REPUBLIC OF SLOVENIA
FISCAL COUNCIL

Assessment of compliance of the general government budgets with the fiscal rules in 2020

June 2021

Document no.: 30-3/2021/7

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SUMMARY

In accordance with the provisions of the Fiscal Rule Act, the Fiscal Council issued its Assessment of compliance of the implemented budgets of the general government sector with the fiscal rules in 2020. At the outbreak of the epidemic in March 2020, the Fiscal Council confirmed that the situation allowed a period of exceptional circumstances to be invoked. Over this period, the fiscal rules apply but the legislation permits temporary action and deviation from achieving medium-term balancing of public finances for measures related to mitigating the consequences of such an event, provided that their medium-term sustainability is not compromised. The assessment of the rules during the period of exceptional circumstances was therefore carried out on the basis of indicators that are also used in normal circumstances. Despite increased flexibility in the application of fiscal rules, it must be ensured that, even in exceptional circumstances, government expenditure is consistent with the established budgetary frameworks.

According to the Fiscal Council, the fiscal rules were mostly complied with in 2020. The national rule referring to the maximum allowable level of government expenditure was complied with in the past year. The minimum permitted level of structural balance under the EU rules (MTO) in 2020 was attained, considering the permitted deviation. Growth in general government expenditure, excluding one-off effects, was also below the limit permitted under the expenditure rule of the Stability and Growth Pact. Despite the favourable outcome in 2020, the average deviation of both the structural balance and the structural effort over a two-year period, which exceeded 0.25 pps of GDP according to current calculations, was exceeded due to the expansionary fiscal policy implemented in 2019. General government debt increased in 2020 contrary to the rules, which required it to decrease. The Fiscal Council did not assess the balance over the business cycle due to the temporary deviation from the medium-term balance permitted during a period of exceptional circumstances.

The framework for drawing up budgets was frequently and substantially adjusted and failed in its core function of setting the medium-term orientation of the fiscal policy. Last year it was amended twice, by a total of over EUR 3 billion. General government expenditure (excluding one-off effects) thus remained below the maximum level permitted under the current framework for drawing up budgets, including in terms of the current assessment of the output gap and one-off factors. Expenditure for individual public finance budgets, calculated using the cash flow methodology, were below the maximum permitted level of expenditure, considering the applicable budgetary framework.

Economic activity in 2020 was marked by a sharp drop. GDP declined by 5.5 %, which was less than expected at the start of the epidemic. A greater fall in GDP was prevented by an improvement in the epidemiological situation in the middle of the year, a successful adjustment of the economy to restrictive measures in the second wave of the epidemic at the end of the year and comprehensive measures to counter the impact of the epidemic on the economy. Together with the fall in economic activity and the functioning of automatic stabilisers, these also contributed to a general government deficit of 8.4 % of GDP, which was the second highest to date. Revenue decreased by 4.7% and expenditure increased by 14.9%. General government debt rose by 15.2 pps last year, reaching 80.8% of GDP at the end of the year. Approximately a quarter of this came from adjustments in balances and flows, mainly pre-financing of future borrowing, reflected in increased resources in the single treasury account of the general government.

The outbreak of the COVID-19 epidemic posed a major challenge for fiscal policy management, to which countries responded with large-scale measures, also because of the flexibility of formal fiscal frameworks. The scope of discretionary measures in Slovenia with a direct impact on the general government balance, estimated by the Ministry of Finance at 6% of GDP last year, was higher by about a half compared to the EU average. Estimates suggest that their short-term impact on cushioning the fall in economic activity was smaller than the EU average, as the fall in real GDP last year was similar to the EU average, despite the fact that the share of tourism in value added is lower in Slovenia than the EU average. Most discretionary measures were aimed at preserving jobs through subsidies, as in other countries. However, the main deviation from measures in other countries was the higher share of employee compensation (allowances for public employees) and social transfers (transfers to certain population groups). In all countries, job preservation measures significantly contributed to a smaller increase in unemployment, although in Slovenia it was slightly higher than the EU average; in addition, estimates of the short-term impact of measures on unemployment point to similar effectiveness.

Effectiveness, correct targeting and transparency should remain fundamental guidelines even when measures are taken when exiting the crisis. If measures are not only temporary, then they must maximise economic potential. No measures were adopted in 2020 to mitigate the expected adverse fiscal impacts of structural, particularly demographic pressures to which the economy and public finances will be exposed in this decade. On the contrary, some economic policy measures adopted in 2020 have even weakened the sustainability of public finances in the medium and long term.

Legislative basis

Pursuant to point 4 of paragraph two and point 3 of paragraph three of Article 7 of the Fiscal Rule Act (the ZFisP), the Fiscal Council is required to produce an assessment of compliance of the implemented budgets of the general government sector with the fiscal rules by 30 June of the current year for the previous year. On 31 March 2021, the Statistical Office of the Republic of Slovenia published the data on the *Main Aggregates of the General Government 2017–2020* according to the ESA methodology and on 19 April 2020 the *Report on the Excessive Deficit and Debt 2017–2020, 2021 Forecast*. The Fiscal Council also obtained data from the consolidated public finance balance sheet from the Ministry of Finance compiled under the cash flow methodology.

The legislation does not explicitly prescribe the method for assessing how the implemented budgets comply with the fiscal rules over the period during which exceptional circumstances are in force. When exceptional circumstances have been invoked, the assessment of the medium-term balance of public finances over the economic cycle, as defined by the ZFisP, is suspended if this does not jeopardise their sustainability in the medium term. Despite increased flexibility in the application of fiscal rules, even in exceptional circumstances, it must be ensured that government expenditure is consistent with the established budgetary frameworks. The assessment of the Stability and Growth Pact (SGP) rules in exceptional circumstances is purely indicative and is carried out on the basis of indicators also applicable under normal circumstances. The Fiscal Council used the approach verifying (i) compliance with the fiscal rules on the basis of the Stability and Growth Pact (SGP) and (ii) compliance with the national fiscal rules referred to in Article 3 of the ZFisP, including on the basis of an ex-post assessment of the maximum allowable level of government expenditure.

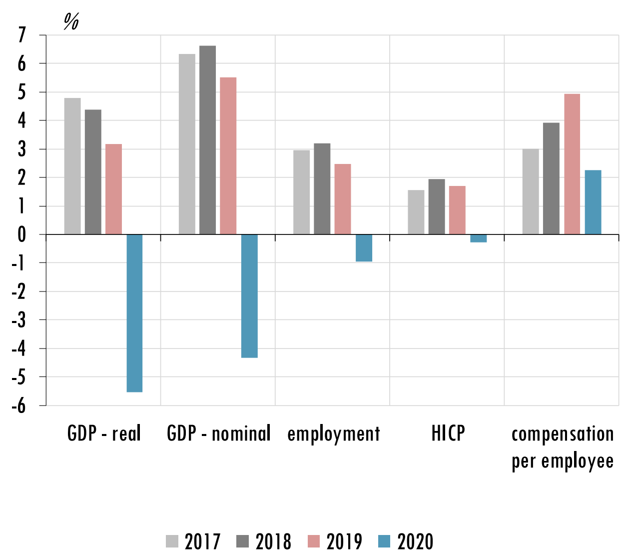
1. Macroeconomic and budgetary trends in 2020

1.1 The macroeconomic situation and assessment of the cyclical position of the economy

Last year's fall in economic activity was lower than forecast at the start of the epidemic, mostly due to part of the economy successfully adapting to restrictive measures during the second wave of the epidemic. In 2020, the GDP decreased by 5.5% in real terms, while the nominal fall was 4.3%. The latter was similar to that of the financial crisis a decade ago, but the structure of the fall was quite different. The nature of the restrictive measures to curb the epidemic meant that the total fall was mostly due to a fall in service sector activity, which was reflected in a 9.7% decrease in private consumption. Increased uncertainty and deterioration in business indicators contributed to a decline in investments in machinery and equipment, while construction investment, after increasing in the second half of the year, remained at the same level as before the epidemic. The volume of foreign trade decreased by around 7% on an annual basis, but it increased in the second half of the year as foreign demand recovered and companies adapted to the restrictive measures containing the epidemic. The latter holds particularly true for trade in goods, while in the last quarter of 2020, trade in services lagged behind the level recorded the year before by around 15%. Government consumption was the only aggregate of demand which increased last year, up to a similar extent as the year before. The general decline in economic activity also reduced all key tax bases, with the exception of compensation for employees or gross wages, which was also a major consequence of the nature of support measures and methodological effects.[1]

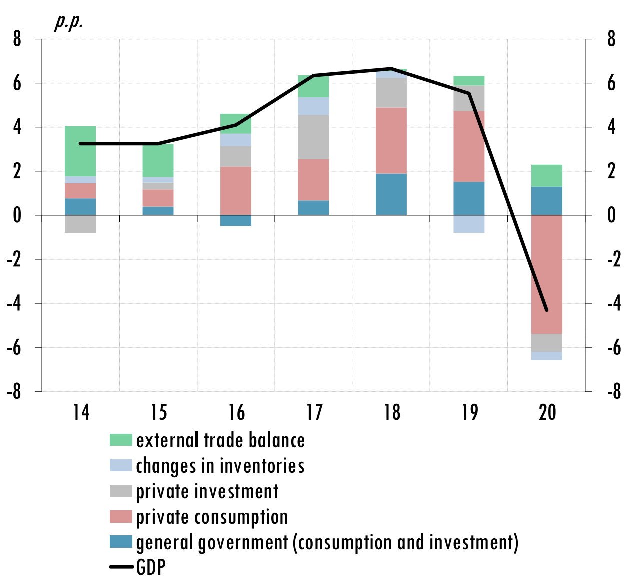
Based on various currently available output gap estimates and an overview of a broader set of indicators that determine the state of the economic cycle, the Fiscal Council estimates that the level of GDP in 2020 was below the level of potential product. Output gap estimates differ due to different methodologies and differences in input data; furthermore, they can significantly change over time or especially in the event of a major shock, as they are sensitive to major changes in economic growth forecasts (see Figure 1.3). Due to the extent of the current crisis, its heterogeneous impact on economic activity and, in particular, its possible long-term consequences, the assessments of the cyclical

Figure 1.1: Macroeconomic indicators



Source: SORS, Eurostat.

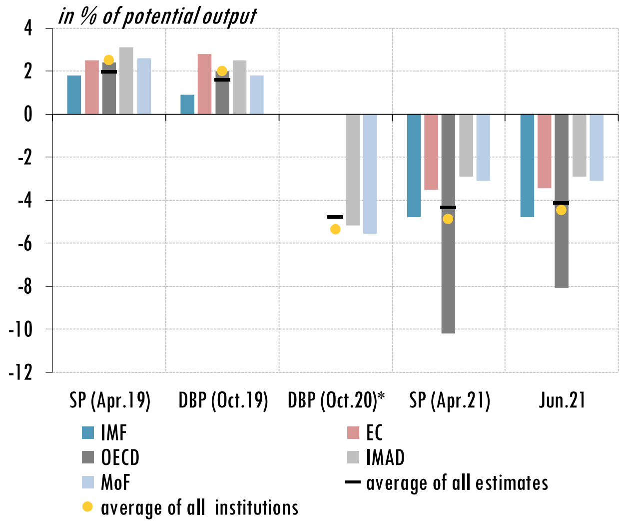
Figure 1.2: Contributions to nominal GDP growth



Source: SORS, FC calcuations.

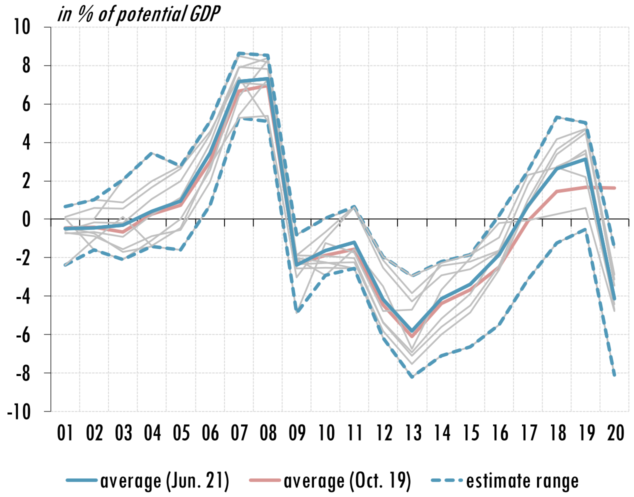
[1] For more information on the impact of methodological effects, see IMAD's Spring Forecast of Economic Trends 2021 (Box 1).

Figure 1.3: Output gap estimates for 2020 by documents



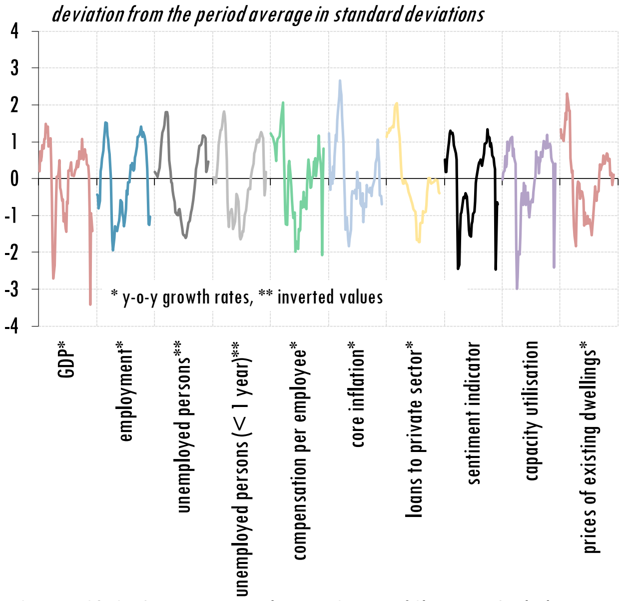
Source: EC, IMF, MoF, OECD, IMAD, FC calculations. *During the preparation of the assessment up-to-date estimates by IMF, EC and OECD were not available.

Figure 1.4: Output gap estimates



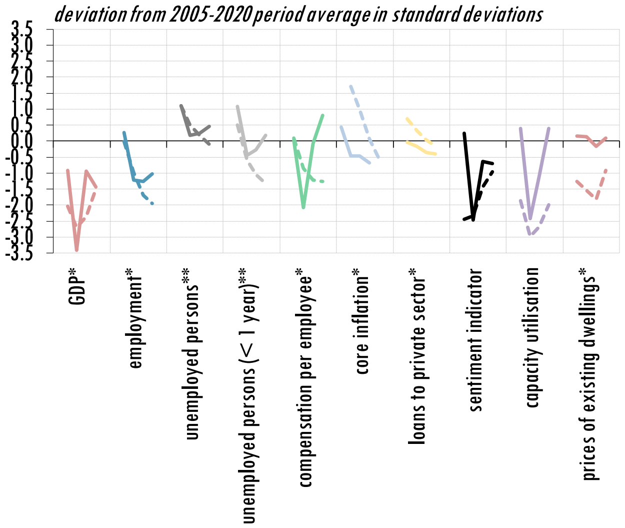
Sources: EC, IMF, MoF, OECD, IMAD, FC calculations. See note under Table 4.3 in Assessment of compliance of the Proposal of budgets of the Republic of Slovenia for 2020 and 2021 with the fiscal rules (https://www.fs-rs.si/wp-content/uploads/2019/10/Ocena-oktober-2019_koncna_ANG.pdf).

