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Assessment of the 2019 Stability Programme for

Slovakia

(Note prepared by DG ECFIN staff)

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EXECUTIVE SUMMARY

Slovakia is subject to the preventive arm of the Stability and Growth Pact (SGP). With a gross public debt of 48.9% of GDP in 2018, Slovakia is compliant with the debt criterion.

The Slovak economy expanded by 4.1% in 2018 in real terms and economic growth is expected to remain solid, moderating slightly to 3.8% in 2019 and to 3.4% in 2020, according to the Commission 2019 spring forecast. Growth is expected to be mainly driven by robust domestic demand, while net trade also contributes positively. With a short-term growth outlook above the level of potential growth, the positive output gap is forecast to widen to above 2% of potential GDP in 2019. Employment is expected to grow moderately, leading the unemployment rate to decline to below 6%. Wage growth is projected to accelerate in 2019 due to continued tightening in the labour market, contributing to overall inflation remaining elevated at around 2.5%. The macro-economic scenario included in the Stability Programme is plausible.

In this context, the general government deficit declined to 0.7% of GDP in 2018. The 2019 Stability Programme (hereafter called Stability Programme) expects balanced budgets in both 2019 and 2020. The Stability Programme forecasts an improvement in the structural balance in 2019 by 0.5 percentage points of GDP, which is not confirmed by the Commission 2019 spring forecast. The main differences for 2019 between the Stability Programme and the Commission forecast are attributable to different assumptions on the drawdown profile for EU funds, wage bill developments in 2019 and investment growth in both 2019 and 2020. Risks to the fiscal outlook mainly stem from the effect of fiscal measures decreasing taxes in 2020 that could be taken in the context of the parliamentary elections. Government discretionary measures, presented in the Stability Programme, are primarily on the expenditure side and have an overall deficit-increasing impact of around ½% of GDP.

Based on the Commission forecast, Slovakia is at risk of significant deviation from the adjustment path towards the medium-term budgetary objective (MTO) in both 2019 and 2020.

1. INTRODUCTION

On 25 April 2019 Slovakia submitted its Stability Programme, covering the period 2017-2022.[1] An updated and corrected version of the Stability Programme was delivered on 2 May 2019, leaving the fiscal outlook unchanged. The government approved the Stability Programme on 17 April 2019 and it was submitted to the Parliament on 23 April 2019.

Slovakia is currently subject to the preventive arm of the SGP and should ensure sufficient progress towards its MTO.

This document complements the Country Report published on 27 February 2019 and updates it with the information included in the Stability Programme.

Section 2 presents the macroeconomic outlook underlying the Stability Programme and provides an assessment based on the Commission 2019 spring forecast. The subsequent

[1] The English version of the Stability Programme was submitted on 25 April and the updated version on 2 May 2019. The updated version was without an impact on the assessment.

section presents the recent and planned budgetary developments, according to the Stability Programme. In particular, it includes an overview on the medium term budgetary plans, an assessment of the measures underpinning the Stability Programme and a risk analysis of the budgetary plans based on the Commission forecast. Section 4 assesses compliance with the rules of the SGP, including based on the Commission forecast. Section 5 provides an overview on long-term sustainability risks and Section 6 on recent developments and plans regarding the fiscal framework. Section 7 provides a summary.

2. MACROECONOMIC DEVELOPMENTS

Slovakia's economic growth rate increased markedly to 4.1% in 2018 on the back of strong household spending and a boost in investment. Domestic demand was supported by strong employment growth and robust increases in real wages, as well as the construction of a new car factory.

According to the Stability Programme, economic growth is set to ease slightly to 4.0% in 2019 and to 3.7% in 2020. Final domestic demand is forecast to contribute by 2.5 percentage points and 2.4 percentage points to real GDP growth in 2019 and in 2020, respectively: While investment growth is projected to slow down markedly in 2019 and to stabilise at around 3% thereafter, private consumption is projected to remain robust, though softening from 2020 onwards. Net exports are projected to make a strong contribution of 1.5 percentage points to real GDP growth in 2019, with expanded production facilities in the car industry boosting Slovakia's export capacities.

Table 1: Comparison of macroeconomic developments and forecasts

	2018		2019		2020		2021	2022
	COM	SP	COM	SP	COM	SP	SP	SP
Real GDP (% change)	4.1	4.1	3.8	4.0	3.4	3.7	3.2	2.5
Private consumption (% change)	3.0	3.0	3.2	3.3	2.9	2.9	2.2	1.7
Gross fixed capital formation (% change)	6.8	6.8	2.6	1.9	2.8	2.9	3.1	3.6
Exports of goods and services (% change)	4.8	4.8	6.1	6.9	5.5	6.1	5.2	4.1
Imports of goods and services (% change)	5.3	5.3	5.2	5.9	5.0	5.3	4.5	3.8
Contributions to real GDP growth:								
- Final domestic demand	3.5	4.0	2.8	2.5	2.7	2.4	2.0	1.8
- Change in inventories	0.5	0.5	0.0	0.1	0.0	0.0	0.0	0.0
- Net exports	-0.3	-0.1	1.0	1.5	0.7	1.3	1.2	0.7
Output gap[1]	1.5	1.2	2.1	1.8	2.3	1.9	1.6	0.9
Employment (% change)	2.0	2.0	0.8	1.1	0.4	0.8	0.6	0.5
Unemployment rate (%)	6.5	6.6	5.9	6.0	5.6	5.6	5.5	5.3
Labour productivity (% change)	2.1	2.1	3.0	2.9	3.0	2.9	2.6	2.0
HICP inflation (%)	2.5	2.5	2.4	2.6	2.3	2.4	2.4	2.4
GDP deflator (% change)	2.1	2.1	2.6	2.6	2.5	2.4	2.4	2.4
Comp. of employees (per head, % change)	5.4	5.4	6.8	6.7	6.7	6.3	5.3	4.4
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	-1.6	-0.9	-1.0	-0.4	-0.6	0.1	0.5	0.6

Note:

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

Source:

Commission 2019 spring forecast (COM); Stability Programme (SP).

The macroeconomic scenario in the Stability Programme constitutes a downward revision of 0.5 percentage points of projected 2019 GDP growth compared to the latest Draft Budgetary Plan (DBP), largely due to weaker expected trade dynamics and lower expected investment growth.

The macroeconomic scenario underlying the Stability Programme is broadly in line with the Commission 2019 spring forecast. The slightly lower Commission spring forecast of GDP headline growth of 3.8% for 2019 and of 3.4% for 2020 results from a lower assumed contribution of net trade (1.0 vs 1.5 percentage points in 2019 and 0.7 vs. 1.3 percentage points in 2020). This is partially offset by the Stability Programme's lower assumed contribution of final domestic demand. As the Stability Programme is based on the forecast published in February, it may not yet have taken into account some data showing a worsening external environment. The forecast is furthermore subject to an uncertain trade outlook, with risks tilted to the downside including faltering growth in Germany, Slovakia's main trading partner, and developments affecting the car industry, such as the possible imposition of U.S. tariffs.

Both the Stability Programme and the Commission 2019 spring forecast expect the labour market to further tighten further on the back of continued economic expansion, albeit at a slowing pace, with the unemployment rate gradually declining to around 6% in 2019. Both forecasts project accelerating wage growth in 2019 to continue to prop up earnings and incomes and to support consumer spending, also contributing to HICP inflation remaining elevated at around the 2018 value of 2.5%.

The output gap, as recalculated by the Commission based on the information in the Stability Programme and following the commonly agreed methodology, is somewhat below the estimates in the Commission 2018 spring forecast in both 2018 and 2019. At the same time, both the Stability Programme and the Commission estimate the output gap to have entered positive territory in 2017 and to continue widening in 2019, reflecting the quickened pace of economic expansion.

Overall, the macroeconomic assumptions underpinning the Stability Programme appear to be plausible.

3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS

3.1. DEFICIT DEVELOPMENTS IN 2018 AND 2019

In 2018, the general government deficit declined to 0.7% of GDP (Table 2). The outturn was slightly better than the 2018 deficit target of 0.8% of GDP presented in the 2018 Stability Programme. It thereby also exceeded the expected outcome of 0.8% of GDP presented in the Draft Budgetary Plan (DBP) for 2018.

