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Delegations will find attached document SWD(2013) 611 final.

This document is aimed for discussion in the **Eurogroup.**

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COMMISSION STAFF WORKING DOCUMENT

Analysis of the Draft Budgetary Plan of SLOVENIA

Accompanying the document

COMMISSION OPINION

on the Draft Budgetary Plan of SLOVENIA

{C(2013) 8010 final}

COMMISSION STAFF WORKING DOCUMENT

Analysis of the Draft Budgetary Plan of SLOVENIA

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COMMISSION OPINION

on the Draft Budgetary Plan of SLOVENIA

1. INTRODUCTION

Slovenia has submitted its Draft Budgetary Plan (DBP) for 2014 on 15 October 2013[1] in compliance with Regulation (EU) No 473/2013 of the Two-Pack together with a report on effective action and an economic partnership programme as recommended by the Council in June 2013.

Slovenia is currently subject to the corrective arm of the Stability and Growth Pact. The Council opened the Excessive Deficit Procedure for Slovenia on 2 December 2009 and recommended to correct the excessive deficit by 2013. On 21 June 2013, the Council concluded that Slovenia had taken effective action but adverse economic events with major implications on public finances had occurred, and issued revised recommendations based on Article 126(7) TFEU. Slovenia was given a deadline of 1 October 2013 to take effective action to ensure a sustainable correction of the excessive deficit by 2015.

Section 2 of this document presents the macroeconomic outlook underlying the Draft Budgetary Plan and provides an assessment based on the Commission 2013 Autumn forecast (hereinafter Commission Forecast). The following section presents the recent and planned fiscal developments, according to the Draft Budgetary Plan, including an analysis of risks to their achievement based on Commission Forecast. In particular, it also includes an assessment of the measures underpinning the Draft Budgetary Plan. Section 4 assesses the recent and planned fiscal developments in 2013-2014 (also taking into account the risks to their achievement) against the obligations stemming from the Stability and Growth Pact. Section 5 provides an analysis of the fiscal structural reforms presented in the economic partnership programme, as requested in the latest Council recommendations. Section 6 summarises the main conclusions of the present document.

2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

The macroeconomic scenario underpinning the Draft Budgetary Plan projects real GDP to contract further by 2.4% and 0.8% in 2013 and 2014, respectively. Domestic demand will continue to act as drag on growth on the back of the on-going deleveraging process in the economy and tight financing conditions. By contrast, net exports will remain the only positive contributor to economic activity. As GDP is set to decline, the lagged adjustment in the labour

[1] An addendum to the Draft Budgetary Plan explaining the institutional setting of the body making the macroeconomic scenario underpinning the budget was submitted on 23 October 2013.

market is expected to continue, with employment and compensation of employees per head contracting in both 2013 and 2014, also under the impact of measures to contain the public sector wage bill. Relative to the 2013 Stability Programme, real GDP growth for 2013 has been revised downwards mainly due to lower-than-expected gross capital formation in the first half of the year.

Compared to the Draft Budgetary Plan, the Commission Forecast projects a slightly larger real GDP decline in both 2013 and 2014, resulting from a more modest net export contribution and larger fall in final domestic demand in 2013 and more severe retrenchment in gross capital formation in 2014. Assessed against currently available information, the Draft Budgetary Plan's macroeconomic scenario for both years appears broadly plausible. Risks to growth and domestic demand in particular are related to the financing conditions for the overall economy, which in turn hinge upon the speed of the ongoing deleveraging process and the implementation of the needed bold structural reforms.

Table 1. Comparison of macroeconomic developments and forecasts

	2012	2013			2014		
	COM	SP	DBP	COM	SP	DBP	COM
Real GDP (% change)	-2.5	-1.9	-2.4	-2.7	0.2	-0.8	-1.0
Private consumption (% change)	-4.8	-4.0	-3.5	-3.6	-1.3	-2.7	-2.6
Gross fixed capital formation (% change)	-8.2	-0.5	-1.6	-4.2	0.8	-4.0	-2.7
Exports of goods and services (% change)	0.6	1.2	2.0	1.3	3.3	3.0	2.6
Imports of goods and services (% change)	-4.7	-0.7	0.1	-0.2	2.4	2.1	0.8
Contributions to real GDP growth:							
- Final domestic demand	-4.5	-3.3	-2.8	-3.3	-0.6	-2.6	-2.4
- Change in inventories	-1.8	-0.2	-1.0	-0.4	0.2	0.9	0.0
- Net exports	3.8	1.4	1.5	1.1	0.8	0.9	1.4
Output gap[1]	-2.3	-3.5	-3.1	-3.1	-2.7	-3.2	-3.2
Employment (% change)	-0.8	-1.6	-2.3	-2.4	-0.8	-1.4	-1.3
Unemployment rate (%)	8.9	10.0	9.7	11.1	10.0	9.9	11.6
Labour productivity (% change)	-1.7	-0.2	-0.1	-0.2	1.0	0.6	0.3
HICP inflation (%)	2.8	2.1	2.0	2.1	1.6	1.9	1.9
GDP deflator (% change)	0.2	1.3	1.3	1.7	1.1	1.4	1.1
Comp. of employees (per head, % change)	-1.0	0.0	-1.4	-0.2	0.7	-0.4	0.0
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	2.9	n.a.	n.a.	3.1	n.a.	n.a.	2.5