Figure 1.5: Indicators of economic cycle dynamics 2005-2020



Sources: SORS, ECB, Eurostat, Employment Service of Slovenia, FC calculations.

Figure 1.6: Indicators of economic cycle dynamics for 2009 and 2020



Note: * y-o-y growth rates, ** inverted values. Data for 2009 are shown as dashed line, data for 2020 are shown as solid line.
Sources: SORS, ECB, Eurostat, Employment Service of Slovenia, FC calculations.

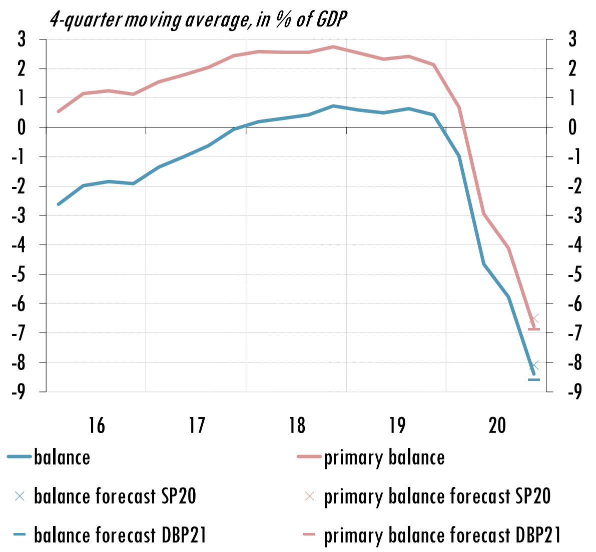
position of the economy are even more uncertain.[2] This is illustrated by the extremely wide range of different output gap assessments, which, according to the latest available estimates, ranges between -1.5% and -8.1%. In addition to the demand shock, this epidemic has been accompanied by a strong supply shock, which could affect changes in the response and structure of production factors and the changed level and dynamics of the economy's potential. This impact largely depends on the structure and flexibility of the economy and on the economic policy response[3], and it will probably be only possible to estimate its actual extent with a few years' delay. Other indicators monitored by the Fiscal Council to determine the cyclical position of the economy show that the negative deviation from the long-term average for the vast majority of indicators was similar to that of the financial crisis a decade ago, but at the same time their recovery from the initial shock was faster.

[2] For an analysis of the uncertainty of estimates of the output gap during the current crisis in Slovenia, see last year's estimates (Box 1.1) (https://www.fs-rs.si/wp-content/uploads/2020/06/Assessment.pdf).
[3] European Commission (2009). Impact of the current economic and financial crisis on potential output.

1.2 Budgetary trends – the general government sector (ESA)

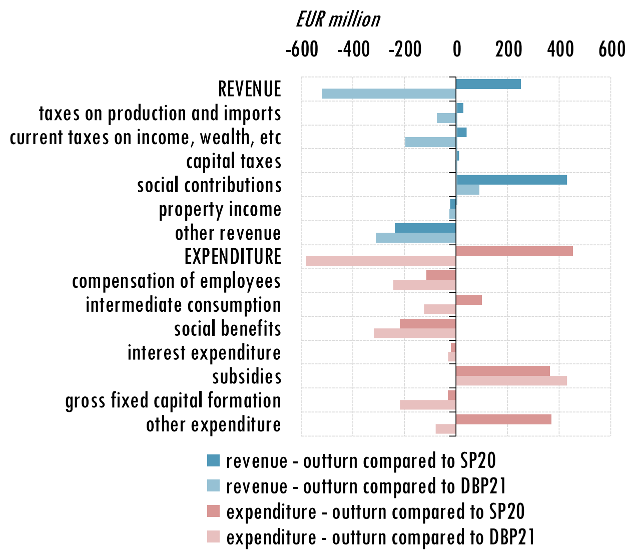
Last year's general government deficit, which was the second highest to date, was to a large extent directly and indirectly due to the epidemic. The deficit was EUR –3.893 billion or –8.4% of GDP, which is around EUR 300 million less than projected in the Draft Budgetary Plan 2021. According to the ESA methodology, the direct impact of measures to limit the consequences of the epidemic was estimated by the Ministry of Finance to be EUR 2.780 billion or 6.0% of GDP.[4] Without this impact, last year's deficit was EUR –1.113 billion or –2.4% of GDP. This deficit was mainly due to the indirect impact of the epidemic, when the fall in economic activity led to a fall in revenue, while expenditure growth was lower than it had been in the two years before the crisis, though approximately two times higher than average expenditure growth in the last decade.[5]

Figure 1.7: General government balance and primary balance



Source: SORS, MoF forecasts: SP20(Apr.20) in DBP21(Oct.20); FC calculations.

Figure 1.8: 2020 outturn compared to SP20 and DBP21



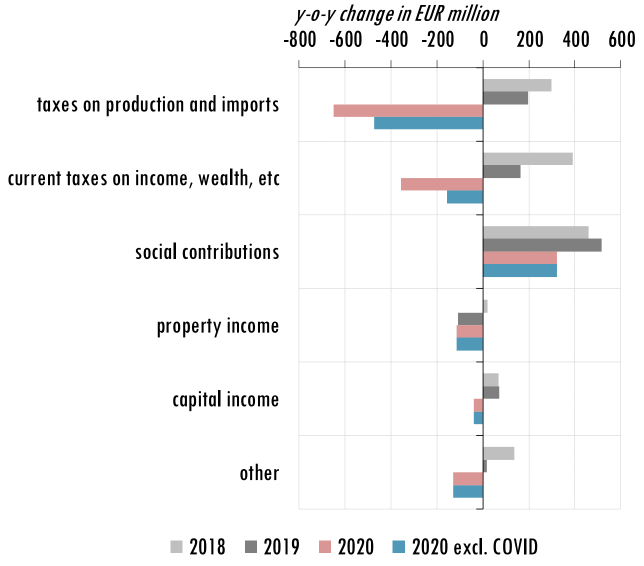
Source: SORS, MoF forecasts: SP20(Apr.20) in DBP21(Oct.20); FC calculations.

Revenues fell by 4.7% last year; without taking into account the direct effect of COVID measures they fell by 2.9%. The direct effect of COVID measures of EUR 374 million on the revenue side only affected the evolution of revenue from taxes on production and imports and from taxes on income. The measures included the possibility of deferral or instalment payment of tax liabilities and unaccounted advance payments of corporate income tax and personal income tax from income from self-employment during the first wave of the epidemic last spring. The overall decline was mainly due to a decline in taxes on production and imports, which decreased by around a tenth, but without taking into account the direct effect of the measures, their decline was around 7% and mainly due to a significant drop in consumption. Revenue from taxes on income also declined by around a tenth last year. In this context, the decline in revenue from taxes on income of individuals or households was minimal, which is also associated with the large amount of benefits to employees. On the other hand, revenue from taxes on income or profits of companies declined by more than a third, but their decline, without taking into account the impact of the measures, was much smaller. Among all key categories, only

[4] Overview of trends in the general government sector without taking into account the direct effect of COVID measures is fully based on the assessment of the Ministry of Finance in the Stability Programme 2021. The Statistical Office of the Republic of Slovenia (SORS) had not yet published an assessment at the time this document was prepared.

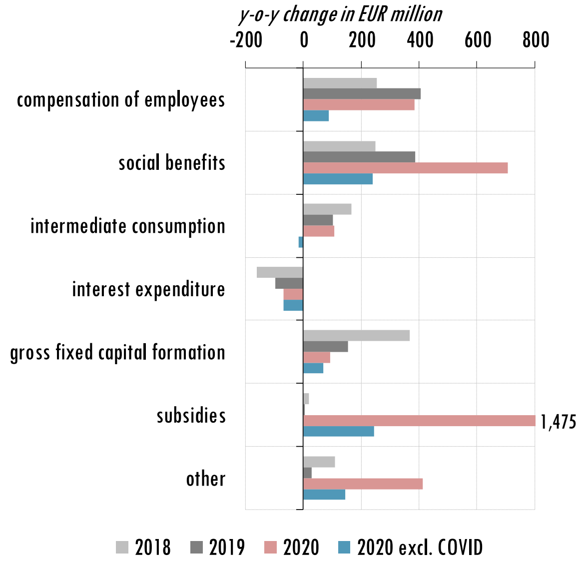
[5] In the 2010–2019 period, total expenditure growth stood at 1.9% annually on average, and without taking into account capital transfers, which were high, particularly in 2013 and 2014 due to bank recovery, the growth totalled 1.6%.

Figure 1.9: General government revenue



Source: SORS, MoF, FC calculations.

Figure 1.10: General government expenditure



Source: SORS, MoF, FC calculations.

revenue from social security contributions increased, up by 4.1% on the previous year. In total, revenues from other key categories of revenue decreased by around a tenth.

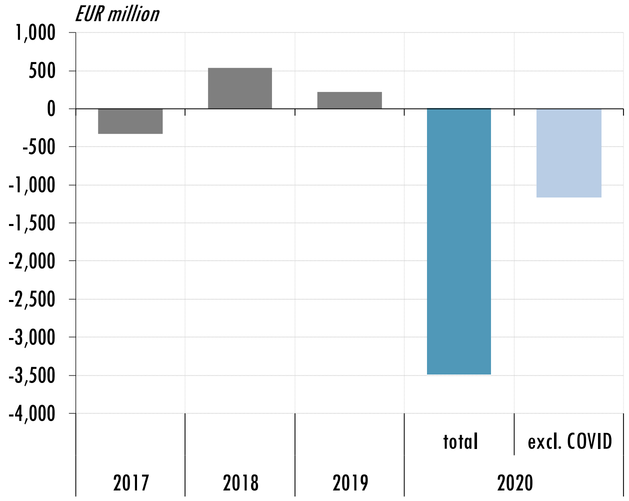
Expenditure increased by 14.9% last year, growth without a direct effect of COVID measures of EUR 2.406 billion was 3.8%. Overall growth was mainly due to significantly higher expenditure on subsidies, with around half of all expenditure on measures to limit the effects of the epidemic being realised in this category of expenditure. According to the Ministry of Finance estimate, their growth was by far the highest ever, even without taking into account the effect of the measures.[6] The 8.4% higher expenditure on social transfers also contributed significantly to overall growth. Without taking into account the effect of the EUR 465 million worth of measures, their growth was around 3% and was mainly the result of higher pension expenditure. Due to adopted measures, increased expenditure on compensation of employees and other current transfers made an important contribution last year. Total compensation of employees increased by 7.0% last year or by 1.6% without taking into account COVID allowances of EUR 298 million. Expenditure on gross investment increased by 5.0% last year, which is less than the projections in the Draft Budgetary Plan that expected almost 17% growth. Overall growth was again curtailed by lower interest expenditure; however, their decline was slightly lower than in previous years due to the increased government debt. Overall expenditure growth fell behind the projections in the Draft Budgetary Plan by EUR 580 million; the Fiscal Council was already pointing out that these projections were unrealistic when the document was evaluated in October last year.

1.3 Budgetary trends – public finance budgets (cash-flow methodology)

According to the data provided by the Ministry of Finance, the state budget deficit in 2020 was EUR 3.486 billion (7.5% of GDP), which would amount to EUR 1.157 billion (2.5% of GDP) if the direct effects of COVID measures were not taken into account. As the Fiscal Council expected, implementation was somewhat better than the projections from the revised budget adopted in

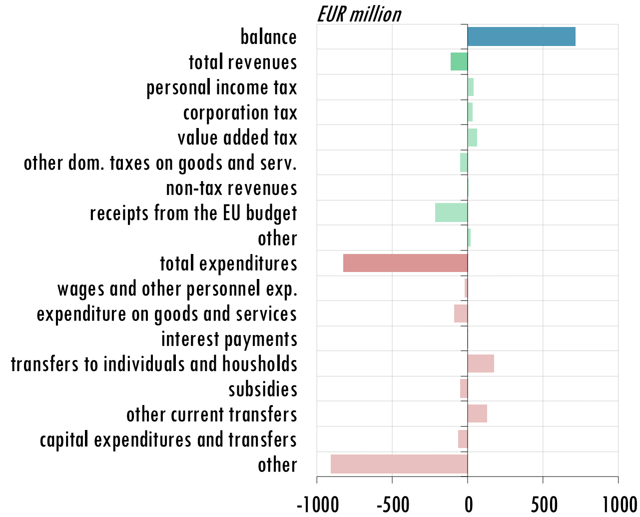
[6] Without taking into account the impact of measures, the growth in expenditure on subsidies was expected to be 70.3% while the highest so far was seen in 2013, when it stood at 15.3%.

Figure 1.11: State budget balance



Source: MoF, FC calculations.

Figure 1.12: Difference between outturn and revised state budget for 2020



Source: MoF, state budget outturn and Revised budget of the Republic of Slovenia for 2020 (Sep. 20).

September, although the revised budget was drafted before the second wave of the epidemic and the related adoption of additional measures to mitigate its consequences. Already in its assessment of the draft revised budget, the Fiscal Council found that, in spite of the fact that the revised budget was planned under conditions of high uncertainty, the projected expenditure in particular were high and unfeasible. The overall effect of COVID measures on the state budget under the cash-flow methodology was EUR 2.3 billion in 2020, the predominant part on the expenditure side.

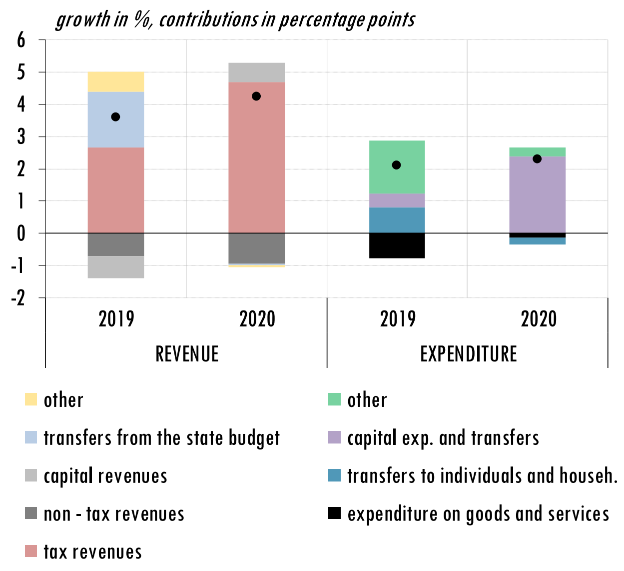
Revenue declined by 10.4% last year, in particular due to the economic downturn, without the direct effect of COVID measures (EUR 324 million) the decline would be smaller (-7.2%). In comparison to the preceding year, the largest decrease was recorded in revenue from corporate income tax, where the direct impact of COVID measures was the strongest due to unaccounted advance tax payments in April and May and the deferral of tax payments. A substantial reduction in revenue from personal income tax and excise duties was mainly related to the reduction of taxable income and, in the context of personal income tax, this was partially related to the decrease in tax burden and the increase in lump sum expenditure for municipalities, while the effect of COVID measures was relatively small. Among the main categories of tax revenue, the decline was the smallest in VAT revenue (−8.9%) and was primarily related to the decline in consumption, while the possibility to defer tax payments contributed 3 pps to the decline in total VAT revenue. Non-tax revenue grew slightly in the preceding year; however, revenue from profit sharing fell significantly due to poor business results and privatisation from previous years. Extraordinary non-tax revenue increased substantially due to treasury operations. A slightly lower amount of funds was received from the EU budget than in 2019, while the decrease in these funds without considering the part of this revenue spent for COVID measures amounted to 10.4%. Thus, the realisation of EU funds received again failed to meet the targets projected from the revised budget (growth of 29.5%), although these were already lower than the projections in the adopted budget.

