EXECUTIVE SUMMARY

On 24 April 2020, the Fiscal Council received the proposal for the Ordinance amending the Ordinance on the framework for the preparation of the general government budgets for the 2020–2022 period and the draft Stability Programme 2020 in order to assess their compliance with the fiscal rules. According to the assessment of the Fiscal Council of 17 March 2020, the COVID-19 epidemic constitutes exceptional circumstances, which, under Article 12 of the Fiscal Rule Act, allow a temporary deviation from the medium-term balance of public finances. In such circumstances, extensive and multi-stage fiscal measures are appropriate and necessary. The measures are more effective when they are appropriately targeted, timely and simple. Due to their extensive nature, they must be fully transparent and, with regard to fiscal sustainability, temporary and appropriately embedded in a credible medium-term framework. While recognising a high uncertainty of the depth and duration of the decline in economic activity and the actual fiscal effect of the accepted and the announced measures, we find that the measures adopted so far do not fully comply with the stated principles.

Slovenia has entered this crisis after years of relatively high economic growth and a general government surplus, but with a higher general government debt than prior to the financial crisis. Moreover, economic growth had already declined more than expected before the outbreak of the epidemic, while fiscal policy has been inappropriately expansionary over the past two years. Whether the current crisis is only temporary or if it becomes a structural crisis with long-term negative consequences for prosperity and fiscal sustainability depends on the effectiveness of the measures.

The Fiscal Council's assessments about the macroeconomic and fiscal projections are as follows:

- The economic situation is extremely uncertain, with all currently available projections indicating a considerable decline in economic activity in 2020. In the given circumstances, the uncertainties are, even more than usual, linked to long-term economic growth estimates and thus to the estimates of the level of the output gap. It is not known whether the current shock will be only temporary or whether the effects of the epidemic on the contribution of individual production factors to the economic potential will become more significant in the long-term and to what extent.
- The draft Stability Programme 2020 predicts a general government deficit of approximately 8% of GDP in 2020. This is due to lower revenue, mainly because of the decline in economic activity, and even more so to an increased expenditure resulting from the operation of automatic stabilisers and the measures to prevent the consequences of the epidemic. The general government debt is projected to exceed 80% of GDP by the end of 2020. In addition to the institutional framework and the measures at the Eurozone level that are currently contributing to maintaining favourable financing conditions, efficient measures for maintaining the economic potential could particularly contribute to the sustainability of the increased debt in the long-term.

The main findings regarding compliance with the applicable fiscal rules on the basis of the Framework proposal and the projections of the draft Stability Programme 2020:

- In 2020, declaring extraordinary circumstances provides for a temporary deviation from pursuing the medium-term balance of public finances; however, the part of the expenditure that is not temporary or related to the measures adopted to limit the consequences of the epidemic must remain in accordance with the applicable fiscal rules. Only in this case, remaining in accordance with the legislation, the temporary deviation will not compromise the medium-term fiscal sustainability.

- The projections in the submitted documents and thus the inputs determining the maximum permitted level of general government expenditure are exposed to significant risks. The Fiscal Council assesses that, according to the mathematical formula determined in the Fiscal Rule Act, the general government expenditure for 2020 that is projected in the Framework proposal and is not one-off or temporary or aimed at eliminating the consequences of the epidemic is too high; however, considering the high level of uncertainty, the regular expenditure projected in the Framework proposal could fall within the range that is still in accordance with the permitted maximum expenditure level arising from all the currently available data.

The received budgetary documents do not include all the measures to eliminate the consequences of the epidemic, since some of them are still in the process of adoption or preparation. The Fiscal Council does not assess the adequacy of measures but gives an assessment of their impact on public finances. Room for manoeuvre for expenditure that is not related to the epidemic also depends on this assessment. Its main findings are as follows:

- The content and the estimated scope of the measures are similar to those in other countries and address the direct social and economic consequences of the crisis in order to maintain the economic potential.

- The complexity of the measures may contribute to the delay and the efficiency of their implementation, thus increasing the risk of job losses that could be prevented with a simpler and faster implementation.

- A significant part of the measures includes lump-sum transfers to certain population groups that will have a smaller impact on maintaining the consumption level while the restrictive measures to contain the epidemic still apply than they would have at the exit from the crisis. Moreover, the conditions of entitlement to benefits for individual groups are unclear.

- While introducing extensive measures to eliminate the consequences of the epidemic, decision-makers must be aware that this will place a significant burden on public finances. The government will have to finance the measures by borrowing on financial markets or using predominantly debt instruments available at the EU institution level.

The received documents contain some shortcomings regarding the legislative provisions that could have negative consequences for the transparency of fiscal planning. According to the Fiscal Council, transparency should be one of the basic guidelines of economic policy-makers despite the current uncertainty, in particular considering significant fiscal consequences of the current situation:

- The Government of the Republic of Slovenia submitted the proposal for the Ordinance amending the Ordinance on the framework for the preparation of the general government budgets for the 2020–2022 period and the draft Stability Programme 2020 to the National Assembly and the Fiscal Council after the expiry of the deadlines determined by the Fiscal Rule Act. According to the Act, the draft documents should be submitted 20 days before the due date for submitting the Stability Programme to the European Commission, which is at the end of April and the National Assembly should adopt the framework five days before the end of April. The delay is somewhat understandable, since the new government was formed in mid-March and, in the following weeks, proceeded to adopt measures to mitigate the consequences of the epidemic, which are mostly included in both documents.

- The Public Finance Act stipulates that the Institute of Macroeconomic Analysis and Development (IMAD) elaborates and publishes the macroeconomic scenario for the preparation of fiscal projections in the Stability Programme. The draft Stability Programme 2020 did not comply with this stipulation, since the IMAD forecasts have not been published and the document contains only a limited part of the macroeconomic scenario. Since comprehensive forecasts, on the basis of which the general government revenue projections were prepared, are unavailable, the Fiscal Council cannot fully assess the latter, which, considering the current risks, raises additional doubts about their credibility.

- While, in accordance with the legislation, both submitted documents should provide the basis for medium-term budget planning and budget preparation for 2021, they only include assessments for 2020. Thus, formally they do not comply with the legal requirements for medium-term budget planning. The Fiscal Council anticipates that the expected further changes to the budgetary documents will set out an appropriate path towards the gradual rebalancing of public finances in the medium-term already this year. According to the Fiscal Council, the proposed solution of the Act on Providing Additional Liquidity to the Economy to Mitigate the Consequences of the COVID-19 Epidemic, which has not been adopted yet, providing that the government would not adopt a National Development Policy Programme and a medium-term fiscal strategy in 2020 and 2021, which are determined by the Public Finance Act, also means a deviation from a transparent medium-term budget planning.