Note:

[1]In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

Source :

Stability programme (SP); Draft Budgetary Plan (DBP); Commission services' 2013 Autumn Forecast (COM); Commission services' calculations.

Box 1: The macro economic forecast underpinning the Draft Budgetary Plan in Slovenia

The macroeconomic scenario underpinning the Draft Budgetary Plan is the Autumn 2013 Forecast of Economic Trends prepared by the Institute of Macroeconomic Analysis and Development (hereinafter IMAD) and made available to the Ministry of Finance on 17 September.

The Ministry of Finance uses IMAD's forecast to underpin its budgetary planning documents; it does not produce its own macroeconomic forecasts. The independent status and tasks of IMAD are stipulated in a specific Resolution. So far IMAD has produced regular economic forecasts twice a year (in March and October) to underpin the stability programme update in April and the draft budget, and additional forecasts to support other possible planning documents (i.e. supplementary budgets). The authorities are currently preparing an overhaul of the legislation underpinning Slovenia's fiscal framework, including independent bodies, in order to comply with the Treaty on Stability, Coordination and Governance in EMU and the EU legal requirements on fiscal governance.

3. RECENT AND PLANNED FISCAL DEVELOPMENTS

3.1. Deficit developments

The main objectives of the Draft Budgetary Plan are to contribute to the correction of the excessive deficit by 2015 and ensure a gradual consolidation of public finances in a sustainable manner. The general government deficit targets, including estimated bank recapitalisation needs, stand at 5.6% and 6.7% of GDP in 2013[2] and 2014, respectively. Without bank support, the deficit targets would stand at 3.8% and 3.3% of GDP[3].

Compared to the 2013 Stability Programme, the targeted deficit is lower for 2013 and higher for 2014 (both with and without bank recapitalisaitons). In particular, for 2013, the Draft Budgetary Plan incorporates on the one hand higher revenue projections from sales of market output and property income and on the other hand lower social transfers and intermediate consumption. Moreover, it projects a significantly lower absorption of EU funds[4] and lower capital transfers to banks[5]. The Commission Forecast projects the general government deficit for 2013 to be slightly higher, at 5.8% of GDP (4% of GDP without bank recapitalisation[6]), on account of lower revenue from social contributions and sales of market output. Such projections are consistent with the budgetary outturns over the first half of 2013.

The Draft Budgetary Plan forecasts the budgetary adjustment in 2014 to be achieved almost entirely through higher taxes, in particular direct taxes due to the introduction of the new real estate tax[7]. The size of the estimated capital transfers to banks explains much of the difference between the deficit target in the 2013 Stability Programme and Draft Budgetary Plan.

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2 The September 2013 EDP notification sets the general government deficit target for 2013 at 5.7% of GDP.

3 Neither the Draft Budgetary Plan nor the Commission Forecast include recapitalisations of state-owned non-financial corporations.

4 In the September 2013 EDP notification, the Statistical Office of the Republic of Slovenia excluded from the general government accounts, on both the revenue and the expenditure sides, EU funds for which the final beneficiaries are outside the general government. This revision has no impact on the general government deficit, however it reduces expenditure and revenue ratios by around ¾ pp. of GDP. The exclusion also makes projections in the Stability Programme and Draft Budgetary Plan for current and capital revenue (payable and receivable) and subsidies hardly comparable.

5 According to the revised timeline for the Asset Quality Review and Stress Tests in banks, the authorities project the bulk of bank recapitalisations to happen in 2014.

6 Before the conclusion of the stress tests for the banking system which will determine definite bank recapitalisation needs, the Commission Forecast incorporates identical estimates about them as the national authorities.

7 Revenues from taxes on production and import decrease as the higher VAT rates are more than offset by the cancellation of the compensation for the use of building land, which will be replaced by the new real estate tax (taxes on income and wealth).

The Commission Forecast for the deficit in 2014, which incorporates the draft budget for 2014 , is 7.1% of GDP (3.6% of GDP without the bank recapitalisations). Compared to the Draft Budgetary Plan, tax revenues and social contributions and sales of market output are lower. Furthermore, in line with past significant shortfalls in the absorption of EU funds, the increase in capital transfers received is moderate. On the expenditure side, this assumption translates into a significantly lower projection for public investment[8]. In addition, compensation of employees is expected to be slightly higher than in the Draft Budgetary Plan in light of past regular overruns.

