Stability Programme of the Slovak Republic for 2013 - 2016

April 2013

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INTRODUCTION

The main objective of Slovakia's fiscal policy is to ensure efficient public finances which are sustainable in the long term, support sustainable economic development and contribute towards a better quality of life in the context of population ageing, while taking due account of contingent liabilities. This objective is laid down in the constitutional Fiscal Responsibility Act.

Along with other 19 EU Member States, Slovakia is currently under the excessive deficit procedure and must correct its excessive deficit by 2013. The consolidation of public finances progresses according to the plan adopted by the Government. The 2012 general government deficit reached 4.3% of GDP, which is 0.3% of GDP below the fiscal target of 4.6% of GDP. In 2013, general government deficit is planned to reach 2.9% of GDP. According to the up-to-date information and in light of certain consolidation measures adopted in addition to the valid general government budget, this target is expected to be achieved.

The Stability Programme presents a fiscal strategy which should lead to the abrogation of the excessive deficit procedure next year and the attainment of a fiscal position conducive to making public finances sustainable in the long run. This requires that the public finance consolidation be continued also after 2013 in line with both the national and EU budgetary rules in order to bring Slovakia closer to its medium-term budgetary objective.

The Stability Programme of the Slovak Republic seeks to achieve the following objectives:

- The basic objective is to reduce general government deficit to 2.9% of GDP in 2013 on a permanent and sustainable basis and thus comply with the EDP requirements.
- In the years to come, the deficit is expected to diminish gradually in line with the provisions of the Stability and Growth Pact, respecting the constraints given by the national fiscal rules. **Hence, the target deficit values have been set at 2.6% of GDP in 2014, 2.0% of GDP in 2015 and 1.3% of GDP in 2016.** The meeting of these targets would stop the public debt-to-GDP ratio from growing further and, from 2015 onward, enable its gradual reduction. The size of the consolidation effort needed to meet the targets, as opposed to the no-policy-change scenario, reaches 1.0% of GDP in 2014, 1.6% of GDP in 2015 and 1.8% of GDP in 2016. Some of these measures have already been incorporated into the General Government Budget Framework for 2014-2016. The remaining measures will be specified in the course of the budget proposal preparation.
- The consolidation of public finances will continue also after 2016 in order to **meet the medium-term budgetary objective (MTO) for the general government's structural deficit of 0.5% of GDP by 2018**.

In 2013, the Stability Programme is based on the General Government Budget for 2013-2015 as approved by the Parliament in December 2012, as well as on the latest available balance estimates. In 2014 to 2016, it is based on the 2014-2016 General Government Budget Framework. The data for 2017 and 2018, which are necessary to propose a timetable of convergence towards the MTO, represent gross estimates by the MF SR. The Stability Programme, once approved by the Government, is submitted to the Parliament.

The stability programmes and convergence programmes, required under the Stability and Growth Pact, are submitted annually to the European Commission (the Commission) and the EU Council. Their purpose is to present the development of fiscal position, expected economic development, and a description of the budgetary and economic measures adopted to achieve the goals of the programme in the medium term. The programmes are submitted to the Commission within the framework of the European Semester, the objective of which is to improve the coordination of fiscal and structural policies, taking into account the rules set by the Stability and Growth Pact and the Europe 2020 strategy. The process this year started by the publication of the Annual Growth Survey for 2013 in which the Commission outlined five main priorities. The first of them is differentiated growth-friendly fiscal consolidation. When preparing their stability programmes and national reform programmes, Member States should follow the recommendations made under individual priority areas.

The content and the format of the document are in full compliance with the Commission's guiding principles. These guiding principles are described in the *"Specifications on the Implementation of the Stability and Growth Pact"* and the *"Guidelines on the Format and Content of Stability and Convergence Programmes"*. The present Stability Programme reflects the latest revision of the above mentioned documents from September 2012. It also takes into account the deliberations, documents and recommendations of the Economic and Financial Committee.

I. OVERALL POLICY FRAMEWORK AND OBJECTIVES

The objective of the Government's economic policy is to react flexibly to the current economic situation, yet the underling priority remains unchanged – making economic growth sustainable in the long run in order to accelerate growth in the standard of living and the process of catching up with the advanced EU Member States. Membership of the euro area and monetary policy integration have underscored the importance of pursuing a responsible fiscal policy aimed at making public finances sound and sustainable and enabling effective operation of automatic stabilisers and structural policies designed to foster potential economic growth.

I.1. Fiscal policy

The objective of Slovakia's fiscal policy is to attain a fiscal position that creates conditions for long-term sustainability of public finances.

The essential prerequisite for meeting this objective is to reduce general government deficit below 3% of GDP in 2013 on a sustainable basis, which would result in the abrogation of the excessive deficit procedure.

In the next period, the fiscal consolidation is expected to continue so as to ensure that Slovakia meets its MTO, set as a structural deficit of 0.5% of GDP by 2018, respecting the provisions of the Stability and Growth Pact and the constraints given by the national budgetary rules.

Given the macroeconomically restrictive nature of the 2014-2016 fiscal policy, it will be necessary to adopt measures with the least possible adverse impact on economic growth, and continue growth-friendly structural reforms. The drawing of EU funds may also provide an important impetus for the economy. At the same time, improved tax collection and a more efficient allocation of public expenditures can alleviate the negative impacts of fiscal consolidation.

Given the future demographic development, apart from improving fiscal discipline, attention should also be given to those sectors that are sensitive to population ageing, in particular the pension system and healthcare. Also for this reason, Slovakia adopted a pension system reform in 2012 which significantly improves long-term sustainability public finances. [1]

I.2. Monetary policy

After Slovakia's accession to the euro area, price stability remains the main monetary policy objective. The European Central Bank defines price stability as a year-on-year increase in the Harmonised Index of Consumer Prices (HICP) for the euro area below or close to 2%. However, with Slovakia's real and nominal convergence still underway, a slightly higher rate of inflation should be expected given the absence of the exchange-rate channel. From a long-term perspective, responsible fiscal policy and implementation of structural policies focusing on improvements in the functioning of the labour market and the markets of goods and services, particularly their high competitiveness and flexibility and low information asymmetries, will be essential to ensuring price stability in Slovakia.

[2] FED used the "Operation Twist" at the turn of 2011-2012 to lower interest rates through the sale of short-term securities and subsequent reinvestment of proceeds into bonds with long maturities.

[1] Details are presented in Chapter V

I.3. Structural policies

The objective of the Government's structural policies is to achieve permanently sustainable growth, increase employment, and improve the quality of life. The priorities and measures necessary to achieve these objectives have been chosen based on GDP decomposition and analysis of the most significant obstacles to growth, taking into account also other factors affecting the living standard. The defined priorities are: education and training, science and innovation, employment, social inclusion, business environment, transport and telecommunication infrastructure, modern and efficient public administration, environmental sustainability, and energy.

The specific measures for individual priorities are specified in the National Reform Programme (NRP), which the Government submits to the Commission together with the Stability Programme. Structural measures are complemented by short-term instruments designed to prevent loss in industrial capacity, as well as situations in which the "surviving" businesses cannot invest in enhancing their competitiveness. These measures should also prevent the loss of working skills by maintaining employment. Certain short-term expenditure policies support long-term economic growth. These include, for example, training schemes for the unemployed or construction of transport infrastructure.

I.4. Overview of compliance with the EU Council recommendations

Pursuant to Article 126(6) of the Treaty on the functioning of the European Union (TFEU), on 2 December 2009 the ECOFIN Council adopted Council Decision on the existence of an excessive deficit in Slovakia, placing Slovakia under the excessive deficit procedure. At the same time, the EU Council approved, under Article 126(7) of the TFEU, recommendations for Slovakia, which are together with Government's reactions included in the following table:

TAB 1 - Reactions of the Slovak Government to EU Council recommendations

Recommendation	Reaction
Excessive deficit should be corrected by 2013.	The goal of the Slovak Government is to reduce the general government deficit to 2.9% of GDP in 2013 and continue fiscal consolidation in the years to come.
The deficit-reducing measures should be implemented in 2010, as planned in the general government budget for 2010-2012.	The first package of consolidation measures was adopted with effect from 2011. The 2012 shortfall in revenues from taxes and social contributions by 1.0% of GDP against the budget was offset by additional measures in the area of taxes and contributions and cuts in public expenditures. Additional significant consolidation is taking place during 2013.
Annual average consolidation effort should reach 1% of GDP over the period of 2010–2013.	The annual average consolidation effort in 2010 to 2012 represented 1% of GDP. With the 2013 consolidation effort estimated at 1.2% of GDP, the average annual consolidation over the period of 2010-2013 represents 1.1% of GDP.
The Slovak government should specify the measures needed to achieve correction of the excessive deficit by 2013 and accelerate the reduction of the deficit if the macroeconomic developments turn out better than currently expected.	The measures designed to correct the excessive deficit have been specified in the approved General Government Budget for 2013-2015 (described in Part III.2.2). Even if the developments are adverse, the government remains determined to adopt, when and as needed, additional measures to reach the 2013 budget deficit target.
To limit risks to the adjustment, enforceability of the medium-term budgetary framework should be strengthened and monitoring of the budget execution throughout the year should be improved, in particular to avoid expenditure overruns.	The (constitutional) Fiscal Responsibility Act was adopted in 2011 based on a broad consensus. The introduction of expenditure ceilings, which is under preparation, will strengthen the multiannual planning horizon of the budget and convergence towards the MTO. Expenditure ceilings will be probably linked with the fiscal compact through an automatic correction mechanism (i.e. once activated, expenditure ceilings will be adjusted).

In July 2012, based on the evaluation of Slovakia's Stability Programme for 2012–2015 and the National Reform Programme, the Council approved a set of country-specific recommendations. Their wording and detailed account of compliance is included in the National Reform Programme 2013.

II. ECONOMIC OUTLOOK AND PROJECTIONS

In 2012, the economic growth of Slovakia slowed down considerably. Despite the generally unfavourable situation caused by the deepening debt crisis in the eurozone, the economy of Slovakia grew by 2%, which was the fourth fastest growth in the EU. This was mainly thanks to the launch of new automobile production programmes which helped to offset considerable deceleration in foreign demand. The structure of economic growth was thus dominated by net exports, while domestic demand declined.

II.1. External environment

The development of the Slovak economy was largely influenced by adverse developments in the external environment. Global economy slowed down in 2012, primarily due to the deepening debt crisis in the eurozone. The eurozone economy, as a whole, slumped by 0.6%, with considerable differences across Member States. The German economy grew by 0.7% mainly thanks to the revived industrial activity and lower unemployment in early 2012. On the other hand, the peripheral members of the eurozone felt the full impact of the debt crisis and their economic activity contracted considerably (Greece and Portugal by 6.4% and 3.2%, respectively). However, as the year was drawing to an end, the signs of the crisis spilling over to the German economy, which slowed down in Q4 against Q3, began to appear. Although the U.S. economy grew by 2.2% in 2012 (compared with 1.8% in 2011), it slowed down fairly significantly in the second half of the year. In spite of the higher economic growth, the 2012 unemployment in the U.S. dipped only slightly and the economy got into stagnation towards the year-end.

The generally unfavourable development at the end of 2012 was reflected also in the first months of 2013. The leading indicators (PMI) and economic sentiment indicators suggest a slight GDP contraction in the first quarter of 2013 in the eurozone countries, including Germany. On the other hand, the soft-indicators in the eurozone and mainly in Germany (IFO, ZEW) continue to suggest that the German economy should pick up markedly in the second half of 2013.

On the whole, the economic revival of Slovakia's major trading partners in 2013 will be feeble at best, the main reason being the expected simultaneous consolidation across several eurozone countries. The gradual process of household deleveraging, coupled with persisting low confidence, will curb consumption and thus impede economic growth.

In its Winter Forecast published in February 2013, the Commission downgraded its 2013 growth outlook for both for the eurozone and the EU as a whole. According to the forecast, the eurozone is expected to slip into a shallow recession in 2013 (-0.3%). This downward growth outlook revision also applies to Germany which is expected to grow only by 0.5%. In 2013, the U.S. economic growth will reach approximately 1.9%, which is slightly below the 2012 level. In spite of the downward revision, the assumptions used in the Commission's Winter Forecast are in tune with the assumptions used in the present MF SR forecast for the external environment. The slight differences, where any, are negligible.

TAB 2 - External assumptions for the January forecast

		MF SR			EK	
	2012	**2013**	**2014**	**2012***	**2013***	**2014***
Economic growth						
EU	-0.3	0.2	1.5	-0.3	0.1	1.6
Euro area	-0.6	-0.1	1.2	-0.6	-0.3	1.4
Germany	0.7	0.5	1.8	0.7	0.5	2.0
USA	2.2	1.9	2.6	2.2	1.9	2.6
China	7.8	8.0	8.1	7.8	8.0	8.1
Imports of Slovakia's trading partners	0.5	2.4	4.5	0.5	**2.1**	5.4
Long-term interest rates (10Y)						
Euro area	1.6	1.7	2.3	1.6	1.7	2.0
ECB key interest rate	0.9	0.8	1.0	-	-	-
Exchange rate (USD/EUR)	1.29	1.30	1.25	1.28	1.35	1.35
Oil price (Brent, USD/bl)	112.0	111.7	114.5	111.8	113.7	106.4
Oil price (Brent. EUR/bl)	87.1	85.7	91.3	87.0	84.2	78.8

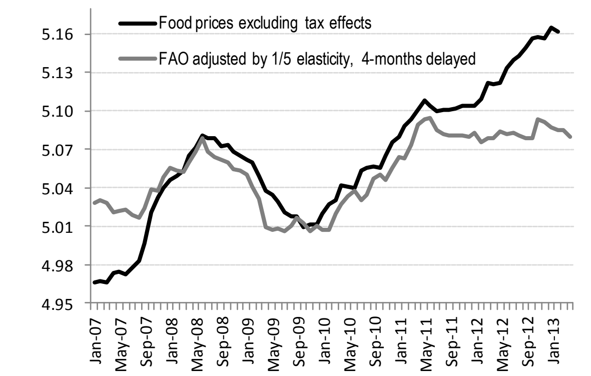
*Source: MF SR January 2013, *EC Winter Forecast February 2013*

In contrast with macroeconomic developments, situation on the international financial markets in 2012 improved considerably. Markets sensed excess liquidity and, following ECB verbal interventions, positive sentiments prevailed. On a number of occasions the ECB governor voiced clear support for the euro and emphasised that the ECB would do all it takes to save it. The ECB also announced preparedness to launch, if necessary, its sovereign bond-buying programme through the secondary market. The euro exchange rate against the dollar and most other currencies continued to appreciate, hovering above 1.3 to the dollar for quite some time. The yields of the Spanish and Italian bonds which, given their size, represent major risks for the fate of the eurozone, continued to dive (save for short-lived fluctuations), slipping under 5.0% for Spain and 4.7% for Italy (compared with 7.5% and 6.5%, respectively, in July 2011).

Oil prices in 2012 remained relatively stable, around 110 USD/bl (Brent), with some short-term fluctuations. In the spring of 2012, oil price surged above 125 USD/bl, plummeted to 90 USD/bl in the summer and then regained the 110 USD/bl level. Its impact on inflation in 2012 was more-or-less neutral. However, apart from oil price increases in dollar terms, the eurozone is also susceptible to EUR/USD fluctuations. Unlike in 2011 when USD appreciated against EUR on a sustained basis, the exchange-rate impact on oil prices in euro terms, and thereby on inflation, was also neutral. Although the dollar/euro currency pair neared 1.2 EUR/USD in the summer of 2012, the shift was not long-lived and, after ECB verbal interventions, the swung back to settle at about 1.3 EUR/USD.

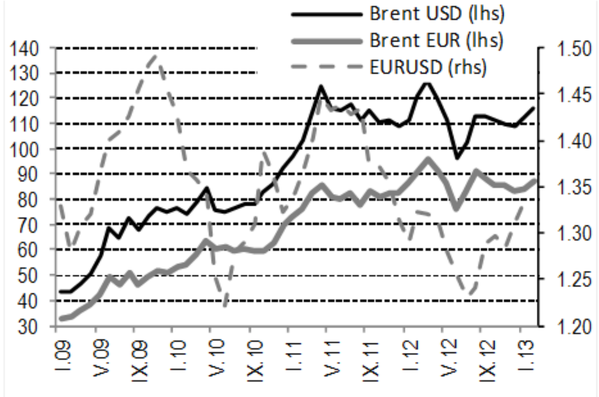
Global inflationary pressures were on the wane in the course of 2012 and the pace of price growth towards the year-end decelerated mainly due to the relatively stable oil prices and falling commodity prices, but also as a consequence of a feeble recovery of economic activity in Europe. Despite the gradual slowdown in the rise of prices in the eurozone, particularly in the second half of the year, the average price growth in 2012 reached 2.5% year-on-year (2.7% in 2011), which is above the inflation target of 2%. Food prices on global markets stabilised at the end of 2012 and the expected 2013 inflation rate in the eurozone should, according to the Commission's forecast, drop to 1.8%, i.e. below the ECB's inflation target.

GRAPH 1 - Development of FAO food price index and domestic food index (index in logs)



Source:MF SR. FAO

GRAPH 2 - BRENT oil (USD/bl) and EUR/USD



Source: Bloomberg

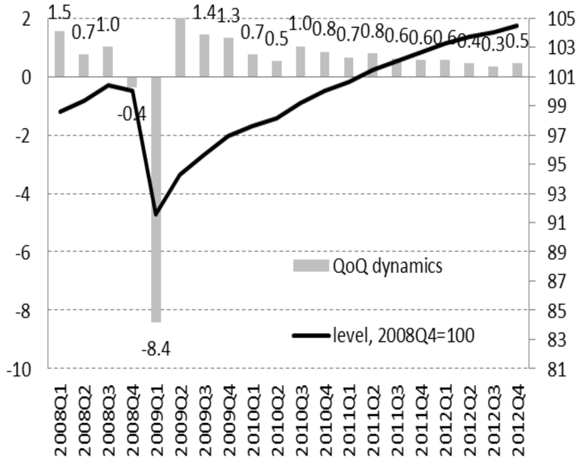
The monetary policy pursued by most major central banks remained expansionary in 2012, with rates kept at record lows. The key central bank, FED, kept its interest rates at record lows unchanged throughout 2012. The FED's main interest rate has thus remained unchanged at 0.25% since December 2008. In addition, after two rounds of quantitative easing and the "Operation Twist"[2], the FED announced and launched the third round of quantitative easing (QE3). For the third round, the FED set a minimum volume of securities it would purchase on the secondary market but, unlike in QE2, this round is open-ended.[3] In contrast to the FED whose main rate is practically zero, the ECB has still some margin for cuts. The ECB decided to use this margin in 2012 just once, reducing the rate by 0.25 p.p. to its all-time-low at 0.75%.

II.2. Economic development in Slovakia in 2012

The growth of the Slovak economy slowed down to 2.0% in 2012 from 3.2% in 2011. Despite the adverse situation in the eurozone, Slovakia was the fourth fastest growing economy in the EU. The slowdown is attributable to deterioration in the external environment which, coupled with overall uncertainty, negatively affected domestic demand.

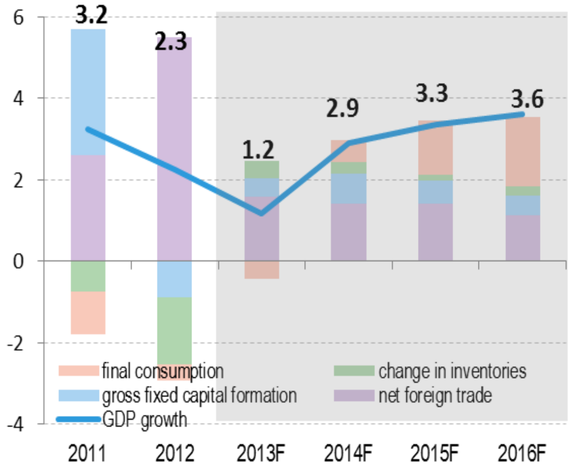
GDP growth was driven solely by foreign trade. New production capacities in the Slovak automotive industry, created by previous-years' investments by major car manufacturers helped Slovakia to avoid recession despite slacking foreign demand. The contribution of net exports to the GDP growth reached 5.5 p.p. in 2012. All other components affected GDP growth negatively. Change in inventories had the most negative impact on growth (1.7 p.p.). Household consumption continued to decline for the third year in a row, reflecting unfavourable labour market situation. Investments also declined. Government consumption declined due to the additional consolidation measures taken to offset shortfalls in tax revenues

GRAPH 3 - GDP, adjusted for seasonal and one-off effects *



**GDP adjusted for cigarettes stockpiling and one-off VAT payments after final inspection of R1 highway* *Source: MF SR*

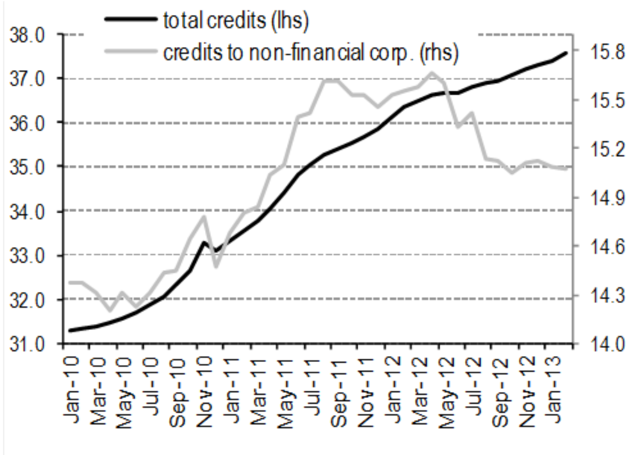
GRAPH 4 - Contributions to GDP growth in 2011-16



Source: MF SR

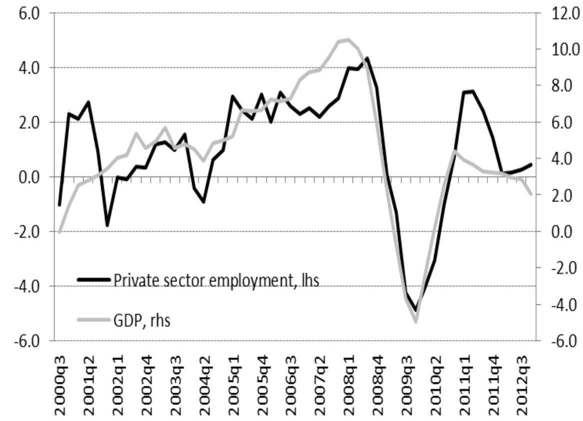
[3] The stability programme features indicators calculated according to the ESA 95 methodology; as of 01/09/2014 the official statistical data will be published under the ESA 2010 methodology.

GRAPH 5- Credits in the economy and credits to non-financial corporations (stock at the end of month, bln. €)



Source: Bloomberg

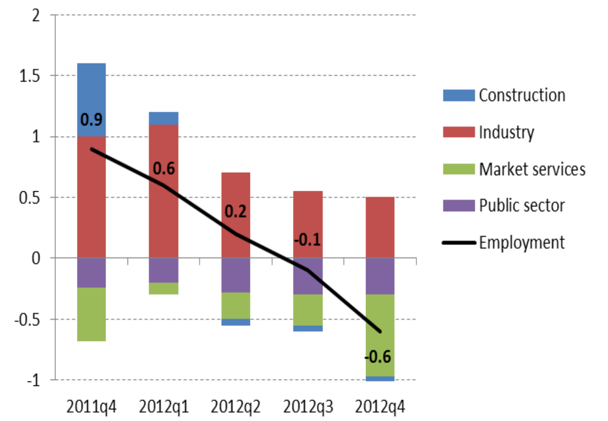
GRAPH 6- Annualised q/q growth of private sector employment and y/y GDP growth



Source: ŠO SR

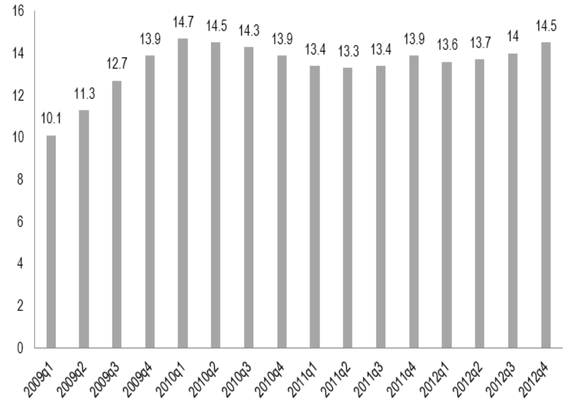
The 2012 economic growth was not sufficient to help generate new jobs in high numbers. Moreover, the year-end was influenced by uncertainties about the external environment and the anticipated impacts of fiscal consolidation. Employment (under the ESA95 methodology) stagnated in 2012, with about 1,000 new jobs created (up 0.1%). Economic growth was thus driven by gains in labour productivity. Although the output side of the economy returned to its pre-crisis level back in 2010, employment gap is still at more than 38,000 jobs. The highest number of jobs was lost in the construction and manufacturing sectors, while the services sector reported the highest number of new employees in 2012.

GRAPH 7- Growth of employment in selected sectors (annual growth)



Source: SO SR

GRAPH 8 - Unemployment rate seasonally adjusted, LFS, %



Source: SO SR

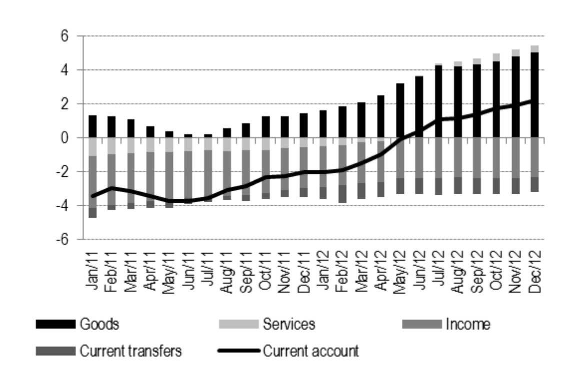
Unemployment rate (LFS methodology) rose to 14% and Slovakia remains among the EU countries with the highest unemployment. The problem of long-term unemployment still persists and its share in total employment reached almost 64% in 2012.

The average nominal monthly wage of an employee in the economy in 2012 reached EUR 805. It rose 2.4% year-on-year, which is a slightly higher increase than in the year before. The growth of wages in the private sector abated slightly as a consequence of uncertainties around the debt crisis. On the contrary, the wage growth in public administration pushed the average wage upwards. This was mainly due to a rise in wages paid by municipalities and self-governing regions and the social and health insurance funds. The real wage dropped by 1.2%.

The 2012 trade balance closed at 5.1% of GDP, 4.6 p.p. higher than in 2011. The main reason behind this historically highest surplus lies in the launch of new automobile production programmes which boosted exports, while imports of goods remained stifled due to a week domestic demand. Goods exports surged by 10.7%, with car exports clearly in the vanguard. Imports rose only by 6.7%. Imports of capital goods rose most significantly, whereas the increase in consumer goods imports was minimal (0.3%).

