent, non-residents.

At end-April, the Spanish government submitted the Stability Programme Update (SPU) to the European Commission. The SPU establishes the main lines of budgetary policy for the period 2017-2021. It sets the general government budget deficit target for 2017 at 3.1% of GDP, in line with the European Council's recommendations of August 2016. To comply with this target, the budget deficit would have to improve by 1.4 pp of GDP this year. According to the SPU estimates, this improvement would be achieved through a combination of the projected positive cyclical developments and the tight fiscal policy stance, with a change in the general government's primary structural balance of 0.5 pp of GDP. The SPU also includes budget deficit targets for the medium term of 2.2%, 1.3% and 0.5% of GDP in 2018, 2019 and 2020, respectively. This path is consistent with the commitment to exit the "excessive deficit" situation established in the EDP (a deficit over 3% of GDP) in 2018.

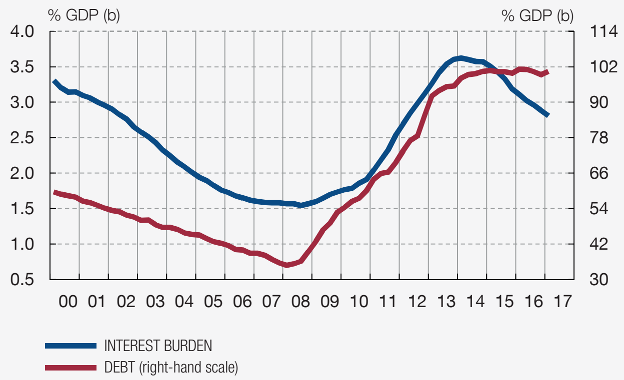
The SPU indicates that the improvement in the general government balance projected for 2017 as a whole is due to a decrease of 0.9 pp in the government expenditure to GDP ratio and to a 0.5 pp higher weight of government revenue in output. The SPU envisages a path of expenditure containment based on the measures included in the budgets of the various tiers of general government for this year and on the saving derived from the reforms undertaken in previous years (particularly the reform of local government and the additional measures linked to implementation of the CORA report). Also, the SPU assumes that interest payments will fall further given the favourable financing conditions, unemployment benefit expense will continue to ease due to the ongoing economic recovery and pension expenditure will moderate somewhat as the new revaluation index is applied. Also, the SPU includes the multi-year public-sector employment plans announced in the draft State budget, designed to reduce the proportion of temporary jobs in government. The SPU assumes the weight of public investment in

GENERAL GOVERNMENT DEBT

Panel 1
GROSS FINANCING
RATE (y-o-y) AND CONTRIBUTION BY INSTRUMENT



Panel 2
INTEREST BURDEN (a) AND DEBT RATIO



SOURCE: Banco de España.

a Cumulative four-quarter data.
b GDP at market prices was prepared drawing on the official rates of the Quarterly Annual Accounts published by INE, aggregating the last four quarters for each reference date.

GDP will remain steady in the medium term. However, if the impact of various temporary effects is corrected, the public investment to GDP ratio would continue the downward trend it has shown since it peaked in 2009. The increase in the weight of revenue in GDP projected by the SPU for 2017 is largely based on the expected positive effect of the measures approved on 2 December 2016, consisting, inter alia, of the enlargement of the corporate income tax base, higher levies on alcohol and tobacco[3] and increased maximum contribution bases.[4]

The path of the ratio of government debt to GDP set out in the SPU represents a continuation of the downtrend that began in 2015, such that this ratio would stand at 98.8%, 97.6%, 95.4% and 92.5% of GDP in 2017, 2018, 2019 and 2020, respectively, compared with 99.4% last year. This decrease would be driven by the projected strong economic growth and improved public finances, which would allow a primary budget surplus from 2018, compared with a primary deficit in 2016.

The latest macroeconomic projections of the Banco de España, published on 13 June,[5] are for a general government deficit of 3.2%, 2.6% and 2.2% of GDP in 2017, 2018 and 2019, respectively. This projection is based on the macroeconomic forecast set out in that report, on the most recent budgetary plans described above and on the available data relating to government revenue and expenditure up to the cut-off date of the projection exercise (23 May 2017).[6] However, it should be noted that this projection does not consider a number of temporary factors, included in the Stability Programme but not yet crystallised, relating to the possible additional cost of assistance to financial institutions in 2017 and to the liability derived from litigation on the eight toll roads subject to insolvency proceedings, which will foreseeably be effectively incurred in the period 2017-2018.

3 Royal Decree-Law 3/2016 adopting tax measures to strengthen the public finances and other urgent social measures.

4 Also, the approval of the national minimum wage (Royal Decree 742/2016) prompted an increase of 8% in the minimum contribution base.

5 See this link.

6 More specifically, the projections in this report on the fiscal policy variables for 2017-2019 are based on three elements. First, it is assumed that the budgetary items subject to greater scope for discretion, notably including, by virtue of their volume, public investment and government purchases, evolve in keeping with the nominal potential growth of the Spanish economy in the medium term and the measures announced in the Stability Programme. Second, it is assumed that all other general government account items evolve, in the absence of measures, in keeping with their habitual determinants. Specifically, in the case of government revenue, irrespective of the inclusion of the legislative changes approved at end-2016, it has been assumed that it will grow in keeping with its tax bases, which chiefly depend on the macroeconomic environment. Likewise the expenditure items that offer less scope for discretion, such as pensions (where developments are essentially determined by the revaluation formula established by law, and by population ageing), unemployment benefits (which primarily depend on developments in unemployment) and the interest burden (affected by changes in government debt levels and interest rates). Finally, these projections include an assessment of the impact of the short-term data available on the behaviour of government revenue and expenditure up to the cut-off date of this report.