REPUBLIC OF SLOVENIA
FISCAL COUNCIL

Assessment of the Draft Revised Budget of the Republic of Slovenia for 2023

August 2023

Document No: 30-4/2023/10

This assessment is made on the basis of the Draft Revised Budget of the Republic of Slovenia for 2023 II, which was received by the Fiscal Council on 11 August 2023. Data available up to and including 18 August 2023 were used.

EXECUTIVE SUMMARY

The scale of the August floods in Slovenia represents also an exceptional macroeconomic and fiscal shock. Although its financial impact is currently unknown, the draft revised state budget for 2023 represents only the first step in the budgetary financing aimed at addressing the large financial impact of the floods. The impact will be more clearly reflected in the autumn draft budget documents for 2024 and 2025, which should include damage assessments and estimates of the effects of the Government's recovery measures. The natural disaster occurred at a time when the state budget deficit for the first seven months was higher than in the same period of the previous year. As regards the outturn of the adopted state budget, the deficit for the last five months of the year is expected to amount to about EUR 2.6 billion, almost twice as high as for the whole of last year. Against this background, economic activity has been at a relatively high level, with some signs of a slowdown in the otherwise solid economic dynamics, amid growing pessimism and unfavourable economic trends in the EU.

In April this year, the Fiscal Council assessed the Stability Programme and, on this basis, in May presented its assessment of the revised state budget for 2023. In this regard, it highlighted the expansionary fiscal policy stance this year, in which exceptional circumstances still apply. The Fiscal Council noted that the set high level of state budget expenditure in 2023 and the declining cyclical revenue-to-GDP ratio also contribute significantly to the limited room for manoeuvre for additional fiscal policy measures in the coming years, as they weaken the structural position of public finances and thus affect the medium-term sustainability of public debt.

According to the Fiscal Council, a change in only one component of budget expenditure, amounting to EUR 220 million, in the current revised state budget for 2023 does not affect the assessment of the fiscal policy situation and compliance with the fiscal rules adopted at the time of the first revised budget this year. The impact of the projected change of EUR 300 million in the financial assets and liabilities account on the general government balance and on the debt position, and thus on compliance with the fiscal rules, cannot be assessed at this stage. In principle, a large-scale natural disaster is "one-off event", which is not taken into account in the calculation of the indicators of compliance with the fiscal rules. In addition, the amendment presented in the draft revised state budget will increase the net debt but not the gross debt of the general government. This is because the financing will come from the reduction of funds in the state budget account. These remain high, also because of the effective public debt management.

The Fiscal Council regularly draws attention to deficient budgeting, insufficient assessment of the impact of discretionary measures, systematic under- or over-estimation of individual revenue and expenditure categories, and uncoordinated processes for the drafting of budget documents. All of the above warnings will be particularly relevant in the uncertain situation ahead, when the Government will have to ensure even greater transparency in the drafting and implementation of the state budget, in particular in the case of the establishment of an extra-budgetary flood relief fund and in the case of a fund that would be part of the entire general government sector subject to fiscal rules. The same applies to already existing budgetary funds that could be a source of financing for flood relief. The warnings about the need to create fiscal space in good times in order to make fiscal policy work in bad times have also proven to be adequate.

This natural disaster should be seen as an additional incentive to integrate a greater degree of risk analysis into the medium-term budget planning. Such analyses are also part of the recommendations of international institutions to ensure more stable and sustainable public finances, as the state is usually the first to help those affected by natural disasters. Such an analysis would probably suggest that Slovenia's small size, geographical features and the frequent occurrence of natural disasters would require the creation of a dedicated budget fund. In this context, it would also be necessary to limit the moral hazard associated with increasing the role of the state by raising private sector awareness of property insurance. The funds available to Slovenia, in particular from various EU sources, are unlikely to be available at the current high levels in the coming decades. Notwithstanding the need to act urgently, the emergency measures should also be well targeted and ensure the efficient use of public money. Against this background, and given the medium-term implications of delayed action for the sustainability of public finances, the Government should also address in its future budget plans the related challenges that had not been addressed before the natural disaster.