Both revenues and expenditure recorded faster growth than GDP in 2018. Total revenues rose more quickly than expected in the 2019 DBP and the general government revenues-to-GDP ratio increased to 39.9% of GDP, mainly on the back of higher than expected EU funds drawdown reflected in current and capital transfers' developments. Higher property income was also reported. Value added taxes and current income taxes grew more slowly than the DBP anticipated. This was despite the fact that labour market developments and average monthly wage growth were roughly the same as assumed in the DBP. The effective tax rates (ETR) estimated for 2018 based on observed tax collection developments are lower in

comparison to the DBP. The ETR was revised slightly downwards for value added tax. Lower growth than the macroeconomic base was reported for corporate income tax. On the other hand, personal income tax receipts surpassed wage bill growth and the DBP expectations. Compared to the DBP, excise taxes were revised down, which resulted in a declining ETR for this tax type. The Stability Programme attributes around 20% of the observed rise in tax revenues to better tax collection. Overall, legislated fiscal measures had a broadly neutral impact. The tax burden was 0.4 percentage points lower than expected in the DBP, and reached 33% of GDP. Higher than budgeted revenues from VAT and income taxes were partly eliminated by shortfalls in emission allowances and gaming. Social contributions were boosted by stronger labour market developments than expected in the budget. Some revenue items were not traditionally included in the DBP – e.g. interest incomes, revenues from business activities of universities or JAVYS, a.s.[2]

On the expenditure side, the general government expenditure-to-GDP ratio increased to 40.6% due to more robust investment activity in both central and local government. Spending on current transfers also exceeded expectations. In comparison with the DBP, compensations of employees increased more rapidly, particularly in the regional and municipal sector and also in the social insurance company. Trends in all these items can be explained by, among other factors, by the higher EU funds drawdown rate. This was neutral in terms of balance but the deficit was affected by the corresponding national part of funding. Higher-than-expected gross fixed capital formation could be partly attributed to municipal elections held in November 2018. The Stability Programme also attributes the stronger-than-anticipated outturn to investments in transport infrastructure.

For 2019, the Stability Programme forecasts a balanced budget, which is identical to the target presented in the DBP for 2019 when adjusted for the supplementary structural measure of 0.1% of GDP on the expenditure side announced additionally by Slovak authorities on November 20, 2018.[3] The originally submitted DBP assumed higher capital expenditure due to an unallocated budgetary reserve. Discrepancies between the Stability Programme and the DBP concern the revenue and expenditure levels, which are both 0.7 percentage points higher in the Stability Programme (39.1% of GDP). The revenue structure differs due to higher social contributions (by 0.2 percentage points), which is consistent with the assumption of a stronger labour market and higher state payments for the state-insured, and due to other revenues including transfers from the EU (by 0.4 percentage points). The revenue side is affected by measures approved in the Parliament after the budget approval (e.g. exemption of holiday vouchers from taxes and levies, decreased VAT rate on accommodation services etc.). However, the impact of these was covered by the reserve included on the expenditure side in the budget[4].

On the expenditure side, the main differences are due to higher compensation of employees (by 0.2 percentage points), social transfers (by 0.3 percentage points), gross fixed capital formation (by 0.3 percentage points) and interest (by 0.1 percentage point). The first three items are partly linked to higher EU fund absorption capacity than expected by the DBP. Social transfers includes an increase of child tax bonus (60 million euros), which was not

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[2] Nuclear and Decommissioning Company

[3] 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-2019_en#slovakia

[4] E.g. lower VAT rate on accommodation services (-24 million euros) and the exemption of holiday vouchers from taxes and health and social insurance (-61 million euros).

included in the DBP. Higher gross fixed capital formation is expected in municipalities and transport infrastructure (Railways of the Slovak Republic and National Motorway Company). These increases are somewhat subdued by lower intermediate consumption (by 0.1 percentage point) and other expenditure (by 0.3 percentage points) including e.g. other current transfers. The former item encompassed the aforementioned reserves reflecting measures not yet approved at the moment of the DBP submission.

For 2019 Slovakia has not been granted a temporary deviation from the required adjustment path under the structural reform or investment flexibility clauses.

The Stability Programme does not explicitly quantify any one-off or temporary measures in any of the years covered by the projections.

3.2. MEDIUM-TERM STRATEGY AND TARGETS

The aim of the fiscal strategy presented in the Stability Programme is to bring down the headline deficit from 0.7% of GDP in 2018 to 0.0% of GDP in 2019 and maintain a balanced budget between 2020 and 2022 (see figure 1). According to the Stability Programme, this strategy would allow the structural balance to meet the MTO from 2019 onwards. The structural balance recalculated by the Commission based on the information in the Stability Programme according to the commonly agreed methodology is projected to decline to -0.7% of GDP in 2019 and remain at -0.7% of GDP in 2020. This implies that Slovakia would be close to the MTO in 2019 according to the 2019 Stability Programme.

According to the Stability Programme, the structural balance at face value should reach -0.4% of GDP in both 2019 and 2020. This is somewhat smaller than the recalculated structural balance of the Stability Programme of -0.7% of GDP in both years, the difference being accounted for mainly by a higher positive output gap underpinning the recalculation according to the commonly agreed methodology.

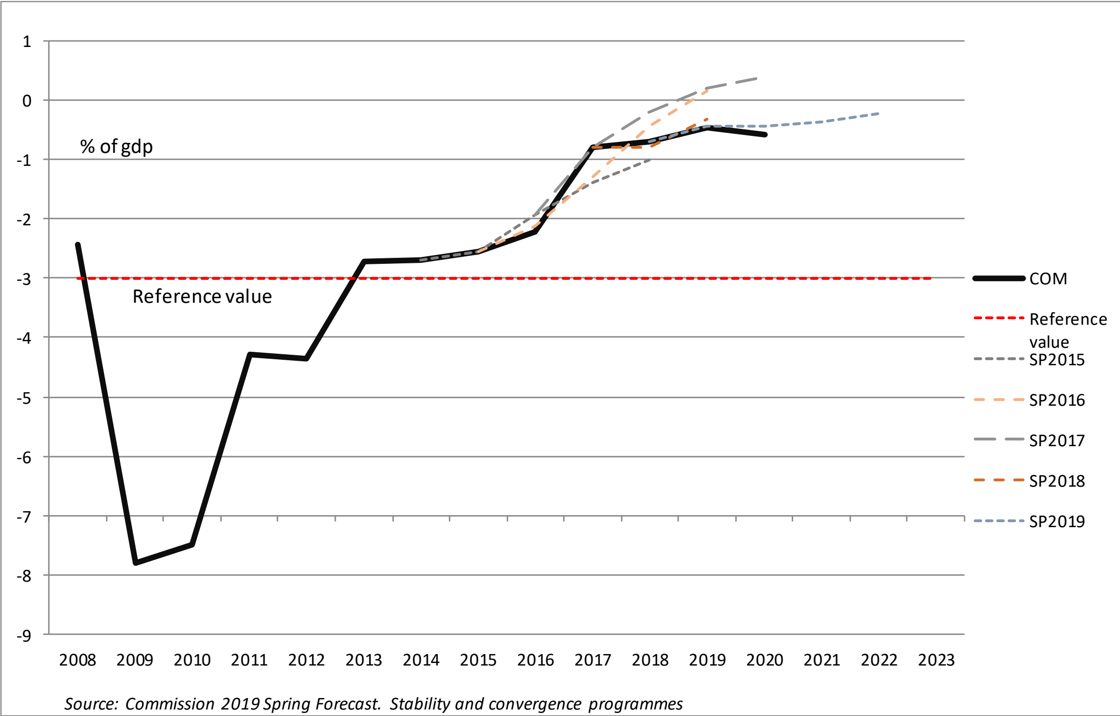
Slovakia does not assume to be covered by the structural reform or investment clauses in its Stability Programme plan.

The Programme's budgetary targets for 2020 and 2021 are affected by specified measures. Under a no-policy-change assumption (NPC), surpluses of 0.4% and 0.2% of GDP are projected to be achieved in years 2020 and 2021 respectively according to the Stability Programme.

