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COMMISSION OPINION

of 18.11.2020

on the Draft Budgetary Plan of Slovakia

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(Only the Slovak text is authentic)

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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, to ensure 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 by 15 October, presenting the main aspects of the budgetary situation of the general government and its subsectors for the forthcoming year.

3. On 20 March 2020, the Commission adopted a Communication[1] on the activation of the general escape clause[2] of the Stability and Growth Pact. In its Communication, the Commission set out its view that, given the expected severe economic downturn resulting from the COVID-19 outbreak, the conditions to activate the general escape clause were met. On 23 march 2020, the Ministers of Finance of the Member States agreed with the assessment of the Commission.[3] As indicated in the Annual Sustainable Growth Strategy 2021[4] and as communicated in the letter of 19 September 2020 from the Commission to the EU ministers of Finance[5], Member States should continue to provide targeted and temporary fiscal support in 2021 in a context where the general escape clause is activated, while safeguarding fiscal sustainability in the medium term.

4. On 27 May 2020, the Commission put forward its proposal for the creation of a new recovery instrument Next Generation EU[6], alongside the proposal for the reinforced long-term budget of the EU for 2021-2027.[7] This proposal includes the establishment

[1] Communication from the Commission to the Council on the activation of the general escape clause of the Stability and Growth Pact, Brussels, 20.3.2020, COM(2020) 123 final.

[2] The clause, as set out in Articles 5(1), 6(3), 9(1) and 10(3) of Regulation (EC) 1466/97 and Articles 3(5) and 5(2) of Regulation (EC) 1467/97, facilitates the coordination of budgetary policies in times of severe economic downturn.

[3] https://www.consilium.europa.eu/en/press/press-releases/2020/03/23/statement-of-eu-ministers-of-finance-on-the-stability-and-growth-pact-in-light-of-the-covid-19-crisis/

[4] Communication from the Commission on Annual Sustainable Growth Strategy 2021, Brussels, 17.9.2020, COM(2020) 575 final.

[5] https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/stability-and-growth-pact/annual-draft-budgetary-plans-dbps-euro-area-countries/draft-budgetary-plans-2021_en

[6] Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions - Europe's moment: Repair and Prepare for the Next Generation, Brussels, 27.5.2020, COM(2020) 456 final.

[7] Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions - The EU budget powering the recovery plan for Europe, Brussels, 27.5.2020, COM(2020) 442 final.

of a Recovery and Resilience Facility offering large-scale financial support both public investments and reforms. By contributing to the economic recovery and by providing financial support to strengthen the economy´s long-term growth, the Recovery and Resilience Facility will help public finances to return to more favourable positions in the near term and will contribute to strengthening their sustainability in the medium and long term.

CONSIDERATIONS CONCERNING SLOVAKIA

5. On 14 October 2020, Slovakia submitted the Draft Budgetary Plan for 2021. On that basis, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

6. On 20 July, the Council recommended Slovakia[8] to take all necessary measures, in line with the general escape clause, to effectively address the pandemic, sustain the economy and support the ensuing recovery. It also recommended Slovakia to pursue, when economic conditions allow, fiscal policies aimed at achieving prudent medium-term fiscal positions and ensuring debt sustainability, while enhancing investment.

   On 20 May 2020, the Commission issued a report under Article 126(3) TFEU, as Slovakia´s general government deficit in 2020 was planned to exceed the 3% of GDP Treaty reference value. The report concluded that, after the assessment of all relevant factors, the deficit criterion was not fulfilled. In light of the exceptional uncertainty created by the outbreak of COVID-19 and its extraordinary macroeconomic and fiscal impact, including for designing a credible path for fiscal policy, which will have to remain supportive in 2021, the Commission considered that a decision on whether to place Member States under the Excessive Deficit Procedure should not be taken.

