IN-DEPTH ANALYSIS

European Parliament

Economic Dialogue with the Commission on 2018 Draft Budgetary Plans

ECON on 27 November 2017

Vice-president Dombrovskis and Commissioner Moscovici have been invited to an Economic Dialogue on the European Commission Opinions on the 2018 Draft Budgetary Plans of the Euro Area Member States based on Articles 7 and 15 of EU Regulation 473/2013.

Euro area States which are not subject to a macro-economic adjustment programme shall submit annually their **Draft Budgetary Plan** (DBP) for the forthcoming year to the European Commission (COM) and the Euro-group by 15 October. All of the 18 concerned Euro Area Member States have submitted their 2018 DBPs and, on the basis of its autumn 2017 forecast, the COM issued on 22 November 2017 its Opinions (see also COM press release) on all of them.

Box 1: Autumn Budgetary Surveillance

The objective of submitting DBPs to the COM and the Eurogroup is to enable an **enhanced monitoring of national budgetary policies** in the euro area and ensure that the national budgets are consistent with the economic policy recommendation issued in the context of the SGP and the European Semester for economic policy coordination.

This autumn surveillance of the DBPs **is complementary and linked** to other EU economic governance procedures i.e.:

(1) The COM assesses in its DBP Opinions the extent to which Member States have implemented the Country-Specific Recommendations, in particular the compliance with their Medium-Term Objective (MTO) or with the adjustment path towards it;

(2) For Member States subject to the Excessive Deficit Procedure (EDP), the COM assesses the compliance with the latest EDP recommendation.

Six countries (**Germany, Lithuania, Latvia, Luxembourg, Finland and the Netherlands**) are assessed to be compliant with the SGP, six (**Estonia, Spain, Ireland, Cyprus, Malta and Slovakia**) are assessed to be broadly compliant with it and six (**Belgium, France, Italy, Austria, Portugal and Slovenia**) are judged to be at risk of non-compliance. The assessment is altogether slightly better than the assessment of the 2017 DBPs, since the most critical category “risk of compliance” contains now six countries, compared to seven last time, and the best category (“compliance”) has increased by one Member State.

ECONOMIC GOVERNANCE SUPPORT UNIT
Authors: J. Angerer, M. Ciucci, T. Japunčić
Directorate-General for Internal Policies
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The positive and negative developments at Member States' level are:

- Better assessments than in the last exercise: (a) three Member States have left the category "risk of non-compliance", either towards the category "broad compliance (**Cyprus)** or even towards "compliance" (**Lithuania** and **Finland**) and (b) one country (**Latvia**) moved from "broad compliance" towards "compliance".
- Worse assessments than in the last exercise: **Estonia** and **Slovakia** moved from "compliance" towards "broad compliance" and **France** and **Austria** from "broad compliance" towards "risk of non-compliance".

An overview of the Opinions of the euro area Member States **at risk of non-complinace with the SGP** is in the **annex to this briefing**; that overview provides the main arguments underpinning the assessments of these countries.

For Belgium and Italy, the COM opinions conclude, exclusively on the basis of the autumn 2017 forecast, that the **debt reduction benchmark** (see Box 2) will be breached. They also state that the DBPs for these countries (and also for other Member States, such as France, Austria, Portugal and Slovenia) do not include sufficient information to assess compliance with the debt reduction benchmark or with transitional arrangements.

In a letter of 22 November 2017 to the Italian authorities, the COM informed about its intention to reassess Italy's compliance with the debt reduction benchmark in spring 2018. The letter states *inter alia* that "*The adoption of the 2018 budget with no watering down on the key provisions will be crucial, as will its subsequent strict implementation to deliver a structural effort of at least 0,3 % of GDP. We would also like to underline the importance of avoiding backtracking on the important fiscal structural reforms, notably as regards pensions, which underpin the long-term sustainability of Italy's debt*."

When finalising the opinions, the COM highlighted in letters (of 27 October 2017) to Belgium, France, Italy and Portugal **potential non-compliances ("significant deviations") of the DBPs** of these countries from the requirements under the SGP and asked the respective governments to submit further information so that the COM can use in the final COM opinions on the DBP. The replies of 30/31 October (Belgium, France, Italy and Portugal) focused on fiscal measures and structural reforms which were not included in the calculations of the structural balance by the COM ("no policy change scenario") or on methodological issues (notably Italy).

Box 2: Entry into force of the debt reduction benchmark

EU Regulation 1467/97 stipulates that the debt rule (which is relevant for countries with a debt above 60% of GDP) is applicable after a transition period of three years from the correction of the excessive deficit, if the country was in an EDP on 8/11/2011.

Member States within the transition period have to comply with a Minimum Linear Structural Adjustment (MLSA). The COM staff working documents of May 2016 stated that the transition periods for Italy and Hungary expired in the end of 2015 and that they will expire for Belgium, Austria and the Netherlands in the end of 2016. Germany, Finland and Malta were already before 2016 subject to the debt rule. Since Ireland, Cyprus and Slovenia exited the EDP (opened before 8/11/2011) in 2016, their transition periods will expire in the end of 2018.

