Slovak economic policies in the context of EU semester

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Slovak economic policies

Main objectives:

- Economic growth
- Fiscal sustainability
- Quality of life – ultimate objective of the public policy

- Policies to address them defined in the Stability Programme and National Reform Programme
- Delivered as part of the EU semester

Country-specific Recommendations 2013

1. Consolidation continued, MTO, preserving growth enhancing expenditures, pension system, health-care sector
2. Improvement of VAT collection and tax compliance, real-estate taxation
3. Enhancing public employment services, link activation measures to social assistance, addressing long-term unemployment, child-care facilities, reduced tax-wedge for low-paid workers

Country-specific Recommendations 2013

4. Addressing youth unemployment, increasing attractiveness of teaching profession, work-based learning in companies in vocational education, job-oriented bachelor programmes, pre-school education for marginalised communities
5. Transparent tariff-setting mechanism, interconnection with neighbouring countries, improving energy efficiency
6. Human resources in public administration, analytical capacities, improving absorption of EU funds, efficiency of judicial system, promote alternative dispute resolution procedures

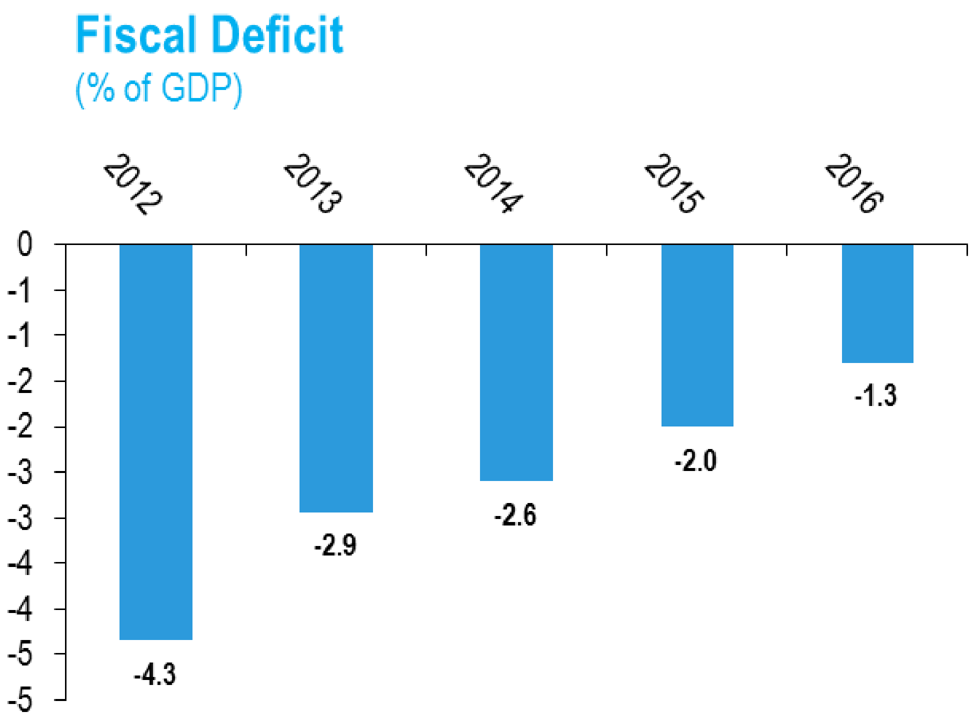
CSR: What's new in 2013

- Efficiency of health care
- Better functioning of energy markets and their regulation
- Human resources in public administration
- Absorption of EU funds

Positive highlights (not) in CSR – MoF view

- Consolidation of public finance
- Fiscal Responsibility Act
- Pension reform
- Tax collection

Headline fiscal deficit targets



- The latest **fiscal deficit estimate** for 2012 is 4.3% of GDP, lower than the target of 4.6%
- The latest estimate for 2013 is **in line with the deficit target** of 2.9% of GDP
- Deficit targets for 2014 to 2016 reflect two constraints:
  1) **EU rules (SGP)** - structural deficit reduction by 0.5% of GDP as a benchmark
  2) **National rules** - upper debt limit of 57% of GDP
- Meeting the **MTO** (structural deficit of 0.5 % of GDP) in 2018