The legislative basis and background for drawing up the assessment of the Draft Revised Budget for 2023

On 11 August 2023, the Government of the Republic of Slovenia submitted the Draft Revised Budget of the Republic of Slovenia for 2023 II (hereinafter: the Draft Revised Budget) to the Fiscal Council for an assessment of compliance with the fiscal rules. The Fiscal Council has received a clarification from the Ministry of Finance that more detailed data are not available solely due to the limited amendments to the Draft Revised Budget. At the time of receiving the Draft Revised Budget for its assessment, the Fiscal Council was not provided information regarding the impact of the revised state budget on the balance of the general government sector as a whole, nor with the revised framework for the drafting of general government budgets for the 2022–2024 period.[1]

Pursuant to point two of paragraph two of Article 7 of the Fiscal Rule Act (hereinafter: the FRA), the Fiscal Council is obliged to make an assessment of compliance with the fiscal rules on the basis of a draft revised state budget. The assessment of compliance with the fiscal rules is made for the general government sector as a whole in accordance with paragraph one of Article 1, the definition in Article 2 and the definition of the implementation of the medium-term balance in Article 3 of the FRA. Pursuant to paragraph two of Article 9f of the Public Finance Act, the Fiscal Council is obliged to make an assessment of the Draft Revised Budget within fifteen days of its receipt. The deadline for the Fiscal Council to submit its assessment of the Draft Revised Budget to the National Assembly and the Government is thus 26 August 2023.

Pursuant to Articles 3 and 15 of the FRA, the Fiscal Council is required to monitor compliance with the fiscal rules for the entire general government sector in accordance with the European System of Accounts methodology (ESA, 2010). The Government must ensure compliance with the fiscal rules by including all public finance budgets and institutional units that constitute the general government sector. The state budget constitutes the largest unit, but still only slightly more than one third of the non-consolidated expenditure of the entire general government sector and is, like other public finance budgets (social security systems, local communities), drawn up according to the methodology of the International Monetary Fund for monitoring government financial statistics (GFS) based on the cash flow principle.[2]

The Fiscal Council gave its assessment of the first revised budget for 2023 regarding compliance with the fiscal rules in the first half of May 2023.[3] As the Fiscal Council did not receive updated data for the general government sector as a whole at the time of the submission of the Draft Revised Budget for assessment, it is not able to assess the compliance with the fiscal rules in the submitted budget documents in accordance with the FRA. Given that the set of amendments in the Draft Revised Budget is limited to only one expenditure component, in this paper the Fiscal Council mainly summarises the main findings of the May assessment of the Revised State Budget and indicates the possible impact of the amendments resulting from the Draft Revised Budget on compliance with the fiscal rules.

In September 2022[4], the Fiscal Council assessed that the outlook for 2023 was shrouded in extreme uncertainty and characterised by a high risk of further deterioration of the economic growth outlook,

[1] The latest applicable framework for the drafting of the general government budgets for the 2022-2024 period was published in Official Gazette No 146/2022. This framework was assessed by the Fiscal Council in October 2022.

[2] The structure of the general government sector is available at: http://mf.arhiv-spletisc.gov.si/si/delovna_podrocja/javne_finance/tekoca_gibanja_v_javnih_financah/sektor_drzava/(Only in Slovene).

[3] Fiscal Council (2023).

[4] https://www.fs-rs.si/wp-content/uploads/2022/10/Exceptional-circumstances_September-2022.pdf.

which could have significant financial implications for the financial situation of the general government sector, calling for flexible action by the Government. Thus, the exceptional circumstances allowing a temporary deviation from the medium-term fiscal balance under Article 12 of the FRA continue to be invoked in 2023 for a set of measures to address their consequences.

1. Comparison of revenue and expenditure in the Draft Revised Budget with the budget currently in force

The revenue in the Draft Revised Budget does not deviate in any of its components from the budget currently in force for 2023. In the absence of updated macroeconomic forecasts and, consequently, an updated estimate of changes in tax bases, the projected revenue growth remains slightly above 6%. Revenues are thus projected to lag behind GDP growth but contribute significantly to building up the state budget deficit in 2023. The main driver behind the relatively low revenue growth is subdued tax revenue growth.

The already high projected expenditure growth in 2023 based on the current budget increases to 18.9% in the Draft Revised Budget. The main components contributing to the high expenditure growth remain investments, labour costs, current transfers to the social security funds and reserves.[5] The only change in the Draft Revised Budget that has an impact on the budget balance is the reserves, which were one of the main reasons for the high expenditure growth in the current budget.[6] Compared to the current budget, reserves are increased by EUR 220 million.

In addition to the change in the level of reserves directly affecting state budget expenditure, the second change in the Draft Revised Budget is included in the financial assets and liabilities account.

