



ECONOMY

2009 STATE BUDGET: CRISIS, DEFICIT AND UNEMPLOYMENT

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2007-2009 MACROECONOMIC TABLE FORECAST OF ZAPATERO'S BUDGET PROJECT

% OF YEARLY VARIATION	2007	2008	2009
GDP	3,7	1,6	1,0
FINAL CONSUMPTION	3,8	1,7	1,3
HOUSEHOLDS	3,5	0,7	0,4
PUBLIC ADMINISTRATIONS	4,9	4,9	3,8
FORMACIÓN BRUTA CAPITAL FIJO	5,3	0,3	-1,5
GROSS FIXED CAPITAL FORMATION	7,5	3,2	3,1
EQUIPMENT GOODS AND OTHER PRODUCTS	3,8	-1,8	-5,1
DOMESTIC DEMAND	4,2	1,3	0,5
EXPORTS OF GOODS AND SERVICES	4,9	4,1	4,0
IMPORTS OF GOODS AND SERVICES	6,2	2,6	1,9
FOREIGN SECTOR (Contribution to GDP Growth)	-0,8	0,2	0,4
EMPLOYMENT	2,9	0,2	-0,5
OUTPUT PER WORKER	0,8	1,4	1,5
NOMINAL GDP	7,0	4,6	3,5

In the last 12 years Spain has followed two models of budget policies. Between 1996 and 2004, with the Partido Popular in office, public deficit was eliminated — from a negative budget balance of 6.6% of GDP, budget balance was achieved —, public spending was reduced from 43.2% of GDP to 38.9%, thus increasing the sphere for private initiative to create employment. Austerity, spending control and a legal frame for budget stability and for tax and structural reforms enabled the accession to the Eurozone, the reduction of interest rates and an unprecedented growth and creation of employment. The economic and budget policies of Zapatero's Government, in contrast, are dominated by inertia and uncritical self-satisfaction. In his term of office, the regulations of the Budgetary Stability Act have been relaxed, structural reforms have been rejected, spending has grown systematically more than our economy, and tax burdens have increased. The budgets for 2009 were the opportunity to change this situation, but this has not happened. The consequences are and will be suffered by all Spaniards.

The tax burden in Spain increased by 3 points of GDP between 2004 and 2007, six times more than the average of the OECD countries. This way, the surplus of the Socialist Governments was born bearing an original sin: the said surplus was not achieved by lowering spending, but by increasing incomes. Later, the insufficient budget surplus achieved through the increase of taxes has been dilapidated, in just 6 months, over populist measures such as the famous “400 euros” promised by Zapatero at the Presidential campaign and which — with a cost of 5,400 million euros — will ultimately not benefit the people who are most in need.

“In Spain, unemployment has increased by 3.3 points in one year, according to the latest Eurostat data, while in the Eurozone it has done so by only 0.1%, and in the European Union as a whole it has decreased by two tenths”

While State Budgets are always important — they're the main economic annual law — they grow even more important in a situation of crisis such as the current one, where monetary policies, a responsibility transferred to the European Central Bank, cannot be used. Our economy needs a change of direction. At this moment, when the international financial crisis blazes at full intensity, Spain is suffering a rapid worsening of real economy which bears no comparison to that of the countries surrounding us. A deterioration which can be summarised in 807,000 unemployed more in just one year and a public deficit forecast for this year of 2.3% of GDP.

In Spain, unemployment has increased by 3.3 points in one year, according to the latest Eurostat data, while in the Eurozone it has done so by only 0.1%, and in the European Union as a whole it has decreased by two tenths. Retail consumption also exhibits a greater weakness in our country, it has fallen 5.8% in one year, versus the 0.2% drop experienced in the EU as a whole. Our current account deficit continues orbiting around 11%, while inflation carries a difference of 1% with respect to the rest of the countries of the Eurozone.

Lack of credibility of macro-economic scenarios

The macro-economic table presented as a basis for the 2009 Budgets has no credibility at all and all analysts have said as much. The Government already drafted a totally unrealistic Budget for 2008. In it, the prediction was that Spanish economy would grow by 3.3% something which has proved to be totally wrong (see table). The Government has had to reduce this figure consistently more until reaching, according to the latest revision, 1.6%. Nevertheless, nobody doubts today that 2008 will end with an even lower growth rate than the one forecasted in the latest revision. The drop in incomes from taxes up to the month of August already exceeds 10% and it is difficult to see how the loss of incomes at the end of the year will stop at the 24,500 millions predicted. This means that from the surplus initially forecasted we have passed over to a deficit exceeding 1.6% of GDP, as the Socialist Administration predicts today.

