REPUBLIC OF SLOVENIA
FISCAL COUNCIL

Monthly Information

February 2024

Document No.: 30-1/2024/2

Key highlights[1]

- A key short-term risk to the sustainability of public finances is the renewed demands for public sector wage increases. It should be pointed out that measures taken in the past have maintained, on average, the real purchasing power of public employees at its pre-epidemic level, and large bonuses have been paid as part of the intervention measures. Given that the share of the general government wage bill in GDP is the sixth highest in the EU, we estimate that any increase in the wage bill without a systemic adjustment of wages and other parameters of the employment relationship and, in particular, without the simultaneous adoption of measures to increase the efficiency and accessibility of public services would only increase the risks to public finances (see more on pages 9–11). The latter have already increased since the beginning of the epidemic, due to the adoption of permanent discretionary measures unrelated to crisis mitigation.
- According to preliminary data, the state budget recorded a surplus in January 2024 (EUR 333 million), which, excluding the direct impact of the intervention measures, amounted to EUR 351 million. In both comparisons, the surplus was slightly higher than in January last year.
- The Health Insurance Institute of Slovenia ended 2023 with a deficit, despite increased growth in social contributions revenue and a substantial increase in the transfers from the state budget. The latter is becoming an increasingly important source of financing for the health insurance budget. Since 2017, it has increased by an average annual rate of almost 40%, and its share in GDP was almost 0.6% last year.
- The real purchasing power of pensions has increased over the past four years, as growth in all types of pensions has outpaced cumulative inflation. With pension expenditure growth almost matching the increase in nominal GDP over this period, the share of pension expenditure remained the same last year as in 2019 (9.6% of GDP). The favourable labour market conditions allowed for a reduction in the total transfer from the state budget, which last year (1.8% of GDP) was the lowest since 1995. According to the Pension and Disability Insurance Institute of Slovenia's financial plan for 2024, the transfer from the state budget is expected to increase to 2.1% of GDP this year, due to the high regular adjustment of pensions.
- Municipal budget accounts recorded their largest ever surplus last year, thanks to the increase in the lump sum funding and, in particular, a large transfer from the state budget for post-flood recovery. In addition, expenditure growth slowed, mainly as a result of the stagnation of investment activity, which is linked to the electoral cycle at the local level.

[1] The Fiscal Council will continue to regularly publish an overview of the implementation of the state budget under the cash flow methodology and intervention measures in its monthly publication, provided that the data continue to be available in the future. All comments refer to data known on 2 February 2024.

The state budget – January 2024[2]

- According to preliminary data, the state budget recorded a surplus in January (EUR 333 million), which, excluding the direct impact of the intervention measures, amounted to EUR 351 million. In both comparisons, the surplus was slightly higher than in January last year.
- Total revenue increased by 10.5% year-on-year. The growth was driven predominantly by higher VAT revenue. VAT revenue growth has picked up slightly in recent months but is still well below the 2022 level. The other key driver of revenue growth is higher EU funding, which we attribute to the payment of EUR 536 million following the second payment request under the Recovery and Resilience Facility (RRF), which was partially booked in January.
- Total expenditure was 7.2% lower year-on-year in January, while "core" expenditure (excluding intervention measures) was 2.9% lower. The decrease was mainly related to lower expenditure on subsidies and partly also on interest. At the same time, relatively high growth in other key spending components continued. This is particularly the case for transfers to the Pension and Disability Insurance Institute[3] and investment, while expenditure on labour costs and expenditure on goods and services also increased.

Implementation of intervention measures in January 2024

- There was no expenditure on COVID-19 and cost-of-living crisis under the intervention measures in January; such expenditure is budgeted to decrease significantly this year to a total of EUR 130 million (2023: EUR 1,150 million). In January, EUR 17 million was paid from the state budget for post-flood recovery; a total of EUR 567 million has been paid for this purpose so far. According to the adopted state budget, flood recovery expenditure is expected to amount to EUR 1,115 million this year.

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[2] The comments on the implementation of the state budget refer to the daily data available at https://proracun.gov.si/# (Only in Slovene).

