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COMMISSION OPINION

of 20.11.2019

on the Draft Budgetary Plan of Estonia

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GENERAL CONSIDERATIONS

1. Regulation (EU) No 473/2013 sets out provisions for enhanced monitoring of budgetary policies in the euro area for ensuring that national budgets are consistent with the economic policy guidance issued in the context of the Stability and Growth Pact and the European Semester for economic policy coordination.

2. Article 6 of Regulation (EU) No 473/2013 requires Member States to submit annually to the Commission and to the Eurogroup a Draft Budgetary Plan presenting by 15 October the main aspects of the budgetary situation of the general government and its subsectors for the forthcoming year.

CONSIDERATIONS CONCERNING ESTONIA

3. On 15 October 2019, Estonia submitted the Draft Budgetary Plan for 2020. On that basis, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

4. Estonia is subject to the preventive arm of the SGP. On 9 July 2019, the Council recommended Estonia to ensure that the nominal growth rate of net primary government expenditure does not exceed 4.1% in 2020, corresponding to an annual structural adjustment of 0.6% of GDP towards the medium-term budgetary objective of -0.5% of GDP. [1]

5. According to the Commission 2019 autumn forecast, real GDP is expected to grow by 3.2% in 2019 and 2.1% in 2020. The macroeconomic scenario underlying the Draft Budgetary Plan is plausible, forecasting 0.1 percentage point higher GDP growth rates for 2019 and 2020. Estonia complies with the requirement of Regulation (EU) No 473/2013, since the draft budget is based on independently endorsed macroeconomic forecasts.

6. The Draft Budgetary Plan expects a headline budget deficit of 0.1% of GDP in 2019 and a balanced position in 2020. The structural balance[2] of the Draft Budgetary Plan is estimated to improve from a deficit of 1.3% of GDP in 2019 to a deficit of 0.6% of GDP in 2020. The Commission 2019 autumn forecast foresees a slightly larger headline deficit of 0.2% of GDP in 2019 and in 2020, reflecting the differences in the macro economic scenario. The structural deficit in the Commission forecast is larger, forecast at 1.6% of GDP in 2019 and 0.9% of GDP in 2020. The larger structural deficit is explained by the difference in headline surpluses, in combination with a somewhat different assessment of one-off measures.

7. According to both the Draft Budgetary Plan and the Commission 2019 autumn forecast, the fiscal stance in 2020 is projected to be contractionary based on the

[1] Council Recommendation of 9 July 2019 on the 2019 National Reform Programme of Estonia and delivering a Council opinion on the 2019 Stability Programme of Estonia OJ C 301, 5.9.2019 p. 30

[2] Cyclically-adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology.

change in the (recalculated) structural balance. Over recent years, Estonia has shifted the tax burden from labour to consumption taxes. The most recent and notable measure is the income tax reform for low- to medium-income earners, which took effect in 2018. Its costs were offset by increases in other taxes and excise duties. That measure has reduced the tax wedge on low- to medium-income earners. The Draft Budgetary Plan presents a number of relatively minor fiscal measures, which on the aggregate have a net deficit-decreasing effect of 0.2% of GDP in 2019, and a deficit-increasing effect of 0.2% of GDP in 2020. They were taken specifically in the context of the 2020 budget negotiations. The largest revenue increase comes from higher dividends from State-owned companies. Several expenditure items were allocated more funding, linked to wage increases by 2.5% in some public sector priority areas, higher operating expenses, some specific investments and a small extraordinary rise of pensions.

8. In 2019, for Estonia to comply with the requirements of the preventive arm, the nominal growth rate of government expenditure, net of discretionary revenue measures and one-offs, should not exceed 4.9%, corresponding to a structural balance improvement by 0.3% of GDP. According to the Draft Budgetary Plan, the expenditure benchmark points to a risk of some deviation from the requirement in 2019, while the recalculated structural deficit complies with the structural adjustment requirement for 2019. An overall assessment based on the government plans points to a risk of some deviation from the adjustment path towards the medium-term budgetary objective in 2019. Based on the Commission 2019 autumn forecast, the expenditure benchmark points to a risk of some deviation in 2019 (gap of 0.4% of GDP) and a risk of significant deviation over 2018 and 2019 taken together (gap of 0.5% of GDP), while the structural deficit complies with the structural adjustment requirement for 2019. An overall assessment gives priority to the expenditure benchmark, which indicates a risk of some deviation in 2019 and in 2018-2019 taken together once adjusted for the impact of the use of a lower GDP deflator underlying that indicator for 2018 and 2019 compared to latest estimates. Thus, the current assessment indicates a risk of some deviation in 2019.

In 2020, for Estonia to comply with the requirements of the preventive arm, the nominal growth rate of government expenditure, net of discretionary revenue measures and one-offs, should not exceed 4.1%, corresponding to a structural balance improvement by 0.6% of GDP. According to the Draft Budgetary Plan, the expenditure benchmark points to a risk of some deviation from the requirement in 2020, while the recalculated structural deficit complies with the structural adjustment requirement for 2020. An overall assessment based on the government plans points to a risk of some deviation from the adjustment path towards the medium-term budgetary objective in 2020. Based on the Commission 2019 autumn forecast, the expenditure benchmark points to a risk of some deviation in 2020 (gap of 0.4% of GDP) and a risk of significant deviation over 2019 and 2020 taken together (gap of 0.4% of GDP), while structural deficit complies with the structural adjustment requirement for 2020. An overall assessment gives priority to the expenditure benchmark, which indicates a risk of some deviation in 2020 and in 2019-2020 taken together, once adjusted for the impact of a lower GDP deflator underlying that indicator for 2019 and the smoothing of investment expenditure for 2020, as public investment is planned to be reduced from the elevated levels in the preceding years. Thus, the current assessment indicates a risk of some deviation in 2020.

9. Overall, the Commission is of the opinion that the Draft Budgetary Plan of Estonia is broadly compliant with the provisions of the Stability and Growth Pact. The Commission therefore invites the authorities to stand ready to take the necessary measures within the national budgetary process to ensure that the 2020 budget will be compliant with the Stability and Growth Pact rules.

   A comprehensive description of progress made with the implementation of the country-specific recommendations will be made in the 2020 Country Reports and assessed in the context of the country-specific recommendations to be proposed by the Commission in spring 2020.

Done at Brussels, 20.11.2019

For the Commission
Pierre MOSCOVICI
Member of the Commission