REPUBLIC OF SLOVENIA
FISCAL COUNCIL

Assessment of the draft 2025 Annual Progress Report

April 2025

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Data available up to and including 16 April 2025 were used.

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EXECUTIVE SUMMARY

The Fiscal Council assesses that fiscal trends in 2024 have contributed to medium-term fiscal sustainability. The general government deficit in 2024 was lower than in 2023 and, in line with the Fiscal Council's expectations, significantly below the government's autumn projections. Net expenditure growth was lower than the commitments made in the Medium-Term Fiscal and Structural Plan drafted last autumn. The Fiscal Council's projections, based on the no-policy change scenario, indicate a deterioration of the fiscal position over the next three years. It would therefore be reasonable to address the various risks, including longer-term challenges, in the autumn budget documents and through the adoption of the reforms currently being prepared, in order to avoid the need for excessive fiscal adjustment in the future.

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In 2024, fiscal trends were consistent with medium-term fiscal sustainability. The general government deficit stood at -0.9% of GDP in 2024, a decrease of 1.7 percentage points of GDP compared to 2023, mainly due to the reduced scope of intervention measures. In line with the Fiscal Council's expectations, the deficit was also significantly lower than the Ministry of Finance’s projection for 2024 from last October, which had forecast a deficit of -2.9% of GDP. This large discrepancy confirms the Fiscal Council’s assessment that fiscal planning remains inadequate and insufficiently realistic, and that substantial systemic improvements are needed. Net expenditure growth was around 5%, lower than assumed in the Medium-Term Fiscal and Structural Plan.

As in autumn, the Fiscal Council’s updated projections also suggest a likely deterioration in the fiscal position over the remaining period covered by the Plan. Based on currently known measures and adopted legislation, net expenditure growth is projected to exceed the commitments – particularly in 2026 and 2027 – and will also be significantly higher than the allowed deviations, both on an annual and cumulative basis. Current estimates suggest that these deviations will mainly result from the adopted public sector wage reform. However, the projections are subject to a number of risks, including those related to macroeconomic conditions and the potential adoption of additional discretionary measures. These may include increased defence spending during the period of the escape clause, as well as compensatory measures to mitigate the structural deterioration of public finances after the expiry of the escape clause. The lower deficit in 2024, along with the resulting more favourable starting position, has created some fiscal manoeuvring space, while the government debt-to-GDP ratio in 2028 is not expected to deviate significantly from the projection in the Plan. However, it should be noted that the anticipated deterioration of the fiscal situation in the second half of the plan period may pose a challenge to maintaining medium-term fiscal sustainability.

To ensure medium-term fiscal sustainability and avoid excessive adjustment demands when preparing the next medium-term fiscal and structural plan, additional measures should already be included in the autumn budget documents. These documents should be prepared in accordance with the principle of prudence – particularly in the election year – and should avoid, as far as possible, the current practice of regularly overestimating expenditure, which contributes to inefficient spending. Projections show that the assessment of fiscal policy adequacy is highly dependent on assumptions of EU funding, which has fluctuated significantly over the years and has recently fallen well short of expectations. This item also largely determines the level of public investment, which should better reflect the cyclical position of the economy and focus on the investment structure to strengthen economic potential as sustainably as possible. Further pressures on public debt levels could arise particularly from the expected additional defence spending and a possible deterioration in macroeconomic conditions, especially as a result of further escalation of the trade war. According to the Fiscal Council, the adoption of the reforms currently under preparation could largely mitigate the risks of medium-term and long term fiscal sustainability.

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Legislation

In accordance with Article 6 of the Fiscal Rule Act (hereinafter: the ZFisP-1)[1] the Fiscal Council received a request from the Government on 10 April 2025 to assess the draft 2025 Annual Progress Report (hereinafter: the Report). The Report is a regular annual document under the new EU economic governance framework, introduced by Regulation (EU) 2024/1263 (hereinafter: the Regulation)[2] and transposed into the Slovenian legislation by the amended Fiscal Rule Act.

