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**COMMISSION STAFF WORKING DOCUMENT**

**Analysis of the Draft Budgetary Plan of Estonia**

***Accompanying the document***

**COMMISSION OPINION**

**on the Draft Budgetary Plan of Estonia**

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## EXECUTIVE SUMMARY

- According to the Draft Budgetary Plan, real GDP is projected to fall in 2020 by 5.5% and to rebound in 2021 by 4.5%. This scenario is broadly in line with the Commission 2020 autumn forecast, although the Commission expects a smaller GDP decline in 2020 by 4.6% (reflecting more favourable short-term economic developments), but also a smaller rebound in 2021 by 3.3%.
- The Draft Budgetary Plan projects the general government deficit to decline from a surplus of 0.1% of GDP in 2019 to a deficit of 6.6% of GDP in 2020 and 6.7% in 2021. The Commission 2020 autumn forecast projects a smaller headline deficit of 5.9% of GDP in both 2020 and in 2021, reflecting the more favourable macroeconomic projection for 2020, which carries forward to 2021.
- On 20 May 2020, the Commission has prepared a report under Article 126(3) TFEU analysing whether Estonia was compliant with the deficit criterion of the Treaty. Overall, the analysis suggested that the deficit criterion as defined in the Treaty and in Regulation (EC) No 1467/1997 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.
- The Draft Budgetary Plan indicates that the debt-to-GDP ratio will increase from 18.2% at the end of 2020 to 23.6% in 2021, similar to the Commission's projection of 22.6%.
- In 2020, in addition to allowing automatic stabilisers to work, the government implemented expansionary fiscal measures of 3% of GDP. The bulk of these were additional expenditures on healthcare, wage subsidy, additional funding for local governments, investments, and sectoral support to shipping, education and culture. Guarantee and loan schemes were also provided, but the take-up of these schemes has been limited. The 2021 budget plan allocates additional resources in 2021 to a multitude of small-scale investment projects, pensions, R&D and defence (amounting to 1.8% of GDP).
- Overall, the measures in the Draft Budgetary Plan of Estonia are supporting economic activity against the background of considerable uncertainty. Most of the measures set out in the Draft Budgetary Plan are temporary. At the same time, it would be useful to regularly review the use, effectiveness and adequacy of the support measures and stand ready to adapt them as necessary to changing circumstances.

## 1. INTRODUCTION

This document assesses the economic and budgetary projections contained in the 2021 Draft Budgetary Plan of Estonia (hereafter called the Plan), which was submitted for 2021 on 15 October 2020 in compliance with Regulation (EU) No 473/2013. The Plan was prepared at the same time with the State Budget Strategy 2021–2024, which was approved on 29 September 2020 by the government.

On 20 March 2020, the Commission adopted a Communication on the activation of the general escape clause of the Stability and Growth Pact and on 23 March 2020 the Ministers of Finance of the EU Member States agreed with the Commission assessment. The clause facilitates the coordination of budgetary policies in times of severe economic downturn. As indicated in the Annual Sustainable Growth Strategy 2021 and as communicated in the letter of 19 September 2020 from the Commission to the EU Ministers of Finance, the activation of the general escape clause allows for a temporary departure from the adjustment path towards the medium-term budgetary objective of each Member State, which should continue to provide targeted and temporary fiscal support in 2021, provided that this does not endanger fiscal sustainability in the medium term. The general escape clause does not suspend the procedures of the Stability and Growth Pact. It allows Member States to depart from the budgetary requirements that would normally apply while enabling the Commission and the Council to undertake the necessary policy coordination measures within the framework of the Pact.

Public finances in 2021 are also expected to be influenced by the proposed establishment of the Recovery and Resilience Facility (RRF) and the reinforced long-term budget of the EU for 2021-2027. RRF is envisaged to provide a total envelope of €672.5 billion in loans and non-repayable financial support (grants) to support the implementation of investments and reforms in the EU Member States. The 2021 Draft Budgetary Plan of Estonia indicatively takes into account the implementation of the reforms and investments envisaged under the RRF in the amount of 0.5% of GDP.

On 20 May 2020, the Commission issued a report under Article 126(3) TFEU, as Estonia'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.

