Annual assessment of implementation of stability and convergence programmes

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In the context of the cycle of reviewing Member States' updated stability and convergence programmes, the Council examined a third package of stability programmes, relating to Luxembourg and Portugal. - LUXEMBOURG : as regards the Council's opinion on the updated stability programme of Luxembourg (2001-2005) : the programme does not fully comply with the requirements of the Code of Conduct on the content and format of the programmes endorsed by the ECOFIN Council on 10 July 2001; in particular it has been transmitted with a six-week delay. The programme partly conforms with the recommendations of the BEPGs. The Council notes that government finances deteriorated markedly in 2002 as revenues decelerated in response to the combined impact of the tax reform and the economic slowdown, while expenditure growth remained very strong. Consequently, the general government budget balance is expected to show a deficit of 0,3% of GDP in 2002, a sharp deterioration compared to the large surplus of 6,1% of GDP in 2001. The general government balance is projected to remain in deficit by 0,3% of GDP in 2003, to deteriorate slightly further in 2004 to a deficit of 0,7% of GDP, and to reach a position close to balance in 2005, with a slight nominal deficit of 0,1% of GDP. The underlying general government balance is expected to remain positive over the horizon covered by the stability programme. Consequently, the Council considers that Luxembourg continues to be in conformity with the requirement of the stability and growth pact to reach a budgetary position of close to balance or in surplus in the medium term. The Council notes that sound management of public finances continues to be the guiding principle of the 2002 update. In addition, the Council welcomes the main elements of the budgetary framework currently in place, which inter alia encompasses the use of cautious macro-economic projections as the basis for budgetary policy, as well as the principle to let net public sector lending be positive, to achieve a balanced budget for central government, and not to let the rise in current expenditure exceed the growth of total expenditure. The Council welcomes the reduction of the tax burden through the implementation of tax reform while aiming for a sound budgetary position in the medium term. In this context it encourages a future government to adhere to real expenditure ceilings that are compatible with achieving a budgetary position close to balance or in surplus in the medium term. However, the Council expresses some concern over the rapid deterioration of the budget balance of the central government, which only accounts for part of the general government sector. The balance of central government was still in surplus by 2,6% of GDP in 2001 but is projected to register a deficit of 2,2% of GDP in 2002 and of 2,1% of GDP in 2003, while the central government deficit is expected to deteriorate further to 2,8% of GDP in 2004 and 2005. The Council notes that this is partly due to revenue shortfalls in response to the economic slowdown, while central government expenditure is projected to increase rapidly; although the starting position of public finances in Luxembourg is extremely sound, a continued fast increase of current expenditure might become a factor of risk should economic growth in the medium term slow significantly. On the basis of current policies, the Council considers that public finances in Luxembourg are in a good position to meet the projected costs of an ageing population. However, the Council notes that the assessment of the sustainability of public finances in Luxembourg is very sensitive to developments as regards the number of cross-border workers. - PORTUGAL : as regards the Council's opinion on the updated stability programme of Portugal 2003-2006) : the updated programme projects general government finances to improve steadily, from a deficit of 2.8% of GDP in 2002 to a deficit of 0.5% of GDP in 2006. Government gross debt is expected to decrease from 58.8% of GDP in 2002 to 52.7% in 2006. The Council notes that the updated programme broadly complies with the requirements of the revised code of conduct on the content and format of stability and converge programmes. The updated programme was adopted by the government on 20 December and presented to parliament, which discussed it and adopted early in January a declaration of approval by a large majority, including the support of the main opposition party. The updated programme was then formally submitted to the Commission. The Portuguese authorities have thus effectively kept the commitment made to the Council

on 5 November, in the framework of the recommendation under Article 104(7), to present before the end of the year an updated stability programme. The Council considers that the economic policies as reflected in the planned measures in the programme update broadly comply with the 2002 Broad Economic Policy Guidelines. On 5 November 2002, in the light of a government deficit of 4.1% of GDP in 2001, the Council decided that an excessive deficit existed in Portugal and issued a recommendation to Portugal according to Article 104(7) of the Treaty. In the terms of this recommendation, the Portuguese authorities were urged to implement with resolve their budgetary plans for 2002 which aim at reducing the deficit to 2.8% of GDP in that year. The Council established a deadline of 31 December 2002 for the Portuguese government to take all necessary measures to bring the excessive deficit to an end; adopt and implement the necessary budgetary measures to ensure that the government deficit in 2003 is further reduced clearly below 3% of GDP and that the government debt ratio is kept below the 60% of GDP reference value. The Council notes with satisfaction that, according to preliminary figures, the general government deficit has been reduced below 3% of GDP in 2002, in spite of weaker-than-anticipated growth. The Council acknowledges the firm resolve of the Portuguese government in pursuing budgetary consolidation. Budgetary developments in the further course of 2002 turned out less favourable than expected in the rectifying budget adopted in June, mainly due to the further weakening in economic activity, but also to lower-than-expected proceeds from sales of government property. As a consequence, and with a view to reducing the deficit as recommended by the Council, the Portuguese authorities adopted a number of one-off measures at the end of the year, which in total are estimated to have raised additional revenue of about 1.5% of GDP. The Council notes that substantial challenges remain in 2003 to achieve the deficit target of 2.4% of GDP and to put the deficit on a downward trajectory. The Council therefore urges the Portuguese authorities to ensure that the deficit remains well below 3% of GDP in 2003. The Council welcomes the Portuguese authorities intentions to bring the debt level down to 52.7% of GDP by 2006, unwinding the sharp deterioration registered between 2000 and 2002. On the basis of current policies, the risk of unsustainable public finances in the light of ageing populations cannot be excluded. If debt reduction is to make a noticeable contribution towards meeting the budgetary cost of ageing populations, then reaching a balanced position by 2006 is essential.