Draft Budgetary Plan of the Slovak Republic for 2017

October 2016

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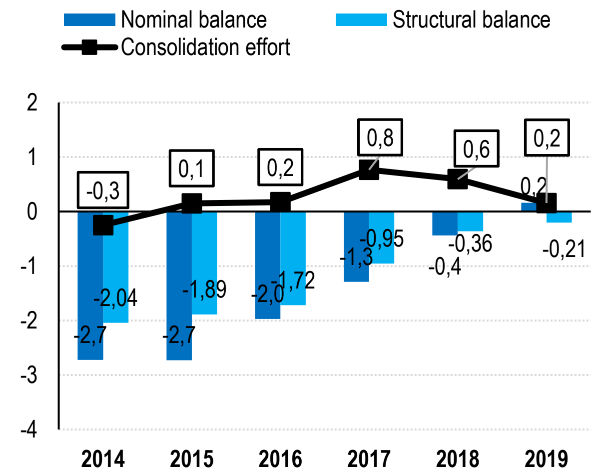
Summary

In the following year, the Slovak economy is expected to grow by 3.5 per cent, despite facing negative risks associated with UK's 'leave' vote on the European economy. Even in the case of their materialisation, Brexit is expected to affect Slovak exports and investments only moderately and its total impact on GDP in 2017 is estimated at 0.2 p. p. Thus, **we expect the economic growth to be driven mainly by domestic demand**. A solid growth in household consumption will stem from dynamic wage growth and favourable developments in the labour market. After prices have been following a downward drift for the last three years, inflation will return back to the positive territory. In the medium term, the economy will further accelerate and growth is expected to exceed 4 per cent by the end of the forecast horizon. Risks to the macroeconomic forecast are balanced.

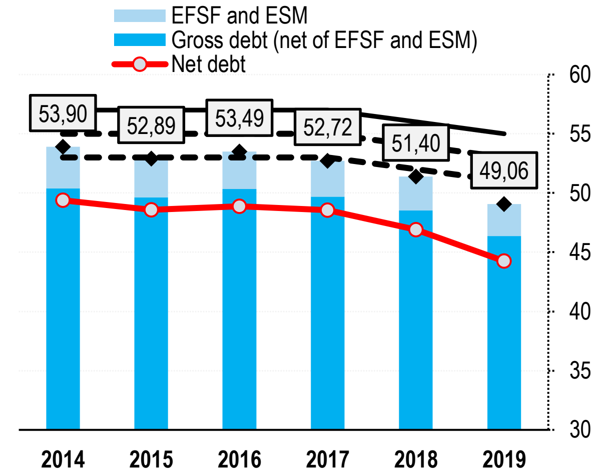
The ongoing monitoring implies that general government deficit will stand at 1.97 per cent this year, a level in line with the objectives set out for 2016. This ensures an adequate route to structurally balanced general government balance, while fully respecting the government expenditure priorities. The submitted Draft Budget Plan continues the already taken road and confirms the nominal objectives for general government deficit for the period 2017-2019 as defined by the Stability Programme.

FIGURE 1: Structural balance (per cent of GDP)



Source: MF SR

FIGURE 2: Gross debt of the general government (per cent of GDP)



Source: MF SR

According to the latest estimate, general government gross debt is expected to reach 53.5 per cent of GDP in 2017. **For the first time in the history, general government is expected to end up with a primary surplus in 2017. Afterwards, the primary balance is expected to improve** and together with accelerating inflation and solid GDP growth will contribute to a significant reduction in the debt-to-GDP ratio, which is expected to reach 49 per cent in 2019.

The Government's medium-term budgetary strategy continues to fully comply with both, national and European fiscal rules. The structural deficit which stood at 1.72 per cent of GDP in 2016, ensured year-on-year consolidation in the amount of 0.17 per cent of GDP. In terms of consolidation efforts which are subject to evaluation over a one-year horizon, the disclosed amount shows a moderate deviation. However, full compliance is ensured when the evaluation is based on a two-year horizon. Updates of the cyclical component and one-off factors with a fixed nominal goal in 2017 correspond to structural consolidation efforts equal to 0.77 per cent of GDP. **Thus, a sufficient buffer is maintained for achieving the required year-on-year consolidation at 0.5 per cent of GDP.**

A moderate growth in general government expenditures recorded in 2016 and as compared to the potential of the economy, makes it possible to target expenditures in 2016 with only a minor deviation from the expenditure benchmark over a two-year horizon. In 2017, expenditures will grow in line with the expenditure benchmark, which is estimated at 1.3 per cent of GDP in 2017. **In the following years, the planned development of expenditures over one-year and two-year horizons will meet the expenditure benchmark with a sufficient reserve, a thus is expected to contribute to reaching and/or maintaining the MTO level.**

The government has prepared a set of structural measures aiming at fostering economic growth and employment in order to address major challenges faced by the Slovak economy: the labour market, elementary education and healthcare. The assessments of public expenditures efficiency and combating tax frauds continue. As regards to the education sector, the government is focused, in particular, on increasing the attractiveness of teaching jobs and linking the vocational education and apprenticeship (dual education), development of new kindergartens and supporting the integration of marginalised communities. Capacities will be increased in childcare for children aged below three years. The positive development in the labour market will be further supported by the employment services reform and reallocation of active labour market policy tools. In healthcare, the government will focus itself on improving the efficiency of expenditures for consumption of pharmaceuticals and operating costs of hospitals.

Combating tax frauds continues to be a top priority for the Government. The primary efforts reflected in the three-phase action plan of combating tax frauds helped to reverse the long-lasting adverse development in collection of income taxes. Similarly positive is the development on **effective corporate tax rate, which keeps growing at a historical pace.** The budget assumes a **stable development** in the proportion of tax income and the GDP.

The "Value for Money" project is another instrument established by the Government in the budgeting process to improve effectiveness of public expenditures. The first results were obtained from the revision of expenses for healthcare, transportation and informatization, equalling to approximately 8.6 per cent of GDP. In healthcare, the revision identified potential measures, a part of which was reflected in the budget for 2017. In transportation and informatization, the revision identified potential savings and defined the process of evaluation for large investment projects with the Ministry of Finance playing a more active role. In 2017, a revision is scheduled with the focus on the labour market and the social system, regional schools and universities and the environment. The expenditures in these budgeting areas cover 15 per cent of GDP. The revision will primarily be focused on increasing the value of public expenditure.

The current draft budgetary plan is based on the general government budget proposal for 2017 to 2019 over the medium term horizon. Moreover, it is prepared under the requirements introduced through Regulation (EU) No 473/2013 of the European Parliament and of the Council on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area (part of the so-called Two Pack), approved in May 2013**.**

The aim of the Regulation is to improve the coordination of fiscal and structural policies while taking into account the rules of the Stability and Growth Pact and the Europe 2020 strategy. The submission of the draft budgetary plan, which presents the developments of fiscal position, the forecast of the economy and a description of budgetary policy measures to achieve the defined medium-term objectives, is a specific monitoring instrument. The presented data will enable, apart from other things, a more detailed assessment of the development in public finances in the upcoming year, which are based on the current general government budget proposal as opposed to the Stability Programme. The European Commission will subsequently publish its opinion on the budgetary plan. If a serious breach of the Stability and Growth Pact is identified, the Commission may request that the concerned Member State redrafts its budgetary plan.

The content and the format of the document are fully based on the European Commission guidelines. Similarly to the Stability Programme, draft budgetary plans are prepared on the basis of documents specifying the minimum requirements for draft budgetary plans – updated Specifications on the implementation of the Two Pack and Guidelines on the format and content of draft budgetary plans, economic partnership programmes and debt issuance reports.

I. Macroeconomic assumptions underlying the draft budget

In the following year, the Slovak economy is expected to grow by 3.5 per cent, despite facing the negative risk stemming from Brexit on the European economy. Even if the risk materialises, Brexit is expected to affect Slovak exports and investments only marginally with its total impact on GDP at around 0.2 p. p. in 2017. Thus, we expect economic growth to be driven mainly by domestic demand. A solid growth in household consumption is underlain by dynamic wage growth and favourable developments in the labour market. After prices have been following a downward drift for the last three years, inflation will return back to positive figures. In the medium term, the economy will further accelerate and growth is expected to exceed 4 per cent by the end of the forecast horizon. Risks to the macroeconomic forecast are balanced.

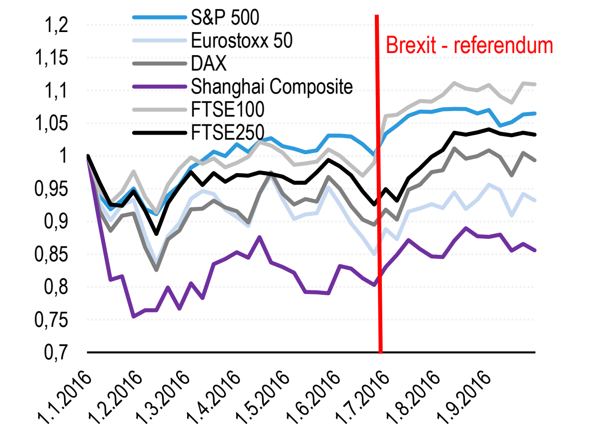
I.1. External assumptions underlying the forecast

Despite several challenges, the global economy continued to grow at a moderate pace. While economic performance in the euro area and the US was solid, the Japanese economy fell behind expectations. Developing countries experienced a recovery: higher oil prices spurred the rebound in Russia and Brazil, while growth in China stabilised.

Central banks' decisions diverge. The **Fed has indicated a possible interest rate hike at the end of the year**, after the rate has been kept on hold since the end of last year. The expected hike is supported by a robust labour market, while inflation keeps wavering well below the policy target. On the other hand, the **ECB has opted for a"wait-and-see" mode for the time being**. Even though ECB's QE programme, after several adjustments, has not yet brought the expected price growth, no significant steps will probably be taken by the year-end. **Bank of England has adopted stabilization measures.** It reacted to the results of the UK referendum by lowering the deposit rate by 25 bp to 0.25 per cent and by expansion of the asset purchase scheme.

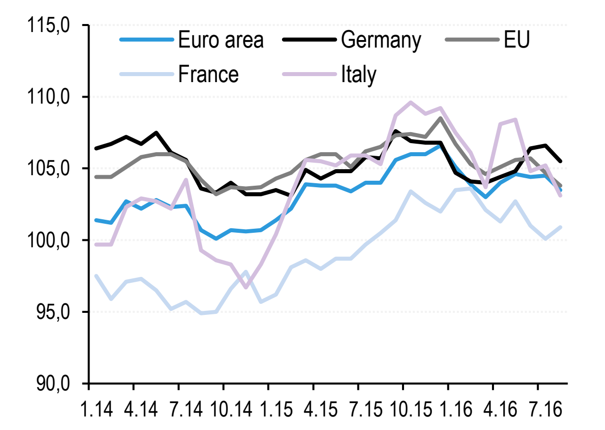
European markets largely recovered from the Brexit vote, although its future consequences remain uncertain. Weak economic growth recorded in Europe alongside increased geopolitical uncertainty resulted in stagnation of equity markets and the fall in government bond yields of major European economies. The British Pound reached 1.33 GBP/USD, which should supportUK-based companies in generating profits overseas. The average price of oil settled just below 50 USD per barrel. The commodity index encouraged growth in agricultural commodities, gold and iron ore prices.

FIGURE 3: Development of commodity markets after Brexit



Source: Bloomberg

FIGURE 4: Development of trust indicators in euro area countries



Source: Eurostat, EK

Growth in euro area slowed down in the second quarter in line with expectations. Foreign trade has significantly contributed to growth, while domestic consumption and investment have slowed down. Among large economies, Germany and Spain confirmed strong growth momentum. On the other hand, stagnation in France and Italy was rather disappointing. The impact of Brexit on economic indicators has not been observed yet. The euro area still faces low inflation and weak productivity growth.

Growth in V4 countries was among the fastest in the EU. Hungary and Poland returned to growth after a drop in 1Q and the Czech economy accelerated. This confirmed the assumption that the regional slowdown in the first quarter was only temporary and the solid growth will continue throughout the year.

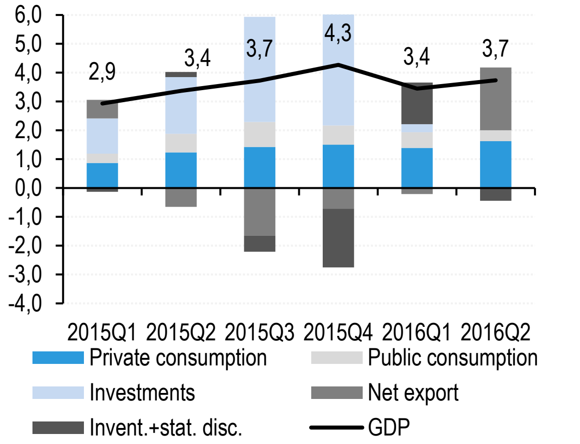
Falling leading indicators suggest a slowdown of growth in the euro area. Growth in both, the euro area and Germany will hardly exceed 1.5 per cent this year. **The euro area economy is expected to grow at around 1.6 per cent in 2016.** V3 countries will experience a slight correction from last year's EU-funds-driven growth in 2016, but this will be compensated by growth stemming from their fundaments. Moreover, Brexit will decelerate the expected growth of Slovakia's major business partners in 2017. The UK 'leave'vote will adversely affect the core of the euro area, which is expected to grow at about 1.5 per cent in 2017.

I.2. Macroeconomic forecast

Growth of the Slovak economy in the second quarter exceeded expectations. The quarter-on quarter growth rate accelerated to 0.9 per cent, and was driven predominantly by foreign demand. Positive developments in industrial production, supported by the automotive industry, metals and machinery production, were reflected in a robust growth of exports. Slovak households benefitted from positive labour market developments and the ongoing decline in prices. Consumer spending accelerated to fastest levels seen since the crisis, both, in quarter-on-quarter and year-on-year terms. Investments partly recovered from the decline seen in the first quarter. The fall in public investments was owing to slower absorption of EU funds and to the onset of the new programming period. However, the decline in government expenditures is compensated by investments in the private sector. **Since the solid quarterly growth is expected to stay the course, the Slovak economy will grow at 3.6 per cent this year on the back of household consumption and net exports.**

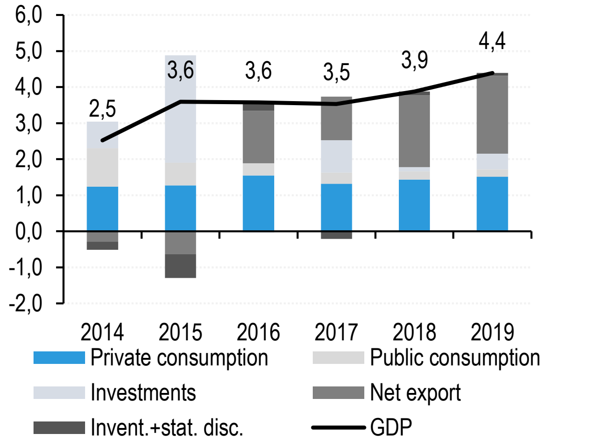
Despite **Brexit, the economy will grow at a dynamic 3.5 per cent over the course of next year.** Growth will be driven mainly by domestic demand. Investment activity will accelerate significantly as a result of the continuing construction of JLR and VW car plants as well as D4/R7. Household spending rate will slightly decelerate, in line with mildly lower growth rates in real wages and employment. Brexit will dampen the growth of the European economy, as well as Slovak exports and investments. Overall, we estimate that Brexit will reduce the growth of the Slovak economy by 0.2 p. p. in 2017. In the following years, the growth rate of the economy will gradually accelerate towards 4.4 per cent in 2019, driven by both domestic and foreign demand.

FIGURE 5: Contributions to GDP growth (quarterly, p.p.)



Source: MF SR

FIGURE 6: Contributions to GDP growth – forecast (p.p.)

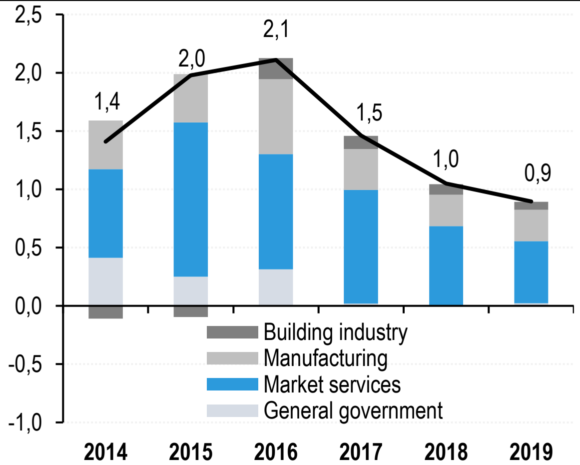


Source: MF SR

In 2017, employment will continue to grow rapidly. Whilst the pace of employment growth will level off slightly, it will nonetheless post 1.5 per cent corresponding to about 34,000 new jobs. Jobs will be created across all sectors of the economy, with an emphasis on market services. Owing to the favourable employment developments, the unemployment rate will fall to a new historical minimum at 8.5 per cent. We expect a moderate slowdown in the labour market dynamics thereafter with an annual unemployment growth at around 1.0 per cent.

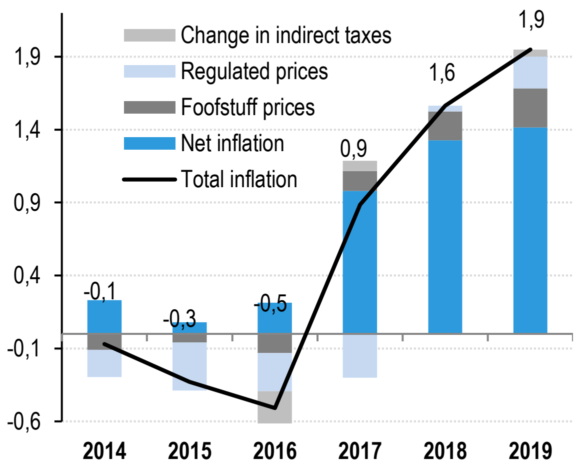
Nominal wages will accelerate to 3.5 per cent year-on-year in 2017. Real wage growth will continue to outpace that of labour productivity. In terms of sectors, wages will grow most rapidly in the public sector, construction and industry, while wage growth in market services will be again subdued. In the upcoming years, nominal wages are expected to stretch above 4 per cent in line with improvements in labour productivity and with the return to ordinary price developments.

FIGURE 7: Contribution of sectors to employment growth (p.p.)



Source: MF SR

FIGURE 8: Contributions to inflation (p.p.)



Source: MF SR

We expect inflation to return to the 0.9 per cent rate next year. Energy prices will be falling further, while the acceleration in price growth will be driven mostly by net inflation, as well as – to a smaller extent – the growth in prices of marketable goods, market services, and later foodstuff prices. A major growth stimulus, both, for Slovakia and for the euro area, will be the culminating impact of the ECB's QE measures. In the following years, we anticipate a gradual acceleration of inflation. The fastest growth is expected for prices of services. Foodstuff prices will grow slowly over the whole forecasted horizon, as we believe that the positive development on global markets is mostly structural. Inflation is expected to reach the ECB inflation target by the end of 2019.

Risks to the macroeconomic forecast are broadly balanced. Heightened geopolitical tensions possibly premature interest rate hike in the USA with a negative impact on the US labour market; and the instability of the banking sector in Italy and Portugal constitute downside risks to the forecast coming from the external environment. **Positive risks** stem from delayed, but stronger impact of QE on the domestic demand in the euro area, as well as from **postponed Brexit decision and its weaker-than-expected impact on the economy of the euro area and the UK**. In the domestic environment, the decrease of extraordinarily high household savings and potential acceleration of household consumption pose further upside risks to the forecast.. The overheated labour market may bring additional pressure on wage growth in the private sector.

BOX 1 – Estimate of the output gap for 2016 and 2017

The Slovak negative output gap should stand at around 0.9 per cent in 2016 and remain at that level throughout 2017, according to the Ministry of Finance's projections using the European Commission (EC) methodology. In line with that, the economy will continue being under-heated (i.e. below its potential). However, using the national methodology of the Ministry of Finance, the output gap in 2016 will nearly close (-0.1 per cent), and will become positive in 2017 (0.4 per cent of potential output).

The aim of the presented output gap forecast is to methodologically approximate the estimates of the EC, according to which the budgetary structural position will be assessed. Against this backdrop, the Ministry of Finance has deployed the uniform EC methodology in producing the output gap estimates. The macroeconomic data from 2016 on come from the September projections round of the Ministry of Finance. The aim is to estimate the output gap using the uniform EC methodology but based on the latest Ministry of Finance's forecast.

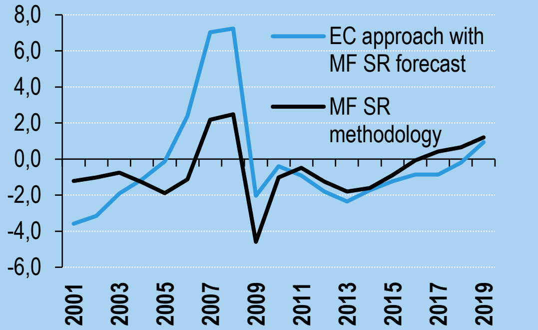
The EC methodology is a two-step process. First, the trend unemployment rate – consistent with the stable wage growth in the economy (i.e. NAWRU) – and the trend total factor productivity (i.e. trend TFP) is estimated and forecasted. To this end, the EC developed and applied a **publicly available GAP programme**, which, using a Phillips curve and a Kalman filter, extracts the trend and the cyclical components from the unemployment rate and TFP. Since the actual parameterization of the model is not yet available, the Ministry of Finance used NAWRU and trend TFP from EC's Spring forecast. In the second step, the trend components of NAWRU and TFP are estimated and subsequently used as inputs for the forecast of the output gap in the CONV routine. The output gap model in CONV routine relies on the production function decomposition using the contributions or labour, capital and TFP.

The national potential output and output gap estimates of the Ministry of Finance are methodologically different from those produced by the EC methodology. The Ministry publishes its estimates following regular Macroeconomic Forecasting Committees. In line with the Ministry of Finance's methodology, the output gap will stand at -0.1 per cent of GDP in 2016, and at 0.4 per cent of GDP in 2017 when it will close. The economy in so doing enters a period of mild over-heating.

The two methodologies are different at almost all levels of computations, although the basic method is the same. Both institutions estimate potential output using the Cobb-Douglas production function approach. **The most significant difference relates to the historical data underlying TFP**. The Ministry of Finance increases the potential output in 2005 through 2008 in order for it to correspond with the structural changes in the economy, which the EC methodology fails to capture. In the aforementioned period the Slovak Republic experienced a significant supply-side shock resulting from the adoption of structural reforms. The comparatively much higher output gap resulting from the EC methodology has not been confirmed by other imbalance indicators, including net inflation, balance of payments and unit labor costs.

The dynamic growth in the real estate market constitutes an exception to some extent. In the post-crisis period the divergences in the estimates resulting from these two methodologies eased. Nonetheless, they seem to re-appear, especially at the forecast horizon as the national methodology anticipates over-heating beginning 2017. **EC methodology envisages the output gap to close two years later, in 2019**. In this way, the estimates will align more closely towards the end of medium term.

FIGURE 9: Development of output gap (per cent pot. GDP) – EC approach and methodology of MF SR



Source: MF SR

TABLE 1: Output gap and contribution of factors to potential product growth – EC approach

	Output gap (per cent pot. HDP)	Pot. GDP (growth, per cent)	TFP*	Capital stock	Labour
2011	-0.9	3.4	**1.9**	**0.8**	**0.6**
2012	-1.8	2.4	**1.9**	**0.2**	**0.4**
2013	-2.4	2.0	**1.9**	**0.0**	**0.1**
2014	-1.7	1.9	**1.8**	**0.0**	**0.0**
2015	-1.2	3.1	**1.9**	**0.5**	**0.6**
2016F	-0.9	3.2	**2.1**	**0.4**	**0.7**
2017F	-0.9	3.5	**2.2**	**0.5**	**0.7**
2018F	-0.2	3.2	**2.4**	**0.5**	**0.3**
2019F	0.9	3.2	**2.5**	**0.5**	**0.2**

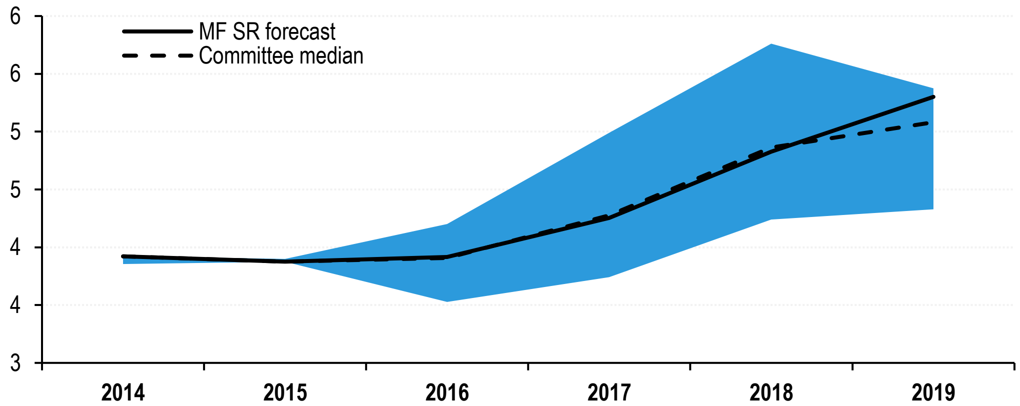
*Total productivity of factors *Source: MF SR*

I.3. Forecast assessment by the Macroeconomic and Tax Revenue Forecasting Committees

The medium-term **forecast was evaluated as realistic by all members of the Macroeconomic Forecasts Committee** (NBS, ČSOB, Infostat, SLSP, Tatrabanka, Unicredit, VÚB and Sberbank).

Considering the effects on budgetary revenues in 2017, the forecast prepared by the Ministry of Finance is almost identical with the median calculated by members of the Committee. The effect is expressed as a weighted average of individual relevant bases for budgetary revenues, where weights are given by the share of individual taxes in the total budgetary revenues[1].

FIGURE 10: Macroeconomic bases forecasts comparison[1] for budgetary revenues with Committee members



Source: MF SR

The updated tax revenue forecast prepared by the Ministry of Finance of the Slovak Republic and included in the budget proposal is a follow-up to the macroeconomic forecast which was **evaluated by all members** of the Tax Revenue Forecasting Committee (KRRZ, NBS, Infostat, SISP, ČSOB, UniCreditBank, and Tatrabanka) as **realistic**.