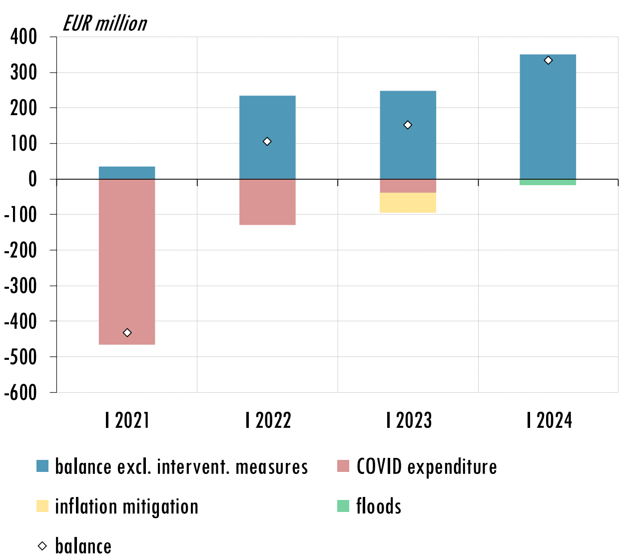
[3] Provisional data on the transfer to the Health Insurance Institute of Slovenia are no longer available, as of the beginning of last year, although it was at a record high last year and is projected to increase further by around a third this year.

Table 1: State budget

EUR million, unless stated otherwise	I 2023					I 2024					I 24/ I 23, %		I 24/ I 23	
	total	COVID	infl. mitig.	floods	excl. interv. measures	total	COVID	infl. mitig.	floods	excl. interv. measures	total	excl. interv. measures	total	excl. interv. measures
Revenue	**1,082**		**-36**		**1,118**	**1,196**				**1,196**	**10.5**	**7.0**	**114**	**78**
VAT	451		-15		466	515				515	14.1	10.5	64	49
Excise duties	132		-9		141	137				137	3.2	-3.4	4	-5
Personal income tax	147				147	166				166	12.7	12.7	19	19
Corporate income tax	94				94	102				102	8.4	8.4	8	8
EU funds	83				83	116				116	39.9	39.9	33	33
Non-tax	60				60	46				46	-23.2	-23.2	-14	-14
Other revenue	115		-12		127	114				114	-0.3	-9.7	0	-12
Expenditure	**930**	**39**	**21**		**871**	**863**	**0**		**17**	**845**	**-7.3**	**-2.9**	**-67**	**-25**
Total labour costs	332	6			326	346			0	346	4.3	6.2	14	20
Transfers to individ. and hou.	167	1	21		145	159			5	154	-5.0	5.6	-8	8
Exp. on goods and services	72	2			71	81	0		12	69	12.0	-2.6	9	-2
Investment	27	2			25	40				40	47.0	61.4	13	15
Curr. transf. to soc. sec. funds	79	0			79	124				124	57.1	57.2	45	45
Subsidies	98	16			82	10				10	-90.1	-88.1	-88	-72
Interest	47				47	21				21	-55.9	-55.9	-26	-26
Payments to the EU budget	49				49	45				45	-8.9	-8.9	-4	-4
Other expenditure	59	12			47	38	0			37	-36.1	-20.5	-21	-10
Balance	**152**	**-39**	**-56**		**247**	**333**	**0**		**-17**	**351**			**181**	**103**

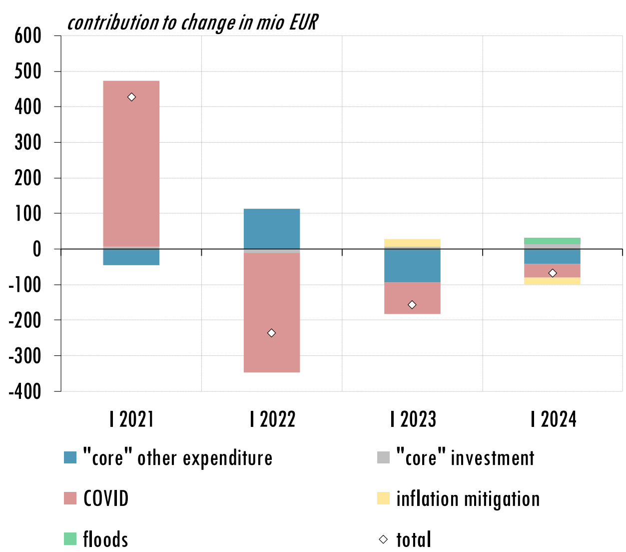
Source: MoF, FC calculations.

Figure 1: State budget balance



Source: MoF, FC calculations.

Figure 2: Structure of state budget expenditure growth

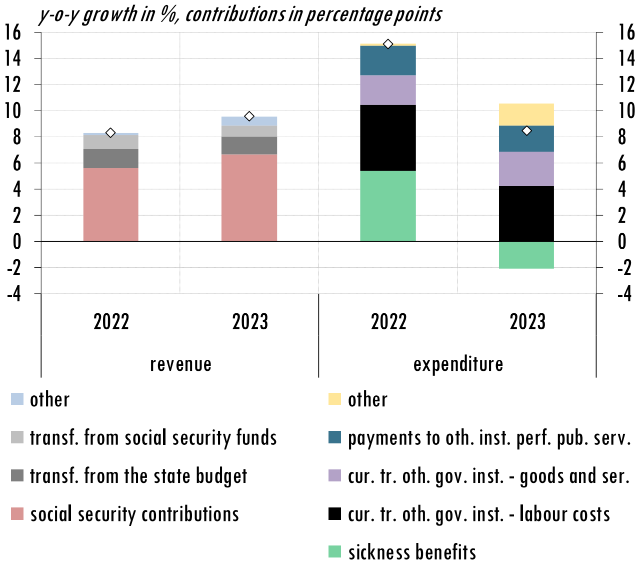


Source: MoF, FC calculations.

