REPUBLIC OF SLOVENIA
FISCAL COUNCIL

Report on the Fiscal Council's operations in 2022

May 2023

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FOREWORD

2022 was characterised by a strong rebound in economic activity after the end of the epidemic. Slovenia recorded high economic growth and an increase in employment. At the same time, however, this was accompanied by high inflation, which is actually a broader European and global phenomenon, stemming mainly from global supply-side restrictions and expansionary economic policies. The ECB has responded to rising inflation by tightening monetary policy, which lags somewhat behind the US Fed in both the initiation and scope of action. Such a response brings characteristic risks to the financial system and thus to European economies, and indirectly increases the cost of financing the general government. While inflation was largely imported into Slovenia, the adjustment process, which autonomously generates domestic inflation, started already in the second half of the year.

Domestic fiscal policy did not align with the European monetary policy stance. The actual general government deficit, while slightly lower than forecast, was relatively high given the buoyant economic activity. Excluding the impact of measures to limit the impact of the epidemic and of the cost-of-living crisis, the budget was close to balanced. Deficits are projected to persist over the medium term, but to decline gradually – provided that economic growth rates are not lower than projected. The outlook for economic activity is related to a number of risks, stemming from both the global environment and possible ill-considered domestic policy decisions.

Slovenia's public debt is above the Maastricht limit of 60% of GDP. In the short term, risks are relatively low, as they are mitigated by the good liquidity position of the government budget, while rising interest rates will only gradually increase budget interest costs. Deficits will lead to an increase in public debt in absolute terms, but debt will decline in relative terms if nominal GDP growth rates are sufficiently high. However, demographic challenges and other expected costs that will be borne by public finances in the future are accumulating risks related to the long-term sustainability of public debt.

Despite the proposal made by the European Commission in April this year, uncertainties regarding the revamp of the European fiscal rules are currently still present. Whatever the individual countries' interests in their formulation are, it is important that on the financial markets the EU as a whole enjoys the full confidence of investors as a reliable partner. Credible fiscal rules that are binding and are acceptable to Member States without any reservations are a prerequisite for government bonds to be sold on financial markets under appropriate conditions, thus allowing the smooth financing of development plans.

Also in these uncertain circumstances, the Fiscal Council will consistently pursue its mission of monitoring and warning about the sustainability of public finances in the medium and long term. Here the main tool remains the power of argumentation. At this point, I would like to thank the media for their extensive coverage of the Fiscal Council's activities. Fiscal policy decisions, while guided by democratically elected bodies, affect everyone's lives. It is therefore important that the transparency made possible by the wide publication of the Fiscal Council's assessments ensures that everyone can follow fiscal policy. In this way, democratic pressure is created on decision-makers, while at the same time the assessments help decision-makers to take fiscally sustainable decisions on budget documents.

All members of the Fiscal Council were re-appointed in March 2022 for a new five-year term of office.

May 2023

Dr Davorin Kračun,

President of the Fiscal Council

1. The Fiscal Council's operations in 2022

The Fiscal Rule Act (hereinafter: the FRA),[1] adopted in July 2015 by the National Assembly of the Republic of Slovenia (hereinafter: the National Assembly), constitutes the basis for the establishment and operation of the Fiscal Council. The FRA defines, *inter alia*, the tasks, composition and method of operation of the Fiscal Council. Its members were appointed by a constitutional majority in the National Assembly for a five-year term of office on 21 March 2017, when the Fiscal Council began its work. Thus, in 2022, five years after the Fiscal Council started its work, the existing members of the Fiscal Council were reconfirmed for a new five-year term after the expiry of their first term of office. In accordance with Article 10 of the FRA, the Fiscal Council is required to submit an annual report on its work to the National Assembly for consideration by the end of May each year for the previous year. The Fiscal Council drew up its first annual report for 2017 in May 2018. The present report covers the main aspects of the operation of the Fiscal Council in 2022.

1.1 The composition and operation of the Fiscal Council

The Fiscal Council is an independent and autonomous state authority that assesses the appropriateness of the planned and implemented fiscal policy, i.e. its compliance with statutory fiscal rules. It is accountable solely to the National Assembly, which approves and may replace its members, who are otherwise appointed for a five-year term of office. The autonomy of its authority is an essential condition for the provision of opinions that are not subject to political developments each time a new government takes office. This is facilitated by the two-thirds majority vote of all deputies required for the appointment of the Fiscal Council's members and the autonomous management of the funds allocated from the state budget.[2] In budget planning, the Fiscal Council itself proposes the funds it needs for its operation in accordance with the FRA. The autonomy of and strong analytical support for the Fiscal Council's opinions are essential for its credible and autonomous operation. The guiding principle in the formulation of the Fiscal Council's opinions on public finances is a focus on the medium and long term, as only long-term stable and sustainable public finances can provide the basis for economic development and thus for the well-being of the population.

The tasks of the Fiscal Council are defined by the FRA. They are linked above all to assessing the adequacy of budget documents, which must ensure compliance with statutory fiscal rules and fiscal stability in the medium term. The Fiscal Council also assesses whether exceptional circumstances that justify a deviation from the medium-term fiscal balance have arisen and when they cease to exist. The full range of the Fiscal Council's tasks is described in Article 7 of the FRA. In addition to the provisions of the FRA, the Act Amending the Public Finance Act of February 2018 (hereinafter: the ZJF-H)[3] imposed on the Fiscal Council the task of assessing the bias of the previous macroeconomic forecasts that represent the basis for preparing the budget documents. The Decree amending the Decree on development planning documents and procedures for the preparation of the central government budget of May 2018[4] imposes on the Fiscal Council the biennial task of subsequently assessing the general government sector's revenue and expenditure forecast. Considering the transitional periods

[1] http://www.pisrs.si/Pis.web/npbDocPdf?idPredpisa=ZAKO7056&type=doc&lang=EN

[2] For more information on operating costs and selected components of the Fiscal Council's 2022 balance sheet, see Annex 1.

[3] https://www.uradni-list.si/glasilo-uradni-list-rs/vsebina/2018-01-0544?sop=2018-01-0544 (Only in Slovene)

[4] https://www.uradni-list.si/glasilo-uradni-list-rs/vsebina/2018-01-1754?sop=2018-01-1754 (Only in Slovene)

Table 1.1: Annual schedule of releases by Fiscal Council and by other institutions

	week 1	week 2	week 3	week 4
January	**FC: Monthly information**			
February		**FC: Public Finance and Macroeconomic Dev.**	*SORS: National Accounts*	
March	**FC: Monthly information** *IMAD: macro projection*			*SORS: General Govt Accounts*
April	**FC: Monthly information** *MoF: proposed SP*	**FC: assess SP/FR**		
May	**FC: Monthly information**		*SORS: National Accounts* *EC: assess SP/CSR*	**FC: Annual Report**
June	**FC: Monthly information**			*SORS: General Govt Accounts* **FC: assess previous year**
July		**FC: Public Finance and Macroeconomic Dev.**		
August			*SORS: National Accounts*	
September	**FC: Monthly information** *IMAD: macro projection*			*SORS: General Govt Accounts* *MoF: FR*
October	**FC: Monthly information**	*MoF: SP, FR, DBP*	*SORS: EDP* **FC: assess FR/SB/DBP**	
November	**FC: Monthly information**	*EC: assess DBP*	*SORS: National Accounts*	
December	**FC: Monthly information**			*SORS: General Govt Accounts*

Note: This scheme shows the time aspect of Fiscal Council regular publication releases (in red) during a calendar year. Fiscal Council may publish assessments which are not mandated by law outside this schedule. Abbreviations: CSR: Country Specific Recommendation, DBP: Draft Budgetary Plan, EDP: Excessive Deficit Procedure Report, FR: Framework, SB: State Budget, SP: Stability Programme. In August 2020, the Fiscal Council published for the first time an analysis of deviations of forecasts of macroeconomic and fiscal aggregates. In accordance with legislation, this analysis must be prepared every two years, however, the legislation does not prescribe a deadline within an individual calendar year.
Source: Fiscal Council.

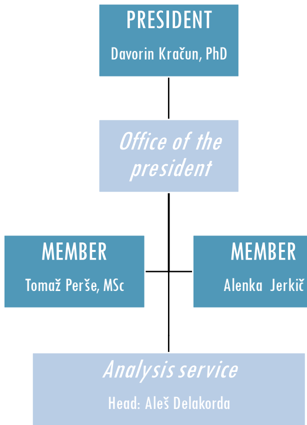
laid down by law, the Fiscal Council prepared the first two assessments of the past forecasts in 2020 and, in line with the legal constraints, the second one in a reduced form in 2022.[5]

The Fiscal Council has three members, i.e. its President and two members. The Fiscal Council members are elected for a term of five years and for no more than two consecutive terms. Article 8 of the FRA lays down that the office of a member of the Fiscal Council is incompatible with holding public office and activities entailing the management, supervision or representation of direct and indirect spending units of the budgets of the general government sector. After the expiry of the first term of office (2017–2022), all three existing members of the Fiscal Council had their term reconfirmed in March 2022 for a new five-year period.

The President represents the Fiscal Council, and organises and manages its work. In accordance with the provisions of Article 10 of the FRA, the President of the Fiscal Council must be employed by the

[5] Article 33 of the Act Providing Additional Liquidity to the Economy to Mitigate the Consequences of the COVID-19 Epidemic (ZDLGPE), adopted at the end of April 2020, stipulates that "...Notwithstanding the first paragraph of Article 9g of the ZJF, the Fiscal Council shall not take into account macroeconomic aggregates and revenue and expenditure forecasts for 2020 and 2021 in its analysis."

Figure 1.1: Organizational chart of the Fiscal Council



Source: Fiscal Council.

Fiscal Council for at least 50% of full-time employment. Currently, the President of the Fiscal Council is employed full-time with the Fiscal Council and the two members for 50% of full-time employment each.

