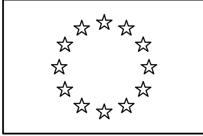

EUROPEAN COMMISSION
DIRECTORATE GENERAL
ECONOMIC AND FINANCIAL AFFAIRS

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SLOVAKIA: MACRO FISCAL ASSESSMENT

AN ANALYSIS OF THE JANUARY 2010 UPDATE OF THE STABILITY PROGRAMME

The Stability and Growth Pact requires each EU Member State to present an annual update of its medium-term fiscal programme, called 'stability programme' for countries that have adopted the euro as their currency and 'convergence programme' for those that have not. The most recent update of Slovakia's stability programme was submitted on 29 January 2010.

The attached technical analysis of the programme prepared by the staff and under the responsibility of the Directorate-General for Economic and Financial Affairs (DG ECFIN) of the European Commission, was finalised on 17 March 2010. Comments should be sent to Vladimír Solanič and Petr Maleček (Vladimir.Solanic@ec.europa.eu, Petr.Malecek@ec.europa.eu). The main aim of the analysis is to assess the realism of the budgetary strategy presented in the programme as well as its compliance with the requirements of the Stability and Growth Pact. However, the analysis also looks at the overall macro-economic performance of the country and highlights relevant policy challenges.

The analysis takes into account (i) the Commission services' autumn 2009 forecast, (ii) the code of conduct ("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 10 November 2009) and (iii) the commonly agreed methodology for the estimation of potential output and cyclically-adjusted balances.

Based on this analysis, the European Commission adopted a recommendation for a Council opinion on the programme on 17 March 2010. The ECOFIN Council is expected to discuss the opinion on the programme on 16 April 2010.

* * *

All these documents, as well as the provisions of the Stability and Growth Pact, can be found on the following website:

http://ec.europa.eu/economy_finance/sgp/index_en.htm

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1. INTRODUCTION

This document assesses the January 2010 update of the Slovakia's stability programme, which was submitted on 29 January 2010 and covers the period 2009-2012. The programme builds on the 2010-2012 budget approved by government and parliament. The programme was approved by the government and presented to parliament for a debate (without a vote).

This assessment is structured as follows. Section 2 discusses the key challenges for public finances in Slovakia. Section 3 assesses the plausibility of the macroeconomic scenario underpinning the public finance projections of the stability programme against the background of the Commission services' economic forecasts[1]. Section 4 analyses budgetary implementation in the year 2009, the budgetary plans for 2010 and the medium-term budgetary strategy. It also assesses risks attached to the budgetary targets. Section 5 reviews recent debt developments and medium-term prospects, as well as the long-term sustainability of public finances. Section 6 discusses institutional features of public finances. Finally, Section 7 concludes with an overall assessment of the programme. The annex provides a detailed assessment of compliance with the code of conduct, including an overview of the summary tables from the programme.

2. KEY CHALLENGES IN THE ECONOMIC DOWNTURN AND THE POLICY RESPONSE

This section describes recent economic and budgetary developments for Slovakia, which form the background against which the current programme assessment should be viewed, and outlines the key challenges to be addressed by future economic policies.

With an average real GDP growth rate of over 7% over the period 2003-2008, Slovakia was one of the best performing EU countries during the boom phase that preceded the crisis. Sound macroeconomic and structural policies allowed avoiding large macroeconomic imbalances. The external position remained strong, government debt was low and, while a few signs of overheating emerged by mid-2008, inflation hovered in a range from 2 to 5 percent, broadly preserving cost competitiveness. These achievements enabled Slovakia to adopt the euro in January 2009, which helped shield the country from potential exchange rate pressures and instil confidence during the crisis.

Given its large trade openness, the Slovak economy was strongly exposed to the crisis. Plummeting demand from trading partners triggered a plunge of exports in the first half of 2009 (by some 25% compared to the first half of 2008). Moreover, uncertainties related to the crisis triggered an increase in savings for both households and the corporate sector. As a result, real GDP tumbled by over 8% q-o-q in the first quarter of 2009. Despite the deep recession and intense stress in global financial markets, the Slovak banking sector was resilient, due to a good liquidity situation of credit institutions and low dependence on cross-border lending.

[1] This assessment uses the Commission services' 2009 autumn forecast, as published on 3 November 2009, as a benchmark. However, more recent information that has become available has also been taken into account to assess the risks to the programme scenario.

Table 1. Comparison of key macroeconomic and budgetary projections

		2008	2009	2010	2011	2012
Real GDP (% change)	**SP Jan 2010**	**6.4**	**-5.7**	**1.9**	**4.1**	**5.4**
	COM Nov 2009	6.4	-5.8	1.9	2.6	n.a.
	CP Apr 2009	*6.4*	*2.4*	*3.6*	*4.5*	*n.a.*
HICP inflation (%)	**SP Jan 2010**	**3.9**	**1.2**	**2.6**	**3.7**	**4.1**
	COM Nov 2009	3.9	1.1	1.9	2.5	n.a.
	CP Apr 2009	*3.9*	*2.2*	*3.6*	*4.1*	*n.a.*
Output gap[1] (% of potential GDP)	**SP Jan 2010**	**8.9**	**-1.1**	**-2.9**	**-3.0**	**-1.0**
	COM Nov 2009[2]	9.2	-0.8	-2.1	-3.0	n.a.
	CP Apr 2009	*6.5*	*3.5*	*1.7*	*1.0*	*n.a.*
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	**SP Jan 2010**	**-5.3**	**-4.2**	**-3.2**	**-2.7**	**-1.9**
	COM Nov 2009	-5.6	-4.8	-4.3	-4.2	n.a.
	CP Apr 2009	*-5.8*	*-4.2*	*-2.9*	*-2.6*	*n.a.*
General government revenue (% of GDP)	**SP Jan 2010**	**32.5**	**32.8**	**32.5**	**32.3**	**31.7**
	COM Nov 2009	32.5	31.3	31.4	31.4	n.a.
	CP Apr 2009	*33.4*	*32.1*	*31.6*	*31.8*	*n.a.*
General government expenditure (% of GDP)	**SP Jan 2010**	**34.8**	**39.1**	**38.0**	**36.5**	**34.7**
	COM Nov 2009	34.8	37.5	37.5	36.9	n.a.
	CP Apr 2009	*35.6*	*35.1*	*34.5*	*34.1*	*n.a.*
General government balance (% of GDP)	**SP Jan 2010**	**-2.3**	**-6.3**	**-5.5**	**-4.2**	**-3.0**
	COM Nov 2009	-2.3	-6.3	-6.0	-5.5	n.a.
	CP Apr 2009	*-2.2*	*-3.0*	*-2.9*	*-2.2*	*n.a.*
Primary balance (% of GDP)	**SP Jan 2010**	**-1.1**	**-4.5**	**-3.6**	**-2.3**	**-1.1**
	COM Nov 2009	-1.1	-5.0	-4.7	-4.1	n.a.
	CP Apr 2009	*-0.9*	*-1.7*	*-1.7*	*-1.0*	*n.a.*
Cyclically-adjusted balance[1] (% of GDP)	**SP Jan 2010**	**-4.9**	**-6.0**	**-4.7**	**-3.3**	**-2.7**
	COM Nov 2009	-5.0	-6.0	-5.4	-4.6	n.a.
	CP Apr 2009	*-4.1*	*-4.0*	*-3.4*	*-2.5*	*n.a.*
Structural balance[3] (% of GDP)	**SP Jan 2010**	**-4.2**	**-6.0**	**-4.7**	**-3.3**	**-2.7**
	COM Nov 2009	-5.2	-6.2	-5.4	-4.6	n.a.
	CP Apr 2009	*-3.8*	*-4.4*	*-3.5*	*-2.6*	*n.a.*
Government gross debt (% of GDP)	**SP Jan 2010**	**27.7**	**37.1**	**40.8**	**42.5**	**42.2**
	COM Nov 2009	27.7	34.6	39.2	42.7	n.a.
	CP Apr 2009	*27.6*	*31.4*	*32.7*	*32.7*	*n.a.*

Notes:

[1]Output gaps and cyclically-adjusted balances according to the programmes as recalculated by Commission services on the basis of the information in the programmes.

[2]Based on estimated potential growth of 4.7%, 3.6%, 3.2% and 3.6% respectively in the period 2008-2011

[3]Cyclically-adjusted balance excluding one-off and other temporary measures. One-off and other temporary measures are 0.7% of GDP in 2008, deficit-increasing, according to the most recent programme and 0.2% of GDP in both 2008 and 2009, both deficit-reducing, in the Commission services' autumn 2009 forecast.

Source :

Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations

The policy response of the Slovak government to the crisis aimed at supporting domestic demand to partly offset the slump in external demand. On the fiscal side, the authorities allowed a full operation of automatic stabilisers and, in line with the European Economic Recovery Plan (EERP), adopted anti-crisis packages in November 2008 and February 2009. The stimulus measures amount to roughly ½% of GDP for both 2009 and 2010. They were mainly financed through reallocation of resources within the budget, and therefore had virtually no impact on the government balance. Measures are targeted at

specific sectors (car-scraping scheme) and disadvantaged groups (increase in tax credit for low earners), and aim at supporting employment and R&D activities.