Expenditure increased by 26.8% last year, in particular due to the direct effect of COVID measures; without taking into account the effect of EUR 2.004 billion, the growth was 6.5%. In accordance with the Fiscal Council's expectations, the growth in both comparisons was lower than projected in the revised budget, in which an exceptionally high growth in expenditure, which did not include the effect of COVID measures and significantly deviated from the trends in 2020 before the adoption of the revised budget, was forecast for the final months of the year. The increase in total expenditure was mainly due to subsidies, which constitute the bulk of direct COVID measures. Without observing this effect (EUR 965 million), the growth of total expenditure was similar to the one in 2019 and lower than projected in the revised budget. Transfers to individuals and households increased by more than a third compared to the preceding year. Without taking into account COVID measures (EUR 384 million), the increase was also considerably lower compared to 2019. In both comparisons, the increase was higher than projected in the revised budget. The Fiscal Council drew attention to the risk of underestimating projections of transfers to individuals and households both when adopting the budget in autumn 2019 and when adopting the revised budget in autumn 2020. Transfers to social security funds also significantly increased in the preceding year, while their growth was stimulated by the COVID measures in the amount of EUR 135 million from solidarity allowances for pensioners. Due to lower revenue from social contributions, the transfer to the Pension and Disability Insurance Institute of Slovenia was larger by approximately a quarter than in 2019. The rise in total labour costs, including transfers to public institutions, was 12.2%. If one does not take into account the effect of employee benefits disbursed under the COVID measures (EUR 196 million), the rise is almost halved and is mainly attributed to the wage agreements from the preceding years. The increase in total expenditure on goods and services was related primarily to expenditure under the COVID measures (EUR 166 million). Again, the year-on-year expenditure growth was particularly pronounced at the end of the year. After significant growth in 2019, investment expenditure and transfers declined (−2.8%) last year, while the revised budget projected growth (3.8%). The lag behind the projected levels is also related to the lower than projected spending of EU funds, which is an important source of financing state investments.

The surplus of municipal budgets (EUR 31.3 million) was the highest since 2016. This improvement was produced by a higher revenue growth compared to 2019 (4.2%; 2019: 3.6%). The growth was predominantly a result of stronger growth of income tax revenue (10.2%) due to the lump sum expenditure, which increased by almost six per cent to EUR 624 per capita last year. The revenue growth was further promoted by higher capital revenue due to increase in revenue from the sale of building land and state funding, which was higher by half to cover current spending. The remaining revenue categories were lower than in the preceding year. Expenditure growth was higher than last year (2.3%; 2019: 2.1%). This was mainly the result of enhanced investments (7.1%), while the growth was primarily contributed to by higher expenditure for new construction, reconstruction and adaptation and for the purchases of buildings and premises. Total growth was curbed by a drop in expenditure on transfers to individuals and households, which mainly resulted from lower reimbursement of school transport costs. Transfers to public institutions for intermediate consumption and transfers to non-profit institutions also declined.

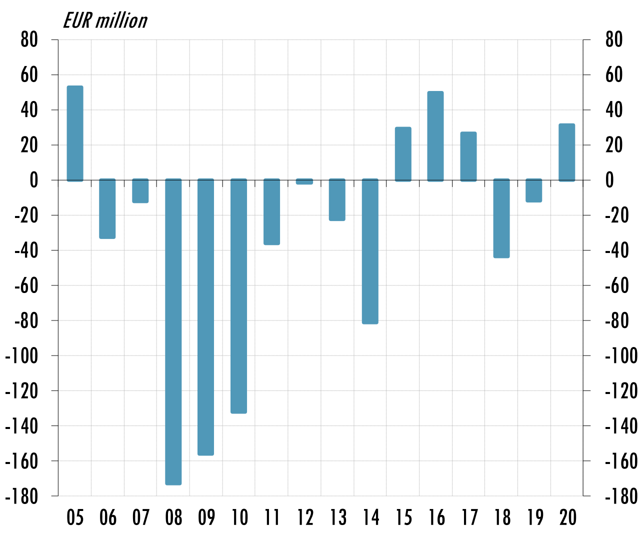
In 2020, growth of the Pension and Disability Insurance Institute of Slovenia expenditure increased to 7.1% (2019: 4.1%) due to substantially higher growth in pension expenditure (6.2%), the highest since 2008. The growth was primarily a result of the increase in the average pension following the extraordinary and regular indexations of pensions in December (2.0%) and January (3.2%), respectively. Thus, the old-age pension rose by 4.2%, while the number of pension recipients also grew slightly compared to the preceding year. With the strengthened growth of the average pension in the last three years, total pension expenditure increased by EUR 616 million or

Figure 1.13: Revenue and expenditure of local government



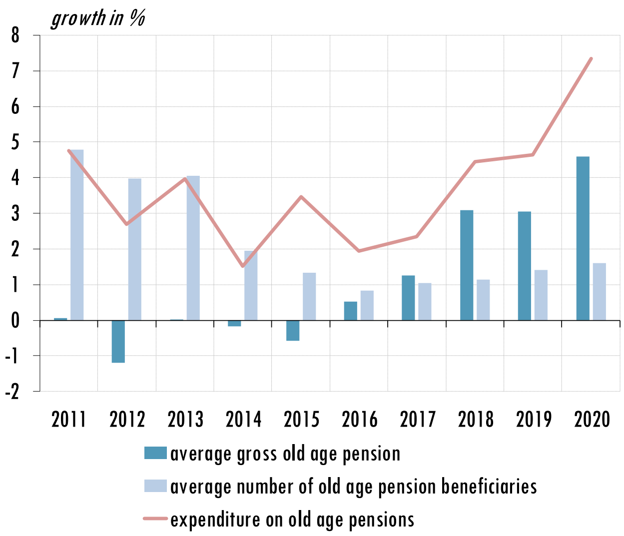
Source: MoF, FC calculations.

Figure 1.14: Budget balance of local government



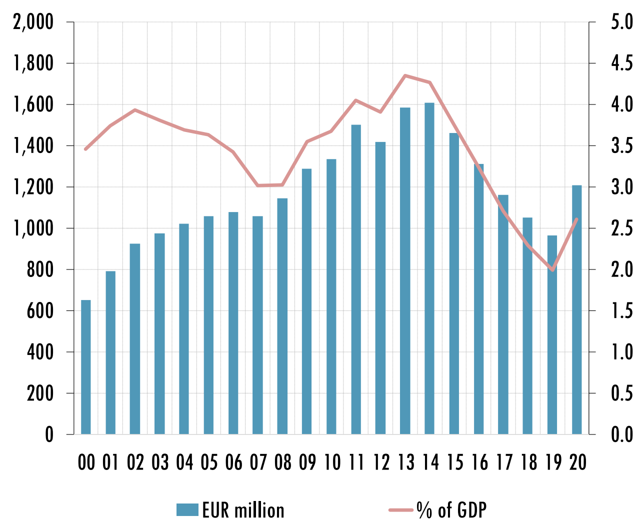
Source: MoF.

Figure 1.15: Pensions



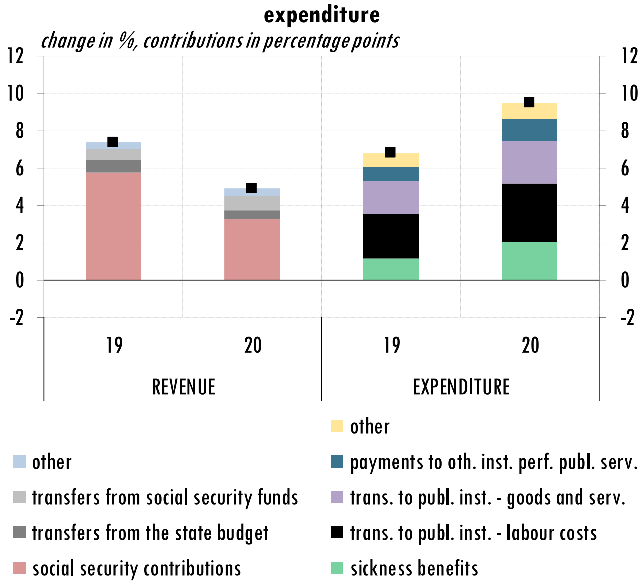
Sources: Pension and Disability Insurance Fund of Slovenia (ZPIZ), MoF, FC calculations.

Figure 1.16: Pension and Disability Insurance Fund - transfers from the state budget



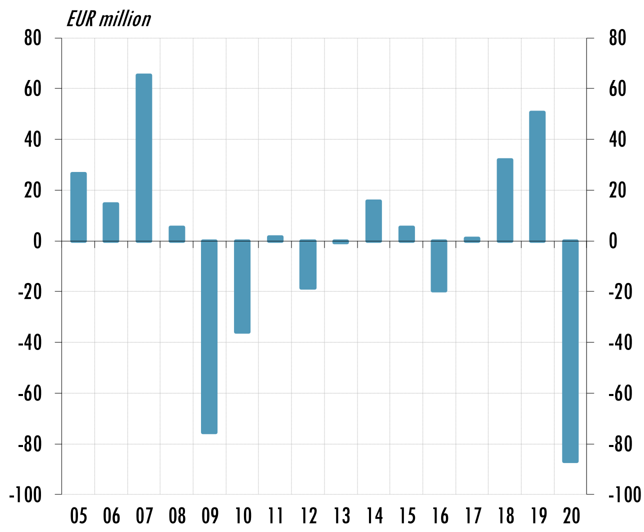
Sources: MoF, SORS, FC calculations.

Figure 1.17: The Health Insurance Institute revenue and expenditure



Source: MoF, FC calculations.

Figure 1.18: The Health Insurance Institute budget balance



Source: MoF.

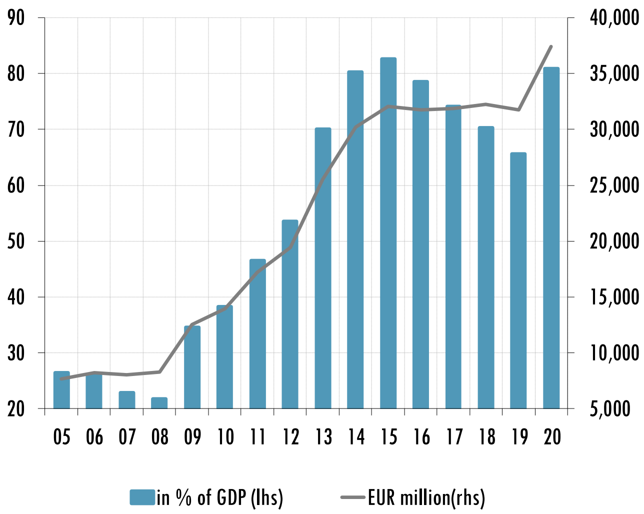
14.3% cumulatively in this period. More than a year ago, total growth was also fuelled by social security expenditure, which was a result of one-off transfers to pensioners within the COVID measures, while the increase in expenditure on annual bonuses for pensioners was smaller compared to 2019. Considering that the growth of tax revenue was almost halved compared to 2019 and that non-tax revenue fell significantly, a considerably larger transfer from the state budget, which grew by a quarter to EUR 1.207 billion last year, was required to balance the higher expenditure.

The Health Insurance Institute of Slovenia ended 2020 with its largest recorded deficit to date (EUR −87 million). The increase in revenue slowed down to 4.9% (2019: 7.4%), which was mainly due to a significant slowdown in growth of revenue from social contributions compared to the preceding year. Expenditure growth (9.5%) was the highest since 2008, which is primarily the result of higher spending on the measures adopted to mitigate the epidemic. The growth mostly came from transfers to public institutions for labour costs (contribution: 3.2 pps), which rose more than in the preceding year. The same applies to the other three revenue categories, which made significant contributions to the total growth. Transfers to public institutions for expenditure on goods and services and the payments to public service contractors that are not budget users rose by roughly a tenth and sickness benefits by as much as 16.5%.

1.4 General government debt

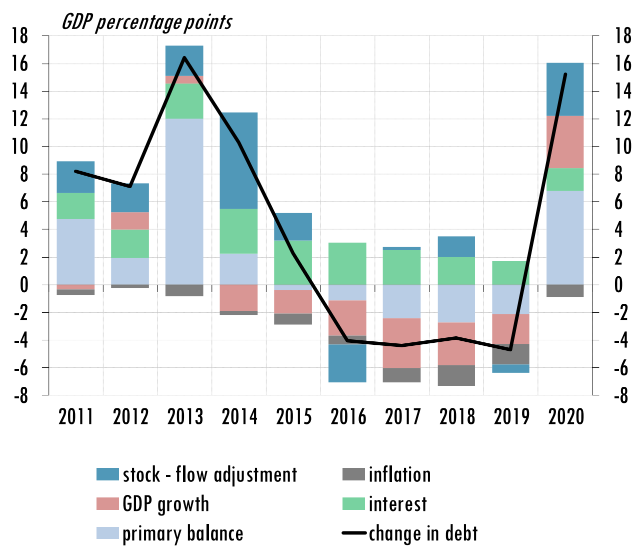
Last year, general government gross debt increased to 80.8% of GDP (EUR 37.4 billion) and after four years of decline almost reached highest level ever, set in 2015. In nominal terms, debt increased by EUR 5.7 billion and its share in GDP by 15.2 pps. About half of the increase was due to the deterioration of the primary balance, while around 4 pps of GDP were contributed by both the fall in economic activity and the stock-flow adjustment. The increase in debt was somewhat more pronounced than the EU average and the ninth largest among the member states. Again last year and despite the epidemic, borrowing took place under favourable financial market conditions, mainly due to the ECB's expansionary policy. At the beginning of the epidemic, it launched a new programme for the purchase of government bonds (Pandemic Emergency Purchasing Programme – PEPP), under which it had purchased EUR 4.224 billion in Slovenian public debt by the end of March, representing about a tenth of the total debt. The European Central Bank has become one of the main holders of government debt securities in recent years. The required yield on the Slovenian 10-year bond further

Figure 1.19: General government debt



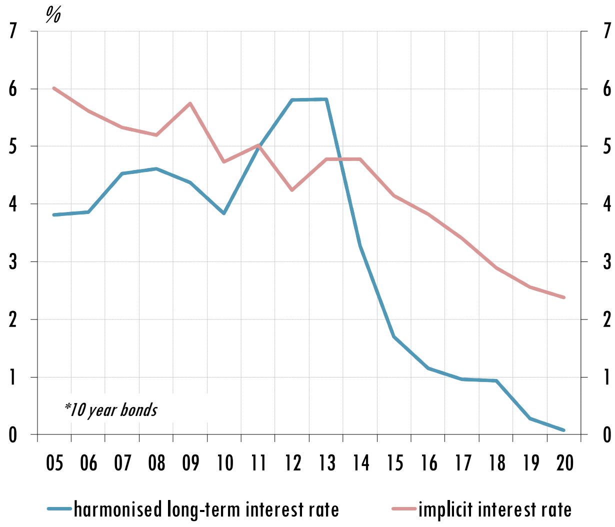
Source: SORS.

