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COMMISSION OPINION

of 22.11.2022

on the Draft Budgetary Plan of Slovakia

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(Only the Slovakian text is authentic)

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GENERAL CONSIDERATIONS

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

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

3. The general escape clause of the Stability and Growth Pact has been active since March 2020.[1] On 23 May 2022, the Commission indicated, in its Communication on the European Semester[2], that heightened uncertainty and strong downside risks to the economic outlook in the context of war in Europe, unprecedented energy price hikes and continued supply chain disturbances warrant the extension of the general escape clause of the Stability and Growth Pact through 2023 and it considered that the conditions to deactivate it as of 2024 were met. The continued activation of the general escape clause in 2023 will provide the space for national fiscal policy to react promptly when needed, while ensuring a smooth transition from the broad-based support to the economy during the pandemic times towards an increasing focus on temporary and targeted measures and fiscal prudence required to ensure medium-term sustainability.[3]

4. The Recovery and Resilience Facility, as established by Regulation (EU) 2021/241, provides financial support for the implementation of reforms and investment, notably to promote the green and digital transitions, thereby strengthening the economies' resilience and potential growth. Part of this support is in the form of non-repayable financial support ("grants"), entailing a fiscal impulse financed by the Union. Together with cohesion policy funds and the Just Transition Mechanism, the RRF is supporting a fair and inclusive recovery in the EU in line with the European Pillar of Social Rights. It also boosts growth and job creation in the medium and long term, and thereby strengthens sustainable public finances. According to the Commission proposal of 18 May 2022[4], the Facility should also aim at increasing the resilience of

[1] Communication from the Commission to the Council on the activation of the general escape clause of the Stability and Growth Pact, COM(2020) 123 final of 20 March 2020.

[2] COM(2022) 600 final.

[3] On 17 June 2022, the Council agreed its recommendations on the 2022 National Reform Programmes and the opinions on the 2022 Stability and Convergence Programmes, which takes into account the continuation of the Stability and Growth Pact's general escape clause into 2023. (See: https://www.consilium.europa.eu/en/meetings/ecofin/2022/06/17/)

[4] COM(2022) 231 final.

the Union energy system by reducing dependence on fossil fuels and diversifying energy supplies at Union level ('REPowerEU objectives').

5. On 12 July 2022, in the recommendations delivering Council opinions on the 2022 Stability Programmes[5], the Council recalled that the overall fiscal stance is currently best measured as the change in primary expenditure (net of discretionary revenue measures and excluding temporary emergency measures related to the COVID-19 crisis), including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other Union funds, relative to medium-term potential growth.[6] Going beyond the overall fiscal stance, in order to assess whether national fiscal policy is prudent and its composition is consistent with the green and digital transitions, energy security and ensuring social and economic resilience, attention is also paid to the evolution of nationally financed[7] primary current expenditure (net of discretionary revenue measures and excluding temporary emergency measures related to the COVID-19 crisis) and investment.

6. The shocks unleashed by the Russian invasion of Ukraine are impacting the EU economy both directly and indirectly, setting it on a path of lower growth and higher inflation. Intensifying and broadening inflationary pressures have been prompting faster normalisation of monetary policy in the euro area. Public spending measures containing the social and economic impact of high energy costs, on security and defence and on humanitarian assistance to the displaced persons from Ukraine is weighing on public finances. The specific nature of the macroeconomic shock imparted by Russia's invasion of Ukraine, as well as its long-term implications for the EU's energy security needs, call for a careful design of fiscal policy in 2023. A broad-based fiscal impulse to the economy in 2023 does not appear warranted. The focus should instead be on protecting the vulnerable, allowing automatic stabilisers to operate and providing temporary and targeted measures to mitigate the impact of the energy crisis and to provide humanitarian assistance to people fleeing from Russia's invasion of Ukraine, while maintaining the agility to adjust, if needed. Fiscal policy should combine higher investment with controlling the growth in nationally financed primary current expenditure. Full and timely implementation of the Recovery and Resilience Plans is key to achieving higher levels of investment. Fiscal policies should aim at preserving debt sustainability as well as raising the growth potential in a sustainable manner, thus also facilitating the task of monetary policy to ensure the timely return of inflation to the ECB's 2% medium-term target. Fiscal plans for 2023 should be anchored by prudent medium-term adjustment paths reflecting fiscal sustainability challenges associated with high debt-to GDP levels that have increased further due to the pandemic as well as reforms and investment challenges associated with the twin transition, energy security and social and economic resilience.