Although growth has been positive since the spring 2009, the recovery remains fragile. The unemployment rate is still on the rise despite efforts to increase the employment content of growth, including through reduced working hours. Deterioration of payment discipline from households and companies is showing up in an increase of non-performing loans. The position of public finances worsened considerably in 2009, when the government deficit is expected at some 6% of GDP (this triggered an excessive deficit procedure for Slovakia, see Box 1), which may weight on consumers' confidence. Finally, depreciation of neighbouring countries' currencies during the crisis implied a further appreciation of Slovakia's real effective exchange rate.

Success within the euro area will require an appropriate conduct of fiscal, incomes, prudential and structural policies. For instance, following entry in the euro area, maintaining external competitiveness will require control of domestic relative prices and costs vis-à-vis competitors and improvements in non-price competitiveness. Considering the weakening of Slovakia's external competitiveness due to temporary depreciation of neighbouring countries' currencies and widening fiscal imbalances during the crisis, a credible and sustainable reduction of the government deficit, while preserving the quality of public finances, would have to be a key element of the authorities' strategy for the coming years.

3. MACROECONOMIC OUTLOOK

Against the background of the current macroeconomic situation and the main policy challenges set out in the previous section, this section makes an assessment of the plausibility of the macroeconomic scenario underpinning the public finance projections of the programme.

The programme projections for 2010 are very much in line with the Commission services' autumn 2009 forecast. After a decline by 5% in 2009[2], real GDP is projected to increase by around 2% in 2010. The shallow recovery projected for 2010 reflects the influence of several factors playing in various directions. On the positive side, business confidence seems to slowly recover, exports have started to grow again and the inventories cycle is slowly turning. But powerful headwinds will slow the upturn. The adjustment of the labour market will come with a lag, which will contribute to maintaining the households' saving ratio at a high level, and the underutilisation of production capacities after the large fall in output seems to prevent a rebound of investment, at least in the short run.

The authorities assume more favourable macroeconomic development than the Commission services for 2011 and 2012. The Commission services' autumn forecast projected real GDP growth at 2.6% in 2011, and potential growth was estimated to average 3% over the years 2011-2012. In the programme, real GDP is projected to increase by 4.1% in 2011 and 5.4% in 2012, well above these levels. The cyclical upturn would be driven by a strong recovery of domestic demand and, although there are no major deviations from the external assumptions underlying the Commission services' autumn 2009 forecast, a significant contribution of foreign trade to growth. While by no

[2] In March the Statistical Office published the GDP figures according to which the annual contraction in 2009 amounted to 4.7%.

means impossible – real GDP growth averaged 7% over 2003-2008 – these assumptions may not reflect the degree of prudence that should underpin fiscal consolidation strategies, especially given the unusually high uncertainties in the current post-crisis environment.

According to output gap estimates, as recalculated by Commission services based on the information in the programme following the commonly agreed methodology, the crisis has eliminated the very positive output gap that prevailed in 2008 (9 percent of potential GDP). The output gap would remain negative over the entire programme period and narrow only in 2012.[3] Interestingly, over the years 2009-2011 the output gap would evolve in parallel with the path projected by the Commission services in the autumn forecast, despite significantly higher real GDP growth in the programme in 2011. This apparent contradiction is due to the fact that, compared to Commission services' estimates, potential growth numbers calculated using the assumptions in the programme are pushed up by the high GDP growth rates assumed for the years 2011 and 2012.

Table 2: Comparison of macroeconomic developments and forecasts

	2009		2010		2011		2012
	COM	SP	COM	SP	COM	SP	SP
Real GDP (% change)	-5.8	-5.7	1.9	1.9	2.6	4.1	5.4
Private consumption (% change)	-1.2	-0.4	0.5	1.5	2.2	3.4	4.9
Gross fixed capital formation (% change)	-12.4	-10.3	2.5	2.9	3.3	4.1	5.1
Exports of goods and services (% change)	-15.7	-15.2	2.4	2.9	5.0	7.1	10.0
Imports of goods and services (% change)	-13.5	-14.7	2.4	3.2	4.9	5.6	8.4
Contributions to real GDP growth:							
- Final domestic demand	-3.1	-2.4	1.5	1.4	2.6	2.7	3.9
- Change in inventories	-1.3	-2.5	0.3	0.6	0.0	0.3	0.0
- Net exports	-1.5	-0.8	0.0	-0.1	0.1	1.1	1.5
Output gap[1]	-0.8	-1.1	-2.1	-2.9	-3.0	-3.0	-1.0
Employment (% change)	-2.0	-1.9	0.0	-0.1	0.6	0.9	1.6
Unemployment rate (%)	12.3	11.7	12.8	12.1	12.6	11.6	11.0
Labour productivity (% change)	-3.9	-3.7	1.9	2.0	2.0	3.2	3.7
HICP inflation (%)	1.1	1.2	1.9	2.6	2.5	3.7	4.1
GDP deflator (% change)	4.5	0.2	3.0	3.8	2.9	3.2	3.4
Comp. of employees (per head, % change)	3.6	2.4	3.9	option	4.3	option	option
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	-4.8	-4.2	-4.3	-3.2	-4.2	-2.7	-1.9

Note:

[1]In percent of potential GDP, with potential GDP growth according to the programme as recalculated by Commission services.

Source :

Commission services' autumn 2009 forecasts (COM); Stability programme (SP).

Consistent with the real GDP growth assumptions, the Commission services' autumn 2009 forecast projected a more pronounced deterioration of the unemployment rate, to

[3] There are consistent differences between the output gaps as recalculated by Commission services and those calculated in the Programme, with the programme implying worse cyclical conditions in 2009 and 2010, and similar cyclical development in 2011. This is to be attributed to different initial position (output gap in 2008) and lower projections of potential GDP growth in the Programme, mainly due to significantly lower contributions of TFP between 2009 and 2011.

more than 12% of the labour force in 2009-2011, on average about 1 pp. higher than expected in the programme. Both the Commission and the programme foresee a gradual decline of unemployment over the programme period. Whereas anti-crisis measures aimed at supporting labour markets are indeed temporary, they constitute a fairly small part of the stimulus package and their phasing-out is not expected to have a major impact on labour market developments. The programme's projection for inflation is higher by about 1 pp. in 2011 than in the Commission services' autumn 2009 forecast, which is consistent with the stronger recovery assumed in the programme.

Overall, assessed against currently available information, the programme scenario appears to be based on plausible growth assumptions until 2010, and on favourable growth assumptions thereafter.

4. GENERAL GOVERNMENT BALANCE

This section consists of four parts. The first three parts discuss the budgetary implementation in the year 2009, the budgetary plans for 2010 and the medium-term budgetary strategy in the programme. The final part analyses the risks attached to the budgetary targets.

4.1. Budgetary implementation in 2009

According to the programme, the general government deficit in 2009 widened by 4 percentage points of GDP compared to 2008, to 6.3% of GDP. In line with the European Economic Recovery Plan and available fiscal space, the authorities adopted anti-crisis amounting to only ½% of GDP for both 2009 and 2010, which were mainly financed through a reallocation of resources within the budget, and therefore did not have a sizeable negative impact on the deficit.

Table 3 compares the projected outcome for the government balance, revenue and expenditure (as a percentage of GDP) in 2009 as presented in the new stability programme with the targets from the previous update of the programme. Differences between outcomes and targets (excluding the impact of unanticipated GDP developments which may have affected the ratio, referred to as the ‘denominator effect’) are decomposed in the impact of a different starting position (i.e. the outcome of 2008 may also have been different from what was anticipated in the previous programme update) and the impact of differences in the revenue / expenditure growth rates from the planned growth rates[4].

The envisaged budgetary outcome for 2009 is well above the target of 3.0% of GDP included in the previous update of the stability programme. The gap is due, in almost equal parts (about 1½ percentage point of GDP each), to lower than expected revenue growth and faster than anticipated growth in expenditures. In both cases the surprises can be explained by the crisis:

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[4] Mathematically, the difference in the revenue ratio in Table 3 can be expressed as:

$$\rho^o - \rho^p = \underbrace{\frac{1+r^p}{1+g^p}\Delta\rho_{-1}}_{\text{Base effect}} + \underbrace{\frac{\rho^o_{-1}}{(1+g^o)(1+g^p)}\Delta r}_{\text{Revenue growth effect}} - \underbrace{\frac{\rho^o_{-1}}{(1+g^o)(1+g^p)}\Delta g}_{\text{Denominator effect}} + \underbrace{\frac{\rho^o_{-1}\left(r^o g^p - r^p g^o\right)}{(1+g^o)(1+g^p)}}_{\text{Residual}}$$

where r is the growth rate of revenue and g is the growth rate of GDP. The subscript -1 refers to the previous year’s value. Superscripts o and p refer to the outcome and the planned value respectively. Similar for the expenditure ratio.

- The fall of government revenue compared to plans was almost exclusively due to a worse-than-expected collection of taxes as a result of the economic slowdown. The biggest losses were recorded for the income tax, VAT, excise duties and social security contributions. In addition, a one-off income from a transfer of assets from the second fully-funded pillar to the PAYG pillar fell short of expectations as fewer pension savers decided to switch to the PAYG pillar.
- In 2009, government expenditure growth surpassed the originally budgeted figures by about 3.5 percentage points. Higher-than-budgeted social benefits, in line with the government policy of allowing the automatic stabilizers to operate freely, constituted the largest negative surprise on the expenditure side. The faster increase of expenditure was not affected by the government stimulus measures under the EERP, which were financed by reallocations of spending within the budget.