The Rules of Procedure of the Fiscal Council, which were published in the Official Gazette of the Republic of Slovenia [*Uradni list RS*], No. 26/2017,[6] define the organisation and method of the Fiscal Council's work. The Fiscal Council usually meets once per week at closed sessions to discuss the current macroeconomic and fiscal developments and, *inter alia*, to decide on the publication of its opinions, press releases and documents.

Four public employees are employed by the Fiscal Council. This is also the maximum number of employees as laid down by paragraph five of Article 10 of the FRA. Public employees provide administrative and expert support to the Fiscal Council's members. The staffing of expert services was completed in October 2017 and remained unchanged in 2022. One public employee works in the President's office and performs administrative and organisational tasks, and three public employees work in the Analysis Service.

In accordance with paragraph six of Article 10 of the FRA, administrative and technical tasks (tasks related to staffing, information technology, accounting, public relations, etc.) for the Fiscal Council are performed by the services of the Court of Audit of the Republic of Slovenia (hereinafter: the Court of Audit), where the Fiscal Council's premises were located until April 2020. Due to changes in the Court of Audit's spatial requirements, the Fiscal Council began to look for new rental premises in which to perform its activities in 2019. The Court of Audit assisted the Fiscal Council in this process by looking for appropriate premises at the Ministry of Public Administration, but the Ministry was unable to provide such premises. The Fiscal Council moved to its new rented premises on Likozarjeva ulica 3 in Ljubljana in April 2020, where it has been operating since then. In agreement with the Fiscal Council, part of the premises is also used for the needs of the Court of Audit, which, also at the new location, provides administrative and technical support to the Fiscal Council under the FRA.

The Analysis Service provides expert assistance to the Fiscal Council's members. It regularly monitors and analyses macroeconomic and fiscal developments in Slovenia and abroad and prepares working

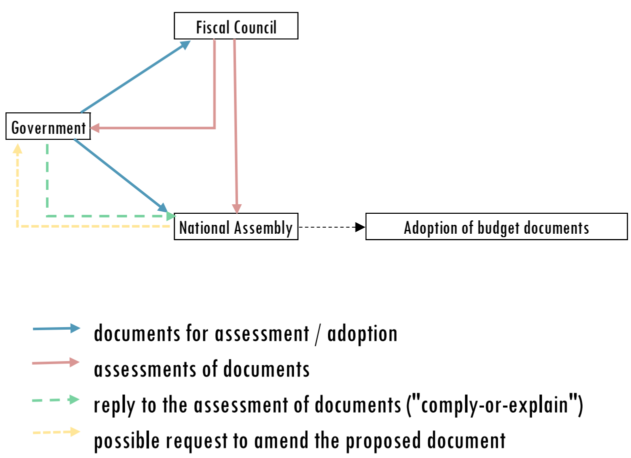
[6] https://www.uradni-list.si/glasilo-uradni-list-rs/vsebina/2017-01-1384?sop=2017-01-1384 (Only in Slovene)

documents for the members and expert groundwork for their opinions. The Analysis Service's priority tasks in 2022 included, in particular, monitoring the fiscal effects of measures to prevent the effects of the COVID-19 epidemic and to limit the impact of the cost-of-living crisis, permanent database management, maintaining and upgrading the automation of processes to monitor economic indicators, upgrading analytical tools for the analysis of cyclical and fiscal trends, managing the Fiscal Council's presence on Twitter and preparing regular and extraordinary publications of the Fiscal Council.

1.2 The main guidelines for the Fiscal Council's operation in 2022

In 2022, the Fiscal Council operated within the framework of its regular annual operating cycle, which was updated with new analyses and publications after the outbreak of the epidemic. The schedule of the annual cycle is largely defined by the FRA and the ZJF-H, and specifically by the procedure for preparing budget documents and by the publication of important macroeconomic and fiscal data. In addition to carrying out its statutory tasks, the Fiscal Council publishes opinions and press releases based on current macroeconomic and fiscal developments and planned legislative amendments that could have an impact on fiscal sustainability. The existing legislation, particularly Articles 12–14 of the FRA, also determines Fiscal Council actions in the event of exceptional circumstances, such as an epidemic. Thus, in March 2020, the Fiscal Council identified the existence of exceptional circumstances to support increased fiscal policy flexibility during the period of the epidemic and, in the following months, regularly monitored and published the fiscal effects of the measures taken to limit the impact of the epidemic. It also made significant changes to its publications to address the new situation, distinguishing between the analysis of aggregate fiscal data and the analysis of data that did not include the effects of fiscal measures taken to limit the impact of the epidemic. In addition, in January 2021 it launched a regular publication, entitled Monthly Information, which presents current developments in the state budget alongside ongoing monitoring of the fiscal impact related to the epidemic. The FRA does not explicitly prescribe the monitoring and publication of such data, but, in the Fiscal Council's opinion, this was necessary to ensure transparency on the one hand, and on the other to analyse on an ongoing basis the credibility of the budget documents prepared by the Government in

Figure 1.2: Relations between the Fiscal Council, the Government and the National Assembly during the process of adoption of budget documents



Source: Fiscal Council.

the period of exceptional circumstances and their compliance with applicable fiscal rules. The Fiscal Council continued the preparation of this publication also in 2022, which attracted considerable public interest (see Chapter 4).

To support its own operation, the Fiscal Council has concluded cooperation agreements with the Institute of Macroeconomic Analysis and Development (hereinafter: the IMAD) and the Ministry of Finance (hereinafter: the MoF).[7] In comparison with similar institutions operating in other EU Member States, the Fiscal Council is one of the smallest bodies in terms of staffing. This is one of the reasons why paragraph seven of Article 10 of the FRA also provides for the possibility of concluding cooperation agreements with institutional units of the general government sector, which are obliged under this Act to provide the Fiscal Council with all the information, analyses and data they have at their disposal. The two agreements define the data and documents that the two institutions have to provide to the Fiscal Council and the time limits for their provision. The cooperation agreement with the Ministry of Finance was supplemented in 2021, at the initiative of the Fiscal Council, by an agreement to extend the set of data produced by the Ministry of Finance and needed by the Fiscal Council for the performance of its tasks.

In 2022, the Fiscal Council met with representatives of domestic institutions on several occasions. The cooperation agreements concluded with the MoF and the IMAD also include a provision on holding regular meetings at the technical level for the purpose of informing the Fiscal Council of the current macroeconomic and fiscal developments and forecasts. The Fiscal Council's Analysis Service held meetings at the technical level with the representatives of the two institutions on a regular basis in 2022.

For the purpose of its operation, the Fiscal Council also needs data and information that are not available to the public. In 2022, for the purpose of making analyses and providing opinions, the Fiscal Council, in accordance with the FRA, requested data and information from the Ministry of Labour, Family, Social Affairs and Equal Opportunities, the Ministry of Finance, the Ministry of Economic Development and Technology, the Ministry of Infrastructure, the Ministry of Public Administration, the Ministry of the Environment and Spatial Planning, the Ministry of Health, the Eco Fund, the Employment Service of Slovenia, the Finance Office of the Republic of Slovenia, the Agency of the Republic of Slovenia for Public Legal Records and Related Services, the Statistical Office of the Republic of Slovenia, the Health Insurance Institute of Slovenia, the Pension and Disability Insurance Institute of Slovenia and the Slovene Enterprise Fund, with which it does not otherwise have a cooperation agreement in place.

In 2022, the Fiscal Council met once (May) with the Prime Minister and the Minister of Finance, and the President of the Fiscal Council met additionally (September) with the Minister of Finance.

In 2022, after a one-year interval due to the epidemiological constraints, the Fiscal Council resumed regular consultations with Slovenian economists engaged in public finances. The first consultation focused on various aspects of the changes to the fiscal rules,[8] while the second one was devoted to the proposed reform of the EU's economic governance system.[9]

[7] Both agreements are published on the Fiscal Council's website: https://www.fs-rs.si/fiscal-council/co-operation/ (Only in Slovene).

[8] https://www.fs-rs.si/fiscal-council-consultation-on-fiscal-rule-changes/

[9] https://www.fs-rs.si/fiscal-council-consultation-at-the-end-of-2022/

2. The Fiscal Council's opinions and the Government's responses in 2022

The main part of the Fiscal Council's operation in 2022 continued to relate to the tasks set out in the FRA. In this regard, it should be noted that paragraph four of Article 7 of the FRA lays down that the Government of the Republic of Slovenia (hereinafter: the Government) is obliged to respond to the opinions provided by the Fiscal Council in accordance with this Act. The Government must draw up a written reasoned opinion on the assessments of the Fiscal Council and submit it to the National Assembly. This is the "comply-or-explain" principle laid down in EU law in Directive 2011/85/EU. The drafting of written reasoned opinions by the Government increases the transparency of its operations, while its failure to adhere to Fiscal Council recommendations increases its political responsibility in the conduct of public fiscal policies.

In accordance with the FRA, the Fiscal Council made the following assessments in 2022:[10]

- on 10 May 2022, it submitted to the National Assembly and the Government the Assessment by the Fiscal Council of the compliance of fiscal policy with the fiscal rules on the basis of the draft 2022 Stability Programme (as laid down in point 1 of paragraph two of Article 7 of the FRA); in this regard, it informed the public on 13 April 2022 that it had not received the draft 2022 Stability Programme from the Government by the statutory deadlines;

- on 24 May 2022, it submitted to the National Assembly the Report on the Fiscal Council's operation in 2021 (as laid down in point 8 of Article 10 of the FRA);

- on 21 June 2022, it submitted to the National Assembly and the Government the Assessment by the Fiscal Council of the compliance of the implemented general government budgets with the fiscal rules in 2021 (as laid down in point 4 of paragraph two of Article 7 of the FRA);

- on 22 August 2022, it submitted to the National Assembly and the Government its Analysis of deviations of macroeconomic and fiscal aggregates in the period 2018–2021 (as laid down in Article 9g of the Public Finance Act),

- on 22 September 2022, it submitted to the National Assembly and the Government its Assessment of the compliance of the revised budget of the Republic of Slovenia for 2022 and of the proposed Ordinance amending the Ordinance on the framework for the preparation of the general government budgets for 2022–2024 with the fiscal rules (as laid down in point 2 of paragraph two of Article 7 of the FRA);

- on 26 September 2022, it submitted to the National Assembly and the Government its Assessment of the fulfilment of the conditions for the existence of exceptional circumstances in 2023 (as laid down in point 2 of Article 12 of the FRA);

- on 17 October 2022, it submitted to the National Assembly and the Government its Assessment of budget documents for 2023 and 2024 (as laid down in point 2 of Article 12 and points 1 and 2 of Article 7 of the FRA).

