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Assessment of the 2020 Stability Programme for

Slovakia

(Note prepared by DG ECFIN staff)

CONTENTS

EXECUTIVE SUMMARY 3

1. INTRODUCTION 4

2. MACROECONOMIC DEVELOPMENTS 4

3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS 6

3.1. DEFICIT DEVELOPMENTS AND MEDIUM-TERM STRATEGY AND TARGETS 6

3.2. MEASURES UNDERPINNING THE PROGRAMME 8

3.3. DEBT DEVELOPMENTS 10

3.4. RISK ASSESSMENT 12

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT 12

4.1. COMPLIANCE WITH THE DEFICIT CRITERION 12

4.2. COMPLIANCE WITH THE MTO 12

EXECUTIVE SUMMARY

- On 6 April 2020, the Commission provided guidelines to Economic and Financial Committee on how the format and content of the 2020 Stability and Convergence Programmes can be streamlined in light of the exceptional circumstances related to the Covid-19 pandemic. This assessment takes into account the severe constraints that Member States faced in providing the information usually required in their Programmes. The assessment focuses on the near term in light of the high uncertainty attached to the projections.
- The 2020 Stability Programme projects GDP to fall by 7.2% in 2020 and a subsequent recovery with growth of 6.8% in 2021. This compares to a contraction by 6.7% in 2020, followed by a recovery of 6.6% in 2021 projected in the Commission 2020 spring forecast.
- The Stability Programme expects deficits of 8.4% and 4.9% of GDP in 2020 and 2021. Allowing for differences in the underlying macroeconomic scenarios and assumptions, the economic and budgetary projections in the Stability Programme are broadly in line with the Commission's spring 2020 forecast with the deficit expected to be at 8.5% of GDP in 2020 and 4.2% of GDP in 2021.
- The Stability Programme suggests that the cumulative impact of the deficit increasing measures taken in response to the COVID-19 outbreak amounts to 2.6% of GDP. These measures include wage compensation for employees, subsidies for the self-employed, sickness and nursing schemes and purchases of medical goods linked to the COVID-19 pandemic. In addition, Slovakia has announced measures that, while not having a direct budgetary impact, will contribute to support liquidity to businesses. They include tax and social security contributions deferrals (1.4% of GDP) and loan guarantees (1.6% of GDP). There are differences in the quantification of measures between the Stability Programme and the Commission forecast, stemming mainly from different forecast cut-off dates and assumptions regarding the measures and their impact.
- The macroeconomic and fiscal outlook are affected by high uncertainty due to the outbreak of the COVID-19 pandemic.

1. INTRODUCTION

This document assesses the economic and budgetary projections contained in the Stability Programme[1] covering the period 2020-2023, which was submitted on 18 May 2020[2]. The note also assesses Slovakia´s compliance with the preventive arm of the Stability and Growth Pact (SGP) in 2019. The government approved the Programme on 18 May 2020 and it was submitted to the Parliament subsequently.

Slovakia is currently subject to the preventive arm of the Stability and Growth Pact.

On 20 March 2020, the Commission adopted a Communication on the activation of the general escape clause of the Stability and Growth Pact. The clause, as set out in Articles 5(1), 6(3), 9(1) and 10(3) of Regulation (EC) 1466/97 and Articles 3(5) and 5(2) of Regulation (EC) 1467/97, facilitates the coordination of budgetary policies in times of severe economic downturn. In its Communication, the Commission shared with the Council its view that, given the expected severe economic downturn resulting from the COVID-19 outbreak, the current conditions permit the activation of the clause. On 23 March 2020, the Ministers of Finance of the Member States agreed with the assessment of the Commission. The activation of the general escape clause allows for a temporary departure from the adjustment path towards the medium-term budgetary objective, provided that this does not endanger fiscal sustainability in the medium term. For the corrective arm, the Council may also decide, on a recommendation from the Commission, to adopt a revised fiscal trajectory. 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.