Public finance budgets in 2023 (GFS cash flow methodology)

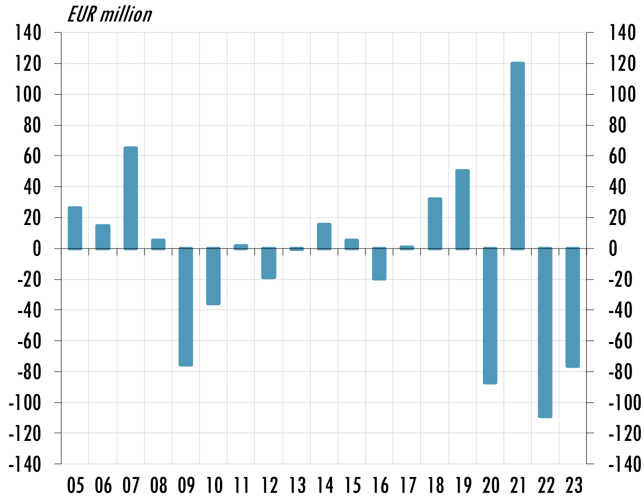
The Health Insurance Institute of Slovenia ended 2023 with a deficit of EUR 76 million. The growth in total expenditure, which represented 7.0% of GDP last year (0.7 p.p. of GDP more than in 2019), was mainly driven by higher transfers to public institutions for labour costs, while the growth in key spending components continued to strengthen. Transfers to public institutions for intermediate consumption and transfers to entities other than budget users also increased by more than a tenth. The slowdown in the growth of total expenditure (from 15.1% in 2022 to 8.5% in 2023) was exclusively due to a decrease in expenditure on sickness benefits. Nevertheless, sickness benefit expenditure accounted for 13.7% of total expenditure of the Health Insurance Institute of Slovenia last year, which is 4.2 p.p. more than in 2014, before the start of the rapid growth. Revenue growth picked up slightly last year (from 8.3% in 2022 to 9.6% in 2023). In fact, favourable labour market conditions, together with relatively high wage growth, allowed for growth in social contributions revenue at a rate that has

Figure 3: ZZZS revenue and expenditure



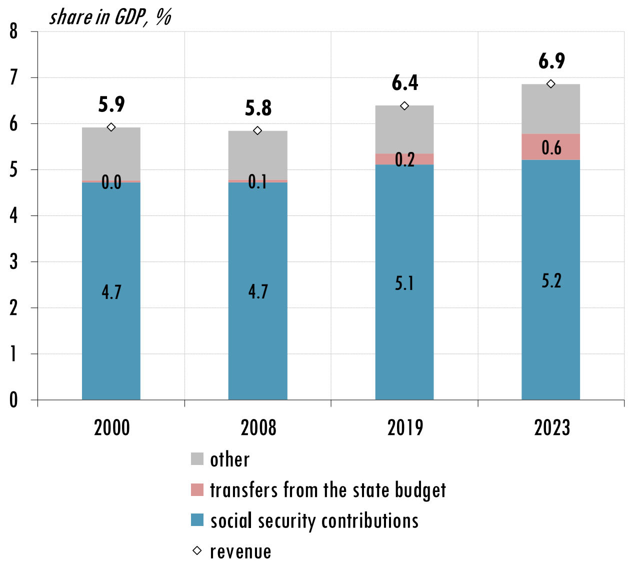
Source: MoF, FC calculations.