7. According to the Commission 2020 autumn forecast, the Slovak economy is expected to contract by 7.5% in 2020 and grow by 4.7% in 2021. According to the Draft Budgetary Plan, the Slovak economy is expected to contract by 6.7% in 2020 before rebounding by 5.5% in 2021, driven by the fall and subsequent recovery of both domestic and foreign demand, in particular private consumption, investment and net exports. While uncertainty, liquidity constraints and restrictions to business activity are projected to weigh heavily on investment in 2020, private investment is expected to grow strongly in 2021 according to the Draft Budgetary Plan. The recovery is expected to be uneven across sectors, with the manufacturing sector resuming activity more quickly than the service sector, where restrictions are expected to remain in place for longer. Trade activity is projected to decrease sharply in 2020 but to recover quickly in 2021. The main differences compared to the Commission 2020 autumn forecast stem from the larger contraction in private consumption, investment and external trade, contributing to a slower recovery.

   Slovakia complies with the requirement of Regulation EU No 473/2013 since the draft budget is based on independently-endorsed macroeconomic forecasts produced by the Institute for Financial Policy and endorsed by the Macroeconomic Forecasting Committee.

8. For 2020, the Draft Budgetary Plan foresees the general government deficit to rise to 9.7% of GDP. This increase in the government deficit by more than 9 percentage

[8] Council Recommendation of 20 July 2020 on the national Reform Programme of Slovakia and delivering a Council opinion on the 2020 Stability Programme of Slovakia and delivering a Council opinion on the 2020 Stability Programme of Slovakia, OJ C 282, 26.8.2020, p 164.

points compared to the preceding year results from both the operation of the automatic stabilisers, which led to a contraction in revenue and an increase in cyclical expenditure, and from discretionary COVID-19-related measures. On the expenditure side, there is also a sharp increase due to higher expenditure that is not classified by the Draft Budgetary Plan as discretionary measures, but which is largely of a permanent character. When comparing with previous years there appears to be a continuation of strong upward expenditure trends, in particular with regard to wages and social benefits. According to the 2021 Draft Budgetary Plan, the deficit ratio is expected to narrow to 7.4% of GDP in 2021, helped by the rebound in activity and a phasing out of temporary measures implemented to contain the economic effects of the pandemic. The Draft Budgetary Plan does not include any grants and expenditure under the Recovery and Resilience Facility. For the time being, since the submission of the Recovery and Resilience Plans and their subsequent approval are expected to take place in 2021, the Commission forecast assumes in the budgetary projections for 2021 the 10% pre-financing of Recovery and Resilience Facility grants and treats it as a financial transaction with no impact on the budget balance, but with a public debt-reducing impact. In the case of Slovakia, the 10% pre-financing of Recovery and Resilience Facility grants is equivalent to EUR 630 million in 2021. [9] On the expenditure side, in line with its no-policy change assumption, the Commission forecast includes no expenditure related to the Recovery and Resilience Facility, as the corresponding measures were not sufficiently specified at the cut-off date of the forecast.[10] The Commission forecast projects a higher government headline deficit in 2021, at 7.9% of GDP. The main differences between the Commission 2020 autumn forecast and the Draft Budgetary Plan stem from slightly different assumptions on the EU funds draw-down profile and differences in the macroeconomic scenarios. The Draft Budgetary Plan indicates that the government debt-to-GDP ratio will increase from 62.2% of GDP at the end of 2020 to 65% in 2021, compared to the Commission´s projection of 63.4% and 65.7% respectively.

9. According to the Draft Budgetary Plan, total discretionary measures in 2020 amount to 4.9% of GDP. They are reported both on the expenditure (4.5% of GDP) and the revenue (0.5% of GDP) side of the general government budget.. The Draft Budgetary Plan reports discretionary fiscal measures with a direct budgetary impact in 2020 in response to the COVID-19 outbreak and its related economic effects of around EUR 2.8 billion (3.1% of GDP). Those consist of expenditure measures totalling EUR 2.2 billion (2.5% of GDP) and revenue measures costing EUR 0.5 billion (0.6% of GDP). Expenditure measures for 2020 include supporting workers and firms to safeguard employment, nursing and sickness benefits for employees, as well as support to self-employed and small and medium enterprises, subsidised rents in retail

[9] Indicative number based on the Council Presidency compromise proposal for the RRF regulation (11538/20) of 7 October 2020, on which the Council Presidency obtained a mandate for conducting the negotiations with the European Parliament.