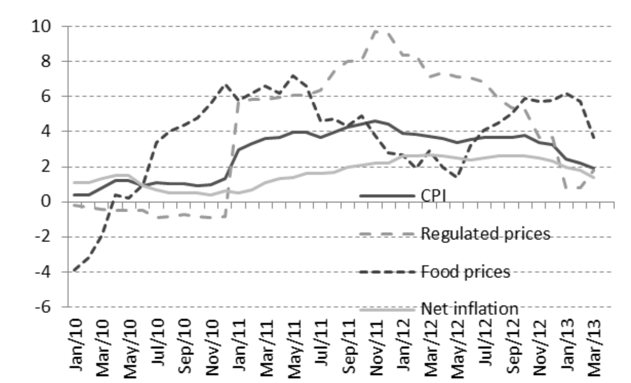
For the first time in history, the current account of the balance of payments showed a surplus of 2.2% of GDP in 2012, compared to the deficit of 2% of GDP in 2011. The improvement is mainly attributable to trade balance, but also to the balance of services. The export of services surged by 17.2%, but their import rose only by 3.3%. The balance of current transfers showed some improvement, while the balance of income deteriorated slightly.

GRAPH 9- External imbalances - components of the CAB (% of GDP for the last 12 months)



Source:NBS

GRAPH 10- Structure of annual CPI growth (%)



Source:MF SR

In the past two years, the inflation rate in Slovakia remained relatively high. Inflation, measured by the national consumer price index (CPI), dropped from 3.9% in 2011 to 3.6% in 2012. The growth in regulated prices and in food prices belong to the common denominators which fuelled inflation in both years. The sharp increase in the prices of gas and heat caused regulated prices to grow by 6.3%. Food prices increased mainly in reaction to the rising prices of agricultural commodities on foreign markets. In the summer of 2012, the prices of agricultural commodities on commodity exchanges attacked their all-time highs. Net inflation (year-on-year price increase by 2.5%), which reflects domestic demand pressures, declined steadily since March 2011. This development points at a weak consumer confidence, which is also obvious from declining retail sales. In comparison with other eurozone members, Slovakia belonged to the group of countries with a higher-than-average inflation.

II.3. Medium-term economic forecast

The updated official MFSR forecast from 30 January 2013 assumes the 2013 economic growth to reach 1.2%. Similarly to 2012, the economic development of Slovakia's major trading partners will continue to be negatively affected by the ongoing global economic downturn in 2013. However, unlike in the year before, this time around, the subdued foreign demand will not be offset by the launch of new production capacities in the automotive industry. The impact of net exports on economic growth should remain positive, but to a lesser extent than in 2012. Another growth-reining factor will be the lower government consumption in line with the planned fiscal consolidation. Household consumption is expected to contract slightly due to the unfavourable labour market situation. Despite slow global economic growth and prevailing uncertainty, investment contribution to growth should be only slightly positive owing to the ongoing investment activity in the automotive sector. In the following years, as the economic recovery of Slovakia's trading partners gains momentum, GDP growth should gradually accelerate and reach 3.6% in 2016.

TAB 3 – Forecast of selected indicators of Slovak economy for the budgetary framework for 2014 - 2016

No.	Indicator		Actual		Forecast			
		Unit	2011	2012	2013	2014	2015	2016
1	GDP, current prices	EUR bn.	69,1	71,5	73,8	77,5	81,7	86,3
2	GDP, constant prices	%	3,2	2,0	1,2	2,9	3,3	3,6
3	Final consumption of households and NPISH[4]	%	-0,5	-0,6	-0,1	1,5	2,6	3,2
4	Final consumption of government	%	-4,3	-0,6	-0,9	-1,4	0,4	0,7
5	Gross fixed capital formation	%	14,2	-3,7	2,3	3,3	2,4	2,0
6	Export of goods and services	%	12,7	8,6	3,3	4,9	4,8	4,7
7	Import of goods and services	%	10,1	2,8	3,5	4,1	4,0	4,3
8	Output gap (share of potential output)	%	-0,4	-0,4	-1,4	-0,9	-0,6	0,1
9	Average monthly wage in the economy (real growth)	%	2,2	2,4	2,3	3,5	4,4	4,7
10	Average employment growth, LFS	%	1,5	0,6	-0,5	0,7	1,0	1,0
11	Average employment growth, ESA95	%	1,8	0,1	-0,5	0,5	0,7	0,8
12	Average unemployment rate, LFS	%	13,5	14,0	14,3	13,8	13,0	12,1
13	Average unemployment rate, registered	%	13,2	13,6	14,1	13,5	12,7	12,5
14	Harmonized index of consumer prices (HICP)	%	4,1	3,7	2,4	2,5	2,5	2,3
15	Current account balance (share of GDP)	%	-2,0	2,5	1,2	1,7	2,4	2,8

Source: MF SR

Given the slower pace of economic growth, the unfavourable trends on the labour market which appeared at the end of 2012 are likely to continue also this year. The uncertainties about future developments in the eurozone, along with fiscal consolidation and the expected slow economic growth (1.2%), will hinder employment growth. Employment is likely to rebound in 2014 as GDP growth becomes more robust. The new jobs created in the next years should bring the number of the employed in Slovakia closer to the pre-crisis levels in 2016. The adverse situation in employment during 2013 will automatically be reflected in the unemployment forecast. According to the LFS, the unemployment rate will peak at 14.3% in 2013 and then gradually decline in the years to come. The number of the economically active population is not expected to change any significantly during 2013.

Wages in 2013 are expected to grow at a pace similar to that in the previous year, oscillating around 2.3%. The wage growth will be significantly influenced by the announced reduction in the public sector's wage expenditures (except for the school sector). The average nominal monthly wage is expected to reach 823 EUR, which is 18 EUR more than in 2012. In the years to come, rising labour productivity in the private sector should be gradually reflected in the level of wages which are expected to grow at a faster pace. Real wage in 2013 is not expected to decline thanks to the slower price growth. In 2016, the real wage growth should exceed 2%.

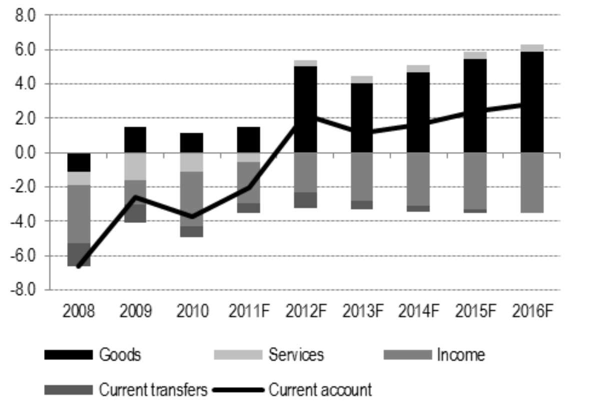
This year's price level increase will be considerably lower than in 2012. Consumer prices are expected to rise 2.4% year-on-year. The main determinants of the slower price growth include the stabilisation of regulated prices and a feeble domestic consumption which curbs net inflation. Regulated prices will be rising only slightly and energy prices will oscillate around the previous year's levels. Compared to 2012, net inflation will slacken under the influence of flat domestic consumption (average increase in 2013 should reach 2.2% YoY). Given the stabilisation and subsequent decline in global food prices in the final quarter of 2012, the food inflation estimate for 2013 has been revised downward to 3.5%. Nonetheless, food prices will be the fastest growing component in the consumer basket and their year-on-year increase may exceed 5% in the first half of the year.

The 2014-2016 outlook is positive and the average growth in consumer prices will be markedly lower than during the past two years. In the years to come, inflation rate should hover around the level estimated for 2013. The negative effect of the net inflation increase, stemming from the projected global recovery, will be offset by slower growth in the prices of food and regulated goods.

[4] In the following text households' consumption denotes consumption of households and non-profit institutions serving households (NPISH).

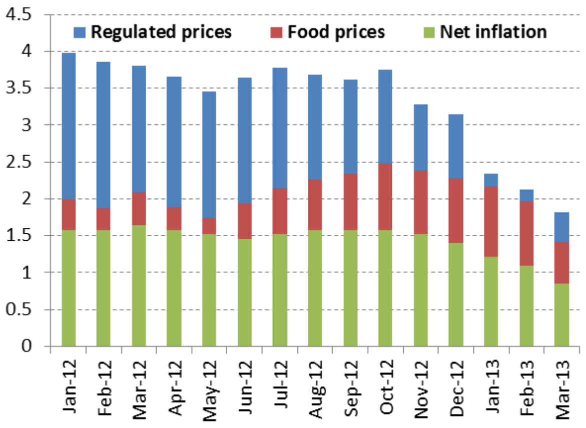
The current account of the balance of payments is expected to drop to 1.2% of GDP, particularly due to slowdown in external demand. After the record increases related to new investments in the automobile sector, the 2013 export of goods will increase only by 5.6% (at current prices) and then slightly accelerate as GDP growth of Slovakia's major trading partners begins to pick up. Likewise, imports in 2013 will slightly decelerate to 6.1%; however, they will still outpace exports in growth terms. In the next years, both imports and exports should accelerate. The trade balance surplus will thus reach 4.1% of GDP in 2013. The contraction of the balance of payments surplus to 1.2% GDP in 2013 will be largely attributable to the expected increase in the balance of income deficit. However, following the 2013 decline, the balance of payments surplus will be rising again.

GRAPH 11- External imbalances - components of the CAB (% of GDP)



Source:NBS, MF SR

GRAPH 12- Contributions to overall growth of CPI (p.p.)



Source: MF SR

Main risks associated with the forecast

The main risks of the forecast relate to the development of the external environment and are currently on the negative side for the most part. The eurozone debt crisis has not yet been resolved and macroeconomic imbalances of its members persist. Notwithstanding the currently stable situation on financial markets, the risk of the situation deteriorating further prevails, with negative repercussions on Slovakia's major trading partners. Positive risks are derived from the favourable development of the lead indicators in Germany (IFO, ZEW).

BOX 1 – How painful is consolidation?

In contrast with monetary policy, there is no broader consensus as to the fiscal policy's impact on the economy. The results of international studies are diverse. The main reason is that fiscal policy influences the dynamics of the economy not only quantitatively, but mainly qualitatively. This is why two consolidations of identical volumes may have differing impacts on GDP dynamics, depending on the structure of the measures taken. Since monetary policy influences growth primarily by one tool (interest rates), the qualitative factor is not that significant. Another problem with the estimation of the fiscal consolidation's impact on GDP dynamics is that it is practically impossible to monitor alternative developments under an unchanged policy scenario. In spite of the uncertainty regarding the parameters and transmission channels, the International Monetary Fund issued the "rule-of-thumb" fiscal multipliers. In general, bigger economies have bigger multipliers, whereas open economies have smaller multipliers. For small and open economies, such as Slovakia, the multipliers are estimated at less than 0.5, while the estimates for big economies span from 0.5 to 1.5 (Spilimbergo, 2009).

The values of these multipliers also differ depending on whether consolidation is taking place on the revenue or expenditure side. A number of studies concur that, on the expenditure side, consolidation through transfers has the least short-term and long-term negative effects. Consolidation through cuts in expenditures on government consumption has a short-term negative effect. The most adverse effect comes with cuts in public investments. On the revenue side, the least adverse short- and long-term effect on growth comes with deficit reductions through consumption and property taxes. On the contrary, increase in taxes on profit and wages has a long-term negative effect. (Autumn Forecast, European Commission, 2010, Cogan, Taylor, Volker, Wieland, Wolters (2012), Kluyev (2012), Hurnik (2004), Elekdag, Epstein, Moreno-Badía (2006))

Given the openness of its economy, the fiscal multipliers for Slovakia are expected to be lower than those applied to bigger and closed economies. All analyses suggest that the multipliers are below 1. **The MF SR estimates show that, compared to consolidation through revenues, consolidation through expenditures entails higher cost through lost growth in the short term. On the other hand, such consolidation is less painful in the medium to long term.** These results generally tally with the general consensus emerging from bibliography. Based on the MF SR estimates, the annual cumulative **revenue multiplier** spans from **0.15 to 0.20**. The **expenditure multiplier** spans from **0.39 to 0.58**.

Estimate intervals for annual cumulative multiplier

Expenditure	0.39 – 0.58
Revenue	0.15 – 0.20

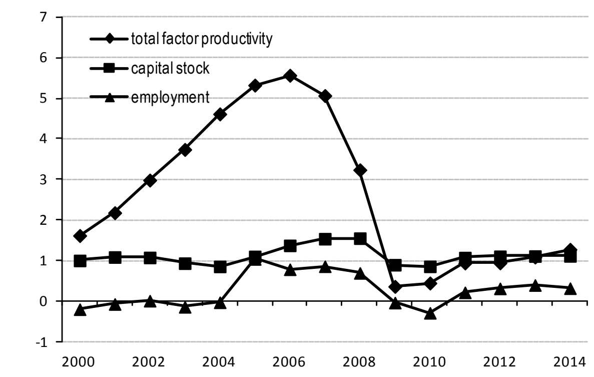
Source: MF SR

Due to the crisis and lingering uncertainties, the current consolidation may be more painful than ever before. The main reason is that the public finance consolidation is taking place simultaneously in a number of countries. Moreover, the possibilities of monetary policy are currently limited. According to the OECD, the fact that consolidation is taking place across several countries simultaneously increases the value of the multiplier by one third. The limited room for monetary policy increases the multiplier by another third. According to the IMF, while fiscal multipliers for the advanced economies hovered typically around 0.5, their current level could have risen to 0.9-1.7. Other studies also concur that the multipliers are likely to be higher than 1 in the current situation (Batini, Callegari, Melina 2012, Auerbach, Gorodnichenko 2012).

II.4. Cyclical development of the economy

According to the MF SR estimates, the growth in potential output in 2012 slowed down very slightly compared to the year before. While the growth in equilibrium employment and factor productivity declined, the contribution of capital stock increased slightly. Potential growth in the following years should accelerate on the back of increases in the total factor productivity and equilibrium employment.

GRAPH 13 – Contributions of production factors to potential growth (p. p.) – MoF approach



TAB 4 – Contributions of production factors to potential growth – MoF approach

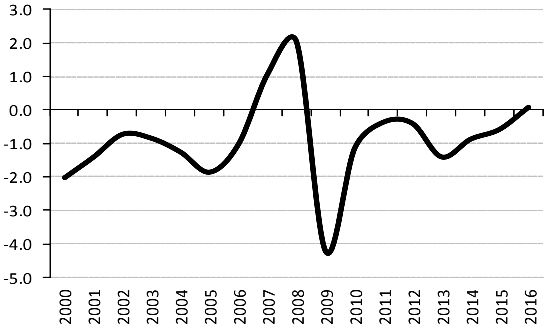
	Pot. GDP (growth, %)	TFP*	Capital stock	Equilibrium employment
2008	5.6	**3.3**	**1.4**	**0.8**
2009	1.3	**0.5**	**0.8**	**0.0**
2010	1.0	**0.6**	**0.6**	**-0.2**
2011	2.3	**1.0**	**0.9**	**0.4**
2012	2.2	**0.9**	**1.1**	**0.2**
2013F	2.3	**0.9**	**1.0**	**0.3**
2014F	2.7	**1.1**	**1.1**	**0.6**
2015F	2.9	**1.2**	**1.1**	**0.6**
2016F	3.0	**1.3**	**1.1**	**0.6**

** total factor productivity*

Source: MF SR

In 2012, GDP growth decelerated and the economy grew at a slightly slower pace than the estimated potential output. However, the output gap remained at -0.4% of potential GDP, exactly as in 2011. However, the 2013 slowdown caused by a slack external demand will widen the output gap again to 1.4% of potential GDP. From 2014 onwards, real GDP will be growing at a considerably faster pace than potential output, closing the output gap again in 2016 (Graphs 13 and 14).

GRAPH 14 – Output gap (% potential GDP) - MoF approach



TAB 5 – Output gap – MoF approach

	GDP*) (real growth, %)	Potential GDP (growth, %)	Output gap (% pot. GDP)
2008	6.6	5.6	**2.0**
2009	-4.9	1.3	**-4.2**
2010	4.4	1.0	**-1.2**
2011	3.2	2.3	**-0.4**
2012	2.0	2.2	**-0.4**
2013F	1.2	2.3	**-1.4**
2014F	2.9	2.7	**-0.9**
2015F	3.3	2.9	**-0.6**
2016F	3.6	3.0	**0.1**

**) Output gap is calcuated based on GDP adjusted for cigarette stockpiling and other one-off effects.* *Source: MF SR*

The potential output estimates prepared by the MF SR differ, in certain regards, from the Commission's estimates prepared under the common methodology. Since the Commission's estimates are decisive for the purpose of evaluating the development of the general government's structural balance, the following part also contains the values of those estimates. Given the nature and purpose of this document, the structural balance calculation in the following parts is based on the Commission's approach.

BOX 2 – Methodological differences in the potential output calculation (COM vs. MF SR)

The differences in the methodologies used by the Commission and MF SR apply to almost all components of the calculation, even though the basic method is identical. Both institutions calculate potential output using the Cobb-Douglas production function. But while the MF SR calculates potential output based on quarterly data, the Commission uses yearly data.

Another difference lies in the differing ratios of production factors. The Commission uses the same ratios for all new MS – 0.63 for labour elasticity and 0.37 for capital elasticity. On the other hand, the MF SR derives the factor ratios from national accounts – labour as the share of employee compensations (without sole-traders) in GDP at 0.43 and capital, analogically, at 0.57 (average values for 1995-2010).

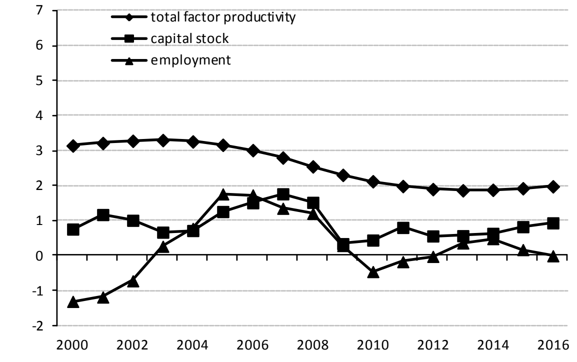
As regards capital stock, the main difference lies in the initial value and depreciation rate. For all new Member States (except for the Czech Republic) the Commission estimated the 1995 capital stock as double GDP and applies a common depreciation rate of 5%. The MF SR uses the real estimate of capital stock from 1999 by the Statistical Office and the depreciation rate is taken from annual national accounts.

To estimate equilibrium employment, both institutions base themselves on the working-age population using the trend of the participation rate, NAIRU and the hours worked trend. However, the difference occurs on the input side – the MF SR uses population aged 15 and more, while the Commission population aged 15 to 64.

The difference in factor productivity (TFP) lies mainly in historical data. The MF SR increases the potential output in 2005-2008 to reflect structural changes in the economy, which the Commission's common method cannot capture. Nevertheless, the excessively high output gap in 2007-2008, based on the Commission's methodology, is not confirmed by other indicators – balance of the current account, net inflation, and unit labour cost.

Under the latest Commission's estimates (February 2013), the potential output growth in 2012 decelerated slightly to 2.5%. While the contributions of factor productivity and capital stock slightly declined, the contribution of labour to potential output slightly increased. The growth in potential output is expected to reach about 3% in 2014 and remain at that level until the end of the forecast period (Graphs 15 and 16).

GRAPH 15 – Contributions of production factors to potential growth (p. p.) – COM approach



TAB 6 – Contributions of production factors to potential growth – COM approach

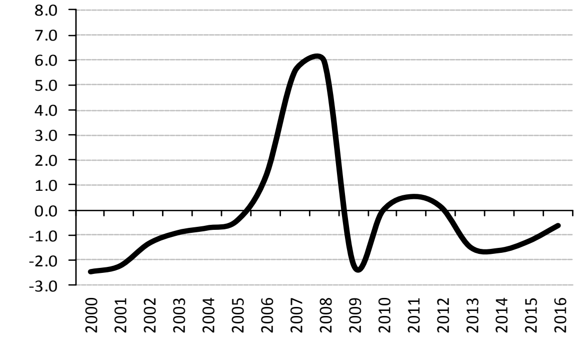
	Pot. GDP (growth, %)	TFP*	Capital stock	Equilibrium employment
2008	5.4	**2.5**	**1.5**	**1.2**
2009	3.0	**2.3**	**0.3**	**0.3**
2010	2.1	**2.1**	**0.4**	**-0.5**
2011	2.6	**2.0**	**0.8**	**-0.2**
2012	2.5	**1.9**	**0.6**	**0.0**
2013F	2.8	**1.9**	**0.6**	**0.4**
2014F	3.0	**1.9**	**0.6**	**0.5**
2015F	3.0	**1.9**	**0.8**	**0.2**
2016F	2.9	**2.0**	**0.9**	**0.0**

** total factor productivity*

Source: MF SR

In this case, output gap was calculated using the latest Commission's estimate for potential output and the real GDP growth forecast by the MF SR[5]. The 2012 slowdown in GDP growth narrowed the positive output gap; its further slowdown in 2013, due to deterioration in the external environment, will widen the negative output gap up to -1.5%. The next year's growth acceleration will not be sufficient to catch up with the potential output growth, which means that the output gap will slightly widen. Although it will begin to narrow on the back of higher GDP growth in 2015, the gap will not close even by 2016.

GRAPH 16 – Output gap (% potential GDP) – COM approach



TAB 7 – Output gap – COM approach

	GDP*) (real growth, %)	Potential GDP (growth, %)	Output gap (% pot. GDP)
2008	6.6	5.4	**6.0**
2009	-4.9	3.0	**-2.2**
2010	4.4	2.1	**0.0**
2011	3.2	2.6	**0.5**
2012	2.0	2.5	**0.1**
2013F	1.2	2.8	**-1.5**
2014F	2.9	3.0	**-1.6**
2015F	3.3	3.0	**-1.2**
2016F	3.6	2.9	**-0.6**

**) Output gap is calcuated based on GDP adjusted for cigarette stockpiling and other one-off effects.*

Source: MF SR

II.5. Comparison of forecasts by the Ministry of Finance and other institutions

The following table compares a set of selected macroeconomic indicators for Slovakia as forecast by selected national and international institutions. Compared with the forecasts published in Q4 2012 (OECD and MMF), the forecasts published this year (IFP, EC, NBS) point at a slower GDP growth for Slovakia in 2013-2014. This is mainly due to the more negative outlook for the external environment (compared with assumptions from autumn 2012) which will have a negative impact on investments and export performance of the Slovak economy in the beginning of the year. The MF SR forecast is in line with the Commission's Winter Forecast from February 2013.

[5] This is because the latest Commission's forecast (February 2013) covers only period until 2014.

TAB 8 – Comparison of MoF and other institutions' forecasts

	Year 2013	Year 2014	Year 2015
	Real GDP growth (%)		
MF SR (Feb 2012)	**1.2**	**2.9**	**3.3**
NBS	0.7	2.8	3.8
EC	1.1	2.9	-
OECD	2.0	3.4	-
IMF	2.8	-	-
	HICP (%)		
MF SR	**2.4**	**2.5**	**2.5**
NBS	1.9	1.6	1.9
EC	1.9	2.0	-
OECD	2.5	2.4	-
IMF	2.3	-	-
	Current account (% HDP)		
MF SR	**1.2**	**1.7**	**2.4**
NBS	2.9	3.8	4.6
EC	0.8	2.0	-
OECD	1.8	3.1	-
IMF	0.3	-	-

Source: MF SR (January 2013), NBS (March 2013), EC (February 2013), OECD (November 2012) and IMF (October 2012)

III. PUBLIC FINANCE POSITION

After accession to the euro area and monetary policy integration, the fiscal and structural policies became the main instruments available to counter the impacts of internal and external shocks on the economy. The global economic downturn deteriorated the fiscal position of the Slovak economy and, consequently, necessitated a major fiscal consolidation effort. A credible medium-term consolidation plan is a key prerequisite for the stabilisation of the general government debt, which is indispensible to ensuring long-term sustainability of public finances.

III.1. Policy strategy and objectives

The main objective of the fiscal policy strategy is to ensure efficient public finances which are sustainable in the long-term and which support sustainable economic development and a better quality of life in the context of population ageing, with due account of contingent liabilities. This objective is laid down in the constitutional Fiscal Responsibility Act. [6]

Assuming that the economy will develop in line with **the baseline scenario presented in this programme, the main short-term objective is to reduce general government deficit to 2.9% of GDP in 2013 in a sustainable manner** and thus comply with the requirements of the excessive deficit procedure. However, in order to attain long-term sustainability of public finances, fiscal consolidation must continue also beyond 2013 if Slovakia is to meet its MTO, i.e. **structural deficit of 0.5% of GDP**.

In the years to come, the deficit is expected to diminish gradually in line with the provisions of the Stability and Growth Pact, respecting the constraints given by the national fiscal rules. The target deficit values have therefore been set at 2.6% of GDP in 2014, 2.0% of GDP in 2015 and 1.3% of GDP in 2016.

The 2014 and 2015 targets for general government balance differ from the previous Stability Programme, particularly due to the worse-than-expected macroeconomic development. Nevertheless, these targets are achievable only through additional consolidation effort going beyond the reference value set by the EU rules at 0.5% of GDP annually. By the same token, the envisaged increase in expenditures in the period from 2013 to 2016 will comply with the reference rate set under the preventive arm of the Stability and Growth Pact.

The targets for 2014 to 2016 have been set in this way to respect, among other things, the constraints of the national fiscal rules, particularly the general government debt limits enshrined in the Fiscal Responsibility Act. If the budget targets for 2014 and 2015 assumed a consolidation effort at the SGP reference value of only 0.5% GDP annually, the debt would overshoot 57% of GDP in 2015. This, under the above-mentioned act, would oblige the Government to propose a balanced budget in 2017, which would entail major fiscal restrictions. In order to avoid such steep fluctuations in fiscal policy, the necessary additional consolidation effort will spread over 2014 and 2015. Structural balance should improve by 0.8% of GDP in 2014 and by 0.9% of GDP the year after.

The Stability Programme also contains a calendar of convergence towards the MTO[7]. After 2016, the annual consolidation effort is planned at 0.5% GDP in order to **meet the MTO in 2018**. This will be one year earlier compared to a situation where the overall annual consolidation effort would reach merely the reference value.

Due to the ongoing fiscal consolidation and the externally driven negative output gap (which will gradually narrow), the Government's fiscal policy will have a restrictive and pro-cyclical impact during 2013-2016. The only exception will be 2013 when increased drawing of EU funds may offset the restrictive impact of consolidation and when the expansionary impact on aggregate demand should reach 1.0% of GDP. In the following years, the **restrictive impact of fiscal policy on aggregate demand will reach an average level of 1.5% of GDP annually**.

[6] Constitutional Act No. 493/2011 on Fiscal Responsibility

[7] The tables with the data necessary to assess the extent to which the calendar of convergence towards the MTO is realistic are presented in Annex 2.

