

30 September, 2014

Excessive Deficit Procedure

2nd notification 2014

Excessive Deficit Procedure (2nd notification for 2014)

According to EU regulations, Statistics Portugal is sending today to Eurostat the second notification for 2014 related to the Excessive Deficit Procedure (EDP). Table 1 of the notification, presented below, summarizes the main results for the period 2010-2014.

The present notification is in accordance with the new European System of Accounts 2010 (ESA2010), implying a significant number of methodological changes that resulted in important revisions compared with the previous notification.

Table 1: Reporting of government deficit/surplus and debt levels and provision of associated data

Member State: Portugal Data are in millions of euros Date:31/03/2014	ESA 2010 codes	2010	2011	2012	2013	2014
		Final	Final	Half-finalized	Half-finalized	Planned
Net borrowing (-)/ net lending (+)	B.9					
General government	S.13	-20 100,2	-12 967,5	-9 310,2	-8 309,2	-8 335,8
- Central government	S.1311	-19 333,3	-13 162,5	-10 392,0	-9 110,1	-9 920,4
- Local government	S.1313	-1 565,8	- 242,5	781,3	391,8	666,7
- Social security funds	S.1314	798,9	437,5	300,5	409,1	917,9
General government consolidated gross debt						
Level at nominal value outstanding at end of year		173 062,5	195 689,6	211 784,3	219 225,0	223 148,1
<i>By category:</i>						
Currency and deposits	AF.2	11 702,5	10 143,0	9 388,1	10 490,6	
Debt Securities	AF.3	135 040,9	123 921,9	116 797,1	114 402,5	
Short-term	AF.31	21 715,2	12 027,0	13 025,4	7 411,7	
Long-term	AF.32	113 325,7	111 894,9	103 771,8	106 990,8	
Loans	AF.4	26 319,1	61 624,7	85 599,1	94 331,9	
Short-term	AF.41	4 354,0	4 486,0	2 948,7	2 381,3	
Long-term	AF.42	21 965,1	57 138,6	82 650,4	91 950,6	
General government expenditure on:						
Gross fixed capital formation	P.51	9 478,7	6 139,5	4 271,2	3 686,1	4 420,1
Interest (consolidated)	D.41 (uses)	5 268,1	7 604,4	8 352,8	8 530,3	8 849,4
Gross domestic product at current market prices	B.1*g	179 929,8	176 166,6	169 668,2	171 211,0	174 548,8
<i>Memorandum items:</i>						
Net lending (+)/Net borrowing (-) on GDP		-11,2%	-7,4%	-5,5%	-4,9%	-4,8%
General government consolidated gross debt on GDP		96,2%	111,1%	124,8%	128,0%	127,8%

I.

As usual since 2006, the present notification was prepared under the Institutional Agreement in the field of General Government Statistics signed on the 10th of January 2006 between Statistics Portugal (National Accounts Department), the Portuguese Central Bank (Statistics Department) and Budget Directorate-General.

For the years prior to 2014, the compilation of the Net lending / net borrowing is prepared by Statistics Portugal and the Gross Debt is compiled by the Portuguese Central Bank.

For the current year (2014), the estimates of Net lending / net borrowing and Gross Debt are a responsibility of the Ministry of Finance¹.

Under Council Regulation (EC) No. 473/2009 the notifications begin a joint work between national statistical authorities and Eurostat which, within a three weeks deadline, should examine the notifications and publish the final results for all Member States.

II.

As usual in previous press releases, the table below details the net lending/net borrowing and the gross debt of (Regional and) Local Government (S1313).

Unit: million euro	2010	2011	2012	2013
Net borrowing (-)/ net lending (+)				
- Regional and Local Government	-1 439,6	- 586,0	855,9	408,3
<i>Regional Government of Madeira</i>	-1 208,3	- 725,3	- 200,5	81,3
<i>Regional Government of Azores</i>	- 112,9	- 104,5	- 82,5	- 7,0
<i>Local Government</i>	- 244,6	587,4	1 064,3	317,5
Gross Debt				
- Regional and Local Government	10 690,5	11 046,6	10 458,4	10 718,6
<i>Regional Government of Madeira</i>	3 641,8	4 058,3	4 117,7	4 290,2
<i>Regional Government of Azores</i>	971,0	1 057,6	1 146,5	1 262,1
<i>Local Government</i>	6 077,7	5 930,7	5 194,1	5 166,4

It is also worth mentioning that the transfers received by Central Government are considered in the compilation of Regional and Local Government net lending / net borrowing. In 2013, these corresponded to the following amounts,

¹ According to information from the Ministry of Finance, the estimated value for 2014 for the net borrowing of general government is 8,336 M€, corresponding to 4.78% of GDP. This value includes the amount of approximately 1,289 M€ (0.74 percentage points of GDP) for the recording of the financing operations of the State to the public enterprises "Carris" and "STCP" and to the write-off of non performing loans by BPN Crédito, held by Parvalorem, SA.