Figure 4: Health Insurance Institute of the Republic of Slovenia (ZZZS) budget balance



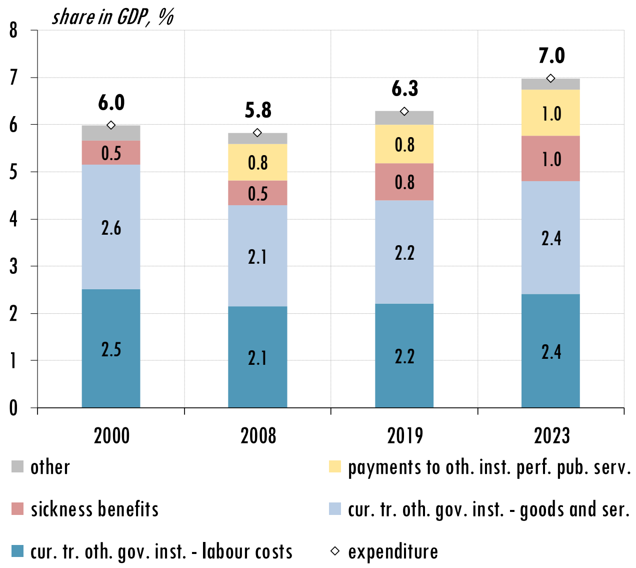
Source: MoF.

Figure 5: ZZZS revenue



Source: ZZZS, SORS, IMAD, FC calculations.

Figure 6: ZZZS expenditure

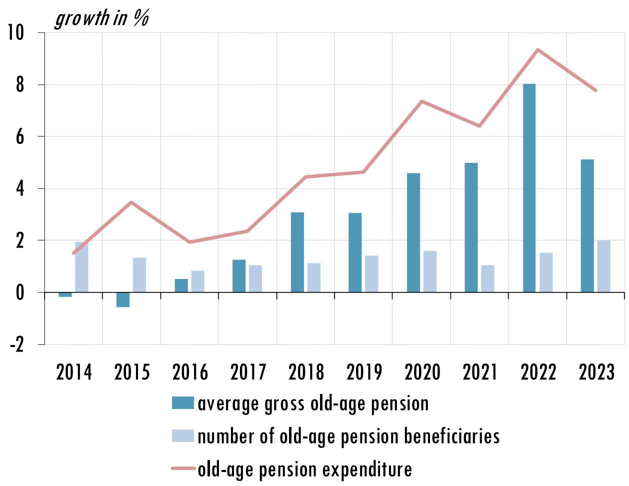


Source: ZZZS, SORS, IMAD, FC calculations.

been noticeably higher over the last three years than the long-term average. However, the even faster growth in expenditure in recent years has led to a substantial increase in the transfer from the state budget, which has become an increasingly important source of financing for the health insurance budget. From 2017, when it began to increase, to last year, it has increased by almost 40% annually on average, rising from EUR 43 million in 2016 to EUR 358 million last year. Its share in GDP was almost 0.6% of GDP last year. According to the draft financial plan for 2024,[4] the financial position of the Health Insurance Institute of Slovenia is expected to be balanced this year with an additional increase of transfers from the state budget by a third. After excluding the impact of transforming complementary health insurance into compulsory health insurance, amounting to EUR 620 million, revenue and expenditure growth is expected to be 9.4%.

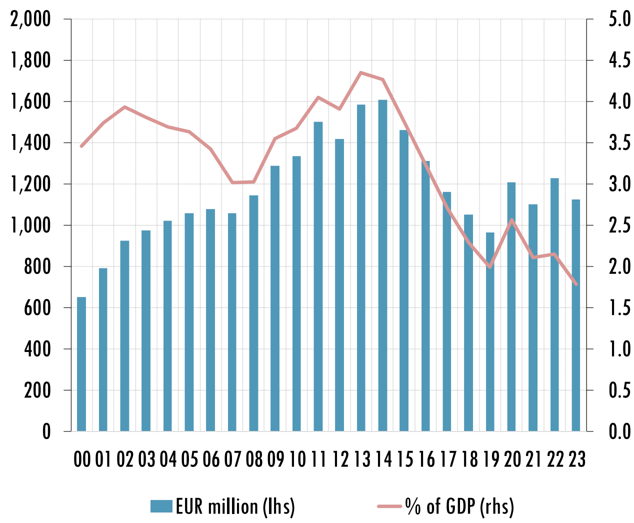
The growth of the expenditure of the **Pension and Disability Insurance Institute of Slovenia** slowed to 5.8% last year (2022: 8.2%), which was mainly due to higher pensions,[5] while the number of beneficiaries increased by 1.1%. Total pension expenditure has increased by EUR 1.4 billion or 30% over the last four years (excluding the intervention allowance). With pension expenditure growth almost matching the increase in nominal GDP over this period, the share of pension expenditure remained the same as in 2019 (9.6% of GDP). The real purchasing power of pensions (excluding allowances) has increased over the past four years, as growth in all types of pensions[6] has outpaced cumulative inflation. The relatively high growth of pensions will continue this year, driven by a high regular adjustment (expected at around 8.2%). Alongside the increase in wage growth, the growth in social contributions revenue also picked up last year (to 8.7%). The favourable labour market conditions allowed for a reduction in the total transfer from the state budget, which fell by EUR 104 million to EUR 1.1 billion last year. This represents 1.8% of GDP forecast for last year, which is the lowest share since 1995. According to the Pension and Disability Insurance Institute of Slovenia's

Figure 7: Old-age pensions*



*Source: Pension and Disability Insurance Fund of Slovenia (ZPIZ), MoF, FC calculations. Note: *Old-age pension beneficiaries represented 76 % of all beneficiaries last year, while volume of old-age pension expenditure represented 81% of all ZPIZ pension expenditure.*

Figure 8: Pension and Disability Insurance Fund of Slovenia (ZPIZ) - state budget funding



Source: MoF, SORS, IMAD, FC calculations.

