Draft Budgetary Plan of the Slovak Republic for 2018

October

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Summary

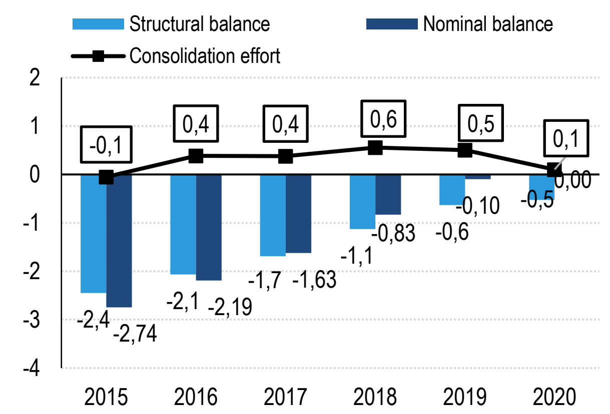
Tthe government deficit will drop to the historically lowest level of 0.83 per cent of GDP in 2018 keeping the public finances on the trajectory towards a medium-term budgetary objective (MTO) to be reached in 2020,. Next year, Slovakia will also report a budget surplus adjusted for the cost of debt financing for the first time in the history of Slovakia. In compliance with the Manifesto of the Government, balanced budget is expected until 2020.

The ongoing consolidation and solid economic growth in the coming year will push the debt under 50 per cent of GDP. The accelerating economic growth and the achievement of a primary surplus create preconditions for getting the debt under the sanction limits set out in the Budgetary Discipline Act in 2019. In the following year 2020, the gross government debt should drop down to the 45 per cent of GDP boundary.

After having posted a solid 3.3 per cent growth in 2017, the Slovak economy will accelerate in the next year to 4.2 per cent and will create more than 33 thousand new job positions. The structure of the economic growth will be backed bv strong fundamenetals. Compared to 2017, the growing household consumption will also be joined by the export backed by automotive investments. The economic growth should culminate in 2019, reaching the 4.4 per cent. The unemployment rate will drop to 7.3 per cent in 2018, the lowest level in history, and will come close to 6 per cent in 2020.

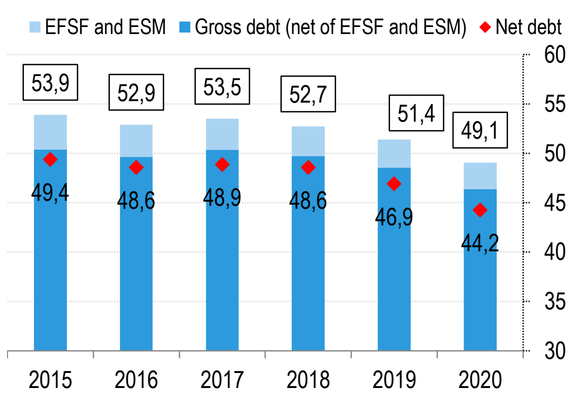
The risks to the macroeconomic forecast are broadly balanced.

CHART 1 - Structural balance (% GDP)



Source: MF SR

CHART 2 - Gross debt of the general government (% GDP)



Source: MF SR

The government has prepared a set of structural measures aiming to increase economic growth and employment by addressing major challenges faced by the Slovak economy: the labour market, elementary education and the healthcare. A package of social measures will support the labour force mobility and increase the income of workers. As regards the education sector, the government is focused, in particular, on increasing the attractiveness of teaching jobs, and development of kindergartens. Multiple projects focusing on the integration of marginalised Roma communities will be supported. Capacities will be increased in childcare for children aged below three years. The positive development in the labour market will be further supported by the employment services reform and extension of active labour market policies. In healthcare, the measures will focus on improving the efficiency of expenditures on consumption of pharmaceuticals and operating costs of hospitals. Work continues within the adoption of tax evasion prevention measures, and more focus goes to the support of innovations. Multiple measures will contribute to the decrease in the administrative and regulatory burden for businesses. Measures concentrating on the improvement of efficiency of courts, fight against corruption, and shortening the duration of debt collection processes have been implemented.

Until the 2020 elections, a majority of public spending will undergo the Value for Money revisions. Spending reviews have focused on the expenditures on education, environment, labour market policies and the social policies amounting to 7.1 per cent of GDP. The public spending totalling 15.4 per cent GDP (39 per cent of public spend) has been reviewed under the project so far. The implementation of measures is checked by a newly established Implementation entity; based on the first check, the measures have been implemented to 50 per cent. In 2018, the expenditures and results in agriculture, inclusion of marginalised groups, and employment and compensations in the state and general government will be checked within the revision process. Final reports will be prepared by 31 March 2019. In the second year of the term, the Government reformed the investment assessment process, with the Ministry of Finance having played a more active role in this process.

In the medium-term horizon, the draft budgetary plan is based on the general government budget proposal for 2018 to 2020. The draft budgetary plan is prepared under the requirements introduced through the Regulation (EU) No 473/2013 of the European Parliament and of the Council on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the Euro area (part of the so-called Two Pack), approved in May 2013.

The aim of the Regulation is to improve the coordination of fiscal and structural policies while taking into account the rules of the Stability and Growth Pact and the Europe 2020 strategy. The submission of the draft budgetary plan, which presents the developments of fiscal position, the forecast of the economy and a description of budgetary policy measures to achieve the defined medium-term objectives is a specific monitoring instrument. The presented data will enable, apart from other things, a more detailed assessment of the development of public finance in the coming year, which are based on the current general government budget proposal as opposed to the Stability Programme. The European Commission will subsequently publish its opinion on the budgetary plan. If a serious breach of the Stability and Growth Pact is identified, the Commission may request that the concerned Member State redrafts its budgetary plan.

The content and the format of the document are fully based on the European Commission guidelines. Similarly to the Stability Programme, draft budgetary plans are prepared on the basis of documents specifying the minimum requirements for draft budgetary plans – updated Specifications on the implementation of the Two Pack and Guidelines on the format and content of draft budgetary plans, economic partnership programmes and debt issuance reports.

I. Macroeconomic assumptions underlying the draft budget

The Slovak economy is projected to confirm last year's performance at 3.3 per cent this year. Growth will be driven mainly by household consumption, owing to the favourable labour market developments. In fact, household consumption is expected to post the strongest performance since 2008. The economy will add over 47 thousand new jobs, creating upward pressure on wages, and supressing unemployment rate to record lows. In addition to domestic demand, exports will support growth at the further end of the forecast horizon, as automotive investments kick in. Pace of real economic expansion is projected to reach its peak at 4.4 per cent in 2019.

I.1. External assumptions underlying the forecast

The euro area has maintained a solid pace of expansion which is set to continue in the upcoming year, driven by domestic demand and with a mild positive contribution from the external sector. The broad-based recovery is buttressed by firming fundamentals, including improving labour market conditions, favourable sentiment indicators, as well as intensified global activity.

The euro area recovery is also tangible across individual euro area economies. Besides the usual powerhouses that the euro area have relied for growth in the recent quarters (Germany, Spain), the pace of growth has picked up also in France and Italy. **The broad-based recovery underway in the euro area continues to contrast with the economic slow-down in the UK.** The external sector of the British economy has been a drag on growth since the beginning of the year, as expected post Brexit vote. Additionally, however, price developments, stagnating wages and low consumer confidence are adversely weighing on the domestic sector of the economy as well.

Most confidence indicators for the euro area and Germany – albeit down from their multiple-year highs – remain at elevated levels, signalling a sustained momentum of growth.

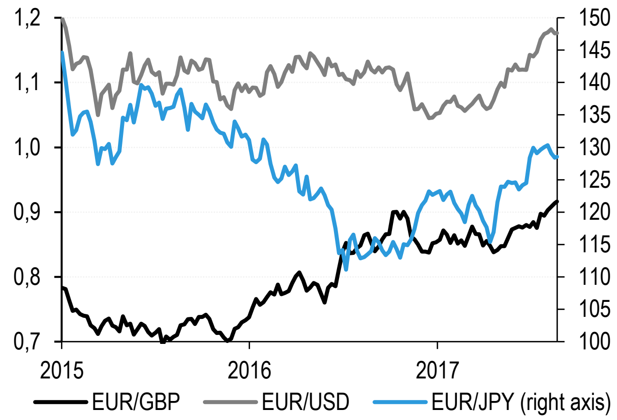
The euro area economy is projected to expand at a steady pace in the medium-term, benefitting from the stable pace of expansion in Germany, a dynamic activity in Spain, and to a lesser extent from the recovery underway in France and Italy. The Visegrad 3 region is set to grow at around 4 per cent annually this year (in the case of the Czech Republic over the 4 per cent threshold), and 3 per cent next year.

The central banks of the two largest economies are faced with an uneasy choice, as the intended tightening of monetary policy clashes with the subdued price developments. The US Federal Reserve has slowed down on plans to pursue interest rate hikes, expected at the close of this year. Currently, markets expect the next Fed interest rate increase in the first half of 2018. Despite the soft inflation readings, the Fed is to pursue monetary policy normalisation via unwinding of its quantitative easing programme, and a gradual reduction of its balance sheet already this year**. In the meantime, the recent volatility of the euro exchange rate constitutes a new source of uncertainty for the inflation projections of the European Central Bank (ECB).** At its last meeting, the ECB pledged to leave the conditions of its asset purchase programme unchanged at least until the end of 2017. Due to subdued inflation developments, markets do not expect the ECB to raise its key interest rates this or next year.

The sharp appreciation of the euro exchange rate against major currencies have caught markets off guard. The euro appreciation owes mostly to the improvements in the euro area fundamentals and favourable expectations about euro area economy. To the contrary, the British pound has depreciated against the euro and other currencies, on the back of this year's marked slow-down of the UK economy. In fact, the British pound has in August reached the weakest level against the euro since 2009.

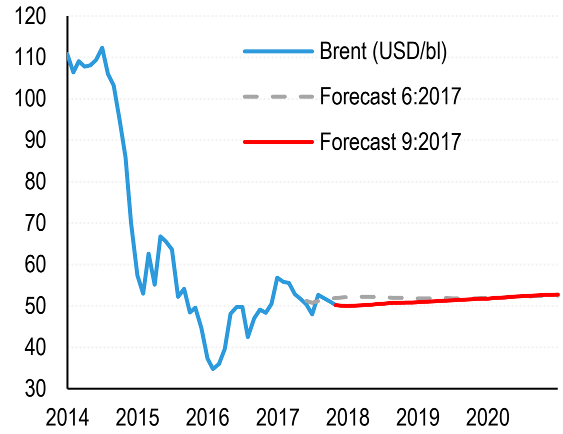
US crude oil production is expected to reach record highs, supressing the oil prices to a level close to 50 dollar per barrel. Such downward pressure on oil prices is counter-acted by a solid growth of crude oil world demand, as well as the OPEC July agreement to extend oil supply cuts for another nine months, well into 2018. Crude oil prices are thus expected to follow a stable trajectory at around 50 USD per barrel

CHART 3 - Euro strengthening under good outlook in the Euro area



Source: Bloomberg

CHART 4 - Development of Brent crude oil prices



Source: Bloomberg

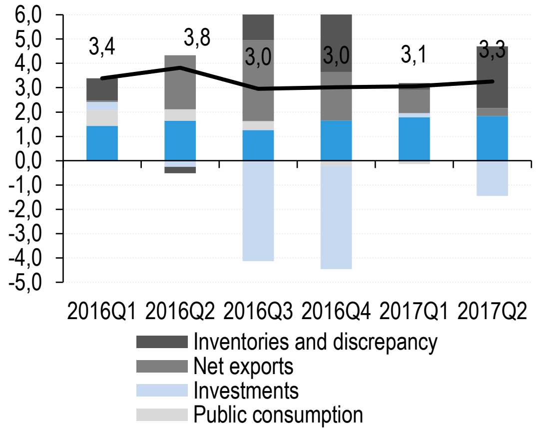
I.2. Macroeconomic forecast

The Slovak economy will grow by 3.3 per cent this year. The main driver is the household consumption which should enjoy the fastest growth since crisis due to improving labour market. Positive expectations of households result in their consumption having a higher dynamics than their disposable income for the first time after four years. Export will grow to a lesser extent than expected by the foreign demand fundamentals, which is a consequence of multiple temporary factors, e.g. the life cycle of some car models manufactured in Slovakia coming to end. The growth of investments is fuelled mainly by private sector; public investments are damped by slow drawing of the EU funds.

The economy will accelerate to 4.2 per cent in the coming year. The structure of the growth will be based on strong foundations. Robust development of household consumption will be joined by export benefiting from the launch of new car production in the Volkswagen (VW) plant and, by the year end, also in the Jaguar Land Rover (JLR) plant. The dynamics of investments will be based on the private sector again. The culmination of the JLR investment and the launching of the Bratislava D4/R7 bypass construction will compensate for the dropout after completion of the massive VW investment.

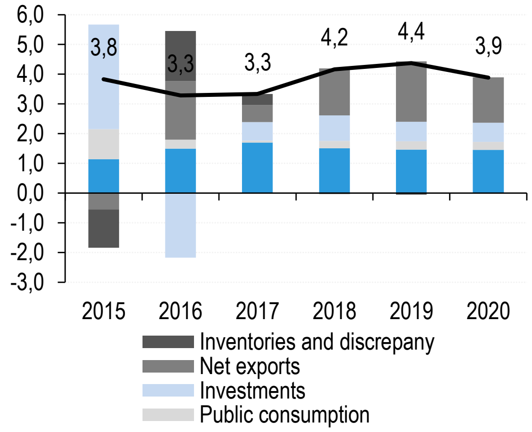
The Slovak economy will grow at a 4.4 per cent and 3.9 per cent rate in 2019 and 2020, respectively. The dynamic export particularly in car production plants will lead to acceleration in 2019. Domestic consumption will retain its sound stable rate throughout the entire medium term horizon. Investments will face a moderate slowdown due to completion of the JLR production plant. At the end of the mid-term horizon, the economic growth will slow down and get closer to its potential.

CHART5 - Contributions to GDP growth - quarterly (p.p.)



Source: MF SR

CHART6 - Contributions to GDP growth - forecast (p.p.)

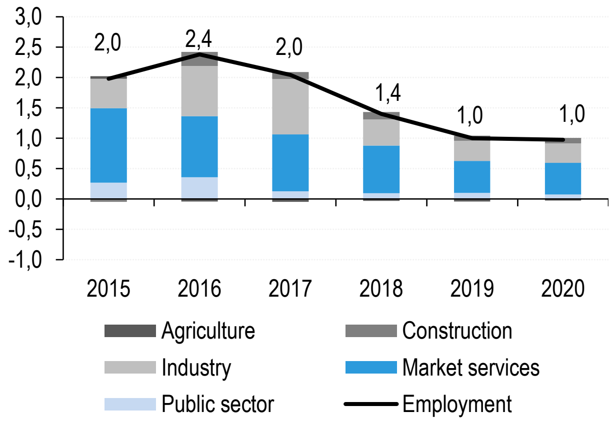


Source: MF SR

The employment will increase by 2 per cent this year, corresponding to about 47 thousand additional jobs (ESA methodology). The growth will be driven particularly by the industry and market services. In the coming year, the employment growth will slow down to 1.4 per cent adding 33 thousand new jobs. Due to insufficiency of labour force, 2019 and 2020 are expected to see slowdown of the employment growth closeto 1 per cent at the expense of the productivity growth. New positions are to be filled not only by domestic workers, but also foreing workers and Slovak nationals returning home**The unemployment rate (based on LFS) is projected to fall to a historical low of 8.2 per cent in 2017.** In 2018, the unemployment rate will drop to 7.3 per cent also as a consequence of commissioning of new investments in the automotive industry and will drop to 6 per cent by 2020.

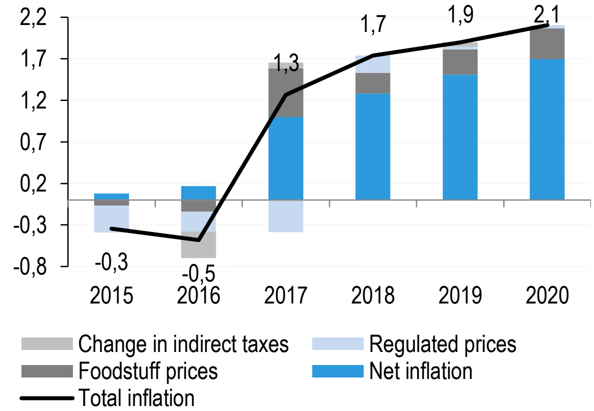
The average nominal wage in economy will grow by 3.9 per cent this year, and accelerate further to 4.5 per cent in 2018. At the end of the forecasted horizon, the wage dynamics will surpass 5 per cent under the pressure of tight labour market. Wage growth would advance most rapidly in industry, where the shortage of workers is most intense. The real wages will grow by 2.6 per cent this year and will be dampened by the pick-up ininflation. In the coming years, the real wage growth is expected to gradually accelerate towards 3 per cent.

CHART 7 - Contributions of sectors to employment growth (p.p.)



Source: MF SR

CHART 8 - Contributions of inflation (p.p.)



Source: MF SR

The prices resumed growth this year with the headline inflation rate reaching 1.3 per cent. The fist six months indicate the renewed link between prices and wages in the economy leading to the accelerated growth of service prices. A significant increase of the food prices is likely a delayed response to the global price trends. Strengthening euro and the falling oil prices dampen price increases in tradeable goods. The price growth is counteracted by the energy price reduction by the regulatory authority early this year.

The demand-pull inflation will continue to accelerate in the following years, with the fastest growth of prices of market services . Based on the growth of energy commodity prices in global markets and the development of future contracts, the regulated energy prices are expected to rise in the coming year. Due to rapid economic growth, the inflation should exceed 2 per cent at the end of the medium term horizon.

The risks to the current forecast are broadly balanced. The threat of global trade protectionism and the fragility of the Italian banking sector continue posing downside risks to our forecast, as well as the more recent threat of geopolitical conflict and the ongoing volatility of the euro exchange rate . On the upside, a smoother-then-expected Brexit proceedings and a positive spill over from the US fiscal stimulus could favourably weigh on our baseline forecast. In terms of domestic risks, a more pronounced wage acceleration as the labour market overheats amid shortage of workers poses an upside risk. However, the qualified workforce shortage may limit firm profitability, which, according to this year's information from the Statistical Office, has already slowed down. In the recent quarters, the performance of the Slovak economy has been divorced from the performance of its largest trading partners. A renewal of such link poses an additional domestic upside risk to our forecast.

BOX 1 - Estimate of the output gap for 2017 and 2018

The output gap of the Slovak economy has gradually closed, reaching 0.2 per cent of potential GDP in 2017, and the economy will begin to overheat in 2018 (0.8 per cent). This estimate is based on the national methodology of the Ministry of Finance (MF) as the reported results for 2017 and 2018 are closer to the estimate of the European Commission (COM) than results based on the COM methodology together with the MF macreconomic projection. At the same time, the results of the MF's national methodology are economically more intuitive and closer to the true, although unobserved, output gap. The national methodology is also applied in this document to the estimate of the cyclical component required to calculate the structural balance.

The purpose of the presented output gap forecast is to mimic the COM estimate which will be used to assess the structural position of the budget. The Ministry of Finance compared and evaluated two approaches: the MF's forecast with the COM methodology, and the MF's national methodology. The data about the condition of the economy after 2017 were in both cases based on the official September forecast of the Ministry of Finance approved by the Macroeconomic Forecasting Committee.

The COM methodology consists of two steps. In the first step, the estimates and forecasts are made for the trend unemployment rate which is consistent with a stable growth of wages in the economy (the so-called NAWRU) and for the trend component of total factor productivity (the so-called TFP trend). For this purpose, the **COM applies the publicly available GAP programme** which uses the Phillips curve and Kalman filter to break down the unemployment rate and total factor productivity into a trend component and a cyclical component. Since the most recent settings of the COM model are not yet available, the MF used the NAWRU and TFP trend contained in the COM spring forecast. In the second step, the estimated trend components of unemployment (NAWRU) and total factor productivity (TFP trend) are used as inputs to forecast the actual output gap in the CONV programme. The output gap estimate model in the CONV programme is based on the decomposition of the production function of the economy into labour, capital and total productivity factor contributions.

According to the Ministry of Finance methodology, in 2017, the output gap is estimated to reach 0.2 per cent of potential GDP and in 2018, the output gap will widen to 0.8 per cent. Thus the economy will enter the phase of mild overheating. On the contrary, the output gap estimate under the COM methodology with the MF's forecast indicates counterintuitively an economic slack until 2018.

The discrepancy between the output gap estimates under individual methodologies has already appeared in the forecasts in the Stability Programme for 2017-2020. While the estimates of the MF's national methodology and the COM official spring forecast predicted closure of the output gap and gradual overheating of the Slovak economy, the output gap calculated under the COM methodology applying the MF's macroeconomic forecast predicted a negative output gap throughout the entire horizon.

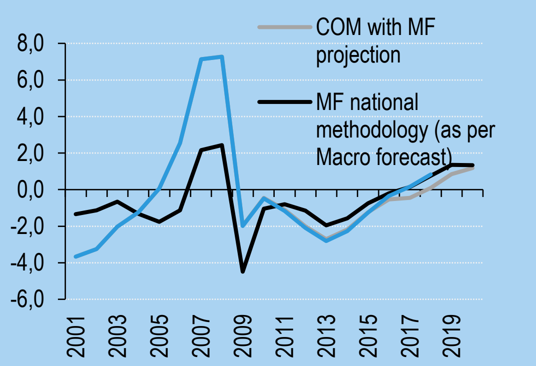
TABLE 1 - Output gap (% GDP)

	2016	2017	2018
Stability Programme for 2017-2020			
2017 COM Spring Forecast	-0.3	0.2	0.8
MF's National methodology (February 2017)	-0.2	0.2	0.7
COM methodology with MF projection	-0.6	-0.6	-0.2

Source: MF SR, EC

The output gap estimate using the MF's national methodology may also bring economically more intuitive results in future. The launching of car production in the new JLR plant within the forecasting horizon will hit the Slovak economy with a positive structural shock, a similar one to the shock of 2005 through 2008. As a consequence, both the actual economic growth as well as the potential output of the economy will jump up. Therefore, the output gap should only grow to a limited extent. While this phenomenon is captured by the MF's national methodology, the COM methodology is likely to indicate excessive overheating of the economy similarly to the overheating during the pre-crisis period from 2005 to 2008.

CHART 9 - Output gap development (per cent of pot. GDP) – EC's approach and methodology of the Ministry of Finance



Source: MF SR

TABLE 2 - Output gap and contribution of factors to potential product growth - national methodology

	Output gap (% pot. GDP)	Pot. GDP (growth, %)	TFP*	Capital stock	Labour
2012	-1.1	2.4	**1.4**	**0.8**	**0.1**
2013	-2.0	2.1	**1.4**	**0.6**	**0.1**
2014	-1.6	2.4	**1.7**	**0.5**	**0.2**
2015	-0.8	3.0	**2.0**	**0.6**	**0.3**
2016	-0.2	2.8	**1.8**	**0.7**	**0.3**
2017F	0.2	2.8	**2.0**	**0.5**	**0.3**
2018F	0.8	3.5	**2.6**	**0.7**	**0.2**
2019F	1.3	3.8	**2.8**	**0.8**	**0.2**
2020F	1.3	3.9	**2.8**	**0.9**	**0.2**

*Total productivity of factors

Source: MF SR

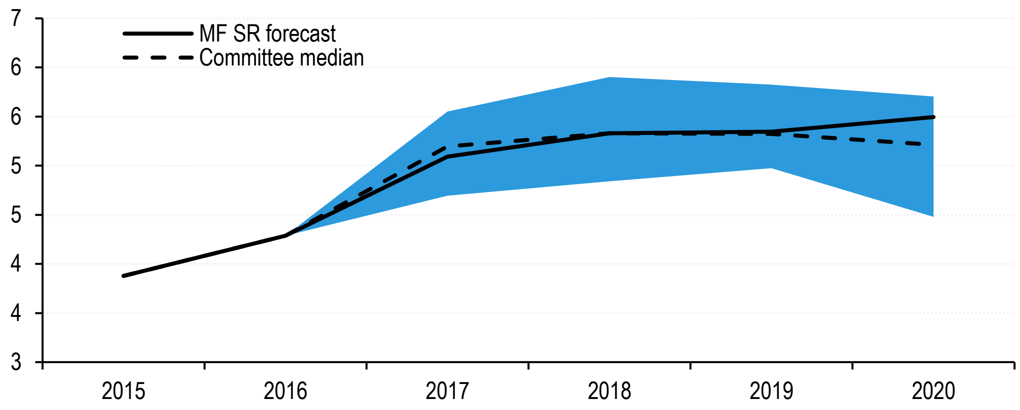
The difference in the output gap estimates of the COM and the MF national methodology is caused by different forecast horizons and different total factor productivities (TFP). While the COM methodology forecasts the output gap for two years ahead, the MF's forecast covers four years. The COM methodology is based on trends and filtration of variables, so the extension of the forecasting horizon may result in different output gap estimates in a shorter horizon even after keeping the macroeconomic input unchanged in the exact same period. The second difference lies particularly in the historical data of the total factor productivity. Although both institutions calculate the potential output using the Cobb-Douglas production function, the Ministry of Finance increases the potential product through TFP in 2005 – 2008 so as to correspond to the structural changes in the economy, which cannot be captured by the COM methodology. In these years, Slovakia, as a small open economy, faced a significant supply shock caused by the adopted structural reforms. The excessive output gap in 2007 – 2008, which follows from the COM method, is not confirmed by other imbalance indicators such as net inflation, balance of the current account of the balance of payments, and unit labour costs. A partial exemption to the rule is the dynamic growth of the real estate market.

I.3. Forecast assessment by the Macroeconomic and Tax Revenue Forecasting Committees

All members of the Macroeconomic Forecasting Committee (NBS, ČSOB, Infostat, SLSP, Tatrabanka, Unicredit, VÚB, Sberbank and the Slovak Academy of Science) assessed the current medium-term macroeconomic development forecast prepared by the Ministry of Finance as realistic.

Considering the effects on budgetary revenues in 2018, the forecast prepared by the Ministry of Finance is almost identical with the median calculated by the members of the Committee. This effect is expressed as a weighted average of individual relevant bases for budgetary revenues, where weights are given by the share of individual taxes in the total budgetary revenues[1].

CHART10 - Comparison of forecasts of macroeconomic bases1 for budgetary revenues with Committee members



Source: MF SR

The updated tax revenue forecast prepared by the Ministry of Finance and included in the budget proposal is a follow-up to the macroeconomic forecast which was **evaluated by all** members of the Tax Revenue Forecasting Committee (KRRZ, NBS, Infostat, SISP, ČSOB, UniCreditBank, and Tatrabanka) **as realistic**.

BOX 2 - Independent Macroeconomic and Tax Revenue Forecasting Committees

The Macroeconomic Forecasting Committee and the Tax Revenue Forecasting Committee have been set up in accordance with the Constitutional Act 493/2011 Coll. on Budgetary Discipline as an advisory body of the Minister of Finance. The purpose of these Committees is to ensure better transparency, objectivity, and quality of macroeconomic and tax forecasts. In accordance with the constitutional act, the Committees elaborate and submit forecast at least twice a year, by 15 February and 30 June of the current budget year. However, it is normal practice for them to also prepare forecasts for the purposes of the budget drafting process until the end of September. In exceptional events, the meeting of the Committee may also be convened by the Chairman of the Committee, the Minister of Finance, or the absolute majority of the Committee members.

Besides the Ministry of Finance, the members of the Committees come from the representatives of the government-independent institutions (NBS, SAV, Infostat, and private banks). The members of the Macroeconomic Forecasting Committee provide a verbal assessment of the macroeconomic forecast of the Ministry of Finance using such words as *conservative*, *optimistic*, or *realistic*. The tax revenue forecast of the Ministry of Finance is assessed by the Tax Revenue Forecasting Committee members through the provision of their own forecast, with their assessment calculated automatically based on a deviation. **The forecast of the Ministry of Finance is accepted as a forecast of the Committee if labelled *conservative* or *realistic* by an absolute majority of the members.** If no such assessment is given to the forecast, the Ministry of Finance is obligated to revise the forecast and submit it to the Committee for review again. The process is repeated until the forecast of the Ministry of Finance is accepted as the Committee's forecast.

[1] Macroeconomic bases for budgetary revenues (the weight of indicators depends on the share of individual taxes in the total tax and social contribution revenues); Wage base (employment + nominal wage) – 51.1%, Nominal private consumption – 25.7%, Real private consumption – 6.6%, Nominal GDP growth – 9.9%, Real GDP growth – 6.7%.

II. Budgetary objectives

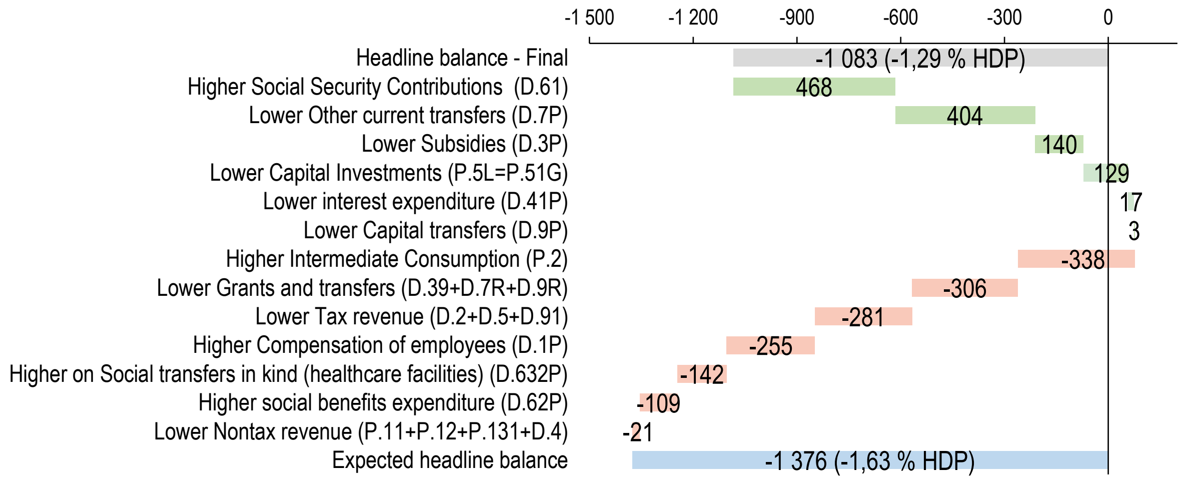
The primary objective of Slovakia's fiscal policy is to ensure effective and sustainable public finance, facilitating permanent growth of quality of life and of public services. Based on the ongoing monitoring of developments in public finance, the general government deficit for the current year will reach 1.63 per cent of GDP. The current draft budget has set the fiscal deficit target at the level of 0.83 per cent of GDP, the lowest level in history. Such a target ensures an adequate route to structurally balanced general government balance, while fully respecting the government expenditure priorities. In compliance with the Manifesto of the Government, balanced budget is expected until 2020. The ongoing consolidation and solid economic growth in the next year will push the debt under 50 per cent GDP. One year later, it should, when compared to the economy performance, get under the sanction zones of the Budgetary Discipline Act, attacking the threshold of 45 per cent of GDP in 2020.

