1 Introduction

The Ministry of Finance is presenting the first issue of a new publication addressing macroeconomic development in the Czech Republic. Until now, this role has been filled only by the traditional Macroeconomic Forecast, the content of which covered all the essential areas of macroeconomic development. In contrast, the Fiscal Outlook is directed to only a single sector of the national economy, that of general government.

The Fiscal Outlook ought to fill a certain gap in the Ministry of Finance’s range of publications. That portfolio includes a wide spectrum of information, starting from the approved state budget and its fulfilment to macroeconomic analyses and forecasts, but it has given only marginal attention to the general government sector. One of the new publication’s ambitions is to clarify and analyse relationships between the budget variables, general government finances and overall macroeconomic development.

This effort aims further to strengthen the transparency and comprehensibility of developments in public finances and fiscal policy. Toward that end, the text sheds light on the meanings of many indicators and interprets data on public finances. At the same time, we are presenting an outlook for general government finances that is consistent with the government’s current objectives. This general government outlook is neither an economic-political document (as is, for example, the Convergence Programme) whose main target would be to present the government’s objectives in the field of budgetary policy nor an autonomous macroeconomic forecast. The purpose is to project the governmental objectives onto the development of the main fiscal indicators. In principle, then, the Fiscal Outlook is consistent with the government’s targets. The benefit of the projection should consist in analysis of measures that lead to the respective targets, and perhaps to draw attention to the risks that may endanger achieving those targets.

The document has the following structure: The first part brings together the basic points of departure, the macroeconomic framework and main fiscal policy objectives. The second part deals with the current development of public finances. First, the public budgets’ balances are presented based on the cash flows used in the budgetary process, then the general government balance is presented using the national accounts accrual methodology. The third part presents the medium-term fiscal outlook – the budgetary outlook as an operating tool for executing fiscal policy and the subsequently derived outlook for the entire general government sector, accompanied by the long-term projection. A substantial part of the publication should be the chapter focusing on a selected topic and containing analyses of current problems of public finances and presenting results of the Ministry of Finance’s analytical and research activities. This part should satisfy the more demanding readers with expert contributions to the discussion of public finances and fiscal policy. The first topic is devoted to the description and evaluation of fiscal rules used in the Czech Republic and within the European Union. The final part contains an annex of tables.

To a certain extent, this first edition is atypical due to its numerous explanatory notes and boxes. We believe that these can help readers to orientate better in the large amount of data about public finances and to facilitate understanding of the information provided.

The Fiscal Outlook will be published every six months, following the compilation of a new medium-term state budget outlook (April and September) and after publishing the statistical data for the general government sector (April and October). We hope the new publication will attract both professionals and the nonspecialist public. We welcome any comments or suggestions that will help us to increase the quality of the publication and bring it closer to the readers' needs.

1.1 Macroeconomic development

The Czech Republic finds itself today in a favourable macroeconomic situation. Gross domestic product in constant prices grew in 2005 and 2006 at rates exceeding 6%. The Czech economy's output is running above the level of its potential. In the outlook's time horizon we expect that this positive output gap will gradually diminish, and therefore the real GDP will come closer to its potential. The expected GDP growth at the outlook's horizon is around 5%.

Real GDP growth is driven mainly by final consumption expenditure, which is likely to be crucial also in the coming years. In addition to the gross fixed capital formation, which will continue to contribute to growth, it is worthwhile noting the growth of private consumption spending. For 2007, we expect this to be around 5.4%, and we look for a temporary slowdown in 2008 due to an increase in indirect taxes and reduction in social transfers. From 2008, government consumption expenditure should decrease by ca 0.5% year on year. When the terms of trade come into positive values, growth of the implicit GDP deflator will increase and growth of nominal GDP should be around 8%.

Since 2005, the trade balance has been in positive numbers (i.e. the Czech Republic's exports exceed its imports). Due to pro-export oriented investments, we expect that foreign trade will gradually increase its contribution to GDP growth up to 1.5 percentage points in the forecast's time horizon.

In past years, consumer inflation hovered steadily beneath the CNB's inflation target. In 2007, we expect only moderate growth of about 2.1% in consumer prices. For 2008, the outlook anticipates a one-time jump in inflation due to the planned increase in indirect taxes and to be followed by a slowdown to 2%.

As a consequence of the continuing economic growth, the unemployment rate is declining, and, in the coming years, we anticipate that it will gradually decrease to 6%. In addition to the cyclical effects, the labour market should reflect the structural changes that will be determined by the anticipated reform of public finances and subsequent changes in the payments of social benefits.

Table 1-1: Main macroeconomic indicators

		2003	2004	2005	2006	2007	2008	2009	2010
						Forecast	*Forecast*	*Outlook*	*Outlook*
Gross domestic product	*(CZK bn, curr.p.)*	2 577	2 781	2 970	3 204	3 462	3 734	4 020	4 333
Gross domestic product	*(growth in %, const.p.)*	3.6	4.2	6.1	6.1	5.3	4.9	5.1	5.3
Private consumption	*(growth in %, const.p.)*	6.0	2.6	2.8	4.6	5.4	3.8	4.6	4.2
Government consumption	*(growth in %, const.p.)*	7.1	-3.2	1.0	0.3	0.3	-0.5	-0.5	-0.5
Gross fixed capital formation	*(growth in %, const.p.)*	0.4	4.7	1.3	7.3	8.2	9.0	7.8	7.2
Contr. of net exports to GDP growth	*(p.p., const.p.)*	-0.6	1.4	4.0	0.5	0.1	0.2	0.9	1.5
GDP deflator	*(growth in %)*	0.9	3.5	0.7	1.7	2.7	2.8	2.5	2.4
Inflation	*(in %)*	0.1	2.8	1.9	2.5	2.1	3.2	1.9	2.0
Employment (LFS)	*(growth in %)*	-0.7	-0.6	1.2	1.3	1.1	1.0	0.6	0.2
Unemployment rate (reg.)	*(average in %)*	.	9.2	9.0	8.1	7.1	6.7	6.4	6.2
Wages and salaries	*(growth in %, curr.p.)*	6.0	6.4	6.6	7.5	7.5	7.1	7.1	7.0
Current account to GDP ratio	*(in %)*	-6.2	-6.0	-2.6	-4.2	-3.5	-2.4	-1.8	-1.2

1.2 Fiscal policy objectives

Public finances in the Czech Republic show deficits that are not sustainable in the long term. The space for executing active fiscal policy, as well as for the functioning of automatic fiscal stabilisers, is considerably limited in such circumstances. As it is necessary to reach long-term sustainability, the fiscal policy is determined especially by the effort to reduce the government deficit. Fiscal policy's stabilisation function is to a large extent stifled. The expected fiscal outlook is based on the objectives of the fiscal policy and on measures in the field of public finances, as these were presented in the government's program declaration and described in details in the published conception for public finances reform during 2007–2010. Both the Macroeconomic Forecast and the Fiscal Outlook of the Ministry of Finance are based on the assumption that it will be possible successfully to push through and implement the proposed reform measures. In particular, this includes the following steps:

1. Adherence to the fiscal targets consisting in the share of the public budgets balance under the fiscal targeting methodology in the gross domestic product at -3.0% in 2008, -2.6% in 2009 and -2.3% in 2010.
2. Implementation of tax reform. The reform will have only minimal impact in 2008 on the amount of tax revenues (in accrual terms). In 2009, tax changes will bring tax collections that are CZK 16.5 bn lower in comparison to the no policy change scenario, and in 2010 revenues will be lower by CZK 27.4 bn (see Table 3-6). The reform anticipates, among other things
    - increase in the reduced value-added tax rate from 5% to 9%,
    - implementation of personal income tax at a flat rate of 15% and broadening of the current tax basis by the social security and health insurance paid by the employer and employee,
    - implementation of an upper limit for the assessment basis for social security and health insurance at quadruple the average wage,
    - reduction in the corporate income tax rate to 22% in 2008, 20% in 2009 and 19% in 2010, while broadening the assessment basis.
3. Savings in the social transfers area that will contribute to deficit reduction by CZK 26.2 bn in 2008, then by CZK 30.8 bn in 2009 and CZK 31.6 bn in 2010 (see Table 3-9).
4. Other savings on the expenditures side which will ensure achieving the fiscal targets.

The fiscal policy will be restrictive in 2008–2010 in view of the economic cycle's phase and fiscal impulse. The rather ambitious deficit reduction in 2008 by 0.8 percentage points will bring a negative fiscal impulse. In the medium-term horizon, we expect that the reform's positive impacts on the potential growth will be seen. These impacts include a reduced tax burden on work and business, simplification of administrative encumbrances, and increased motivation for economic activity.

Table 1-2: Fiscal policy stance (ESA 95, % of GDP)

	2006 *Preliminary*	2007 *Forecast*	2008 *Outlook*	2009 *Outlook*	2010 *Outlook*
General government balance	-2.9	-4.0	-3.2	-2.9	-2.5
Cyclical component	0.2	0.2	0.1	0.0	0.0
Cyclically adjusted balance	-3.1	-4.2	-3.3	-2.9	-2.5
Fiscal effort	-0.3	-1.1	0.9	0.3	0.5

Note: Fiscal effort is defined as year-on-year change of the cyclically adjusted balance.

2 Development of public finances

2.1 Public budgets – cash flows

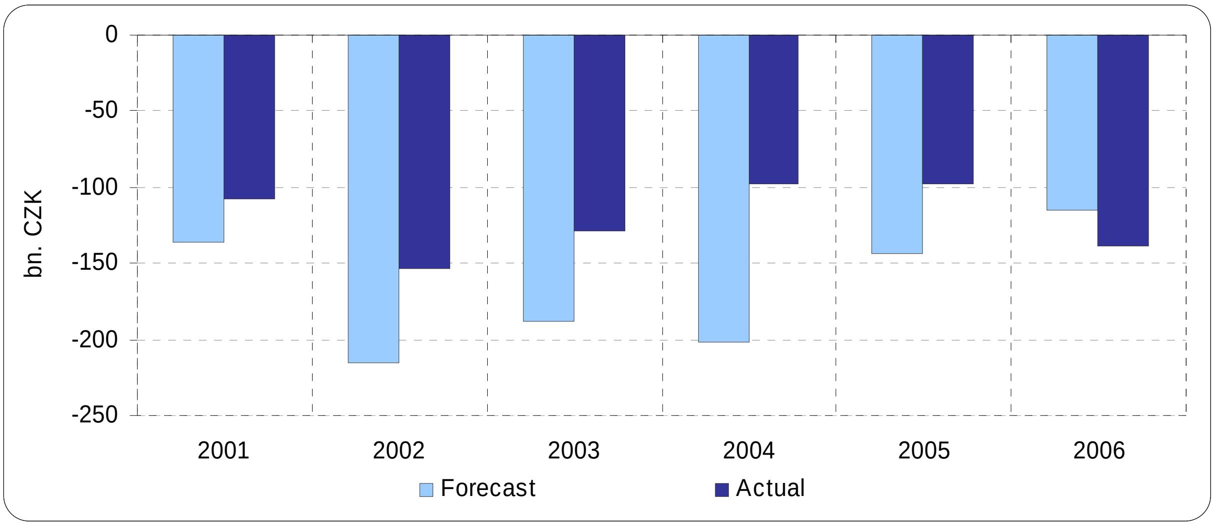
Public budgets in 2006

The **balance of public budgets** net of financial operations came to CZK -139.1 bn, which is -4.3% of GDP. Compared to the original expectations[1], the actual deficit was higher by CZK 12.2 bn while in previous years it was the other way round. In previous years, the results always had been significantly better than the original expectations. The deficit for fiscal targeting amounted to CZK 102.2 bn (i.e. 3.2% of GDP) and was lower by 0.6 percentage points than the established fiscal target (for more, see section 3.2).

The total deficit differs from the original objective due to changes on both the revenue and the expenditure sides of public budgets. Compared to the original expectations, the total revenues were lower by CZK 18.9 bn and expenditures by CZK 6.7 bn.

The following graph shows a comparison of the expected and the actually achieved results for public budgets balances in 2001 to 2006.

Graph 2-1: Anticipated and actual balances in 2001-2006[1]



Total tax revenues of public budgets (including social security and health insurance) amounted to 88.7% of total revenues of public budgets and were underfulfilled by CZK 1.7 bn. From the actual total tax revenues collected, 71.1% went to the state budget, 26.3% to the municipal government budgets and 2.6% to the budget of the State Fund of Transport Infrastructure and State Environmental Fund. The biggest negative deviation from the original expectations occurred in the individual income tax (CZK -8 bn) and excise taxes (CZK -6.7 bn). On the contrary, the collection of the social security and health insurance contributions developed very well, constituting 40.2% of the total tax revenues.

[1] Data are always compared with the budget documents of the previous year.

This amount was higher by CZK 7.9 bn against the original expectation, which was due mainly to growth in state payments for state insurees for health insurance as well as by the favourable economic development (decline in unemployment, rise in wages and salaries, increase in the minimum wage). Furthermore, the volume of EU subsidies received was CZK 25 bn lower than expected. Non-fulfilment of these revenues was partially compensated by exceeding the budget in certain other revenues.