[10] Annex 2 contains a summary of the assessments of the Fiscal Council from 2022.

In addition to the assessments required under the FRA, in 2022 the Fiscal Council prepared the following assessments and opinions:

- on 9 February 2022, it published its regular publication Fiscal and Macroeconomic Trends;

- on 7 March 2022, it published its analysis Financing the climate transition in Slovenia: Current trends and estimated future needs;

- on 6 June 2022, it published its Assessment of the fiscal consequences of the Coalition Agreement entitled "The 15th Government of the Republic of Slovenia: Coalition Work Programme for 2022–2026";

- on 7 July 2022, it published its regular publication Fiscal and Macroeconomic Trends;

- it published eight editions of the publication Monthly Information.

In its assessments of the budget documents in 2022, the Fiscal Council mainly noted that they projected revenue growth that largely stemmed from the relatively favourable macroeconomic environment. The high tax base was thus, in the Fiscal Council's view, a result of the increased economic activity, due considerably to the expansionary fiscal policy, and of the contribution of the higher inflation also related to excess demand. It also noted that the government's fiscal position was largely influenced by the adopted discretionary structural measures which during the period of the application of exceptional circumstances were not directly related to limiting the impact of the epidemic. The adoption of these measures significantly limited the room for manoeuvre for fiscal policy and reinforced expectations about its future actions. In the assessment of the Fiscal Council, additional fiscal policy incentives were not necessary, given the fiscal situation and the current assessment of the cyclical position, as well as, despite the uncertainty, the still favourable macroeconomic outlook, as they could have triggered more significant imbalances. Fiscal policy should mainly ensure sustained growth in current spending, while adequately addressing development challenges and strengthening the resilience of the economy through the effective implementation of investments, financed to the greatest extent possible by means of the increased availability of European funds. In this context, the Fiscal Council concluded that additional fiscal incentives, in the proposed budget documents mainly in the form of a further increase in the already high level of investment, were not necessary or appropriate in the given circumstances and expected economic trends. At the same time, the estimates of projections in the submitted budget documents were made more difficult as their basis was unrealistically set in the 2022 revised budget. As a consequence, and due to the high level of the budgetary reserves, the likelihood in 2023 of higher-than-projected growth rates of government expenditure in particular has increased.

In accordance with the legislation, the government responded to the Fiscal Council's assessments for 2022 with publicly available written explanations.[11] In particular, the Government stressed the uncertainty about the performance of fiscal policy in times of an epidemic and a high cost of living, the period of exceptional circumstances still in place in 2022, as well as the unreliability of the parameters used for calculating the estimates of compliance with the fiscal rules. Moreover, the government emphasised that due to the uncertain situation, budgetary reserves were being created in budget documents to cope with a possible worsening of the cost-of-living situation. In its responses, the Government also mentioned the development orientation of the budgets, reflected in high investments, also as a consequence of the simultaneous availability of funds from several EU sources, and the possibility of changing project schedules according to the submitted plans. At the same time, the

[11] All government opinions are also published on the Fiscal Council's website at the time of each assessment of the budget documents.

Government opined that it ensured a high level of transparency, as the funds earmarked for measures related to the COVID-19 epidemic are kept under the general budget reserve item and can only be used for measures related to the COVID-19 epidemic. Such monitoring is intended to be considerably more transparent than that provided for in the regulations for the implementation of the integral part of the budget.

3. The Fiscal Council and the National Assembly

The Fiscal Council's cooperation with the legislative branch of government is extremely important. As an independent institution providing impartial analyses of economic and fiscal trends, the Fiscal Council provides direct support to deputies' decisions on budget guidelines and public finance topics. In accordance with the received mandate, the Fiscal Council in its work relies consciously on a positive analysis and does not provide regulatory opinions on specific fiscal measures and legislation. This orientation allows the Fiscal Council to maintain its status of impartiality while at the same time ensures the apolitical nature of its operation.

In 2022, the Fiscal Council's representatives attended six meetings of the Committee on Finance, one meeting of the National Assembly's Commission for Public Finance Control and one meeting of the National Council's Commission for the Economy, Trade, Tourism and Finance.

The Fiscal Council also submits its assessments of budget documents and fiscal trends to the Government for response and to the National Assembly for consideration or for assistance in the adoption of budget documents. Accordingly, the Fiscal Council also takes part in the meetings held by the Committee on Finance, where it presents and explains its opinions and weighs them against the Government's opinions. If opinions on budget documents are provided, the Government must respond to them by explaining how such opinions will be taken into account or why they will not be taken into account (the "comply-or-explain" rule).

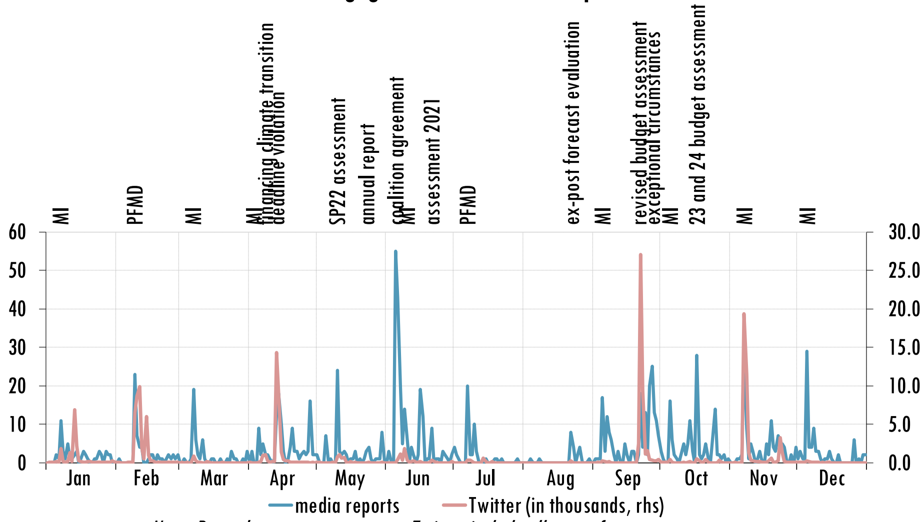
In 2022, the legislation concerning the Fiscal Council's operation remained unchanged.

4. The Fiscal Council's contact with the media

Communicating with the media and informing the general public of its findings is one of the key tasks of independent fiscal institutions. Since the Fiscal Council merely provides opinions on budget documents that the Government is not obliged to take into account (only the “comply-or-explain” principle applies), it can only have an indirect impact on fiscal policy. Therefore, its task is primarily to raise the awareness of the general public, public opinion makers and other stakeholders of the importance of ensuring a sustainable fiscal policy in the long term. The establishment of credibility, i.e. public confidence in the Fiscal Council's analyses and opinions, is a prerequisite for its views to be taken into account in public debate.

In 2022, the Fiscal Council continued to inform the public of its work by publishing recommendations, opinions and interviews. The President of the Fiscal Council held seven interviews with various media, covering a wide range of macroeconomic and fiscal topics. Media coverage of the Fiscal Council's publications was similar to that in the previous year. Media focused on the spring and autumn assessments of the budget documents, the assessment of the coalition agreement, as well as the regular publication Monthly Information.

Figure 4.1: Number of daily media reports about the Fiscal Council and engagements with Twitter posts in 2022

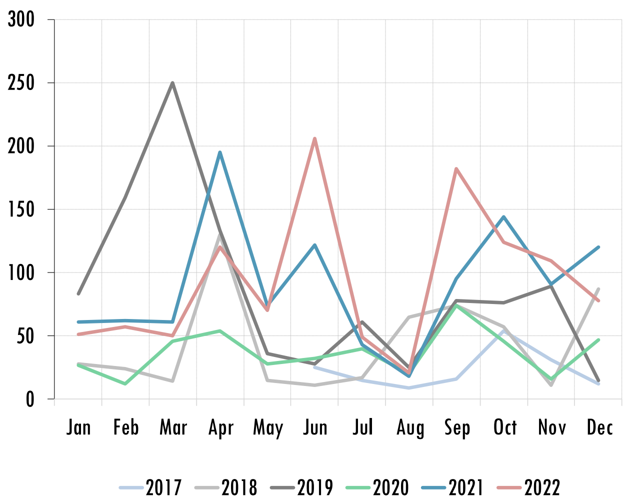


Note: Data about engagements on Twitter include all uses of posts on @FiskalnisvetRS.

Source: Press Clipping d.o.o., Twitter Analytics, Fiscal Council calculations.

As soon as it began to operate in 2017, the Fiscal Council set up its own website with a view to increasing the transparency and impartiality of its operation.[12] Through its website, the Fiscal Council provides access to the current published assessments, opinions, views and recommendations to the wider interested public. Legislation relating to the work of the Fiscal Council, cooperation agreements with other institutions, events in which the Fiscal Council participates and interviews with its members are also available on the website. In the course of the 2019 upgrade of the website, a set of frequently asked questions with answers relating to the Fiscal Council's area of work was added to the website. In this way, the Fiscal Council aims to familiarise the public in a simple way with the basic concepts it uses in its work and communications. In 2020, a special section was added to the website to monitor the fiscal effects of measures designed to limit the impact of the epidemic, where in 2022 the Fiscal Council continued to regularly publish updated data collected with the help of several

Figure 4.2: Number of monthly media reports about the Fiscal Council by year



Source: Press Clipping d.o.o., Fiscal Council calculations.