Risks to public finance projections are tilted to the negative side for several reasons. There are risks that the proposed measures are cancelled or reduced during the adoption process. In addition, the Supreme Court judgement repealing the postponement of the third instalment of the increase in public sector wages adopted in November 2010 is likely to entail higher expenditure in 2014. Finally, additional capital support needs might materialise in the restructuring process of overleveraged state-owned non-financial corporations. These risks might be partially compensated for by the revenue from an envisaged auction of licences for the 4th generation of the mobile network which are not incorporated in the Draft Budgetary Plan. A further important element of uncertainty in the government accounts is related to the bank recapitalistion needs that will be correctly established only after the finalisation of the ongoing Asset Quality Reviews and Stress Tests.

Table 2. Composition of the budgetary adjustment

[8] Consecutive budgets are overly optimistic in projections of public investment partially financed from EU funds. For instance, budgetary projections indicated public investment growth of 11.5%, 5.7% and 26.5% over 2010-2012, but outturns for public investment growth were -3.1%, -18% and -12.6% over these years.

(% of GDP)	2012	2013			2014			Change: 2012-2014
	COM	**SP**	**DBP**	**COM**	**SP**	**DBP**	**COM**	**DBP**
Revenue	**44.2**	**45.5**	***44.8***	**44.3**	**46.8**	***46.2***	**45.0**	**2.0**
of which:								
- Taxes on production and imports	14.3	15.0	*15.1*	15.1	15.6	*14.9*	14.8	0.6
- Current taxes on income, wealth, etc.	7.8	7.6	*7.7*	7.6	8.8	*8.9*	8.8	1.1
- Capital taxes	0.0	0.1	*0.1*	0.1	0.1	*0.1*	0.1	0.1
- Social contributions	15.5	15.4	*15.4*	15.1	15.2	*15.3*	14.9	-0.2
- Other (residual)	6.6	7.4	*6.5*	6.5	7.1	*7.0*	6.4	0.4
Expenditure	**48.1**	**53.4**	**50.4**	**50.1**	**49.4**	**52.9**	**52.0**	**4.8**
of which:								
- Primary expenditure	45.9	50.7	47.7	47.3	46.5	49.8	48.9	3.9
of which:								
Compensation of employees	12.7	12.0	12.3	12.4	11.8	12.0	12.1	-0.7
Intermediate consumption	6.9	6.8	6.7	6.7	6.7	6.4	6.5	-0.5
Social payments	19.8	20.2	20.2	20.1	20.0	20.1	20.2	0.3
Subsidies	1.0	1.3	1.0	1.0	1.1	0.9	0.9	-0.1
Gross fixed capital formation	3.2	3.2	3.4	3.1	4.1	4.6	3.5	1.4
Other (residual)	2.2	7.2	4.1	4.0	2.8	5.8	5.8	3.6
- Interest expenditure	2.2	2.7	2.7	2.7	2.9	3.1	3.1	0.9
General government balance (GGB)	**-3.8**	**-7.9**	**-5.6**	**-5.8**	**-2.6**	**-6.7**	**-7.1**	**-2.9**
Primary balance	**-1.7**	**-5.2**	**-2.9**	**-3.0**	**0.3**	**-3.6**	**-4.0**	**-1.9**
One-off and other temporary measures	0.0	-3.7	-1.8	-1.5	0.0	-3.4	-3.4	-3.4
GGB excl. one-offs	**-3.8**	**-4.2**	**-3.8**	**-4.3**	**-2.6**	**-3.3**	**-3.6**	**0.5**
Output gap[1]	-2.3	-3.5	-3.1	-3.1	-2.7	-3.2	-3.2	-0.9
Cyclically-adjusted balance[1]	-2.8	-6.3	-4.2	-4.3	-1.4	-5.2	-5.6	-2.5
Structural balance (SB)[2]	**-2.7**	**-2.6**	**-2.4**	**-2.9**	**-1.4**	**-1.8**	**-2.1**	**0.9**
Change in SB	*2.2*	*0.1*	*0.4*	*-0.1*	*1.2*	*0.5*	*0.7*	-
Two year average change in SB	*1.0*	*1.2*	*1.3*	*1.0*	*0.7*	*0.5*	*0.3*	-
Structural primary balance[2]	-0.6	0.1	0.3	-0.1	1.5	1.3	0.9	1.8
Change in structural primary balance		*0.7*	*0.9*	*0.4*	*1.4*	*0.9*	*1.1*	-
Expenditure benchmark								
Applicable reference rate[3]	0.63	0.6	0.6	0.6	-0.51	-0.51	-0.51	-
Deviation[4] (% GDP)	-4.4	0.6	-2.0	-1.4	-8.0	-0.9	-0.1	-
Two-year average deviation (% GDP)	-1.6	-2.0	-3.6	-2.9	-3.7	-1.4	-0.8	-

Notes:

[1]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

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

[3] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A lower rate applies as long as the country is adjusting towards its MTO, including in year t.The reference rates applicable to 2014 onwards have been updated in 2013.