Regarding Portugal and Greece, whose deficit is not any more excessive since 2016, the transition period will expire end of 2019. For Croatia, which entered the EU after the entry in to force of the regulation and whose deficit is not any more excessive since 2016, the debt rule is applicable without a transition period, i.e. as from 2017. As regards Spain and France, which are still in EDP (opened before 8/11/2011), the debt rule will become applicable after the transition period of three years from the correction of the excessive deficit.

However, as seen above, they did not change the overall COM assessment of compliance for these countries.

The Eurogroup of 4 December 2017 is expected to discuss the 2018 DBPs on the basis of the COM Opinions on these plans.

A comparison of key features included in the 2018 DBP with the COM autumn 2017 forecasts shows that **six euro area Member States (Spain, France, Italy, Austria, Portugal, Slovenia) are overall clearly more optimistic than the COM in their growth, debt, deficit and/or structural deficit projections** (see separate EGOV table), while only Germany and Cyprus have overall clearly more pessimistic forecasts than the COM on these indicators. For the other countries, the situation is more balanced. Compared to Spring 2017, the differences between forecasts by Member States and COM for 2017 and 2018 have clearly decreased, which seems normal given that by now more economic evidence is available for 2017. Compared to autumn 2016 however, differences have changed more significantly: one year ago, most of the euro area countries had clearly more optimistic forecasts than the COM (see separate EGOV briefing). In other words, a certain convergence of economic forecasts by Member States and COM can be observed. On the other hand, significant differences between Member States and COM remain also in autumn 2017 for the forecasts on structural balance and/or debt levels (including for Spain, France, Belgium, Germany, Italy, Cyprus, Latvia and Slovenia).

Another EGOV note provides an **overview of the role played by independent national fiscal bodies in the preparations of budgets** in Member States. A key finding is that a clear majority of euro area Member States (15 out of 18) have used in their 2018 and 2017 DBP macro-economic forecasts prepared or endorsed by independent fiscal bodies; exceptions being for the 2018 DBP Germany and Finland and for the 2017 DBP Germany, Finland and Lithuania. In October 2017, the European Fiscal Board assessed in this respect: “*The independent fiscal institutions vary significantly across the EU Member States in terms of their design, scope, and mandate. This heterogeneity is mainly determined by pre-existing institutional setups prevailing at the national level, including local traditions, historical experiences and country-specific policy challenges. Although national specificities are to be acknowledged in the setup of independent fiscal institutions, there is also a need to ensure that they enjoy a basic degree of effectiveness and leverage vis-à-vis national governments. The broad panorama of independent fiscal institutions offers a unique opportunity to draw lessons of good practice, in line with the mandate of the European Fiscal Board. However, providing a full and comprehensive review of all EU independent fiscal institutions is a daunting task that goes beyond the scope of this report.*”

The adjustment requirements under the SGP are inter alia set in **structural terms**, especially in the preventive arm. **Table 1** below shows changes in the structural balances as forecast by the COM and the structural efforts recommended by the Council under the preventive arm of SGP. While this comparison indicates that Germany, Estonia, Ireland, Lithuania, Luxembourg, Malta and the Netherlands are in line with the recommended effort by the Council, it does not prima facie mean that the other countries would be in breach of the respective Council recommendations. The assessment of compliance includes other aspects than the change in the structural balance, such as: the magnitude of deviations, bottom-up assessments of individual measures, compliance with expenditure benchmarks, change in the primary structural balance (=structural balances adjusted by interest payments) and relevant factors such as the implementation of reforms with a positive impact on the growth potential.