Based on the MF SR's estimates, the 2016 general government deficit reached the level of 1.99 per cent of GDP. Year-on-year decrease would amount to 0.75 p.p. Compared with the spring notification, the deficit revision of 0.31p.p. has been particularly caused by the downward revision of tax revenues due to worse settlements of the corporate income tax related to postponed submissions of tax return. The Draft Budgetary Plan also counts on the negative risk stemming from additional application of super-dividend test by Eurostat which would correct the accrual non-tax revenues by 0.2 per cent of GDP in 2016. Materializing the above risk, the nominal deficit would total 2.19% GDP with the y/y decrease by 0.55 p.p.. The 2016 gross general government deficit should reach 51.9% GDP[2], falling on a y/y basis by 0.5 p.p.

II.1. Recent development in public finance

The 2017 expected public finance deficit is projected to reach 1.63% GDP, which results in deficit worsening by 0.34% GDP compared to the targeted general government deficit (1.29% GDP[3]),. The expected deficit (ED) of the public finance development is based on the September 2017 macroeconomic and tax forecast[4] and on the current estimate of the development of other revenue and expenditure components of the general government budget, which are monitored on an ongoing basis[5].

CHART 11 - Analysis of development of the general government balance in 2017 (ESA 2010), contributions in EUR mil.



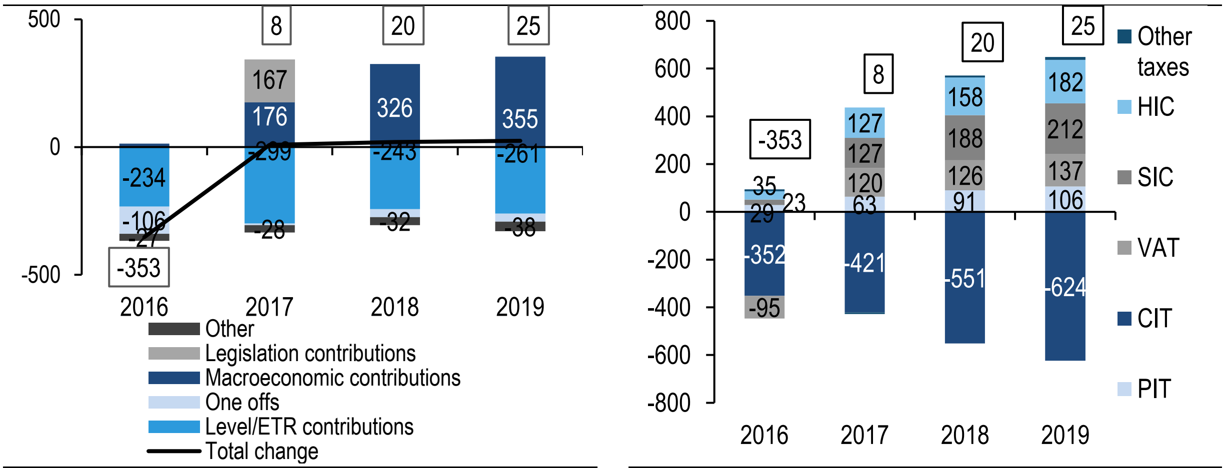
[2] Taking into consideration the 2016 GDP revision, the notified debt will amount to 51.8% GDP. More in BOX 8.
[3] Throughout 2017, two entities were included in the general government budget, namely Jadrová a vyraďovacia spoločnosť (Nuclear and Decommissioning Company/JAVYS) and MH Invest II.
[4] Forecast of the Macroeconomic Forecasting Committee in accordance with its By-laws and with Art. 8(2) of the Budgetary Discipline Act 493/2011 Coll. and the forecast of the Tax Revenue Forecasting Committee in accordance with its By-laws of September 2017.
[5] The Public Finance Management and Monitoring Committee takes care of the internal public finance monitoring process at MF SR.

(+) / (-) means positive / negative impact on the general government deficit *Source: MF SR*
The relevant ESA 2010 classification codes in brackets.
** including the higher payments for the public health care insurance of the individuals who receive government insurance (EUR 100 mil.)*

The 2017 general government budget did not include two entities, namely Nuclear and Decommissioning Company (Jadrová a vyraďovacia spoločnosť - JAVYS) and MH Invest II. Management of JAVYS has a negative influence on the public finance deficit (-EUR 63 mil.) and MH Invest II's influence on deficit is nearly insignificant (-EUR 2 mil.).

The current estimate of tax revenue development which is based on the Tax Forecasting Committee (TFC) forecast only causes a negligible revision of the total revenues from taxes and contributions (Chart 12) compared to the approved budget. Taking a more detailed look at the updating structure of the revenues from taxes and contributions reveals marked differences. A significantly negative surprise compared to the budget was the corporate tax with a striking development in 2016, which also had a structural influence on the update of taxes throughout the entire forecasting horizon.

CHART 12 - Contributions to change of the forecast compared to budget for 2016 - 2017 (EUR mil.)[6]



Source: MF SR, TFC *Source: MF SR, TFC*

Total tax revenues (D.2+D.5+D.91) of the general government are EUR 281 mil.[7] (0.33% GDP), hence below the budget. Negative development of the corporate tax (-EUR 421 mil.) is explained by the significant slowdown of profitability growth for 2016 not counted on by the budget and the positive one-off factors in 2015 which did not recur in 2016[8]. Lower revenue due to lower profits has an impact on the revenue from special levy on business in regulated sectors (-EUR 40 mil.) and lower interest on bank deposits has an impact on the revenues from the withholding tax (-EUR 18 mil.). Corrections of revenues also occur in the event of revenues from emission permits (-EUR 34 mil.). The positive development of the revenue from indirect taxes (EUR 132 mil.) plays a compensatory role; here, the forecast is under the influence of the ongoing growth of successful collection of VAT (EUR 120 mil.) and the excise taxes (EUR 12 mil.). Positive developments in the labour market translate into positive development of the individual income taxes (EUR 63 mil.). Changes in property tax rates which constitute the revenue of local

[6] Contributions to the change of the current TFC forecast compared to the TFC forecast applied in the 2016 and 2017 budget. Exclusive of the difference in non-tax revenues according to the national classification (EKRK) which are not forecasted by TFC and which constitute tax revenues under the ESA2010 methodology.
[7] The tax revenues assessed in the TFC are EUR 245 mil. lower compared to the budget; the difference against EUR 281 mil. is explained by the lower expected revenues from the sale of emission permits (-EUR 33 mil.) and the updated estimate of the revenues from gambling and administrative charges which constitute ESA2010 revenues, but which are not assessed or forecasted by TFC.
[8] The selected costs (of agency, commissions, considerations for the use of intangible assets, or the expenditures on advisory and law services) are, since 2015 with the aim of improving the payment discipline, considered to be tax recognizable only after they have been settled. These costs were not recognized as a tax expenditure in 2015 for the first time. Once paid in 2016, they were treated as a tax expense. This had a positive impact on the tax yield in 2015 and a negative one in 2016, and is one of the factors which has misdirected to a more significant extent the tax forecast for the actual year (more in BOX 1 in the IFP commentary).

governments have contributed to the positive development in this component as well (EUR 21 mil.). Compared to the budget, additional revenue should also flow from the new levy on the non-life insurance policies.

The general government revenues from the contributions for social security (D.61)[9] have significantly overrun the budgeted level by EUR 468 mil. (0.55% GDP). More than a half of these revenues (EUR 254 mil.) is imputable to the more positive development in the labour market which translates accordingly into higher collection of social and health care contributions from the economically active population. The increase in this item compared to the budget is also explained by higher contributions paid by the government for the group of individuals delimited by valid legislation (whereof EUR 100 mil. higher revenues of the public health insurance and EUR 16 mil. higher revenues of the Social Insurance Company). However, the contributions paid by the government have a neutral influence on the deficit. The remaining EUR 98 mil. with equally neutral influence on the deficit is connected with the re-charging of the revenues from the pension saving scheme of the armed force corps in accordance with the ESA2010 principles.

Non-tax revenues of the general government (P.11+P.12+P.131+D.4) influence the general government deficit negatively by EUR 21 mil. (0.03% GDP). The entire correction is explained by the lower expected revenues from the receipts of public entities (P.11+P.12). In particular, expected is the decrease in the receipts in the event of the Slovak Railways ŽSR mainly due to lower payments from carriers (EUR 39 mil.), decrease in the revenues of MH Invest from the sale of land (EUR 27 mil.), and the slump in the revenues of NDS (EUR 27 mil.) which is also related to lower receipts from toll stickers. Lower are also the expected state budget revenues (EUR 17.5 mil.), receipts from passenger transport of ŽSSK (EUR 9.3 mil.), and the receipts of public universities (EUR 6 mil.). On the contrary, this revenue item is positively influenced by the expected receipts of the off-budget entities JAVYS (EUR 90 mil.) and HM Invest II. (EUR 2 mil.). Higher property income (P.131+D.4R) partially outweigh the slump of non-tax revenues (EUR 13 mil.), whereof income from dividend amounts to EUR 8 mil.[10].

Decrease in the revenues from grants and transfers (D.39+D.7R+D.9R) by EUR 306 mil. (0.36 % GDP) is explained particularly by the development of fund drawing from the EU budget, with a EUR 338 mil. dropout in sources from the EU being expected compared to the budgeted level. Higher revenues from grants and transfers amounting to EUR 49 mil. are expected mainly by both railway companies (EUR 13 mil.) and Eximbanka (EUR 10 mil.) that counts on collection of the income from insurance of the non-tradeable risk. On the contrary, a dropout has been reported with regard to lower contributions to the National Nuclear Fund (NJF) from the operators of nuclear facilities (EUR 9 mil.).

The expenditures on the compensation for employees in public administration (D.1P) have grown by EUR 255 mil. (0.30% GDP) compared to the budget. The growth can be, to a substantial extent, attributed to the release of the provision for the public administration employee wages and salaries adjustment from intermediate consumption and other current transfer which has already been taken into account in the budget under other economic items of the budget (EUR 148 mil., more in BOX 3). Further, within the sources from the budget of the EU and national co-financing, the use of sources has been re-directed resulting in the increase in the compensations for employees by EUR 69 mil. (particularly in the event of municipalities and railway companies). The growth of expenditures compared to the budget is also caused by the transfer of JAVYS and MH Invest II to the public finance area (EUR 27 mil.). At the same time, the off-budget sources of public universities coming from business activity[11] were used to increase compensations as well (EUR 12 mil.).

BOX 3 - Analytical modification related to the reserve for wage adjustment in GG

[9] TFC only assesses the development of contributions for social security from the economically active population (social and health care contributions.

[10] Detailed breakdown by entities is specified in the general government budget for 2018-2020.

[11] In accordance with the Act on Universities, the income coming from business activities (per diem, payment for accommodation at the boarding house, administrative fees, etc.) constitutes an off-budget item.

The 2017 budget had a reserve for adjustment of wages of general government employees (EUR 148 mil.) which was allocated to the ESA item of intermediate consumption (EUR 50 mil.) and other current transfers (EUR 98 mil.). The expected deficit of public finance already counts on the use of said reserves under the corresponding economic item of employee compensations (EUR 148 mil.), which misrepresents the economic essence of the transactions made in public finance at simple comparison of expenditure items in the budget and ED. The analytical modification of provisions (their relocation to the corresponding economic item) reveals that according to ED the compensations have only grown by EUR 107 mil. The expenditures on intermediate consumption have grown by EUR 367 mil. (compared to EUR 317 mil.) and the savings of other current transfers actually corresponds to the amount of EUR 306 mil. (and not EUR 404 mil.).

TABLE 3 - Analytical view of the reserves in the general government budget in 2017 in EUR mil.

	ESA code	GG budget (1)	Adjusted budget* (2)	ED (3)	Difference (3)-(1)	Difference (3)-(2)
Total expenditures (D.1P, P.2, D.7P)		**13,957**	**13,957**	**14,146**	**189**	**189**
Compensations	**D.1P**	**7,343**	**7,491**	**7,598**	**255**	**107**
Wages and salaries		5,336	5,446	5,522	185	76
- Social contributions of employers		2,006	2,045	2,076	70	31
Intermediate consumption	**P.2**	**4,696****	**4,646**	**5,034**	**338**	**388**
thereof reserve for compensations		*50*				
Other current transfers	**D.7P**	**1,918**	**1,820**	**1,514**	**-404**	**-306**
thereof reserve for compensations		*98*				
Total provisions		**148**				

* correct allocation of provisions to the corresponding economic items of expenditures
** item in the GGB (EUR 4,717 mil.) also includes the annual clearance of the contributions paid by the government to the public health insurance amounting to (EUR 21 mil.), which item was analytically adjusted and allocated to the relevant corresponding item D.62P

Compared to the budget, the intermediate consumption (P.2) has grown by EUR 338 mil. (0.4 % GDP). Taking the analytical modification connected with the reserves for state employee wage adjustment into consideration, the expenditures on intermediate consumption (purchase of goods and services) reached an EUR 388 mil. growth. The budget is expected to be exceeded particularly in the case of municipalities (EUR 186 mil.); the off-budget expenditure on the purchase of goods and services of JAVYS are at the level of EUR 56 mil.; the liabilities of health care facilities have grown by EUR 30 mil.; and a negative impact, compared to the budget, on deficit also have the higher expenditures of ŽSSK (EUR 25 mil.), Social Insurance Company (EUR 21 mil.), RTVS (EUR 15 mil.), EOSA (EUR 12 mil.), or the settlement of the liabilities from the resolutions concerning privatization and privatization projects in the case of MH Manažment. On the contrary, public universities (-EUR 32 mil.), ŽSR (-EUR 8 mil.), and the higher territorial units (VÚC) (EUR -8 mil.) are expected not to attain the budgeted level of the expenditures on intermediate consumption.

The EUR 140 mil. savings on subsidies (D.3P) have a positive effect on the deficit as well; the co-financing within subsidies in agriculture corresponds to EUR 101 mil. Greater subsidies go to the transport system (EUR 20 mil.), with bus transport taking EUR 12 mil. share of that figure.

Lower interest cost (D.41P) by EUR 17 mil. also bring a positive contribution to the development of the expected deficit compared to the budget. As regards the expenditures on the government debt servicing, an EUR 10.2 mil. saving is expected; interest cost savings are also realised by ŽSSK (EUR 4 mil.), NDS (EUR 2 mil.) and ŽSR (EUR 1 mil.).

Compared to the budget, the total social transfers (D.6) have grown by EUR 251 mil. (0.32 % GDP). Expenditures on public health insurance (D.632P) have grown by EUR 142 mil., and the expenditures on social benefits (D.62P) by EUR 109 mil., with the higher payment for the public health care insurance of the individuals who receive government insurance amounting to EUR 100 mil. As regards the social benefits, the expected deficit reflects higher expenditures of the Social Insurance Company on sick benefits (EUR 23 mil.), unemployment benefits (EUR 20 mil.), and also savings on the retirement benefits (EUR 13 mil.). More favourable conditions in labour market have brought about savings on social benefits amounting to EUR 20 mil. (particularly within social assistance benefits) and an EUR 9 mil. savings within active labour market policies.

The deficit development is also positively influenced by higher other current transfers (D.7p) in the amount of EUR 404 mil. (0.48 % GDP), but the net impact amounts to EUR 306 mil after taking into consideration the wage adjustment reserves. The savings within this expenditure item is related to the expected slow drawdawn of EU funds in the amount of EUR 240 mil. and the induced EUR 73 mil. decrease in co-financing. This item also covers the savings within the contributions to the EU budget totalling EUR 11.9 mil.

The EUR 129 mil. (0.15% GDP) decrease in capital investments (P.5L) has a positive effect on the general government balance. Savings within this item compared to the budget are explained by substantial failure to draw funds from the EU sources (EUR 317 mil.) particularly in the event of NDS (-EUR 222 mil.), ŽSR (-EUR 95 mil.) and ŽSSK (-EUR 43 mil.). Failure to draw the EU funds also leads to savings within co-financing (EUR 66 mill.). Lower EU sources in case of both railway companies are outweighed by their own sources and the sources of credit for investment activities (EUR 70 mil. in total); NDS partially compensates the EU fund dropout through increase in liabilities (EUR 76 mil.). On the contrary, higher investment expenditures have been noticed particularly in the event of municipalities (EUR 127 mil.) and the Social Insurance Company (EUR 13 mil.).

Referring to the expected deficit, additional risks of the general government management are not expected to occur in 2017. In the coming months, the health care facility debt settlement process could be launched - its impact on the GG deficit would be neutral up to moderately positive (BOX 4).

BOX 4 - Influence of health care facility debt settlement on the balance and gross debt of the general government

The government plans to settle the debt of the health care facilities (HCF) until 2019. The debt settlement also includes the stabilisation of the hospital management; the hospitals which would be allowed to take part in the debt settlement must, among other things, elaborate and implement stabilisation plans. Total recorded outstanding liabilities of health care facilities as of the 2016 year end amounted to EUR 647 mil., with EUR 640 mil. falling under the facilities under the general government sector and around EUR 7 mil. under the facilities outside the sector. The health care facility debt settlement concept[12] counts on using no more than EUR 585 mil. for debt settlement within the horizon until 2019.

The debt settlement process should be carried out in independent rounds depending on the age of receivables until 2019 and should be voluntary. In the coming months, the liabilities dating back to 2014 and older liabilities amounting to EUR 76 mil. should be settled. This round may also be joined by the hospitals having stabilisation plans not approved by the MH SR. Private creditors have two options to take part in the debt settlement procedure. Either in the form of an auction in which they would compete based on the discount amount or they may use a fixed discount which depends on the age of the receivable. The debt settlement process will be voluntary both for the creditors and the hospitals. The final amount of settled liabilities will also depend on the discounts on the principal offered by the creditors. The minimum discount for all liabilities registered for the debt settlement process is expected at the level of 2.5% and the precondition for the creditors to join the debt settlement is their waiver of the interest and charges accrued in connection with the receivable.

Hospital debt settlement may have a neutral up to moderately positive influence on the general government deficit[13] in the short-term horizon.[14]

[12] http://www.rokovania.sk/Rokovanie.aspx/BodRokovaniaDetail?idMaterial=26674.

[13] Private hospitals the liabilities of which were included in the GG deficit in the past may register for the debt settlement process as well. The provision of government sources to settle the debt of private hospitals with the exception of their liabilities to the Social Insurance Company would increase the general government deficit to the full extent of the funds which would be provided for the settlement of their debt. The settlement of the liabilities of private hospitals they have to the Social Insurance Company will have a neutral impact on the deficit. The MH SR does not have exact records about the volume of the liabilities of private hospitals - besides the EUR 7 mil. which have been identified, there is an estimate of additional liabilities amounting to EUR 10-20 mil. Involvement of private hospitals in the debt settlement mechanism is not expected by the MH SR due to strict conditions applicable to debt settlement, such as accepting a nominee of the MH SR as a member of the hospital's supervisory bodies.

[14] There is a precondition that the expenditure on the liabilities of hospitals concur with their assignment to the MH SR, or to other legal entity and their settlement.

- Settling the receivables of the Social Insurance Company (EUR 202 mil.) to the fullest extent, satisfying the receivables of private creditors to the extent of the remaining released sources, and applying the minimum discount (2.5%), the general government deficit would improve cumulatively by EUR 9 mil.[15] in 2017 - 2019. The higher the discount, the more positive the impact on the deficit.
- The settlement of the liabilities to the Social Insurance Company should have a neutral effect on the budget. Higher revenues of the Social Insurance Company from the settlement of liabilities[16] will most probably be accompanied by the decrease in the transfer from the state.
- The settlement of liabilities to private suppliers will have a positive impact on the deficit depending on the discount provided and the interest and charges booked on the HCF side.

The gross public debt should not be raised provided that the state will use the available sources for the debt settlement and will not be compelled to make a borrowing.

- The outstanding liabilities of HCF are currently not entered in the gross public debt published by Eurostat.
- Based on the government's plans, the financial sources for debt settlement should be released from the state financial assets based on a resolution of the Parliament.

In the long-term horizon, the debt settlement process should contribute to the stabilisation of HCF management and keep the growth of expenditures at a sustainable level. The objective of debt settlement is the overall stabilisation of the management of hospitals. One of the major preconditions for hospital debt settlement includes stabilisation plans and set up of supervisory bodies. In the event of failure to meet the stabilisation plan, the MH SR may claim recovery of the financial receivable from the hospital amounting to the sum provided to the hospital within the debt settlement process. In the event of failure to meet the stabilisation plan, the MH SR may also enforce other sanction mechanisms:

- wage freezing above the level of the minimum laid down by the legislation;
- impossibility to draw additional funds for debt settlement;
- initiation of a change process covering the statutory body;
- sanction for violation of contractual obligations.

II.2. Monitoring of the development of structural balance and expenditure benchmark within the budgeting horizon

Since 2014, the fiscal policy of the SR has been subject to the rules of the preventive part of the Stability and Growth Pact aiming at achieving the medium-term objective (MTO) expressed as structural deficit of 0.5 per cent of GDP=. Heading towards the MTO is assessed from time to time by way of the structural balance and the expenditure benchmark. Both indicators, which constitute complements at compliance assessment, enable to judge the fiscal position of the country in an analytically more accurate manner than the simple reporting of the general government nominal balance.[17]

Compliance with the European fiscal rules is expected throughout the entire horizon of 2017 - 2020. Accumulative consolidation of the structural balance in the amount of 1.5% GDP (from 2017-2020) corresponds to the achievement of the medium-term objective in 2020. At the same time, the general government expenditures throughout the budgeting horizon do not show significant deviations from the reference trajectory of the expenditure benchmark.

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[15] The quantification does not take into account the interest and charges accrued on the settled receivables which constitute a positive risk for the deficit and neither does it count on debt settlement of private hospitals.
[16] The Social Insurance Company does not account for the receivable in the form of outstanding insurance premiums for the purposes of government account preparation.
[17] Vade mecum on the Stability and Growth Pact – 2016 edition, European Economy. Institutional Paper. 021. March 2016.

BOX 5 - Emphasis on the expenditure benchmark in assessing the compliance with the preventive arm of the Stability and Growth Pact

The European Commission uses two indicators , the structural balance and the expenditure benchmark, to review the compliance of a Member State (MS) budget with the preventive arm of the Stability and Growth Pact. The structural balance was incorporated in the European fiscal framework in 2005 in response to the criticism that the then-valid rules had not taken into consideration the impact of the economic cycle on the general government balance. The evaluation of a MS based on nominal deficit boundaries did not give the countries sufficient motivation towards the counter-cyclical fiscal policy and they did not build an expenditure budget reserve at the times of economy overheating[18]. On the other hand, the upper limit of the nominal deficit hindered fiscal incentive for the countries the GDP of which slumped more significantly under its potential[19].

In the 2011 two-pack reform, the so-called expenditure benchmark was incorporated in the Pact's preventive part. Based on this rule, the expenditures under the government's control must not show a faster y/y growth than the medium-term potential economic growth. The referential potential economic growth rate is based on the 10-year smoothed average which is not subject to significant revisions. Therefore, compared to the structural balance the expenditure benchmark constitutes a more foreseeable and stable indicator which is also under good operative control of the government (expenditure benchmark stipulates the exact limit for the growth of expenditures which is used in the assessment of the compliance of the draft with the budget fulfilment).

Aiming to make the European budgetary rules more simple, the Ministers of Finance of the EU approved at the end of 2016 the Economic and Financial Committee (EFC) report which lays more emphasis on the expenditure benchmark when assessing the compliance with the Pact. The initiative also stems from the **Five Presidents' Report**[20] which states the simplification of the European fiscal framework as one of the priorities. Although the final text approved by the Ministers does not provide an unambiguous description of the hierarchy of the two indicators for the final assessment, the budgets of EU countries for 2018 should be reviewed by the European Commission primarily based on the compliance with the expenditure benchmark. The primary emphasis on the expenditure benchmark in assessing the years 2017 and 2018 was also reiterated by the European Commission in the **May 2017 assessment of the Stability Programme of the SR.**

II.2.1. Structural balance

The compliance with the development of structural balance with the European fiscal rules forms the basis for setting the fiscal policy objectives in the Slovak Republic. Compliance with the European fiscal rules is carried out by comparing attained (in the previous year) or the planned consolidation (in the current and the coming year) with the consolidation requirements on both one-year and two-year horizon. Each year's consolidation requirements are based on the actual economic cycle (larger consolidation required at the time of overheating) and the sustainability of economy (larger consolidation required if the country's gross debt overruns the threshold of 60 per cent of GDP and with existing risks of long-term sustainability).

The interpretation of the EU fiscal rules requires Slovakia to have a year on year structural consolidation in the amount of 0.5 per cent of GDP since 2017 until the medium-term objective (MTO) of the 0.5 per cent of GDP structural deficit[21] is reached. The economy has apporached its potential output since 2016, and the current year is expected to report a faster growth dynamics compared to the estimated potential development. Throughout the entire horizon, the positive output gap is not expected to exceed the level of 1.5 per cent of GDP, when the required rate of y/y consolidation accelerates above 0.5 per cent of GDP.

[18] During the periods of positive output gap, tax revenues are growing above their long-term potential, and therefore it is appropriate to hold the growth of expenditures back, so the return of economy back to its potential does not cause steep worsening of the GG balance.
[19] Considering the falling macroeconomic bases, the slump in economy is also accompanied by the decrease in tax revenues and, consequently, also by worsening balance.
[20] Report by Jean-Claude Juncker elaborated in close cooperation with Donald Tusk, Jeroen Dijsselbloem, Mario Draghi and Martin Schulz.
[21] MTO acknowledged in the Stability Programme of the SR for 2017-2020.

TABLE 4 - Consolidation efforts (ESA 2010, % HDP)

	2013	2014	2015 S	2016 S	2017 OS	2018 R	2019 R	2020 R
Nominal balance	**-2.72**	**-2.71**	**-2.74**	**-2.19**	**-1.63**	**-0.83**	**-0.10**	**0.00**
Cyclic component	-0.7	-0.6	-0.3	-0.1	0.1	0.3	0.5	0.5
One-off impacts	0.0	0.3	0.0	0.0	0.0	0.0	0.0	0.0
Structural balance	**-2.0**	**-2.4**	**-2.4**	**-2.1**	**-1.7**	**-1.1**	**-0.6**	**-0.5**
Consolidation efforts	**1.8**	**-0.4**	**-0.1**	**0.4**	**0.4**	**0.6**	**0.5**	**0.1**
Required consolidation efforts	EDP	-0.4*	0	0.25	0.50	0.5	0.5	MTO
Deviation (1y)**	EDP	**0.0**	**-0.1**	**0.1**	**-0.1**	**0.1**	**0.0**	**MTO**
Deviation (2y)**	EDP		**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**MTO**

** after application of the investment exception for EU fund co-financing ** data rounded to one decimal place* *Source: MF SR*

Taking into consideration the expected headline deficit at the level of 1.63 per cent of GDP, the structural deficit is expected to reach 1.7 per cent of GDP. The structural balance is consolidated by 0.4 per cent of GDP on a y/y basis, a figure tightly under the requested consolidation effort within a one-year horizon. Taking into account the consolidation from the previous year, the deficit reduction rate within a two-year horizon is in full compliance with the Pact's rules.

With the estimated acceleration of the Slovak economy above its potential in 2018, the structural balance is expected to exceed the targeted nominal deficit (0.83% GDP) by three decimals. The 0.6 per cent of GDP y/y consolidation overruns the requirements stemming from the Pact and warrants compliance within both one-year and two-year horizon (at two – year only an insignificant deviation is identified).

From 2019, the Slovak public finance will get close to its medium-term budgetary objective (structural deficit of 0.5 per cent of GDP). The structural deficit is expected to drop to 0.6 per cent of GDP in 2016, i.e. nearly to the level of MTO[22]. In accordance with the Manifesto of the Government, the first nominally balanced management of the general government in history is expected to take place in 2020.

BOX 6 - Fiscal position of Slovakia

The analysis of fiscal position assesses year – on – year changes in the fiscal policy in individual phases of the economic cycle, by showing how the fiscal policy reacts to the changing economic conditions. In accordance with the standard economic theory, larger consolidation is expected at good times and, on the contrary, fiscal contraction during worse economic development. This view allows to assess in a longer time horizon whether the country applies a pro- or a counter-cyclical fiscal policy, i.e. whether the fiscal policy of the government contributes to the stabilisation of the economic cycle.

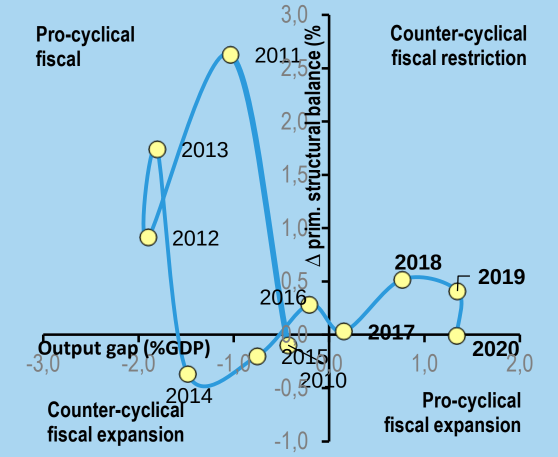
The most illustrative depiction comprises the graphic portrayal of the relationship between the year – on - year change of the primary structural balance and the output gap within four quadrants. A positive change of the primary structural balance means fiscal consolidation, while negative difference corresponds to the fiscal incentive. The standard approach (CHART 13) compares the change of the primary structural balance against the actual level of the output gap. The alternative approach (CHART 14) makes use the year – on – year change of the output gap instead of its level. The advantage of the second approach lies in the lower sensitivity to the revisions of output gap, which tend to be more frequent than the revisions of its changes. EC uses this approach to determine the required consolidation effort, and monitors both the level and the change of the output gap (Annex 1).

After a neutral fiscal policy in 2014-2017, the GG deficit reduction will be held back from 2018 by gradual acceleration of the Slovak economy above its potential. This trend should slow down in 2020, when the structural deficit

[22] The structural balance in this amount would not be enough to assess attainment of MTO at the ex-ante assessment by the European Commission. However, such structural balance would mean the attainment of MTO at ex-post assessment. During ex-post assessment, the Commission considers the MTO to be achieved also in the event that the deviation of the structural balance from the MTO set is less than 0.02% GDP. Vade Mecum on the Stability and Growth Pact, 2017 Edition, p.36.

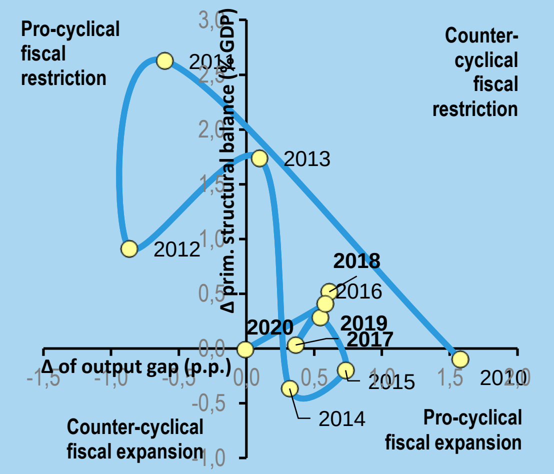
is expected to stabilize at the level of the medium-term budget objective. The primary structural surplus should be attained as early as in 2018.