[1] Macroeconomic bases for budgetary revenues (the weight of indicators depends on the share of individual taxes in the total tax and social contribution revenues); Wage base (employment + nominal wage) – 51.1 per cent, Nominal private consumption – 25.7 per cent, Real private consumption – 6.6 per cent, Nominal GDP growth – 9.9 per cent, Real GDP growth – 6.7 per cent.

The Macroeconomic Forecasting Committee (MFC) and the Tax Revenue Forecasting Committee (TRFC) were established under the constitutional Fiscal Responsibility Act (Act No. 493/2011) as advisory bodies to the Minister of Finance. The role of the committees is to attain greater transparency, objectiveness and quality of macroeconomic and tax revenue forecasts. Both committees prepare their forecasts at least twice a year, by 15 February and 30 June of the current fiscal year. In exceptional cases, the committees may be convoked either by the committee chairman, Minister of Finance or by a simple majority of the committee members.

In addition to the Ministry of Finance officials, the committees consist of representatives of institutions independent from the government (NBS, Slovak Academy of Sciences, Infostat, and private banks). Members of the Macroeconomic Forecasting Committee assess the Ministry of Finance's macroeconomic forecast using the terms *conservative, optimistic* or *realistic*. The Ministry of Finance's tax revenue forecast is assessed by members of the Tax Revenue Forecasting Committee by submitting their own forecasts; their assessment is calculated automatically, based on a deviation between the two. A Ministry of Finance's forecast is accepted as committee forecast if a simple majority of members grade the forecast as conservative or realistic. In the absence of such grading, the Ministry of Finance of the Slovak Republic is required to redraft its forecast and submit it to the Committee for re-assessment. The procedure is repeated until the Ministry of Finance's forecast is accepted as the Committee's forecast.

Budgetary objectives

The primary objective of the fiscal policy of the Slovak Republic is to ensure effective and sustainable public finance that enables permanent improvement in the quality of life. Based on the ongoing monitoring of the developments in public finance, the general government deficit for the current year will reach 1.97 per cent. The draft budget for 2017 expects the deficit at 1.29 per cent of GDP. This ensures an adequate route to structurally balanced general government balance, while fully respecting the government expenditure priorities. Additionally, in 2017, for the first time in the history of Slovakia the economy is expected to reach a surplus budget adjusted for debt financing costs. In the medium-term horizon, the ongoing consolidation and solid economic growth should create room for reduction of the public debt. According to the latest forecast, the public debt should gradually decline to the level of 49 per cent of GDP in 2019.

The improved tax income for 2015, confirmed by the Tax Revenue Forecasting Committee[2], reduced the deficit to 2.73 per cent of GDP[3]. Based on the Eurostat spring notification, the general government deficit reached 2.97 per cent of GDP. The year-on-year consolidation efforts for 2015 will reach 0.15 per cent of GDP[4]. Stability Programme for 2016 to 2019, on the other hand, assumed a year-on-year impairment of the structural balance by 0.25 per cent of GDP. **The submitted data for the autumn notification expect the gross general government debt at 52, 9 per cent of GDP**[5].

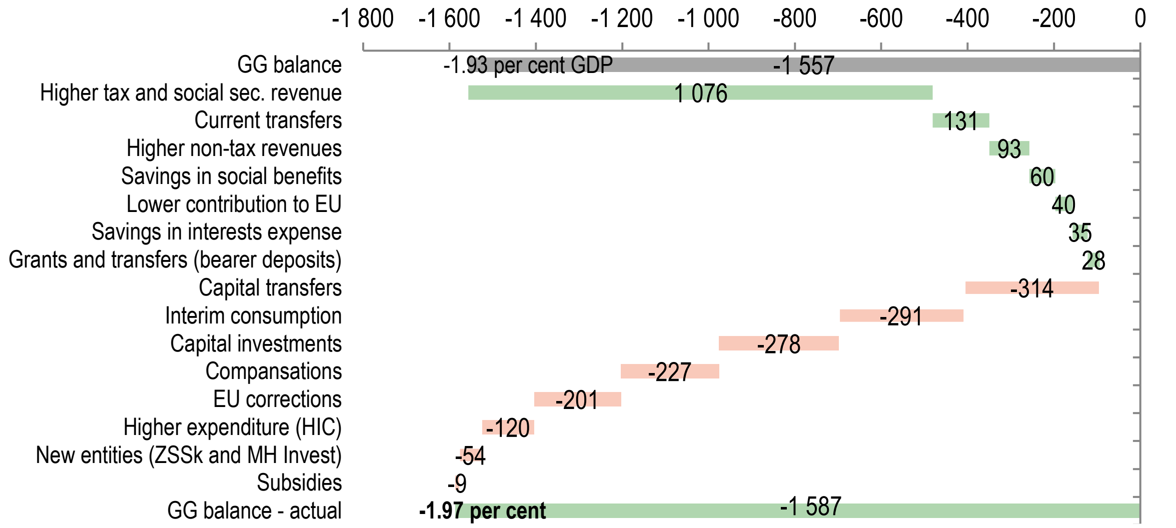
I.4. Recent development in public finance

The monitoring of the general government economy in 2016 is based on the latest macroeconomic and tax forecast of September 2016 and the expected development in other revenue and expenditure components of the general government budget. These data have been also used in the general government budget for 2017 to 2019.

[2] Tax Revenue Forecasting Committee – Forecast of Taxes and Social Security Contributions for 2016 - 2019 (September 2016)
[3] The reduction in the deficit will be confirmed by the autumn notification, the disclosed value does not reflect the GDP revision due to redeployment of entities (BOX 6).
[4] On contrary, the Stability Programme for 2016 - 2019 assumed a year-on-year impairment of the structural balance by 0.25 per cent of the GDP.
[5] The achieved debt level refers to the first sanction threshold under the Constitutional Act on budgeting responsibility.

The actual general government deficit in 2016 is currently at 1.97 per cent of GDP[6], approximately meeting the adopted objective[7].

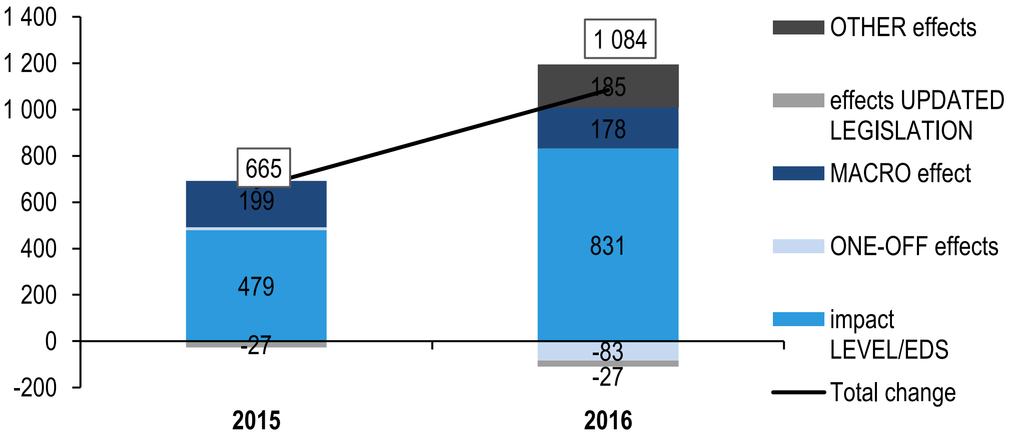
Figure 11: Analytical breakdown of the general government balance in 2016 (ESA 2010), mil. EUR



Source: MF SR, Eurostat

Based on the latest data from the macroeconomic and tax forecasts, the tax and social security contributions for 2016 have been significantly increased by EUR 1 076 million(1.3 per cent of GDP) as compared by the approved budget (excluding the effect of reserves). Compared to the budget, already containing a reserve for a better tax collection, the general government tax revenues were higher by EUR 760 million (0.9 per cent of GDP). The 2016 improvement of tax revenues estimate was influenced, in particular, by the ongoing success in tax collection and a positive development of tax bases (Figure 12). Besides the tax base effect, an optimistic development of majority of the revenues has been identified on a year-on-year basis.

Figure 12: Contributions to change of the forecast compared to budget for 2015 - 2016 (EKRK classification[8], EUR mil.)



Source: MF SR, Committee

[6] General government budget for years 2016 - 2018 did not include ZSSK and MH Invest companies, which were, in the meantime, reclassified by Eurostat to general government sector. For both companies, the present monitoring assumes a moderate contribution to higher deficit (ZSSK -0.03 per centGDP and MH Invest -0.04 per cent GDP).

[7] General government budget 2016 assumed target deficit in the amount of 1.93 per cent GDP.

[8] Contributions to the change in forecast made by the Committee compared to the Committee's forecast in the budget, 2015 and 2016 – Disclosed is the difference between the tax forecast prepared by the Committee. It does not include the difference in non-tax revenues under economic classification of budgetary classification (EKRK), not included in the Committee's forecast which, however, are taxable revenues under ESA2010 methodology.

Tax revenues of the state budget are higher by approximately EUR 620 million compared to the official forecast of the Tax Revenue Committee. The positive driver stems from the better results of corporate tax collection, value added tax (VAT), excise duties and a special levy on gambling games. The ongoing growth of the corporate tax income (net of legislative changes) since 2014, significantly exceeding the growth of the economy and the historical elasticity development, proves the positive impact of the improved VAT collection overlap with the amount of the recognised corporate tax[9].
The positive development of the labour market increases revenues of local government and social and health insurance. Higher income from social security contributions (EUR 238 mil.) and savings in social benefits (EUR 22 mil.)[10] allows to reduce the transfer from the state to the Social Insurance Company (EUR 270 mil.). Pursuant to the ongoing monitoring, and thanks to the retained balances from previous years, the higher income from health insurance payments received from economically active population (EUR 92 mil.) will be used to cover the growing public health insurance expenses (EUR 120 mil.). The tax revenues collected by local government (municipalities and higher territorial units) which were higher by EUR 133 mil., including the received transfer from the state in the amount of around EUR 25 mil. will be used by the local government in proportion 1:2 for higher compensation for employees and purchase of goods and services.

TABLE 2: Tax and social security contribution revenues of the general government in 2016 - difference against the budget and the Committee forecast - (ESA2010)

	Comparison vs the October forecast (Committee)		Comparison vs budget	
	EUR mil.	**per cent of GDP**	**EUR mil.**	**per cent of GDP**
1. Tax revenues	754	0.9	439	0.5
- Personal income tax	98	0.1	98	0.1
- Corporate income tax	394	0.5	394	0.5
- Value added tax	156	0.2	-110	-0.1
- Excise duty	56	0.1	6	0.0
2. Revenues from contributions	330	0.4	330	0.4
- Public health insurance – EAO	92	0.1	92	0.1
- Social insurance company - EAO	238	0.3	238	0.3
Total (1+2)	**1 084**	**1.3**	**768**	**1.0**

Source: MF SR

On the revenue side, the budget for 2016 tied a portion of the revenues for the case of not meeting the goal of higher tax collection as reflected in higher tax revenues. The reserves were primarily allocated to current expenditure items in intermediate government consumption and capital expenditures for the implementation of priority investment projects. The savings in current transfers (EUR 131 mil.) refers only to release of a number of expenditure items not allocated in the budget.

The increase in non-tax revenues (EUR 93 mil.) which included mainly fees and payments for non-industrial or random sale and services, was comprised of amounts collected from activities of public universities (EUR 30 mil.), state treasury dividends from MH manažment a.s. (EUR 18 mil.), public health insurance companies, the Railways of the Slovak Republic and a higher income from toll stickers (EUR 4 mil.).

[9] The underlying assumption is that prevention of decreasing VAT liability through fictitious invoices or multiple claiming of input VAT invoices for legally operating companies, automatically lead to lower amount of recognised costs, higher company profits and higher CIT. On the other hand, in case of reduction of unrecorded transactions (sale without bills and invoices) result in higher sales with unchanged costs.
[10] Total savings in social benefits, including payments on behalf of persons insured with contribution from the state equal EUR 60 mil., as the EUR 37 mil. are just the lower payments for social and health insurance made by the state on behalf of the insured persons.

Other positive factors include savings in lower interest expense on the state debt (EUR 35 mil.), lower contributions to the EU (EUR 40 mil.) and higher grants and transfers (EUR 28 mil.), attributable to revenues from balances on bearer deposits balances.

Capital transfers accounts for largest negative impact EUR 514 mil. This item, *inter alia*, reflects the effects of corrections to EU funds, which, based on preliminary audit results, are estimated at EUR 201 mil. The remaining portion includes higher capital transfers outside the general government sector. This includes transfer from the state treasury to ZSSK and MH Invest, which have been analytically adjusted as they were not a part of the budget and transfers from the state budget including expenditures related to the transfer of funds to common resolution fund.

During the year drawings for current expenses for intermediate government consumption were higher by EUR 290 mil. [11], mainly due to higher purchases of goods and services for other general government entities, specifically municipalities and higher territorial units, universities, organizations receiving contributions from the state budget and healthcare facilities.

Compensations for employees, including higher salaries for teachers (EUR 75 mil., universities without the original competences are also included), growth of other employees' wages in general government (EUR 110 mil.), end local government employees (EUR 28 mil.), were, in the aggregate, higher by EUR 227 mil.

In 2016, the expected development in capital investments exceeded the budgeted amount by EUR 278 mil. The increase in government capital investments referred mainly to implementation of the government's investing priorities. Major contributions resulted from activities of the National Highway Company, where additional expenditures, for purchase of land, in the amount of EUR 220 mil are assumed. The Emergency Oil Stocks Agency (EOSA) experienced higher expenditures by EUR 15 mil. due to financing of oil products material reserves.

Other negative contributions to the deficit (EUR 54 mil.) and higher subsidies (EUR 9 mil.) resulted from the inclusion of new entities (MH Invest and ZSSK).

I.5. Structural balance and expenditure benchmark

Monitoring of the government's fiscal policy is based on analytical indicators that clarify the fiscal stance of the country. Both of them provide analytically precise results comparing the official headline balance of general government. **Below presented indicators play a key role in the assessment of compliance within the preventive part of the Stability and Growth Pact[12].**

Structural balance is the main indicator representing the headline balance of the general government adjusted for economic cycle effects and one-off and temporary budgetary effects. The medium-term budgetary objective of the Slovakia is set to reach a structurally balanced budget, defined by structural deficit of 0.5 per cent of GDP[13]. The analysis of the structural balance is focused on year-on-year changes specifying the **consolidation effort**. In line with the existing methodology, strength of fiscal consolidation is used to assess the pace towards the medium-term budgetary objective (MTO).

The second indicator is the expenditure benchmark, assessing the year-on-year growth of the general government expenditures. The expenditure benchmark brings the fiscal control mechanism by defining the growth

[11] Including expenditures to support the milk sector in the amount of EUR 30 mil.
[12] Vade mecum on the Stability and Growth Pact – 2016 edition, European Economy. Institutional Paper. 021. March 2016.
[13] The budget goal is defined in Act No. 523/2004 on Budget Rules of the Public Service.

of the expenditures controlled by the government. The expenditure growth should not exceed the potential economic growth unless the overrun is explained by additional revenue measures. The key principle of both the structural balance and the expenditure benchmark is to ensure the country aims for the adopted medium-term budgetary objective (MTO). In order to ensure this direction, in line with the Stability and Growth Pact, the "windfall revenues" shall be used for reduction of the deficit and debt, while keeping the sustainable development on the expenditure side of the budget.

Assessment of the two indicators monitors the deviation from the required value. The deviations are tested on a one-year and two-year horizon having a higher importance due to lower volatility and a better predictability. In case of structural balance, the deviation from the required consolidation effort is the key element. As for the expenditure benchmark, the final message comes from the difference between the actual expenditures and the expenditures determined by the expenditure benchmark.

I.5.1. Structural balance

The first step of the structural balance calculation assumes the adjustment of the headline balance for the effects of economic cycle (boom or recession) on general government balance. In line with the existing methodology the economic cycle effects are known as a cyclical component. The Ministry of Finance fully transposes the EC's estimate of the general government balance sensitivity to the output gap change, based on the OECD methodology[14]. In the following step such a balance is further adjusted for one-off and temporary measures. For the purpose of drafting the budget plan, assessed by the EC, the Ministry of Finance tracks one-off effects based on EC methodology (Annex 1)[15], to ensure the ex-ante compliance with EC's assessment.

The purpose of the analytical adjustments is to determine the value of the structural balance, which explains the general government budget balance under the assumption that the economy performs at its potential level, excluding one-off and temporary budgetary measures. Structural balance compliance with European fiscal rules is the starting point of the fiscal policy targets in the Slovak Republic.

TABLE 3: Consolidation effort in EC methodology (ESA 2010, per cent of GDP)

	2014	2015	2016 OS	2017	2018	2019
1. Net lending / borrowing	**-2.72[1]**	**-2.73[1]**	**-1.97**	**-1.29**	**-0.44**	**0.16**
2. Cyclical component	-0.7	-0.5	-0.3	-0.3	-0.1	0.4
3. One-off effects	0.0	-0.4	0.1	0.0	0.0	0.0
4. Structural balance (1-2-3)	**-2.04**	**-1.89**	**-1.72**	**-0.95**	**-0.36**	**-0.21**
5. Consolidation effort (year-on-year change 4)	**-0.25**	**0.15**	**0.17**	**0.77**	**0.59**	**0.16**
- investment clause – co-financing from EU funds	-0.38					
Consolidation effort adjusted for investment clause	0.15					
Deviation over one-year horizon	0.13	0.15	-0.08	0.27	0.09	0.16

[14] The original methodology was presented in Girouard, N., André, Ch. (2005): Measuring cyclically-adjusted budget balances for OECD countries. The process of updating methodology and including new data for calculating elasticity took place in 2014. The methodology was adopted by Member States in September 2014.

[15] Vade Mecum on the Stability and Growth Pact – 2016 Edition – Guiding principles str.28. In the past, MF SR prepared a manual, in accordance with the existing EC methodology, specifying detailed rules for identification of one-off and temporary effects in the national methodology.

Deviation over two-year horizon		**0.14**	**0.03**	**0.09**	**0.18**	**0.12**
p.m. required consolidation effort [2]	*-0.38*	*0.00*	*0.25*	*0.50*	*0.50*	*0.00[2]*
p.m. Net lending/borrowing - spring notification	*-2.69*	*-2.97*				

[1] On the basis of data sent to the Eurostat within autumn EDP notification *Source: MF SR*
[2] In 2019 no consolidation is required, provided that the MTO is met.

BOX 2 – Treatment of EU corrections to EU funds as a one-off effect

EC defines the one-off effect as a **temporary measure without a permanent nature that is independent of governmental decisions.** EC applies 5 principles (Annex 1) in the process of identifying and classifying one-off measures.

Furthermore, EC separately classifies specific cases, which may be classified as a one-off measure although they do not meet the 5 fundamental principles. These include variations in revenues or expenditures resulting from judicial or institutional decisions. Such cases include corrections for EU funds resulting from irregularities in drawings of European structural and investment funds.

EC methodology permits treating EU corrections as one-off corrections in case of identification of a considerably above-average correction, which usually arise at the end of the Programming Period due to extensive drawings from the remaining portions of EU funds (this also applies to the context of SR). To be treated as one-off measures, corrections **have to meet the following criteria:**

1. Corrections should be clearly attributable to a specific event. In the context of EU corrections for the SR, it means the 2007 – 2013 Programming Period, with a prolonged availability for drawing by 2015. In years 2014 and 2015 high corrections were recorded, which was caused by an intensive drawings of remaining portions of EU funds.
2. Corrections should clearly exceed the average level of corrections caused by normal fluctuation.
3. Corrections should relate to incorrect drawings accumulated over the horizon of several years.
4. If the EU Corrections meet the aforementioned characteristics can occur maximally for two consecutive years.

Corrections can be classified as one-off measures only if **all four requirements** are met. Due to the fourth criterion **EU corrections can no longer be classified as** one-off measures in the context of SR.

Provided that the nominal deficit reaches the expected 1.97 per cent of GDP in 2016, the structural deficit should reach the level of 1.72 per cent of GDP[16]. In 2016, the consolidation effort is expected at 0.17 per cent of GDP, which implies a mild deviation over a one-year horizon. However, over the two-year horizon, having the prominent role under the Stability Pact[17], **there is no deviation from the required consolidation effort.**

BOX 3 – Fiscal position of Slovakia

Analysis of the fiscal position is focused on quantification of dependence of changes in the structural primary balance and cyclical indicator of the output gap. The most intuitive illustration of the relationship is a graphical expression of four quadrants. This view expresses, over a longer time horizon, whether the country's fiscal policy is pro-cyclical or anti-cyclical.

The traditional approach compares the change in the structural primary balance to the current level of output gap. That approach illustrates how the fiscal policy responds to the economic cycle (the need of more consolidation in good times and of a fiscal stimulus in the case of worse economic development). A slightly different approach is based on year-on-year change in the output gap rather than the level of output gap. The key benefit of that approach is its lower sensitivity to output gap revisions, since revisions of the size of output gap are more frequent than revisions of its change. EC applies this approach to determine the required consolidation effort; in that case EC monitors the level of output gap and its year-on-year change[18].

[16] Based on EC methodology (Annex 1 and BOX 2).
[17] In 2016, the Stability and Growth Pact assumed the required consolidation for Slovakia (i.e. year-on-year change of structural balance) in the amount of 0.25 per cent GDP.
[18] For example, in case of closing the negative output gap, the required consolidation effort is higher than those for growing negative output gap.

After the moderate anti-cyclical fiscal expansion in 2015, a moderate anti-cyclical fiscal expansion is anticipated in 2016 due to faster decline in interest expense compared to the pace of structural consolidation. In 2017 a stronger shift towards fiscal restriction is forecasted, with similar level of the output gap. Since 2018, provided that the forecasted levels are reached, the economy will consolidate using a faster than potential economic growth. In 2019, similar development of the economic cycle will have an anti-cyclically neutral effect due to lower required consolidation upon reaching the medium-term budget objective.

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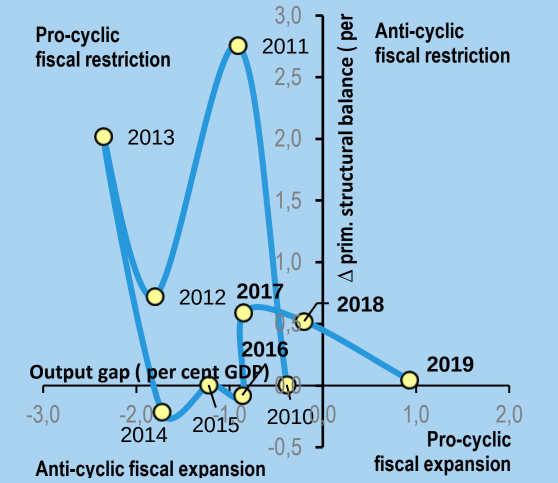
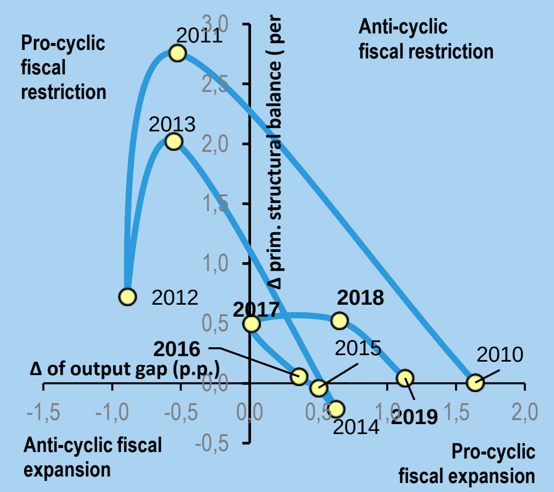
FIGURE 13: Change in primary structural balance vs output gap level (per cent of GDP)



Source: MF SR

FIGURE 14: Change in primary structural balance vs change in output gap (per cent of GDP)



Source: MF SR

If, in 2016, the expected 1.97 per cent deficit level is met, Slovakia will get close to a primary structural balanced budget (deficit of 0.2 per cent of GDP). In the following years, Slovakia should generate a primary structural surplus between 0.4 per cent of GDP and 0.9 per cent of GDP in the period between 2017 and 2019.

TABLE 4: Primary structural balance in EC methodology (per cent of GDP)

	2014	2015	2016	2017	2018	2019
Primary structural balance	-0,1	-0,1	-0,2	0,4	0,9	1,0
Output gap	-1,7	-1,2	-0,9	-0,9	-0,2	0,9

Source: MF SR

The draft budget for 2017 confirms the plan for meeting the medium-term budgetary objective introduced in the Stability Programme for 2016 - 2019[19]. Based on the Policy Statement of the Slovak Government the deadline for meeting the MTO has been postponed to 2019; in compliance with European and national fiscal regulations. The submitted Draft Budgetary Plan follows the indicated route and confirms the nominal objectives for general government balances for years 2017 - 2019 as defined in the Stability Programme.

The budget for 2017 assumes a deficit equal to 1.29 per cent, which refers to the structural consolidation effort equal to 0.77 per cent of GDP, including the update of the cyclical component. The budgetary objective for 2018 assumes the deficit equal to 0.44 per cent of GDP[20]. Along with the positive output gap, a general government balance surplus is expected in 2019 at the level of 0.16 per cent of GDP for the first time in the history

[19] Stability Programme SR for 2016 - 2019.
[20] The present assumptions underlying the calculation of the structural balance indicate meeting the MTO in 2018 (0.4 per cent GDP). The reason for early meeting the MTO under unchanged nominal target deficits, is the update of the cyclical component, which reduced the necessity of consolidation by 0.4 p.p. GDP on the horizon of years 2017 - 2019.

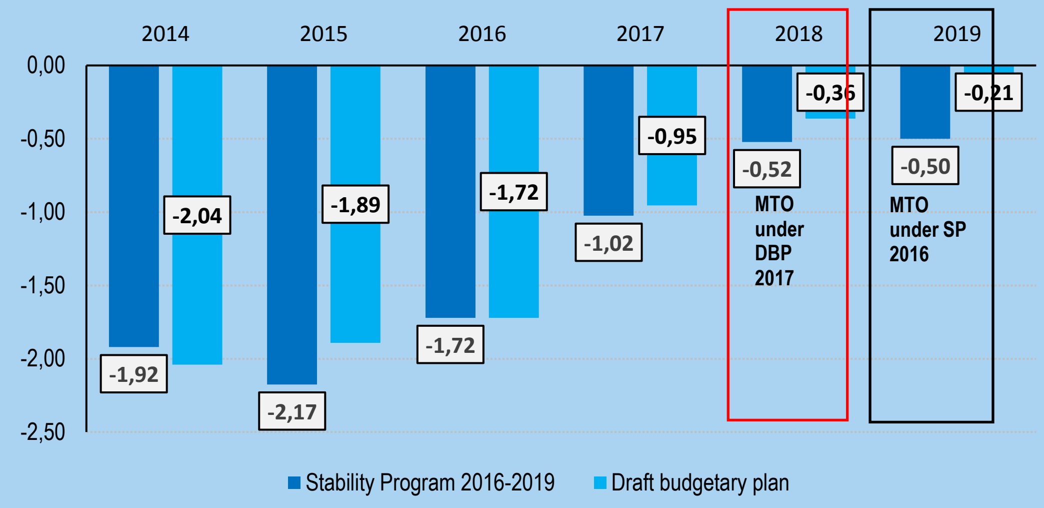
of Slovakia. Compliance with European and national fiscal regulations is preserved over the whole horizon 2017 - 2019.