Fiscal policy measures, the breakdown of which is provided in the subsequent sections 3.3 and 3.4, are predominantly on the expenditure side. The Stability Programme assumes higher indexation of salaries in public administration and a higher increase in investment in the army compared with a NPC scenario. In addition, a reserve provisioning for higher investment activity and slowing economic growth is included on the expenditure side. On the revenue side, the tax allowance linked to the provision of a 13th and 14th month's salary was amended (the minimum amount for which was reduced to 500 euros) at a revenue cost between 30 and 50 million euros. Additionally, there has been an increase in the fee for managing emergency oil reserves by one euro cent, which will mean an increase of 33 million euros in revenues. Hospitals will receive additional resources in comparison with the NPC scenario. This will result in an additional 0.1% of GDP per year throughout the Stability Programme horizon. On the expenditure side, higher expenditure is expected compared to the NPC scenario throughout the Programme horizon by 0.4 percentage points in both 2020 and 2021 and

0.2 percentage points in 2022. Specifically, the following expenditure items are increased: compensation of employees (maintaining the same 10% indexation in 2020 as in 2019; 0.3% of GDP), intermediate consumption linked to army modernisation (0.2% in 2021 and 0.1% of GDP in 2022), social transfers in kind[5] (0.1% of GDP in 2020-2022) and capital expenditure (0.1% in 2020 and 0.05% in both 2021 and 2022).

Figure 1: Government balance projections in successive programmes (% of GDP)



The Stability Programme changes the MTO from a deficit of 0.5% of GDP in 2019 to a deficit of 1% of GDP for 2020-2022. The MTO reflects the objectives of the Pact.

According to the Stability Programme, the expenditure-to-GDP ratio is projected to decline by 0.5 percentage points in 2020, i.e. at the same pace as the revenue ratio, so as to maintain a balanced budget in headline terms. The expected fall in the expenditure ratio between 2019 and 2020 is driven mainly by a decline in the intermediate consumption and social transfers other than in kind - each by 0.5 percentage points. Declines are also expected in capital transfers (by 0.2 percentage points), interest and social transfers in kind (both by 0.1 percentage point). These contractionary measures are primarily offset by increases in other expenditure (by 0.5 percentage points). The Commission 2019 spring forecast projects similar investment activity and other transfers levels as in 2018 and a slower decline in social payments in 2020 in comparison with the Stability Programme.

On the revenue side, the largest decline is projected for social contributions and other revenues, which, as shares of GDP, are projected to decline by 0.3 percentage points each. The Stability Programme does not fully indicate the cause for this decline.

[5] Due to higher income from health insurance.

The Stability Programme suggests that the consolidation effort in all covered years mainly originates from social security funds, while the central government balance is projected to remain unchanged from 2020 and a surplus in local government is expected to decline by 0.1 percentage point every year. The Commission assumes stronger social contributions and mainly revenues from EU funds.

In 2022, the Stability Programme presents the same fiscal target as in 2021, with ongoing declines in both the revenues and expenditure shares to 37.7% of GDP.

Table 2: Composition of the budgetary adjustment

(% of GDP)	2018	2019		2020		2021	2022	Change: 2018-2022
	COM	COM	SP	COM	SP	SP	SP	SP
Revenue	**39.929**	**39.9**	**39.1**	**39.7**	**38.4**	**37.9**	**37.7**	**-2.2**
of which:								
- Taxes on production and imports	10.9	11.0	11.0	10.8	10.9	10.6	10.5	-0.4
- Current taxes on income, wealth, etc.	7.3	7.4	7.3	7.4	7.3	7.3	7.2	-0.1
- Social contributions	14.8	14.8	14.7	14.7	14.4	14.3	14.2	-0.6
- Other (residual)	7.0	6.8	6.0	6.7	5.7	5.7	5.8	-1.2
Expenditure	**40.6267**	**40.4**	**39.1**	**40.2**	**38.4**	**37.9**	**37.7**	**-2.9**
of which:								
- Primary expenditure	39.3	39.2	37.9	39.0	37.4	36.9	36.7	-2.6
of which:								
Compensation of employees	9.3	9.5	9.4	9.7	9.5	9.4	9.2	-0.1
Intermediate consumption	5.4	5.4	5.5	5.4	5.0	5.1	4.9	-0.5
Social payments	18.1	17.7	17.7	17.4	17.1	16.8	16.5	-1.6
Subsidies	0.4	0.5	0.5	0.5	0.5	0.5	0.4	0.0
Gross fixed capital formation	3.6	3.6	2.7	3.6	2.7	2.5	3.1	-0.5
Other (residual)	2.5	2.4	2.2	2.5	2.5	2.7	2.6	0.1
- Interest expenditure	1.3	1.3	1.2	1.2	1.1	1.0	1.0	-0.3
General government balance (GGB)	**-0.7**	**-0.5**	**0.0**	**-0.6**	**0.0**	**0.0**	**0.0**	**0.7**
Primary balance	**0.6**	**0.8**	**1.2**	**0.6**	**1.1**	**1.0**	**1.0**	**0.4**
One-off and other temporary measures	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
GGB excl. one-offs	**-0.7**	**-0.5**	**0.0**	**-0.6**	**0.0**	**0.0**	**0.0**	**0.7**
Output gap[1]	1.5	2.1	1.8	2.3	1.9	1.6	0.9	-0.6
Cyclically-adjusted balance[1]	-1.3	-1.3	-0.7	-1.4	-0.7	-0.6	-0.3	0.9
Structural balance[2]	**-1.3**	**-1.3**	**-0.7**	**-1.4**	**-0.7**	**-0.6**	**-0.3**	**0.9**
Structural primary balance[2]	0.0	0.0	0.5	-0.2	0.3	0.4	0.7	**0.6**

Notes:

[1]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission on the basis of the

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

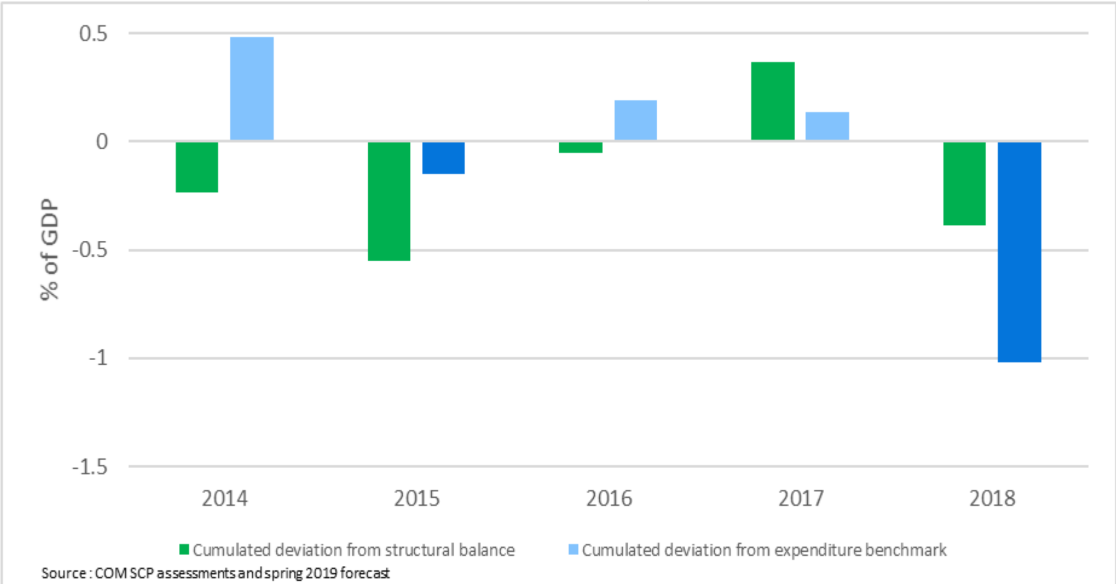
Source :

Stability Programme (SP); Commission 2019 spring forecasts (COM); Commission calculations.