Actual expenditures did not meet the original expectations for either current or capital expenditures. Among the current expenditures, the lower items were especially other non-investment purchases and related expenditures, while, for example, expenditures on transfers to the public, including non-profit organisations, were significantly exceeded, particularly due to legislative changes in the social area. Likewise, the subsidies to financial institutions rose significantly in comparison to expectations (see State Budget below in this text). Non-fulfilment of the capital expenditures is connected to a large extent with the expected implementation of projects co-financed by EU funds.

The state budget deficit (see Box 1) was CZK 23.1 bn higher than expected, amounting to CZK 135.1 bn. This again reflected changes on both the revenues and especially the expenditures side.

State budget revenues missed the originally expected amount by CZK 31.4 bn. One of the reasons was that the total tax revenues (including social security and health insurance contributions) were underfulfilled by CZK 7.6 bn. That was especially apparent for excise taxes and VAT, while the approved budget for corporate income taxes was slightly exceeded. Furthermore, subsidies from international institutions were drawn in a lower volume than was expected. Lower collection of these revenues was partially compensated by higher collection of non-tax revenues.

Actual expenditures of the state budget were CZK 8.3 bn higher than expected. The expected amounts were not reached, for example, for other non-investment expenditures (by CZK 13.4 bn) and capital expenditures (by CZK 8.3 bn). This was caused mainly by transfers into reserve funds in the amount of CZK 45.9 bn. These expenditure savings were largely balanced by, among other things, an increase in spending due to new legislation in the social area (for example, increase in expenditures for pensions by CZK 9.3 bn). Moreover, the originally not budgeted state guarantee in favour of CNB for losses incurred in relation with consolidating the banking sector (CZK 14.0 bn) was settled, as well as the obligation of the Ministry of Finance to CNB resulting from the receivable from the National Bank of Slovakia (CZK 1.2 bn). At the same time, the loss of the Czech Consolidation Agency to be settled was increased from the originally budgeted amount of CZK 10 bn to CZK 20 bn.

Although all other subjects achieved better results than were expected, they did not manage to eliminate the state budget’s deviation from the original expectation, thus affecting the total deficit of public budgets.

The high public budgets deficit was also reflected in their growing **debt**, which rose to CZK 877.7 bn by the end of 2006 and came to 27.4% of GDP. This growth was predominantly caused by the state budget deficit. The growth of public budgets indebtedness leads to an increase in the costs of debt service – with all the negative consequences related to the so-called snowball effect. Higher debt service means, ceteris paribus, less funds available for other public spending.

Public budgets in 2007

Neither will 2007 bring significant changes in the development of public budget finances. The expected deficit should amount to CZK 150.4 bn (i.e. 4.3% of GDP). After improving estimation of the total deficit, it will worsen by CZK 4.4 bn compared to the expectations approved in the budget documentation for 2007. The balance for fiscal targeting will come to CZK -141.9 bn, or -4.1% of GDP (for more, see section 3.2).

Deficits are expected for municipal governments and extra-budgetary funds. Nevertheless, the main factor in the public budgets deficits remains the state budget. An insufficiency of their own revenues for certain state funds (in particular, the State Fund of Transport Infrastructure and State Fund of Housing Development) in relation to the set spending programmes will be the main cause for their expected deficit balances. The exhaustion of funds from previous years (in particular, subsidies from the Privatisation Fund) may endanger the activities of these funds in upcoming years. Although the health insurance companies expect operating surpluses, the health insurance system is not balanced and is unable to maintain long-term stability using its own sources.

The prevailing part of public budgets deficits will be financed by debt instruments, which will amount to CZK 978.5 bn by the end of 2007 (i.e. 28.3% of GDP). The greatest weight in the debt of public budgets will be borne be the state budget (90.9%), followed by municipal governments and state funds (State Agricultural Intervention Fund and State Environmental Fund), which already have been forced to finance their negative balances using debt instruments.

Box 1: Cash flow methodology

The cash flow methodology records revenues and expenditures at the time when individual subjects of public budgets realise the related cash flows. It is used especially in the budgetary documents, and it is directly linked to the state budget, budgets of state funds and other subjects of public budgets that are in the approval process.

The cash principle records revenues and expenditures on the basis of payments made, not on the basis of the origination of a receivable or a payable. The main analytical elements are revenue/expenditure, deficit/surplus and financing (including loans provided and their respective repayment instalments).

Deficit/surplus of public budgets is the difference between the revenues and expenditures and shows the financing need/ability. In this section, the deficit of public budgets is shown without the influence of financial operations, thus representing the balance of revenues and expenditures less privatisation revenues and other *financial operations.*

The **deficit for fiscal targeting** is the public budgets deficit (without the influence of *financial operations*) net of subsidies for transformation institutions and other costs of transformation processes.

Financing is identical with the deficit and represents changes in received governmental loans and bonds, changes in cash, active liquidity management operations, including the change in receivables resulting from the provided loans and the respective instalments. It is used to evaluate the budgetary policy with focus on its impacts and effects on the financial markets and their stability.

Financial operations mean transactions that create or extinguish a financial receivable and therefore are not primary expenditures, as well as the impacts of operations related to reserve funds. These are only changes within financial assets, and include, for example, repayable financial assistance provided, purchase and sale of state ownership interests (stock), i.e. operations where one financial asset (e.g. money) is exchanged for another financial asset (e.g. an account receivable). Similarly, payment for an exercised guarantee represents the creation of a receivable of the state from the entity that has been issued the guarantee. In case that the exercised guarantee is not returnable, it is classified as a capital spending transfer.

Debt in the presented concept represents the volume of debt instruments (foreign loans, bank loans, state bonds and bonds issued by municipal governments).

State debt, defined in Act No. 218/2000 Coll., on budgetary rules, consists of the sum of financial liabilities. State financial liabilities are obligations arisen from the foreign loans and bank loans received by the state, as well as from state bonds issued, and other state obligations. It does not include any obligations of extra-budgetary funds, health insurance and municipalities systems, state guarantees or any other conditional obligations of the general government sector.

Institutional coverage of public budgets

State budget*, including the National Fund and Privatisation Fund (formerly National Property Fund), settlement of losses of the Czech Consolidation Agency according to the bond programme, less the net influence of transfers into reserve funds.*

***Extra-budgetary funds** – state funds, Land Fund of the Czech Republic.*

***Public health insurance** – General Health Insurance Company (VZP), occupational health insurance companies.*

***Municipal governments** – local and regional governments, voluntary associations of local governments, regional committees of cohesion regions.*

The term "public budgets" used in this publication has, as to its institutional coverage, a narrower meaning than the general government sector. **Compared to the institutional coverage of the general government sector,** public budgets **do not include:** Czech Consolidation Agency and its subsidiary companies, Czech Collection Company, Supporting and Guarantee Agricultural and Forestry Fund, Viticultural Fund, public universities, Railway Infrastructure Administration, PPP Centre, public research institutions and a part of semi-budgetary organisations classified in the governmental sector. These subjects are included in the public budgets only by transfers between these subjects and the respective components of public budgets.

2.2 General government – national accounts (ESA 95)

General government finances came to a deficit of CZK 94 bn as of the end of 2006, which represents 2.9% of GDP. As traditionally, the majority share in deficit belonged to the central government subsector, which brought its finances for 2006 to a deficit of CZK 99.7 bn (i.e. 3.1% of GDP).

In 2007, the deficit of the general government sector is expected to grow to CZK 138.1 bn, which represents 4.0% GDP. The deficit in the central government subsector is expected to rise to CZK 142.7 bn (4.1% of GDP).

General government revenues

Revenues of the general government sector in 2006 reached CZK 1 267.1 bn (i.e. 39.5% of GDP). Relative to 2005, they grew by 5.5% and, in comparison with the previous four years, the increase in revenues can be regarded as slower. This development was particularly caused by changes in the tax legislation. This influence is most apparent in income tax revenues, which grew only moderately in 2005 and 2006 after a period of quite high gains. The slower revenues dynamics in 2006 were also caused by the taxes on production and imports, especially due to the value added tax, which marked a moderate decline year on year (particularly influenced by reclassification of certain items that are subject to the tax at the reduced rate). Therefore, the growth of these taxes was one of the lowest in recent years. On the other hand, these taxes had shown a record-breaking growth in 2004. The main reasons for this development were the legislative changes adopted as a result of harmonising tax laws with the EU law, which were most evident in the VAT development and partially that of excise taxes. By contrast, social contributions show a quite stable growth rate over time, as no significant legislative changes were made in this area.

As can be seen from Table 2-1, total revenues of the general government sector show a moderate decrease as a percentage of GDP in a recent period of high economic growth. Such development is mainly attributable to tax revenues, which fell by 1.7 percentage points since 2004 and reached 19.8% of GDP in 2006. They are expected to decline again in 2007. This indicator, along with the social contributions, comprises the so-called tax quota which, since 2004, fell by 1.8 percentage points to 34.8% of GDP in 2006. In 2007, a further significant decline of 1.0 percentage point is expected. The fall of the tax quota is mostly caused by the income tax, but also by VAT and the quite high dynamics of GDP growth. Although the denominator of the tax quota is growing, GDP's increasing dynamics have positively impact on the tax revenues (in contrast to expenditures). Due to an elasticity of total tax revenues relative to GDP that is lower than 1, the autonomous decrease of the tax quota is reflected, as are the active measures taken to reduce taxes.

Table 2-1: Structure of general government revenue

		2002	2003	2004	2005	2006	2007
General government revenue	*(in % GDP)*	39.5	40.7	41.5	40.4	39.5	38.1
-tax revenue	*(in % GDP)*	19.9	20.7	21.5	20.9	19.8	19.3
-social contributions	*(in % GDP)*	14.9	15.1	15.1	15.1	15.0	14.5
-sales	*(in % GDP)*	2.7	2.9	2.7	2.6	2.5	2.4
-other revenues	*(in % GDP)*	2.0	2.0	2.2	1.9	2.2	1.9

Table 2-2: Tax revenue and social contributions

		2002	2003	2004	2005	2006	2007
Social contributions and tax revenue	*(in % GDP)*	34.8	35.8	36.6	36.0	34.8	33.8
-individual income tax	*(in % GDP)*	4.7	4.9	4.8	4.6	4.3	4.2
-corporate income tax	*(in % GDP)*	4.3	4.6	4.7	4.5	4.3	4.3
-VAT	*(in % GDP)*	6.3	6.4	7.3	7.1	6.5	6.2
-excise taxes	*(in % GDP)*	3.2	3.4	3.6	3.7	3.7	3.8
-social contributions	*(in % GDP)*	14.9	15.1	15.1	15.1	15.0	14.5
-other taxes and contributions	*(in % GDP)*	1.5	1.5	1.1	1.0	0.9	0.8

In 2007, we expect general government revenues to grow by 4.2%. Revenues should reach CZK 1 320.3 bn, which represents 38.1% of GDP. The greatest contribution to this growth should be made by current taxes on income, wealth and other (represented especially by the individual and corporate income tax) and social contributions.

Contributions to the growth shown in the following table express the percentage increase or decrease of total revenues in case that only the respective item would be changed.

Table 2-3: Decomposition of revenue growth in 2007

Current taxes on income, wealth etc.	*(p.p.)*	1.3
Social contributions	*(p.p.)*	1.7
VAT	*(p.p.)*	0.5
Excise taxes	*(p.p.)*	0.9
Other taxes	*(p.p.)*	-0.1
Sales	*(p.p.)*	0.4
Other revenue	*(p.p.)*	-0.5
Total	*(growth in %)*	**4.2**

Box 2: Output of the general government sector

The general government sector contributes quite substantially to the growth of gross domestic product. Although this sector's main task is to redistribute national wealth, it also creates the second-greatest added value, after the sector of non-financial enterprises, to be included into the calculation of GDP. In 2006, this sector's output came to CZK 596.1 bn, which represents 18.6% of GDP. Obviously, the dominant part consists of non-market output which, in the long term, represents more than 90% of this sector's output. A smaller part of output is included in revenues as sales. The biggest part of output is created in the local government subsector, very closely followed by the central government subsector. The social security funds participate in this output to an utterly minor extent, which is caused particularly by the fact that the entities to which the health insurance companies pay for health services provided to the household sector are not part of this subsector, and the output is therefore created elsewhere. In 2006, the intermediate consumption of the general government sector reached CZK 213.5 bn and the gross added value of this sector totalled CZK 382.6 bn. As the majority of this sector's output is non-market, it is not possible reliably to determine its value in a market. The valuation is made on the basis of internal costs (fixed capital consumption, compensation of employees, intermediate consumption, other net taxes on output), among which the biggest items are compensation of employees and fixed capital consumption. The majority of this sector's added value is assigned to the employees. In 2006, this value totalled CZK 250.6 bn and represented 65.5% of gross added value; total fixed capital consumption was CZK 138.9 bn, representing 36.3% of gross added value. The net operating surplus of this sector reached moderately negative values, which means that the output of this sector alone cannot cover the costs related to the fixed capital amortisation and employees' salaries. These costs must be consequently paid from other revenues available to this sector (in particular, taxes and social contributions). This confirms the function of the general government sector which, as was already mentioned, consists particularly in redistribution of wealth.

The sum of the added values of the individual sectors of the national economy can be described as the economy's total production, usually represented by gross domestic product.