TAB 9 – Main fiscal indicators in the year 2012-2018 (ESA95, % of GDP)

	2012	2013E	2014	2015	2016	2017*	2018*
1. General government budget balance[8]	**-4.3**	**-2.9**	**-2.6**	**-2.0**	**-1.3**	**-0.7**	**-0.5**
2. Cyclical component	0.0	-0.5	-0.5	-0.4	-0.2	-0.1	0.0
3. One-off effects	0.1	0.8	0.4	0.0	0.0	0.0	0.0
4. Cyclicaly adjusted budget balance without one-off effects (MTO) (1-2-3)	**-4.5**	**-3.3**	**-2.5**	**-1.6**	**-1.1**	**-0.6**	**-0.5**
5. Consolidation effort (y-o-y change of 4)**	**0.2**	**1.2**	**0.8**	**0.9**	**0.5**	**0.5**	**0.1**
6. Expenditure growth rate net of discretionary revenue measures (%)	**-**	**-7.7**	**-0.8**	**-0.1**	**-0.6**	**0.3**	**2.3**
7. Reference rate of expenditure growth (%)	**-**	**1.8**	**1.5**	**1.5**	**1.5**	**-**	**-**
8. Gross general government debt	**52.1**	**54.8**	**56.3**	**56.7**	**55.9**	**53.7**	**51.6**
p.m. Budget balance with y-o-y consolidation effort of 0.5 % of GDP annually	*-4.3*	*-2.9*	*-2.9*	*-2.7*	*-2.0*	*-1.3*	*-0.8*

*Note: * The estimate for the budget balance in 2017 is based on a mechanical computation considering the structural deficit reduction of 0.5% of GDP annually and reaching the MTO of 0.5% of GDP in 2018. A simplified computation is applied to the gross debt calculation, which assumes a direct transmission channel of deficit onto debt (ie. zero stock-flow adjustment).* *** (+) restriction, (-) expansion*

E –estimate, 2014 – 2016 – budgetary framework *Source: MF SR*

The consolidation of public finances progresses in line with the assumptions of the Government. General government deficit in 2012 reached 4.3% of GDP, which is 0.3 p.p. better compared with the budgeted deficit of 4.6% of GDP. The main negative factors, particularly the lower-than-expected revenues from taxes and social contributions as a consequence of a less favourable macroeconomic development, as well as the assumption of hospital debts, were offset by the legislative changes in the area of taxes and social contributions adopted as part of the 2013 consolidation package, whose impact was felt already in the second half of 2012, as well as other positive factors, including better fiscal performance of municipalities and self-governing regions and lower expenditures in the health and social insurance system. The general government gross debt reached 52.1% of GDP at the end of 2012.

The meeting of the target value for the 2013 general government deficit of 2.9% of GDP required, within the framework of the approved general government budget as opposed to the no-policy-change scenario, the adoption of measures amounting to 3.3% of GDP. The externally-driven macroeconomic development increased the consolidation need after the adoption of the budget, but with the additional consolidation measures taken, the target is likely to be met. The lower current estimate of revenues from taxes and social contributions, mainly due to the worse macroeconomic outlook, is offset by expected positive development in non-tax revenues, use of the budget reserve, and the adoption of additional measures on the expenditure side of the budget.

Assuming that the Government does not adopt any additional measures and the general government balance will only be influenced by macroeconomic development – i.e. under the no-policy-change (NPC) scenario – the 2014 general government deficit would rise by 0.7 p.p. year-on-year to 3.6% of GDP, mainly as a consequence of declining tax revenues. It would remain at the same level in 2015 and fall to 3.1% of GDP in 2016.

The table below illustrates the need for consolidation measures. In order to meet the 2.6-percent target for general government deficit, the 2014 consolidation measures will have to reach 1.0% of GDP, of which 0.8% GDP should be measures with permanent impact (assuming that the consolidation effort goes as planned). In 2015, additional consolidation measures should amount to 1.0% of GDP. **Provided that they are permanent, no additional consolidation measures need to be adopted in 2016.**

TAB 10 - Necessary fiscal measures compared to unchanged policies scenario (ESA95, % of GDP)

	2014	2015	2016
1. Primary GG balance – GG budgetary framework 2014–2016 – target	-0.7	0.0	0.8
2. Primary GG balance – GG budgetary framework 2014–2016 – without all consolidation measures	-1.4	-1.2	-0.3

[8] ESA 95 classifies this item as net lending / net borrowing.

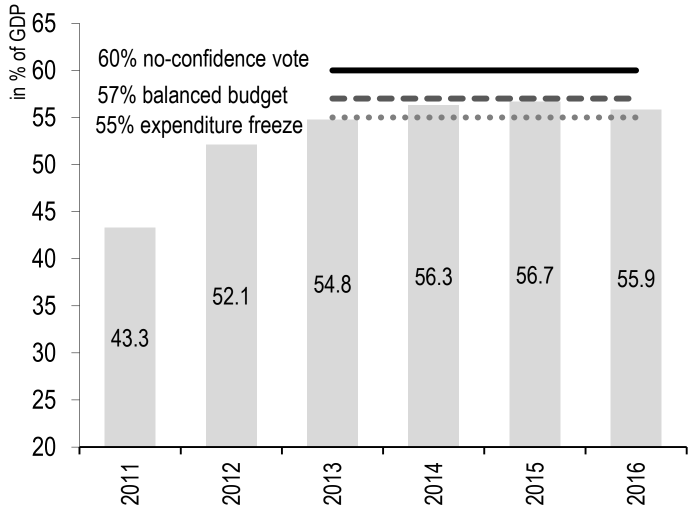
3. Primary GG balance – NPC scenario	-1.7	-1.7	-1.0
4. Difference (1-3)	1.0	1.6	1.8
- consolidation need with a permanent effect against NPC scenario (net of one-off measures)*	0.8	1.8	1.8
- y-o-y change (consolidation need for addition permanent measures)	0.8	1.0	0.0
5. Difference (1-2)	**0.7**	**1.2**	**1.1**
- y-o-y change (consolidation need for additional measures)	**0.7**	**0.5**	**-0.1**
Difference (in EUR mill.)	566	969	947
- y-o-y change (consolidation need for additional measures)	566	403	-22
*p.m. * One-off measures (difference with NPC scenario)*	0.2	-0.2	0.0

Source: MF SR

Some of the necessary measures have already been incorporated in the General Government Budget Framework for 2014–2016. The measures include, in particular, reduced wage expenditures in public administration and reduced subsidies, as well as increased one-off non-tax revenues. **In addition to the aforementioned measures, additional measures amounting to 0.7% of GDP in 2014 and 0.5% of GDP in 2015 have to be taken in order to meet the 2014 fiscal target. At the same time, in order to achieve the planned level of consolidation effort and structural balance, the measures taken need to be of a permanent nature rather than one-offs. Concrete measures will be specified in the proposed General Government Budget for 2014 to 2016.**

The attainment of these fiscal targets is a prerequisite for stabilising the general government debt to GDP ratio. The gross debt of the general government will increase from 52.1% of GDP at the end of 2012 and culminate at 56.7% of GDP at the end of 2015 (of which 2.5 p.p. are Slovakia's commitments under the European Financial Stability Facility assistance to Greece, Portugal and Ireland, and 0.8 p.p. represent contributions to the European Stability Mechanism). In 2016, the debt will fall below 56% of GDP. It means that throughout the entire period **the general government debt will remain below the reference value set by the SGP, as well as below the debt brake upper limit**. **However, such a development will trigger certain sanction mechanisms under the constitutional Fiscal Responsibility Act** (described in detail in Box 3).

GRAPH 17 – Gross general government debt forecast (% of GDP)



Source: MF SR

The debt brake represents an important element of the new fiscal institutional framework laid down in the constitutional Fiscal Responsibility Act. Yet, its linking to the gross debt indicator may be problematic for two reasons. The gross debt rule does not take into account the actual phase of the economic cycle and may thus be causing stronger than desirable fiscal restriction, as confirmed by the targets set for 2014 and 2015. At the same time, it does not take into account development of the general government's assets, for example the currently higher cash reserve which is needed because of uncertainties on financial markets.

BOX 3 - Application of the Fiscal Responsibility Act provisions under the current debt forecast

General government gross debt reached 52.1% of GDP at the end of 2012. This means that the MF SR will send to the Parliament a written explanation of the debt level, along with the measures for its reduction.

At the end of 2013, the debt is expected to reach 54.8% of GDP, which is above the 53-% debt limit. Once the value has been officially published in April 2014, the Government will submit to the Parliament the measures it proposes to reduce the debt; simultaneously, the salaries of Cabinet members will be reduced to the previous year's level.

The limit of 55% of GDP is likely to be exceeded at the end of 2014 when the debt is estimated to reach 56.3% GDP, which will be published probably in April 2015. It means that, in addition to the procedure triggered when the 53-% debt limit is overshot, the MF SR will – within one month of the month in which the debt level is published – cut 3% of total government expenditures less the debt service expenditures, EU funds and co-financing, transfer to the EU budget, transfers to the Social Insurance Agency, and expenditures on the elimination of damages caused by natural disasters. At the same time, the Government may not submit to the Parliament any budget proposal for 2016 which would contain a year-on-year nominal increase in general government expenditures (apart from expenditures on debt service, EU funds and co-financing, transfers to the EU budget, and expenditures on the elimination of damages caused by natural disasters); municipalities will be obliged to approve their budgets with expenditures limited by the previous year's level (apart from EU funds and co-financing and expenditures for the elimination of damages caused by natural disasters). In this situation, no funds from the reserve of the Prime Minister and the reserve of the Government may be disbursed.

The debt level should remain about 55% of GDP also in the following years, which would oblige the Government to propose budgets without year-on-year nominal increases in expenditures until the debt has fallen below that level (the obligation to cut expenditures will not apply).

The Stability Programme is based on the macroeconomic and tax revenue forecasts until 2016 from January and February 2013. The macroeconomic scenario and the forecast of tax revenues are subject to expert scrutiny by committees comprised of domestic experts from the public and private sectors, with deadlines for the publication of these forecasts stipulated in the Fiscal Responsibility Act. The Stability Programme also presents the estimates of selected data after 2016 (calendar of convergence towards the MTO). The post-2016 estimates by the MF SR have not been subject to scrutiny by the above-mentioned committees.

III.2. General government balance in 2012 and its impact on the 2013 budget

A thorough assessment of the current state of public finances is a key prerequisite for setting adequate and realistic objectives in the general government budget. This sub-chapter contains basic information of the general government balance development in 2012. Furthermore, it describes the measures adopted in the course of 2012 with the aim of meeting the 2013 consolidation target and laying the groundwork for further fiscal consolidation. Up-to-date information on developments in 2013 are provided at the end of this sub-chapter.

III.2.1. General government balance in 2012

Under the General Government Budget for 2012-2014, the Government's main fiscal target for 2012 was defined as reaching the general government deficit of 4.6% of GDP. The actual deficit reached 4.3% of GDP, which means an improvement by 0.3% of GDP compared to the budget.

TAB 10 – General government budget balance in 2012 (ESA 95)

	EUR mill.	% GDP
1. General government budget balance - budget	**-3,324**	**-4.64**
Tax and social contributions shortfall	-393	-0.55
- negative macroeconomic impact	-682	-0.95
- consolidation measures (2013 consolidation package)	288	0.40
Shortfall in state budget one-off revenues (licences, digital dividend)	-64	-0.09

Transfers related to EU budget	365	0.51
- savings in co-financing	221	0.31
- savings in operational programme infrastructure	120	0.17
- transfer to EU budget	24	0.03
Municipalities	241	0.34
- non-tax revenues of municipalicites (self-governing regions)	190	0.27
- expenditures of self-governing regions	51	0.07
Healthcare	58	0.08
- savings in health insurance companies	138	0.19
- assumption of health care providers debt	-80	-0.11
Savings in Social Insurance Agency expenditures	69	0.10
Other changes	-60	-0.08
2. General government budget balance	**-3,107**	**-4.35**
p.m. impact of updated nominal GDP (2-1)	*7,842*	*0.01*

Note: (+) indicated improvement and (-) deterioration of the general government balance *Source: MF SR*

Compared to the budget, **government revenues from taxes and social contributions**[7] were 393 million EUR lower (0.6% of GDP). The adverse macroeconomic impacts and shortfalls in tax revenues were mitigated by a number of legislative changes enacted in advance as part of the 2013 consolidation package (reduced rate of contributions to the fully-funded pillar of the pension system and a possibility to opt-out from the fully-funded pillar, increase in the special levy and introduction of an extraordinary levy in the banking sector, and introduction of a special levy on business in regulated industries). Additional revenue from these measures is estimated at EUR 288 million (0.4% of GDP). On a permanent basis, the revenue increase represented EUR 171 million.

This means that the shortfall in revenues from taxes and social contributions, net of the effects of the above-mentioned legislative changes, reached EUR 682 million (1.0% of GDP). The shortfall is mainly attributable to lower revenues from value added tax (down EUR 389 million, i.e., 0.5% of GDP), corporate income tax (lower by EUR 171 million, i.e. 0.2% of GDP) and excise tax (lower by EUR 99 million, i.e. 0.1% of GDP).

The shortfall in **one-off non-tax revenues** reached EUR 64 million (0.1% of GDP). The budgeted revenue from the extension of licences to telecom operators (EUR 24 million) was not realised because the fees had been collected already at the end of 2011. The same is true for the budgeted revenue from the digital dividend (EUR 40 million) because no sale of available frequencies took place in the course of 2012.

Transactions with the EU budget have had a positive impact on the balance in the amount of EUR 365 million (0.5% of GDP). With respect to the lower drawing of EU funds, only at 65% of the budget estimate, the volume of expenditures for co-financing decreased by EUR 221 million. This consequently reduced capital expenditures above the co-financing framework under the operational programmeinfrastructure by EUR 120 million. At the same time, transfers to the EU budget were lower by EUR 24 million.

Expenditure cuts in **municipalities and self-governing regions**[8] reached EUR 51 million, while their non-tax revenues from transfers (mainly revenues from grants and administrative fees) were EUR 190 million above the budgeted level.

The **health insurance expenditures** were EUR 138 million below the budget (0.2% of GDP). However, this saving was offset by including the **payment of a liability to shareholders** (EUR 50 million) and a **private loan principal repayment** (EUR 25.8 million) into general government expenditures. At the same time, the Government **assumed the debts of healthcare provides** in the total amount of EUR 130 million. Since the

[7] Only contributions from from the economically active population and outstanding insurance premiums are compared because only these have an impact on the general government balance.

[8] The development ot tax revenues of local governments is captured under the heading 'tax revenues of general government'.

budgeted level of the debt assumption was EUR 50 million, the resulting negative impact for the budget amounted to EUR 80 million (0.1% of GDP).

Expenditures of **the Social Insurance Agency** were EUR 69 million below the budget (0.1% of GDP) due to lower claims for early retirement pensions. The reduction in expenditures was due to the lower number and lower average amount of the newly granted early retirement pensions compared with the assumptions used in the budget.

III.2.2. General government budget for 2013 and approved measures

The 2013 general government budget set the target value of general government deficit at 2.9% of GDP. The budget and the proposed consolidation measures were prepared based on the development of public finances envisaged under the no-policy-change scenario (the approach applied in developing the no-policy-change scenario was described in the 2012-2015 Stability Programme). Under that scenario, general government deficit would have reached 6.3% of GDP in 2013. The difference between the level under the no-policy-change scenario and the target value represented 3.3% of GDP at the time of the budget preparation, which set the scope of the measures necessary to achieve the target.

TAB 11 – Measures included in the GG budget for 2013 (ESA 95, against NPC scenario*)

	EUR mill.	% of GDP
1. Increasing and unifying maximum assessment bases of social security contributions	126	0.2
2. Increase in social security contributions for self-employed and other related changes	69	0.1
3. Health and social insurance contributions for casual temporary agreement workers	132	0.2
4. Changes in the fully-funded pillar	737	1.0
5. Extension of a special levy in the banking sector	85	0.1
6. Temporary levy on enterprises in regulated sector	77	0.1
7. Changes in income tax rates	351	0.5
8. Retaining of licence fees for public-service broadcasting of Slovak Radio and Television	74	0.1
9. Other tax changes	69	0.1
10. Grants to municipalities and self-governing regions	-134	-0.2
11. Revenues from the digital dividend	130	0.2
12. Reduction in wage expenditures in the state budget	91	0.1
13. Increase in wages in the regional school system	-68	-0.1
14. Reduction in budget expenditures on goods and services	230	0.3
15. Other changes in state budget (current transfers and capital expenditures)	143	0.2
16. Reduced expenditures of municipalities and self-governing regions	427	0.6
17. Increase in healthcare expenditures linked to increase in revenues	-137	-0.2
18. New financing system of strategic oil reserves	198	0.3
19. Changes in expenditures of other general government entities	101	0.1
20. Reserve covering potential revenue shortfall in connection with opt-out from the fully-funded pillar	-229	-0.3
Total	**2,470**	**3.3**
p.m. Nominal GDP in EUR mill.	73,826	

Note : * Based on a NPC scenario prepared in the course of finalizing the GG budget in november 2012, ie. the base for NPC was the actual estimate of the GG budget balance for 2012.

Source: MF SR

1. Increase and unification of the maximum assessment base

As of 1 January 2013, the maximum assessment bases for the calculation of social and health insurance contributions (except for accident insurance, which is not capped) have been harmonised and raised to five times the average wage. The increase in the maximum assessment base will have no effect on the amount of payable benefits.

2. Increased in social contributions for self-employed plus other related changes

As of 1 January 2013, the minimum assessment base for the self-employed has been raised from 44.2% to 50% of the average monthly wage. The assessment base for those paying health insurance voluntarily has also increased.

3. Health and social insurance contributions for temporary agreement workers

As of 1 January 2013, temporary agreement workers (hired to perform specific work) are subject to the same contribution requirements as regular employees. Exceptions from this rule apply only to the students of secondary and tertiary schools earning less than the specified monthly ceiling (EUR 66 below 18 years of age and EUR 155 above 18 years of age) and to certain groups of pensioners, particularly those entitled to disability pension. The contribution rates for these categories of workers are reduced.

4. Changes in the fully-funded pillar

Significant changes occurred in the fully-funded pillar where, as of 1 September 2012, the rate of contributions has been cut from 9% to 4%. Starting in 2017, the rate of contributions to the fully-funded pillar will be increasing by 0.25 p.p. until it reaches 6% in 2024. The fully-funded pillar was ‘opened’ from 1 September 2012 to 31 January 2013 for those who wished to opt-out from the scheme. As a compensation for the reduced contribution rate, those in fully-funded pillar may contribute to the scheme privately. These private contributions are subject to a more favourable tax regime up to 2% of the individual’s tax base, with a cap set at 2% of the maximum assessment base.

5. Extension of a special levy in the banking sector

As of 1 September 2012, the base for the calculation of the special banking levy was extended to also include the value of protected deposits (exempt before). The rate of the levy will be gradually reduced depending on the amount of the accumulated levy payments and the total assets in the banking sector. In the first step (when the total amount of the levy collected exceeds EUR 500 million), the rate will be reduced from 0.4% to 0.2% and, in the second step (when the total amount of the levy collected exceeds EUR 750 million), to 0.1%. The rate may be also be reduced to zero provided that the total amount of the levy collected exceeds EUR 750 million and, at the same time, it reaches 1.45% of total assets in the Slovak banking sector. The law also envisages a situation where the total amount of the levy collected subsequently falls below 1.45% of total assets in the Slovak banking sector – in such a case, the levy will be raised from 0% to 0.05%.

6. Introduction of a temporary levy on business in regulated industries

A temporary levy on business in regulated industries has been introduced as of 1 October 2012. It applies to those companies whose revenues from a regulated activity reach at least 50% of total revenues and the profit exceeds EUR 3 million. This temporary measure applies in 2012 and 2013 only.

7. Changes in income tax rates

A higher rate (25%) of personal income tax has been introduced with effect from 1 January 2013. This tax rate will apply in 2013 on gross monthly income above approximately 3,311 EUR. The corporate income tax rate has been raised from 19% to 23%.

8. Retaining licence fees for public-service broadcasting of Slovak Radio and Television

The Slovak Radio and Television will continue to be financed through licence fees payable for public-service broadcasting. The change adopted in 2011 envisaged full funding of the public radio and television from the state budget. However, the original system of licence fees has been maintained as part of the consolidation package.

9. Other tax changes

The other changes include, in particular, an increase in the minimum rate of excise tax on cigarettes and other tax rates applicable to tobacco products. In the area of administrative fees, the car registration fee and several administrative and court fees have been raised. The measure also includes increased levies on lotteries and changes in the taxation of gambling. Other changes include the introduction of a special income tax rate for selected constitutional officials at 5% on top of the standard rate, restrictions concerning the basic tax allowance for the spouse, exemptions of certain types of in-kind income, exemption of income from the sale of assets by municipalities and self-governing regions, and changes in the taxation of bonds.

10. Grants to municipalities and self-governing regions

The general government's revenues also include grants received by municipalities and self-governing regions (from foreign sources other than EU funds), but they are not taken into account in the budgeting process. All grants actually received have thus a positive impact on the budget.

11. Revenues from the digital dividend

The budget assumed higher non-tax revenues also from the digital dividend, i.e., sale of the frequencies which became available after changeover from the analogue to digital broadcasting (EUR 130 million). This is a one-off revenue measure of the state budget.

12. Reduction in wage expenditures in the state budget

Compared with 2012, the 5% reduction in wage expenditures in the state budget affects most civil servants. The cut does not affect employees of the regional school system and selected employees of universities, employees of the Financial Authority of the SR, and constitutional officials. The salaries of constitutional officials and civil servants in public functions have been frozen at the 2012 level.

13. Increase in wages in the regional school system

As of 1 January 2013 the Government approved a 5-% increase in the tariff salaries for teaching and specialised staff, as well as for non-teaching staff at regional schools and selected staff at universities.

14. Reduction in budget expenditures on goods and services

The budget expenditures on goods and services have been cut by 10% across the board, compared with the level of the 2012 approved budget.

15. Other changes in state budget

Other changes include, in particular, cuts in capital expenditures and, to a lesser degree, also of current transfers from the state budget.

16. Reduced expenditures of municipalities and self-governing regions

The Government, the Association of Towns and Villages of Slovakia (ZMOS) and the Association of Self-governing Regions (SK8) signed a Memorandum of Cooperation in Implementing Budgetary Policy Ensuring Financial Stability of the Public Sector in 2013. Under the memorandum, municipalities and self-governing regions will reduce their 2013 expenditures compared with the 2012 budget, namely 5% for wage expenditures and 10% for expenditures on goods and services. This reduction applies to towns and villages with more than 2,000 inhabitants. The expenditures of villages with less than 2,000 inhabitants should not exceed the 2012 budget levels.

17. Increase in healthcare expenditures linked to increase in revenues

The changes introduced by an amendment to the Social Insurance Act (mainly the increase in maximum assessment bases) should increase the revenues of health insurance companies by EUR 137 million. The budget assumes that these additional revenues will be accompanied by higher expenditures, i.e. the overall impact on the balance will be neutral.

18. New financing system of strategic oil reserves

A new system of management of the strategic oil reserves of oil and oil products should be gradually phased in. This would transfer the activities currently performed by the State Material Reserves of Slovak Republic to an entity outside the general government sector. The positive impacts compared to the no-policy-change scenario are based on the assumption of the sale of the accumulated oil stock to that new entity, plus a reduction in expenditures, because Council Directive 2009/119 introduced a new method for the calculation of strategic oil reserves, which would entail an obligation to increase existing stocks above their current level.

19. Changes in expenditures of other general government entities

These expenditure reductions apply to "other" entities of the general government, mainly the Environmental Fund, Social Insurance Agency and organisations partly funded from the state budget.

20. Reserve in connection with opt-out from the fully-funded pillar

The budget contained a reserve designed to cover a potential shortfall in revenues connected with opening of the fully-funded pillar. It was created mainly due to a degree of uncertainty about the number of those who chose to opt out from the fully-funded pillar and opt solely for the pay-as-you-go scheme between 2012 and 2013. Since the actual shortfall was smaller than projected, the reserve was used to offset lower government revenues as a consequence of worse macroeconomic development.

III.2.3. Developments in 2013

The 2013 development has been estimated on the basis of updated macroeconomic and tax revenue forecasts and development of other general government components, including the measures already taken. Based on the above, the target set by the Government for the **general government deficit at 2.9% of GDP should be met**. However, there are certain risks associated with the budget execution which require rigorous monitoring and, if necessary, reactions by the Government. **Given the importance of this target, the Government is commited to take, when and as needed, additional measures in the course of the year to ensure that the 2013 target is met.**

TAB 12 – Development in 2013 (ESA 95)

	EUR mill.	% of GDP
1. General government balance - budget	**-2,187**	**-2.94**
- Downward revision of tax revenues	-361	-0.49
- Actual effect of the opening of the fully-funded pillar (additional revenues)	4	0.01
- Higher dividends from SPP	60	0.08
- Higher dividends from SEPS	9	0.01
- Dissolution of the reserve intended for the opening of the fully-funded pillar	229	0.31
- Expenditure related compensation due to a cash shortfall of social contributions in public healthcare	39	0.05
- Savings on expenditures on operational proramme infrastructure	42	0.06
- Other expenditure cuts	10	0.01
- Expenditures on road maintenance	-16	-0.02
2. General government balance - current estimate	**-2,170**	**-2.94**
p.m. change in budget balance due to downward revision of nominal GDP estimate (2-1)	*16*	*0.02*

Note: (+) positive effect and (-) negative effect on GG budget *Source: MF SR*

The updated macroeconomic and tax revenue forecasts have led to a **downward revision of the tax revenue estimate by EUR 361 million**[9] (compared with the budget). This shortfall was partly offset by the **actual impact on public finances of the opening of the fully-funded pillar**[10]**,** namely through additional revenue of EUR 4 million. At the same time, given the **downward revision of the nominal GDP estimate,** the identical target for the general government deficit ratio to GDP required the adoption of additional measures worth EUR 16 million. All these changes in aggregate **require the adoption of measures in the order of EUR 373 million**.

In the case of **non-tax revenues,** the **positive impact is expected to reach EUR 69 million**. The budget should also benefit from **higher revenues from dividends** from corporations with state capital participation (SPP and SEPS) in the **total amount of EUR 69 million**.

The remaining savings of EUR 304 million relate to the expenditure side of the budget. These include:

[9] The negative impact of the 2013 consolidation package update, mainly in connection with macroeconomic developments, represents €92m of the amount.

[10] The impact of the opening of the fully-funded pillar of the pension system is included in the tax revenue estimate. However, at the time of the forcast update, the actual figures were not available, i.e. the additional revenue of €4m represents the difference compared to the impact expected at the time of the tax revenue forecast.

