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Madrid presses EU to ease deficit targets

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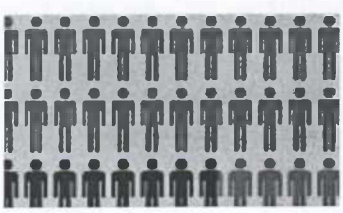
By Victor Mallet in Madrid and Peter Spiegel in Brussels

Mariano Rajoy

Spain is pressing the European Commission to ease the country's strict budget deficit target for this year, arguing that the European Union executive's own pessimism about the Spanish economy shows the potential risks of too much austerity.

Thursday's release of the EU's revised economic forecasts contained troubling news for the entire eurozone, which is now projected to shrink by 0.3 per cent this year. Its autumn forecast had predicted modest growth of 0.5 per cent.

Spain's economy is projected to contract 1 per cent, compared with forecasts of 0.7 per cent growth just three months ago. Only Estonia suffered larger downward revisions.



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Advisers to Mariano Rajoy, the centre-right Spanish prime minister elected in November, are asking the commission to accept that a contracting economy makes a target agreed by the previous government of limiting the national budget deficit to 4.4 per cent of gross domestic product this year unrealistic and even counterproductive. They want a new target above 5 per cent of GDP. "There are conversations under way," said one Madrid official.

"This year will be a hard year for Spain and we must all be aware of this," Mr Rajoy said on a trip to Rome. "Serious governments cannot think about the short term, but about the medium- and long-term to create employment."

The EU's revised forecast of 1 per cent shrinkage is more optimistic than the predictions of other organisations and of Spain itself, and the EU admitted that further austerity measures could darken the picture.

The previous Spanish government of José Luis Rodríguez Zapatero, Socialist prime minister, had agreed with its European partners to cut the national budget deficit to 6 per cent of GDP in 2011. But Mr Rajoy has disclosed figures showing that the 2011 deficit in fact exceeded 8 per cent of GDP.

Mr Rajoy's push to renegotiate deficit targets puts Olli Rehn, the European commissioner in charge of economic issues, in an awkward position.

EU rules give Mr Rehn leeway in assessing whether fines should be imposed on countries missing agreed targets, but only in the case of unforeseen economic circumstances – not a change in government.

Indeed, last month Mr Rehn ordered the Belgian government to cut €1.2bn to €2bn from its 2012 budget or face severe fines, even though it had only been in office for four weeks.

European Commission officials have indicated Mr Rehn is likely to send a similar letter to Mr Rajoy after the Spanish government presents its delayed 2012 budget next month, but on Thursday Mr Rehn would only say that he would review the new budget figures once they are provided by Madrid in March and validated by the EU's statistical agency in April.

"We will work with the Spanish authorities and decisions will be taken once we have a full picture," Mr Rehn said. "I expect the Spanish authorities to share all relevant information."

Additional reporting by Giulia Segreti in Rome