CHART 13 - Change of the primary structural balance compared to the output gap level (% GDP)



Source: MF SR

CHART 14 - Change of the primary structural balance compared to the output gap change (% GDP)



Source: MF SR

TABLE 5 - Primary structural balance (% GDP)

	2015	2016	2017	2018	2019	2020
Primary structural balance	-0.7	-0.4	-0.4	0.1	0.6	0.5
Output gap	-0.8	-0.2	0.2	0.8	1.3	1.3

Source: MF SR

II.2.2. Expenditure benchmark

The expenditure benchmark serves for calculation of the possible annual growth of the adjusted expenditures[23], which should correspond to the medium-term potential economic growth[24]. The permitted rate of adjusted expenditures growth also depends on the fact whether the country has attained its medium-term objective (MTO) or not. If the MTO has not been attained, the expenditure dynamics must contribute to its attainment. Slovakia has not yet reached its MTO, and therefore the potential growth in quantifying the permitted increase in the adjusted expenditures is set to reflect the required consolidation of the structural balance.[25].

In 2016, the adjusted expenditures were growing at a lower rate than the one permitted under the expenditure benchmark (by 0.7 p.p.), which offset the negative development of the previous year. The expenditure side of the budget was also stabilized considering of the new revenue measures taken, with negative impact of 0.2 per cent of GDP.

TABLE 6 - Calculation of the compliance with expenditure benchmark (ESA 2010)*

		2015	2016	2017 OS	2018	2019	2020
Total expenditures	EUR mil.	35,692	33,684	34,686	35,175	37,277	38,859

[23] Adjusted expenditures mean the expenditures adjusted for the expenditure items outside the government's control (interest cost connected with debt financing, expenditures reacting to the economic cycle, expenditures financed from the EU funds, smoothed national investments), discretion revenue measures, and one-off impacts

[24] The expenditure benchmark presupposes unitary elasticity of revenues (1 per cent increase in the nominal GDP corresponds to 1 per cent increase in revenues). If, besides the revenues, also the expenditures are growing in line with the potential growth, the GG balance is being stabilised.

[25] The development of expenditures should contribute to the acceleration of the y/y consolidation of the structural balance at the level of 0.5 per cent GDP which is calculated in the expenditure benchmark through the so-called convergence margin to the extent of which the benchmark long-term growth rate of the economic potential is decreased.

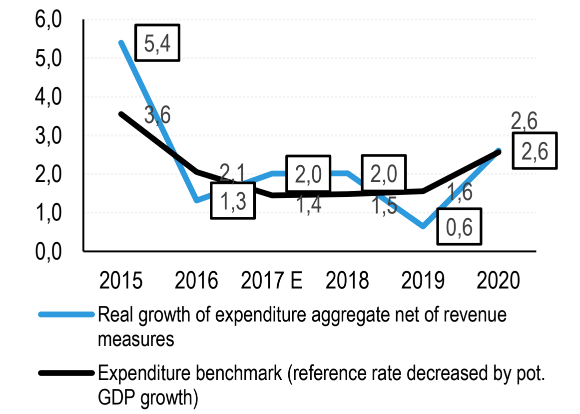
Primary expenditure aggregate	EUR mil.	**30,855**	**31,519**	**32,709**	**33,873**	**34,847**	**36,522**
Discretionary revenue measures (DRM)	EUR mil.	139	-174	184	-1	79	26
Nominal growth of aggregate expenditures after reflecting DRM	%	6.1	2.5	3.2	3.6	2.6	4.7
Real growth of the aggregate expenditures	**%**	**5.4**	**1.3**	**2.0**	**2.0**	**0.6**	**2.6**
Expenditure benchmark (reference rate)	**p.p.**	**3.6**	**2.1**	**1.4**	**1.5**	**1.6**	**2.6**
Deviation from the expenditure benchmark	p.p.	-1.8	0.7	-0.6	-0.5	0.9	0.0
One-year deviation	% GDP	**-0.7**	**0.3**	**-0.2**	**-0.2**	**0.3**	**0.0**
Two-year deviation	(% of GDP)	**0.2**	**-0.2**	**0.0**	**-0.2**	**0.1**	**0.2**

** The input data of the years 2019 and 2020 also reflect the required measures on the revenue and the expenditure sides to attain the nominal deficit targets (BOX 9). Working based on the assumption that the measures will be taken to the approximately same extent on the revenue (as discretionary revenue measures) and the expenditure side in each of the years.* *Source: MF SR*

The gradual shift of the Slovak economy to the positive phase of the economic cycle requires a more intense dampening of the expenditure growth rate from 2017, which is translated into the permitted rate of their real growth of around 1.5 per cent[26] until the MTO is reached. Taking into consideration the additional revenue measures of 0.2% GDP, the real y/y growth of aggregate expenditures in 2017 equals to 2.0 per cent, which is above the reference rate for the expenditure benchmark. This results in slight deviation over the one-year horizon, which had a neutralizing positive impact over the two-year horizon given the compliance of expenditures in 2016.

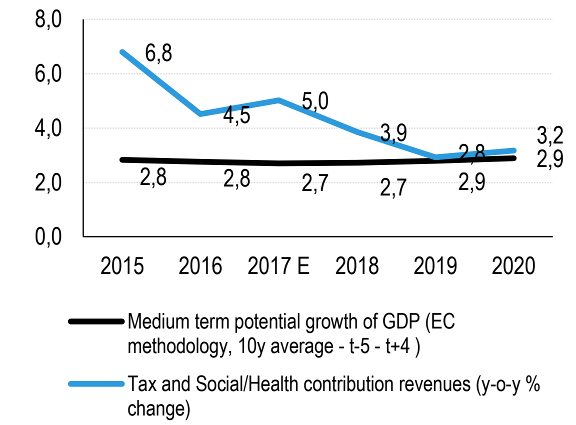
The growth of budgeted expenditures, reflecting the programme priorities of the Government and a slow beginning of EU fund drawing[27] **slightly deviates in 2018 from the reference rate, but is still in line with the requirements of the preventive part of the Pact.** After taking into consideration the measures required[28] to attain the fiscal framework objective, the compliance with the expenditure benchmark should occur both in 2019 and 2020.

CHART 15 - Development of aggregate expenditures compared to the expenditure benchmark (% growth)



Source: MF SR

CHART 16 - Development of revenues from taxes and contributions[29] compared to the potential GDP growth (% growth)



Source: MF SR

[26] The expenditure benchmark influenced by a higher convergence rate due to economy overheating which requires larger consolidation effort of the structural balance. Furthermore, the expected continued excess of revenues over the potential economic growth (chart 14) should not be used for higher expenditures based on the expenditure benchmark.

[27] Replacement of the EU funds with the domestic sources within the capital and particularly current expenditures has a negative effect on the compliance with the expenditure benchmark. The EU fund drawing has a neutral influence on public finance (after abstracting away from the cost of co-financing)

[28] 0.22 per cent of GDP in 2019 and 0.27 per cent of GDP in 2020 - additional amount of measures required to attain the objectives of the fiscal framework set.

[29] Adjusted for the change in revenues due to discretionary revenue measures and the insurance premiums paid by the state.

II.3. General government gross debt forecast

Based on the actual forecast, since 2019, the GG gross debt[30] should fall down under the very below sanction threshold of Fiscal Responsibility Act.[31] After a year-on-year decrease by 0.5 p.p., the overall GG debt reached 51.9 per cent of GDP at the end of 2016. The gross debt is expected to reach 51.1 per cent of GDP this year[32], a figure confirming gradual falling dynamics since 2013. A more noticeable decrease in the debt is expected since 2018. Once the threshold of 50 per cent of GDP is reached, the debt decreasing trend will be more significant also compared to the gradual fall of the sanction zones of the debt brake under the Act. At the end of the budgeting horizon in 2020, the debt is estimated at the level of 45.5 per cent of GDP, remaining outside the sanction zones of the debt brake.

The expected decrease in the debt in 2017-2020 is caused particularly by the rapid real growth of economy, improvement of the GG management leading towards primary surpluses[33], and gradual return of the inflation to the 2 per cent rate (CHART 17). Primary surplus of the GG is expected since 2018. Once the interest cost is deducted, the GG fiscal performance will not contribute to the nominal growth of the debt anymore. At the end of the forecasting period, the GDP growth should accelerate, bringing about a more significant debt decrease as well. Based on the forecast, the interest cost, which increase the nominal debt growth each year, should drop down to 1.1 per cent of GDP until 2020. A relatively steep slump in the debt can also be explained by the active use of the State Treasury funds to finance the government needs throughout the entire forecasting horizon.

TABLE 7 - General government gross debt (% GDP, ESA 2010, status as of 31 Dec)

	2015 S	2016 S	2017 E	2018 N	2019 N	2020 N
General government gross debt	**52.5**	**51.9**	**51.1**	**49.9**	**47.8**	**45.5**
- sovereign debt (net of international commitments)	47.4	47.1	46.5	45.7	43.9	41.9
- Slovakia's share in the EFSF facility debt	2.4	2.3	2.2	2.1	2.0	1.9
- Contribution to the ESM	0.8	0.8	0.8	0.7	0.7	0.7
- Debt of other general government entities	1.8	1.7	1.7	1.4	1.2	1.0
- p.m. change in gross debt	-1.1	-0.5	-0.8	-1.2	-2.1	-2.3
- p.m. net debt	48.2	47.0	46.7	45.5	43.3	41.1
Change of gross debt against the Stability Programme	**0.0**	**0.0**	**-0.6**	**0.0**	**-0.2**	**-0.5**
thereof: effect of GDP forecast change	0.0	0.0	0.0	-0.1	-0.1	-0.1
effect of debt forecast change	0.0	0.0	-0.6	+0.1	-0.1	-0.3

Source: MF SR

The year-on-year change in the general government debt is driven mainly by the amount of the cash deficit of the state budget[34], which needs to be financed through issuance of government debts and other financial instruments. In 2016, the positive balance of the EU flows translated into a more significant drop of the cash deficit of the state budget. Based on the expectations, the return to the 2015 levels in current year is projected, reaching the amount of nearly EUR 2 billion.

Positive impact on the debt development is also due to the overall debt decrease of the other general government entities. The fiscal framework presupposes debt reduction particularly in the case of local governments and NDS.

[30] All of the above values are calculated based on the methodology used in the assessment of the compliance with the Maastricht criterion for the general government gross debt, the so-called Maastricht general government gross public debt. The general government public debt is expressed as a debt-to-GDP ratio.
[31] Based on the Constitutional Act No. 493/2011 on Budgetary Discipline, the bottom limit of sanction zones will hit the level of 48per cent of GDP in 2019.
[32] This corresponds to the second sanction zone under the Constitutional Act No. 493/2011 on Budgetary Discipline.
[33] The primary balance means the general government balance adjusted for the interest cost.
[34] For the purposes of debt forecast, the budget objectives are expected to be attained provided that the required additional measures are taken on the state budget side.

The debt level is also influenced by the so-called methodological adjustments[35], such as the emission discount and discount at bond maturity. Since 2018, higher contribution of emission discount is expected owing to the expected increase in interest rates.

The participation of Slovakia in the European bailout mechanisms since 2012 increases the gross debt of the general government. Commitments connected with the European Financial Stability Facility (EFSF) and the European Stability Mechanism (ESM) amounted in 2017 to around 3.0 p.p. of the GG gross debt. No additional increase in these international commitments of Slovakia is expected in the period from 2018 to 2020. Other changes in the debt forecast result from the changes in the deposits of the State Treasury clients outside the general government cirlces and from the exchange rate differences based on the estimated development of individual currency pairs.

TABLE 8 - Influence on the change of the general government gross debt (EUR mil.)

	2015 S	2016 S	2017 OS	2018 N	2019 N	2020 N
A. General government gross debt (as of 1 Jan)	**40,725**	**41,295**	**42,053**	**43,244**	**44,699**	**45,561**
B. Total y/y change in the GG gross debt	**570**	**758**	**1,191**	**1,455**	**862**	**407**
- Cash-based state budget deficit	1,933	980	1,984	1,973	1,421	1,449
- State Treasury funds used for the financing of government operations	-1,262	20	-867	-453	-612	-983
- Slovakia's contributions to EFSF and ESM	-116	0	0	0	0	0
- Issue discount	18	44	89	51	171	121
- Discount at maturity	-86	-61	-63	-7	-1	-59
- Balance of loans to GG entities	24	-93	52	-110	-117	-122
thereof: ŽSR + ŽSSK	-9	32	41	7	17	18
thereof: NDS	-77	-40	69	-37	-37	-37
thereof: Municipal public transportation companies	33	-23	-3	-8	-13	-14
thereof: Local government (municipalities and higher territorial units (VÚC))	144	-62	-74	-88	-86	-83
thereof: Eximbanka	-65	3	20	0	0	0
- Other	60	-132	-5	1	0	1
C. General government gross debt (as of 31 Dec)	**41,295**	**42,053**	**43,244**	**44,699**	**45,561**	**45,968**
in % of GDP	**52.5**	**51.9**	**51.1**	**49.9**	**47.8**	**45.5**
p.m. year-on-year change of general government gross debt (p.p.)	*-1.1*	*-0.5*	*-0.8*	*-1.2*	*-2.1*	*-2.3*

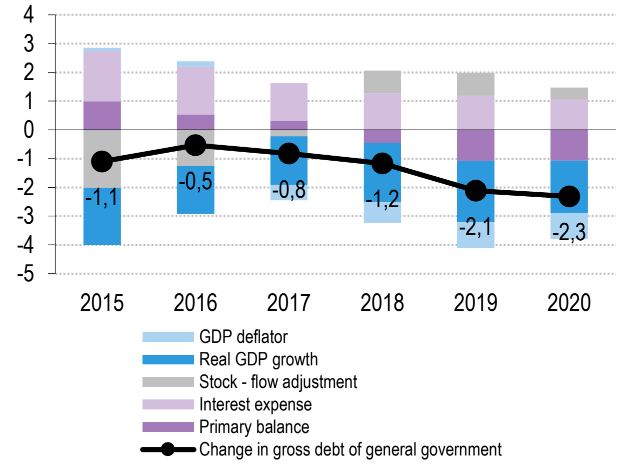
Note: Plus amounts increase the general government debt as at 31 December of the relevant year, minus amounts decrease the debt. *Source: MF SR*

The net debt[36] is expected to reach the level of 46.7 per cent of GDP in 2017. The net debt decreases by 0.3 per cent of GDP on a year-on-year basis. Whereas approximately the same level of cash reserve is expected throughout the forecasting horizon, the net debt should be on average 4.5 p.p. under the gross debt level.

[35] The discount at the government bond and treasury note emissions increases the debt whereas the liabilities of the state would grow by the nominal value of the bonds once the bonds are issued. However, the amount in cash (less the discount) that the state will gain will be lower. On the contrary, the discount at repayment of government bonds has a decreasing effect on the debt. This is because the debt is increased at the bond issue in the amount of the bond's nominal value, and not at the repayment thereof.

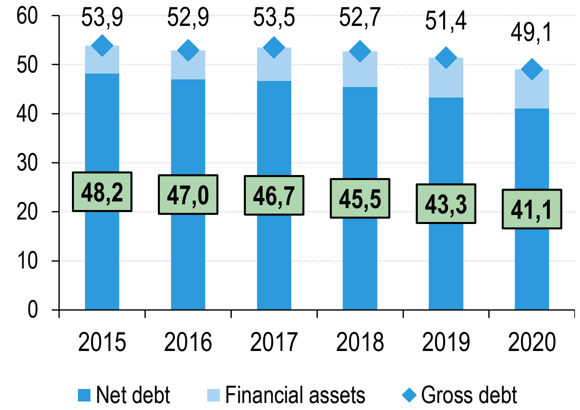
[36] At present there is no standardized methodology which would unambiguously define the quantification of net debt. The MF SR makes use of the concept of adjusting the gross debt for the liquid financial assets (LFA) including in particular the deposits in the accounts of individual general government entities. Net financial debt = Maastricht (gross) debt - gold and SDR - cash - securities - listed stock. Calculations of the net debt also take into consideration the cash in accounts of all general government entities. The general government currently does not have records of any listed stock, gold, or SDR.

CHART 17 - Contributions of factors to the gross debt change (% GDP)



Source: MF SR

CHART 18 - Net debt (% GDP)



Source: MF SR

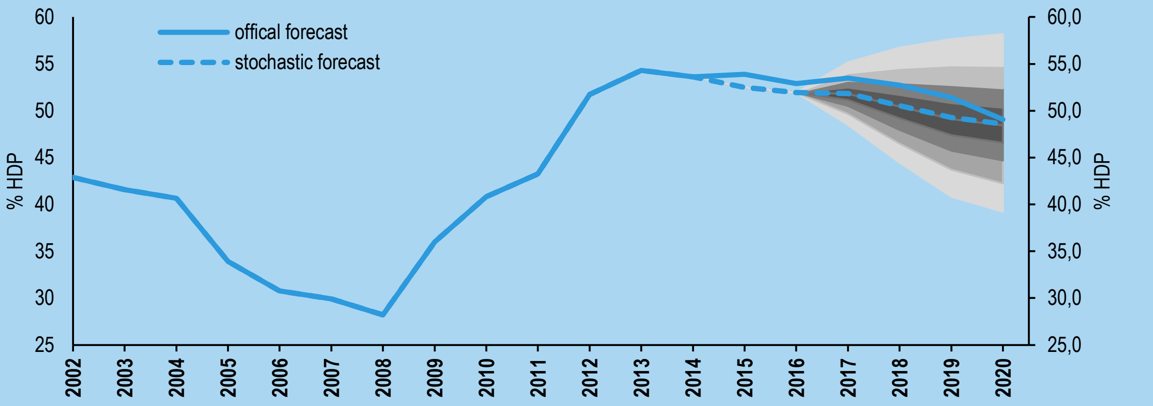
BOX 7 - Stochastic forecast of general government gross debt

The official forecast of the GG gross debt is in compliance with the independent modelling forecast (stochastic model[37]) **and it equally expects gradual decrease in the debt below the sanction zones** (CHART 19). However, compared to the assumptions from the Stability Programme, the entire trajectory of the alternative forecast is rather shifted up. This shift is mostly driven by the update of the primary balance in 2016 and the slowdown of the interest rate decrease. In 2017 and 2018, both forecasts are fully consistent. After 2019, the decrease in the debt below the official forecast is significantly faster. There is a 60 per cent probability that the debt would fall under the 50 per cent threshold until 2020, which is lower than the expectation used in the Stability Programme. Equally, the probability of achieving the planned debt level until the end of the monitored period has decreased.

The primary advantage of such an approach is the lower demand on input assumptions. It provides an independent source of debt estimate as well as quantification of the forecast risks. On the other hand, this approach is limited by the fact that it only takes into account a limited amount of information and presumes that interactions among the components of the model will be the same during the forecasted period as they were in the past. The fan chart graphically illustrates a large number[38] of random simulations of debt level on the horizon of the forecast generated in the stochastic model. The methodology of the estimate is provided in the Draft Budgetary Plan for 2016[39].

CHART 19 - Stochastic debt forecast (% GDP)

[37] The simulated level of debt is determined by its past value, interest expense, GDP growth, primary deficit and non-deficit financing. The model comprises a vector autoregression of interest rates, growth of real GDP, inflation of GDP deflator, of these three variables for the EU and exchange rate. Another component includes the fiscal response function which determines the level of primary deficit with regard to the debt and economic activities. High number of random simulations of this system of models determines various debt trajectories based on which probability distribution of the level of debt in future years is subsequently calculated.
[38] 5,000 random debt trajectories were simulated.
[39] http://www.finance.gov.sk/Components/CategoryDocuments/s_LoadDocument.aspx?categoryId=9307&documentId=13676.



Source: MF SR

BOX 8 - Impact of positive risks from GDP revision on fiscal indicators

For the purpose of the autumn Eurostat deficit and debt notification, the Statistic Office of the Slovak Republic (SO SR) performed the regular backward revision of national accounts**. The revision is expected to increase the GDP in 2014 - 2016 by 0.2 per cent on average compared to the assumptions of the September 2017 official forecast of the Macroeconomic Forecasting Committee (Committee). The forecast (of the Committee) for nominal GDP growths in 2017 – 2020 can be used as the basis for chaining the year-on-year changes to make time line referring to a new level of the GDP historical line.**

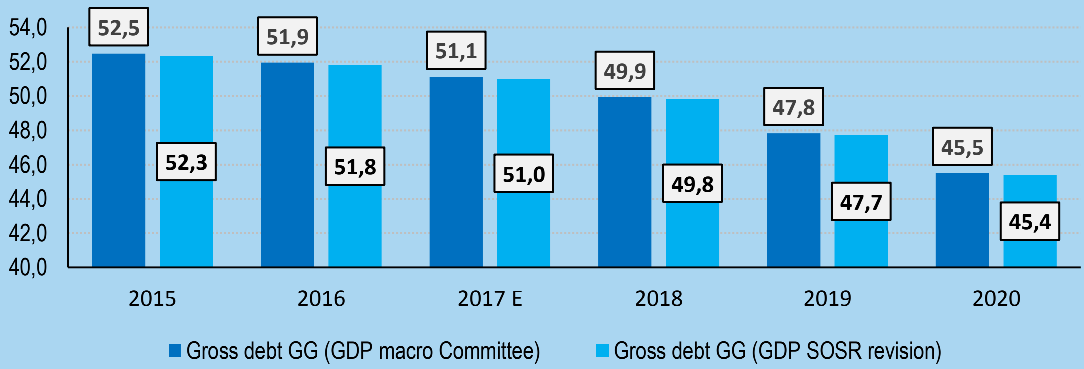
TABLE 9 - GDP revision (EUR bn.)

	2014	2015	2016	2017	2018	2019	2020
GDP Forecast - Committee, September 2016	75.9	78.7	81.0	84.6	89.5	95.3	101.0
GDP - revision SO SR	76.1	78.9	81.2	-	-	-	-
GDP - revision SO SR + Committee forecast	**76.1**	**78.9**	**81.2**	**84.8**	**89.7**	**95.5**	**101.3**
Difference	*0.1*	*0.2*	*0.2*	*0.2*	*0.2*	*0.2*	*0.2*

Source: SO SR, MF SR

The actual GDP revision represents a small positive impact on the fiscal indicators which are expressed as a ratio to GDP (e.g. balance, or general government gross debt). Whereas the budget planning process requires publication of new data by the SO SR and its confirmation in the Committee forecast, the revised GDP could not have been considered either in the General Government Budget or in the Draft Budgetary Plan. Considering the size of the balance to GDP ratio, its revision will decrease its size only insignificantly. In the case of both the gross and net debt, the impact is more noticeable (approx. -0.1 p.p.).

CHART 20 - Change of the gross debt per cent of GDP)



Source: MF SR

II.4. Revenue and expenditure targets of the general government budget

Assuming no changes took place in economic policies in 2017, the general government deficit would reach moderate surplus (0.1% of GDP) in 2018. Compared to the no-policy-change scenario, the general government deficit for the year 2017 is higher by 0.9% GDP (EUR 791 million)in the budget proposal, exclusively owing to the incentive on the expenditure side of the budget (1.05 % of the GDP). The consolidation measures and the additional non-tax revenues (0.17% GDP) partly compensate the size of the expenditure incentive. In 2019 and 2020 in the no-policy-change scenario the general government balance would result in 0.2 or 0.6% GDP. Combating tax evasion remains the priority of the Slovak government in the area of taxes.

The budget policy in the coming years is based on the Manifesto of the Government of the Slovak Republic and focuses on gradual improvement of the budgetary position of the general government, aiming at long-term sustainability of public finance. The general government deficit target for 2018 has been set at the level of 0.83% GDP. The general government budget deficit proposed for 2019 reaches 0.10% GDP and a balanced budget for 2020. From the perspective of the compliance with the Stability and Growth Pact rules, the new objectives are in ex-ante compliance with the requirements of consolidation of the European Commission which will publish the assessment of the Draft Budgetary Plan in November 2017.

The y/y decrease in the general government deficit by 0.8% GDP in 2018 is explained particularly by the decrease in capital expenditures and expenditures on intermediate consumption. While the total general government revenues after adjustment for the effect of the EU funds would show the y/y growth approximately in compliance with the growth of the nominal GDP, the expenditure side of the Proposed Budget in 2018 counts on non-recurrence of multiple one-off and temporary expenditures from 2017 (more in BOX 10). The y/y slump (after adjustment for the EU fund effect) is reported mainly by the capital expenditures in the case of NDS, ŽSR and the municipalities. The decrease in the nominal deficit is also supported by the growing economic performance[40] and the lower expenditures, on a y/y basis, on co-financing from the EU sources.

II.4.1. Revenue targets of the general government budget

In Slovakia, the general government revenues to GDP ratio is below the reference values on the long term basis, i.e. the Euro area average and the V3 average. However, thanks to the successful combating tax evasions and the measures adopted since 2013, general government revenues have converged to both reference average figures over the horizon of the last four years (CHART 21). The year 2015 is a specific exception when the more significant growth of revenues was caused by an accelerated drawing down of the EU funds from the second programming period. In spite of partial convergence, Slovakia continues to have the lowest ratio of tax and social security revenues (hereinafter as tax revenues)[41] to GDP compared to the V4 average and the Euro area average.

Based on the fiscal framework, the total revenues should have a moderate falling trend from 2017 down to the level of 38.3% GDP in 2020. The decrease in revenues compared to the economy ratio is visible both in the case of non-tax and tax revenues, only their contributions differ in individual years. While the decrease of the GG revenues to GDP in 2018 is fully explained by the slump of grants and transfers connected with the expected slower drawing down of the EU funds, in 2019 also the taxes to GDP are expected to fall down owing to a slower development of the macroeconomic bases compared to the economic performance.

[40] The nominal GDP growth results in the growth of revenues approximately to the same extent, while a large part of expenditures in the budget is budgeted based on a slower rate of inflation growth or wage growth.

[41] Hereinafter in the text of tax revenues only, it corresponds to the summation of the ESA items (D.2REC+D.5REC+D.61REC+D.995REC).

CHART 21 - Comparison of development in general government revenues (% GDP)

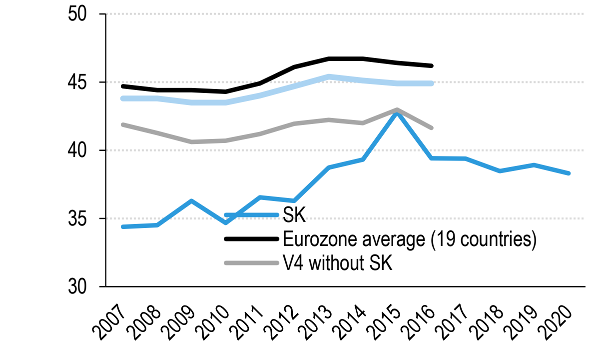
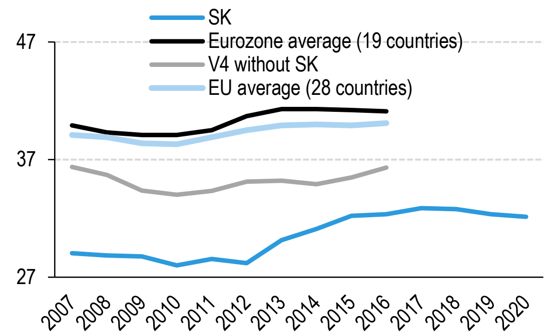


CHART 22 - Comparison of development in general government taxes and contributions (% GDP)



Source: Eurostat, MF

SR

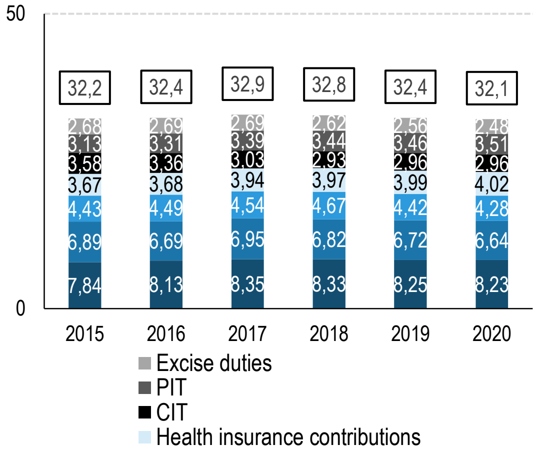
The general government tax revenues to GDP ratio should reach 32.9% in 2017, growing on a y/y basis by 0.5% GDP. The y/y growth of tax to economy performance ratio can be explained by the continuing growth of the VAT collection (0.3% GDP), the adopted legislative changes (0.2% GDP)[42], more positive development of social security contributions than the one indicated by the trend in the labour market and, on the contrary, the potentially higher growth was held back the y/y slump of corporate tax.

In the coming years, the tax to economy performance ratio will slightly fall, reaching the level of 32.1% GDP in 2020 (CHART 23**).** The fiscal framework presupposes a moderate growth in the individual income taxes to GDP ratio, a consequence of the real growth of wages which is not reflected in the adjustment of tax allowances. Stable development in relation to the economy over the entire forecasting horizon is also expected in the case of health and social security contributions[43] whereas the wage base has been growing nearly identically with the GDP development. Except for 2018 which should reflect cancellation of the minimum tax (tax license) in the corporate tax revenue, corporate tax revenue should be stable. A slow down the household consumption compared to the economy growth is releflected in relative decrease of value added tax reveneus. The non-existence of automatic indexing of a part of tax revenues (real estate taxes, selected excise taxes, administrative fees, and other revenues) causes erosion of their yield to GDP ratio in the remaining forecasting years.

[42] The y/y positive effects on the development of taxes and social security contributions: (cancellation of the maximum assessment base (MAB) for the health contributions, increase in the MAB for the social security contributions, increase in the tobacco excise tax, increase in the special levy in regulated sectors, increase in the levy on gambling industry, introduction of the levy on the non-life insurance policies. On the other hand, changes in higher lump-sum allowance for self-employed and the decrease in the corporate income tax have a compensatory effect.

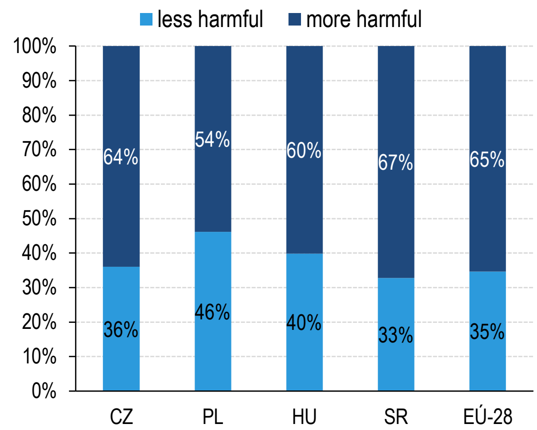
[43] The development of the social security contributions in relation to the economy performance (moderate decrease at the end of the forecast) results in gradual increase in the rate of the contributions to the second pillar pension plan from 2017; the existence of maximum caps and minimum contributions which logically prevent full transformation of the wage base growth into the revenue from the social contributions.

CHART 23 - Tax to GDP ratio (% GDP)



Source: MF SR

CHART 24 - Tax mix based on the impact of individual taxes on the economic potential (% of the tax revenues)[44]



Source: MF SR

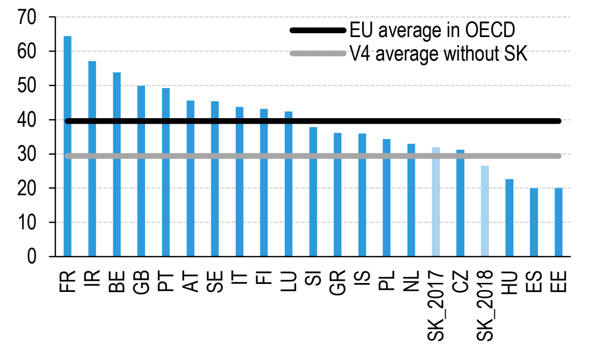
[44] Property taxes (real estate tax), excise taxes, and the environmental taxes are considered to be less harmful from the perspective of the economic growth. OECD (2010), Tax Policy Reform and Economic Growth, OECD Tax Policy Studies, No. 20, OECD.

