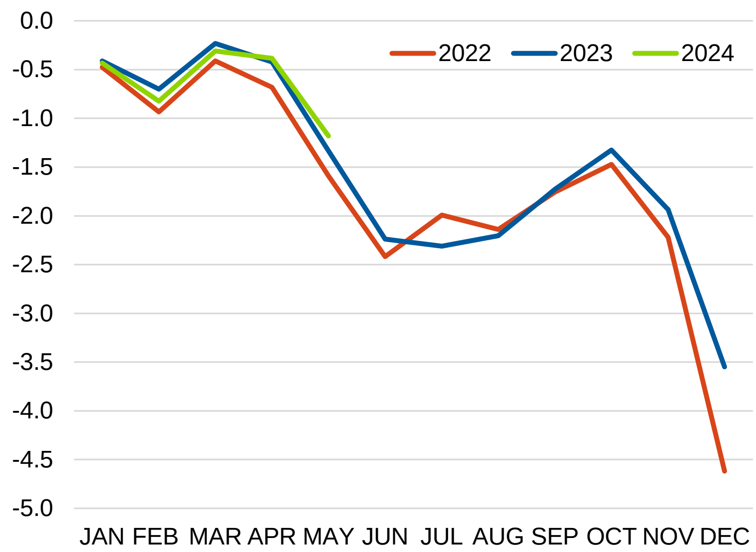
The upward revision of out GDP forecast for 2024 also has a positive effect on our deficit forecasts, which now stand at 2.9% in 2024 and 2.5% in 2025.

To May, the overall deficit stood at 1.2% of GDP.

Today the Ministry of Finance published new budget outturn data for all levels of government, except for the local administrations, to May, with preliminary figures at the state level to June. The **highlights** are:

1. To **May, the overall public deficit**, excluding local government, had fallen to €18.29 billion. In terms of GDP, it stood at **1.2% (down 0.1pp from the same period of 2023)**.

Exhibit 1. Trend in deficit (all levels of govt. except local), % of GDP



Source: Ministry of Finance and Government

Deficit by level of government (% of GDP)

Preliminary data as of June 24

	may-24	jun-24
Central Gov.	**-0.5**	
State	*-0.6*	*-1.2*
Regional Gov	**-0.7**	
Social Secur.	**0.0**	
Total	**-1.2**	

Source: IGAE

2. **The state, up until June, generated a deficit of 1.2% of GDP, down half a point from the 1H23 deficit.** This performance is due to dynamic collections coupled with controlled spending, yet to be affected by the significant outflow due in July under the regional finance system or the updated amounts of the payments on account due in September.

3. **To May, the regional governments' deficit was running 40.6% higher year-on-year at €10.45 billion (0.67% of GDP).** This deterioration is attributable to the limited growth in non-financial income (+2.9% YoY), due to the pushback until September of the updates to the payments on account, mentioned above, coupled with growth in spending of 5.9% YoY. The spending items that are hurting the regional accounts are interest (+26.3% YoY), investment (+14.5% YoY) and employee compensation (+5.4% YoY). By region, besides the Basque region and Navarre, only Catalonia and Valencia have improved from last year, albeit affected by the award of financing system advances.

4. The **Social Security Funds continue to present a balanced budget**, compared to a slight deficit of 0.1pp as of May 2024. The fact that Social Security contributions are increasing at 7.8% YoY and transfers from the state are accelerating is absorbing the growth in non-financial spending (+7.0% YoY), which is coming under pressure mainly from pensions (+6.9% YoY).

Deficit by region (% of GDP)

	May 2023	May 2024	YoY (pp.)
AND	-0.3	-0.9	-0.60
ARA	-0.2	-0.6	-0.35
AST	0.2	-0.2	-0.41
BAL	-1.4	-1.9	-0.48
CAN	-0.3	-0.9	-0.57
CNT	-0.2	-0.8	-0.55
CLM	-0.7	-0.9	-0.12
CYL	-0.3	-0.5	-0.14
CAT	-0.6	-0.6	0.07
EXT	-0.9	-1.1	-0.17
GAL	-0.4	-0.7	-0.33
MAD	-0.5	-0.6	-0.14
MUR	-1.0	-1.4	-0.34
NAV	-0.8	-0.6	0.20
RIO	-0.3	-0.9	-0.63
VAL	-0.9	-0.9	0.05
PVO	0.0	0.4	0.41
TOTAL	**-0.5**	**-0.7**	**-0.16**

Source: Ministry of Finance and Government

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State budget outturn to June 2024

Growth in tax revenue is accelerating, ending the first half at 8% YoY.

