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COMMISSION OPINION

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GENERAL CONSIDERATIONS

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

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

CONSIDERATIONS CONCERNING SLOVAKIA

3. On the basis of the Draft Budgetary Plan for 2017 submitted on 12 October 2016 by Slovakia, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

4. The Commission opinion is to be seen in light of the latest economic and budgetary data. In this context, as indicated in the Commission recommendation for a Council Recommendation on the economic policy of the euro area as well as in the Commission Communication 'Towards a positive fiscal stance for the euro area', it is important that the aggregate fiscal stance of the euro area is positive and supports the ongoing recovery, while ensuring the long-term sustainability of national public finances.

5. Slovakia is subject to the preventive arm of the SGP and should ensure sufficient progress towards its medium-term budgetary objective (MTO) set at -0.5% of GDP in structural terms. In particular, in its country-specific recommendations, the Council on 12 July 2016 recommended Slovakia to achieve an annual fiscal adjustment of 0.25% of GDP towards the MTO in 2016 and of 0.5% of GDP in 2017.

6. The macroeconomic assumptions underpinning the Draft Budgetary Plan appear to be plausible in both years. After an investment-driven expansion in 2015, annual real GDP growth in Slovakia is set to remain solid at 3.6% in 2016, according to the Draft Budgetary Plan. Strengthening private consumption and net exports are expected to largely offset the downturn in public investment linked to the cycle of EU investment co-funding. The Slovak economy is forecast to expand by 3.5% in 2017, with household spending and net exports remaining the main drivers of growth. Compared with the latest Stability Programme, real GDP growth in 2016 was revised upwards, mainly on the back of stronger government consumption. The Draft Budgetary Plan macroeconomic projections are broadly in line with the Commission 2016 autumn forecast, with the latter projecting a slightly slower pace of economic expansion in both years.

7. Slovakia complies with the requirement of Regulation (EU) No 473/2013 that the draft budget has to be based on independently endorsed or produced macroeconomic

forecasts. The macroeconomic forecasts underlying the Draft Budgetary Plan have been produced by the Institute for Financial Policy (IFP) of the Ministry of Finance and have been endorsed by the Macroeconomic Forecasting Committee (MFC). The independence of the MFC from government influence is anchored in its statutes.

8. The Draft Budgetary Plan projects the deficit to decline to 2.0% of GDP in 2016 and to decrease further to 1.3% of GDP in 2017. The target for 2016 is 0.1% of GDP lower compared to the latest Stability Programme while it remains unchanged for 2017. The difference in 2016 is mainly on account of higher receipts from taxes and social contributions compared to the latest Stability Programme. These outweigh higher-than-budgeted spending on investment, intermediate consumption and wages, as well as higher-than-expected financial corrections related to EU-financed projects.

The Draft Budgetary Plan projects the general government debt to increase to 53.5% of GDP in 2016, 0.6 percentage points higher compared to the 2016 Stability Programme. This is mainly due to the expected increase of cash reserves in order to secure debt repayments in early 2017. After peaking in 2016, the Draft Budgetary Plan projects the debt-to-GDP ratio to decline to some 52.7% in 2017. The Commission forecast projects the same debt ratio in 2017.

The public finances of Slovakia have benefitted from interest rate windfalls of some 0.3% of GDP over the period 2012-2016. Their contribution to the cumulative improvement in the structural balance of 1.6% of GDP over the same period has thus been rather limited. The Draft Budgetary Plan expects additional interest windfalls of 0.2% of GDP for 2017. The (recalculated) structural balance is set to improve from -2.3% of GDP in 2015 to -2.0% of GDP in 2016 and further to -1.4% of GDP in 2017, driven mainly by a better primary balance.

9. The Draft Budgetary Plan presents several consolidation measures on the revenue side (0.4% of GDP) in 2017 which are however outweighed by additional spending (1.5% of GDP) when compared to the no-policy-change scenario. On the revenue side, income from measures including the extension and increase of the levy on companies in regulated industries and the prolongation of the bank levy is projected to be higher than the shortfall due to a reduction of the corporate income tax rate and higher lump-sum deductions for self-employed. On the expenditure side, the Draft Budgetary Plan plans measures that would, on balance, increase the overall spending. Despite the fact that the measures introduced in the Draft Budgetary Plan increase revenues and expenditures, the revenue-to-GDP ratio is projected to remain stable while the expenditure-to-GDP ratio is set to decline compared to 2016. This suggests that growth of expenditure assumed under the no-policy-change baseline scenario is very subdued. In addition to the revenue measures included in the Draft Budgetary Plan, in 2017 the Commission forecast also expects higher revenue from an increase of the ceiling for social contributions which was adopted by the Parliament after the submission of the Draft Budgetary Plan. This additional revenue is assumed to be spent on social policies. In terms of expenditure, the Commission forecast takes into account all measures but given different projections of the evolution of the individual expenditure aggregates, overall expenditure expressed as a share of GDP increases.