Table 1.1: State budget

EUR million, unless otherwise stated	2022 outturn	2023 Current budget	2023 Draft Revised Budget	2023 Draft Revised Budget-Current budget
Revenue	**12,345**	**13,144**	**13,144**	**0**
VAT	4,747	5,082	5,082	0
Excise duties	1,446	1,606	1,606	0
Personal income tax	1,586	1,625	1,625	0
Corporate income tax	1,553	1,415	1,415	0
EU funds	957	1,470	1,470	0
Non-tax	770	672	672	0
Other revenue	1,284	1,274	1,274	0
Expenditure	**13,709**	**16,082**	**16,302**	**220**
Total labour costs	3,751	4,328	4,328	0
Transfers to individ. and hou.	1,965	1,897	1,897	0
Exp. on goods and services	1,526	1,416	1,416	0
Investment	1,669	2,465	2,465	0
Curr. transf. to soc. sec. funds	1,526	1,565	1,565	0
Subsidies	632	856	856	0
Interest	655	681	681	0
Payments to the EU budget	730	730	730	0
Reserves	561	1,460	1,680	220
Other expenditure	694	685	685	0
Exp. excl. invest. and interest	*11,385*	*12,937*	*13,157*	*220*
Balance	**-1,364**	**-2,938**	**-3,158**	**-220**
Balance (in % of GDP)	**-2.3**	**-4.5**	**-4.9**	**-0.3**

Source: MoF, SORS, IMAD, FC calculations.

[5] For more information, see the Fiscal Council (2023).

[6] The cost-of-living crisis reserve (just under EUR 500 million), the 'normal' budget reserve (close to EUR 570 million, similar to the 2022 level) and the reserves under the National Recovery and Resilience Plan (around EUR 400 million) contribute to the creation of the reserve in the current budget for 2023.

Table 1.2: State budget

EUR million, unless otherwise stated	2022 (outturn)				2023 (Draft Revised Budget)					2023/2022 %		2023-2022	
	total	COVID	infl. mit.	excl. COVID and infl. mit.	total	COVID	infl. mit.	floods	excl. COVID, infl. mit., floods	total	excl. COVID, infl. mit., floods	total	excl. COVID, infl. mit., floods
Revenue	**12,345**		**-217**	**12,562**	**13,144**		**-202**		**13,346**	**6.5**	**6.2**	**799**	**784**
VAT	4,747		-58	4,805	5,082		-73		5,155	7.1	7.3	335	349
Excise duties	1,446		-99	1,545	1,606		-33		1,639	11.1	6.1	160	94
Personal income tax	1,586			1,586	1,625				1,625	2.5	2.5	39	39
Corporate income tax	1,553			1,553	1,415				1,415	-8.9	-8.9	-138	-138
EU funds	957			957	1,470				1,470	53.5	53.5	513	513
Non-tax	770			770	672				672	-12.7	-12.7	-98	-98
Other revenue	1,284		-60	1,344	1,274		-96		1,370	-0.8	1.9	-11	25
Expenditure	**13,709**	**885**	**253**	**12,570**	**16,302**	**371**	**887**	**220**	**14,824**	**18.9**	**17.9**	**2,594**	**2,253**
Total labour costs	3,751	37		3,714	4,328	40	3		4,285	15.4	15.4	577	571
Transfers to individ. and hou.	1,965	134	104	1,727	1,897	11	29		1,858	-3.4	7.6	-67	131
Exp. on goods and services	1,526	156		1,370	1,416	19			1,397	-7.2	1.9	-111	26
Investment	1,669	55		1,614	2,465	147			2,318	47.7	43.6	796	704
Curr. tr. to soc. sec. funds	1,526	279		1,246	1,565	0			1,565	2.6	25.6	40	319
Subsidies	632	51	150	432	856	97	349		409	35.3	-5.2	223	-22
Interest	655			655	681				681	3.9	3.9	26	26
Payments to the EU budget	730			730	730				730	0.1	0.1	1	1
Reserves	561			561	1,680		503	220	957	199.4	70.6	1,119	396
Other expenditure	694	172		522	685	58	3		624	-1.3	19.5	-9	102
Exp. excl. invest. and interest	*11,385*	*830*	*253*	*10,302*	*13,157*	*225*	*887*	*220*	*11,825*	*15.6*	*14.8*	*1,772*	*1,524*
Balance	**-1,364**	**-885**	**-470**	**-8**	**-3,158**	**-371**	**-1,089**	**-220**	**-1,478**			**-1,794**	**-1,470**
Balance (in % of GDP)	**-2.3**	**-1.5**	**-0.8**	**0.0**	**-4.9**	**-0.6**	**-1.7**	**-0.3**	**-2.3**			**-2.6**	**-2.3**

Source: MoF, SORS, IMAD, FC calculations.

This change has no direct impact on the balance of revenue and expenditure and relates to a decrease of EUR 300 million under the heading "Financial Asset Management" in the framework of support for the restructuring or recapitalisation of financial and non-financial corporations. The appropriations under the heading "Natural Disaster Relief" are increased by the same amount as part of the financing of the emergency measures.