EU constraints

Consolidation effort (% GDP, ESA95)	2012 E	2013 E	2014 B	2015 B	2016 B
1. GG balance	**-4.3**	**-2.9**	**-2.6**	**-2.0**	**-1.3**
2. Cyclical component	0.0	-0.5	-0.5	-0.4	-0.2
3. One-off effects	0.1	0.8	0.4	0.0	0.0
- levy from business in regulated sectors	0.0	0.1	-	-	-
- opt-out from fully-funded pension scheme	0.1	0.3	-	-	-
- mobile spectrum auction (digital dividend)	-	0.2	-	-	-
- reselling emergency oil reserves to private sector	-	0.2	0.4	-	-
4. Structural balance (1-2-3)	**-4.5**	**-3.3**	**-2.5**	**-1.6**	**-1.1**
Consolidation effort (y-o-y change of structural balance)	-	**1.2**	**0.8**	**0.9**	**0.5**
p.m. GG balance (consolidation effort of 0.5% GDP)	*-4.3*	*-2.9*	*-2.9*	*-2.7*	*-2.0*

- Using the common EC methodology for calculating the structural budget balance, the **consolidation effort is 1.2% of GDP in 2013**
- **Above the benchmark consolidation effort of 0.5% of GDP** throughout the forecasting period
- Sticking to the benchmark would yield less strict targets for 2014-2016, while **the debt level would rise above 57% of GDP in 2015** (severe constrains from national rules)

Better budgetary development in 2012

- **The general government deficit for 2012 is 4.35% of GDP, compared to budgeted 4.64% of GDP**

Budget balance in 2012 (ESA 95)		
	EUR mill.	% GDP
1. General government budget balance - budget	**-3 324**	**-4.64**
Tax and SSC shortfall	-392	-0.55
Shortfall in one-off non-tax revenues (licences, digital dividend)	-64	-0,09
Savings in confinancing	221	0,31
Savings in operational programme infrastructure	120	0,17
Transfer to EU budget	24	0,03
Non-tax revenues of local governments	190	0,27
Expenditures of local governments	51	0,07
Savings in health care insurance companies	138	0,19
Liabilities of health insurance companies	-76	-0,11
Assumption of health care providers debt	-80	-0,11
Savings in Social insurance agency expenditures	69	0,10
Other changes	16	0,02
2. General government budget balance	**-3 107**	**-4.35**

Note: (+) indicated improvement and (-) deterioration of the general government balance

Source: MinFin SR

- Major **negative** development:

1. Shortfall in taxes (VAT, CIT)
2. Hospital debts assumptions, liabilities of health insurance companies
3. Shortfall of one-off revenues

- **Positive** development:

1. Savings on co-financing and investments related to EU infrastructure projects
2. Lower health care expenditures and Social security agency savings
3. Consolidation measures of local governments

Consolidation measures in 2013

- **Measures include:**

1. Increasing and unifying maximum assessment bases of social security contributions
2. Increase in social security contributions for self-employed and other related changes
3. Health and social insurance contributions for casual temporary agreement workers
4. Changes in income tax rates
5. Reduced expenditures of municipalities and self-governing regions
6. New financing system of strategic oil reserves
7. Savings of municipalities

- **The updated general government deficit for 2013 remains 2.94% of GDP**
- **Risks for 2013 still remain – worsening of the macroeconomic environment and budgetary developments of municipalities**

2014-2016

Comparison of no policy change scenario with deficit target values (ESA95, in % of GDP)			
	2014	2015	2016
1. General government balance - current target	**-2.6**	**2.0**	**1.3**
2. Primary general government balance – current target	-0.7	0.0	0.8
3. Primary general government balance – GG budget framework 2014 – 2016 (known measures)	-1.4	-1.2	-0.3
4. Primary general government balance – no policy change scenario	-1.7	-1.7	-1.0
5. General government balance - no policy change scenario	**-3.6**	**-3.6**	**-3.1**
Difference with budget framework 2014 - 2016 (3-2) – undefined cummulative measures to reach target	**0.7**	**1.2**	**1.1**
Difference - additional measures (in EUR mill.)	**566**	**969**	**947**