The content of the Report is specified in Article 21 of the Regulation.[3] The Report should include, in particular, information on the adequacy of fiscal policy over the past year in relation to the commitments outlined in the Medium-Term Fiscal and Structural Plan (hereinafter: the Plan).[4] It should also include an assessment of Member States' structural policies and the implementation of recommendations received by a Member State in the context of the European Semester.

In accordance with point 4 of paragraph two of Article 7 of the ZFisP-1, the Fiscal Council must, within seven days of receiving the Annual Progress Report, assess whether the data on the general government budget outturn presented in the Report are in line with the net expenditure path set out in the Plan.

The Report provides a more detailed presentation of the fiscal and macroeconomic trends for 2024 and 2025. In order to provide a comprehensive and forward-looking view of public finances, the Fiscal Council also includes in its assessment its own updated medium-term fiscal projections based on currently applicable policies. On the basis of these projections, the assessment of the risks to the achievement of fiscal targets over the entire period covered by the Plan (2025–2028) has also been updated.

[1] Available at: https://www.fs-rs.si/wp-content/uploads/2025/05/ZAKO9122_NPB0-lektoriran-prevod_eng_.pdf

[2] Available at: https://eur-lex.europa.eu/eli/reg/2024/1263/oj/eng

[3] A more detailed explanation and guidance on the required content can be found in the EU Guidance available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C_202403975

[4] The plans prepared to date for EU Member States, including Slovenia, are available at: https://economy-finance.ec.europa.eu/economic-and-fiscal-governance/stability-and-growth-pact/preventive-arm/national-medium-term-fiscal-structural-plans_en

1. Macroeconomic trends and projections

In 2024, GDP growth was moderate and inflation was lower than in the previous two years. Real GDP grew by 1.6%, approximately 0.5 percentage points below the long-term average. The main contributor to the relatively low economic growth was the decline in investment, particularly in the construction of buildings and infrastructure, and, for the second year in a row, in investment in machinery and equipment. This is likely also one of the key reasons for the continued decline in labour productivity growth, which fell short of the long-term average by one-third (recording 1%) across the economy as a whole and by half (1.6%) in the manufacturing sector. Household consumption increased as a result of strong real wage growth, although its nominal growth was only half that of the previous year. This was also influenced by inflation, which fell to 2% following the temporary energy shock – only a quarter of the rate seen in the previous two years. In 2024, corporate profits remained high, but growth nearly came to a standstill due to rising cost pressures, primarily driven by labour market constraints.

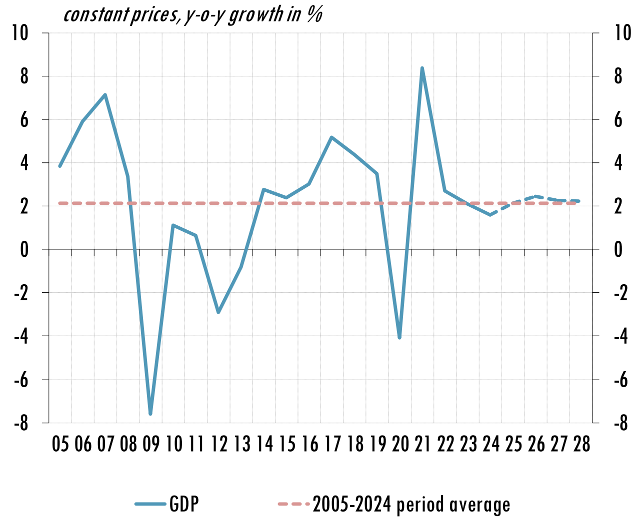
Economic activity growth in 2024 was similar to that assumed when the Plan was drawn up, but the economic outlook deteriorated in the spring of this year. At 4.7%, nominal GDP growth last year was broadly in line with the forecast. However, the spring IMAD forecast[5], compared to the autumn forecast[6] on which the Plan was based, implies a significant reduction in all major tax bases. The level of GDP over the period 2025–2028 is thus projected to be EUR 3.7 billion lower than in the autumn forecast, with the main downward contributions on the expenditure side coming from investment (EUR -5.1 billion) and on the income side from compensation of employees (EUR -3.3 billion).