10. The Commission 2016 autumn forecast projects the deficits at 2.2% of GDP in 2016 and 1.5% of GDP in 2017. Despite projecting higher revenues in 2017, the Commission projects the deficit to be some 0.2% of GDP higher compared to the Draft Budgetary Plan. This is mainly on account of different expectations on public wage developments. While the Commission projects wages in the public sector to

retain the dynamics of previous years also given favourable labour market developments, the Draft Budgetary Plan assumes a relatively low growth of employees' compensations below 2%. The Commission also projects a less marked decline in the social spending-to-GDP ratio, as it expects that additional revenue from higher social contributions will be used on social policies. Addressing inefficiencies in the healthcare sector, as identified in the context of the Value for Money project, frees resources which however are planned to be reallocated within the sector rather than resulting in lower expenditure. The structural balance in the Commission forecast is set to improve from -2.0% in 2016 to -1.4% of GDP in 2017 driven by the improvement in the primary balance.

11. Over 2016, the figures in the Draft Budgetary Plan point to compliance with the requirements under both the structural balance and the expenditure benchmark pillars. When looking over 2015-2016 together, the (recalculated) structural balance pillar points to a risk of some deviation (a gap of 0.1% of GDP) while the expenditure benchmark pillar suggests a risk of significant deviation with a gap of 0.3% of GDP. This warrants an overall assessment. In both cases, the results are driven by the 2015 outcomes, which were largely impacted by a surge in drawdown of EU funds and consequently higher domestic expenditure for co-financing. In addition, the expenditure benchmark pillar was negatively impacted by a base effect induced by past one-off revenue in 2014. Correcting for these effects in 2015, the two-year average for the expenditure benchmark points to some deviation, as does the structural balance. Therefore, information provided in the Draft Budgetary Plan points to a risk of some deviation in 2016. Based on the Commission 2016 autumn forecast, the structural balance pillar would be respected in 2016, while a risk of some deviation is detected under the expenditure benchmark pillar. The expenditure benchmark appears to account more adequately the swings in expenditure on public investment which were particularly pronounced in 2015 due to Slovakia's high absorption of EU funds; moreover it does not take into account savings stemming from lower interest expenditure. As a result the overall assessment points to some deviation based on the Commission forecast. The same goes for 2015-2016 together, in line with the assessment on the basis of the Draft Budgetary Plan.

For 2017, both the (recalculated) structural balance of the Draft Budgetary Plan and the expenditure benchmark point to adherence to the required adjustment of 0.5% of GDP. While the Commission forecast suggests compliance under the structural balance pillar, it signals a risk of some deviation based on the growth rate of government expenditure, net of discretionary revenue measures (a gap of 0.2% of GDP). This is the case for 2017 and over 2016-2017 taken together. Hence, an overall assessment is required. The expenditure benchmark appears to better capture fiscal effort of the government, as it is netted from windfall savings induced by falling interest expenditure and it better accounts for the dynamics in government investment which peaked in 2015 due to the higher absorption of EU funds. An overall assessment based on the Commission 2016 autumn forecast hence points to a risk of some deviation from the required adjustment path towards the MTO in 2017.

In light of the Commission's assessment of additional information about the budgeting of expenditure on the public wage bill, provided by the Slovak authorities and published on the website of the Ministry of Finance, the Commission considers that the projected change in the expenditure benchmark in 2017 would be in line with the requirement. On this basis, the overall assessment points to compliance.

12. The Draft Budgetary Plan includes several policy measures related to the country-specific recommendations issued by the Council in July 2016 in the area of the cost-effectiveness of the healthcare system and tax compliance. The response to the former is covered under the first vintage of the expenditure reviews in the context of the 'Value for Money' project which analysed efficiency of outlays in healthcare, transport and IT. Several measures are envisaged also in the area of tax compliance although these appear to be rather limited in scope.

13. Overall, the Commission is of the opinion that the Draft Budgetary Plan of Slovakia, which is currently under the preventive arm is compliant with the provisions of the SGP. In line with the Commission Communication 'Towards a positive fiscal stance for the euro area', the Commission invites the authorities to rigorously implement the 2017 budget.

    The Commission is also of the opinion that Slovakia has made some progress with regard to the structural part of the fiscal country specific recommendations issued by the Council in the context of the 2016 European Semester and invites the authorities to make further progress especially in the area of improving tax compliance. A comprehensive assessment of progress made with the implementation of the country-specific recommendations will be made in the 2017 Country Reports and in the context of the country-specific recommendations to be adopted by the Council in 2017.

Done at Brussels, 16.11.2016

For the Commission
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Member of the Commission