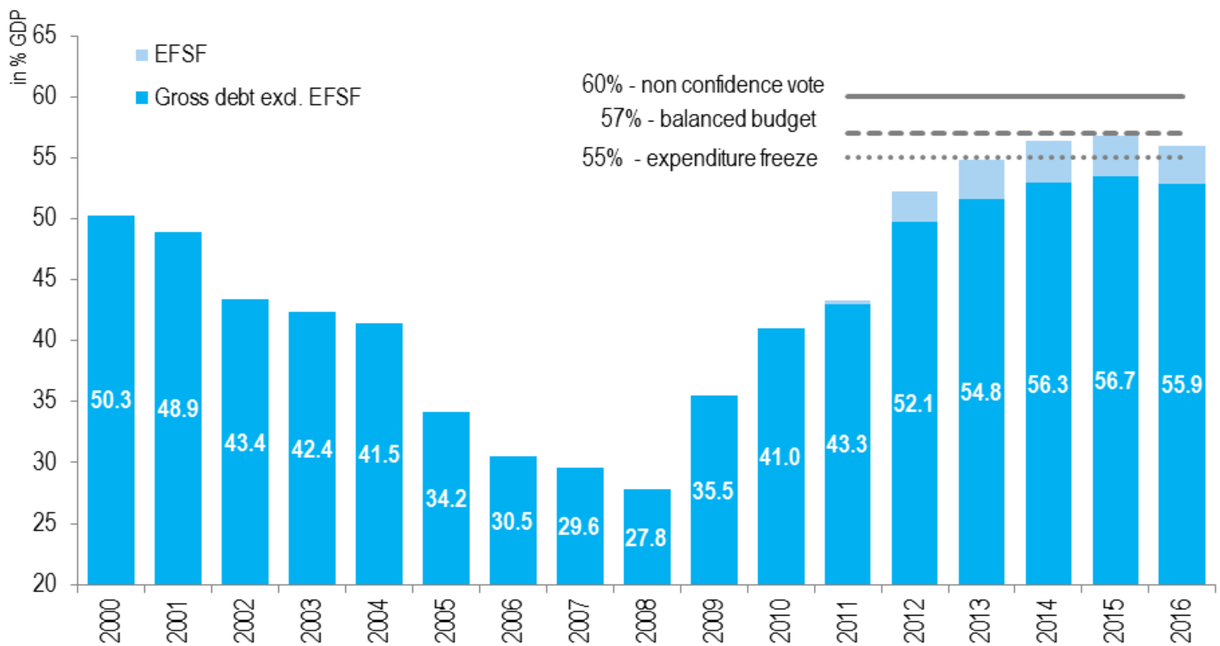
- Based on the no-policy-scenario, the **budget balance would reach -3.6% of GDP in 2014** with a decreasing trend in 2016
- **Measures already incorporated in** Budgetary Framework 2014 – 2016 include **savings on wages**, **lower subsidies and transfers** and **changes in capital expenditures of local governments.** On the revenue side the main changes stem from **higher digital dividend** revenues and **revenues from reselling oil reserves**
- Additional cumulative measures will have to be specified ranging **from 566 Eur mill. in 2014 to 947 Eur mill. 2016 →** to be specified in the draft budget

Fiscal Responsibility Act

1. Establishment of a Fiscal Responsibility Council
2. Rules of fiscal responsibility
3. Rules of fiscal transparency

National debt brake rules

- **Constitutional act on fiscal responsibility** includes sanctions based on the gross debt level - constraints for fiscal policy
- **Exceeding the 57% of GDP** debt level in 2015 – **requirement of a balanced budget** in 2017
- **Higher consolidation effort** (than implied by EU rules) **needed both in 2014 and 2015**
- Gross debt forecast (under current fiscal targets):



Pension system reform – first pillar

- As of 2017, the **retirement age** is going to be automatically adjusted according to change in the life expectancy
- **Indexation mechanism** will be gradually changing from Swiss indexation to inflation indexation (based on pensioners' consumption basket) in 2018.
- The **average pension point value** adjustment is revised in order to **increase the solidarity**.
- As of 2013, the **maximum assessment base** for pension contributions was increased **from 4 to 5 times the average wage** in economy – impact on revenue only (no additional pension rights)