[12] https://www.fs-rs.si/news/

institutions. The majority of publications, including other basic information on the Fiscal Council's operation, are also available on the English website.

In order to keep the wider public informed, the Fiscal Council launched a Twitter account at the beginning of 2021. On this social network, the Fiscal Council mostly posts messages when publishing its assessments, views and analyses, but also short alerts on publications by other institutions, in particular the EU IFIs, other independent fiscal institutions, Eurostat and the European Commission. The Fiscal Council's messages on this online platform received more than 180,000 views in 2022. Again, the most viewed posts were those from the spring and autumn assessments of the budget documents and those on the findings of the publication Monthly Information.

5. International cooperation of the Fiscal Council

Shortly after it began operating, the Fiscal Council joined international networks of similar institutions and participated in discussions with international institutions that analyse economic and fiscal developments in Slovenia. The purpose of joining international networks of independent fiscal institutions is to keep up with the current trends in budgetary control, to exchange information and to transfer good practices of similar institutions. In addition to other institutions that formulate and implement economic policy in Slovenia, the Fiscal Council is also a counterpart to international institutions. In such contacts, it presents and explains its view on macroeconomic and fiscal developments in Slovenia.

5.1 The Fiscal Council and networks of EU independent fiscal institutions

The Fiscal Council is included in the EU IFI and EUNIFI networks. The EU IFI[13] (EU Independent Fiscal Institutions) is a voluntary and informal network of independent fiscal institutions, which provides a platform for exchanging views and information among its members, but without the participation of EU institutions. In 2022, Fiscal Council representatives attended two EUNIFI meetings and five EU IFI regular meetings and two EU IFI seminars. The EUNIFI (EU Network of Independent Fiscal Institutions) is a formal network of EU independent fiscal institutions whose work is organised by the European Commission (hereinafter: the EC) and whose purpose is to link institutions predominantly in terms of public finance management and compliance with the fiscal rules laid down by EU law. Fiscal Council representatives also attended one OECD PBO meeting in 2022.

In 2022, the Fiscal Council prepared two contributions for an online presentation of fiscal developments in Slovenia within the EU IFI framework. The EU IFI regularly publishes brief information on economic and fiscal developments in the Member States in the publication European Fiscal Monitor.[14] Given the type of tasks, the IMAD[15] usually presents macroeconomic forecasts in this context, while the Fiscal Council presents its view on short-term and long-term fiscal developments and the related challenges and risks. In 2022, the Fiscal Council additionally prepared estimates of the fiscal effects of measures to limit the impact of the epidemic and high cost of living. The main topics of this publication, which was produced twice in 2022, were the fiscal responses of individual countries to the epidemic and the cost-of-living crisis, and the impact of inflation on public finances.

[13] http://www.euifis.eu/

[14] https://www.euifis.eu/publicationsfilter/efm

[15] Due to its independent drawing-up of macroeconomic forecasts, which constitute the basis for the preparation of budget documents, the IMAD is recognised as an independent fiscal institution and participates in the EU IFI and the EUNIFI.

5.2 Cooperation with international institutions

The Fiscal Council cooperates with the EC within the framework of the European Semester. Representatives of the EC met virtually with the Fiscal Council's Analysis Service on three occasions in 2022, in March, September and December. Cooperation took place at a technical level and was intended to exchange views on current and future budgetary developments, in particular in terms of the fiscal effects of measures to limit the impact of the epidemic and cost-of-living crisis, and the assessments of budget documents prepared by the Fiscal Council.

The President of the Fiscal Council met the Head of the European Commission Representation in Slovenia in October.

The Fiscal Council started a project in 2022 to receive technical assistance offered by the European Commission (DG REFORM) under the TSI (Technical Support Instrument).[16] The provider of support, the Danish DREAM Institute (https://dreamgroup.dk/), will develop a long-term fiscal model for the Fiscal Council. The model will be focused on social protection systems and, upon the completion of the project, presumably after 16 months, the model simulations will enable the Fiscal Council to prepare independent, impartial and transparent opinions on long-term trends and adopted measures and the related assessment of long-term risks and the sustainability of social protection systems and public finance in general.

The Fiscal Council also cooperates with the Organisation for Economic Co-operation and Development (OECD). Within the OECD, the PBO network of independent fiscal institutions[17] serves as a platform for the exchange of information and good practices. On the basis of multi-annual cooperation and monitoring, the OECD has drawn up good practice guidelines for the effective operation of fiscal councils. Representatives of the Fiscal Council attended the regular annual meeting of the network in 2022. Within the network of independent institutions, the OECD also keeps a database,[18] which includes Slovenia, the purpose of which is to provide an overview of the key features of independent fiscal institutions.[19]

In 2022, the Fiscal Council met once with representatives of the International Monetary Fund mission to Slovenia. The Fiscal Council also met with representatives of credit rating agencies in 2022. In November, it met with representatives of S&P Global. At the meetings, the Fiscal Council provided its opinion on the economic and fiscal situation in Slovenia, especially in terms of the fiscal impact of the measures to limit the epidemic and the cost-of-living crisis. The discussions also focused on long-term challenges to public finances.

As part of international cooperation and in addition to the above-mentioned events, Fiscal Council representatives also took part in the following events:

- SUERF consultations on public debt restructuring (February, virtually);
- an EFB conference on public finance and climate change (February, virtually);
- a joint meeting of the EU IFI Network and EFC Alternates (March, virtually);

[16] https://ec.europa.eu/info/overview-funding-programmes/technical-support-instrument-tsi_en

[17] http://www.oecd.org/gov/budgeting/oecdnetworkofparliamentarybudgetofficialspbo.htm

[18] http://www.oecd.org/gov/budgeting/OECD-Independent-Fiscal-Institutions-Database.xlsx

[19] The overview of key features covers a range of areas, including the legal basis, institutional form, leadership, the relationship with the legislative branch of government, the term of office and tasks, financial resources and the number of staff, independence, publications, access to information, transparency and an external evaluation of the work of independent fiscal institutions.

- a conference organised by the French Fiscal Council and the EU IFI Network on the role of Fiscal Councils in a renewed system of economic governance (May, virtually);
- an EU IFI Network seminar on the TSI instrument (May, virtually);
- an EUNIFI seminar on one-off measures (June, virtually);
- a conference organised by DG ECFIN on the topic of assessing the relations between budgets and the green transition (June, virtually);
- active participation in a Bruegel seminar on the topic of the revised economic governance framework and fiscal rules – Fiscal Council member Alenka Jerkič participated as an invited participant (October); and
- a conference organised by DG ECFIN on the topic of the revised economic governance framework (December).

Annex 1: The Fiscal Council's operations in 2022

Summary of the document "Obrazložitve zaključnega računa proračuna za leto 2022" (Notes on the Annual Financial Statement of the Budget of the Republic of Slovenia for 2022)

In accordance with the provisions of Article 12 of the Rules on the common bases for the work procedures of financial services of direct spending units of the budget of the Republic of Slovenia, in April 2017 the President of the Fiscal Council issued Financial Management Instruction No. 00-1/2017/3, which regulates the organisation and conduct of financial management, responsible persons and signatories, the preparation of the financial plan, the execution of the financial plan, reporting on the use of budgetary resources, and internal control. Financial management is conducted by the Court of Audit's Financial Accounting Service. Financial management is conducted in a uniform computerised accounting programme, MFERAC. The accounting is managed by the Directorate for Public Accounting of the Ministry of Finance. The organisation and management of accounting at the Ministry of Finance is governed by Accounting Rules No. 450-221/2017/1.

Funds in the amount of EUR 710,215.00 were planned for the implementation of the tasks of the Fiscal Council for 2022 (Official Gazette of the Republic of Slovenia [*Uradni list RS*], Nos 174/20 and 129/22), while the financial plan in force amounted to EUR 709,675.00. In 2022, EUR 35,653.63 more than in 2021 was spent, i.e. EUR 540,241.97 in total, which represents 76.07% of the adopted budget and 76.13% of the funds in the financial plan in force.

Notes on some major expenditure items of the Fiscal Council for 2022:

1) Salaries were calculated and paid in accordance with the provisions of the Public Sector Salary System Act (ZSPJS), the Fiscal Balance Act (ZUJF), the Public Employees Act and the Act Regulating the Implementation of the Budget of the Republic of Slovenia for 2022 and 2023 (ZIPRS2223), the provisions of the Collective Agreement for the Public Sector, the Collective Agreement for Non-Commercial Activities in the Republic of Slovenia, Annexes to the Collective Agreement for Non-Commercial Activities in the Republic of Slovenia, the Agreement on Measures Relating to Salaries and Other Labour Costs in the Public Sector for 2022 and 2023 (hereinafter: the Agreement), and other regulations and internal acts of the Fiscal Council. In accordance with the Agreement, the pay scale was harmonised and applied starting with the salary for October 2022 and ending on 31 March 2023. Reimbursement for meals during work and the scientific title allowance were also harmonised under the Agreement. On the basis of the agreement, the Act Amending the ZSPJS was adopted, which also harmonised the reimbursement for meals during work for public office holders at EUR 6.15 as of September 2022, while their commuting allowance was aligned with the allowance for public employees as of December 2022 (a mileage reimbursement equal to 10% of the monthly highest reported retail price of 95 octane unleaded petrol).