The impact of the ongoing tariff war, which increases the downside risks to economic growth, was not taken into account in IMAD's spring projections. It was also estimated that 10% US tariffs and EU retaliatory measures could reduce economic growth in Slovenia by approximately 0.5 percentage points. At the time of the Report's assessment, this estimate can be considered as a realistic scenario. In addition, macroeconomic developments could be further adversely affected by uncertainty in the international environment and financial markets, which has increased significantly since the initial forecasts of much higher tariff rates.

[5] Available at: https://umar.gov.si/fileadmin/user_upload/napovedi/pomlad/pomladanska_2025/PN2025__ST.pdf (Only in Slovene)

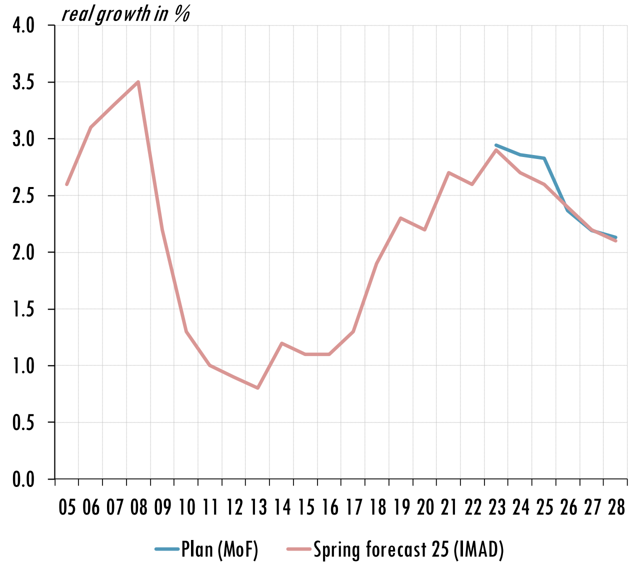
[6] Available at: https://www.umar.gov.si/fileadmin/user_upload/napovedi/jesen/2024/angleska/aJN2024_final.pdf

Figure 1.1: Gross domestic product



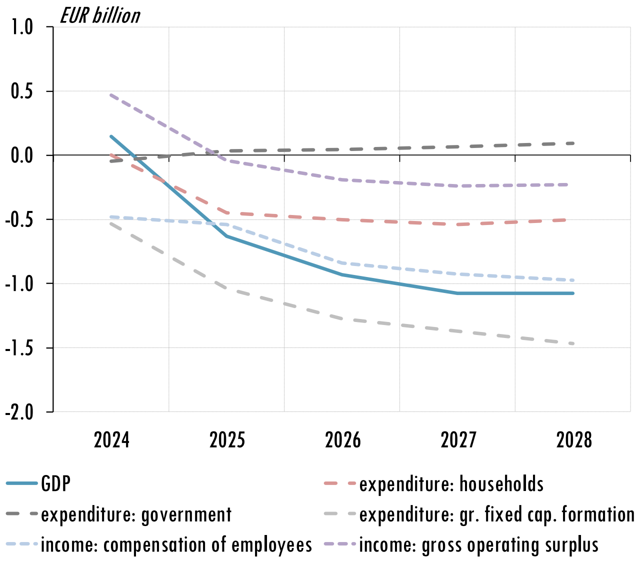
Source: SORS, IMAD, FC calculations.

Figure 1.2: Potential GDP



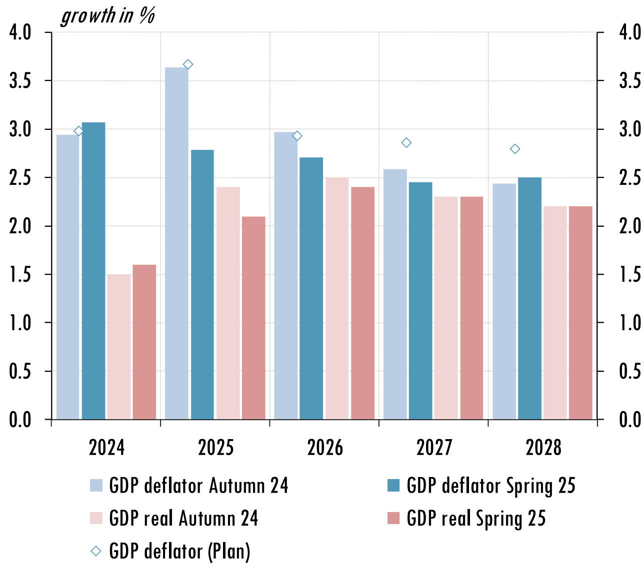
Source: MoF, IMAD, FC calculations.