BOX 4 - „Flexibility“ in meeting the medium-term budgetary objective (MTO)

In accordance with the preventive part of the Stability and Growth Pact, and in respect to the priorities defined by the Government, the deadline for meeting the MTO has been postponed. The Government declared this intention in the Stability Programme for 2016 - 2019, which introduced the updated budgetary plans aiming to achieve the MTO in 2019. The draft budgetary plan confirms the defined nominal target deficits for years 2017 - 2019, respecting the consolidation pace required under the Stability and Growth Pact until meeting the MTO[21].

With the latest estimate of the cyclic component and temporary effects for 2016, the structural deficit equals to 1.72 per cent of GDP[22]; from 2017 it will be necessary to decrease the deficit by 0.50 per cent of GDP annually until the MTO is met. In comparison with **the Stability Programme, the cyclical component has been updated. This change should, under constant nominal objectives, lead to premature meeting of the MTO in year 2018.** In this regard, an important factor is the revision of the cyclical component (due to the update of the estimated development of the economic cycle), which, in general, provides certain flexibility in defining the route towards meeting the MTO. Actual condition of the Slovak economy potential provides a sufficient reserve, so even if a reverse revision of the cycle happen, the MTO can be reached in 2019 without the necessity to change the refined budgetary objectives (Chapter 4).

FIGURE 15: Comparison of the development of the structural balance (per cent of GDP)



Source: MF SR

I.5.2. Expenditure benchmark

The updated Stability and Growth Pact introduced an expenditure benchmark as a supplementary tool to analyse the fiscal position. It shows the year-on-year growth of the expenditure aggregate net of revenue measures. This enables to assess the progress achieved in fiscal consolidation in comparison with the permitted expenditure growth reference rate, similarly to the structural balance development

According to the expenditure benchmark, the real general government expenditures should not grow faster than the average potential economic growth. The expenditures are permitted to grow faster only if additional

[21] In accordance with requirements set by European and national fiscal regulations, in the past, Slovakia elected as its MTO the level of structural deficit at 0.5 per cent GDP, which is explicitly stated in the Act on Budgetary Rules.
[22] Structural deficit for 2016 assumes achieving nominal balance at 1.97 per cent GDP.

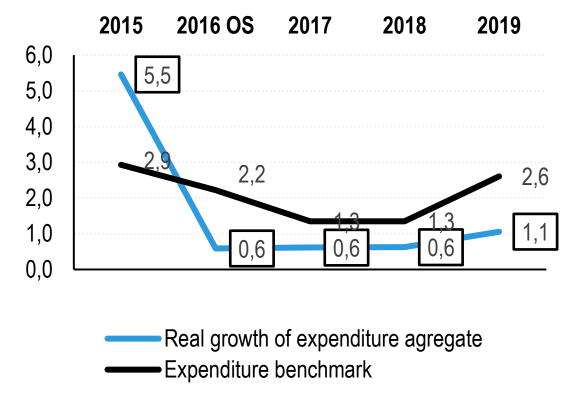
revenues measures are implemented and quantifiably confirmed by an independent Committee (this applies to discretionary measures)[23]. For countries which have already achieved their medium-term budgetary objective (MTO), the growth of expenses can be identical with the potential of the economy. For countries not yet at their MTOs, the expenditure growth rate shall reflect the fiscal consolidation necessary for achieving the MTO. In such case, the potential growth rate of the economy is adjusted for necessary consolidation effort.

The nominal growth of such adjusted expenditures is consequently translated to real growth by means of a GDP deflator, to allow referencing against the expenditure benchmark

The development of expenditures is adjusted for the factors which are beyond the Government's control. This includes interest expenditures, changes in unemployment benefit expenditures resulting from the existing business cycle and expenditures financed from the EU funds. Considering the high volatility of government investments, the amount of the investments is adjusted to average amount of investments for the current year and the prior three years[24]. The nominal growth of such adjusted expenditures is consequently translated to real growth by GDP deflator, to allow referencing against the expenditure benchmark.

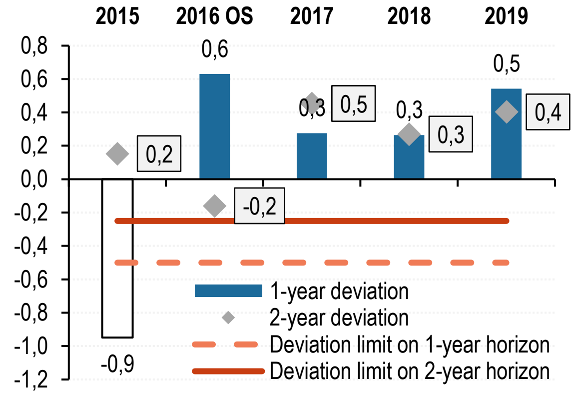
When comparing the year-on-year development of the expenditure aggregate to the expenditure benchmark, it appears that the growth rate of expenditures was exceeded in 2015 (Figure 16) which was partly due to the necessity of co-financing of strong absorption of EU funds. Compliance between the development of expenditures and the expenditure benchmark is assessed on two horizons (Figure 17), expressed as per cent of GDP. **One-year deviation (difference between the expenditure aggregate and the expenditure benchmark calculated as per cent of GDP) with a limit of -0.5 per cent of GDP and a two-year deviation (average of deviations of the current and prior year) which is given a higher priority due to lower volatility and dependence on the current year, with a limit of -0.25 per cent of GDP.** If the deviation is not in line with the pre-set limit, it is regarded as a significant incompliance with the expenditure benchmark and the overall evaluation of the fiscal position is undertaken.

FIGURE 16: Development of expenditure aggregate compared to the expenditure benchmark (growth per cent)



Source: MF SR

FIGURE 17: One-year and two-year deviation from meeting the expenditure benchmark (per cent of GDP)



Source: MF SR

In 2015, the expenditure benchmark enables a year-on-year growth of expenditures by 2.9 per cent. The expenditures, expressed as a percentage of GDP in 2015 exceeded the level specified by the expenditure

[23] Positive cyclical revenues in the time of conjuncture (not included in discretionary measures) tend to allow also growth of expenditures above the potential level. The expenditure benchmark monitors this undesired fiscal impact, as a temporary increase in revenues from unrealised measures should be used for meeting the MTO.
[24] Vade Mecum on Stability and Growth Pact, page 30.

benchmark by 0.9 per cent of GDP. Due to the much slower growth of expenditures in 2014 than was enabled by the economy, the expenditure benchmark two—year deviation is in line with pre-set requirement. In 2015, the two-year deviation is on a positive level of 0.2 per cent of GDP.

In 2016, we expect the real growth of the expenditure aggregate adjusted for the revenue measures to be on 0.6 per cent level, which is a significantly slower growth compared to the prior year. A slower growth of expenditures in 2016 (positive deviation on a one-year horizon: 0.6 per cent of GDP), compared to the potential of the economy, is desirable due to the compensation of high growth of the expenditure aggregate prior year. **This consolidation enables to target expenditures in 2016 with only a minor deviation from the expenditure benchmark on a two-year horizon (-0.2 per cent of GDP).**

In 2017, expenditures will grow in accordance with the expenditure benchmark by 1.3 per cent of GDP. In the following years, the expected development of expenditures should **meet the expenditure benchmark with a sufficient reserve on a one-year and two-year horizon** and thus contribute to reaching and/or maintenance of the MTO.

TABLE 5: Calculation of compliance with expenditure benchmark (ESA 2010)

	unit	2014	2015	2016 E	2017	2018	2019
1. Total expenditure	EUR mil.	**31 911**	**35 865**	**33 659**	**34 498**	**35 632**	**36 329**
2. Interest payments	EUR mil.	1 444	1 379	1 223	1 127	1 124	1 092
3. Expenditure covered by EU (capital)	EUR mil.	1 097	2 157	571	800	1 017	586
3a. Expenditure covered by EÚ funds (total)		1 195	2 600	1 015	1 149	1 644	1 338
4. Capital expenditures covered by national resources	EUR mil.	1 796	2 675	1 886	2 041	1 982	1 795
5. Smoothing (national funds, 4-year rolling average))	EUR mil.	1 819	2 004	2 038	2 099	2 146	1 926
6. Cyclical expenditures - unemployment benefits	EUR mil.	15	11	8	8	2	-10
7. Expenditures fully matched by automatic revenue increase	EUR mil.	0	0	0	0	0	0
8. Primary expenditure aggregate (1-2-3a-4+5-6-7)	EUR mil.	**29 281**	**31 205**	**31 566**	**32 273**	**33 026**	**34 040**
9. Year-on-year change of primary expenditure aggregate (8t-8t-1)	EUR mil.	726	1 924	361	707	753	1 014
10. Change of revenues due to discretionary revenue measures	EUR mil.	-30	109	-187	107	77	12
11. Nominal increase in the expenditure aggregate adjusted for revenue measures ((8t-9t)/7t-1)	per cent	2.6	6.2	1.8	1.9	2.1	3.0
12. Real increase in the expenditure aggregate adjusted for revenue measures	**per cent**	0.7	5.5	0.6	0.6	0.6	1.1
13. Expenditure benchmark (low reference bound)	p.p.	4.1	2.9	2.2	1.3	1.3	2.6
14. Deviation from the expenditure benchmark (13 -12)	p.p.	3.3	-2.5	1.6	0.7	0.7	1.5
15. One-year deviation from the expenditure benchmark	per cent of GDP	**1.3**	**-0.9**	**0.6**	**0.3**	**0.3**	**0.5**
16. Two-year deviation from the expenditure benchmark	per cent of GDP	**1.4**	**0.2**	**-0.2**	**0.5**	**0.3**	**0.4**
p. m. GDP deflator	*per cent*	*1.9*	*0.7*	*1.2*	*1.3*	*1.5*	*2.0*

[1] A positive value represents compliance of the expenditure benchmark

Source: MF SR

[2] Average of two EC forecasts, Macroeconomic forecast of the MF SR from 2018

I.6. General government gross debt forecast

At the end of 2015, the general government gross debt[25] reached the level of 52.9 per cent of GDP[26]. If the state budget cash deficit for 2016 and the fiscal framework for the general government budget for 2017 - 2019 will be as forecasted, the general government gross debt can be expected to gradually decrease compared to the GDP. By the end of the budget horizon, gross debt is expected to approach 49 per cent of GDP, this level lies in the first sanction category of the current year[27].

The gross debt for 2016 is estimated to be at 53.5 per cent of GDP[28]. The year-on-year increase in the gross debt can be partly explained by the necessity to ensure a sufficient level of the cash reserve to finance state liabilities in 2017. **Starting in 2017 general government balance[29] is expected to reach, for the first time in history, a primary surplus. This together with the forecasted accelerating growth of GDP, is expected to contribute to a stronger decrease of the debt.**

TABLE 6: General government gross debt (per cent of GDP, ESA 2010, as at 31.12.)

	2014 S	2015 S	2016 OS	2017 N	2018 N	2019 N
Gross debt of the general government	**53.9**	**52.9**	**53.5**	**52.7**	**51.4**	**49.1**
- Sovereign debt (net of international commitments)	48.4	47.8	48.5	48.0	47.1	45.1
- Slovakia's share in the EFSF facility debt	2.6	2.4	2.3	2.2	2.1	2.0
- Contribution to the ESM	0.9	0.8	0.8	0.8	0.7	0.7
- Debt of other general government entities	2.0	1.9	1.9	1.7	1.5	1.3
p.m. change in gross debt	-1.1	-1.0	0.6	-0.8	-1.3	-2.3
p.m. net debt	49.4	48.6	48.9	48.6	46.9	44.2
p.m. effect of revision of nominal GDP [1]	0.0	0.0	0.0	0.5	1.0	1.1
p.m. effect of revision of debt [1]	0.0	0.0	0.6	0.0	0.7	0.7

[1] Compared to Stability Programme SR for 2016 - 2019 *Source: MF SR*

The year-on-year change in the general government debt is driven mainly by the amount of the state budget[30] cash deficit, which needs to be financed through issuance of government debts and other financial instruments. In 2015, the cash deficit of the state budget reached EUR 1.9 bn. In 2016, the deficit is expected to drop significantly to EUR 1.3 bn.

The magnitude of gross debt is also influenced by Slovakia's participation in European mechanisms (EFSF and ESM) since 2012. In 2016, obligations to the EFSF and ESM increase the general government gross debt by 3.1 per cent of GDP. No additional impacts on general government debt in the period from 2017 to 2019 are expected from the Slovakia's liabilities towards aforementioned mechanisms. The Slovakia's debt is mainly influenced by EFSF obligations that arose due to the providing of financial aid to the Member States of the programme. The EFSF will no longer participate in new financial programmes, however, it will continue to manage the repayment of obligations of the debtor countries. Until then, the EFSF commitments will directly influence the amount of gross

[25] All indicated values are calculated based on the methodology applied in the assessment of compliance with the Maastricht criterion for general government gross debt, the so-called Maastricht general government gross debt. The general government debt is expressed as ratio in GDP.
[26] Based on the data sent to the autumn Eurostat notification, excl. the GDP revision effects.
[27] Pursuant to the constitutional Act No. 493/2011 Coll., on Fiscal Responsibility, in 2019, the lower limit of sanction categories will be 48 per cent of the GDP.
[28] This refers to the second sanction category under constitutional Act No. 493/2011 Coll., on Fiscal Responsibility.
[29] The primary surplus means a balance of revenues higher than the balance of expenditures, adjusted for debt service costs (interest expense).
[30] For the purposes of the debt forecast, budgetary objectives are expected to be reached on the condition of the required additional measures on the state budget side.

debt based on the Slovakia's share in the EFSF. Slovakia's contributions to the ESM reduce the disposable State Treasury funds, which are used to finance government's operations, and therefore they indirectly increase debt.

The debt calculation also considers changes in methodology[31] such as the discount at the issuance and maturity of bonds. The overall effect of both factors reduces debt in 2015 to 2017. Since the year 2018, the influence of higher issue discount is expected due to the expected rebound of interest rates.

Other changes in the debt forecast are connected with exchange rate differences and change in the deposits of State Treasury clients outside of the general government.

TABLE 7: Impact on the change of the general government gross debt (in EUR mil.)

	2014 A	2015 A	2016 E	2017 F	2018 F	2019 F
A. General government gross debt (as at 1.1.)	**40 600**	**40 725**	**41 293**	**43 089**	**44 284**	**45 502**
B. Total year-on-year change in the general government gross debt	**125**	**568**	**1 796**	**1 195**	**1 219**	**721**
- Cash-based state budget deficit	2 923	1 932	1 298	2 017	1 523	890
- State Treasury funds used for the financing of government operations	-2 377	-1 262	434	-678	-245	-159
- Slovakia's share in the EFSF facility debt	102	-116	0	0	0	0
- Slovakia's contributions to the ESM	132	0	0	0	0	0
- Issue discount	11	18	52	24	57	87
- Discount at maturity	-114	-86	-61	-61	-5	-1
- Balance of loans to general government entities	-532	25	63	-108	-113	-97
thereof: ŽSR	-1	0	0	0	0	0
thereof: ŽSSK	-9	-9	53	5	7	18
thereof: NDS	-54	-77	36	-37	-37	-37
thereof: EOSA	-520	0	0	0	0	0
thereof: municipal public transportation companies	85	33	0	-3	-8	-2
- Other	-21	58	10	1	1	0
C. General government gross debt (as at 31.12.)	**40 725**	**41 293**	**43 089**	**44 284**	**45 502**	**46 223**
in per cent of GDP	**53,9**	**52,9**	**53,5**	**52,7**	**51,4**	**49,1**
p.m. year-on-year change of general government gross debt (p.p.)	*-1,1*	*-1,0*	*0,6*	*-0,8*	*-1,3*	*-2,3*

Note: Positive amounts increase the general government debt as at 31 December of the relevant year, negative amounts decrease the debt. .

Source: MF SR

BOX 5 - Stochastic forecast of general government gross debt

An alternative approach to predicting the level of debt is a forecast carried out by means of a stochastic model[32]. The fan Figure confirms the high probability (around 70 per cent per cent) of the debt decrease over the medium-term horizon, by 2019 (Figure 18). Over the entire horizon, the official forecast of the general government debt is close to the independent alternative stochastic forecast (trajectory median). Hence, the official forecast can be considered as realistic and the risks are balanced.

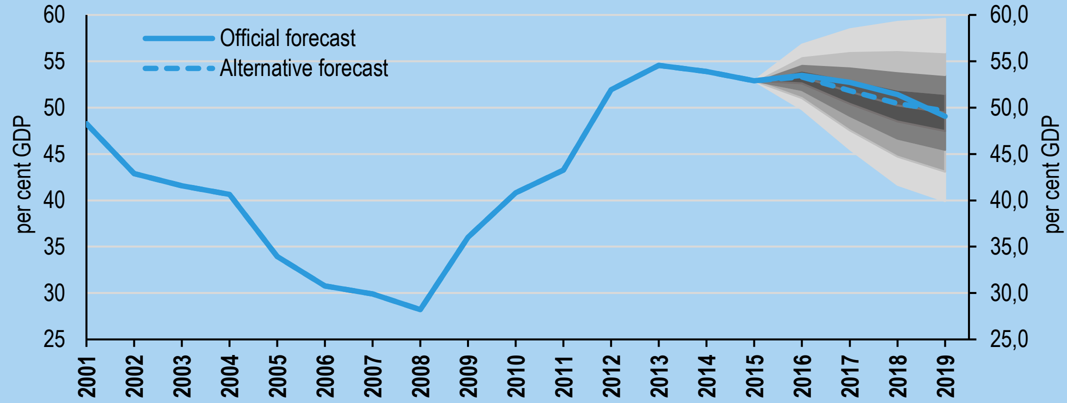
The primary advantage of the alternative approach is the lower demand on input assumptions. It provides an independent source of debt estimate as well as quantification of the forecast risks. On the other hand, this approach is limited by the fact that it only takes into account a limited amount of information and presumes that interactions among the components of the

[31] The discount on the issuance of state bonds and state treasury bills increases the debt, since in the moment of bond issue the state liabilities increase by the nominal value of the bonds. The state, however, gains a lower amount of cash (decreased by the discount). On the other hand, the discount at redemption of state bonds reduces the debt. This is due to the fact that the debt increased when the bonds were issued, namely in the nominal value of the bonds, rather than at the time of their redemption.

[32] The simulated level of debt is determined by its past value, interest expense, GDP growth, primary deficit and non-deficit financing. The model comprises a vector autoregression of interest rates, growth of real GDP, inflation of GDP deflator, of these three variables for the EU and exchange rate. Another component of fiscal response function which determines the level of primary deficit with regard to the debt and economic activities. High number of random simulations of this system of models determines various debt trajectories of which probability distribution of the level of debt in future years is subsequently calculated.

model will be the same during the forecasted period as they were in the past. The fan Figure graphically illustrates a large number[33] of randomly simulated debt levels on the horizon of the forecast generated in the stochastic model. The methodology of the estimate is provided in the Draft Budgetary Plan for 2016[34].

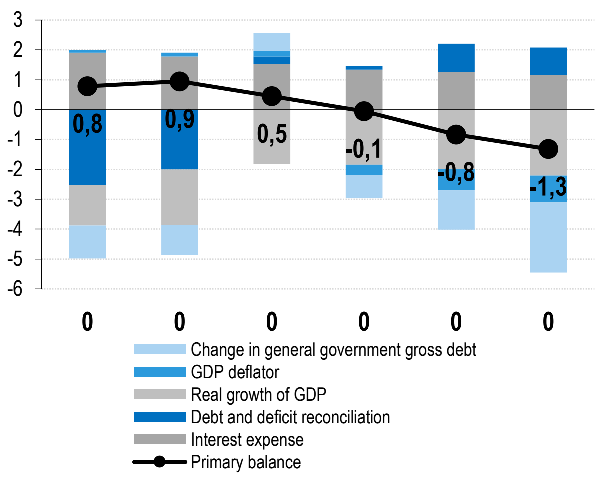
FIGURE 18: Contributions of factors to gross debt change (per cent of GDP)



Source: MF SR

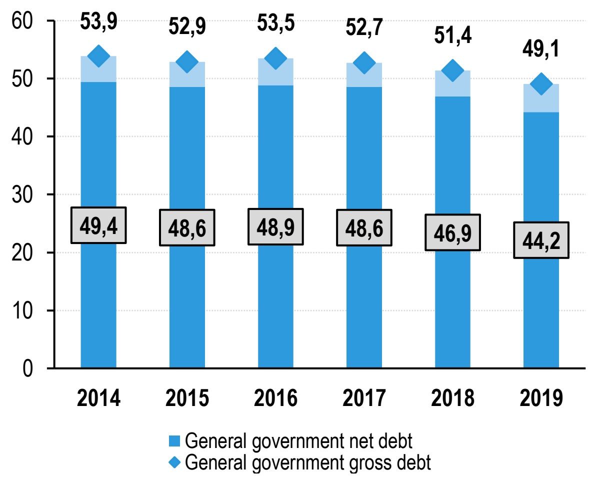
Another option to the standard statistic view of the gross debt development, is the analytical breakdown of the factors contribute to the debt level changes. Under this approach, it can be concluded that the **expected decline of debt during 2017 - 2019 is caused mainly by improvement of the primary balance [35] and by the nominal growth of GDP**. Considering the ongoing effort to meet the MTO, it is assumed that primary surplus will be generated in 2017. The accelerating growth of GDP is expected to support reduction of debt over the whole monitored horizon, with a strong acceleration at the end of the horizon. As for interest expense, which contribute to increase of the debt every year, we expect a positive decline in proportion to the GDP, from 1.5 per cent of GDP in 2016 to 1.2 per cent of GDP in 2019. In the forecasted period, the debt will also be influenced by development of the State Treasury funds and the difference between cash and accrual reporting of general government balance for the purpose of the debt and deficit reconciliation.

FIGURE 19: Contributions of factors to gross debt change (per cent of GDP)



Source: MF SR

FIGURE 20: Net debt (per cent of GDP)



Source: MF SR

[33] 5,000 random debt trajectories were simulated.
[34] http://www.finance.gov.sk/Components/CategoryDocuments/s_LoadDocument.aspx?categoryId=9307&documentId=13676.
[35] Primary balance is the general government balance net of interest expense.

Net debt is the indicator which analytically reflects the real indebtedness. The indicator is based on gross debt net of the state liquid assets, in particular, the actual level of cash and other liquid items. At the end of 2015, the net debt amounted to 48.6 per cent of GDP. Level of cash and other liquid items are expected to stay at similar levels, because of this, the net debt is expected to fluctuate, on average, by 4.5 p.p. below the gross debt level over forecasted period.

BOX 6 – Positive risk from GDP revision on fiscal indicators

For the purpose of the autumn Eurostat deficit and debt notification, the Statistic Office of the Slovak Republic (SO SR) performed the regular backward revision of national accounts. The key factor is the subjects' reclassification from the general government sector under ESA 2010 methodology. The reclassification to the general government sector refers to join-stock companies Železničná spoločnosť Slovensko (ZSSK) and Jadrova a vyraďovacia spoločnosť (JAVYS), increasing the level of nominal GDP over the whole historical time line. In terms of methodology, the change partially results from different valuation methods of added value applied to general government entities and entities outside the general government.

The revision is expected to increase the GDP in 2015 compared to the latest known actual figure by 0.8 per cent, i.e., EUR 0.6 bn. The forecast of the Committee for Macroeconomic Forecasts (Committee) for nominal GDP growths for 2016 – 2019 can be used as the basis for chaining the year-on-year changes to make time line consistent to a new level of GDP (Table 8).

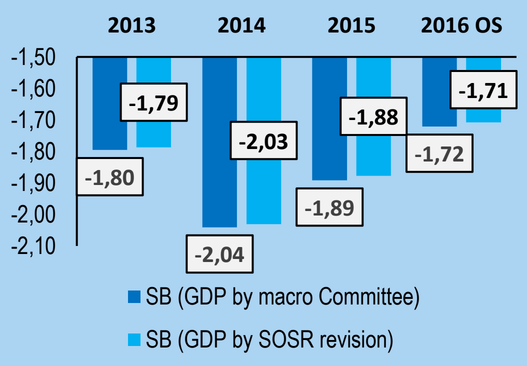
TABUĽKA 8: GDP revision (EUR bn)

	2012	2013	2014	2015	2016	2017	2018	2019
GDP Forecast - Committee, September 2016	72.4	73.8	75.6	78.1	80.5	84.0	88.5	94.2
GDP - revision ŠO SR	72.7	74.2	75.9	78.7	-	-	-	-
GDP - revision ŠO SR + Committee forecast	**72.7**	**74.2**	**75.9**	**78.7**	**81.2**	**84.7**	**89.2**	**95.0**
Difference	*0.3*	*0.3*	*0.4*	*0.6*	*0.6*	*0.7*	*0.7*	*0.7*

Source: SO SR, MF SR

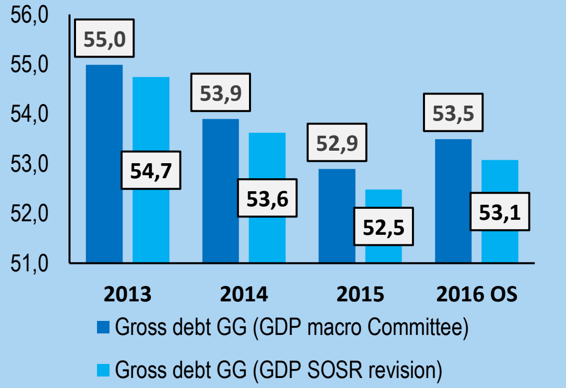
The revision influences fiscal indicators, which are expressed in proportion to GDP (nominal and/or structural balance and the general government gross debt). With respect to the budgeting process, which requires publication of new data by the SO SR and Committee approval of the nominal GDP, it was not possible to include new GDP data either in the general government draft budget or in the Draft Budgetary Plan. The impact of the revision, on the resulting fiscal indicators in years 2012 – 2016, is illustrated in charts 21 and 22. Due to proportion of the structural balance and the gross debt to GDP, the revision of GDP will result in only a moderate decrease of the structural balance, but it will cause relatively high decrease on both gross and net debt.