General government expenditures

In 2006, general government expenditures totalled CZK 1,361.1 bn, representing 42.5% of GDP. The expenditures grew by 4.2% year on year against 2005. Compared to the development for the period from 2002, this was below-average growth. By contrast to the previous year, total expenditures rose more slowly than revenues, by 1.3 percentage points. The government final consumption expenditure grew by 4% against the previous year, thus decreasing the total expenditures growth dynamics. Final consumption was therefore influenced especially by the government collective consumption, which slowed in its growth to 3.4% against 2005. Other budget items that contributed quite significantly to the lower spending dynamics were investment subsidies and other capital transfers. Total expenditures showed the record-smallest contribution in 2004, when they grew by only 1.3%. The major role in this development was played by modestly declining collective consumption and intermediate consumption, and by a more significant decrease in subsidies for production, investment subsidies and other capital transfers.

Total expenditures of the general government sector measured against GDP have tended to decrease in recent years. Since 2003, it has dropped by 4.8 percentage points to 42.5% of GDP, and for 2007 another decrease of 0.4 percentage points is expected. The major role in this decrease is played by government final consumption expenditure, which has fallen by 1.9 percentage points to 21.5% of GDP since 2003. A moderately decreased share in GDP is recorded also for social benefits (other than social transfers in kind). By contrast, gross fixed capital formation is growing moderately. The numerator of the fraction for the share of expenditures in GDP is influenced less by the GDP dynamics than are revenues, and therefore the decreasing share of total expenditure in GDP can be largely credited to rapidly growing GDP. In the light of expenditures on social transfers, however, such development is not flattering. Greater GDP dynamics should lead, in addition to sharp growth in the denominator, to a decrease in unemployment and citizens' reduced dependence on social benefits. Nevertheless, the share of social transfers in GDP fell only slightly, and it will increase again in 2007.

Table 2-4: Structure of general government expenditure

		2002	2003	2004	2005	2006	2007
General government expenditure	*(in % GDP)*	46.3	47.3	44.4	44.0	42.5	42.1
-government consumption	*(in % GDP)*	22.3	23.4	22.4	22.3	21.5	20.6
-social benefits other than social transfe	*(in % GDP)*	12.4	12.2	11.8	11.5	11.4	11.8
-gross fixed capital formation	*(in % GDP)*	3.9	4.5	4.9	4.9	5.1	5.1
-other expenditure	*(in % GDP)*	7.8	7.1	5.2	5.2	4.6	4.6

Table 2-5: Decomposition of growth of expenditure in 2007

Individual consumption	*(p.p.)*	1.4
Collective consumption	*(p.p.)*	0.5
Social benefits other than social transfers	*(p.p.)*	3.2
Interest	*(p.p.)*	0.3
Subsidies on production	*(p.p.)*	-0.3
Gross fixed capital formation	*(p.p.)*	1.0
Other	*(p.p.)*	1.0
Total	*(growth in %)*	**7.1**

In 2007, the general government expenditures are expected to rise to CZK 1,458.4 bn, which should represent 42.1% of GDP. Their growth pace will rise very sharply against 2006 to 7.2%. This is clearly caused by the dominant contributor to the total expenditure growth, which is social benefits other than social transfers in kind and reflects changes in laws adopted in the election year 2006. Should we fix all items at their 2006 levels and anticipate only growth of individual consumption and social benefits, it would result in a growth of total expenditures even higher than was the total growth in 2006. Rather high dynamics is also seen in gross fixed capital formation (which has a similar growth rate in the long term) and in individual consumption.

Box 3: Expenditures on general government final consumption

Besides summing up the added values, it is possible to calculate the general government's contribution to GDP growth using the expenditures of individual entities. Government spending may be presented within the national accounts as individual transactions in their sequence of national accounts. This sequence may also be shown in the concept of government final consumption expenditure that is directly linked to gross domestic product. Government final consumption expenditures make up some 50% of total government expenditure in the long term. Their main components are collective consumption expenditures (i.e. goods and services of collective consumption, such as defence) and individual consumption (i.e. payments for goods and services that are provided to households and have the character of individual consumption, such as education or public health). The subsector of social security funds finances that part of individual consumption that corresponds to the payments to health care institutions for providing services to households, and this item regularly constitutes about one-quarter of government final consumption spending. Collective consumption expenditures are paid especially by the central government subsector and, to a smaller extent, by the local government subsector. The participation of social security funds in collective consumption expenditures is absolutely insignificant; their final consumption expenditures consist mainly of individual consumption. A relatively large part of individual consumption is financed also by local governments, while the central government participates only very little in this financing.

Government final consumption expenditure forms approximately one-fifth of nominal GDP. In addition to government consumption, the GDP calculation using the consumption method involves also the formation of general government gross capital.

General government deficit

The general government deficit preliminarily reached CZK 94 bn for 2006, which represents 2.9% of GDP and stands slightly below the reference value given by the Maastricht criterion (for the second time since 2002). However, it must be mentioned that this value was achieved in periods of rapid economic growth which are likely to fade away in the coming years. The general government deficit in 2007 is expected to be CZK 138.1 bn, which represents 4.0% of GDP, in particular because of a significant acceleration in spending due to growth in social benefits. That would represent a significant worsening in comparison to 2006.

The crucial influence on government's deficit operations has the central government subsector. Similarly, though, the local governments subsector has regularly recorded deficits since 2000, thus contributing negatively to the balance of the whole sector. The deficit of the social security funds subsector stands nearly in balance over the long term. A notable value was reached in 2006, when this subsector's balance came to a surplus of CZK 15.1 bn, and a relative high surplus is also expected in 2007. This outstanding result occurred especially due to lower costs of health care paid using health insurance and by increased payments for state insurees (however in this case it is not an increase in revenues of the general government sector, because the insurance for state insurees is settled from the state budget, i.e. the central government subsector).

Table 2-6: Net lending/net borrowing

		2002	2003	2004	2005	2006	2007
General government net lending (+) /net borrowing (-)	*(in % GDP)*	-6.8	-6.6	-2.9	-3.5	-2.9	-4.0
Central government net lending (+) /net borrowing (-)	*(in % GDP)*	-6.1	-6.0	-2.8	-3.6	-3.1	-4.1
Local government net lending (+) /net borrowing (-)	*(in % GDP)*	-0.5	-0.5	-0.1	0.0	-0.3	-0.1
Social security funds net lending (+) /net borrowing (-)	*(in % GDP)*	-0.2	-0.1	0.0	0.1	0.5	0.2
Primary balance	*(in % GDP)*	-5.5	-5.5	-1.7	-2.4	-1.8	-2.8

Note: Primary balance is the general government deficit with the exclusion of expenditure interest payments.

Debt of the general government sector

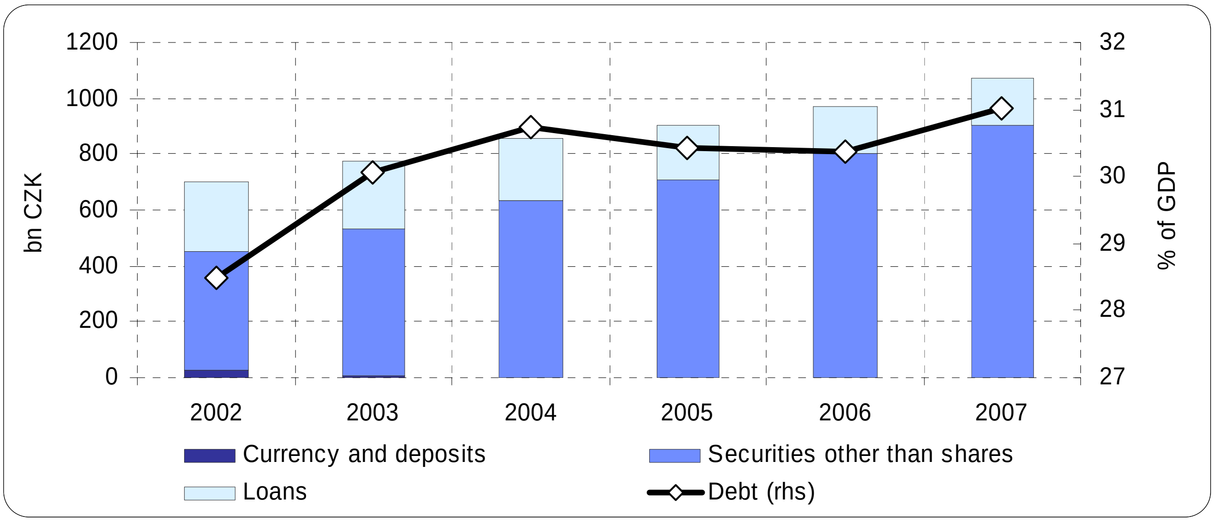
In 2006, the debt of the general government sector reached CZK 973.0 bn, which represented 30.4% of GDP. After a slowdown in 2005, the debt's growth began accelerating, and in 2006 the debt grew by 7.7%. The greatest part of the debt is generated by the central government institutions, and far behind them is the local government subsector. The social security funds contribute only slightly to the total debt, recording low indebtedness rates in the long term.

Table 2-7: Debt

		2002	2003	2004	2005	2006	2007
Central government debt	*(in % GDP)*	26.8	28.2	28.4	28.0	27.8	28.6
Local government debt	*(in % GDP)*	2.0	2.3	2.6	2.7	2.7	2.7
Social security funds debt	*(in % GDP)*	0.0	0.0	0.0	0.0	0.0	0.0

Government debt is defined by the following financial instruments: currency and deposits, along with securities issued other than shares with the exclusion of financial derivatives and loans. Government debt is recorded at its nominal value which is regarded as equivalent to the face value and is consolidated (i.e. debt instruments held by other entities in the subsector or in the general government sector are excluded).

Graph 2-2: Debt by instruments



The structure of government debt by individual instruments is shown in Graph 2-2. The greatest part of the government debt is in the form of debt securities. Their share in the debt is dominant and continues to grow. The second most frequent instrument is loans, whose share in the debt has been decreasing in recent years. A part of the debt was created by deposits in previous years. Currency and deposits on the liabilities side of the balance sheets are hold mainly by commercial banks and the central bank. They are included in the financial institutions sector. In this case the deposits were those received by Consolidation Bank and assumed by the Czech Consolidation Agency as the legal successor to the bank. Currently, they have zero value.

Table 2-8: Stock-flow adjustment

		2002	2003	2004	2005	2006
Gross debt	*(in % GDP)*	28.5	30.1	30.7	30.4	30.4
Change in gross debt	*(p.p.)*	3.4	1.6	0.7	-0.3	0.0
Decomposition of change in gross debt						
Nominal GDP growth	*(p.p.)*	-1.1	-1.2	-2.2	-2.0	-2.2
General government net lending (+) /net borrowing (-)	*(p.p.)*	6.8	6.6	2.9	3.5	2.9
Other factors	*(p.p.)*	-2.3	-3.8	0.0	-1.9	-0.8
- Difference between cash and accrual	*(p.p.)*	-1.4	-0.4	-0.2	-1.5	0.0
- Net accumulation of financial assets	*(p.p.)*	-1.5	-3.6	0.1	-0.4	-0.7
of which: privatisation revenue		-5.1	-1.0	-0.6	-3.6	-0.1
- Revaluation and other factors	*(p.p.)*	0.7	0.2	0.0	0.0	0.0

Box 4: Relation between the deficit and debt (so-called stock-flow adjustment)

The relationship between the change in debt and the realised deficit/surplus is recorded in Table 2-8. The government deficit (so-called “net borrowing” in the terminology of national accounts) or surplus (so-called “net lending”) is not the only factor whose amount determines the increase or decrease of debt during the period under review. Let’s begin from the fact that net lending/borrowing is the balance of the financial account that records only changes in financial assets and liabilities due to transactions (i.e. not due to revaluation and other volume changes), and moreover does so at market value. The relation between this balance and the change in debt liabilities due to transactions involves also net change in financial assets and other “non-debt” liabilities due to transactions. These include, among others, net change in volume of receivables and liabilities due to transactions which express the difference in profit/loss values calculated using the so-called cash basis and accrual principle, which represent the main pillar of the ESA 95 – or national accounts – methodology. Then the debt liabilities must be adjusted by the influence of revaluation and other changes that were not accounted for in the financial account, and, due to the fact that government debt is presented at its nominal value, any differences between its market and nominal values must be taken into account. If the data are presented as a percentage of GDP, it is necessary to account for the influence of growth in nominal GDP on the indicator as to the share of total debt in GDP. Last but not least, as to the relation between the amount of the government deficit and the change of government debt, an important role is played by revenues from privatisation. The privatisation itself does not lead to a net change in financial assets because one financial asset (investments in privatised companies) is exchanged for another (currency). However, the funds received may be used to finance the deficit without the need to issue bonds or take new loans, i.e. without increasing the debt.

In recent years, the development of the debt as a proportion of GDP has shown a moderate decrease or stagnation. In 2006, it reached 30.4% of GDP and its value changed only modestly compared to 2005.

A significant part in such development was played by the rapid growth in nominal GDP, which itself caused a decrease in debt as a proportion of GDP by 2.2 percentage points in 2006. By contrast, the most significant contribution to the growth of debt relative to GDP was made by the general government balance (in our case a deficit). A significant influence preventing the rise in debt may be caused also by privatisation revenues involved in expenditures. They reached their highs in 2002 and 2005. However, the period for obtaining these funds may be different from the period of their use, and they may therefore slow the development of debt in the years to come.

