

## FOCUS · Fiscal adjustment in the periphery: a never-ending story

In spite of the efforts made over the last few years, the peripheral countries have yet to complete their fiscal adjustment. Nevertheless, some figures indicate that the consolidation is well advanced. Now that these countries can benefit from some tailwinds and are no longer the main focus of attention of the markets, we will examine whether the policies announced for 2017 are appropriate or whether, conversely, fiscal policy has been relaxed in the absence of such market pressure.

When analysing the planned public deficit reduction in the periphery, several figures stand out: both the pace of adjustment and the level reached should be viewed positively. In 2017, the peripheral governments expect to reduce their public deficit by an average of 0.8 pps of GDP, a similar rate to that observed over the last few years. And, if these forecasts are met, the primary surplus in the periphery will increase to 0.9% of GDP (from 0.4% in 2014). Moreover, public debt will fall slightly, from 119.9% of GDP in 2016 to 119.3% in 2017.

However, we need to consider the expected economic context and examine both the composition and credibility of the planned adjustment in order to analyse it thoroughly.

When the expected environment for fiscal adjustment is taken into account, we can see that this will largely occur thanks to economic growth.<sup>1</sup> Consequently, in Ireland and also in Portugal and Spain the respective governments forecast that fiscal policy will practically be neutral. In Italy, however, the government plans to implement an expansionary fiscal policy and reduce its primary structural surplus by 0.8 pps.

This positive view is further compromised when we look at the composition of the announced adjustment. On the expenditure side, the aim is still to improve public administration efficiency, albeit differently depending on the country and measure used. However, this has been a recurring proposal over the last few years, and its success has been limited. On the revenue side, part of the increase in tax receipts is expected to come from a reduction in the size of the informal economy (also a recurring strategy in the last few years and which, with the odd exception, has had limited success).

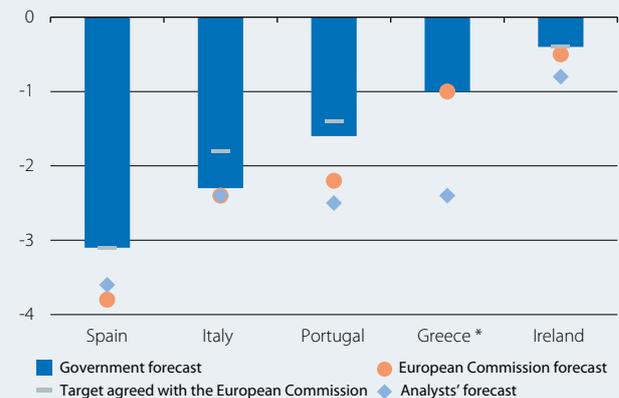
Various analysts believe that the deficit reductions announced by the peripheral governments are not entirely realistic. First of all, it is notable that, in several countries, the budgets presented propose a deficit target that is higher than the target agreed with Brussels.

1. The expected reduction in financial costs is also notable and especially due to the ECB's accommodative monetary policy.

Moreover, analysts forecast an even greater deviation from target, and expect fiscal policy in the periphery to be slightly accommodative in 2017.

### Fiscal balance

(% of GDP)



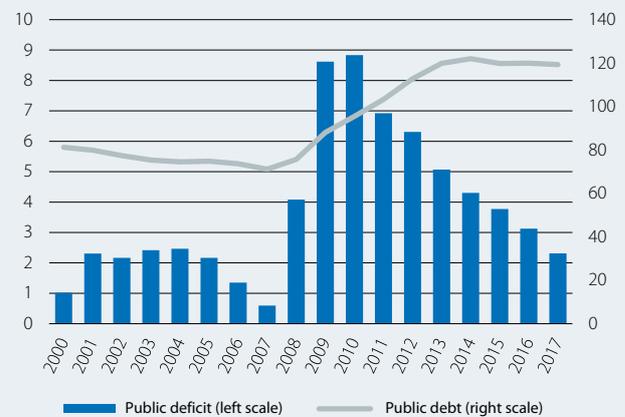
Note: \* Greece's target is not available as the agreement relates to the primary balance.

Source: CaixaBank Research, based on data from the European Commission and Bloomberg.

### Public deficit and public debt in the periphery

(% of GDP)

(% of GDP)



Source: CaixaBank Research, based on European Commission data.