CHART 21: Change in structural balance (per cent of GDP)



Source: SOSR

CHART 22: Change in gross debt (per cent of GDP)



Source: SO SR

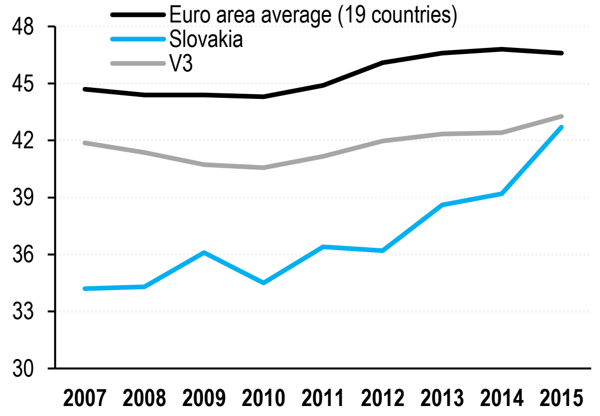
I.7. Revenue and expenditure targets of the general government budget

Assuming no changes in economic policies in 2017, the general government deficit would reach 0.29 per cent of GDP in 2017. Compared to the no-policy-change scenario, the general government deficit in the budget proposal for the year 2017 is higher by 1.00 per cent of GDP (EUR 839 million), exclusively due to the expenditure incentives on the expenditure side of the budget (1.45 per cent of GDP). The consolidation measures and the additional non-tax revenues (0.45 per cent of GDP) partly compensate the expenditure incentive. Under the no-policy-change scenario in 2018, the general government balance would approach the level of the balanced budget, and it would result in surplus of 0.55 per cent of GDP in 2019. Combating tax evasion remains the priority of the Slovak government in the area of taxes.

I.7.1. Revenue targets of the general government budget

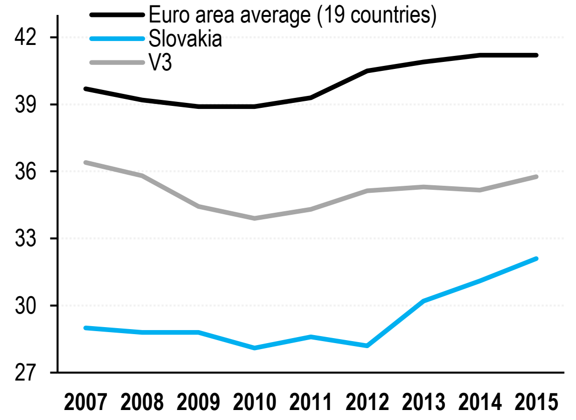
In Slovakia, the general government revenues to GDP ratio is, in the long term, below the reference values, i.e., the euro area average and the V3 average. However, thanks to the successful *combating of the tax evasion problem* and revenue consolidation, over the horizon of the last three years, general government revenues converge to both reference points (Figure 23). **Furthermore, Slovakia has, compared to the V3 average and the euro area average, still the lowest ratio of tax and social security revenues to GDP.**

FIGURE 23: Comparison of development in general government revenues (per cent of GDP)



Source: Eurostat

FIGURE 24: Comparison of development in general government tax revenues (per cent of GDP)



Source: Eurostat

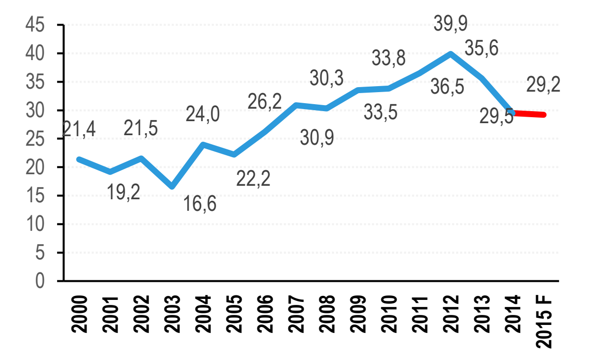
I.7.2. Combating tax evasions

Combating tax evasion **remains the key priority of the Slovak government. The primary effort was focused on VAT evasions.** The measures from the three-phase action plan adopted during 2012 - 2015 helped to reverse the long-term decreasing trend of VAT collection efficiency (Figure 25). The aforementioned fact is also confirmed by the decline in the VAT gap, which was reduced by one fourth over the years 2012 - 2015. For 2016, we estimate that the additional benefit from the improved VAT collection, resulting from implementation of the measures to combat tax evasions, equal to 1.13 per cent of GDP compared to 2012. **In recent years, the effective corporate income tax (CIT) rate keeps growing at a previously unseen pace, which, besides the pro-cyclical nature of CIT[36] can also be attributed to VAT measures having a positive impact also on revenues from CIT[37].**

[36] Development of CIT elasticity vs macro-base is procyclical. During the financial crisis (2008 - 2012) the effective tax rate was decreasing; in the following years the effective tax rate has been increasing along with the growth of the economy

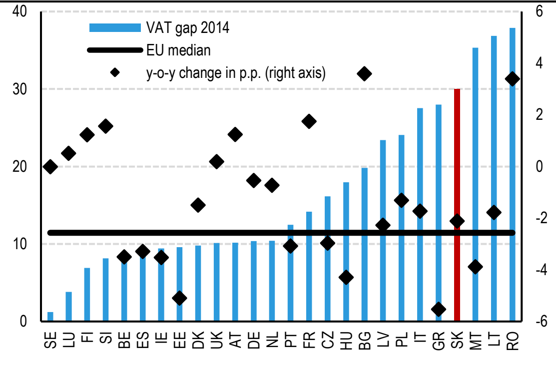
[37] Measures focused on prevention of fraudulent input VAT claims in form of duplicate or fictitious invoices and elimination of unrecorded supplies to the customer will be reflected not only in a higher VAT liability, but also in a higher profitability and, consequently, a higher CIT liability. On the other hand,

FIGURE 25: VAT gap (per cent of potential revenue)



Source: MF SR

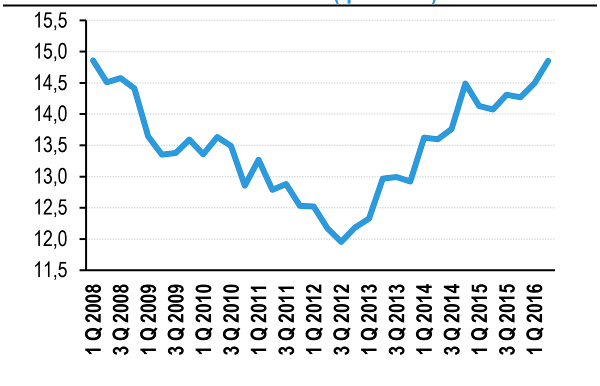
FIGURE 26: VAT gap in EU, 2014 (per centof potential revenue)



Source: MF SR

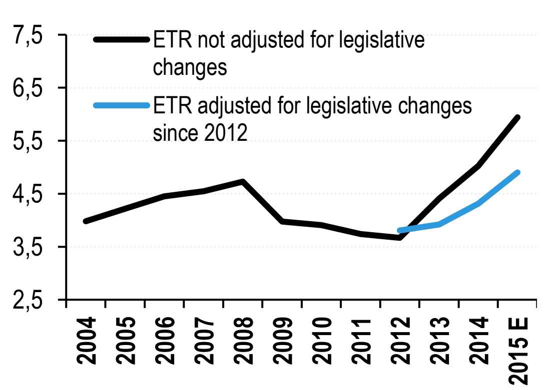
In addition to implementation of the updated action plan for combating tax frauds, further measures effective from 2017 will be adopted, aimed mostly at a more effective tax administration. There is a new regulation adopted for the concept of preliminary ruling, which is an effective instrument to ensure that taxable entities will meet their future obligations. The tax administrator will have the opportunity to respond in a more flexible way, if there is a reasonable doubt of whether the not-yet-collected tax or not-yet-assessed tax will be paid, or if there is a reason to believe that it is uncollectible. In order to avoid obstructions in tax administration by raising repeated and often groundless objections of the prejudice, the provision on raising objections is amended so that the taxable entity shall support the raised objection with a proper reasoning and shall specify against whom is the objection directed. A new concept, the "*accelerated assessment procedure*", has been established, the result of the procedure will be issuance of the assessment order. The assessment order will be issued by the tax administrator, if the tax administrator doubts correctness or validity of the filed tax return and the taxable entity does not respond to the tax administrator's request to eliminate the defects.

FIGURE 27: Effective VAT rate (per cent)



Source: MF SR

FIGURE 28: Effective CIT rate (per cent)



Source: MF SR

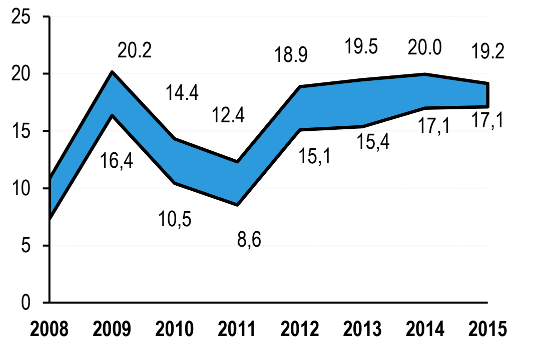
Besides VAT, the effort is also focused on excise duty. Numerous measures have been adopted in this area in order to restrict the scope for optimization of excise duty on tobacco[38], or a general abatement of tax evasions on excise duties. **The updated tax gap on excise duty on mineral oils shows signs of stabilization in recent years.** In 2015, the gap decreased moderately and the spread of the estimate ranked from 17.1 per cent to 19.2

measures focused on frauds involving VAT refunds will, most likely, have no impact on revenues from CIT, as fraudulent companies usually either do not recognise the tax or do not pay it.

[38] Tax on cigars and cigarettes, depending on weight, by contrast to number of pieces.

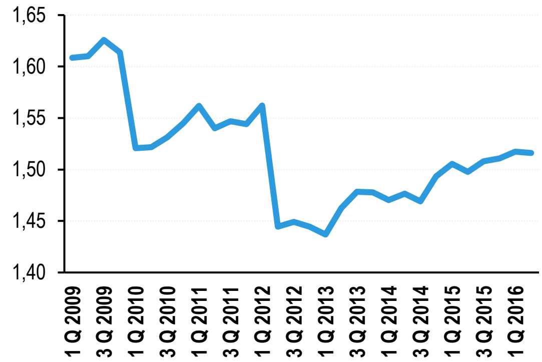
per cent of the potential yield on this tax (which equals EUR 234 - 269 mil.). Unlike VAT the gap on excise duty on mineral oils is not only comprised of evasions but also of cross-border shopping[39]. The trend in the development of the tax gap is also considerably influenced by the developments in foreign exchange rates with neighbouring countries. More relevant is the information on the development of the tax gap over time, in particular, the excise duty on diesel which is, in terms of tax evasions, easier to smuggle, and/or easier to be confused with other mineral oils.

FIGURE 29: Tax gap of excise duty on mineral oil (potential tax per cent)



Source: MF SR

FIGURE 30: Effective rate of excise duty on mineral oil (per cent)



Source: MF SR

I.7.3. General government revenues in years 2016 and 2017

In 2017 and 2018 we assume a stable proportion of the general government revenues to GDP. In 2019 a more significant decrease across all revenue categories is expected, approximately by 1.2 p.p. of GDP.

TABLE 9: General government revenues in years 2016 - 2019 (per cent of GDP , ESA2010)

	OS 2016	2017	2018	2019
Total general income revenues	**39.8**	**39.8**	**39.8**	**38.7**
1. Tax revenues	**18.6**	**18.6**	**18.5**	**18.3**
- Taxes on production and imports	10.8	10.9	10.7	10.5
- Value added tax	6.8	6.9	6.8	6.7
- Excise duties	2.7	2.7	2.6	2.6
Current taxes on income, wealth, etc.	7.8	7.7	7.8	7.8
- Corporate income tax	3.8	3.6	3.6	3.7
2. Contributions to social security	**14.3**	**14.2**	**14.1**	**14.0**
3. Non-tax revenues	**4.7**	**4.7**	**4.5**	**4.3**
4. Grants and transfers	**2.3**	**2.3**	**2.7**	**2.2**
thereof: EÚ	1.3	1.4	1.9	1.4

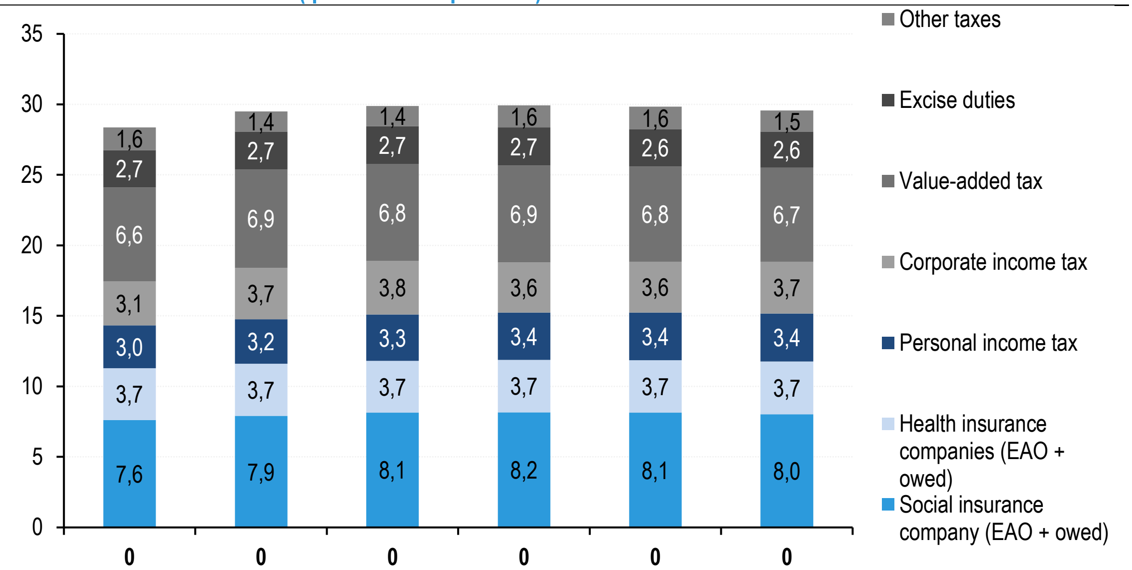
Source: MFSR

The budget assumes a **stable development** in personal income tax and health insurance contributions in proportion to GDP over the whole forecasted horizon. The decrease in the VAT to GDP ratio is caused by a slower growth rate of household consumption compared to overall growth rate of the economy. For CIT, the decrease in 2017 results from the tax rate reduction to 21 per cent. The decrease in the social security contributions to GDP ratio is caused by gradual increase of the 2nd pension pillar contributions since 2017, , the existence of maximum

[39] Presently it is not possible to quantify each factor.

assessment base and minimum amount of contribution, which, logically, do not allow for full transformation of the wage base growth in assessed base, and, consequently, to contribution revenue. **The absence of automatic indexation** of part of tax revenues (real estate tax, administrative fees, and other revenues) **causes erosion of their yield on GDP** in the remaining forecasted years. In this context, MoF prepared a tax schedule for gradual increase of excise duty on tobacco products.

FIGURE 31: Tax to GDP ratio (per centGDP per cent)

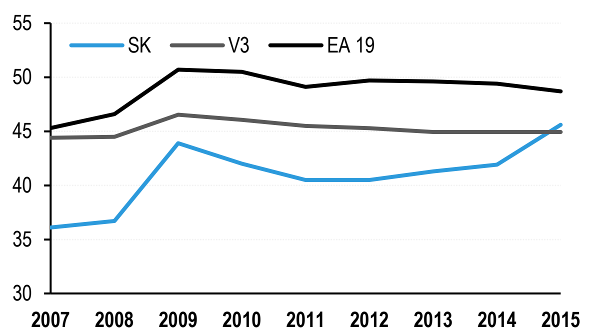


Source: MF SR

I.8. Expenditure targets of the general government budget by function [40]

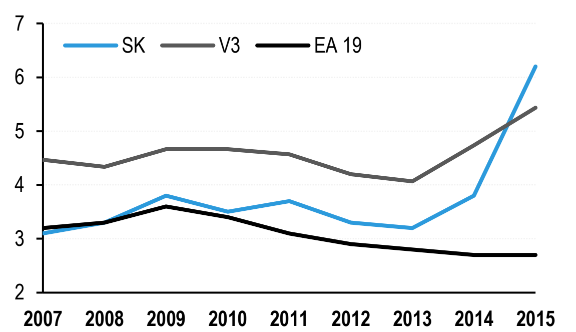
In Slovakia, the proportion of total general government expenditures to GDP was, in the long run, below reference values, i.e. the euro area average and the V3 average. On the two-year horizon, however, general government expenditures have converged to the two reference average values (Figure 32). However, Slovakia further ranks among European countries with a lower ratio of public expenditures to GDP. The accelerated drawing of EU funds in Slovakia and in V3 countries resulted in a strong increase of public capital investments in 2014 and 2015.

FIGURE 32: Comparison of development of general government expenditures (per cent of GDP)



Source: Eurostat

FIGURE 33: Comparison of development of general government capital expenditures (per cent of GDP)



Source: Eurostat

[40] Note: The methodology of recording expenditures based on functional classification can vary between countries. As a result, different data can enter into the same category in different countries (e.g. taxed and non-taxed pensions). COFOG classification also doesn't take into account expenditure realized through the tax system.

The international comparison of the structure of expenditures by function [41] versus V3 countries shows that in the examined areas, major difference is apparent in healthcare and in social security. The strong difference in these two areas is caused by the change in methodology [42] -changed accounting treatment of expenditures for healthcare services purchased by health insurance companies, which were subsequently reclassified under social security. The change was applied by Slovakia, but apparently not by all EU countries. The proportion of expenditures in GDP is higher, mainly in public order and safety compared to V3 average. On the other hand, it is lower mainly in general public services and education.

TABLE 10: General government expenditures based on COFOG

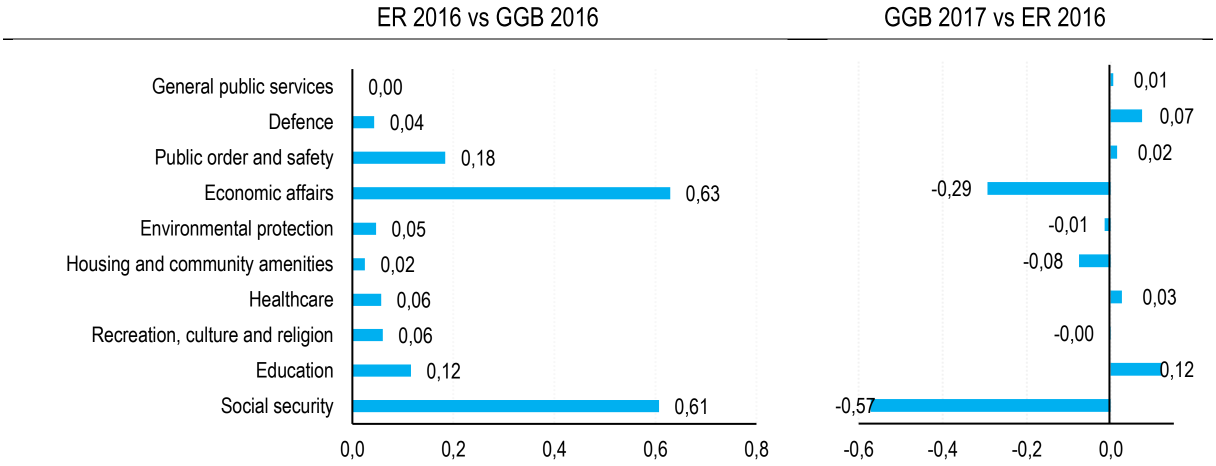
Functions	COFOG	SK 2016		SK 2017		V3 2014	
		per cent of GDP	per cent TE	per cent of GDP	per cent TE	per cent of GDP	per cent TE
1. General public services	1	5.5	13.2	5.5	13.5	6.7	14.5
2. Defence	2	1.1	2.5	1.1	2.7	0.9	2.1
3. Public order and safety	3	2.2	5.2	2.2	5.4	1.9	4.4
4. Economic affairs	4	5.2	12.4	4.9	11.9	6.0	13.4
5. Environmental protection	5	0.5	1.1	0.4	1.1	1.1	2.3
6. Housing and community amenities	6	0.5	1.3	0.5	1.1	0.8	1.9
7. Healthcare	7	1.9	4.6	1.9	4.7	5.8	13.0
8. Recreation, culture and religion	8	1.0	2.4	1.0	2.4	1.5	3.2
9. Education	9	3.9	9.3	4.0	9.8	5.2	11.7
10. Social security	10	20.0	48.0	19.5	47.4	15.0	33.5
Total expenditures	**TE**	**41.8**	**100**	**41.4**	**100**	**44.9**	**100**

Note.: TE – total general government expenditure

Based on the ongoing monitoring for 2016 public expenditure is higher by 1.8 p.p. of GDP compared to the approved budget. The increase compared to the budget has been recorded mainly in social security and in economic affairs (Figure 34 on the left). The higher social security expenditure is mainly in social benefits including pensions [43] and expenditures for healthcare services purchased by health insurance companies. Actual expenditures exceeded the approved budget also in public order and security and in education. In other areas, the level of expenditures is close to the level assumed by the budget approved for 2016.

[41] Latest available COFOG data are from 2014.
[42] In May 2015 Eurostat amended the methodology for COFOG classification of public expenditures by function. Under the new classification, all social fund expenditures (S.1314) are regarded as social security. The relatively small differences in data reported by other EU countries for 2014 for healthcare and social security indicate that the new methodology (based on decision of their national statistical agencies) has not been consistently applied by all countries. This issue is further discussed in the Stability Programme 2016, BOX 11.
[43] The number of new approved old age pensions during 2016 exceeds the initial assumptions of the budget. A part of the difference is due to the fact that the 2016 budget did not include social security expenditures for armed forces, however these figures influence the results of the ongoing monitoring.

FIGURE 34: Comparison of general government expenditures under COFOG classification (changes p. p. GDP)



Note. GGB – general government budget (approved by the parliament) ER - expected reality *Source: MFSR*

Under the draft general government budget for 2017 public expenditure is to reach the level of 41.1 per cent of GDP, which, compared to the expected actual results of 2016 means a drop by 0.7 p.p. GDP. Major year-on-year changes in the 2017 budget are in social security and economic affairs. Despite the year-on-year increase in social security expenditures, their proportion to GDP is falling. This is mainly due to the improving situation on the labour market and lower amount of social expenditures, and implementation of measures to decelerate the growth of expenditures for healthcare purchased by health insurance companies. In other functions, there are no major expected changes in the proportion of expenditures to GDP (Figure 34).

I.9. General government balance under the no-policy-change scenario

The no-policy-change (NPC)[44] scenario, defined as a development of public finance under the assumption of no amendments to legislature and updating the estimated macroeconomic development, quantifies the size of measures necessary to meet the budget objectives. The size of necessary measures (the fiscal scope) to meet the budget objectives can be quantified by comparing the general government balance in the NPC scenario compared to the budget objective. Based on the NPC, it is also possible to assess the size of the measures (consolidation and/or incentive) necessary to reach budgetary objectives.

The starting point for development of a no-policy-change scenario is the latest estimate of general government deficit in 2016 in the amount of 1.97 per cent of GDP. Provided that there are no changes in the economic policies, in 2017 the general government deficit would drop down to 0.29 per cent of GDP (compared to the nominal objective 1.29 per cent of GDP) and in 2018 it will further decrease to reach the level of 0.04 per cent of GDP (vs 0.44 per cent of GDP). For 2019, we assume, similarly to the budget objective, reaching a surplus balance in the amount of 0.55 per cent of GDP[45].

The difference in the general government balance between the NPC scenario and the draft budget for 2017 equals to 1.00 per cent of GDP (EUR 839 mil.). The revenue side includes a difference amounting to 1.45 per cent of GDP, which resulted from the increase in both current (1.02 per cent of GDP) and capital expenditures (0.43 per cent of GDP). As to the current expenditures, these include in particular, growth of expenditures in intermediate government consumption (0.56 per cent of GDP) and compensations for employees (0.16 per cent of GDP). On

[44] The manual for development of the NPC scenario is published on the Ministry of Finance website: http://www.finance.gov.sk/Default.aspx?CatID=9301.
[45] The overall quantification of the difference between the budget and the no-policy-change scenario does not take into account the impact of changes in interest expenses. In other words, after budgetary objectives are achieved, the interest expense related to financing the existing cash deficit will also change.

the revenue side, there is a consolidation compared to NPC at the level of 0.45 per cent of GDP, which partly offsets the fiscal expansion in expenditures.

