

## **Public Finance Assessment of the 2025 draft budget (“2025 DB”) and the draft multiannual financial programming law for the years 2024-2028 (“2024-2028 PLPFP”)**

### **Autumn 2024**

The National Council of Public Finances (CNFP) notes that the structural balance is in line with the medium-term budgetary objective (MTO) of 0.00% of gross domestic product (GDP) over the period 2024 to 2028.

The macroeconomic forecasts underlying the 2024-2028 PLPFP anticipate an improvement of Luxembourg's economic environment in the short term. After a contraction in activity of -1.1% in 2023, real GDP is expected to grow by 1.5% in 2024 and 2.7% in 2025, before slowing down to 2.0% in 2026. Regarding the labor market, employment growth is expected to grow at a historically low rate (0.9% in 2024 and around 1.5% in 2025-2026) and the unemployment rate is expected to rise and stabilize at around 6.0% over the years 2024 to 2026. Inflation should continue to ease in 2024 (2.3%), but a temporary rebound in inflation is expected in 2025 (2.6%) following the removal of the majority of the energy price cap measures (scheduled for December 31, 2024).

Despite a downward revision of the average economic forecasts compared to the 2023-2027 LPFP (March 2024) and additional measures taken by the Government, the central government balance forecasts in the 2024-2028 PLPFP (-1 421 million euros in 2024, -1 288 million euros in 2025, -1 083 million euros in 2026, -685 million euros in 2027 and -667 million euros in 2028) are considerably more favorable than anticipated in March. This equals an average annual improvement of 493 million euros over the 2024-2027 period, compared with the 2023-2027 LPFP. This confirms the result of the Assessment of the accuracy of forecast of macroeconomic and budgetary data published by the CNFP in May 2023, which revealed a significant systematic underestimation of budget forecasts.

Despite the upward revision, the CNFP still considers the central government balance forecasts as cautious. In fact, according to the State's financial position, presented in early October, the central government balance is -706 million euros on September 30<sup>th</sup>, 2023 and +471 million euros on September 30<sup>th</sup>, 2024, amounting to an improvement of 1 177 million euros. In the 2024-2028 PLPFP, however, the Government forecasts an equivalent balance for the two years (of respectively -1 462 and -1 421 million euros). This points to an underestimation of the balance for 2024, and probably also for subsequent years, especially as the average revenue growth rate forecast for the 2026-2028 period (5.3%) is lower than the historical growth rate (6.4%). On the other hand, it should be noted that the average expenditure growth rate forecast for the 2026-2028 period (4.4%) is also lower than the historical growth rate (6.7%), which would require saving efforts on the current expenditure side.

Even if central government balances are likely to be underestimated, the surpluses (positive balances) recorded in the years prior to 2020 at general government level (comprising the three sub-sectors: central government, local government, and social security) would no longer be reached. This is attributable to the persistence of expenditure growth rates exceeding revenue growth rates in the social security sub-sector. The social security balance is forecast to move from a surplus (+937 million euros in 2024) to a deficit (-15 million euros in 2028). The question that then arises is what potential the State has for increasing its resources in the event of future economic and geopolitical shocks.

In the context of the reformed European budgetary governance framework of April 29<sup>th</sup>, 2024, the Government submitted its first medium-term national structural budget plan to the European Commission in mid-October 2024. The CNFP has only briefly addressed this plan in the present assessment. It will come back to it in a later assessment, but already notes that Luxembourg is not concerned by a large part of the preventive arm as long as it complies with the Maastricht criteria. The

CNFP points out that, with a view to the transposition into national law of Directive (EU) 2024/1265 amending Directive 2011/85/EU on requirements for budgetary frameworks of the Member States (deadline: 31.12.2025), the reformed national framework could usefully adopt a medium- and long-term view and be adapted to the state of Luxembourg's public finances and the country's current and future challenges (aging population, housing, energy and digital transition, mobility, defense, etc.).