Table 1: Structural efforts and commitments under the SGP in 2017 and 2018

Member State	MTO (structural budget position = sbp)	Recommended annual structural effort (percentage points=pp) (to adjust towards or remain at the MTO for the Member States under the preventive arm of the SGP)[1]		Projections on the structural budget balance (Commission Autumn 2017 forecast)			
				pp	sbp	pp	sbp
		2017 (CSRs 2016)	2018 (CSRs 2017)	2017		2018	
BE	0.0 sbp	0.6 pp	0.6 pp	0.6 pp	-1.5 sbp	0.0 pp	-1.5 sbp
DE	-0.5 sbp	In line with its MTO	In line with its MTO	0.0 pp	0.9 sbp	0.0 pp	0.9 sbp
EE	-0.5 sbp	In line with its MTO	In line with its MTO	-0.7 pp	-1.1 sbp	-0.3 pp	-1,4 sbp
IE	-0.5 sbp	0.6 pp	0.6 pp	0.6 pp	-1.3 sbp	0,8 pp	-0.5 sbp
IT	0.0 sbp	0.6 pp	0.6 pp	-0.4 pp	- 2.1 sbp	0.1 pp	-2.0 sbp
CY	0.0 sbp	In line with its MTO	0.2 pp	-0.7 pp	0.4 sbp	-0.4 pp	0.0 sbp
LV	-1.0 sbp	In line with its MTO	-0.3	-1.2 pp	-1.8 sbp	0.0 pp	-1.8 sbp
LT	-1.0 sbp	In line with its MTO	In line with its MTO	-0.7 pp	-0.9 sbp	0.0 pp	-0.9 sbp
LU	-0.5 sbp	In line with its MTO	In line with its MTO	-1.4 pp	0.6 sbp	-0.3 pp	0.3 sbp
MT	0.0 sbp	0.6 pp	In line with its MTO	-0.2 pp	0.6 sbp	-0.5 pp	0.1 sbp
NL	-0.5 sbp	0.6 pp	In line with its MTO	-0.6 pp	0.3 sbp	-0.5 pp	-0.2 sbp
AT	-0.5 sbp	0.3 pp	0.3 pp	0.1 pp	-0.9 sbp	-0.1 pp	-1.0 sbp
PT	0.25 sbp	0.6 pp	0.6 pp	0.2 pp	-1.8 sbp	0.0 pp	-1.8 sbp
SI[2]	0.25 sbp	0.6 pp	1.0 pp	-0.1 pp	-1.6 sbp	0.0 pp	-1.6 sbp
SK	-0.5 sbp	0.5 pp	0.5 pp	0.4 pp	-1.6 sbp	0.4 pp	-1.2 sbp
FI	-0.5 sbp	0.6 pp	0.1 pp	-0.6 pp	-1.0 sbp	-0.4 pp	-1.4 sbp
BG	-1.0 sbp	0.5 pp	In line with its MTO	-0.1 pp	0.0 sbp	-0.2 pp	-0.2 sbp
CZ	-1.0 sbp	In line with its MTO	In line with its MTO	-0.1 pp	0.8 sbp	-0.4 pp	0.4 sbp
DK	-0.5 sbp	0.25 pp	In line with its MTO	-0.7 pp	-0.5 sbp	-0.1 pp	-0.6 sbp
HR	-1.75 sbp	0.6 pp	In line with its MTO	-0.6 pp	-0.9 sbp	-1.0 pp	-1.9 sbp
HU	-1.5 sbp	0.6 pp	1.0 pp	-1.2 pp	-3.2 sbp	-0.4 pp	-3.6 sbp
PL	-1.0 sbp	0.5 pp	0.5 pp	0.1 pp	-2.1 sbp	-0.2 pp	-2.3 sbp
RO[3]	-1.0 sbp	0.5 pp	0.5 pp	-1.1 pp	-3.3 sbp	-1.0 pp	-4.3 sbp
SE	-1.0 sbp	In line with its MTO	In line with its MTO	-0.3 pp	0.8 sbp	-0.2 pp	0.6 sbp

Sources: COM Autumn 2017 forecast for the estimated and projected structural budget balances; country specific recommendations (CSRs) adopted by the Council in July under the preventive arm of the SGP (the country specific MTO and the quantitative fiscal effort requested by the Council are included in the recitals of the CSRs).

Notes: [1] In the case a Member States does not have a quantitative fiscal effort request for 2017 and/or 2018, it is indicated in the table as being "in line with its MTO" (this may cover cases (a) where the actual structural budget balance is above the target or (b) below the target due to temporarily flexibility allowed in the preventive arm or (c) only with a minor deviation below the target). For other Member States (which have not reached their MTO), the Council has requested specific fiscal efforts in quantitative years (these specific requests for 2018 are included in the recitals of the 2017 CSRs). This table does not prejudge the assessment of "effective action" by the COM, which follows an EU methodology that takes into account more aspects than the change in the structural balance;

[2] The MTO of Slovenia amounts to 0.0, but the 2016 CSR for Slovenia states that this does not respect the requirements of the SGP; 0.25 sbp is the minimum MTO calculated by the COM;

[3] On 16 June 2017, the Council adopted a specific recommendation with a view to correcting the significant observed deviation from the adjustment path toward the MTO in Romania.

In October 2017, the European Fiscal Board issued recommendations on how to strengthen the SGP, inter alia by simplifying rules (see **Box 3**). Also the Eurogroup addressed this issue in its latest meeting (November 2017); the Present of the Eurogroup summarised the corresponding discussion as follows: "*On the **rules** themselves, the returning issue is that they **are complex, they are not predictable, they are sometimes not based on observable criteria**. That makes it difficult for national ministers to design their budgets, to explain what happens to their electorates, and that is an issue that keeps coming back. On the other hand, we all know why the rules are complex: because we want to take into account all different circumstances that may arise and we have allowed for a number of flexibilities. (...) we have to be realistic there: when people say let's make rules much more simple, I am not sure that they want accept that they could also become much more harsh, in difficult circumstances. So that is a trade-off that we must realise. **There was a general agreement that reducing debt levels would become more and more important**, and is already if you realise that fiscal deficit in the eurozone is now less than 1,5% and will continue to go down, looking forward. So debt will become a bigger issue (...)*" See annex 2 for recent fiscal sustainability assessments by the Commission and some public debt indicators.

Box 3: European Fiscal Board: Suggestions related to reforming the SGP

- Under the corrective arm of the SGP, allow for updating EDP recommendations in the event of an unexpected improvement of economic conditions. This would enhance the symmetry of rules and prevent a recurring practice to replace structural adjustments with budgetary windfalls.

- Under the preventive arm of the SGP, require Member States to compensate for past deviations from the adjustment path towards the medium-term budgetary objective (MTO). This would prevent Member States from systematically planning deviations within the allowed margins.

- Broaden and simplify the use of macroeconomic conditionality in the EU budget in order to strengthen the enforcement of the rules and safeguard the effectiveness of EU finances.