Figure 1.20: Change in general government debt



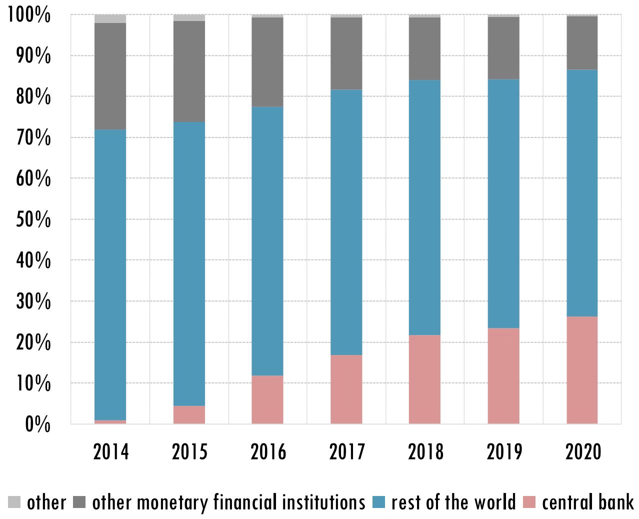
Source: SORS, FC calculations.

Figure 1.21: Harmonised long-term interest rate* and implicit public debt interest rate



Source: ECB, SORS, FC calcuations.

Figure 1.22: Structure of government debt securities holders



Source: BoS, FC calculations.

decreased (from 0.28% on average in 2019 to 0.08%), while the implicit interest rate on total debt declined by an additional 0.2 pps to 2.4%. The time distribution of liabilities remains favourable. The average weighted time to debt maturity (9 years) remained the same as at the end of 2019 and remained longer than the OECD average (8 years).[7] After a decrease in 2019, the amount of the general government's funds in the single treasury account increased by EUR 2.2 billion and totalled EUR 6.2 billion or 13.4% of the GDP at the end of December.

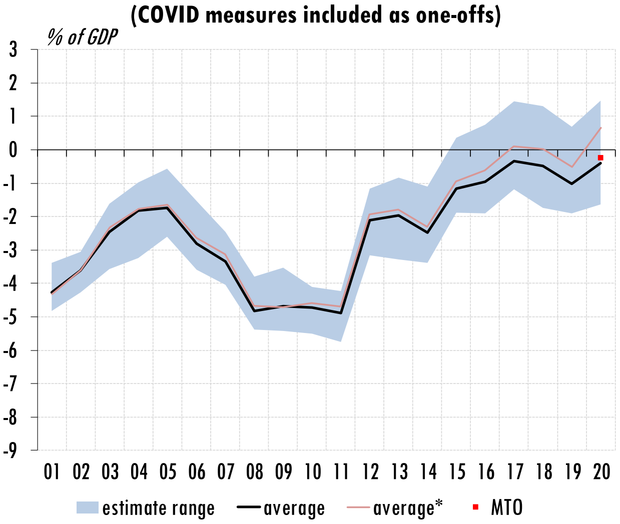
[7] OECD Sovereign borrowing outlook for OECD countries 2021.

2. Compliance with the fiscal rules in 2020

In its assessment of the compliance of the implemented general government sector budgets with the fiscal rules in 2020, the Fiscal Council (i) indicatively verified whether the minimum level of structural balance under the EU rules (MTO) and other requirements under the EU rules had been attained and (ii) verified whether the implementation of the national fiscal rule defined in Article 3 of the Fiscal Rule Act (ZFisP) regarding the maximum permitted level of expenditure had been attained. To determine the cyclical position for 2020, the range of output gap estimates set in Section 1.1 and Annex 4.2 — which is presented and applied by the Fiscal Council in each assessment of compliance with the fiscal rules — was once again used in assessing compliance with fiscal rules. In addition to assessing the cyclical position of the economy, the key factor in the findings on compliance with fiscal rules in 2020 relates to including the fiscal implications of the measures limiting the consequences of the epidemic as one-off effects.[8] Such an approach provides for a more adequate estimate of fiscal policy orientation, which is also consistent with the position of the European Commission.

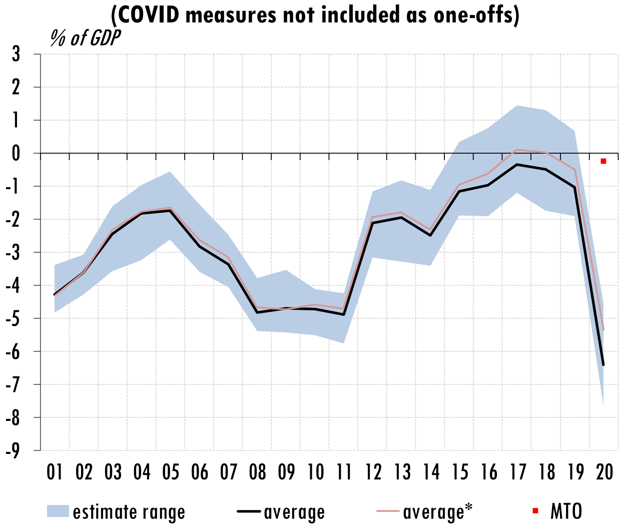
The national rule referring to the maximum allowable level of government expenditure was complied with in the past year. The minimum permitted level of structural balance under the EU rules (MTO) in 2020 was attained, taking into account the permitted deviation. Growth in general government expenditure, excluding one-off effects, was also below the limit permitted under the expenditure rule of the Stability and Growth Pact. Despite the favourable outcome in 2020, the average deviation of both the structural balance and the structural effort over a two-year period exceeded the threshold of 0.25 pps of GDP according to current calculations, due to the expansionary fiscal policy implemented in 2019. The general government debt increased in 2020, contrary to the benchmark according to which it should have decreased. The Fiscal Council did not assess the budget balance over the business cycle due to the temporary deviation from the medium-term balance permitted during a period of exceptional circumstances. The framework for drawing up budgets was adjusted frequently and

Figure 2.1: Structural balance estimates (COVID measures included as one-offs)



*Sources: SORS, OECD, IMF, IMAD, EC, MoF, FC. *Based on output gap estimated on the basis of potential output growth estimates from autumn 2019 and current GDP forecast (see also Box 4.2 in Assessment of budgetary documents for 2021 – 2024).*

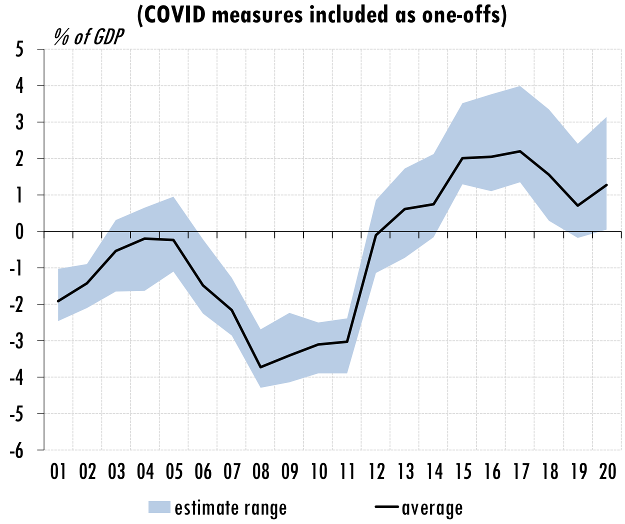
Figure 2.2: Structural balance estimates (COVID measures not included as one-offs)



*Sources: SORS, OECD, IMF, IMAD, EC, MoF, FC. *Based on output gap estimated on the basis of potential output growth estimates from autumn 2019 and current GDP forecast (see also Box 4.2 in Assessment of budgetary documents for 2021 – 2024).*

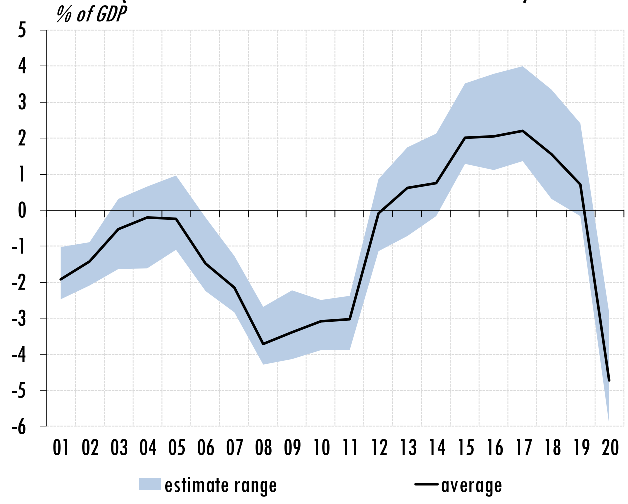
[8] For uncertainties about incoming variables determining the position of fiscal policy in the current crisis, see e.g. the publications of the Fiscal Council: Assessment of compliance of the public finance policy with the fiscal rules on the basis of the draft Stability Programme 2020 and the proposed Ordinance amending the Ordinance on the framework for the preparation of the general government budget for the 2020–2022 period, (Box 2.1; available at:https://www.fs-rs.si/wp-content/uploads/2020/04/Ocena_April2020_ANG.pdf), the Assessment of budget documents for the 2021–2022 period (Box 4.1; available at:https://www.fs-rs.si/wp-content/uploads/2020/10/Assessment.pdf), the Assessment of budget documents for the 2021–2024 period (Box 4.1; available at: https://www.fs-rs.si/wp-content/uploads/2021/04/Assessment2021.pdf).

Figure 2.3: Estimates of structural primary balance (COVID measures included as one-offs)



*Sources: SORS, OECD, IMF, IMAD, EC, MoF, FC. *Based on output gap estimated on the basis of potential output growth estimates from autumn 2019 and current GDP forecast (see also Box 4.2 in Assessment of budgetary documents for 2021 – 2024).*

Figure 2.4: Estimates of structural primary balance (COVID measures not included as one-offs)



*Sources: SORS, OECD, IMF, IMAD, EC, MoF, FC. *Based on output gap estimated on the basis of potential output growth estimates from autumn 2019 and current GDP forecast (see also Box 4.2 in Assessment of budgetary documents for 2021 – 2024).*

substantially and failed in its core function of setting the medium-term orientation of fiscal policy. Last year it was amended twice, by a total of over EUR 3 billion. General government expenditure (excluding one-off effects) thus remained below the maximum level permitted under the current framework for drawing up budgets, also in terms of the current assessment of the output gap and one-off factors. Expenditure of individual public finance budgets calculated using the cash flow methodology were below the maximum permitted level of expenditure, taking into account the applicable budgetary framework.

2.1. Achieving a minimum structural balance under the EU rules (MTO)

Based on currently available data, the Fiscal Council estimates that Slovenia attained the minimum permitted level of structural balance under the EU rules (MTO) in 2020 taking into account the permitted deviation. The MTO for Slovenia in the 2020–2022 period set under the EU rules[9] requires that structural deficit should not exceed 0.25% of GDP.[10] The structural balance estimates may also diverge due to different output gap estimates[11] and in this assessment differ mainly due to inclusion or non-inclusion of fiscal measures to prevent the consequences of the epidemic as one-off factors.[12] The current structural balance estimates that were considered in the production of assessments of compliance of general government budgets with the fiscal rules range from –1.6% of GDP to 1.5% of GDP for 2020. This is an assessment of the structural balance based on current output gap assessments and excluding the effects of measures to limit the consequences of the epidemic.[13]

[9] Regulation EC 1466/97. Due, inter alia, to uncertainties in structural balance calculations, EU rules permit a deviation from the required MTO of up to one quarter of pps of GDP (see Section 1.3.2 in Vade Mecum on the Stability and Growth Pact, 2019).

[10] See Annex 2 to Vade Mecum on the Stability and Growth Pact (2019).

[11] In producing its estimates, the Fiscal Council uses the estimates of five institutions and four statistical methods of output gap assessment. The Fiscal Council started to use the latter when it drew up its assessment of the 2018 Stability Programme. For more information on the output gap calculations used by the Fiscal Council, see the Report on the Fiscal Council's operations in 2017, pp. 23–26 (May 2018).

[12] It should be noted that, contrary to the guidance given to Member States at the beginning of the epidemic, in its assessment of draft budget plans in November 2020 the EC did not consider these effects as one-off measures; however, it did pointed out that the exclusion of temporary measures to mitigate the consequences of the epidemic more accurately illustrates the fiscal policy orientation.

[13] Inclusion of the effects of one-off measures yields completely different results, indicating a markedly expansionary fiscal policy in 2020 (compare Figures 2.1 and 2.2 or Figures 2.3 and 2.4 respectively). See also the European Commission (2020): Communication from the Commission to the European Parliament, the Council and the European Central Bank on the 2021 Draft Budgetary Plans: Overall Assessment. COM (2020) 750 final. November. European Commission. Brussels. Available at: https://ec.europa.eu/info/sites/info/files/economy-finance/dbps_overall_assessment.pdf

Current estimates show that a structural effort of 0.6 pps of GDP was achieved in 2020 if temporary measures are considered as one-off factors. The estimated negative output gap exceeded 4% of GDP in 2020. Despite the favourable outcome in 2020, the average deviation of both the structural balance and the structural effort over a two-year period, which exceeded the threshold of 0.25 pps of GDP[14] according to current calculations due to the expansionary fiscal policy implemented in 2019. The structural primary balance recorded a surplus last year for the eighth consecutive year and considering the range of current output gap estimates it ranged between 0.1% and 3.1% of GDP.