7. Russia's war of aggression against Ukraine has resulted in substantial additional increases in and volatility of the prices of energy. The price shock in imported energy implies a substantial terms-of-trade loss to Member States' economies. In parallel,

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[5] Council Recommendation of 12 July 2022 on the 2022 National Reform Programme of Slovakia and delivering a Council opinion on the 2022 Stability Programme of Slovakia, OJ C 334, 12.7.2022, p. 1-8.

[6] The estimates on the fiscal stance and its components in this Opinion are Commission estimates based on the assumptions underlying the Commission 2022 autumn forecast. The Commission's estimates of medium-term potential growth do not include the full positive impact of reforms that are part of the Recovery and Resilience Plan and that can boost potential growth.

[7] Not financed by grants under the Recovery and Resilience Facility or other Union funds.

the exceptionally high temperatures in summer 2022 pushed up demand for electricity, while, at the same time, energy production from certain technologies has been significantly below historical levels due to technical and weather-dependant circumstances. All Member States have been negatively affected by the current energy crisis, albeit to a different extent, calling for a rapid and coordinated response.

8. Given that budgetary resources are limited and need to be used in the most efficient way, in order to manage a durable and equitable adjustment across society, the quality and design of the policy response is highly important. Therefore, also in line with the Council Regulation on an emergency intervention to address high energy prices adopted on 6 October 2022, measures should focus on providing temporary support, targeted to households and firms most vulnerable to energy price increases, while maintaining the right incentives to reduce energy demand and increase energy efficiency, in line with the European Green Deal.[8] Policies should also help reducing the energy consumption and develop the energy autonomy of the Union.

CONSIDERATIONS CONCERNING SLOVAKIA

9. On 14 October 2022, Slovakia submitted the Draft Budgetary Plan for 2023. On that basis, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

10. On 12 July 2022, the Council recommended that Slovakia[9] take action to ensure in 2023 that the growth of nationally financed primary current expenditure is in line with an overall neutral policy stance[10], taking into account continued temporary and targeted support to households and firms most vulnerable to energy price hikes and to people fleeing Ukraine. Slovakia should stand ready to adjust current spending to the evolving situation. Slovakia was also recommended to expand public investment for the green and digital transitions, and for energy security taking into account the REPowerEU initiative, including by making use of the Recovery and Resilience Facility and other Union funds. For the period beyond 2023, Slovakia should pursue a fiscal policy aimed at achieving prudent medium-term fiscal positions.

11. On 23 May 2022, the Commission issued a report under Article 126(3) TFEU.[11] This report assessed the budgetary situation in several Member States, including in Slovakia as its general government deficit in 2021 exceeded the 3% of GDP Treaty reference value, while its general government debt exceeded the 60% of GDP Treaty reference value but was expected to decrease to below 60% of GDP in 2023. The report concluded that the deficit criterion was not fulfilled by Slovakia while the debt criterion was complied with.

12. According to the Commission 2022 autumn forecast, the Slovak economy is expected to grow by 1.9% in 2022 and by 0.5% in 2023, while inflation is forecast at 11.8% in 2022 and 13.9% in 2023.

[8] Communication from the Commission, the European Green Deal, COM(2019) 640 final.

[9] Council Recommendation of 12 July 2022 on the National Reform Programme of Slovakia and delivering a Council opinion on the 2022 Stability Programme of Slovakia, OJ C 334, 12.7.2022, p. 1-8.