Box 5: The ESA 95 national accounts methodology

Data under the national accounts methodology covers the entire general government and its operations are recorded on the accrual principle (i.e. transactions are recorded at the time when the economic value is created, transformed or ceases to exist or when receivables and liabilities increase or decrease regardless of the moment when the realised transaction will be settled in money terms).

Generally speaking, the general government in the national accounting system represents all institutional units that are controlled by the government and are non-market producers, i.e. more than half of their output is financed by the government and less than a half is financed from receipts. General government in the Czech Republic is divided into three subsectors: central government, local government and social security funds (for details, see below). From the perspective of institutional coverage, the rules for defining the general government sector are harmonised internationally and its composition is updated regularly.

The conventional sector accounts in the national accounting system show various stages of the economic process: production, formation, distribution, redistribution and use of income, and accumulation. Nevertheless, for the purposes of using data for the general government sector, particularly in evaluating the fiscal discipline and formulating fiscal policy, data for the general government sector are presented in a classification as revenues and expenditures.

General government revenues consist of the following transactions: current taxes on income, wealth and others, taxes on production and imports, capital taxes, social contributions, sales, subsidies on production, property income, other current and capital subsidies and transfers.

General government expenditures can be regarded from several points of view. In this publication, they are presented according to final consumption transactions. Government final consumption expenditures are then directly linked to GDP presentation using the expenditure method.

Considered as government final consumption, general government expenditures consist of the following items: government final consumption expenditure, social benefits other than social transfers in kind, interest, subsidies, gross fixed capital formation and other expenditures.

General government expenditures by transactions consist of the following items: intermediate consumption, gross fixed capital formation, compensation of employees, other taxes paid on production, subsidies paid, property income, current taxes on income, wealth and others, social benefits other than social transfers in kind, social transfers in kind related to the expenditures on products provided to households through market producers, other current transfers, capital transfers, and net acquisition of non-financial, non-produced assets.

The general government deficit is the difference between total revenues and total expenditures.

General government debt means total gross debt in its nominal value at the end of the respective year (i.e. consolidated after excluding debt held by various government institutions). Government debt is defined as the following financial instruments: currency and deposits, securities issued other than shares, exclusive of financial derivatives and loans. According to the current European standards other receivables (for example, commercial loans) are not included in the government debt.

Moreover, the ESA 95 methodology is used to determine the so-called Maastricht criteria in relation to the deficit (reference value 3% of GDP) and of government debt (reference value 60% of GDP).

Institutional coverage of the general government sector in the Czech Republic:

Central government subsector: *state budget, including operations of the National Fund and Privatisation Fund, state funds, semi-budgetary organisations controlled and predominantly financed by the central government, public research institutions, Land Fund, Supporting and Guarantee Agricultural and Forestry Fund, Viticultural Fund, Czech Collection Company, Czech Consolidation Agency (since the last quarter of 2001), including its subsidiary companies (since 2002), public universities, Railway Infrastructure Administration (since 2003), PPP Centre (since 2004).*

Local government subsector: *local governments, voluntary associations of local governments, semi-budgetary organisations controlled and predominantly financed by local government, and regional committees of cohesion regions.*

Social security funds subsector: *health insurance companies, Association of Health Insurance Companies (since 2005) and Centre for International Reimbursements (since 2005).*

3 Medium-term fiscal outlook

3.1 Medium-term outlook of the state budget and expenditure frameworks

Since 2004, the Czech Republic's budgetary policy has been carried out within a regime of so-called fiscal targeting (for more, see Chapter 4). The current fiscal targets (see Table 3-1), upon which the fiscal outlook is based, as well as the current strategy for decreasing the public budgets deficit that is expressed by these fiscal targets, are substantially more ambitious compared to the previous fiscal outlook from September 2006. This fiscal outlook counts upon a rapid decrease of the deficit in 2008 and anticipates that the deficit will continue to decreasing gradually in 2009 and 2010.

Comparison of set fiscal targets with the no policy change indicates that reaching these targets will require fiscal consolidation in the approximate amount of 1 percentage point of GDP. Consolidation effort will be concentrated nearly to the full extent as early as by 2008. Therefore, the presented scenario may only be fulfilled on condition that austerity measures are pushed through, and in particular those on the expenditures side of public budgets.

Table 3-1: Fiscal targets – balance of public budgets (national fiscal targeting methodology, % of GDP)

		2007 *Forecast*	2008 *Outlook*	2009 *Outlook*	2010 *Outlook*
Actual fiscal targets (April 2007)	*[1]*	-	**-3.0**	**-2.6**	**-2.3**
Previous fiscal targets (September 2006)	*[2]*	-4.0	-3.5	-3.2	-
No policy change scenario	*[3]*	-4.1	-4.0	-3.7	-3.0
Consolidation effort	*[4=3-1]*	x	**1.0**	**1.1**	**0.7**

Fiscal targets and the public revenues forecast determine spending limits. The binding expenditure frameworks are derived as follows:

1. Establishment of fiscal targets for total public budgets (PB) as proportions of GDP.
2. Acceptance of assumption regarding the balances of the components of public budgets excluding the state budget (SB) and state funds (SF)[2] as proportions of GDP.
3. Derivation of the target for SB and SF as the difference between the target for total PB and the anticipated balance of other PB components.
4. Derivation of an expenditure framework for SB and SF as the difference between the SB and SF revenues forecast and the absolute value of the targeted balance for SB and SF.

The deficit of components excluding SB and SF will increase moderately in the coming years. We expect that, as in past years, the regional and municipal governments budget balances will show a deficit of ca 0.2% of GDP and the health insurance companies' finances will be in balance. The increase in the deficit will be brought about especially by the operations of the Privatisation Fund,

[2] For the purposes of fiscal targeting, the public budgets consist of the following components (besides the state budget and state funds): Privatisation Fund (former National Property Fund), Land Fund, municipal and regional governments, and health insurance companies.

which will bear higher costs resulting from the settlement of liabilities relating to the removal of old environmental burdens. The Privatisation Fund's finances will record a deficit of around 0.5% of GDP.

Expenditure frameworks thus established will ensure (on condition that assumptions about the deficit for components of public budgets other than the state budget and state funds are met, and so are the assumptions regarding revenues) that the fiscal targets set for public budgets will be achieved. The principle of fiscal targeting consists therefore in determining the amount of public expenditures that are under the government's direct control so that such amount is consistent with the given targets.

Table 3-2: Calculation of expenditure frameworks from fiscal targets (fiscal targeting methodology)

		2006	2007 *Forecast*	2008 *Outlook*	2009 *Outlook*	2010 *Outlook*
Target for public budgets	*% of GDP [1]*	-3.2	-4.1	**-3.0**	**-2.6**	**-2.3**
Balance of public budgets other than state budget and state funds	*% of GDP [2]*	-0.2	-0.4	-0.7	-0.7	-0.7
Target for state budget and state funds	*% of GDP [3=1-2]*	-3.0	-3.7	-2.2	-2.0	-1.6
	(CZK bn) [4]	-95.5	-128.8	-83.1	-78.6	-70.4
Revenue foracast of SB and SF	*(CZK bn) [5]*	915.7	1005.2	972.4	999.1	1032.8
State budget	*(CZK bn) [5a]*	856.1	943.1	928.7	955.4	984.7
State funds	*(CZK bn) [5b]*	59.6	62.1	43.8	43.7	48.1
New expenditure frameworks	*(CZK bn) [6=5-4]*	1011.1	1134.0	**1055.5**	**1077.7**	**1103.2**
State budget	*(CZK bn) [6a]*	928.4	1031.8	1004.9	1028.3	1053.7
State funds	*(CZK bn) [6b]*	82.7	102.1	50.6	49.4	49.5

According to the law on budgetary rules, the already approved expenditure frameworks may be modified only in expressly specified cases. In addition to the state budget for 2007, expenditure frameworks were approved in 2006 for 2008 and 2009. After taking into account the changes in the mutual subsidy relations between the state budget and the state funds, the approved expenditure framework would amount to CZK 1 094.4 bn for 2008 and CZK 1 136.5 bn for 2009.

Table 3-3: Adjustments of approved expenditure frameworks according to the budgetary rules (fiscal targeting methodology, bn CZK)

		2008	2009
Approved frameworks (2006) - unconsolidated	*[1]*	**1088.7**	**1130.7**
Consolidation (2006)	*[2]*	18.0	18.1
Approved frameworks (2006) - consolidated	*[3=1-2]*	1070.7	1112.6
Consolidation (2007)	*[4]*	23.7	23.9
Approved frameworks adjusted - unconsolidated	*[5=3+4]*	**1094.4**	**1136.5**

Newly derived expenditure frameworks come to smaller amounts than did the originally approved expenditure frameworks, which represent the maximum limit for expenditures of the state budget and state funds in 2008 and 2009. The reason for that lies mainly in the fact that the new frameworks are based on more ambitious fiscal targets. Therefore, after two years of exceeding expenditure frameworks, the spending discipline for the budgetary policy is to be tightened substantially.

Table 3-4: Assessment of the fulfilment of expenditure frameworks (fiscal targeting methodology, bn CZK)

		2008	2009
Approved frameworks adjusted	[1]	1094.4	1136.5
New expenditure frameworks	[2]	1055.5	1077.7
Tightening (+) / breach (-) of frameworks	[3=1-2]	**38.9**	**58.8**

3.2 General government medium-term outlook

General government balance

The medium-term fiscal outlook presented in the previous section represents the most important component of the general government balance. At the same time, it is the government's main tool for implementing the macroeconomic policy and executing other public finance functions. However, the economic development and results of the entire general government may deviate from the government's objectives for many reasons. A considerable part of government institutions is not under the government's direct control – in particular, municipal and regional governments, health insurance companies, and others. Moreover, the statistical record of the general government is different from the budgeting method. While the budgeting process deals with planning cash transactions, in the national accounts system the general government sector is recorded on an accrual basis.

Table 3-5: Balance according to national fiscal targeting methodology and national accounts

		2006 *Preliminary*	2007 *Forecast*	2008 *Outlook*	2009 *Outlook*	2010 *Outlook*
Balance of public budgets (fiscal targeting)	*(CZK bn)*	-102.2	-141.9	-110.7	-105.0	-99.4
	(% of GDP)	-3.2	-4.1	-3.0	-2.6	-2.3
Differences between ESA 95 and fiscal targeting	*(CZK bn)*	7.7	3.5	-8.5	-13.3	-10.7
of which: differences between cash and accrual tax revenues	*(CZK bn)*	4.2	-3.5	-15.0	-18.0	-6.0
General government balance (ESA 95)	*(CZK bn)*	-94.5	-138.4	-119.1	-118.3	-110.1
	(% of GDP)	-2.9	-4.0	-3.2	-2.9	-2.5

For purposes of budgetary policy, the general government balance is approximated by the public budgets balance in the so-called fiscal targeting methodology (see Box 6). Table 3-5 shows the relationship between the targeted balance for cash revenues and expenditures of public budgets in the fiscal targeting methodology and the balance of the general government sector according to the national accounts (ESA 95). The differences between those two concepts are not great, but neither are they negligible. Above all, they fluctuate significantly through time and are difficult to predict. This complicates forecasting the balance of the general government sector consistently with the targeted balance of public budgets.

One of the important factors that will influence the differences between the balances in both methodologies in the fiscal outlook's horizon is the different cash and accrual impacts of tax reform on tax revenues (see Table 3-8). While the accrual revenues (tax liability) will decrease immediately in case of a tax rate reduction, the cash impact is delayed in time due to the advance payment method. In a period of decreasing taxes, the accrual revenues come to a smaller amount than do the cash collections, and we can expect that this factor will moderately deepen the deficit according to the national accounts relative to the fiscal targets.

Box 6: Differences between the fiscal targeting methodology (state budget's outlook, expenditure frameworks) and the ESA 95 national accounts methodology (Maastricht criteria, Convergence Programme)

The national fiscal targeting methodology begins from recording the balances of selected public budgets on a cash basis (for more, see Box 1). For the purpose of **fiscal targeting**, these balances are adjusted for operations of a financial nature (lending and repayments), and for revenues from privatisation and subsidies to transformation institutions (for example, settlement of losses of the Czech Consolidation Agency). The goal is to net out the balance by financial operations that are cash revenues or expenditures but that nevertheless, from the economic point of view, do not represent changes in assets of public finances (e.g. privatisation), and then to exclude one-off transactions (e.g. settlement of past transformation costs) and, finally, to bring the results closer to the ESA 95 international methodology.

The international **ESA 95 methodology** is based on the accrual recording of the entire general government as defined by the national accounts (for more, see Box 5). The balance does not represent the difference between the cash revenues and expenditures. It is a profit/loss that in fact represents a change in financial assets and liabilities of the sector due to revenue and expenditure transactions. Along with other factors representing changes in assets and liabilities (revaluation, etc.), it constitutes the change in net wealth of the general government. A deficit under the ESA 95 methodology, in the case of zero revaluation and other volume changes, directly expresses the decrease of the sector's net wealth. A deficit under the cash methodology expresses (only) the increase or decrease of cash sources.

The main differences between the fiscal target in the fiscal targeting methodology and the balance under ESA 95 are the following:

- differences between the cash and accrual principles (time shift between the origin of the payable or receivable and the corresponding cash flow),
- differences from unlike coverage (national fiscal target includes only balances of selected parts of general government),
- other differences in classification (e.g. remission of uncollectible receivables that represent an accrual expenditure but not a cash expenditure).