The holiday allowance for 2022 for public office holders and public employees in pay band 51 and above amounted to EUR 1,074.43 pursuant to the provisions of the Employment Relationships Act, the minimum pay for 2022 published in the Official Gazette of the Republic of Slovenia [*Uradni list RS*] No. 5/22, and the Agreement on Measures Relating to Salaries and Other Labour Costs in the Public Sector for 2022 and 2023 (Official Gazette of the Republic of Slovenia [*Uradni list RS*] No. 136/22). The holiday allowance was paid in the May 2022 salary. Public employees in pay bands 41–50 were paid a balancing allowance of EUR 100 net in November.

Labour costs were higher in 2022 compared to 2021 due to the transfer of a public employee, the harmonisation of pay bands to a level 4.5% higher with effect from 1 October 2022 and higher performance-related bonuses for regular work. However, the payment of the commuting allowance was lower compared to 2021 due to work from home.

2) Pursuant to Article 10 of the Fiscal Rule Act (Official Gazette of the Republic of Slovenia [*Uradni list RS*], Nos 55/15, 129/22), on 27 March 2017 the Fiscal Council and the Court of Audit entered into the Agreement on providing administrative and technical support and premises for the needs of the Fiscal Council No. 014-1/2017/1 as amended (hereinafter: the Agreement). In order to share a meeting room, on 8 July 2020 the Court of Audit and the Fiscal Council concluded a new Agreement on providing administrative and technical support and the sharing of premises and equipment, No. 014-2/2020/1, as amended (hereinafter: the Agreement). In October 2022, a new Agreement was concluded, No. 014-2/2022/1, redefining the tasks to be performed by the Court of Audit's staff for the Fiscal Council.

In accordance with the Agreement, tasks relating to information technology, the main office, human resources and general affairs, finance, legal affairs and other tasks for the Fiscal Council are

Table 1: Fiscal Council expenditure

	2021 EUR	2022 EUR	% share in total expenditure 2022
Expenditure on salaries and duties			
Salaries, supplements and other	296,040	311,886	57.7
Annual allowance	6,248	6,613	1.2
Restitutions, work-related bonuses	18,160	20,146	3.7
Social security contributions	46,785	49,306	9.1
Collective supplementary pension insurance according to ZKDPZJU	2,636	2,793	0.5
Total	369,869	390,743	72.3
Material expenditure			
Stationery and general goods and services	12,936	18,471	3.4
Special goods and services	355	49	0.0
Energy, water, communal services and communications	8,041	13,339	2.5
Transport costs and services	0	90	0.0
Expenses on business travel	0	6,986	1.3
Regular maintenance	2,987	2,509	0.5
Business rents	54,280	48,986	9.1
Other operative expenditure	55,380	41,703	7.7
Total	133,979	132,133	24.5
Expenditure on investment and investment maintainance			
Other means of transport	0	0	0.0
Hardware computer equipment	49	15,748	2.9
Telecommunication equipment	203	60	0.0
Audio-visual equipment	30	357	0.1
Intangibles (computer software)	457	1,200	0.2
Other equipment	0	0	0.0
Total	739	17,365	3.2
Total expenditure	**504,588**	**540,242**	**100.0**

Source: Notes on the Annual Financial Statement of the Budget of the Republic of Slovenia for 2021 and 2022.

performed by the services of the Court of Audit. In 2022, EUR 41,149.91 was spent on administrative and technical assistance. The costs of administrative and technical assistance are recorded as "other operating expenditure".

In accordance with the Agreement, the Court of Audit may use the meeting room on the business premises of the Fiscal Council, for which it pays the corresponding average daily usage fee, which amounts to a share of 11.09% per month of use. The reimbursement for the use of the business premises in 2022 was EUR 245.86.

Under the "commercial rents and leases" account, the highest cost is the rent for the business premises at Likozarjeva ulica 3 in Ljubljana (EUR 41,568.83). The monthly rent for the premises was reduced from EUR 4,266.50 to EUR 3,524.50. The Fiscal Council also covers the general costs of building management and common areas, which are determined by a special contract.

The Fiscal Council is also part of the EU IFIs network, which is linked to the CEPS (Centre for European Policy Studies), and performs the tasks of the EU IFI Secretariat. The membership fee for 2022 was EUR 500.

3) For investments and major maintenance, EUR 37,000 in budget funds was allocated in the existing financial plan (under budget item 160003 – Investments and major maintenance) which represented 5.21% of the total funds under the 2022 financial plan in force.

A total of EUR 17,365.31 was spent, which represented 46.93% realisation of the total funds for investment under the financial plan in force or 3.21% of the total expenditure in 2022. Investment expenditure was financed from budget funds.

Investments in 2022 included:

- two instalments of Microsoft licensed software (EUR 742.94),

- seven laptops with docking stations (EUR 10,570.00),

Table 2: Value of tanglible and intangible fixed assets in 2022

	Intangible assets	Immovable assets	Equipment and other tangible assets	Total
PURCHASE VALUE				
As at 1 January 2022	17,736	0	35,789	53,525
Direct acquisition	457	0	16,175	16,632
Removal – transfer	0	0	-58	-58
As at 31 December 2022	18,193	0	51,907	70,100
VALUE ADJUSTMENT				
As at 1 January 2022	11,873	0	30,924	42,796
Reduction of value due to exclusions or transfers			-58	-58
Value adjustment	3,197	0	7,114	10,310
As at 31 December 2022	15,069	0	37,979	53,049
RESIDUAL VALUE				
As at 31 December 2022	**3,123**	**0**	**13,927**	**17,051**

Source: Notes on the Annual Financial Statement of the Budget of the Republic of Slovenia for 2022.

- two mobile phones (EUR 60.00),

- one Logitech camera (EUR 356.90)

- a Matlab software update (EUR 457.20),

- three 2-in-1 hybrid laptops with docking stations (EUR 5,175.00) and

- four modems (EUR 3.27).

Notes on some balance sheet items for 2022

As at 1 January 2022, the Fiscal Council's outstanding expenditure shown on the balance sheet amounted to EUR 47,918.58, which was settled at the beginning of 2022. The payables relate to documents received in December 2021 and January 2022 for liabilities incurred in 2021, namely:

– the payment of salaries, benefits and reimbursements of costs, and collective supplementary insurance premiums for December 2021 in the amount of EUR 31,314.25;

– payments to suppliers for services rendered and materials supplied in the amount of EUR 11,351.63;

– provided services and charges of budget users in the amount of EUR 5,252.70.

As at 31 December 2022, the Fiscal Council did not have any funds recorded in the account of the Ljubljana Office of the Public Payments Administration of the Republic of Slovenia. The Fiscal Council operates through the budget account of the Republic of Slovenia.

As at 31 December 2022, the Fiscal Council's outstanding expenditure shown on the balance sheet amounted to EUR 47,682.97, which it carried forward to 2023. These debts relate to outstanding current expenditure amounting to EUR 47,682.97 (which includes already calculated but unpaid salaries, benefits, premiums for collective supplementary insurance for public employees and reimbursements of expenses for December 2022 amounting to EUR 33,071.35, services received and materials and equipment supplied, amounting to EUR 11,730.62, and services rendered to direct budget users amounting to EUR 2,881.00).

As at 31 December 2022, a general restricted tangible and intangible fixed assets fund totalling EUR 17,050.63 was recorded in the Fiscal Council's books under own resources and long-term liabilities. The gross balance sheet also shows long-term payables for the purchase of Microsoft software for the period 2021–2023 totalling EUR 371.47 for the payment of the third instalment due in 2023.

As at 31 December 2022, the Fiscal Council also had off-balance-sheet equipment on its books, which is not owned by the Fiscal Council and which has been received for temporary use, in a total amount of EUR 1,961.55. This equipment includes communication technology equipment (owned by T-2 d.o.o.) in the amount of EUR 454.85 and a Canon multifunctional device in the amount of EUR 1,506.70.

The Fiscal Council did not conduct an internal audit of its operations for 2022. The Fiscal Council's annual budget is less than EUR 2,086,000 and it is therefore obliged to provide an internal audit of its operations at least once every three years. An audit was carried out for the years 2020 and 2021.

Annex 2: Summaries of Fiscal Council's assessments in 2022

5/10/2022
Assessment by the Fiscal Council: Assessment of the 2022 Stability Programme

The no-policy-change scenario of the 2022 Stability Programme foresees a gradual improvement in the fiscal situation. However, this improvement will be somewhat limited by the discretionary measures already adopted, and the planned 2025 deficit is set to be higher than last year, without taking into account the COVID-related measures. Revenue growth is expected to continue, largely based on the prediction that relatively favourable macroeconomic conditions will continue despite a number of negative risks. The high tax bases are a result of the increased level of economic activity, due considerably to the expansionary fiscal policy, and the contribution of the higher inflation, which is also related to excess demand. In the medium term, the relatively favourable fiscal balance achieved before the epidemic will not be fully restored, mainly due to the adopted discretionary structural measures which, since the invocation of exceptional circumstances, have not been directly linked to mitigating the consequences of the epidemic. The adoption of these measures significantly limits the room to manoeuvre for the future conduct of fiscal policy. Given the fiscal situation and the current estimates of the cyclical position and despite the uncertainties continued favourable macroeconomic projection, additional fiscal policy incentives are not necessary, as they could trigger more serious imbalances. Alternative estimates of levels and growth of expenditure show that, even under the no-policy change policy scenario, these are mainly above the thresholds ensuring medium-term fiscal policy sustainability. The fiscal policy's main aims should be to ensure sustainable growth of current expenditure, to respond in an appropriate manner to development challenges and to strengthen the economy's resilience with efficient investments financed, to the greatest possible extent, with a higher amount of available European funding.

* * *

Despite the high level of expenditure, the nominal deficit is set to decrease to the permitted threshold of -3% of GDP next year. Throughout the projection period, its decrease should be largely due to the currently expected relatively high and cyclical growth in revenue. Despite its assumingly appropriate decrease, the general government debt should exceed the Maastricht criteria at the end of the period covered by the 2022 Stability Programme, amounting to 68.0% of GDP in 2025.