[10] Based on the Commission autumn 2022 forecast, the medium-term (10-year average) potential output growth of Slovakia, that is used to measure the fiscal stance, is estimated at 14.0% in nominal terms. The Commission’s estimates of medium-term potential growth do not include the full positive impact of reforms that are part of the Recovery and Resilience Plan and that can boost potential growth.

[11] Report from the Commission prepared in accordance with Article 126(3) of the Treaty on the Functioning of the European Union, COM(2022) 630 final of 23 May 2022.

According to the Draft Budgetary Plan, the Slovak economy is expected to grow by 1.9% in 2022 and 0.6% in 2023, while inflation is projected at 11.6% in 2022 and 13.5% in 2023. While the profiles of GDP growth and HICP inflation are very similar in both projections, they differ slightly in their composition, reflecting different cut-off dates across the two sets of projections. According to the Draft Budgetary Plan, consumption is expected to decrease slightly more than in the Commission 2022 autumn forecast. The Draft Budgetary Plan expects somewhat stronger investment activity, especially in 2023. Although the growth dynamics of exports and imports are similar in both sets of projections, the Draft Budget Plan assumes a somewhat stronger recovery in exports, which are set to grow faster than imports in 2024. The Commission forecasts slightly higher inflation mainly due to higher expected growth in prices of non-energy components, especially food and industrial goods.

Overall, the macroeconomic assumptions underpinning the Draft Budgetary Plan are plausible both in 2022 and in 2023.

The macroeconomic assumptions as well as the assumptions on fiscal developments were formulated in a period of high uncertainty. Lower investments and a slower absorption of capital expenditures constitutes a risk for the fiscal projection. A faster increase in interest rates, affecting the costs of servicing the government debt, could also pose a risk.

Slovakia complies with the requirement of Regulation (EU) No 473/2013 since the draft budget is based on independently produced macroeconomic forecasts.

13. The Draft Budgetary Plan assumes that expenditure amounting to 0.6% of GDP in 2022, 0.8% in 2023 and 0.8% in 2024 will be financed by non-repayable financial support (grants) from the Recovery and Resilience Facility. Expenditures financed by Recovery and Resilience Facility grants will enable high-quality investment and productivity-enhancing reforms without a direct impact on the general government deficit and debt of Slovakia. The estimates of the Commission are higher, specifically 1.7% of GDP in 2023 and 1.1% of GDP in 2024. The difference stems from the fact that the Draft Budgetary Plan only includes public sector expenditures in the amount of expenditures financed by non-repayable financial support (grants) from the Recovery and Resilience Facility and does not include private sector expenditures.

14. In its 2023 Draft Budgetary Plan, Slovakia's general government deficit is planned to increase from 5.0% of GDP in 2022 to 6.4% of GDP in 2023, mainly due to budgetary appropriations for government support to mitigate the economic and social impacts of high energy prices. The planned general government deficit is higher than in the Commission 2022 autumn forecast (4.2% of GDP in 2022 and 5.8% of GDP in 2023). One of the reasons for this is that the Commission projects lower total expenditures on government support to mitigate the economic and social impact of the energy price increase than the Draft Budgetary Plan for both 2022 and 2023.[12] The second reason is different assumptions on the profile of government gross fixed capital formation. The Commission 2022 autumn forecast estimates lower amount of investments in 2022, which will be compensated to some extent by stronger investment activity in 2023, while the Draft Budgetary Plan expects higher

[12] It is to be noted that while the above-mentioned budgetary appropriations have been reflected in the Commission forecast, the lack of sufficient specification of their ultimate use prevents the Commission from treating them as 'fiscal policy measures'.

government gross fixed capital formation already in 2022. The general government debt ratio is planned to decrease from 59.8% of GDP in 2022 to 59.0% of GDP in 2023, in line with the Commission projections.

The outlook for public finances continues to be subject to the high uncertainty that surrounds the macroeconomic projections, including macroeconomic risks related to the Russian invasion of Ukraine, energy price hikes and continued supply chain disturbances.