This raises the question as to why the fiscal targets are established as a specifically defined balance of public budgets if the most frequently used indicator for evaluating the general government balance is the balance under the ESA 95 methodology. The main reason is to ensure the direct relation between the fiscal targeting methodology and the methodology for compiling the state budget, first in the phase when the state budget parameters and its outlook are derived (expenditure limits of the budget and state funds) from the fiscal target and then in the phase of evaluating the fulfilment of the targets. In setting a target using the fiscal targeting methodology, it is possible unambiguously to evaluate to what extent the government policy contributes to fulfilling or not fulfilling targets (as a result of the state budget and state funds that are under its direct control) and to what extent the fulfilment or non-fulfilment was caused by inaccurate estimates of other components of public budgets or by non-fulfilment of the revenue forecast.

During 2008–2010, the general government deficit will gradually decrease in accordance with the proposed consolidation strategy. The general government revenues will grow at a rate far below the nominal growth of GDP. This will lead to a decrease of their share in GDP, which will be partly due to the autonomous decrease of the tax quota and partly due to the active measures taken to reduce the tax burden. The deficit decrease will thus be provided by the austerity measures on the spending side. The share of government expenditures in GDP should fall by nearly 4.0 percentage points by 2010.

Table 3-6: General government developments (ESA 95)

		2006 *Preliminary*	2007 *Forecast*	2008 *Outlook*	2009 *Outlook*	2010 *Outlook*
General government balance	*(% of GDP)*	**-2.9**	**-4.0**	**-3.2**	**-2.9**	**-2.5**
Total revenue	*(% of GDP)*	**39.5**	**38.1**	**38.0**	**37.1**	**36.2**
	(growth in %)	5.5	4.2	7.3	5.3	5.1
Total expenditure	*(% of GDP)*	**42.5**	**42.1**	**41.1**	**40.1**	**38.7**
	(growth in %)	4.2	7.1	5.3	4.8	4.2

General government revenues

In 2008, restructuring from direct taxes towards indirect taxes is noticeable in tax revenues, as the reduction of income taxes (taxes on income and wealth) is offset by an increase in collection of value added tax (taxes production). Overall, the tax revenues in real terms will almost stagnate in 2009 and 2010, and the tax quota will decrease by 4.7 percentage points of GDP against 2006.

Revenues from social contributions will be negatively influenced by, among other things, adjustments in the sickness insurance system and by introducing the maximum assessment base for social contributions. Their dynamics will therefore range much farther below the expected growth rate in wage volumes.

The most dynamic item on the revenues side will be transfers received (part of the “Other” item), due to the inflow from the EU funds.

Table 3-7: General government revenue

		2006 *Preliminary*	2007 *Forecast*	2008 *Outlook*	2009 *Outlook*	2010 *Outlook*
Total revenue	*(bn CZK)*	**1267.1**	**1320.3**	**1417.3**	**1492.3**	**1568.4**
	(growth in %)	5.5	4.2	7.3	5.3	5.1
Tax revenue	*(bn CZK)*	**633.8**	**667.0**	**718.3**	**735.3**	**757.7**
	(growth in %)	2.3	5.2	7.7	2.4	3.0
Taxes on production and imports	*(bn CZK)*	**352.2**	**368.3**	**431.0**	**446.7**	**460.7**
	(growth in %)	2.4	4.6	17.0	3.6	3.1
Current taxes on income, wealth, etc.	*(bn CZK)*	**280.9**	**297.9**	**286.8**	**288.1**	**296.5**
	(growth in %)	2.2	6.1	-3.7	0.4	2.9
Capital taxes	*(bn CZK)*	**0.7**	**0.7**	**0.5**	**0.5**	**0.5**
	(growth in %)	1.4	-2.1	-38.4	0.8	0.8
Social contributions	*(bn CZK)*	**481.8**	**503.3**	**528.4**	**554.9**	**588.2**
	(growth in %)	7.4	4.5	5.0	5.0	6.0
Property income	*(bn CZK)*	**25.8**	**16.0**	**17.8**	**19.4**	**21.1**
	(growth in %)	21.6	-37.8	11.1	8.8	8.9
Other	*(bn CZK)*	**125.7**	**134.0**	**152.7**	**182.7**	**201.5**
	(growth in %)	12.0	6.6	13.9	19.7	10.3
Tax burden	*(% of GDP)*	**34.8**	**33.8**	**33.4**	**32.1**	**31.1**

Table 3-8: Impact of tax reform on tax revenues (bn CZK)

	Cash terms			Accrual terms		
	2008	2009	2010	2008	2009	2010
Value added tax	25.6	27.0	27.9	25.6	27.0	27.9
Personal income tax	-16.2	-24.3	-27.5	-21.3	-24.3	-27.4
Corporate income tax	0.0	-6.1	-28.2	-4.1	-18.8	-27.5
Inheritance and gift taxes	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Total impact	**9.0**	**-3.8**	**-28.2**	**-0.2**	**-16.5**	**-27.4**

General government expenditures

Due to the gradual decrease in revenues as a percentage of GDP, the expenditure side needs to undergo a relatively significant consolidation to ensure the deficit will decrease.

The slow nominal growth rate of final consumption expenditures will reflect low growth of wages and salaries in the government sector, made possible by a reduction of employment in the public administration, as well as by savings in purchases of goods and services. Wages and salaries in general government will apparently grow faster than is the objective set by the government for the public administration (annual growth 1.5%), because the employment in general government considerably exceeds that of the regulated sphere, and the rest of general government may not follow closely the government's objectives.

Nevertheless, the decisive factor for achieving the fiscal targets will be savings in the social benefits area (social transfers other than in kind). The positive impact of measures in the social field on the government balance should come to 0.7–0.8% of GDP in 2008-2010.

Gross fixed capital formation will achieve high dynamics due to implementing investment projects financed using the EU funds. A gradual onset of drawing from the EU funds should be reflected in the growth rate of government investments, which will be high at first and then decreasing gradually.

Table 3-9: General government expenditure

		2006 Preliminary	2007 Forecast	2008 Outlook	2009 Outlook	2010 Outlook
Total expenditure	*(bn CZK)*	**1360.4**	**1457.7**	**1535.4**	**1609.5**	**1677.4**
	(growth in %)	4.2	7.2	5.3	4.8	4.2
Final consumption expenditure	*(bn CZK)*	**687.7**	**713.3**	**734.5**	**763.7**	**794.1**
	(growth in %)	4.0	3.7	3.0	4.0	4.0
Collective consumption	*(bn CZK)*	**345.0**	**351.6**	**357.5**	**371.5**	**386.5**
	(growth in %)	3.4	1.9	1.7	3.9	4.0
Individual consumption	*(bn CZK)*	**342.7**	**361.6**	**377.0**	**392.3**	**407.6**
	(growth in %)	4.6	5.5	4.3	4.1	3.9
Social transfers in kind	*(bn CZK)*	**171.2**	**182.0**	**192.6**	**200.0**	**208.1**
	(growth in %)	2.3	6.3	5.8	3.9	4.0
Transfers of individual non-market goods and services	*(bn CZK)*	**171.5**	**179.6**	**184.4**	**192.2**	**199.5**
	(growth in %)	7.0	4.8	2.7	4.2	3.8
Social transfers other than in kind	*(bn CZK)*	**364.4**	**408.4**	**413.1**	**429.3**	**446.7**
	(growth in %)	6.4	12.1	1.2	3.9	4.0
Interest	*(bn CZK)*	**35.4**	**39.7**	**49.5**	**54.9**	**59.6**
	(growth in %)	2.9	12.1	24.9	10.7	8.7
Subsidies	*(bn CZK)*	**62.0**	**57.6**	**63.7**	**64.8**	**66.1**
	(growth in %)	12.3	-7.0	10.5	1.9	2.0
Gross fixed capital formation	*(bn CZK)*	**162.0**	**176.3**	**203.0**	**224.7**	**238.1**
	(growth in %)	10.6	8.8	15.2	10.7	6.0
Other	*(bn CZK)*	**48.8**	**62.5**	**71.5**	**72.1**	**72.8**
	(growth in %)	-25.2	28.0	14.4	0.8	1.0
Compensation of employees	*(bn CZK)*	**250.6**	**262.3**	**268.7**	**279.1**	**290.4**
	(growth in %)	5.9	4.6	2.5	3.9	4.0
Total social transfers	*(bn CZK)*	**535.7**	**590.4**	**605.7**	**629.4**	**654.8**
	(growth in %)	5.0	10.2	2.6	3.9	4.0

The outlook also indicates that in 2008 savings will be concentrated on the social benefits area. In 2009 and 2010, the majority of savings will be achieved in other components of government expenditures.

Table 3-10: Impact of the public finance reform in the social area (bn CZK)

	2008	2009	2010
	Impact on revenue		
Introduction of max. assesment base for social contributions	-4.6	-4.7	-4.8
Postponement of the act on casualty insurance	-5.9	-5.1	1.0
Postponement of the act on sickness insurance	11.3	10.1	0.0
Total impact on social revenue	**0.9**	**0.3**	**-3.8**
	Impact on expenditure		
Sickness insurance benefits	-6.8	-2.6	-6.5
Government welfare benefits	-8.5	-9.8	-13.1
Postponement of the act on casualty insurance	-3.4	-3.5	0.0
State's payment into the public health insurance system	-3.4	-6.4	-2.0
Other changes to the health insurance system from 2010	0.0	0.0	-7.1
Pension insurance benefits	-1.6	-1.1	0.0
Other changes in the social area	-1.6	-7.1	-6.7
Total impact on social expenditure	**-25.3**	**-30.5**	**-35.4**
	Impact on balance		
Total impact on balance	**26.2**	**30.8**	**31.6**
Total impact on balance (in % of GDP)	**0.7**	**0.8**	**0.7**

General government debt

The absolute level of gross government debt will continue to grow each year of the outlook due to the debt financing for a part of the expected deficits. However, the significant decrease of the deficit along with the dynamic growth of nominal GDP will lead to stabilisation and in 2010 even to a decrease of the debt as a percentage of GDP. Moreover, this is an indicator that is more suitable for use in assessing the indebtedness rate of the general government than is the absolute amount of the debt.

Table 3-11: Gross consolidated government debt

		2005	2006 Preliminary	2007 Forecast	2008 Outlook	2009 Outlook	2010 Outlook
General government	*(bn CZK)*	**903.5**	**973.0**	**1074.2**	**1183.8**	**1284.4**	**1375.6**
Central government	*(bn CZK)*	830.9	891.7	991.7	1084.2	1177.0	1259.2
Local government	*(bn CZK)*	72.3	81.1	82.5	99.2	107.4	116.4
Social security funds	*(bn CZK)*	0.3	0.2	0.0	0.4	0.0	0.0
Government debt to GDP ratio	*(% of GDP)*	**30.4**	**30.4**	**31.0**	**31.7**	**32.0**	**31.7**
Contribution to change in debt							
Change in debt	*(p.p.)*	**-0.3**	**0.0**	**0.7**	**0.7**	**0.3**	**-0.2**
Primary balance	*(p.p.)*	**2.4**	**1.8**	**2.8**	**1.9**	**1.6**	**1.2**
Interest	*(p.p.)*	**1.2**	**1.1**	**1.1**	**1.3**	**1.4**	**1.4**
Nominal GDP growth	*(p.p.)*	**-2.0**	**-2.2**	**-2.3**	**-2.3**	**-2.3**	**-2.3**
Stock-flow adjustment	*(p.p.)*	**-1.9**	**-0.8**	**-1.1**	**-0.2**	**-0.4**	**-0.4**
Difference between cash and accruals	*(p.p.)*	-1.5	0.0	0.4	0.3	0.1	0.1
Net acquisition of financial assets	*(p.p.)*	-0.4	-0.7	-1.5	-0.5	-0.5	-0.5
of which: privatisation	*(p.p.)*	-3.6	-0.1	-1.0	0.0	0.0	0.0
Revaluation effects and other	*(p.p.)*	0.0	0.0	0.0	0.0	0.0	0.0

Government debt will grow more slowly than would correspond to the simple summing up of the full amount of the deficit. The reason for that is the fact that only a part of deficits is financed through debt instruments. The significant source of financing that slows the debt growth are privatisation revenues. Thay are not general government revenues (privatisation represents only a change in financial assets from shares into cash) and do not decrease the balance. They do, however, limit the necessity for debt financing.

We expect that until 2010 the privatisation revenues accumulated in the previous period will be gradually involved in financing the deficits (see negative acquisition of financial assets). This outlook does not count on other, as yet unapproved privatisation projects. In view of the fact that these are likely to be realised, the debt projection includes a risk that the share of debt in GDP will be lower.

Cyclical development

The Czech economy is in a cyclical upswing. Estimates of the output gap indicate that GDP stands approximately at 0.7 percentage points above its potential, which is reflected in a positive cyclical component of the government balance. Thus, the cyclically adjusted deficit currently attains greater values of some 0.2 percentage points than the recorded nominal deficit.

The macroeconomic forecast looks for GDP to grow moderately below its potential until 2010, which will lead to gradually filling the positive output gap. The cyclical component of the general government balance will therefore lose its significance, coming close to zero in 2009 and 2010.

Fiscal effort defined as the change of the cyclically adjusted balance will be close to the change in the nominal deficit. After a significant deficit decrease in 2008, the fiscal effort in 2009 and 2010 will weaken and it is probable that the rule of the Stability and Growth Pact that requires making fiscal effort at the minimum level of 0.5 percentage points of GDP annually will not be met.

