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**REPORT FROM THE COMMISSION**

**Slovakia**

**Report prepared in accordance with Article 126(3) of the Treaty on the Functioning of the European Union**

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## 1. INTRODUCTION

On 20 March 2020, the Commission adopted a Communication on the activation of the general escape clause of the Stability and Growth Pact. The clause, as set out in Articles 5(1), 6(3), 9(1) and 10(3) of Regulation (EC) 1466/97 and Articles 3(5) and 5(2) of Regulation (EC) 1467/97, facilitates the coordination of budgetary policies in times of severe economic downturn. In its Communication, the Commission shared with the Council its view that, given the expected severe economic downturn resulting from the COVID-19 outbreak, the current conditions permit activation of the clause. On 23 March 2020, the Ministers of Finance of the Member States agreed with the assessment of the Commission. The activation of the general escape clause allows for a temporary departure from the adjustment path towards the medium-term budgetary objective, provided that this does not endanger fiscal sustainability in the medium term. For the corrective arm, the Council may also decide, on a recommendation from the Commission, to adopt a revised fiscal trajectory. The general escape clause does not suspend the procedures of the Stability and Growth Pact. It allows Member States to depart from the budgetary requirements that would normally apply while enabling the Commission and the Council to undertake the necessary policy coordination measures within the framework of the Pact.

Data notified by the Slovak authorities on 14 April 2020 and subsequently validated by Eurostat[1] show that the general government deficit in Slovakia reached 1.3% of GDP in 2019, while general government gross debt stood at 48% of GDP. According to the letter sent by Slovak authorities to the Commission on 11 of May, Slovakia plans a deficit of 8.4%[2] of GDP in 2020, while debt is planned at 61.2% of GDP.

The planned deficit for 2020 provides *prima facie* evidence of the existence of an excessive deficit as defined by of the Stability and Growth Pact.

Against this background, the Commission has therefore prepared this report, which analyses Slovakia's compliance with the deficit criteria of the Treaty.The debt criterion can be considered to be met as the debt ratio is below in 2019 the Treaty reference value of 60% of GDP. It takes into account all relevant factors and gives due consideration to the major economic shock linked to the COVID-19 pandemic.

[1] https://ec.europa.eu/eurostat/documents/2995521/10294648/2-22042020-AP-EN.pdf/6c8f0ef4-6221-1094-fef7-a07764b0369f

[2] The Stability Programme was officially submitted on 18 May.

**Table 1. General government deficit and debt (% of GDP)**

| | | 2016 | 2017 | 2018 | 2019 | 2020 COM | 2021 COM |
|---|---|---|---|---|---|---|---|
| Deficit criterion | General government balance | -2.5 | -1.0 | -1.0 | -1.3 | -8.5 | -4.2 |
| Debt criterion | General government gross debt | 52.0 | 51.3 | 49.4 | 48.0 | 59.5 | 59.9 |
| | | | | | | | |

Source: Eurostat, Commission 2020 spring forecast

## 2. DEFICIT CRITERION

Based on the letter sent by Slovak authorities to the Commission on 11 of May, Slovakia´s general government deficit in 2020 is expected to reach 8.4% of GDP, above and not close to the Treaty reference value of 3% of GDP. The increase in deficit reflects the planned stimulus of 2.5% of GDP and the effects of the economic contraction.

The planned excess over the Treaty reference value in 2020 is exceptional, as it results from a severe economic downturn. Taking into account the impact of the COVID-19 pandemic, the Commission 2020 spring forecast projects a contraction of real GDP in 2020 by 6.7%.

The planned excess over the Treaty reference value is not temporary based on the Commission 2020 spring forecast, which projects the general government deficit to be above 3% of GDP in 2021.

In sum, the planned deficit for 2020 is above and not close to the 3%-of-GDP Treaty reference value. The planned excess is considered to be exceptional but not temporary as defined by the Treaty and the Stability and Growth Pact. Hence, the analysis suggests that *prima facie* the deficit criterion for the purpose of the Treaty and Regulation (EC) No 1467/97 is not fulfilled.