In 2018 and 2019, consolidation of public finance occurs mainly on the revenue side of the budget, with persisting and decreasing fiscal incentive in the expenditure side. Compared to the NPC scenario, the fiscal framework on the 2018 - 2019 horizon, assumes mainly growing employee compensations, which will be to certain extent set-off by lower transfers for healthcare. In both above mentioned years, we expect that expenditures for common goods and services and social transfers[46] will grow faster compared to the NPC scenario,

TABLE 11: Comparison between the balance of expenditures and revenues and the no-policy-change scenario in 2017 - 2019 (per cent of GDP)

		NPC			GGBP 2017-2019			GGBP-NPC		
	ESA code	**2017**	**2018**	**2019**	**2017**	**2018**	**2019**	**2017**	**2018**	**2019**
Total revenues	**TR**	**39.3**	**39.4**	**38.4**	**39.8**	**39.8**	**38.7**	**0.5**	**0.4**	**0.3**
Taxes on production and imports	D.2	10.7	10.5	10.2	10.9	10.7	10.5	0.2	0.2	0.2
Current taxes on income, wealth, etc.	D.5	7.7	7.8	7.8	7.7	7.8	7.8	0.0	0.1	0.0
Capital taxes	D.91	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Social security contributions	D.61	14.2	14.1	14.0	14.2	14.1	14.0	0.0	0.0	0.0
Property income	D.4R	0.7	0.6	0.6	0.7	0.6	0.6	0.0	0.0	0.0
Other (1)		6.1	6.4	5.8	6.3	6.6	5.9	0.2	0.2	0.1
Tax burden (2)		32.6	32.4	32.0	32.8	32.6	32.3	0.2	0.3	0.2
Total expenditure	**TE**	**39.6**	**39.4**	**37.8**	**41.1**	**40.3**	**38.6**	**1.4**	**0.8**	**0.7**
Compensation for employees	D.1P	8.7	8.8	8.7	8.7	8.7	8.6	0.0	-0.1	-0.2
Intermediate consumption	P.2	5.1	4.9	4.7	5.6	5.2	5.0	0.6	0.3	0.3
Subsidies	D.3P	0.5	0.4	0.4	0.6	0.5	0.4	0.0	0.0	0.0
Interest expense	D.41P	1.3	1.3	1.2	1.3	1.3	1.2	0.0	0.0	0.0
Total social transfers	D.6P. D632	18.5	18.1	17.6	18.6	18.2	17.7	0.1	0.1	0.1
Incl.: unemployment benefits		0.2	0.2	0.1	0.2	0.2	0.1	0.0	0.0	0.0
Gross fixed capital generation	P.51G	3.0	3.3	2.6	3.4	3.4	2.5	0.4	0.1	-0.1
Capital transfers	D.9P	0.2	0.2	0.2	0.2	0.2	0.2	0.0	0.0	0.0
Other (3)		2.0	2.2	2.1	2.3	2.5	2.7	0.3	0.3	0.6
General government balance (4)	**B.9 (4)**	**-0.29**	**-0.04**	**0.55**	**-1.29**	**-0.44**	**0.16**	**-1.00**	**-0.40**	**-0.39**

Note.: (1) P.11+P.12+P131+D.39rec+D.7rec+D.9rec (other than D.91rec) *Source: MF SR*

(2) D.2+D.5+D.61+D.91

(3) D.29p+D.5p+D.7p+NP

I.10. Description of measures

The following section quantifies and describes the effects of measures incorporated into the draft budget. The items above the scope of specified measures include differences between the NPC scenario and the results of budgeting negotiations included in the draft budget. The following section describes incorporated measures including their quantification. The most important measures on the revenue side are: changes in Special levy on enterprises in regulated sectors and reduction of the CIT rate from 22 per cent to 21 per cent. On the expenditure side, the most important measures include: valorization of pensions by 2 per cent and increase in salaries of teachers and professional staff at regional and university education

[46] Including valorisation of pensions over the horizon of years 2017 - 2019 in the amount of EUR 112, 113 and 114 mil., respectively (0.13 per cent of GDP).

TABLE 12: Measures included in the draft general government budget (ESA 2010, compared to NPC)

Revenues	Subsector	ESA2010	2017	2018	2019
Tax revenues - total	**S. 13**		**0.26**	**0.32**	**0.29**
Taxes on production	S. 13	D.2	0.26	0.28	0.31
Income taxes	S. 13	D.5	-0.01	0.06	0.00
Revenues from fees and charges	S. 13	D.61	0.00	-0.01	-0.02
Changes in special levy on enterprises in regulated sectors			0.20	0.19	0.14
Changes in special levy on selected financial institutions			0.06	0.06	0.06
Increase in excise duties on tobacco			0.04	0.04	0.07
Introduction of 8 per cent rate on non-life insurance			0.05	0.06	0.06
Introduction of withholding tax on dividends			0.00	0.06	0.05
Increasing the gambling duty			0.02	0.02	0.02
Increasing CIT rate from 22 per cent to 21 per cent			-0.17	-0.17	-0.17
Increase of lump sum allowances for self-employed persons			-0.02	-0.02	-0.03
Exemption from CIT payments to resolution fund			-0.01	-0.01	0.00
Introduction of interest charges on retained VAT refunds			-0.01	0.00	0.00
Increase in capital income (EKRK classification 230)			0.09	0.09	0.09
Non-tax revenues - total	**S.13**	**D.7/P.11/ P.12**	0.19	0.12	0.05
Total revenues (tax + non-tax)	-	-	**0.45**	**0.43**	**0.33**
Expenditures	**Sub-sector**	**ESA2010**	**2017**	**2018**	**2019**
Compensations, thereof:	**S.13**		-0.05	0.07	0.16
Increase in salaries of teachers	S.13	D.1P	-0.12	-0.11	-0.10
Intermediate consumption, thereof:	**S.13**		-0.56	-0.33	-0.28
Reserves		P.2	-0.38	-0.26	-0.24
Subsidies, thereof	**S.13**		-0.04	-0.03	-0.02
Agricultural subsidies	S.1311	D.3P	-0.03	-0.02	-0.02
Social transfers, thereof:	**S.13**		-0.17	-0.16	-0.16
Valorisation of pensions (2 per cent)	S.1311	D.62P	-0.13	-0.13	-0.12
Amendment – compensations for severe health disability	S.1311	D.62P	-0.04	-0.04	-0.04
Natural social transfers	**S.1314**	D.632P	0.06	0.06	0.07
Other ordinary transfers	**S.13**		-0.26	-0.34	-0.64
Reserves		D.7P	-0.05	-0.05	-0.04
Capital expenditures, thereof	**S.13**		-0.43	-0.11	0.15
Reserves for major capital investments		P.51g/NP	-0.27	-0.12	-0.02
Public transportation companies	S13.13	P.51g	-0.07	-0.07	0.00
Defence development	S.1311	P.51g	-0.06	-0.08	0.00
Development of sports infrastructure	S.1311	D.9P	-0.06	-0.08	-0.01
Renovation of the Slovak National Gallery	S.1311	P.5	-0.01	-0.03	0.00
Total expenditures	-	-	**-1.45**	**-0.84**	**-0.72**

Note. (+) increase in revenues and decrease in expenditures *Source: MFSR*

Revenue measures

1. Measures with a positive effect on tax revenues

- Amendment to Act No. 235/2010 Coll. **on special levy on enterprises in regulated sectors** revises the calculation of a special levy and introduces a higher rate on regulated sectors. Effective from 1.1.2017, the rate will double to reach the level of 0.726 per cent. Since 2019 it will go down to 0.545 per cent and in 2021 it is expected to reach the present level (0.363 per cent). The new legislation does not longer insist on the requirement that in order to qualify for the levy 50 per cent of sales shall be generated from regulated activities; the only eligibility criterion is generating a profit equal to EUR 3 million or higher. Under the new legislation the levy will only be charged on revenues from domestic regulated activities and the present reduction of the payment base to EUR 3 million will be cancelled. Thus, regulated entities generating a profit, total amount of which exceeds EUR 3 million, will be charged on every euro of revenues made from regulated activities.

- Amendment to Act No. 384/2011 Coll. **on special levy on selected financial institutions** cancels the automatic adjustment of the levy rate depending on total amount of the accumulated paid levies, and retains the present level of 0.2 per cent for years 2017 - 2020 (the initial automatic reduction of the rate to 0.1 per cent should apply since Q1 2017).
- In order to prevent the ongoing erosion in collection of excise duty on tobacco vs GDP, a tax indexation is introduced in form of predefined changes in tax rates over a 4-year period. Effective from 1.2.2017 and 1.2.2019 **rates of excise duty on tobacco products** will increase. The changes will affect tax rates applicable to all tobacco products.

TABLE 13: Planned changes in tax on tobacco products

		Present state	From 1.2.2017	From 1.2.2019	Change in EUR 2017	Change in EUR 2019
Cigarettes						
specific part	EUR / 1000 pcs	59.5	61.8	64.1	2.3	2.3
percentage part	per cent of the price of cigarettes	23	23	23	-	-
minimum rate	EUR / 1000 pcs	91	96.5	100.1	5.5	3.6
Tobacco	EUR / kg	71.11	73.9	76.7	2.79	2.8
Cigars, cigarillos	EUR / kg	71.11	71.11	76.7	-	5.59

- Effective from 1.7.2017 excise duty will be introduced on smoke-free tobacco products which are not consumed during burning. The tax base will be the weight of the tobacco in the product expressed in kilograms and the tax rate will be the same as the tax rate on tobacco. We assume that during years 2017 – 2019, this measure will only have a negligible impact on general government tax revenues.
- Effective from 1.1.2017 **an 8 per cent rate on insurance premium for non-life insurance is introduced**. The levy does not apply to mandatory third-party liability insurance, as it already is subject to an 8 per cent contribution. The contribution is paid on a quarterly basis, or within one month after the end of each quarter.
- The amendment to Act No. 595/2003 Coll. on Income Tax introduces **withholding tax with 7 per cent rate** on distributed corporation profits (dividends) paid to individuals in Slovakia, effective from 1.1.2018. For the first time, the withholding tax will be applied to dividends paid from profits for 2017 tax period. The amendment further regulates taxation of dividends paid for taxation periods until 31.12.2003 in form of a positive retroactivity due to the reduction of the tax rate from 19 per cent, and/or 25 per cent to the present 7 per cent. The withholding tax has been introduced along with existence of health insurance contributions on dividends at a 10 per cent rate, paid out from tax period 2011 through 2012 and 14 per cent from tax period 2013 through 2016. The health insurance contributions will no longer be applied on dividends referring to periods after 2017.
- With the aim of better regulation of gambling levy on four types of gambling, (video lotteries, gaming machines, gaming machines in casinos and live casino games) is increased as of 1.1.2017.

- The amendment of the act on administrative fees regulates the vehicle registration fee. Since 2017, the fee depends on engine power and the age of vehicle, and the same approach applies to every vehicle, irrespective of whether the vehicle is acquired in Slovakia or imported from abroad. Vehicles powered with an alternative fuels are subject to 50 per cent relief on the amount of the registration fee, up to EUR 33.

TABLE 14: Vehicle registration fee - coefficients

Output in kW		Fee	Vehicle age	Amortization
0	80	33	New vehicle	100 per cent
80	86	90	1	82 per cent
86	92	112	2	68 per cent
92	98	155	3	56 per cent
98	104	206	4	46 per cent
104	110	264	5	38 per cent
110	121	365	6	32 per cent
121	132	526	7	26 per cent
132	143	700	8	23 per cent
143	154	870	9	19 per cent
154	165	1 100	10	16 per cent
165	176	1 250	11	14 per cent
176	202	1 900	12	12 per cent
202	228	2 300	13	10 per cent
228	254	2 700	14	9 per cent
	> 254	3 900	15	8 per cent
			16	7 per cent
			17 +	6 per cent

2. Measures aimed to support the business environment, with negative effect on tax revenues

- Effective from 1.1.2017 the **corporate income tax rate will be reduced by 1 percentage point**, from the present 22 per cent to 21 per cent.
- As a part of support to business activities, effective from 1.1.2017 **lump-sum allowance will be increased** from present 40 per cent to 60 per cent of total income. Additionally, the maximum annual amount of claimable lump-sum allowance will be changed from EUR 5 040 to EUR 20 000.
- Effective from 2017, **payments made by banks to resolution fund** (Council for solving emergency events) will be regarded as tax-deductible expenses for income tax purposes.
- Effective from 2017, interest charges were introduced on **retained VAT refunds**. A tax payer becomes entitled to interest charged on retained VAT refund if the tax office returns the VAT refund 6 months after the date when the VAT refund was due for repayment; the interest will be charged at double the basic ECB interest rate valid on the first day of the calendar year for which the interest is charged. The minimum interest rate on a retained VAT refund is 1.5 per cent.

3. Other revenue measures under NPC scenario

- Besides measures of legislative nature regarding the NPC scenario, the budget also assumes higher non-tax income from sold market production and current transfers. With respect of the aforementioned income types, in the following years, the NPC scenario assumes keeping the same level as achieved in the base year, i.e., the latest estimate from the ongoing monitoring for 2016

Expenditure measures

1. Compensations

The draft budget of the general government for 2017 assumes growth of compensations above the NPC level, by 0.05 per cent of GDP. The budget also reflects the effect of growth in salaries of teachers and professional staff in regional schools and universities effective from September 2016 for 2017 (0.12 per cent of GDP). As for compensations, the draft budget so far does not include the effect of collective bargaining in other sections of the general government; however, it should be possible to cover the expenses for the discussed 4 per cent valorisation from non-allocated resources in other sections of the budget.

2. Subsidies

Compared to NPC scenario, expenditures for subsidies are growing over the whole horizon of the budget. The growth of the expenditures is caused, in particular, by higher agricultural subsidies (0.03 per cent in 2017) and, to a lower extent, the growth is due to higher subsidies for transportation.

3. Social security contributions

Pension benefits under old-age and disability insurance will grow by 0.14 per cent of GDP due to one-off valorisation of pensions by 2 per cent depending on the type of pension. The measure involves growth of old-age pensions above the indexation level under the valid legislation. Besides the valorisation of pensions, the draft budget also includes increasing benefits to support people with severe health disabilities (0.04 per cent of GDP).

4. Capital expenditures

A stronger growth in capital expenditures in 2017 results mainly from renewal of rolling stock of public transport companies using own funds, increase in expenditures for defence to 1.2 per cent of GDP , renovation of the Slovak National Gallery and capital investments in sports infrastructure through capital transfers. In the following years, the growth of investments will decelerate.

5. Reserves

The draft budget includes several reserves totaling 0.7 per cent of GDP in 2017. The reserves include the following items:

- Intermediate government consumption (0.38 per cent of GDP), in particular due to potential faster drawing of EU projects and for development in 2017,
- other current transfers (0.05 per cent of GDP) in particular for government reserves and solution of emergency events,
- capital expenditures (0.27 per cent of GDP) for major capital investments and possible accelerated drawing of EU projects.

BOX 7 – One-off and temporary expenditures in 2016

In 2017, most of last year's temporary expenditures **will not be repeated or are expected in a substantially lower amount.** When estimating the development of the deficit under the no-policy-change scenario, **one-off expenditures** were excluded from the basis of the base year 2016**.** It refers mainly to expenditures related to preparation of Nitra industrial park, project D4/R7 (total: EUR 485 mil.), corrections of EU funds (EUR 201 mil.) and one-off items to cover higher expenditures incurred by Health Insurance Company (EUR 96 mil.). Additionally, the base of 2016 is net of one-off expenditures in relation to Slovakia's presidency of the Council of the EU (EUR 50 mil.), contribution to households for gas consumption (EUR 48 mil.), payment to Resolution fund (EUR 34 mil.) and agricultural subsidies (EUR 30 mil.).

TABLE 15: List of one-off measures in 2016 for the NPC scenario (ESA 2010, EUR mil. and in per cent of GDP)

	ESA2010	2016	2016 (in per cent of GDP)
SK Pres	D.1/P.2	50	0.06
Agricultural subsidies (dairy production)	P.2	30	0.04
One-off expenditures to cover higher expenses of HIC	D.632	96	0.12
Subsidies to households for gas consumption	D.7	48	0.06
Investment priorities (D4/R7, industrial parks)	P.5g/NP	485	0.60
EU corrections	D.9	201	0.25
Contribution to Single Resolution Fund	D.9	34	0.04

Source: MF SR

Development compared to NPC scenario in 2018 - 2019

The draft budgetary plan for 2018 – 2019 assumes consolidation of public finance exclusively on the revenue side of the budget, the development of which will be just partly compensated by planned fiscal impulses in expenditures. Compared to the no-policy-change scenario, total expenditure will be higher by 0.8 per cent of GDP in 2018 and by 0.7 per cent of GDP in 2019. The strongest growth is budgeted in intermediate consumption, where expansion of 0.3 per cent of GDP is expected in both aforementioned years. Unlike NPC scenario, a slower growth is expected in compensations for employees. While in 2018, capital investments are planned to grow by 0.1 per cent of GDP, for 2019, we assume savings at similar proportion to GDP. Development in current transfers (+0.3 and/or +0.6 per cent of GDP compared to NPC) means an accumulation aiming to release several expenditure items not allocated in the budget. Capital transfers will show similar dynamics as assumed under NPC scenario. Compared with the no-policy-change scenario, the revenue side expects continuation of the started positive trend, as a consolidation impulse in expected in both monitored years: 0.4 per cent of GDP in 2018 and 0.3 per cent of GDP in 2019. The development will be caused by growth of both tax and non-tax revenues in proportion of around 2:1.

I.11. Consolidation effects

No-policy-change scenario (NPC) serves as a base in the process of quantifying the impact of fiscal measures. The impact of the fiscal policy in the period 2017 to 2019 is based on measures necessary to achieve the fiscal targets contained in the general government budget for 2017 to 2019 compared to the NPC. However, the increase in compensations (in general government) resulting from collective bargaining is not included in the fiscal framework on the expenditure side.

TABLE 16: Total size of measures necessary to reach the fiscal targets, compared with NPC (ESA2010, per cent GDP)

	2017	2018	2019
1. General government balance - Fiscal targets	-1.29	-0.44	0.16
2. General government balance – NPC scenario	-0.29	-0.04	0.55
3. Size of measures (1-2)	-1.00	-0.40	-0.38
- year-on-year change	**-1.00**	**0.55**	**-0.01**

Source: MF SR

In 2017, a fiscal space in the amount of 1 per cent of GDP arises compared to the NPC scenario and based on the fiscal framework, the fiscal impulse is concentrated mainly in the intermediate consumption and investments in general government. Overall expenditure expansion equals to 1.4 per cent of GDP. Besides higher intermediate consumption and investments in general government, the fiscal framework on the expenditure side also assumes a 2 per cent valorisation of pensions, growth of compensations, higher current transfers and subsidies. The consolidation measures on the revenue side equals to 0.5 per cent of GDP. These include expansionary revenue measures (reduction in the CIT rate and increased limit for deduction of lump-sum expenses) necessary to achieve the objectives (higher excise duties, extension of special levies in regulated sectors, retaining the special levy for financial institutions, charge on insurance premium and increasing the general government market production).

In 2018, given that permanent measures are adopted to meet the budgetary objectives, consolidation measures are needed in the amount of 0.5 per cent of GDP. In 2019 no additional measures are needed. In 2018, saving measures are assumed exclusively on the expenditure side of the budget. On the revenue side, expansionary measures (increased limit for deduction of lump-sum expenses and decreasing the general government market production) are compensated by restrictive measures (higher excise duties and withholding tax). Effects of the fiscal policy were calculated excluding measures having no direct effect on GDP[47].

In 2017 the positive impact on growth of GDP is estimated at 0.5 p. p. The consolidation necessary to achieve the budgetary objective in 2018 will decrease the growth of GDP by 0.2 p. p. In 2019, the minimum size of expansionary measures will have a negligible impact on economy.

In 2017 the implied fiscal multiplier is estimated at 0.47. The size of the multiplier corresponds to the structure of the incentive, which is concentrated almost exclusively on the expenditure side of the budget, in particular in the intermediate consumption and investments in general government. The growth of pensions, compensations, subsidies and current transfers and, on the revenue side, the reduction of CIT and the higher limit for deduction of lump-sum expenses, have a positive impact on the economic growth through higher gross disposable income and private investments**. In 2008, the fiscal multiplier of the consolidation package[48] is estimated at 0.39.**

[47] On the expenditure side this means the category additions less disposals of non-financial non-produced assets, which in 2017 are by EUR 83 million higher compared to NPC and in 2018 by EUR 83 million lower compared to NPC scenario.
[48] The difference between the NPC scenario and the draft fiscal framework for each separate revenue and expenditure item.

II. Linking the budgetary plan to the objectives of the Growth and Employment Strategy and Country-specific Recommendations of the European Commission

The government has prepared a set of structural measures focused on supporting economic growth and employment, as a response to major challenges of the Slovak economy – labour market, primary education and the healthcare system. Assessment of efficient use of public funds and combating tax frauds are ongoing processes. In education the government will be mainly focused on increasing the attractiveness of teaching profession, the interconnection of vocational education and practical training (dual education), expansion of kindergarten capacities and supporting integration of children from marginalized communities. It is planned to expand the capacity of childcare facilities. Positive labour market development will be further supported by the public employment services reform, as well as the broadening of active labour market policies. In healthcare the government will focus on building up data infrastructure and reference pricing for large expenditure items.

II.1. Structural measures

Major challenges in terms of falling behind other countries include: the labour market, primary education and the quality of healthcare[49]. This chapter describes major structural measures in these and other areas, which have already been adopted by the Slovak government, or which are planned for implementation within next two years in accordance with the National Reform Programme of SR 2016.

A new instrument allowing to arrive at a balanced budget and to increase the value for money is the assessment of efficient use of public funds. The project has started under the leadership of the MF SR and in close cooperation with the Government Office of the Slovak Republic and all executive departments. The rules will be reformed, processes will be set up and institutions will be supported in order to encourage adoption of good decisions in the public interest and increase the value for money in Slovak public sector. The decisions on key investments, policies, regulation of behaviour of both the population and corporations and decisions on public operating expenditures will be subject to a comprehensive evaluation. In July 2016, first interim reports were published on revision of expenditures in transportation, healthcare and informatization[50] and the final reports for the aforementioned three areas are part of the draft budget of the general government.

According to the latest EC report[51] since 2012 the **VAT collection gap** has been reduced from 37 per cent to 30 per cent in 2014. Based on interim estimate of the MF SR, further, although milder reduction of the VAT gap is expected for 2015. Despite the strong reduction, however, Slovakia has not reached the EU average with VAT gap equal to 14 per cent. In 2015 the action plan for combating tax frauds was updated; the plan includes measures aimed at prevention of tax evasions, but also at improving effectiveness of tax recovery and tax collection. MF SR prepared a pilot study of spending review of the Financial Administration SR[52], which identified additional space for further improving the effectiveness of tax and customs duty collection and reduction of administrative expenses per collected euro.

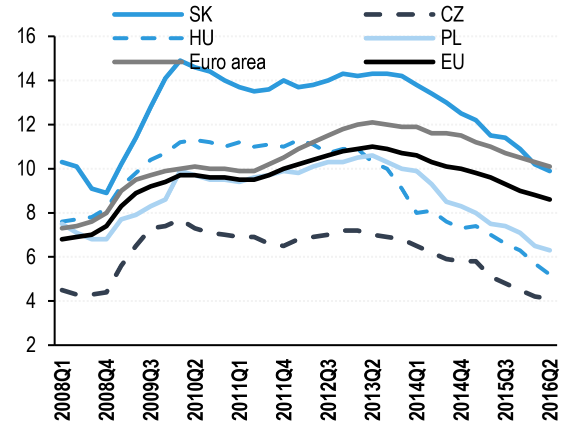
Attractiveness of teaching profession will increase. Effective from September 2016, salaries of teachers and professional staff at regionall schools and universities will increase by 6 per cent. The rise in salaries assumes supporting a faster growth of salaries for starting teachers in order to make the teaching profession more attractive to talented young people. The **dual education project** is focused on linking the education at vocational schools to

[49] The priorities were identified in the National Reform Programme SR 2016.
[50] Priebežné správy, Útvar hodnoty za peniaze, MF SR.
[51] https://ec.europa.eu/taxation_customs/sites/taxation/files/2016-09_vat-gap-report_final.pdf.
[52] To be published on the MF SR website

labour market needs. During the new programming period 2014 – 2020, **national projects in the area of inclusion** will be linked to the presently applied all-day education system, development of inclusive education for children from marginalized Roma communities, involvement of assistant teachers and edification activities for Roma communities. In the following years new kindergarten facilities will be built, also in regions with marginalized Roma communities.

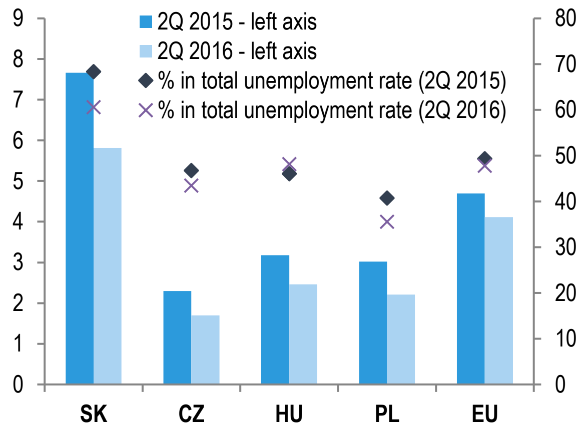
Despite the present positive development, **the labour market is still** one of the key problems faced by Slovak economy on a long-term run. The **total unemployment rate,** adjusted for seasonal factors, continues to decrease since the third quarter of 2013. In the second quarter of this year, the unemployment rate was 9.9 per cent which is below the unemployment rate of the euro area. **The long-term unemployment rate,** however, remains considerably high above the average of EU and V3 countries. In the second quarter of 2016, the share of long-term unemployed total number of unemployed dropped on a year-on-year basis from 68.4 per cent to 60.6 per cent, which further is one of the highest among EU countries.

FIGURE 35: Unemployment rate development by quarters per LFS (per cent active population, data net of seasonal effects)



Source: Eurostat

FIGURE 36: Long-term unemployment (per cent, 2Q 2015, 2Q 2016)



Source: Eurostat

Supporting the capacity and quality of **public employment services** including provision of targeted customised services to job seekers is one of the key measures aimed at reduction of long-term unemployment. In the new programming period the support to job seekers is further provided through instruments of the **active labour market policy (ALMP)**. The implemented measures are focused on **disadvantaged groups of job seekers** on the labour market (long-term unemployed, low-skilled people and people above 50). The pilot study of spending review of labour offices identified a space for improvement in the operating efficiency of labour offices and opportunities for reallocation of funds for ALMP instruments and operation aimed at a better placement of the unemployed on the labour market[53].

In order to support employment of mothers with children, effective from January 2016, the maximum amount of the **childcare allowance** increased from EUR 230 to EUR 280 in order to cover the costs of parents for childcare services. Administrative burden of its provision is also reduced. The budgeted amount for 2016 is EUR 9.4 million, of which EUR 6.8 million is planned to be financed by the ESF. In order to provide a financial support to **development of childcare services for children up to three years,** the conditions have been set up to enable implementation of this measure in the new programming period (Integrated Regional Operational Programme and Operational Programme Human Resources). A new legislation has been enacted to create a uniform framework

[53] Common study of MF SR and the Ministry of Labour, Social Affairs and Family SR available at http://www.finance.gov.sk/Default.aspx?CatID=5947.

for provision of care to children up to three years. Since January 2016 **the maternity benefit** increased from the current 65 per cent of the daily assessment base to 70 per cent. Due to the tax wedge on labour income, this measure has reached a level of reimbursement of net salary at around 90 per cent. Additional budgetary impact is expected to be EUR 8.7 million in 2016.

A number of changes are pending and/or are planned in **healthcare** in order to increase efficiency of expenditures and to improve results. Implementation of reference pricing of special medical materials started and a system was launched for central procurement of medical equipment. As to external services purchased by hospitals through tenders, maximum prices were defined centrally based on internal benchmarks. In 2017, measures will be adopted to reduce consumption of pharmaceuticals and to decrease the expenditures for pharmaceuticals, while maintaining availability and quality of the provided healthcare. By the end of 2017, regular internal and external benchmarking will be introduced on performance of hospitals, minimum personal and technical standards will be subjected to revision, the hospital bed capacity will be optimised to fit the needs of regions. During this year, implementation of DRG system will be launched as a payment mechanism for hospitals. The legislative regulation which is presently under preparation is expected to restrict re-exports of pharmaceuticals abroad effectively from 2017. Consideration will be given to establishing transparent rules for payments made by patients and developing a multi-source financing system.