Table 3: Budgetary implementation in 2009

	2008		2009	
	Planned SP Apr 2009	Outcome SP Jan 2010	Planned SP Apr 2009	Outcome SP Jan 2010
Government balance (% of GDP)	-2.2	-2.3	-3.0	-6.3
Difference compared to target [1]	-0.1		-3.3	
Difference excluding denominator effect [1,2]			**-3.1**	
Of which : due to a different starting position end 2008			-0.1	
due to different revenue / expenditure growth in 2009			-2.8	
p.m. Residual [3]			-0.2	
p.m. Nominal GDP growth (planned and outcome)			*4.1*	*-5.5*
Revenue (% of GDP)	33.4	32.5	32.1	32.8
Revenue surprise compared to target [1]	-0.9		0.7	
Revenue surprise excluding denominator effect [1,2]			**-2.5**	
Of which : due to a different starting position end 2008			-0.9	
due to different revenue growth in 2009			-1.5	
p.m. Residual [3]			-0.1	
p.m. Revenue growth rate (planned and outcome)			*0.0*	*-4.6*
Expenditure (% of GDP)	35.6	34.8	35.1	39.1
Expenditure surprise compared to target [1]	0.8		-4.0	
Expenditure surprise excluding denominator effect [1,2]			**-0.6**	
Of which : due to different starting position end 2008			0.8	
due to different expenditure growth rate in 2009			-1.3	
p.m. Residual [3]			-0.1	
p.m. Expenditure growth rate (planned and outcome)			2.6	6.2

Notes:

[1] A positive number implies that the outcome was better (in terms of government balance) than planned.

[2] The denominator effect captures the mechanical effect that, if GDP turns out higher than planned, the ratio of revenue or expenditure to GDP will fall because of a higher denominator. Although the denominator effect can be very significant for revenue and expenditure separately, on the balance they usually largely cancel against each other.

[3] The decomposition leaves a small residual that cannot be assigned to the previous components. The residual is generally small, except in some cases where planned and actual growth rates of revenue, expenditure and GDP differ significantly.

Source : Commission services

Box 1: The excessive deficit procedure (EDP) for Slovakia

On 2 December 2009 the Council adopted a decision stating that Slovakia had an excessive deficit in accordance with Article 126(6) of the Treaty on the Functioning of the European Union (TFEU). At the same time, the Council addressed a recommendation under 126(7) TFEU specifying that the excessive deficit had to be corrected by 2013.

In particular, Slovakia was recommended to implement the deficit reducing measures in 2010 as planned in the budget for 2010-2012, ensure an average annual deficit effort of 1% of GDP over the period 2010-2013, and specify the necessary measures for achieving the correction of the excessive deficit by 2013, cyclical conditions permitting. It was also recommended to accelerate the reduction of the deficit if economic or budgetary conditions turned out better than expected. In addition, to limit risks to the adjustment, Slovakia was recommended to strengthen the enforceability of its medium-term budgetary framework as well as improve the monitoring of the budget execution throughout the year, in particular to avoid expenditure overruns compared to budget plans. The Council established the deadline of 2 June 2010 for the Slovak government to take effective action to implement the deficit reducing measures in 2010 as planned in the draft budget for 2010-2012 and to outline in some detail the consolidation strategy that will be necessary to progress towards the correction of the excessive deficit. The assessment of effective action will take into account economic developments compared to the economic outlook in the Commission services' autumn 2009 forecast.

The Slovak authorities should report on progress made in the implementation of these recommendations in a separate chapter in the updates of the stability programmes prepared between 2010 and 2013.

4.2. The programme's budgetary strategy for 2010

The 2010-2012 budget, which forms the basis for the stability programme, was approved by parliament on 4 November 2009. For 2010, the programme targets a general government deficit of 5.5% of GDP, in line with the December Council recommendation under the EDP (Article 126(7)). The budget includes anti-crisis measures estimated at some 0.6% of GDP, most of which are planned to be withdrawn at the end of the year.

The expenditure ratio is expected to fall by 1.1 percentage point of GDP in 2010. This decline would reflect savings in goods and services expenditure, a moderate increase in the public wage bill, and cuts in capital spending. The revenue to GDP ratio is projected to decline by 0.3 percentage point of GDP, reflecting a decline in dividends from public companies, which would be partially offset by increased excise duties on alcohol, and a temporary increase of tax allowances and in-work benefits. A downside risk for revenues in 2010 stems from the reduction of the excise duty on diesel fuels adopted in January 2010 (0.1-0.2% of GDP), which is not taken into account in the programme projections.

Commission services' calculations of the structural balance based on the information in the programme (using the commonly agreed methodology) point to an improvement in the structural deficit by 1.3 percentage points of GDP in 2010, significantly more than the 0.8 percent of GDP projected by the Commission in the autumn forecast. The difference reflects both uncertainties on the yield of some expenditure savings measures and different assumptions for potential growth.

Table 4. Main budgetary measures for 2010

Revenue measures[1]	Expenditure measures[2]
• Reduction of excise duties on diesel fuels (-0.1 - -0.2% of GDP) • Increase of tax allowance (-0.1% of GDP)	• Cuts in expenditures on goods and services, capital expenditures and current transfers (-1.2% of GDP)
Notes: [1] Estimated impact on general government revenue [2] Estimated impact on general government expenditure *Source: Commission services and Stability programme (SP)*	

4.3. The programme's medium-term budgetary strategy

This section describes the medium-term budgetary strategy outlined in the programme - and how it compares with the one in the previous update - as well as the composition of the budgetary adjustment, including the broad measures envisaged.

The main aim of the programme's budgetary strategy is to ensure fiscal consolidation and bring the fiscal position to a sustainable level. According to the programme, the general government deficit should reach 3% of GDP in 2012, one year earlier than recommended under the EDP. Afterwards, the consolidation effort is planned to continue, and the MTO of a balanced budget in structural terms would be reached in 2015 (see Box 2 for more details), which is outside the programme period.

Box 2: The medium-term objective (MTO) for Slovakia

As noted in the Code of Conduct[5], the MTO aims to (a) provide a safety margin with respect to the 3% of GDP deficit limit; (b) ensure rapid progress towards fiscal sustainability; and (c) allow room for budgetary manoeuvre, in particular taking into account the needs for public investment. The MTO is defined in cyclically adjusted terms, net of one-off and other temporary measures. On 7 July 2009, the ECOFIN Council took note of a new methodology for setting MTOs, ensuring that implicit liabilities (costs related to ageing populations, in particular projected healthcare and pension expenditure) are also accounted for.

Specifically, the country-specific MTOs should take into account three components: (i) the debt-stabilising balance for a debt ratio equal to the (60% of GDP) reference value (dependent on long-term potential growth), implying room for budgetary manoeuvre for Member States with relatively low debt; (ii) a supplementary debt-reduction effort for Member States with a debt ratio in excess of the (60% of GDP) reference value, implying rapid progress towards it; and (iii) a fraction of the adjustment needed to cover the present value of the future increase in age-related government expenditure. This implies a partial frontloading of the budgetary cost of ageing irrespective of the current level of debt. In addition to these criteria, MTOs should provide a safety margin with respect to the 3% of GDP deficit reference value and, for euro area and ERM II Member States, in any case not exceed a deficit of 1% of GDP.

[5] "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 on 10 November 2009, available at: http://ec.europa.eu/economy_finance/sgp/legal_texts/index_en.htm

As communicated by the authorities, the MTO of Slovakia is a balanced budget in structural terms. In view of the new methodology and given the most recent projections and debt level, the MTO more than adequately reflects the objectives of the Pact.

The general government deficit is expected to fall from 5.5% of GDP in 2010 to 4.2% of GDP in 2011 and 3.0% of GDP in 2012. Two thirds of the deficit reduction between 2010 and 2012 would reflect a structural improvement (as measured according to the commonly agreed methodology applied to the information provided in the programme); the remaining third would result from favourable cyclical developments. The fiscal consolidation effort is frontloaded, with the structural balance improving by 1.3 percentage point of GDP in 2011 (similar to the effort planned for 2010), and by only 0.5 percentage point in 2012. It is in line with the December EDP recommendation.

Consolidation would be achieved on the expenditure side. The expenditure/GDP ratio is expected to fall by over 3 percentage points between 2010 and 2012, mainly due to a reduction of the public wage bill, intermediate consumption and social transfers as the crisis-related spending fades away. The programme however provides few details on how to achieve these ambitious targets. The programme also projects a continuous fall of government capital formation expenditure to the low level of 1.2% of GDP in 2012. This is potentially easier to achieve, but raises concerns regarding the quality of public spending and the contribution of fiscal policy to growth. The revenue to GDP ratio is projected to fall by about 1 percentage point between 2010 and 2012. The programme is not explicit on the reasons for the decline, but does not announce discretionary tax cuts, suggesting that the decline in the revenue ratio could reflect the spontaneous response of the tax system to economic activity.