- Introduce in the SGP a link to the Macroeconomic Imbalance Procedure (MIP) by regulating the speed of adjustment towards the MTO in relation to Member States' macroeconomic imbalances. This would address the risks that imbalances may pose to fiscal sustainability.

- Reduce the complexity of the SGP, while introducing well defined escape clauses to be triggered and applied with the involvement of independent judgement. This would serve the triple aim of simplifying rules, safeguarding flexibility and enhancing transparency.

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Contact: egov@ep.europa.eu

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Annex 1: Overview of the COM opinions on 2018 DBP of countries at risk of non-compliance with the SGP

The table overleaf summarises the European Commission's (COM) **opinions on the 2018 Draft Budgetary Plans** (DBP) which are judged to be at risk of non-compliance with the Stability and Growth Pact (SGP). Please note that the current Council recommendations under the SGP are available in a separate EGOV briefing "Implementation of the SGP".

According to the categories used by COM of "*Risk of non-compliance*" means

- Under the Excessive Deficit Procedure (EDP): The COM forecast, if confirmed *ex post*, could lead to the stepping up of the EDP as the fiscal effort is not projected to be delivered and the nominal target of below 3 % is expected to be missed.

- Under the preventive arm of SGP: The COM forecast projects a significant deviation from the required adjustment path towards the MTO in 2016 and/or non-compliance with the debt reduction benchmark, if applicable.

The COM opinions include assessments of fiscal effort/effective action, which have follow a methodology agreed by Council and the COM. The last update of the methodology was published in July 2016 and the previous one in June 2014. In accordance with this methodology, all relevant data used by the COM, including data on the yields of discretionary fiscal measures, are shared with the Member States in a timely manner, enabling them to replicate the calculation underlying the COM's assessments and recommendations. Furthermore, the "terms of reference" specify in detail the "**top down**" and "**bottom up**" approaches used in the assessment of effective action by the COM. In accordance with the methodology, the whole period of the Council decision to correct the excessive deficit and not only individual years are to be assessed (see also page 39 of "Public Finances in EMU"). In addition, the Council agreed in October 2016 of two methodological steps relating to the estimation of potential output and output gaps.

Table: Overview of the COM opinions on 2018 DBP of countries with overall risks of non-compliance with the SGP

	Overall compliance with current Council recommendations under SGP** (colour code defined above)* ***Overall compliance with current fiscal related Council Country Specific Recommendations (CSRs)	***Detailed assessment as regards compliance with current Council SGP-recommendations:*** *- Member States subject to EDP: compliance with nominal target and/or fiscal effort as requested by Council EDP- recommendations* *- Member States subject to the preventive arm: compliance with MTO (or adjustment path towards MTO) and with the (transitional) debt rule as requested by the relevant Council CSR-recommendation* **2017**	**2018**
Euro area Member States subject to an Excessive Deficit Procedure (EDP)			
France	*"Overall, and after considering the need to balance the two objectives of strengthening the ongoing recovery and ensuring fiscal sustainability, the Commission is of the opinion that the Draft Budgetary Plan of France for 2018, which is currently under the corrective arm and could become subject to the preventive arm and the transitional debt rule from 2018, is **at risk of non-compliance with the provisions of the Stability and Growth Pact**. In particular, the Commission **projects a risk of significant deviation from the required adjustment towards the MTO for 2018.**"* (p. 5)	Nominal target: *"**The Commission 2017 autumn forecast expects the headline deficit to be at 2.9% of GDP in 2017, in line with the plans of the authorities.** However, two major risks underlie the official target for 2017. First, the budgetary impact in 2017 stemming from the recapitalisation of AREVA could be higher than currently envisaged by the authorities. Compared to the DBP, the risk to the Commission 2017 forecast is even greater to the extent that this operation is not included at all. Second, the total invalidation of the 3% tax on dividends by the French Constitutional Court entails a risk for both the 2017 and 2018 deficit targets. While the total cost of around 0.45% of GDP could be spread over several years, the decision could trigger significant reimbursements already in 2017. The authorities introduced an exceptional tax on*	Nominal target: *"**For 2018, the Commission 2017 autumn forecast projects the headline deficit to remain at 2.9% of GDP, 0.3 percentage points higher than the planned deficit in the Draft Budgetary Plan.** When compared with the Commission forecast, the risks underlying the official plans are mostly related to a more dynamic spending by central and local authorities and stronger social spending. The invalidation of the 3% tax on dividends, which will probably entail some budgetary effect in 2018, is another main risk to the official plans as regards the durability of the correction of the excessive deficit."* (p. 3) Top-down assessment: *"According to the Draft Budgetary Plan, **the nominal growth rate of net***