The Government is forecasting a growth of 1% for 2009, a very low rate of growth, but which is still far away from the predictions made by analysts and economic observatories, which set it below 0.3% or 0.5% next year. The International Monetary Fund has checked its predictions on world economy growth, and now anticipates a recession in Spain, with a reduction of GDP of 0.2%. The Governor of the Bank of Spain himself has not rejected a null growth for next year at his appearance at the Congress of Deputies. With this outlook for growth, the Government calculating a decrease of incomes of only 0.1% is irresponsible with respect to the forecast calculated for the end of 2008.

“Confronting the weaknesses of the Spanish economy with respect to its lack of competition capacity and low productivity is becoming an increasingly pressing necessity”

Acknowledging that Spain is going through a double crisis is essential: on the one hand, we have the international financial crisis which is affecting our financial system and its capacity to grant credits to families and companies; and on the other hand, we have the competition crisis of our economy which, sharpened by the financial crisis, damages our production sector with the resulting increase of unemployment and of company destruction.

By submitting unrealistic macro-economic figures based on an incorrect diagnosis, the Government is complicating decision-making by economic agents even more. Budgets for 2009, by denying to confront the crisis, contribute to make it even worse, as they undermine international confidence in our country and institutions. The driving force behind growth in recent years has been domestic demand and, specifically, household consumption. These magnitudes have plummeted and neither foreign demand nor investment have taken over. In fact, the Government's forecast predicts a drop in private consumption of 0.4%, but deeper still is the predicted drop of investment, which will contract down to -1.5%. The indebtedness situation dragged by households and families hinders our getting out of the crisis and diminishes families' quality of life and entrepreneurial development.

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Return to public deficit due to excessive spending

While year 2008 had been calculated to end with a predicted surplus of 1.15%, the current outlook is that it will do so with a deficit of at least 1.6% of GDP. This sudden change is the logical consequence of not designing a good budget. The said Budget was based on a GDP growth of 3.3%, which has proved unrealistic. Furthermore, the crisis has unleashed a collapse of economy, which has led to incomes staying below the predicted 17,500 million euros, expenditure, working as automatic stabilizers, rocketing upwards, and Government spending increasing 10% more than was initially calculated.

The Government's forecast for 2009 is a deficit of 1.5% of GDP for the Central Administration, improving the results for 2008 (deficit of 1.6% of GDP). If we add Social Security (surplus of 0.8% of GDP), Autonomous Communities (deficit of 1% of GDP) and local entities (deficit of 0.2%), the deficit for 2009 of all Public Administrations together will reach, according to the Government's forecast, 1.9% of GDP. But this will only happen if two very unlikely things take place: economy should start to grow as of June 2009 and the unemployment rate must stay below 12.5%. As both hypotheses are unrealistic, the most likely thing is that we will have problems to meet the targets of the Stability and Growth Pact, which sets the deficit limit at 3% for Public Administrations as a whole.

In a situation such as the current one, where the capacity of Government's economic policy is limited to Budget policy and structural reforms, Government spending and account stability acquire special relevance. The Government should have drafted more austere public accounts. After the 2005 Budget, Government spending has been increasing much more than economic growth, and much more than what it had grown in the four previous years.

The proposal for 2009 is to increase non-financial total spending by 3.3%, greatly surpassing the desirable one, of approximately 2%. When the Government modified the Budget Stability Act and relaxed the Budget balance criteria, it opened the way for Spain's return to public structural deficit. By acting without restriction during the years of economic growth, the Socialist Government has consolidated an extraordinary growth of spending, and when difficulties have come our way, the financial capacity of the State has drained empty in just two quarters.

Employment Destruction

In 2008 employment evolution has suffered a radical change. After 14 years of uninterrupted employment creation, the trend has been disrupted. In 2008 the figure of employed people has gone down and the unemployment rate has rallied again to 11.3% in the third quarter of 2008, according to EPA (Economically Active Population Survey) data. The Government's forecast for 2009 is an increase of the unemployment rate to 12.5% with a drop of employed workers of 0.5%. Spanish economy has ceased to create employment and the PSOE has already registered worse unemployment figures than the Governments of the Partido Popular, in spite of Zapatero's declarations when he said that the worst unemployment figures of the PSOE would always be better than those of the PP Governments.

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Budgets will not help to create employment. Spain will end 2008 with an increase of unemployment of more than 800,000 people and a very worrying outlook for 2009. In fact, the budget allocation for unemployment benefits has a growth forecast of 24.4%. In absolute terms, the allocation for unemployment reaches 19,292 million euros, twice the sum allocated to R&D. The Budget needs to come with work reforms attached to it enabling to boost employment creation, reforms where employment is encouraged over benefits and production expenses outweigh current expenses.