Table 3-12: Cyclically adjusted government balance (% of GDP)

		2006	2007	2008	2009	2010
		Preliminary	*Forecast*	*Outlook*	*Outlook*	*Outlook*
Real GDP growth	*(in %)*	6.1	5.3	4.9	5.1	5.3
General government balance		**-2.9**	**-4.0**	**-3.2**	**-2.9**	**-2.5**
Interest		1.1	1.1	1.3	1.4	1.4
Potential GDP growth	*(in %)*	5.1	5.1	5.4	5.4	5.5
Output gap		0.7	0.8	0.3	0.0	-0.2
Cyclical budgetary component		**0.2**	**0.2**	**0.1**	**0.0**	**0.0**
Cyclically adjusted balance		**-3.1**	**-4.2**	**-3.3**	**-2.9**	**-2.5**
Cyclically adjusted primary balance		-2.0	-3.1	-1.9	-1.6	-1.1
Fiscal effort		**-0.3**	**-1.1**	**0.9**	**0.3**	**0.5**

3.3 General government long-term projection

Long-term analyses look at the general government expenditures and their dynamics by means of the long-term trends connected with population development. Therefore they primarily focus on those components of public expenditures that are sensitive to changes in the population structure, such as pensions, health and long-term care, and education.

Long-term projections do not aim at quantifying to the most reliable extent the volumes of future expenditures or specific values for certain indicators with the possibility of subsequent verification with the actual situation. They only should help to discover the direction, dynamics and relations of the projected data in the currently established horizon to 2050. More accurate estimations may not be made due to the large extent of uncertainty and the design of the model apparatus. The projections are not made in the same level of detail as are the short-term forecasts that allow certain verification.

The long-term projections methodology is based mainly on international experience gained from cooperation with the European Commission, which is now actively involved in making projections, with the contributions from all member states. This cooperation allows using the results of analyses for the purposes of international comparisons.

Population trends and their impacts on macroeconomic indicators

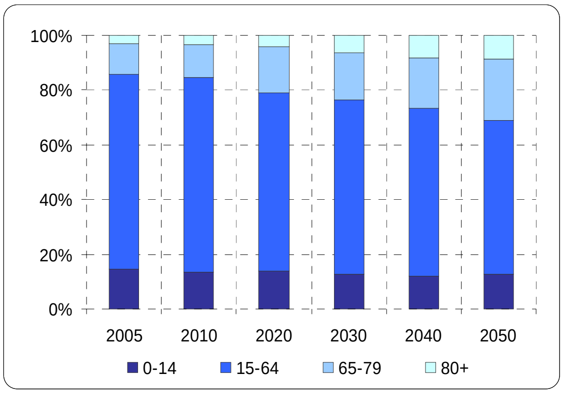
In the present European context, the Czech population is relatively among the youngest. In the coming decades, however, very dynamic changes in its structure are expected. Within the next 50 years, the Czech population will rank among the oldest in Europe. The reason behind these changes is the rapidly increasing life expectancy accompanied by a low aggregate fertility rate. Population projections[3] assume that life expectancy at birth will increase between 2005 and 2050 by 7.1 years for men (from 72.6 to 79.7 years) and by 5.1 years for women (from 79.0 to 84.1 years). The aggregate fertility rate will remain far below the level that ensures simple reproduction (an increase from 1.15 to

[3] This is primarily based on the demographic projection that is produced by Eurostat in cooperation with the national statistical offices and is the basis for calculating the long-term projections. Use of this projection ensures comparability with the projections of demographic developments in other EU countries.

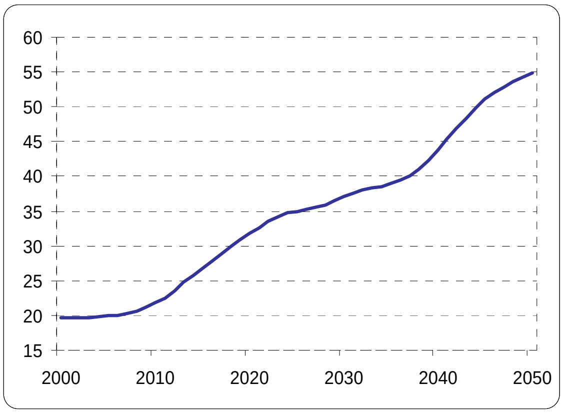
1.5). Even significant growth in net immigration (from 4,300 to 20,000 annually) will not prevent an overall decline in the population (from 10.2 to 8.8 million people).

These trends can be seen in the following graphs that document the changes in the age structure of the population towards a decreased proportion of persons in the active age and an increasing proportion of those of retirement age. The dependency ratio indicates that the proportion between these two groups will nearly double in favour of the oldest persons. This development is perceptible in the whole of Europe. That is why this topic is currently more and more emphasised in order to draw attention to this situation in time and to solve it through adequate reforms of social systems and the labour market.

Graph 3-1: Changes in age structure of the population



Graph 3-2: Dependency ratio (in %)



Note: The dependency ratio is defined as the proportion of people aged 65 and older to the population aged 15–64 in the central demographic scenario.

The present analyses do not, however, anticipate any possible legislative changes and embody the assumption that the policies will not change. They indicate which tendencies will occur if no institutional and legislation changes will be implemented.

The changes in population do not project only into the public expenditures, but they also influence the economy's overall output as measured by real GDP growth. That growth is expected to gradually attenuate to the limit value of 0.8%. This is caused by, among other things, a decrease of available labour. Table 3-13 shows an overview of the selected macroeconomic assumptions used in the long-term projections.

Table 3-13: Macroeconomic assumptions (in %)

	2005	2010	2020	2030	2040	2050
Real GDP growth	6.1	5.3	2.5	1.9	0.4	0.8
Labour productivity growth	4.8	3.4	3.0	2.7	1.9	1.7
Participation rate males (aged 20–64)	83.5	84.6	87.4	87.1	84.4	85.6
Participation rates females (aged 20–64)	68.2	70.6	76.4	76.1	72.9	74.0
Total participation rates (aged 20–64)	75.8	77.6	81.9	81.6	78.7	79.8
Unemloyment rate	7.9	5.6	6.5	6.5	6.5	6.5

Public expenditure development

Expenditures related to the ageing of the population will accelerate in the coming decades. This growth will be reflected most significantly in the pension system, which will be most demanding as to the expenditures, due to the increased number of persons in retirement age and the lengthening period for drawing pensions. These expenditures, along with the spending on health care, represent the main sources of public expenditures growth.

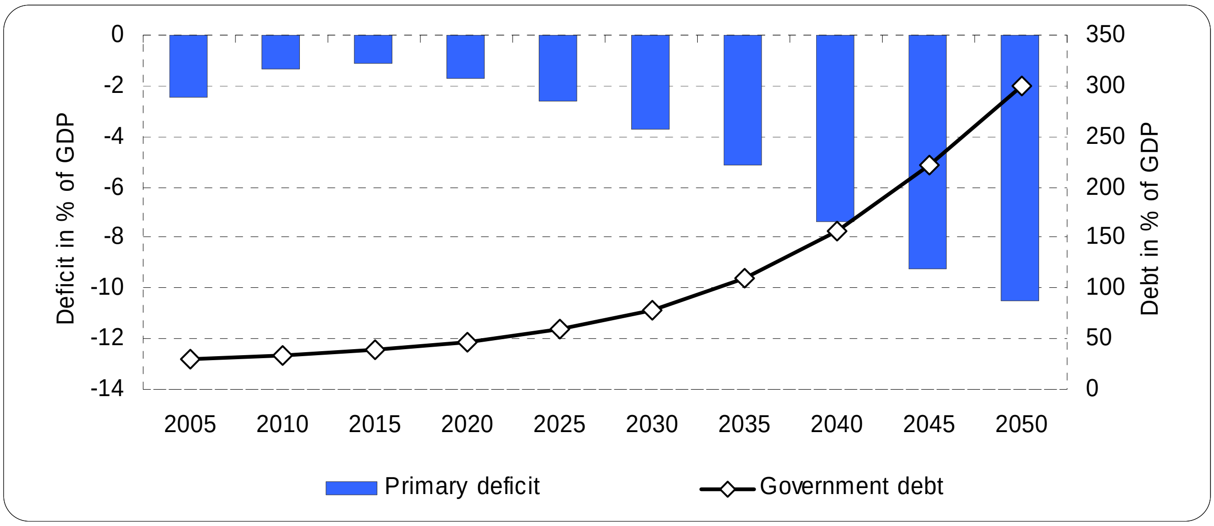
As regards the revenues of the social system, their existing share in GDP is expected to be maintained, because their sole source is the contribution rate that is constant over time.

Table 3-14: Long-term sustainability of public finances (in % of GDP)

	2005	2010	2020	2030	2040	2050
Total expenditure	44.0	42.5	43.3	46.2	52.0	59.2
of which: Age-related expenditure	19.9	18.5	18.9	20.9	24.5	27.7
Pension expenditures	8.4	7.7	8.3	9.5	12.1	14.2
Health care	6.5	6.4	6.7	7.3	8.1	8.9
Long-term care	0.3	0.3	0.3	0.4	0.5	0.6
Education expenditures	3.6	3.1	2.7	2.8	2.9	3.0
Other age-related expenditures	1.2	1.0	1.0	0.9	1.0	1.1
Interest expenditures	1.2	0.9	1.3	2.2	4.3	8.4
Total revenue	40.4	40.3	40.3	40.3	40.3	40.3
of which: property income	0.7	0.7	0.7	0.7	0.7	0.7
of which: pension contributions	8.7	8.7	8.7	8.7	8.7	8.7

These facts will cause further widening of the gap between revenues and expenditures, and therefore to the gradual rise in the primary deficits and interest payments that will cause the government debt to accumulate. Without implementing reforms, the development of public finances cannot be sustained in the long term.

Graph 3-3: Primary deficit and debt



The seriousness of the impacts from these trends is described in the sustainability analysis that further determines the scope of fiscal imbalance using so-called sustainability indicators. These can take two forms:

- The S1 indicator indicates, as a percentage of GDP, the need to decrease expenditures' share in GDP or to increase revenues' share in GDP from the respective year in order to ensure maintaining the debt below the limit of 60% of GDP until the end of the projection horizon (2050).

- The S2 indicator expresses, as a percentage of GDP, the need to permanently decrease expenditures or increase taxes in order to keep the general government solvent in an indefinite time horizon (i.e. so that the debt would not grow ad infinitum).

The following table contains a brief overview of these indicators that represent the quantitative evaluation of the imbalance rate.

Table 3-15: Long-term requirements for public finances (in % of GDP)

		2009	2010	2011
Revenues	[1]	40.3	40.3	40.3
Primary expenditures	[2]	41.7	41.6	41.5
Primary balance	[3=1-2]	-1.4	-1.3	-1.3
Sustainability gap S1	[4]	3.9	4.0	4.1
Required primary balance	[5=3+4]	2.5	2.7	2.9
Required total balance	[6]	1.0	1.8	1.9
Sustainability gap S2	[7]	7.9	8.1	8.2

The sustainable primary balance transforms the "consolidation requirement" given by the S1 indicator into the figures of the primary difference between the revenues and primary expenditures. The sustainable total balance indicates that, for example, for 2009, it is necessary that the surplus of the general government balance will amount to 1% of GDP.

The conclusions of the sustainability analysis are not favourable. The overall evaluation that contains both the quantitative and qualitative evaluations[4] classifies the Czech Republic in the European context among those countries for which the future development is the most risky as regards the demographic changes.

[4] The qualitative evaluation focuses on the amount of indebtedness, age-related expenditure dynamics, projected revenue development, the so-called stock-flow adjustment (see Box 4) and the total tax burden.

4 Topic: Fiscal rules

4.1 Introduction

History of fiscal policy

Fiscal policy is one of the main instruments of government macroeconomic policy. One of the targets is to stabilise economic growth and to counteract the fluctuations of the economic cycle. Fiscal policy has been recognised and used as an economic policy tool since the economic crisis in the 1930s. The most famous theoretical groundwork for fiscal policy is described in the work of John Maynard Keynes. Fiscal policy was then used in practice in the US and especially in Sweden.[5] Afterwards, fiscal policy became a common tool of economic policy.

In the second half of the 20th century, however, imprudent fiscal policy[6] induced the problem of excessive deficits (continually in the US from the 1960s until 1997 when the American budget was in surplus for the first time after 30 years) and an increase of government debt which, in certain countries, reached enormous levels (in Belgium and Italy around 140% of GDP). This situation increased interest in fiscal rules which could help to bring fiscal policy under control and to make the development of public finances sustainable. In the EU, this process culminated in the Maastricht Agreement and the so-called Stability and Growth Pact, which define a fiscal framework that should be stabilising on the one hand and sustainable on the other.

Automatic stabilisers and discretionary measures

An automatic stabiliser is a mechanism that "smoothes" the economic cycle without the active participation of other subjects. It is a system element that, from its nature, works independently, automatically. The most frequently mentioned example of an automatic (built-in) stabiliser is the progressive income tax (i.e. the tax rate increases in correspondence with growing income and the average tax rate decreases with decreasing income). This should lead to lower volatility of the disposable income and consumption depending upon changes in GDP.

