EN

COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 11.11.2009
SEC(2009) 1538 final

COMMISSION OPINION

on the existence of an excessive deficit in Slovakia

Application of Article 104(5) of the Treaty establishing the European Community

COMMISSION OPINION

on the existence of an excessive deficit in Slovakia

THE APPLICATION OF THE STABILITY AND GROWTH PACT IN THE CURRENT CRISIS SITUATION

1. Many EU countries are presently facing general government deficits above the 3% of GDP reference value set in the Treaty. The often strong deterioration in the deficit as well as the debt positions must be seen in the context of the unprecedented global financial crisis and economic downturn in 2008/09. Several factors are at play. First, the economic downturn brings about declining tax revenue and rising social benefit expenditure (e.g. unemployment benefits). Second, recognising that budgetary policies have an important role to play in the current extraordinary economic situation, the Commission called for a fiscal stimulus in its November 2008 European Economic Recovery Plan (EERP), endorsed by the European Council in December. The Plan explicated that the stimulus should be timely, targeted and temporary and differentiated across Member States to reflect their different positions in terms of public finance sustainability and competitiveness and should be reversed when economic conditions improve. Finally, several countries have taken measures to stabilise the financial sector, some of which have impacted on the debt position or constitute a risk of higher deficits and debt in the future[1], although some of the costs of the government support could be recouped in the future.

2. The Stability and Growth Pact requires the Commission to initiate the excessive deficit procedure (EDP) whenever the deficit of a Member State exceeds the 3% of GDP reference value. The amendments to the Stability and Growth Pact in 2005 aimed at ensuring that in particular the economic and budgetary background was taken into account fully in all steps in the EDP. In this way, the Stability and Growth Pact provides the framework supporting government policies for a prompt return to sound budgetary positions taking account of the economic situation, and thereby ensuring long-term sustainability of public finances.

LEGAL BACKGROUND

3. Article 104 of the Treaty lays down an excessive deficit procedure (EDP). This procedure is further specified in Council Regulation (EC) No 1467/97 "on speeding up and clarifying the implementation of the excessive deficit procedure"[2], which is part of the Stability and Growth Pact.

---

[1] See the Eurostat decision of 15 July 2009 on the statistical recording of public interventions to support financial institutions and financial markets during the financial crisis, Eurostat News Release No 103/2009.

[2] OJ L 209, 2.8.1997, p. 6. Account is also taken of the Opinion of the Economic and Financial Committee on the "Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes", endorsed by the ECOFIN Council of 11 October 2005, available at: http://ec.europa.eu/economy_finance/other_pages/other_pages12638_en.htm.

4. According to Article 104(2) of the Treaty, the Commission has to monitor compliance with budgetary discipline on the basis of two criteria, namely: (a) whether the ratio of the planned or actual government deficit to gross domestic product (GDP) exceeds the reference value of 3% (unless either the ratio has declined substantially and continuously and reached a level that comes close to the reference value; or, alternatively, the excess over the reference value is only exceptional and temporary and the ratio remains close to the reference value); and (b) whether the ratio of government debt to GDP exceeds the reference value of 60% (unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace).

5. Article 104(3) stipulates that, if a Member State does not fulfil the requirements under one or both of these criteria, the Commission has to prepare a report. This report also has to "take into account whether the government deficit exceeds government investment expenditure and take into account all other relevant factors, including the medium-term economic and budgetary position of the Member State".

6. On the basis of the Commission services' spring 2009 forecast and in particular the forecast for the general government balance, which pointed to a risk of an excessive deficit, the Commission adopted a report under Article 104(3) for Slovakia on 7 October 2009[3].

7. Subsequently, and in accordance with Article 104(4), the Economic and Financial Committee formulated an opinion on the Commission report on 27 October 2009.

8. Article 104(5) of the Treaty requires the Commission to address an opinion to the Council if the Commission considers that an excessive deficit in a Member State exists or may occur. In order to reach a conclusion on whether an excessive deficit exists or may occur, the Commission considers that account should be taken of: (i) the conclusions of its report under Article 104(3) and (ii) the opinion of the Economic and Financial Committee on this report. On the basis of these elements, the Commission has established a number of considerations for Slovakia.

CONSIDERATIONS CONCERNING SLOVAKIA

9. An EDP for Slovakia was initiated in May 2004 by the Commission with the adoption of a report under Article 104(3) in view of a deficit of 3.6% of GDP in 2003[4], i.e. above the reference value. On 5 July 2004, following a recommendation from the Commission, the Council decided that the Slovak republic was in excessive deficit according to Article 104(6) and addressed recommendations to Slovakia in line with Article 104(7) with a view to bringing the deficit below 3% of GDP by 2007 at latest. On 3 June 2008, following an overall assessment which showed that the correction of the excessive deficit situation in Slovakia was completed in 2007, the Council decided to abrogate its decision on the existence of an excessive deficit in Slovakia under Article 104(12).