[4] Available at https://www.zzzs.si/?id=126&detail=A20E8986D69D38EFC1258AA8003F6499 (Only on Slovene).

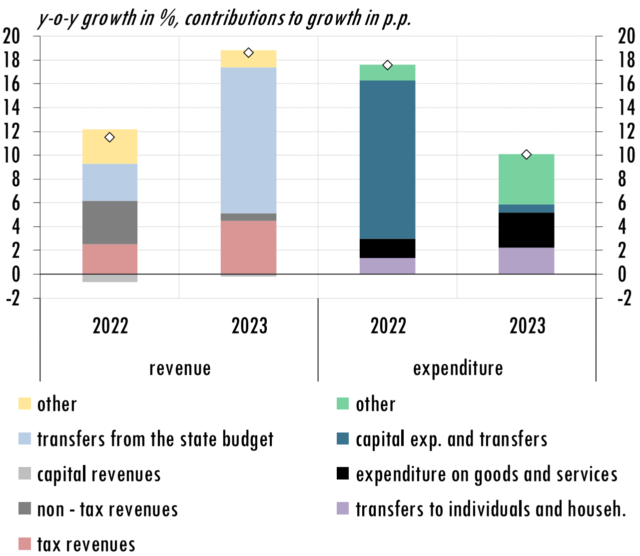
[5] The average old-age pension increased by 5.1% last year.

[6] Old-age pensions account for the largest share of expenditure; the average old-age pension was 24.7% higher on average last year than in 2019. The average disability pension increased by 24.6% over this period, while survivor's and widow's pensions increased by 21.8%. Inflation was 19% in this period.

financial plan for 2024,[7] the transfer is expected to strengthen significantly this year (to 2.1% of GDP), due to the expected higher expenditure growth in the context of the projected increase in pension expenditure due to the high regular adjustment.

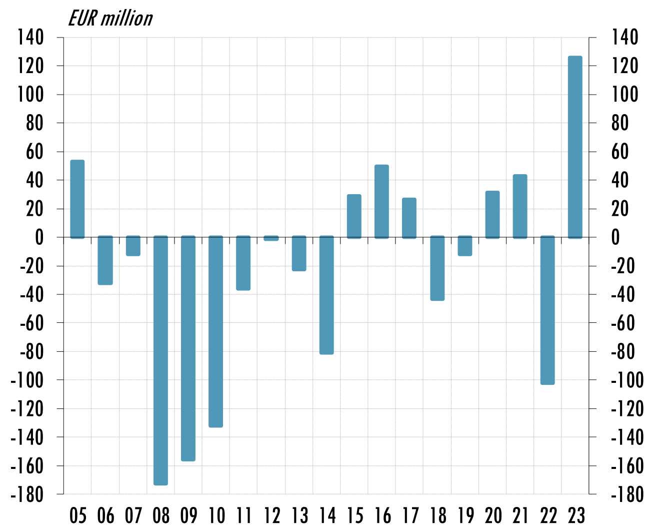
Municipal budget accounts recorded their largest ever surplus last year (EUR 126 million), with revenue growth strengthening further (from 11.5% in 2022 to 18.6%) and expenditure growth slowing (from 17.6% to 10.1%). Growth in personal income tax revenue, a key source of municipal budgets, strengthened further last year on the back of a rise in lump sum funding. A key factor behind the stronger revenue growth was the growth in the transfer from the state budget, which more than doubled due to the floods. Indeed, of the EUR 631 million received from the state budget, EUR 234 million was related to flood recovery costs. The slowdown in expenditure growth was mainly due to the stagnation of investment activity, which is linked to the electoral cycle at the local level. Investment activity typically picks up sharply in the year of local elections and then decelerates markedly. Expenditure growth was mainly driven by increased intermediate spending (also related to flood recovery) and by a further increase in transfers to individuals and households, in particular higher payments of the difference between the price of kindergarten programmes and parents' payments.

Figure 9: Revenue and expenditure of local government



Source: MoF, FC calculations.

Figure 10: Local government budget balance



Source: MoF.