## 3. RELEVANT FACTORS

Article 126(3) of the Treaty provides that, if a Member State does not fulfil the requirements under one or both of those criteria, the Commission has to prepare a report. That report must also "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".

Those factors are further clarified in Article 2(3) of Regulation (EC) No 1467/97, which also provides that "any other factors which, in the opinion of the Member State concerned, are relevant in order to comprehensively assess compliance with the deficit and debt criteria and which the Member State has put forward to the Council and to the Commission" need to be given due consideration.

In the current situation, a key additional factor to take into consideration regarding 2020 is the economic impact of the COVID-19 pandemic, which has a very substantial impact on the budgetary situation and results in a highly uncertain outlook. The pandemic has also led to the activation of the general escape clause.

### 3.1. COVID-19 pandemic

The COVID-19 pandemic has led to a major economic shock that is having a significant negative impact throughout the European Union. The consequences for GDP growth will depend on the duration of both the pandemic and of the measures taken by national authorities and at European and global level to slow its spread, protect production capacities and support aggregate demand. Member States have already adopted or are adopting budgetary measures to increase the capacity of health systems and provide relief to those individuals and sectors that are particularly impacted. Significant liquidity support measures and other guarantees have also been adopted. Subject to more detailed information, the competent statistical authorities are to examine whether those measures entail an immediate impact on the general government balance or not. Together with the fall in economic activity, those measures will contribute to substantially higher government deficit and debt positions.

### 3.2 Medium-term economic position

Economic growth reached 2.3% in 2019, mainly due to the robust performance of domestic demand in Slovakia. However, due to the COVID-19 pandemic, the Commission 2020 spring forecast projects GDP to decline by 6.7% in 2020, reflecting the disruption in economic activity caused by the lockdown measures and an unprecedented fall in external demand. Private consumption is projected to be hard-hit due to an increase in unemployment, a sharp drop in wage growth and weak consumer confidence. Investment is also set to fall strongly in 2020 as uncertainty mounts and expectations of lower demand are likely to have an impact on firms’ investment plans. Output is set to drop strongly in the first half of 2020 and then to gradually recover from the third quarter onwards. This a mitigating factor in the assessment of Slovakia´s compliance with the deficit criterion in 2020. Moreover, the medium-term economic outlook is marked by an exceptional degree of uncertainty on the duration of the pandemic and its economic impact.

### 3.3 Medium-term budgetary position

On 13 July 2018, Slovakia was recommended to ensure that the nominal growth rate of net primary government expenditure does not exceed 4.6% in 2019 (‘the expenditure benchmark’), corresponding to a structural adjustment of 0.3% of GDP[3]. The overall assessment points to a significant deviation from the recommended adjustment path towards the medium-term budgetary objective in 2019. A similar assessment is obtained from looking at 2018-2019 taken together.

Over the course of 2019, the Slovakia adopted several measures that further endangered the fiscal position (in particular in pensions).

The letter sent by Slovak authorities to the Commission on 11 of May provides information on substantial new spending to contain the pandemic and to support the economy. Those fiscal measures so far adopted by the government are often not clearly limited in duration. The letter sent by Slovak authorities to the Commission on 11 of May estimates the budgetary impact of those direct support measures at 2.5% of GDP in 2020. The medium-term fiscal outlook remains subject to high uncertainty.