## 2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

According to the macroeconomic scenario underlying the Draft Budgetary Plan, real GDP is projected to fall in 2020 by 5.5% and to increase in 2021 by 4.5%; GDP levels at the end of 2021 are set to remain below those of 2019. The macroeconomic and fiscal outlook continue to be affected by high uncertainty due to the COVID-19 pandemic and its economic consequences. The main difference in the macroeconomic scenario compared to that of the Stability Programme stems from more up-to-date information about the first half of 2020, leading to slightly milder projected drop in GDP in 2020 and a less pronounced recovery in 2021. The macroeconomic and fiscal outlook continue to be affected by high uncertainty due to the COVID-19 pandemic.

According to the Plan, COVID-19 restrictions had a significant negative effect on private consumption. Export of goods remained relatively strong; in combination with the drop in imports, this led to a rising current account surplus. In 2021, a growth rebound is set to be supported by export, investment and recovering private consumption. The scenario assumes that national policies cushion the economic sectors that are not directly affected by the virus, and that the recession does not become widespread. While the unemployment rate is projected to double in 2020 and 2021 from its 2019 level, wage growth is set to stall and turn slightly positive in 2021. HICP inflation is forecast to be moderate around 1.4% in 2021.

This scenario is broadly in line with the Commission 2020 autumn forecast, although the Commission expects a smaller GDP decline in 2020 (reflecting the still favourable short-term economic developments), but also a smaller rebound in 2021. The projections for inflation for both 2020 and 2021 are broadly similar. The projections for unemployment are similar, while the Commission expects slightly higher wage growth in both 2020 and 2021 (reflecting recent short-term data).

The macroeconomic forecast underlying the Draft Budgetary Plan was prepared by the Fiscal Policy Department in the Ministry of Finance of Estonia and was assessed by the Fiscal Council (Eelarvenõukogu), which is an independent advisory body attached to the Bank of Estonia. The Council assesses the macroeconomic and fiscal forecasts of the Ministry of Finance and the extent to which the budgetary rules are followed, in accordance with the requirements of the State Budget Act and European Union law. On 21 September 2020, the Fiscal Council published an opinion[1] on the macroeconomic forecast of the Ministry of Finance. The Fiscal Council found that the forecast was a suitable basis for preparing the 2021 budget and the budgetary strategy, while flagging the higher-than-usual uncertainty surrounding the forecast. The Fiscal Council emphasised that the 2021 deficit should only exceed the 3% limit if justified by weak cyclical conditions and the increased coronavirus spending, recommending that the government improves the fiscal balance substantially in the years ahead.

[1] https://eelarvenoukogu.ee/news/fiscal-discipline-needs-to-be-restored-after-the-crisis

### Table 1. Comparison of macroeconomic developments and forecasts

| | 2019 | 2020 | | | 2021 | | |
|---|---|---|---|---|---|---|---|
| | COM | SP | DBP | COM | SP | DBP | COM |
| Real GDP (% change) | 5.0 | -8.0 | -5.5 | -4.6 | 8.0 | 4.5 | 3.4 |
| Private consumption (% change) | 3.3 | -11.3 | -4.9 | -4.4 | 8.9 | 2.8 | 3.5 |
| Gross fixed capital formation (% change) | 11.1 | -5.7 | -10.1 | -12.3 | 5.6 | 5.1 | 6.8 |
| Exports of goods and services (% change) | 6.2 | -12.3 | -8.5 | -10.4 | 12.0 | 5.8 | 7.3 |
| Imports of goods and services (% change) | 3.7 | -14.4 | -10.5 | -11.5 | 12.8 | 6.4 | 8.6 |
| *Contributions to real GDP growth:* | | | | | | | |
| - Final domestic demand | 4.9 | -7.0 | -4.9 | -4.7 | 5.7 | 2.7 | 3.7 |
| - Change in inventories | -0.6 | -2.3 | -1.8 | -0.3 | 1.7 | 1.9 | 0.1 |
| - Net exports | 2.0 | 0.9 | 1.0 | 0.4 | 0.2 | -0.1 | -0.4 |
| Output gap[1] | 4.2 | -6.4 | -3.6 | -3.7 | -2.4 | -2.2 | -3.6 |
| Employment (% change) | 1.3 | -8.2 | -2.9 | -3.5 | 2.8 | -0.3 | 0.2 |
| Unemployment rate (%) | 4.4 | 12.5 | 7.5 | 7.5 | 9.5 | 8.0 | 7.8 |
| Labour productivity (% change) | 3.7 | 0.2 | -2.7 | -1.1 | 5.0 | 4.8 | 3.2 |
| HICP inflation (%) | 2.3 | 0.5 | -0.4 | -0.5 | 2.2 | 1.4 | 1.4 |
| GDP deflator (% change) | 3.2 | 0.4 | -0.1 | 0.8 | 2.3 | 1.7 | 1.3 |
| Comp. of employees (per head, % change) | 9.3 | -1.5 | 0.2 | 3.1 | 7.0 | 1.3 | 1.5 |
| Net lending/borrowing vis-à-vis the rest of the world (% of GDP) | 3.1 | 5.9 | 5.9 | 4.1 | 5.2 | 5.8 | 3.3 |