It should be mentioned that these values are already registered in the quarterly accounts by institutional sector in Q2 2014, also published today.

expressed in million Euros: Regional Government of Madeira, 241.8; Regional Government of Azores 318.9; Local Government, 2,319.8.

These transfers are recorded as expenditure in Central Government, implying that they consolidate in the General Government Account.

As far as gross debt is concerned, according to European legislation, the following clarifications are relevant: i) Trade credits are excluded; ii) Debt of public corporations not classified inside General Government is not considered; iii) Debt of municipalities and parishes located in the territory of the Autonomous Regions is included in Local Government.

III.

Statistics Portugal released, on August 29th, National Accounts compiled according to the new European System of Accounts (ESA 2010). The present notification on the Excessive Deficit Procedure (EDP) is also in accordance with this new system, implying a significant number of methodological changes compared with the previous notification.

ESA 2010 introduced several methodological changes in the process of the compilation of General Government Accounts, with significant impacts on its balance. Simultaneously, as mentioned in previous press releases, the level of GDP was also revised due to methodological changes arising from the implementation of ESA2010 and the incorporation of new structural information.

The next table presents the net borrowing in percentage of GDP, with the decomposition of the effect of changes in the net borrowing (numerator) and the effect of changes in GDP (denominator).

	2010	2011	2012	2013
EDP Balance in % of GDP (ESA95)	-9,8	-4,3	-6,4	-4,9
Balance	-1,8	-3,3	0,8	-0,1
GDP	0,5	0,2	0,2	0,2
Total Revision	-1,3	-3,0	1,0	0,0
EDP Balance in % of GDP (ESA10)	-11,2	-7,4	-5,5	-4,9

The main changes associated with the new system of accounts are:

a) **New rules of analysis of the sector classification of public institutional units**

ESA 2010, as well as the new version of the Manual Deficit and Debt associated with it, has introduced major changes in the criteria that should be analysed in the classification of public institutional units. ESA 2010 significantly strengthens the qualitative analysis criteria of public institutional units, highlighting aspects related to the control and the nature of revenues. Moreover, the quantitative criterion ("market / non-market test") was also amended, now including, in the denominator, corresponding to operating costs, the net interest charge.

In consequence of the amendments, several institutional units, previously classified in other institutional sectors, were reclassified in the General Government (GG) sector. Please see the box at the end of this press release with additional details about the new rules for sector classification of public entities.

Overall, the entities now included in the GG sector present deficits, leading to an increase of net borrowing of GG. However, the inclusion of some units in GG that in the past had originated the registration of specific transactions with impact on the deficit, namely capital injections classified as capital transfers, implied the cancellation of these operations, which translates into an improvement in the balance in the years in which those operations occurred. Moreover, the deficits that these units recorded in previous years are now reflected in the balance of GG.

The most relevant specific operations were the following:

- In 2011, the debts of the Regional Government of Madeira to the company SESARAM and the assumption of its guaranteed debt (approximately 430 M€), no longer have impact due to the inclusion of that company in the GG sector (subsector of Regional and Local Government).
- In 2012, the conversion of loans granted by Parpública, public shareholdings (SGPS) in a capital increase of SAGESTAMO - Shareholdings Management Company Real Estate, SA (750 M€), which was recorded as a capital transfer of GG, no longer have impact due to the inclusion in the GG sector of the entities involved.

b) **New rules for registration of transfers of pension funds**

According to ESA 95, the transfer of pension funds (public or private companies) for the GG sector, in which the State initially receives a high amount of financial assets in exchange for the future pension payments, was accounted, at the time it occurred, as revenue (capital transfer) with a positive effect on its balance.

With ESA 2010 no revenue with effect on the balance is recorded, since the transfer of the pension fund is now considered a financial transaction. Consequently, as well as the initial payment has no effect on the balance of GG, also pensions paid in the following years, relative to employees / pensioners who were previously in the transferred pension funds, have no effect on the balance. Assuming that the financial assets initially transferred cover the present value of future pensions, this new way of recording the transfer of pension funds guarantees the inter-temporal neutrality on the GG balance.

Compared to the results published in ESA 95, this change led to an increase in net borrowing of GG in the years where there was a transfer of pension funds, notably in 2010 and 2011, as well as an improvement in subsequent years.

c) Change in the registration of interests related to swap transactions

In the previous system there were two different balances of GG: the so-called balance in national accounts, where interests did not include interest flows associated with swap transactions; and the EDP balance, which included interest on swap transactions.