15. Measures underpinning the Draft Budgetary Plan include changes in the first pillar of the pension system that amount to one-time expenditure of a total of 0.2% of GDP in 2023. Furthermore, permanent expenditure related to the valorisation of salaries of health professionals in public sector amounts to 0.2% of GDP in 2023. The Draft Budgetary Plan includes also a contribution to the child's leisure activity in the amount of EUR 440 million, which is not included in the Commission forecast, since the implementation of the measure is still a subject of discussions.

The government deficit is also impacted by the measures adopted to counter the economic and social impact of the exceptional increases in energy prices, which aggravated over the course of the summer[13]. The budgetary cost of these measures is projected in the Commission 2022 autumn forecast to amount to 0.5% of GDP in 2022 and 0.0% of GDP in 2023. They consist of measures increasing expenditure, such as an additional benefit for groups of people most exposed to high inflation, a one-time increase in child allowance, a one-time payment of the "14th pension", and a one-time bonus paid to all employees in public sector. The cost of these measures is partly offset by new taxes on windfall profits of energy producers, namely a special levy applied to the state enterprise Vodohospodárska výstavba (water management construction), which are projected to bring budgetary revenues of 0.1% of GDP in 2023. Taking these revenues into account, the net budgetary cost of these measures in the Commission 2022 autumn forecast is estimated at 0.5% of GDP in 2022 and -0.1% of GDP in 2023.[14] These measures have been announced as temporary. Most measures do not appear targeted to vulnerable households or firms[15], although they preserve the price signal to reduce energy demand and increase energy efficiency.[16] As a result, the amount of temporary and targeted support to households and firms most vulnerable to energy price hikes, that can be taken into account in the assessment of compliance with the fiscal country-specific recommendation for 2023, is estimated in the Commission 2022 autumn forecast at 0.2% of GDP in 2022 and 0.0% of GDP in 2023.

The government deficit is also impacted by the costs to offer temporary protection to displaced persons from Ukraine, which in the Commission 2022 autumn forecast are projected at 0.2% of GDP in 2022 and 0.1% in 2023.

16. Based on the Commission 2022 autumn forecast and including the information incorporated in Slovakia's 2023 Draft Budgetary Plan, gross fixed capital formation

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[13] Deficit developments in 2023 are also affected by the complete phasing out of COVID-19 emergency temporary measures, which are estimated in the Commission autumn 2022 forecast at 1.0% of GDP in 2022.

[14] The figures represent the level of annual budgetary costs of those measures taken since autumn 2021, including current revenue and expenditure as well as – where relevant – capital expenditure measures.

[15] Targeted measures amount to 0.2% of GDP in 2022, while untargeted measures amount to 0.3% of GDP in 2022.

[16] Income measures amount to 0.5% of GDP in 2022 and 0.0% of GDP in 2023, while price measures amount to 0.0% of GDP in 2022 and 0.0% of GDP in 2023.

is expected to amount to 3.5% of GDP in 2022 and 4.6% of GDP in 2023, compared to 3.1% of GDP recorded in 2021.

17. In 2023, the fiscal stance is projected in the Commission 2022 autumn forecast to be expansionary (- 2.6% of GDP[17]). This follows an expansionary fiscal stance in 2022 (- 1.3% of GDP).

The growth in nationally financed primary current expenditure (net of new revenue measures) in 2023 is projected to provide an expansionary contribution of 1.7 percentage points[18]. This takes into account the reduced impact from the support measures adopted to counter the economic and social impact of the exceptional increases in energy prices by 0.5% of GDP[19], with the temporary and targeted support measures to households and firms most vulnerable to energy price hikes accounting for 0.2 % of GDP of this reduction. This also includes lower costs to offer temporary protection to displaced persons from Ukraine (by 0.1 % of GDP). Therefore, the expansionary contribution of nationally financed primary current expenditure is not due to the temporary and targeted support to households and firms most vulnerable to energy price hikes and to people fleeing Ukraine.