2.2. Compliance with the national fiscal rule – medium-term balance

In addition to achieving the medium-term budgetary objective, the medium-term balance under the SGP rules also implies that at least a balanced structural position is achieved over the entire economic cycle. Paragraph one of Article 3 of the ZFisP states that the medium-term balance is achieved if the structural balance of the general government sector in an individual year is not lower than the minimum value as defined in the SGP while in the medium term it should be at least in balance or in surplus. Point 5 of Article 2 of the ZFisP defines the medium term as a business cycle in which the actual level of GDP shifts from a level that is above the potential level of GDP to a level below and is on average equal to the potential level of GDP. In economic terms, the opposite also applies: the medium term can also be defined as a business cycle in which the actual level of GDP shifts from a level that is below the potential level of GDP to a level above and on average equals the potential level of GDP.[15]

The Fiscal Council examined compliance with the medium-term balance objective in 2020 due to exceptional circumstances The Fiscal Council assesses that the minimum value of the MTO for 2020 set by the SGP was attained, despite a slight structural balance deficit (see Section 2.1) and thereby the first condition of the definition of medium-term balance was achieved. However, in order to implement exceptional circumstances permitting a temporary deviation from the medium-term balance provided that this does not endanger fiscal sustainability in the medium term, the Fiscal Council did not check the medium-term fiscal balance over the period of the economic cycle. Such verification is currently also difficult due to uncertain output gap assessments, where the ranges for 2020 are extremely wide (see Section 1.1). As in previous assessments[16], the Fiscal Council noted that the period after the Slovenia's exit from the Excessive Deficit Procedure (EDP) or after the adoption of the ZFisP in 2015 was too short to meet the medium-term balance, as extensive annual structural efforts[17] would be needed during this period due to the high structural deficits attained in the past or in the previous crisis.

[14] For EU rules on deviations from the MTO, see Vade Mecum on the Stability and Growth Pact (2019: Chapter 1.3.7).

[15] For the purposes of economic analysis, both definitions indicate the period in which the sum of the output gap estimate deviations from the balanced position in the sequence of the indicated two phases of the economic cycle to the selected year amounts to 0. The IMF analysis (Aiyar and Voigts, 2019) points out that due to downward wage inflexibility, the average output gap estimates in the economic cycle would generally be less than 0.

[16] See the Assessment of compliance of the general government budgets with the fiscal rules in 2019 (Section 2.2.), available at: https://www.fs-rs.si/assessment-by-the-fiscal-council-compliance-of-the-general-government-budgets-with-the-fiscal-rules-in-2019/

[17] The Fiscal Council's calculations show that in 2016–2020, following the adoption of the ZFisP or after Slovenia's exit from the EDP in 2015, a structural effort of around 2 pps of GDP would be required in order to attain the medium-term balance in 2020, according to current estimates of the cyclical position of the economy. Based on various output gap indicators and at different lengths of the economic cycle, the average sum of structural balances in 2020 indicates a cumulative structural deficit slightly above 10 pps of GDP.

2.3. Compliance with the national fiscal rule – maximum level of expenditure

The Framework relevant for the current assessment of compliance with the national fiscal rule, also referring to 2020 (the 2020–2022 period), was last amended in November 2020.[18] The values for 2020 were last changed by the amendment to the Ordinance in September 2020.[19] The Ordinance on a framework for drawing up budgets sets a maximum permitted level of general government sector expenditure[20] and a target balance, both of which must be in accordance with ESA methodology. The maximum level of expenditure and the target balance for the state budget, the health insurance budget, the pension insurance budget and the local communities budgets are set according to the cash flow methodology. The Ordinance on the Framework related to 2020 was first adopted by the Slovenian Government in April 2017 and subsequently amended on seven occasions, whereby the maximum permitted level of general government sector expenditure for 2020 was amended three times (in April 2019, April 2020 and September 2020). Although partly understandable in uncertain circumstances, frequent changes to the Framework distort the medium-term budgetary planning, as its purpose is to provide formal guidance for conducting countercyclical fiscal policy. This has already been pointed out by the Fiscal Council in the past, including the warning regarding the latest high correction of the maximum allowable expenditure of the general government sector (and in particular the expenditure of the state budget) in September 2020. In this context, the

Table 2.1: Frameworks for drawing up budgets for 2020

	general government		state budget		local governments		pension fund (ZPIZ)		health fund (ZZZS)	
	balance (GDP %)	E	balance (GDP %)	E	balance (GDP %)	E	balance (GDP %)	E	balance (GDP %)	E
Framework, May 2017, OG 21/2017	0.4	19,952	-0.6	9,942	0.1	2,219	0.0	5,842	0.0	3,087
Framework, Nov. 2017, OG 65/2017	0.4	19,952	-0.6	9,942	0.1	2,219	0.0	5,842	0.0	3,087
Framework, Aug. 2018, OG 57/2018	0.4	19,952	-0.6	9,942	0.1	2,219	0.0	5,842	0.0	3,087
Framework, Dec. 2018, OG 82 2018	0.4	19,952	-0.6	9,942	0.1	2,219	0.0	5,842	0.0	3,087
Framework, Apr. 2019, OG 26/2019	1.0	21,480	0.8	10,450	0.1	2,320	0.0	5,845	0.0	3,320
Framework, Apr. 2020, OG 67/2020	-8.1	23,630	-8.1	12,525	...	2,340	...	5,930	...	3,320
Framework, Sep. 2020, OG 128/2020	-8.6	24,650	-9.3	13,395	...	2,340	...	5,930	...	3,370
Framework, Nov. 2020, OG 168/2020	-8.6	24,650	-9.3	13,395	...	2,340	...	5,930	...	3,370
outturn	-8.4	24,066	-7.5	12,564	0.1	2,296	0.0	5,899	-0.2	3,343
outturn-Framework Nov. 20		-584		-831		-44		-31		-27
Memo:										
outturn-Framework Apr. 20	-0.3	436	0.6	39	...	-44	...	-31	...	23
Framework change in 2020 (Nov.-Apr.)	-0.5	1,020	-1.2	870	...	0	...	0	...	50
Framework change Nov.20 - Apr. 19	-9.6	3,170	-10.1	2,945	...	20	...	85	...	50

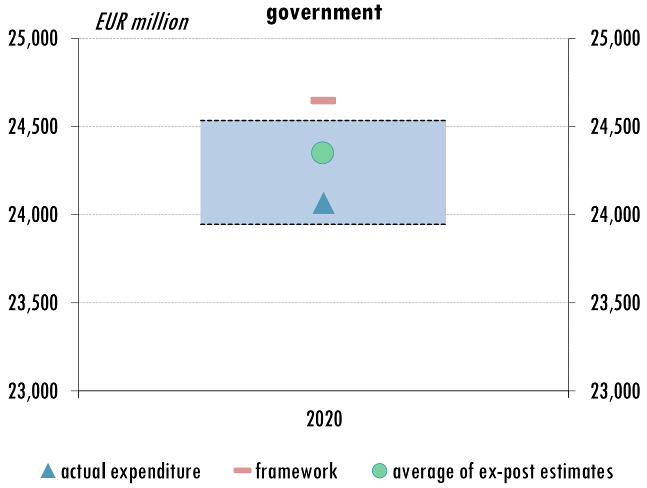
Source: OG RoS, MoF, SORS. Calculations: FC.

[18] This decree amended the values for 2021 and 2022. Available at: https://www.uradni-list.si/glasilo-uradni-list-rs/vsebina/2020-01-2923/odlok-o-spremembah-odloka-o-okviru-za-pripravo-proracunov-sektorja-drzava-za-obdobje-od-2020-do-2022-odpsd20-22-c - Only in Slovene.

[19] See: https://www.uradni-list.si/glasilo-uradni-list-rs/vsebina/2020-01-2286/odlok-o-spremembah-odloka-o-okviru-za-pripravo-proracunov-sektorja-drzava-za-obdobje-od-2020-do-2022-odpsd20-22-b - Only in Slovene.

[20] The maximum level of expenditure is calculated in accordance with the mathematical formula set out in points 3 and 4 of Article 3 of the ZFisP depending on the state of the economy in the cycle. The maximum level of expenditure is determined by deducting the projected level of potential GDP multiplied by the factor corresponding to the state of the economy in the business cycle from the projected scope of general government revenue. Temporary or one-off expenditures are not taken into account.

Figure 2.5: Maximum level of expenditures of the general government



Note: The blue field denotes the zone between the lowest and highest calculated maximum permitted expenditure estimated ex-post and based on currently available data.
Source: SORS, MoF, FC calculations.

Fiscal Council drew attention, in particular, to the creation of high surplus reserves, i.e. the creation of a wide room for manoeuvre in the remainder of the year.[21]

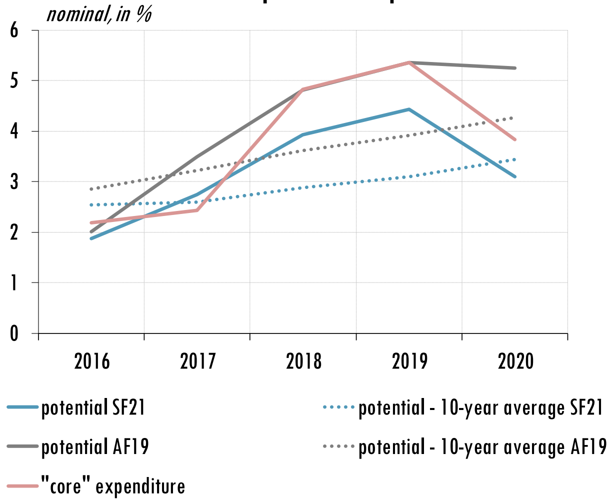
According to realisation in 2020, general government sector expenditure complied with the maximum level permitted under the applicable Framework for drawing up budgets. In 2020, general government sector expenditure was around EUR 600 million below the level permitted in the applicable Framework for 2020 as set in November 2020, while revenue, with a smaller decline of economic activity, was slightly higher than expected when the amendment to the Framework was drawn up. Thus, the general government deficit at -8.4% of GDP was slightly below the target set in the Framework of -8.6% of GDP. The state budget expenditure and expenditure of local communities and the pension and the health insurance fund budgets were lower than the maximum level permitted in the Framework of November 2020. The sum of expenditure of the abovementioned four budgets was by around EUR 35 million above the total general government expenditure; however, it was still below the maximum permitted level of general government expenditure. In part, these differences can be attributed to methodological differences[22] and in part they result from revenue and expenditure trends in the general government sector units not under the direct supervision of the Ministry of Finance or the Government.

An ex-post evaluation shows that in 2020 the level of government expenditure was below the maximum level of expenditure In the ex-post evaluation of the maximum allowable expenditure, we took into account the currently available data of the variables entering the calculation, in particular the assessment of the output gap and one-off effects. Since, according to most currently available estimates, the level of GDP in 2020 was below the level of the potential product (see Section 1.1), the

[21] See Assessment of compliance of the draft revised budget of the Republic of Slovenia for 2020 and of the proposal for the Ordinance amending the Ordinance on the framework for preparing the general government budgets for the 2020–2022 period with the fiscal rules, available at: https://www.fs-rs.si/assessment-by-the-fiscal-council-compliance-of-the-draft-revised-budget-of-the-republic-of-slovenia-for-2020-and-of-the-draft-ordinance-amending-the-ordinance-on-the-framework-for-the-preparation-of/

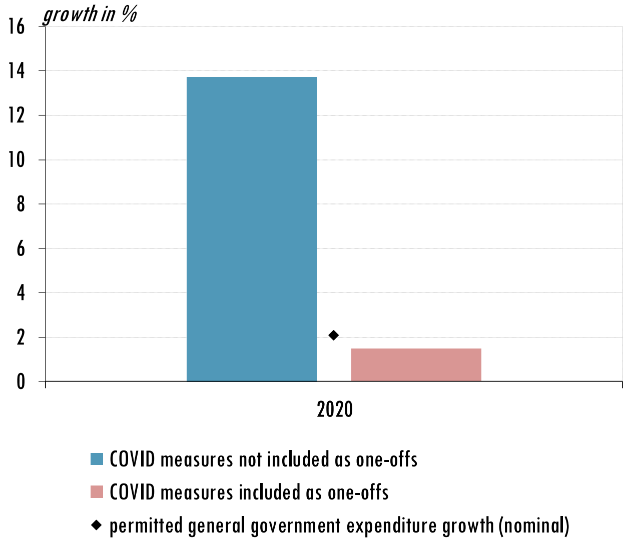
[22] The general government sector includes a broader range of institutional units than only four public finance budgets. More information on the broader range is available at: http://mf.arhiv-spletisc.gov.si/si/delovna_podrocja/javne_finance/tekoca_gibanja_v_javnih_financah/sektor_drzava/#lg=1&slide=0 – Only in Slovene. The list of institutions classified into the general government sector in Slovenia is available at: https://ec.europa.eu/eurostat/documents/1015035/7110762/SI-EDPI-Annex-I-201512.xlsx. In addition, developments in the general government sector are monitored on the basis of the methodology of the European system of accounts (ESA 2010) and the public finance budgets on the basis of the International Monetary Fund's methodology for monitoring the Government Finance Statistics (GFS).

Figure 2.6: Growth of "core" general government expenditure and the potential output



Note: "Core" expenditure is general government expenditure excluding COVID-19 related expenditure, investment and interest expenditure.
Sources: SORS, MoF, IMAD, FC calculations.

Figure 2.7: Net expenditure growth (EU expenditure rule)



Source: MoF, IMAD, FC calculations.

formula from paragraph 3 of Article 3 of the ZFisP was used. While the 2020 output indicates that the fall in GDP in 2020 was lower, the current estimate of the output gap is less negative, but at the same time the level of one-off expenditure was greater than that which provided the basis for setting the maximum expenditure limit in September and November 2020. The calculations thus show that expenditure without one-off measures in 2020 could be slightly higher than the actual outturn.

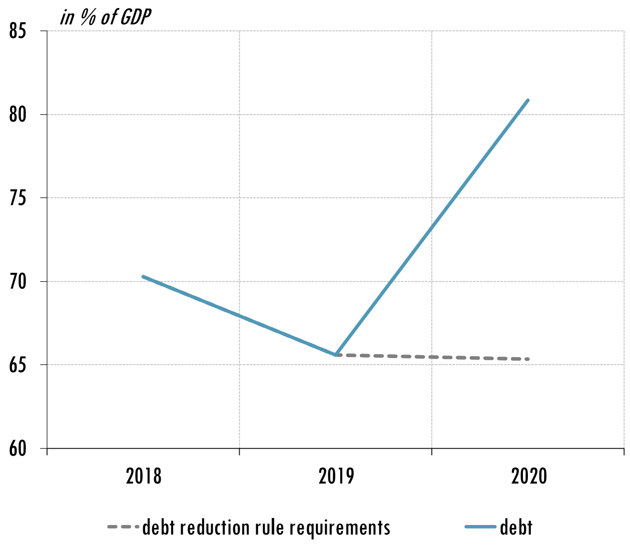
2.4. Compliance with the EU expenditure rule

The growth of net expenditure in 2020 was slightly below the maximum limit set by the EU expenditure rule. Within the framework of the EU expenditure rule the calculation of appropriate expenditure growth excludes certain types of expenditure that cannot be directly influenced[23] by fiscal policy. This expenditure includes interest payments, the cyclical component of unemployment benefits and expenditure resulting from the income from EU funds. The rule also takes into consideration that government investments vary considerably from year to year, therefore assessment of compliance with the expenditure rule takes into account the four-year average of investment expenditure, excluding received EU funds earmarked for investment spending. The growth of expenditure determined in this manner must not exceed the average 10-year growth of the potential output[24], while for countries that do not meet the medium-term target, expenditure growth must be even lower or adjusted for the convergence margin that ensures the expenditure rule is harmonised with the required adjustment of the structural balance. Due to possible annual fluctuations, the estimate also considers the two-year average of the growth of expenditure determined in this manner. In addition, one-off effects that influence the trend of general government expenditure and revenue are deducted from the expenditure. As shown in Figure 2.7 the inclusion or non-inclusion of one-off effects considerably affects the assessment of compliance with the expenditure rule. In 2020, the actual growth of net expenditure without taking into account one-off effects stood at 1.5% and was thus

[23] For more information about the expenditure rule, see Vade Mecum on the Stability and Growth Pact (2019, pp. 27–32).