The public revenue figures to June **extend the trend of recent months,** ending the first half **8% higher YoY on a like-for-like** basis. Although the growth in personal income tax receipts stands out, **unlike in 2023, the indirect taxes are also making a significant contribution**, thanks to the gradual removal of the tax relief on VAT and other electricity taxes.

Table 1. Trend in revenue by tax on a like-for-like basis (incl. regional governments' share)

	JUN. 2023	JUN. 2024	*YoY 24/23*	DEC. 2023	YoY 23/22
Direct taxes	**62,101**	**68,384**	***10.1%***	**161,406**	***15.3%***
Personal income tax	***51,043***	***55,854***	***9.4%***	***120,691***	***16.0%***
Corporate income tax	9,266	10,271	*10.8%*	36,304	*13.9%*
Other taxes	1,792	2,259	*26.1%*	4,411	*4.9%*
Indirect taxes	**56,388**	**59,573**	***5.6%***	**111,732**	***14.5%***
VAT	***43,313***	***45,968***	***6.1%***	***84,816***	***17.1%***
Special taxes	10,212	10,715	*4.9%*	21,258	*2.5%*
Other taxes	2,863	2,890	*0.9%*	5,658	*27.0%*
TOTAL TAX REVENUE	**118,488**	**127,957**	***8.0%***	**273,137**	***14.9%***

Source: IGAE

Personal income tax remains the main growth driver but…

- **Personal income tax:** There were no major developments in June with respect to the factors propping up the sharp growth in receipts from this tax: job creation, which while easing is still making a positive contribution; wage increases; and the increase in the effective rate.
- **Corporate income tax:** Here the healthy trend continues and is unlikely to change until August, which is when the increase in annual returns is accounted for.
- **VAT:** Like-for-like VAT receipts registered year-on-year growth of 6.1% in 1H24 thanks to the elimination of temporary measures, in line with the growth in expenditure on the taxed items.

…growth in VAT receipts is accelerating thanks to the elimination of the temporary relief measures

Meanwhile, growth in non-financial expenditure remains stable at moderate levels (+1.5% YoY). The headings coming under the greatest pressure are interest (+12.9%), employee compensation (+3.2%) and sundry current transfers (+37.9%).

Growth in non-financial expenditure remains stagnant at 1.5% YoY.

Come July, we expect an uptick in inter-governmental transfers following recognition for accounting purposes of the outflow of funds associated with the regional financing system settlements for 2022[1]. By the end of the first half, the regional governments had been transferred 3% more than in 2023, **which is still well below the forecast increase of 8.3%**. Elsewhere, the Social Security Funds have received 9.6% more funding than in 1H23, with the Social Security System the main beneficiary.

Deficit forecasts for 2024 and 2025: upward revision of growth forecast and presentation (uncertain) of the new stability targets and roadmap

The upward revision of the nominal growth forecast leads us to likewise improve our deficit forecast for 2024 to 2.9% of GDP.

Regarding the 2024 deficit, we are improving our forecast for the full year by 0.2pp to **2.9% of GDP**, albeit with different patterns in the various subsectors. The key reasons for this improvement are:

- **Upward revision of our nominal growth forecast for 2024 to 5.9% YoY** (from 5.5% YoY) and, due to a base effect, to 5% YoY in 2025 (from 4.9% YoY). (The improved growth forecasts are shaped by the **real growth component**, in turn influenced by: i) the statistical revision of the historical series by Spain's statistics office (INE); ii) a surprisingly strong 2Q24, when

[1] Over €20 billion contemplated for the regional governments with a negative impact on state revenue and a positive impact on spending.