II.4.2. Competitiveness of the Slovak tax system

Slovakia is a small open economy and its potential growth depends on the right tax mix which would be supportive and motivating for the inflow of direct foreign investments. Tax mix should be looked at through the effect of individual taxes on the economic growth. In this context, stable tax ratio from the perspective of its impact on the economic growth is expected over the horizon of the fiscal framework[45]. The tax mix offers opportunities for increasing the proportion of less harmful taxes, which would have a positive influence on the potential performance of the Slovak economy in future (CHART 24).

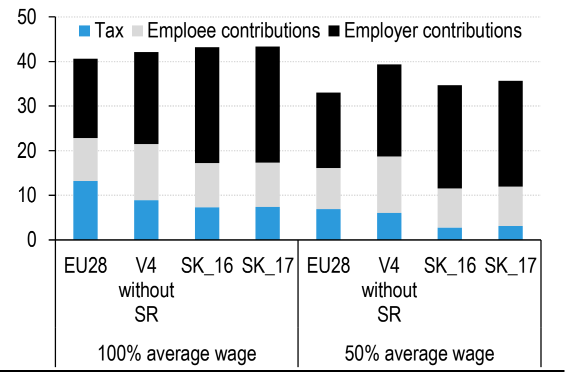
When it comes to the attractiveness for potential investors, the efficient taxation of labour and profit in the relevant country is the most important. Multiple tax measures were taken in the area of labour and capital taxation throughout the last year. These measures will take effect in 2017 (decrease in the corporate income tax) or in 2018 (changes in dividend taxation or cancellation of the tax license). Changes in the dividend taxation will decrease the effective taxation compared to the legislation valid until 2017 and will even drop under the taxation level in the neighbouring V4 countries, except for Hungary (CHART 25). Changes in the social and health contributions (cancellation of the maximum assessment base or its increase from the quintuple to the septuple of the average wage) will contribute to the greater progressiveness of the tax system, but will not influence the tax burden of the employees earning average wage and the low-income workers. Moderate increase in the burden of the low-income worker (50% of the average wage) is connected with non-indexing the tax deductible item in the health insurance contribution allowance (CHART 26).

CHART 25 - Efficient taxation of dividends in the EÚ (2017, 2018 and SR, in %)



Source: MF SR

CHART 26 - Tax wedge, individual, income 50% and 100% of average wage in 2016 (in % of the labour cost)



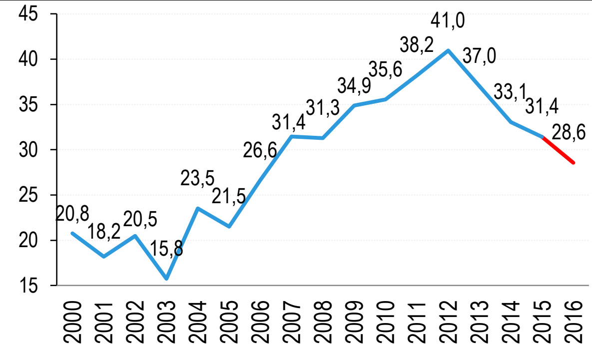
Source: MF SR

II.4.3. Combating tax evasions

Combating tax evasion remains the key priority of the Slovak government. The primary effort was focused on combating VAT evasions. The measures from the three-phase action plan adopted during 2012 - 2016 helped to turn around the long-term adverse results of VAT collection (CHART 27). This is also supported by the decrease in the VAT gap which fell from 41.0 % to 28.6 % from 2012 to 2016. For 2016, we estimate that the additional benefit from the improved VAT collection resulting from implementation of the measures to combat tax evasions equal to 1.2% GDP compared to 2012. Cumulatively from 2012 until the end of 2016, the improved VAT collection brought additional revenues in the amount of 3.1% GDP, corresponding to EUR 2 bn.

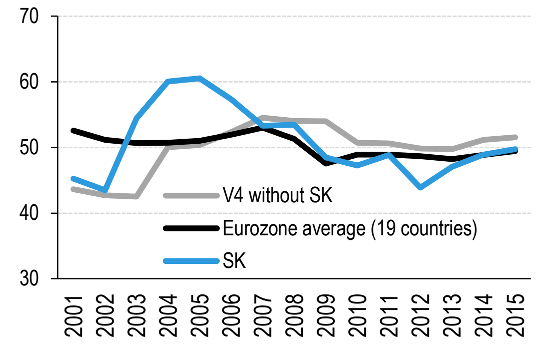
[45] Simply, less harmful taxes as a sum of the ESA items (D.2+D.59A).

CHART 27 - VAT gap (% potential revenue)



Source: MF SR

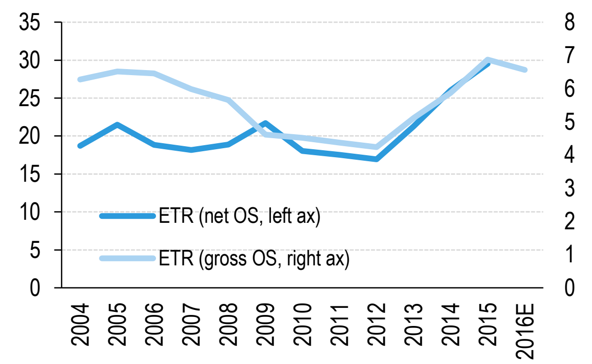
CHART 28 - VAT collection efficiency indicator[46] (in %)



Source: MF SR

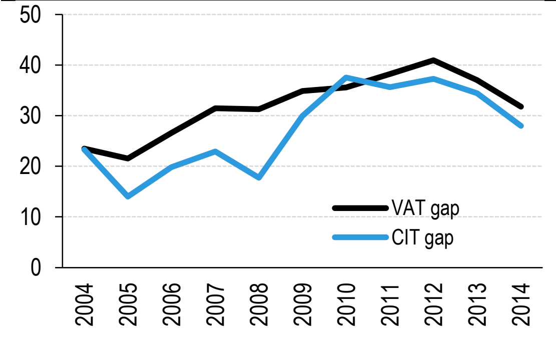
The efficient corporate income tax rate has been growing at a record rapid rate in recent years (Chart 29), which may be, in addition to the procyclical nature of this tax[47], also attributed to the successful VAT measures which translate into the corporate income tax revenues. Striving to reach better understanding of how the development of the efficient corporate income tax rate is supported by the tax evasion prevention, the MF SR in cooperation with the IMF have rolled out the pilot project of the corporate income tax gap estimate. The preliminary results of the corporate tax gap estimate (**Chart 30**) confirm the initial assumption of the MF SR that the measures focused on combating VAT evasions are directly proportional to the development of the collection of the tax paid by corporations.

CHART 29- Effective corporate income tax rate (tax collected from the net and gross operational surplus)



Source: MF SR

CHART 30 - Comparison of the VAT and corporate income tax gap development[48] (% potential revenue)



Source: IMF's RA-GAP

The efforts of the Financial Authority of SR (FA SR) concentrates on the excise taxes which is, **after the previous decrease spanning over several years, supported also by the stabilisation of the mineral oil excise tax gap** (see DBP 2017).

[46] The so-called VAT C-efficiency represents the ratio of the collected VAT to the nominal consumption multiplied by the VAT base rate. It expresses the efficiency of the VAT collection in the broader sense of the word, including also the size of existing exceptions, allowances, and decreased rates in the value added taxation in the country (i.e. also influenced by the so-called policy gap). The indicator compares the actual VAT collection against the potential VAT collection if the entire consumption in the economy would be subject to the base rate.

[47] The corporate income tax elasticity trend compared to the macroeconomic base is procyclical, in the years after the financial crisis the efficient tax rate has been falling down also due to accumulated losses.

[48] The preliminary calculation of the tax gap in the corporate tax based on the International Monetary Fund (IMF) methodology, actual joint project of IFP and IMF results of which will be published in the course of this year) using the "top-down" estimating approach.

New measures adopted to combat tax evasions (2017 summary and measures adopted by the Government for 2018)

Effective as of 2017, further measures focusing on combating tax evasion have been adopted based on the Action Plan update. Complying with the challenges and recommendations identified by the EC, the FA SR will continue to support the improvement of business environment, voluntary compliance with tax obligations, and decrease in the administrative burden of clients supporting two-way electronic communication, improving the efficiency of the Call Centre services, and sending pre-filled tax returns for the selected types of taxes.

The FA SR has been improving its processes for a more efficient collection of taxes aiming to make simpler and easier the compliance with tax obligations for the taxpayers. Improvement of the collection of arrears is driven by the new tax debtor risk assessment system aiming at obtaining information for distraint officers in a single point and accelerating debt collection process. Cooperating with the Slovak Banking Association, the FA SR is working on the implementation of the two-way electronic communication of distraint officers by way of direct collection of arrears from the accounts of tax entities. The 2nd stage of automation of the customs surveillance over import of goods by e-DOVOZ system is being finalized. A "soft warning" concept has been implemented; automation of this concept is planned within the second stage, aiming to warn tax entities of a suspicion of their involvement in a fraud, and the need of payment of arrears, and of the option to file a subsequent tax return. An **interdepartmental analytical centre** dealing with financial crimes will be set up in cooperation with other general government departments until the end of 2018, and this centre will actively cooperate in the preparation of drafts of legislative changes to prevent tax frauds.

Important changes will take place effective as of the next year (2018) under the amendment act on tax administration which reforms and releases, in a fundamental manner, the tax secrecy, introduces the tax reliability index, and other measures in the tax evasion fight. Within improvement of tax transparency, the Financial Directorate will, observing the rights and maintaining the minimum protection standard of taxpayers of SR, publish lists of tax entities disclosing the amount of tax claimed and the tax liability reported by them. These lists make the public more informed, which may lead to improved transparency of the business environment and, at the end of the day, they may help in the fight against tax evasion. The tax reliability index constitutes an instrument for objective, independent, and lawful assessment of tax entities the Financial Authority would use internally to "grade" corporations based on how they meet their tax liabilities. This measure should be particularly of a preventive nature and motivational elements are being prepared for the entities which would meet their liabilities in time and in a due manner.

Changes within the fight against tax evasions include changes in the mineral oil excise tax in response to the knowledge obtained by the FA SR about the fraud in this area. The law makes the conditions for traders in mineral oils stricter and stipulates the option to suspend business in the event of a suspicion that the entity violates tax and customs regulations.

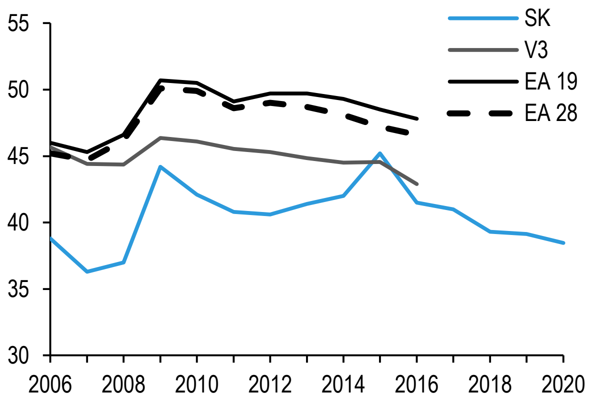
The Government passed an amendment act to the Income Tax Act, continuing in the coming year in the implementation of the measures against tax evasion, paying more attention to the support of innovations, and making more attractive the conditions in the area of spa business. In accordance with the obligations stemming from the transposition of the Directive (EU) 2016 of the Council, the governmental draft act lays down further rules to reinforce the protection against aggressive tax planning and the base erosion and profit shifting (BEPS) outside Slovakia (e.g. the rules for the controlled foreign corporations, for property taxation shifting, hybrid mismatch arrangements, etc.).

II.4.4. Expenditure targets of the general government budget by function[49]

In Slovakia, the general government total expenditures to GDP ratio has been below the reference values, i.e., the Euro area average and the V3 average. In recent years, however, the general government expenditures has converged to the two reference average values. Large growth in 2015 was driven by excessive drawing from the EU funds from the second programming period allocation. Last year, the expenditures reached the 2013 level again. Slovakia remains one of the European countries with a lower public spending to GDP ratio when compared to the average. The accelerated drawing of the EU funds in Slovakia and in V3 countries resulted in a strong increase of the public capital investments in 2014 and 2015, which did not recur in 2016.

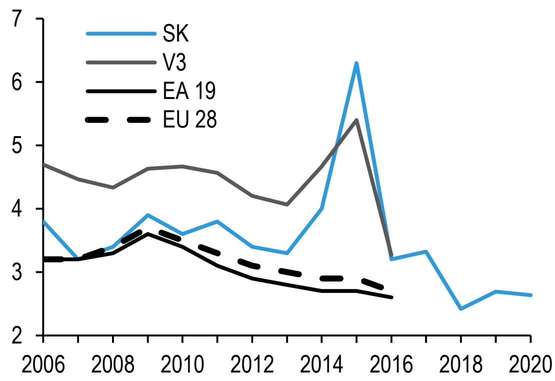
Despite the growth of the nominal public spending, its ratio to GDP follows a decreasing path over the horizon. The growth of the nominal GDP will outpace the expenditure growth in spite of multiple measures on the expenditure side. Expected lower drawing from the EU funds allocated for the third programming period also affects the level of the estimated capital expenditures.

CHART 31 - Development of the general government expenditures (% GDP)



Source: Eurostat

CHART 32 - Development of the general government capital expenditures (% GDP)



Source: Eurostat

International comparison of the spending structure by function[50] to other V4 countries reveals that Slovakia spends less on education, economic affairs and the general public services areas. Compared to the average of the other V4 countries (and also to the EU average), the expenditure to GDP ratio is higher in the healthcare system and in the public order and safety areas. When compared to the EU average, the largest difference is observed in the ratio of the expenditures set aside for the social security area. The reason behind this is relatively lower expenditures on the long-term care and other social services[51] and also on the transfers targeted to help the unemployed.

TABLE 10 - General government expenditures according to the COFOG classification

Functions	COFOG	SK 2017 (ED)		SK 2018 (GGB)		V3 (2015)		EU 28 (2015)	
		% GDP	% TE	% GDP	% TE	% GDP	% TE	% GDP	% TE
1. General public services	1	5.4	13.2	5.1	13.0	6.0	13.6	6.2	13.1
2. Defence	2	1.1	2.7	1.1	2.9	1.0	2.2	1.4	3.0
3. Public order and safety	3	2.2	5.3	2.1	5.2	2.0	4.6	1.8	3.8
4. Economic area	4	4.4	10.7	3.6	9.1	6.6	14.8	4.3	9.1

[49] Note: The methodology of data recording based on functional classification can vary from country to country. As a result, different data can enter the same category in different countries (e.g. taxed and non-taxed pensions). COFOG classification also doesn't take into account expenditure realized through the tax system (e.g. child benefits).

[50] The most recent available data for the COFOG date to 2015.

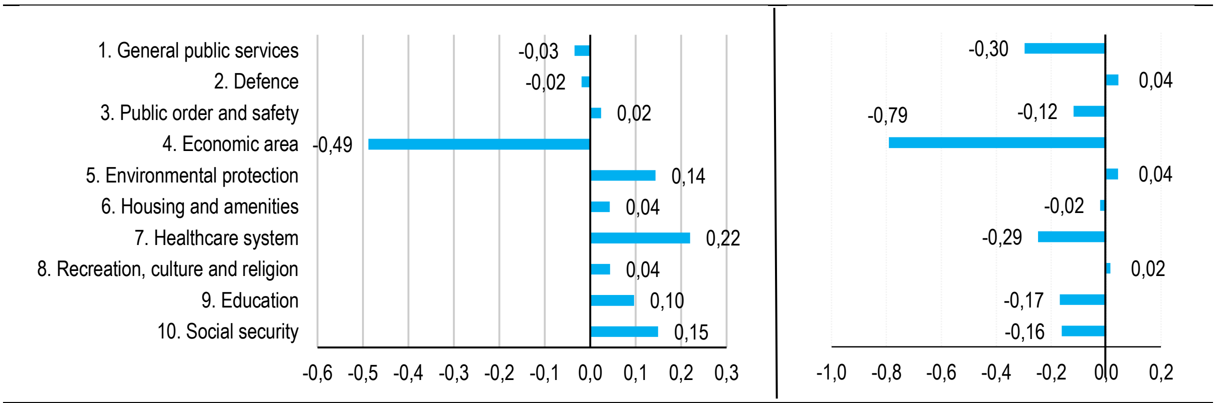
[51] E.g. care for children, people in crisis.

5. Environmental protection	5	0.6	1.4	0.6	1.6	1.0	2.2	0.8	1.7
6. Housing and amenities	6	0.5	1.2	0.5	1.2	0.8	1.9	0.6	1.3
7. Healthcare system	7	7.6	18.4	7.3	18.6	5.9	13.2	7.2	15.3
8. Recreation, culture and religion	8	1.0	2.5	1.0	2.7	1.5	3.4	1.0	2.1
9. Education	9	4.1	10.0	3.9	10.0	5.1	11.5	4.9	10.4
10. Social security	10	14.2	34.5	14.0	35.6	14.5	32.7	19.2	40.7
Total expenditures	**TE**	**41.0**	**100.0**	**39.3**	**100**	**44.5**	**100**	**47.2**	**100**

Note: TEGG - Total expenditure

Based on the expected realized values for 2017, the public spending is moderately higher with respect to the approved budget. The increase is noticeable particularly in the healthcare system, the social security and the environmental protection areas. Higher revenues from healthcare and social security contributions resulting from better labour market performance are associated with higher expenditures in the healthcare and the social security system areas[52]. In the environmental protection area, the expenditures have risen due to relocation of JAVYS to the general government sector while the approved bugdet had not accounted for this change. Lower expenditures in the economic area are observed due to slower drawing of the EU funds. Other areas do not reveal substantial differences when compared to the 2017 approved budget.

CHART 33 - Comparison of general government expenditures according to the COFOG classification (changes in p.p. GDP)



Note: RVS - General government budget (approved by the Parliament), ERV - expected realised value *Source: MF SR*

The expenditures to GDP ratio linked to the 2018 budget is lower than the 2017 ERV due to faster growth of GDP which outpaces the growth in nominal expenditures. These expenditures increased due to the social security, health care and defence areas. The expenditures for social security grows in relation to minimal pension valorisation, recalculation of pensions granted before 2004, higher transfers to organisations providing social services, increased transfer for people taking care of disabled other legislation measures. Nominal expenditures on healthcare grows at half of the rate observed during the last years. The increase in the defence expenditures is driven by the planned modernisation of army. The expenditures on the economic area drops both in nominal terms and also as a ratio to GDP due to slowdown in tge EU fund drawing, lower capital expenditures of state-owned enterprises (NDS, ŽSSK, ŽSR) and lower subsidies in the agriculture sector.

[52] From May 2017, the maternity benefit is increased to 75% of the gross wage, which is also reflected in higher expenditures on sick benefits (EUR 22.6 mil.). Higher expenditures associated with unemployment benefits are also expected (+EUR 19.8 mil.) .

II.5. General government balance under the no-policy-change scenario

The no-policy-change (NPC)[53] scenario, defined as a development of public finance under the assumption of no amendments to legislature and updating the estimated macroeconomic development, quantifies the size of measures necessary to meet the budget objectives. The size of necessary measures (the fiscal scope) to meet the budget objectives can be quantified by comparing the general government balance in the NPC scenario compared to the budget objective. Based on the NPC, it is also possible to assess the size of the measures (consolidation or incentive) necessary to reach budgetary objectives. The starting point for development of a no-policy-change scenario for 2018-2020 is the expected deficit of the general government in 2017 in the amount of 1.63% GDP

Provided that there are no changes in the economic policies, in 2018 the general government deficit would reach a slight surplus at the level of 0.05% GDP (compared to the budget objective of 0.83% GD). The surplus in the no-policy-change scenario would gradually grow in 2019 and 2020 as well.

The difference in the general government balance between the NPC scenario and the draft budget for 2018 equals to 0.88% GDP (EUR 792 mil.). The expenditure side includes a total difference amounting to 1.05% GDP, which resulted from the increase in both current (0.71% GDP) and capital expenditures (0.34% GDP). As to the current expenditures, these include in particular, development within intermediate consumption (0.18% GDP) and compensations for employees (0.20% GDP) and pension benefits (0.16% GDP). On the revenue side, there is a consolidation compared to NPC at the level of 0.17% GDP, which partly offsets the fiscal expansion in expenditures.

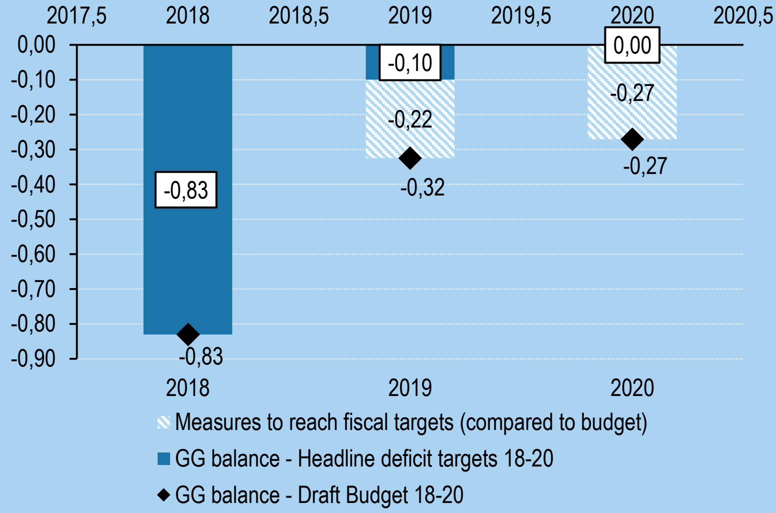
The continuing incentive on the expenditure side in 2019 and 2020 exceeds the measures taken by the Government on the revenue side. Compared to the no-policy-change scenario, the fiscal framework on the 2018 - 2019 horizon assumes mainly growing employee compensations and pension benefits, which will be to certain extent set-off by lower transfers for healthcare. The intermediate consumption is expected to grow faster again in 2020 compared to the NPC scenario[54].

BOX 9 - Required measures to attain the planned objectives in the GG Draft Budget for 2018-2020

Budgeted deficits in the General Government Draft Budget are at the level of 0.32% GDP and 0.27% GDP in 2019 and 2020, respectively, levels moderately above the planned budget objectives. In order to attain the planned deficits at the level of 0.1 or 0% GDP, additional measures amounting to 0.22 or 0.27% GDP will have to be specified in 2019 and 2020 in excess of the budget. The no-policy-change scenario (just like other analytical indicators in the actual Draft Budgetary Plan for 2018) works consistently on the assumption that the measures required to attain the budget objectives would be implemented on both the revenue and the expenditure side to the approximately the same extent in each of the years.

CHART 34 – Comparison of deficits in the General Government Draft Budget and the fiscal objectives set

[53] The manual for the development of the NPC scenario is published on the Ministry of Finance's website: http://www.finance.gov.sk/Default.aspx?CatID=9301.



Source: MF SR

TABLE 11: Comparison between the balance of expenditures and revenues and the NPC in 2018 - 2020 (% GDP)

		NPC			GGB			GGB-NPC		
	ESA code	**2018**	**2019**	**2020**	**2018**	**2019**	**2020**	**2018**	**2019**	**2020**
Total revenues	**TR**	**38.3**	**38.8**	**38.2**	**38.5**	**39,0****	**38,5****	**0.2**	**0.2**	**0.3**
Taxes on production and imports	D.2	10.8	10.6	10.4	11.0	10.7	10.5	0.1	0.1	0.1
Current taxes on income, wealth	D.5	7.2	7.1	7.2	7.1	7.1	7.1	0.0	0.0	0.0
Capital taxes	D.91	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Social security contributions	D.61	14.6	14.4	14.4	14.6	14.5	14.5	0.1	0.1	0.1
Property income	D.4R	0.6	0.6	0.6	0.6	0.6	0.6	0.0	0.0	0.0
Other (1)		5.1	6.0	5.7	5.1	6.0	5.6	0.0	-0.1	-0.1
Required measures*		-	0.0	0.0	-	0.1	0.2	-	0.1	0.2
Tax burden (2)		32.6	32.2	32.0	32.8	32.5	32.3	0.2	0.3	0.3
Total expenditure	**TE**	**38.3**	**38.6**	**37.7**	**39.3**	**39,1****	**38,5****	**1.1**	**0.5**	**0.8**
Compensations for employees	D.1P	8.9	8.9	8.8	9.1	9.2	9.0	0.2	0.3	0.2
Intermediate consumption	P.2	5.3	5.2	4.9	5.5	5.2	5.2	0.2	0.0	0.3
Subsidies	D.3P	0.4	0.4	0.4	0.4	0.4	0.4	0.0	0.0	0.0
Interest cost	D.41P	1.3	1.2	1.1	1.3	1.2	1.1	0.0	0.0	0.0
Total social transfers	D.6P D632	18.1	17.7	17.3	18.3	18.0	17.6	0.2	0.3	0.3
thereof: Unemployment benefits		0.2	0.2	0.1	0.2	0.2	0.1	0.0	0.0	0.0
Gross fixed capital generation	P.51G	2.2	2.7	2.6	2.4	2.7	2.6	0.2	0.0	0.0
Capital transfers	D.9P	0.2	0.2	0.2	0.3	0.2	0.2	0.1	0.0	0.0
Other (3)		1.9	2.3	2.4	2.0	2.3	2.5	0.2	0.0	0.1
Required measures*		-	0.0	0.0	-	-0.1	-0.1	-	-0.1	-0.1
General government balance (4)	**B.9 (4)**	**0.05**	**0.17**	**0.56**	**-0.83**	**-0,10****	**0,00****	**-0.88**	**-0.27**	**-0.56**

Note: (1) P.11+P.12+P131+D.39rec+D.7rec+D.9rec (other than D.91rec) *Source: MF SR*

(2) D.2+D.5+D.61+D.91

(3) D.29p+D.5p+D.7p+NP

** not included in the GGB for 2018 - 2020*

*** GG balance after figuring in the required measures to attain the objective*

II.6. Description of measures

The following section quantifies and describes the effects of measures incorporated into the general government draft budget. The items above the scope of specified measures include differences between the NPC scenario and the results of budgeting negotiations included in the Draft Budget.

TABLE 12 - Measures included in the draft general government budget (ESA 2010, compared to NPC)

Revenues	Subsector	ESA2010	2018	2019	2020
Total tax revenues	**S. 13**		**0.21**	**0.30**	**0.33**
Taxes on production	S. 13	D.2	0.14	0.12	0.11
Income taxes	S. 13	D.5	-0.01	-0.01	-0.02
Revenues from fees and charges	S. 13	D.61	0.08	0.08	0.08
Total non-tax revenues	S.13	P.11+P.12	0.12	0.04	-0.02
Grants and transfers	S.13		-0.16	-0.11	-0.06
Required revenue measures*	S.13			0.11	0.16
Total revenues			**0.17**	**0.23**	**0.26**
Expenditures					
Compensations - thereof:	**S.13**	**D.1**	**-0.20**	**-0.29**	**-0.21**
Adjustment of wages of teachers and GG employees			-0.24	-0.30	-0.38
Allowance for work during weekends and on public holiday			-0.01	-0.02	-0.02
Intermediate consumption - thereof:	**S.13**	**P.2**	**-0.18**	**0.08**	**-0.25**
Provisions for worsening tax and non-tax revenues			-0.16	-0.00	-0.00
Subsidies	**S.13**	**D.3p**	**0.01**	**0.01**	**0.01**
Social transfers - thereof	**S.13**	**D.62p**	**-0.23**	**-0.28**	**-0.30**
Minimum pension adjustments and other effects of the amendment act 461/2003	S.1311		-0.10	-0.12	-0.15
Adjustment of pensions granted before 2004	S.1311		-0.06	-0.05	-0.04
Increased care allowance	S.1311		-0.02	-0.06	-0.06
Higher payments of the state for social services	S.1311		-0.05	-0.05	-0.04
Natural social transfers	**S.13**	**D.632**	**0.03**	**0.01**	**0.01**
Amendment act to Act 363/2011 on the Reimbursement of Drugs (innovative drugs)	**S.1314**		0.03	-0.01	-0.02
Other current transfers, thereof	**S.13**		**-0.14**	**-0.10**	**-0.13**
Provision for the 13th and 14th salary and the exemption of income from agreements of pensioners			-0.06	-0.05	-0.05
Capital expenditures, thereof	**S.13**		**-0.34**	**-0.04**	**-0.05**
National Football Stadium	S.1311	P.51g	-0.07	-0.01	-0.00
Higher expenditures on defence modernisation	S.1311	P.51g	-0.10	-0.10	-0.40
Transport modernisation	S.1311	P.51g	-0.10	-0.00	-0.00
SNG reconstruction	S.1311	P.51g	-0.03	-0.00	-0.00
Provision for significant investments	S.1311	P.51g/D.9p	-0.18	-0.05	-0.04
Required expenditure measures*	S.13		-	0.11	0.11
Total expenditures			**-1.05**	**-0.51**	**-0.82**

Note: (+) increase in revenues and decrease in expenditures *Source: MF SR*

**not included in the GGB 2018 – 2020*

Revenue measures

The revenue side of the budget is being consolidated over the horizon, reaching the level of 0.17% to 0.26% GDP. The 2018 yield from tax revenues will show the effect of amendment acts to tax acts (see below) being prepared and passed by the Government. Measures on the side of contributions include the increased payments of the state for social services, a measure taken to the same extent as the measure on the expenditure side. The higher non-tax revenues which have been gradually decreasing over the budgeting horizon are connected with the growth of receipts of healthcare facilities compared to the corresponding index in the NPC scenario. Lower grants of municipalities in relation to the NPC scenario compensate the consolidation on the revenue side.

Measures approved by the Tax Forecasting Committee and incorporated into the GGB

The Government passed an amendment act to the Income Tax Act (595/2003 Coll.), continuing in the coming year to implement measures against tax evasion, paying more attention to the support of innovations, and making more attractive the conditions in the area of spa business. The implementation of rules to reinforce protection against aggressive tax planning and the rules against tax base erosion and profit shifting (BEPS) outside the territory of the Slovak Republic (e.g. it introduces the rules for controlled foreign corporations (CFC), for property taxation shifting, hybrid mismatch arrangements, etc.) constitute a positive, non-quantified risk for the budget.

- **Increased deduction of the cost of research and development (Act No. 595/2003)**

  The additional deduction of the cost of research and development has been increased from the actual 25% to 100%, plus additional 100% of the adjusted y/y accrual expenses (cost) on research and development. The objective of the application of the average y/y increment for 2 years is to hinder motivation of entities for tax planning aiming to maximize the tax deduction. The proposed provision also supports companies in making real research and development investments. The estimated effect in the first year after implementation ranges around EUR 9 million.

  The introduction of patent-boxes which enable partial exemption of the income from commercial use of intangible assets stimulates higher value-added production and supports employment of highly qualified workers. This measure could not be quantified ex-ante.

- **Introduction of tax allowance for spa treatment (Act 595/2003)**

  The aim of this measure is to make more attractive the business conditions in the spa sector. Workers who undergo spa treatment in the course of the year and prove to have paid at least EUR 50 for the services connected with spa care will be eligible to claim tax allowance up to the maximum amount of EUR 50. The MF SR expect around 200 thousand workers who pay individual income tax to claim this allowance.