Since the correction of the excessive deficit in 2013 and the abrogation of EDP in 2014, Slovakia has been subject to the preventive arm of the SGP. Slovakia was granted the investment clause for 2014 that allowed a deviation of 0.4% of GDP from the requirement. In 2016, 2017 and 2018, structural balance improvements of 0.25%, 0.5% and 0.44% of GDP respectively were required under the preventive arm. Over the 2014-2018 period, Slovakia did not meet these recommendations and its cumulative deviation was -0.39% of GDP (see Figure 2). Although positive deviations were achieved in years 2016 and 2017, these were more than compensated by negative deviations recorded in 2014 and 2015, as well as by the 2018

deviation. The expenditure benchmark pointed to deviations in years 2015, 2017 and 2018. The cumulative deviation for the last five years was around -1% of GDP. The expenditure benchmark recorded a positive deviation in 2016. Discrepancies with the structural balance arose mainly from the negative impact of revenue shortfalls on the structural balance and the role of the deflator on the expenditure benchmark. However, a part of the difference was offset by a significant fall in investment in 2016. By contrast, the structural balance was positively impacted by revenue windfalls and declining interest expenditure in 2017 and 2018, generating a more negative picture for the expenditure benchmark On cumulative basis, as regards the evolution in the preventive arm, the expenditure benchmark was more stringent than the structural balance for Slovakia.

Figure 2: Cumulative deviations of the preceding five years from the upper limit for net growth of government expenditure and from structural effort requirements (in % of GDP)



3.3. MEASURES UNDERPINNING THE PROGRAMME

In 2019, additional revenue measures with a net income of 155.5 million euros (around 0.16% of GDP) are presented in the Stability Programme. Sold automotive fuels have to be newly added with identification substances, which is expected to help in the fight against tax evasion in the field of excises. The financial administration has launched an online project connecting all cashiers on a mandatory basis to eKasa's financial administration portal. In the first phase, hotels, restaurants, cafes and gas stations should be connected to the eKasa. Later, retail, services and other sectors will be involved. Additional revenues of 90 million euros are expected from both measures taken together. Retail chains operating in Slovakia were supposed to be subject to a special levy on their net turnover from 2019. The levy was expected to yield 85 million euros (around 0.09% of GDP) by the Stability Programme. At the beginning of April 2019, Parliament approved the cancellation of the levy. The Stability Programme does not take this cancellation into consideration, but notes that in order to keep the targeted balance, it will be necessary to respond to this action also on the expenditure side during the fiscal year. This is the main difference in revenue measures compared to the Commission 2019 spring forecast, which factors in the cancellation on the revenue side. Revenues from the cancelled special levy on retail chains were earmarked for agricultural spending, which means that the measure was originally intended to have a neutral impact on balance. Remaining discretionary revenue measures are recorded in the Stability Programme

and the Commission 2019 spring forecast in a broadly similar way. On the expenditure side, measures are mainly expansionary in nature when compared to the NPC scenario. The main measures are the increase of salaries by 10% (0.6% of GDP), the introduction of free lunches for pupils (0.07% of GDP), a reserve for projects (0.2 % of GDP), the increase in the so-called Christmas pensions and doubling the tax bonus for parents of children under 6 years of age (0.06% of GDP each).

Main budgetary measures included in the Programme

Revenue	Expenditure
2018	
• Abolition of minimum corporate income tax (-0.1% of GDP)	
2019	
• eKasa and gas additives (0.09% of GDP)	• Growth of wages (0.7% of GDP)
2020	
• eKasa and gas additives (0.09% of GDP) • Higher sales of hospitals (0.1% of GDP)	• Growth of wages (0.3% of GDP) • Social transfers in kind (0.1% of GDP) • Capital expenditure – modernisation of army and other yet unspecified recovery measures (0.1% GDP)
2021	
• Abolition of bank levy (-0.1% of GDP) • Higher sales of hospitals (0.1% of GDP)	• Growth of wages (0.1% of GDP) • Social transfers in kind (0.1% of GDP) • Intermediate consumption – army modernisation (0.15% of GDP)
2022	
• Higher sales of hospitals (0.1% of GDP)	• Social transfers in kind (0.1% of GDP) • Intermediate consumption – army modernisation (0.1% of GDP)
Note: The table refers to the main measures included in the 2019 Stability Programme that have an incremental budgetary impact over the programme period. The budgetary impact in the table is the impact reported in the programme, i.e. by the national authorities. A positive sign implies that revenue / expenditure increases as a consequence of this measure.	

The total impact of revenue measures for the years 2020-2022 is approximately neutral compared to the NPC scenario presented in the Stability Programme. Legislative measures identified relate mainly to taxes, social contributions and transfers and compensate each other in the Stability Programme's horizon. In 2020, the most important consolidation measures relate to the eKasa project and gas additives (0.09% of DGP taken together). In 2021, the negative impact of the abolition of the bank levy, introduced in 2012 to ensure that the banking sector adequately contributes to financing the cost of solving financial crises, will impact the balance by 0.1% of GDP.

When comparing expenditure plans to the NPC scenario presented in the Stability Programme, the government expects to carry out expenditure-increasing measures in the areas of wages, social transfers in kind and investment. An additional increase of wages above the NPC scenario is expected in 2020 and 2021 by 10% and 2%, respectively. Higher intermediate consumption is projected e.g. due to additional expenditure for army modernisation. Furthermore, higher expenditure for social transfers in kind will be

compensated by growing revenues from health insurance premia. Higher investment and capital spending than in the NPC scenario are expected for the aforementioned army modernisation and other, yet unspecified, recovery measures. The decline below the NPC scenario is due to slower growth in capital transfers compared to the nominal GDP growth. While receipts from discretionary measures will rise by 0.2 percentage points between 2020 and 2022, expenditure will be increased by around 1 percentage point of GDP.

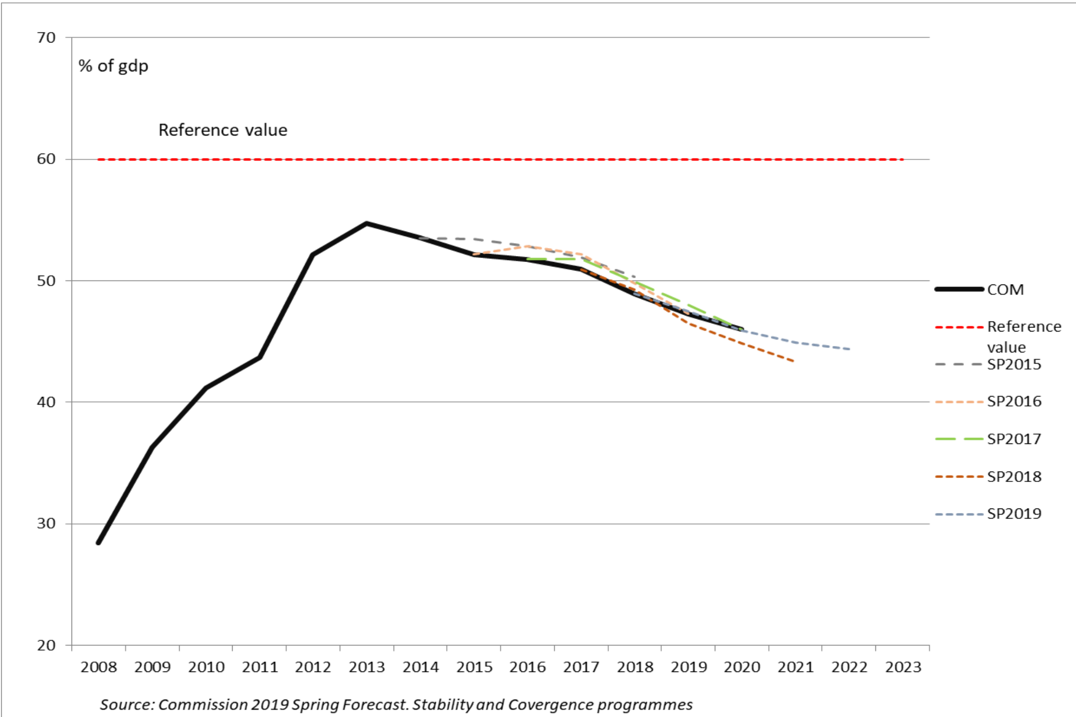
Measures that the Stability Programme describes in sufficient detail (i.e. the revenue-side measures) are also included in the Commission 2019 spring forecast.

No one-offs are planned in 2019 or the following years. The Commission 2019 spring forecast also does not assume any one-off measures.