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foreign demand was the main growth engine; and iii) an improved outlook for the rest of 2024, underpinned by household consumption and a rebound in investment (see our **economic report** here). The expected improvement in economic activity has a positive knock-on effect on forecast public revenue, via both tax receipts (impact at the state level) and Social Security contributions (impact on the Social Security administration), which together improve the forecast deficit by 0.3pp.

- **Risk of faster growth in spending at the regional level**. The budgeted growth in regional spending in 2024 (5% YoY) compared to the budget outturn observed in the first five months of the year (+5.9% YoY in non-financial expenditure) leads us to revise our forecast for regional spending growth 0.1pp higher to 0.2% of GDP.

The positive outlook on the macro front should underpin ongoing momentum in collection dynamics. Contained spending is expected to unlock a significant improvement in the central government deficit to 1.9% of GDP.

As for our **deficit estimate for 2025**, the key considerations at the various levels of government (assuming that the recent failure to approve deficit targets could delay approval of the budget for 2025):

- **Central govt**.: the ongoing momentum in economic growth underpinned by internal demand, thanks to household consumption (recovery in purchasing power and still-high stock of savings), foreshadows **continued positive dynamics in tax collection of around 5.4% YoY (versus 6.5% in 2024)**. This trend is in line with the growth forecast and also factors in the withdrawal of the measures associated with the war in Ukraine, the impact of which is bigger in 2024 than in 2025. On the **spending side, the contribution to the deficit compared to 2024 is small**. The reasons are: 1) growth in non-financial spending in line with forecast inflation (2.1%) in the components exposed to inflation, such as wages and consumption; 2) more moderate growth in funds under the regional financing system (payments on account and system settlements) than the year before (€3.7 billion at the regional govt. level and €378m at the local govt. level; 3) full withdrawal of the anti-crisis measures. As a result, our forecast for the **central govt. deficit is now 1.9% of GDP** (compared to the government's forecast of 2.2%), marking a reduction of 0.6pp relative to year-end 2024).

The restatement of certain spending items such as wages will absorb the positive contribution from the regional financing system.

- **Regional govt**.: the growth in regional financing system funds improves the forecast deficit by 0.2pp. However, the restatement of wages in line with CPI will add to the deficit by the same amount. This, coupled with the trend in spending as a whole and the difficulties facing the regions in drawing up their budgets for 2025 in the current climate of uncertainty, leads us to forecast a **deficit across the regional governments as a whole of around 0.2% of GDP in 2025** (versus the government's forecast of 0.1%).
- **Local govt**.: **we are forecasting budget equilibrium for 2025** as spending picks up, in line with the government's forecasts.

The resilience of the labour market should translate into ongoing growth in contributions. However, pressure on spending via pensions will make it hard to contain the Social Security deficit.

- **Social Security**: we are expecting the labour market to remain strong, unlocking growth in contributions of 6.1% YoY (versus 7% YoY in 2024), including the upward revision of 0.1pp in the 'Intergenerational Equity Mechanism' to 0.8% in 2025 (0.7% in 2024). On the pension front, we are estimating similar growth due to the trend in the number of contributors and pensioners, coupled with the restatement of pensions for CPI (+2.1%). Leaving all other assumptions unchanged, the **Social Security deficit is expected to come in in line with the 2024 estimate, at around 0.3% of GDP**.

As a result, our forecast for the deficit in 2025, at all levels of government, is now around 2.4%, in line with the government's new targets and roadmap.

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Table 2. Public deficit forecasts. % of GDP

	2023	2024			2025		
		Afi	AIReF	Govern.	Afi	AIReF	Govern.
Central	-2.1	-2.5	-2.5	-3.0	-2.1	-2.2	-2.2
Regional	-0.9	-0.2	-0.3	0.0	-0.2	-0.3	-0.1
Local	-0.1	0.1	0.1	0.2	0.0	0.0	0.0
Social Sec.	-0.6	-0.3	-0.3	-0.2	-0.3	-0.4	-0.2
TOTAL	**-3.7**	**-2.9**	**-3.0**	**-3.0**	**-2.5**	**-2.9**	**-2.5**

Source: Afi, AiREF, Ministry of Finance, IGAE

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