As to **social assistance to people with severe health disabilities,** effective from 2017, the home care service allowance will be increased. The impact on the budget in 2017 is estimated at EUR 29.5 mil.

In 2017, there will be a one-off adjustment on **valorisation of pensions by fixed amount of 2 per cent** on average of the given type of pension, while maintaining sustainability of public finance. The impact on the budget in 2017 will be EUR 113.7 mil. Presently a discussion is pending on possibilities to extend eligibility for the programmed withdrawal under the second pension pillar for a broader range of savers.

The expenditures for **construction of motorways and expressways** reached their historical peaks in 2015. 54 per cent was financed by EU funds, which were higher than amount reported in prior years. One of the reasons is the end of the programming period. Thus, total expenses for this area in 2015 exceeded EUR 1 bn. (approximately 1.35 per cent of GDP). For the following years the budget further assumes strong investments in transportation. Key measures in transportation further include construction of missing motorway and expressway sections and construction, renewal and maintenance of class A roads. The transportation priorities will, for the first time, be determined based on the national multimodal transportation model. In public transport, the effort will be further focused on systematic increase of the significance of railway transportation in Slovakia's transport system and improvement of public passenger transport efficiency.

In 2016, **action plans** were approved **to assist the least developed districts**[54]. The support prefers selected districts for using finance from EU funds or obtaining investment incentives. Besides funds from operational programs a special regional contribution will be granted to support business activities and investors, HR development and improving the quality of the infrastructure. Under this type of assistance, effective from December 2015 **a SSC relief is granted for employment of persons from the underdeveloped districts**. The extension of the SSC relief applies to a new group of employees, who have been registered as unemployed for at least 6 months. For such employees, the employers will have to pay only accident insurance and the guarantee insurance for not more than 12 calendar months.

[54] This presently applies to 12 districts: http://www.nro.vlada.gov.sk/akcny-plan/.

In **the judicial system** the government approved changes in **distraint proceedings**. The following concept have been adopted: random selection of the distrainor in order to support independence in distraint proceedings, lump-sum compensations for distrainors, enhancing the importance of electronic communication and the central register of distraint proceedings to support transparency of distraint proceedings. Further changes will be implemented in the process **of judicial restructuring**. Since March 2017, the amendment of the Bankruptcy Act cancels the option of practical forgiving more than a half of debts and imposes a 5-year maturity on the remaining portion of the debt under corporate restructuring, unless the creditors voluntarily agree otherwise. The so called **"anti-mailbox" act** approved by the government imposes an obligation on companies effective from January 2017 to be registered in the register of partners to the public sector and to disclose their ownership structure up to the level of the ultimate beneficial owner.

III. Higher value for money

Value for Money is another instrument applied by the government to increase efficiency in using public funds. The first results were achieved from spending reviews of healthcare, transportation and public sector IT, amounting to around 8.6 per cent of GDP. In healthcare, the review identified potential measures totalling €363m, including €174m incorporated in the 2017 budget to improve the results of this sector. In transportation and IT, the revision identified potential savings and established a process for appraisal of large investment projects with a more active involvement of the Ministry of Finance. In 2017, the labour market and the social system, education, and the environment, together equal to 15 per cent of GDP, will be subject to spending reviews. The review will focus primarily on increasing the value of public expenditures. From 2017 onwards, final reports will have to be prepared by 30 June. The government will approve the reviews together with the general government budget by 15 October.

The Value for Money project is a new instrument to improve public expenditure efficiency. The government intends for this project to increase the value of public services and contribute to a balanced budget. The government has committed itself to the project in the Manifesto of the Government of the Slovak Republic and in the Stability Programme. Implementation of the Value for Money project will involve a reform of rules, a setup of processes and supporting institutions which encourage the adoption of good decisions in the public interest. Decisions on key investments, policies, regulation of behaviour of both the population and corporations, and the decisions on public operating expenditures will be subject to a comprehensive economic evaluation. In sectors which underwent a spending review, all future investment projects above €40m, and IT projects above €10m, will be subject to a comprehensive economic evaluation by the Ministry of Finance SR.

III.1. Spending reviews 2016

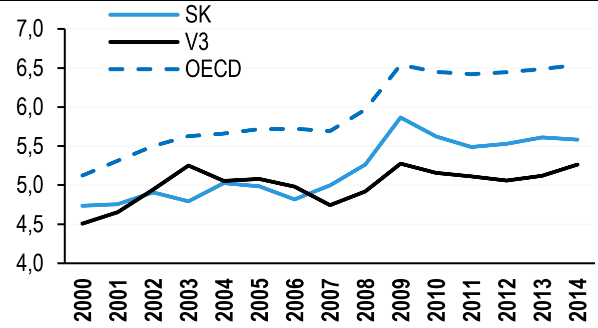
The first results were achieved from spending reviews of healthcare, transportation and public sector IT, amounting to around 8.6 per cent of GDP, as an integral part of the Value for Money project. Measures in the healthcare sector are included in the general government budget for 2017 - 2019. The government's ambition is to revise public expenditure on a regular and systematic basis so that most of the expenditures are assessed within the horizon of the election period. Findings from the reviews are reflected in general government budgets.

III.1.1. Healthcare spending review

Review of healthcare spending in an annual amount of 5.6 per cent of GDP (€4.4bn) aims to identify potential savings, particularly in healthcare expenditure, and then use them for efficient and necessary investments in inpatient facilities and for decelerating the growth in expenditures so that it is in line with the growth rate of prices in the economy.

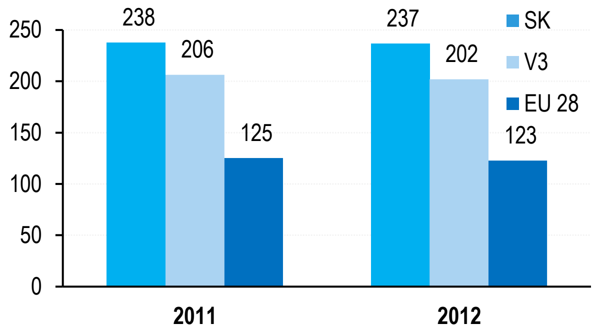
The review objective is to achieve a reduction in number of deaths which are amendable by the healthcare system to equal the average of V3 countries – the Czech Republic, Poland and Hungary. The current number is 18 per cent higher than the average, despite relatively high expenditures compared to neighbouring countries.

FIGURE 37: Public expenses on healthcare (per cent of GDP)



Source: OECD

FIGURE 38: Mortality amendable by healthcare system (per 100 000 persons)



Source: Eurostat

The review identifies potential measures in a total amount of €363m, including €174m already incorporated in the 2017 budget. From the total amount, €143m is public health insurance spending. Based on the identified measures, public health insurance spending will be internally restructured without saving in the scope or volume of provided healthcare.

TABLE 17: Saving measures (millions of €)

	2017	2018	2019	*potential saving*
Measures reducing costs of public health insurance	**143**	**159**	**165**	**268**
Overprescription of medications – introduction of prescription limits for outpatient service providers	20	20	20	59
Exceptions for medications – introduction of rules on refund of exceptions	10	10	10	10
Cost inefficient medications – central procurement of medications covered by health insurance	25	25	25	42
Special medical material – price reduction through reference pricing	35	45	45	55
Medical devices – reference pricing and inspection activities	15	15	15	15
Diagnostic exams – reduction of unit prices and limits to CT and MRI examinations	10	16	22	25
Diagnostic exams– introduction of limits for outpatient service providers	3	3	3	37
Improvement of inspection activities of VšZP	25	25	25	25
Measures reducing hospital costs (subordinate organisations of the Ministry of Health)	**31**	**31**	**31**	**95**
Operational expenses optimisation	5	5	5	10
Medical processes optimisation	15	15	15	74
Medication and special medical material procurement optimisation	8	8	8	8
Medical equipment procurement	3	3	3	3

Source: MF SR

Review of the healthcare sector identified measures in the following areas with a significant potential for improving cost-efficiency and increasing value for money:

1. Medications, medical equipment and special medical material – In 2017, spending on medications, medical equipment and special medical material will be reduced by €105m, mainly thanks to measures addressing overprescription of medications and reference pricing of special medical material and devices. The review has identified the overall potential to improve efficiency by €105 - 389m.

2. Healthcare providers – Thanks to measures optimizing operations, processes and procurement, in 2017, hospitals (reporting to the Ministry of Health SR) will save €31m. The spending review identified potential annual savings of up to €84m in operations and procurement in university hospitals (excluding purchases of medications, special medical material and medical equipment). Improved efficiency of operations and procurement will help to stop the growing indebtedness of hospitals, which will in turn create a space for capital investments in reconstruction and equipment. Implementation of the DRG (system of financing hospitals through payments for diagnosis related groups) will also strengthen a direct responsibility of hospitals for their expenses and will result in transparent and fair payments for healthcare.

3. Radio diagnostics and laboratories – In 2017, the reduction of unit prices for CT and MR examinations, together with established limits, is expected to result in savings of €13m. The analysis of prescribing radio diagnostic and laboratory examinations identified potential savings between €13 - 91m.

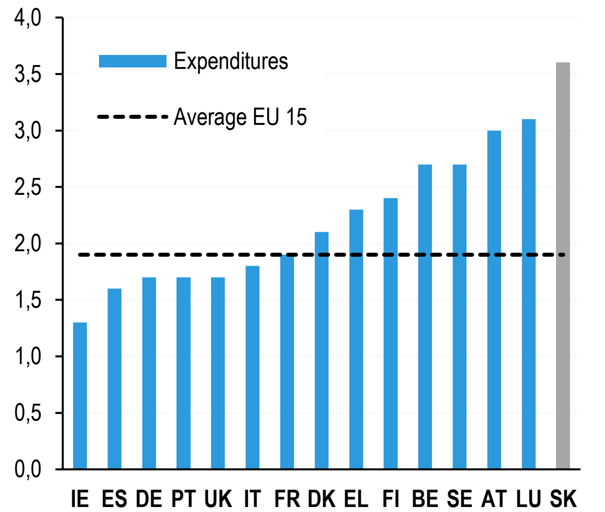
Further issues for analysis in terms of value for money include mainly patient transportation and ambulance services, healthcare professionals, doctor's visits and the health insurance system.

III.1.2. Transportation spending review

The review of transportation spending, in an annual amount of 2.4 per cent of GDP (€2.0 bn), aims to prepare measures to improve efficiency of the present investment envelope, while maintaining its size and improving, in a sustainable way, the efficiency of unit operating costs within the budgetary chapter of the Ministry of Transport, Construction and Regional Development of the SR (MDVRR SR).

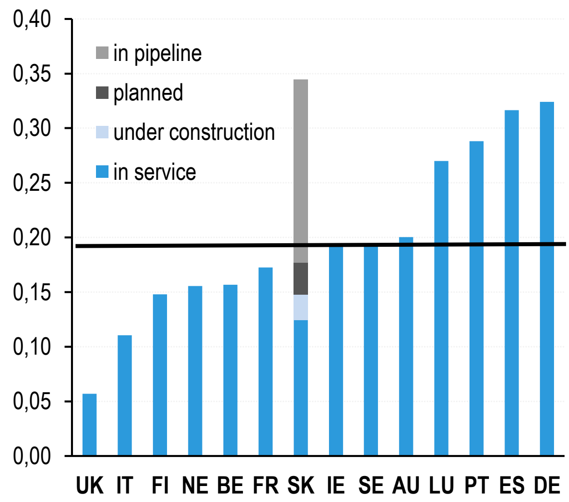
In 2013, Slovakia's total transportation spending reached 3.8 per cent of GDP. In proportion to GDP, the expenditures were higher than those in West European countries (EU 15). On the other hand, operating expenses are relatively lower. Compared to EU countries, Slovakia spends less on repairs and maintenance of 1st class roads and railways. Consequently, the condition of roads and railways is worse.

FIGURE 39: General government expenditures on transportation (per cent of GDP)



Source: Eurostat 2013

FIGURE 40: Length of motorways/number of citizens* (km/1000 persons)



Source: Eurostat 2013, NDS, MDVRR SR

Note: The data for the SR includes motorways and expressways.

In comparison with West European countries (EU15), Slovakia has fewer motorways and expressways, which is typical of converging countries. Investments are directed to the construction of new sections. After completing the priority package of projects, Slovakia will get closer to EU15 average in length of motorways/land area ratio. As for 1st class roads and railways, investments are focused in particular on modernization and renovation of the existing infrastructure.

The transportation review identified measures in the following areas with a considerable space for improving spending efficiency, and for measuring the results in transportation better:

1. **Evaluation and prioritization of projects**. Based on review conclusions, prepared projects will be subject to business evaluation, with the goal to find the optimal scope for, in particular, roads infrastructure and construction prioritization. The investment projects in pipeline for infrastructure construction amounts to approximately €9bn.

2. **Funding for maintenance and repairs of 1st class roads.** A major share of 1st class roads is in a poor condition. Besides capital investments, it is also necessary to increase funding for maintenance and repairs.

3. **Reduction of operational expenditure on railway infrastructure.** The expenses can be decreased by reducing the scope of underutilized infrastructure, and by changing transportation management. The changes require initial investments.

4. **Preparation of investment projects.** The review identified opportunities for improving the methodology, data collection and selection of projects.

The revision of expenditures for informatization identified potential annual savings in the amount of €22 - 40m in case of better purchases of licenses, telecommunication services and measures increasing the additional value of services in the amount of €4m. The delivery is expected in the following period.

III.1.3. Public IT spending review

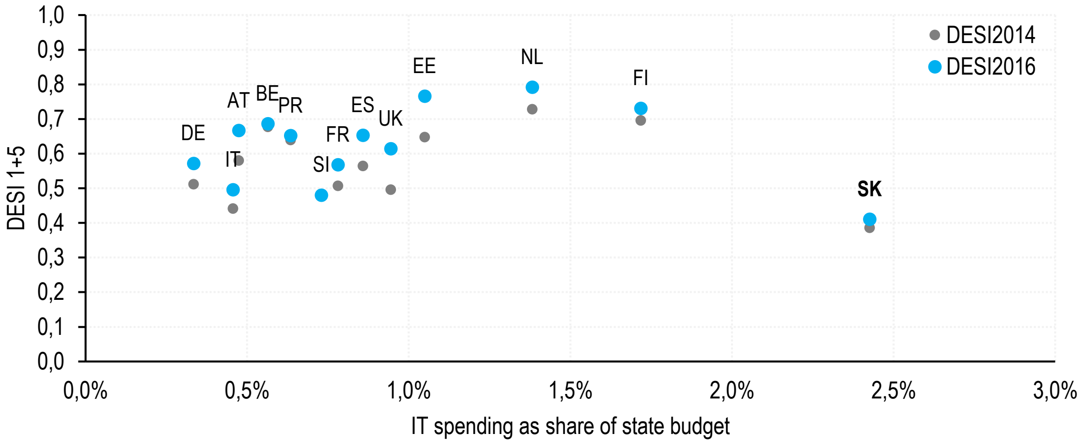
The review of public IT spending, in an annual amount of 0.6 per cent of GDP (€500m), aimed to identify proper measures to create an additional fiscal space of 30 per cent of the planned investment and operating expenses within three years of implementation.

Slovakia lags behind in public digital services considerably. According to the Digital Economy and Society Index (*DESI*), Slovakia ranked as 21st among EU28 at the end of 2015[55].

On the other hand, in 2011, Slovakia spent the highest share of the state budget on IT (2.5 per cent) and the second highest share of GDP (0.6 per cent) among OECD countries. The disproportion between the amount of expenditures and the results from citizens' perspective can be due to catching up to technical debt.

[55] The evaluation did not reflect the completion of OP IS projects at the end of 2015.

FIGURE 41: Relationship between results of DESI1+5 and IT spending (DESI 2014 and 2016, expenses 2011)



Source: OECD, RIS 2016, EC, ÚHP

The spending review involves potential measures which offer opportunities for direct savings in the amount of approximately 5 - 9 per cent of IT expenditures for 2017 (€22 - 40m annually) and result in higher value of the existing investments of at least 1 per cent (€4m annually).

TABLE 18: Potential saving measures (millions of €)

Saving measures	**25-43**
Improve effectiveness of terms for obtaining Microsoft licences	6.5
Centralized procurement of IT support services such as telecommunications and connectivity	9-27
Develop a binding migration plan to the public cloud and bind it to IT budgets	9.7
Measures bringing higher value	**4.3**
Reassess the level of required safety of electronic services	
Automatic issue safety personal codes for new eIDs	2.3
Develop a binding UX manual for government services	
Open eID to businesses by publishing the API	2

Source: MF SR

The review identified measures in the following areas with a considerable space for improving efficiency of expenditures – increasing the value for money and a more efficient measuring of results of the state IT:

1. **A higher availability and usability of digital services.** Increasing distribution of electronic ID cards, and thus increasing the value of the project by at least €2.3m annually in potential time savings. The annual amount will be increased by additional €2m a year by making the eID services available to the commercial sector. Additionally, it will be necessary to reassess the security of the digital services and to simplify authentication for digital services using alternative methods. Only 6 per cent of citizens holding the electronic ID card (1.7m) have safety elements required by eight out of ten digital public services.

2. **Utilizing the investment in the government cloud.** A binding plan of migration to the government cloud will be developed and its existence will be reflected in departmental IT budgets. Systems with high saving potential will be deployed to the cloud without an undue delay. Thereby, declared benefits of the cloud can be achieved, in the annual amount of €10 - 15m.

3. **Centralization of responsibilities for IT support services.** Centralization and optimization of IT support services in the areas of telecommunication services and communication infrastructure can result in annual savings amounting to €9 - 27m. Additionally, the need and use of software licences (Microsoft, Oracle, SAP) will be audited, aiming to improve consumption of licences, and to identify the most cost-effective way of procuring the licences. Potential annual savings in obtaining Microsoft software licenses have been estimated at €6.5m.

4. For a more efficient management of IT projects, it will be necessary to improve the collection of data on IT systems, to build internal capacities and a uniform and efficient framework for the selection and assessment of projects. All projects with a budget over €10m will be also subject to an economic assessment by the MF SR.

III.2. Spending reviews 2017

In 2017, the scheduled review will refer to the environment, labour market and the social system and regional schools and universities, totalling 15 per cent of GDP. The review will be primarily focused on increase of value of public expenses.

The spending review for labour market policies and social policies of the Ministry of Labour, Social Affairs and Family SR and the Social Insurance Agency in the annual amount of 11.5 per cent of GDP will be focused on potential improvement of efficiency and targeting of policies, in particular with regard to expenditures on social transfers and insurance, pensions, social services, employment policies and operation and investments of the Ministry, its agencies and the Social Insurance Agency, while maintaining the budgeted level of expenditures. The objective is to increase the employment rate and to reduce the proportion of population affected by poverty. The review will be linked to the pilot assessment of local branches of the Office for Labour, Social affairs and Family.

The spending review of regional schools and universities will assess annual expenditures in the amount of 2.7 per cent of GDP. The review will be linked to the prepared National Programme for Development of Education and Upbringing aiming to efficiently allocate additional funds directed to education. In regional education, the review will be focused in particular on optimization of the network of schools (and will be linked to the pilot evaluation of the primary school network) and increasing the attractiveness of teaching profession including the compensation system. The review will identify instruments to improve inclusion and equality in education including pre-school education. In university education, the review will reassess the accreditation process and the method of financing and evaluation of results of university science. It will examine the system for monitoring of successful placement of high school and university graduates on the labour market. The review will reassess the compliance between the structural funds programming activities and the identified priorities of the department.

The review of environmental spending in an annual amount of 0.6 per cent of GDP will propose measures to improve efficiency of the investment portfolio, increase effectiveness of environmental programmes and reduce unit operating costs in a sustainable way within the budgetary chapter of the Ministry of Environment SR. The objective of environmental public investments and policies is to improve the quality of the environment.

BOX 8 – Organization of the spending review

Strategic decisions regarding spending review are made by the government. Along with the Stability Programme and the general government budget it will make the most important decisions – review mandates and final reports. The sponsor of the agenda is the Ministry of Finance. The Ministry proposes objectives, organization and technical parameters of the review. A new division has been established at the Ministry of Finance to deal with management of the Value for Money project and preparation and coordination of the revision of expenditures including their linkage to the budgeting process.

Individual sector reviews are prepared by joined teams of the Ministry of Finance and the ministry of particular sector. In the first year, the timing of the review was flexible considering the short period between the approval of the Manifesto of the Government of the Slovak Republic and the public finance budget for 2017 - 2019.

Measures identified by the completed review will be incorporated in action plans by December 2017. Implementation of the measures will be monitored by the Ministry of Finance SR (financial measures) and the Office of the Deputy Prime Minister for Informatization and Investments (value).

Starting in 2017, the teams will be preparing final reports by 30 June. The government approves reviews together with general government budget by 15 October. The subjects for spending reviews in the following years and related mandates are decided by the government during the discussion of the Draft Budgetary Plan every year in October.

It is the responsibility of the Ministry of Finance to carry out the final reports of the reviews in cooperation with relevant ministry. For preparation of analyses of the areas mentioned before, other departments agree to cooperate in providing complete and detailed data.

Annex 4: Mandates for public spending reviews

Mandates for spending review of labour market policies and social policies

The spending review of labour market policies and social policies of the Ministry of Labour, Social Affairs and Family (MPSVR SR) and the Social Insurance Agency, in an annual amount of 11.5 per cent of GDP, will be focused on the potential improvement of efficiency and of targeting of policies, in particular, with regard to expenditures on social transfers and insurance, pensions, social services, employment policies and operation and investments of the Ministry, its agencies and the Social Insurance Agency, while maintaining the budgeted level of expenditures. The objective is to increase the employment rate and to reduce the share of population affected by poverty. The review will be linked to the pilot assessment of local branches of the Office of Labour, Social affairs and Family.

Performance objectives

The key objectives of the Government of the SR in employment and social policies is to increase the employment rates and to reduce the proportion of population affected by poverty. Slovakia has achieved a significant improvement in both indicators since 2010, however, it still has not met the objectives set in the National Reform Programme of the SR and in Europe 2020 Strategy, and stays below the EU level. The performance indicators are largely linked to target-oriented assistance to the beneficiaries (mothers, families, the disabled, the unemployed, persons in material need and socially disadvantaged communities). The purpose of the review will be also to improve consistency of the social insurance and pension system and to increase motivation to work and pay social security contributions. Consideration will be also given to sustainability of the system and the balanced intergeneration solidarity. The improved efficiency of public expenses **of the Ministry of Labour, Social Affairs and Family and the Social Insurance Agency** will contribute to meet government's goals in social and employment policies.

TABLE 25: Performance indicators for labour market and social policies

		2009	2010	2011	2012	2013	2014	2015	Target 2020
Long-term unemployment rate	**SK**	6.5	9.3	9.3	9.4	10.0	9.3	7.6	3.0
(per cent active population above 15 years)	**EU**	3.0	3.8	4.1	4.7	5.1	5.1	4.5	-
Employment rate	**SK**	66.4	64.6	65.0	65.1	65.0	65.9	67.7	72.0
(per cent in 20 - 64 age group)	**EU**	69	68.6	68.6	68.4	68.4	69.2	70.1	75.0
Reduction of poverty by soc. transfers	**SK**	24.9	26.2	25.3	24.7	25.2	25.4	25.8	-
(p.p.)	**EU**	26	27	27.1	27.1	27.7	27.5		-

Source: MF SR, MPSVR SR

Fiscal objectives

The purpose of the review will be to assess expenditures of the Ministry of Labour, Social Affairs and Family SR (MPSVR) and the Social Insurance Agency focusing on higher efficiency of current expenditures and analysis of economic benefits and the planned investment costs, while maintaining the budgeted level of expenditures. Reallocation of expenditures will be proposed towards programmes with the highest efficiency. The expenditures on projects implemented from EU funds under the programming period 2014 – 2020 should be used evenly until 2020.

Areas subject to review

Major areas subject to review include: social benefits and contributions, social insurance and pensions, social services, employment policies and operation and investments of the Ministry, its agencies and the Social Insurance Agency. Additionally, review will be focused on thematic areas analysed by types of beneficiaries, such as mothers, families, the disabled, the unemployed, persons in material need and socially disadvantaged communities. The review is to assess the operation of the pension saving system by employing "value for money" principle, including possible implementation of annual statement of social insurance payments.

Responsibilities and deadlines

It is the responsibility of the MF SR to carry out the interim and final report; the report is to be prepared in cooperation with the Ministry of Labour Social Affairs and Family SR. For the purpose of preparation of analysis of the above mentioned issues, MPSVR SR and MF SR agree to cooperate in providing complete and detailed data and information. The interim report will be prepared by the end of April 2017, the final report will be prepared and published by the end of June 2017.

Mandate for spending review of regional schools and universities

The spending review of regional schools and universities will assess annual expenditures in the amount of 2.7 per cent of GDP. The review will be linked to the prepared National Programme for Development of Education and Upbringing aiming to efficiently allocate additional funds directed to education. In regional education, the review will be focused in particular on optimization of the network of schools (and will be linked to the pilot evaluation of the primary school network), an increasing the attractiveness of teaching profession including the compensation system. The review will identify instruments to improve inclusion and equality in education including pre-school education. In university education, the review will reassess the accreditation process and the method of financing and evaluation of results of university science. It will examine the system for monitoring of successful placement of high school and university graduates in the labour market. The review will reassess the compliance between the structural funds programming activities and the identified priorities of the department.

Performance objectives

The key objective in regional education is to provide children and students with access to education irrespective of their social situation to enable them to gain education, competences and skills, and to teach them how to develop and cultivate their personalities and to gain and encourage their respect to human rights and basic freedoms. In case of universities, their mission is to develop harmonic personalities, knowledge, wisdom, goodness and creativity in people and to contribute to the development of education, science, culture and health for the benefit of the whole society and thus contribute to building of the knowledge society.

Performance indicators for regional schools, universities including science are given below:

TABLE 26: Performance indicators for regional schools and universities

		2009	2010	2011	2012	2013	2014	2015	Target 2020
PISA	**SK**	488,1			472				505
(average of achieved score)	**OECD**	496,7			497				-
Early termination of school attendance	**SK**	4,9	4,7	5,1	5,3	6,4	6,7	6,9	6,0
(per cent in 18 - 24 age group)	**EÚ**	14,2	13,9	13,4	12,7	11,9	11,2	11,0	10,0
per cent of population with university education	**SK**	17,6	22,1	23,2	23,7	26,9	27	28.4	40
(per cent in 30 - 34 age group)	**EU**	32,3	33,8	34,8	36,0	37,1	37,9	38,7	40
PIAAC score	**SK**								
(average score, 16-29 cohort)	**OECD**								
Citation response to publication	**SK**								
(normalized citation index)	**OECD**	1	1	1	1	1	1		
Research grants from abroad won by Slovak universities (millions of €)	**SK**	6,0	6,2	6,1	5,0	5,9	5,7		

Source: MF SR, MŠVVŠ SR

Fiscal objectives

Total amount of the public funds increase to be used in education and upbringing for this election period will be €2bn in accordance with the Manifesto of the Government of the Slovak Republic. By the end of the election period, in 2020, the annual amount of public funds spent on education will be comparable to the average of EU countries.