3.4. DEBT DEVELOPMENTS

General government debt declined to 48.9% of GDP in 2018 (Table 3), driven mainly by favourable developments in the denominator of the ratio, in particular faster real GDP growth and accelerating inflation. A primary surplus also supported the decline in the debt burden in 2018, though by far less than the combined effect of nominal GDP growth. The 2018 debt outrun was below the projection presented in the 2018 Stability Programme but above the 2019 DBP projections (Figure 2). In 2019, the Stability Programme projects the debt-to-GDP ratio to decline to 47.5%, which is higher than projected in the DBP (47.3%). The reduction in the debt-to-GDP ratio will be primarily driven by real GDP growth, as well as by higher inflation and primary surplus. The slower debt decline in 2019 compared to previous years is due to a relatively large stock-flow adjustment.

Figure 3: Government debt projections in successive programmes (% of GDP)



These favourable debt developments are set to continue in 2020 (debt level of 45.9% of GDP) and beyond according to the Stability Programme, with real GDP growth remaining the principal driver of the decline in the debt ratio. While primary surpluses are projected to

play a stable part in Slovakia's debt reduction of close to 1% of GDP in the outer years, positive stock-flow adjustments are expected in 2021 and 2022. This is attributable to advances paid for the purchase of military equipment that will affect the balance at the point of delivery. In 2020, a one-time contribution to the ESM of 0.1% of GDP is included.

The Commission's 2019 spring forecast projects a similar downward trajectory in the general government debt compared to the Stability Programme in 2019 and 2020. The Commission projections are driven by smaller negative contributions from the primary balance than in the programme but also lower positive contributions from stock-flow adjustments.

The ratio of net debt to GDP is expected to decline over the whole forecast horizon from 43% of GDP in 2018 to around 37% of GDP in 2022 according to the 2018 Stability Programme. The reason for the faster decline in net debt relative to gross debt is due to an increase in financial assets from cash surpluses of individual general government units. Liquid financial assets of the public administration will rise from 6.0% in 2018 to 7.2% of GDP in 2022.

Table 3: Debt developments

(% of GDP)	Average 2013-2017	2018	2019		2020		2021	2022
			COM	SP	COM	SP	SP	SP
Gross debt ratio[1]	**52.6**	**48.9**	**47.3**	**47.5**	**46.0**	**45.9**	**44.9**	**44.4**
Change in the ratio	-0.2	-2.0	-1.7	-1.4	-1.3	-1.6	-1.0	-0.6
Contributions [2] :								
1. Primary balance	**0.5**	**-0.6**	**-0.8**	**-1.2**	**-0.6**	**-1.1**	**-1.0**	**-1.0**
2. "Snow-ball" effect	**0.1**	**-1.7**	**-1.7**	**-1.9**	**-1.4**	**-1.7**	**-1.4**	**-1.1**
Of which:								
Interest expenditure	1.7	1.3	1.3	1.2	1.2	1.1	1.0	1.0
Growth effect	-1.5	-2.0	-1.7	-1.8	-1.5	-1.7	-1.4	-1.1
Inflation effect	-0.1	-1.0	-1.2	-1.2	-1.1	-1.1	-1.0	-1.0
3. Stock-flow adjustment	**-0.8**	**0.3**	**0.8**	**1.7**	**0.8**	**1.2**	**1.5**	**1.6**
Of which:								
Cash/accruals diff.				1.2		1.0	0.7	0.1
Acc. financial assets				0.7		0.3	0.6	1.2
Privatisation				0.0		0.0	0.0	0.0
Val. effect & residual				-0.2		-0.1	0.2	0.3

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 :

Commission 2019 spring forecast (COM); Stability Programme (SP), Comission calculations.

3.5. RISK ASSESSMENT

Following the 2019 spring EDP notification, Eurostat expressed a reservation on the quality of the data reported by Slovakia in relation to the recording of certain expenditures incurred

by government in 2018, which could increase the deficit by 0.3% of GDP in 2018. Eurostat will investigate the issue in cooperation with the Slovak statistical authorities.[6]

A key risk surrounding the Stability Programme is its possible underestimation of public expenditure trends. In both 2019 and 2020, the Stability Programme projects considerably lower general government gross fixed capital formation compared to both 2018 and the Commission 2019 spring forecast. The ratio of government gross fixed capital formation to GDP expected in the Stability Programme is considerably lower than its long-term average and even lower than during the crisis and the weak post-crisis years (2008-2013). Already the 2018 Stability Programme had underestimated government investment in 2018 by more than 1 percentage point of GDP compared to the ex-post outcome. The discrepancy is closely linked to differences in the expected EU funds drawdown profile in the Commission forecast and the Stability Programme; however, part of it is compensated by higher current and capital revenue transfers projected in the spring forecast. The likelihood of the above expenditure risks in public investment materialising in part depends on the extent to which the EU funds are drawn as planned.

On 3 April 2019, the National Council of the Slovak Republic approved the cancellation of special taxation of retail chains that was expected to raise around 0.1 percentage point of GDP. As the Stability Programme does not factor in this decision, the achievement of compensating measures on the expenditure side that would allow for maintaining a balanced budget constitutes a risk factor for 2019.

In 2020, risks are again concentrated on the expenditure side. The Stability Programme presents only very limited details on the planned expenditure savings underlying its no-policy-change scenario, which is supplemented with additional measures with a negative impact on the government headline balance of 0.4% of GDP in both 2020 and 2021. Additional risks to the achievement of the targets outlined in the Stability Programme are ad hoc operations accounted for in the category of budgetary reserves. By contrast, the Commission 2019 spring forecast projects higher intermediate consumption and gross fixed capital formation, which in total accounts for higher expenditure equivalent to 1.8% of GDP. Nevertheless, the Commission 2019 spring forecast projects also commensurately higher revenues by 1.3% of GDP.

In early 2020, parliamentary elections will be held in Slovakia. In connection with this, measures with a negative fiscal impact were proposed by one of the coalition partners this spring. For instance, a reduction in the corporate income tax rate from 21% to 15% and the extension of a reduced VAT rate of 10% to most foodstuffs[7] will be discussed in the Parliament. Both proposals were assessed by Slovakia's independent fiscal council, which estimates the negative impact to be 0.8% for the former measure and 0.4% of GDP for the latter in 2020.[8]

The final fiscal outcome for 2020 will depend on whether the proposed tax cuts will be passed by the Parliament, probably in May or June 2019. If so, the compliance outlook for 2019 could drastically worsen.

[6] See ESTAT news release 67/2019 from 23 April 2019.

[7] The estimate of negative impact on public finances is based on the assumption that the VAT rate reduction will be reflected in food prices from 50%.

[8] https://www.rozpoctovarada.sk/vo_download/ko_2019_04_dppo_sadzba.pdf and https://www.rozpoctovarada.sk/vo_download/ko_2019_03_dphpotraviny.pdf

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

Box 1. Council Recommendations addressed to SLOVAKIA

On 13 July 2018, the Council addressed recommendations to Slovakia in the context of the European Semester. In particular, in the area of public finances the Council recommended to Slovakia to ensure that the nominal growth rate of net primary government expenditure does not exceed 4.1 % in 2019, corresponding to an annual structural adjustment of 0.5 % of GDP.

4.1. Compliance with the MTO or the required adjustment path towards the MTO

Slovakia is subject to the preventive arm of the SGP. Based on outturn data for 2018, the growth of nominal[9] primary government expenditure, net of discretionary revenue measures and one-offs, reached 6.2%, thereby exceeding the applicable expenditure benchmark and leading to a deviation of 1.2% of GDP in the underlying fiscal position. This points to a significant deviation in 2018 from the recommended adjustment path towards the MTO. When assessed over 2017 and 2018 together, the expenditure benchmark points to a deviation of 0.6% of GDP. The structural balance deteriorated by 0.3 percentage points of GDP in 2018, thus also pointing to a significant deviation in 2018 by close to 0.8% of GDP from the recommended structural adjustment of 0.4% of GDP towards MTO. When assessed together over 2017 and 2018, the structural balance points to a deviation of 0.2% of GDP. An overall assessment of the two pillars shows that in 2018 the structural balance was influenced by a higher point estimate for potential growth than reflected in the expenditure benchmark, and by differences in the underlying deflator. The expenditure benchmark appears to provide a more reliable picture of the underlying fiscal position, suggesting that a significant deviation from the preventive arm requirements occurred in 2018, as well as in 2017 and 2018 taken together. While the indicators used to assess compliance with the requirements of the preventive arm therefore point to a significant deviation from the adjustment path towards the medium-term budgetary objective in 2018, Slovakia was 0.8% of GDP away from its MTO of 0.5% of GDP in 2018 and is projected to move even closer to the MTO by 2020. In fact, by 2020, Slovakia’s structural balance is estimated to be 0.4% of GDP away from its revised MTO. The general government deficit was well below the Treaty reference value of 3% of GDP in 2018 and is projected to remain well below 3% of GDP over the forecast horizon. Moreover, Slovakia’s general government debt ratio is below 60% of GDP and further declining over the forecast horizon. Overall, the fiscal policy of Slovakia does not represent a clear and persistent challenge to the principles of the Stability and Growth Pact. Taking into account these considerations, there is currently no sufficient ground to conclude on the existence of an observed significant deviation in 2018.