Table 5: Composition of the budgetary adjustment

(% of GDP)	2008	2009		2010		2011		2012	Change: 2009-2012
	COM	COM	SP	COM	SP	COM[1]	SP	SP	SP
Revenue	**32.5**	**31.3**	**32.8**	**31.4**	**32.5**	**31.4**	**32.3**	**31.7**	**-1.1**
of which:									
- Taxes on production and imports	10.4	9.9	10.8	9.8	10.9	9.7	10.6	10.4	-0.4
- Current taxes on income, wealth, etc.	6.4	5.9	5.9	5.8	5.6	5.7	5.9	6.0	0.1
- Social contributions	12.1	11.7	12.4	11.5	12.0	11.4	11.9	11.9	-0.5
- Other (residual)	3.6	3.8	3.7	4.4	4.0	4.6	3.9	3.4	-0.3
Expenditure	**34.8**	**37.5**	**39.1**	**37.5**	**38.0**	**36.9**	**36.5**	**34.7**	**-4.4**
of which:									
- Primary expenditure	33.6	36.2	37.3	36.1	36.1	35.5	34.6	32.9	-4.4
of which:									
Compensation of employees	6.6	7.0	7.4	6.9	7.0	6.9	6.7	6.3	-1.1
Intermediate consumption	5.0	5.5	4.8	5.5	4.2	5.6	4.1	3.7	-1.1
Social payments	15.6	17.1	18.4	16.9	18.5	16.4	18.2	17.7	-0.7
Subsidies	1.7	1.8	1.8	1.8	1.7	1.7	1.6	1.6	-0.2
Gross fixed capital formation	2.0	1.8	1.9	1.9	1.6	1.8	1.6	1.2	-0.7
Other (residual)	2.7	3.0	3.0	3.2	3.0	3.1	2.5	2.3	-0.7
- Interest expenditure	1.2	1.3	1.8	1.3	1.9	1.4	1.9	1.8	0.0
General government balance (GGB)	**-2.3**	**-6.3**	**-6.3**	**-6.0**	**-5.5**	**-5.5**	**-4.2**	**-3.0**	**3.3**
Primary balance	**-1.1**	**-5.0**	**-4.5**	**-4.7**	**-3.6**	**-4.1**	**-2.3**	**-1.1**	**3.4**
One-off and other temporary measures	0.2	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0
GGB excl. one-offs	**-2.5**	**-6.4**	**-6.3**	**-6.0**	**-5.5**	**-5.5**	**-4.2**	**-3.0**	**3.3**
Output gap[2]	9.2	-0.8	-1.1	-2.1	-2.9	-3.0	-3.0	-1.0	0.1
Cyclically-adjusted balance[2]	-5.0	-6.0	-6.0	-5.4	-4.7	-4.6	-3.3	-2.7	3.3
Structural balance[3]	**-5.2**	**-6.2**	**-6.0**	**-5.4**	**-4.7**	**-4.6**	**-3.3**	**-2.7**	**3.3**
Change in structural balance		*-1.0*	*-0.8*	*0.8*	*1.3*	*0.8*	*1.3*	*0.6*	
Structural primary balance[3]	-3.9	-4.9	-4.2	-4.1	-2.8	-3.3	-1.4	-0.8	3.4
Change in structural primary balance		*-0.9*	*-0.2*	*0.8*	*1.4*	*0.8*	*1.3*	*0.6*	

Notes:

[1]On a no-policy-change basis.

[2]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the information in the programme.

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

Source:

Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations

4.4. Risk assessment

This section discusses the plausibility of the programme's budgetary projections by analysing various risk factors. For the period until 2011, Table 5 compares the detailed revenue and expenditure projections in the Commission services' autumn 2009 forecast, which are derived under a no-policy change scenario, with those in the updated programme. However, although the assessment uses the Commission services' forecast as a benchmark, it also takes explicitly into account all available information about more recent developments.

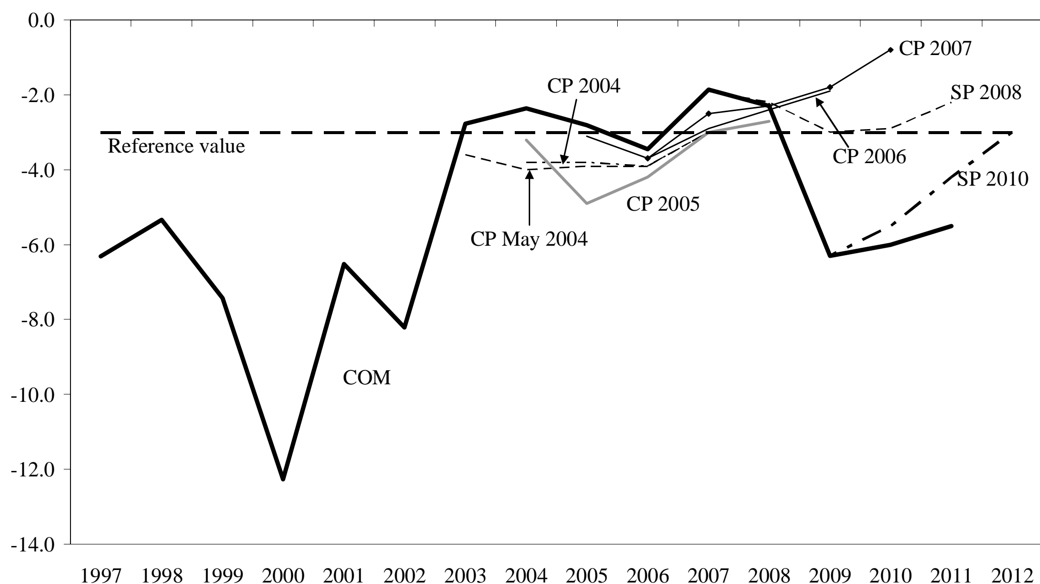
There are moderate downside risks to the government balance target for 2010. Government revenues may turn out lower than expected due to the reduction of taxes on diesel fuels approved by the government by early January (impact is estimated between 0.1 and 0.2% of GDP). There are also uncertainties on the expenditure side, where some measures may not yield the expected savings (e.g. reduction of spending in goods and services).

Risks are larger for the following years. Macroeconomic assumptions for 2011 and 2012 are on the optimistic side. Worse-than-expected economic developments would pose an

immediate threat to the consolidation path. Moreover, further details on the planned reduction in government consumption (as a share of GDP) by 1 p.p. of GDP over the 2009-2012 period will have to be specified to enhance the credibility of the consolidation plan. An additional risk to the consolidation strategy is the assumption that local governments will retain approximately balanced budget balance over the 2010-2012 period. While this assumption may be plausible for the outer years, it is less so for 2010 when the economic crisis materialises into lower tax revenues.

Overall, the budgetary projections for 2010 are subject to moderate downside risks. Risks are larger for the outer years, for which the programme is based on favourable macroeconomic assumptions and insufficient specification of the measures planned to achieve the fiscal targets.

Figure 1: Government balance projections in successive programmes (% of GDP)



Source: Commission services' autumn 2009 forecast (COM) and successive convergence and stability programmes

5. GOVERNMENT DEBT AND LONG-TERM SUSTAINABILITY

This section is in two parts. A first part describes recent debt developments and medium-term prospects, including risks to the outlook presented in the programme. A second part takes a longer-term perspective with the aim of assessing the long-term sustainability of public finances.

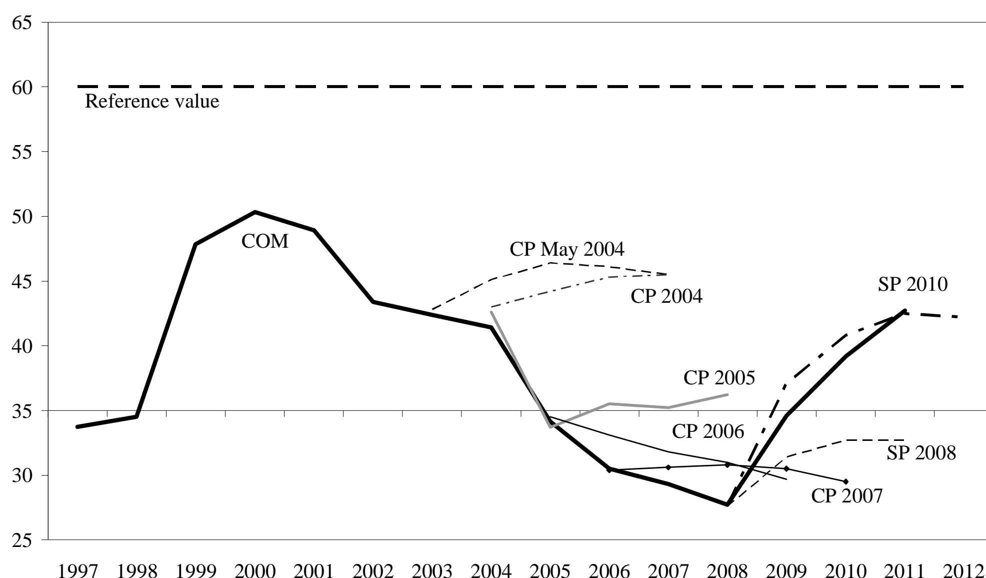
5.1. Recent debt developments and medium-term prospects

5.1.1. Debt projections in the programme

The debt to GDP ratio was steadily declining from its peak of 50.4% in 2000 up to 2008 when it reached 27.7% of GDP. In 2009, the debt ratio reached 37.1% of GDP according to the stability programme. This is significantly more than the projection of the previous programme and somewhat more than foreseen in the Commission services' 2009 autumn forecast. This worse outcome reflects higher interest expenditure and stock-flow adjustments reported in the programme. The latter comprises an increase in net accumulated financial assets as a result of returnable financial assistance and capital

injections in state-owned companies. In the subsequent years, the programme expects a further increase of debt to 42.5% of GDP in 2011 and a small decline in 2012. The developments over the 2010-2011 period are well in line with the Commission forecast.