Note:

[1]In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

*Source:*

*Stability Programme 2020 (SP); Draft Budgetary Plan for 2021 (DBP); Commission 2020 autumn forecast (COM); Commission calculations*

## 3. RECENT AND PLANNED FISCAL DEVELOPMENTS

On 20 July 2020 the Council addressed recommendations to Estonia in the context of the European Semester. In the area of public finances and in line with the general escape clause, the Council recommended Estonia to take all necessary measures to effectively address the pandemic, sustain the economy and support the ensuing recovery. When economic conditions allow, Estonia should pursue fiscal policies aimed at achieving prudent medium-term fiscal positions and ensuring debt sustainability, while enhancing investment.

### 3.1. Deficit developments

The Plan projects the general government balance to decline from a surplus of 0.1% of GDP in 2019 to a deficit of 6.6% of GDP in 2020 (Table 2), reflecting the operation of automatic stabilisers and fiscal measures. The deficit projection for 2020 shows an improvement by 3.5 percentage points compared to the 2020 Stability Programme, arising mainly from better than expected GDP growth in 2020 and higher tax revenues.

In 2021, the general government deficit is projected to remain high at of 6.7% of GDP. This is substantially higher (by 2.9 percentage points) than the Stability

Programme's target. The worsening of the budget balance in 2021 compared to the Stability Programme reflects the projected weaker GDP recovery in 2021 (lower tax bases), additional expenditure programmes in the 2021 budget, and carry over of some 2020 expenditure programmes into 2021, notably healthcare costs (see Section 4.2.).

The Commission 2020 autumn forecast projects a headline deficit of 5.9% of GDP in both 2020 and in 2021. The Commission forecasts smaller deficits than the Draft Budgetary Plan, reflecting Commission's more favourable macroeconomic and labour market condition for 2020 and 2021. Similarly, both forecasts project the deficit in 2021 to remain close to 2020 level. Compared to the pre-crisis year 2019, the deficit in 2021 is driven by the expenditure side (notable increases in social payments, subsidies and investments), while the revenue to GDP ratio is projected to remain broadly stable (Table 2).

The recalculated[2] structural balance in the DBP is estimated to have amounted to -2.4% of potential GDP in 2019, thereafter worsening to -5.3% in 2020 and to -6.3% in 2021. The better nominal balance and a somewhat different assessment of one-off measures[3] and output gap profile result in less negative structural deficit projections for 2020 and 2021 in the Commission forecast, -4.2% and -4.3% of GDP respectively. However, a mechanical reading of traditional indicators is not well suited at the current juncture to assessing the fiscal stance. The introduction and subsequent withdrawal of sizeable temporary emergency measures distort the picture, as the corresponding changes in the level of public spending from one year to the next affect the indicators used to assess the fiscal stance. Excluding the temporary emergency measures from the calculation of the fiscal stance indicators provides a more representative assessment of the underlying fiscal support to economic activity.