2. MACROECONOMIC DEVELOPMENTS

After growing at a rate of 2.3% in 2019, in 2020, the economy is expected to be strongly hit by the COVID-19 pandemic as the government adopted stringent measures including closing borders, social distancing, and closing most retail stores and all schools. The macroeconomic scenario underpinning the Programme is based on the assumption that the lockdown will last about two months and the rebound will be gradual. Some sectors will be limited in activity for longer (e.g. culture, art, some parts of trade). Against this background, the Programme projects the real GDP to fall by 7.2% in 2020 and a subsequent recovery with growth of 6.8% in 2021, primarily driven by private consumption and fixed investment. The unemployment rate is projected to rise to 8.8% in 2020 and to decline to 7.7% in 2021. Inflation is expected to moderate to 1.7% in 2020 and to 0.2% in 2021. In addition to this central scenario, the Programme also presents two alternative scenarios. The first alternative scenario

[1] The Stability Programme submitted by Slovakia states that it also constitutes the national medium-term fiscal plan required under Article 4(1) of Regulation (EU) 473/2013.

[2] The Stability Programme contains only short-term budgetary projections, in line with the guidelines for a streamlined format of the 2020 Stability and Convergence Programmes in light of the COVID-19 outbreak, provided by the Commission services on 6 April 2020.

assumes a longer quarantine with a deeper economic downturn in the second quarter while the second alternative scenario assumes a slower recovery.

In the Commission 2020 spring forecast (hereafter Commission forecast), Slovakia's real GDP is set to contract sharply by a comparable 6.7% in 2020, and to recover swiftly as containment measures are lifted and grow by 6.6% in 2021. Private consumption is expected to drop sharply in 2020. It is expected to recover in 2021, but not to fully return to its previous trajectory, as employment and wage growth are also impacted. The uncertainty, liquidity constraints and restrictions to business activity are projected to weigh even more heavily on investment growth in 2020. Trade is also projected to decrease sharply in 2020, but to offset most of the losses in 2021. Employment is projected to fall by over 3% in 2020, but should partially recover in 2021. Consumer price inflation is projected to moderate substantially due to lower energy prices and less price pressures from demand, from 2.8% in 2019 to 1.9% in 2020 and to 1.1% in 2021.

Table 1: Comparison of macroeconomic developments and forecasts

	2019		2020		2021		2022	2023
	COM	SP	COM	SP	COM	SP	SP	SP
Real GDP (% change)	2.3	2.3	-6.7	-7.2	6.6	6.8	4.1	3.2
Private consumption (% change)	2.2	2.2	-7.1	-8.4	7.2	7.8	4.1	2.9
Gross fixed capital formation (% change)	4.4	4.4	-14.7	-20.3	10.7	17.0	5.2	5.8
Exports of goods and services (% change)	1.7	1.7	-12.4	-21.4	13.4	17.6	6.5	3.6
Imports of goods and services (% change)	2.6	2.6	-12.6	-25.5	13.3	19.0	6.5	4.0
Contributions to real GDP growth:								
- Final domestic demand	2.9	2.8	-6.3	-8.7	6.4	7.5	3.7	3.2
- Change in inventories	0.2	0.2	-0.5	-1.8	0.0	-0.7	0.1	0.0
- Net exports	-0.8	-0.7	0.1	3.3	0.3	0.0	0.3	-0.1
Output gap[1]	2.7	2.5	-5.0	-5.5	-0.6	-1.2	0.8	1.9
Employment (% change)	1.2	1.2	-3.4	-3.6	2.0	1.6	1.0	0.3
Unemployment rate (%)	5.8	5.8	8.8	8.8	7.1	7.7	6.8	6.4
Labour productivity (% change)	1.0	1.0	-3.4	-3.8	4.6	5.1	3.0	2.9
HICP inflation (%)	2.8	2.8	1.9	1.7	1.1	0.2	1.9	2.0
GDP deflator (% change)	2.6	2.6	2.2	1.9	1.3	0.2	1.4	2.1
Comp. of employees (per head, % change)	6.2	n.a.	1.3	n.a.	2.5	n.a.	n.a.	n.a.
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	-2.3	n.a.	-2.6	n.a.	n.a.	n.a.	n.a.	n.a.