Figure 1.3: Differences between tax base levels in Autumn 2024 and updated Spring 2025 forecasts



Source: IMAD, FC calculations.

Figure 1.4: IMAD forecasts and assumptions in the Plan



Source: MoF, SORS, IMAD, FC calculations.

2. Fiscal trends and projections

In 2024, the general government deficit decreased significantly, primarily due to a reduced negative impact of intervention measures. The deficit was -0.9% of GDP, a decrease of 1.7 percentage points from the previous year. The negative impact of the intervention measures was reduced by 2.3 percentage points of GDP.[7] The revenue ratio (excluding intervention measures) increased by 1.2 percentage points of GDP, mainly due to higher revenues from social contributions and income tax, reflecting the continuation of favourable labour market conditions. Discretionary measures, namely the transformation of supplementary health insurance into a compulsory contribution[8] and the non-adjustment of income tax brackets with inflation[9], also contributed to the growth of these two revenue categories. Last year, higher inflows from dividends and corporate income tax, driven by strong corporate performance, also contributed significantly to revenue growth. The expenditure ratio (excluding the intervention measures) increased by 1.8 percentage points of GDP in 2024. The main reason was the almost 20% growth in social benefits, which caused their share in GDP to increase by 1.3 percentage points. In particular, the share of pensions increased due to the largest regular adjustment to date, while the share of social benefits in kind – particularly for medicines – also rose significantly as a result of the transformation of supplementary health insurance into a compulsory contribution. The actual general government deficit was significantly lower than the Government's October 2024 projection (-2.9% of GDP) which was in line with the Fiscal Council's expectations. The general government gross debt stood at 67.0% of GDP at the end of 2024, 1.4 percentage points of GDP lower than at the end of 2023. The reduction continued to be mainly driven by inflation. The net government debt is much lower, standing at 45.6% of GDP at the end of the third quarter of last year, mainly due to the maintenance of high liquidity reserves.

This year, a smaller increase in the deficit is expected than forecast by the Ministry of Finance. In the 2026–2028 period, leading up to the end of the current Plan's validity, the deficit could increase again, averaging just under -2.0% of GPD.[10] In 2025, the deficit is expected to increase slightly, mainly due to the implementation of the public sector wage agreement. According to our projections, the increase in the deficit will be smaller than that projected by the Ministry of Finance, as investment and subsidies are expected to increase less. Over the next three years, the deficit is expected to increase again, averaging around -1.8% of GDP. The main reason for this will be the continued implementation of the wage agreement, as the share of compensation of employees is projected to increase by more than 0.5 percentage points of GDP, reaching around 12% of GDP by 2028 compared to 2024. The expected fluctuation of the deficit in the coming years will mainly be linked to the dynamics of European fund spending during the final phase of the Recovery and Resilience Plan's implementation and under the assumption that cohesion fund spending from the 2021-2027 multiannual financial framework will once again intensify in the final years of availability. It is expected that the level of domestic investment funding will remain similar to the average of recent years. In preparing the projection, it was also assumed that the newly introduced long-term care contribution would be almost fully spent, in line with the Government's estimates. Similarly, it was assumed that the funds collected in the Reconstruction Fund would be used for post-flood recovery.