The Draft Budgetary Plan includes in its revenue projections grants of 0.5% of GDP under the Recovery and Resilience Facility in 2021 with corresponding expenditure of 0.5% of GDP.[4] 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 projection for 2021, the 10% pre-financing of the Recovery and Resilience Facility grants, and treats them as a financial transaction with no impact on the budget balance, but with a public debt-reducing impact. In the case of Estonia, the 10% pre-financing of Recovery and Resilience Facility grants is equivalent to EUR 110 million.[5] On the expenditure side, in line with its no-policy change assumption, the Commission forecast includes no

[2] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology. The estimates of the structural budget balance are affected by high uncertainty due to the economic consequences of the COVID-19 pandemic.

[3] The DBP includes one offs which increase the structural deficit for 2020 and 2021. The one-offs reflect the temporary suspension of state contributions to the second pillar pension funds.

[4] The statistical treatment of the financial support provided by the Recovery and Resilience Facility is subject to ongoing discussions between Eurostat and the Member States.

[5] The amount of pre-financing is 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.

expenditure related to the Recovery and Resilience Facility as the corresponding measures were not sufficiently specified at the cut-off date of the forecast.[6]

Overall, the risks associated with the Draft Budgetary Plan fiscal targets can be considered as tilting to the upside for 2020 and 2021, assessed against the more favourable Commission projection. The evolution of the deficit in 2021 could also turn out more favourable as a result of the higher economic growth from the implementation of measures financed by the Recovery and Resilience Facility.

[6] 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). 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.

## Table 2. Composition of the budgetary adjustment

| (% of GDP) | 2019 | | 2020 | | | 2021 | | | Change: 2019-2021 |
|---|---|---|---|---|---|---|---|---|---|
| | COM | DBP | SP | DBP | COM | SP | DBP | COM | DBP |
| **Revenue** | **39.0** | **39.0** | **39.2** | ***39.3*** | **39.5** | **38.7** | ***39.0*** | **39.0** | **0.0** |
| *of which:* | | | | | | | | | |
| - Taxes on production and | 14.0 | 14.0 | 13.3 | *13.4* | 13.2 | 13.1 | *13.3* | 13.4 | -0.7 |
| - Current taxes on income, | 7.3 | 7.3 | 7.0 | *7.4* | 7.3 | 7.1 | *6.8* | 7.0 | -0.5 |
| - Capital taxes | 0.0 | 0.0 | 0.0 | *0.0* | 0.0 | 0.0 | *0.0* | 0.0 | 0.0 |
| - Social contributions | 11.8 | 11.8 | 12.2 | *13.0* | 12.8 | 12.4 | *12.6* | 12.7 | 0.8 |
| - Other (residual) | 5.9 | 5.9 | 6.7 | *5.5* | 6.1 | 6.1 | *6.3* | 5.9 | 0.4 |
| **Expenditure** | **38.9** | **38.9** | **49.3** | **45.9** | **45.3** | **42.5** | **45.7** | **44.8** | **6.8** |
| *of which:* | | | | | | | | | |
| - Primary expenditure | 38.9 | 38.9 | 49.3 | 45.8 | 45.3 | 42.4 | 45.7 | 44.8 | 6.8 |
| *of which:* | | | | | | | | | |
| Compensation of employees | 11.5 | 11.5 | 13.5 | 12.5 | 12.7 | 11.9 | 12.1 | 12.4 | 0.6 |
| Intermediate consumption | 6.5 | 6.5 | 7.1 | 8.0 | 7.3 | 6.4 | 6.9 | 7.3 | 0.4 |
| Social payments | 13.4 | 13.4 | 16.6 | 17.0 | 15.8 | 14.4 | 15.0 | 16.0 | 1.6 |
| Subsidies | 0.5 | 0.5 | 0.4 | 1.4 | 1.4 | 0.4 | 0.4 | 0.7 | -0.1 |
| Gross fixed capital formation | 5.0 | 5.0 | 6.3 | 5.5 | 5.5 | 5.8 | 6.7 | 5.9 | 1.7 |
| Other (residual) | 2.1 | 2.1 | 5.4 | 1.4 | 2.5 | 3.5 | 4.6 | 2.6 | 2.5 |
| - Interest expenditure | 0.0 | 0.0 | 0.1 | 0.0 | 0.0 | 0.1 | 0.0 | 0.0 | 0.0 |
| **General government balance (GGB)** | **0.1** | **0.1** | **-10.1** | **-6.6** | **-5.9** | **-3.8** | **-6.7** | **-5.9** | **-6.8** |
| **Primary balance** | **0.1** | **0.1** | **-10.1** | **-6.6** | **-5.8** | **-3.7** | **-6.7** | **-5.8** | **-6.8** |
| One-off and other temporary measures | 0.0 | 0.0 | 0.0 | 0.5 | 0.0 | 0.0 | 0.7 | 0.0 | 0.7 |
| **GGB excl. one-offs** | **0.1** | **0.1** | **-10.1** | **-7.1** | **-5.9** | **-3.8** | **-7.4** | **-5.9** | **-7.5** |
| Output gap[1] | 4.2 | 5.0 | -6.4 | -3.6 | -3.7 | -2.4 | -2.2 | -3.6 | -7.2 |
| Cyclically-adjusted balance[1] | -2.0 | -2.4 | -7.0 | -4.8 | -4.1 | -2.7 | -5.6 | -4.1 | -3.5 |
| **Structural balance (SB)[2]** | **-2.0** | **-2.4** | **-7.0** | **-5.3** | **-4.1** | **-2.6** | **-6.3** | **-4.1** | **-4.2** |
| Structural primary balance[2] | -2.0 | -2.3 | -6.9 | -5.3 | -4.0 | -2.6 | -6.3 | -4.1 | -4.2 |