[4] Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A positive sign implies that expenditure growth exceeds the applicable reference rate.

Source :

Stability programme (SP); Draft Budgetary Plan (DBP); Commission 2013 Autumn Forecast (COM); Commission services' calculations.

The projected change in the structural balance[9] in the Draft Budgetary Plan is estimated at 0.4% and 0.5% of GDP in 2013 and 2014, respectively. The estimated structural improvement from the 2013 Stability Programme was lower for 2013 and higher for 2014, which is consistent with its less (more) ambitious headline deficit target for 2013 (2014). Relative to the Draft Budgetary Plan, the Commission Forecast also projects a lower structural improvement in 2013 and a higher one in 2014.

9 Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission services on the basis of the information provided in the Draft Budgetary Plan, using the commonly agreed methodology.

3.2. Debt developments

The Draft Budgetary Plan expects the general government gross debt to reach 63.1% and 65.5% of GDP in 2013 and 2014, respectively. Relative to the 2013 Stability Programme, the debt projections are higher due to the building-up of the cash buffer through two large sovereign bond issues in May 2013 and the higher primary deficit in 2014.

Table 3. Debt developments

(% of GDP)	2012	2013			2014		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio[1]	**54.4**	**61.8**	**63.1**	**63.2**	**63.2**	**65.5**	**70.1**
Change in the ratio	7.3	7.4	8.7	8.8	1.4	2.4	7.0
Contributions[2] :							
1. Primary balance	**1.7**	**5.2**	**2.9**	**3.0**	**-0.3**	**3.6**	**4.0**
2. "Snow-ball" effect	**3.3**	**3.0**	**3.3**	**3.3**	**2.0**	**2.7**	**3.0**
Of which:							
Interest expenditure	2.2	2.7	2.7	2.7	2.9	3.1	3.1
Growth effect	1.2	1.0	1.3	1.5	-0.1	0.5	0.6
Inflation effect	-0.1	-0.7	-0.7	-0.9	-0.7	-0.9	-0.7
3. Stock-flow adjustment	**2.4**	**-0.8**	**2.5**	**2.5**	**-0.3**	**-3.9**	**0.0**
Of which:							
Cash/accruals difference		n.a.	n.a.		n.a.	n.a.	
Net accumulation of financial		n.a.	n.a.		n.a.	n.a.	
of which privatisation proceeds		n.a.	n.a.		n.a	n.a.	
Valuation effect & residual		n.a.	n.a.		n.a.	n.a.	

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); Draft Budgetary Plan (DBP); Commission services' 2013 Autumn Forecast (COM); Commission services' calculations.

The Commission forecasts the debt ratio at 63.2% and 70.1% of GDP in 2013-2014. Its 2014 projection does not incorporate the debt-reducing contribution from the stock-flow adjustment included (but not specified) in the Draft Budgetary Plan, while the primary deficit and snowball effect add to the debt ratio in both years. Neither the Draft Budgetary Plan nor the Commission Forecast include any debt accumulation from the envisaged transfer of impaired banking assets to the Bank Asset Management Company (BAMC).

Risks to the debt projections, in both the Draft Budgetary Plan and the Commission Forecast, arise from the same factors listed above in relation to the deficit forecast as well as from the stock-flow adjustment with regard to asset transfers to the BAMC. Possible privatisation proceeds not explicitly included in the Draft Budgetary Plan, especially for the telecommunication incumbent, would represent a positive risk.

3.3. Measures underpinning the Draft Budgetary Plan

The public finances in 2013 are affected by successive consolidation packages (the 2012 supplementary budget, 2013 budget[10] and 2013 supplementary budget).

Table 4. Main discretionary measures reported in the DBP

Discretionary measures taken by General Government - revenue side

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2013	**2014**	**2015**
Taxes on production and imports	0.5	0.5	n.a.
Current taxes on income, wealth, etc.	0	0.8	0.1
Capital taxes	0.1	0	n.a.
Social contributions	n.a.	0.1	n.a.
Property Income	n.a.	n.a.	n.a.
Other	0	0.2	n.a.
Total	0.6	1.7	0.1

Note:

The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that revenue increases as a consequence of this measure.