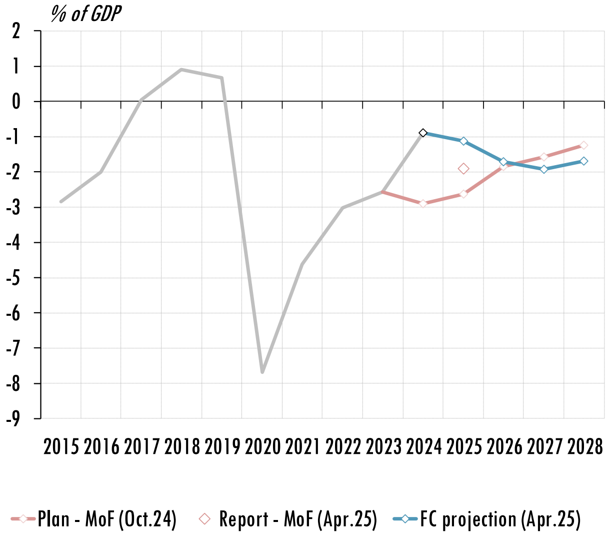
[7] The impact of measures to mitigate the effects of the epidemic was reduced by around 0.4 percentage points of GDP, the impact of measures to alleviate the cost-of-living crisis by around 1.1 percentage points of GDP and the impact of post-flood recovery measures by around 0.7 percentage points of GDP. In 2023 and 2024, post-flood recovery expenditure was financed from the state budget, and its negative impact on the balance was much smaller in 2024 than in 2023, due to the revenues of the Reconstruction Fund, which had not yet been spent.

[8] In 2024, compulsory social contribution revenue amounted to EUR 624 million.

[9] In 2024, this measure also resulted in an additional EUR 130 million in income tax revenue.

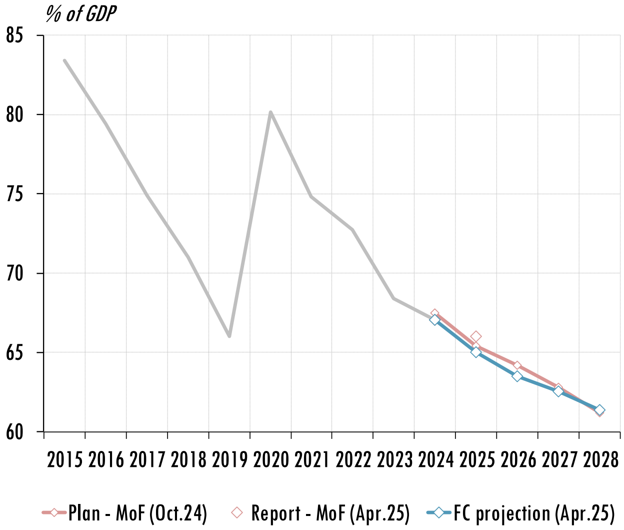
[10] The Fiscal Council's projections are based on the assumption that the current policies will remain in place, meaning they only take into account the applicable and known legislation.

Figure 2.1: General government budget balance



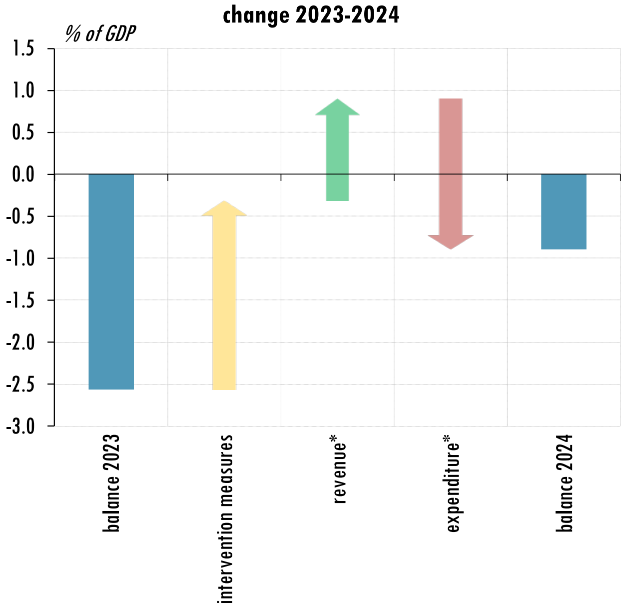
Source: SORS, IMAD, MoF, FC calculations.