Notes:

[1] Output gap (in % of potential GDP) and cyclically-adjusted balance according to the DBP/Programme as recalculated by Commission on the basis of the DBP/Programme scenario using the commonly agreed methodology.

[2] Structural (primary) balance corresponds to cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

Source:

*Stability Programme 2020 (SP); Draft Budgetary Plan for 2021 (DBP); Commission 2020 autumn forecast (COM); Commission calculations*

### 3.2. Debt developments

The Draft Budgetary Plan indicates that the government debt-to-GDP ratio will increase from 8.4% at the end of 2019 to 23.6% in 2021, below the Commission's projection of 22.5%. The difference between the two projections is mainly explained by the differences in the primary balance (see Table 3).

**Table 3. Debt developments**

| (% of GDP) | 2019 | 2020 | | | 2021 | | |
|---|---|---|---|---|---|---|---|
| | | SP | DBP | COM | SP | DBP | COM |
| **Gross debt ratio**[1] | **8.4** | **21.9** | **18.2** | **17.2** | **23.4** | **23.6** | **22.5** |
| Change in the ratio | 0.2 | 13.5 | 9.8 | 8.8 | 1.5 | 5.4 | 5.3 |
| Contributions[2]: | | | | | | | |
| **1. Primary balance** | **-0.1** | **10.1** | **6.6** | **5.8** | **3.7** | **6.7** | **5.8** |
| **2. "Snow-ball" effect** | **-0.6** | **0.8** | **0.5** | **0.4** | **-1.9** | **-1.0** | **-0.7** |
| *Of which:* | | | | | | | |
| Interest expenditure | 0.0 | 0.1 | 0.0 | 0.0 | 0.1 | 0.0 | 0.0 |
| Real growth effect | -0.4 | 0.7 | 0.5 | 0.4 | -1.6 | -0.8 | -0.6 |
| Inflation effect | -0.2 | 0.0 | 0.0 | -0.1 | -0.5 | -0.3 | -0.2 |
| **3. Stock-flow adjustment** | **0.9** | **2.7** | **2.7** | **2.6** | **-0.2** | **-0.2** | **0.2** |
| *Of which:* | | | | | | | |
| Cash/accruals difference | | 0.0 | 0.0 | | 0.0 | 0.0 | |
| Net accumulation of financial | | 0.0 | 0.0 | | 0.0 | 0.0 | |
| of which privatisation proceeds | | 0.0 | 0.0 | | 0.0 | 0.0 | |
| Valuation effect & residual | | 0.0 | 0.0 | | 0.0 | 0.0 | |

Notes:

[1] End of period.