- **Introduction of separate depreciation of technical upgrade of buildings (Act 595/2003)**

  The legislation adopted will enable depreciation of technical upgrade of buildings. The depreciation itself will be done separately if its volume totals more than 10% of the input value of the building. The depreciation term is 6 years.

- **Change of mineral oil excise tax rate (Act 98/2004)**

In connection with the termination of the state aid scheme application (tax bonus for the use of fuels made of renewable sources[55]) and non-termination of the notification process for its extension, a legislative measure had to be adopted in reaction to this situation.

- **Heatlh insurance contribution allowance (Act 580/2004)**

Health insurance contribution allowance (HIC) has been drafted as a measure to support low-income workers. However, in some specific cases also the employees who did not belong in the low-income worker category but became, in the course of the year, insurants could become eligible for HIC allowance (having met this condition on a full-year horizon). In order to prevent this option when an individual is employed for a part of the period only, the claim to HIC allowance is inversely proportional to the growth of the assessment base by double the part of the assessment base which overruns the aliquot part of HIC allowance.

Measures incorporated in the GGB, and not approved by TFC

- **Insurance priemum tax**

The Government expects the actual deduction from non-life insurance policy to be replaced with an insurance premium tax on the volume of both the life and non-life insurance, except the mandatory contractual insurance.

- **Changes in gambling tax**

The Government has prepared and plans to implement de-monopolization of on-line gambling games operated by the companies with business activities in the area of gambling in Slovakia. The measure also introduces a uniform surveillance and regulation of gambling games.

Expenditure measures

The draft budget is associated with higher expenditures level than the NPC scenario expeditures over the entire horizon. The 2018 expenditure measures consist of valorisation of salaries, one-off capital expenditures and a reserve accounting for possible lower tax and non-tax revenues (intermediate consumption). Due to temporary nature of some of the measures, the level of expenditues in excess of the NPC scenario decreases in 2019. In 2020, the budget expects the defence expenditures to accelerate in order to reach the level of 1.6 per cent GDP.

- **Compensations**

The draft budget assumes growth of compensations in excess of the NPC level over the whole horizon. In 2018, it accounts for the effects linked to the valorisation of salaries of pedagogical and professional staff in regional schools and universities effective from September 2017 by 6%, as well as the additional adjustment of tariff salaries of civic servants.[56] The budget also accounts for the expenses stemming from the legislative changes associated with the introduction of new legislative measures[57].

- **Intermediate consumption**

[55] By way of negative motivation of higher tax on fuels which do not contain the required biofuel content.
[56] Based on the Manifesto, the tariff salaries should grow by 4% in 2018 and the temporary bonus at the level of 2% of the wage is budgeted for the period from 1 Sep 2018 to 31 Dec 2018.
[57] Additional transfer to employees working during the weekends is at the level of 100 per cent of the minimum hourly wage, while the additional transfer to emplyees working during bank holidays reached 100 per cent of the individual average hourly wage.

In excess of the NPC framework, the 2018 budget incorporates a reserve accounting for possible lower tax and non-tax revenues.

- **Social benefits**

The expenditures on social benefits is in excess of the NPC level throughout the entire budgeting horizon due to ongoing and already adopted legislative measures. These measures include increased transfers to people taking care of disabled and increased tranfers to organisations providing social services. Minimum pension valorisation measure is implemented for a temporary four year period and pensions granted before 2004 are recalculated. The budget also accounts for the cost associated with increased transfers to people commuting to work and the family relocation cash benefit.

- **Natural social transfers**

In excess of the NPC level, the 2018 budget reflects the expected positive impact stemming from the legislative amendment to 363/2011 (Drug Repayment Act).

- **Other current transfers**

When compared to the NPC scenario, higher expenditures within the current transfers includes the reserve accounting for the effects linked to the ongoing legislative changes associated with the introduction of the 13th and the 14th salary and the tax cut for pensioners on partial contracts.

- **Capital expenditures**

The draft budget assumes higher level of capital expenditures when compared to the planned level under the NPC scenario. Additional expenditures are associated with the defence modernisation, the construction of an investment park and the ongoing investment projects (reconstruction of the Slovak National Gallery, expansion of the sports infrastructure network).

BOX 10 - One-off and temporary expenditures in 2017

Similarly to the last year, some of the last year expenditures do not recur or are expected to occur in a significantly lower volume in 2017. One-off expenditures are substracted from the reference year level (2016) and this is indexed into the next years in order to estimate the development of the deficit under the no-policy-change scenario. The total volume of one-off measures in 2017 amounted to EUR 771 mil. (0.9% GDP) and it was dominated by the investment measures (0.58% GDP).

TABLE 13 - List of one-off measures in 2017 for the NPC scenario (ESA 2010, EUR mil. and in % GDP)

	ESA 2010	2017	2017 (in % GDP)
One-off effect in wages	D.1	14	0.02
Loss of ŽSSK	D.7p	44	0.05
Environmental and Recycling Fund	D.7/D.9	27	0.04
Capital investments, thereof	P.5L	335	0.42
Investments of public importnace	P.51g+NP	256	0.30
Transportation projects (MTC SR - SSC)	P.51g+NP	83	0.10
Reconstruction and modernization of buildings (MARD SR)	P.51g	16	0.02
Capital transfers, thereof	D.9p	143	0.17
EU corrections	D.9p	78	0.09
Sports infrastructure	D.9p	43	0.04
SNG reconstruction	D.9p	12	0.01
Transfer for SVP	D.9/D.3	13	0.02
Other		175	0.21
Total		**771**	**0.91**

Note: Ministry of Agriculture and Rural Development of SR (MARD SR), Ministry of Transport and Construction of SR (MTC SR), Slovenská správa ciest (SSC/ Slovak Road Administration), Slovenský vodohospodársky podnik, š. p. (SVP/Slovak Water Management Enterprise), Slovak National Gallery (SNG)

Source: MF SR

II.7. Consolidation effects

The starting point for quantification of the size of the fiscal measures that affect the economy is the no-policy-change scenario (NPC). The impact of the fiscal policy in the period 2018 to 2020 is based on measures necessary to achieve the fiscal targets contained in the general government budget for 2018 to 2020 compared to the NPC.

TABLE 14 - Total size of measures necessary to reach the fiscal targets, compared with NPC (ESA2010, % GDP)

	2018	2019	2020
1. General government balance - Fiscal targets	-0.83	-0.10	0.00
2. General government balance - GGB	-0.83	-0.32	-0.27
3. General government balance – NPC scenario	0.05	0.17	0.56
4. Size of measures - scenario analysed (1-3)	-0.88	-0.27	-0.56
- year-over-year change	**-0.88**	**0.56**	**-0.31**

Source: MF SR

In 2018, there is a fiscal impulse in the amount of 0.9 per cent of GDP compared to the NPC scenario, concentrated mainly on the expenditure side of the general government budget. Overall expenditure expansion equals 1.1 per cent of GDP The fiscal framework on the expenditure side assumes positive stimulus in intermediate consumption, compensations and public investments. The consolidation measures on the revenue side equal 0.2 per cent of GDP. These include expansionary revenue measures related to the taxes on production.

The 2018 positive effect of the fiscal impulse on the GDP growth is estimated at the level of 0.6 p.p. The implied fiscal multiplier corresponds to 0.71.

In 2019, provided that permanent measures are adopted to meet the budgetary objectives, consolidation measures are needed in the amount of 0.6% GDP. The 2019 consolidation is undertaken particularly on the expenditure side of the budget mainly within the intermediate consumption and investments, while several measures of the previous year are not repeated. The revenue side is dominated by restrictive measures mainly in the area of taxes on production. The negative effect on the GDP growth in estimated at the level of 0.4 p.p. in 2019. The implied fiscal multiplier is estimated to reach 0.68.

The year 2020 should, based on the fiscal objective, bring additional impulse in the amount of 0.3 per cent of GDP which should concentrate again on the expenditure side. The positive effect on the GDP growth is estimated to reach 0.2 p.p. and the implied fiscal multiplier in the amount of 0.58.

III. Linking the budgetary plan to the objectives of the Growth and Employment Strategy and Country-specific Recommendations of the European Commission

The government has prepared a set of structural measures aiming to encourage the economic growth and employment in order to respond to major challenges of the Slovak economy – the labour market, primary education and the healthcare system. The second round of spending reviews of education, labour market policies and environment continues to assess efficient use of public funds. A package of social measures will support the labour force mobility and increase the income of workers. In education the government is focused, in particular, on increasing the attractiveness of teaching profession and expansion of kindergarten capacities. Multiple projects focusing on the integration of marginalised Roma communities will be supported. Capacities of childcare facilities for children under three years of age will be increased. The positive development in the labour market will be further supported by the reform of public employment services, as well as the broadening of active labour market policies. In healthcare the measures will focus on improving the efficiency of expenditures for consumption of pharmaceuticals and operating costs of hospitals. Measures concentrating on the improvement of efficiency of courts, fight against corruption, and shortening the debt collection processes have been implemented. Multiple measures will contribute to the reduction of the administrative and regulatory burden of businesses.

III.1. Structural measures

This chapter describes major structural measures, which have already been adopted by the Slovak government or which are planned for implementation within the next two years in accordance with the National Reform Programme od the Slovak Republic 2017[58]. The greatest challenges in terms of falling behind other countries are represented by the quality of primary education, the labour market, and the quality of healthcare[59]. Furthermore, the measures focus mainly on the areas of tax collection, research and development, judiciary, and support of business environment. The Value for Money project (more in Chapter IV) has proved to work well for the Government in the budget planning process and improvement of efficient use of public funds.

The budget for 2018 – 2020 also presupposes the funding of the social measures package. Measures focus on increasing the labour force mobility and the income of workers. Throughout 2018, the extra pay for work on weekend and public holiday and the extra pay for the night work should rise. The labour force mobility would improve as a result of the reinforcement of the commuting allowance and the relocation allowance. The payment of the 13th and the 14th salary will be supported by the tax and contribution relieves.

The measures in education are focused mainly on increasing the attractiveness of teaching proffesion, and expansion of kindergarten capacities. In spite of the increased expenditure on the regional education in recent years, the Slovakia's results in the 15-year-old students in the PISA 2015 testing have worsened again. The salaries of teaching and professional staff in regional and tertiary schools grew by 6% in September 2017. This should increase the attractiveness of teaching profession. The published National Programme for Education Development presents a draft reform document for the area of education for the next 10 years. Expansion of kindergarten capacities also continues in 2017 with the use of structural funds.

The reforms within the tertiary education include the reform of accreditation commission and the accreditation process, a new assessment system and institutional funding of research and development at universities will be developed, and the instruments to increase accessibility of tertiary education will be made more targeted. Higher share of funding of the research and development activities through grants will reinforce the competition in the area

[58] National Reform Programme of the Slovak Republic 2017.
[59] Priorities were identified in the National Reform Programme SR 2017.

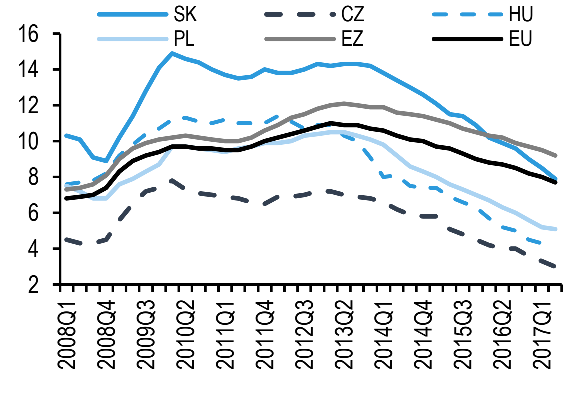
of research, development and innovations. The transformation of the organisations of the Slovak Academy of Sciences (SAS) to public research institutions from July 2018 will allow closer cooperation with business and industry and more efficient use of their funds.

The government will support investments in research and development (R&D) through significant increase in the tax relief for expenditure on research and development in businesses. In addition to the tax-deductible expenses, taxpayer will be allowed to claim additional 100% deduction of the R&D expenses and 100% deduction of the average increase in the expenses on R&D in a 2-year period. The R&D deduction was claimed in 2015 tax period by 85 entities in amount of EUR 9.2 million, meaning that the negative fiscal impact amounted to EUR 2 million. Around 60% of the volume was claimed by large enterprises employing 250 or more employees. Beside this introduction of the so-called patent-boxes stimulates higher value-added production and supports employment of highly qualified workers and it will allow partial tax relief for income from commercial use of intangible assets.

Projects in the area of inclusion of individuals from marginalized Roma communities (MRC) focus within the new programming period 2014 – 2020 on funding the construction and reconstruction of kindergartens and community centres, waste management, better access to drinking water, and establishment of local neighbourhood watch schemes. National projects will be implemented to support community centres, field social work, land settlement, better access to health care, and to preschool education. The national projects in the new programming period also continue in the functional full-day education system, development of inclusive education of children from MRC, work of teacher assistants, and the educational activities in Roma communities.

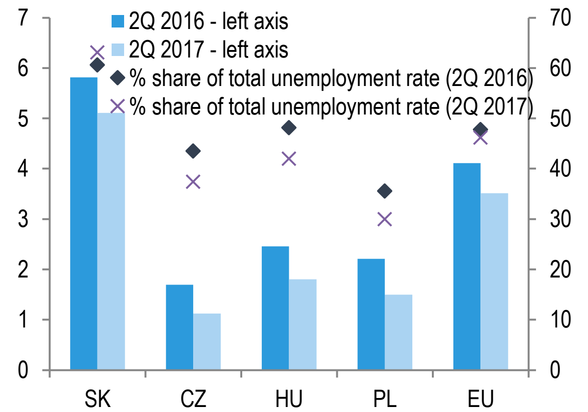
Despite recent positive developments, the labour market remains one of the main long-term challenges of the Slovak economy. The seasonally adjusted overall unemployment rate hits the record lows. In the second quarter of this year, it dropped down to 7.9% coming closer to the EU average (7.7%). In spite of the year on year decrease, the long-term unemployment rate (from 5.8% to 5.1% in the second quarter 2017) is still significantly above the EU average and the average of the remaining V4 countries. The share of long-term unemployed exceeds 60%, one of the highest values within the EU countries.

CHART 35 - Quarterly development of the unemp. rate according to the LFS (%active population, seasonally adjusted data)



Source: Eurostat

CHART 36 - Long-term unemployment (%, 2Q 2016, 2Q 2017)



Source: Eurostat

Revisions of the expenditures on the labour market policy[60] identified opportunities for improving the operational efficiency of labour offices and opportunities for reallocation of funds for active labour market measuresand operation. Internal evaluations of labour office efficiency led to the continued employee relocations to more frequent and demanding activities. The MoLSAF SR adopted an action plan in 2016 to implement several

[60] Pilot study of the revision of expenditures on employment services (October 2016) and the MoLSAF SR spending revision (July 2017).

forms of support for the integration of long-term unemployed in the labour market, particularly the individualised counselling including jobseeker profiling, or education and re-qualification programmes. Projects within the active labour market policies (ALMP) have been launched in the course of the year in order to support the employment of jobseekers by private and public employers, self-employed and commuting in the least developed districts.

Employment of women will be supported by the reinforced provision of child care for children up to three years of age. In order to develop childcare facilities for children under three years of age, construction of 90 childcare facilities with a capacity of 1,800 children with a financial allocation of EUR 40.2 million is expected within the IROP and the OP Human Resources in 2017-2020[61]. In January 2017, the Parliament adopted legislation, effective as of March 2017, (the so-called nursery law) implementing the legislative framework for childcare facilities for children up to three years of age.

The Government increased the social benefits for families and the social care. After the 2016 increase, the maternity benefit was increased in May 2017 again from 70% of the daily assessment base to 75%. An individual who earns an average salary and is entitled to maternity benefit receives nearly full compensation of his/her net income. Also the parental benefit was increased in May from the current EUR 203.20 to EUR 213.20. The impact of the parental benefit and the maternity benefit increase amounts to EUR 29.9 mil. (0.03% of GDP) annually. An increased allowance for the care of disabled persons is provided from 2017 within welfare services for the disabled. The budget counts on additional expenditure in the amount of EUR 29.5 mil. annually (0.03% of GDP) for this purpose. In August 2017, the Government passed the amendment act on social services which changes particularly the method of calculation of the financial allowance for the providers of social service in facilities conditional on dependency. The list of entities eligible to claim financial allowance for social service provision (besides municipalities and non-public providers, also non-public providers under the competence of the higher territorial units) will be extended.

The Government adopted multiple measures to increase the pensions from 2018. In June 2017, the Parliament approved one-off revision of pensions granted before and after 2004. In 2018, this measure will amount to EUR 50 mil. (0.06% of GDP), while the annual costs are expected to fall down in the coming years. The Government has also passed temporary minimum adjustment of pensions which should grow by at least 2% of the average pension amount in 2018-2021. The cost in the first year equals EUR 75 mil. (0.1% of GDP).

BOX 11 - 2012 Slovak pension reform and update of pension expenditure projection until 2070

An extensive pension reform took place in 2012 which has brought significant improvement of the long-term sustainability of the pension scheme. Main changes having positive impact on the public finance include linking statutory retirement age to life expectancy, change of pension benefit indexation rules, reinforcement of solidarity in the calculation of newly granted pension benefits, and change of the maximum assessment base on contributions.

The yearly growth of the statutory retirement age will slow down in future. Based on the most recent estimates, the retirement age will not reach the level of 65 years before 2038. Until then, it will be extended each year by 52 days on average, which is significantly less than 76 days in 2017. Greater extension of the retirement age is currently driven by the convergence towards Western European standard of living which will slow down in future. At the same time, the life spent at retirement will remain at the same level. Percentage of adult life spent in retirement was 31% on average in 2016 and should remain at the level of 31% in 2070 based on actual projections. The Slovak statutory retirement age was one of the lowest among the EU countries in 2013.

Gradual extension of the retirement age, together with other changes under the 2012 reform allows funding of ad-hoc measures aiming to improve pension adequacy. Multiple measures were adopted, or have been considered, in the area of pensions since 2012. The most significant is the one-off increase in pension benefit indexing to 2% in 2017 which increased the expenditures by EUR 113.6 mil. a year, and the implementation of minimum adjustment for 2018-2021. The replacement rate (average pension benefit to the average wage in economy) was slightly above the EU average in 2013.

[61] Integrated Regional Operating Programme and the Operating Programme Human Resources.

TABLE 15 - Pension measures adopted after the 2012 reform and their effect in the GG deficit (EUR mil.)

	2013	2014	2015	2016	2017	2018
			Saving measures			
Lower pension indexation	0.0	-5.9	-60.1	-104.5	-183.6	-268.7
Linking retirement age to life expectancy	0.0	0.0	0.0	0.0	-29.3	-58.6
			Measures increasing pension adequacy			
Increase in the Christmas pension bonus	0.0	9.2	9.3	9.5	9.6	9.7
Minimum pension benefits	0.0	0.0	9.1	22.4	22.8	23.3
Alignment of widow's pension benefits	0.0	0.0	0.0	7.9	8.7	9.6
Alignment of widower's pension benefits	0.0	0.0	0.0	2.9	3.2	3.5
Higher indexation in 2017	0.0	0.0	0.0	0.0	113.6	116.0
Minimum indexation in 2018-2021	0.0	0.0	0.0	0.0	0.0	81.5
Re-calculation of old-age pension benefits granted before 2004	0	0	0	0	0	50.2
Total	0.0	3.3	-41.7	-61.8	-55.0	-33.5
Cumulative	0.0	3.3	-38.4	-100.2	-155.2	-188.7
Cumulative savings (1)	0.0	5.9	66.0	170.5	383.4	710.7
Cumulative ad-hoc expenditures after reform (2)	0.0	9.2	27.6	70.3	228.2	522.0
(2)/(1) ratio		**156%**	**42%**	**41%**	**60%**	**73%**
			Measures on the revenue side			
Increase in the maximum assessment base to the five timesthe average wage	-103.6	-110.8	-119.8	-128.8	-138.5	-149.0
Increase in the maximum assessment base to seven times of the average wage	0.0	0.0	0.0	0.0	-67.2	-70.5
Cumulative measures on the revenue side	-103.6	-214.4	-334.2	-463.0	-668.8	-888.2

Source: IFP based on the documents of the MoLSAF SR and own calculations

The MF SR updated the long-term forecast of age-related expenditures for the pension area, which is based on the Eurostat's new demographic projection and the EC's macroeconomic forecast. The projection has not been approved by the Working Group on Ageing Populations yet, and therefore is subject to change. The final projection for the areas of pensions, healthcare, and long-term care will be published by the EC in spring 2018 in the Ageing Report.

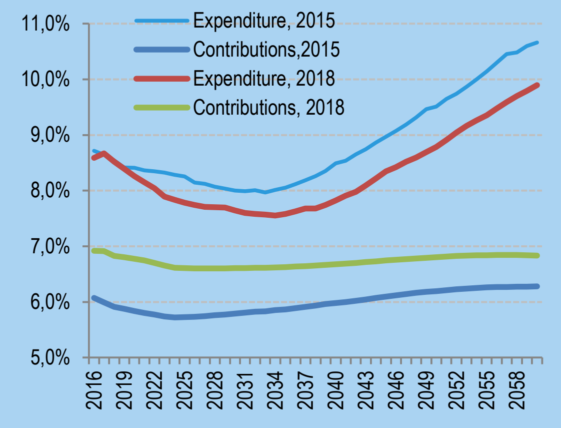
Based on the preliminary MF SR's projection, the expenditures on pensions should grow by 1.2% of GDP until 2070. In the course of the next generation (until 2030), the expenditures will slightly fall, particularly due to the 2012 reforms adopted, robust GDP growth, and the demographic structure. Thereafter, the retirement of the baby boomers generation along with a slower GDP growth and longer careers will cause a significant growth of the expenditures on pension benefits. The pension scheme deficit should culminate above 3% of GDP close after 2060.

Compared to previous 2015 Ageing Report, it constitutes improvement in both expenditure and revenue which should also translate into the assessment of sustainability of Slovakia[62]. Compared to the previous projection, the pension expenditures should be 0.8% of GDP lower in 2060. The improvement is caused mainly by a more positive demographic forecast of Eurostat and higher estimate of participation rate which increases the long-term real growth of GDP. Expenditures are also under strong influence of the updates of the inputs used in the model (mainly more savers in the second pillar, lower pensioner's inflation). Revenues were higher by 0.8% of GDP as early as in 2016 also due to changes in contributions. Until 2070, revenues are mainly under the influence of the second pillar, which is now expected to be joined by relatively more people based on the IFP analysis (31% of the young population vs. the initial 10%).

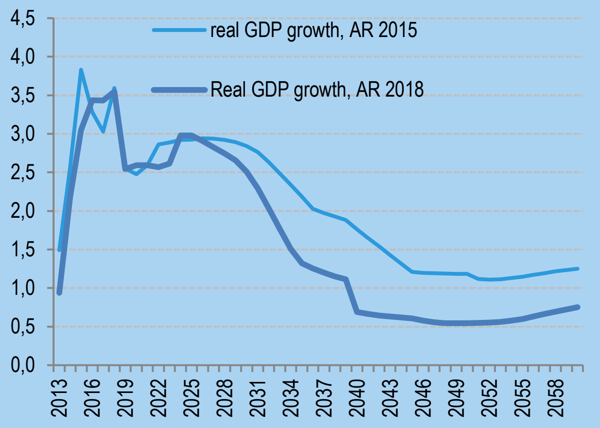
CHART 37 - Comparison of revenue and expenditure of the pension system under the initial and current projection (% of GDP)

CHART 38 - Real GDP growth under the initial and revised projection (%)

[62] Thorough evaluation of the impact on long-term sustainability will be possible after the EC makes accessible the projection of expenditures on education, healthcare, education, and long-term care.



Source: MoF SR



Source: EC

Measures identified by the 2016 healthcare spending review are being implemented. A majority of measures focus on the area of pharmaceuticals , medical devices and material, diagnostics and hospitals. The set up of the supervisory bodies in hospitals and Unit for the management of organisations operated by the MoH SR reinforces surveillance of state-owned hospitals. The centralized procurement process continues to be implemented for the state-owned hospitals at the level of the MoH SR. A diagnostic-related group-linked payment mechanism was launched early in 2017. In the first year, individual hospitals have individual rates in order to avoid significant financial fluctuations and destabilization of the system. The five-year taking convergence process of individual rates to a single nation-wide basic rate will be initiated in 2018. The implementation of *eHealth* with gradual connection of physicians continues in 2017. The selected parts of *eHealth - National health portal, ePrescription and eMedication, Electronic health documentation* and *eAllocations*, should be fully functional in 2018. The terminal network of hospitals and the network of outpatient care providers will be optimized with the emphasis on regional-based needs and patient's safety. Inpatient capacities will be adapted to regional needs and the long-term care capacities will be strengthened. The MoH SR has developed a new emergency department system covering also the completion of the urgent care network. Upcoming amendment to the law on the reimbursement of medicinal products will ensure faster entrance of innovative medicines to the Slovak market.

The transport spending review in 2016 identified a great opportunity to increase effectiveness of expenditures and better measurement of the outcomes in the area of evaluation, priority identification, and preparation of investment projects. Based on review conclusions, during 2017 the MoF SR has been working on an economic evaluation of the investment projects developed in the transport sector with the estimate of total cost amounting to EUR 7.5 billion. A uniform standardized methodology of CBA for investment projects with consistent and validated assumptions has been developed in cooperation with the MoF SR and JASPERS[63]; a methodology for feasibility study of construction projects is being developed as well. In January 2017, the Slovak government approved the Strategic Development Plan for Transport until 2030. In the development and evaluation of measures, the first outputs of the Transport Model of SR were used. As soon as it becomes fully functional, it should gradually become one of the basic instruments for the development and assessment of transport policy and its impacts in the future. The completion of the motorway D1 from Bratislava to Košice remains the main priority of the transport infrastructure construction[64]; the 2016 capital expenditures on the construction of the missing sections of motorways and highways amounted to EUR 711 mil[65]. The significance of railway transport and the efficiency of the public passenger transport should continue to be systemically increased in the public transport area.

[63] JASPERS is a partner of the EC and the European Investment Bank, it assists countries aiming to improve the quality of investments funded through EU funds.
[64] Based on the strategy of the MoTaC.
[65] The capital expenditures also include the purchase of land and creation of gross fixed capital (investments).

Measures in judiciary focus on the improvement of efficiency of courts, fight against corruption, and shortening processes related to enforcing contracts. Collective selection procedures to occupy vacant positions of judges at district courts will be implemented and committees to assess the work of judges will be set up. The MoJ SR launched the audit of judiciary in 2017. In November 2016, the Parliament approved changes in the distraint proceeding which accelerated the debt collection processes. Effective as of January 2017, the anti-offshore law lays down an obligation for the corporations to register in the registry of public sector partners and disclose the ownership structure down to the ultimate beneficiary. Effective as of March 2017, the amendment to the bankruptcy and restructuring law (the so-called Bankruptcy Law) decreased costs connected with initiation of the personal bankruptcy proceeding for individuals in debt trap. The amendment act also revoked the option of forgiving more than a half of debts and changes the maturity of the remaining debts to five years in the company restructuring process, unless the creditors give a voluntary consent. Effective as of August 2017, the Government passed changes of the Commercial Code improving protection of creditors. The obligations of statutory bodies will be made stricter in the cases using the services of the so-called cat's paws. Further, amendment act reacts to the issues connected with corporate consolidations aiming to avoid their obligations.

The implementation of electronic processes in the area of tax payment and debt collection will reduce the administrative burden for the business environment. The Financial Administration will continue to reduce the administrative burden for businesses by expanding the opportunities of two-way electronic communication with businesses with regard to tax paperwork, and particularly the VAT, and by providing pre-filled forms of certain types of tax returns. In September 2017, the Parliament passed the e-Government amendment act which should simplify the use of electronic services and introduce mechanism for monitoring compliance with obligations for involved actors. Changes with a positive impact on the business environment have also been adopted in the process of judicial restructuring and debt collection (distraint proceeding). Reduction of the regulatory burden and improvement of the business environment should also be supported by a package containing the proposal of 35 specific measures in various areas across multiple Ministries which was approved by the Government in June 2017. One of the first measures out of this package which has already been approved by the Government includes the optimisation of the occupational health service which presupposes reduction of administrative costs for entrepreneurs. Effective as of December 2017, the administrative burden will be reduced for small enterprises which generate less than 100 kg of packaging and non-packaging materials a year. They will not be obligated to become members of Producer Responsibility Organisations anymore, they will only have to register with the MoEnv SR.

The amendment act on air pollution brings environmental improvement measures. The new legislation passed by the Government in August 2017 will allow the towns and villages to create low-emission zones which may only be entered by low-emission vehicles. It will also set more strict emission limits and monitor for medium combustion plants.

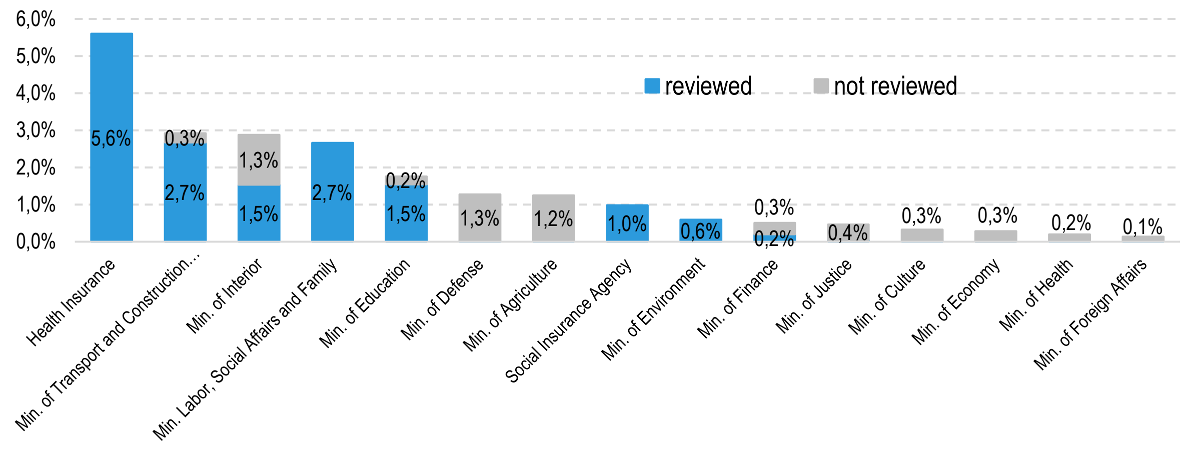
IV. Higher value for money

The Value for Money project serves from 2016 as an instrument of the Government to improve the efficiency of public spending. Spending reviews carried out in in 2017 focused on the expenditures in education, environment, labour market policies and the social policies amounting in total to 7.3 % GDP. The public spending totalling 15.9 % GDP (39% of public spend) has been reviewed under the project so far. The Government has also reformed the investment assessment process, with the Ministry of Finance having played a more active role in this process. The implementation of measures is monitored by a newly established Implementation entity; based on the first report, the measures have been implemented to 50%. In 2018, the expenditures and results in agriculture, inclusion of marginalised groups, and employment and remuneration in the general government (wage bill) will be analysed.. Final reports will be prepared by March 2019. Until the 2020 elections, majority of public spending will undergo spending reviews.