[7] Available at https://www.zpiz.si/cms/content2019/finanni-nart-za-leto-2024 (Only in Slovene).

Highlighted: Risks to the sustainability of public finances

Since the beginning of the epidemic, risks to the sustainability of public finances have been further increased by the adoption of permanent discretionary measures unrelated to crisis mitigation.[8] The Fiscal Council estimates that the measures adopted since the beginning of 2022 alone weaken the general government balance by 1.5% of GDP per year over the period 2022–2025.[9] In this context, it should be pointed out that, following the proposed changes to the fiscal rules at the European level, the room for manoeuvre of fiscal policy in the medium term[10] will be determined to an important extent by the initial structural position of public finances. Slovenia's structural deficit is among the largest in the EU, according to the latest available forecast by the European Commission.[11] The possible adoption of additional discretionary measures with a lasting negative impact on public finances would therefore further constrain the room for manoeuvre of fiscal policy in the years to come.

A key short-term risk to the sustainability of public finances is the renewed calls for public sector wage increases. It should be pointed out that measures taken in the past have, on average, maintained the real purchasing power of public employees at its pre-epidemic level. In fact, real compensation of employees[12] was on average 2.7% higher in the first three quarters of last year than in the first quarter of 2020, and the generous COVID-19 allowances, and many of the measures to address the cost of living crisis that affect households' financial situation, are not included in this comparison. The agreement reached in January to adjust pay bands to 80% of year-on-year inflation at the end of last year implies that the average public sector wage will increase by 2.0% in 2024, which, given the latest available IMAD forecast of 3.9% average inflation this year, means that real purchasing power will not deteriorate significantly this year or will be higher at the end of this year than it was before the epidemic. Total government spending on employee compensation averaged 11.5% of GDP in the first three quarters of last year, which is at the level of the long-term average (1995–2019: 11.4% of GDP) but the sixth highest share among EU Member States. Public satisfaction with the quality of public services is close to the average of EU Member States, but satisfaction with the health system has declined significantly over the last 15 years.

In the past, partial pay agreements with individual occupational groups in the public sector have led to across-the-board increases or to the creation of new (dis)proportions, leading to new demands for partial or across-the-board pay rises. The partial problem-solving is also illustrated by the significant differences in wage trends within the public sector in the period since the start of the epidemic. According to the Ministry of Public Administration, the range of average wage growth in the wage sub-groups since the start of the epidemic in 2020 is between 4.5% and 25.3% in nominal terms.[13] During the epidemic, the most bonuses were paid in the wage sub-groups with the highest wage growth, further increasing disparities and triggering demands for their elimination. The risks to the sustainability of public finances are considerable even without taking into account the financial impact

[8] See Table 3 and Box 2.3 in the Assessment of Budget Documents for 2024 and 2025 (Fiscal Council, October 2023; available at: https://www.fs-rs.si/wp-content/uploads/2023/10/Assessment_Oct23.pdf).

[9] This is the "dynamic simulation of the impact of measures", where we also assess reverse effects. Most measures increase household disposable income or stimulate domestic demand through other levers, with an indirect positive impact on government revenue. The direct or static effect of the measures is on average 2.5% of GDP per year.

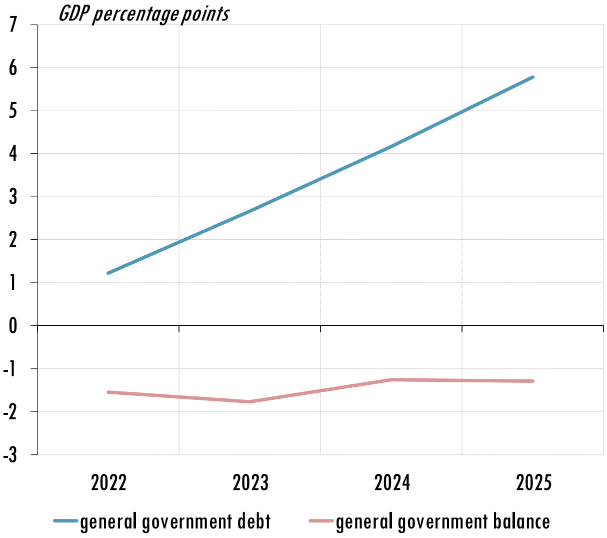
[10] Under the proposed amendment to the European rules, the central element of the new fiscal framework will be a medium-term fiscal plan covering four years, which could be extended to seven years if appropriate reforms and credible investment plans are adopted.

[11] According to the EC forecast of last November, it is expected to amount to 3.7% of GDP in 2023, which would be the tenth largest structural deficit among Member States and 0.5 p.p. of GDP higher than the EU average.

[12] National accounts statistics.