[2] The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

*Source:*

*Stability Programme 2020 (SP); Draft Budgetary Plan for 2021 (DBP); Commission 2020 autumn forecast (COM); Commission calculations*

## 4. MEASURES UNDERPINNING THE DRAFT BUDGETARY PLAN

The Draft Budgetary Plan focuses on the policy response undertaken in the context of the COVID-19 outbreak in 2020 and the measures planned to sustain the recovery in 2021. Supportive fiscal measures should be tailored to the specific situation of each Member State, but as a rule, they should be well targeted and temporary. Their use and effectiveness should be regularly reviewed by the national authorities. Depending on the development of the pandemic, emergency fiscal measures should to be adjusted and combined with other measures that improve economic fundamentals, support the green and digital transition and have a positive impact on demand.

### 4.1. Measures in 2020

In response of the COVID-19 pandemic, Estonia's fiscal measures were adopted with the Supplementary Budget on 16 April 2020. The crisis alleviation measures in the budget amounted to EUR 1.15 billion, or 4.3% of GDP, including the calculated fiscal deficit effect (losses) of liquidity and loan measures. Compared to the supplementary budget (and the spring Stability Programme), the new Plan contains an updated costing of these measures, now estimated to amount to 3% of GDP in 2020. Notably, the estimated fiscal costs have been also substantially revised downwards taking into account that the uptake of the guarantee schemes has been substantially less than initially planned.

The largest fiscal measures for 2020 on the revenue side include: lowering excises on fuels for 2 years; stopping state payments to the second pillar pension funds (improving the budget balance); rescheduling and lowering interest rates on tax liabilities. Measures on the expenditure side include: raising of healthcare-related spending; wage subsidy scheme supporting employment (scheme ended in June); additional funding for local governments; and specific investment programmes (housing insulation and road construction). Various smaller measures were targeted to specific sectors, such as shipping, education, and culture. The Plan presents these measures in a grouped way (see Table 4 below). The Plan and the Commission forecast include a similar assessment of these measures. The maximum contingent liability from guarantee measures amount to 1.26% of GDP, but only over 20% of this has been taken up as of September (Table 4.1b). In addition to the guarantee measures, direct loan schemes were also provided (details not specified in the Plan). The Plan and the Commission forecast include the same estimate for losses that will likely result from the liquidity measures (guarantees and loans), largely starting from 2021. This reflects the standardised nature of the instruments and past practices applied by the national statistical authorities.

Overall, the measures taken by Estonia 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.

## Table 4.1.a. Main discretionary measures adopted/announced with budgetary impact reported in the Draft Budgetary Plan

| List of measures | Detailed description | ESA Code (Expenditure / Revenue) | Adoption status | Budgetary impact (% of GDP - change from previous year, positive sign for deficit-increasing measures) | |
|---|---|---|---|---|---|
| | | | | **2020*** | **2021*** |
| | | | | *% of GDP* | *% of GDP* |
| **Supplementary budget 2020** | | | | | |
| 1) Changes in law | Temporary suspension of contributions to the second pillar pension funds, reduction of fuel excise duties (diesel, liquid gas, natural gas, electricity), reduction of the interest rate on tax arrears rescheduling up to 100% instead of 50% | Revenue, D61, D2, D7 | Submitted with supplementary budget | -0.02 | -0.38 |
| 2) Personal support | Wage support measure managed, extrabudgetary support to Health Insurance FundState, reimbursement of sick days for workers from the first to the third day of sickness insurance | Expenditure, D61 | Submitted with supplementary budget | 1.39 | |
| 3) Additional operating grants | Local government support measure, support measure in the tourism sector, micro and small business measure through capital injections, reimbursement of 75% of all types of port dues for passenger ships by 2020 | Expenditure, D9 | Submitted with supplementary budget | 0.57 | 0.04 |
| 4) Finance instruments | Support purchases of shares in strategic companies or capital expansion of state-owned companies, operating and investment loan losses | Expenditure, P2 | Submitted with supplementary budget | 0.06 | 0.34 |
| 5) Investments | Renovation support measure for apartment buildings and private houses via KredEx, reconstruction of local government and Road Administration roads, last mile support for sparsely populated areas | Expenditure, P51g | Submitted with supplementary budget | 0.18 | 0.46 |
| 6) Government reserves | Creation of a COVID specific reserve and increasing government reserve | Expenditure, P2 | Submitted with supplementary budget | 0.87 | |
| **Draft Budget 2021** | | | | | |
| 1) Tax changes | Changes in VAT and tobacco excise duty | Revenue, D2 | Submitted with budget | | -0.02 |
| 2) Additional grants | Intensive use of funds of the new EU financial period, replacement of KredEx expenses with EU funds | Revenue, D7 | Draft is not required | | -1.11 |
| 3) Additional dividends | Additional dividends with CIT | Revenue, D5 | Draft is not required | | -0.005 |
| 4) Changes in operating costs | Support for different budgetary and extrabudgetary institutions incl. increase in defence and R&D costs | Expenditure, P2 | Submitted with budget | | 0.43 |
| 5) Additional investments | Road projects, defence and IT investments, support for local governments | Expenditure, P51g | Submitted with budget | | 0.5 |
| 6) Additional investments from new EU funds | Hospitals, public buildings and infrastructure | Expenditure, P51g | Submitted with budget | | 0.75 |
| 7) Social transfers and other transfers | Increase in pensions | Expenditure, D62 | Submitted with budget | 0.01 | 0.19 |
| 8) Cut in management costs | Cut in management costs of budgetary institutions | Expenditure, D1 | Submitted with budget | | -0.04 |
| | | | **TOTAL** | **3.1** | **1.2** |

