

Press conference held by Pedro Solbes on the excessive deficit in Portugal (Brussels, 16 October 2002)

Caption: On 16 October 2002, in an opinion to the Council, the European Commission concludes that an excessive deficit exists in Portugal and recommends that the Council take a decision in this area. During a press conference, Pedro Solbes, Member of the European Commission with special responsibility for Economic and Monetary Affairs, outlines the aims of the procedure and the scale of the efforts to be undertaken to resolve the problems.

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Excessive Deficit in Portugal — Commission Opinion and Recommendations to the Council

Press Conference

Brussels, 16 October 2002

Good morning,

The Commission today took important decisions in the framework of the excessive deficit procedure for Portugal. In our Opinion to the Council we conclude that an excessive deficit exists in Portugal.

The general government deficit in 2001 amounted to 4.1% of GDP, thereby clearly exceeding the reference value of 3% of GDP. Moreover, government debt, rose in 2001 to 55.5% of GDP, albeit still below the 60% reference value. These figures were confirmed in Portugal's submission by 1 September under the semi-annual reporting of government deficits and debt levels.

As I commented last July, the revision of the Portuguese government accounts revealed that there are **significant deficiencies in the Portuguese statistical services, which I urge the Portuguese government to address** with resolve and urgency.

From 1999 to 2001, according to the revised data, the government deficit increased from 2.4% to 4.1% of GDP. While economic growth slowed markedly during that period, **the increase in the deficit mainly reflects a weakening in the underlying budgetary position**. The cyclically-adjusted deficit has widened nearly as much as the actual deficit. Obviously, the rectifying budget adopted by the Portuguese government in June 2001, involving cuts in expenditure to the amount of 0.6% of GDP, was not enough to keep the deficit under control.

It can therefore be concluded that the deficit in 2001 did not result from an unusual event outside the control of Portugal, nor did it result from a severe economic downturn.

We also analysed developments in 2002. The new government adopted supplementary budget consolidation measures late last spring with a view to bring the budget deficit to 2.8% of GDP in 2002. They are also ready to adopt additional saving measures this year, if needed, in order to honor this target.

This is a very positive development and I do hope that the expected results are reached. In our opinion, **in the absence of the rectifying budget, the 2002 deficit could have been above 3½% of GDP**.

However, **at this stage**, while it is clear that the deficit would be substantially reduced, **it is not yet possible to assess whether the deficit would stay below the 3% of GDP reference value in 2002**.

On the basis of Article 104.6 of the Stability and Growth Pact we recommend therefore to the Council to decide that an excessive deficit exists in Portugal.

Finally, the Commission recommends to the Council to issue a recommendation to Portugal in the sense of Article 104.7 of the Treaty. In the Commission's view, Ecofin should recommend to the Portuguese government to put an end to the present excessive deficit situation as rapidly as possible and by 2003 at the latest. The government debt ratio should also be kept below the 60% of GDP reference value. The Portuguese authorities should implement with resolve all saving measures announced. My first impression is that **the Portuguese government 2003 budget proposal is also a step in the right direction and should be implemented with vigour**. But of course what counts for the Commission are the final results.

The Portuguese authorities shall therefore present before the end of the year an updated stability programme

covering 2003 and the years **beyond including ambitious budgetary targets for the achievement of the medium term budgetary position of close to balance or in surplus**. They should also secure that the debt ratio is brought back to a declining path.

Finally, given that Portugal took already prompt action in May to reduce the excessive deficit **the Commission today did not recommend the suspension of the cohesion fund to Portugal**.

Although today's Commission decision only concerns Portugal, I would like to place it in the broader picture regarding the budgetary situation of the euro area. Besides Portugal, the budgetary situation is crucial in France, Germany and Italy. Deficits in these countries are dangerously close if not above the 3.0% threshold. The adjustment required by these countries in order to reach the close to balance position is substantial. And I know it is painful. But our history teaches us that **any alternative is dangerous for the stability of our economies and our currency the euro**.

I also know that growth is slower than expected and substantial risks remain on the horizon. Against this background, the Commission presented at the end of September a pragmatic strategy on how to deal with the budgetary consolidation challenge.

The 3.0% of GDP deficit threshold is and should remain a binding constraint. **Any breaching of this threshold requires swift and corrective action by the member states concerned**.

On the other hand, in the monitoring of the path to the close to balance position **we should pay increasing attention to the cyclically adjusted budgetary positions**, i.e. the underlying budget deficit position excluding the effects of the economic cycle. We have now a common methodology in the Union on how to calculate cyclically adjusted budget deficits and we should put it to good use. I am very satisfied that Eurogroup Ministers last week in Luxembourg took a similar view and agreed with our proposal that countries still in deficit should achieve as a minimum a 0.5% of GDP per annum reduction in their underlying budgetary position until they reach a close to balance position.

All countries with deficit positions have accepted this approach and with the exception of France are striving to implement it as of 2003. Of course the Commission will have to analyse in detail the 2003 budgets and new stability programmes. We will have to **analyse both the pace and the quality** of the budgetary adjustment effort. We will also have to **ensure that such efforts are consistent with the growth stimulating structural reforms that are necessary for the European economy**.

I believe that we have critical months ahead of us but it would only be possible to solve current problems if we work within the letter and the spirit of our EMU framework. Budgetary policies are national but subject to a necessary degree of coordination. This approach is essential to ensure an appropriate policy mix for the euro area.

Let me finally add that **the procedures for preventing and correcting excessive deficits must be implemented in a strict and timely manner**. This is what the Commission has done today for Portugal and what we will do if necessary in the case of other member states. It is important for preserving sound public finances in the EU and the credibility of the fiscal policy coordination framework. This is the Commission's clear position and **I am happy that Eurogroup ministers came to the same conclusion in Luxembourg last week**.