Responsibilities and deadlines

The interim and final reports will be carried out by MF SR in cooperation with the Ministry of Education, Science, Research and Sport SR (MESRS), they both agree to cooperate in providing complete and detailed data and information for preparation of analyses of the above mentioned issues. The interim report will be prepared by the end of April 2017 and the final report will be prepared and published by the end of June 2017. MF SR will publish the final report and submit it to the meeting of the Government of the SR.

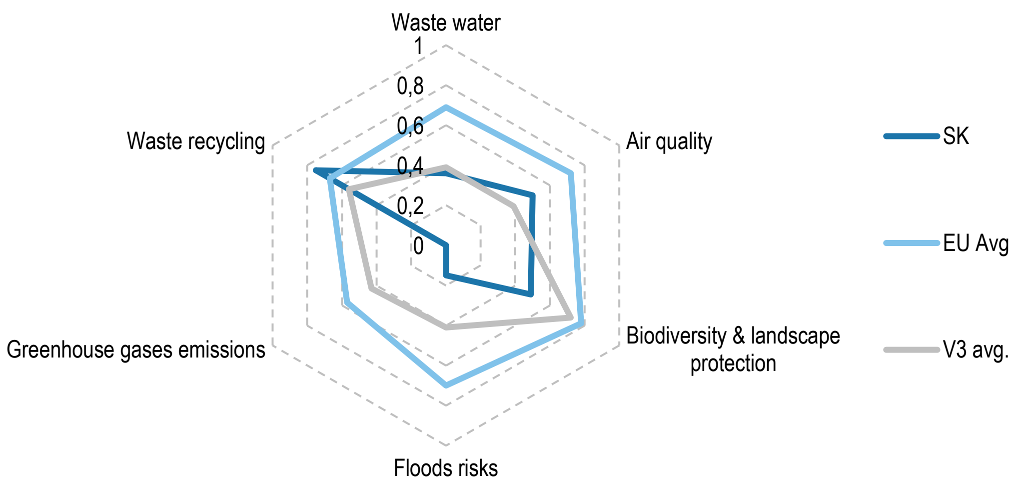
Mandate for environmental spending review

The environmental spending review in an annual amount of 0.6 per cent of GDP will propose measures to improve efficiency of the investment portfolio, to increase effectiveness of environmental programmes and to reduce unit operating costs in a sustainable way within the budgetary chapter of the Ministry of Environment SR. The objective of environmental public investments and policies is to improve the quality of the environment.

Performance objectives

The key objective of the environmental policy is to improve quality of the environment in order to protect health of the population, to avoid loss of biodiversity and ecosystems, to avoid environmental risks and to support market with secondary raw materials. Considering the complexity of environmental issues, the results will be monitored using a set of indicators. The purpose is to improve the effectiveness and thus get closer to the EU average.

FIGURE 44: Performance indicators for environmental issues



Source: MF SR, MŽP SR

Fiscal objectives

Investment expenditures will be derived mainly from drawdown of financial funds from the Operational Programme Quality of Environment (OP QoE). During the programming period 2014 – 2020, €3.1bn plus co-financing are available to finance the objectives. The cost-benefit analysis will examine environmental investment projects financed from the state budget and from EU funds with the aim to prioritize those bringing the highest value for money.

Efficiency and target-orientation of expenditures for waste, sewage water, reduction of pollution, nature and landscape protection and water supply will be evaluated, with the aim to reallocate expenditures towards programmes with the highest effectiveness. The review will seek ways to reduce operating costs of the Ministry of Environment, its subordinate organisations, state-owned enterprises established by the Ministry and the Environmental Fund.

Responsibility and deadlines

The interim and final reports fall under the responsibility of the MF SR; the report is to be prepared in cooperation with the Ministry of the Environment SR. For the purpose of preparation of analysis of the above mentioned issues, MŽP SR and MF SR undertake to cooperate in providing complete and detailed data and information. The interim report will be prepared by the end of April 2017, the final report will be prepared and published by the end of June 2017.

IV. Comparison with the Stability Programme

The Stability Programme was based on data from the Ministry of Finance's macroeconomic forecast from February 2016. It anticipated GDP growth of 3.2 per cent in 2016 and 3.6 per cent in 2017. The present forecast of the Ministry of Finance from September 2016, which was used for compilation of the draft general government budget, assumes higher economic growth in 2016 (3.6 per cent) and a slightly lower growth in 2017 (3.5 per cent). It is expected that in the following years the growth will accelerate to reach 3.9 per cent in 2018 and 4.4 per cent in 2019.

TABLE 19: Forecast of selected economic development indicators in SR

No.	Indicator		Stability Programme				Draft budget			
		unit	2016	2017	2018	2019	2016	2017	2018	2019
1	GDP, current prices	bn eur	80.6	84.8	90.2	96.4	80.5	84.0	88.5	94.2
2	GDP, permanent prices	per cent	3.2	3.6	4.1	4.6	3.6	3.5	3.9	4.4
3	Final consumption of households and non-profit institutions serving households (NISD)	per cent	3.2	2.6	2.7	2.9	2.9	2.5	2.7	2.9
4	Final general government consumption	per cent	-0.6	2.1	1.3	0.8	1.8	1.7	1.3	1.1
5	Gross fixed capital formation	per cent	0.9	1.4	0.9	2.0	-0.1	4.0	0.5	2.0
6	Export of goods and services	per cent	4.9	6.1	7.5	8.5	5.5	5.8	7.3	7.7
7	Import of goods and services	per cent	3.6	4.6	5.8	6.6	4.2	4.9	5.8	6.3
8	Average monthly wage in the economy (nominal growth)	per cent	3.3	4.5	4.7	5.1	2.8	3.5	4.3	4.8
9	Average employment growth, Labour Force Sample Survey, LFSS	per cent	1.4	1.0	1.2	1.0	2.8	1.5	1.1	1.0
10	Average employment growth by ESA 2010	per cent	1.3	0.9	1.1	0.9	2.1	1.5	1.0	0.9
11	Average unemployment rate by LFSS	per cent	10.4	9.5	8.3	7.3	9.8	8.5	7.4	6.4
12	Average registered unemployment rate	per cent	10.3	9.3	8.2	7.2	9.8	8.4	7.3	6.3
13	Harmonised index of consumer prices (HICP)	per cent	0.2	1.6	2.1	2.2	-0.5	0.9	1.6	1.9
14	Current account balance (percentage of GDP)	per cent	-0.5	0.2	1.0	2.6	-0.7	-0.3	0.5	1.4

Source: MF SR

Compared with the Stability Programme the general government balance in 2015 should improve on the basis of the data sent to Eurostat as part of the autumn EDP notification, caused mainly by the update of revenues from the corporate income tax. The draft budgetary objectives for 2017 - 2019 remain unchanged compared to the assumptions of the Stability Programme.

TABLE 20: Comparison with the Stability Programme

	ESA code	2015	2016	2017	2018	2019
		per cent of GDP	per cent of GDP	per cent of GDP	per cent of GDP	per cent of GDP
Target general government balances	**B.9**					

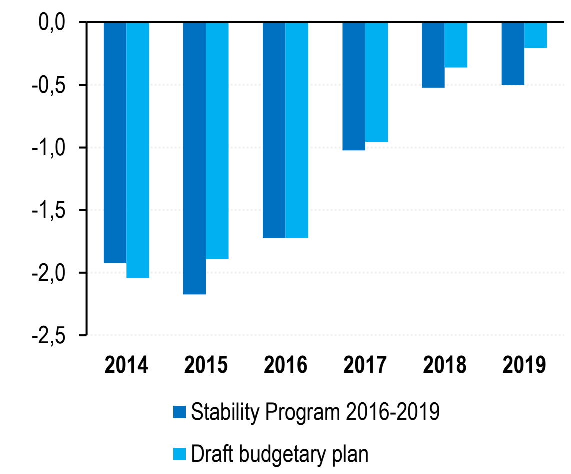
Stability Programme (1)		-2,97	-2,13	-1,29	-0,44	0,16
Draft budgetary plan (2)		-2,73	-1,97	-1,29	-0,44	0,16
Difference (2-1)		**0,24**	**0,16**	**0,00**	**0,00**	**0,00**
General government balances under NPC scenario	**B.9**					
Stability Programme (1)		-	-	-0,92	-0,67	-0,09
Draft budgetary plan (2)		-	-	-0,29	-0,04	0,55
Difference (2-1)		**-**	**-**	**0,63**	**0,63**	**0,64**

Source: MFSR

Since the publication of the Stability Programme for 2016 - 2019, the data on the output gap which enter into calculation of the structural balance, have been updated. Compared to prior estimates in the EC methodology, over the horizon of years 2013 – 2016, the economy was, on average, similarly undercooled. A significant revision took place at the end of the forecasted period in years 2018 and 2019. Unlike the expectations from the Stability Programme, the economy will only start overheating in 2019, and the overheating will be milder than expected.

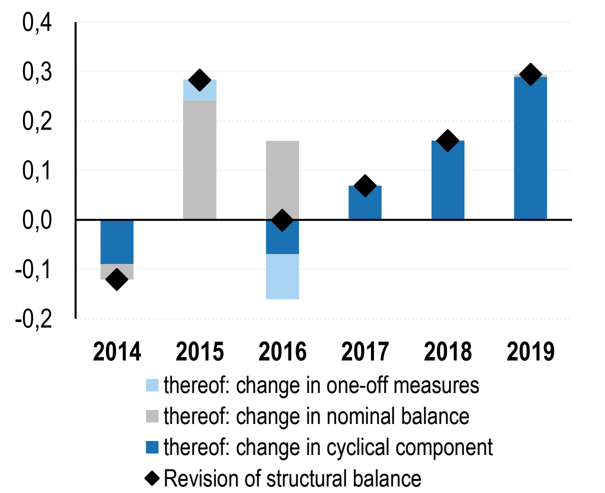
The Draft Budgetary Plan confirmed the nominal objectives defined in the Stability Programme for years 2016 - 2019. Compared to the Stability Programme, a positive change was noted in the nominal balance (better tax revenues). The change was fully neutralised by the updated cyclic component and the newly classified one-off effects. Despite the above described development, it is expected that the required fiscal consolidation with the MTO will be achieved in 2019.

FIGURE 42: Comparison of structural balance under Stability Program and the Draft Budgetary Plan



Source: MF SR

FIGURE 43: Contributions of factors to revision of the structural balance



Source: MF SR

ANNEXES

Annex 1: One-off measures for the purposes of calculating the structural balance

Methodology of the European Commission (EC) [56] characterizes one-off measure as a temporary measure which is not of a permanent nature and which arose independently of government decisions. EC developed a Directive for classification of one-off measures:

Principle 1: Only temporary and non-recurring impact on general government revenues or expenses can be classified as a one-off.

Principle 2: One-off nature cannot be decreed by law or by an autonomous government decision.

Principle 3: Volatile components of revenue and expenditure should not be considered one-off. Smoothing of time series is done using the cyclical component in calculation of the SB.

Principle 4: Deliberate policy actions that increase the deficit cannot be classified as one-offs.

Principle 5: Only measures with a significant impact on general government budget (higher than 0.05 per cent of GDP) should be classified as a one-offs.

All typical one-off measures are described in Chapter 3.3 (Report of Public Finances in EMU[57]). Moreover, EC has defined as specific exceptions and procedures thereto, as to when a one-off measure can be classified as an impact which contradicts the aforementioned principles; such examples are also provided in the aforementioned chapter.

As at the date of preparation of the Draft Budgetary Plan, the following one-off measures were identified for years 2016 – 2019:

TABLE 21: One-off and temporary measures (ESA 2010, EUR mil.)

	2014	2015	2016	2017	2018	2019
Digital dividend	164	-	-	-	-	-
Penalty by Anti-Monopoly Office for a building cartel	45	-	-	-	-	-
Contribution to EU budget	58	-	-	-	-	-
Old-age pensions paid to armed forces	-58	-	-	-	-	-
Contribution to National Resolution Fund	-	-34	34	-	-	-
Correction of the contribution to EÚ budget	-	-	40	-	-	-
Correction EÚ funds	-209	-243	-	-	-	-
TOTAL	**-1**	**-277**	**74**	**0**	**0**	**0**

(+) improving the balance, (-) worsening the balance *Source: MF SR*

Despite the conflict with Principle 5 (the rule of impact above 0.05 per cent of GDP) of the EC Directive, considering the horizontal nature (applicable to all countries), the following can be classified as one-offs:

- Contribution to the National Resolution Fund
- Correction of the contribution to EU budget

In 2016, corrections to EU funds cannot be classified as one-offs (BOX 2).

[56] Vade Mecum on the Stability and Growth Pact – 2016 Edition – Guiding principles page 28.
[57] Report on Public Finances in EMU, December 2015: http://ec.europa.eu/economy_finance/publications/eeip/pdf/ip014_en.pdf.

Annex 2: Measures included in the draft general government budget (ESA 2010, vs NPC)

TABLE 22: Impact of legislative measures on tax and security contributions revenues of the GG (per centGDP, ESA 2010)

	Subsector	ESA2010	2017	2018	2019
Act No. 595/2003 Coll. on income tax			-0.19	-0.14	-0.15
Personal income tax	S.1311	D.51A	-0.02	-0.02	-0.01
Personal income tax from employment	S.1311	D.51A	0.00	0.00	0.00
Personal income tax from self-employment	S.1311	D.51A	-0.02	-0.02	-0.01
- thereof: municipalities	S.1313	D.51A	0.00	-0.02	-0.01
- thereof: higher territorial units	S.1313	D.51A	0.00	-0.01	0.00
- thereof: state	S.1311	D.51A	-0.02	0.02	0.00
Corporate income tax	S.1311	D.51B	-0.17	-0.17	-0.17
Withholding tax	S.1311	D.51E	0.00	0.06	0.06
Social security contributions	S.1314	D.61	0.00	0.00	-0.01
Health insurance	S.1314	D.61	0.00	-0.01	-0.01
Act No. 253/2010 Coll. on a special levy on business activities in regulated sectors			0.20	0.19	0.14
Corporate income tax	S.1311	D.51B	-0.05	-0.05	-0.04
Special levy on regulated sectors			0.25	0.25	0.18
Act No. 384/2011 Coll. on a special levy on selected financial institutions			0.06	0.06	0.06
Corporate income tax	S.1311	D.51B	-0.02	-0.02	-0.02
Special levy on financial institutions	S.1311	D.29H	0.08	0.07	0.07
Act No. 222/2004 Coll. on value added tax			-0.01	0.00	0.00
VAT	S.1311	D.211	-0.01	0.00	0.00
Act No. 106/2004 Coll. on excise duty on tobacco products			0,04	0.04	0.07
Excise duty on tobacco	S.1311	D.214A	0.03	0.03	0.06
VAT	S.1311	D.211	0.01	0.01	0.01
Act No. 171/2005 Coll. on gambling	S.1311	D.214F	0.02	0.02	0.02
Act No. 145/1995 Coll. on administrative fees	S.1311	D.29/D.59	0.00	0.00	0.00
Act No. 39/2015 Coll. on insurance	S.1311	D.29	0.05	0.06	0.06
TOTAL			**0.17**	**0.23**	**0.20**

Annex 3: Assumptions underlying quantification of legislative effects

Reduction of the CIT rate to 21 per cent (Amendment of Act No. 595/2003 Coll.)

The quantification of the impact is based on the present estimate of the tax revenue for 2015 and the estimated revenue for 2016 - 2019. We applied a simple calculation of the transition from the 22 per cent rate to 21 per cent rate, excluding any dynamic effects.

Prolongation of the special levy on selected financial institutions (Act No. 384/2011 Coll.)

The quantification of the revenue from prolongation of the special levy on selected financial institutions is determined by actual tax base values available for Q2 2016. The tax base is defined as a sum of banks' liabilities excluding equity less subordinated debt. The revenue until 2019 has been estimated based on assumed development of the volume of deposits based on the latest forecast of the Committee.

Changes in the special levy on business activities in regulated sectors (Act No. 253/2010 Coll.)

Presently, 64 companies meet the key requirement for payment of the levy on revenues generated from above 50 per cent regulated activities. In 2015, the obligation to pay the levy applied to 40 companies whose total profit exceeded EUR 3 mil. The remaining 24 companies did not pay the levy as their profits were lower than EUR 3 mil.

The new legislation does no longer apply the requirement of 50 per cent of revenues from regulated activities, the only eligibility criterion is to generate a profit equal to EUR 3 mil. or higher. Under the new rules, the levy will only be charged on revenues from local regulated activities and the present reduction of the assessment base to EUR 3 mil. will be cancelled. The levy rate will be doubled (0.726 per cent), effective from 2019 it will go down to 0.545 per cent and in 2021 it will return to the present level. Thus, regulated entities, whose total profit exceeds the EUR 3 mil. threshold will be obliged to pay the levy on every euro of revenues generated from regulated activities.

In 2014, 504 companies reported profits higher than EUR 3 mil., which is the maximum potential for the number of companies to qualify for levy on regulated activities. The cancellation of the EUR 3 mil. tax base requirement has a positive impact on the quantification, on the other hand, a partly compensating effect has the change to charging the levy on regulated activities only. The quantification is based on the latest forecast of the regulated levy and individual data of the affected entities.

TABLE 23: Quantification of changes in special levy on business activities in regulated sectors since 2017 (EUR mil)

	2016F	2017F	2018F	2019F
Present estimate of revenue from the special levy(SL) (Sep. Committee)	**95.1**	**96.8**	**99.5**	**102.9**
1. Increased number of payers (cancellation of the 50 per cent		15.3	15.7	16.3
2. Transition to tax base on regulated activities		-11.5	-11.8	-12.2
3. Elimination of the EUR 3 mil. deduction from the tax base		5.2	5.4	5.5
Impact on SL in reg. sector (0.00363 rate)	**95.1**	**105.8**	**108.8**	**112.5**
- thereof: net effect on general government (CIT expenditure)	74.2	83.6	85.9	88.8
Impact on SL in reg. sector under changed rate	**-**	**211.6**	**217.5**	**168.7**
- thereof: net effect on general government (CIT expenditure)	**-**	**167.2**	**171.8**	**133.3**

Introduction of tax on dividends and cancellation of health insurance contributions on dividends (Act No. 595/2003 Coll.)

The data source is the amount of paid out dividends from records kept by health insurance companies and the data on primary distribution of pensions from the Statistical Office SR. Based on the records kept by health insurance companies, in 2014, the value of paid out dividends was indexed by the actual development of profitability in 2015 and 2016, or GDP growth since 2017. The quantification takes account of the gradually received payments of health insurance contributions on dividends paid out from retained earnings for 2011 - 2012 tax periods at 10 per cent rate and 2013 - 2016 at a 14 per cent rate up to the amount of the maximum assessment base. Another consequence of the cancellation of the health insurance contributions on profits distributed since 2017 is the dropout of the initially budgeted revenues from health insurance contributions. A positive risk of the quantification is the resulting rate of the withholding tax on dividends has been determined considering the reduced rate (7 per cent vs. 19 per cent or 25 per cent) on dividends from retained earnings from periods before 2003.

TABLE 24: Quantification of changes in taxation of dividends (EUR mil.)

	2015	2016	2017	2018	2019
Withholding tax on dividends 7 per cent	-	-	-	56	59
Cancelled health insurance contributions (HIC)	-	-	-	-19	-20
Accrued HIC from previous years	23	19	16	13	11
Estimated revenue (net effect)	**23**	**19**	**16**	**50,5**	**50,3**

Increase in lump-sum expenses (Act No. 595/2003 Coll.)

The quantification was done using individual tax returns of sole traders for years 2013 and 2014, data from the Social Insurance Company for 2015 and data from the Register of VAT Payers for 2015. Only sole traders who are not VAT payers can claim lump-sum expenses. Therefore, all sole traders registered as VAT payers (both mandatory and voluntary registrations) have been excluded from the quantification. The quantification assumes that sole traders claim deduction of lump-sum expenses only if it results in reduction of their tax liability in the amount equal to or higher than the present claiming of actual expenses. The increase in lump-sum expenses in the first year will decrease the revenue from personal income tax, which is the revenue of the local government. In the following years, it will also have a negative impact on revenue from social and health insurance contributions, which are paid by sole traders in arrears.

Contributions to the Resolution Fund becoming a tax expense (Act No. 595/2003 Coll.)

The quantification of reclassification of the contribution to the Resolution Fund as tax expenses is based on the amount of protected and covered deposits in the banking sector and their anticipated growth.

Introduction of interest charges on retained VAT refunds above the scope of tax review (Act No. 222/2004 Coll.)

The quantification of the effects was based on data on paid VAT refunds for 2015. The data was used for development of a VAT refund distribution schedule by number of months from the standard deadline for payment of the VAT refund. The interest rate was applied on VAT refunds where the delay exceeded the statutory deadline.

Increased rates of excise duty on tobacco products (Act No. 106/2004 Coll.)

The rates will be increased in two steps, as at 1 February 2017 and as at 1 February 2019. The quantification is based on the assumption that there will be an average increase in the price of a cigarette packet by 10 cents (3.2 per cent), thereof 8 - 9 cents attributable to higher taxes (excise duty on tobacco and VAT) and 1 - 2 cents for sales margins. The above described assumption is derived from historically observed changes in tax rates in the Slovak Republic, as each change in tax rate was associated with rounding of cigarette packet consumer price to the nearest ten eurocents. Aggregated tax returns for 2015 indicate that 6 839 mil. pieces of cigarettes were released to tax free circulation. After both above assumptions are reflected in the calculation, the average final price per cigarette packet is expected to increase to EUR 3.20. For tobacco, cigars and cigarillos, the data underlying the quantification were taken from aggregated tax returns for 2014, owing to frontloading in 2015. The effect of prolongation by 1 year of the clearance sale of cigars and cigarillos will have a negative effect on tax revenues in 2017 in the amount of EUR 0.3 mil. (The estimate is based on data reported by importer and distributors of cigars and cigarillos). The effect on tax revenues of the tax on new tobacco products has not been estimated as these are new issues and also owing to absence of available statistical data. This is expected to have only a marginal effect over the forecasted horizon.

Re-assessment of the amount of levies (Amendment of Act No. 171/2005 Coll. on Gambling Games) and administrative fees on operation of gambling games (Amendment of Act No. 145/1995 Coll. on Administrative Fees)

The quantification is based on actual number of gambling machines. The increase in the levy will result in reduction of the number of gambling machines which will be fully replaced by video games. The total number of machines is recently growing and video games a more-than-equal substitute for gambling machines. Replacement of gambling machines by video lotteries has already been observed since 2008.

Amendments to vehicle registration fee (Amendment of Act No. 145/1995 Coll. on Administrative Fees)

The quantification used data from the Police Database SR, Ministry of Interior SR and selected sellers of used cars, and the final amount of the fee has been scaled depending on the age of the vehicle and the vehicle performance parameters. This approach is applied consistently to every vehicle irrespective of whether it has been purchased in Slovakia or imported. Vehicles with alternative drive systems (hybrid, electric vehicles, CNG, LNG) are subject to 50 per cent discount on fees, with a EUR 33 limitation on the discount. The resulting fiscal effect is neutral compared to the present state.

Special taxation scheme applied to insurance companies (Amendment of Act No. 39/2015 Coll. on Insurance)

The quantification is based on data provided by the National Bank of Slovakia on paid insurance premium by type of insurance; the 8 per cent rate is introduced only for non-life insurance (excluding mandatory third-party liability insurance, where the 8 per cent charge already exists).

Annex 4: Mandates for revisions of public expenditures

Mandates for revision of expenditures for labour market policies and social policies

The revision on expenditures for labour market policies and social policies of the Ministry of Labour, Social Affairs and Family and the Social Insurance Company, in the annual amount of 11.5 per cent of GDP, will be focused on potential improvement of efficiency and improving of efficiency and directness of policies, in particular, with regard to expenditures for social transfers and insurance, pensions, social services, employment policies and operation and investments of the Ministry, its agencies and the Social Insurance Company, while maintaining the budgeted level of expenditures. The objective is to increase the employment rate and to reduce the proportion of population affected by poverty. The revision will be linked to the pilot assessment of expenses incurred by local offices for labour, social and family affairs.

Performance objectives

The key objectives of the Slovak government in employment and social policies is to increase the employment rates and to reduce the proportion of population affected by poverty. Slovakia has achieved a significant improvement in both aforementioned indicators since 2010, however, it still has not met the objectives set in the National Reform Programme SR and/or on Europe 2020 Strategy, and is below EU level. The performance indicators are largely linked to target-oriented assistance to the beneficiaries (mothers, families, the disabled, the unemployed, persons in material need and socially disadvantaged communities). The purpose of the revision will also be to improve consistency of the social insurance and pension system and to increase motivation to work and pay social security contributions. Consideration will also be given to sustainability of the system and the balanced intergeneration solidarity. The improved efficiency of public expenses incurred by **the Ministry of Labour, Social Affairs and Family and the Social Insurance Company** will contribute to meeting the government's goals in social and employment policies.

TABLE 25: Performance indicators for labour market and social policies

		2009	2010	2011	2012	2013	2014	2015	Target 2020
Long-term unemployment rate	**SK**	6.5	9.3	9.3	9.4	10.0	9.3	7.6	3.0
(per cent active population above 15 years)	**EU**	3.0	3.8	4.1	4.7	5.1	5.1	4.5	-
Employment rate	**SK**	66.4	64.6	65.0	65.1	65.0	65.9	67.7	72.0
(per cent in 20 - 64 age group)	**EU**	69	68.6	68.6	68.4	68.4	69.2	70.1	75.0
Reduction of poverty by soc. transfers	**SK**	24.9	26.2	25.3	24.7	25.2	25.4	25.8	-
(p.p.)	**EU**	26	27	27.1	27.1	27.7	27.5		-

Source: MF SR, MLSA&F SR

Fiscal objectives

The purpose of the revision will be to assess expenditures of the Ministry of Labour Social Affairs and Family SR (MLSA&F) and the Social Insurance Company focusing on higher efficiency of current expenditures and analysis of economic benefits and the planned investment costs, while maintaining the budgeted level of expenditures. Draft reallocation of expenditures will be prepared for programmes with the highest efficiency. The expenditures for projects implemented from EU funds under the programming period 2014 – 2020 should be used evenly until 2020.