2. Outlook for the 2023 state budget outturn compared with the January-July 2023 outturn

The currently known outturn of the state budget until the end of July 2023 indicates possible deviations of certain budget items in 2023 from the current budget. All of the likely deviations outlined below were identified by the Fiscal Council when it assessed the budget documents at the time of the adoption of the amendments to the 2023 budget last autumn and the adoption of the revised 2023 budget this spring.[7]

[7] Fiscal Council (2022) and Fiscal Council (2023).

Table 2.1: State budget

EUR million, unless otherwise stated	Jan.-Jul.				Aug.-Dec.				2022	2023**	2023 compared to 2022	
	2022	2023	2023 compared to 2022		2022	2023*	2023 compared to 2022					
				%				%				%
Revenue	**7,267**	**7,246**	**-21**	**-0.3**	**5,077**	**5,898**	**820**	**16.2**	**12,345**	**13,144**	**799**	**6.5**
VAT	2,749	2,907	158	5.7	1,998	2,175	177	8.9	4,747	5,082	335	7.1
Excise duties	815	950	135	16.5	631	656	25	4.0	1,446	1,606	160	11.1
Personal income tax	832	884	52	6.3	754	741	-13	-1.8	1,586	1,625	39	2.5
Corporate income tax	1,044	843	-202	-19.3	509	572	63	12.5	1,553	1,415	-138	-8.9
EU funds	569	516	-53	-9.3	388	953	565	145.6	957	1,470	513	53.5
Non-tax	434	396	-38	-8.7	337	276	-60	-17.9	770	672	-98	-12.7
Other revenue	824	750	-74	-9.0	461	524	63	13.7	1,284	1,274	-11	-0.8
Expenditure	**7,520**	**7,833**	**313**	**4.2**	**6,189**	**8,469**	**2,280**	**36.8**	**13,709**	**16,302**	**2,594**	**18.9**
Total labour costs	2,180	2,413	233	10.7	1,571	1,915	344	21.9	3,751	4,328	577	15.4
Transfers to individ. and hou.	1,156	1,133	-23	-2.0	809	764	-44	-5.5	1,965	1,897	-67	-3.4
Exp. on goods and services	813	739	-74	-9.1	713	677	-36	-5.1	1,526	1,416	-111	-7.2
Investment	522	641	119	22.8	1,147	1,824	677	59.0	1,669	2,465	796	47.7
Curr. transf. to soc. sec. funds	903	968	65	7.2	623	597	-26	-4.1	1,526	1,565	40	2.6
Subsidies	390	522	132	34.0	242	333	91	37.5	632	856	223	35.3
Interest	406	434	29	7.0	249	246	-3	-1.2	655	681	26	3.9
Payments to the EU budget	408	388	-20	-4.9	321	342	21	6.5	730	730	1	0.1
Other expenditure	742	595	-148	-19.9	513	1,770	1,257	245.1	1,255	2,365	1,110	88.4
Balance	**-252**	**-587**	**-334**		**-1,111**	**-2,571**	**-1,460**		**-1,364**	**-3,158**	**-1,794**	

*Source: MoF, FC calculations. Note: *implicitly calculated to match MoF forecast.** Draft Revised Budget (Aug. 23).*

Based on a seven-month outturn, total revenue is expected to be lower than the current budgetary projections for the whole of 2023. While revenues for the first seven months of the year were in line with the same period last year, revenues for the last five months of the year are expected to exceed the same period last year by more than EUR 800 million. The most likely slippage is on the side of revenues from EU funds. In the remaining five months of 2023, a full year's revenue would be needed to meet the current budget projections. This is also unlikely to happen even if we take into account EU aid from the EU Solidarity Fund and the accelerated absorption of funds from other EU sources. Already in May this year, the Fiscal Council assessed that the EU revenue projections were optimistic, mainly due to delays in meeting the milestones of the National Recovery and Resilience Plan, which are a condition for the disbursement of funds.[8] The Fiscal Council assesses that the lower volume of revenues from EU funds could be partly offset by higher revenues from personal income tax and excise duties compared to the projections of the adopted revised budget.