In 2019, according to the information provided in the Stability Programme, the expenditure benchmark pillar points to compliance in that year alone but to a risk of significant deviation (0.4% of GDP) in 2018 and 2019 taken together. The (recalculated) structural balance also points to compliance in 2019 alone but to a significant deviation in 2018 and 2019 taken together. This supports the conclusion that Slovakia is facing a risk of a significant deviation from the SGP requirements in 2018 and 2019 together, based on the information provided in

[9] As part of the agreement on the EFC Opinion on *"Improving the predictability and transparency the SGP: a stronger focus on the expenditure benchmark in the preventive arm"*, which was adopted by the EFC on 29 November 2016, the expenditure benchmark, that is the maximum allowable growth rate of expenditure net of discretionary revenue measures, is expressed in nominal terms as from 2018.

the Stability Programme. The Commission 2019 forecast points to a risk of a some deviation from the expenditure benchmark in 2019 alone (0.3% of GDP). When looking at the two-year average for 2018 and 2019, a significant deviation of 0.7% of GDP is observed in the underlying fiscal position. The structural balance pillar mirrors these signals, pointing to a risk of some deviation in 2019 alone (0.4% of GDP) and a risk of significant deviation (0.6% of GDP) when 2018 and 2019 are taken together. An overall assessment shows only minor differences between signals from the two pillars. Both pillars therefore support the conclusion that, based on the Commission 2019 spring forecast, there is a risk of significant deviation in 2019 due to fiscal slippages that occurred in 2018 not being sufficiently compensated for in 2019.

Table 4: Compliance with the requirements under the preventive arm

(% of GDP)	2018	2019		2020	
Background budgetary indicators[1]					
Medium-term budgetary objective (MTO)	-0.5	-0.5		-1.0	
Structural balance[2] (COM)	-1.3	-1.3		-1.4	
Setting the required adjustment to the MTO					
Structural balance based on freezing (COM)	-0.8	-1.3		-	
Position vis-a -vis the MTO[3]	Not at MTO	Not at MTO		Not at MTO	
Required adjustment[4]	0.4	0.3		0.3	
Required adjustment corrected[5]	0.4	0.3		0.3	
Corresponding expenditure benchmark[6]	3.0	4.6		4.6	
Compliance with the required adjustment to the MTO					
	COM	**SP**	**COM**	**SP**	**COM**
Structural balance pillar					
Change in structural balance[7]	-0.3	0.5	0.0	0.0	-0.2
One-year deviation from the required adjustment[8]	-0.8	0.1	-0.4	-0.3	-0.4
Two-year average deviation from the required adjustment[8]	-0.2	-0.3	-0.6	-0.1	-0.4
Expenditure benchmark pillar					
Net public expenditure annual growth corrected for one-offs[9]	6.2	3.8	5.4	4.3	5.4
One-year deviation adjusted for one-offs[10]	-1.2	0.3	-0.3	0.1	-0.3
Two-year deviation adjusted for one-offs[10]	-0.6	-0.4	-0.7	0.2	-0.3
Finding of the overall assessment	**No sufficient ground***	**Significant deviation**		**Significant deviation**	

Legend

'Compliance' - the recommended structural adjustment or a higher adjustment is being observed.

'Some deviation' - a deviation from the recommended structural adjustment is being observed, but it is below the threshold for a significant deviation.

'Significant deviation' - a deviation which has reached or breached the threshold for a significant deviation (i.e. 0.5% of GDP over one year, 0.25% of GDP over two years on average).

*There is currently no sufficient ground to conclude on the existence of an observed significant deviation in Slovakia in 2018.

Notes

[1] The most favourable level of the structural balance, measured as a percentage of GDP reached at the end of year t-1, between spring forecast (t-1) and the latest forecast, determines whether there is a need to adjust towards the MTO or not in year t. A margin of 0.25 percentage points (p.p.) is allowed in order to be evaluated as having reached the MTO.

[2] Structural balance = cyclically-adjusted government balance excluding one-off measures.

[3] Based on the relevant structural balance at year t-1.

[4] Based on the position vis-à-vis the MTO, the cyclical position and the debt level (See European Commission: Vade mecum on the Stability and Growth Pact, page 38.). In case of a SDP, the requirement corresponds to the Council recommendation when available, otherwise it refers to the Commission recommendation to the Council.

[5] Required adjustment corrected for the clauses, the possible margin to the MTO and the allowed deviation in case of overachievers.

[6] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A corrected rate applies as long as the country is adjusting towards its MTO, including in year t.

[7] Change in the structural balance compared to year t-1, i.e. ex post assessment for 2018 is carried out on the basis of Commission 2019 spring forecast.

[8] The difference of the change in the structural balance and the corrected required adjustment.

[9] Net public expenditure annual growth (in %) corrected for discretionary revenue measures, revenue measures mandated by law and one-offs (nominal)

[10] Deviation of the growth rate of public expenditure net of discretionary revenue measures, revenue increases mandated by law and one-offs from the applicable reference rate in terms of the effect on the structural balance. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.

Source *:*
Stability Programme (SP); Commission 2019 spring forecast (COM); Commission calculations.

In 2020, according to the information provided in the Stability Programme, the expenditure benchmark pillar points to compliance in both 2020 alone and 2019 and 2020 taken together. The recalculated structural balance, however, shows a risk of some deviation from the required structural adjustment in 2020 alone and the two-year average for 2019 and 2020. The Commission 2019 spring forecast shows that in 2020, the expenditure benchmark is expected to exceed the applicable expenditure benchmark of 5.4% in 2020, leading to a deviation of 0.3% of GDP in the underlying fiscal position, thus pointing to a risk of some deviation in 2020, but given the considerable deviation in the preceding year there is a risk of a significant deviation when considering the two-year average for 2019 and 2020. The structural balance figure confirms the risk of some deviation (0.4% of GDP) from the requirement in 2020 alone and the risk of significant deviation (0.4% of GDP) based on the two-year average. An overall assessment shows that revenue shortfalls affect the structural balance but are partly offset by a higher point estimate for potential growth. In summary, both pillars support the conclusion of a risk of significant deviation occurring in 2019 and 2020 taken together, which again results from fiscal slippages in 2019 persisting into 2020 instead of being sufficiently compensated for in 2020.

Based on the outturn data and the Commission 2019 spring forecast, the ex-post assessment suggests a significant deviation from the adjustment path towards the MTO in 2018.

Following an overall assessment, a significant deviation from the adjustment path towards the MTO is currently expected in year 2019 and 202,0 putting at risk the compliance with the requirements of the preventive arm of the Pact.

5. DEBT SUSTAINABILITY ANALYSIS AND FISCAL RISKS

Slovakia does not appear to face fiscal sustainability risks in the short run.[10]

Based on Commission 2019 spring forecasts and a no-fiscal policy change scenario beyond the forecast horizon, government debt, projected at 47.3% of GDP in 2019, is expected to decrease to 40.1% in 2029, thus remaining below the 60% of GDP Treaty threshold. Over this horizon, government debt is projected to decline steadily from its 2019 peak level of 47.3% of GDP. Sensitivity analysis shows balanced risks.[11] Overall, this highlights low risks for the country from debt sustainability analysis in the medium term. The full implementation of the Stability Programme would put debt on a clearly decreasing path by 2029, remaining below the 60% reference value of GDP in 2029.