- **dissolution of a reserve in the budget** created in connection with the opening of the fully-funded pillar of the pension system (**EUR 229 million)**;
- **reduction in expenditures of the public health insurance system** in connection with the downward revision of health-insurance revenue estimates (**EUR 39 million)**;
- **reduction in capital expenditures** in excess the co-financing framework under the operational programme infrastructure (**EUR 42 million).**
- **other expenditure cuts** in the total amount of **EUR 10 million;**
- at the same time, the **expenditures on repair of roads** administered by municipalities and self-governing regions have been increased by **EUR 16 million**.

In addition to the risks of macroeconomic development and their impact on the general government revenues, the risks of the budget lie, in particular, in the negative impact of the expenditure limits rolled over from the previous year, as well as in the fiscal performance of hospitals, municipalities and self-governing regions.

III.3. Medium-term budgetary outlook

The Government has drawn up the General Government Budgetary Framework for 2014-2016, where it defined its fiscal targets for that period. For 2014, general government deficit is expected to reach 2.6% of GDP. For 2015 and 2016, fiscal targets for general government deficit have been set at 2.0% and 1.3% of GDP, respectively.

This section aims to quantify the impact of the measures incorporated in the budgetary framework and define the magnitude of additional measures necessary to meet the fiscal targets. The basic assumption is that the 2013 fiscal objective is met, i.e., general government deficit does not exceed 2.9% of GDP. Subsequently, based on the no-policy-change scenario (which assumes no changes in economic policies), estimates of the medium-term general government balance can be made. By comparing this scenario with the general government balance targets, the magnitude of the necessary additional measures can be quantified.

III.3.1. No-policy-change scenario

The estimation of the no-policy-change scenario was based on the **updated estimate of general government deficit in 2013 at 2.9% of GDP**. Assuming that no changes in economic policies are made, general government deficit would reach 3.6% of GDP in 2014 and 2015 and then decline to 3.1% of GDP in 2016. If we disregard the changes in interest payments, under the unchanged policy scenario the primary deficit would initially rise from 1.0% of GDP in 2013 to 1.7% of GDP in 2014 and 2015. It would then decline to 1.0% of GDP in 2016.

TAB 13 – General government balance – no-policy-change scenario 2014 – 2016 (ESA 95, % of GDP)

	2013 E	2014	2015	2016
TOTAL REVENUES*	**32.5**	**31.0**	**30.4**	**30.0**
Tax revenues	**15.5**	**15.1**	**14.7**	**14.7**
Personal income tax	2.6	2.7	2.7	2.7
Corporate profit tax	2.7	2.7	2.7	2.7
Withholding tax on capital income	0.3	0.2	0.3	0.3
Value added tax	5.9	5.8	5.5	5.5
Excise taxes	2.7	2.6	2.5	2.4
Tax from international trade and transfers	0.0	0.0	0.0	0.0
Property tax and others	1.4	1.1	1.1	1.0
Social contributions	**13.3**	**12.7**	**12.6**	**12.6**
Non-tax revenues	**3.7**	**3.1**	**3.0**	**2.7**
Grants and transfers	**0.1**	**0.1**	**0.1**	**0.0**
TOTAL EXPENDITURES*	**35.5**	**34.6**	**34.0**	**33.1**
Current expenditures	**33.3**	**32.5**	**32.2**	**31.7**
Gross wages	5.9	5.9	5.9	5.9

Goods and services	9.2	8.8	8.6	8.5
- Health insurance companies	5.1	4.9	4.9	4.8
Subsidies and transfers	16.3	15.9	15.7	15.2
Interest	2.0	1.9	2.0	2.1
Capital expenditures	**1.3**	**1.4**	**1.3**	**0.9**
Capital assets	0.8	0.8	0.8	0.8
Capital transfers	0.5	0.6	0.5	0.2
Co-financing	**0.8**	**0.8**	**0.5**	**0.4**
GENERAL GOVERNMENT BALANCE	**-2.9**	**-3.6**	**-3.6**	**-3.1**
GENERAL GOVERNMENT PRIMARY BALANCE	**-1.0**	**-1.7**	**-1.7**	**-1.0**
p. m. GG balance – target	*-2.9*	*-2.6*	*-2.0*	*-1.3*
Primary GG balance – target	*-1.0*	*-0.7*	*0.0*	*0.8*
** Without EÚ funds*	*4.8*	*4.3*	*3.2*	*2.7*

Note: E -estimate *Source: MF SR*

The comparison of this scenario with the general government balance targets shows the magnitude of the measures which need to be taken. The general government balance indicator may provide a somewhat distorted picture, because the meeting of the target values will simultaneously decrease interest payments in comparison with the no-policy-change scenario. For this reason, it is more appropriate to compare primary balances, i.e., general government balance net of debt interest payments. In view of the above, the measures to be taken to improve the primary general government balance represent EUR 811 million in 2014, EUR 1,346 million in 2015 and EUR 1,571 million in 2016. This illustrates a cumulative sum of measures compared with the no-policy-change scenario; in other words, if permanent (structural) measures are adopted, the need to adopt additional measures in subsequent periods is reduced by the sum of the already adopted structural measures.

TAB 14 - Comparison of the no-policy-change scenario with fiscal targets (ESA95, % of GDP)

	2014	2015	2016
1. Primary GG balance – budgetary framework 2014-2016 - target	-0.7	0.0	0.8
2. Primary GG balance – NPC scenario	-1.7	-1.7	-1.0
Overall consolidation need (1-2)	**1.0**	**1.6**	**1.8**
- consolidation need with a permanent effect against NPC (net of one-off measures)*	0.8	1.8	1.8
- y-o-y change(consolidation need for additional measures)	0.8	1.0	0.0
- in EUR mill. (total consolidation need)	**811**	**1,346**	**1,571**
*p.m. * one-off measures (against the NPC scenario)*	0.2	-0.2	0.0

Source: MF SR

III.3.2. Description and quantification of the measures necessary to achieve fiscal targets

The total amount of the measures necessary to achieve fiscal targets is quantified in the preceding section. This is the basis on which the 2014-2016 General Government Budgetary Framework has been prepared and which includes (among other things) the following measures:

1. **Revenues from the sale of strategic oil reserves**
   The medium-term budgetary framework contains changes in the planned sale of strategic oil reserves to an entity outside the general government sector which will administer these stocks. The 2013-2015 General Government Budget assumed the sale of these stocks during 2013 to 2015. Their sale is now expected to take place in the course of 2013 and 2014. For the year 2013, this means a revenue in the amount as planned in the approved General Government Budget. The 2014 budget revenue will be higher by EUR 160 million compared with the no-policy-change scenario. On the other hand, the 2015 budget will be lower by exactly the same amount.

2. **Other changes in revenues**

Other changes in revenues (compared with the no-policy-change scenario) relate, in particular, to the increase in administrative revenues of public universities, municipalities and self-governing regions.

3. **Reduced wage expenditures in public sector**
The draft General Government Budgetary Framework for 2014 to 2016 assumes a freeze on wages at the 2013 budget level. This measure is expected to generate the biggest savings compared with the no-policy-change scenario, i.e. from about EUR 100 million in 2014 to about EUR 500 million in 2016.

4. **Lowering of selected subsidies**
The subsidies paid in 2014 to 2016 will be about EUR 50-66 million annually lower than under the no-policy-change scenario.

5. **Changes in capital expenditures of municipalities**
The communal elections slated for 2014 have been reflected in the General Government Budgetary Framework through higher capital expenditures in the election year. Municipal capital expenditures in 2015 are expected to decline slightly.

TAB 15 – Measures included in the General Government Budgetary Draft 2014-2016 (ESA95)*

	EUR mill.			in % GDP		
	2014	2015	2016	2014	2015	2016
Revenue measures	**181**	**-113**	**78**	**0.2**	**-0.1**	**0.1**
- revenues from the sale of strategic oil reserves	160	-160	0	0.2	-0.2	0.0
- other changes	21	47	78	0.0	0.1	0.1
Expenditure measures	**63**	**489**	**546**	**0.1**	**0.6**	**0.6**
- savings on wages	104	302	507	0.1	0.4	0.6
- state budget	78	164	252	0.1	0.2	0.3
- other general government entities	27	138	255	0.0	0.2	0.3
- lowering of selected subsidies	50	60	66	0.1	0.1	0.1
- changes in capital expenditures of municipalities	-93	94	-51	-0.1	0.1	-0.1
- other changes	2	33	24	0.0	0.0	0.0
TOTAL	**245**	**376**	**624**	**0.3**	**0.5**	**0.7**
- one-off measures	160	-160	0	0.2	-0.2	0.0
- other	85	536	624	0.1	0.7	0.7

Note: (+) indicates positive and (-) negative effects on the budget balance in ESA 95 classification
** against NPC scenario based on actual estimates of the GG budget balance for 2013 (sub-chapter III.2.3)*

Source: MF SR

Compared to the no-policy-change scenario, the positive impact of these measures for the general government balance represent 0.3% of GDP in 2014, 0.5% of GDP in 2015 and 0.7% of GDP in 2016.

TAB 16 – General government balance – Budgetary Framework 2014 – 2016 (ESA95, % of GDP)

		Budgetary Framework			Difference against NPC		
	2013 E	2014	2015	2016	2014	2015	2016
TOTAL REVENUES*	**32.5**	**31.2**	**30.2**	**30.0**	**0.2**	**-0.1**	**0.1**
Tax revenues	**15.5**	**15.1**	**14.7**	**14.7**	**0.0**	**0.0**	**0.0**
Personal tax income	2.6	2.7	2.7	2.7	0.0	0.0	0.0
Corporate profit tax	2.7	2.7	2.7	2.7	0.0	0.0	0.0
Withholding tax on capital income	0.3	0.2	0.3	0.3	0.0	0.0	0.0
Value added tax	5.9	5.8	5.5	5.5	0.0	0.0	0.0
Excise taxes	2.7	2.6	2.5	2.4	0.0	0.0	0.0
Tax from international trade and transactions	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Property tax and others	1.4	1.1	1.1	1.0	0.0	0.0	0.0

Social security contributions	**13.3**	**12.7**	**12.6**	**12.6**	**0.0**	**0.0**	**0.0**
Non-tax revenues	**3.7**	**3.4**	**2.8**	**2.8**	**0.2**	**-0.1**	**0.1**
Grants and transfers	**0.1**	**0.1**	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**
TOTAL EXPENDITURES*	**35.5**	**34.6**	**33.4**	**32.4**	**-0.1**	**-0.6**	**-0.6**
Current expenditures	**33.3**	**32.3**	**31.7**	**31.1**	**-0.2**	**-0.5**	**-0.6**
Gross wages	5.9	5.8	5.5	5.3	-0.1	-0.4	-0.6
Goods and services	9.2	8.8	8.6	8.5	0.0	0.0	0.0
- Health insurance companies	5.1	4.9	4.9	4.8	0.0	0.0	0.0
Subsidies and transfers	16.3	15.8	15.6	15.2	-0.1	-0.1	0.0
Interest	2.0	1.9	2.0	2.1	0.0	0.0	0.0
Capital expenditures	**1.3**	**1.5**	**1.2**	**0.9**	**0.1**	**-0.1**	**0.0**
Capital assets	0.8	1.0	0.7	0.8	0.2	-0.1	0.1
Capital transfers	0.5	0.5	0.5	0.1	0.0	0.0	0.0
Co-financing	**0.8**	**0.8**	**0.5**	**0.4**	**0.0**	**0.0**	**0.0**
GENERAL GOVERNMENT BALANCE	**-2.9**	**-3.3**	**-3.2**	**-2.4**	**0.3**	**0.5**	**0.7**
GENERAL GOVERNMENT PRIMARY BALANCE	**-1.0**	**-1.4**	**-1.2**	**-0.3**	**0.3**	**0.5**	**0.7**
** Without EU funds*	*4.8*	*4.3*	*3.2*	*2.7*	*0.0*	*0.0*	*0.0*

Note: E -estimate

Source: MF SR

After incorporating these measures into the 2014-2016 General Government Budgetary Framework, the total amount of the necessary measures has decreased.

TAB 17 - Comparison of the GG Budgetary Framework with fiscal targets (ESA95, in % of GDP)

	2014	**2015**	**2016**
1. Primary GG balance – GG budgetary framework - target	-0.7	0.0	0.8
2. Primary GG balance – GG budgetary framework – without all consolidation measures	-1.4	-1.2	-0.3
Consolidation need beyond of the Budgetary Framework (1-2)	**0.7**	**1.2**	**1.1**
- in EUR mill.	**566**	**969**	**947**

Source: MF SR

This means that, in order to meet the 2014 fiscal objective, it will be necessary to adopt (above and beyond the measures already incorporated in the 2014-2016 General Government Budgetary Framework) additional measures totalling EUR 566 million (0.7% of GDP).

The measures needed to meet the budget targets will be specified during the preparation of the 2014-2016 budget. The Government will focus, in particular, on the following:

- Since the funds spent on social benefits represent a significant part of government expenditure, it is necessary to consider changes in the system of these benefits in order to increase the scope of means-testing and make them more efficient.
- Measures in the healthcare sector will focus on attaining the highest possible efficacy of expenditures without undermining the access to and compromising the quality of healthcare services; the halting of debt accumulation in the healthcare sector, optimisation of the network of providers, and better coordination with the sector of social services in the provision of care for the elderly represent the main challenges.
- Streamlining of authorities (ESO Programme) will further reduce public expenditures, make the operations of the Government more efficient, and bring better services to citizens and businesses.
- At the same time, the Government has launched a programme of fight against tax evasions which, in systemic terms belongs to one of the most appropriate programmes in order to achieve consolidation targets; the implementation of concrete measures is already underway.

III.4. Structural balance and fiscal position of public finance

The estimated development of the general government structural balance and the reference value of its year-on-year change (the consolidation effort) defined in the preventive arm of the Stability and Growth Pact were used as a basis for defining fiscal policy objectives. Estimated growth of the expenditure aggregate net of discretionary revenue measures, enabling the assessment of the progress of fiscal consolidation compared against the reference value of expenditure growth, was used as a supporting indicator. In both cases, the data refer to the period until 2018, i.e., the year of the expected achievement of the MTO. In view of the decisive role of the Commission's evaluation for assessing compliance with the rules set out in the preventive arm of the Stability and Growth Pact, the indicators presented strive for maximum compatibility with its approach.

Box 4 presents also the MF SR's approach to general government balance adjustments. Compared with the procedure used to estimate the structural balance under the Stability and Growth Pact, this approach is more detailed and also takes account of national specificities to estimate the output gap and individual balance adjustment items. The Box also presents the estimate of the impact of fiscal policy on aggregate demand based on the estimate of the fiscal impulse.

The first step in the calculation of the **general government structural balance** is the adjustment of the real (officially reported) general government balance for the **cyclical component**. The cyclical component expresses the response of public finance revenues and expenditures and of the GDP as such to changes in the output gap. The size of the cyclical component depends on the size of the output gap and on the elasticities of selected revenue and expenditure categories responding to fluctuations in economic activity. The output gap was estimated on the basis of the MF SR's forecast of the real GDP growth and of the Commission's current forecast of the potential product (Part II.4). In its assessment of the sensitivity of general government balance to the changes in the output gap, the MF SR fully relied on the Commission's estimates based on the OECD methodology.[11]

The second item which the general government balance must be adjusted for are **one-off and temporary measures**. These were identified in keeping with the principles defined by the Commission[12] (for instance, the impact manifested only in a single year or a small number of years, or a significant impact considered as the impact at the level of 0.1% of GDP in at least one year). Based on the available information, the following one-off effects may be identified in the period of 2012 to 2014 (no one-off measures have been envisaged for the remaining projection years):

- Introduction of a temporary special levy on business in regulated industries in 2012 and 2013.
- In the framework of changes in the pension system's second (fully-funded) pillar, the pillar was temporarily open at the turn of 2012 and 2013 to enable savers to either exit from or enter into the pillar. The exits from the fully-funded generated one-off revenues for the Social Insurance Agency in the amount corresponding to the amount of assets accumulated by savers. As against the 2012 revenues of 0.1% of GDP, the revenues generated in 2013 amount to 0.3% of GDP.
- One-off non-tax revenue of 0.2% of GDP is also expected to be generated in 2013 by the digital dividend.
- Under the new system of strategic oil reserve management, the existing oil and oil product reserves will be sold to an entity outside of the general government; this will have a positive effect for revenues at the level of 0.2% of GDP in 2013 and 0.4% of GDP in 2014.

TAB 18 – Consolidation effort (ESA95, in % GDP)

	2012	2013	2014	2015	2016	2017	2018
1. General government budget balance	**-4.3**	**-2.9**	**-2.6**	**-2.0**	**-1.3**	**-0.7***	**-0.5***
2. Cyclical component	0.0	-0.5	-0.5	-0.4	-0.2	-0.1	0.0

[11] Girouard, N., André, Ch.: Measuring cyclically-adjusted budget balances for OECD countries. OECD Economics Department Working Papers, No. 434, 2005.

[12] Public Finances in EMU, 2006.

3. One-off effects	0.1	0.8	0.4	0.0	0.0	0.0	0.0
- temporary special levy on business in regulated industries (incl. CIT)	0.0	0.1	-	-	-	-	-
- opt-out from the fully-funded pillar	0.1	0.3	-	-	-	-	-
- digital dividend	-	0.2	-	-	-	-	-
- sale of oil reserves outside the GG sector	-	0.2	0.4	-	-	-	-
4. Structural balance (1-2-3)	**-4.5**	**-3.3**	**-2.5**	**-1.6**	**-1.1**	**-0.6**	**-0.5**
Consolidation effort (y-o-y change of of 4)	**0.2**	**1.2**	**0.8**	**0.9**	**0.5**	**0.5**	**0.1**
p.m. Output gap	*0.1*	*-1.5*	*-1.6*	*-1.2*	*-0.6*	*-0.2*	*0.0*

** The estimate for the budget balance in 2017 is based on a mechanical computation considering the structural deficit reduction of 0.5% of GDP annually and reaching the MTO of 0.5% of GDP in 2018.*

Source: MF SR

Assuming that the fiscal objective will be achieved, and based on the estimated impact of the economic cycle and one-off effects, the consolidation effort in 2013 is estimated at 1.2% of GDP. In view of the restrictions imposed by the constitutional Fiscal Responsibility Act (the debt level close to 57% of GDP in 2015 and the ensuing obligation to establish a balanced budget in 2017), the fiscal objectives that were fixed for the subsequent years require a consolidation effort at the level of 0.8% of GDP in 2014 and 0.9% of GDP in 2015. Consolidation contemplated for 2016 meets the minimum level defined in the Stability and Growth Pact, whichcorresponds to the consolidation effort of 0.5% of GDP.

The revised Stability and Growth Pact lays emphasis also on the analysis of the fiscal position through the growth of general government expenditures compared with the reference growth rate. This approach is embodied in the so-called **expenditure benchmark.**

In Slovakia, a country that does not currently achieve its MTO, adjusted primary general government expenditures net of discretionary revenue measures should grow in real terms more slowly compared to the average potential growth of the economy, i. e. at a rate ensuring a year-on-year improvement of the cyclically adjusted balance net of one-off effects by 0.5% of GDP. The expenditure benchmark has been taken over from the Commission's documents.[13]

The expenditure benchmark, rather than being compared with total expenditures, is compared with expenditures that are analytically adjusted for factors which are outside of the Government's control and have no impact on the general government balance. These include interest expenditures, changes in expenditures on unemployment benefits unrelated to government policies, expenditures financed from EU funds, and expenditures covered by revenue-side measures. Moreover, in view of the high year-on-year volatility of Government investment (especially in smaller EU Member States), the average investment rate of the last three years and in the current year is considered. Using the GDP deflator, the nominal growth of expenditures adjusted accordingly is translated into the real growth in order to make it comparable with the expenditure benchmark.

TAB 19 – Expenditure aggregate net of discretionary revenue measures (ESA 95, EUR mill.)

	2012	2013E	2014	2015	2016	2017	2018
1. Total expenditures*	**26,768**	**27,314**	**26,687**	**26,644**	**28,454**	**28,638**	**30,073**
2. Interest expenditure	1,322	1,416	1,443	1,584	1,775	1,847	1,870
3. Gross fixed capital formation [9]	1,365	1,255	1,011	581	540	569	597
4. Gross fixed capital formation (averaged over t-3 to t)	1,532	1,481	1,304	1,053	847	675	572
5. Government expenditure on EU programmes which is fully matched by EU funds revenue	807	1,484	1,035	543	1,646	983	1,179
6. Non-discretionary changes in unemployment benefit expenditure	-2	26	30	24	13	5	1

[13] Updated reference rates for the assessment against the expenditure benchmark. Note for AEFC, 4 March 2013, Brussels.

[9] A substantial decline of this item in 2015 on yearly basis is mainly due to lower drawing of EU funds, as well as with a decline in capital expenditure of municipalities connected with an election year in 2014 and an expected decline of investment activities in the subsequent year. Výrazný pokles tejto položky v roku 2015 oproti roku 2014 súvisí najmä s nižším predpokladaným čerpaním prostriedkov z fondov EÚ, ako aj poklesom kapitálových výdavkov u obcí súvisiacim s konaním komunálnych volieb v roku 2014 a predpokladaným znížením investičných aktivít v ďalšom roku.

7. Revenue measures mandated by law to match expenditure increases	0	0	0	0	0	0	0
8. Primary expenditure aggregate (1-2-3+4-5-6-7)	**24,808**	**24,613**	**24,473**	**24,965**	**25,327**	**25,909**	**26,998**
9. y-o-y change of primary expenditure aggregate (8)	-	-195	-140	492	363	582	1,089
10. Effect of discretionary revenue measures	-	1,271	-434	9	26	0	0
11. Nom. growth of expenditure aggregate net of discretionary revenues measures $((9_t-10_t)/8_{t-1})$	-	-5.9	1.2	2.0	1.3	2.3	4.2
12. Expenditure growth rate net of discretionary revenue measures (%)	**-**	**-7.7**	**-0.8**	**-0.1**	**-0.6**	**0.3**	**2.3**
13. Reference rate of expenditure growth (%)	**-**	**1.8**	**1.5**	**1.5**	**1.5**	**-**	**-**
14. Compliance with expenditure benchmark (12<13)	**-**	**yes**	**yes**	**yes**	**yes**	**-**	**-**
*p. m. GDP deflator ***	*-*	*1.9*	*2.0*	*2.1*	*2.0*	*2.0*	*1.9*

** given that the budget balance targets will be met, ie.lowered by the amount of additional measures in order to meet the targets* *Source: MF SR*
***Till 2013 EC forecast and from 2014 onwards MF SR forecast*
E - estimate, 2014-2016 budgetary framework

Taking account of general government expenditures and revenue-side measures incorporated into the 2013 general government budget, the real growth of adjusted expenditures presented in the assumptions for the general government budgetary framework 2014 to 2016 should be negative. **Since this expenditure growth rate is below the reference value in every year, the current proposal of the level of general government expenditures in 2013 to 2016 meets the expenditure benchmark.**

BOX 4 – Consolidation effort and fiscal impulse – approach of the Ministry of Finance

The approach taken by the MF SR to consolidation effort calculations slightly differs from the Commission's approach and had been presented in the previous updates of the Stability Programme. It accounts for national specificities, for instance when estimating the output gap or in connection with balance adjustment factors (like the effect of the pension system's fully-funded pillar or motorway and speedway construction outside the general government balance). It addresses one-off effects in more detail, as it also includes measures having the impact at the level of 0.05% of GDP in at least one year. Moreover, adjustments are applied also to measures with a neutral impact on the balance in medium to long term (see, e.g., point 2b below).

Under the MF SR approach, the balance used for the purpose of calculating the consolidation effort (year-on-year changes of adjusted balance) is analytically adjusted for:

1. **Cyclical component** – using the Ministry's forecast of output gap and semi-elasticity (budget to output gap) calculated by the Commission
2. **One-off effects** – in comparison with effects referred to in the main section, these include the following additional one-off measures:
   a) Temporary rise in 2011 of the basic VAT rate from 19% to 20% until the year when the notified general government balance falls below 3% of GDP. The current fiscal objectives indicate that the rate will be reversed from 2015 onwards.
   b) Repayment of reimbursable financial assistance, which was entered in the past as a capital transfer with a negative effect on the general government balance. If it is repaid, it will be entered with a positive effect on the balance. These cases include the repayments by companies Cargo (capital transfer in 2009) and Vodohospodárska výstavba (capital transfer from before 2002).

TAB 20 – One-off measures (ESA95, in % of GDP)

	2012	2013	2014	2015	2016
- temporary special levy on business in regulated industries (incl. CIT)	0.0	0.1	-	-	-
- opt-out from the fully-funded pillar	0.1	0.3	-	-	-
- special levy in the banking sector	0.1	-	-	-	-
- increase in VAT rate from 19 % to 20 %	0.3	0.3	0.3	-	-
- digital dividend	-	0.2	-	-	-
- sale of oil reserves outside the GG sector	-	0.2	0.4	-	-
- repayments of reimbursable fin. assistance (Cargo and VHV)	0.1	0.1	0.1	0.1	0.0
Total	**0.5**	**1.2**	**0.8**	**0.1**	**0.0**

Source: MF SR

3. **Implementation of the 2nd pillar of pension scheme** – representing a significant structural change, the fully-funded pillar has an immediate impact on the general government balance in forecast years, but its effect on long-term sustainability remains unchanged.
4. **Interest expenditure** – the level of interest expenditures is determined mainly by the level of general government debt in the past period, by refinancing needs, and by the situation on the financial markets. This item falls outside direct Government control.
5. **Construction of motorways and speedways outside of the general government balance** – through PPP projects and credit financing by the National Highway Company (Národná diaľničná spoločnosť, a.s., NDS hereinafter) which is classified as being outside of the general government sector.

The next analytical indicator is the **fiscal impulse,** which measures the contribution of general government budgets to year-on-year changes in aggregate demand. In other words, the fiscal impulse informs whether the Government's fiscal policy is expansionary or restrictive. In combination with the output gap, it characterises the fiscal policy and analyses it in order to establish whether it has a stabilising (anticyclical) effect on the economy or whether, on the contrary, it behaves procyclically. Fiscal impulse is calculated on the basis of adjusted balance used to calculate the consolidation effort, adjusted also for financial transfers from/to the EU budget. These include the payments to the EU budget that do not increase aggregate demand, and income from the EU which, while not impairing the balance (being on both the revenue and the expenditure sides), has an expansionary effect on the economy.