Pension system reform – second pillar

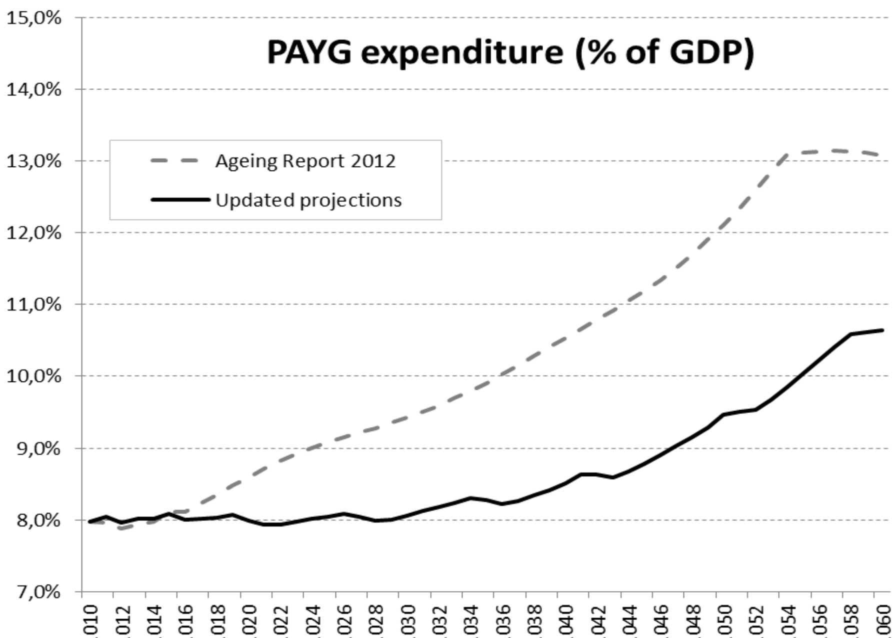
- Became **voluntary for newcomers to the labour market** with the possibility to decide until the age of 35.
- As of September 2012, **contributions to the second pillar** have been decreased **from 9 to 6 percent** (final level of 6 percent reached in 2024)
- **Minimum participation period in the second pillar changed from 15 to 10** years

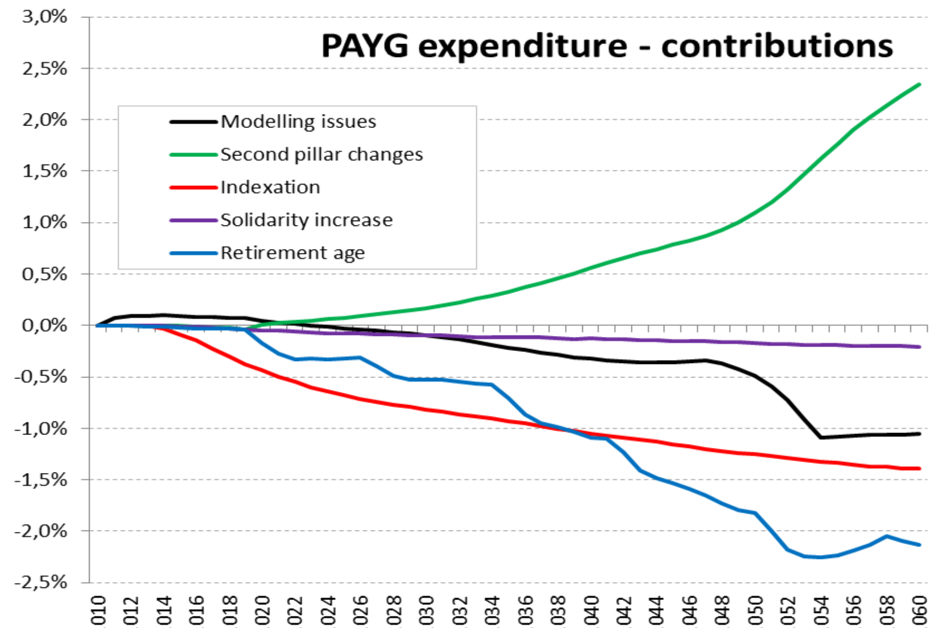
OVERALL

- Decreasing pressure on **pension expenditures by 2.6% GDP**, whereas revenues should be higher by 1.6% of GDP in 2060 (compared to NPC).
- The balance of the pension scheme should improve the S2 indicator by 2.6% of GDP.