The Value for Money project is a new instrument started in 2016 with aim to improve efficiency of public expenditure; through this project the government intends to improve public services and contribute to a balanced budget. The Government presented the project both in its manifesto and 2016 Stability Programme.

The 2016 and 2017 spending reviews have reviewed public spending amounting to 15.9 % GDP (39% of the total public expenditures, **Chyba! Odkaz na záložku nie je platný.**), and identified potential savings worth amounting to 0.6% GDP (1.5 % of the total public expenditures).

CHART39 - Expenditures reviewed under spending revision in 2016 - 2017 (% GDP)[66]



Source: MF SR

TABLE 16 - Significant measures with positive effect on budget identified by revisions (EUR mil.)*

	2017	2017ED	2018	2019	*2020*	*potential savings* EUR mil.	% GDP
Healthcare (2016) - Measures decreasing the expenditures of VZP health insurance company	143	34	159	165	193	268	0.33
Healthcare (2016) - Measures reducing spending of hospitals (controlled by the MH SR)	31	-7	31	31	31	95	0.12
Environment (2017) - Revocation of exemptions in excise taxes and other measures	-	-	0	65	65	130	0.16

* 2017 saving based on the spending review, compliance based on the expected deficit, 18-20 under the GGB

Source: MF SR

[66] Volume of reviewed expenditures - 2016 revisions - existing status, 2017 revisions - budget, draft 2018 budget - not reviewed

The implementation of the measures identified by the revisions conducted from 2017 is monitored by the Implementation Unit located at Deputy Prime Minister for Investments and Informatization Government Office. Based on its first implementation report, the measures of the revisions in healthcare, transport and informatization were only met to 50%. Fiscal measures of the Ministry of Health incorporated in the general government budget were fulfilled to 31% in the first six months[67].

The Government reformed the significant investment assessment process in 2017. Adopting the *Public Investment Project Assessment Framework,* the Government defined a methodological framework for the process and preparation of large investment projects and their assessment in accordance with the Value for Money principles. The Ministry of Finance is obligated to prepare and publish assessment of the investment project funded from the public sources of the general government with costs above EUR 40 mil., or above EUR 10 mil. in the informatization area. In the upcoming period, 124 transport projects amounting to EUR 32.5 bn in total (38.4% GDP, TABLE 17) and other projects in other sectors are expected to be assessed.

TABLE 17 - Future investment projects in transport subject to the Value for Money review

	expected cost	
	EUR bn	**% GDP**
Slovak railways (ŽSR)	9.7	11.4
Motorways and 1st class roads (NDS and SSC)	22.8	27.0
TOTAL	**32.5**	**38.4**

Source: MF SR

IV.1. 2017 spending review

The 2017 spending reviews on education, environment, labour market policies and the social policies reviewed expenditures amounting to 7.3% GDP. The revisions identified measures with potential savings of EUR 277 mil. covering 4.7% of the envelope reviewed. This figure comprises EUR 88 mil. within education, EUR 59 mil. within labour market policies and social policies, and EUR 130 mil. within the environment. The reviews recommend to increase the value in education quality, air pollution, waste water processing, and pension saving performance.

IV.1.1. Education spending review

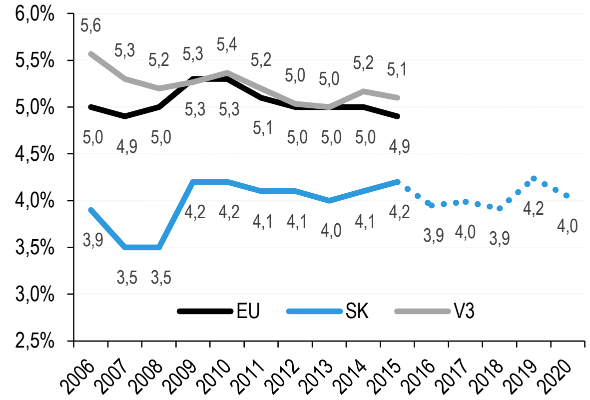
The education spending review amounting to 3% GDP a year has set a goal to prepare measures leading to the improvement of the quality of education in Slovakia. Support of the teaching profession with emphasis on beginner teachers, and stronger link between remuneration and education quality were identified as key factors in education quality. The revision also outlined a potential space for cost saving within rationalization of the regional education network, cancellation of bonus for continuous education credits, and higher proportion of students not continuing in postgraduate study, amounting in aggregate to EUR 88 mil. a year.

Compared to the most developed countries, Slovak education expenditurs are approximately 1% GDP lower on a long term basis, but in recent years they have come closer to the EU average. Perceived as total public spending share, Slovakia will, based on the general government budget projection, reach the EU average in 2020. The international OECD PISA testing shows below-average and continuously worsening results of 15 year old students. Furthermore, the proportion of students with weak results is one of the highest from among the OECD countries and keeps growing.

CHART 40 - Public expenditures on education (2006 - 2015 and forecast until 2020, COFOG methodology)

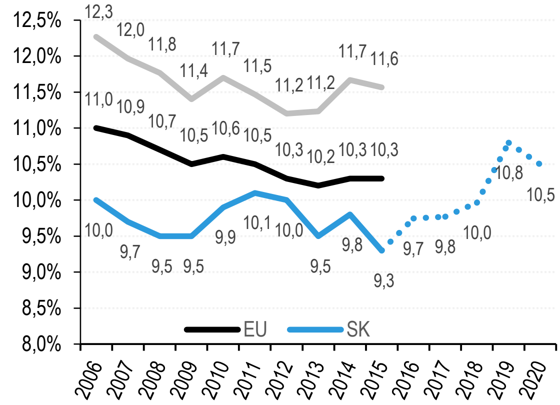
[67] EUR 27 mil. out of the planned EUR 87 mil. during the first six months of 2017.

in % of GDP



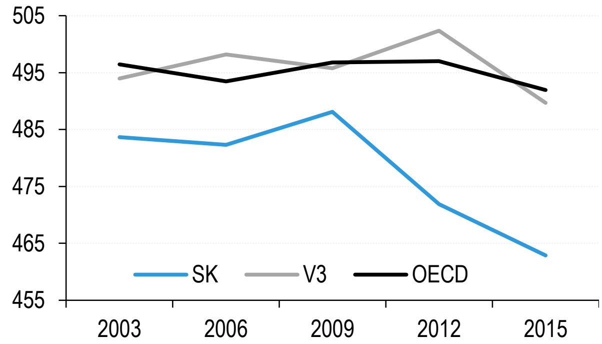
Source: Eurostat, RIS, MF SR forecast

in % of total public spending



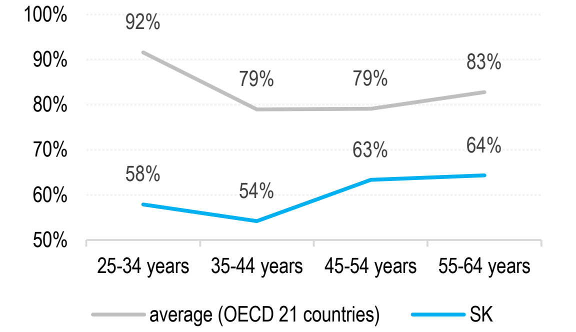
Source: Eurostat, RIS, MF SR forecast

CHART 41 - PISA test results - average of tested subjects



Source: OECD

CHART 42 - Ratio of wages of teachers and employees with tertiary education by age (%, 2014)



Source: OECD EAG, Trexima

Spending review notes that besides increase in the expenditures other reforms are also required to improve the quality of education. The report points out following measures as the crucial ones:

1. **Better teacher pay.** Lower expenditures affect particularly the teacher salaries; in 2015, they reached including all extra pays 62% of the average salary of employees with the second level university degree, the OECD average being 88%. The tariff-based pay rise in accordance with the Manifesto of the Government will get the teacher salaries at the level of 67% of the average wage by 2020. The revision recommends pay rise for young teachers and a stronger link between remuneration and provable quality. It recommends that the current system of formalized, theory-oriented attestations be replaced with a certification based on demonstrated pedagogical skills and an elaborated portfolio.

2. **Better preparation and support for teachers.** The offer of professional development courses should be improved and the students of departments of education should have a significantly greater volume of on-spot training directly at schools.

3. **University accreditation process reform.** The revision recommends establishment of a new, better Accreditation Agency which would certify institutions based on internationally accepted standards. Complex accreditation should be replaced with a system focusing on the audit of the internal quality assurance system in accordance with the trends prevailing in this area in Europe. More emphasis should be paid to evaluation of education results. Expert assessment university research activities outputs should be implemented in accordance with international standards.

4. **Research funding reform.** The university research funding system is characteristic for a weak link between the output quality and low proportion of competititve grants. Both factors indicate weak development of research assessment concept. Therefore, the revision recommends implementation of an expert assessment of research outputs in accordance with international standards and increase in the proportion of competitive grants in public expenditures on research aiming at a more direct support of excellent science.

5. **Collection of relevant information and its regular assessment.** It is necessary to carry out longitudinal research and testing on samples focused on evaluation of trends, systemic changes, and other aspects of the education system. Universities lack regular feedback from graduates and the labour market. Graduate tracking system by way of using administrative data and the data of graduate and employer surveys could diminish the mismatch between the education system and the labour market.

Although total expenditures on education lag behind the expenditures of the OECD countries, there is a space to save in education as well. The revision identified the following:

TABLE 18 - Cost saving measures in education (EUR mil.)

	2018	*2019*	*2020*	*Potential annual saving**
Adopt measures to support the elementary school network rationalization	1	3	8	14
Discontinue continuous education “credit scheme”	0	5	10	46
Adopt measures to increase the proportion of undergraduate students who would not continue in the graduate study	2	7	12	28

*Note: * - Annual saving compared to the 2017 budget* *Source: MF SR*

1. **Rationalization of the elementary school network.** The ES network is less efficient than it used to be in past due to negative demographic trend. However, the rationalization should not take into account the financial savings only, but also the potential impacts on the quality, inclusion, and accessibility of education for all children in their mother tongue, and should also be supported by such measures as broader compensation of travel expenses or provision of school buses.

2. **Discontinue continuous education “credit scheme”.** This bonus is connected with the participation in and passing of educational programmes, while the contribution of such programmes to the improvement of teacher's work is not assessed at all. Owing to this, teachers take part in education not because they wish to improve their work, but because they want to earn continuous education credits. The revocation of the option to earn credits to get the extra pay would remove the negative motivation and create space for better allocation of the funds saved to the non-tariff components of teacher pay.

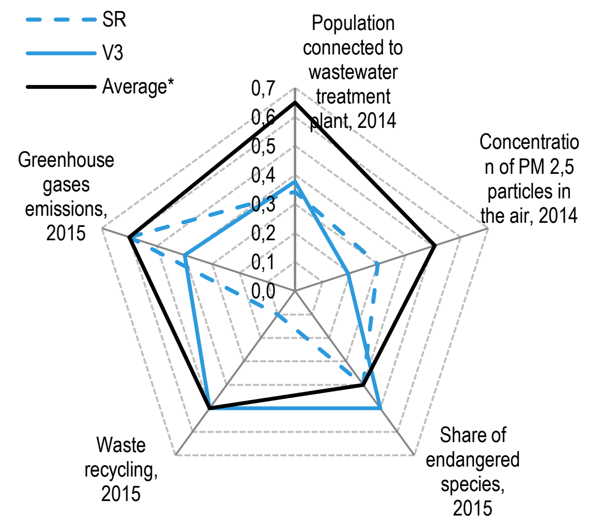
3. **Increase in the proportion of undergraduate students who do not continue in postgraduate study**. The structure of graduates in Slovakia differs significantly from the other OECD countries - twice as many students continue in graduate study (MA degree) and few bachelors choose professionally oriented study programmes. This calls for the support for setting up professionally oriented bachelor study programmes or improving acceptance of the bachelor's degree in the labour market on the side of the state.

IV.1.2. Environmental spending review

The environmental spending review amounting to 0.6% GDP proposes combination of lower expenditures and higher revenues with the potential amount of EUR 130 mil. (0.1% GDP). It identified measures in improving the efficiency of the Slovak Water Management Company operation, higher fees for dumping which would also motivate greater degree of waste recycling, implementation of innovative forms of nature protection funding, better subsidy management, and revocation of optional exemptions in the area of

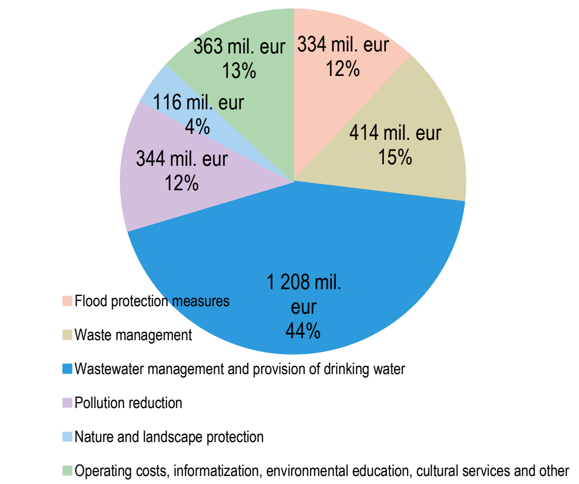
excise taxes (coal, electricity, gas). The proposed measures aimed to increase value could lead to the creation of a significant social and economic value.

CHART 43 - Group of indicators monitoring the environmental objectives



** Sample of countries depending on the indicator is diverse.* *Source: IEP according to OECD, Eurostat*

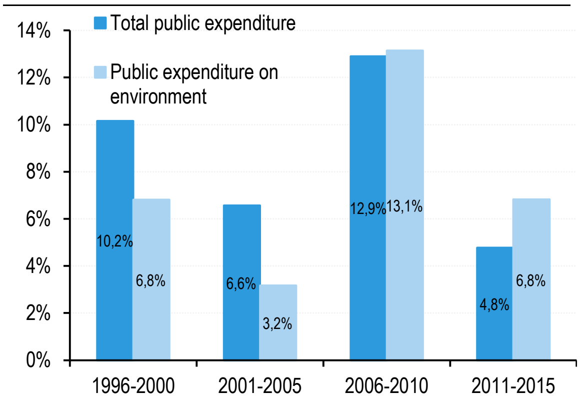
CHART 44 - Average proportion of total expenditures in individual areas in 2010 – 2016



Source: RIS

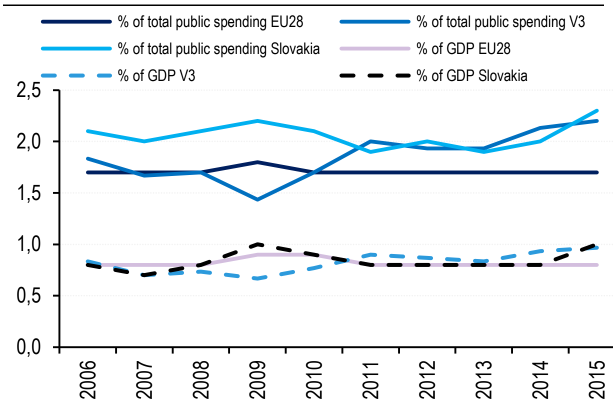
Regarding the environmental quality, Slovakia reports above-average results for the decrease in greenhouse gases considering the size of economy; nevertheless, in international comparisons it continues to lag behind in the area of waste water management, waste management and air quality.

CHART 45 - Average growth of general government spending in %)



Source: Eurostat

CHART 46 - Public expenditures on the environment (in % GDP and % of total public spending, COFOG 05)



Source: Eurostat

The spending review identified measures reducing expenditure and increasing revenues:

TABLE 19 - Cost saving measures in environment (EUR mil.)

Area	Task	2018	2019	2020
SVP, š.p.	Gradual implementation of the operation efficiency improvement measures according to the BCG audit	8	14	20
Waste management	Gradual increase in the dumping fees and implementation of mandatory quantity-based waste charging	0	14	20

Air protection	Revoke facultative exemptions in excise taxes (coal, electricity, gas)	0	65	65
Nature protection	Implement innovative forms of nature protection funding	0	6	6

Source: MF SR

1. **Improvement of the efficiency of the Water Management Company SVP, š.p. operation**

   Through gradual implementation of optimization measures, the operating costs of the Slovak Water Management Company will be reduced by EUR 20 mil. until the end of 2020. The centralization of executive and support functions, elimination of unnecessary activities, and greater outsourcing, as well as rationalization of the machinery fleet would lead to higher efficiency and lower costs.

2. **Increase in the dumping fees**

   Slovakia's recycling rate is low in spite of extensive construction of the sorting and recovery infrastructure. In order to improve the recycling rate, the dumping fees will be gradually growing and a mandatory quantity-based waste charge will be stipulated for municipalities.

3. **Revocation of exemptions from excise taxes**

   The extension of environmental taxes and restriction of the existing exemptions will drive more efficient use of energy. The revenue from revocation of facultative exemptions of around EUR 65 mil. a year can be used for reducing local pollution, e.g. for replacement of boilers in households. Phasing out of electricity production from coal should also have a significant impact on the local air quality.

4. **Alternative forms of nature protection funding**

   A sustainable nature protection funding system which would also make use of the sources outside the state budget and the EU needs to be set up from the long-term perspective. Therefore, the review suggests gradual introduction of innovative funding forms, e.g. instituting an admission fee to national parks (EUR 6 mil. a year) or a charge for accommodation in a protected area (EUR 2.7 mil. a year).

The environmental spending review identified measures in the following areas opening space to increase the value for money:

5. **Phasing out of electricity production from coal**

   Based on the 2015 data, phasing out of the electricity production from coal is estimated to bring EUR 500 mil. in health benefits through improvement of the local air quality. At the same time, the expenses of electricity consumers may drop by as much as EUR 100 mil. a year.

6. **Increasing connection of population to the waste water treatment plants**

   Multiple small villages are building water management infrastructure and the investments made so far do not allow for connection and improvement of results. Therefore, the subsidies from the Environmental Fund should focus primarily on the villages having projects in the terminal stages. New projects should be funded in a complex manner. Greater emphasis on the control of waste water disposal could drive connection of around 240 thousand citizens who already have the option but have not used it for some reason.

7. **Compliance with the priority identification of flood protection projects**

In spite of better tools in the flood risk management, a lower or low priority projects are being implemented for various reasons. Adoption of measures addressing bottlenecks which prevent faster implementation of the priority measures could reduce future damages by as much as EUR 1.3 bn compared to the existing construction trend.

8. Priority identification and management of the Environmental Fund

The Environmental Fund implements the state's support of the care for the environment. The form of support is currently dominated by subsidies; loans which are more efficient tools of support for the state are not attractive for the market. The review recommends improvement of their promotion and implementation of a loan-subsidy scheme. More efficient management could be achieved through the creation of support strategy based on priority identification of target areas and better analytical assessment of projects. Large percentage of unsuccessful applications brings unnecessary administrative burden which would be reduced by a more accurate specification and improvement of the application recording electronic system.

9. Better assessment of investments in the environment

The mandatory procedures for priority identification and efficient decision-making process regarding large investment projects are absent. Each large investment will follow the attainment of strategic objective and will have in place a feasibility study, relevant analysis of investment efficiency, and careful assessment of other implementation options.

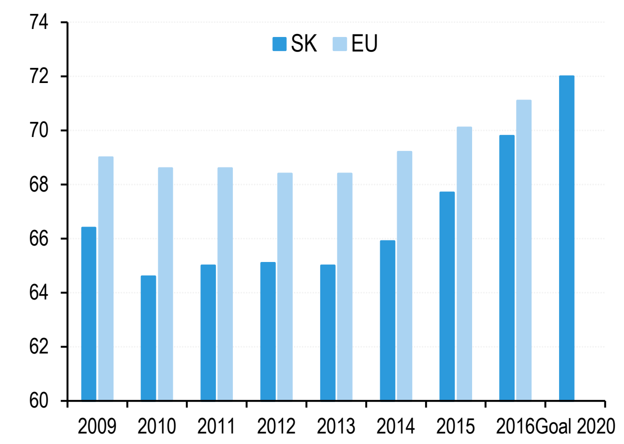
IV.1.3. Spending review on labour market policies and social policies

The spending review of labour market policies and social policies of the Ministry of Labour, Social Affairs, and Family and of the Social Insurance Company addressed expenditures amounting to 3.7% GDP a year. The main objective of the MLSAF SR policies focuses on the increase in the employment rate and the decrease the at-risk-of-poverty rate of citizens. Measures concentrate on the introduction of annual declaration of social insurance contributions, suggestions of better targeting of social policy, more efficient operation of labour offices and the Social Insurance Agency, and of the second and third pillar pension scheme.

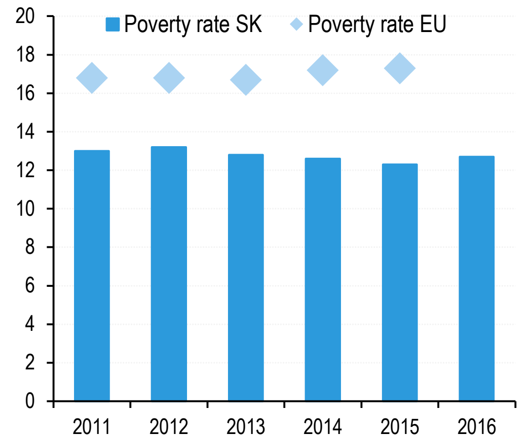
The main objective of the MLSAF SR policies focuses on the increase in the employment rate and the decrease in the population at risk of poverty. Slovakia's employment rate results are good, with the 72% target to be attained in 2018 under current development. Slovakia is successful in reducing the at-risk-of-poverty rate. Although the results are significantly better than the European Union average, a relatively large number of individuals (above the EU average) lives in severe material deprivation, despite the decrease in last years.

CHART 47 - Employment rate (% in a group aged 20-64 years)

CHART 48 - At-risk-of-poverty rate after social transfers (%)



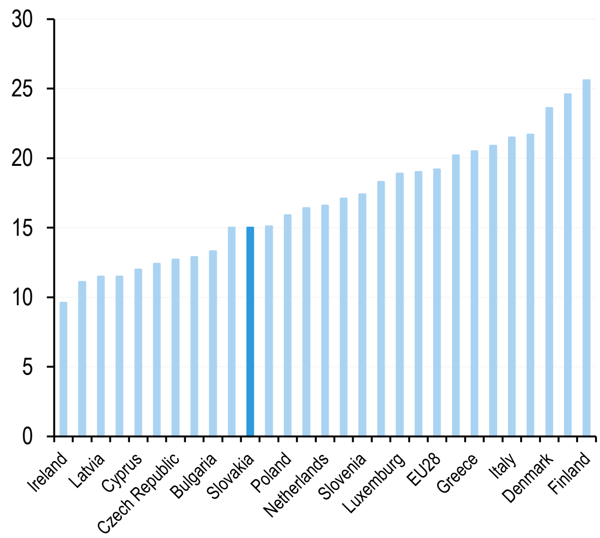
Source: Eurostat, MLSAF SR



Source: Euroslat

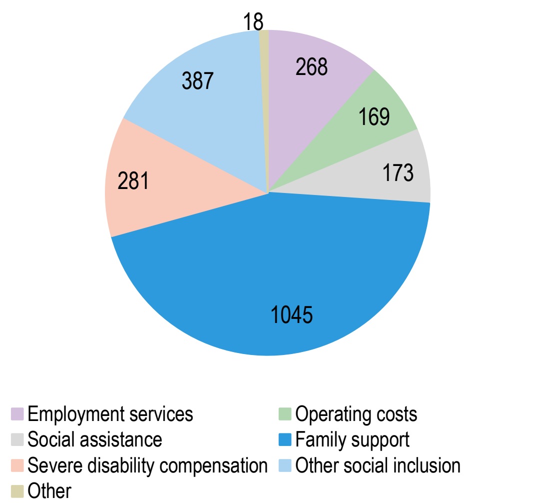
The MLSAF SR's expenditure will reach EUR 2.34 bn in 2018, amounting to 2.6% GDP and 6.6% of the general government budget spend. Three programmes with largest budget concentrate on social inclusion (mainly family support, social protection, and support for people with severe health disability), active labour market policies, and operational expenditures.

CHART 49 - Public expenditures on social security in 2015 (% GDP)



Source: Eurostat, COFOG classification

CHART 50 - MLSAF SR's expenditures in 2018 (EUR mil.)



Source: MF SR

Spending review of the labour market policies and social policies identified measures in the following areas, creating a significant space for spending efficiency improvement - Value for Money increase:

TABLE 20 - Cost saving measures in labor market policies and social policies (EUR mil.)

Area	Task	Potential savings
Family policy	Investigate into the options of better addressability of family benefits	N/A

Fairness of the social system	Implement annual clearance of social security contributions	49
Operation	Improve efficiency of the Social Insurance Company branches	10

Source: MF SR

1. Investigate the possibilities of better targeting of family benefits

The support of family is provided to the beneficiaries regardless of their income. Ideally, family benefits would be conditional upon low income of the household. However, the available data and the controlling possibilities currently do not allow the implementation of effective income testing system. Spending review therefore recommends alternative methods to introduce better targeting into the system and to implement the proper income testing system in a medium-term horizon.

2. Implementation of annual declaration of social security contributions

The social insurance system should be characterized by fair distribution of both the contributions of citizens to the Social Insurance Company and the benefits from the Social Insurance Company provided to the citizens. Therefore, annual declaration of social security contributions will be implemented. introduction of a legislative framework and a reporting methodology would prevent decreases in contributions of high-income groups of population.

3. Improve efficiency of the Social Insurance Company branches

The analysis of the Social Insurance Company branches identified space for better efficiency of their operation amounting up to EUR 10 mil. throughout the horizon of three years, amounting to 16% of their expenditures. It consists of the option to relocate employees to more efficient positions or achieving higher outputs, and nearly one quarter lower costs of energies, goods and services, and lower costs of IT operation.

4. Efficient provision of ALMP based on jobseekers' profile and better placement of jobseekers in the labour market

The expenditures on the ALMP are one of the lowest among OECD countries, their effectiveness and efficiency is low. The number of vacant positions has been growing and their creation does not have to be subsidized any longer. Thus, support of the policies should gradually shift from demand-oriented programmes to supply-oriented programmes (educational and training programmes and consultancy services), which are proofed to be most efficient based on international experience. Better addressability of the ALMP tools based on jobseeker profiling as early as at their first registration with a labour office could increase the number of employed ALMP participants nearly by one half.

5. Deinstitutionalization of foster care provided primarily by foster families

Care by foster families give the child higher value than care by institutional care facilities. It allows for better utilization of public spending, as well.

6. Timely intervention in the case of children with severe health disability and their integration into normal educational process

The number of children with severe health disability placed in foster homes has been growing. Therefore, the MLSAF SR will develop a timely intervention support programme. Their number has grown by nearly 50% since 2010, with the 2015 figure equalling 815. Timely intervention may prevent the need to place a child with SHD into a foster home or his/her placement in a special school. The experience of other countries proofs that timely intervention may improve integration of individual with severe health disability later in life.

7. Return-performance of funds in the second and third pillar and their lower cost

Return-performanceof funds in the second and third pillar is one of the lowest among the OECD countries. Majority of savers' funds are in more conservative guaranteed bond funds which achieve lower returns. The rate of return could be improved by mandatory harmonization of the investment strategy of the existing and new savers with the time horizon of their saving (with the saver's option to choose his/her own strategy). Increased competition and support of motivation of managers and agents to recommend higher return strategies could be helpful as well.

The voluntary pension saving scheme (the third pillar) should be made more attractive by a mixture of policies, including ones to increase the competition. Higher average real appreciation in the third pillar by 1 p.p. could increase monthly pension by as much as 25%. Two policies will be assessed - to allow employer to send voluntary contribution also to the second pillar and a mandatory introduction of an index fund in the third pillar as well.

IV.2. 2018 spending review

One sector revision and two cross-section analyses will be conducted in 2018. The sector analysis will focus on the expenditures and results in agriculture, the cross-section ones on the expenditures on integration of at-risk-of-poverty-and-social-exclusion groups and employment and remuneration in the state and general government.

Agriculture and rural development spending review

The revision will review expenditures amounting to 1.9% GDP a year (EUR 1.8 bn) on the agricultural policy and support of rural development, including the expenditures of the affiliated organisations of the department and the largest enterprises under its managerial control. The aim of the revision is to assess the efficiency of the MARD SR's spending with the emphasis on attainment of better results.

Spending review of integration of the at-risk-of-poverty-and-social-exclusion groups

The spending review will review the expenditures impacting integration of the at-risk-of-poverty-and-social-exclusion groups. It will focus on the efficiency of current protection and integration policies, investigate data collection set-up, outline the of best practice examples, and investigate into the option of their systematic implementation.

Spending review of employment and remuneration in general government

The spending review of public wage bill will assess employment and wages in general government sector, excluding employees working in two sectors - healthcare and education - or employed under special acts (police officers, etc.). Such scope encompasses approx. 234 thousand employees and amounts to EUR 3,3 bn (4,1% of GDP; 9,8% of total general government expenditure). The main objective of the review is to identify possibilities of efficiency increase in human resources utilization.

V. Comparison with the Stability Programme

The February 2017 macroeconomic forecast[68] which was used to compile the Stability Programme for 2017-2020 presupposed GDP growth at the level of 3.3% in 2017 and 4.0% in 2018. The updated Macroeconomic Forecasting Committee's September 2017 forecast which was used for the preparation of the General Government Draft Budget confirms the 3.3% growth for 2017. The economy growth actually estimated for 2018 is faster (4.2%). The GDP growth forecast in the next years is at the level of 4.4% in 2019 and 3.9% in 2020.

TABLE 21 - Forecast of selected economic development indicators in SR

No.	Indicator	unit	Stability Programme				Draft budget			
			2017	2018	2019	2020	2017	2018	2019	2020
1	GDP, current prices	EUR bn	84.6	89.4	95.1	100.7	84.6	89.5	95.3	101.0
2	GDP, permanent prices	%	3.3	4.0	4.4	3.8	3.3	4.2	4.4	3.9
3	Final consumption of households and non-profit institutions serving households (NISD)	%	2.5	2.7	2.9	2.9	3.4	2.9	2.9	2.9
4	Final general government consumption	%	1.6	2	1.9	1.4	0.4	1.3	1.6	1.6
5	Gross fixed capital generation	%	3	1.9	2	3.6	3.0	4.2	3.2	3.2
6	Export of goods and services	%	5.6	7.3	7.7	6.2	7.4	9.1	9.8	8.2
7	Import of goods and services	%	4.2	6	6.3	5.5	7.6	8.2	8.4	7.4
8	Output gap (share in potential product)	%	0.2	0.7	1.3	1.3	0.2	0.8	1.3	1.3
9	Average monthly wage in the economy (nominal growth)	%	3.5	4.4	4.8	5.1	3.9	4.6	4.8	5.2
10	Average employment growth, Labour Force Sample Survey, LFS	%	1.7	1.1	0.9	0.9	1.6	1.1	0.8	0.7
11	Average employment growth by ESA 2010	%	1.8	1.1	0.9	0.9	1.9	1.4	1.0	1.0
12	Average unemployment rate by	%	8.4	7.6	4.9	6.2	8.2	7.3	6.7	6.1
13	Average registered unemployment rate	%	8.1	7.4	6.7	5.9	7.2	6.4	5.8	5.2
14	Harmonised index of consumer prices (HICP)	%	1.1	1.7	1.9	2.1	1.3	1.7	1.9	2.1
15	Current account balance (percentage of GDP)	%	1.7	2.4	3.2	3.7	-0.9	-0.1	1.1	1.9

Source: MF SR

The current Draft Budgetary Plan confirms the plan of attainment of a balanced budget until 2020 in accordance with the Manifesto of the Government. Compared to the Stability Programme, the general government balance result is expected to worsen in 2016 by 0.5 p.p which is caused particularly by the dropout of the corporate tax revenues and, further, by the application of the super-dividend test which had a backward corrective effect on the accrual income from the dividends of the state. The 0.4 p.p. higher deficit in the current year compared to the budget reflects the structural correction of the corporate tax revenues and the use of higher revenues from contributions for additional funding of healthcare. The corporate tax revenue dropout has a structural effect within the entire horizon and explains the revision of objectives in 2018 and 2019. Subject to the Manifesto of the Government and the assumptions of the Stability Programme, the Government plans to attain budget equilibrium until 2020.