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 2020 spring forecast (COM); Stability Programme (SP).

Overall, the Programme and the Commission's growth projections including projections of growth components, are broadly similar. The only sizeable difference in

the components relates to the trade profile, where the Programme expects significantly sharper decreases for both exports and imports in 2020 and subsequent recovery rates in 2021.

The macroeconomic forecast underpinning the medium-term fiscal plan and the tax forecast underlying the Programme were prepared by the Institute for Financial Policy of the Ministry of Finance and endorsed by the Macroeconomic Forecasting Committee on 8 April 2020 (where all ten present members assessed the macroeconomic scenario as realistic or conservative) and the Tax Revenue Forecasts Committee on 16 April 2020 (where all seven present members assessed the tax forecast as realistic), respectively.[3] [4]

3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS

3.1. DEFICIT DEVELOPMENTS AND MEDIUM-TERM STRATEGY AND TARGETS[5]

The government headline deficit was 1.3% of GDP in 2019. The deficit was 1.2 percentage points higher than the Draft Budgetary Plan due to weaker-than-expected household consumption and labour market developments but also due to newly adopted measures (the introduction of a lower VAT rate on some food items, an increase of tax allowances and the introduction of minimum pensions and capping the retirement age). Some measures strengthening the revenue side such as levies on retail chains were cancelled or delayed (eKasa[6] and nanomarkers[7]). On the revenue side, receipts from value added tax improved thanks to the better tax collection and growing effective tax rate. Also the effective tax rate of the corporate income tax improved. Still, on the back of higher-than-projected transfers from the EU Funds, the share of general government revenue on GDP increased by 0.7 percentage points to 39.1% of GDP. Total expenditure level exceeded the projected levels (by 1.8% of GDP) and reached 40.3% of GDP, due to higher wages, social transfers and mainly investments. In 2019, it was affected also by higher-than-expected carryovers from previous years, mainly in the central government whose deficit outcome was worse by 0.9 percentage points compared to the approved budget.

The Programme expects general government revenue of 41.4% of GDP and expenditure of 49.8%, resulting in a deficit of 8.4% of GDP in 2020. The Commission forecast expects broadly similar total revenue (41.3% of GDP) and expenditure (49.8% of GDP) ratios as the Programme. The main differences are due to worse developments in the labour market assumed in the Commission forecast reflected in lower income taxes, social contributions and sales. In contrast, the Commission forecast expects higher revenue from value added tax and from the EU funds

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[3] https://www.mfsr.sk/sk/financie/institut-financnej-politiky/ekonomicke-prognozy/makroekonomicke-prognozy/51-zasadnutie-vyboru-makroekonomicke-prognozy-april-2020.html

[4] https://www.mfsr.sk/sk/financie/institut-financnej-politiky/ekonomicke-prognozy/danove-prognozy/57-zasadnutie-vyboru-danove-prognozy-april-2020.html

[5] In light of the activation of the general escape clause, the measures taken in response to the coronavirus outbreak in 2020 are not treated as one-off and are thus not excluded from the estimation of the structural budget balance.

[6] The project directly connecting all online electronic cash registers to the financial administration.

[7] Additives to the diesel and petrol with aim to reduce tax evasion.

compared to the Programme. On the expenditure side, the Commission forecast projects slightly lower compensation of employees, intermediate consumption and capital transfers. While the Programme classifies some COVID-19 measures as social transfers, the Commission classifies them as subsidies. The Commission forecast expects also higher investment, which can be explained by higher expected financing from the EU funds.