		companies designed to compensate the budgetary impact of the decision in 2017, that is expected to amount to around half of the total cost and is not included in the Commission 2017 autumn forecast. It is not excluded, however, that the impact in 2017 would be higher. If these risks materialise, the deficit target of 2.9% of GDP and the correction of the excessive deficit in 2017 could be at risk." (p. 3) Top-down assessment: "***The structural balance is expected to improve by 0.2% of GDP in 2017, compared to the recommended effort of 0.9% of GDP.*** *Regarding the change in the structural balance adjusted for changes in potential growth and revenue windfalls since the recommendation, the gap vis-à-vis the recommended fiscal effort amounts to 0.7% of GDP in 2017."* (p. 4) Bottom-up assessment: "*Based on the bottom-up method, the fiscal effort is projected to have a* ***gap of 0.6% of GDP in 2017****."* (p. 4) Top-down and bottom-up assessment: *"The cumulated shortfall over 2015-2017 would be of 1.6% of GDP based on both the top-down and bottom-up metrics. France is thus* ***not expected to deliver the fiscal effort recommended under the EDP****."* (p. 4)	***primary government expenditure exceeds significantly the benchmark rate in 2018 (gap of 0.5% of GDP). The (recalculated) structural balance also signals a risk of significant deviation (gap of 0.6% of GDP).*** *The small difference between both indicators stems primarily from the projected revenue windfalls that are broadly offset by the planned increase in public investment above its four-year average in 2018. Therefore, an overall assessment confirms the reading of the expenditure benchmark and concludes that the Draft Budgetary Plan plans a significant deviation from the requirements of the preventive arm in 2018.* ***The Commission 2017 autumn forecast projects a wider deviation by 0.9% of GDP from the expenditure benchmark and by 1.0% of GDP the required change in the structural balance.*** *The difference between the two pillars is marginal and, accordingly, the overall assessment would point to a risk of significant deviation from the recommended adjustment path towards the MTO in 2018."* (p. 4)
	"Concerning the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 2017, the Draft Budgetary Plan confirms the implementation of a more pronounced decrease over five years in the	Debt rule: "*If the excessive deficit were to be corrected in a timely and durable manner, France would have to comply with the requirements of the preventive arm of the Stability and Growth Pact from 2018 onwards and, as its debt ratio is planned to be at 96.8% of GDP in 2017 according to the Draft Budgetary Plan, would be in the three-year transition period to make sufficient progress towards compliance with the debt reduction benchmark.* ***Based on the Draft Budgetary Plan, France would not make sufficient progress***	

	corporate income statutory rate compared to what was already planned. Further measures are specifically addressed to improve the growth-friendliness of the French tax structure, to promote investment and to increase the purchasing power of households, therefore ***to sustain domestic demand and growth****."* (p. 5) The Commission opinion does not provide an assesment on this part.	***towards compliance with the debt reduction benchmark in 2018. The same conclusion is reached based on the projections in the Commission 2017 autumn forecast*** *as the structural balance is projected to deteriorate by 0.4% of GDP in 2018, which implies a gap of 0.8% of GDP from the required minimum linear structural adjustment. Should the excessive deficit be corrected in 2017, as the debt ratio is projected to be at 96.8% of GDP in 2017 according to the DBP, France would be in the transition period for the following three years to make sufficient progress towards compliance with the debt reduction benchmark as defined by the minimum linear structural adjustment."* (p. 4)	
Euro area Member States not subject to an EDP			
Belgium	*"Overall, and after considering the need to balance the two objectives of strengthening the ongoing recovery and ensuring fiscal sustainability, the Commission is of the opinion that the Draft Budgetary Plan of Belgium, which is currently under the preventive arm and subject to the debt reduction benchmark, is* ***at risk of non-compliance with the provisions of the SGP****."* (p. 5)	*"The Draft Budgetary Plan points to a risk of some deviation from that adjustment path in 2017 on the basis of the real growth rate of net primary government expenditure. The planned change in the (recalculated) structural balance is compliant. In 2016 and 2017 together, the expenditure aggregate points to a risk of significant deviation while the structural balance signals some deviation."* (p. 3) *"The Commission 2017 autumn forecast shows similar deviations for both indicators in 2017 as well as in 2016-2017."* (p. 3) *"The overall assessment concludes* ***a risk of significant deviation from the recommended structural adjustment path towards the medium-term budgetary objective in 2017****, both on the basis of the Draft Budgetary Plan (gap of 0.4% of GDP) and the Commission 2017 autumn forecast (gap of 0.5% of GDP)."* (p. 3)	*"According to the Draft Budgetary Plan* ***the expenditure aggregate exceeds the benchmark rate in 2018, with a deviation at the limit of significance (gap of 0.5% of GDP). The (recalculated) structural balance points to some deviation from the requirements (gap of 0.3% of GDP)****. For 2017 and 2018 together, the Draft Budgetary Plan signals a risk of significant deviation for the expenditure aggregate (average gap of 0.4% of GDP) while the structural balance indicates a risk of some deviation (average gap of 0.1% of GDP)."* (p. 4) *"The Commission 2017 autumn forecast projects a* ***significant deviation from the expenditure benchmark in 2018 (gap of 0.8% of GDP), which is confirmed by the adjustment in the structural balance (gap of 0.7% of GDP)****. Also for 2017 and 2018 together both indicators point to a risk of significant deviation.* (...) *the overall assessment on the basis of the Commission 2017 autumn forecast confirms the reading of the expenditure benchmark, namely a risk of significant deviation from the recommended structural adjustment path towards*