Total expenditure in 2023 is also likely to be lower than projected in the current budget, and the deviation could be even larger than on the revenue side. In line with the lower revenues from EU funds as mentioned above, among the expenditure components, investments are expected to show the largest deviation from the annual budget plans. According to the Draft Revised Budget, expenditure in the seven months was about EUR 310 million higher than in the same period last year, and in the five months to the end of the year it is expected to be EUR 2.3 billion higher than in the corresponding

[8] For more information, see the Fiscal Council (2023).

period last year. While investments in the first seven months were around EUR 120 million higher than in the same period last year, on an annual basis they are expected to be almost EUR 800 million higher than in the full year 2022. Despite continued high levels of investment, particularly in the construction sector, we assess that such an acceleration to reach the full-year target is highly unlikely in the remainder of the year, also in view of the tight labour market.[9] According to the projections of the revised state budget, the funds earmarked to alleviate the effects of the cost-of-living crisis also fell short in the first seven months of the year, compared with plans of just under EUR 900 million for the whole year as expenditure for this purpose amounted to around EUR 260 million.[10] However, with energy prices easing and certain measures being withdrawn, no further acceleration in the use of these funds is expected before the end of the year.

Despite the additional expenditure planned in the Draft Revised Budget, the outturn of the state budget up to July suggests the possibility of a lower-than-projected deficit this year. Reaching or even exceeding the planned deficit of EUR 3.2 billion would only be possible in the event of an exceptionally sharp economic downturn or a significant increase in expenditure, which is not foreseen in the Draft Revised Budget. The state budget deficit in the first seven months of the year totalled around EUR 600 million, and in order to reach the projected deficit for the whole year it would have to reach EUR 2.6 billion in the five months to the end of the year.[11] However, the state budget deficit in 2023 is expected to be higher than in 2022, when it totalled just under EUR 1.4 billion or -2.3% of GDP.

3. Macroeconomic and fiscal aspects of drawing up the Draft Revised Budget and other possible steps to recover from the floods

In the Draft Revised Budget, the Ministry of Finance has not been able to take into account the new macroeconomic projections. The comprehensive forecasts taken into account by the Ministry of Finance[12] in its budget projections were last prepared by the Institute of Macroeconomic Analysis and Development (hereinafter: IMAD) in March 2023. All institutions, with the exception of the Bank of Slovenia, are forecasting lower real GDP growth in 2023 than the IMAD forecast. However, since the publication of the IMAD forecast, the majority of macroeconomic forecasters for Slovenia have revised upwards their real GDP growth forecasts for this year. Regarding the inflation forecasts for 2023, the changes in the institutions' forecasts were somewhat more hetereogenous after the presentation of the IMAD forecasts, but on average no major revisions were made. The IMAD is expected to produce new forecasts in the first half of September following the full publication of national accounts data.

Based on currently available data, economic activity remains solid, but with a moderation in both household consumption and export dynamics. The release of GDP data for the second quarter of this year suggests strong growth, as GDP increased at a quarterly rate of 1.4%, which is contrary to the expected slowdown in the dynamics of economic activity.[13] Data on the main macroeconomic bases underlying the budget revenues show that household consumption in particular is easing, while

[9] In fact, the change in the state budget's investments over the same period has so far only once (at the end of 2022) reached the level that would allow this target to be met in 2023.

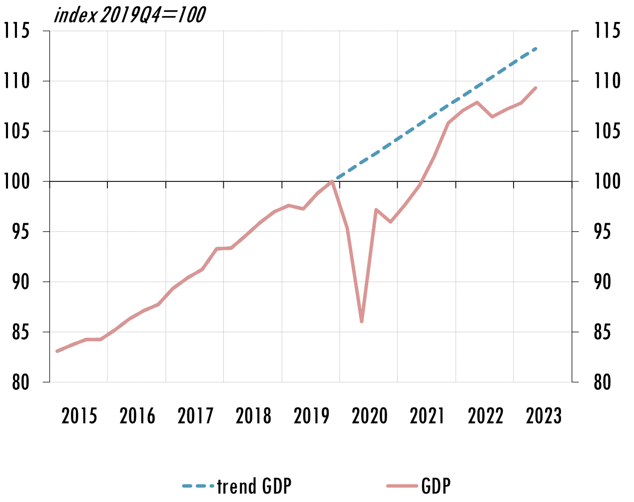
[10] Revenue from this heading was estimated by the Fiscal Council to be around EUR 170 million lower over the same period, which is in line with the projected outturn for the full year.

[11] The highest ever state budget deficit in five consecutive months was EUR 2.2 billion in March 2021 (during the COVID-19 epidemic).

[12] The IMAD forecasts provide the basis for budgeting as laid down in the Decree on development planning documents and procedures for the preparation of the draft state budget and draft local government budgets (Official Gazette of the Republic of Slovenia [*Uradni list RS*], Nos 44/07 and 54/10).