Source: Draft Budgetary Plan

Discretionary measures taken by General Government - expenditure side

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2013	**2014**	**2015**
Compensation of employees	-1	-0.5	n.a.
Intermediate consumption	n.a.	n.a.	n.a.
Social payments	-0.5	-0.1	n.a.
Interest Expenditure	n.a.	n.a.	n.a.
Subsidies	n.a.	n.a.	n.a.
Gross fixed capital formation	n.a.	n.a.	n.a.
Capital transfers	n.a.	n.a.	n.a.
Other	-0.3	n.a.	n.a.
Total	-1.8	-0.6	0

Note:

The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that expenditure increases as a consequence of this measure.

Source: Draft Budgetary Plan

After the extension of the deadline for the correction of the excessive deficit, the new government turned the consolidation towards structural revenue-increasing measures. The 2013 supplementary budget increased the standard and reduced VAT rates (0.35% of GDP), to 22% and 9.5%, respectively, as of 1 July; raised road user charges and legal fees; and introduced a new tax on lottery tickets (0.05% of GDP). Revenues in 2013 also benefit from three one-off transactions: (i) the payment of ¾ (vs. ¼ in the past) of the Bank of Slovenia exceptionally high surplus in 2012 (0.23% of GDP), (ii) the concession fee for student work for 2012 and past years (0.1% of GDP); and (iii) social contributions and personal income tax revenues from the third instalment of the increase in public sector wages as requested by the

[10] Measures from the 2012 supplementary budget and 2013 budget are described in detail in the Commission Staff Working Document accompanying the Recommendation for a Council recommendation with a view to bringing an end to the situation of an excessive government deficit in Slovenia (COM(2013) 396 final).

Supreme Court (0.05% of GDP). On the expenditure side, the key new measure in 2013 is a temporary cut (until end 2014) in nominal public sector wages by around 1.25% on average coupled with cuts in some work-related benefits (supplements for educational degree, work tenure, sickness leave pay, etc.) introduced in June (0.17% of GDP). Payment of promotions from 2011, envisaged for 2013, is postponed to 2014 (0.19% of GDP). Moreover, a cut in intermediate consumption (0.15% of GDP) is envisaged. One-off recapitalisation of banks, including conversions of hybrid debt-equity instruments into equity of the two largest banks, amounting to 1.8% of GDP (€620m) is counted among expenditure-raising measures. On top, the Commission Forecast projects an additional decline in public investment (0.2% of GDP) given the track record in past years and the outturn in the first half of 2013.

The Draft Budgetary Plan for 2014 incorporates the draft budget for 2014 as approved by the government on 30 September 2013. The government accounts will benefit from the full-year effects of the June 2013 temporary cut in the nominal public sector wages (0.17% of GDP); increased VAT rates (0.35% of GDP); higher road charges and legal fees; and the new lottery ticket tax (0.08% of GDP). The tax-to-GDP ratio is projected to increase further because of the new real estate tax (0.52% of GDP), higher contributions for health insurance (0.13% of GDP) from mainly certain categories of self-employed, the elimination of the indexation for personal income tax allowances and tax bracket thresholds (0.08% of GDP) and the elimination of the personal income tax allowance for older people (0.05% of GDP). The government has also decided to stabilise the corporate income tax rate at 17%. Expenditure side measures are mainly temporary. The freeze of social benefit rates, including pensions (0.18% of GDP), will be extended to 2014. The government plans to reduce the number of public sector employees by 1% (0.1% of GDP). Public sector wages in 2014 are not indexed (0.18% of GDP), performance bonuses are not paid, workload bonuses are reduced and promotions in position grades and payment brackets are frozen[11]. Pension expenditure growth will decelerate, after the moderate increase in the number of new old-age pensioners recorded in 2013.

The estimate of the budgetary impact of consolidation measures as provided by the authorities seems plausible on current information and is as such included in the Commission Forecast.

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

Box 2. Council recommendations addressed to Slovenia

On 21 June 2013, the Council recommended Slovenia under Art. 126(7) of the Treaty to correct its excessive deficit by 2015. To this end, Slovenia should (i) put an end to the present excessive deficit situation by 2015; reach a headline general government deficit target of 4.9% of GDP in 2013 (3.7% of GDP without 1.2% of GDP one-off expenditure to recapitalise the two largest banks as estimated in June 2013), 3.3% of GDP in 2014 and 2.5% of GDP in 2015, which is consistent with an annual improvement of the structural balance of 0.7% of GDP in 2013, 0.5% of GDP in 2014 and 0.5% of GDP in 2015, in order to bring the headline general government deficit below the 3% GDP threshold by 2015, based on the Commission updated 2013 Spring Forecast; (iii) rigorously implement the measures already adopted to increase mainly indirect tax revenue and reduce the public sector wage bill and social transfers, while standing ready to complement them with additional measures if their yield would prove less than foreseen or if any measure is repealed by the justice system; and specify, adopt and implement new structural consolidation measures, on top of those already

[11] Nonetheless, the government has agreed to pay to public sector employees promoted in 2011 higher wages from 2014 onwards, but with no compensation for the period 2011 to 2013.

included in the Commission updated 2013 Spring Forecast that are necessary to achieve the correction of the excessive deficit by 2015.