			the medium-term budgetary objective in 2018 as well as in 2017 and 2018 taken together." (p. 4)
	*"The Commission is also of the opinion that Belgium has made **some progress with regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 2017** in the context of the 2017 European Semester and invites the authorities to make further progress."* (p. 5)	<u>Debt rule</u>: *"On 22 May 2017, the Commission issued a report under Article 126(3) TFEU, as Belgium did not make sufficient progress towards compliance with the debt reduction benchmark in 2016. The report concluded that, after the assessment of all relevant factors**, the debt criterion should be considered as complied with.** (...) The Draft Budgetary Plan does not include sufficient information to assess compliance with the debt reduction benchmark. **Based on the Commission 2017 autumn forecast, the debt reduction benchmark is not projected to be met in 2017 and 2018.**"* (p. 3)	
<u>Italy</u>	*"Overall, and after considering the need to balance the two objectives of strengthening the ongoing recovery and ensuring fiscal sustainability, the Commission is of the opinion that the Draft Budgetary Plan of Italy, which is currently under the preventive arm and subject to the debt reduction benchmark, is **at risk of non- compliance with the provisions of the Stability and Growth Pact**. **The fiscal adjustment projected in the Commission 2017 autumn forecast for 2018 is not adequate** in light of the sustainability challenges that Italy faces."* (p.6)	*"Based on the Draft Budgetary Plan, **the expenditure benchmark points to a risk of significant deviation in 2017 both over one year (gap of 1.2% of GDP) and over two years (gap of 0.6% of GDP per year, on average).** (..) Overall, Italy's Draft Budgetary Plan plans a significant deviation from the required adjustment towards the MTO in 2017."* (p. 4) *"Based on the Commission 2017 autumn forecast, **the expenditure benchmark points to a risk of significant deviation in 2017 both over one year (gap of 0.9% of GDP) and over two years (gap of 0.4% of GDP per year, on average).** (...) the overall assessment points to a risk of significant deviation in 2017 based on the Commission 2017 autumn forecast."* (p. 4)	*"Based on the Draft Budgetary Plan, **the expenditure benchmark points to a risk of some deviation over one year (gap of 0.1% of GDP) and to a risk of significant deviation over two years (gap of 0.6% of GDP per year, on average).** (...) Overall, Italy's Draft Budgetary Plan plans a significant deviation from the required adjustment towards the MTO in 2018."* (p. 4-5) *"Based on the Commission 2017 autumn forecast, **the expenditure benchmark points to a risk of significant deviation in 2018 both over one year (gap of 0.5% of GDP) and over two years (gap of 0.7% of GDP per year, on average).** (...) the overall assessment points to a risk of significant deviation in 2018 (...)."* (p. 5)

	*"The Commission is also of the opinion that Italy has made **some progress with regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 2017** in the context of the 2017 European Semester and invites the authorities to make further progress."* (p. 6)	<u>Debt rule</u>: *"On 22 February 2017, the Commission issued a report under Article 126(3) TFEU as Italy had not made sufficient progress towards compliance with the debt criterion in 2015. The report concluded that the **debt reduction benchmark should be considered as not complied with at that stage, unless additional measures worth 0.2% of GDP were delivered**. Following the enactment of those measures, the Commission indicated that no further assessment of compliance with the debt criterion in 2015 would be needed, and a new assessment of compliance with the debt criterion in 2016 based on the Commission 2017 autumn forecast was announced."* (p. 4)	
Austria	*"Overall, while acknowledging the no-policy-change nature of its projections, the Commission is of the opinion that the Draft Budgetary Plan of Austria, which is currently under the preventive arm and subject to the debt reduction benchmark, is **at risk of non-compliance with the provisions of the Stability and Growth Pact**. The Commission invites the authorities to take the necessary measures within the national budgetary process to ensure that the 2018 budget will be compliant with the SGP."* (p. 4)	*"According to the information provided in the Draft Budgetary Plan, in 2017 **the expenditure benchmark points to a risk of some deviation from the applicable real reference rate of 1.1% (gap of 0.3% of GDP), while the (recalculated) structural balance points to compliance**. (...) Therefore, the overall assessment points to a risk of some deviation in 2017 and of significant deviation for 2016 and 2017 together."* (p. 3) *"This conclusion is **confirmed based on the Commission 2017 autumn forecast**, and would not change in case the additional budgetary impact of the inflow of refugees and the exceptional security measures in 2017 were excluded from the assessment."* (p. 3)	*"In 2018, based on the information provided in the Draft Budgetary Plan, **the expenditure benchmark points to a risk of significant deviation from the applicable nominal reference rate of 2.6% (gap of 0.7% of GDP), while the (recalculated) structural balance points to a risk of some deviation from the required adjustment of 0.1% of GDP (gap of 0.4% of GDP)**. (...) Therefore, the overall assessment points to a risk of significant deviation from the required adjustment in 2018."* (p. 3) *"Based on the Commission 2017 autumn forecast and applying similar arguments, the overall assessment points to **a risk of some deviation in 2018 and of significant deviation for 2017 and 2018 together**. This conclusion would not change in case the carry-over of the additional budgetary impact of the inflow of refugees and the exceptional security measures in 2017 were excluded from the assessment."* (p. 3)
	*"The Commission is also of the opinion that Belgium has made **some progress with regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 2017** in the*	<u>Debt rule:</u> *"The Draft Budgetary Plan does not include sufficient information to assess compliance with the debt reduction benchmark. Based on the Commission 2017 autumn forecast, the **debt reduction benchmark is projected to be met in 2017 and 2018**."* (p. 3)	