TAB 21 - Consolidation effort and fiscal impulse (ESA 95, % of GDP)

	2012	2013	2014	2015	2016
1. General government budget balance	**-4.3**	**-2.9**	**-2.6**	**-2.0**	**-1.3**
2. Cyclical component	-0.1	-0.5	-0.4	-0.3	0.0
3. One-off effects	0.5	1.2	0.8	0.1	0.0
4. Implementation of the 2nd pillar of pension scheme	-1.0	-0.5	-0.6	-0.6	-0.6
5. Interest payments	-1.7	-1.9	-1.9	-1.9	-2.1
6. Construction of motorways outside of the GG balance	-0.1	-0.2	-0.1	-0.1	-0.1
7. Adjusted balance for computation of consolidation effort (1-2-3-4-5-6)	**-1.8**	**-0.9**	**-0.5**	**0.8**	**1.4**
Consolidation effort (y-o-y change 7)	**0.5**	**0.9**	**0.4**	**1.3**	**0.6**
p.m. Consolidation effort without adjusting for the fully-funded pillar	*0.7*	*1.4*	*0.4*	*1.3*	*0.6*
8. Financial links the EU budget	1.9	3.8	3.4	2.2	1.8
- revenues from EU budget	2.8	4.8	4.3	3.2	2.7
- contributions to the EU budget	-0.9	-1.0	-0.9	-0.9	-0.9
9. Aggregated balance for the purposed of fiscal impulse calculations (7-8)	**-3.7**	**-4.8**	**-4.1**	**-1.4**	**-0.3**
Fiscal impulse (y-o-y change 9)	**1.0**	**-1.0**	**0.9**	**2.4**	**1.1**
p.m. Output gap	*-0.4*	*-1.4*	*-0.9*	*-0.6*	*0.1*

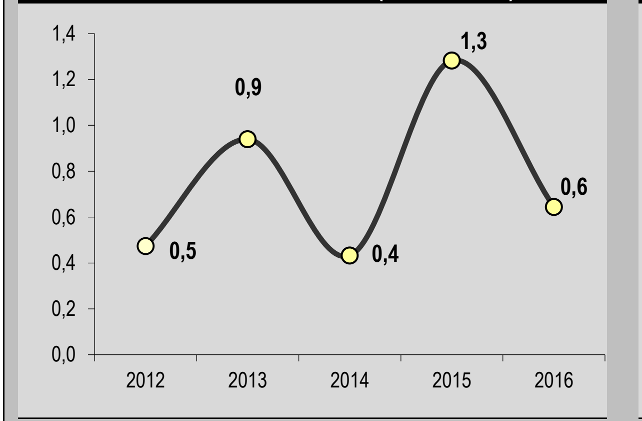
Note: (+) restriction (-)expansion

Source: MF SR

It is expected that the consolidation of public finances in 2013 will be offset by the expansionary impulse of the drawing of EU funds (the year-on-year increase of the drawing of EU funds is expected to reach the level of 2.0% of GDP). Fiscal consolidation is expected to continue also in the subsequent years; as a consequence of the slowing down of the absorption of EU funds due to the gradual exhaustion of funds available in the 2007-2013 programming period, the restrictive impact of fiscal policy will prevail and the output gap will be gradually closed.

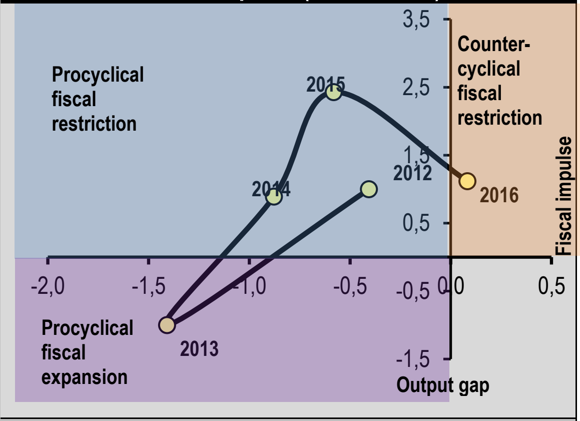
Procyclical fiscal restriction in 2014 and 2015 is mainly due to the implementation of the EU and national fiscal rules. While the European rules call for pursuing fiscal consolidation at a certain pace in a structural manner (0.5% of GDP annually), compliance with national rules in the above period will call for a greater restriction irrespective of the cycle. It can be noted in this regard that the debt brake (linked to the gross debt indicator) intensifies the procyclical fiscal restriction.

GRAPH 18 - Consolidation effort (in % of GDP)



Source: MF SR

GRAPH 19 - Fiscal impulse (in % of GDP)



Source: MF SR

III.5. General government debt and its development

At the end of 2012, the gross general government debt[14] reached the level of 52.1% of GDP. Assuming that fiscal objectives are achieved, the debt in the following year will increase to 54.8% of GDP. The 2014 debt is expected to be at the level of 56.3% of GDP; in 2015, the debt will grow at a slower rate and will start declining in 2016. If the debt evolved in this way, it would overshoot certain limits laid down in the Fiscal Responsibility Act and triger sanctions (Box 3). Throughout the entire period, the general government debt will be below the Maastricht criterion reference value. **At the end of the forecast period, net general government financial debt will reach the level of 49.2% of GDP.**

TAB 22 - General government debt development between 2012 to 2016

		2012	2013	2014	2015	2016
Gross debt (EUR mill.)		**37,245**	**40,431**	**43,622**	**46,319**	**48,204**
Gross debt (% of GDP)	(1)	**52.1**	**54.8**	**56.3**	**56.7**	**55.9**
Change in gross debt (p. p.)		8.8	2.6	1.5	0.4	-0.8
- Growth in nominal GDP		-1.4	-1.7	-2.6	-2.9	-3.0
- Primary balance		2.5	1.0	0.7	0.1	-0.8
- Interest payment		1.9	1.9	1.9	1.9	2.1
- Stock-flow adjustment		5.9	1.4	1.5	1.3	0.9
Liquid financial assets (% of GDP)	(2)	5.1	5.4	5.7	6.3	6.7
- Cash on GG accounts		4.8	5.1	5.4	6.0	6.4
- Securities*		0.3	0.3	0.2	0.2	0.2
- Other (shares, gold deposits)		0.0	0.0	0.0	0.0	0.0
Net debt (% of GDP)	(1-2)	**47.0**	**49.4**	**50.6**	**50.4**	**49.2**
p.m. Implicit interest rate (%)		*4.4*	*3.8*	*3.6*	*3.6*	*3.8*
Impact of ESM and EFSF on gross debt		*2.5*	*3.2*	*3.5*	*3.3*	*3.1*

** According to the Maastricht definition, shares have to be valued at market prices. Given the fact, that neither MF SR or SO SR revaluate shares, nominal prices were used instead.*

Source: MF SR

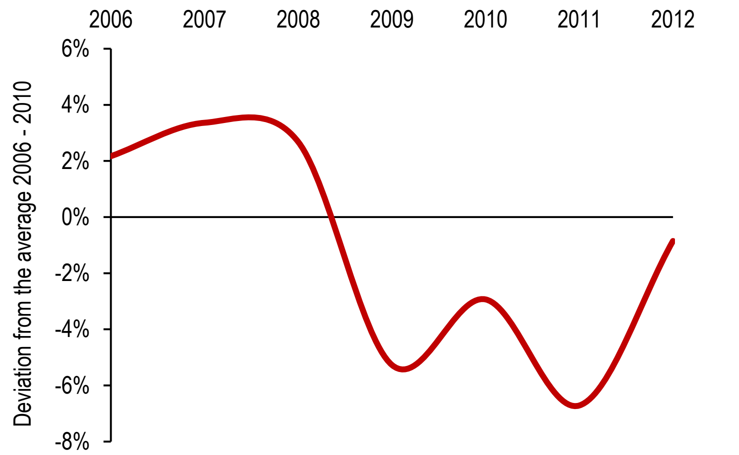
[14] All reported values were calculated using the methodology applied to assessing compliance with the Maastricht criterion on the general government gross debt – the so-called Maastricht debt.

- **Development in 2012**

In 2012, the gross general government debt increased in nominal terms by EUR 7,333 million, mainly due to the contribution of the **state budget cash deficit of EUR 3,811 million (52% of total increase**). Another important factor that contributed to the growth of gross debt was the increase in general government assets, resulting mainly from the need **to top up the reserves for liquidity management purposes**. Adverse situation on the financial markets at the end of 2011 did not allow to issue bonds and the needs of government debt financing were met at the cost of a fall in reserves. When the financial markets turned around in the course 2012, it became possible to increase the low level of reserves. Nevertheless, the reserves are still below their average level of 2006-2010 (Graph 20). The overall effect of these factors reached the level of **EUR 2,051 million (28% of total increase)**. The third most significant factor behind the growth of debt was the increase in the **Slovakia's share in the EFSF debt by EUR 1,321 million (18% of total increase).**

The debt of other general government entities fell by EUR 62 million, mainly as a result of the decline in the debt of self-governing regions and municipalities. At the same time, however, they took over the liabilities of health establishments in the total amount of EUR 130 million.

GRAPH 20 – Development of the reserve against the average share on state debt in 2006-2010 (%)



Source: MF SR

The graph shows variations in the development of the reserve for liquidity management purposes[15] to public debt[16] ratio against its mean value in 2006-2010[17]. In the 2006-2010 period, average reserves amounted to 9.1% of the debt managed by the Debt and Liquidity Management Agency. This simplified view of adequate amount of reserves would allow interpreting the development in the course of 2012 as a significant increase in reserves. Their level went up from 2.4% of state debt in 2011 to 8.9% in 2012. They, however, are still slightly below their average in 2006-2010.

- **Forecast for 2013-2016**

The main contributor to changes in the general government debt during the forecast period is the level of the state budget deficit. If fiscal objectives are achieved, its negative contribution will be gradually reduced. As regards the performance of other general government entities, it is estimated that **local government will contribute to debt reduction, except in 2014.**

[15] Amount of deposits in commercial banks as to 31 December of every year.

[16] State debt net of assumed liabilities of hospitals, i.e. the debt which falls directly under the Debt and Liquidity Management Agency.

[17] The State Treasury system was introduced in 2004, but reliable data are available only from 2006.

Another factor that has an impact on the debt level is **the State Treasury (ST) system**. It is assumed that the amount of funds for financing the needs of the state will increase during the forecast period and will thus contribute to debt reduction, especially in 2013.

To a lesser extent, the debt is increased by **discounts on issuing** new debt instruments. Since, at the moment of issuing the bonds, state liabilities increase by the nominal value of the bonds, but the state gets a lower cash amount (reduced by the discount), the discount at the issue is a factor which contributes to the growth of the debt. When the bonds reach maturity, the amount of paid discount is part of cash expenditures from the state budget, but this sum does not contribute to increasing the debt. If the cash deficit of the state budget increases the government debt by its full amount, then the discount upon redemption of Government bonds has a positive effect on the debt. This is due to the fact that the debt increase occurs already at the time when bonds are issued – at the level of the nominal bond value – rather than at the time of bond redemption.

The amount of the gross debt is influenced also by **Slovakia's contributions to the ESM**. According to the Eurostat[18] decision, liabilities under the ESM are not, unlike those under the EFSF, directly included in the general government debt of the Member States. However, Slovakia's contributions to the ESM represent a factor that increases the debt. This is because the ESM contributions reduce available state budget resources which could be used to finance the needs of the state, and thus contribute to increasing gross debt.

Debt forecasts also reflect the effect of **Slovakia's commitments under the EFSF** connected with the granting of financial assistance to Ireland, Portugal and Greece. The EFSF will not enter into new financial programmes, but will continue to manage the settlement of liabilities by debtor countries until their full repayment. Until that time, the EFSF liabilities will have a direct impact on the debt level in the amount equal to Slovakia's share in the EFSF.

The forecast takes into account also the effects of **foreign exchange differences** in relation to the portion of the debt denominated in foreign currency which is not hedged against currency fluctuation.

TAB 23 – Year-on-year change of gross debt according to contributing factors (EUR mill.)

	2012	2013 E	2014 E	2015 E	2016 E
General government gross debt (31.12.)	**37,245**	**40,431**	**43,622**	**46,319**	**48,204**
Total year-on-year change of GG gross debt (1+2+3)	**7,333**	**3,186**	**3,191**	**2,697**	**1,885**
1. State debt	**6,074**	**2,952**	**2,964**	**2,752**	**1,934**
State budget deficit	3,811	3,085	2,746	2,593	1,899
Discounts on issuing debt	141	55	200	202	116
Paid discounts on maturity	-311	-65	-64	-79	-14
State treasury system	2,051	-383	-47	39	-67
ESM	264	264	132	0	0
Assumed debt from healthcare providers	130	0	0	0	0
Foreign exchange differences*	-8	-3	-3	-2	0
Deposits of other ST clients outside of GG**	-8	0	0	0	0
Other	4	0	0	0	0
2. Change in debt of other GG entitites	**-62**	**-107**	**38**	**-55**	**-50**
3. Commitments of SR under EFSF	**1,321**	**341**	**189**	**0**	**0**

Note: Positive items increase gross debt, negative items decrease debt, E –Estimate *Source: MF SR*

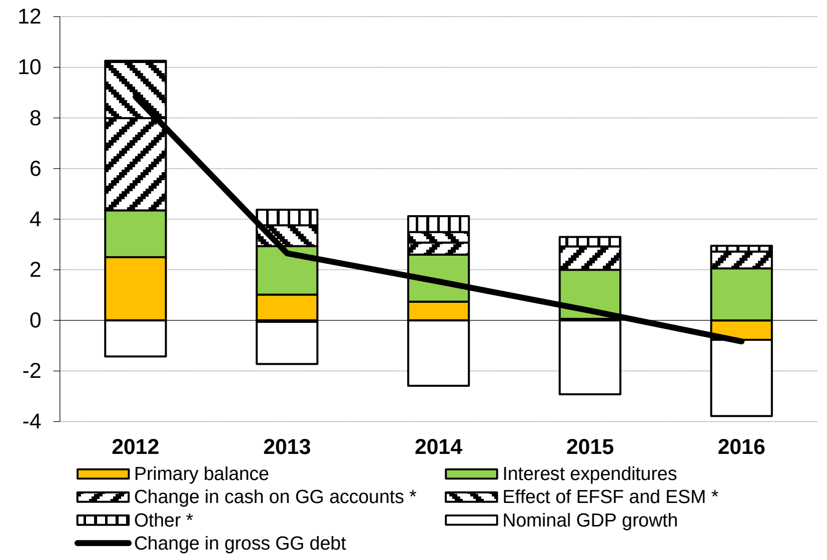
** Foreign exchange differences are computed only from debt instruments in foreign currency, which are not fixed against changes in exchange rates*

*** For example, entities which are not within the general government sector according to ESA 95 methodology but have voluntary accounts in the State Treasury.*

[18] In its opinion of 30 January 2013, Eurostat confirmed that the ESM meets the criteria for being classified as an institutional financial unit and that as such it may independently enter into contractual relations. Based on this decision, ESM liabilities will not be assigned to the Member States, but directly to the ESM.

As regards the relative contributions of individual factors to debt changes, the most important factor increasing the debt in the forecast period will be the planned general government deficits. In addition to higher interest costs over the relevant period, a relatively large primary deficit is also expected which, however, will progressively decline as the planned fiscal consolidation gets underway. The stock-flow adjustment factor will also positively contribute to the growth of the gross debt, and its level – especially in 2012 – will be significantly influenced by the growing reserves for debt and liquidity management purposes, and by the increase in Slovakia's guarantees under the EFSF. The only factor contributing to reducing the debt-to-GDP ratio since 2012 is the nominal GDP growth which will prevail over the other previously mentioned adverse factors in 2016.

GRAPH 21 – Contribution of factors to the change in gross GG debt (p. p.)



* *Stock-flow adjustment* *Source: MF SR*

The value of the stock-flow adjustment in 2013 will be influenced, in particular, by the net increase in financial assets, due to the expected development of available financial resources of the State Treasury, and by positive cash balances of other general government entities. The difference between cash and accrual accounting methods also influences the stock-flow adjustment of general government. Slovakia's guarantees under the EFSF and its deposits in the ESM also contribute to debt growth. Because a large portion of the general government gross debt is denominated in EUR, the impact of exchange rate fluctuations is negligible.

TAB 24 - Stock-flow adjustment (% of GDP)

	2012	2013	2014	2015	2016
Stock-flow adjustment	**5.9**	**1.4**	**1.5**	**1.3**	**0.9**
Differences between cash and accruals	**-0,1**	**0.5**	**0.5**	**0.4**	**0.2**
Net accumulation of financial assets	**5.9**	**0.8**	**1.0**	**1.0**	**0.7**
- of which: change in cash on GG accounts VS	3.7	-0.1	0.5	0.9	0.7
- of which: effect of ESM and EFSF	2.2	0.8	0.4	0.0	0.0
Foreign exchange differences*	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Other	**0.2**	**0.1**	**0.0**	**-0.1**	**-0.1**

** Foreign exchange differences are computed only from debt instruments in foreign currency, which are not fixed against changes in exchange rate* *Source: MF SR*

IV. SENSITIVITY ANALYSES AND COMPARISON WITH THE PREVIOUS UPDATE

Slovakia's Stability Programme is built on the baseline scenario of economic development and exogenous assumptions concerning the development of the external environment as described in Table 2. This section presents risk scenarios derived from the simulations based on the assumptions of slowdown in foreign demand, lower nominal consumption of the Slovak Government, and increased interest rates.

IV.1. Risk scenarios

Scenario 1. Slowdown in foreign demand

The underlying assumption in Scenario 1 is that the economic growth of Slovakia's trade partners will slow down and that the demand for Slovak exports will fall as a result. This type of development appears to be supported by moderately pessimistic estimates of economic activity in the euro area dating from the end of 2012. The simulation assumes a one-off slowdown of the rate of increase of the weighted foreign demand indicator by 1 percentage point against the initial forecast.

A sharp decline in the dynamics of foreign demand would bring about a fall in exports compared with the baseline scenario. Lower production capacity utilisation in export-oriented industries would deter investment expenditures of companies. It would also lead to cuts in employment which, in turn, would force households to reduce consumption. Weaker aggregate demand would also reduce inflationary pressures in the national economy. Lower exports would push the current account balance towards negative figures. This effect would, however, be partly offset by weaker dynamics of imports connected with adverse developments of domestic demand. Slower economic activity would have an adverse effect on general government balance which would fall by 0.2% of GDP a year, and the debt at the end of the period would increase by 0.8 percentage point.

TAB 25 - Scenario 1 – Slowdown in foreign demand by 1 p.p. in 2013
Cumulative change of parameters compared to baseline scenario in p. p.

	Household consumption	Gross fixed investment	GDP	Unemployment rate	CPI	CA balance (% of GDP)	GG balance (% of GDP)	GG gross debt (% of GDP)
2013	-0,6	-0,7	-0,7	0,1	-0,2	-0,1	-0,2	0,3
2014	-0,4	-0,5	-0,6	0,2	-0,4	-0,1	-0,2	0,5
2015	-0,4	-0,5	-0,5	0,2	-0,6	0,0	-0,2	0,6
2016	-0,4	-0,4	-0,5	0,3	-0,8	0,1	-0,2	0,8

Source: MF SR

Scenario 2. Lower government consumption

The second scenario is drawn up against the backdrop of the on-going global debt crisis and its negative impact on economic growth, which often compels the governments to consider additional measures necessary to achieve their fiscal targets. The scenario examines the effects of a decline in the rate of growth of nominal government consumption by 1 percentage point in 2013 in terms of government demand for finished products. At the same time, wage costs in the public sector are assumed to remain unchanged compared with the baseline scenario of economic development.

The decline in government demand would moderately slow down the GDP growth and would subsequently entail a decrease in household consumption and investment. Weaker domestic demand would be reflected in the subsequent years also in a lower job creation and moderate increase in unemployment. Lower demand would also slow down the inflation. On the positive side, lower domestic demand would be positively reflected in the current account balance through lower imports. The current account balance could partly benefit also from a moderate increase in exports due to enhanced price competitiveness. The primary effect of lower government consumption in 2013 would shift the general government balance towards positive figures, although the secondary impact of the reduced economic activity would partly cancel this positive effect. On the whole, the general government balance would annually improve by 0.1% of GDP. The general government debt at the end of the period would be reduced by 0.3 percentage point.

TAB 26 - Scenario 2 – Decrease in nominal government consumption by 1 p.p. in 2013
Cumulative change of parameters compared to baseline scenario in p. p.

	Household consumption	Gross fixed investment	GDP	Unemploym ent rate	CPI	CA balance (% of GDP)	GG balance (% of GDP)	GG gross debt (% of GDP)
2013	-0,1	-0,2	-0,1	0,0	0,0	0,1	0,1	0,0
2014	-0,1	-0,1	-0,1	0,0	-0,1	0,1	0,1	-0,1
2015	-0,1	-0,1	-0,1	0,1	-0,1	0,1	0,1	-0,2
2016	-0,1	-0,1	-0,1	0,1	-0,2	0,1	0,1	-0,3

Source: MF SR

Scenario 3. Increased interest rates

The third scenario describes the effects of the increase in short- and long-term interest rates by 2 percentage points over the 2013-2014 period. This shift in interest rates is interpreted in terms of the increased risk premium to interest rates on private and public debt. Risk premiums could be raised in response to increased uncertainty concerning the manner of handling the debt crisis and its possible implications for the financial markets.

Higher interest rates mean a more costly financing of consumption and investment through loans, and impair access to credits for households and businesses, thus slowing down household consumption and investment growth. Lower consumption and investment would also cause a moderate slowdown in the economic growth. Lower domestic demand would slightly decrease the rate of inflation and, due to reduced imports of consumer and investment goods, would moderately improve the current account balance. An overall adverse impact on the general government balance, including direct interest costs of general government debt, has been quantified at 0.1% of GDP to 0.3% of GDP. The general government debt at the end of the period would increase by 0.9 percentage point.

TAB 27 - Scenario 3 – Increase of short-term and long-term interest rates by 2 p. p. in 2013 and 2014
Cumulative change of parameters compared to baseline scenario in p. p.

	Household consumption	Gross fixed investment	GDP	Unemploy ment rate	CPI	CA balance (% of GDP)	GG balance (% of GDP)	GG gross debt (% of GDP)
2013	-0,1	-0,2	0,0	0,0	0,0	0,1	-0,1	0,1
2014	-0,1	-0,3	-0,1	0,0	0,1	0,2	-0,2	0,4
2015	0,0	-0,3	0,0	-0,1	0,0	0,3	-0,3	0,6
2016	0,0	-0,3	0,0	-0,1	0,0	0,3	-0,3	0,9

Source: MF SR

IV.2. Comparison with the previous update

The Stability Programme of the Slovak Republic for 2013-2016 presents updated macroeconomic objectives and fiscal objectives. Compared to the last year's update of April 2012, the forecast of general government debt forecast has deteriorated, as did the target values of general government balance in 2014 and 2015; these deviations are explained in Chapter III.

TAB 28 - Comparison between the previous forecast and the updated forecast

	ESA code	Year 2012	Year 2013	Year 2014	Year 2015	Year 2016
Real GDP growth (%)						
Previous update*		1,1	2,7	3,6	3,7	-
Current update		2,0	1,2	2,9	3,3	3,6
Difference		0,9	-1,5	-0,7	-0,4	-
General government balance (% of GDP)	EDP B.9					
Previous update*		-4,6	-2,9	-2,3	-1,7	-
Current update		-4,3	-2,9	-2,6	-2,0	-1,3
Difference		0,3	0,0	-0,3	-0,3	-
General government gross debt (% of GDP)						
Previous update*		50,2	52,0	53,0	52,3	-
Current update		52,1	54,8	56,3	56,7	55,9
Difference		1,9	2,8	3,3	4,4	-

*Note: * Stability Programme of the Slovak Republic for 2012 - 2015*

Source: MF SR

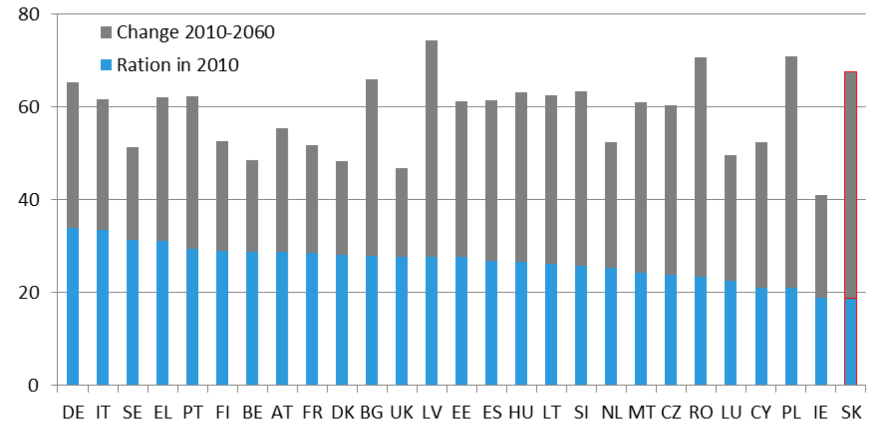
V. SUSTAINABILITY OF PUBLIC FINANCES

The long-term sustainability of public finances has an economic and a moral dimension. From the economic point of view, sound public finance is an essential precondition for high and sustainable economic growth. The moral dimension consists in ensuring the intergenerational fairness. This is because the resources are redistributed through general government budgets not only among individual groups of the population (solidarity), but also between the generations. The policy of high deficits and debt growth pursued over the long run automatically means placing a burden on the future generations who will not necessarily be able to enjoy its previously existing benefits.

V.1. Policy strategy

The 2012 Ageing report[19] of the European Commission confirmed that during the upcoming 30 to 50 years all EU Member States will face substantial demographic changes that will have adverse effects on their pension and health insurance systems. Slovakia belongs among the countries that will feel the biggest impact of demographic changes.[20]

GRAPH 22 – Old-age dependency ratio*



*Old-age dependency ratio is defined as a ratio between population aged 65+ and population aged 20-64

Source: EUROPOP (2010)

The need for pension system reforms has been exacerbated by the economic crisis, which has profoundly deteriorated the fiscal positions of EU countries, and has evolved into a debt crisis in the countries on the periphery of the euro area. The countries gradually started pursuing policies whose key objective is fiscal consolidation aimed at the stabilisation or reduction of the general government debt. However, improvements in the management of public finance are not necessarily sufficient to ensure long-term sustainability, even if the consolidation has been successful (to compensate for the effects of population ageing, the country would have to permanently work with large surpluses), and it is therefore inevitable to implement reforms in the pension and healthcare systems which account for the largest share of general government expenditures, and are sensitive to population ageing.

In 2012, the Slovak Government introduced important changes into the pension system aimed at improving its all-round long-term sustainability. The key changes that have a positive effect on public finances include automatic adjustments of the retirement age linked to life expectancy, change in the indexation of pension benefits, strengthening the solidarity principle in awarding new pensions, and changes related to the maximum assessment base for the payment of social insurance contributions. Changes introduced in the fully-funded pillar

[19] European Commission (DG ECFIN) and the Economic Policy Committee (AWG) (2012) The 2012 Ageing report: Economic and budgetary projections for the EU27 Member States (2010-2060), European Economy, No. 2, 2012.