On 9 July 2013, the Council also addressed recommendations to Slovenia in the context of the European Semester. In particular, in the area of public finances the Council recommended to Slovenia for the year 2013 and beyond to implement and reinforce the budgetary strategy, supported by sufficiently specified structural measures, to ensure the correction of the excessive deficit by 2015 in a sustainable manner and the improvement of the structural balance specified in the Council recommendation under the EDP. After the correction of the excessive deficit, Slovenia is recommended pursuing a structural adjustment effort that will enable it to reach the MTO by 2017. Durable correction of the fiscal imbalances requires from Slovenia the implementation of ambitious structural reforms, which would increase the adjustment capacity of the economy and boost potential growth and employment. Moreover, Slovenia is advised to safeguard growth-friendly spending, adopt measures to improve tax compliance and implement measures on the expenditure side underpinned by systematic reviews of public expenditure at all government levels. To improve the credibility of consolidation, Slovenia is expected to complete the adoption of a general government budget balance/surplus rule in structural terms, make the medium-term budgetary framework binding, encompassing and transparent, and strengthen the role of independent bodies monitoring fiscal policy by end 2013. It is recommended to take measures to gradually reduce the contingent liabilities of the state. Slovenia was also recommended to strengthen the long-term sustainability of the pension system beyond 2020 by further adjusting all relevant parameters, including through linking the statutory retirement age to gains in life expectancy, while preserving the adequacy of pensions. Finally, Slovenia was suggested containing age-related expenditure on long-term care and improve access to services by refocusing care provision from institutional to home care, sharpening targeting and means-testing of benefits, and reinforcing prevention to reduce disability/dependency.

4.1. Compliance with EDP recommendations

In light of the general government deficit projected for 2013 in the Commission Forecast, at 5.8% of GDP, Slovenia is seen to miss the headline deficit target for 2013 of 4.9% of GDP as recommended by the Council in June. Moreover, according to the Commission Forecast, the structural improvement is estimated at -0.1% of GDP. When adjusted for the downward revision in potential output growth[12] since the time when the revised EDP recommendation was issued and the impact of the composition of economic growth and employment on revenue[13], the annual corrected structural effort (0.6% of GDP) comes slightly short of the recommended annual structural effort (0.7% of GDP). Based on a bottom-up assessment, which estimates the size of the additional fiscal effort on the basis of the discretionary revenue measures and the expenditure developments under the control of the government between the baseline scenario underpinning the Council Decision and the Commission Autumn Forecast, the overall fiscal effort for 2013 adopted after the June 2013 EDP recommendation amounts to around 1.1% of GDP (see Section 3.3. for a quantitative assessment of the key measures). This is just above 1% of GDP of additional consolidation measures mentioned in the June 2013 EDP recommendation as consistent with reaching the structural target for 2013.

[12] Potential growth is estimated significantly lower than in the revised EDP recommendation first and foremost due to deteriorated labour market projections and the recent revision of data on average hours worked per employee by the Statistical Office of Slovenia.

[13] A larger-than-projected fall in social contributions from negative employment and average nominal wage growth projections and a lower projection of direct taxes and revenue from sales of market output are crucial to explain unexpected revenue shortfalls.

For 2014, the Commission Forecast projects the headline deficit at 7.1% of GDP, which is well above the recommended headline deficit target at 3.3% of GDP. At the time the revised EDP recommendation was issued, no bank recapitalisations in 2014 were foreseen relative to their current estimate at 3.4% of GDP. The annual corrected structural effort is estimated at around 0.6% of GDP in 2014, which is slightly above the recommended adjustment (0.5% of GDP). A bottom-up analysis assesses the size of individual consolidation measures for 2014 adopted after the June 2013 EDP recommendation at around 1.4% of GDP (see Section 3.3. for quantitative assessment of key measures), which is only slightly short of the 1½% of GDP of additional consolidation measures mentioned in June 2013 EDP recommendation as consistent with reaching the structural target for 2014.

Under the usual no-policy change assumption, the general government deficit for 2015 would stand at 3.8% of GDP according to the Commission Forecast. The corrected structural effort is estimated at -0.1% of GDP which falls markedly short of the recommended effort and thus indicates the need for additional structural consolidation measures for 2015 to underpin a credible and sustainable correction of the excessive deficit.