Figure 2: Debt projections in successive programmes (% of GDP)



Source: Commission services' autumn 2009 forecast (COM) and successive convergence and stability programmes

Table 6: Debt dynamics

(% of GDP)	average 2003-07	2008	2009		2010		2011		2012
			COM	SP	COM	SP	COM	SP	SP
Gross debt ratio[1]	**35.6**	**27.7**	**34.6**	**37.1**	**39.2**	**40.8**	**42.7**	**42.5**	**42.2**
Change in the ratio	-2.8	-1.6	7.0	9.4	4.6	3.7	3.5	1.7	-0.3
Contributions [2] *:*									
1. Primary balance	**0.8**	**1.1**	**5.0**	**4.5**	**4.7**	**3.6**	**4.1**	**2.3**	**1.1**
2. "Snow-ball" effect	**-1.8**	**-1.2**	**1.6**	**3.4**	**-0.3**	**-0.1**	**-0.7**	**-0.9**	**-1.5**
Of which:									
Interest expenditure	1.9	1.2	1.3	1.8	1.3	1.9	1.4	1.9	1.9
Growth effect	-2.4	-1.7	1.6	1.7	-0.6	-0.7	-1.0	-1.6	-2.1
Inflation effect	-1.3	-0.7	-1.3	-0.1	-1.0	-1.4	-1.1	-1.2	-1.3
3. Stock-flow adjustment	**-1.7**	**-1.5**	**0.3**	**1.5**	**0.1**	**0.3**	**0.1**	**0.3**	**0.2**
Of which:									
Cash/accruals diff.	0.6	-0.3		0.8		-0.1		0.0	0.0
Acc. financial assets	-1.9	-0.5		0.7		0.4		0.3	0.2
Privatisation	-0.5	0.0		n.a.		n.a.		n.a.	n.a.
Val. effect & residual	-0.4	-0.7		0.0		0.0		0.0	0.0

Notes:

[1]End of period.

[2]The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source:

Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations

5.1.2. Assessment

While still at a relatively low level by EU standards, the debt ratio is now on a firmly ascending path – an increase by almost 15 pp. of GDP is projected between 2008 and 2011. A risk of an even higher increase in the debt ratio, especially after 2010, can not be excluded given the general risks related to the budgetary consolidation strategy and the possibility of less favourable real GDP growth than assumed in the programme (see section 4.4). However, the specific risks related to debt developments seem to be limited as government contingent liabilities to the financial sector are amongst the lowest in the EU and no further capital injections are expected.

5.2. Long-term debt projections and the sustainability of public finances

5.2.1. Long-term debt projections and the sustainability of public finances

This section presents sustainability indicators based on the long-term age-related government spending as projected by the Member States and the EPC in 2009 according to an agreed methodology[6].

Table 7 shows that projected increase in age-related spending between 2010 and 2060 reaches 5.5 percentage points of GDP, which is above the EU average (4.6 p.p.). Sustainability indicators for two scenarios are presented in Table 8. 'The 2009 scenario' is based on a no-policy-change assumption and the 2009 structural primary balance as a starting position, while 'the programme scenario' takes into account the consolidation planned in the programme up to 2012 and the projected 2012 structural primary balance as a starting position. Including the increase of age-related expenditure and assuming that the structural primary balance remains at its 2009 level, the sustainability gap (S2)[7] would amount to 8.5% of GDP, about 4.5 percentage points more than in last year's assessment This is mainly due to an deterioration in the estimated structural primary balance in the starting year (also the rise in age-related expenditure is higher in the 2009 projections than in the previous ones). The starting budgetary position is not sufficient to stabilize the debt ratio over the long-term and entails a risk of unsustainable public finances even before considering the long-term budgetary impact of ageing.

In contrast to the "2009 scenario", the "programme scenario" shows a smaller gap (Table 8). If the budgetary consolidation planned in the programme was achieved, risks to long-term sustainability of public finances would be somewhat mitigated but would remain significant because the improvement in the structural primary balance would not yet be sufficient to close the gap stemming from the initial budgetary position.

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[6] Economic Policy Committee and the European Commission (2009), '2009 Ageing Report: Economic and budgetary projections for the EU-27 Member States (2008-60)', *European Economy* No. 2/2009. European Commission (2009), 'Sustainability Report 2009, European Economy No. 9/2009. European Commission (2008), 'Public finances in EMU – 2008', *European Economy* No. 4/2008..

[7] The S2 indicator is defined as the change in the current level of the structural primary balance required to make sure that the discounted value of future structural primary balances (including the path of property income) covers the current level of debt.

Table 7: Long-term age-related expenditure: main projections

(% of GDP)	2007	2010	2020	2040	2060	Change 2010- 60
Total age-related spending	**15.2**	**14.9**	**14.5**	**17.5**	**20.4**	**5.5**
- Pensions	6.8	6.6	6.3	8.3	10.2	3.6
- Healthcare	5.0	5.2	5.7	6.7	7.2	2.1
- Long-term care	0.2	0.2	0.2	0.4	0.6	0.4
- Education	3.1	2.8	2.2	2.1	2.3	-0.5
- Unemployment benefits	0.1	0.1	0.1	0.1	0.1	-0.1
Property income received	**1.5**	**1.4**	**1.2**	**1.1**	**1.0**	**-0.4**

Source: Economic Policy Committee and Commission services.

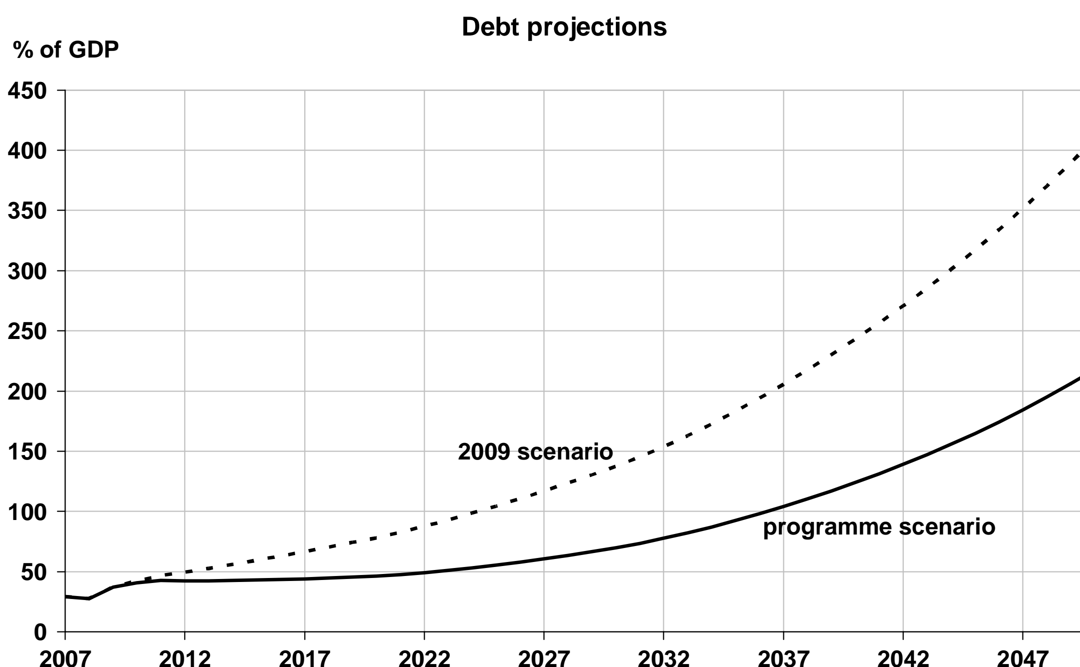
Table 8: Sustainability indicators and the required primary balance

	2009 scenario			Programme scenario		
	S1	S2	RPB	S1	S2	RPB
Value	6.9	8.5	4.4	3.5	5.2	4.3
of which:						
Initial budgetary position (IBP)	5.0	5.2	-	1.7	1.9	-
Debt requirement in 2060 (DR)	-0.1	-	-	-0.2	-	-
Long-term change in the primary balance (LTC)	2.1	3.3	-	2.1	3.3	-

Source: Commission services.

Based on the assumptions used in the projection of age-related expenditure and the calculation of the sustainability indicators, Figure 3 displays the projected debt/GDP ratio over the long-term.