The high structural deficit is, among other things, the result of a series of measures taken during the epidemic that have brought about a permanent deterioration in the fiscal situation. The total impact of measures not directly related to the epidemic on the general government balance in 2022 is estimated at approximately 2.3% of GDP and is expected to increase to approximately 3.2% of GDP by 2025. The adoption of such measures has intensified further since the adoption of the budget documents in autumn of last year, which is reflected in the strengthened pro-cyclical expansionary fiscal stance in 2022. To a significant extent, this represents the materialisation of risks that the Fiscal Council has recently been calling attention to on a regular basis. The temporary deterioration in the fiscal situation enabled by the epidemic will thus become structural. This type of policy limits the room to manoeuvre that would allow extensive fiscal policy action to be taken in case of future shocks. This room would be even smaller if the many currently detected negative risks and the consequently slower economic growth were to be materialised, taking into consideration also the expected tightening of the monetary policy.

Based on the current forecasts, the economy is expected to operate under favourable cyclical conditions with signs of exceeding the supply potential in the coming years, despite increased uncertainties. Under such conditions, it is essential to create ample room to manoeuvre for public finance. Additional fiscal incentives that would lead to increased demand could cause macroeconomic imbalances. The latter are already starting to show in the form of increased limitations in ensuring the appropriate workforce, inflationary pressures, which do not originate only in the international environment, and the rapid shrinking of the surplus in foreign trade. The deterioration in the structural fiscal policy position is less noticeable due to the rapid recovery of economic growth, partly enabled, after the drop in GDP in 2020, by the stimulative fiscal policy as well as the extremely accommodative monetary policy, which has thus far ensured favourable financing conditions and deterred the responses of the financial markets to the deteriorated fiscal situation.

In the given situation, the fiscal policy should restrain the planned growth in current spending, excluding expenditure for interest, investments and one-time expenditure and spending associated with the COVID-related measures, which was set too high. It's 2021 growth was the highest after 2008 and is set to increase further this year. Growth in current public spending should remain within the limits permitted by long-term growth in revenue. It is important to ensure that room for future priorities is created by increasing the efficiency of government expenditure and strengthening bases on the revenue side. The public investments envisaged in budget documents should appropriately address the development challenges and strengthen the economy's resilience. It is necessary that their implementation takes into consideration the limitations of the absorption capacities of the administration and the economy, which, among other things, can lessen investment efficiency or further increase inflationary pressures.

In the current uncertain situation, the Fiscal Council does not state its opinion on extending the period of exceptional circumstances into 2023. In accordance with the law, it expects to receive a request to prepare such an assessment from the Government and present it before the preparation of the autumn budget documents. The Fiscal Council once again calls attention to the fact that, after the conclusion of the period of exceptional circumstances, the Fiscal Rule Act provides for the institution of a correction mechanism. At the same time, it expects the Government to respond to the challenges of ensuring the long-term sustainability of public finance in a timely manner, the latter having deteriorated again in recent years according to certain indicators.

On several occasions in the current procedure of submitting the documents required by law, the Government acted in contravention of the established norms or relevant legislation. It delayed taking note of the macroeconomic forecasts of the Institute of Macroeconomic Analysis and Development (IMAD), which proved to be consistent with the principles of accuracy and unbiasedness over the long term. Among other things, it made it more difficult for the Fiscal Council to conduct a comprehensive analysis of budgetary projections within the short statutory time limits. The Government provided the Fiscal Council with the draft Stability Programme with an 18-day delay relative to the legislation in force and failed to submit for assessment the framework for the preparation of the general government budget, the central medium-term budget planning document. The legislation in force does not contain any provisions releasing the Government from this obligation. Moreover, after the publication of favourable national accounts data for 2021 at the end of February and in light of the improved epidemiological situation, the Government once again failed to ask the Fiscal Council for its assessment as to whether the reasons for the invocation of exceptional circumstances have ceased or continue to exist.

5/24/2023
Report on the Fiscal Council's operations in 2021

In line with the persistence of pandemic, the exceptional circumstances identified in March 2020 have remained in place throughout 2021. Until they are lifted, they allow for a temporary deviation from the medium-term fiscal objectives provided that medium-term fiscal sustainability is not jeopardised. At the same time, a strong economic rebound was also visible in 2021, and especially at its end. The high annual GDP growth in 2021 was thus the result of both the low base of the previous year and the recovery of economic potential, with the relaxation of epidemiological constraints and the consequent removal of barriers to economic life.

One of the two criteria for exceptional circumstances, as defined in Article 12 of the Fiscal Rule Act, has was not valid at the end of 2021. Not only is there no serious economic downturn, but the rebound has been increasingly accompanied by clear signs of economic overheating, which have persisted well into 2022. However, there remains an uncertainty about the second criterion, an unusual event outside the control, which has a major impact on the financial situation of the general government sector. The epidemiological risk, which seems to be evolving towards seasonal cycles, has been compounded by the geopolitical risk in 2022. That is why the timeline for lifting the exceptional circumstances by activating the correction mechanism has still not been finalised. However, public debt is rising with high fiscal deficits, and financing conditions will tighten as monetary policy begins to normalise.

Fiscal policy has responded to the changing epidemiological situation both by taking a number of temporary measures that were directly linked to the epidemic and by introducing measures that will change public finances in a more permanent way. As the measures have an impact on the state of public finances, the Fiscal Council has monitored and analysed them in its – including new – regular publications and expressed its views on them when assessing the budget documents submitted. In doing so, it pointed, *inter alia*, to the lack of transparency in assessing their impact and tried to compensate for such shortcomings with its own assessments. The Fiscal Council aims to raise awareness among economic policy makers, and especially the general public, of the risks to fiscal sustainability in the medium and long term.

In such a situation, the expected, but at the moment still not timetabled, deactivation of the escape clause at the European level also raises a debate on possible fiscal rule adjustments. Of course, with the strong tendency to allow greater flexibility to facilitate economic development, we quickly encounter constraints imposed by the financial markets given their perception of the sustainability of government financing. Relaxations of rules and the associated borrowing increase risks for investors, and the real question is how much risk financial markets are willing to take when deciding on the financing of governments. As the experience of the debt crisis less than a decade ago showed, smaller countries with weak fiscal governance can quickly approach this limit.

As a small, medium-developed and below-average indebted country in the EU, Slovenia needs fiscal rules, strictly dedicated to ensuring medium term public finance sustainability in order to prevent consequences of stronger and more indebted members increasing uncertainty and thereby crowding out other member states from financial markets.

6/21/2022
Assessment by the Fiscal Council: Assessment of compliance of the general government budgets with the fiscal rules in 2021

Last year, fiscal trends were again seriously affected by the epidemic. The scope of measures taken to mitigate its impact was again substantial, however, the general government deficit decreased, mainly due to a marked rebound in economic activity and the resulting cyclically driven high revenue growth. Nevertheless, fiscal policy was pro-cyclically expansionary according to the latest available assessments of the cyclical position of the economy, which are in the current situation more uncertain than usual. The procyclicality was partly due to an increased investment activity and partly to a rise in public spending not related to the epidemic. While the growth in investment activity was as expected lower than budgeted, its increase was financed equally by European and domestic funds. The remaining part of public expenditures, which, in addition to investment, excludes interest expenditure and one-off expenditure, together with expenditure on COVID measures, increased last year by the most since 2008 and significantly exceeded estimates of potential economic growth. Despite the deficit reduction, a significant part of the unexpectedly high revenue growth thus also translated into higher current spending, which was in many respects of a structural or permanent character. Furthermore, a number of new discretionary measures were adopted at the end of last year, further constraining manoeuvring room for future fiscal policy.

Economic activity picked up significantly last year after a contraction in 2020, surpassing the pre-crisis level and growing at the highest rates in the EU. The high growth was mainly driven by the adaptation of business entities and households to the epidemic situation. The economic recovery also benefited from government measures, both directly through the strengthening of investment activity and indirectly through measures that contributed to an increase in disposable income and thus to private consumption growth. Economic growth exceeded all the available forecasts owing to, primarily, favourable trends at the end of the year when, contrary to assumptions and despite the worsening of the epidemiological situation, restrictive measures were milder than in the preceding outbreaks.

The general government deficit decreased to -5.2% of GDP last year and, while excluding the impact of expenditure on COVID measures, it amounted to -0.7% of GDP. The decrease was mainly due to strong revenue growth, notably from tax and social contributions, combined with growth in domestic consumption and improvements in the labour market. On the other hand, non-epidemic expenditure growth picked up further last year. This was only partly related to higher government investment activity, and partly stemmed from a strong pick-up in growth of other public spending. The deterioration of the public finance balance during the epidemic was among the largest in the EU Member States, both overall and when the impact of expenditure on COVID measures is excluded.

Last year, general government gross debt decreased to 74.4% of GDP, thus exceeding the pre-crisis level by around 10 pps of GDP. The decline in the share was largely driven by economic growth, which more than offset the further deterioration in the primary balance. Last year, borrowing continued in a favourable financial market environment, mainly as a result of the ECB's accommodative policy. The central bank's share of government debt securities owners further increased to almost 40% last year due to the government bond-buying programme introduced in the epidemic.

The epidemic also led to the application of exceptional circumstances last year in accordance with the legislation. This means that, in particular, due to the growing uncertainty in the calculation of key input variables, the Fiscal Council's ex-ante and ex-post quantitative assessments of compliance with the fiscal rules are only indicative and, similar to the European Commission, place more emphasis on qualitative assessments. Despite the application of exceptional circumstances, the Fiscal Council must determine, based on national legislation, whether the actual volume of general government expenditures was in line with the last applicable maximum set by the amendment of the Framework under Article 13 of the Fiscal Rule Act. The threshold of the Framework for the maximum permitted level of general government expenditures was increased three times between November 2020 and September 2021, i.e. by EUR 900 million. The level of expenditure outturn was lower than the last maximum defined by the ordinance, but the ex-post assessment based on the latest known estimates of the output gap shows that the realisation was slightly higher than the current estimates of the maximum permitted level of expenditure.