Social Expenditure

Defending social expenditure is the main reason given by the Government in support of their 2009 Budgets. But reality is quite different. In the first place, the Government cannot take for itself unemployment benefits and pensions as if they were a discretionary policy promoted by the Government itself. These are rights that belong to citizens and, therefore, the allocation of money is not to be negotiated. This is never a matter decided on by the Government, but the result of an agreement of all political forces. The necessity of increasing in such

a significant amount the sums allocated to unemployment show, once again, the failure of the policies followed these years.

In the second place, two of the most important social items of social expenditure are education and healthcare which, being as they are a responsibility of the Autonomous Communities, will be affected by the reduction of resources allocated to the said communities. In the third place, the budget allocation for the Dependency Act is only of 1,158 million euros, an insufficient amount in light of the needs they are already taking care of in the Autonomous Communities. The “core law” of the Socialist Government is still lacking a sufficient allocation to fully satisfy the necessities it wants to cover.

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Investments

Real investments (chapter VI) of the 2009 Budgets are reduced by 1.7% with respect to 2008. Nevertheless, the said decrease does not affect all Autonomous Communities. The allocation of State investments does not respond to necessity and objective criteria, but has much to do with the need of getting enough Parliamentary support for the Budgets and of meeting the precepts of the Statutes of Autonomy passed during Zapatero’s first term in office. In fact, as there are no projects under study for Catalonia and the Balearic Islands, a budgetary credit of 1,000 million euros for 2009 is established for these two Autonomous Communities without specific projects. Investments reveal that these budgets are not designed to face a crisis, but rather to “skirt the issue” seeking nationalist votes. An example that speaks for itself is the price surpassing 200 million euros that all Spaniards will have to pay for the support of PNV and BNG to the Budgets.

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Local and Autonomic Financing

This Budget continues without confronting the reform of the financing model of the Autonomous Communities; something which the Government had committed itself to do as top priority. Neither does it tackle the necessary reform of the financing system of city councils. The real estate crisis has

revealed with no shadow of a doubt the perversity of a system through which some city councils financed their current accounts with the surpluses emanating from urban development management. In fact, the transfers to Autonomous Communities will increase by 2.2% in 2009, while those to local entities will decrease by 0.1%. All this anticipates that the difficult financial situation suffered by the Autonomies and the city councils in 2008 will get significantly worse in 2009, in spite of the debt margin that the Budget itself acknowledges for them, with a predicted deficit of 1% of GDP for the former and of 0.2% of GDP for the latter. Any of the solutions to unblock the autonomic and local financing model will invalidate the Budget submitted by the Government.

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Absence of Reforms

The Budget for 2009 does not include any type of structural reform. Nevertheless, for the first time since 2004, the Government has submitted a bill containing tax measures but to which it denies its nature and rejects calling it a Complementary Act. In it are several technical amendments and the important reforms only deal with the elimination of the tax on wealth. This measure will promote savings in the long term and satisfies one of the proposals of the Programme of the Partido Popular. Nevertheless it should never have been the first nor the only reform devised in response to the crisis, both from a situational and structural point of view. Missing are measures promoting investment, reducing the tax burden on SMEs, favouring small savers or contributing to reactivate the real estate market. There is no reform promoting a change of the economic growth model or encouraging competition and economic freedom, or that increases the productivity and competition levels of our economy.

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The Budget should also include a structural reform of public spending but also, other structural reforms should be tackled. The international bodies and investors are punishing Spain for its low reformist profile and the inactivity of our Government is making the Spanish Treasury pay a higher interest for its debt than other economies of the Eurozone (more than 50 basic points' difference with the German bond).

Uncertainty at the Social Security

The evolution of the Social Security Budget is one of the great uncertainties generated by the accounts presented for 2009. At a time when unemployment is increasing and the figures of social security contributors have significantly decreased in recent months, the forecast of an increase of the Social Security surplus in 2009 comes indeed as a surprise. While the Budget for 2008 predicts a surplus of 0.6% of GDP, in the Budget for 2009 the Government expects a surprising increase of the surplus of 0.8%, as a consequence of expecting an increase of current incomes of 8.5%.

Meeting the deficit target of 1.9% of GDP and enabling the reserve fund of the Social Security to continue increasing depends upon maintaining that unlikely surplus. Up to now, the Government has refused to call for a meeting of the Toledo Agreement which, through the conformity of all the political forces, seeks to guarantee the sustainability of the pension system. Reality may make this meeting unavoidable.

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