---

[3] All EDP-related documents for Slovakia can be found at the following website: http://ec.europa.eu/economy_finance/netstartsearch/pdfsearch/pdf.cfm?mode=_m2.

[4] The general government deficit was subsequently revised downwards in the April 2007 notification due to a data revision resulting from a change in the accrualization method for tax revenue.

10. In 2007, the general government deficit declined to 1.9% of GDP, mainly reflecting exceptionally strong economic growth of 10.4%. While decelerating, real GDP growth remained very high at 6.4% in 2008, but the government deficit started to deteriorate on the back of rapid spending growth, reaching 2.3% of GDP. The structural balance deteriorated during 2007-2008, implying insufficient use of favourable economic environment to further consolidate public finances.

11. The Commission services' spring 2009 forecast projected the general government deficit in Slovakia at 4.7% of GDP in 2009, thus exceeding the 3% of GDP reference value. The Commission report under Article 104(3) considered that the projected deficit was not close to the 3% of GDP reference value but that the projected excess over the reference value could be qualified as exceptional within the meaning of the Treaty and the Stability and Growth Pact, on the basis of the information available at the time of the report. Furthermore, the projected excess over the reference value could not be considered temporary. The report under Article 104(3) concluded that there was a high risk that the deficit criterion in the Treaty was not fulfilled.

12. According to the data notified by the Slovak authorities in October 2009[5] the general government deficit in Slovakia is now planned to reach 6.3% of GDP in 2009, thus remaining above and not close to the 3% of GDP reference value. Based on the Commission services' autumn 2009 forecast, the planned excess over the reference value still qualifies as exceptional within the meaning of the Treaty and the Stability and Growth Pact. In particular, it results, among other things, from a severe economic downturn in the sense of the Treaty and the Stability and Growth Pact. The Commission services' 2009 autumn forecast projects real GDP to contract by 5.8% in 2009 after increases of 10.4% and 6.4% in 2007 and 2008, respectively. While the excess over the 3% reference value mainly reflects the severity of the economic downturn, it also results from the significant deterioration of the structural balance since 2005. Furthermore, the planned excess over the reference value cannot be considered temporary, since the Commission services' autumn 2009 forecast projects the general government deficit to reach 6% of GDP in 2010 and 5.5% of GDP in 2011 based on the no-policy change assumption. The forecast takes into account the fiscal stimulus package introduced by the Slovak government amounting to 0.4% of GDP in 2009 and 0.6% of GDP in 2010, which is in line with the EERP and is an adequate response to the crisis given the limited fiscal space. The adopted measures target disadvantaged groups (e.g. an increase of the tax allowance and tax credit), and are in most cases of temporary nature (e.g. car scrapping scheme). The deficit criterion in the Treaty is not fulfilled.

13. According to data notified by the Slovak authorities in October 2009, the general government gross debt remains well below the 60% of GDP reference value and is planned to stand at around 30% of GDP in 2009. According to the Commission services' autumn forecast, the debt ratio is set to increase rapidly, reaching 42.7% of GDP in 2011 under the no policy change assumption.

---

5 According to Council Regulation (EC) No 479/2009, Member States have to report to the Commission, twice a year, their planned and actual government deficit and debt levels. The most recent notifications of Slovakia can be found at: http://epp.eurostat.ec.europa.eu/portal/page/portal/government_finance_statistics/procedure/edp_notification_tables.

14. In line with the provisions in the Stability and Growth Pact, the Commission in its 104(3) report gave due consideration to systemic pension reforms introducing a multi-pillar system that includes a mandatory, fully funded pillar. While the implementation of these reforms leads to a temporary deterioration of the budgetary position, the long-term sustainability of public finances clearly improves. Based on the estimates of the Slovak authorities, the net costs of this reform amount to 1.1% of GDP in 2009-2011, rising to 1.2% in 2012. According to the Stability and Growth Pact, these can be taken into account on a linear degressive basis for a transitory period and only in case where the deficit remains close to the reference value. Since the deficit does not remain close to the reference value in 2009-2011, the cost of the pension reform cannot be taken into account.

15. In line with the provisions in the Treaty and the Stability and Growth Pact, the Commission also analysed in its report “relevant factors”. According to the Stability and Growth Pact, these can only be taken into account in the steps leading to the decision on the existence of an excessive deficit if the deficit satisfies the double condition of closeness and temporariness. In the case of Slovakia, the double condition is not met. Considered on their own merit, the relevant factors in the current case on balance present a mixed picture.

16. The opinion of the Economic and Financial Committee in accordance with Article 104(4) of the Treaty is consistent with the assessment in the Commission report under Article 104(3).

CONCLUSION

17. The monitoring of the budgetary situation in Slovakia and, in particular, the examination of the compliance with the criteria laid down in Article 104(2) has led the Commission to prepare a report in accordance with Article 104(3) of the Treaty. The Commission, having taken into account its report and the opinion of the Economic and Financial Committee, is of the opinion that an excessive deficit exists in Slovakia.