Pension reform - results

- Strongest **positive effect** on PAYGO expenditure **parametric changes** - mainly retirement age and indexation
- Changes in the second pillar **increases** PAYGO expenditure – especially after 2050 (voluntary entry)





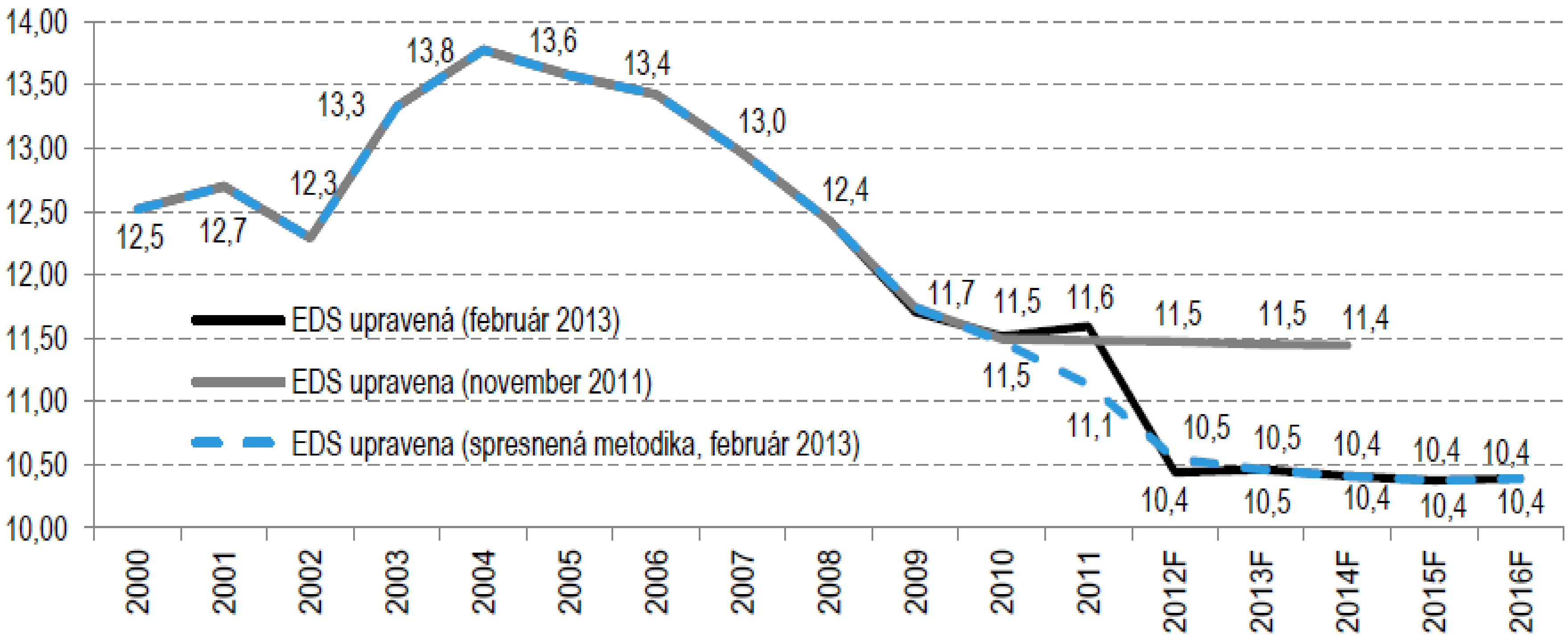
Tax collection

- **Action plan to fight tax fraud intrduced in 2012 has three phases**
- **First is implemented, second on-going**

1. Special unit to enforce tax collection (Daňová kobra)
2. Cancellation of registrations for VAT purposes of non-compliant persons
3. Introduction of joint and equal tax guarantees
4. Deposition of a financial guarantee upon their registration for high-risk persons
5. Mandatory electronic payments above 5 000 eur

Tax collection

- Effective VAT rate decreasing for a decade
- Unprecedent development



Other reforms of 2012

- **Expenditure priorities** – prioritization of expenditures promoting the economic growth – transport infrastructure, R&D, and education

- **Active Labour Market Policies** – simplification of the system of ALMP measures with emphasis on improvement in targeting and support of the employment; the acquired spare administrative capacities will be used to increase individual job counselling

- **Support of job creation for youth** – reallocation of the European funding to support new job positions creation in the private sector for young people, particularly in the regions with the highest unemployment rates.

- **Tertiary education reform** – accreditation reform, changes in duration and assessment criteria for part time studies, more stringent criteria to obtain professor and assistant professor academic titles

- **Analytical capacities** - setting up analytical units within the key ministries (partially accomplished)

Plan of reform measures for 2013 - 2015

- Additional consolidation measures
- Real estate tax – based on market value
- Additional tax-evasion reduction measures
- Institutional reform of the state administration
- Educational reform
- Healthcare reform
- Development and modernisation of transport infrastructure

Thank you for your attention