Table 2: General government budgetary position

(% of GDP)	2019	2020		2021		2022	2023	Change: 2019-2023
	COM	COM	SP	COM	SP	SP	SP	SP
Revenue	**41.5**	**41.3**	**41.4**	**40.9**	**n.a.**	**n.a.**	**n.a.**	**n.a.**
of which:								
- Taxes on production and imports	12.1	12.2	12.0	12.1	n.a.	n.a.	n.a.	**n.a.**
- Current taxes on income, wealth, etc.	7.3	6.2	6.6	6.7	n.a.	n.a.	n.a.	**n.a.**
- Social contributions	15.2	15.3	16.1	14.8	n.a.	n.a.	n.a.	**n.a.**
- Other (residual)	6.9	7.7	6.7	7.4	n.a.	n.a.	n.a.	**n.a.**
Expenditure	**42.8**	**49.8**	**49.8**	**45.1**	**n.a.**	**n.a.**	**n.a.**	**n.a.**
of which:								
- Primary expenditure	41.6	48.5	48.6	43.8	n.a.	n.a.	n.a.	**n.a.**
of which:								
Compensation of employees+Intermediate consumption	15.8	17.3	17.7	16.6	n.a.	n.a.	n.a.	**n.a.**
Compensation of employees	10.2	11.2	11.3	10.8	n.a.	n.a.	n.a.	**n.a.**
Intermediate consumption	5.6	6.1	6.4	5.8	n.a.	n.a.	n.a.	**n.a.**
Social payments	18.5	22.1	23.4	19.3	n.a.	n.a.	n.a.	**n.a.**
Subsidies	1.1	2.3	1.2	1.3	n.a.	n.a.	n.a.	**n.a.**
Gross fixed capital formation	3.6	3.7	3.2	3.6	n.a.	n.a.	n.a.	**n.a.**
Other (residual)	2.6	3.2	3.0	3.0	n.a.	n.a.	n.a.	**n.a.**
- Interest expenditure	1.2	1.3	1.2	1.3	n.a.	n.a.	n.a.	**n.a.**
General government balance (GGB)	**-1.3**	**-8.5**	**-8.4**	**-4.2**	**-4.9**	**-3.7**	**-2.9**	**-1.6**
Primary balance	**-0.1**	**-7.1**	**-7.2**	**-2.9**	**n.a.**	**n.a.**	**n.a.**	**n.a.**
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	**-1.3**	**-8.5**	**-8.4**	**-4.2**	**-4.9**	**-3.7**	**-2.9**	**-1.6**
Output gap[1]	2.7	-5.0	-5.5	-0.6	-1.2	0.8	1.9	**-0.6**
Cyclically-adjusted balance[1]	-2.3	-6.6	-6.2	-4.0	-4.4	-4.0	-3.6	**-1.3**
Structural balance[2]	**-2.3**	**-6.6**	**-6.2**	**-4.0**	**-4.4**	**-4.0**	**-3.6**	**-1.3**
Structural primary balance[2]	-1.1	-5.2	-5.0	-2.7	n.a.	n.a.	n.a.	**n.a.**
Gross debt ratio	**48.0**	**59.5**	**61.2**	**59.9**	**61.9**	**61.4**	**60.1**	**12.1**

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 programme scenario using the commonly agreed methodology.

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

Source :

Stability Programme (SP); Commission 2020 spring forecasts (COM); Commission calculations.

The cumulative impact of the direct measures taken in response to the COVID-19 outbreak reported in the Programme amount to 2.6% of GDP. Expenditure measures include additional spending on medical goods of 0.2% of GDP. In the Commission forecast, the impact of measures taken in response to the COVID-19 outbreak is 2.2% of GDP on the expenditure side and of 1.3% of GDP on the revenue side. The difference in the projected impact of revenue measures is due to the fact that the

Programme does not consider them to be direct effects of measures, but as a consequence macroeconomic developments.[8]

After addressing the COVID-19 pandemic economic consequences, the main aim of the Programme´s medium-term budgetary strategy is to bring the deficit below the 3% headline deficit threshold by 2023. The fiscal targets set in the Programme are deficits of 4.9% of GDP in 2021, 3.7% of GDP in 2022 and 2.9% of GDP in 2023. The envisaged consolidation strategy is not sufficiently supported by measures and relies on unspecified measures[9] (see sections 3.3 and 3.4). It will be necessary to specify other discretionary measures of 0.9% of GDP in 2021, 2.4% of GDP in 2022 and 3.2% of GDP in 2023 according to the Programme.