Figure 3: Long-term projections for the government debt ratio

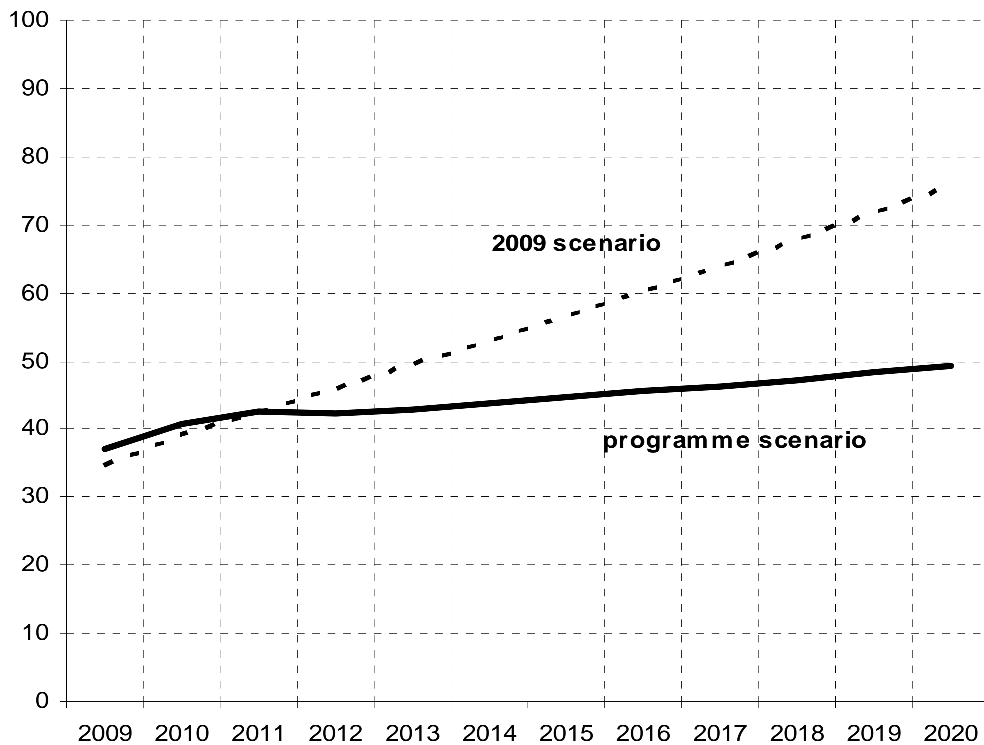


Note: Being a mechanical, partial-equilibrium analysis, the long-term debt projections are bound to show highly accentuated profiles. As a consequence, the projected evolution of debt levels should not be seen as a forecast similar to the Commission services' short-term forecasts, but as an indication of the risks faced by Member States.

Source: Commission services calculations

Based on the alternative assumptions of economic developments presented in the Commission services' autumn 2009 forecast publication[8], Figure 4 shows projected medium-term trajectory of the debt/GDP ratio. The projected debt trajectories show relatively similar paths under both sets of assumptions, however, the debt ratio in the 2009 scenario when account is taken on most recent economic developments would increase slightly faster than under the baseline assumptions presented above.

Figure 4: Medium-term projections for the government debt ratio



Source: Commission services' calculations

5.2.2. Additional factors

For an overall assessment of the sustainability of public finances, other relevant factors are taken into account. These factors, which are summarized in Table 9, do not change the overall assessment.

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8 Section 3.5 in European Commission (2009), 'European Economic Forecast – autumn 2009', European Economy No. 10/2009. This economic scenario assumes that the output gap caused by the crisis will be closed by 2017.

Table 9: Sustainability indicators and the required primary balance

	Impact on risk
Debt and pension assets	na
Decline in structural balance until 2011 in COM Autumn 2009 forecast	na
Alternative projection of cost of ageing	na
Strong decline in benefit ratio	na
High tax burden	na
Difference between S1 and S2	na

Note: '-': factor tends to increase the risk to sustainability, '+': factor tends to decrease the risk to sustainability.
'na': not applicable.

Alternative projections are often presented in the programmes, whose assumptions often diverge from the common method. Projections currently discussed in the Economic Policy Committee but not yet published, are for the time being also considered "unofficial".

An explanation on these factors can be found in chapter V of: European Commission (2009), Sustainability Report 2009, European Economy No. 9/2009.

Source: Commission services.

5.2.3. Assessment

The long-term budgetary impact of ageing population is slightly higher than the EU average, due to a relatively high increase in pension expenditure during the coming decades. The budgetary position in 2009 is considerably worse than the starting position of the previous programme and compounds the budgetary impact of population ageing on the sustainability gap. Achieving higher primary surpluses over the medium term, as foreseen in the programme, would contribute to reducing the high risks to the sustainability of public finances.

Medium-term debt projections until 2020 that are based on more recent economic developments and projections on the potential growth show that the budgetary consolidation envisaged in the programme is not sufficient to stabilise debt in the medium term and that consolidation should continue after the programme period. The '2009 scenario' based on the budgetary situation of 2009 shows that debt would be increasing to about 75% of GDP by 2020 if the policy measures described in the programme would not be implemented.

6. FISCAL FRAMEWORK AND QUALITY OF PUBLIC FINANCES

This section is subdivided into two elements: the fiscal framework and the quality of public finances in a broader sense.

6.1. Fiscal framework

In 2005, Slovakia introduced a medium term budgetary framework, which is based on tri-annual planning cycles. Whereas the first year figures are those of the budget law, the figures of the outer two years are mostly informative and are adjusted on a rolling basis. One interesting element of the framework is that the medium-term plans are very detailed (almost as detailed as a standard budget). Nevertheless, when assessed against indices measuring the strength of multiannual fiscal frameworks, Slovakia's framework scores below the EU average. This is mainly due to the indicative and non-binding

nature of the multiannual expenditure targets. Very sizeable revisions to targets are allowed – and observed in practice – which over time undermine their credibility. This weakness has been pointed out several times by the Commission in the past. Slovakia has also three fiscal rules on central government expenditure, golden rule and borrowing of local governments. These three rules cover the majority of government finances and they contribute to budgetary discipline. However, a weakness of Slovakia's fiscal framework is that there is no independent institution that would provide inputs in the budget process and monitor fiscal developments.

The 2009 update of the stability programme proposes to strengthen the fiscal framework in three ways.

- It proposes the introduction of multiannual expenditure ceilings. The purpose would be to strengthen the enforceability of the multiannual general government budget. The expenditure ceilings would have a broad coverage – only local governments would be excluded – and would be adjusted to match the deficit targets. Such rules would also have escape clauses in case of unexpected events or negative economic shocks.
- The programme also proposes the introduction of an upper limit on government debt in a constitutional law. According to the programme, this rule should be invoked as an "emergency brake".
- Finally, the programme envisages improvements in monitoring of budget execution during the year through better information systems, which would enable collection of data from all sectors of general government and public institutions. Expenditure slippages would be identified earlier, allowing for introduction of corrective measures.

These efforts to strengthen the institutional set-up for public finances are welcome and should be encouraged. However, as the presented proposals are only at a very initial stage, they should be seen as complementary efforts rather than driving factors of the fiscal consolidation strategy.

6.2. Quality of public finances

Slovakia has one of the smallest public sectors in the EU. Nevertheless, there is a scope to improve the quality of government spending. The share of government investment in total government expenditure is low (2% of GDP). Spending in R&D, education and environment protection is also low by EU standards and compared to regional peers. Against this background, the projected reduction of capital formation spending over the programme horizon is a source of concern. It may not be sustainable, and desirable, in a catching up economy like Slovakia. Low efficiency of public spending has been documented by several cases involving EU funding, where the European Commission refused to reimburse project costs or challenged public procurement procedures.

The programme envisages several measures to enhance the efficiency of general government including (i) reorganization of the central administration through fusion of ministries; (ii) creation of a "GovCity" which would bring all the ministries to one location; (iii) centralisation of public procurements; (iv) centralisation of the management of state property; and (v) deployment of information technologies that would improve public services. These measures, which all go in the right direction, are generally at an early stage. The authorities need to ensure that they will be implemented

and have to complement them as necessary to improve the efficiency of the public sector.

7. OVERALL ASSESSMENT

Taking into account risks attached to the budgetary targets discussed above, this section assesses the appropriateness of the fiscal strategy in relation to the Council Recommendations under Article 126(7) of 2 December 2009 with a view to correcting the excessive deficit and the budgetary objectives of the Stability and Growth Pact, against the background of the current economic situation, the debt and long-term sustainability position of the country, and the institutional features of its public finances.

The programme presents an ambitious plan to bring the government deficit from 6.3% of GDP in 2009 to 3.0% of GDP in 2012, one year before the deadline of 2013 set by the Council in December. The projected average annual structural effort of around 1% of GDP is also in line with the Council recommendation under the excessive deficit procedure. It seems adequate to bring the fiscal position to a more sustainable level and prevent the occurrence of macroeconomic imbalances in Slovakia over the period covered by the programme.

However, both revenue and expenditure targets are subject to risks, especially in 2011 and 2012 when macroeconomic growth assumptions seem to be on the high side. On the basis of current information, there is uncertainty regarding the achievement of expenditure targets. Therefore, further details of measures included in the programme will have to be specified to enhance the credibility of the consolidation plan. Although still at a very early stage, the intentions and measures announced to strengthen the institutional framework for the conduct of fiscal policy are welcome.

Overall, the budgetary strategy in the programme is largely consistent with the Council recommendations. It will be important to rigorously implement the 2010 budget and to further specify the measures needed to achieve the projected savings on the expenditure side. Also, the authorities should be ready to react to possible less favourable macroeconomic developments than expected in the programme, if this jeopardises the correction of the excessive deficit by 2013 at the latest.

* * *

ANNEX. COMPLIANCE WITH THE FORMAT AND CONTENT REQUIREMENTS FOR STABILITY AND CONVERGENCE PROGRAMMES

This annex provides an assessment of whether the programme respects the requirements of Section II of the code of conduct (guidelines on the format and content), notably as far as (i) the model structure (Annex 1 of the code of conduct); (ii) the formal data provisions (Annex 2 of the code of conduct); and (iii) other information requirements is concerned. It also assesses to what extent Country followed up on the Council's recommendation to report on progress made in the correction of the excessive deficit, in a separate chapter of the programme.

(i) Model structure

The 2010 update of the stability programme adheres overall to the model structure presented by the code of conduct. The chapter on institutional aspects of public finances is missing as there were no changes in this regard vis-à-vis the previous update. Nevertheless, the programme presents a number of envisaged measures to strengthen the budgetary framework in other subchapters.

