Speech delivered by President Kračun at the meeting of the Commission for Public Financial Control (3 February 2023)

Efficient management of compensation of employees in the general government sector is important in terms of both their impact on the sustainability of public finances and ensuring an adequate quality of public services. As the debate on this topic is accompanied by strong vested interests and deep-rooted perceptions, I will start by presenting some key facts about compensation of employees in the public sector over a slightly longer time horizon.

Funds for compensation of employees constitute about a quarter of all general government expenditure and thus have a significant impact on the sustainability of the fiscal situation. With the exception of the period between 2013 and 2015, when it fell slightly, their share in total expenditure was fairly constant between 2004 and 2018. A general agreement on an increase in wages was then adopted at the end of 2018, and work performance payments were freed up in mid 2020 after several years of being frozen. These two factors contributed to a slight increase in the share of total expenditure.

The share of compensation of employees in GDP has fluctuated more widely over the period since 2004. On average for the first three quarters of last year, for which the latest data are available, their share was at its lowest level since the introduction of the single wage system in 2007 and 2008, respectively. This indicator is considered by the Fiscal Council to be one of the most relevant when discussing public sector labour costs. Indeed, it shows the burden that public sector financing represents in the light of the capacity of the national economy as a whole.

At 11% on average in the first three quarters of last year, this share was around 1 percentage point higher than the EU average, with considerable variation between the Member States. It is important to note that in the period between 2004 and the start of the epidemic, employment in the general government sector in Slovenia increased by around four times more than the average of the 22 EU Member States for which data are available. However, real growth in compensation per employee or in wages was cumulatively around 10%, practically the same as the average of the 22 Member States.

Against this general background, trends have of course varied considerably from one part of the public sector to another. The largest increases in compensation of employees between 2004 and the epidemic have been in social protection and health, which is more prominent because of its size. While the increase in social protection was largely driven by employment growth, the increase in health care, alongside employment growth, was also driven by real wage growth, which was the highest in the public sector. On the other hand, the increase in the compensation of employees in education and administration was smaller, but due to completely opposite factors. While employment in education increased, real wages were practically at their 2004 level before the epidemic. By contrast, employment in the administrative sector is at its 2004 level, and real wages increased at a similarly high rate as in the health sector before the epidemic. These factors are important for understanding the demands of different parts of the public sector.

The increased expectations in the public sector could be largely due to the large epidemic bonuses, which, according to the Court of Audit's assessment, were paid in a non-transparent manner and largely expired last year. A number of partial agreements in recent years have also contributed significantly to raising expectations. The large number of stakeholders restricts the effectiveness of the negotiation process and, in the light of the preservation of a centralised wage determination system, allows the possibility of general wage increases even when they are not justified in terms of employee performance or fiscal sustainability. At the same time, the wage agreements did not, or even this time do not, include measures that would lead to improvements in the efficiency and accessibility of public services. The fragmentation of negotiations also reduces the transparency of the wage system. This, together with the regular practice where wage agreements are largely reached only after the adoption of budget documents, reduces the quality of budgetary planning and is also contrary to the law. In terms of its impact on the sustainability of public finances, one of the major shortcomings of the system for managing compensation of employees is the lack of emphasis on planning and active management of the number of employees.

In the context of the current demands for additional pay rises, a few facts are key.

First, average compensation per employee in the general government sector was, according to the latest available data, at a similar level in real terms in the third quarter of last year as before the start of the epidemic. The general agreement on wages in the public sector concluded last October should at least compensate for projected inflation this year. The real purchasing power of public employees has thus been largely preserved, despite the two major crises in the last three years, by the agreements adopted so far.

Second, extensive inflation mitigation measures were taken that had a significant impact on public finances, which also benefit public employees.

Third, the projected deficit for this year is already among the highest in the EU, without additional pay rises. At the same time, spreads on Slovenian government bonds have risen more than they did in some comparable countries over the past year. Additional permanent increases in current spending could lead to a further deterioration in the perception of Slovenia on financial markets.

Fourth, a new EU fiscal framework is in the process of being adopted, with a stronger focus on medium-term debt sustainability than in the past. However, the first simulations carried out at the Fiscal Council show that the medium-term fiscal policy room for manoeuvre will to a large extent be defined by the initial position of the structural balance. That is also why it is necessary to avoid a structural deterioration of the fiscal situation due to wage agreements without adequate measures to balance public finances.

Fifth, with the announced reform of the wage system, it would be naïve to expect, based on past experience, that it will not lead to an increase in general government expenditure.

Thus, the Fiscal Council calls on all stakeholders to refrain, until the reform is implemented, from taking steps that would lead to further increases in labour costs compared to the situation before the adoption of the 2023 budget documents. The dissatisfaction with the partial agreements reached after the introduction of the general agreement last October is to a certain extent understandable. However, additional increases in budgetary expenditure on wages before the introduction of the reform are not acceptable in the light of the above-mentioned facts, not least because they indirectly reduce, at least in part, the effectiveness of the inflation mitigation measures. We also call for the entire process of adopting the wage reform, as well as all other reforms, to give due weight to their financial impact and, taking into account available resources, to their impact on the medium-term sustainability of public finances.