In 2021, the Commission forecast projects, under a no-policy-change assumption, the general government deficit to fall to 4.2% of GDP. A direct comparison of underlying assumptions is not possible, as the breakdown of the adjustment by revenue/expenditure components and its main drivers was not submitted. The Programme does not classify the COVID-19 measures as one-offs. It also does not present any other measures as one-offs.

3.2. MEASURES UNDERPINNING THE PROGRAMME

Measures adopted in response to the COVID-19 outbreak consist of direct aid, deferrals of tax and social contributions and bank guarantees for business loans. The government has adopted budgetary measures to increase the capacity of its health system, contain the pandemic, and provide relief to those citizens and sectors that have been particularly impacted. According to the Programme, these budgetary measures with direct impact amount to 2.6% of GDP[10]. These measures include, amongst others, wage compensation for employees, subsidies to self-employed persons, sickness and nursing schemes and purchases of medical goods linked to the COVID-19 pandemic (for more details see table 3). In addition, Slovakia has announced measures that, while not having a direct budgetary impact, will contribute to support liquidity to businesses, which the Programme estimates at 1.4% of GDP. These measures include deferrals of income taxes and social contributions for employers and self-employed when revenue decreased by more than 40%. A loan guarantee scheme was also introduced (1.6% of GDP). Overall, the measures taken by Slovakia are in line with the guidelines set out in the Commission Communication on a coordinated economic response to the COVID-19 outbreak. [11] The measures seem well targeted, temporary and timely in terms of cushioning the pandemic induced by COVID-19. The full implementation of those measures, followed by a

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[8] The Commission forecast presents the drop in income taxes and social security contributions due to compensation of wages (exempted from taxation) paid to employees and self-employed by the state as discretionary measures on the revenue side of the general government budget.

[9] "Unspecified measures" are measures that are not spelled out in sufficient detail or the total impact of known measures and automatic stabilisers does not fully explain the change in the government balance projected in the Programme.

[10] The total magnitude of all direct measures, liquidity support measures and guarantees is 5.2% of GDP (direct revenue and expenditure measures of 0.8% and 1.8% of GDP, tax deferrals of 1.2% of GDP and guarantees of 1.6% of GDP) according to the Stability Programme in 2020.

[11] https://ec.europa.eu/info/sites/info/files/communication-coordinated-economic-response-covid19-march-2020_en.pdf

refocusing of fiscal policies towards achieving prudent medium term fiscal positions when economic conditions allow, will contribute to preserving fiscal sustainability in the medium term..

Table 3: Discretionary measures adopted in response to COVID-19 outbreak

List of measures	Description	ESA Code (Expenditure / Revenue component)	Adoption Status	Budgetary impact (% of GDP - change from previous year)		
					2020	2021
Nursing and sickness benefits schemes changes	Provided to sick employees or employees nursing for family members – 55% of gross wage	n.a.	adopted		-0.76	0.76
Compensation of the employee´s salary	100% of compensation in businesses closed due to the government measures, max. EUR 880	n.a.	adopted		-0.78	0.78
Employment support	Contributions to maintain employment – 80% for closed businesses	n.a.	adopted		-0.35	0.35
Support to self-employed persons, Ltd. and other than employment contract	Subsidies provided to self-employed persons, which did not pay social sickness insurance, single-member Ltd. and people working under other than employment contract	n.a.	adopted		-0.25	0.25
Lump sum contribution per employee	For all employees in companies whose sales declined for more than 40%	n.a.	adopted		-0.14	0.14
Purchase of medical supplies	Purchase of medical goods linked to COVID-19	n.a.	adopted		-0.18	0.18
Temporary waiver of employers´social security contributions	For all employers with closed businesses in April. It can be combined with other measures – e.g. payment of 80% employees´gross wages	n.a.	adopted		-0.05	0.05
Other measures	Loss-carry forwards already in the current 2019 tax returns; extension of possibility to receive unemployment benefits by 1 month; suspension of tax audits and tax proceedings etc.	n.a.	adopted		-0.09	0.09
				Total	**-2.6**	**2.6**