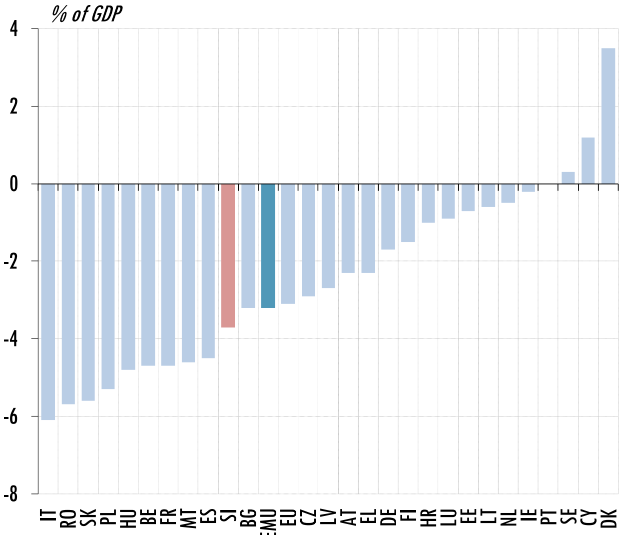
[13] The average of the 11 months of last year for which data are currently available, compared to the first three months of 2020.

Figure 11: Simulation of impact of discretionary measures adopted in 2022 and 2023



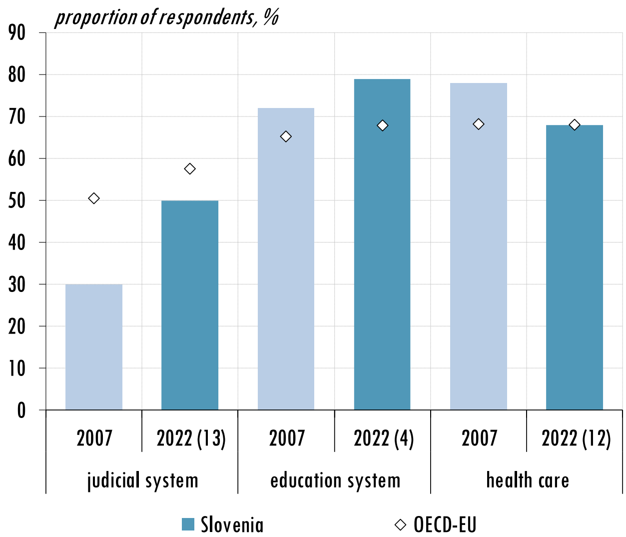
Source: FC estimate (October 2023).

Figure 12: Structural balance 2023



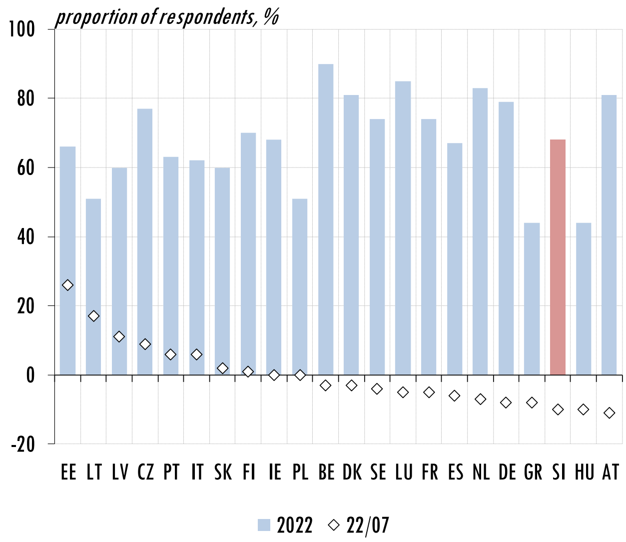
Source: EC forecast (November 23).

Figure 13: Satisfaction with public services



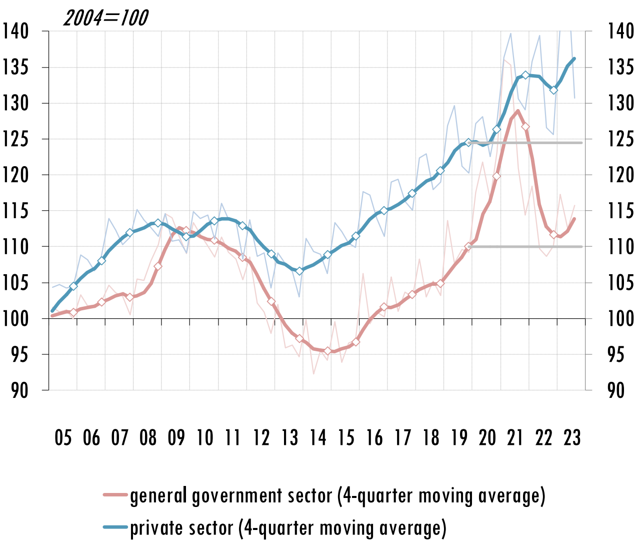
Source: OECD, FC calculations. Note: Slovenia's rank amongst 22 countries that are members of both OECD and EU.