The positive contribution to economic activity of expenditure financed by Recovery and Resilience Facility grants and other EU funds is projected to increase by 1.0 percentage points of GDP in 2023 compared to 2022. Nationally financed investment is projected to provide an expansionary contribution to the fiscal stance of 0.2 percentage points in 2023.[20]

18. The Draft Budgetary Plan includes medium-term budgetary projections until 2025. The government deficit is projected to decrease gradually to 3.4% of GDP in 2024, and to 2.7% in 2025. These plans assume a constant structural annual adjustment of 0.5% of GDP each year from 2023 onwards. In turn, government debt is envisaged to reach 59.4% of GDP in 2024 and to decline again to 59.0% of GDP in 2025. With the current projection of the gross debt for 2023, according to the currently applicable constitutional Budget Responsibility Act, debt brake sanctions leading to a reduction in indebtedness should be automatically triggered in May 2023. Without the adoption of the expected amendment to the Budget Responsibility Act, the government would have to submit to the National Council a balanced (or surplus) Draft Budgetary Plan for 2024. Such a situation would require, according to the Draft Budgetary Plan, to adopt consolidation measures in the amount of 4.3% of GDP.

19. On 12 July 2022 the Council also recommended Slovakia to make the tax mix more efficient and more supportive to inclusive and sustainable growth, including by leveraging the potential of environmental and property taxation, and to continue to strengthen tax compliance, including by further digitalising tax administration. The Draft Budgetary Plan does not present measures to address these recommendations.

[17] A negative (positive) sign of the indicator corresponds to an excess (shortfall) of primary expenditure growth compared with medium-term economic growth, indicating an expansionary (contractionary) fiscal policy. The fiscal stance includes the fiscal impulse funded by the Union.

[18] This follows an expansionary contribution from this component of 0.6 percentage points in 2022.

[19] The budgetary impact of targeted price and income measures is projected to remain stable and decrease by 0.2% of GDP respectively, while the budgetary impact of untargeted price and income measures is projected to remain stable and decrease by 0.3% of GDP respectively.

[20] Other nationally financed capital expenditure is projected to provide a contractionary contribution of 0.3 percentage points of GDP.

20. In 2023, based on the Commission's forecast and including the information incorporated in the Draft Budgetary Plan, the overall fiscal policy stance is estimated to be expansionary in a situation of high inflation. This includes an expansionary contribution to the overall fiscal stance from nationally financed current expenditure, also reflecting the above-mentioned sizeable budgetary appropriations for government support to mitigate the impact of high energy prices that were not sufficiently specified in the Draft Budgetary Plan. The expansionary stance cannot at this stage be considered the result of temporary and targeted support to households and firms most vulnerable to energy price hikes and the cost to assist people fleeing Ukraine. Overall, the growth of nationally financed primary current expenditure is not in line with the recommendation of the Council. Slovakia plans to finance additional investment through the RRF and other EU funds and it also preserves nationally financed investment. It plans to finance public investment for the green and digital transitions, and for energy security.

Overall, the Commission is of the opinion that the Draft Budgetary Plan for Slovakia is partly in line with the fiscal guidance contained in the Council recommendation of 12 July 2022. The Commission invites Slovakia to take the necessary measures within the national budgetary process to ensure that the 2023 budget is consistent with the recommendation adopted by the Council on 12 July 2022.

While Slovakia rapidly deployed energy measures as part of the emergency policy response to the exceptional energy price hikes, a prolongation of existing and/or an enactment of new support measures in response to high energy prices would contribute to higher growth in net nationally financed current expenditure and to an increase in the projected government deficit and debt in 2023. Therefore, it is important that Member States better focus such measures to the most vulnerable households and exposed firms, to preserve incentives to reduce energy demand, and to be withdrawn as energy price pressures diminish.

The Commission is also of the opinion that Slovakia has not yet made progress with regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 12 July 2022 in the context of the European Semester and thus invites the authorities to accelerate progress. A comprehensive description of progress made with the implementation of the country-specific recommendations will be made in the 2023 Country Report and assessed in the context of the country-specific recommendations to be proposed by the Commission in spring 2023.

Done at Brussels, 22.11.2022

For the Commission
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