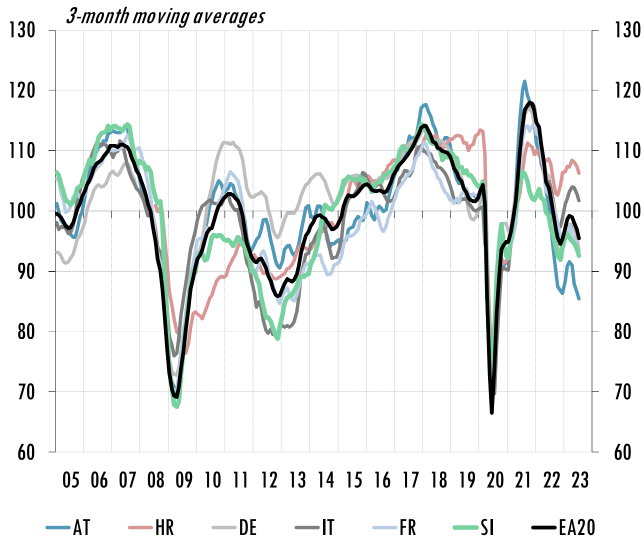
[13] The Bank of Slovenia's short-term predictive models indicated a 0.3% decline in economic activity in the second quarter. See Box 3.1 in: Bank Slovenia (2023).

Figure 3.1: GDP compared to pre-crisis trend



Source: SORS, FC calculations. Note: Trend is calculated on the basis of 2015-2019 period.

Figure 3.2: Economic sentiment indicator (ESI)



Source: European Commission, FC calcualtions.

employment continues to grow.[14] Nominal GDP grew by just over 12% year-on-year in the first half of the year, while IMAD's spring forecast projects growth of just under 10% for the whole of 2023. Against this background, the updated average assessment of the output gap for 2023 used by the Fiscal Council has changed by only 0.1 percentage points compared to the data available at the time of the assessment of the Stability Programme 2023 and of the first revised state budget of this year.

A number of indicators point to increasing macroeconomic risks, especially in the international environment. In the EU countries, confidence indicators for most activities were significantly lower in the summer months than at the beginning of the year. The exceptions were consumers, who were more optimistic than the business sector. Although the current GDP momentum in the EU remained positive in Q2 2023, it halved compared to the beginning of the year. Activity also contracted in some important trading partners such as Austria and Germany, the latter being one of only four EU countries where GDP contracted in each of the first two quarters of this year.

Slovenia reportedly suffered the highest per capita damage from natural disasters of all EU countries in the last few decades.[15] The assessment of the damage caused by the floods in August this year is not yet known, but the extent of the damage will have a major impact on fiscal developments in the coming years. On the basis of the per capita costs of other selected floods around the world, the financial impact of floods in Slovenia could be extremely high, given the small size of the country.[16] Experiences of the recent flooding events in Central Europe[17] suggest that the share of the general government sector in the total damage due to public infrastructure damage was just over 50%, with the household sector accounting for around 30% of the total damage, and the business sector accounting for the remaining damage.[18]

[14] Data on the income structure of GDP, which also includes compensation of employees and gross operating surplus, will be published at the end of August.

[15] See Radu (2022).

[16] In terms of flood costs per capita (calculation based on https://en.wikipedia.org/wiki/List_of_disasters_by_cost), Slovenia's recent floods would rank as one of the top 50 flood events, with the highest ever flood costs per GDP (source: https://ourworldindata.org/natural-disasters). These comparisons must take into account methodological differences, unreliable data sources and therefore different estimates even for the same flood event.

[17] See, for example: Mechler and Weichselgartner (2003).

[18] Damage to the business and private sectors depends on factors such as industrialisation, but also on the intensity of tourism in the areas affected by natural disasters.

Based on the information provided so far, Slovenia is expected to receive a grant from the EU Solidarity Fund, but finding additional resources will also be a challenge due to many other development tasks. The EU is expected to allocate a total of EUR 400 million to Slovenia from the EU Solidarity Fund[19], EUR 100 million in 2023 and EUR 300 million in 2024.[20] There are also opportunities for the accelerated use of EU funds in the form of large EU loans and grants under the Multiannual Financial Framework and the Recovery and Resilience Facility.[21] The Government also has some resources available from existing dedicated budgetary funds (e.g. the Water Fund, the Climate Fund, the Forest Fund) to cover the flood and post-flood reconstruction costs. However, in deciding how to use these funds it will also be important to take into account the other purposes for which these funds were installed and to respond to the challenges in areas where reforms were needed before the disaster.