	context of the 2017 European Semester and invites the authorities to make further progress." (p. 4)		
Portugal	*"Overall and after considering the need to balance the two objectives of strengthening the ongoing recovery and ensuring fiscal sustainability, the Commission is of the opinion that the Draft Budgetary Plan of Portugal, which is currently under the preventive arm and subject to the transitional arrangements as regards compliance with the debt reduction benchmark, is* ***at risk of non-compliance with the provisions of the Stability and Growth Pact****."* (p. 5) *"In particular, the Commission projects* ***a risk of significant deviation from the required adjustment towards the MTO for both 2017 and 2018****. Therefore, the Commission invites the authorities to take the necessary measures within the national budgetary process to ensure that the 2018 budget will be compliant with the SGP."* (p. 5)	<u>Top down assessment</u>: *"For 2017, Portugal is required to pursue an annual structural adjustment towards the MTO of at least 0.6% of GDP.* ***While the expenditure benchmark points to a risk of significant deviation (gap of 1.0% of GDP), the structural balance points to a risk of some (but close to significant) deviation (gap of 0.5% of GDP).*** *Taking into account the negative impact of medium-term potential growth on the expenditure benchmark and the positive impact of revenue windfalls and lower interest costs on the structural balance, both indicators would point to a significant deviation. Based on the overall assessment, the planned structural adjustment in the DBP thus points to a risk of significant deviation from the recommended structural adjustment towards the MTO. This* ***risk of significant deviation for 2017 is confirmed by an overall assessment based on the Commission 2017 autumn forecast.****"* (p. 4)	<u>Top down assessment</u>: *"For 2018, the nominal growth rate of net primary government expenditure should not exceed 0.1 %, corresponding to a structural adjustment of at least 0.6 % of GDP.* ***While the expenditure benchmark again points to a risk of significant deviation (gap of 1.0% of GDP), the (recalculated) structural balance points to risk of some deviation (gap of 0.2% of GDP) from the recommended structural adjustment.*** *Taking into account the negative impact of medium-term potential growth assumptions on the expenditure benchmark, the positive impact of revenue windfalls and lower interest costs on the structural balance and the negative impact of the high planned increase in gross fixed capital formation on the structural balance, both indicators would point to a risk of significant deviation. Taking into consideration the above-mentioned effects, both indicators would point to a risk of significant deviation from the requirements over 2017 and 2018 taken together, suggesting that the 2017 deviations are not planned to be compensated for in 2018. Therefore, based on an overall assessment, the DBP plans a significant deviation from the recommended structural adjustment towards the MTO over 2017 and 2018 taken together."* (p.4) *"The Commission 2017 autumn forecast also points to* ***a risk of significant deviation from the recommended structural adjustment towards the MTO in 2018. Both the expenditure benchmark (gap of 1.3% of GDP) and***

			the structural balance (gap of 0.6% of GDP) point to a risk of significant deviation. *Also over 2017 and 2018 taken together, both indicators point to a risk of a significant deviation (average gap of 1.3% of GDP for the expenditure benchmark and 0.5% of GDP for the structural balance). Taking into consideration the above-mentioned elements, the risk of a significant deviation in both 2018 and over 2017 and 2018 taken together is confirmed based on. the Commission forecast."* (p. 4)
	"With regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 20173, ***limited progress appears to have been achieved in terms of increasing the scope of the expenditure review, which now also includes justice and internal affairs as well as more ambitious savings targets****." (p. 5)*	<u>Debt rule</u>: *"The Draft Budgetary Plan does not include sufficient information to assess compliance with the transitional arrangements to make sufficient progress towards compliance with the debt reduction benchmark. According to the Commission 2017 autumn forecast, Portugal is* ***projected to make sufficient progress towards compliance with the debt reduction benchmark in 2017 and 2018 as a result of the allowed annual deviation of 0.25% of GDP.*** *However, since Portugal would take advantage of the room for manoeuvre embedded in the rule, a stronger adjustment would have to be made in the remaining year of the transition period to ensure compliance with the benchmark at the end of the transition period."* (p. 4)	