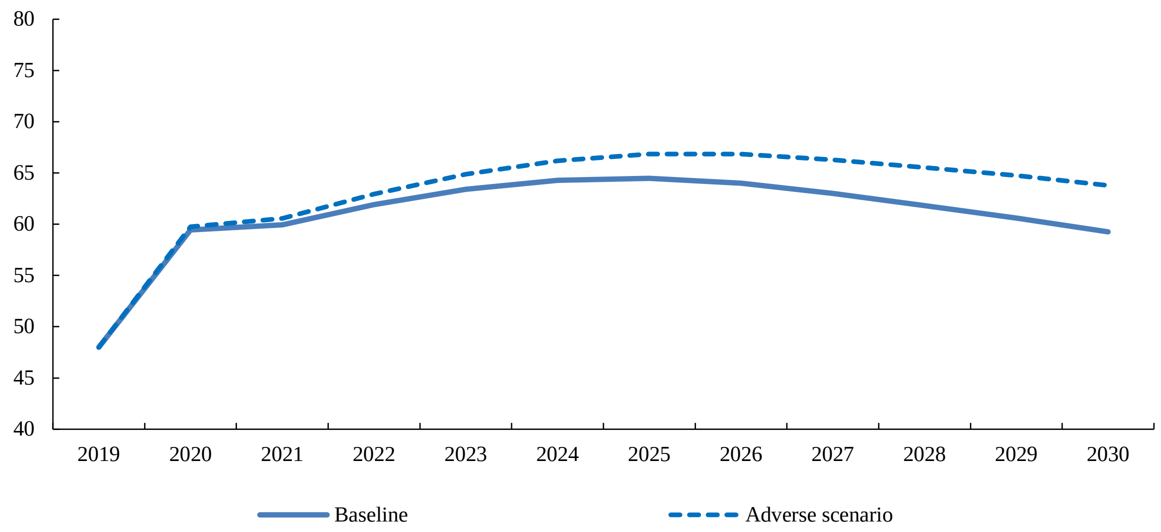
[3] Council Recommendation of 13 July 2018 on the 2018 National Reform Programme of Slovakia and delivering a Council opinion on the 2018 Stability Programme of Slovakia (OJ C 320, 10.9.2018, p. 107).

### 3.4 Medium-term government debt position

According to the Commission 2020 spring forecast, general government debt is expected to rise from 48.0% of GDP in 2019 to 59.5% in 2020.

The debt sustainability analysis has been updated with the Commission 2020 spring forecast. Overall, the debt sustainability assessment indicates that notwithstanding some risks, the debt position remains sustainable over the medium-term, also given important mitigating factors (including the debt profile). In particular, while the government debt position deteriorates as a result of the COVID-19 crisis, the debt ratio in the baseline is expected to be on a sustainable (declining) trajectory over the medium term.[4]

**Graph 1: General government debt (% of GDP)**




Source: Commission services

### 3.5 Other factors put forward by the Member State

On 11 of May 2020, the Slovak authorities transmitted a letter with relevant factors in accordance with Article 2(3) of Regulation (EC) No 1467/97. The analysis presented in the previous sections already broadly covers the key factors put forward by the authorities.

## 4. CONCLUSIONS

According to the letter sent by Slovak authorities to the Commission on 11 of May, Slovakia's general government deficit in 2020 is planned to increase to 8.4% of GDP, above

[4] The baseline is based on the Commission Spring 2020 forecast. Beyond 2021, a gradual adjustment of fiscal policy is assumed, consistent with the EU economic and fiscal coordination and surveillance frameworks. Real GDP growth is projected according to the so-called EPC/OGWG T+10 methodology. In particular, (real) actual GDP growth is driven by its potential growth and affected by any additional fiscal adjustment considered (through the fiscal multiplier). Inflation is assumed to converge gradually to 2%. Interest rates assumptions are set in line with financial market expectations. Under the adverse scenario, higher interest rates (by 500 bps.) and lower GDP growth (by -0.5 pp.), with respect to the baseline, are assumed (throughout the projection horizon)

and not close to the 3% of GDP Treaty reference value. The planned excess over the reference value is considered to be exceptional but not temporary.

In line with the Treaty and the Stability and Growth Pact, this report also examined relevant factors. Overall, since the planned deficit is well above 3% of GDP and the excess not temporary, and taking into account all relevant factors, the analysis suggests that the deficit criterion as defined in the Treaty and in Regulation (EC) No 1467/1997 is not fulfilled.