**Table 4.1.b. Guarantees adopted/announced in response to COVID-19 outbreak**

| Description of measures | Adoption status | Maximum amount of contingent liability (% of GDP) | Current take-up (actual contingent liability, % of GDP) |
|---|---|---|---|
| Loan guarantees for bank loans already issued in order to allow for repayment schedule adjustments and other (Kredex) | Already adopted | 1.15 | 0.18 |
| Loan guarantees for bank loans already issued, increase of the guarantee reserve and reduction of guarantee fees (MES) | Already adopted | 0.11 | 0.04 |
| | **Total** | 1.26 | 0.22 |

Source: Draft Budgetary Plan

## 4.2. Measures in 2021

In order to support the economic recovery, the government decided not to reduce the costs of general government in 2021. In addition, the 2021 budget plan has allocated resources to some specific expenditure programmes, amounting to 1.8% of GDP (partly offset by measures improving the budget balance by 1.1% of GDP, with the net effect on budget balance of 0.7% of GDP). Notably, additional funding is given to a multitude of small-scale investment projects (1% of GDP), to an extraordinary rise in pensions above the indexation, on average by 20 euros (0.2% of GDP), to spending on R&D (0.2% of GDP) and defence (0.2% of GDP). Also, EU-funded projects are brought forward and in some cases replace domestically funded projects, which the Plan assumes to improve the budget balance by 1.1% of GDP. The Plan grouped these measures under different headings (see Table 4.1).

Some of these measures appear not to be temporary and matched by offsetting measures, notably the rise in pensions, R&D and defence[7] expenditure (all together amounting to 0.5% of GDP). The Commission 2020 autumn forecast considers the described measures credibly announced and sufficiently specified and incorporates them with no difference in their assessment.

The Plan's measures do not include an extension of liquidity, guarantee or short term working schemes into 2021.

The Plan includes one-off measures for both 2020 and 2021 (0.5% and 0.7% of GDP respectively), reflecting the temporary suspension of state contributions to the second pillar pension funds until 2022[8]. In effect, it leads to a temporary increase in revenues for 2020 and 2021 (and a decrease in 2022). The Commission does not include this measure as a one-off, but as a COVID-related temporary measure.

[7] Defence spending rise is likely permanent at least in the medium term as it is linked to specific mid-term projects.

[8] The description of one-offs is not included in the DBP document, but supplementary information was provided by the Ministry of Finance.

Overall, the measures in the Draft Budgetary Plan of Estonia are supporting economic activity against the background of considerable uncertainty. Most of the measures set out in the Draft Budgetary Plan are temporary. It would be useful 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 Estonia 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.

## 5. ANNEX – MANDATORY VARIABLES NOT INCLUDED IN THE DRAFT BUDGETARY PLAN

The Draft Budgetary Plans does not include some mandatory variables, notably: ‘GDP growth attributable to the estimated impact of aggregated budgetary measures’. Not included mandatory variables do not impede the Commission’s ability to assess the Draft Budgetary Plan based on the plan’s assumptions.