In the new system the relevant balance for EDP purposes does not include those interests on swap transactions, which are now considered financial transactions.

Thus, as a result of this change, the GG balances of the present notification, compared with the previous notification, are upwards revised in the reporting year. The balance improvement is determined by the fact that, in the previous system, the interest payments associated to swap was higher than its revenues. The impact of this change in 2013 and thereafter is significantly reduced due to the cancellation of several swap operations that had been previously contracted.

The next table presents the changes occurred in the net borrowing of General Government accounts.

	subsector	2010	2011	2012	2013
Net borrowing (-)/ net lending (+)	S.13	-3.118,7	-5.569,1	1.331,0	-187,4
- Central Government	S.1311	-3.006,7	-5.911,8	1.404,8	-168,0
- Local Government	S.1313	-126,2	343,5	-74,7	-16,4
- Social Security Funds	S.1314	14,2	-0,9	0,9	-3,0
Revisions related to the introduction of ESA 2010	S.13	-3.189,8	-5.510,9	1.379,1	-370,7
<i>of which:</i>					
Sector Reclassification	S.13	-738,6	54,5	800,2	-787,3
Transfers of pension schemes	S.13	-2.535,2	-5.774,8	368,6	378,6
Interest on sw aps	S.13	84,1	209,3	210,2	38,0
Other revisions (namely data sources)	S.13	71,1	-58,2	-48,0	183,3

In the gross debt the revisions are the following:

	subsector	2010	2011	2012	2013
Revisions related to the introduction of ESA 2010	S.13	11.047,4	10.935,0	7.421,3	6.076,5
<i>of which:</i>					
Sector reclassification	S.13	11.047,4	10.935,0	7.421,3	6.076,5
Other revisions (namely data sources)	S.13	-458,3	-486,2	-496,7	-482,1

Box: New rules in the General Government sector delimitation

ESA 2010, and the new version of the Manual Deficit and Debt associated with it, has introduced major changes in the criteria that should be analysed in the classification of public institutional units.

ESA 2010 significantly strengthens the qualitative analysis criteria of public institutional units, such as the control criterion by GG. This aspect is particularly relevant in the case of public holdings: if a public holding acts as an agent of GG for public policy purposes (channelling funds between subsidiaries or privatizations organization) demonstrating not truly having autonomy of decision, then it should be included in the GG sector, as it was the case of Parpública. The subsidiaries of this holding must be analysed individually, determining that some are classified outside the GG and others are classified within the GG (e.g. SAGESTAMO and Estamo).

Another relevant aspect in the qualitative analysis of public institutional units is the nature of the revenue. The new ESA2010 clearly defines the concept of "economically significant prices" and establishes some criteria for evaluation, as the fact that all (or the majority of) the production of a public institutional unit be sold to the GG or the capacity of GG to impose the price charged when no private competitors exist. When prices are not economically significant, revenues cannot be regarded as market income for the purpose of calculating the 50% ratio. This determined the change in classification of corporation public hospitals, which became part of the GG sector.

Regarding the nature of revenues obtained by public institutional units, they must be analyzed if some have characteristics of tax. As a matter of fact, some units, taking into consideration specific legislation conferring them certain responsibilities, have the capacity to charge fees. This is the case of the various market regulators, who have the capacity to charge fees to the units that they regulate, which, in accordance with the new ESA2010 should now be considered tax, not being included in revenue for the purposes of calculating the ratio. In consequence, the majority of market regulators are now integrated into the GG sector, with the exception of financial regulators, who have a specific subsector within the financial corporations sector.

In terms of the quantitative dimension for the analysis of the sector classification of public institutional units, the so called 50% ratio or "market/non-market ratio" some changes were also introduced. This ratio now includes in the denominator, corresponding to operating costs, the net interest charge. The changing in this criterion led to the inclusion in the GG sector of CP – Comboios de Portugal, as well as several small units.

Finally, some particular cases of reclassifications into the GG sector, namely: i) "holdings" held by public bodies with a small number of employees that do not have current management of subsidiary activities; ii) Guarantee funds of deposits controlled by the GG and with no autonomy of decision.

The following table groups, by reason, the 268 entities that were reclassified as a result of the above mentioned changes.

Units reclassified in the General Government Sector in ESA 2010

Nº	Reason
117	Quantitative criterion: sales of the producer are below than 50% of the the production costs including net interest charge (new)
92	Qualitative criterion, namely: prices are not "economically significant"; demand fully or almost exclusively done by General Government
38	Non Profit Institutions controlled by government
13	Holding Companies with zero or a reduced number of employees and that do not perform management activities of their subsidiaries
8	Market regulatory bodies (excluding financial insinstitutions)

The complete list of entities classified in the GG sector can be found in Statistics Portugal website.