Discretionary measures are mechanisms of the authority's direct interference in the system, ad hoc measures whose objective is to have a stabilising impact.

Compared to discretionary measures, the benefit of automatic stabilisers is that they are embedded in the system and do not involve a delay from the time of identifying the problem until implementing the measure.

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[5] There was a so-called Stockholm School in Sweden, and some of its representatives, in particular the awardees of the Nobel Prize for Economics Gunnar Myrdal and Bertil Ohlin, were engaged in fiscal policy on a similar theoretical level at the same time as was Keynes.
[6] See the sub-chapter Fiscal Rules below in the text.

Fiscal rules

Fiscal policy is executed by the government, or Ministry of Finance, using public budgets, and in particular the state budget. Compared to monetary policy, fiscal policy is burdened by direct political influence. Over the years, a generally accepted opinion has developed that the central bank should be independent in order to prevent high inflation. On the contrary, the Ministry of Finance is not independent and, of course, it cannot be. Therefore, there may be situations (in particular before elections) where public finances have not only their economic function but also serve political purposes. As a result, fiscal discipline may be impaired.

The growth of deficits and debts due to too-generous fiscal policy has increased interest in so-called fiscal rules. The fixed rules and limits are set with the aim of bringing public finances under control and reducing the influence of the political cycle.

Fiscal rules may concern revenues, expenditures, a budget balance or debt. In principle, these rules may be substituted with one another. Generally, only one rule is binding, while other targets are indicative. This applies also to the Czech Republic.

4.2 Fiscal rules in the Czech Republic

Fiscal rules that regulate the regime for carrying out fiscal policy were incorporated into the budgetary rules as part of the 2003 reform of public finances. The institution of fiscal targeting and derived medium-term expenditure frameworks was introduced. Fiscal targeting and medium-term expenditure frameworks are prepared for the next three years. By setting the fiscal target, the government determines the trajectory of the future development in the balance of public finances and, at the same time, declares its responsibility for public finances, their health and sustainability. In deriving medium-term expenditure frameworks, the government determines such expenditure limits as will allow it to achieve its fiscal target.

Principle of fiscal targeting and medium-term expenditure frameworks

The government sets its targets in the form of a balance of public budgets as percentages of GDP for the next three years on a rolling basis (i.e. each year the three-year horizon moves ahead by one year).

Nevertheless, the government may influence only a part of the public budget balances. For that reason, the planned balance will be broken down into the planned balances for the individual parts of the public budgets and the balances of the state budget and state funds (i.e. those budgets directly controlled by the government) are determined.

To define the needed active government measures, the autonomous scenario is prepared (by its nature it is prepared to be conservative) and is based on the existing legal and institutional framework. This scenario determines the balance of the government finances in the absence of any new active steps.

On the basis of a GDP forecast, the absolute amount of the central government planned balance is calculated and compared to the autonomous scenario. The difference between the planned and autonomous balances determines the amount of the needed measures on the revenues side (increase in revenues) or on the expenditures side (decrease of expenditures).

After taking into account the active measures on the revenues side, the central government revenues forecast is calculated from which the planned absolute balance of the central government is substracted. Based on the difference between the revenues and balances, while accounting for the expected inflation, the medium-term expenditure frameworks (“ceilings”) are set in current prices for the entire planning period (hereinafter referred to as the “MTEF”).

In accordance with the fiscal targeting principle, MTEFs are prepared for the next three years on a rolling basis and are binding upon the government. Based on the total MTEF, and according to the government’s priorities, the MTEF will be divided into binding expenditure limits for the various chapters of the state budget and state funds for the respective years.

The government may change the MTEF for the originally second and third years when a state budget bill is introduced. Nevertheless, this is possible only in defined cases, such as a change in budgetary tax rating, change in expenditures financed by EU funds, significant deviations from the macroeconomic forecast and exceptional circumstances (e.g. natural disasters). These cases are stipulated by Act No. 218/2000 Coll. on budgetary rules.

Fiscal policy has a stabilising function – the main economic reason for the expenditure frameworks is that they counteract the economic cycles. If GDP growth is lower than expected, one of the consequences will be lower tax collections and, under given expenditure limits, a higher deficit. By contrast, if GDP growth is higher than expected, the tax collection will be higher, which, under given expenditures, will result in a lower deficit. The deficit amount thus adapts to the economic cycle and counteracts it. At the same time, to ensure that the fiscal targeting and MTEF work as stabilisers, it is obvious that the rule for the expenditure volume must be binding while the target in the form of the balance must play only an indicative role.

Along with the state budget bill, the government introduces the proposal of the total MTEF, both of which are based on the fiscal targets for the respective period, and it is then responsible only for the total MTEF. MTEFs are approved by a resolution of the Chamber of Deputies of the Parliament. On the contrary, due to the reasons mentioned above, the fiscal target is approved as a source parameter only by the government. The government is obliged to give reasons regarding any extraordinary deviations from the approved MTEF to the Chamber of Deputies and to have these approved.

4.3 Functioning of medium-term expenditure frameworks to date

To evaluate the functioning of the institute of fiscal targeting and MTEFs to date, it is crucial to adhere to the MTEF, because these frameworks are binding while the budget balances are not. An evaluation of the MTEFs is given in the following table.

Table 4-1: Expenditure frameworks in 2003-2007 (national fiscal targeting methodology, bn CZK)

		2005	2006	2007	2008	2009
2003	Approved Expenditure Framework	937.7	966.3	-	-	-
2004	Approved Expenditure Framework	938.4	963.9	1001.3	-	-
	Adjustments Permitted by Law	0.0	0.0	-	-	-
	Overrun	**0.7**	**-2.4**	x	x	x
2005	Approved Expenditure Framework	-	994.0	975.0	1011.9	-
	Adjustments Permitted by Law	-	5.7	-46.7	-	-
	Overrun	x	**24.4**	**20.4**	x	x
2006	Approved Expenditure Framework	-	-	1095.2	1070.7	1112.6
	Adjustments Permitted by Law	-	-	63.6	2.0	-
	Overrun	x	x	**56.6**	**56.8**	x
2007	Approved Expenditure Framework	-	-	-	1031.8	1053.8
	Adjustments Permitted by Law	-	-	-	.	.
	Overrun	x	x	x	**-38.9**	**-58.8**

Table 4-1 shows that MTEFs were not really adhered to in the past. An overrun here actually means an increase (if the figure is positive) of expenditure frameworks over allowed adjustments.

MTEFs are prepared for the current fiscal year and the two following years. Each following year, the MTEF projection will shift one year ahead and adjustments permitted by law will be considered for the two years already projected. If an expenditure framework is increased more than the adjustments permitted by law, this means violation of the original MTEF.[7]

In 2004, fulfilment of the approved expenditure frameworks was still relatively successful. In September 2004, a budget was prepared exceeding the approved expenditure framework by only CZK 0.7 bn. The fiscal outlook for 2006 even ended with a result CZK 2.4 bn better than was the original plan.

On the contrary, in 2005 the expenditure framework in the draft budget was increased in total by CZK 30.1 bn, of which only CZK 5.7 bn was an approved increase, and thus CZK 24.4 bn represents the overrun of the previously determined limit. In the 2007 fiscal outlook, an approved adjustment was made, i.e. the expenditure framework was reduced by CZK 46.7 bn, however the actually projected expenditures fell by only CZK 26.3 bn. The overrun of the expenditure framework was then CZK 20.4 bn.

With respect to adherence to the expenditure frameworks, the year 2006 was the poorest so far. The approved increase of the expenditure framework for 2007 was CZK 63.6 bn, and the actual increase in the draft national budget for 2007 is CZK 120.2 bn. The expenditure limits overrun is CZK 56.6 bn. In the fiscal outlook for 2008, the projected expenditures anticipate an additional increase by another CZK 56.8 bn.

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[7] Specifically, frameworks for the 2005 fiscal year and the two following years, 2006 and 2007, were approved in 2004. In 2005, the approved adjustment for 2006 amounted to CZK 5.7 bn, so that adhering to the previous expenditure framework would mean that the 2006 expenditure framework should be approved as CZK 969.6 bn (i.e. 963.9 + 5.7). The newly approved MTEF was CZK 994.0 bn, which caused the framework to be overrun by CZK 24.4 bn.

In 2007, new expenditure frameworks were approved in accordance with the government's policy declaration and a different fiscal target based on the declaration. The expenditure framework was reduced by CZK 38.9 bn for 2008 and by 58.8 bn for 2009.

4.4 Evaluating the concept and its problems

Introducing the institution of fiscal targeting and MTEF is undoubtedly an advance in a positive direction. This modern regime of executing fiscal policy contributes to reducing political influence on public finances. It is appropriate to recognise the fact that the government deficits fell after introducing the fiscal targeting regime. Nevertheless, this development must be evaluated cautiously for the time being, because reduction of the deficits was given particularly by the impacts of other favourable factors. Moreover, the established frameworks were not adhered to successfully in the previous two years.

At present, we can identify three main problems with the institution of fiscal targeting and MTEF and to which we must draw attention:

- Fiscal targets and the MTEF concern only a narrow area of public budgets – the state budget and the state funds. A similar mechanism should be introduced for other public budgets as well, such as for municipal government budgets.
- No sanction mechanism. The government is responsible for MTEF fulfilment to the Chamber of Deputies of the Parliament, but no sanction mechanism is defined for when these are violated.
- So far, little political, media or public attention has been paid to evaluating fiscal rules. The state budget balance remains the most observed parameter of public finances, and this balance has, for many reasons, a limited ability to inform on the economic status of public finances.

4.5 EU fiscal rules

By its accession to the European Union in 2004, the Czech Republic also entered into the EU system of fiscal rules. We are not a full member of the common economic and currency union so far (and thus do not have the euro). Nevertheless, regarding the fact that upon accession we undertook to adopt the euro, at present we only have a temporary exemption, and thus we are subject to the majority of duties resulting from the fiscal rules stated below. At the same time, the EU rules do not replace the national fiscal rules, but they should complement one another.

The basic and clearly best known EU fiscal rules in this country are included in the Maastricht Treaty, signed in 1993, which determines the reference limits for the government deficit amounting to 3% of GDP and the government debt amounting to 60% of GDP (Article 104). However, these limits do not by any means represent all the EU fiscal rules. As stated below, it is not sufficient only to meet these two criteria.

For smooth launching and subsequent functioning of the eurozone, the member states agreed in 1997, in addition to the Maastricht Treaty, that ensuring budget discipline was of essential importance and thus they concluded the so-called Stability and Growth Pact. In this Pact, they undertook to achieve budget surpluses or at least a balanced or nearly balanced budget in the medium-term horizon (about 3–5 years). The Pact did not change the basic requirements for adoption of the euro, nevertheless it specified preventive and sanction mechanisms for coordination of the economic and fiscal policies so that neither potential high national budgets deficits nor high public debts may threaten the euro's stability or increase inflation in the eurozone. The Pact thus covered the so-called "free-rider" issue. Adhering to these rules is monitored by multilateral supervision, i.e. by the European Commission and the other member states through the Council of Ministers of Finances and Economy (ECOFIN).

Reform of the Stability and Growth Pact

At the time of signing the Pact, its main principles were the limits for general government deficits of 3% of GDP, and for government debts of 60% of GDP, along with the requirement for public budget finances that are balanced or in surplus on a long-term basis. Such established rules were fairly criticised for several reasons. First of all, the system lacked any institutions for conducting preventive operations. A member state could be exposed to effective pressure only at the time of an excessive deficit's occurrence, by which time its quick correction would usually be already very costly. Moreover, the original rules did not take sufficient account of the cyclical character of economies' development or the influence of the economic cycle on the public budgets balance. If the countries reported a deficit approaching the 3% limit in a period of economic growth, they fell into an excessive deficit in the period of economic slowdown, when, however, the fiscal consolidation aimed at correcting such a deficit was economically inappropriate. Finally, let us mention the criticism of the unnecessarily strict requirement for a balanced or surplus government balance, which, moreover, ignored very different parameters of public finances in various countries.

The failure of the Pact in its original form led to discussions by numerous member states in the first half of this decade regarding its effectiveness in that form. In 2005, the intensive debate led to the Pact's reform, which aims to eliminate the aforementioned defects. The aims of the changes were to strengthen the preventive power of the rules, to take account of the cyclic character of fiscal development, and to consider the different initial parameters of individual countries.

At present, the Pact includes the resolution of the Council of Europe from Amsterdam in 1997, the ECOFIN Council's report on "Improving the Implementation of the Stability and Growth Pact" dated 2005, and two resolutions specifying the basic policies and measures (one on the budget discipline control and coordination of economic policies and the other on application of a procedure for reducing an excessive deficit – the so-called Excessive Deficit Procedure).

In addition, the Pact enables the Council to sanction those eurozone countries that are not able to adopt appropriate policies to reduce excessive deficits. At first, the punishment is in the form of an interest-free deposit with EU institutions, but if the excessive deficit is not corrected in the course of two years such deposit may be transformed into a non-refundable penalty.

Stabilisation and Convergence programmes

The supervision over the member states' success or failure in adhering to the Pact's principles is carried out each year through detailed evaluation of updated Stabilisation Programmes. States which have not yet introduced the euro submit the so-called Convergence Programmes.

The basic target of the rules is certainly healthy public finances – i.e. a balanced or nearly balanced budget and keeping the country's indebtedness sustainable on a long-term basis. To achieve this status, the member states have laid down the following auxiliary objectives.