Source: Stability Programme

The list of COVID-19 measures included in the Commission forecast and their budgetary impacts[12] are broadly in line with the Programme. The largest discrepancy is, as mentioned above, due to differences in the macroeconomic scenarios and assumptions underlying the projections. For instance, the Programme does not present the impact of the drop in taxes and social security contributions due to wage compensation and nursing and sickness paid out by the government, which are tax free, as measures. These declines are presented in the Programme as a result of the functioning of existing automatic fiscal stabilisers. In contrast to the Programme, the

[12] The total impact of COVID-19 measures is around 6.4% in the Commission forecast (direct expenditure measures of 2.2% of GDP, revenue measures of 1.3% of GDP, liquidity support measures of 1.2% of GDP and guarantee scheme of 1.6% of GDP).

Commission forecast is based on the assumption of a capital transfer due to the call of 10% guarantees for business loans provided by the government in 2020.

Table 4: Liquidity measures adopted in response to COVID-19 outbreak

List of measures	Description	Adoption Status	Budgetary impact (% of GDP - change from previous year)	
Deferral of social contributions payments	Employers and self-employed are entitled to delay their social security contributions and health insurance payments if their sales declined more than 40% in comparison with the same month in previous year or are closed due to the pandemic. The gradual repayment should take effect from July. The measure is expected only with cash impact:	adopted		0.85
Deferral of income tax advances payments	Businesses are entitled to use it if their sales declined more than 40% in comparison with previous year – cash impact in 2020, accrual impact in 2021 at the moment of annual tax settlement.	adopted		0.39
Other measures	The shift of advances on motor vehicles from April to the end of the pandemic; the optional deferral of the obligation to submit a tax return to natural and legal persons; the extension of the deadline for employers to pay out income tax overpayments after the end of the pandemic period.	adopted		0.14
			Total	**1.38**

Source: Stability Programme

Table 5: Guarantees adopted/announced in response to COVID-19 outbreak

List of measures	Description	Adoption Status	Maximum amount of contingent liability* (% of GDP)	
Guarantee of business loans	The government has committed to guarantee loans of up to EUR 1.5 billion for entrepreneurs affected by the COVID-19. The guarantee will be carried out through the Slovak Investment holding financial instruments. It will be mainly used by small and medium-sized enterprises.	Adopted		**1.59**
			Total	**1.59**

* Any possible budgetary impact related to the call of those guarantees should be provided in Table 1

Source: Stability Programme

3.3. Debt developments

The general government debt declined to 48% of GDP in 2019 (Table 6), driven mainly by the use of accumulated liquid assets and favourable developments in the denominator, in particular faster real GDP growth and accelerating inflation. A primary surplus also supported the decline in the debt ratio in 2019, though only marginally. The 2019 debt outrun was slightly above the projection presented in the 2019 Stability Programme but almost the same as in the 2020 DBP projections. In 2020, the Programme projects the debt-to-GDP ratio to increase to 61.2%, which is significantly higher than projected in the DBP (46.8% of GDP). The increase in the debt-to-GDP ratio will be primarily driven by a high primary deficit, but also by the contraction in real GDP, interest expenditure and stock-flow adjustment effects. The only factor contributing to the debt ratio decline is the inflation effect.