09/22/2022

Assessment by the Fiscal Council: Assessment of compliance of the Draft Revised Budget of the Republic of Slovenia for 2022 and of the Proposal for the Ordinance amending the Ordinance on the framework for preparing the general government budgets for the 2022– 2024 period with the fiscal rules

The draft revised budget foresees a reduction in the overall state budget deficit from EUR 3.1 billion in 2021 to EUR 2.0 billion in 2022. The decrease compared to last year is due to high nominal GDP growth and consequently higher revenues, and a much less negative impact of one-off factors on the balance than last year, despite the adoption of inflation-mitigation measures. The Draft Revised Budget shows that the expected deficit in the last four months will be as high as EUR 1.7 billion, only partly as a result of measures to mitigate the effects of the epidemic and inflation. The draft revised budget implicitly foresees a considerable increase in spending at the end of the year, including spending unrelated to investment plans, which has no basis in the measures currently in force. Spending volumes, which exclude the impact of investment as well as one-off factors, are expected to increase by EUR 1.2 billion or 11.4% this year, which would be a record high. Such growth would be well above the medium-term sustainable growth path as defined by the currently estimated long-term potential output growth of around 4.5%.

We consider the draft revised budget to be unrealistic, as the deficit is likely to be smaller than projected, but this will set the basis for the autumn budget documents for 2023 and 2024 too high. Should the projections presented actually materialise, we consider the Draft Revised Budget to be risky from the point of view of spending rationality and, due to its expansionary trend, inappropriate in view of the current macroeconomic situation, which, according to the currently available data, remains favourable despite the uncertainties. At the same time, the implementation of the fiscal policy outlined in the Draft Revised Budget would also increase the risks of a prolonged persistence of high inflation and of a move away from the medium-term sustainability of public finances. These risks are exacerbated by the above-mentioned exceedance of spending growth in successive years, and point to structural pressures on public finances. The decision to prepare the revised budget separately from the revision of the budget documents for the coming two years also represents another departure from medium-term budgetary planning, which is the basis for the creation of a comprehensive and coherent fiscal policy. At the same time, the revised budget also does not fully take into account the updated macroeconomic forecasts, which, in a highly uncertain environment, further contributes to the unreliability of the presented fiscal plans.

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On aggregate, trends of public finance aggregates show an improvement on last year's unfavourable situation. The general government deficit, as shown in the proposed revised budget, is projected to reach -3.8% of GDP in 2022, which is 1.4 percentage points of GDP less than last year. In our estimate, the general government debt is projected to fall below 70% of GDP in 2022, especially due to the high nominal economic activity. However, such developments mask the actual deterioration in public finances, as fiscal aggregates are largely determined by changes in the volume of one-off factors. These are indeed expected to halve compared to last year, when they amounted to 4.5% of GDP at the general government level, despite the continuation of measures to mitigate the effects of the epidemic and inflation. In view of the accelerated adoption of inflation-mitigation measures, the Fiscal Council reiterates the importance of targeted and temporary action, which is implied by the adoption of the vulnerable group allowance, while the predominant financial impact, however, originates from general measures that limit price signals and may, inter alia, lead to an irrational response by consumers.

State budget expenditure, excluding one-off factors, is expected to increase significantly this year, which will be only partly a result of the anticipated high investment activity. Although investment projections are less unrealistic than in the existing budget, they still show very high growth, especially in the last months of the year. The reduction in investment plans compared to the current budget is almost entirely due to the expected lower planned volume of investments financed by EU funds. However, according to the Government, the need to use up the remaining cohesion funds from the previous financial perspective is one of the main reasons for the proposed increase in the expenditure ceiling. It would also represent a remarkable acceleration in the final months of the year, given this year's outturn to date. Such a projection only partly reflects measures taken after the entry into force of 2022 budget amendments, which were of a permanent nature and not directly linked to the epidemic, and instead indicates unrealistic planning to a significant extent. Due to the again partial budgetary process, where public finance parameters are changed only a few months before the end of the year for no more than one year at a time, this projection also implies the creation of inadequate baselines for the preparation of the budgets in the following years and thus a risk of further divergence from the medium-term sustainability of public finances.

In the Fiscal Council's opinion, the realisation of the draft revised budget is questionable. We estimate that the actual state budget deficit in 2022 will be lower than the one proposed in the revised budget, based on the outturn in the first eight months of the year. The revenue estimate in the Draft Revised Budget is cautiously projected, which is appropriate given the considerable uncertainty. However, the extremely high state budget expenditure reflects in particular an unrealistically high level of investment, as well as high levels of other expenditure unrelated to the epidemic or inflation, the acceleration of which over the rest of the year is largely inconsistent with the legislation currently in force. If the Draft Revised Budget is actually implemented, this would imply a highly expansionary fiscal policy. Such a position would not be appropriate in the current circumstances, given supply-side constraints and high inflation, and is also ineffective given current economic trends, constraints and risks. The implementation of the Draft Revised Budget could therefore further deepen macroeconomic imbalances and increase the risks of a prolonged persistence of high inflation.

The Draft Revised State Budget and the revised framework for drafting general government budgets also reflect inappropriate budgetary planning. The Fiscal Council has regularly drawn attention to the latter in its assessments of budget documents, especially in the autumn, over the past few years, including in the period before the epidemic crisis. The 2022 Draft Revised Budget is thus prepared separately from the autumn budget documents for 2023 and 2024, which are also covered by the current framework for drafting general government budgets. This is another departure from medium-term budgetary planning, which is the basis for the preparation of a comprehensive and coherent fiscal policy. Adopting the revised budget before the preparation of the updated autumn macroeconomic forecast introduces additional uncertainty into the projections, as the economic environment has changed considerably since the spring forecast, which formed the basis for the current Draft Revised Budget. In addition to higher levels of nominal revenue bases for budgets, risks to economic growth have also increased, which, if realised, could represent a moderation of the current cyclically high and given the available data probably unsustainable level of economic activity, based on the existing labour market constraints.

9/26/2022

Assessment by the Fiscal Council: Fulfilment of conditions for the existence of exceptional circumstances in 2023

The outlook for 2023 is currently characterised by extreme uncertainty, which requires flexible government action, and high risks of a further deterioration in the economic growth outlook, which could have important financial implications for the general government sector's financial position. While taking urgent action to limit the impact of the energy price increases, the Government needs to preserve as much room for manoeuvre as possible for future action, in particular by limiting the growth of current spending. Measures to address the energy crisis must be timely, targeted and temporary and must not worsen the structural position of public finances. In the event of uncertain duration of price shocks, this is particularly true for the adjustment of different categories of public expenditure to the current high level of energy prices.

10/17/2022

Assessment by the Fiscal Council: Assessment of budgetary documents for 2023 and 2024

Under current circumstances, fiscal policy needs to maintain the flexibility to act fast and ensure effective measures to cushion the blow of the cost of living crisis but at the same time avoid creating additional inflationary pressures and putting at risk the sustainability of public debt in the medium term. The draft budgets have taken such orientations into account to some extent, but they come with a number of shortcomings and risks. We assess that the fiscal stimulus envisaged in the proposed budget documents, mainly in the form of a further increase in the already high level of investment, is neither necessary nor appropriate under the given circumstances and in view of expected economic trends. The assessment of projections in the submitted budget documents was made more difficult as their basis was set unrealistically in the 2022 revised budget. This increases the likelihood of higher-than-projected growth rates in 2023, particularly for government expenditure. In addition to the continued acceleration of investments, the rapid growth in expenditure is primarily due to discretionary measures taken after the entry into force of the applicable budget last autumn. These measures, coupled with a deteriorated starting position of public finances in 2022, the envisaged large-scale measures to tackle the cost of living crisis and the cooling of economic activity, contribute to the projected high deficit in 2023.

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According to the proposed budgets, the general government deficit should reach 5.0% of GDP in 2023 and 2.4% of GDP excluding one-off factors. The latter deficit is expected to remain at a similar level in 2024. The general government debt is projected to fall to 70% of GDP by the end of 2024 and thus remain higher than in the pre-pandemic period. The Fiscal Council estimates that such an outturn would imply a relatively neutral fiscal policy stance on average over the next two years, taking into account large one-off factors, overestimated investment and high inflation. If demand were boosted further, fiscal policy would run counter to the ongoing monetary policy efforts to contain the upswing in inflation expectations and also counter to economic policy's own efforts to mitigate the cost of living crisis.

The outlook for 2023 is shrouded in extreme uncertainty and marked by high geopolitical risks of a further deterioration in the economic growth outlook, which calls for flexible action by the Government. This can be described as an unusual event beyond control, which may have significant implications for the financial situation of the general government sector. As a result, exceptional circumstances continue to be invoked in 2023, as also foreseen by the Government in its budget documents. Flexibility in tackling the cost of living crisis in the proposed budget documents entails the creation of a high reserve, which the Fiscal Council considers appropriate, while ensuring its exclusively dedicated and transparently presented spending. Measures to tackle the high cost of living must be effective and must not permanently worsen the public finance position, so it is essential that they are temporary and, as far as possible, targeted at helping the most vulnerable groups of the population and the most exposed sectors of the economy. In introducing them, consideration should also be given to the burden-sharing between the State and the private sector of the energy shock, which is unlikely to be temporary, since, in our assessment, the private sector also has some room for manoeuvre.