The Government has announced that it will create a special extra-budgetary fund to cover the costs of the floods, as also indicated by the changes in the balance of financial assets and liabilities in the Draft Revised Budget. Similar funds have been in place in the EU for a long time to finance the high costs of certain projects. The resources of such funds account for about 3% of GDP in developed countries, according to the IMF[22]. The EC analysis[23] suggests that the share of the general government sector in the financing of natural disasters has increased over the last decades. Germany has also introduced a number of extra-budgetary funds since World War II, at both the national and federal state levels, and as many as six since the global financial and economic crisis.[24] Two such extra-budgetary funds were set up by Germany after the 2002 floods and in 2013, with a value of between 0.2% and 0.3% of GDP.[25] However, a number of international organisations (e.g. the OECD, the IMF)[26] have warned Germany about the pitfalls of excessive use of extra-budgetary funds.

It is therefore essential to ensure full transparency in the functioning of extra-budgetary funds and in their use. Indeed, there are already issues with public access to data on the performance of existing budgetary funds. According to the IMF[27] definition, extra-budgetary fund transactions are those that are exempted from regular annual budget documents and legislation, even though they relate to the general government sector. One of the most important reasons for the existence of extra-budgetary funds is that they are exempt from standard parliamentary procedures, allowing for simpler and faster decision-making on the purpose of using such funds.[28] Another possible reason for the use of

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[19] The EU Solidarity Fund is an instrument designed to provide rapid assistance to EU Member States or countries in the process of negotiating their accession to the EU. Aid is granted when the damage caused by a major natural disaster exceeds EUR 3 billion or represents at least 0.6% of gross national income (aid has been also granted for public health emergencies since the outbreak of the COVID-19 epidemic). According to the estimate of the Fiscal Council, the threshold for this aid, based on the IMAD spring forecast, is just under EUR 400 million (the first estimates of flood damage to businesses have already exceeded this figure). See also: https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:02002R2012-20200401&qid=1601971117690

[20] https://www.gov.si/en/news/2023-08-09-eur-400-million-from-the-eu-solidarity-fund-to-help-slovenia-cope-with-floods/. Slovenia has received around €48 million in aid for natural disasters from this fund (Source: https://ec.europa.eu/regional_policy/funding/solidarity-fund_en).

[21] The use of funds under the Recovery and Resilience Facility is conditional on the achievement of pre-agreed targets and milestones. Slovenia has so far indicated a limited need for loans from the Facility, with about one fifth (EUR 0.7 billion) of the available loans (EUR 3.2 billion) expected to be drawn. The underlying cost of a Recovery and Resilience Facility (RRF) loan is linked to the required yields on the bonds issued by the EU to finance the Facility. According to the Fiscal Council's estimate for the 10-year bond at end-July 2023 this was very similar to the required yield for Slovenian benchmark bonds. See, for example: https://commission.europa.eu/system/files/2023-08/EU%20Investor%20Presentation%2026July2023.pdf

[22] Allen and Radev (2010).

[23] Radu (2022).

[24] According to the IMF estimates (2023), the assets held in these funds are estimated at around 9% of GDP, while the OECD (2023) estimates them at 10% of GDP.

[25] See, for example: Mechler and Weichselgartner (2003).

[26] See, for example: OECD (2023) and IMF (2022).

[27] Allen and Radev (2010).

[28] Shick (2007).

extra-budgetary funds is to circumvent national fiscal rules (e.g. in Germany).[29] However, according to the ESA2010 methodological rules, the transactions of extra-budgetary funds – similarly as for other institutional units that are not direct budget users but are part of the general government – are also reflected in the general government balance, debt or other indicators, as well as in the fiscal compliance indicators at the EU level.[30] This is also the reason why the functioning of any extra-budgetary fund should be fully transparent, in terms of both financing and expenditure.

4. The compliance of the Draft Revised Budget with other budget documents and fiscal rules

Given that the exceptional circumstances still apply, the Fiscal Council has not yet formally assessed the framework for setting the 2023 expenditure ceilings for the general government balance. The multi-annual budgetary framework for drawing up general government budgets was last revised in October 2022 for 2023. On the basis of the current Draft Revised Budget, it can be concluded that, despite the projected increase in expenditure, the state budget expenditure in 2023 would remain within the ceiling set in the framework for budgeting. With the increase in state budget expenditure, general government expenditure would exceed the expenditure set in the framework. However, this would not be the case if the one-off nature of the additional expenditure in the event of a natural disaster is taken into account. In fact, budget categories related to "one-offs" are not taken into account when assessing compliance with fiscal rules, both under the Fiscal Rule Act (hereinafter: the FRA) and in the context of fiscal rules at the EU level.