[68] Officially approved by the Macroeconomic Forecasting Committee.

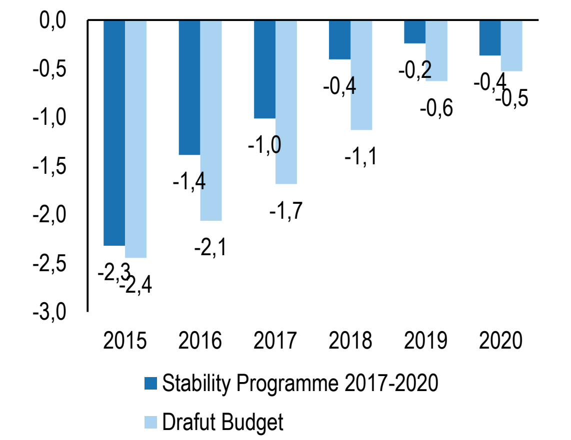
TABLE 22 - Comparison with the Stability Programme

	ESA code	2016	2017	2018	2019	2020
		% GDP	% GDP	% GDP	% GDP	% GDP
Target balances of general government	**B.9**					
Stability Programme (1)		-1.68	-1.24	-0.50	0.00	0.00
Draft Budgetary Plan (2)		-2.19	-1.63	-0.83	-0.10	0.00
Difference (2-1)		**-0.51**	**-0.39**	**-0.33**	**-0.10**	**0.00**
Balances of general government based on NPC scenario	**B.9**					
Stability Programme (1)		-	-	0.00	0.13	0.63
Draft Budgetary Plan (2)		-	-	0.05	0.17	0.56
Difference (2-1)		-	-	0.05	0.04	-0.07

Source: MF SR

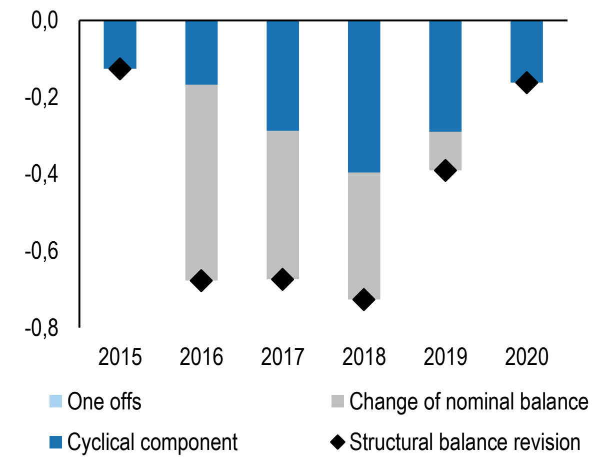
Further to the update of the budget objectives and the economy overheating rate over the budgeting horizon, the medium-term objective is expected to be attained in 2020[69]. Structural balance was significantly revised for 2016-2018 which is, to the extent of one third up to one half, explained by the update of the GG nominal balances. The remaining portion can be attributed to the revision of the output gap estimate[70]. Current estimates of output gap expect faster movement of the Slovak economy above its potential. With nearly identical nominal objectives in 2019 and 2020, this leads to the correction of structural deficit upwards by 0.4 or 0.2 per cent of GDP[71].

CHART 51 - Comparison of structural balance under the Stability Programme and the Draft Budgetary Plan



Source: MF SR

CHART 52 - Contributions of factors on the structural balance revision



Source: MF SR

[69] Under the budget objectives set and the estimate of the cyclical component in the Stability Programme for 2017-2020, MTO was expected to be attained in 2018.

[70] Since publication of the Stability Programme for 2017-2020, also the output gap estimate was affected; output gap estimate is an input for the structural balance calculation through the cyclical component estimate. Besides standard update of the macroeconomic data, the MF SR compared to the Stability Programme made use of the September 2017 output gap approved by the Macroeconomic Forecasting Committee (instead of the standard method of replicating the EC's estimates based on the MF SR's macroeconomic assumptions). More in BOX 1.

[71] Rounded to one decimal point

ANNEXES

Annex 1 - Structural balance

The structural balance is the difference between the revenues and expenditures of the general government without one-off and temporary impacts and provided that the economy is at the level of its potential. Despite use of multiple unobserved variables for its calculation, the structural balance is likealy to provide a more accurate picture of the medium-term fiscal position of a country compared to the nominal balance.

The Stability and Growth Pact is based on the assumption that the Member States should adopt a symmetric approach to the fiscal policy in accordance with the cyclical development of economy. The basic objective is to focus more on budgetary discipline in the years of economic recovery aiming to avoid the pro-cyclical nature of fiscal policy and gradually attain medium-term budgetary objective. Such behaviour should lead to accumulation of fiscal buffers for future years marked by economic recession, decrease in the public debt at a reasonable rate, and positive influence on the long-term sustainability of public finance.

The below matrix clarifies and specifies the requirements of the Stability and Growth Pact for fiscal consolidation within its preventive arm. This matrix is symmetric and distinguishes between larger consolidation efforts which should be used at better times and smaller efforts used under hard economic conditions.

		Required y/y consolidation	
	Condition	Debt under 60% and no sustainability risk	Debt above 60% or sustainability risk
Exceptionally severe period	Real GDP growth < 0 or output gap < -4	Without requirement for consolidation	
Very severe period	-4 ≤ output gap (OG) < -3	0	0.25
Severe period	-3 ≤ output gap (OG) < -1.5	0 in the event of opening OG, 0.25 in the event of closing OG,	0.25 in the event of opening OG, 0.5 in the event of closing OG,
Normal period	-1.5 ≤ output gap (OG) < 1.5	0.5	> 0.5
Good period	output gap (OG) ≥ 1,5	> 0.5 in the event of opening OG, ≥ 0,75 in the event of closing OG	≥ 0,75 in the event of opening OG, ≥ 1 in the event of closing OG

The assessment of compliance with structural balance and the expenditure benchmark is reviewed based on a one-year and two-year deviation given as a percentage GDP. One-year deviation with the limit of -0.5% GDP and two-year deviation with the limit of -0.25 per cent of GDP.

Calculation of structural balance

Within the first step, the nominal balance of public finance is adjusted using the cyclical component for the effect of economic fluctuations (estimated with the help of output gap, i.e. difference between the actual and potential GDP level). The output gap estimate is based on the actual September 2017 macroeconomic forecast of the Ministry of Finance SR (more in BOX 1). The estimate of the general government balance sensitivity to changes in the output gap based on the OECD[72] methodology is adopted by the Ministry of Finance SR in full extent from the EC. In the next year, this balance is adjusted for the effect of the so-called one-off and temporary measures the fiscal influence

[72] Original methodology was presented in Girouard, N., André, Ch. 2005): Measuring cyclically-adjusted budget balances for OECD countries. The methodology was updated in 2014 and new data was incorporated for elasticity calculation purposes. The methodology was approved by the Member States in September 2014.

of which will not recur in the coming years. For the purposes of the draft budgetary plan, the Ministry of Finance SR proceeds in their identification in accordance with the EC methodology[73].

Methodology of the European Commission (EC) [74] characterizes one-off measure as a temporary measure which is not of a permanent nature and which arose independently of government decisions. EC developed a Directive for classification of one-off measures.

1. **Principle:** Only temporary and non-recurring impact on general government revenues or expenses can be classified as a one-off impact.
2. **Principle:** One-off nature cannot be decreed by law or by an autonomous government decision.
3. **Principle:** Volatile components of revenue and expenditure should not be considered as one-off impacts. Smoothing of time series is done using the cyclical component in calculation of the SB.
4. **Principle:** Deliberate policy actions that increase the deficit cannot be classified as one-offs.
5. **Principle:** Only measures with a significant impact on general government budget (higher than 0.05% GDP) should be classified as a one-offs.

All typical one-off measures are described in Chapter 3.3 (Report of Public Finances in EMU[75]). Moreover, EC has defined as specific exceptions and procedures thereto, as to when a one-off measure can be classified as an impact which contradicts the aforementioned principles; such examples are also provided in the aforementioned chapter

TABLE 23 - One-off and temporary measures (ESA 2010, EUR mil.)

	2015	2016	2017	2018	2019	2020
Correction of the contribution to EU budget	-	-35	-	-	-	-
TOTAL	**0**	**-35**	**0**	**0**	**0**	**0**

(+) improving the balance, (-) worsening the balance *Source: MF SR*

Despite the conflict with Principle 5 (the rule of impact above 0.05% of the GDP) of the EC Directive, considering the horizontal nature (applicable to all countries), the following can be classified as one-offs:

- Correction of the contribution to EU budget

[73] Vade Mecum on the Stability and Growth Pact – 2017 Edition – Guiding principles p. 28. The MF SR developed a manual in past in accordance with the existing EC methodology which details the rules for identification of one-off and temporary effects in the national methodology.
[74] Vade Mecum on the Stability and Growth Pact – 2016 Edition – Guiding principles p. 28.
[75] Report on Public Finances in EMU, December 2015: http://ec.europa.eu/economy_finance/publications/eeip/pdf/ip014_en.pdf.

Annex 2 - Expenditure benchmark

The revised Stability and Growth Pact introduced an expenditure benchmark as a supplementary tool to analyse the fiscal position. It shows the year-on-year growth of the expenditure aggregate net of revenue measures, which enables the assessment of the progress achieved in fiscal consolidation compared against the permitted expenditure growth reference rate, similarly to the structural balance development.

According to the expenditure benchmark, the real growth of general government expenditures should not exceed the average potential economic growth. The expenditures are permitted to grow faster only if in case of implementation of additional revenue measures confirmed by quantification by an independent Committee (as a discretionary revenue measure)[76]. For countries which have already achieved their medium-term budgetary objective (MTO), the growth of expenses can be identical with the potential of the economy. For countries which have not yet achieved their MTOs, the expenditure growth rate shall reflect the fiscal consolidation necessary for achieving the MTO. In such case, the potential growth rate of the economy is adjusted for necessary consolidation effort.

The development of expenditures is adjusted for the factors which are beyond the Government's control. This includes interest expenditures, changes in unemployment benefit expenditures resulting from the existing business cycle and expenditures financed from the EU funds. Considering the high volatility of government investments, the amount of the investments is smoothed to average amount of investments for the current year and the prior three years[77]. The nominal growth of such adjusted expenditures is consequently translated to real growth by means of a GDP deflator, to allow referencing against the expenditure benchmark.

When comparing the year-on-year development of the expenditure aggregate to the expenditure benchmark, it appears that the growth rate of expenditures was exceeded in 2015 (Chart 16) which was partly owing to the necessity of co-financing of strong absorption of EU funds. Evaluation of the conformity between the development of expenditures and the expenditure benchmark, account is taken of the deviations over two horizons (Chart 17), expressed as % of GDP. **Subject to monitoring is a one-year deviation (difference between the expenditure aggregate and the expenditure benchmark calculated as % of the GDP) with a limit of -0.5 per cent of GDP and a two-year deviation (average of deviations of the current and prior year) which is given a higher priority owing to lower volatility and dependence on the current year, with a limit of -0.25 per cent of GDP.** If the deviation is worse than the pre-set limit, it is regarded as a significant non-compliance with the expenditure benchmark and we proceed with overall evaluation of the fiscal position.

TABLE 24 - Expenditure benchmark*

		2015	2016	2017 OS	2018	2019	2020
1. Total expenditures	EUR mil.	**35,692**	**33,684**	**34,686**	**35,175**	**37,277**	**38,859**
2. Interest cost	EUR mil.	1,379	1,336	1,110	1,136	1,126	1,079
3. Expenditures covered by EU (capital)	EUR mil.	2,345	507	483	51	463	419
3a. Expenditures covered by EU sources (total)	EUR mil.	2,789	796	810	346	1,375	1,227
4. Capital expenditures covered by national sources	EUR mil.	2,606	2,093	2,328	2,113	2,103	2,244
5. Smoothed capital expenditures (national sources 4-year moving average)	EUR mil.	1,944	2,062	2,270	2,285	2,159	2,197
6. Cyclical expenditures on unemployment benefits	EUR mil.	7	2	-2	-8	-15	-16
7. Expenditures fully covered by the automatic increase in revenues	EUR mil.	0	0	0	0	0	0
8. Primary expenditure aggregate (1-2-3a-4+5-6-7)	EUR mil.	**30,855**	**31,519**	**32,709**	**33,873**	**34,847**	**36,522**

[76] Positive cyclical revenues at the time of economic boom (not gained through discretionary measures) allow for the growth of expenditures above the potential of the economy. The expenditure benchmark monitors this unwanted fiscal impact whereas temporary increase in revenues from measures not taken should be used for the attainment of MTO.

[77] Vade Mecum on Stability and Growth Pact, p. 30.

9. Y/y change of primary expenditure aggregate (8t-8t-1)	EUR mil.	1,914	664	1,190	1,164	974	1,675
10. Change in revenues due to discretionary revenue measures	EUR mil.	139	-174	184	-1	79	26
11. One-off measures on the revenue side	EUR mil.	0	0	0	0	0	0
12. One-off measures on the expenditure side	EUR mil.	0	-35	0	0	0	0
13. Methodological adjustments	EUR mil.	0	-34	0	0	0	0
14. Nominal growth of expenditure aggregate adjusted for revenue measures ((9t-10t)/8t-1)	%	6.1	2.5	3.2	3.6	2.6	4.7
15. Real growth of expenditure aggregate adjusted for revenue measures	%	5.4	1.3	2.0	2.0	0.6	2.6
16. Expenditure benchmark (reduced reference rate of the GDP potential growth)	p.p.	3.6	2.1	1.4	1.5	1.6	2.6
17. Deviation from the expenditure benchmark (16-15)	p.p.	-1.8	0.7	-0.6	-0.5	0.9	0.0
One-year deviation from the expenditure benchmark	% GDP	**-0.7**	**0.3**	**-0.2**	**-0.2**	**0.3**	**0.0**
Two-year deviation from the expenditure benchmark	% GDP	**0.2**	**-0.2**	**0.0**	**-0.2**	**0.1**	**0.2**
p. m. GDP deflator	*%*	*0.7*	*1.2*	*1.2*	*1.5*	*2.0*	*2.1*
Deviation limit on 1y horizon		-0.5	-0.5	-0.5	-0.5	-0.5	-0.5
Deviation limit on 2y horizon		-0.25	-0.25	-0.25	-0.25	-0.25	-0.25

** The input data of the years 2019 and 2020 also reflect the required measures on the revenue and the expenditure sides to attain the nominal deficit targets. Working based on the assumption that the measures will be taken to the approximately same extent on the revenue (as discretionary revenue measures) and the expenditure side in each of the years.* *Source: MF SR*

Annex 3 - Discretionary revenue measures (DRM)

The EC methodology defines discretionary revenue measures as legislative measures having impact on the revenues of the general government. They are assessed using the so-called additional impacts (marginal changes) of these measures. They are either permanent or one-off measures. Permanent measure is recorded along with the impact in the first year (when it becomes effective) and without the impact in the following years. In other words, the change of an impact of the measure in the following years due to macroeconomic development is not taken into account. If there occur various impacts due to postponed validity of the measure, only the marginal change is recorded.[78] As regards one-off revenue measures, the impact is recorded in one year and the following one reports a dropout in the same amount, this means that the whole impact of the measure in two consecutive years is nil.

TABLE 25 - Discretionary measures (EUR mil., ESA 2010)

	Total impact						Additional impact					
Description	2015	2016	2017	2018	2019	2020	2015	2016	2017	2018	2019	2020
Decrease in the bank levy rate from 2015, planned to be revoked from 2017	-42		-50				-42		-50			
Changes in burden on contributions	-8						-8					
Changes in tax depreciation of assets	123						123					
Measures to increase tax collection (ERP and farmafirmy)	56						56					
Thin capitalisation rules implementation	47						47					
Deduction of research and development expenses from the tax base	-2						-2					
Audit of tax expenses and other	12						12					
Opening of the second pillar - current impact	16	29					16	13				
Tax deductible item from contributions	-62	-171	-155	-143	-122	-107	-62	-109	16	12	20	15
Act 222/2004 Coll. on VAT, loosening conditions for payment of NO within 30 days	-3	3					-3	7				
VAT - rate reduction for selected foodstuff		-77						-77				
Increase in the number of cigarettes in a pack from 19 to 20 from 1 March 2016		4	6					4	1			
Taxation of cigars and cigarillos depending on the weight			6						6			
Acts 595/2003 and 580/2004 - support of investments in capital market		-11						-11				
Corporate income tax - rate reduction to 21%			-113						-113			
Increase in the compensation for services			25						25			
Doubling of OO rate in regulated sectors, amending conditions and calculation, decrease in 2019			60		33				60		-27	
Increase in the excise tax on tobacco products from 1 Feb 2017 and 1 Feb 2019			30		68				30		39	
Keeping the OO rate of financial institutions at 0.2%			50						50			
Taxation of dividends - 7% excise tax				51						51		
Other - interest on retained NO, more efficient tax administration			3						3			
Individual income tax - exemption from the corporate income tax for the income of the Resolution Council (Rada pre riešenie krízových situácií)			-5						-5			
Lump-sum expenditures - 60% max. EUR 20 thousand			-13	-21	-25				-13	-7	-4	
Cancellation of the MAB for health insurance			90	77					90	-14		

[78] An illustrative example explaining DRM is an adopted legislative measure with the impact estimated at 200. The measure was implemented halfway through the year, which means that its total impact in that year is 100. In the next year, the impact will grow reaching the whole amount 200, but in marginal terms only the difference of these two years will be recorded, i.e. 100. Cumulative impact equals 200, it is only split into two years.

Increase in the MAB for social contributions			57						57			
Revocation of tax license				-83						-83		
Increase in the real estate tax rate			16						16			
Non-life insurance (8% levy)			18	20					18	2		
Fee for development			1						1			
Higher revenues from gambling (change in contributions)			18						18			
Increase in the contribution to the second pillar (automatic from 2017 by 0.25 p.p./year)			-27	-59	-93	-131			-27	-32	-34	-38
Increased deduction of the cost of research and development from 1 Jan 2018				-9						-9		
Introduction of separate depreciation of technical upgrade from 1 Jan 2018				0	-1					0	-1	
Introduction of non-deductible component on spa care from 1 Jan 2018				-2						-2		
Mineral oil excise tax - change in rates for naphtha oil and gasoline from 1 Jan 2018				-1	0					-1	0	
Licenses in gambling + change in gambling taxation				65	28					65	-38	
Excise tax on premiums				16	32					16	16	
Required revenue measures					107	156					107	49
TOTAL	**139**	**-223**	**17**	**-88**	**28**	**-82**	**139**	**-174**	**184**	**-1**	**79**	**26**

Source: MF SR

Annex 4 - Macroeconomic and Tax Forecasting Committees

The Draft Budgetary Plan for 2018-2020 is based on the September 2017 macroeconomic and tax forecasts over the horizon of 2018-2020. Both the macroeconomic scenario and the forecasted tax revenues are subject to ongoing discussion, approval and inspection by experts by way of committees which comprise national experts from both the public and the private sectors. Deadlines for publication of forecasts and the principles of the activity of the committees are laid down in the Budgetary Discipline Act.

After the September 2017 meeting of the Macroeconomic Forecasting Committee, all members assessed the medium-term macroeconomic forecast of the MF SR as **realistic**.

TABLE 26 - Assessment of the February forecast of the MF SR by the Macroeconomic Forecasting Committee

Committee member	Forecast characteristics
NBS, Infostat, UNICREDIT Bank, VÚB, Tatrabanka, SLSP, Sberbank, ČSOB, SAV	realistic

Source: Macroeconomic Forecasting Committee

TABLE 27 - Average forecast of the Committee members* (except the MF SR) and the forecast of the MF SR

	2016	2017		2018		2019		2020	
in %, unless provided otherwise		Committee	MF SR	Committee	MF SR	Committee	MF SR	Committee	MF SR
Gross domestic product, real growth	3.3	3.3	3.3	3.9	4.2	4.2	4.4	3.7	3.9
Gross domestic product in current prices; EUR bn	81.0	84.5	84.6	89.2	89.5	95.0	95.3	100.2	101.0
Final consumption of households; real growth	2.9	3.4	3.4	3.3	2.9	3.0	2.9	2.8	2.9
Final consumption of households; nominal growth	2.5	4.7	4.8	5.1	4.6	5.1	4.8	5.0	5.0
Average monthly wage; real growth	3.8	3.0	2.6	2.8	2.9	2.7	2.9	2.7	3.1
Average monthly wage; nominal growth	3.3	4.3	3.9	4.5	4.6	4.6	4.8	4.9	5.2
Employment rate growth (statistical reporting)	2.5	1.9	1.9	1.2	1.4	1.0	1.0	0.9	1.0
Consumer price index; average growth; CPI	-0.5	1.2	1.3	1.8	1.7	2.0	1.9	2.1	2.1
Current account balance; percentage of GDP	-0.7	-0.6	-0.9	-0.1	-0.1	0.9	1.1	0.8	1.9

**Macroeconomic Forecasting Committee Macroeconomic Forecasting Committee*

Tax Forecasting Committee

The MF SR presented their updated medium-term forecast of tax revenues for 2017-2020 in the September 2017 session of the Tax Forecasting Committee. The medium-term forecast of tax revenues and social contributions of the MF SR was assessed by all members of the Committee as **realistic**.

TABLE 28 - Assessment of the forecast of the MF SR by the Tax Forecasting Committee

Committee member	Forecast characteristics
NBS, Infostat, Tatra banka, ČSOB, KRRZ, SLSP, UniCredit Bank	realistic

Annex 5 - Mandate for spending reviews for 2018

Terms of Reference: Agriculture and rural development spending review

The agriculture and rural development review in the amount of 1.9% GDP a year (EUR 1.8 bn[79]) will review the expenditures on the agricultural policy and support of rural development, including the expenditures of the affiliated organisations of the department and the largest enterprises under its managerial control. The aim of the revision is to assess the efficiency of the MARD (Ministry of Agriculture and Rural Development of the Slovak republic) spending with the emphasis on attainment of better results.

Performance objectives

The main objectives of the government in the area of agriculture include support of rural development and improvement of the living conditions of rural population. Government seeks to support agriculture and livestock production productivity increase, development of free market with agricultural products and free competition in agricultural business. In compliance with the Common Agricultural Policy rules, the Government will seek higher support to sectors which could potentially work as sources of employment. The Government perceives the agricultural land and forests as an integral part of the rural environment which requires to be managed in line with the principles of sustainable development.

TABLE 29 - Performance indicators for agriculture and rural development

		2009	2010	2011	2012	2013	2014	2015	2016
Forest land fund and forest plots (km²)	SK	20,093	20,108	20,115	20,124	20,134	20,143	20,147	
Hectare yields (cereals) (t/ha)	SK	4.3	3.7	5.01	3.8	4.5	6.0	5.08	6.4
Hectare yields (oil crops) (t/ha)	SK	2.2	1.9	2.23	2.0	2.4	3.1	2.3	3.1
Hectare yields (fodder plants) (t/ha)	SK	4.3	4.3	3.88	3.8	4.2	4.5	4.07	4.7
Nitrogen balance (kg/ha)	SK		46	34	42	49	46		
	EU		51	51	52	51	51		
	V3		52	54	60	56	44		
Gross livestock production (EUR/ha)	SK	392	438	404	427	429	406	373	
Rural population (% of total population)	SK	45.0	45.3	45.6	45.8	46.1	46.2	46.4	46.5
	EU	26.5	26.3	26.1	25.8	25.6	25.4	25.2	25.0
	V3	32.4	32.3	32.2	32.1	32.0	31.9	31.7	31.6

Source: SO SR, Eurostat, World Bank

Fiscal objectives

The review will focus on the evaluation of the MARD SR's expenditures with the emphasis on higher efficiency and analysis of social and economic effects and costs of planned investments and policies. Reallocation of expenditures to the programs with the highest efficiency and optimum allocation in the coming programming period of the Common Agricultural Policy will be suggested.

Future expenditures on projects implemented from the EU funds in the program period 2014-2020 are taken from the general government budget for 2018-2020.

A majority of the department's expenditures goes to direct payments for farmers, rural development measures, and the regional operating program measures.

TABLE 30 - Expenditures of the Department of Agriculture and its state-owned enterprises*

[79] Average of 2018-2020 spending of the department under the draft GGB, most recent available cost of state-owned enterprises and proportionally allocated spending of the Integrated Regional Operating Programmes in 2021-2023.

EUR mil.	2014 A	2015 A	2016 A	2017 E	2018 B	2019 B	2020 B
Stabilization of agriculture and the market with agricultural commodities	381	401	419	661	485	491	492
Rural development 2014-2020	70	60	163	880	310	301	318
Operating Programs of Regional Development 2014-2020	-	-	39	200	221	615	472
Regional development	114	341	54	1			
Rural development	124	318	4	0	0	0	0
Creation, regulation and implementation of policies	46	58	45	53	36	36	36
Food safety, health and protection of animals and plants	35	39	43	34	28	28	28
Support of competitiveness of agriculture and food industry	54	32	46	13	3	3	3
Sustainable forest management	5	5	4	5	2	2	2
Information technologies funded from the state budget	-	-	-	4	3	3	3
Other programs	1	1	1	0	0	0	0
Total for the Department of Agriculture	**827**	**1,256**	**820**	**1,851**	**1,089**	**1,480**	**1,355**
Department's state-owned enterprises	**232**	**249**	**267**				
out of that Lesy Slovenskej republiky, š.p. (*Forests of the Slovak Republic*)	207	213	219				
Total for the Department of Agriculture and state-owned enterprises	**1,059**	**1,504**	**1,087**	**1,851**	**1,089**	**1,480**	**1,355**

* state-owned enterprises - costs in the relevant year or most recent data
** A – actual, E – estimate, B – budget

Source: MF SR

Areas subject to review

The most important areas of the review will include the efficiency of direct payments to farmers, expenditures on rural development within the Rural Development Programme, and expenditures of the Integrated Regional Operating Program. The review will also focus on the analysis of monitoring and evaluation tools and increasing the quality of forest fund. Furthermore, it will review the options of reducing agriculture-incited environmental burden.

The review will also concentrate on the efficiency of the MARD SR and the affiliated organisations including the state-owned enterprises. The Department of Agriculture comprises of 19 affiliated organisations employing around 7.5 thousand employees. The most important, in terms of budget, out of the organisations under the Department's control is the Agricultural Paying Agency (*Pôdohospodárska platobná agentúra*). The MARD SR has important state-owned enterprises under its managerial control with the yearly expenses reaching around EUR 280 mil.; the most significant include Lesy Slovenskej republiky, Plemenárske služby, and Agrokomplex.

Responsibility and deadlines

The interim and final reports are the responsibility of the MF SR which creates them in cooperation with MARD SR. For the purposes of preparation of the analyses of the areas above, the MARD SR and the MF SR commit to cooperate in the provision of complete and detailed data and information. The interim report will be drafted and published by the end of October 2018; the final report will be prepared and published by March 2019.

Terms of Reference: Integration of the at-risk-of-poverty-and-social-exclusion groups spending review

The spending review will assess public expenditures with an impact on social inclusion of groups at risk of poverty and social exclusion. It will focus on the effectiveness and efficiency of current protection and inclusion policies, evaluate the current system of data collection, highlight examples of good practices and explore the possibilities of their mainstreaming.

Performance objectives In 2016, 18.1% of Slovaks were at risk of poverty or social exclusion, 8.2% of the population suffered severe material deprivation. While aggregate national values are comparable with the EU average, the situation of selected groups is considerably unfavorable.

In case of marginalized Roma communities, segregation, unemployment, low level of educational attainment and health, poor housing conditions and poverty are cause and consequence of social exclusion and discrimination and leads to intergenerational prevalence. Compared to the EU countries, the labor market participation of people living with disabilities is below average, and as much as third of single parent households with dependent children face the risk of poverty. The Slovak education system is lagging behind in its ability to correct the adverse impact of socio-economic disadvantage, to engage the most vulnerable in pre-school education and to develop a quality and inclusive education system.

The need for a cross-cutting, cross-sectoral spending review was already revealed in the previous spending reviews on education, labor market policies and social policy. This terms of reference builds upon these commitments, as well as on related strategic documents; in particular on the National Framework Strategy on Support of Social Inclusion and Fight against Poverty and others focusing on related target groups and sectoral policies[80]..

TABLE 31 - Performance indicators of social inclusion

		2009	2010	2011	2012	2013	2014	2015	2016	Target 2020
People at risk of poverty or social exclusion (%)	SR	19.6	20.6	20.6	20.5	19.8	18.4	18.4	18.1	17.2
	EU	23.3	-	24.3	24.7	24.6	24.4	23.8	-	
Children at risk of poverty or social exclusion (%, parents with less than primary, primary and lower secondary education)	SR	97.9	97.1	87.5	94.0	89.8	89.9	93.2	90.8	
	EU	-	63.4	62.9	65.1	65.6	66.5	68.2	-	
Severe material deprivation of people with long-standing activity limitation due to health problems (%)	SR	13.8	14.1	14.0	13.7	12.6	11.6	12.5	-	
	EU	-	11.2	12.1	12.8	12.6	12.1	11.3	-	
PISA - performance by students' socio-economic status (average score of students in the bottom quarter of ESCS[81])	SR	430 *(2006)*	-	-	-	-	-	414	-	
	OECD	453 *(2006)*	-	-	-	-	-	452	-	
Share of 15-year-old pupils who are at level 1 or below of the PISA combined reading literacy scale (%)	SR	22.2			28.2			32.1		
	EU	19.5			17.8			19.7		
PISA – percentage of variation in performance explained by pupils´ socio-economic status (%)	SR	14.6	-	-	24.6	-	-	16.2	-	
	OECD	14.0	-	-	14.8	-	-	12.6	-	
Pre-school enrolment rate of children living in Marginalised Roma	MRC	-	-	25	-	-	-	-	-	100
	close to MRC	-	-	56	-	-	-	-	-	-

[80] Strategy of the Slovak Republic for Integration of Roma up to 2020, National Programme for the Development of living conditions of persons with disabilities 2014 – 2020, National Action Plan for Children 2013-2017, National Strategy for Protection of Children against Violence, National Program for Development of Education and Training (Učiace sa Slovensko), Migration and Integration policy of the Slovak Republic, etc.
[81] ESCS – index of economic, social and cultural status, more details at https://stats.oecd.org/glossary/detail.asp?ID=5401

		2009	2010	2011	2012	2013	2014	2015	2016	Target 2020
communities(MRC) and nearby MRC (%, 3-6 years)										
Gross enrolment rate in upper-secondary education (%, 16-19 years)	MRC	-	-	35	-	-	-	-	-	-
	close to MRC	-	-	74	-	-	-	-	-	-
Early leavers from education and training (% of the population aged 18-24 with at most lower secondary education and not in further education or training)	SR	4.9	4.7	5.1	5.3	6.4	6.7	6.9	7.4	6
	EU	14.2	13.9	13.4	12.7	11.9	11.2	11.0	10.7	10
Long-term unemployment rate (% of active population aged more than 15 years)	SR	6.6	9.3	9.3	9.4	10	9.3	7.6	5.8	-
	EU	3	3.8	4.1	4.6	5.1	5.0	4.5	4.0	-
Young people not in education, employment, or training (NEET, % aged 15-24)	SR	18.8	20.9	20.9	21.2	21.5	21.4	19.9	18.2	
	EU	15.9	16.4	16.6	17.1	17.2	16.6	16.1	15.6	
Unemployment rate for low-skilled workers (less than primary, primary and lower secondary education, %, aged 15-64)	SR	41.7	44.3	42.6	44.7	42.6	41.4	37.7	31.7	
	EU	14.8	16.0	16.7	18.6	19.7	19.0	17.8	16.6	
Unemployment rate of people living with disability – LFS (%)	SR	-	-	-	-	14.0	17.2	16.6	-	-

Source: MF SR

Fiscal objectives

The objective of the spending review is to identify and assess public expenditures and policy instruments with an impact on the inclusion of groups at risk of poverty and social exclusion in the field of education, social and labor market policies, health, housing, regional development, financial inclusion and antidiscrimination. The spending review will present recommendations on changes in policies and highlight financial measures needed to implement them with the aim of improving the social inclusion of the groups concerned. The revision will also outline the social costs of discrimination.