Figure 2.2: General government gross debt



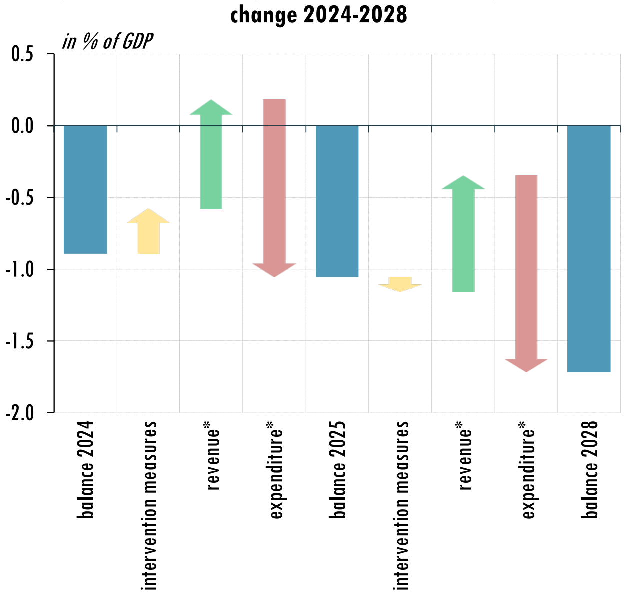
Source: SORS, IMAD, MoF, FC calculations.

Figure 2.3: Factors of general government budget balance change 2023-2024



*Source: MoF, SORS, FC calculations. Note: * excluding intervention measures.*

Figure 2.4: Factors of general government budget balance change 2024-2028



*Source: MoF, SORS, IMAD, FC. Note: * excluding intervention measures.*

Should the difficulties in recruiting long-term care staff result in lower expenditure than currently estimated by the Government, and should the implementation of the post-flood recovery projects fall behind the government's plans, the resulting deficit could be lower. Gross government debt is projected to be around 61% of GDP by the end of the Plan period in 2028, a level similar to that assumed in the Plan.

3. Achievement of the Plan objectives and associated risks

The Fiscal Council's assessment is that fiscal trends in 2024 and 2025 are, or will be, consistent with the commitments made in the Plan. The overall general government deficit is projected to be around 3.5 percentage points of GDP lower than projected in the Plan for both years. The significantly lower deficits in 2024 and 2025 also reflect slower net expenditure growth compared to the commitments outlined in the Plan. However, a significant degree of compliance was achieved in 2024, although the Fiscal Council had already warned in its autumn assessment of the Plan that it was based on unrealistic planning assumptions. While 2024 is not part of the Plan period, it represents an important starting point for fiscal policy management in the coming years. The net expenditure growth shown in the Plan for 2024 (6.2%) was in line with, rather than lagging behind, the assumed growth of nominal potential output (around 6%) at the time the Plan was prepared. According to the Fiscal Council's assessment, the lag should be around 1 percentage point. The assumed net expenditure growth should therefore be close to 5%, taking into account the average structural adjustment required over the Plan period to ensure medium-term fiscal sustainability. Consequently, the lag in net expenditure for 2024 (4.6% vs. 6.2%) is overestimated and, although partly the result of fiscal policy management, is to a much greater extent due to unrealistic planning.

The current estimates suggest a likely deterioration of the fiscal position over the rest of the period covered by the Plan. The Fiscal Council estimates that net expenditure growth will exceed the commitments outlined in the Plan, particularly in 2026 and 2027, and will also be significantly higher than the annual deviations allowed in the control account.[11] The currently adopted and known measures are projected to result in net expenditure growth during the 2026–2028 period that exceeds the Plan's commitments by approximately EUR 2 billion or 2.5 percentage points of GDP. This would more than offset the fulfilment of the net expenditure growth commitments for 2024 and 2025, which the Fiscal Council estimates at around -0.7 percentage points of GDP in total, with the majority occurring in 2024. This estimate is in line with both the Fiscal Council's estimates from the review of the Plan last autumn and the Fiscal Council's updated projections (see Chapter 2).[12]