(ii) Data requirements

The 2010 update of the stability programme adheres closely to the data requirements specified in the Annex 2 of the code of conduct. Nevertheless, it misses some of the required data, notably changes in inventories and net acquisition of valuables. Regarding the optional data, the programme does not provide figures on compensation of employees for the 2010-2012 period.

The tables on the following pages show the data presented in the January 2010 update of stability programme, following the structure of the tables in Annex 2 of the code of conduct. Compulsory data are in bold, missing data are indicated with grey-shading.

(iii) Separate chapter on progress made in the correction of the excessive deficit

In its recommendations under Article 126(7) of 2 December 2009 with a view to bring the excessive deficit situation to an end, the Council also invited Slovakia to report on progress made in the implementation of the Council's recommendations in a separate chapter in the updates of the stability programmes. Slovakia complied with this recommendation.

(iv) Other information requirements

The table below provides a summary assessment of the adherence to the other information requirements in the code of conduct.

* * *

The SCP…	Yes	No	Comments
a. Involvement of parliament			
… mentions status vis-à-vis national parliament.	X		
… indicates whether Council opinion on previous programme has been presented to national parliament.		X	
b. Economic outlook			
… (for euro area and ERM II Member States) uses "common external assumptions" on main extra-EU variables.	X		
… explains significant divergences with Commission services' forecasts[1].		X	
… bears out possible upside/downside risks to economic outlook.		X	

The SCP…	Yes	No	Comments
… analyses outlook for sectoral balances and, especially for countries with high external deficit, external balance.		X	
c. Monetary/exchange rate policy			
… (CP only) presents medium-term monetary policy objectives and their relationship to price and exchange rate stability.			not applicable
d. Budgetary strategy			
… presents budgetary targets for general government balance in relation to MTO and projected path for debt ratio.	X		
… (in case new government has taken office) shows continuity with respect to budgetary targets endorsed by Council.			not applicable
… (when applicable) explains reasons for deviations from previous targets and, in case of substantial deviations, whether measures are taken to rectify situation (+ provides information on them).	X		The measures lack sufficient detail.
… backs budgetary targets by indication of broad measures necessary to achieve them and analyses their quantitative effects on balance.	X		
… specifies state of implementation of measures.	X		
e. "Major structural reforms"			
… (if MTO not yet reached or temporary deviation is planned from MTO) includes comprehensive information on economic and budgetary effects of possible 'major structural reforms' over time.		X	
… includes quantitative cost-benefit analysis of short-term costs and long-term benefits of reforms.		X	
f. Sensitivity analysis			
… includes comprehensive sensitivity analyses and/or develops alternative scenarios showing impact on balance and debt of: a) changes in main economic assumptions b) different interest rate assumptions c) (for CP only) different exchange rate assumptions d) if common external assumptions are not used, changes in assumptions for main extra-EU variables.	X		
… (in case of "major structural reforms") analyses how changes in assumptions would affect budget and potential growth.			not applicable
g. Broad economic policy guidelines			
… provides information on consistency with broad economic policy guidelines of budgetary objectives and measures to achieve them.		X	
h. Quality of public finances			
… describes measures to improve quality of public finances, both revenue and expenditure sides.	X		
i. Long-term sustainability			
… outlines strategies to ensure sustainability.		X	
… includes common budgetary projections by the AWG and all necessary additional information (esp. new relevant information).	X		
j. Other information (optional)			
… includes information on implementation of existing national budgetary rules and on other institutional features of public finances.		X	

Notes: SCP = stability/convergence programme; CP = convergence programme
[1]To the extent possible, bearing in mind the typically short time period between the publication of the Commission services' autumn forecast and the submission of the programme.

Source:
Commission services

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Tables from Annex 2 of the code of conduct

Table 1a. Macroeconomic prospects

	ESA Code	2008	2008	2009	2010	2011	2012
		Level	rate of change	rate of change	rate of change	rate of change	rate of change
1. Real GDP	B1*g	*50.4*	6.4	-5.7	1.9	4.1	5.4
2. Nominal GDP	B1*g	*67.2*	9.5	-5.5	5.9	7.5	8.9
Components of real GDP							
3. Private consumption expenditure	P.3	*26.6*	6.1	-0.4	1.5	3.4	4.9
4. Government consumption expenditure	P.3	*8.3*	4.3	2.3	2.4	3.0	2.4
5. Gross fixed capital formation	P.51	*13.2*	6.8	-10.3	2.9	4.1	5.1
6. Changes in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.
7. Exports of goods and services	P.6	*48.3*	3.2	-15.2	2.9	7.1	10.0
8. Imports of goods and services	P.7	*46.7*	3.3	-14.7	3.2	5.6	8.4
Contributions to real GDP growth							
9. Final domestic demand		-	5.9	-2.4	1.4	2.7	3.9
10. Changes in inventories and net acquisition of valuables	P.52 + P.53	-	0.5	-2.5	0.6	0.3	0.0
11. External balance of goods and services	B.11	-	0.0	-0.8	-0.1	1.1	1.5

Table 1b. Price developments

	ESA Code	2008	2008	2009	2010	2011	2012
		Level	rate of change	rate of change	rate of change	rate of change	rate of change
1. GDP deflator		*1.3*	3.0	0.2	3.8	3.2	3.4
2. Private consumption deflator		*1.4*	4.5	2.0	3.0	3.8	4.0
3. HICP[1]		*n.a.*	3.9	1.2	2.6	3.7	4.1
4. Public consumption deflator		*1.4*	4.4	3.1	3.0	3.8	4.0
5. Investment deflator		*1.3*	2.0	-1.1	2.8	2.4	2.3
6. Export price deflator (goods and services)		*1.2*	1.4	-5.0	0.8	0.5	0.6
7. Import price deflator (goods and services)		*1.2*	3.0	-5.0	1.2	1.1	0.7

Table 1c. Labour market developments

	ESA Code	2008	2008	2009	2010	2011	2012
		Level	rate of change	rate of change	rate of change	rate of change	rate of change
1. Employment, persons[1]		*2 237.1*	2.8	-1.9	-0.1	0.9	1.6
2. Employment, hours worked[2]		*3958.3*	2.4	-6.6	2.9	2.6	1.8
3. Unemployment rate (%)[3]		*9.6*	1.4	2.1	0.4	-0.5	-0.6
4. Labour productivity, persons[4]		*22566*	4.3	-3.7	2.0	3.2	3.7
5. Labour productivity, hours worked[5]		*12753*	3.9	1.0	-1.0	1.4	3.6
6. Compensation of employees	D.1	*24129*	8.1	2.6	3.4	6.5	7.5
7. Compensation per employee		*10786*	5.1	2.4	optional	optional	optional

[1]Occupied population, domestic concept national accounts definition.

[2]National accounts definition.

[3]Harmonised definition, Eurostat; levels.

[4]Real GDP per person employed.

[5]Real GDP per hour worked.

Table 1d. Sectoral balances

% of GDP	ESA Code	2008	2009	2010	2011	2012
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	-5.3	-4.2	-3.2	-2.7	-1.9
of which :						
- Balance on goods and services		-1.8	-2.5	-2.9	-2.3	-1.4
- Balance of primary incomes and transfers		-4.7	-3.3	-2.3	-2.5	-2.6
- Capital account		1.2	1.6	2.0	2.1	2.1
2. Net lending/borrowing of the private sector	B.9	-3.0	2.1	2.3	1.5	1.1
3. Net lending/borrowing of general government	EDP B.9	-2.3	-6.3	-5.5	-4.2	-3.0
4. Statistical discrepancy		n.a.	optional	optional	optional	optional