4.2. Other considerations

The authorities have recently approved several measures aimed at strengthening tax compliance. In particular, measures for stricter monitoring of and limitations on cash transactions, prevention of undeclared work and employment, improved cooperation and clearer competences of inspection bodies, control of construction activities and prevention of illegal construction as well as measures for closer supervision of economic sectors subject to fraud risks and for building public awareness on tax compliance have been adopted. While these steps appear to go in the right direction, a full assessment towards compliance with the July Council recommendation issued under the European Semester on fiscal consolidation appears premature. Gaps in the implementation of this recommendation are indicated by a lack of structural expenditure measures[14] and likely delayed full transposition of the TSCG. The former could be defined by conducting systematic reviews of public expenditure at all government levels.

5. ANALYSIS OF THE ECONOMIC PARTNERSHIP PROGRAMME

Slovenia submitted the economic partnership programme, including two annexes (Description of measures and their quantitative impact, Estimate of quantitative impact of key measures) on 1 October 2013. Its scope goes beyond fiscally relevant reforms. The economic partnership programme is a combination of backward and forward looking measures, highlighting progress made and next envisaged steps towards the implementation of all Council recommendations issued under the European Semester. However, recently launched or forthcoming reforms are described in rather general terms.

The economic partnership programme includes a set of fiscal structural reforms that is partially adequate to support an effective and lasting correction of the excessive deficit. Reforms of the tax system and fiscal framework stand out as most advanced. At the same time, work on possible further adaptations of the pension system reform has only just started

[14] The 2013 Stability Programme announced a cut in unemployment allowances and new structural expenditure side consolidation measures to avoid the possible crisis personal income tax. None of such measures have been approved. By contrast, at the expiry of current, temporary expenditure measures high expenditure growth could reappear.

and information on envisaged concrete measures and timelines in this field is not available. More progress can be detected in the preparation of the long-term care reform.

Over the last months, Slovenia has stepped up the pace of non-fiscal structural reforms relevant for the adjustment of macroeconomic imbalances. However, the majority of key reforms recommended in the Council recommendations and/or described in the economic partnership programme remain in preparation or implementation. In the labour market area, a thorough monitoring of the impact of the March 2013 reform, which will constitute a basis for further legal modifications, is underway, with first results expected in March 2014. Revisions to the minimum wage act and student work as well as several other active labour market policy measures are under consideration, but no structural reform as such is planned yet. Implementation of measures to stabilise the banking sector is on-going, notably a thorough Asset Quality Review and Stress Tests covering almost 70% of the banking sector are being conducted and due to be completed before end-2013. Such an assessment is expected to be followed by a comprehensive strategy of restructuring, consolidation and recapitalisation of the banking sector, which would also include plans for disinvestment of direct and indirect public sector participations in domestic banks. The latter would significantly reduce risks for reappearance of contingent liabilities in coming years. The reform of the Slovenia Sovereign Holding Law currently discussed, if well designed and thoroughly implemented, including swift progress with the privatisation of certain SOEs, could on the one hand, generate revenues and reduce contingent liabilities of the general government and, on the other hand, contribute to an improved and more efficient strategic management of state owned assets in particular regarding the possibilities to attract foreign investors. As regards the regulated professions, revision of entry conditions for some of them is being considered by the Slovenian authorities, but the process is behind schedule. As to the judiciary system, improvements in case management appear to have had a positive effect on its efficiency. In the area of corporate restructuring, the general concept of the proposed changes to the insolvency code, including new provisions for out-of-court restructuring, appears appropriate, but a draft consolidated text of relevant legislation is still needed for a full assessment.

6. SUMMARY

The headline deficit targets presented in the Draft Budgetary Plan for 2013 and 2014 are above the headline deficit targets recommended in June under the EDP. This is also due to different assumptions regarding the bank recapitalisation needs, especially for 2014. The corrected structural effort, however, comes only slightly short of the required structural effort in 2013, while it is slightly above in 2014. A bottom-up analysis which estimates the size of the fiscal effort for 2013 and 2014 on the basis of the additional discretionary revenue measures and the expenditure developments under the control of the government[15] between the EDP baseline scenario and the Commission Forecast shows that Slovenia has taken additional measures for 2013 adding up to around 1.1% of GDP. This is just above the amount of measures deemed necessary to reach the structural targets spelled out in the EDP recommendation. For 2014 the additional measures taken, adding up to around 1.4% of GDP, fall slightly short of the 1½% mentioned in the EDP recommendation. These estimates are on current information consistent with amounts from individual specified and quantified measures included in the Draft Budgetary Plan. In addition, Slovenia has partly addressed the other elements of the fiscal Council recommendation issued in July under the European Semester.

[15] Excluding notably unemployment benefit payments related to the evolution of the number of unemployed and changes in interest expenditure related to interest and exchange rate changes.