[24] In accordance with the rule, five preceding years, the current year and the following four years are taken into account. In view of the availability of data for the whole period, the Fiscal Council uses the potential growth calculations prepared by IMAD for each forecast.

Figure 2.8: Debt reduction rule



Source: MoF, SORS, FC calculations.

below the permitted level (2.1%). An additional indicator, which excludes from expenditure only interest expenditure, current expenditure on investment and one-off effects, indicates a certain excess of the long-term average growth of the potential output, while at the same time lagging behind the growth of the potential output estimated in the pre-crisis period.

2.5. Compliance with the general government debt rule

Slovenia did not comply with the Fiscal Pact's rule on gradual debt reduction in 2020. Since 2019 inclusive, Slovenia has been required to reduce general government debt following the yearly dynamics that in a three-year average corresponds to a 1/20 deviation in the debt level from the base-year level of 60% of GDP. At the end of 2019, general government debt was 65.6% of GDP, thus exceeding the 60% of GDP level. According to the aforementioned rule, it should decrease by at least 0.25 pps of GDP in 2020. At the end of 2020, general government debt was 80.8% of GDP, thus exceeding the general government debt at the end of 2019 by more than 15 pps of GDP. Most of the increase in 2020 was due to the primary balance sheet deficit, while the pre-financing of future liabilities under favourable financing conditions in debt securities markets also had relatively high contribution (less than 4 pps of GDP) to the debt change.

3. Overview of the volume and effectiveness of measures to limit the consequences of the epidemic in 2020

The outbreak of the COVID-19 epidemic posed a major challenge for fiscal policy management, to which countries responded with large-scale measures, also helped by the flexibility of formal fiscal frameworks. In substance, fiscal policy action at the time of the epidemic can be divided into two periods, a period of direct control of the epidemic and a period of ensuring recovery through stimulus measures once the epidemic has been contained. In the first period following the outbreak of the epidemic, the measures focused mainly on three areas, namely to provide sufficient resources to the health system to manage the epidemic, to maintain jobs and the social situation of the most vulnerable groups of the population and to maintain the liquidity of economic agents. The main objectives of the measures were twofold: ensuring the health of the population, and maintaining economic potential. Depending on the actual course of the epidemic, this period refers to the year 2020, which is the subject of this review. Flexibility of formal fiscal frameworks enabled wide-ranging fiscal policy action. On 17 March 2020 the Fiscal Council found that the declaration of an epidemic in Slovenia[25] met the definition from Point 2 of Paragraph 1 of Article 12 of the Fiscal Rule Act (ZFisP), which, in the case of an unusual event outside the control of the party concerned, enabled a resort to exceptional circumstances for measures concerning the alleviation of the consequences of such an event and thus temporary deviation from the mid-term fiscal sustainability.[26] On 23 March 2020 the EU Council[27], on a proposal from the EC[28], adopted a decision on the implementation of the 'general escape clause', which permits a temporary deviation from the path towards the medium-term fiscal objective. A deviation is possible in the case of both Slovenian and European legislation, provided that this does not jeopardise medium-term fiscal sustainability.

The introduction of measures to limit the consequences of the epidemic was conditioned on the fulfilment of formal conditions. The national Fiscal Rule Act does not specify exactly what action should be taken in the event of the implementation of exceptional circumstances. Article 13 of the ZFisP stipulates that the extent of permitted deviations from the medium-term balance shall be defined by the National Assembly by adopting an amended framework proposed by the government. On the other hand, European legislation provides that measures in the context of the application of the general escape clause can only be considered in compliance with the following principles: (i) additional spending should be directly linked to exceptional circumstances, (ii) deviations can only be permitted on a temporary basis; (iii) the permitted deviations should only reflect the additional costs related to tackling exceptional circumstances compared with the previous year; (iv) countries should present the deviations in a transparent manner.[29] At the start of the epidemic, the IMF recommended that measures be timely, simple, temporary and targeted, and, given the scale of the action, transparent and embedded in a credible medium-term fiscal framework.[30] In pursuing the formal conditions for the adoption of measures and recommendations for their effectiveness, independent fiscal institutions also played an important role. The independent fiscal institutions agreed at the start of the epidemic that, in a given situation, large-scale fiscal policy action is appropriate but at the

[25] https://www.uradni-list.si/glasilo-uradni-list-rs/vsebina/2020-01-0532/odredba-o-razglasitvi-epidemije-nalezljive-bolezni-sars-cov-2-covid-19-na-obmocju-republike-slovenije – Only in Slovene.

[26] https://www.fs-rs.si/wp-content/uploads/2020/03/Assessment_extraordinary-event-under-the-Fiscal-Rule-Act-_March-2020.pdf.

[27] https://www.consilium.europa.eu/en/press/press-releases/2020/03/23/statement-of-eu-ministers-of-finance-on-the-stability-and-growth-pact-in-light-of-the-covid-19-crisis/.

[28] https://ec.europa.eu/info/sites/info/files/economy-finance/2_en_act_part1_v3-adopted_text.pdf.

[29] Vade Mecum on the Stability and Growth Pact 2019 Edition, p. 26 (https://ec.europa.eu/info/sites/info/files/economy-finance/ip101_en.pdf).

[30] IMF Fiscal Monitor, April 2020 (p. 15).

same time pointed out that, once the crisis is over, it will be necessary to ensure a return to the path of achieving medium-term sustainability. Independent fiscal institutions were active in four main areas: (i) ensuring rapid analyses of the macroeconomic and fiscal consequences of the crisis; (ii) monitoring the activation and implementation of the escape clauses; (iii) assessing the financial effect of proposed legislation; (iv) ensuring transparency and accountability.[31] Last year, in addition to the assessment of the budgetary documents provided for by legislation, the Fiscal Council issued regular impact assessments of the measures taken, issued calls to fiscal policy-makers when individual legislative proposals were adopted, and at the very beginning of the crisis, enabled rapid action by the Government with an own-initiative declaration that the legal conditions for the enforcement of exceptional circumstances[32] had been met.

The scope of measures to limit the consequences of the epidemic depended on a number of factors. At the start of the epidemic, the nature of the measures taken, i.e. the distribution between direct (subsidies, transfers) and indirect (guarantees, loans) effects on the balance depended in particular on the state of public finances in the individual country prior to the start of the epidemic, as well as on the expected fall of GDP.[33] In the continuation of the year and during the second wave of the epidemic towards the end of 2020, when financing conditions remained favourable due primarily to monetary policy measures, fiscal space at the beginning of the crisis no longer played a significant role in the selection of measures. The volume of measures was influenced more significantly by the actual course of the epidemic in each country. It depended to a large extent on the intensity of the restrictive measures and on the timing of their introduction in view of the course of the epidemic.[34] As a rule, the fall in economic activity or private demand and the scope of aid measures were lower in the countries that adopted restrictive measures in timely manner.[35] The scope of measures or the effect of the epidemic on the public finance situation in each country was also significantly influenced by the structure of the economy. In countries with a relatively higher proportion of tourism or service activities involving personal contact, the nature of the restrictive measures required a larger scope of aid and, in particular, in these countries there was a greater decline in economic activity (see Figure 3.4).[36]

Countries responded to the crisis with extensive measures, which were the key factor in a significant deterioration of public finances. According to the IMF, the estimated volume of discretionary measures announced or adopted at the end of 2020 was 13.5% of GDP globally, of which 7.4% of GDP having a direct effect on the balance of public finances.[37] At EU level, the IMF estimated that the measures announced by the end of 2020 were worth 10.6% of GDP, of which 3.8% with a direct effect on the state of public finances. In the course of the epidemic, however, in most countries, including Slovenia,[38] the assessment of the measures at the time of their adoption proved to be much higher than the actual outturn. In addition to discretionary measures, the operation

[31] https://read.oecd-ilibrary.org/view/?ref=133_133360-7vldtk948h&title=Independent-fiscal-institutions-promoting-transparency-and-supporting-accountability-during-the-Coronavirus-%28COVID-19%29-pandemic.

[32] For more information on the activities of the Fiscal Council of the Republic of Slovenia, see the Report on the Fiscal Council's operation in 2020 (https://www.fs-rs.si/wp-content/uploads/2021/05/Report-on-the-FC-operations-in-2020.pdf).

[33] The assessments of the Fiscal Council show that the size of direct measures throughout 2020 was statistically significantly positively related to the baseline debt level at the end of 2019 and statistically significantly negatively related to the projected GDP growth in spring 2020.

[34] According to the Fiscal Council estimates, this relationship is also statistically significant.

[35] See IMF Fiscal Monitor, April 2021 (p. 11).

[36] Assessments of the Fiscal Council show that the fall in GDP in 2020 in the EU average was greater by about 0.4 pps for each of the pps of the share of tourism in GDP.

[37] https://www.imf.org/en/Topics/imf-and-covid19/Fiscal-Policies-Database-in-Response-to-COVID-19.

[38] At the time of the adoption of the Act determining the Intervention Measures to Contain the COVID-19 Epidemic and Mitigate its Consequences for Citizens and the Economy (PKP1) the government estimated the effect at EUR 3 billion. Its actual realisation was by half lower. At the time of the adoption of the Act determining the Intervention Measures to Mitigate and Remedy the Consequences of the COVID-19 Epidemic (PKP3), the effect was estimated at EUR 1 billion; however, its realisation represented only around one third of the estimated amount.

of automatic stabilisers also contributed to the deterioration.[39] The general government deficit at EU level increased from -0.5% of GDP to -6.9% of GDP last year, while the EC estimated that approximately half of the deterioration is a direct consequence of measures to limit the consequences of the epidemic.[40] At global level, average public debt reached its peak so far (99% of GDP),[41] and at EU level it increased by 13.2 pps to 90.8% of GDP last year.

In Slovenia, the deterioration of the general government balance, mainly due to the large amount of discretionary measures to limit the consequences of the epidemic in 2020, was among the largest in the EU. The general government balance in Slovenia turned from a surplus of 0.4% of GDP in 2019 to a deficit of -8.4% of GDP last year. This was the fourth largest deterioration among EU Member States. At the same time, various impact assessments of automatic stabilisers indicate that their effect is slightly lower than the average of the euro area.[42] Thus, the deterioration was mainly due to the scope of discretionary measures. On the basis of the 2021 Stability Programme data, these measures accounted for 6.0% of GDP last year, the fourth largest of the 22 EU Member States for which data are available.[43] At the same time, last year gross government debt increased by 15.2 pps to 80.8% of GDP, which was the ninth largest increase among EU Member States, around one quarter of this being contributed by an increase in the treasury account balance. In addition to measures with direct effect, guarantees were introduced under two guarantee schemes and a guarantee from the Slovene Enterprise Fund, the possibility of borrowing via liquidity loans and the possibility of deferring the payment of credit liabilities, which will only have a conditional effect on the balance. Under the two guarantee schemes, a total of EUR 15 million of guarantees were issued last year, representing around 5% of the total available value, while the European Commission estimated that around a quarter of all available guarantees were issued on average.[44]

The structure of discretionary measures in Slovenia deviates slightly from other countries for which data are available.[45] Most measures to limit the consequences of the epidemic had an effect on public expenditure. Measures in Slovenia on expenditure side accounted for 5.2% of GDP last year, while the EU average was 3.3% of GDP according to European Commission data.[46] Among Member States for which data are available, the scope of measures with an effect on expenditure was higher only in Lithuania. Looking at expenditures, a major part of the effect of the measures in most countries consisted of subsidies aimed primarily at maintaining jobs, while in Slovenia they accounted for half of all discretionary expenditure. Measures in the field of social transfers accounted for 1.0% of GDP in Slovenia, their share was higher only in Luxembourg and Lithuania. Deviation was greatest in the structure of measures to limit the consequences of the epidemic on compensation for employees covering public sector employee allowances. Last year, these measures accounted for 0.7% of GDP in Slovenia, a maximum among 15 Member States, for which detailed data on the structure of measures according to the ESA methodology are available. On the revenue side, last year, discretionary

[39] For more information on the functioning of automatic stabilisers in euro area countries during the epidemic, see the ECB Economic Bulletin 06/2020, pp. 115-132 (https://www.ecb.europa.eu/pub/pdf/ecbu/eb202006.en.pdf).

[40] EC Spring Forecast, May 2021 (p. 38).

[41] IMF Fiscal Monitor, April 2020 (p. xi).

[42] See ECB Economic Bulletin 06/2020, p. 121 and 123.

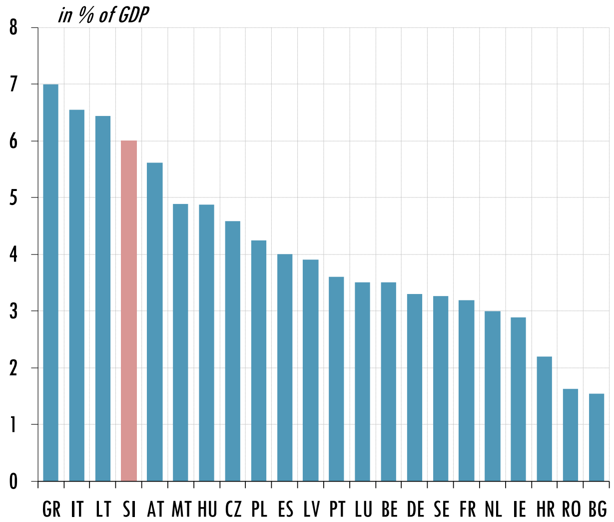
[43] Based on the Stability Programmes of individual Member States, the scope of discretionary measures to limit the consequences of the epidemic under the ESA methodology is available for 22 Member States. Stability programmes 2021 are available at: https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/european-semester/european-semester-timeline/national-reform-programmes-and-stability-or-convergence-programmes/2021-european_en.

[44] https://ec.europa.eu/info/sites/default/files/economy-finance/1_en_act_part1_v9.pdf.