Table 2. General government budgetary prospects

	ESA Code	2008	2008	2009	2010	2011	2012
		Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
Net lending (EDP B.9) by sub-sector							
1. General government	S.13	*-1549*	-2.3	-6.3	-5.5	-4.2	-3.0
2. Central government	S.1311	*-1801*	-2.7	-5.6	-5.5	-4.3	-3.0
3. State government	S.1312	*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.
4. Local government	S.1313	*-48*	-0.1	-0.2	0.0	0.0	0.0
5. Social security funds	S.1314	*300*	0.4	-0.6	0.0	0.2	0.1
General government (S13)							
6. Total revenue	TR	*21844*	32.5	32.8	32.5	32.3	31.7
7. Total expenditure	TE[1]	*23393*	34.8	39.1	38.0	36.5	34.7
8. Net lending/borrowing	EDP B.9	*-1549*	-2.3	-6.3	-5.5	-4.2	-3.0
9. Interest expenditure	EDP D.41	*833*	1.2	1.8	1.9	1.9	1.9
10. Primary balance[2]		*-715*	-1.1	-4.5	-3.6	-2.3	-1.1
11. One-off and other temporary measures[3]		*-452*	-0.7	0.0	0.0	0.0	0.0
Selected components of revenue							
12. Total taxes (12=12a+12b+12c)		*11318*	16.8	16.7	16.4	16.5	16.4
12a. Taxes on production and imports	D.2	*6995*	10.4	10.8	10.9	10.6	10.4
12b. Current taxes on income, wealth, etc	D.5	*4322*	6.4	5.9	5.6	5.9	6.0
12c. Capital taxes	D.91	*0*	0.0	0.0	0.0	0.0	0.0
13. Social contributions	D.61	*8137*	12.1	12.4	12.0	11.9	11.9
14. Property income	D.4	*816*	1.2	1.4	0.9	0.8	0.7
15. Other[4]		*1573*	2.3	2.3	3.2	3.1	2.7
16=6. Total revenue	TR	*21844*	32.5	32.8	32.5	32.3	31.7
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)[5]		19455.0	28.9	29.1	28.4	28.5	28.3
Selected components of expenditure							
17. Compensation of employees + intermediate consumption	D.1+P.2	*7781*	11.6	12.3	11.2	10.8	10.0
17a. Compensation of employees	D.1	*4417*	6.6	7.4	7.0	6.7	6.3
17b. Intermediate consumption	P.2	*3364*	5.0	4.8	4.2	4.1	3.7
18. Social payments (18=18a+18b)		*10515*	15.6	18.4	18.5	18.2	17.7
18a. Social transfers in kind supplied via market producers	D.6311, D.63121, D.63131	*2924*	4.3	5.0	5.1	5.0	5.0
18b. Social transfers other than in kind	D.62	*7591*	11.3	13.4	13.4	13.2	12.7
19=9. Interest expenditure	EDP D.41	*833*	1.2	1.8	1.9	1.9	1.8
20. Subsidies	D.3	*1116*	1.7	1.8	1.7	1.6	1.6
21. Gross fixed capital formation	P.51	*1314*	2.0	1.9	1.6	1.6	1.2
22. Other[6]		*1833*	2.7	3.0	3.0	2.5	2.3
23=7. Total expenditure	TE[1]	*23393*	34.8	39.1	38.0	36.5	34.7
p.m.: Government consumption (nominal)	P.3	*11691*	17.4	19.0	18.0	17.5	16.7

[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 and including an adjustment for uncollected taxes and social contributions (D.995), if appropriate.

[6] D.29+D4 (other than D.41)+ D.5+D.7+D.9+P.52+P.53+K.2+D.8.

Table 3. General government expenditure by function

% of GDP	COFOG Code	**2008**	**2012**
1. General public services	1	3.7	4.7
2. Defence	2	1.4	1.0
3. Public order and safety	3	2.3	1.5
4. Economic affairs	4	5.4	4.4
5. Environmental protection	5	0.6	1.0
6. Housing and community amenities	6	0.6	0.8
7. Health	7	6.7	7.3
8. Recreation, culture and religion	8	0.9	0.9
9. Education	9	3.3	4.1
10. Social protection	10	9.8	11.5
11. Total expenditure (=item 7=23 in Table 2)	TE[1]	34.7	37.1

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

Table 4. General government debt developments

% of GDP	ESA Code	**2008**	**2009**	**2010**	**2011**	**2012**
1. Gross debt[1]		27.7	37.1	40.8	42.5	42.2
2. Change in gross debt ratio		-1.7	9.4	3.7	1.7	-0.3
Contributions to changes in gross debt						
3. Primary balance[2]		1.1	4.5	3.6	2.3	1.1
4. Interest expenditure[3]	EDP D.41	1.2	1.8	1.9	1.9	1.9
5. Stock-flow adjustment		-1.5	1.5	0.3	0.3	0.2
of which:						
- Differences between cash and accruals[4]		0.1	0.8	-0.1	0.0	0.0
- Net accumulation of financial assets[5]		-0.9	0.7	0.4	0.3	0.2
of which:						
- privatisation proceeds		n.a.	n.a.	n.a.	n.a.	n.a.
- Valuation effects and other[6]		-0.7	0.0	0.0	0.0	0.0
p.m.: Implicit interest rate on debt[7]		4.6	6.2	5.5	5.0	4.8
Other relevant variables						
6. Liquid financial assets[8]		3.7	4.1	3.9	3.7	3.3
7. Net financial debt (7=1-6)		24.0	33.0	36.9	38.8	38.9

[1]As defined in Regulation 3605/93 (not an ESA concept).

[2]Cf. item 10 in Table 2.

[3]Cf. item 9 in Table 2.

[4]The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant.

[5]Liquid assets, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant.

[6]Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant.

[7]Proxied by interest expenditure divided by the debt level of the previous year.

[8]AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted in stock exchange; including mutual fund shares).

Table 5. Cyclical developments

% of GDP	ESA Code	2008	2009	2010	2011	2012
1. Real GDP growth (%)		6.2	-5.7	1.9	4.1	5.4
2. Net lending of general government	EDP B.9	-2.3	-6.3	-5.5	-4.2	-3.0
3. Interest expenditure	EDP D.41	1.2	1.8	1.9	1.9	1.9
4. One-off and other temporary measures[1]		-0.7	0.0	0.0	0.0	0.0
5. Potential GDP growth (%)		4.9	2.1	1.9	2.7	3.6
contributions:						
- labour		0.6	0.4	0.3	0.3	0.4
- capital		1.9	1.5	1.4	1.4	1.5
- total factor productivity		2.4	0.2	0.3	0.9	1.8
6. Output gap		3.9	-3.9	-4.3	-2.9	-1.2
7. Cyclical budgetary component		1.1	-1.1	-1.2	-0.8	-0.4
8. Cyclically-adjusted balance (2 - 7)		-3.4	-5.2	-4.3	-3.4	-2.6
9. Cyclically-adjusted primary balance (8 + 3)		-2.2	-3.4	-2.3	-1.5	-0.8
10. Structural balance (8 - 4)		-2.8	-5.2	-4.3	-3.4	-2.6

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

Table 6. Divergence from previous update

	ESA Code	2008	2009	2010	2011	2012
Real GDP growth (%)						
Previous update		6.4	2.4	3.6	4.5	5.1
Current update		6.2	-5.7	1.9	4.1	5.4
Difference		-0.2	-8.1	-1.7	-0.4	0.3
General government net lending (% of GDP)	EDP B.9					
Previous update		-2.2	-3.0	-2.9	-2.2	n.a.
Current update		-2.3	-6.3	-5.5	-4.2	-3.0
Difference		-0.1	-3.3	-2.6	-2.0	n.a.
General government gross debt (% of GDP)						
Previous update		27.6	31.4	32.7	32.7	n.a.
Current update		27.7	37.1	40.8	42.5	42.2
Difference		0.0	5.7	8.1	9.8	n.a.

Table 7. Long-term sustainability of public finances

% of GDP	2007	2010	2020	2030	2040	2050
Total expenditure	34.4	38.0	39.1	43.0	48.8	57.5
Of which: age-related expenditures	15.2	14.9	14.5	16.1	17.5	19.2
Pension expenditure	6.8	6.6	6.3	7.3	8.3	9.4
Social security pension	6.8	6.6	6.3	7.3	8.3	9.4
Old-age and early pensions	4.3	4.0	3.6	4.1	4.8	5.6
Other pensions (disability, survivors)	2.5	2.6	2.7	3.2	3.5	3.8
Occupational pensions (if in general government)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Health care	5.0	5.2	5.7	6.2	6.7	7.1
Long-term care *(this was earlier included in the health care)*	0.2	0.2	0.2	0.3	0.4	0.5
Education expenditure	3.1	2.8	2.2	2.2	2.1	2.1
Other age-related expenditures	0.1	0.1	0.1	0.1	0.1	0.1
Interest expenditure	1.4	1.6	3.1	5.5	9.8	16.9
Total revenue	32.5	32.5	32.2	32.1	32.0	31.9
Of which: property income	1.5	1.4	1.2	1.1	1.1	1.1
Of which : from pensions contributions (or social contributions if appropriate)	11.8	12.0	11.7	11.6	11.5	11.4
Pension reserve fund assets	2.5	5.5	16.5	28.4	41.7	53.4
Of which : consolidated public pension fund assets (assets other than government liabilities)	0.0	0.0	0.0	0.0	0.0	0.0
Assumptions						
Labour productivity growth	5.3	4.7	3.1	2.7	1.7	1.7
Real GDP growth	6.4	6.2	3.4	2.0	0.5	0.2
Participation rate males (aged 20-64)	76.6	77.7	79.1	78.2	75.7	75.5
Participation rates females (aged 20-64)	61.2	62.9	66.7	67.5	65.3	65.2
Total participation rates (aged 20-64)	68.8	70.3	72.9	72.8	70.5	70.4
Unemployment rate	11.1	11.0	6.2	6.2	6.2	6.2
Population aged 65+ over total population	11.9	12.3	16.4	21.3	25.3	31.6

Table 8. Basic assumptions

	2008	2009	2010	2011	2012
Short-term interest rate[1] (annual average)	4.6	1.3	1.5	2.1	2.8
Long-term interest rate (annual average)	4.0	3.2	3.5	4.1	4.1
USD/€ exchange rate (annual average) (euro area and ERM II countries)	1.47	1.48	1.48	1.49	1.50
Nominal effective exchange rate	n.a.	n.a.	n.a.	n.a.	n.a.
(for countries not in euro area or ERM II) exchange rate vis-à-vis the € (annual average)	-	-	-	-	-
World excluding EU, GDP growth	3.9	-0.4	3.8	4.1	4.1
EU GDP growth	1.0	-4.1	0.7	1.6	1.6
Growth of relevant foreign markets	1.5	-4.1	0.9	1.9	2.2
World import volumes, excluding EU	4.1	-12.6	4.6	5.0	5.0
Oil prices (Brent, USD/barrel)	98.5	61.3	76.5	80.5	85.5

[1]If necessary, purely technical assumptions.