Areas of the spending review The spending review will examine the expenditures and service programs addressing needs of particularly vulnerable groups; especially marginalized Roma communities, vulnerable children, single parent households with dependent children, people living with disabilities, people with difficult access to housing and homeless people.

Considering the multidimensional nature of social exclusion and poverty, the spending review will examine the effectiveness and efficiency of public expenditures, identify examples of good practices as well as the institutional and financial preconditions of their systematic mainstreaming into public policies. Since data at national level often do not sufficiently reflect socially excluded groups, the review will also draw on available anonymized administrative data. It will also assess the framework of data collection and define suitable indicators for monitoring social inclusion policy outcomes, building also on surveys of the European Union Agency for Fundamental Rights (FRA) and the United Nations Development Programme (UNDP) as well as the Atlas of Roma Communities.

Responsibilities The Ministry of Finance will be responsible for the interim and final reports in cooperation with the Office of the Plenipotentiary of the Government of the Slovak Republic for Roma communities and other relevant ministries, especially the Ministry of Education, Science, Research and Sport, Ministry of Labour, Social Affairs and Family and the Ministry of Interior. The revision will be supported by the Ministry of Health, Ministry of Justice, Ministry of Transport and Construction and the Ministry of Agriculture and Rural Development. For the purposes of analyzing the above-mentioned areas, they are committing to cooperate in providing complete and detailed data and information. The interim report will be prepared and published by the end of October 2018, the final report will be drafted and published by March 2019.

Terms of Reference: Employment and compensation in general government spending review

The spending review of public wage bill will assess employment and wages in general government sector, excluding employees working in two sectors - healthcare and education - or employed under special acts (police officers, etc.). Such scope encompasses approx. 234 thousand employees and amounts to € 3,3 bn (4,1% of GDP; 9,8% of total general government expenditure). The main objective of the review is to identify possibilities of efficiency increase in human resources utilization.

Objectives, tasks and results

The main purpose of public wage bill assessment is to ensure proper operation of public institutions and appropriate public administration execution. Public employment and wages should be managed in a way that guarantees effective allocation of human resource and provides public employees with competitive conditions compared to the private sector.

The review will be focused on three main issues: adequacy of number of employees, level and structure of employees' compensations and productivity of employees. Moreover, there will be several institutions selected for detailed wage audit.

Share of employment in public administration, defense, education, human health and social work activities as a percentage of total employment in Slovakia is lower than both the Eurozone and also EU28 average. Similarly, the position of Slovakia is below the EU average when looking at the compensation of employees in general government sector as a percentage of GDP. The review will examine structure of employment and wages in public sector in a detailed way.

TABLE 32 – Selected employment and compensation indicators

		2010	2011	2012	2013	2014	2015	2016
Compensation of employees in general government sector, % of GDP (%)	SK	8,5	8,3	8,2	8,6	8,8	9	9,1
	V3	9,7	9,8	9,7	9,8	9,8	9,8	10,1
	EU (28)	10,9	10,6	10,5	10,4	10,3	10,1	10,1
	EA (19)	10,7	10,5	10,4	10,4	10,3	10,1	10
Employment in public administration, defense, education, human health and social work activities, % of total employment (%)	SK	20,9	20,5	20,3	20,4	20,6	20,4	20,3
	V3	19,9	19,7	19,7	20,2	20,2	20,3	20,2
	EU (28)	23,4	23,3	23,4	23,7	23,7	23,7	23,6
	EA (19)	23,9	23,8	23,9	24,2	24,2	24,2	24,2

Source: Eurostat

Scope of the review

In 2016, there were over 411 thousand employees working in the general government sector. Sum of their compensations amounted to around € 6,8 bn, which is approximately 20% of total general government expenditure.

The review will assess employees employed under the Civil Service Act, Labor Code and Act on Service in public interest. The review excludes employees of healthcare and education sectors and employees under special acts (e.g. police officers, firefighters, etc.). Total number of employees included in the scope of revision is approx. 234 thousand.

TABLE 33 – General government employees (2016)

	Included in the Review	Number of empl. (th.)	Wages (€ bn)	Personal expenses (€ bn)
Labor Code*	yes	84,6		
Civil service Act	yes	38,6	0,5	0,7

Service in Public Interest performance*	partially	240,4		
education	no	83,5	1,1	1,5
healthcare	no	44,2	0,6	0,9
Special acts	no	49,5	0,9	1,2
Total		**411,4**	**5,0**	**6,8**
included in the review*		**234,2**	**2,4**	**3,3**

** - estimate*

Source: MF SR, RIS, ÚHP

The review will include assessment of total public wage bill based on available international comparison. Subsequently a detailed analysis of personal expenses concerning above mentioned groups of general government employees will be performed. The review will focus on assessment of number of employees, level and structure of wages, employee productivity (taking in account methodological limitations), for all concerned public bodies. Homogenous groups of employees will be defined, so that various comparisons will be possible. Wage level of particular group of employees will be compared with private sector, with other public bodies, as well as among employees internally. Detailed analyses of several selected institutions will also include key processes mapping.

Responsibilities and deadlines

The interim and final reports will be carried out by MF SR. All concerned institutions agree to cooperate in providing complete and detailed data and information for preparation of analyses of the above mentioned issues. The interim report will be prepared by the end of October 2018 and the final report will be prepared and published by the end of March 2019.

Annex 6 - Required tables

Table 0i - Basic assumptions

	2016	2017	2018
Short-term interest rate (annual average)	-0.3	-0.3	-0.2
Long-term interest rate (annual average)	0.5	1.1	1.3
Exchange rate USD/EUR (average	1.1	1.1	1.2
World GDP growth	-0.4	0.9	0.6
Nominal effective exchange rate (change in %)	n/a	n/a	n/a
EU GDP growth	1.7	2.1	2.0
GDP growth of relevant foreign markets	2.0	2.9	2.3
World imports growth in constant prices excl. EU	n/a	n/a	n/a
Oil price (Brent, USD/barrel)	40.7	46.1	43.2

Source: MF SR

Table 0ii - Key assumptions

	2016	2017	2018
1. External environment			
Oil price (€)	48.3	40.1	46.0
2. Fiscal policy			
Net lending/net borrowing of the general government	-2.2	-1.6	-0.8
Gross debt of the general government	51.9	51.1	49.9
3. Monetary policy, financial sector			
Interest rates:			
Euribor 3M (average)	0.0	-0.3	-0.3
Deposits	0.6	0.4	0.4
Yield from 10-year Slovak government bonds (average)	0.8	0.5	0.7
Balance of deposits (growth)	7.2	7.2	6.0
4. Demographic trends			
Economic-active population (growth)	-0.8	-0.7	-0.7
Total dependency ratio	43.8	45.0	46.3

Source: MF SR

Table 1.a – Macroeconomic overview

	ESA code	2016 Actual	2016 growth rate	2017 growth rate	2018 growth rate
1. Real GDP	B1*g	78.9	3.3	3.3	4.2
thereof 1.1 estimated impact of aggregate budgetary measures on economic growth		-	-	-	0.6
2. Potential GDP		79.1	2.8	2.8	3.5
contributions:					
- labour		-	0.3	0.3	0.2
- capital		-	0.7	0.5	0.7
- total productivity of factors		-	1.8	2.0	2.6
3. Nominal GDP	B1*g	81.0	2.9	4.5	5.8

Components of real GDP					
3. Final consumption of households and NISD	P.3	40.9	2.9	3.3	2.9
4. Final general government consumption	P.3	14.7	1.6	0.4	1.3
5. Gross fixed capital generation	P.51g	16.3	-9.3	3.0	4.2
6. Change in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53		1.3	1.7	1.6
7. Exports of products and services	P.6	78.3	4.8	5.0	7.8
8. Imports of products and services	P.7	72.5	2.9	4.8	6.8
Contributions to real growth of GDP					
9. Total local demand		-	-0.4	2.4	2.6
10. Change in inventories and net acquisition of valuables	P.52 + P.53	-	1.2	0.5	0.0
11. External balance of products and services	B.11	-	2.0	0.6	1.6

Source: MF SR

Table 1.b – Price development

	ESA code	2016 Actual	2016 growth rate	2017 growth rate	2018 growth rate
1. GDP deflator		1.0	-0.4	1.1	1.6
2. Private consumption deflator		1.1	-0.3	1.4	1.7
3. HICP		99.5	-0.5	1.3	1.7
4. Public consumption deflator		1.1	1.3	3.0	2.4
5. Investment deflator		1.0	-0.6	1.3	2.0
6. Export price deflator (goods and services)		1.0	-1.4	2.3	1.2
7. Import price deflator (goods and services)		1.0	-1.1	2.7	1.3

Source: MF SR

Table 1.c – Labour market indicators

	ESA code	2016 Actual	2016 growth rate	2017 growth rate	2018 growth rate
1. Employment, persons (thousands) [1]		2,321	2.4	2.0	1.4
2. Hours worked (mil.) [2]		4,039	1.6	1.0	0.9
3. Unemployment rate (%) [3]			9.7	8.2	7.3
4. Labour productivity, per person (EUR) [4]		33.974	0.9	1.3	2.7
5. Labour productivity, per hour (EUR) [5]		20	1.7	2.3	3.2
6. Compensation for employees (EUR mil.)	D.1	31,627	4.6	6.2	5.9
7. Compensation per employee (EUR)		15,824	1.8	3.9	4.5

[1] Occupied population, domestic concept national accounts definition

Source: MF SR

[2] National accounts definition

[3] Harmonised definition, Eurostat; levels

[4] Real GDP per person employed

[5] Real GDP per hour worked

Table 1.d - Sectoral balances (ESA 2010, % GDP)

	ESA code	2016	2017	2018
1. Net lending to/net borrowing from rest of the world	B.9	1.3	0.3	1.1
thereof:				
- Goods and services		3.3	3.2	4.2

- Primary income and transfers		-4.0	-4.1	-4.3
- Capital account		2.0	1.2	1.2
2. Net lending to/net borrowing from other sectors	B.9	4.0	2.3	2.4
3. Net lending/net borrowing of the general government	B.9	-2.7	-2.0	-1.3
4. Statistical discrepancy		0.0	0.0	0.0

Source: MF SR

Table 2.a: Development of the general government budget (% GDP)

Net lending /borrowing (EDP B.9) general government subsectors	ESA code	2017 % GDP	2018 % GDP
1. General government	S.13	-1.6	-0.8
2. Central government	S.1311	-2.1	-1.3
3. Regional state government	S.1312	n/a	n/a
4. Local state government	S.1313	0.3	0.3
5. Social security funds	S.1314	0.1	0.2
6. Interest cost	D.41	1.3	1.3
7. General government primary balance (1+6)		-0.3	0.4
8. One-off and temporary effects		0.0	0.0
9. Real GDP growth (%)		3.3	4.2
10. Potential GDP growth (%)		2.8	3.5
contributions:		2.8	3.5
- labour		0.3	0.2
- capital		0.5	0.7
- total productivity of factors		2.0	2.6
11. Output gap (% of potential GDP)		0.2	0.8
12. Cyclical component (% of potential GDP)		0.1	0.3
13. Cyclically-adjusted balance (1-12) (% of potential GDP)		-1.7	-1.1
14. Cyclically-adjusted primary balance (13+6) (% of potential GDP)		-0.4	0.1
15. Structural (13-8) (% of potential GDP)		-1.7	-1.1

Source: MF SR

[1] Adjusted for swap-related net flows so that TR-TE=EDP B.9.
[2] The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9).
[3] A plus sign means deficit-reducing one-off measures of the general government.
[4] Including those collected by the EU

Table 2.b: Development of the general government debt (% GDP)

	ESA code	2017	2018
1. Gross debt[1]		51.1	49.9
2. Change in gross debt		-0.8	-1.2
Contributions to change in gross debt			
3. Primary balance		0.3	-0.4
4. Interest cost	D.41	1.3	1.3
5. Stock-flow adjustment		-0.2	0.8
Differences between cash and accruals		0.2	0.5
- Net accumulation of financial assets		-0.3	0.4
thereof: privatisation proceeds		0.0	0.0
- Valuation effects and other		-0.1	-0.1
p.m. Implicit interest rate		2.6	2.6

Other relevant factors		
6. Liquid financial assets	4.4	4.5
7. Net financial debt (1-6)	46.7	45.5
8. Debt amortization (existing bonds) since the end of the previous year	7.9	5.0
9. Percentage of debt denominated in foreign currency	3.1	2.7
10. Average maturity*	8.3	9.4

Note: *maturity of the government debt at the end of the year *Source: MF SR*

Table 2.c: Contingent liabilities (% GDP)

	2015	2016	2017
Public guarantees	16.9	16.0	n/a
thereof: connected with EFSF and ESM	9.3	9.0	n/a

Source: MF SR

Table 3: General government expenditure and revenue projections according to the no-policy-change scenario (breakdown by components)

General government (S13)	ESA code	2017 ED % GDP	2018 NPC % GDP	2017 ED EUR mil.	2018 NPC EUR mil.
1. Total revenue	**TR**	**39.4**	**38.3**	**33,310**	**34,284**
thereof		-	-	-	-
1.1. Taxes on production and imports	D.2	11.0	10.8	9,265	9,706
1.2. Current taxes on income, wealth, etc.	D.5	7.1	7.2	6,048	6,403
1.3. Capital taxes	D.91	-	-	-	-
1.4. Social security contributions	D.61	14.8	14.6	12,502	13,037
1.5. Property income	D.4	0.7	0.6	560	561
1.6. Other[1]		5.8	5.1	4,934	4,576
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)		31.3	32.6	26,466	29,146
2. Total expenditures	**TE**	**41.0**	**38.3**	**34,686**	**34,235**
thereof		-	-	-	
2.1. Compensation for employees	D.1	9.0	8.9	7,598	7,929
2.2. Intermediate consumption	P.2	6.0	5.3	5,034	4,724
2.3. Total social transfers	D.62, D.632	18.8	18.1	15,911	16,227
thereof: unemployment benefits		0.2	0.2	173	154
2.4. Interest cost	D.41	1.3	1.3	1,110	1,136
2.5. Subsidies	D.3	0.4	0.4	340	401
2.6. Gross fixed capital generation	P.51	3.3	2.2	2,811	1,969
2.7. Capital transfers	D.9	0.3	0.2	278	142
2.8. Other[2]		1.9	1.9	1,604	1,708

Note: Data for 2016 express expected actual results. *Source: MF SR*
[1] P.11+P.12+P.131+D.39r+D.7r+D.9r (excl. D.91r)
[2] D.29p + D.4p (excl. D.41p) +D.5p +D.7p +P.52+P.53+NP+D.8.

Table 4.a: General government expenditure and revenue targets (breakdown by components)

General government (S13)	ESA code	2017 % GDP	2018 % GDP	2017 EUR mil.	2018 EUR mil.
1. Total revenues	**TR**	**39.4**	**38.5**	**33,310**	**34,432**
thereof		-	-	-	
1.1. Taxes on production and imports	D.2	11.0	11.0	9,265	9,831

1.2. Current taxes on income, wealth, etc.	D.5	7.1	7.1	6,048	6,392
1.3. Capital taxes	D.91	0.0	0.0	0	0
1.4. Social security contributions	D.61	14.8	14.6	12,502	13,108
1.5. Property income	D.4	0.7	0.6	560	561
1.6. Other [1]		5.8	5.1	4,934	4,540
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)		31.3	32.8	26,466	29,331
2. Total expenditures	**TE**	**41.0**	**39.3**	**34,686**	**35,175**
thereof		-	-	-	
2.1. Compensation for employees	D.1	9.0	9.1	7,598	8,105
2.2. Intermediate consumption	P.2	6.0	5.5	5,034	4,888
2.3. Total social transfers	D.62, D.632	18.8	18.3	15,911	16,403
thereof: unemployment benefits		0.2	0.2	173	163
2.4. Interest cost	D.41	1.3	1.3	1,110	1,136
2.5. Subsidies	D.3	0.4	0.4	340	394
2.6. Gross fixed capital generation	P.51	3.3	2.4	2,811	2,163
2.7. Capital transfers	D.9	0.3	0.3	278	229
2.8. Other [2]		1.9	2.1	1,604	1,857

[1] P.11+P.12+P.131+D.39r+D.7r+D.9r (excl. D.91r) *Source: MF SR*

[2] D.29p + D.4p (excl. D.41p) +D.5p +D.7p +P.52+P.53+NP+D.8.

Note: Data for 2016 express expected actual results.

Table 4.b: Amounts to be excluded from the expenditure benchmark

	2016	**2016**	**2017**	**2018**
	EUR mil.	% GDP	% GDP	% GDP
1. Expenditure on EU programmes fully matched by EU funds revenue	796	1.0	1.0	0.4
1.a. thereof investments fully matched by EU funds revenue	507	0.6	0.6	0.1
2. Cyclical unemployment benefit expenditure	2	0.0	0.0	0.0
3. Effect of discretionary revenue measures	-174	-0.2	0.2	0.0
4. Revenue increases mandated by law	0	0	0	0

Source: MF SR

Table 4.c.i): General government expenditure on education, healthcare and employment

	2017		**2018**	
	% GDP	% TGE	% GDP	% TGE
Education	4.1	10.0	3.9	10.0
Healthcare system	7.6	18.4	7.3	18.6
Employment	0.1	0.2	0.1	0.2

Note: TGGE - Total general government expenditures *Source: Eurostat*

Table 4.c.ii): General government expenditures according to the COFOG classification

Functions	**COFOG code**	**2017**		**2018**	
		% GDP	% TGE	% GDP	% TGE
1. General public services	1	5.4	13.2	5.1	13.0
2. Defence	2	1.1	2.7	1.1	2.9

3. Public order and safety	3	2.2	5.3	2.1	5.2
4. Economic area	4	4.4	10.7	3.6	9.1
5. Environmental protection	5	0.6	1.4	0.6	1.6
6. Housing and amenities	6	0.5	1.2	0.5	1.2
7. Healthcare system	7	7.6	18.4	7.3	18.6
8. Recreation, culture and religion	8	1.0	2.5	1.0	2.7
9. Education	9	4.1	10.0	3.9	10.0
10. Social security	10	14.2	34.5	14.0	35.6
Total expenditures	**TE**	**41.0**	**100.0**	**39.3**	**100.0**

Note: *TGGE – Total general government expenditure The methodology of recording expenditures based on functional classification can vary between individual countries As a result, different data can enter into the same category in different countries (e.g. taxed and non-taxed pensions). COFOG classification also doesn't take into account expenditure realized through the tax system (e.g. tax benefits).*

Source: MF SR

Table 5a: Measures included in the draft general government budget (ESA 2010, % GDP, compared to NPC)

Revenues	Subsector	ESA2010	2018	2019	2020
Total tax revenues	**S. 13**		**0.21**	**0.3**	**0.33**
Taxes on production	S. 13	D.2	0.14	0.12	0.11
Income taxes	S. 13	D.5	-0.01	-0.01	-0.02
Revenues from fees and charges	S. 13	D.61	0.08	0.08	0.08
Total non-tax revenues	S.13	P.11+P.12	0.12	0.04	-0.02
Grants and transfers	S.13		-0.16	-0.11	-0.06
Required revenue measures*	S.13			0.11	0.16
Total revenues			**0.17**	**0.23**	**0.26**
Expenditures					
Compensations - thereof:	**S.13**	**D.1**	**-0.2**	**-0.29**	**-0.21**
Adjustment of wages of teachers and GG employees			-0.24	-0.3	-0.38
Allowance for work during weekends and on public holiday			-0.01	-0.02	-0.02
Intermediate consumption - thereof:	**S.13**	**P.2**	**-0.18**	**0.08**	**-0.25**
Provisions for worsening tax and non-tax revenues			-0.16	0	0
Subsidies	**S.13**	**D.3p**	**0.01**	**0.01**	**0.01**
Social transfers - thereof	**S.13**	**D.62p**	**-0.23**	**-0.28**	**-0.3**
Minimum pension adjustments and other effects of the amendment act 461/2003	S.1311		-0.1	-0.12	-0.15
Adjustment of pensions granted before 2004	S.1311		-0.06	-0.05	-0.04
Increased care allowance	S.1311		-0.02	-0.06	-0.06
Higher payments of the state for social services	S.1311		-0.05	-0.05	-0.04
Natural social transfers	**S.13**	**D.632**	**0.03**	**-0.01**	**-0.01**
Amendment act to Act 363/2011 on the Reimbursement of Drugs (innovative drugs)	**S.1314**		0.03	-0.01	-0.02
Other current transfers, thereof	**S.13**		**-0.14**	**-0.1**	**-0.13**
Provision for the 13th and 14th salary and the exemption of income from agreements of pensioners			-0.06	-0.05	-0.05
Capital expenditures, thereof	**S.13**		**-0.34**	**-0.04**	**-0.05**
National Football Stadium	S.1311	P.51g	-0.07	-0.01	0
Higher expenditures on defence modernisation	S.1311	P.51g	-0.1	-0.1	-0.4
Transport modernisation	S.1311	P.51g	-0.1	0	0

SNG reconstruction	S.1311	P.51g	-0.03	0	0
Provision for significant investments	S.1311	P.51g/D.9p	-0.18	-0.05	-0.04
Required expenditure measures*	S.13		-	0.11	0.11
Total expenditures			**-1.05**	**-0.51**	**-0.82**

Note: (+) increase in revenues and decrease in expenditures

**not included in the GGB 2018 – 2020*

Source: MF SR

Table 6.a: NRP response to specific recommendations for Slovakia

CSR	Measure	Objectives
1	**Pursue its fiscal policy in line with the requirements of the preventive arm of the Stability and Growth Pact, which translates into a substantial fiscal effort for 2018. When taking policy action, consideration should be given to achieving a fiscal stance that contributes to both strengthening the ongoing recovery and ensuring the sustainability of Slovakia's public finances. Improve the cost effectiveness of the healthcare system, including by implementing the value for money project.**	
1	DRG - complete convergence of basic rates	A diagnostic-related group-linked payment mechanism was launched early in 2017. In the first year, individual hospitals have individual rates in order to avoid significant financial fluctuations and destabilization of the system. The five-year taking convergence process of individual rates to a single nation-wide basic rate will be initiated in 2018.
1	*eHealth* implementation	Gradual connection of all doctors to the *eHealth* environment is taking place throughout 2017. The selected parts of *eHealth - National health portal, ePrescription and eMedication, Electronic health documentation* and *eAllocations*, should be fully functional in 2018.
1	Implementation of the health spending review outcomes	The measures listed in the Healthcare spending review under Annex 7 of the general government budget for 2017-2019 (Resolution No. 461/2016 of the Slovak Government, task C4) are being implemented.
2	**Improve activation measures for disadvantaged groups, including by implementing the action plan for the long-term unemployed and by providing individualised services and targeted training. Enhance employment opportunities for women, especially by extending affordable, quality childcare. Improve the quality of education and increase the participation of Roma in inclusive mainstream education.**	
2	Reform of employment services and active labour market policies (ALMP).	Internal evaluations of labour office efficiency led to the continued employee relocations to more frequent and demanding activities. The MoLSAF SR adopted an action plan in 2016 to implement several forms of support for the integration of long-term unemployed in the labour market, particularly the individualised counselling including jobseeker profiling, or education and re-qualification programmes. Projects within the active labour market policies have been launched in the course of the year in order to support the employment of jobseekers by private and public employers, self-employed and to support commuting in the lagging regions.
2	Expansion of kindergarten capacities and development of childcare for children up to three years of age	The capacities of kindergartens continue to be expanded through the construction of new kindergartens and the expansion of the existing capacities in 2017 using the structural funds. In order to implement provision of childcare facilities for children under three years of age, construction of 90 childcare facilities with a capacity of 1,800 children with a financial allocation of EUR 40.2 million is expected within the IROP and the OP Human Resources in 2017-2020. In January 2017, the Parliament adopted legislatiolegislation, effective as of March 2017, in January 2017 (the so-called nursery law) implementing effective as of March 2017 the legislative framework for childcare facilities for children up to three years of ageeffective as of March 2017.

2	Integration of marginalized Roma communities (education, labour market, and social inclusion)	Projects in the area of inclusion of individuals from MRC focus within the new programming period 2014 – 2020 on funding the construction and reconstruction of kindergartens and community centres, waste management, better access to drinking water, and establishment of local neighbourhood watch schemes. National projects will be implemented to support community centres, field social work, land settlement, better access to health care, and to preschool education. The national projects in the new programming period also continue in the functional full-day education system, development of inclusive education of children from MRC, work of teacher assistants, and the educational activities in Roma communities. The spending review of Groups at Risk of Poverty and Social Exclusion including MRC was initiated in 2017.
3	**Improve competition and transparency in public procurement operations and step up the fight against corruption by stronger enforcement of existing legislation. Adopt and implement a comprehensive plan to lower administrative and regulatory barriers for businesses. Improve the effectiveness of the justice system, including a reduction in the length of civil and commercial cases.**	
3	Anti-offshore law	Effective as of January 2017, the anti-offshore law lays down an obligation for the corporations to register in the registry of public sector partners and disclose the ownership structure down to the ultimate beneficiary.
3	Reducing the duration of the debt collection processes	Effective as of March 2017, the amendment to the bankruptcy and restructuring law (the so-called Bankruptcy Law) decreased costs connected with initiation of the personal bankruptcy proceeding for individuals in debt trap. The amendment act also revoked the option of forgiving more than a half of debts and changes the maturity of the remaining debts to five years in the company restructuring process, unless the creditors give a voluntary consent. Effective as of August 2017, the Government passed changes of the Commercial Code improving protection of creditors.
3	Measures to improve the business environment	Reduction of the regulatory burden and improvement of the business environment should also be supported by a package containing the proposal of 35 specific measures in various areas across multiple Ministries which was approved by the Government in June 2017. One of the first measures out of this package which has already been approved by the Government includes the optimisation of the occupational health service which presupposes reduction of administrative costs for entrepreneurs.
3	Two-way electronic communication between the Financial Administration and businesses	The Financial Administration will continue to reduce the administrative burden for businesses by expanding the opportunities of two-way electronic communication with businesses with regard to tax paperwork, and particularly the VAT, and by providing pre-filled forms of certain types of tax returns.
3	Amendment act on e-Government	In September 2017, the Parliament passed the e-Government amendment act which should simplify the use of electronic services and introduce mechanism for monitoring compliance with obligations for involved actors.

Table 6.b: EU growth and employment objectives

Key EU2020 indicator	Measure	Objective
Employment	Continuation of employment services reform	Internal evaluations of labour office efficiency led to the continued employee relocations to more frequent and demanding activities. The Ministry of Labour, Social Affairs and Family of the SRMoLSAF SR adopted an action plan in 2016 to implement multiple several forms of support for the integration of long-term unemployed in the labour market, particularly the individualised consultancy counselling including jobseeker profiling, or education and re-qualification programmes. Projects within the active labour market policies have been launched in the course of the year in order to support the employment of jobseekers by private and public employers, self-employed freelancers, and to support commuting in the lagging regions.
	Measures to increase labour force mobility and the income of workers.	Throughout 2018, the extra pay for work on weekend and public holiday and the extra pay for the night work should rise. The labour force mobility would improve as a result of the reinforcementof the commuting allowance and the relocation

		allowance. The payment of the 13th and the 14th salary will be supported by the tax and contribution relieves.
Research and development	Research and innovation support	Support will go to investments in research and development (R&D) through significant increase in the tax relief for expenditure on research and development in businesses. In addition to the tax-deductible expenses, taxpayer will be allowed to claim additional 100% deduction of the R&D expenses and 100% deduction of the average increase in the expenses on R&D for 2 year.
Climate changes and energy	Decision-making about greenhouse gas emission reduction	The Environmental policy Strategy until 2030 which will set forth framework measures for environmental protection direction will be presented in 2018. The Low-Carbon Strategy until 2050 identifies the reduction potential and the cost-efficient forms of decreasing emissions. The Air Quality Improvement Strategy will present the measures to help reduce air pollution.
	Amendment act on air pollution	The amendment act on air pollution passed by the Government in August 2017 will allow the towns and villages to create low-emission zones which may only be entered by low-emission vehicles. It will also set more strict emission limits and monitoring for medium combustion plants.
Education	Expansion of the pre-school facility capacities	In order to develop childcare facilities for children under three years of age, construction of 90 childcare facilities with a capacity of 1,800 children with a financial allocation of EUR 40.2 million is expected within the IROP and the OP Human Resources in 2017-2020. In January 2017, the Parliament adopted legislatiolegislation, effective as of March 2017, in January 2017 (the so-called nursery law) implementing effective as of March 2017 the legislative framework for childcare facilities for children up to three years of ageeffective as of March 2017. The expansion of kindergarten capacities continues in 2017 using the structural funds.
	Teacher pay	The attractiveness of teaching profession is being increased. The Government committed to increase the salaries of teaching and professional staff by 6% a year on average based on the assumption of implementation of crucial internal changes in the education system. The salaries of teaching and professional staff in regional and tertiary schools grew by 6% in September 2017.
	Reform of accreditation commission and accreditation process	The reforms within the tertiary education include the reform of accreditation commission and the accreditation process, a new assessment system and institutional funding of research and development at universities will be developed, and the instruments to increase accessibility of tertiary education will be made more targeted.
Poverty and social inclusion	Inclusive education at elementary schools	The national projects in the new programming period also continue in the functional full-day education system, development of inclusive education of children from MRC, work of teacher assistants, and the educational activities in Roma communities.
	Inclusion of marginalized Roma communities	Projects in the area of inclusion of individuals from marginalized Roma communities (MRC) focus within the new programming period 2014 – 2020 on funding the construction and reconstruction of kindergartens and community centres, waste management, better access to drinking water, and establishment of local neighbourhood watch schemes. National projects will be implemented to support community centres, field social work, land settlement, better access to health care, and to preschool education. education. The spending revision in the area of MRC social inclusion and integration has been initiated in 2017.