Slovenia	*"Overall and after considering the need to balance the objectives of strengthening the ongoing recovery and of ensuring fiscal sustainability, the Commission is of the opinion that the Draft Budgetary Plan of Slovenia, which is currently under the preventive arm and subject to the transitional period to make sufficient progress towards compliance with the debt reduction benchmark, is **at risk of non-compliance with the provisions of the Stability and Growth Pact**. (...) Therefore, the Commission invites the authorities to take the necessary measures within the national budgetary process to ensure that the 2018 budget will be compliant with the SGP."* (p. 5)	*"In 2017, Slovenia was recommended to achieve a structural adjustment of 0.6 % of GDP. **The expenditure benchmark** pillar based on the Draft Budgetary Plan **indicates compliance. By contrast, the change in the (recalculated) structural balance planned in the Draft Budgetary Plan points to a risk of a significant deviation, both over one year (deviation of 0.6 % of GDP) and two years (average annual deviation of 0.4 % of GDP).** (...) Therefore, the Draft Budgetary Plan submitted by Slovenia is assessed to plan compliance with the requirements of the preventive arm in 2017."* (p. 3) *"According to the Commission autumn forecast, **both the structural balance and the expenditure benchmark point to a risk of a significant deviation** in 2017 (gap of 0.7% of GDP and 0.6% of GDP respectively)."* (p. 3)	*"**The expenditure benchmark based on the Draft Budgetary Plan points to a risk of some deviation over 2018 (gap of 0.4 % of GDP) and over 2017 and 2018 taken together (average annual deviation of 0.2 % of GDP). At the same time, the (recalculated) structural balance planned in the Draft Budgetary Plan points to a risk of a significant deviation, both in 2018 (gap of 0.5 % of GDP) and over 2017 and 2018 together (gap of 0.6 % of GDP).** (...) Therefore, the Draft Budgetary Plan is assessed to plan a risk of some deviation from the requirements of the preventive arm in 2018."* (p. 3-4) *"According to the Commission's autumn forecast, **both pillars point to a risk of a significant deviation** (gap of 1.2% and 1.0% of GDP based on the expenditure benchmark and the structural balance respectively). An overall assessment confirms the conclusion of a risk of significant deviation."* (p. 4)
	*"The Commission is also of the opinion that Slovenia has made **some progress with regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 2017** in the context of the 2017 European Semester and thus invites the authorities to make further progress."* (p. 5)	<u>Debt rule:</u> *"The Draft Budgetary Plan does not include sufficient information to assess compliance with the transitional arrangements regarding the debt reduction benchmark. On the basis of the Commission 2017 autumn forecast, Slovenia is **projected to make sufficient progress towards compliance with the debt reduction benchmark in 2017 and 2018**. "* (p. 3)	

Annex 2: Fiscal sustainability assessments and selected indicators

Table: Fiscal Sustainability Indicators 2017

	BE	DE	EE	IE	ES	FR	IT	CY	LV	LT	LU	MT	NL	AT	PT	SI	SK	FI
Overall SHORT-TERM risk category[1]	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW	LOW
Overall MEDIUM-TERM risk category[2]	HIGH	LOW	LOW	LOW	HIGH	HIGH	HIGH	MEDIUM	LOW	MEDIUM	LOW	LOW	LOW	MEDIUM	HIGH	MEDIUM	LOW	HIGH

Source: Communication from the Commission, [2018 Draft Budgetary Plans: Overall Assessment](), November 2017.

Notes: (1) The short-term risk category indicator highlights risks of fiscal stress in the upcoming year and is based on two sub-indicators, the fiscal and the financial-competitiveness index; (2) the medium-term risk category indicator highlights risks of medium-term debt sustainability and is based on the joint measure of debt projections over 10-years and cumulated adjustments in the structural primary balance over 5 years needed to reach the target of a 60% debt-to-GDP ratio by 2030.

Table: General Government Gross Debt and Interest Expenditure in 2007 and 2016 and Expected Gross Financing Needs in 2017, as % of GDP

Member State	Debt/GDP[1]			Interest Expenditure/GDP[2]			Expected GFN/GDP[3]
	2007	2016	Variation	2007	2016	Variation	2017
EL	103.1	180.8	+77.7	4.5	3.2	-1.3	n.a.
ES	35.6	99.0	+63.4	1.6	2.8	+1.2	17.8
PT	68.4	130.1	+61.7	2.9	4.2	+1.3	12.0
SI	22.8	78.5	+55.7	1.2	3.0	+1.8	8.1
CY	53.5	107.1	+53.6	2.8	2.6	-0.2	n.a.
IE	23.9	72.8	+48.9	1.0	2.2	+1.2	5.8
LV	8.0	40.6	+32.6	0.4	1.0	+0.6	n.a.
FR	64.3	96.5	+32.2	2.6	1.9	-0.7	13.2
IT	99.8	132.0	+32.2	4.8	4.0	-0.8	16.5
FI	34.0	63.1	+29.1	1.4	1.1	-0.3	7.8
LT	15.9	40.1	+24.2	0.7	1.3	+0.6	5.6
EA19	64.9	88.9	+24.0	2.9	2.2	-0.7	n.a.
SK	30.1	51.8	+21.7	1.4	1.6	+0.2	9.2
NL	42.7	61.8	+19.1	2.0	1.1	-0.9	5.6
AT	64.7	83.6	+18.9	3.1	2.1	-1.0	4.9
BE	87.0	105.7	+18.7	4.0	2.9	-1.1	17.5
LU	7.7	20.8	+13.1	0.3	0.3	+0.0	n.a.
EE	3.7	9.4	+5.7	0.2	0.1	-0.1	n.a.
DE	63.7	68.1	+4.4	2.7	1.3	-1.4	2.7
MT	62.3	57.6	-4.7	3.5	2.2	-1.3	6.4

Sources: Eurostat and IMF staff estimates and projections.

Notes: (1) General Government Consolidated Gross Debt, code GD, Eurostat; (2) Interest payable, code D41, Eurostat; (3) Gross financing needs are defined as the projected overall deficit and maturing government debt in 2017; for more details on the assumptions, see note 1 in Table A23 of the IMF's April 2017 Fiscal Monitor.