Areas subject to revision

Major areas subject to revision include: social benefits and contributions, social insurance and pensions, social services, employment policies and operation and investments of the Ministry, its agencies and the Social Insurance Company. Additionally, the revision will be focused on issues analysed by types of beneficiaries, such as mothers, families, the disabled, the unemployed, persons in material need and socially disadvantaged communities. The revision is to assess the operation of the pension saving system in view of the "value for money" principle, including possible implementation of annual statement social insurance account.

Responsibilities and deadlines

Interim and final reports are the responsibility of the MF SR; the report is to be prepared in cooperation with the Ministry of Labour Social Affairs and Family SR (MLSA&F). For the purpose of preparation of analysis of the aforementioned issues, MLSA&F SR and MF SR undertake to cooperate in providing complete and detailed data and information. The interim report will be prepared by the end of April 2017, the final report will be prepared and published by the end of June 2017.

Mandate for revision of expenditures for regional schools and universities

The revision of expenditures for regional schools and universities will assess annual expenditures in the amount of 2.7 per cent of GDP. The revision will be linked to the prepared National Program for Development of Education and Upbringing aiming to efficiently allocate additional funds directed to education. In regional education, the revision will be focused in particular on optimization of the network of schools (and will be linked to the pilot evaluation of the primary school network), an increasing the attractiveness of teaching profession including the compensation system. The revision identifies instruments to improve inclusion and equality in education including pre-school education. In university education, the revision will reassess the accreditation process and the method of financing and evaluation of results of university science. It will examine the system for monitoring of successful placement of high school and university graduates on the labour market. The revision will reassess the compliance between the structural funds programming activities and the identified priorities of the department.

Performance objectives

The key objective in regional education is to provide children and students with access to education irrespective of their social situation to enable them to gain education, competences and skills, and to teach them how to develop and cultivate their personalities and to gain and encourage their respect to human rights and basic freedoms. In case of universities, their mission is to develop harmonic personalities, knowledge, wisdom, goodness and creativity in people and to contribute to development of education, science, culture and health for the benefit of the whole society and thus contribute to building the knowledge society.

Performance indicators for regional schools, universities including science are given below:

TABLE 26: Performance indicators for regional schools and universities

		2009	2010	2011	2012	2013	2014	2015	Target 2020
PISA	**SK**	488,1			472				505
(average of achieved score	**OECD**	496,7			497				-
Early termination of school attendance	**SK**	4,9	4,7	5,1	5,3	6,4	6,7	6,9	6,0
(per cent in 18 - 24 age group)	**EÚ**	14,2	13,9	13,4	12,7	11,9	11,2	11,0	10,0
per cent of population with university education	**SK**	17,6	22,1	23,2	23,7	26,9	27	28.4	40
(per cent in 30 - 34 age group)	**EU**	32,3	33,8	34,8	36,0	37,1	37,9	38,7	40
PIAAC score	**SK**								
(average score, 16-29 cohort)	**OECD**								
Citation response to publication	**SK**								
(normalized citation index)	**OECD**	1	1	1	1	1	1		
Research grants from abroad won by Slovak universities (EUR mil.)	**SK**	6,0	6,2	6,1	5,0	5,9	5,7		

Source: MF SR, MŠVVŠ SR

Fiscal objectives

Total amount of the increase in public funds to be used in education and upbringing for this election period will be EUR 2 bn in accordance with the Policy Statement of the Government. By the end of the election period, in 2020, the annual amount of public funds spent for education will be comparable to average of EU countries.

Responsibilities and deadlines

The interim and final reports will be prepared by MF SR in cooperation with the Ministry of Labour Social Affairs and Family SR (MLSA&F), they both undertake to cooperate in providing complete and detailed data and information for preparation of analyses of the above mentioned issues. The interim report will be prepared by the end of April 2017 and the final report will be prepared and published by the end of June 2017. MF SR will publish the final report and submit it to the meeting of the Slovak Government.

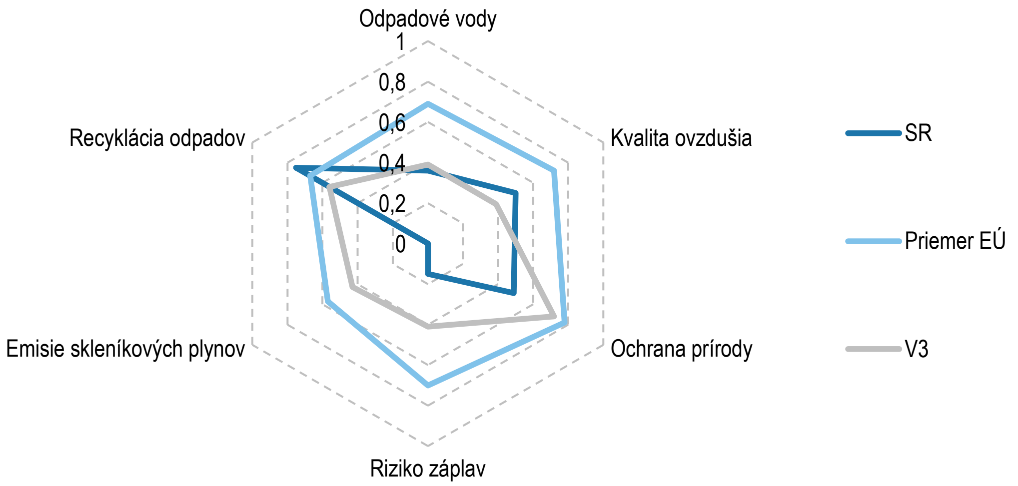
Mandate for revision of environmental expenditures

The revision of environmental expenditures in annual amount of 0.6 per cent of GDP will propose measures to improve efficiency of the investment portfolio, increasing effectiveness of environmental programmes and reduction of unit operating costs in a sustainable way in the Chapter of the Ministry of Environment SR. The objective of environmental public investments and policies is to improve the quality of the environment.

Performance objectives

The key objective of the environmental policy is to improve quality of the environment in order to protect health of the population, to avoid loss of biodiversity and ecosystems, to avoid environmental risks and to support market with secondary raw materials. Considering the complexity of environmental issues, the results will be monitored using a set of indicators. The purpose is to improve the effectiveness and thus get closer to EU average.

FIGURE 44: Performance indicators for environmental issues



Source: MF SR, MoE SR

Fiscal objectives

Investment expenditures will be derived mainly from drawdown of financial funds from the Operational Programme Quality *of* Environment (OP QoE), where during the programming period 2014 – 2020 EUR 3.1 bn plus co-financing are available to finance the objectives. The cost-benefit analysis will examine environmental investment projects financed from the state budget and from EU funds with the aim to give priority to those bringing the highest value for money.

Subject to evaluation will be efficiency and target-orientation of expenditures for waste, sewage water, reduction of pollution, nature and landscape protection and water supply with the aim to reallocate expenditures for programmes with the highest effectiveness. The revision will seek ways to reduce operating costs of the Ministry of Environment, its subordinate organisations, state-owned enterprises established by the Ministry and the Environmental Fund.

Responsibility and deadlines

The interim and final reports are the responsibility of the MF SR; the report is to be prepared in cooperation with the Ministry of the Environment SR (MoE SR). For the purpose of preparation of analysis of the aforementioned issues, MoE SR and MF SR undertake to cooperate in providing complete and detailed data and information. The interim report will be prepared by the end of April 2017, the final report will be prepared and published by the end of June 2017.

Annex 5: Required tables

Table 0i – Basic assumptions

	2015	2016	2017
Short-term interest rate (annual average)	0.0	-0.3	-0.3
Long-term interest rate (annual average)	0.8	0.5	0.7
Exchange rate USD/EUR (average)	1.1	1.1	1.2
World GDP growth	0.1	-0.2	0.0
Nominal effective exchange rate (change in per cent)	3.2	3.2	3.5
EA GDP growth	1.6	1.7	1.5
Growth of relevant foreign markets	2.2	1.9	2.0
World imports growth in constant prices excl. EU	2.8	3.1	3.8
Oil price (Brent, USD/barrel)	48.3	40.1	46.0

Source: MF SR

Table 0ii – Key assumptions

	2015	2016	2017
1. External environment			
Oil price (€)	48.3	40.1	46.0
2. Fiscal policy			
Net lending/net borrowing of the general government	-2.7	-2.0	-1.3
Gross debt of the general government	52.9	53.5	52.7
3. Monetary policy, financial sector			
Interest rates:			
Euribor 3M (average)	0.0	-0.3	-0.3
Deposits	0.6	0.4	0.4
Yield from 10-year Slovak government bonds (average)	0.8	0.5	0.7
Balance of deposits (growth)	7.2	7.2	6.0
4. Demographic trends			
Economic-active population (growth)	-0.5	-0.6	-0.7
Total dependency ratio	41.4	42.4	43.7

Source: MF SR

Table 1.a – Macroeconomic overview

	ESA code	2015 Actual	2015 growth rate	2016 growth rate	2017 growth rate
1. Real HDP	B1*g	75.8	3.6	3.6	3.5
thereof					
1.1 estimated impact of aggregate budgetary measures on economic growth		-	-	-	-0.5
2. Potential GDP		76.5	2.9	2.8	3.0
contributions:					
- labour		-	0.2	0.2	0.1
- capital		-	0.7	0.9	0.9
- total productivity of factors		-	1.9	1.7	1.9
3. Nominal GDP	B1*g	78.1	3.3	3.2	4.3
Components of real GDP					
3. Final household consumption and NISH	P.3	40.2	2.4	2.9	2.5
4. Final consumption of general government	P.3	14.0	3.4	1.8	1.7
5. Gross fixed capital formation	P.51g	17.8	14.0	-0.1	4.0
6. Change in inventories and net acquisition of valuables (per cent of GDP)	P.52 + P.53		-0.1	0.0	-0.1
7. Exports of products and services	P.6	74.4	7.0	5.5	5.8
8. Imports of products and services	P.7	70.1	8.2	4.2	4.9
Contributions to real growth of GDP					
9. Total local demand		-	4.9	1.9	2.5
10. Change in inventories and net acquisition of valuables	P.52 + P.53	-	-0.2	0.0	-0.1
11. External balance of products and services	B.11	-	-0.6	1.5	1.2

Source: MF SR

Table 1.b – Price development

	ESA code	2015 Actual	2015 Growth rate	2016 Growth rate	2017 Growth rate
1. GDP deflator		1.0	-0.3	-0.4	0.7
2. Private consumption deflator		1.1	-0.1	-0.5	0.9
3. HICP		100.0	-0.3	-0.5	0.9
4. Public consumption deflator		1.1	0.8	1.7	1.7
5. Investment deflator		1.0	0.0	-0.2	0.9
6. Export price deflator (goods and services)		1.0	-1.4	-1.1	0.7
7. Import price deflator (goods and services)		1.0	-1.1	-0.9	0.9

Source: MF SR

Table 1.c – Labour market indicators

	ESA code	2015 Actual	2015 Growth rate	2016 Growth rate	2017 Growth rate
1. Employment, persons (thousands) [1]		2 267	2.0	2.1	1.5
2. Hours worked (mil.) [2]		3 977	1.7	2.0	1.4
3. Unemployment rate (per cent) [3]			11.5	9.8	8.5
4. Labour productivity, per person (EUR) [4]		33.432	1.6	1.4	2.0
5. Labour productivity, per hour (EUR) [5]		19	1.9	1.5	2.1
6. Compensation for employees (EUR mil.)	D.1	29 942	4.9	4.4	5.3
7. Compensation per employee (EUR)		15 406	2.4	1.9	3.8

[1] Occupied population, domestic concept national accounts definition

Source: MF SR

[2] National accounts definition

[3] Harmonised definition, Eurostat; levels

[4] Real GDP per person employed

[5] Real GDP per hour worked

Table 1.d - Sectoral balances (ESA 2010, per cent of GDP)

	ESA code	2015	2016	2017
1. Net lending to/net borrowing from rest of the world	B.9	2.3	0.5	0.9
thereof:				
- Goods and services		2.5	3.4	4.0
- Primary income and transfers		-3.8	-4.1	-4.3
- Capital account		3.6	1.2	1.3
2. Net lending to/net borrowing from other sectors	B.9	5.0	2.5	2.2
3. Net lending to/net borrowing from general government	B.9	-2.7	-2.0	-1.0
4. Statistical discrepancy		0.0	0.0	0.0

Source: MF SR

Table 2.a: Development of the general government budget (per cent of GDP)

Net lending /borrowing (EDP B.9) general government subsectors	ESA code	2016 per cent of GDP	2017 per cent of GDP
1. General government	S.13	-2.0	-1.3
2. Central government	S.1311	-1.9	-1.6
3. Regional state government	S.1312	-	-
4. Local state government	S.1313	0.2	0.3
5. Social security funds	S.1314	-0.3	0.1
6. Interest expense	D.41	1.5	1.3
7. General government primary balance (1+6)		-0.5	0.1
8. One-off and temporary effects		0.1	0.0
9. Real GDP growth (per cent)		3.6	3.5
10. Potential GDP growth (per cent)		2.8	3.0
contributions:		2.8	3.0
- labour		0.2	0.1
- capital		0.9	0.9
- total productivity of factors		1.7	1.9
11. Output gap (per cent of potential GDP)		-0.9	-0.9
12. Cyclical component (per cent of potential GDP)		-0.3	-0.3
13. Cyclically-adjusted balance (1-12) (per cent of potential GDP)		-1.6	-1.0
14. Cyclically-adjusted primary balance (13+6) (per cent of potential GDP)		-0.1	0.4
15. Structural balance (13-8) (per cent of potential GDP)		-1.7	-1.0

[1] Adjusted for swap-related net 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 of the general government
[4] Including those collected by the EU

Source: MF SR

Table 2.b: Development of the general government debt (per cent of GDP)

	ESA code	2016	2017
1. Gross debt[1]		53.5	52.7
2. Change in gross debt		0.6	-0.8
Contributions to change in gross debt			
3. Primary balance		-0.5	0.1
4. Interest expense	D.41	1.5	1.3
5. Stock-flow adjustment		0.3	0.1
- Differences between cash and accruals		0.4	0.0
- Net accumulation of financial assets		0.5	0.0
thereof: privatisation proceeds		0.0	0.0
- Valuation effects and other		-0.6	0.2
p.m. Implicit interest rate		3.0	2.6
Other relevant factors			
6. Liquid financial assets		4.6	4.2
7. Net financial debt (1-6)		48.9	48.6
8. Debt amortization (existing bonds) since the end of the previous year		4,0	5.2
9. Percentage of debt denominated in foreign currency		3,6	3.4
10. Average maturity*		6.9	7.5

Note: maturity of the government debt at the end of the year

Source: MF SR

Table 2.c: Contingent liabilities (per cent of GDP)

	2015	2016	2017
Public guarantees	17.8		
thereof:			
Financial sector	0		

Source: MF SR

Table 3: General government expenditure and revenue projections according to the no-policy-change scenario (breakdown by components)

General government (S13)	ESA code	2016 per cent of GDP	2017 per cent of GDP	2016 mil. eur	2017 mil. eur
1. Total revenue	**TR**	**39.8**	**39.8**	**32 073**	**33 415**
thereof		-	-	-	-
1.1. Taxes on production and imports	D.2	10.8	10.9	8 688	9 138
1.2. Current taxes on income, wealth, etc.	D.5	7.8	7.7	6 257	6 489
1.3. Capital taxes	D.91	-	-	-	-
1.4. Social security contributions	D.61	14.3	14.2	11 521	11 942
1.5. Property income	D.4	0.7	0.7	579	548
1.6. Other		6.2	6.1	5 028	5 092
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)		32.9	32.6	26 466	27 396
2. Total expenditure	**TE**	41.8	39.6	33 659	33 281
thereof		-	-	-	
2.1. Compensation for employees	D.1	9.0	8.7	7 222	7 302
2.2. Intermediate consumption	P.2	5.6	5.1	4 512	4 245
2.3. Total social transfers	D.62, D.632	19.1	18.5	15 401	15 551
thereof: unemployment benefits		0.2	0.2	160	153
2.4. Interest expense	D.41	1.5	1.3	1 223	1 127
2.5. Subsidies	D.3	0.5	0.5	412	443
2.6. Gross fixed capital formation	P.51	3.1	3.0	2 457	2 506
2.7. Capital transfers	D.9	0.7	0.4	566	337
2.8. Other		2.3	2.1	1 867	1 770

Note: Data for 2016 express expected actual results.

Source: MFSR

[1] P.11+P.12+P.131+D.39r+D.7r+D.9r (excl. D.91r)

[2] D.29p + D.4p (excl. D.41p) +D.5p +D.7p +P.52+P.53+NP+D.8.

Table 4.a: General government expenditure and revenue targets (breakdown by components)

General government (S13)	ESA code	2016 per cent of GDP	2017 per cent of GDP	2016 EUR mil.	2017 EUR mil.
1. Total revenues	**TR**	**39.8**	**39.8**	**32 073**	**33 415**
thereof		-	-		
1.1. Taxes on production and imports	D.2	10.8	10.9	8 688	9 138
1.2. Current taxes on income, wealth, etc.	D.5	7.8	7.7	6 257	6 489
1.3. Capital taxes	D.91	0.0	0.0	0	0
1.4. Social security contributions	D.61	14.3	14.2	11 521	11 942
1.5. Property income	D.4	0.7	0.7	579	548
1.6. Other [1]		6.2	6.3	5 028	5 298
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)		32.9	32.8	26 466	27 569
2. Total expenditure	**TE**	**41.8**	**41.1**	**33 659**	**34 498**
thereof		-	-		
2.1. Compensation for employees	D.1	9.0	8.7	7 222	7 343
2.2. Intermediate consumption	P.2	5.6	5.6	4 512	4 717
2.3. Total social transfers	D.62, D.632	19.1	18.6	15 401	15 641
thereof: unemployment benefits		0.2	0.2	160	153
2.4. Interest expense	D.41	1.5	1.3	1 223	1 127
2.5. Subsidies	D.3	0.5	0.6	412	480
2.6. Gross fixed capital formation	P.51	3.1	3.4	2 457	2 841
2.7. Capital transfers	D.9	0.7	0.3	566	281
2.8. Other [2]		2.3	2.5	1 867	2 069

[1] P.11+P.12+P.131+D.39r+D.7r+D.9r (excl. D.91r)

Source: MFSR

[2] D.29p + D.4p (excl. D.41p) +D.5p +D.7p +P.52+P.53+NP+D.8.

Note: Data for 2016 express expected actual results.

Table 4.b: Amounts to be excluded from the expenditure benchmark

	2015 EUR mil.	2015 per cent of GDP	2016 per cent of GDP	2017 per cent of GDP
1. Expenditure on EU programmes fully matched by EU funds revenue	2 600	3.3	1.3	1.4
2. Cyclical unemployment benefit expenditure	11	0.0	0.0	0.0
3. Effect of discretionary revenue measures	109	0.1	-0.2	0.1
4. Revenue increases mandated by law	0	0	0	0

Source: MFSR

Table 4.c.i): General government expenditure on education, healthcare and employment

	2016		2017	
	per cent of GDP	per cent TGE	per cent of GDP	per cent TGE
Education	3.9	9.3	4	9.8
Healthcare	1.9	4.6	1.9	4.7
Employment	0.1	0.2	0.1	0.2

Note.: TGGE – *Total general government expenditure* . *Source: Eurostat*

Table 4.c.ii): General government expenditure according to the COFOG classification

Functions	COFOG code	2016		2017	
		per cent of GDP	per cent TGE	per cent of GDP	per cent TGE
1. General public services	1	5.5	13.2	5.5	13.5
2. Defence	2	1.1	2.5	1.1	2.7
3. Public order and safety	3	2.2	5.2	2.2	5.4
4. Economic affairs	4	5.2	12.4	4.9	11.9
5. Environmental protection	5	0.5	1.1	0.4	1.1
6. Housing and community amenities	6	0.5	1.3	0.5	1.1
7. Healthcare	7	1.9	4.6	1.9	4.7
8. Recreation, culture and religion	8	1.0	2.4	1.0	2.4
9. Education	9	3.9	9.3	4.0	9.8
10. Social security	10	20.0	48.0	19.5	47.4
Total expenditure	**TGE**	**41.8**	**100.0**	**41.1**	**100.0**

Note: *TGE – Total general government expenditure. The methodology of recording expenditures using the function classification may differ from country to country. As a result, data recognised under individual items in various countries differ (e.g. taxable and non-taxable pensions). COFOG classification does neither reflect expenditures realised through the taxation system (e.g. tax bonuses).*

Source: MF SR

Table 6.a: NRP response to specific recommendations for Slovakia

CSR	Measure	Objectives
1	In 2016, achieve the annual fiscal adjustment by 0.25 per cent of GDP and in 2017 by 0.5 per cent of GDP towards the MTO. Improve the cost-effectiveness of the healthcare sector. Take measures to increase tax collection.	
1	Payments for DRG groups	Introduction of a system of data reporting required for the correct calculation of the individual weights and the implementation of the system of payments for treatment, which takes into account the difficulty of diagnosis, complications and length of hospital stay (case-mix). This applies to in-patient facilities
1	Integration of healthcare provision	Clear definition of hospital types and the scope of the provided healthcare and better coordination of involvement of outpatient and inpatient facilities in individual phases of medical treatment.
1	Analytical capacities at the Financial Directorate of the SR	Establishing an analytical unit at the Financial Directorate of the SR
2	Improving activation measures for long term unemployed persons and other disadvantaged groups, including individualized services and tailored vocational training. Facilitate employment of women, in particular by improved availability of affordably priced and skilled care for children. Improving results in education by increasing attractiveness of teaching profession and encouraging Roma children from their early years to be participate in the mainstream education.	
2	New or innovated active labour market policies (ALMP)	Implementation of projects focused on disadvantaged groups of the unemployed at the labour market (long-term unemployed, low-skilled and people aged above 50). Labour offices will cooperate with non-public providers of employment services. A so-called "second chance for education" will be introduced in form of ALMP retraining and education tools.
2	Continuation of employment services reform	Technical modernization of provided employment services, e.g. establishing self-employment systems, building a monitoring system to evaluate progress in achieving objectives of employment policies and monitoring of clients' satisfaction. This will result in improving effectiveness of activities at regional labour offices and it will be enabled to clients to file various applications from home
	Extension of kindergarten capacities	Building of new and extension of the existing kindergarten capacities from EU funds, including in regions with marginalized Roma communities. Along with continued provision of childcare allowance in the new programming period 2014-2020 support will be provided to childcare facilities intended for children aged below 3 years.
3	Consolidate the system of management, encourage transition from tenders focused exclusively on price to procurement based on quality and improve prosecution of illegal practices in public procurement. Improve transparency, quality and effectiveness of HR management in general government – mainly by adoption of the new State Service Act –, and effectiveness of the judicial system. Adopt a comprehensive plan to eliminate administrative and regulatory obstacles for the business sector.	
3	New act on public service	The Government approved the bill of the state service. One of the objectives is the professionalization and depolitisation of state service. A State Service Board is to be established as an independent coordinating and monitoring body. Increasing transparency of tenders when hiring employees to state service vacancies.
3	Anti-Mailbox act	The Government approved the Anti-Mailbox act which is to increase the transparency in deals between the state and the private sector. Since January 2017 an obligation is established for companies to be registered in the register of partners of the public sector to disclose the ownership structure to the level of the ultimate beneficial owner.
3	Anti-corruption clause for effects	In the legislative process, an anti-corruption clause will be introduced for effects upon presentation of bills. For bills presented by MPs for the second reading, an obligation will be established that the bill shall be made subject to interdepartmental comment proceedings with involvement of public

Table 6.b: EU growth and employment objectives

Key EU2020 indicator	Measure	Objective
Employment	Continuation of employment services reform	Technical modernization of provided employment services, e.g. establishing self-employment systems, building a monitoring system to evaluate progress in achieving objectives of employment policies and monitoring of clients' satisfaction. This will result in improving effectiveness of activities at regional labour offices and it will be enabled to clients to file various applications from home
	New or innovated active labour market policies (ALMP)	Implementation of projects focused on disadvantaged groups of the unemployed at the labour market (long-term unemployed, low-skilled and people aged above 50). Labour offices will cooperate with non-public providers of employment services. A so-called "second chance for education" will be introduced in form of ALMP retraining and education tools.
Science and research	Reform in research and development financing	Comprehensive changes in system of grants and supports with focus on quality, concentration of funds for high-quality projects and encouraging cooperation with private sector. Systematic support provided to every phase of scientific exploration (basic research, applied research, experimental development at universities, sectoral research institutions, Slovak Academy of Science and businesses). Merging the financing agencies into Research Agency and Technological Agency.
Climate changes and power engineering	In 2012 greenhouse gas emissions in non- ETS sectors were by 6.3 per cent lower compared to 2005. Thus, the government considerably exceeded its commitment not to increase the emissions by more than 13 per cent.	
	In 2014 the proportion of energy from renewable sources in gross final consumption is 11.6 per cent. Thus, under the no-policy–change assumption, Slovakia will most likely exceed the existing 14 per cent target by 2020.	
	Support to use of renewable energy sources	The government will encourage development of electromobility by providing support to building the necessary infrastructure.
	Deciding on policies for reduction of greenhouse gas emissions	A more effective decision-making will be supported by preparation of the Environmental Strategy, Low-Carbon Strategy and Analysis of Meeting More Strict Reduction Goals by 2030. Overview of the reduction potential of various measures and estimated expenses for their implementation will be included in the Low-Carbon Strategy of Development until 2030. The purpose is to identify and to support the best cost-effective opportunities for reduction of emissions.
Education	Extension of kindergarten capacities	Building of new capacities and extension of the existing kindergarten capacities from EU funds, including in regions with marginalized Roma communities. Along with continued provision of childcare allowance in the new programming period 2014-2020 support will be provided to childcare facilities intended for children aged below 3 years
	Dual education	Support will be provided to activities focused on promotion of dual education and studies at technology-oriented branches of study.
	Salaries for teachers	Attractiveness of teaching profession will increase. Wage tariffs for teachers and professional staff at regional schools have been increased effective from September 2016 and in the following years it is expected that the salaries will further grow.
Poverty and social inclusion	Inclusive education at primary schools	Improving conditions at schools for students with special teaching and education needs, including pupils from socially disadvantaged communities. Special attention will be paid to examination of compliance with provisions of the amended School Act, which aims to prevent and avoid confusing special teaching and education needs resulting exclusively from socially disadvantaged communities for those resulting from health disadvantages.
	Inclusion of marginalized Roma communities	Implementation of a program to support education of children in their early childhood and program of assistance in settlement of land and legalization of residential buildings. Implementation of projects focused on supporting community centers an field social work in municipalities with Roma population