[45] Detailed data on the structure of discretionary measures under the ESA methodology on the basis of the submitted Stability Programmes 2021 are available for 15 Member States.

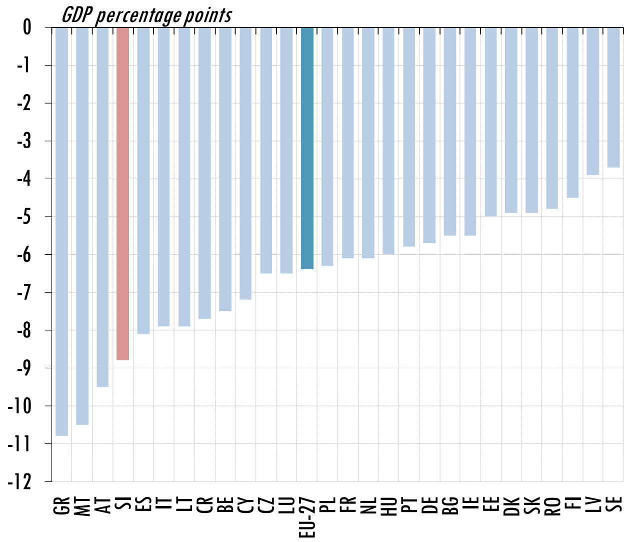
[46] https://ec.europa.eu/info/sites/default/files/economy-finance/1_en_act_part1_v9.pdf.

Figure 3.1: Volume of discretionary measures to mitigate the effects of the epidemic, 2020



Source: ECFIN.

Figure 3.2: Change in general government balance 2020/2019



Source: Eurostat, FC calculations.

measures in Slovenia accounted for 0.8% of GDP, which is twice as high as the EU average.[47] This share was only higher in Luxembourg while being at the same level in Germany and Austria.

Discretionary measures made a significant contribution to mitigating the fall in economic activity in Slovenia last year; however, the fall was only slightly smaller than the EU average, despite a higher scope of measures. Slovenia ranked 10th in the EU in 2020 by percentage fall in GDP. According to the assessment of the Fiscal Council, the level of GDP last year, without measures of 6% of GDP, would be around 3% lower than the current estimates, according to seasonally adjusted data, that real GDP declined by 6.1%.[48] The decline in GDP at EU level was similar, it amounted to -6.3% of GDP, whereas without discretionary measures of 3.8% of GDP the European Commission estimated that the decline in GDP would be deeper by 4.5 pps.[49] The finding is similar when based on a simple estimate of a short-term "multiplier" of the impact of the measures on the GDP change[50], which in Slovenia is about one half below the EU average[51] in 2020. Despite possible methodological differences in the calculation of the impact of measures on economic activity and the impact of differences in the structure of the economy[52], it can be estimated on the basis of these data that measures to limit the effects of the epidemic in Slovenia in 2020 were less effective or less suitably targeted than the EU average. The inadequate orientation of the measures is also reflected in the evolution of household savings. In Slovenia, an important part in absolute terms and in relation to other countries was measures that affected disposable household income (particularly employee allowances and social transfers to different population groups). According to the data available for the 18 EU Member States, last year the highest increase in household savings in the EU was recorded in Slovenia. It increased by 11.7 pps, whereas the EU average increased by almost half less, by 6.5 pps. Studies

[47] https://ec.europa.eu/info/sites/default/files/economy-finance/1_en_act_part1_v9.pdf.

[48] The UMAR estimated that without measures the last year's fall in GDP would be higher by 4 pps. (https://www.umar.gov.si/fileadmin/user_upload/napovedi/pomlad/pomladanska_2021/angleska/Spring_Forecast_of_Economic_Trends_2021_01.pdf).

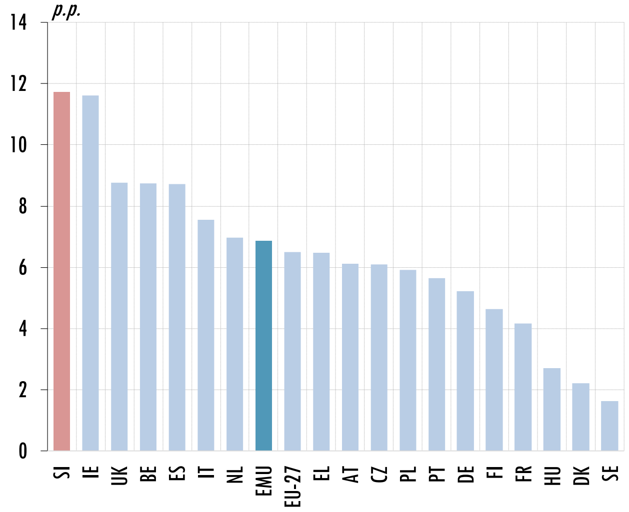
[49] https://ec.europa.eu/info/sites/default/files/economy-finance/1_en_act_part1_v9.pdf.

[50] GDP change as a result of measures is defined on the basis of the change between autumn and spring GDP forecasts prepared by the EC for individual countries in 2020.

[51] For the EU average, this "multiplier" is around 0.6, and for Slovenia just below 0.3 (1 pps of GDP measures contributed to a change in the forecast or to a higher GDP growth of 0.3 pps in the short term).

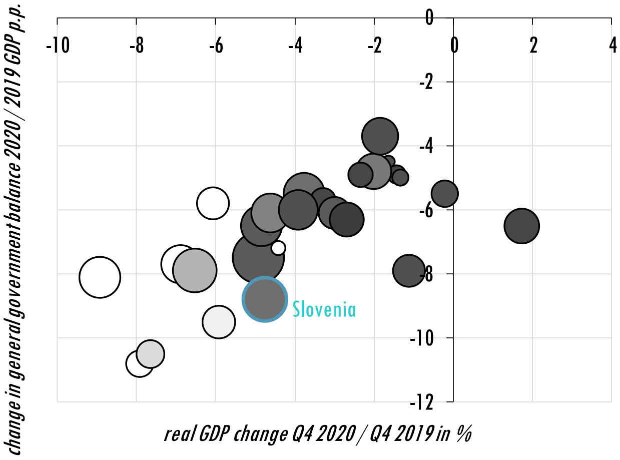
[52] The fall in value added in Slovenia last year was 4.9%; with the same structure as the EU average, it would be lower by 0.3% pps.

Figure 3.3: Change in household saving rate 2020/2019



Source: Eurostat, FC calculations.

Figure 3.4: EU countries according to change in GDP and general government balance in 2020



-size of the bubble reflects the number of COVID deaths per million in 2020
-lighter colour reflects a bigger share of activty I (Accommodation and food service activities) in the GDP in 2019
Source: Eurostat, ourworldindata.org, FC calculations.

of similar measures in other countries[53] also point to the fact that the transfers to the population, in a period when consumption is limited due to restrictive measures, are inefficient. In the field of the labour market, measures contributed significantly to a less pronounced increase in the unemployment rate in all countries. In Slovenia, according to seasonally adjusted data, the survey unemployment rate increased by 1.1 pps between the last quarter of 2019 and the last quarter of 2020, which was slightly above the EU (by 0.7 pps).[54] It should be noted that a significant proportion of employees were still included in measures to preserve jobs (temporary lay-off, subsidised short-time work, quarantine and force majeure) even at the beginning of 2021, which is the reason that a final assessment of the effectiveness of these measures cannot be given. While internationally comparable data on the number of employees included in these measures are not available, it should be pointed out that in December last year 87,283 unemployed persons were registered in Slovenia, and according to the Employment Service of Slovenia, 90,876 persons were included in the abovementioned measures this month.[55] What proportion of these persons might become unemployed on withdrawal of the measures depends on the further development of the epidemic, duration of the aid measures, speed of recovery in demand and economic activity in general, and financial situation in enterprises.

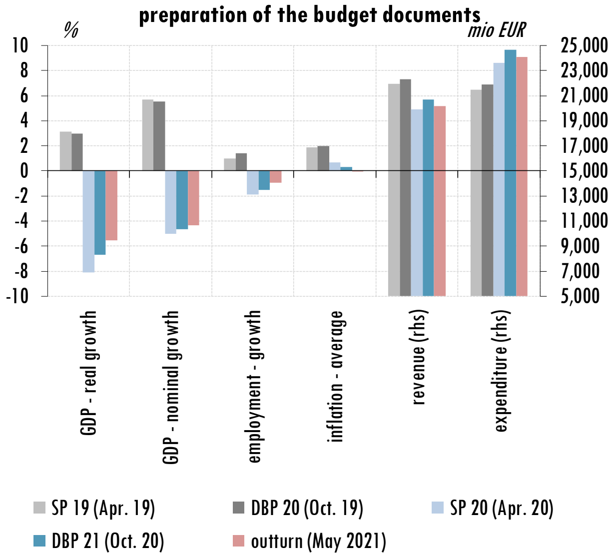
[53] See for example://www.nber.org/system/files/working_papers/w27693/w27693.pdf.

[54] Estimates of short-term unemployment "multiplier" (changes between autumn and spring forecasts of EC unemployment rates considering the full range of measures) show that it was almost the same as in the EU (-0.3).

[55] According to the Employment Service of Slovenia data of 27 May 2021.

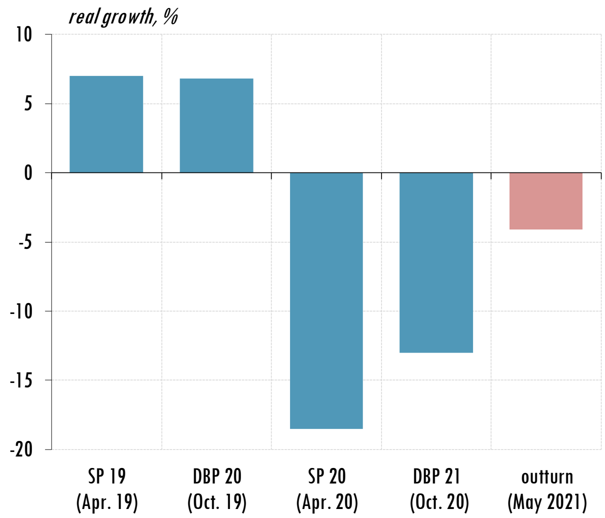
Annex 4.1 Changes in the macroeconomic and fiscal projections for 2020

Figure 4.1: Forecasts for 2020 available at the time of preparation of the budget documents



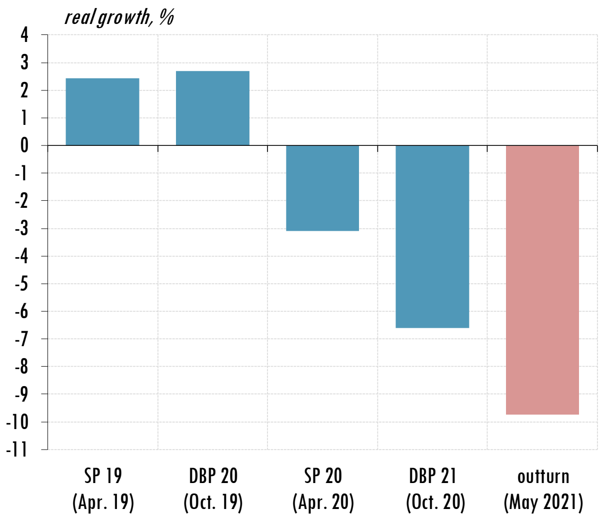
Source: forecasts IMAD, MoF; outturn SORS.

Figure 4.2: Changes in the 2020 forecast – gross fixed capital formation



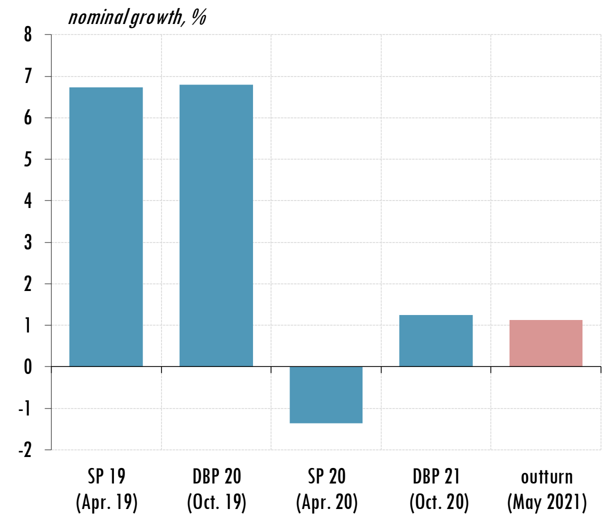
Source: SORS, forecasts IMAD.

Figure 4.3: Changes in the 2020 forecast – private consumption



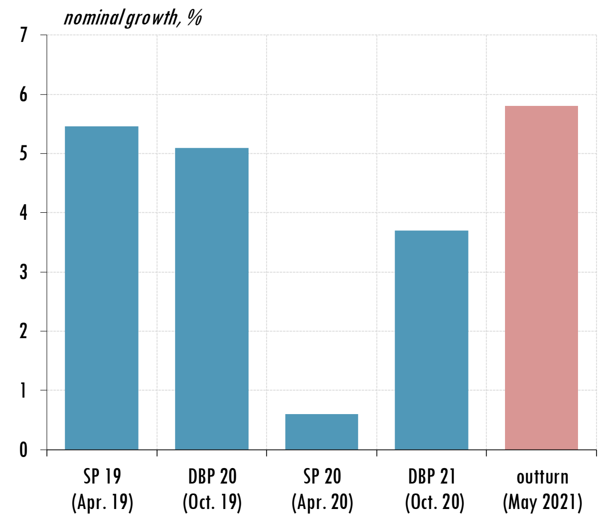
Source: SORS, forecasts IMAD.

Figure 4.4: Changes in the 2020 forecast – compensation of employees



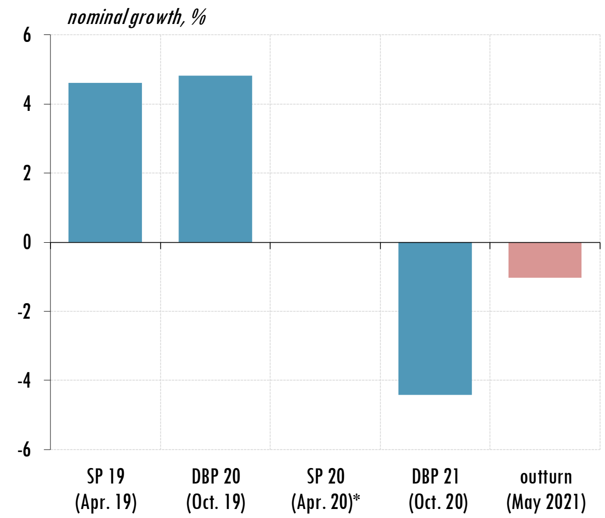
Source: SORS, forecasts IMAD.