[20] According to the latest demographic projects of Eurostat (EUROPOP), Slovakia will be the country with the second biggest change in the age structure of the population in the EU after Poland. Its old-age dependency ratio will deteriorate from 5.3 in 2010 to 1.5 in 2060.

increase the revenues for the pension system on the one hand but, on the other hand, they also increase future expenditures of the system. Over the relevant period of up to 2060, they have a positive cumulative effect on general government balance.[21]

In addition to parametric or systemic reforms, in order to counteract the adverse effects of ageing it is necessary to implement structural reforms promoting growth and employment. Higher employment, productivity and economic growth constitute not only the single sustainable source for improving the standard of living of the population, but they can also significantly foster the sustainability of the pension system and the overall consolidation of public finance. Adequate and effective tax burden, intelligent labour market regulation, and flexible markets for goods and services are the prerequisites for employment and productivity growth.

V.2. Long-term budgetary outlook in the context of population ageing

Population ageing is a global phenomenon that currently affects mainly advanced economies. Slovakia is no exception. In the EU framework, this issue is given utmost attention. It is addressed by a special working group, the Ageing Working Group (AWG), which has a mandate to develop and to regularly update, in cooperation with the Commission, long-term projections of expenditures that are sensitive to demographic trends, and to examine their impact on the development of public finance. Its objective is to obtain comparable and the most complete data concerning the risks connected with expected demographic changes.

The present subchapter consists of two parts. The first part describes the magnitude of the problem that the public finances in Slovakia will have to grapple with in the future, while the second part addresses the long-term sustainability measured by sustainability indicators based on the Commission's methodology.

Long-term projection of revenues and expenditures sensitive to population ageing

The AWG identified those general government expenditures that may be positively or adversely affected by demographic changes. These include expenditures on pensions,[22] healthcare,[23] long-term care, education, and unemployment benefits. In addition to the expenditure side, the revenue side reflects changes in property income [24] and, in case of certain countries including Slovakia, also changes resulting from pension system adjustments. In Slovakia, these include a shortfall in general government revenues brought about by the situation in the fully-funded pillar of the pension system. Together with the Commission, the AWG presented in 2012 also other official projections for the period of up to 2060. In accordance with the requirements concerning the content of Stability Programmes,[25] Member States must incorporate into these programmes also the AWG's projections.

Because the pension reform (Box 5) was introduced only after the publication of these projections, the **Ministry of Finance as an AWG member has prepared new pension forecasts and has asked the AWG and the**

[21] The time horizon of up to 2060 is too short to objectively evaluate this measure because its adverse effects are manifested with a longer delay.

[22] Pension benefits comprise – in addition to retirement pensions, early retirement pensions and survivor pensions – also social assistance. This is due to the fact that the current system does not explicitly guarantee the amount of minimum pension which means that the effects of ageing could be underestimated for those pensioners who will receive a supplementary social benefit on top of their pension. Pension expenditures do not include expenditures on years-of-service pensions of members of armed and police forces amounting to approx. 0.3 % of GDP. In accordance with the approved AWG methodology, expenditures on Christmas benefits have been also left out.

[23] To enable their international comparability, the expenditures on healthcare, long-term care, education and unemployment benefits are reported in line with the AWG definition and are precisely recorded in the "2012 Ageing Report."

[24] The fall in property income to GDP ratio in the AWG projections is not caused by demographic factors. It stems from the assumption that the debt development dynamics (as % of GDP) is, besides the influence of the interrelationship between the development of average interest rate and economic growth, determined exclusively by the general government primary balance. In the light of this assumption, it is implicitly assumed that the nominal sum of general government assets will remain fixed over time and that the income from them as a GDP ratio will be falling.

[25] The directive on the format and content of stability programmes and convergence programmes.

Commission for their examination and approval.[26] Updated forecasts were presented to and approved by the AWG in March 2013, and received final approval from the EPC (Economic Policy Committee) in April 2013.

BOX 5 – Legislative changes in the pension system – the 2012 pension reform

1. **Changes in the pension system's fully-funded pillar**
With effect from 1 September 2012, the pension contribution rate to the fully-funded pillar was reduced from 9 percent to 4 percent. From 2017 onwards, the contribution rate will be annually raised by 0.25 percentage point until 2024 when it will reach its final level of 6 percent. Moreover, between the beginning of September 2012 and the end of January 2013, the fully-funded pillar was opened both for exits and for new entrants. Since a part of the contributions paid to private pension fund management companies will be redirected to the general government sector, this will immediately increase revenues according to ESA95. A significant change is also represented by new rules applying to new entrants to the labour market; their entry into the fully-funded pillar is no longer automatic, but they must apply for it (they can make this decision up to 35 years of age).

2. **Linking the pension indexation mechanism to the pensioners' inflation rate**
The current method of increasing pensions (50 percent of the increase based on the inflation rate and 50 percent on the growth of average nominal wage in the economy) will be changed over the 2014-2018 period; the weight of inflation indexation will be annually increased by 10 percentage points, with parallel identical decreases in the weight of wage indexation. Starting in 2018, indexation of pensions will thus be equivalent to the rate of inflation of pensioners' households (the pensioners' inflation rate). In parallel, pensions will be temporarily raised between the years 2013 and 2017 by a fixed sum calculated as the indexation percentage for the average amount of the relevant type of pension.

3. **Increase in maximum assessment base**
With effect from 2013, maximum assessment base for social and health insurance payments was raised to 5 times the average wage in the economy, bringing increased revenues for the system, including in the long run. This measure will not have any impact on expenditures from the pay-as-you-go system, since the abovementioned increase will not result in increasing pension entitlements for the insured.

4. **Linking the retirement age to life expectancy trends**
Due to the on-going process of raising retirement age for women, adjustments in the retirement age of women will be linked with life expectancy only after the retirement age of childless women has become equal with that of men (from 2017 onwards). In order to ensure smooth and even adjustments, account will be taken of the five-year moving average of life expectancy. Based on the current demographic projections this would mean that the retirement age would be annually raised by approximately 50 days. The link between retirement age adjustments and life expectancy is automatic and is not subject to the subsequent approval by Government or Parliament.

5. **Strengthening solidarity in awarding pensions from the pay-as-you-go pillar**
This objective will be achieved by adjusting solidarity coefficients in the direction of moderate increases in low pensions and moderate reductions of higher pensions. This adjustment will be carried out between 2013 and 2018 gradually in order to prevent large divergences between the pensions of persons who meet identical parameters (such as years worked, career income).

The general government balance will be adversely influenced until 2060 by expenditures on pensions, healthcare and long-term care, and by the decline in income from property. Conversely, positive effects will be generated by the fully-funded pillar and by expenditures on education and unemployment benefits.

TAB 29 - Change in GG revenues and expenditures induced by demographic changes (% of GDP)

	2010	2020	2030	2040	2050	2060	Change 2010-2060
A. Revenue shortfall due to second pillar	**-1.1**	**-0.6**	**-0.6**	**-0.4**	**-0.2**	**-0.2**	**0.9**
B. Age-related expenditures	**17.8**	**18.0**	**18.7**	**19.8**	**21.6**	**23.3**	**5.5**
- Pension expenditure	8.0	8.0	8.1	8.5	9.5	10.6	2.7

[26] This is a standard procedure, the so-called peer review where a Member State may ask the AWG Working Group and the Commission to assess the update of projections upon implementation of a major reform.

- Health care	6.2	6.8	7.5	8.2	8.9	9.2	3.0
- Long-term care	0.3	0.3	0.4	0.5	0.5	0.7	0.4
- Education expenditure	3.1	2.8	2.7	2.5	2.6	2.7	-0.5
- Other age-related expenditures	0.2	0.1	0.1	0.1	0.1	0.1	-0.1
C. Property income	**1.4**	**1.1**	**1.0**	**1.0**	**1.0**	**1.0**	**-0.4**
Impact on general government balance							**-4.2**

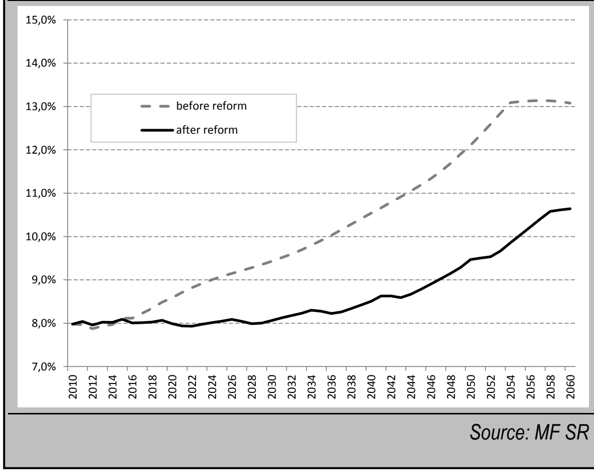
Source: MF SR, EC

If no remedial measures are taken in the relevant areas, adverse demographic trends and falling general government revenues will reduce the primary general government balance by the year 2060 by 4.2% of GDP.

BOX 6 – Impact of the pension reform on public finances

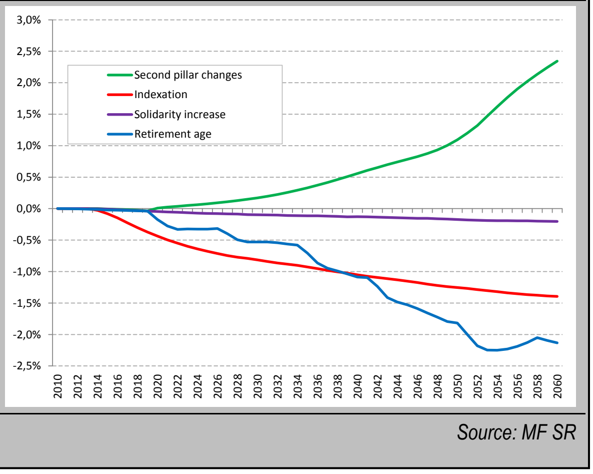
The following graphs present the impact of the pension reform on public finance, including the respective contributions of individual measures. Pension reform as a whole will reduce expenditures on pensions in 2060 by 2.6 % of GDP (compared with the pre-reform scenario).

GRAPH 23 - Public pension expenditures (% of GDP)



Source: MF SR

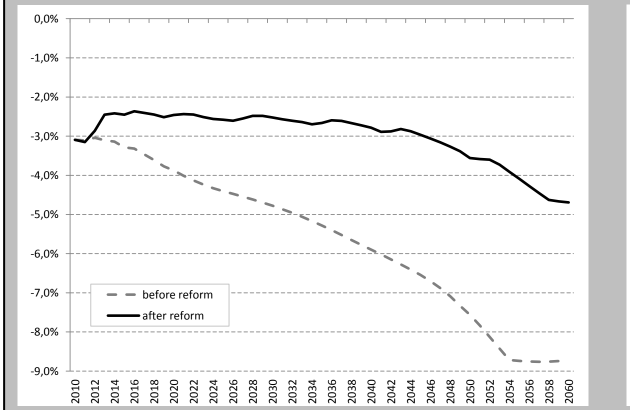
GRAPH 24 -Effect of individual reform measures on public pension expenditures (% of GDP)



Source: MF SR

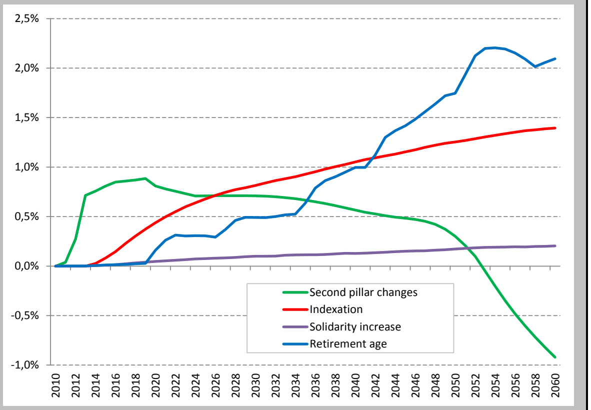
The most positive effect on pension expenditures is obtained from the increase in the retirement age and from changes in the indexation of pensions. The change in the solidarity aspect has only a slightly positive effect, while changes in the fully-funded have an adverse effect on expenditures.

GRAPH 25 - Public pension balance (% of GDP)



Source: MF SR

GRAPH 26 - Effect of individual reform measures on public pension balance (% of GDP)



Source: MF SR

Because the fully-funded changes are not introduced only on the expenditure side, it is necessary to examine the balance of revenues and expenditures of the pension system. The reform will have a positive effect on the balance of the pension system until 2050. However, adverse effects will prevail in the post-2050 period as a consequence of the reduced pension contribution rate (from 9 % to 6 %), and especially of the fact that the system became voluntary. However, the horizon of up to 2060 is too short for a comprehensive evaluation of the impact.

Assessment of long-term sustainability using sustainability indicators

The aim of the assessment of the long-term sustainability is to evaluate the current situation of public finances from the perspective of the future growth of age-related public finance expenditures (and/or fall in revenues) described in the preceding section, i. e. to judge whether the current policy mix (fiscal discipline, pension system, healthcare system) is sustainable in the long run (capable of preventing an uncontrolled growth of debt and maintaining its stable level) with the government debt at its present level. To this end, the Commission uses the so-called sustainability indicators[27]: *S1* indicator and *S2* indicator.

- ***S1 indicator*** (medium-term) – shows the value of the durable adjustment of the primary structural balance required to reach the gross debt level of 60% of GDP in 2030. Initially, the indicator recorded changes in the primary balance by the year 2060. Another change compared with the past is that the consolidation needed to reach the target debt is spread over several years (in the Commission's report, over the years 2015 to 2020). On the basis of the value of the S1 indicator, countries are classified into several risk groups – if their S1 indicator is lower than 0, they are classified as low risk. Indicator values between 0 and 3 place the countries in the medium risk group and the values of more than 3 in the high-risk group.

- ***S2 indicator*** (long-term) – shows the value of the durable adjustment of the current primary structural balance required to make the current value of future primary balances equal to the current level of gross debt. The countries whose S2 indicator is lower than 2 are classified as low risk. If the S2 indicator is higher than 6, the country is classified as high risk.

The Ministry of Finance evaluates the sustainability using the long-term sustainability indicator according to the Commission's methodology; however, in contrast to the Commission, the Ministry also includes in its calculation the impact of the fully-funded pillar not only on expenditures but also on revenues. In the opinion of the Ministry of

[27] European Commission-DG ECFIN (2012) Fiscal Sustainability Report 2012, European Economy, No. 8, 2012.

Finance, this approach is economically more appropriate because changes in fully-funded pillar systems affect not only the expenditures of pension systems, but also their revenues.

BOX 7 – Methodological differences between the calculation of sustainability indicators (COM vs. MF SR)

The table below compares the values of indicators after incorporating the impact of the fully-funded pillar on the revenues. The base year for the calculation is 2014 in which, according to the Commission's estimate, the structural primary balance would stand at -0.8 % of GDP and the debt at 55.9 % of GDP. The higher value of the indicator obtained under the MF SR approach results from the fact that the calculation was made before the pension reform (and before changes in the fully-funded pillar), when it was expected that social contribution revenues of the pension system would fall (especially because of the mandatory entry into the system). By contrast, the value of the MF SR indicator obtained after accounting for the impact of the reform will be lower than the value calculated by the Commission because social contribution revenues are expected to gradually increase as a result of the reduced pension contribution rate and the voluntary entry.

TAB 30 - Sustainability indicators

	S1	IBP	COD	DR	LTC	2P	S2	IBP	PE	HLC	EUB	2P
Správa Komisie	**2.2**	0.8	0.3	-0.2	1.3	-	**6.9**	1.8	3.5	1.7	-0.1	-
MF prístup	**2.3**	0.8	0.3	-0.2	1.3	0.2	**7.3**	1.8	3.5	1.7	-0.1	0.4

Source: Ageing report 2012, MF SR

IBP - initial budgetary position
COD – cost of delaying adjustment
DR – debt requirement in the final year
LTC – long-term component

2P - revenue shortfall due to second pillar
PE – pension expenditures
HLC – healthcare and long-term care
EUB – education and unemployment benefits expenditure

It follows from the Ministry of Finance quantification that if the consolidation objectives set out in the Stability Programme for 2016 (primary structural surplus of 1% of GDP and general government debt of 55.9% of GDP) are achieved, the achievement of **durable long-term sustainability of public finance (S2 indicator)** would**,** even in spite of the introduction of a pension reform, require an additional improvement of primary structural balance by 3.3% of GDP. This is due to the growth in expenditures on pensions, healthcare and long-term care, especially after 2030. However, such S2 indicator value will probably also mean the **reclassification of Slovakia among medium-risk countries**. The factor that significantly improves the S2 value (e.g. in comparison with the value of 7.3), besides the consolidation of public finances, is the pension reform which reduces the value of the indicator by additional 2.1 percentage points. In the absence of the reform, public finances would immediately require an additional consolidation by 5.4% of GDP. Even if Slovakia achieves its medium-term fiscal objective (MTO) in 2018, without further reforms of long-term public finance systems it would need an immediate additional consolidation by 2.7% of GDP in order to achieve the sustainability of public finance over the infinite period.

In the medium term (S1 indicator), no additional consolidation measures will be required to attain the 60% debt limit in 2030 **provided that the Government meets the Stability Programme objectives (2016) or MTO (2018), since the S1 values are negative.**

TAB 31 - Sustainability indicators S1 a S2

Scenario	S1	IBP	COD	DR	LTC	2P	S2	IBP	PE	HLC	EUB	2P
1. SP (without reform)	**0.4**	-0.6	0.0	-0.3	1.2	0.1	**5.4**	0.1	3.5	1.6	-0.1	0.3
2. SP (with reform)	**-0.5**	-0.7	-0.1	-0.3	0.4	0.1	**3.3**	0.0	1.5	2.2	-0.3	-0.2
3. MTO	**-1.5**	-1.2	-0.1	-0.7	0.4	0.1	**2.7**	-0.5	1.5	2.1	-0.2	-0.2

Source: MF SR

IBP - initial budgetary position
COD – cost of delaying adjustment
DR – debt requirement in the final year
LTC – long-term component

2P - revenue shortfall due to second pillar
PE – pension expenditures
HLC – healthcare and long-term care
EUB – education and unemployment benefits expenditure

TAB 32 - Assumptions used in computation of S1 and S2 indicators

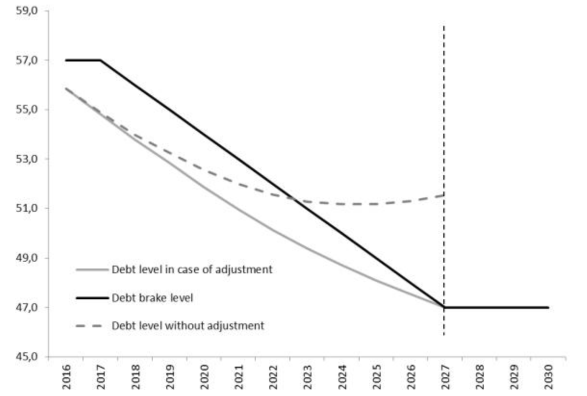
Scenario	base year (t_0)	SPB in t_0	debt in t_0	end year (t_1)	debt in t_1	adjustment
1.-2. SGP	2016	1.0	55.9	2030	60	2017- 2020
3. MTO	2018	1.5	51.6	2030	60	2019 - 2020

SPB - structural primary balance

Owing to the existence of Slovakia's national fiscal rules, the S1 indicator is not very practical in the Slovak context. The reason lies in the fact that according to debt brake provisions, the Government must submit the Parliament a balanced budget when the debt reaches the level of 57% of GDP. Moreover, the 57% limit will be decreasing in a linear fashion (by 1 percentage point a year) between 2018 and 2027 down to the 47% level. Because the future debt level is close to the limit, it is important to estimate whether the fulfilment of the objectives of the Stability Programme or of the MTO will be sufficient to avoid hitting the debt brake limit by 2027 when it will reach its final level of 47%.

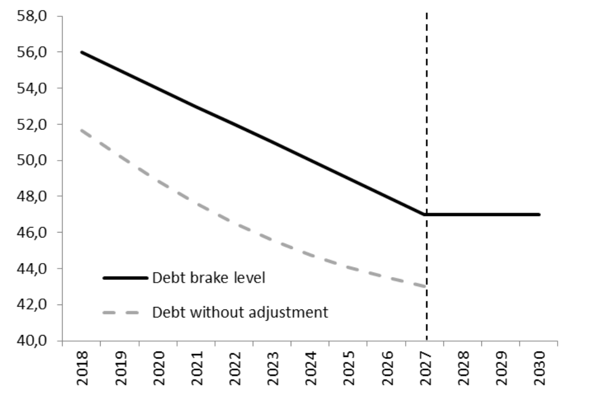
The next section therefore presents the quantification of a modified S1 sustainability indicator for the two above scenarios (SP and MTO), according to which the 47% debt level is to be achieved in 2027. The results indicate that even if fiscal objectives set out in the Stability Programme are achieved, **additional consolidation will be required if the Government is to avoid the debt brake limit for establishing a balanced budget. If the Government spreads this improvement over the years 2017 to 2027, the need for additional consolidation will be at the level of 0.7% of GDP.** If the Government decides for a more vigorous consolidation over a shorter time span, the need of consolidation would be lower. By contrast, if no additional consolidation were carried out, the debt level at which the Government would be required to establish a balanced budget **would be reached in 2023**[28].

GRAPH 27 - Dynamics of general government debt (SGP scenario) - comparison with the debt brake level



Source: MF SR

GRAPH 27 - Dynamics of general government debt (MTO scenario) - comparison with the debt brake level



Source: MF SR

In the MTO scenario, the gross debt falls to a level which enables the Government to avoid the obligation to establish a balanced budget (see the figure below), and **no additional consolidation measures are thus required.**

TAB 33 - Sustainability indicator S1- required additional effort to the debt level of 47%

Scenario	S1	IBP	COD	DR	LTC	2P
1. SP - debt level of 47% in 2027	**0.7**	-0.8	0.3	0.8	0.3	0.1
2. MTO - debt level of 47 % in 2027	**-0.8**	-1.3	-0.4	0.5	0.3	0.1

[28] It needs to be borne in mind that this is a simplified calculation of general government gross debt which takes into consideration only the direct influence of the balance on the gross debt (i.e. a zero stock-flow adjustment item).

TAB 34 - Assumptions used in computation of S1 indicator

Scenario	base year (t_0)	SPB in t_0	debt in t_0	end year (t_1)	debt in t_1	adjustment
1. SP - debt level of 47% in 2027	2016	1.0	55.9	2027	47	2017 - 2027
2. MTO - debt level of 47% in 2027	2018	1.5	51.6	2027	47	2019 - 2027

Source: MF SR

VI. QUALITY OF PUBLIC FINANCE

The 2013 Commission's Annual Growth Survey recommends the EU countries to focus, in order to achieve economic recovery, on the following key priorities at national and EU level:

- pursuing differentiated growth-friendly fiscal consolidation,
- restoring normal lending to the economy,
- promoting growth and competitiveness through structural reforms,
- tackling unemployment and the social consequences of the crisis,
- modernising public administration.

The main focus is on the fiscal consolidation as a necessary prerequisite for restoring macroeconomic and financial stability and confidence in the financial markets. The Commission also recommends to increase the effectiveness of public finances. In case of cuts in expenditures, it recommends using a selective approach. The cuts should not be made in education, science, research and innovations, energy and active labour market policies. In order to promote growth and employment, taxation of low-income work should be avoided. The Commission recommends focusing the additional tax burden on consumption, property and environmental taxes.

VI.1. Developments on the revenue side

The fact that the consolidation of public finance in 2013 is taking place mainly through changes on the revenue side has implications also for the qualitative side of general government revenues. The most important of these changes is the reduction of disparities in the tax and contribution burden (tax wedge) on different types of work. Moreover, the government has taken steps to counter tax evasion, mainly with a view to improving VAT collection. The fight against tax evasion will continue also in the forthcoming period; further steps will be taken towards unifying the collection of taxes, customs duties and social contributions, and improvements will be made in the tax mix with a view to ensuring a fairer taxation.

Reducing disparities in the tax wedge on different forms of work

As result of amendments to social insurance and health insurance acts effective from 2013, **the tax wedge on income** of temporary agreement workers (hired to perform specific work,) was put **on equal footing** with that on income of self-employed persons and of persons in dependent employment. Temporary agreement workers will continue to enjoy exemption in the case of secondary school students and full-time higher education students whose monthly income from one employer does not exceed EUR 155 (or EUR 66 for those under 18). Partial exemptions in connection with temporary agreement work will continue to apply also to pensioners, especially those receiving old-age or disability pensions. As regards self-employed persons, a change has been made in the calculation of their assessment base for the payment of social and health contributions; this will also contribute to equalising the tax burden on income from work. These changes, together with the adjustment of the minimum assessment base (applicable to 87% of self-employed persons), will contribute to increasing future pension entitlements of these persons. The amended income tax introducing a ceiling on flat-rate (deductible) expenditures is also expected to contribute to making taxation more equal.

Combating tax evasion

In May 2012, the Government adopted an Action Plan to Combat Tax Fraud, containing 50 concrete measures targeting mainly the collection of the value added tax, and approved amendments of several related acts. The Action Plan is to be implemented in three stages:

- The steps taken within the ongoing **stage one of the Action Plan** include the publication of lists of VAT-payers who fulfil the criteria for having their VAT registration withdrawn (e. g. persons avoiding communication or contact), and the introduction of joint tax liability. The amended act lays down the obligation of risky entitites applying for VAT registration to deposit a financial security. There is a new requirement that the tax reliability aspect must be considered and a certificate from the tax administrator must be submitted in the registration process of a new company or the transfer of a majority holding. Tax fraud and obstruction of tax administration were introduced as new types of criminal offences. Other legislative measures that already entered into effect include: mandatory monthly filing of VAT returns during a 12-month period for newly registred companies, reduction in the number of persons filing quarterly VAT returns, mandatory VAT registration prior to the first-time sale of real property, extension of the reverse-charge mechanism, stricter requirements concerning the application of special rules in transactions of second-hand goods, stricter requirements concerning tax representatives for imports of goods, obligation to produce evidence of intra-Community supply of goods, reduced threshold for documents serving as simplified invoices for cash payments using electronic cash registers, tax security deposits upon import from third countries.

- Other key measures that have already been implemented under the Action Plan include the introduction of obligatory non-cash payments in business transactions above a certain limit aimed at averting the issuance of fictitious invoices or cash register receipts not accompanied by the flow of funds. The Financial Directorate launched a programme for the fight against corruption in the financial administration aimed at eliminating corrupt behaviour inside financial administration. The "Tax Cobra", a specialised joint police and financial administration unit, was created to investigate serious tax-related crime, and the organisational structure of the police force was revamped in order to create specialised units for combating serious economic crime.

- **Phase two and phase three** of the Action Plan to Combat Tax Fraud will bring the obligation to submit information on domestic supplies of goods and services to the tax administrator in electronic form (control statement). This will increase the effectiveness of tax collection using the real-time analysis of detailed information from the corporate sphere and improve the targeting of tax controls. Moreover, the newly introduced mandatory rating of taxpayers will provide information on their financial stability and tax reliability. The Financial Directorate, working with the relevant ministries, will link its databases with the systems of registers containing records on taxpayers' assets (such as banks, building departments, motor vehicle and population registers, toll system); it will subsequently identify and analyse the risks for tax administration and select taxpayers for the performance of tax controls.