Budget developments will be largely driven, in addition to one-off factors, by sizeable discretionary measures taken over the past year and the expected high level of investment. Discretionary measures are expected to worsen the state of public finances by about 2% of GDP per year in the coming years, acting on both the revenue and expenditure sides. The discretionary expenditure measures are strongly predominant due to the proposed adjustments to the tax legislation, which partly neutralise the effect of the original changes. The bulk of them relate to public sector salaries and social benefits, which, in a context of high inflation and on the basis of existing legislation, in addition to measures to address the cost of living crisis, ensures that their real value is preserved. The projected growth in current government expenditure over the next two years is around 6% per year, which is about twice the long-term average. The risks of even higher growth are significant, especially as regards salaries.

In the budget documents, investments are planned at a record high level, though we estimate this will not be realised in full. A focus on investments is reasonable if they address the risks to which the economy will be exposed in the future and may have an impact on growth in economic potential and on the sustainability of public finances. However, their rapid increase is usually marked by inefficiency, which could be particularly pronounced in the face of constraints on the supply side and the absorption capacity of the administration. A relatively high share of the planned investments is expected to be financed with EU funds, which reflects the conclusion of the past and the beginning of the new multi-annual financial framework (hereinafter: MFF), and the RRF funds, where there are already delays in meeting the milestones as a condition for disbursements. However, the projected funding structure also increases the already high level of domestic resources compared to the existing budget documents, which also increases the risks of inefficient project implementation.

In a period of heightened uncertainty, fiscal policy needs to ensure credibility and transparency and preserve the medium-term sustainability of the public debt, as assessed by the Fiscal Council, the European Commission and other international institutions. Realistic planning can largely contribute to the credibility of fiscal policy, where shortcomings have been perceived, in particular in the context of the adopted revised budget for 2022 and in terms of the public investment projections. A heightened uncertainty does not justify the significant deviation in the estimate of budget outturns a few months before the end of the year from the likely developments, as witnessed for the third consecutive year. We assess that this is to some extent a repetition of the abuse of the flexibility allowed by the exceptional circumstances instrument, which introduces unnecessary opacity into the budget planning process and opens up room for inefficient spending of public money. Improving the investment planning system or including more realistic estimates of the investment volumes in budgets could also play an important role in increasing the transparency and reliability of budget plans. The highest level of transparency should also be ensured in the use of funds in order to ease the effects of rising prices, which is envisaged in the accompanying budget legislation.

According to our analysis based on the proposed budget documents, the potential risks of a deterioration in the medium-term sustainability of government debt are relatively limited. The Fiscal Council has assessed that the short-term deterioration of fiscal position, which increases the risk of adverse reactions from financial markets and a rise in the required rate of return on new borrowings, is likely to be smaller than predicted. At the same time, the State has ample liquid assets, which gives it some leeway to neutralise the impact of the deficit on government debt. In the medium term, one of the key economic policy tasks remains the preparation of comprehensive set of measures to limit the impact of long-term risks to which public finances are exposed.

Annex 3: Glossary

Automatic stabilisers:
Automatic stabilisers are features of public finances that react automatically to the economic cycle and thus contribute to the stabilisation of activity in the economy without adopting additional measures. The most typical automatic revenue stabiliser is a progressive tax on the household income; on the expenditure side such a stabiliser includes social transfers, in particular unemployment allowances.

Budget balance:
The balance between total public expenditure and revenue in a specific year. A positive balance indicates a surplus and a negative balance indicates a deficit. The EU uses general government aggregates (according to the ESA2010 methodology) for the monitoring of Member State budgetary positions.

Cyclical component of budget balance:
A part of the change in the budget balance that follows automatically from the cyclical conditions of the economy, due to the reaction of public revenue and expenditure to changes in the output gap.

Discretionary fiscal policy:
Change in the budget balance and/or in its components under the direct control of government. It is usually measured as the residual of the change in the balance after the exclusion of the budgetary impact of automatic stabilisers.

Discretionary revenue measures:
The estimated effect of discretionary measures that change the government revenue (e.g. increasing or reducing tax rates).

Draft budgetary plan:
Presentation of the main orientations and elements in terms of the objectives and measures at the level of the general government and its subsectors for the coming year prior to their adoption by the national parliaments. By 15 October every year the draft budget plan must be submitted by EU Member States to the European Commission and the Eurogroup for evaluation.

Excessive Deficit Procedure:
Excessive Deficit Procedure (EDP), a procedure according to which the EC monitors the development of national budget balances and the general government debt in order to assess and/or correct the risk of an excessive deficit in each Member State.

Expenditure rules:
A subset of fiscal rules that target (a subset of) public expenditure. Expenditure rules in the EU set expenditure benchmarks that are estimated by the movement of expenditure excluding the impact of expenditure on the basis of EU flows and taking into account discretionary revenue measures.

Fiscal consolidation:
An improvement in the budget balance through measures of discretionary fiscal policy.

General government:
The general government sector covers state government, regional and local governments, as well as social security funds, public institutions, funds and agencies. State-owned enterprises are excluded. Such a definition of the general government sector is also used by the EC in its process of budgetary surveillance under the Stability and Growth Pact. For more details, see:
http://www.mf.gov.si/en/areas_of_work/general_government_finance/public_finances/general_goverment_sector/.

Maastricht reference values for public debt and deficits:
A 60% general government debt-to-GDP ratio,
a 3% general government deficit-to-GDP ratio.
Both reference values were specified within the framework of the Treaty of Maastricht establishing the EU (1992).

Maximum expenditure:
The maximum level of expenditures of the general government and individual budgets (state budget, the Health Insurance Institute of Slovenia – ZZZS, the Pension and Disability Insurance Institute of the Republic of Slovenia – ZPIZ, local communities), which is defined in the Framework for the Preparation of the General Government Budget. The level of expenditures depends on the cyclical position of the economy and the formula for its determination is laid down in Article 3 of the Fiscal Rule Act.

Medium-term budgetary framework:
An institutional fiscal device that lets policy-makers extend the horizon for fiscal policy making beyond the annual budgetary calendar, typically for a period from three to five years. Targets can be adjusted under medium-term budgetary frameworks (MTBF) either on an annual basis (flexible frameworks) or only at the end of the MTBF horizon (fixed frameworks).

Medium-term budgetary objective (MTO):
According to the reformed Stability and Growth Pact, Member States must present a medium-term objective in stability programmes and convergence programmes. The adequate minimum benchmark is country-specific to take into account the diversity of economic and budgetary positions and developments as well as of fiscal risks to the sustainability of public finances and is defined in structural terms.

Minimum benchmarks:
The lowest value of the structural budget balance that provides a safety margin against the risk of breaching the Maastricht reference value for the deficit during normal cyclical conditions while also being one of the determinants for the medium-term budgetary objectives. Minimum benchmarks do not cater to other risks such as unexpected budgetary developments and interest rate shocks. They are estimated by the EC.

Neutral fiscal policy:
This orientation of fiscal policy ensures that cyclically adjusted budgetary balance remains unchanged over the business cycle, while allowing for the operation of automatic stabilisers.

One-off and temporary measures:
Government measures and transactions having a transitory budgetary effect that does not lead to a sustained change in the budgetary position.

<u>Output gap:</u>
The difference between actual output and estimated potential output. In the average of the entire normal economic cycle, this difference is zero.

<u>Potential GDP:</u>
The level of real GDP in a given year that is consistent with a stable rate of inflation. If actual GDP rises above its potential level, then constraints on capacity begin to bind and inflationary pressures build; if GDP falls below potential, then resources are lying idle and inflationary pressures abate. In terms of methodology the measuring of potential output is associated with significant risks, wherefore the estimates of potential GDP may be subject to change.

<u>Primary budget balance:</u>
The budget balance net of interest payments on general government debt.

<u>Primary structural budget balance:</u>
The structural budget balance net of interest payments.

<u>Pro-cyclical fiscal policy:</u>
A fiscal stance that amplifies the economic cycle by increasing the structural primary deficit during an economic upturn, or by decreasing it in a downturn. A neutral fiscal policy keeps the cyclically-adjusted budget balance unchanged over the economic cycle but lets the automatic stabilisers work.

<u>Public debt:</u>
Consolidated gross debt for the general government sector. It includes the total nominal value of all debt owed by public institutions in the Member State, except that part of the debt owed to other public institutions in the same Member State.

<u>Significant deviations:</u>
Under EU law significant deviations in terms of budgetary developments are deemed to be those in which deviations from the adjustment path towards the medium-term budgetary objective is at least 0.5 percentage point of GDP in one year or 0.25 percentage point of GDP in the two year average. The same applies to deviations from the expenditure rule. If a significant deviation is established ex post, it may trigger a significant deviation procedure, which may also result in the imposition of fines on the Member State that violates the rules.

<u>Stability and Growth Pact (SGP):</u>
Approved in 1997 and reformed in 2005 and 2011. It is a set of rules which are to ensure the proper functioning of fiscal policies in EU Member States. It transposes the requirements of the Maastricht Treaty regarding the surveillance of Member State budgetary policies into EU legislation. A detailed description of the application of the SGP's provisions is published annually by the EC in the publication Vade Mecum on the Stability and Growth Pact.

<u>Stability programme:</u>
Medium-term budgetary strategies presented annually to the EC by those Member States that have already adopted the euro. The stability programme must be drafted in accordance with the provisions of the Stability and Growth Pact. In Slovenia the stability programme as a key medium-term budget document is also defined by the Fiscal Rule Act. Slovenia must submit it to the European Commission by the end of April every year.

Stock-flow adjustment:
The stock-flow adjustment (also known as the debt-deficit adjustment) ensures consistency between the net borrowing (flow) and the variation in the stock of gross debt. It includes the accumulation of financial assets, changes in the value of debt denominated in foreign currency, and remaining statistical adjustments.

Structural budget balance:
The actual budget balance net of the cyclical component and one-off and other temporary measures. As a result, the structural budget balance, in comparison with the budget balance, gives a better measure of the underlying trend in the budget balance, and the offset structural balance in the long run creates conditions for the functioning of the general government without borrowing.