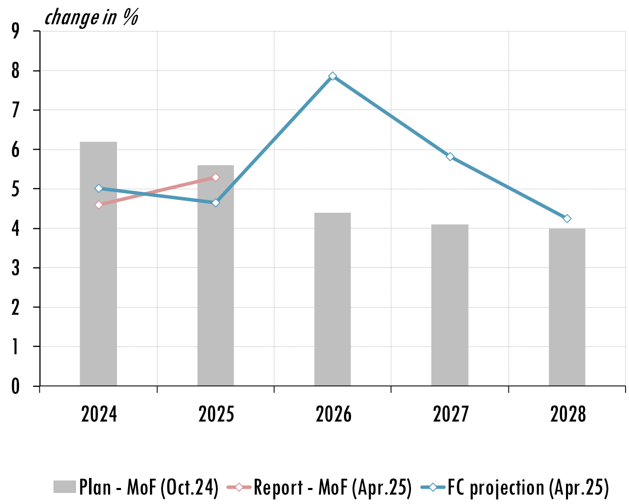
However, the anticipated deterioration in the fiscal position is not expected to jeopardise fiscal sustainability as defined by EU legislation and the ZFisP-1. The overall deviation of the deficits projected in the Plan for the 2026–2028 period compared to the Fiscal Council's updated projections may even be smaller than implied by last year's projections. This is mainly attributed to a lower deficit in 2024, providing a more favourable starting point and thereby creating some fiscal manoeuvring room. As a result, the government debt-to-GDP ratio in 2028 could be very similar to that projected in the Plan. While this implies the maintenance of fiscal sustainability, it could become more challenging in the medium term due to a deterioration in the fiscal position during the second half of the Plan.

Other pressures on public finance may also emerge in the future, which could be addressed, at least in part, by the reforms under preparation. Further pressures on the level of public debt could particularly arise from the expected additional defence spending and a possible deterioration of the macroeconomic situation, especially due to the further escalation of the trade war. The future macroeconomic situation will also be influenced to some extent by the fiscal policy stance in certain key EU Member States, which could partly offset the negative outlook for international trade and its

[11] According to Article 1 of Regulation 2024/1264 the allowed annual deviation in the control account is 0.3 percentage points of GDP or 0.6 percentage points cumulatively.

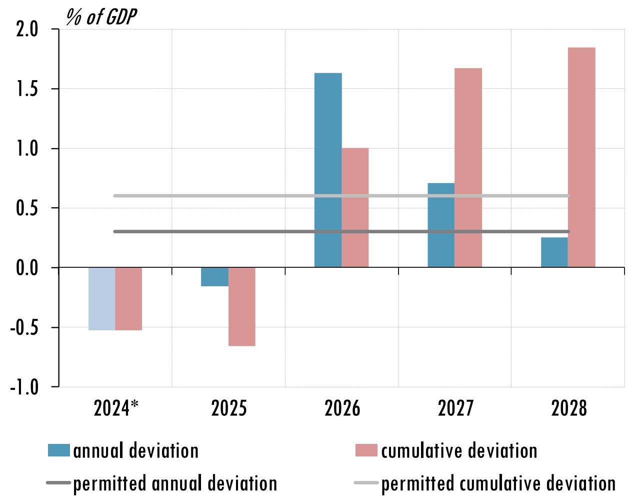
[12] According to the guidelines for the preparation of the Annual Progress Report (the document is available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C_202403975), the Government is not obliged to publish the forecast for 2026–2028. As the Report only includes fiscal projections for 2025, a comparison for the entire period is not possible.

Figure 3.1: Net nationally financed primary expenditure



Source: SORS, IMAD, MoF, FC calculations.

Figure 3.2: Net expenditure deviations in the Plan period



*Source: FC calculations. Note: * as 2024 is not part of the Plan period, the deviation in this year is not noted.*

impact on economic activity. At the same time, the adoption of certain structural measures, in particular pension reform, could help alleviate the pressure on public finances in terms of the longer-term impact on public debt sustainability.[13]

[13] The Fiscal Council's estimates, for example, suggest that in terms of the impact on medium-term debt sustainability, the adoption of the pension reform (since the official calculations of its impact are not yet available, IER's estimates from last year's baseline have been used) could largely offset the structural increase in defence spending.