The fulfilment of all measures outlined in the 2012-2016 Action Plan to Combat Tax Fraud is on track, but efforts at fighting tax fraud are far from completed. The Ministry of Finance and the Financial Administration share the ambition of gradually expanding the already approved measures on fighting fraud to include new measures required by the needs of the application practice. An evaluation is currently underway to assess the use of instruments for the protection of the domestic tax base against erosion caused by crossborder tax planning; it will be followed by the drafting of relevant legislation expected to take effect from 2014, and by organisational changes that will become effective already in the course of 2013. These measures will be complemented by an analysis into the possibility of automatic reporting by Slovak financial institutions of crossborder transactions above a certain value to the financial administration.

Preparations for a lottery of cash register receipts are underway, aimed at motivating customers to request receipts for their payments, thus preventing tax evasion. The lottery will be organised through the network and well established communication channels of state lottery company Tipos, a.s. The Financial Administration and the Ministry of Finance launched a campaign aimed at involving all state and public employees into the effort to improve tax collection, which will be ultimately reflected in their own wage level.

Provision of information to natural persons and legal entities is one of the strategic objectives of the Financial Administration of the Slovak Republic that will contribute to improving the fulfilment of obligations of natural persons and legal entities under tax and customs legislation.

Uniform Collection of Taxes, Customs Duties and Insurance Contributions – UNITAS

The UNITAS project adopted as part of The Concept of Tax and Customs Administration Reform approved by the Government in 2008 has been implemented in the form of activities aimed at unifying collection of taxes and customs duties at the technological, organisational and procedural level (UNITAS I). At the beginning of 2012, the Customs Directorate of the Slovak Republic merged with the Tax Directorate of the Slovak Republic to create the

Financial Directorate of the Slovak Republic. Activities of the Tax Administration Criminal Bureau also contribute to improving tax collection.

The project envisages launching a parallel operation of the integrated information system of financial administration by mid-2014. The date on which the system is to be made operational has been set at 1 January 2015. Communication with the general public and with business entities will be greatly facilitated by linking electronic portals of the Financial Directorate, i.e. the Central Electronic Desk and the Financial Administration Portal. Unification of social insurance contributions (stage two of the programme – UNITAS II) is also in progress; its time frame and relevant activities are being currently prepared in cooperation with all stakeholders, especially the Social Insurance Agency.

Tax mix

One of the challenges for the tax system is the real estate tax reform designed to ensure fairness of taxation and, at the same time, generate more tax revenues for general government and/or create the possibility to reduce certain taxes with negative effects on economic growth. The real estate tax could play a more important role in the tax system than it did to date, as shown by the experience of the neighbouring countries, and also because of its less adverse effect on economic growth, high effectiveness of collection, and narrow space for tax avoidance.

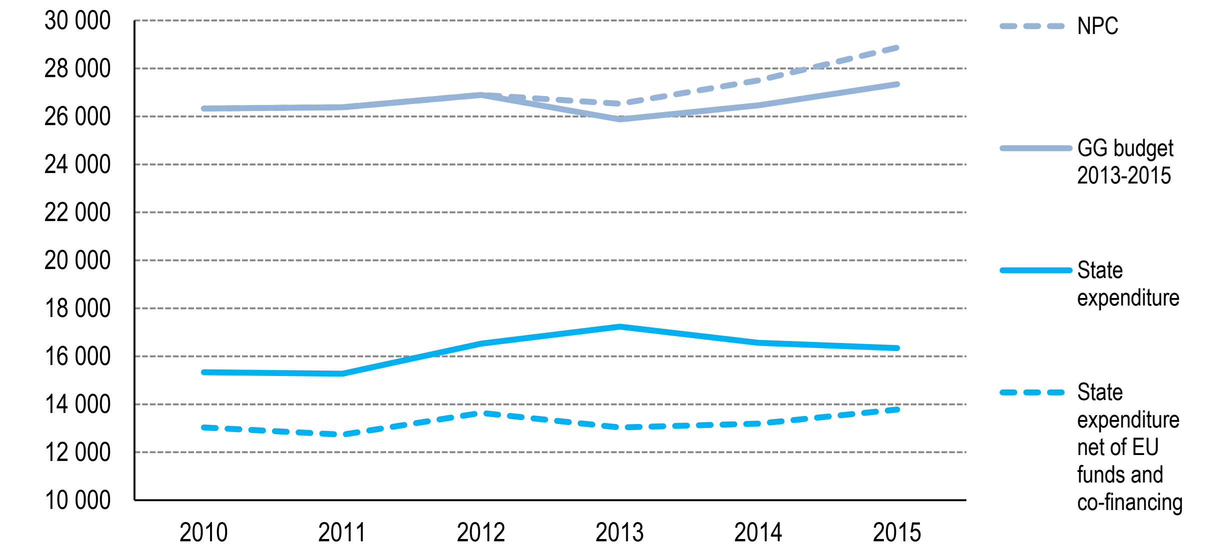
- Compared with other OECD or EU countries, **real estate taxes** in Slovakia represent an almost negligible portion of local governments' tax revenues, and administration costs related to this type of taxes often seem to be only slightly lower than the tax revenues themselves. Moreover, the current design of the system (the tax rate fixed in euro depending on the floor area) is unfair since the tax base does not reflect the actual value of the real property (defined by the location, age, amenities and other characteristics of the property) and is derived only from its floor area. This results in different tax burdens on real property (the ratio of the tax paid to the price of the property) and in the regressiveness of the system. The best solution from the tax fairness perspective would be to create a system linking the real property tax base with its market value. Such system would ensure that the tax base mirrors changes in the market value of the property, while effective taxation would remain constant at the unchanged rate. The Ministry of Finance currently considers various options of the system of taxation based on the market value of real estate. Concrete proposals will be presented in the course of 2013 and the new system will be introduced in 2015 at the latest.

- Other possibilities for improving the quality of public finance by means of the tax mix include increasing the share of **energy taxes** in the overall tax burden. There is only a limited possibility of raising the rates of taxes on fossil fuels in Slovakia due to the following reasons:
    - The limiting element for excise taxes on fuels (especially gasoline and diesel) is their final price which should be regionally competitive. However, gasoline price is already higher than average prices in the neighbouring countries. The price of diesel, which has a very high price elasticity of demand, has the same level as average prices in the region. Because of the geographical specificities of Slovakia, there is a risk that excessive fuel tax burden would not generate expected tax revenues.
    - The effect of a substantial increase in taxes on other energies (electricity, coal, natural gas) would be extremely regressive, i.e. a disproportionate burden would be placed on low-income households because the data on energy consumption, especially of natural gas, do not constitute a reliable basis for estimating the real wealth of households in Slovakia. However, raising tax rates is not the only option in Slovakia for increasing the share of energy taxes in the tax mix.
    - A relatively high number of optional (i.e. voluntary) tax exemptions were granted in Slovakia for these energies (electricity, coal, natural gas). The withdrawal of these exemptions would contribute to increasing tax revenues by approximately EUR 50 million a year.

VI.2. Developments on the expenditure side

The developments on the expenditure side reflect the on-going consolidation of public finance which brought a significant decrease in expenditures in 2013 compared with the previous year and with the no-policy-change scenario. General government expenditures will reach the level of EUR 25.9 billion in 2013 and are expected to grow to EUR 27.3 billion by 2015. However, the ratio of general government expenditures to GDP will gradually fall during the budgetary period from 34.8% to 33%. State budget expenditures in 2013 will slightly grow to the level of 23.2% of GDP, but this growth will stem exclusively from a significantly higher share of EU resources (EU funds hereinafter[29]) and co-financing.

GRAPH 29 – General government and state budget expenditures (in EUR mill.)



Source: MF SR

There are certain expenditures that do not fully meet the objectives for which they were allocated and do not contribute to sustainable economic growth. Ineffectively deployed resources unjustifiably increase state budget expenditures, a fact which is particularly evident in the period of on-going consolidation. The Government, in an effort to increase the effectiveness of public expenditures and promote growth within the existing budget envelope, therefore identifies the expenditures that fail to fully meet the objectives for which they were allocated. The real need to finance relevant budget items will be reassessed and the outcome of this exercise will be reflected in the elaboration of the general government budget for 2014.

As stated in the Government Manifesto, economisation of general government will be based on the examination of cost-effectiveness of individual general government products and/or activities. This makes it necessary to conduct a systematic evaluation of the performance of general government, using precise and clear **general government indicators** that will make it possible to evaluate the results and efficient fulfilment of not only the cross-sectional objectives of the Slovak Government, but also of the work of individual ministries and all other public finance chapters. The Government will improve its monitoring by developing a set of relevant indicators. The first set of indicators will be developed for the ministries responsible for the collection, monitoring and publication of relevant data. The monitoring of the results will be subsequently expanded also to other general government organisations and entities. At the same time, indicators will be regularly published and incorporated into the evaluation of general government effectiveness and into key documents, such as the general government budget or the National Reform Programme.

Priorities pursued by the Slovak Government with the aim to achieve sustainable economic growth, employment and quality of life as defined in the National Reform Programme include, besides fiscal policy, also education, science and innovation, employment and social inclusion, business environment, transport and telecommunication infrastructure, modern and effective public administration, healthcare, environmental sustainability and energy. To increase the effectiveness of drawing of EU funds, the Government has taken steps in 2013 in agreement with the European Commission to concentrate resources on better targeted projects in key

[29] They are also referred to as European Structural and Investment Funds (ESIF) comprising the European Regional Development Fund (ERDF), the European Social Fund (ESF), the Cohesion Fund (CF), the European Agricultural Fund for Rural Development (EAFRD) and the European Maritime and Fisheries Fund (EMFF).

areas. In the proposal for the 2014-2020 Multiannual Financial Framework of the EU, approved in the Council in February 2013, the EU funds allocation for the Slovak Republic is foreseen at EUR 18.2 billion. Also in this respect, the government will strive to prepare programme documents in order to achieve maximum efficiency.

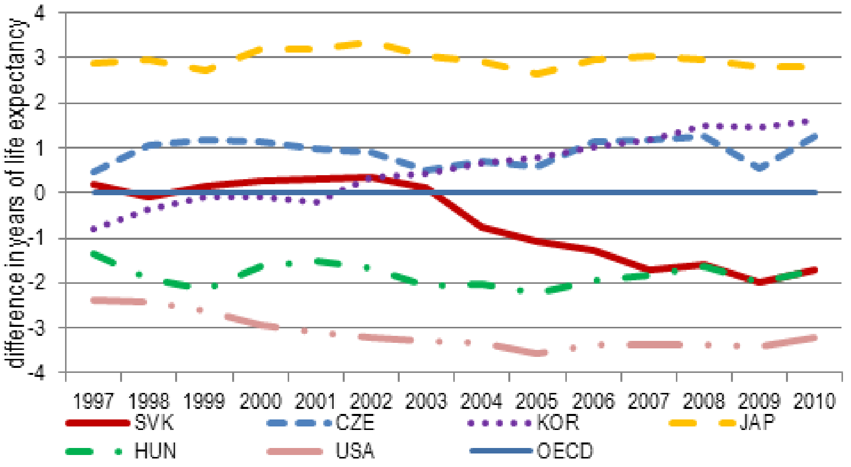
By 2020, the Government will increase the amount of public expenditure allocations on education to 6% of GDP. Prioritisation of education funding will require structural changes that will be designed to enhance the quality and effectiveness of the education system already in the short- and medium term. Expenditures on science, research and innovation will, after their increase in 2013, be slightly falling in the subsequent years because of the decline in EU funding. Educational outcomes, especially those of pupils from socially disadvantaged backgrounds, are the most strongly influenced at the level of pre-school and primary education. Consequently, the Government will support efforts at increasing the effectiveness of the school system through the inclusion of children from marginalised communities into the system of education with the aim of improving their educational outcomes. In addition, the quality of the regional school system will be enhanced by improving the status of teachers, continued external evaluation of schools, and better adaptation of vocational schools to the needs of the labour market. A reform will take place in connection with the funding of science, research and innovation. Greater emphasis will be laid on the results. The growth in expenditures in 2013 has the objective to build institutions and the research infrastructure. Other supported areas include the transfer of knowledge to practice and funding for innovative small and medium-sized enterprises.

Employment policy is designed to improve the skills of the unemployed and to increase their employment chances, thus contributing to improving the productivity of human capital. Allocations for employment policy in 2013 of almost EUR 265 million represent a 14% increase over 2012. The Government will continue to strengthen the effectiveness and efficiency of active labour market policies. The ESF will be used to promote youth employment, focusing on the prevention of the loss of skills and work habits of young people upon completion of their studies. Expenditures on social inclusion are also growing at a year-on-year rate of 1.6% in 2013, 2.5% in 2014, and 3.2% in 2015. The focus of structural policies in this area will be on better targeted social benefits and on the inclusion of marginalised communities. Employment of women will be promoted also by means of increasing the capacity of day nurseries and kindergartens, and by the continuation of childcare allowance payments.

The transport infrastructure will be expanded through motorway construction and rehabilitation of roads and railways. Expenditures allocated for this area in 2013 will grow by 38% (in comparison with the estimate for 2012), attaining their historically highest level. As much as one half of the costs will be covered from EU funds. More attention than to date will be given to the modernisation of main roads and railways. Train transport should be able to compete with automobile transport. The upcoming auction of telecommunication frequencies will strengthen the competition and increase state budget revenues.

Modernisation of public administration will be promoted by means of increasing expenditures into computerisation of society. Thanks to the uptake of EU funds under the programming period that is drawing to its end, they will increase year-on-year more than twofold. In the subsequent years they will stabilise at a level of around EUR 150 million a year. The aim of computerisation is to enable full electronic exchange of data between citizens, the public and the private sector, and between public authorities themselves. The reform implemented across the entire public administration will increase its effectiveness, reliability and openness. Mergers or closures of some public authorities in 2013-2016 and optimisation of their procedures are estimated to generate savings for the state of more than EUR 500 million. Analytical capabilities of state administration authorities will also continue to be strengthened.

GRAPH 30 – Efficiency of the Slovak healthcare system



Source: IFP, OECD

Effectiveness of the Slovak healthcare system is among the lowest in the OECD countries. A moderate nominal increase in expenditures into this sector will be therefore accompanied by measures designed to improve its effectiveness and quality of results. The Government will take steps to increase the long-term sustainability of the sector, to put a stop to the growing indebtedness of hospitals, and to strengthen their financial management. Unification of treatment methods and introduction of the DRG system will make it possible to better compare and control medical interventions, and will increase the transparency of the relations between hospitals and insurance companies. The Government will prepare the project of unitarisation of the public health system in the medium term and will examine the possibility of investment into new hospitals. The reform of the drug policy is also on-going.

The growing number of and the ever more demanding tasks in the area of climatic change impact reduction and environmental protection entail also increasing expenditures in this field. In 2013, the relevant budget heading was increased by 50% year-on-year, mainly as a result of income from emission trading under the EU ETS scheme and the uptake of EU funds. In view of the need for further reductions of greenhouse gas emissions, the Government will prepare a low-carbon strategy comprising an optimum set of measures for reducing emissions with emphasis on cost effectiveness. In parallel, support for renewable energies, combined heat and power cogeneration, and coal extraction will be reassessed with the aim to achieve EU objectives in this area in a cost-effective manner, and to minimise negative impact on electricity prices.

The Government will also continue to improve the business environment by increasing the transparency and enforceability of law. Due to the fact that these priorities fall within the competence of several government offices, it is not possible to quantify allocations on the implementation of policies in these fields. Structural measures will be therefore aimed mainly at reducing the administrative burden for entrepreneurs, increasing the transparency of regulation and effectiveness of judicial proceedings. The work on the digitalisation of the collection of laws will continue, as will the work on amending the execution procedure code and the civil procedure code.

TAB 35 – Expenditure on priorities in key areas (EUR mill.)

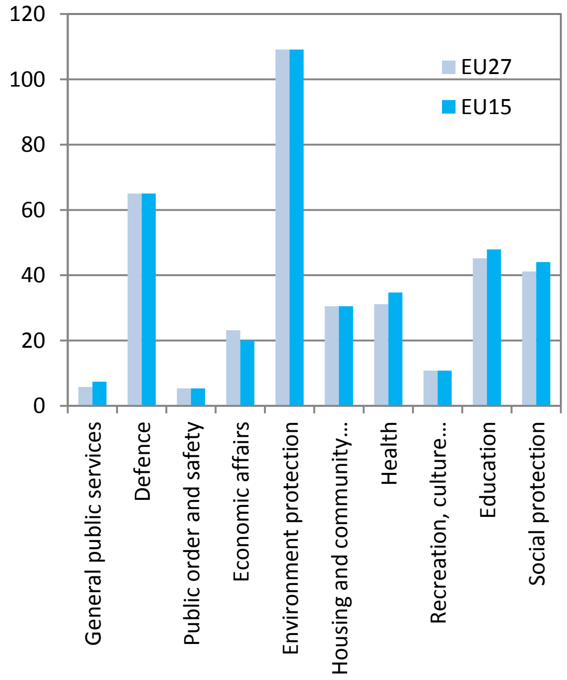
	2011O	2012E	2013	2014	2015
Education	1,776	1,824	1,824	1,827	1,826
- of which EU funds and co-financing	95	166	273	227	120
Science, research and innovations	318	472	550	460	409
- of which EU funds and co-financing	72	193	284	198	147
Employment	216	232	265	61	19
- of which EU funds and co-financing	131	170	248	55	13
Social inclusion	1,659	1,738	1,766	1,809	1,867
- of which EU funds and co-financing	12	33	39	44	60

Transport infrastructure	1,353	1,507	2,077	1,934	1,852
- of which EU funds and co-financing	332	580	1 035	892	620
Informatisaton of society	20	180	379	158	152
- of which EU funds and co-financing	4	101	374	152	147
Healthcare	3,747	3,968	4,063	4,187	4,386
- of which EU funds and co-financing	92	118	67	15	4
Environment protection	416	402	604	394	425
- of which EU funds and co-financing	328	349	534	344	375

Note.: O – outcome, E –estimate, 2013 – 2015 general government budget *Source: MF SR*

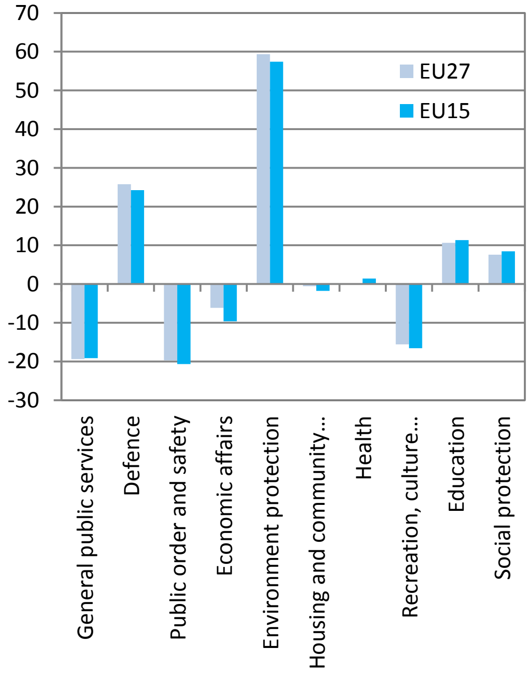
In international comparison, Slovakia has a significantly lower ratio of general government expenditure to GDP. This is largely due to the size of the public sector in Slovakia, which is one fourth smaller than the EU average. The sectors with comparatively lower shares in total general government expenditures are especially the defence, environmental protection, education, and social security. In contrast, spending is higher on public services (e.g. administration, public offices and debt service), public order and safety (e.g. police and judiciary), as well as on recreation, culture and religion. The level of Slovakia's spending on healthcare is comparable.

GRAPH 31 – Comparison of public expenditure of EU member states (% of GDP, percentage difference against SR)



Note: SVK – 2013, EÚ – 2011 *Source: Eurostat, SO SR, MF SR*

GRAPH 32 - Comparison of public expenditure of EU member states (% of GG expenditure, percantage difference against SR)



Note: SVK – 2013, EÚ – 2011 *Source: Eurostat, SO SR, MF SR*

VII. INSTITUTIONAL ASPECTS OF PUBLIC FINANCE

Institutional changes in public finance are taking place mainly in connection with the implementation of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union , and Council Directive 2011/85/EU of 8 November 2011 on requirements for budgetary frameworks of the Member States.

• Treaty on Stability, Coordination and Governance in the Economic and Monetary Union

Under the Treaty that entered into effect on 1 January 2013, the euro area countries have the obligation to implement certain provisions, i.e. the **fiscal compact**[30], within one year. Slovakia ratified the Treaty in December 2012 and after the submission of relevant documents the Treaty entered into force on 1 February 2013.

The fiscal compact includes the obligation to enact a rule on general government structural balance in the national legislation with a view to achieving the MTO**.** It also comprises a correction mechanism, which is automatically triggered in case of a significant deviation, and the definition of the tasks of an independent body to monitor compliance with these rules.

The process of drawing up the relevant legislation which is currently underway will lead to the adoption of concrete legislative provisions. The aim is to implement the fiscal compact through the amendment of the act on general government budgetary rules.[31] The time-frame for the convergence towards the medium-term fiscal objective is attached as annex to this document. The responsibility for monitoring compliance with the rule, identification of a significant deviation and of the facts allowing granting an exemption will be probably vested in the Council for Fiscal Responsibility. The correction mechanism will be probably linked to the change in the expenditure ceiling.

The introduction of a ceiling on expenditures was envisaged already in the previous Stability Programme. However, the need to implement the fiscal compact caused a delay, and the proposal can thus be brought in line with new fiscal rules.

• Directive on requirements for budgetary frameworks of the Member States

The Member States of the European Union should transpose the Directive by 31 December 2013. Most of its provisions have already been incorporated into the budgetary process, and the remaining ones will be implemented within the fixed deadline. The most significant changes include the timely publication of fiscal data, bringing the content of the multiannual budget in line with the minimum requirements of the directive, and improving the quality of fiscal rules.

With a view to the timely publication of data on economic performance of individual general government entities, the Ministry of Finance adopted a regulation[32] which defines the frequency of and the deadlines for the submission of financial statements by individual entities. Local government authorities submit the required data quarterly, all other entities monthly within the deadlines set out in the Directive.[33]

The three-year general government budget will also comprise a no-policy-change scenario, including the impact of the proposed measures to achieve the fiscal objectives.

[30] Articles 3 to 8 of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union.

[31] Act No. 523/2004 Coll. on budgetary rules for public administration bodies.

[32] Based on the Ministry of Finance Measure of 22 November 2012 MF/215513/2012-31.

[33] The deadline for quarterly-reported data is 30 calendar days after the end of the quarter, except for the data reported as to 31 December the deadline for which is 5 February. The deadline for monthly-reported data is the 26th day after the end of the month.

At the same time, fiscal rules will be reinforced by introducing a ceiling on expenditures. Expenditure ceiling will strengthen the multiannual planning horizon of the budget and, as a result of its link to the fiscal compact, will support convergence towards the MTO.

ANNEXES

Annex No. 1 – Required tables

Table 1a: Macroeconomic prospects (ESA95, EUR bn.)