The medium-term fiscal sustainability risk indicator S1[12] is at -1.9 percentage points of GDP, primarily related to the low level of government debt and the initial budgetary position, which contribute to the final score in broadly equal amounts. This indicator thus signals low risks in the medium term. The full implementation of the Stability Programme would put the sustainability risk indicator S1 at -3.3 percentage points of GDP. Based on the debt sustainability analysis and the S1 indicator, overall medium-term fiscal sustainability risks are, therefore, low. Fully implementing the fiscal plans in the Stability Programme would decrease those risks.

[10] This conclusion is based on the short-term fiscal sustainability risk indicator S0. See the note to Table 5 for a definition of the indicator.
[11] Sensitivity analysis includes several deterministic debt projections, as well as stochastic projections (see Fiscal Sustainability Report 2018 for more details).
[12] See the note to Table 5 for a definition of the indicator.

The long-term fiscal sustainability risk indicator S2 is at 3.2% of GDP. In the long term, Slovakia therefore appears to face medium fiscal sustainability risks, primarily related to the projected ageing costs, which contribute 2.4 percentage points of GDP. Full implementation of the programme would nonetheless put the S2 indicator at 2.5 percentage points of GDP, leading to a lower long-term risk.[13] The debt sustainability analysis discussed above points to low risks. Overall, therefore, long-term fiscal sustainability risks are assessed as medium for Slovakia.

[13] The projected costs of ageing that are used to compute the debt projections and the fiscal sustainability indicators S1 and S2 are based on the projections of the 2018 Ageing Report. The impact of the recent pension reform is thus not yet reflected in these indicators.

Table 5: Debt sustainability analysis and sustainability indicators

Time horizon			Commission Scenario		Stability / Convergence Programme Scenario	
Short-term			**LOW risk**			
S0 indicator [1]			0.3			
Fiscal subindex			0.0	LOW risk		
Financial & competitiveness subindex			0.4	LOW risk		
Medium-term			**LOW risk**			
DSA [2]			LOW risk			
S1 indicator [3]			-1.9	LOW risk	-3.3	LOW risk
of which	Initial Budgetary Position		-0.8		-2.0	
	Debt Requirement		-1.1		-1.5	
	Cost of Ageing		0.1		0.2	
	of which	Pensions	-0.5		-0.3	
		Health care	0.3		0.3	
		Long-term care	0.1		0.1	
		Other	0.1		0.1	
Long-term			**MEDIUM risk**			
DSA [2]			LOW risk			
S2 indicator [4]			3.2	MEDIUM risk	2.5	MEDIUM risk
of which	Initial Budgetary Position		0.8		-0.1	
	Cost of Ageing		2.4		2.6	
	of which	Pensions	0.9		1.2	
		Health care	0.9		0.9	
		Long-term care	0.4		0.4	
		Other	0.1		0.1	

Source: Commission services; 2019 stability/convergence programme.

Note: the 'Commission' scenario depicts the sustainability gap under the assumption that the structural primary balance position evolves according to the Commissions' spring 2019 forecast until 2020. The 'stability/convergence programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented over the period covered by the programme. Age-related expenditure as given in the 2018 Ageing Report.

[1] The S0 indicator of short term fiscal challenges informs the early detection of fiscal stress associated to fiscal risks within a one-year horizon. To estimate these risks S0 uses a set of fiscal, financial and competitiveness indicators selected and weighted according to their signalling power. S0 is therefore a composite indicator whose methodology is fundamentally different from the S1 and S2 indicators, which quantify fiscal adjustment efforts. The critical threshold for the overall S0 indicator is 0.46. For the fiscal and the financial-competitiveness sub-indexes, thresholds are respectively at 0.36 and 0.49*.

[2] Debt Sustainability Analysis (DSA) is performed around the no fiscal policy change scenario in a manner that tests the response of this scenario to different shocks presented as sensitivity tests and stochastic projections*.

[3] The S1 indicator is a medium-term sustainability gap; it measures the upfront fiscal adjustment effort required to bring the debt-to-GDP ratio to 60 % by 2033. This adjustment effort corresponds to a cumulated improvement in the structural primary balance over the 5 years following the forecast horizon (i.e. from 2021 for Commission scenario and from last available year for the SCP scenario); it must be then sustained, including financing for any additional expenditure until the target date, arising from an ageing population. The critical thresholds for S1 are 0 and 2.5, between which S1 indicates medium risk. If S1 is below 0 or above 2.5, it indicates low or high risk, respectively*.

[4] The S2 indicator is a long-term sustainability gap; it shows the upfront and permanent fiscal adjustment required to stabilise the debt-to-GDP ratio over the infinite horizon, including the costs of ageing. The critical thresholds for S2 are 2 and 6, between which S2 indicates medium risk. If S2 is below 2 or above 6, it indicates low or high risk, respectively*.

* For more information see Fiscal Sustainability Report 2018.

However, the introduction of a retirement age cap, which was approved by a Constitutional Act at the end of March 2019, will have a substantially negative impact on the sustainability of the pension system in the long run. Growth in the statutory retirement age will be capped at 64 years and the ceiling for women will depend on the number of children. The Stability Programme estimates that pension expenditure will increase by about 2.9% GDP between 2016 and 2070. The retirement age ceiling of 64 years should be reached after 2028, in contrast to a further increasing retirement age under the previous rules.

6. FISCAL FRAMEWORK

Two main national fiscal rules exist in Slovakia; a balanced budget rule and a debt brake. The rules' assessment is under the authority of the Ministry of Finance and the Council for Budget Responsibility (CBR) evaluates compliance with the rule. The balanced budget rule is enshrined in national legislation related to the Fiscal Compact.[14] It requires the government to achieve a balanced budget or surplus in the general government sector. A balanced budget is defined as a structural deficit equal or lower than 0.5% of GDP, which is the same as the MTO currently presented in the Stability Programme. However, as Slovakia's government debt-to-GDP ratio is significantly lower than 60%, national legislation allows for a structural deficit of up to 1% of GDP, which is in line with the MTO for year 2020 and onwards. The structural balance overachieved the abovementioned requirement for a balanced budget by 0.3 percentage points in 2018. In years 2019-2022, the requirements of the rule will be met according to the data presented in the current Stability Programme.

A constitutional debt brake was introduced in Slovakia in 2012, which foresees corrective measures once certain debt thresholds are exceeded. Its upper limit was set at the level of 50% of GDP.[15] As of 2018, the thresholds are lowered by 1 percentage point per year until the lower bound reaches 40% of GDP.[16] In 2018, general government debt reached 48.9% of GDP, and thus is below the debt brake's threshold. The CBR published its regular annual report on the evaluation of fiscal responsibility rules in August 2018.[17]

The Constitutional Act also includes the obligation to introduce binding limits on public expenditure, while the procedure for their determination is to be laid down by another law. However, it is not specified by which deadline legislation should be approved. According to information provided in the Stability Programme, the Ministry of Finance will prepare options for setting spending limits by the end of the current parliamentary term.

Based on the information provided in the Stability Programme, the planned and forecast performance in Slovakia appears to broadly comply with the requirements of the applicable national numerical fiscal rules for general government. Nevertheless, the balanced budget rule will not be met during 2019-2020 according to the Commission 2019 spring forecast (see section 3.5 for risks description).

Slovakia considers the Stability Programme to be the national medium-term fiscal plan (NMTFP) pursuant to Art. 4(1) of the Two-Pack Regulation 473/2013. Member States were required to include in their NMTFP (or national reform programmes) indications on the expected economic returns on non-defence public investment projects that have a significant budgetary impact. Such an assessment is, however, neither part of the Stability Programme, nor of the National Reform Plan. Nevertheless, at the end of 2018, the cabinet approved an amendment of the Act on Budgetary Rules of Public Administration, according to which the Ministry of Finance is obliged to assess all investments over 40 million euros (10 million euros for IT-related cases) of all units fully and partly paid from the state budget and selected enterprises, while the law also requires the cooperation of other state budget

[14] The requirements of the Fiscal Compact are enshrined in the national legislation (Act on Budgetary Rules of Public Administration, § 30a).
15 Upper limit was increased temporarily by 10 percentage points (60% of GDP) until 2017. During 2018-2027, it will be decreased by 1.0 percentage point per year.
16 Lower limit was increased temporarily for 10 percentage points (50% of GDP) until 2017. During 2018-2027, it will be decreased for 1.0 percentage point per year.
[17] https://www.rozpoctovarada.sk/svk/rozpocet/385/sprava-o-hodnoteni-plnenia-pravidiel-rozp-zodp-a-transp-082018

chapters. The government will have to prepare and publish feasibility studies for their investments and concessions. The assessment of feasibility studies will be done and released by the Ministry of Finance.