Figure 14: Satisfaction with health care



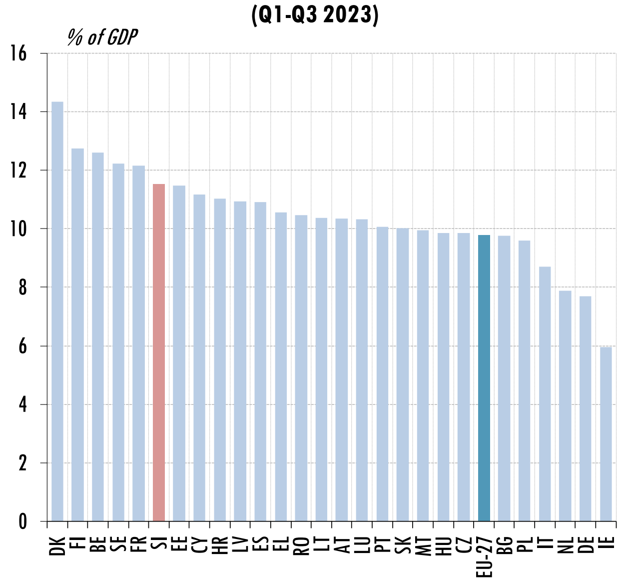
Source: OECD, FC calculations.

Figure 15: Real compensation per employee indices by sector



Source: SORS, FC calculations.

Figure 16: General government compensation of employees (Q1-Q3 2023)



Source: Eurostat.

of addressing a number of known and new challenges.[14] Any increase in the compensation of employees without a systemic adjustment of wages and other parameters of the employment relationship and, in particular, without the simultaneous adoption of measures to increase the efficiency and accessibility of public services would only increase the risks to public finances in the current situation.

Table 2: Direct impact of discretionary measures unrelated to alleviating the impact of the epidemic and the cost of living crisis

in % of GDP	entry into force	2022	2023	2024	2025
Act Amending the Personal Income Tax Act	Mar. 22, Jan. 23	-0.5	-0.6	-0.5	-0.5
Agreement on raising the salaries of doctors	Jan. 22	-0.2	-0.2	-0.2	-0.2
Scientific Research and Innovation Activity Act	Jan. 22	-0.1	-0.1	-0.1	-0.1
Extraordinary indexation of pensions – ZPIZ-2L	Jan. 22	-0.3	-0.2	-0.2	-0.2
Act Amending the Health Care and Health Insurance Act	Feb. 22	-0.1	-0.1	0.0	0.0
Students Status Act	Apr. 22	-0.1	-0.1	-0.1	-0.1
Act Determining Emergency Measures to Ensure Stability of the Healthcare System	July 22	0.0	-0.2	0.0	0.0
Agreement on measures relating to salaries and other labour costs in the public sector for 2022 and 2023	Oct. 22	-0.2	-0.7	-0.8	-0.7
Point 5 of the general agreement (health, nursery assistants, young researchers)	Dec. 22	0.0	-0.1	-0.2	-0.2
Agreement on the settlement of strike demands in healthcare and social care activities	Dec. 22	0.0	-0.1	-0.1	-0.1
Act Regulating Alternative Fuels Infrastructure and Promoting the Transition to Alternative Fuels in Transport	May 23	0.0	0.0	-0.1	0.0
Act Amending the School Meals Act	June 23	0.0	0.0	0.0	-0.1
Act Amending the Health Care and Health Insurance Act	July 23	0.0	0.0	-0.4	-0.4
Long-Term Care Act	July 23	0.0	0.0	-0.1	-0.4
Other measures[1]		-0.1	-0.4	-0.3	-0.1
TOTAL		**-1.5**	**-2.7**	**-2.8**	**-3.0**

Sources: Government of the Republic of Slovenia, DZ RS, IMAD; FC calculations. Note: the line indicates the measures taken since the adoption of the April 2023 revised budget. [1] All other discretionary measures with an impact of less than 0.1% of GDP in a given year.

[14] For an analysis of fiscal risks, see Chapter 3 and in particular Box 3.1 in the Fiscal Council's Assessment of Budget Documents for 2024 and 2025, produced in October 2023 (available at https://www.fs-rs.si/wp-content/uploads/2023/10/Assessment_Oct23.pdf).