Table 6: Debt developments

(% of GDP)	Average 2014-2018	2019	2020		2021		2022	2023
			COM	SP	COM	SP	SP	SP
Gross debt ratio[1]	**51.6**	**48.0**	**59.5**	**61.2**	**59.9**	**61.9**	**61.4**	**60.1**
Change in the ratio	-1.1	-1.4	11.5	13.3	0.5	0.7	-0.4	-1.4
Contributions [2] *:*								
1. Primary balance	**0.4**	**0.1**	**7.1**	**7.2**	**2.9**	**n.a.**	**n.a.**	**n.a.**
2. "Snow-ball" effect	**-0.3**	**-1.1**	**3.6**	**3.9**	**-3.1**	**n.a.**	**n.a.**	**n.a.**
Of which:								
Interest expenditure	1.6	1.2	1.3	1.2	1.3	n.a.	n.a.	n.a.
Growth effect	-1.7	-1.1	3.4	3.7	-3.7	-3.9	-2.4	-1.8
Inflation effect	-0.2	-1.2	-1.1	-0.9	-0.7	-0.1	-0.8	-1.2
3. Stock-flow adjustment	**-1.2**	**-0.4**	**0.6**	**2.1**	**0.7**	**-0.2**	**n.a.**	**n.a.**
Of which:								
Cash/accruals diff.				0.1		1.0	-0.1	-0.5
Acc. financial assets				2.0		-1.4	-1.0	-1.0
Privatisation				0.0		0.0	0.0	0.0
Val. 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 :

Commission 2020 spring forecast (COM); Stability Programme (SP), Commission calculations.

According to the Programme these unfavourable debt developments are set to continue in 2021 (debt level of 61.9% of GDP) and beyond, with the primary deficit remaining the principal driver of the increase in the debt ratio. While primary deficits are projected to play an important role in Slovakia´s debt developments, they are projected to be gradually offset by the positive cumulative impact of snow-ball and stock-flow adjustment effects. A positive stock-flow adjustment in 2021 is attributable to advances paid for the purchase of military equipment that will affect the balance at the point of delivery and will exceed the use of accumulated financial assets. The related financing needs are estimated close to 14% of GDP in the Programme.

The Commission forecast projects a slightly more optimistic trajectory in the general government debt ratio compared to the Programme in 2020 and 2021. The Commission projections are driven by a smaller positive contribution from the primary balance than in the Programme, but also by a lower positive contribution from stock-flow adjustment in 2020.

The ratio of net debt to GDP is expected to grow over the whole forecast horizon from 43.2% of GDP in 2019 to around 57.4% of GDP in 2023 according to the Programme. The reason for the faster decline in net debt relative to gross debt is due to the slower decrease of liquid financial assets, which will be mainly in 2020 accumulated due to higher debt securities issuances. However, liquid financial assets

of the public administration are projected to decrease from 4.8% of GDP in 2018 to 3.8% of GDP in 2023.

3.4. Risk assessment

The macroeconomic and fiscal outlook are affected by high uncertainty due to the outbreak of the COVID-19 pandemic. The pandemic could become more severe and last longer than assumed, requiring more stringent and longer lasting containment measures. This would result in worse economic and fiscal outcomes. It could also require further fiscal policy measures. That would result in worse fiscal outcomes but help to mitigate the economic impact.An additional risk stems from the considerable size of public guarantees issued in response to the crisis.

The Council for Budget Responsibility (CBR) highlighted the following risks related to the 2020 general government balance[13]: the estimated impact of government measures to support the economic recovery of 1.7% of GDP (EUR 922 million covered from EU funds); the estimate of tax revenue shortfalls of 4.1% of GDP in particular related to value added tax and corporate income tax; an increase in social transfers not related to the COVID-19 crisis of 0.8% of GDP, including mainly the impact of 13th pensions payments without any counterbalancing measures (0.5% of GDP).