Annex. EDP related tables

Table A1. Baseline scenario underlying the EDP recommendation

% of GDP	2012	2013	2014	2015
Revenues	45.0	45.0	44.2	43.9
Current revenues	44.6	44.3	43.5	43.1
Discretionary measures with impact on current revenue[1]	0.1	0.5	0.0	0.0
Expenditure	49.0	50.5	49.1	49.4
Real GDP growth (%)	-2.3	-2.0	-0.1	1.3
Nominal GDP growth (%)	-2.0	-0.6	1.0	3.1
Potential GDP growth (%)	-1.1	-1.1	-0.7	-0.2
Structural balance	-2.7	-2.6	-3.4	-4.7
General government balance	-4.0	-5.5	-4.9	-5.5
p.m CAB methodology revenue elasticity	0.9	0.9	0.9	0.9
p.m Apparent revenue elasticity	0.6	4.0	-0.9	0.8
p.m Output gap (% of potential output)	-2.7	-3.6	-3.1	-1.9

Note:
[1] Measures clearly specified and committed to by governments ahead of the recommendation
Source: Commission staff working document accompanying the June 2013 EDP recommendation to Slovenia

Table A2. EDP scenario underlying the EDP recommendation

% of GDP	2012	2013	2014	2015
Real GDP growth (%)	-2.3	-2.2	-1.2	0.3
Potential GDP growth (%)	-1.3	-1.4	-1.0	-0.5
Structural balance	-2.8	-2.1	-1.6	-1.1
General government balance	-4.0	-4.9	-3.3	-2.5
p.m Output gap (% of pot. output)	-2.5	-3.3	-3.5	-2.8

Source: Commission staff working document accompanying the June 2013 EDP recommendation to Slovenia

Table A3. Current estimates of the macroeconomic and fiscal developments

% of GDP	2012	2013	2014	2015
Revenues	44.2	44.3	45.0	44.6
Current revenues	44.1	44.2	44.5	44.2
Discretionary measures with impact on current revenue[1]	0.1	1.2	0.9	0.3
Expenditure	48.1	50.1	52.0	48.4
Real GDP growth (%)	-2.5	-2.7	-1.0	0.7
Nominal GDP growth (%)	-2.3	-1.0	0.1	1.6
Potential GDP growth (%)	-1.0	-1.9	-0.9	-0.5
Structural balance	-2.7	-2.9	-2.1	-2.8
General government balance	-3.8	-5.8	-7.1	-3.8
p.m CAB methodology revenue elasticity	0.9	0.9	0.9	0.9
p.m Apparent revenue elasticity	0.5	3.4	-9.9	0.1
p.m Output gap (% of potential output)	-2.3	-3.1	-3.2	-2.0

Note:
[1] Measures clearly specified and committed to by governments ahead of the recommendation
Source: Commission autumn 2013 forecast

Table A4. Adjustment of apparent structural effort for the revision in potential growth – details of calculation

	Potential GDP growth underlying the Council Recommendation (%)	Potential GDP growth at the time of assessment (%)	Forecast error (%)	Structural expenditure (% of potential GDP)	Correction coefficient α (% of nominal potential GDP)
	(1)	(2)	(3)=(1)-(2)	(4)	(5)=(3)*(4)/100
2013	-0.1	0.4	-1.0	15.6	-0.4
2014	0.1	0.3	0.1	15.4	-0.2
2015	0.1	0.1	1.6	15.6	-0.2

Table A5. Adjustment of apparent structural effort for the unexpected revenue windfalls/ shortfalls – details of calculation

	Change in current revenues (yoy) (€ billions)		Discretionary current revenue measures (€ billions)		Nominal GDP growth assumptions (%)		Current revenues in year t-1 (€ billions)		Revenue gap (€ billions)*	Correction coefficient β (% of nominal potential GDP)
	2013 EDP	2013 AF	2013 EDP	2013 AF	2013 EDP	2013 AF	2013 EDP	2013 AF	(5)=[(1')-(2')-ε*(3')*(4')]-[(1)-(2)-ε*(3)*(4)]	
	(1)	(1')	(2)	(2')	(3)	(3')	(4)	(4')		
2010	0.4	0.5	0.0	0.0	0.1	0.2	14.9	14.9	0.1	0.2
2011	0.3	0.3	0.0	0.0	1.6	1.9	15.3	15.4	-0.1	-0.2
2012	-0.2	-0.2	0.0	0.0	-2.0	-2.3	15.6	15.7	0.0	0.1
2013	-0.2	-0.1	0.2	0.4	-0.6	-1.0	15.5	15.6	-0.1	-0.3
2014	-0.1	0.1	0.0	0.3	1.0	0.1	15.3	15.4	0.1	0.2
2015	0.4	0.1	0.0	0.1	3.1	1.6	15.1	15.6	-0.1	-0.3

Note: * Revenue elasticity ε=0.907551194672111