Table 4.1: Framework for 2023

General government		State budget		Local govt.	ZPIZ	ZZZS	GDP
targ. balance % of GDP	max E EUR million	targ. balance % of GDP	max E EUR million	max E EUR million	max E EUR million	max E EUR million	EUR million
-5.0	30,055	-5.4	16,700	2,955	7,065	4,340	61,951

Source: Official Gazette of the Republic of Slovenia [Uradni list RS] 146/2022, IMAD (Spring Forecast 2022).

As a rule, expenditure related to natural disasters falls under "one-offs". As defined by the European Commission (2015), the condition for defining a budget category as “one-off” is that it has a purely transitory effect on the budget balance and does not change the fiscal position permanently. Even in the case of a natural disaster, an exceptional event must be linked to a specific event and have an unexpected and rapid impact on general government revenue or expenditure, or on the general government assets or liabilities, which exceeds the normal fluctuations and requires a government response. Only costs directly related to the natural disaster and paid in that connection within a relatively short period after the occurrence of the exceptional event can be considered to be "one-offs". A more precise definition of the listed aspects of "one-offs" related to natural disasters is not provided, leaving room for discretion in classifying budget components as "one-offs".

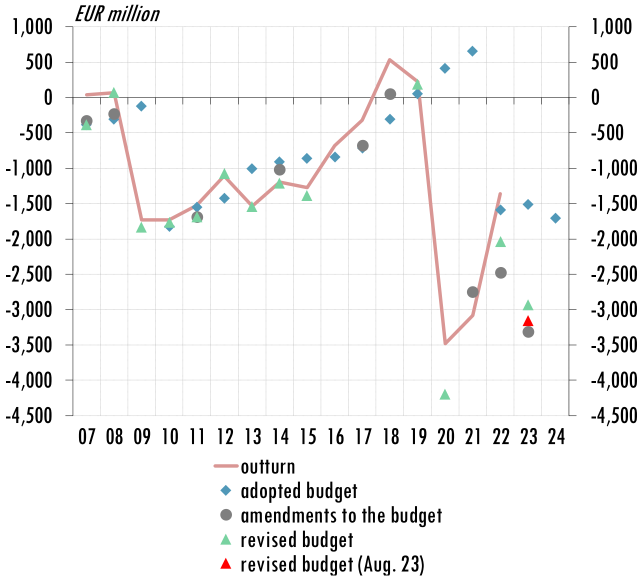
[29] See, for example: https://country.eiu.com/article.aspx?articleid=982925281&Country=Germany&topic=Politics&subtopic=Forecast&subsubtopic=Political+stability&u=1&pid=172836800&oid=312836814

[30] See, for example: https://www.europarl.europa.eu/doceo/document/E-9-2023-001558-ASW_EN.html

According to the indicative assessment from May 2023[31], most of the indicators used for 2023 suggested a deviation in fiscal policy from compliance with the fiscal rules. Mainly due to the high inflation and the projected further strengthening of investment activity, the projections for the general government balance in the 2023 Stability Programme, which also included the revised state budget, suggested an expansionary fiscal policy stance this year, while exceptional circumstances still apply. In this context, the Fiscal Council noted that the high level of state budget expenditure planned for 2023 and the declining cyclical revenue-to-GDP ratio also contribute significantly to the limited room for manoeuvre for additional fiscal policy measures in the coming years, which would worsen the structural position of public finances and thus affect the medium-term sustainability of public debt. Against this background, the deviations in 2023 are slightly lower for most indicators than in 2022, when exceptional circumstances also applied.

According to our assessment, the adoption of the Draft Revised Budget would not have any significant impact on the Fiscal Council's assessment of compliance with the fiscal rules, which was already presented in relation to the revised 2023 state budget adopted in May. Classifying the additional expenditure in the form of reserves of EUR 220 million as a "one-off" would result in this value being excluded from the calculations of the fiscal rule indicators at both national and EU levels. The increase in the deficit resulting solely from the proposed change in the level of reserves will not lead to an increase in government gross debt, which is of relevance for the assessment of compliance with the fiscal rules. Instead of an increase in debt, which would be in line with an increase in the deficit of EUR 220 million, the Draft Revised Budget foresees the financing of this expenditure through a change in resources in the State budget account. The net general government debt will increase by the same amount. The current budget for 2023 foresees a reduction of EUR 1 billion in the state budget account. According to the latest available data, the balance of the state budget account at the end of July 2023 was around EUR 8 billion, some EUR 300 million higher than at the end of 2022 and equivalent to just over 12% of the estimated GDP for 2023.

Figure 4.1: State budget balance



Source: MoF.

[31] Fiscal Council (2023).

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