		2012	2012	2013	2014	2015	2016
	ESA code	Level	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
1. Real GDP	B1*g	65.2	2.0	1.2	2.9	3.3	3.6
2. Nominal GDP	B1*g	71.5	3.4	3.1	5.0	5.5	5.6
	Components of real GDP						
3. Private consumption expenditure	P.3	32.8	-0.6	-0.1	1.5	2.6	3.2
4. Government consumption expenditure	P.3	10.6	-0.6	-0.9	-1.4	0.4	0.7
5. Gross fixed capital formation	P.51	14.8	-3.7	2.3	3.3	2.4	2.0
6. Changes in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	-	-1.1	-0.5	-0.2	-0.1	0.1
7. Export of goods and services	P.6	63.7	8.6	3.3	4.9	4.8	4.7
8. Imports of goods and services	P.7	55.8	2.8	3.5	4.1	4.0	4.3
	Contribution to real GDP growth						
9. Final domestic demand (total)		-	-1.3	0.3	1.3	1.9	2.2
10. Changes in inventories and net acquisition of valuables	P.52 + P.53	-	-2.2	0.6	0.3	0.1	0.2
11. External balance of goods and services	B.11	-	5.5	0.2	1.3	1.3	1.1

Source: SO SR, MF SR

Table 1b: Price developments (ESA95)

		2012	2012	2013	2014	2015	2016
	ESA code	Level	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
1. GDP deflator		1.10	1.4	1.9	2.0	2.1	2.0
2. Private consumption deflator		1.22	3.7	2.1	2.4	2.4	2.3
3. HICP		3.7	3.7	2.4	2.5	2.5	2.4
4. Public consumption deflator		1.19	1.9	2.0	2.2	2.2	2.1
5. Investment deflator		1.04	0.2	1.5	1.8	1.8	1.8
6. Export price deflator (goods and services)		1.07	1.4	1.9	2.0	1.9	1.6
7. Import price deflator (goods and services)		1.16	2.3	2.0	2.3	1.9	1.6

Source: MF SR

Table 1c: Labour market development (ESA95)

		2012	2012	2013	2014	2015	2016
	ESA code	Level	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
1. Employment, persons (thousands) [1]		2 209	0.1	-0.5	0.5	0.7	0.8
2. Employment, hours worked (thousands) [2]		3 944	-0,4	-0.8	0.3	0.7	0.8
3. Unemployment rate (%) [3]		14	14.0	14.3	13.8	13.0	12.1
4. Labour productivity per persons (EUR) [4]		29 557	2,1	1.7	2.3	2.6	2.8
5. Labour productivity per hours worked (EUR) [5]		16 579	2,7	2.0	2.6	2.6	2.8
6. Compensation of employees (EUR mill.)	D.1	26 465	2.5	2.8	3.5	4.4	4.7
7. Compensation per employee (EUR)		14 197	2.0	2.6	3.5	4.4	4.7

[1] Total occupied population, domestic concept – national accounts definition

[2] National accounts definition

[3] Harmonised definition according to Eurostat; levels

[4] Real GDP per person employed

[5] Real GDP per hour worked

Source: SO SR, MF SR

Table 1d: Sectoral balance (ESA95, % of GDP)

	ESA code	2012	2013	2014	2015	2016
1. Net lending / borrowing vis-à-vis the rest of the world	B.9	2.4	1.9	2.4	3.1	3.7
of which:						
- Balance on goods and services		3.4	3.3	4.0	4.8	5.4
- Balance of primary incomes and transfers		-2.9	-3.3	-3.4	-3.5	-3.5
- Capital account		1.9	1.9	1.9	1.8	1.8
2. Net lending / borrowing of the private sector	B.9	6.7	4.8	5.0	5.1	5.0
3. Net lending / borrowing of general government	EDP B.9	-4.3	-2.9	-2.6	-2.0	-1.3
4. Statistical discrepancy						

Source: MF SR

Table 2a: General government budgetary prospects *

	ESA code	2012 EUR mill.	2012 % of GDP	2013 % of GDP	2014 % of GDP	2015 % of GDP	2016 % of GDP
Net lending (EDP B.9) by sub-sector							
1. General government	S.13	-3 107	-4.3	-2.9	-3.3	-3.2	-2.4
2. Central government	S.1311	-3 449	-4.8	-3.2	-3.5	-3.7	-2.8
3. State government	S.1312	-	-	-	-	-	-
4. Local government	S.1313	97	0.1	0.2	0.1	0.4	0.3
5. Social security funds	S.1314	245	0.3	0.1	0.1	0.0	0.0
General government (S13)							
6. Total revenue	TR	23 651	33.1	34.1	31.8	30.6	31.7
7. Total expenditure	TE [1]	26 758	37.4	37.0	35.2	33.8	34.1
8. Net lending/borrowing	EDP B.9	-3 107	-4.3	-2.9	-3.3	-3.2	-2.4
9. Interest expenditure	EDP D.41	1 322	1.9	1.9	1.9	1.9	2.1
10. Primary balance	[2]	-1 785	-2.5	-1.0	-1.5	-1.2	-0.3
11. One-off and other temporary measures	[3]	77	0.1	0.8	0.4	0.0	0.0
Selected components of revenue							
12. Total taxes (12=12a+12b+12c)		11 031	15.4	15.7	15.2	14.9	14.8
12a. Taxes on production and imports	D.2	7 057	9.9	9.8	9.3	8.8	8.7
12b. Current taxes on income, wealth, etc.	D.5	3 973	5.6	5.9	5.9	6.0	6.1
12c. Capital taxes	D.91	0	0.0	0.0	0.0	0.0	0.0
13. Social contributions	D.61	9 065	12.7	13.4	12.8	12.7	12.7
14. Property income	D.4	835	1.2	1.0	0.8	0.7	0.8
15. Other	[4]	2 720	3.8	4.0	3.0	2.3	3.4
16=6. Total revenue	TR	23 651	33.1	34.1	31.8	30.6	31.7
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)	[5]	20 096	28.1	29.1	28.1	27.6	27.5
Selected components of expenditure							
17. Compensation of employees + intermediate consumption	D.1+P.2	8 101	11.3	10.4	10.3	9.6	10.9
17a. Compensation of employees	D.1	5 014	7.0	6.4	6.2	5.9	5.6
17b. Intermediate consumption	P.2	3 088	4.3	4.0	4.1	3.7	5.3
18. Total social payments		13 291	18.6	18.4	17.9	17.6	17.4
of which: unemployment benefits	[6]	176	0.2	0.2	0.2	0.2	0.2
18a. Social transfers in kind supplied via market producers	D.6311, D.63121, D.63131	3 502	4.9	5.1	4.9	4.9	4.8
18b. Social transfers other than in kind	D.62	9 790	13.7	13.3	13.0	12.8	12.5
19.=9. Interest expenditure	EDP D.41	1 323	1.9	1.9	1.9	1.9	2.1
20. Subsidies	D.3	994	1.4	1.2	1.1	1.1	1.0
21. Gross fixed capital formation	P.51	1 365	1.9	1.7	1.3	0.7	0.6
22. Capital transfers	D.9	583	0.8	0.8	0.8	0.7	0.1
23. Other	[7]	1 101	1.5	2.6	1.9	2.1	2.0
24=7. Total expenditure	TE [1]	26 758	37.4	37.0	35.2	33.8	34.1
p.m.: Government consumption (nominal)	P.3	12 510	17.5	16.8	16.7	15.9	17.2

Source: MF SR

[1] Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.

[2] The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9)

[3] A plus sign means deficit-reducing one-off measures

[4] P.11+P.12+P.131+D.39+D.7+D.9 other than D.91)

[5] Including those collected by the EU

[6] Comprises cash benefits (D.621 a D.624) and benefits supplied via market producers (D.631) in relation to unemployment benefits

[7] D.29+D4 (other than D.41) +D.5+D.7+P.52+P.53+K.2+D.8.

* Table reflects the 2014-2016 GG Budgetary Framework which means that the headline deficits are different from the targets of the Government. In order to achieve the fiscal targets, it will be necessary to adopt additional measures. Due to the fact that at the moment it is not known which measures will be adopted, it was not possible to prepare a table with GG revenues and expenditures reflecting fiscal targets for 2014-2016.

Table 2b: No-policy-change scenario

	2012 Level	2012 % of GDP	2013 % of GDP	2014 % of GDP	2015 % of GDP	2016 % of GDP
1. Total revenue at unchanged policies	23 651	33.1	33.8	31.8	30.5	31.6
2. Total expenditure at unchanged policie	26 758	37.4	37.0	35.5	34.2	34.7

Note: The base for the NPC purposes is the actual estimate for 2013 incl. EU funds and co-financing. Data for 2012 is the outcome for expenditures and revenues.

Source: MF SR

Table 2c: Amounts to be excluded from the expenditure benchmark

	2012 level	2012 % of GDP	2013 % of GDP	2014 % of GDP	2015 % of GDP	2016 % of GDP
1. Expenditure on EU programmes fully matched by EU funds revenue	807	1.1	2.0	1.3	0.7	1.9
2. Cyclical unemployment benefit expenditure	-2.1	0.0	0.0	0.0	0.0	0.0
3. Effect of discretionary revenue measures	300	0.4	1.7	-0.6	0.0	0.0
4. Revenue increases mandated by law	0.0	0.0	0.0	0.0	0.0	0.0

Source: MF SR

Table 3: General government expenditures by function (% of GDP)

	COFOG code	2011	2016*
1. General public services	1	5.9	
2. Defence	2	1.0	
3. Public order and safety	3	2.4	
4. Economic affairs	4	3.7	
5. Environmental protection	5	1.0	
6. Housing and community amenities	6	1.0	
7. Health	7	5.9	
8. Recreation, culture and religion	8	1.1	
9. Education	9	4.0	
10. Social protection	10	11.9	
11. Total expenditures	**TE**	**38.2**	

* Given the early stage of the budgetary process, data for 2016 in cofog classification are not available

Source: SO SR

Table 4 - General governement debt development (% of GDP)

	ESA code	2012	2013	2014	2015	2016
1. Gross debt		52.1	54.8	56.3	56.7	55.9
2. Change in gross debt ratio		8.8	2.6	1.5	0.4	-0.8
Contributions to change in gross debt						
3. Primary balance		2.5	1.0	0.7	0.1	-0.8
4. Interest expenditure	EDP D.41	1.9	1.9	1.9	1.9	2.1
5. Stock-flow adjustment		5.9	1.4	1.5	1.3	0.9
of which:		0.0	0.0	0.0	0.0	0.0
- differences between cash and accruals		-0.1	0.5	0.5	0.4	0.2
- net accumulation of financial assets		5.9	0.8	1.0	1.0	0.7
of which: revenues from privatisation		0.0	0.0	0.0	0.0	0.0
- valuation effects and others		0.2	0.1	0.0	-0.1	-0.1

p.m. implicit interest rate on debt	4.4	3.8	3.6	3.6	3.8
Other relevant variables					
6. Liquid financial assets	4.8	5.1	5.4	6.0	6.4
7. Net financial debt (7=1-6)	47.0	49.4	50.6	50.4	49.2
8. Debt repayment (existing debts) from previous year	3,3	4.2	4.9	4.9	5.1
9. Share of debt denominated in foreign currency	5,7	5.1	4.8	4.5	3.4
10. Average maturity (years)*	5.6	6.3	-	-	-

Note: * maturity of state debt

Source: MF SR

Table 5: Cyclical developments (% of GDP)

	ESA code	2012	2013	2014	2015	2016
1. Real GDP growth (%)		2.0	1.2	2.9	3.3	3.6
2. Net lending of general government	EDP B.9	-4.3	-2.9	-2.6	-2.0	-1.3
3. Interest expenditure	EDP D.41	1.9	1.9	1.9	1.9	2.1
4. One-off and other temporary measures	[1]	0.1	0.8	0.4	0.0	0.0
5. Potential GDP growth (%)		2.5	2.8	3.0	3.0	2.9
contributions:		0.0	0.0	0.0	0.0	0.0
- labour		0.0	0.4	0.5	0.2	0.0
- capital		0.6	0.6	0.6	0.8	0.9
- total factor productivity		1.9	1.9	1.9	1.9	2.0
6. Output gap		0.1	-1.5	-1.6	-1.2	-0.6
7. Cyclical budgetary component		0.0	-0.5	-0.5	-0.4	-0.2
8. Cyclically-adjusted balance (2 - 7)		-4.4	-2.4	-2.1	-1.6	-1.1
9. Cyclically-adjusted primary balance (8 + 3)		-2.5	-0.5	-0.2	0.4	1.0
10. Structural balance (8 - 4)		-4.5	-3.3	-2.5	-1.6	-1.1

[1] A plus sign means deficit-reducing one-off measure

Source: MF SR

Table 6: Comparison between the previous forecast and the updated forecast

	ESA code	Year	Year	Year	Year	Year
		2012	**2013**	**2014**	**2015**	**2016**
Real GDP growth (%)						
Previous update*		1.1	2.7	2.6	3.7	-
Current update		2.0	1.2	2.9	3.3	3.6
Difference		0.9	-1.5	-0.7	-0.4	-
General government balance (% of GDP)	EDP B.9					
Previous update*		-4.6	-2.9	-2.3	-1.7	-
Current update		-4.3	-2.9	-2.6	-2.0	-1.3
Difference		0.3	0.0	-0.3	-0.3	-
General government gross debt (% of GDP)						
Previous update*		50.2	52.0	53.0	52.3	-
Current update		52.1	54.8	56.3	56.7	55.9
Difference		1.9	2.8	3.3	4.4	-

*Note: * Stability Programme for 2012 - 2015*

Source: MF SR

Table 7 - Long-term sustainability of public finances (% of GDP)**						
	2010	**2020**	**2030**	**2040**	**2050**	**2060**
Total expenditure	**42.9**	**44.5**	**45.3**	**47.0**	**50.4**	**55.2**
Of which: age-related expenditures	**17.8**	**18.0**	**18.8**	**19.8**	**21.6**	**23.3**
A. Pension expenditure	8.0	8.0	8.1	8.5	9.5	10.6
1. Social security pension	8.0	8.0	8.1	8.5	9.5	10.6
a) Old-age and early pensions	6.1	6.0	5.8	6.1	7.0	8.0
b) Other pensions (disability, survivors)	1.9	2.0	2.2	2.4	2.4	2.6
2. Occupational pensions (if in general government)	-	-	-	-	-	-
B. Health care	6.2	6.8	7.5	8.2	8.9	9.2
C. Long-term care	0.3	0.3	0.4	0.5	0.5	0.7
D. Education expenditure	3.1	2.8	2.7	2.5	2.6	2.7
E. Other age-related expenditures	0.2	0.1	0.1	0.1	0.1	0.1
F. Interest expenditure*	1.3	2.7	2.7	3.4	5.0	8.1
Total revenue	**32.4**	**32.5**	**32.3**	**32.4**	**32.6**	**32.8**
Of which: property income (D.4)	1.4	1.1	1.0	1.0	1.0	1.0
Of which: pensions contributions	12.6	13.0	12.9	13.0	13.2	13.4
Pension reserve fund assets	-	-	-	-	-	-
Of which: consolidated public pension fund assets	-	-	-	-	-	-
Systemic pension reforms						
Social contributions diverted to voluntary private scheme	1.1	0.6	0.6	0.4	0.2	0.2
Pension expenditure paid by voluntary private scheme	-	-	-	-	-	-
Underlying assumptions						
Labour productivity growth	5.5	2.7	2	2	1.8	1.5
Real GDP growth	4.0	3.1	1.9	1.3	0.9	1.0
Participation rate males (aged 15-64)	76.4	77.4	75.8	75	76.5	77.6
Participation rate females (aged 15-64)	61.4	65	65.5	64.1	65.1	66.5
Total participation rate (aged 15-64)	68.9	71.2	70.7	69.6	70.8	72.1
Unemployment rate (aged 15-64)	14.4	13.1	8.1	7.5	7.3	7.3
Population aged 65+ over total population	12.3	16.4	20.7	24.4	29.9	33.5

**Stability programme scenario* *Source: MF SR*

***Age-related expenditures as well as macroeconomic assumptions were updated after issuing Ageing report 2012*

Table 7a: Contingent liabilities		
	2012	**2013 ***
	% of GDP	% of GDP
Public guarantees	0.05	
of which: linked to the financial sector	0.0	

** estimates for 2013 are not available* *Source: MF SR*

Table 8: Basic assumptions					
	2011	**2012**	**2013**	**2014**	**2015**
Short-term interest rate (annual average)	0.6	0.3	0.8	1.9	2.7
Long-term interest rate (annual average)	1.6	1.7	2.3	2.9	3.4
USD/€ exchange rate (annual average) (euro area and ERM II countries)	1.29	1.30	1.25	1.23	1.22
World excluding EU, GDP growth	3.9	4.0	4.5	4.6	4.6
EU GDP growth	-0.3	0.1	1.6	1.5	1.5
Growth of relevant foreign markets	-0.2	0.5	1.8	1.7	1.7
World import volumes, excluding EU	3.8	4.4	6.1	6.3	6.5
Oil prices (Brent, USD/barrel)	112	111.7	114.5	116.8	119.1

Source: Common external assumptions, MF SR

Annex No. 2 – Calendar of convergence towards the medium-term budgetary objective

Table 9 - Macroeconomic assumptions

	ESA code	2012	2012	2013	2014	2015	2016	2017	2018
		Outco me	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
1. Real GDP growth	B1*g	65.2	2.0	1.2	2.9	3.3	3.6	3.3	3.1
2. Nominal GDP growth	B1*g	71.5	3.4	3.1	5.0	5.5	5.6	5.3	5.0
3. GDP deflator growth		1.1	1.4	1.9	2.0	2.1	2.0	2.0	1.9
4. Potential GDP growth			2.5	2.8	3.0	3.0	2.9	2.9	2.9
5. Output gap			0.1	-1.5	-1.6	-1.2	-0.6	-0.2	0.0
6. Employment, persons (thous.) [1]			2 209	2 198	2 210	2 226	2 244	2 258	2 270
7. Employment, houres worked (mill.) [2]			3 944	3 912	3 926	3 954	3 986	4 012	4 032
8. Unemployment rate (%) [3]		14.0	0.4	0.5	-0.6	-0.8	-0.9	-0.6	-0.4
9. Gross fixed capital formation (constant prices)		14,8	-3.7	2.3	3.3	2.4	2.0	2.1	2.4
10. Compensation per employee (eur)		14 189	2.0	2.6	3.5	4.4	4.7	4.6	4.5

[1] Total employment, national accounts - home concept

Source: MFSR, SO SR

[2] According to national accounts definition

[3] Harmonized rate according to Eurostat, change in p.p.

Table 10 - Budgetary plan

% of GDP	ESA code	2012	2013	2014	2015	2016	2017	2018
1.General government balance	EDP B.9	-4.3	-2.9	-2.6	-2.0	-1.3	-0.7	-0.5
2. Structural balance		-4.5	-3.3	-2.5	-1.6	-1.1	-0.6	-0.5
3. Cyclical budgetary component		0.0	-0.5	-0.5	-0.4	-0.2	-0.1	0.0
4. One-offs and other temporary measures		0.1	0.8	0.4	0.0	0.0	0.0	0.0
5. General government balance	EDP B.9	-4.3	-2.9	-2.6	-2.0	-1.3	-0.7	-0.5
6. Total revenues		33.1	34.1	31.8	30.6	31.7	30.9	31.0
6a. Total revenues at no-policy-change scenario from 2013		-	33.8	31.8	30.5	31.6	30.8	30.9
7. Total expenditure *		37.4	37.0	34.4	32.6	33.0	31.5	31.5
7a. Interest expenditure	EDP D.41	1.9	1.9	1.9	1.9	2.1	2.0	2.0
7b. Expenditure on EU programmes fully matched by EU funds revenue		1.1	2.0	1.3	0.7	1.9	1.1	1.2
7c. Cyclical unemployment benefit expenditure		0.0	0.0	0.0	0.0	0.0	0.0	0.0
7d. Effect of discretionary revenue measures (y-o-y change)		0.4	1.7	-0.6	0.0	0.0	0.0	0.0
7e. Revenue increases mandated by law		0.0	0.0	0.0	0.0	0.0	0.0	0.0
7f. Gross fixed capital formation (actual)		1.9	1.7	1.3	0.7	0.6	0.6	0.6
7g. Gross fixed capital formation (average for t-3 to t)		2.1	2.0	1.7	1.3	1.0	0.7	0.6
8. Tax burden		28.1	29.1	28.1	27.6	27.5	27.5	27.4
9. Gross debt		52.1	54.8	56.3	56.7	55.9	53.7	51.6

* assuming, that the deficit targets will be met, ie. the figures are lowered by the amount of not specified measures

Source: MF SR

Annex No. 3 – Forecast of the Ministry of Finance - key macroeconomic and fiscal indicators till 2016

Table 11 - Estimate up to 2016

	unit	2012	2013F	2014F	2015F	2016F
GDP; constant prices	%	2.0	1.2	2.9	3.3	3.6
Final consumption of households	%	-0.6	-0.1	1.5	2.6	3.2
Final consumption of government	%	-0.6	-0.9	-1.4	0.4	0.7
Gross fixed capital formation	%	-3.7	2.3	3.3	2.4	2.0
Export of goods and services	%	8.6	3.3	4.9	4.8	4.7
Import of goods and services	%	2.8	3.5	4.1	4.0	4.3
Harmonised index of consumer prices (HICP) growth	%	3.7	2.4	2.5	2.5	2.3
Current account balance	% GDP	2.5	1.2	1.7	2.4	2.8
Average employment growth; LFS	%	0.6	-0.5	0.7	1.0	1.0
Average unemployment rate; LFS	%	13.9	14.3	13.8	13.0	12.1
Average registered unemployment rate	%	13.6	14.1	13.5	12.7	12.5
Average real growth of monthly wages	%	-1.1	0.1	1.1	1.9	2.3
GG balance (ESA 95)	% GDP	-4.3	-2.9	-2.6	-2.0	-1.3

F- forecast *Source: MF SR*

Annex No. 4 – Macroeconomic Forecasts Committee

In an effort to achieve a greater transparency and objectiveness of macroeconomic forecasts, the Ministry of Finance regularly consults the members of the Macroeconomic Forecasts Committee. At the January 2013 session of the Committee, most of its members assessed the medium-term macroeconomic forecast of the Ministry of Finance as being **realistic tending towards the optimistic.**

Assessment of Ministry of Finance´s forecast by members of committee

Member	Forecast assessment
NBS	realistic
Infostat	realistic
VÚB	optimistic
ING Bank	-
Tatrabanka	realistic
SLSP	optimistic
UNICREDIT Bank	realistic
ČSOB	realistic
Volksbank / Sberbank	optimistic
SAV	-

Source: Macroeconomic Forecasts Committee

Average forecasts of the selected indicators of the Slovakia's economic development by the members of the Macroeconomic Forecasts Committee (excluding MoF) and MoF forecasts

	2012	2013		2014		2015		2016	
in % if not indicated otherwise		MFC	MFSR	MFC	MFSR	MFC	MFSR	MFC	MFSR
GDP (real growth)	2.0	1.0	1.2	2.7	2.9	3.1	3.3	3.4	3.6
GDP (current prices; bn. EUR)	69.1	73.6	73.8	77.0	77.5	80.6	81.7	84.8	86.3
Final consumption of households (real growth)	-0.6	-0.3	-0.1	0.8	1.5	1.7	2.6	2.1	3.2
Final consumption of households (nominal growth)	3.1	2.2	2.0	3.6	3.9	4.5	5.0	5.0	5.6
Average monthly wages (real growth)	-1.1	-0.4	0.1	0.7	1.1	1.1	1.9	1.5	2.3
Average monthly wages (nominal growth)	2.4	1.9	2.3	3.2	3.5	4.0	4.4	4.4	4.7
Average employment growth, LFS	-0.1	-0.1	-0.3	0.3	0.5	0.5	0.7	0.7	0.8
Consumer price index, (average growth)	3.9	2.4	2.3	2.6	2.4	2.8	2.4	2.9	2.3
Current account balance (% of GDP)	2.5	1.6	1.2	1.9	1.7	1.9	2.4	1.8	2.8

Source: Committee for Macroeconomic Forecasts

Annex No. 5 – Tax Revenue Forecasts Committee

The meeting of the Macroeconomic Forecasting Committee was followed by a session of the Tax Forecasting Committee on 6 February 2013. At the session, the Ministry of Finance presented its updated medium-term forecast of tax revenues in 2013-2016. All Committee members consider the medium-term forecast of tax revenues and social fund contributions **to be realistic**.

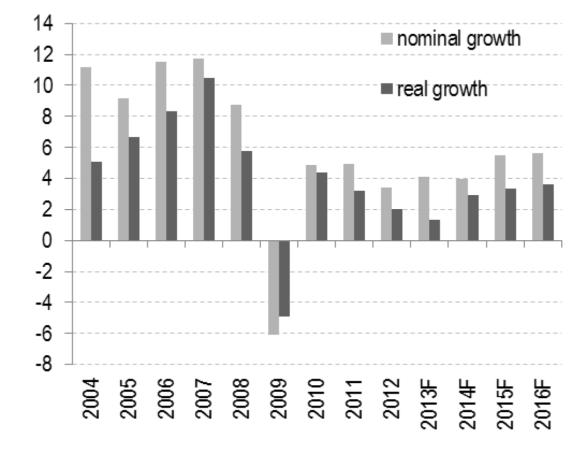
Assessment of MoF´s forecast by members of Tax Revenue Forecasts Committees

Member	Forecast assessment
NBS	realistic
Infostat	realistic
ING Bank	realistic
Tatra banka	realistic
ČSOB	realistic
SLSP	realistic
UniCredit Bank	realistic

Source: Tax Revenue Forecast Committee

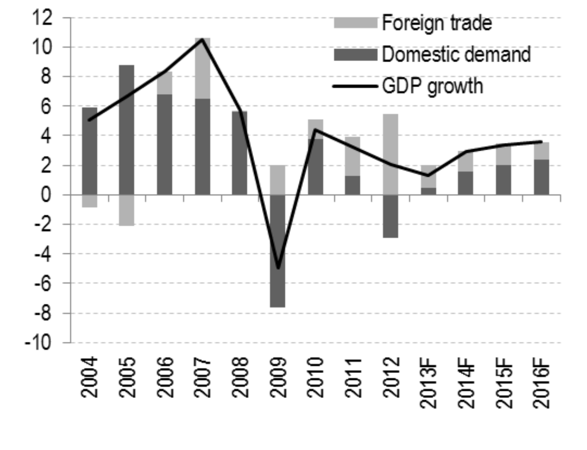
Annex No. 6 – Graphs

GDP growth (%)



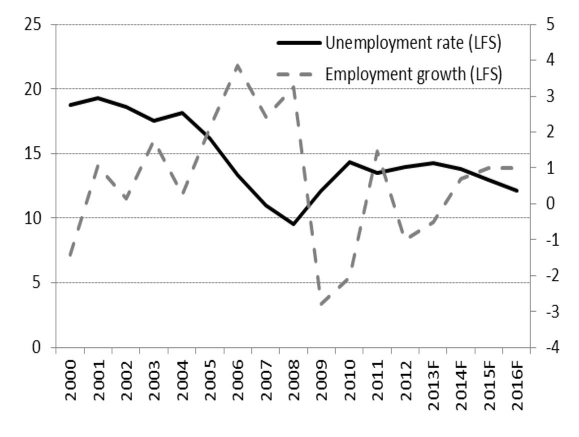
Source: SO SR, MF SR

Contributions to GDP growth (p. p.)



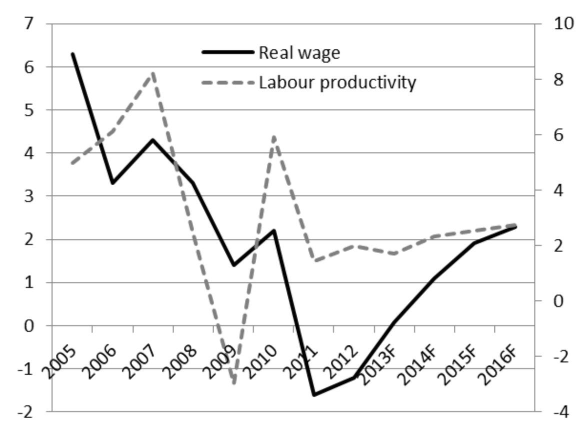
Source: SO SR, MF SR

Economic activity, LFS (%)



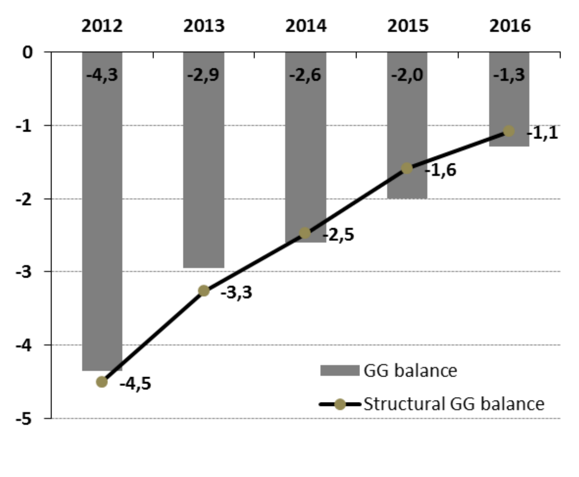
Source: SO SR, MF SR

Real wages and labour productivity growth (%)



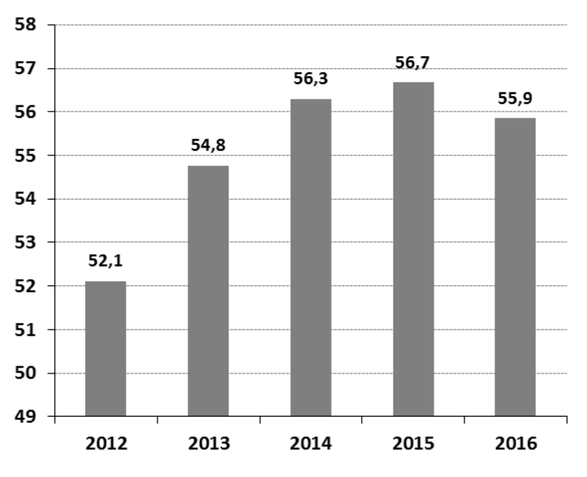
Source: SO SR, MF SR

General government deficit (% of GDP)



Source: SO SR, MF SR

Gross general government debt (% of GDP)



Source: SO SR, MF SR