[10] The treatment of the Recovery and Resilience Facility (RRF) in the Commission's 2020 autumn forecast is explained in detail in Box I.4.3 of the European Commission's Economic Forecast Autumn 2020 (https://ec.europa.eu/info/sites/info/files/economy-finance/ip136_en.pdf). In line with the costumary no policy-change assumption, the forecast only incorporates those measures that are credibly announced and sufficiently detailed in the Draft Budgetary Plans, irrespective of whether they are planned to be part of Recovery and Resilience Plans. No financing from the RRF has been included on the revenue side of the budgetary projections. Only the pre-financing of RRF grants is included in the forecast for 2021. The assumptions on expenditure measures linked to the RRF in the Commission forecast are without prejudice to the assessment of the Recovery and Resilience Plans.

businesses and additional spending on health care to cope with the medical emergency. On the revenue side, the biggest measure is an increase in tax allowances. Approximately 1.9% of GDP of the total discretionary measures in 2020 are of a permanent nature. These include mainly higher public sector wages, pension increases and the above-mentioned increase in tax allowances.

The Commission forecast includes a large share of measures reported in the Draft Budgetary Plan, with the exception of some lower tax revenue resulting from the operation of the automatic stabilisers. Moreover, the Commission forecast includes as discretionary measures a part of the increase in expenditure that the the Draft Budgetary Plan does not list as measures. They include, for example, subsidies to green energy producers, and additional expenditure of municipalities and state enterprises managed by the Ministry of Transport. The total impact of discretionary measures amounts to 5.8% of GDP (0.3% of GDP in revenues and 5.4% of GDP in expenditure) in the 2020 Commission autumn forecast in 2020, with a large part being considerd of a permanent nature (3.3% of GDP).

Beyond the expenditure and revenue measures that have a direct impact on the deficit, the Draft Budgetary Plan also includes liquidity support measures in 2020 amounting to EUR 0.5 billion (0.5% of GDP), in the form of tax deferrals. Furthermore, Slovakia has extended public guarantees, which the 2021 Draft Budgetary Plan estimates at 1.9% of GDP. There is no publicly available information on the take-up of guarantees. Overall, while many of the measures taken by Slovakia in 2020 were in line with the guidelines of the Commission Communication of 13 March 2020 on a coordinated economic response to the COVID-19 outbreak, there are also substantial permanent measures adopted in 2020.

10. For 2021, the Draft Budgetary Plan presents a set of measures aimed at supporting the economic recovery, amounting to 4.1% of GDP. Revenue measures are estimated to have a budgetary impact of 0.4% of GDP and include those focused on ensuring sufficient liquidity in the banking sector (abrogation of the bank levy). Expenditure measures carry a budgetary impact of 3.7% of GDP in 2021, including provisions for the negative effects of the pandemic COVID-19 and support of regional education and research. On the expenditure side, the Plan also encompasses measures contributing to the long-term sustainability of public finances, such as a 10% reduction in wages of some central government employees and expenses for the purchase of goods and services. Liquidity measures, namely in the form of guarantees on loans are also expected to continue to play a role as support to businesses. At the same time, some measures set out in the Draft Budgetary Plan, while supporting economic activity against the background of considerable uncertainty, appear not to be temporary or matched by offsetting measures. According to the Comission forecast, these measures are estimated at 0.6% of GDP. These include a lower retirement age for certain parents, higher minimum pensions and support of regional education and research.

11. The Commission is of the opinion that the Draft Budgetary Plan of Slovakia is overall in line with the recommendation adopted by the Council on 20 July 2020. Most of the measures set out in the Draft Budgetary Plan of Slovakia are supporting economic activity against the background of considerable uncertainty. However, some measures do not appear to be temporary or matched by offsetting measures. Slovakia is invited to regularly review the use, effectiveness and adequacy of the support measures and stand ready to adapt them as necessary to changing circumstances.

It is anticipated that Slovakia will submit its Recovery and Resilience Plan in 2021. The Regulation establishing a Recovery and Resilience Facility will set out how the Commission is to assess that the reforms and investments included in the Recovery and Resilience Plan are coherent with the policy priorities of the Union and the challenges identified in the context of the European Semester. This assessment by the Commission will inform the approval of the Plan by the Council and the information to the European Parliament.

Done at Brussels, 18.11.2020

For the Commission
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Member of the Commission