Figure 4.5: Changes in the 2020 forecast – gross wages per employee



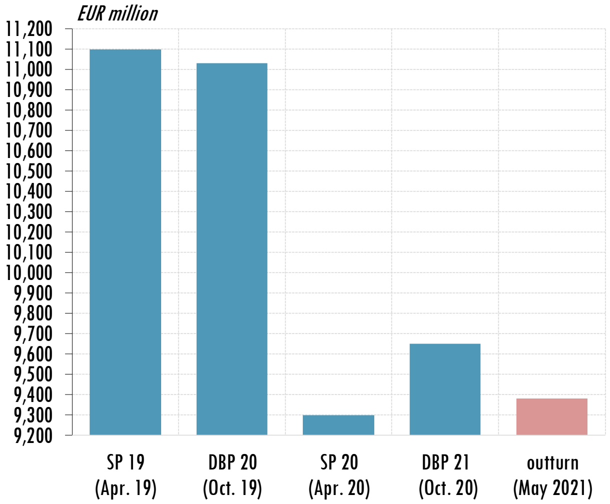
Source: SORS, forecasts IMAD.

Figure 4.6: Changes in the 2020 forecast – gross operating surplus/mixed income



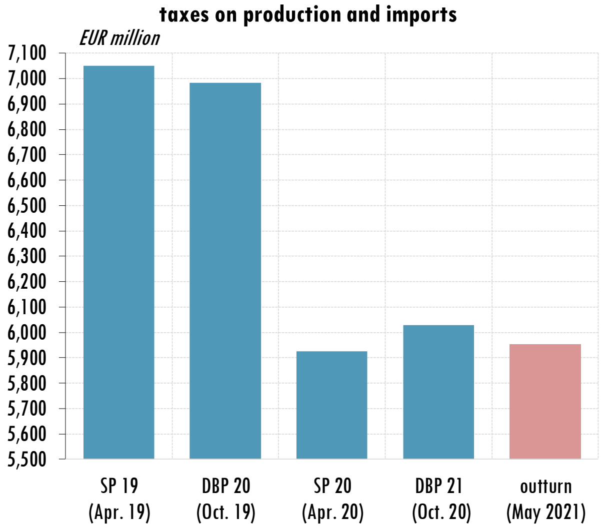
Source: SORS, forecasts IMAD. *A forecast of this aggregate was not published.

Figure 4.7: Changes in the 2020 forecast – total taxes



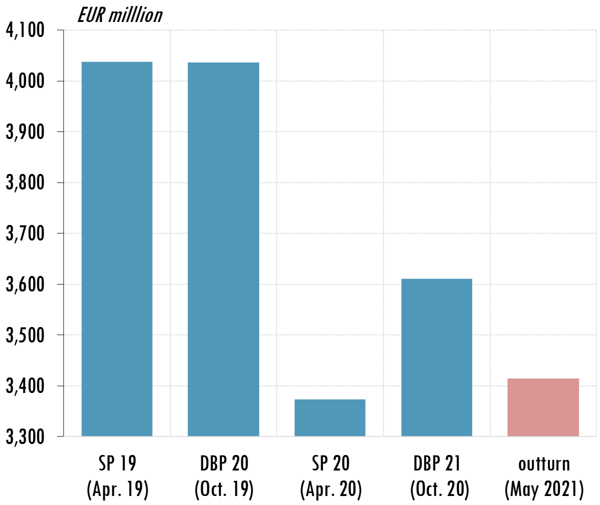
Source: SORS, forecasts MoF.

Figure 4.8: Changes in the 2020 forecast – taxes on production and imports



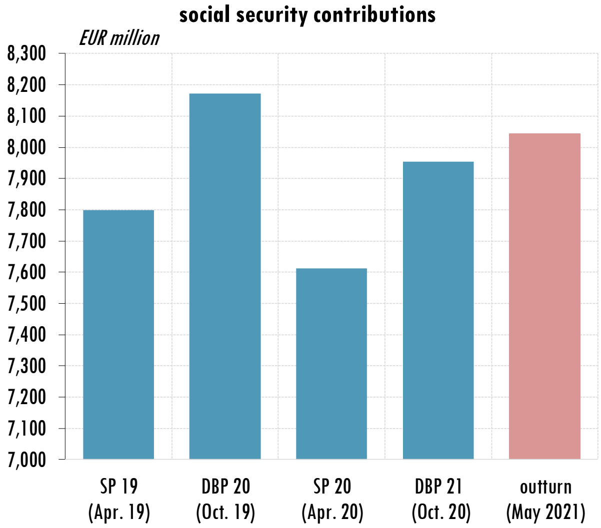
Source: SORS, forecasts MoF.

Figure 4.9: Changes in the 2020 forecast – current taxes on income and wealth



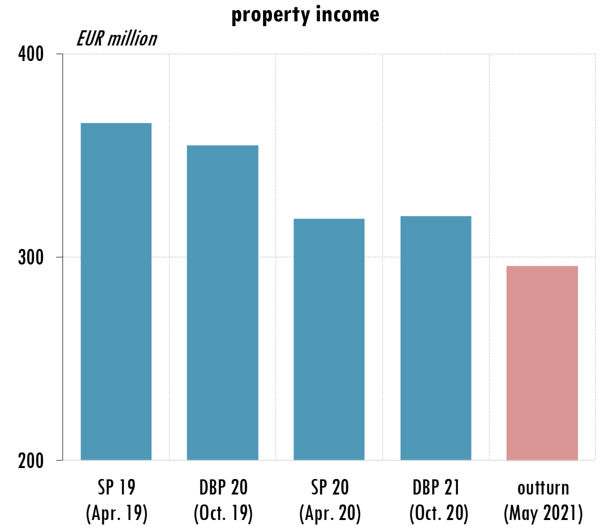
Source: SORS, forecasts MoF.

Figure 4.10: Changes in the 2020 forecast – social security contributions



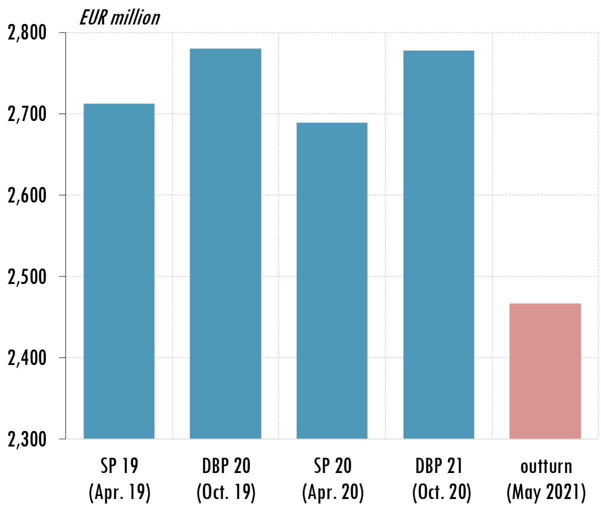
Source: SORS, forecasts MoF.

Figure 4.11: Changes in the 2020 forecast – property income



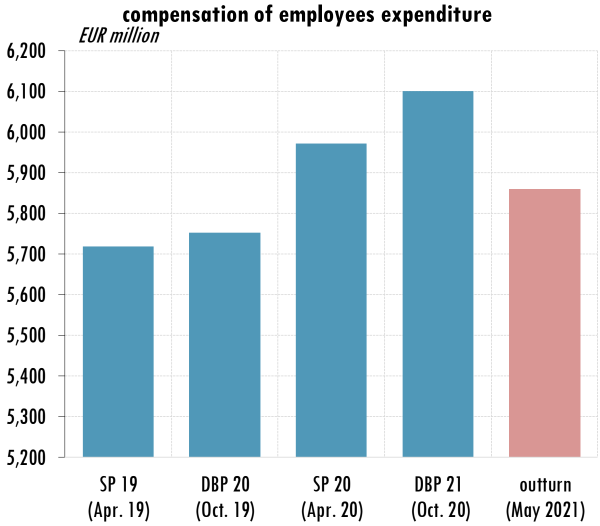
Source: SORS, forecasts MoF.

Figure 4.12: Changes in the 2020 forecast – other revenue



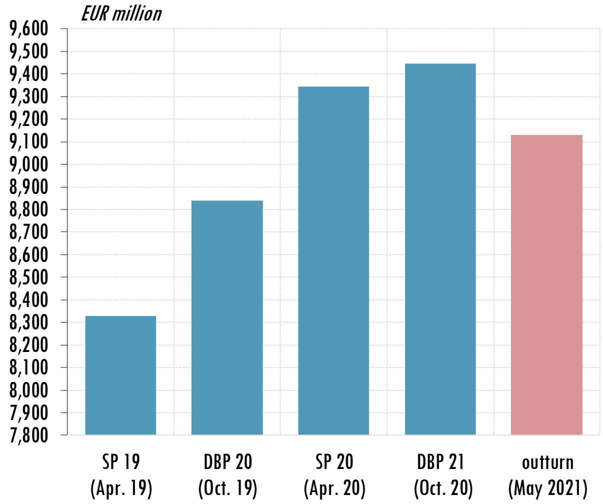
Source: SORS, forecasts MoF.

Figure 4.13: Changes in the 2020 forecast – compensation of employees expenditure



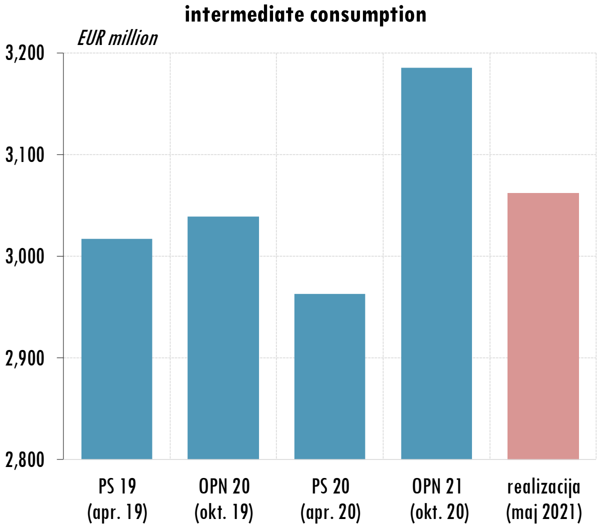
Source: SORS, forecasts MoF.

Figure 4.14: Changes in the 2020 forecast – social benefits



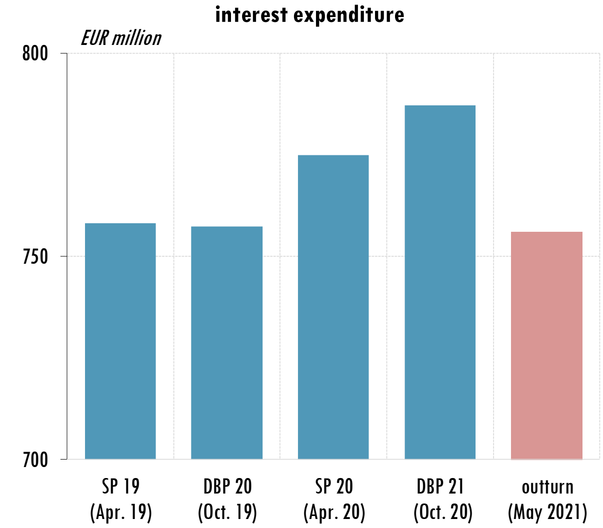
Vir: SURS, napovedi MF.

Figure 4.15: Changes in the 2020 forecast – intermediate consumption



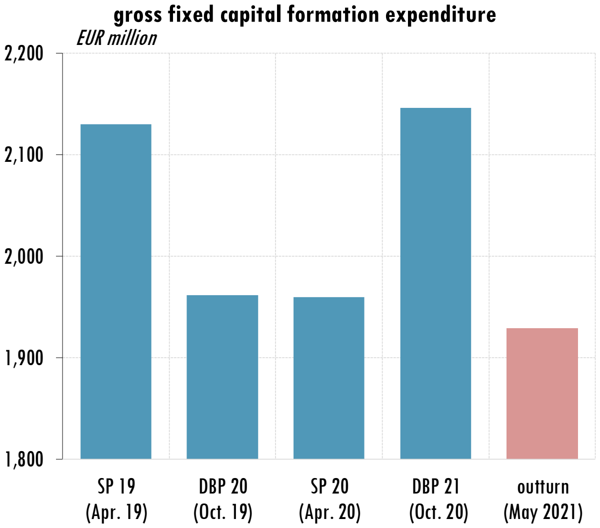
Source: SORS, forecasts MoF.

Figure 4.16: Changes in the 2020 forecast – interest expenditure



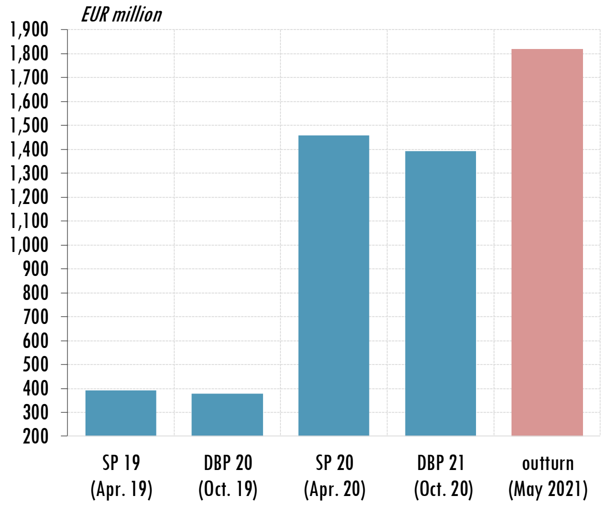
Source: SORS, forecasts MoF.

Figure 4.17: Changes in the 2020 forecast – gross fixed capital formation expenditure



Source: SORS, forecasts MoF.

Figure 4.18: Changes in the 2020 forecast – subsidies



Source: SORS, forecasts MoF.

Annex 4.2 Output gap and structural balance estimates for 2020

Table 4.1: General government structural balance according to various output gap estimates

2020	Blanchard Quah (Apr.21)	Factor models (Apr.21)	HP (Apr.21)	Long.term average (Apr.21)	IMF (Apr.21)	OECD (May 21)	EC (May 21)	IMAD (Mar.21)	MoF (Apr.21)	average EC, MoF,IMAD*	**average total**	min	max	MTO
Output gap	-1.5	-4.4	-4.1	-4.7	-4.8	-8.1	-3.4	-2.9	-3.1	-3.1	**-4.1**	-8.1	-1.5	-
COVID measures included as one-offs														
Structural balance	-1.6	-0.3	-0.4	-0.1	-0.1	1.5	-0.7	-1.0	-0.9	-0.9	**-0.4**	-1.6	1.5	-0.25
COVID measures not included as one-offs														
Structural balance	-7.6	-6.3	-6.4	-6.1	-6.1	-4.5	-6.7	-7.0	-6.9	-6.9	**-6.4**	-7.6	-4.5	-0.25

*Note: *institutions that calculate output gap on the basis of commonly agreed methodology according to SGP.*
Sources: IMAD, EC, MoF, IMF, OECS, FC calculations.