4. Compliance with the provisions of the Stability and Growth Pact

4.1. Compliance with the deficit criterion

According to the Stability Programme, Slovakia's general government deficit is expected to reach 8.4% of GDP in 2020, thereby exceeding the Treaty reference value of 3% of GDP. This provides *prima facie* evidence of the existence of an excessive deficit in Slovakia for the purposes of the Treaty and the Stability and Growth Pact. The Commission has therefore prepared a report under Article 126(3) TFEU, which analyses Country's compliance with the deficit criterion of the Treaty. Overall, since the planned deficit is well above 3% of GDP and the excess not temporary, and taking into account all relevant factors, the analysis suggests that the deficit criterion as defined in the Treaty and in Regulation (EC) No 1467/1997 is not fulfilled.

[13] http://www.rozpoctovarada.sk/svk/rozpocet/400

4.2. COMPLIANCE WITH THE MEDIUM-TERM OBJECTIVE IN 2019[14]

In 2019, Slovakia is subject to the preventive arm of the Stability and Growth Pact.

The growth of nominal primary government expenditure, net of discretionary revenue measures and one-offs, exceeded the applicable expenditure benchmark of 4.6% in 2019, leading to a deviation of -1.3% of GDP in the underlying fiscal position, thus pointing to significant deviation in 2019. The structural balance deteriorated by 0.2 percentage points of GDP in 2019, thus pointing to significant deviation in 2019 by -0.6% of GDP from the recommended structural adjustment of 0.3% of GDP towards the MTO. The finding of a significant deviation based on both pillars is confirmed when taken 2018 and 2019 together.

Based on the outturn data and the Commission forecast, the ex-post assessment finds that the adjustment towards the MTO was neither appropriate nor compliant with the requirement of the preventive arm of the Pact in year 2019 and points to a significant deviation from the adjustment path towards the MTO in year 2019.

[14] The possible retroactive impact on output gap estimates as a result of the recession induced by the COVID-19 outbreak and the possibility of abnormal responses of government revenues to major swings in economic activity underline that compared to the structural balance the expenditure benchmark is likely to provide a more reliable and predictable indicator in times of severe economic downturn.

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Table 7: Compliance with the requirements under the preventive arm

	(% of GDP)	2019	2020		2021	
	Background budgetary indicators[1]					
(1)	Medium-term objective (MTO)	-0.5	-1.0		-1.0	
(2)	Structural balance[2] (COM)	-2.3	-6.6		-4.0	
	Setting the required adjustment to the MTO					
(3)	Structural balance based on freezing (COM)	-1.3				
(4) = (1) - (3)	Position vis-a -vis the MTO[3]	Not at MTO				
(5)	Required adjustment[4]	0.3				
(6)	Required adjustment corrected[5]	0.3				
(8)	Corresponding expenditure benchmark[6]	4.6				
	Compliance with the required adjustment to the MTO					
		COM	**COM**	**SP**	**COM**	**SP**
	Structural balance pillar					
(8) = Δ (2)	Change in structural balance[7]	-0.2				
(9) = (8) - (6)	*One-year deviation from the required adjustment*[8]	-0.6				
	Two-year average deviation from the required adjustment[8]	-0.7				
	Expenditure benchmark pillar					
(10)	Net public expenditure annual growth corrected for one-offs[9]	8.1				
(11) = (10) - (8)	One-year deviation adjusted for one-offs[10]	-1.3				
	Two-year deviation adjusted for one-offs[10]	-1.2				
	Finding of the overall assessment	**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).

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.).

[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. Ex post assessment (for 20XX-1) is carried out on the basis of Commission 20XX 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.

[11] Defines the remaining annual structural adjustment over the transition period which ensures that - if followed – Member State will comply with the debt reduction benchmark at the end of the transition period, assuming that COM (S/CP) budgetary projections for the previous years are achieved.

[12] Applicable only during the transition period of three years from the correction of the excessive deficit for EDP that were ongoing in November 2011.

[13] Not relevant for Member Sates that were subject to an EDP procedure in November 2011 and for a period of three years following the correction of the excessive deficit.

[14] Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark.

Source :
Stability Programme (SP); Commission 2020 spring forecast (COM); Commission calculations.