The macroeconomic forecast underlying the Stability Programme was published by the Institute for Financial Policy (IFP) of the Ministry of Finance on 4 February 2019 and was endorsed as realistic by the Macroeconomic Forecasting Committee at its meeting of 30 January 2019.[18] The Macroeconomic Forecasting Committee[19] was established by the Constitutional Act on Fiscal Responsibility as an advisory body to the Mister of Finance. According to the Committee's statutes, it is independent from the government's influence in its deliberations.

7. SUMMARY

In 2018, Slovakia did not achieve the MTO. A deterioration of the structural balance of -0.3 percentage points of GDP was recorded, which points to a significant deviation of 0.8% of GDP from the required adjustment. The growth rate of government expenditure, net of discretionary revenue measures, exceeded the applicable expenditure benchmark rate by 1.2% of GDP. After taking into account the factors explaining the difference between the two indicators, both pillars point to a significant deviation from the recommended adjustment path towards the MTO. However, taking into account further considerations, regarding in particular the distance to the MTO, the headline deficit and debt reduction, there is currently no sufficient ground to conclude on the existence of an observed significant deviation in 2018.

According to the Stability Programme, Slovakia plans a growth rate of government expenditure, net of discretionary revenue measures, which is in line with the applicable expenditure benchmark rate in both 2019 and 2020. On this basis Slovakia also plans an improvement of the structural balance of 0.5% of GDP in 2019, when it plans to be close to the MTO. The Programme is based on unspecified consolidation measures, posing risks to meeting the headline targets. By contrast, based on the Commission 2019 spring forecast, the headline deficit is expected to fall to 0.5% of GDP in 2019 but increase again to 0.6% of GDP in 2020. This path implies significant deviations from the required adjustment path towards the MTO according to both pillars in both 2019 and 2020 when looking at the respective two-year averages. The lack of consolidation effort in 2018 is expected not to be compensated sufficiently in years 2019 and 2020.

[18] https://www.finance.gov.sk/sk/financie/institut-financnej-politiky/ekonomicke-prognozy/makroekonomicke-prognozy/47-zasadnutie-vyboru-makroekonomicke-prognozy-februar-2019.html

[19] The Macroeconomic Forecasting Committee consists of a chairman (a director of the IFP) and members from nine independent institutions entitled to vote on a macroeconomic forecast nature – "conservative", "realistic" or "optimistic" (the Central Bank, the Academy of Science, the Institute of Informatics and Statistics and six commercial banks). Other three members are with an observer's status without voting rights (the Council for Budgetary Responsibility, the Statistical Office of the Slovak Republic and one commercial bank). The draft forecast is approved by the Committee if the majority of voting members assess the forecast as "conservative" or "realistic".

8. ANNEXES

Table I. Macroeconomic indicators

	2001-2005	2006-2010	2011-2015	2016	2017	2018	2019	2020
Core indicators								
GDP growth rate	5.1	4.9	2.6	3.1	3.2	4.1	3.8	3.4
Output gap [1]	-2.4	2.2	-2.3	-0.3	0.4	1.5	2.1	2.3
HICP (annual % change)	5.9	2.3	1.8	-0.5	1.4	2.5	2.4	2.3
Domestic demand (annual % change) [2]	5.3	3.3	1.4	1.2	2.6	4.2	2.9	2.8
Unemployment rate (% of labour force) [3]	18.2	12.2	13.3	9.7	8.1	6.5	5.9	5.6
Gross fixed capital formation (% of GDP)	27.4	24.7	22.2	21.3	21.4	22.0	21.6	21.4
Gross national saving (% of GDP)	21.8	20.5	21.7	21.8	22.3	22.9	23.0	23.1
General Government (% of GDP)								
Net lending (+) or net borrowing (-)	-4.5	-4.7	-3.3	-2.2	-0.8	-0.7	-0.5	-0.6
Gross debt	41.5	33.4	51.3	51.8	50.9	48.9	47.3	46.0
Net financial assets	-5.6	-18.7	-33.4	-36.2	-35.5	n.a	n.a	n.a
Total revenue	36.9	35.0	38.7	39.2	39.4	39.9	39.9	39.7
Total expenditure	41.4	39.7	42.0	41.5	40.2	40.6	40.4	40.2
of which: Interest	2.7	1.4	1.8	1.6	1.4	1.3	1.3	1.2
Corporations (% of GDP)								
Net lending (+) or net borrowing (-)	-2.3	0.6	4.2	0.2	-0.4	-0.7	0.1	0.9
Net financial assets; non-financial corporations	-62.1	-60.5	-64.0	-58.2	-58.8	n.a	n.a	n.a
Net financial assets; financial corporations	-2.6	-1.3	3.0	-1.2	-4.8	n.a	n.a	n.a
Gross capital formation	19.5	17.2	14.0	15.2	14.7	15.5	15.1	14.9
Gross operating surplus	25.4	26.9	26.2	24.8	24.1	24.5	25.1	25.7
Households and NPISH (% of GDP)								
Net lending (+) or net borrowing (-)	-1.0	-0.8	-0.3	0.7	0.3	0.1	-0.4	-0.7
Net financial assets	38.4	33.7	37.9	41.1	39.7	n.a	n.a	n.a
Gross wages and salaries	30.7	30.3	30.4	31.7	32.7	33.0	33.1	33.3
Net property income	2.6	1.2	0.7	0.6	0.5	0.4	0.4	0.4
Current transfers received	16.8	17.1	18.5	19.5	19.3	19.2	18.8	18.1
Gross saving	4.6	4.2	4.1	5.2	4.9	5.0	4.5	4.2
Rest of the world (% of GDP)								
Net lending (+) or net borrowing (-)	-7.7	-4.9	0.6	-1.4	-0.8	-1.6	-1.0	-0.6
Net financial assets	31.8	46.8	56.5	54.4	59.3	n.a	n.a	n.a
Net exports of goods and services	-4.9	-2.2	2.4	3.0	3.1	2.2	2.8	3.2
Net primary income from the rest of the world	-2.4	-2.1	-2.1	-1.9	-2.0	-2.0	-2.1	-2.1
Net capital transactions	-0.5	0.8	1.5	-0.2	-0.6	-0.5	-0.5	-0.5
Tradable sector	53.5	51.9	50.6	49.2	49.2	48.6	n.a	n.a
Non tradable sector	36.4	38.5	40.1	41.2	40.9	41.3	n.a	n.a
of which: Building and construction sector	5.9	7.9	7.6	7.1	7.4	7.8	n.a	n.a
Real effective exchange rate (index, 2000=100)	69.2	93.4	98.9	98.6	101.9	103.6	104.4	105.8
Terms of trade goods and services (index, 2000=100)	106.5	102.1	97.4	96.5	95.9	95.4	95.2	95.0
Market performance of exports (index, 2000=100)	74.8	99.1	116.5	120.8	120.9	122.0	125.1	127.4

Notes:

[1] The output gap constitutes the gap between the actual and potential gross domestic product at 2010 market prices.

[2] The indicator on domestic demand includes stocks.

[3] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.

Source :
AMECO data, Commission 2019 spring forecast

Mandatory variables not included in the Stability Programme

The following mandatory variables are missing in the submitted Stability Programme: changes in inventories and net acquisition of valuables (% of GDP) in Table 1a

Macroeconomic Prospects; total revenues and expenditures in 2007 and 2010 and age-related expenditures of them in Table 7 Long-term sustainability; estimate for public guarantees for 2019 in Table 7a Contingent liabilities; assumptions on GDP growth for world excluding EU, world import volumes, excluding EU and nominal effective exchange rate in Table 8 Basic assumptions. Not included mandatory variables do not impede the Commission's ability to assess the Stability Programme on the basis of the Programme's assumptions.