Medium-term objective (MTO)

Within its Pact review, each country has laid down its individual medium-term fiscal target reflecting both the growth potential of the country and its indebtedness level. For the Czech Republic, this target for the government balance comes to -1.0% of GDP, which should be achieved in 2013 according to the latest update of the Czech Convergence Programme. At present, there is a discussion in the EU on how to include in this target the so-called implicit liabilities, i.e. long-term obligations of public finances, and especially in the form of the future old-age pensions and other expenditures depending on the age structure of the population. This will mean even stricter targets particularly for those countries – such as the Czech Republic – which have a problem with the population's ageing and the long-term non-sustainability of public finances.

Minimum fiscal effort

The Pact also determines that until the member states achieve their medium-term targets, they must consolidate their public budgets and improve their fiscal positions at least by a half percent of GDP each year (less the economic cycle influence and excluding one-off and extraordinary measures). In economically good times, the member states, then, have to try to consolidate more and so create a reserve for worse times. Any revenues beyond the expectations should be used to reduce the deficit. Deviation from this path to the medium-term fiscal target is only possible if the principal structural reforms (e.g. pension reform) are carried out, bringing immediate negative impacts but, from a long-term point of view, improving the state of public finances.

The countries that have achieved their medium-term targets already should let automatic stabilisers act and avoid pro-cyclical policies (i.e. in particular, reducing taxes and increasing government expenditures at a time of cyclical growth).

Safety margin

For cases of unfavourable economic development, the member states have determined a so-called safety margin from the reference 3% limit. It represents a certain margin, respecting which will ensure that no deficits over 3% of GDP[8] may occur even in a period of economic decline. For the Czech Republic, this margin is calculated as 1.4% of GDP. This means that the minimum limit of the budget balance (the minimum benchmark) is -1.6% of GDP, ensuring that the Czech Republic will not fall beneath 3% of GDP again (i.e. into the Excessive Deficit Procedure).

If any of the member states does not meet these rules or if a significant deviation from the medium-term target or from the path to its achievement has been identified, the Council may, in its annual evaluation, recommend upon what the concerned country should focus (a so-called early warning).

The parts of the Pact described thus far are referred to as the preventive portion. The other branch includes the so-called sanctions parts and deals with the progress of the Excessive Deficit Procedure (i.e. for the situation in which the concerned country has exceeded or will exceed the reference 3% limit of the government deficit or the 60% limit of the government debt).

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[8] In determining the safety margin, no extraordinary circumstances are considered that would lead to a significant decline in the economic output.

Excessive Deficit Procedure

This Procedure was launched with the Czech Republic very soon after its accession to the EU in 2004, and, regarding its special circumstances (as a transforming country), it was given a four-year term to correct the excessive deficits. However, the standard procedure is different. An excessive deficit must usually be corrected within one year after it is identified.

Upon the Procedure's initiation, the Council issues a recommendation first, and the member state has a six-month period for submitting measures that will lead to correcting of this deficit. If such measures are ineffective or implemented insufficiently, the Council may issue another call in which specific measures are established for the concerned country to adopt to correct the situation. At the same time, so-called intensified budget supervision can occur, wherein the member state is obliged to provide regular information according to a schedule agreed in advance. If even then the member state does not meet the recommendation, the Council may impose sanctions that may become stricter after two years.

The final stage is different for those member states outside the eurozone, because they are not subject to the intensified budget supervision. "Only" a decision on suspending drawing funds from the Cohesion Fund may be imposed as a sanction.

To complete the Procedure successfully, it is important to remove the excessive deficit in a credible and sustainable manner. Therefore the measures cannot be one-off or non-systematic ones. The expected future development and the fiscal strategy are evaluated as well.

Operation of the rules

Two rounds of evaluating the member states' programmes have taken place since the reform of the Pact, and the general feeling on EU soil is that, while the sanctions part of the Pact more or less works (however against a background of thus far good economic times), the preventive mechanisms are rather lagging behind.

This year's evaluation showed that the member states are only rather little taking advantage of the current favourable economic times for the necessary consolidation and that the average deficits reduction is under the required minimum. Moreover, those countries that have not yet achieved their medium-term targets and which are not in the Excessive Deficit Procedure allowed their fiscal positions to deteriorate last year.

That is to say that, in the future, we may expect a discussion at the EU level on how to strengthen the preventive part of the Stability and Growth Pact.

5 Annex of tables – general government in the ESA 95 methodology

Data for government revenues and expenditures are consolidated at the appropriate level. The consolidation represents the exclusion of mutual flows of interest, and of current and capital transfers within one subsector as well as among the individual subsectors of the general government.

5.1 Revenues

Table 5-1: General government revenue

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total revenue	*bill. CZK*	**660.8**	**713.6**	**761.7**	**802.3**	**833.9**	**911.4**	**974.4**	**1049.4**	**1154.7**	**1201.4**	**1267.1**
	prev.year=100	109.8	108.0	106.7	105.3	103.9	109.3	106.9	107.7	110.0	104.0	105.5
Current taxes on income, wealth, etc.	*bill. CZK*	**140.5**	**160.1**	**165.6**	**176.1**	**181.4**	**206.8**	**223.8**	**247.4**	**271.0**	**274.8**	**280.9**
	prev.year=100	100.1	114.0	103.4	106.3	103.1	114.0	108.3	110.5	109.5	101.4	102.2
Social contributions[1)]	*bill. CZK*	**239.8**	**264.8**	**281.7**	**292.7**	**312.0**	**335.0**	**367.4**	**388.9**	**419.4**	**448.4**	**481.8**
	prev.year=100	113.5	110.4	106.4	103.9	106.6	107.4	109.7	105.8	107.8	106.9	107.4
Taxes on production and imports[2)]	*bill. CZK*	**203.6**	**208.8**	**218.9**	**240.3**	**247.9**	**258.0**	**266.7**	**285.4**	**326.8**	**344.0**	**352.2**
	prev.year=100	113.3	102.5	104.8	109.8	103.2	104.1	103.4	107.0	114.5	105.3	102.4
Capital taxes[3)]	*bill. CZK*	**0.5**	**0.6**	**0.6**	**0.5**	**0.6**	**0.7**	**0.7**	**0.9**	**0.6**	**0.7**	**0.7**
	prev.year=100	118.6	123.0	96.5	96.7	109.7	117.0	108.9	115.6	71.9	118.5	101.4
Property income	*bill. CZK*	**13.8**	**15.6**	**15.7**	**12.8**	**18.3**	**26.2**	**29.8**	**24.5**	**23.2**	**21.2**	**25.8**
	prev.year=100	87.2	113.0	100.8	81.2	143.4	142.8	113.9	82.3	94.5	91.6	121.6
Interest	*bill. CZK*	**11.3**	**12.3**	**13.1**	**9.9**	**15.0**	**15.4**	**22.0**	**17.2**	**14.2**	**12.6**	**12.8**
	prev.year=100	107.1	109.4	106.1	76.1	151.0	102.5	143.1	78.1	82.5	88.5	101.6
Other property income	*bill. CZK*	**2.6**	**3.3**	**2.7**	**2.8**	**3.3**	**10.8**	**7.8**	**7.3**	**9.0**	**8.7**	**13.0**
	prev.year=100	47.8	128.9	81.0	106.6	116.7	325.2	72.4	93.9	122.7	96.4	150.6
Sales[4)]	*bill. CZK*	**47.1**	**47.2**	**58.2**	**56.4**	**58.3**	**63.0**	**66.4**	**75.4**	**75.2**	**77.6**	**79.7**
	prev.year=100	112.3	100.2	123.2	96.9	103.5	108.0	105.5	113.4	99.8	103.1	102.7
Other current transfers and subsidies	*bill. CZK*	**12.7**	**15.9**	**19.5**	**22.1**	**12.4**	**15.8**	**16.5**	**21.3**	**28.6**	**26.3**	**28.0**
	prev.year=100	269.0	124.9	122.6	113.5	56.2	126.8	104.2	129.7	134.2	91.8	106.3
Investment grants	*bill. CZK*	**-**	**0.0**	**0.0**	**0.0**	**0.1**	**0.5**	**0.9**	**2.8**	**3.1**	**4.7**	**14.0**
	prev.year=100	x	x	314.3	145.5	225.0	754.2	171.8	301.5	110.1	151.6	298.1
Other capital transfers	*bill. CZK*	**2.8**	**0.7**	**1.5**	**1.4**	**2.9**	**5.5**	**2.1**	**2.8**	**6.8**	**3.6**	**4.1**
	prev.year=100	36.7	24.4	227.0	92.5	206.2	186.2	37.8	134.8	243.3	53.8	112.6

[1)] *Compulsory and voluntary payments of employers´ (on behalf of employees´), employees´, self-employed and non-employed persons to social security funds and insurance enterprises.*

[2)] *Compulsory, unrequited payments, in cash or in kind, which are levied by general government, in respect of the production and importation of goods and services, the employment of labour, the ownership or use of land, buildings or other assets used in production.(for example VAT, excises etc.)*

[3)] *Taxes levied at irregular and very infrequent intervals on the values of the assets or net worth owned by institutional units or on the values of assets transferred between institutional units as a result of legacies, gifts or other transfers.*

[4)] *Consists of market output, output produced for own final use and payments for other non-market output.*

Table 5-2: General government revenue - ratios to GDP

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total revenue	*(in % GDP)*	39.3	39.4	38.2	38.6	38.1	38.7	39.5	40.7	41.5	40.4	39.5
Current taxes on income, wealth, etc.	*(in % GDP)*	8.3	8.8	8.3	8.5	8.3	8.8	9.1	9.6	9.7	9.3	8.8
Social contributions	*(in % GDP)*	14.2	14.6	14.1	14.1	14.2	14.2	14.9	15.1	15.1	15.1	15.0
Taxes on production and imports	*(in % GDP)*	12.1	11.5	11.0	11.5	11.3	11.0	10.8	11.1	11.7	11.6	11.0
Capital taxes	*(in % GDP)*	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Property income	*(in % GDP)*	0.8	0.9	0.8	0.6	0.8	1.1	1.2	1.0	0.8	0.7	0.8
Interest	*(in % GDP)*	0.7	0.7	0.7	0.5	0.7	0.7	0.9	0.7	0.5	0.4	0.4
Other property income	*(in % GDP)*	0.2	0.2	0.1	0.1	0.2	0.5	0.3	0.3	0.3	0.3	0.4
Sales	*(in % GDP)*	2.8	2.6	2.9	2.7	2.7	2.7	2.7	2.9	2.7	2.6	2.5
Other current transfers and subsidies	*(in % GDP)*	0.8	0.9	1.0	1.1	0.6	0.7	0.7	0.8	1.0	0.9	0.9
Investment grants	*(in % GDP)*	-	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.1	0.2	0.4
Other capital transfers	*(in % GDP)*	0.2	0.0	0.1	0.1	0.1	0.2	0.1	0.1	0.2	0.1	0.1

Table 5-3: General government tax revenue and social contributions

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Taxes and social contributions	*bill. CZK*	**584.3**	**634.2**	**666.7**	**709.6**	**741.8**	**800.5**	**858.7**	**922.6**	**1017.8**	**1068.0**	**1115.6**
	prev.year=100	109.9	108.5	105.1	106.4	104.6	107.9	107.3	107.4	110.3	104.9	104.5
Current taxes on income, wealth, etc.	*bill. CZK*	**140.5**	**160.1**	**165.6**	**176.1**	**181.4**	**206.8**	**223.8**	**247.4**	**271.0**	**274.8**	**280.9**
	prev.year=100	100.1	114.0	103.4	106.3	103.1	114.0	108.3	110.5	109.5	101.4	102.2
Tax on individual or household income incl. holding gains	*bill. CZK*	**80.2**	**87.4**	**94.0**	**93.0**	**99.7**	**106.2**	**114.9**	**125.3**	**134.8**	**136.1**	**137.5**
	prev.year=100	114.0	108.9	107.6	98.9	107.2	106.5	108.2	109.0	107.5	101.0	101.0
Taxes on the income or profits of corporations incl. holding gains	*bill. CZK*	**56.5**	**69.4**	**67.5**	**79.5**	**76.2**	**96.3**	**105.7**	**118.0**	**132.0**	**133.8**	**138.3**
	prev.year=100	84.0	122.7	97.3	117.8	95.9	126.4	109.8	111.6	111.9	101.3	103.4
Levy on lottery revenue	*bill. CZK*	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**0.5**	**0.6**	**0.6**	**0.7**
	prev.year=100	x	x	x	x	x	x	x	x	117.4	112.5	110.0
Other current taxes	*bill. CZK*	**3.8**	**3.4**	**4.2**	**3.6**	**5.6**	**4.3**	**3.2**	**3.6**	**3.7**	**4.3**	**4.5**
	prev.year=100	141.6	91.0	122.2	87.0	153.6	77.6	74.0	112.6	101.6	117.8	104.2
Social contributions	*bill. CZK*	**239.8**	**264.8**	**281.7**	**292.7**	**312.0**	**335.0**	**367.4**	**388.9**	**419.4**	**448.4**	**481.8**
	prev.year=100	113.5	110.4	106.4	103.9	106.6	107.4	109.7	105.8	107.8	106.9	107.4
Actual social contributions	*bill. CZK*	**239.7**	**264.7**	**281.5**	**292.5**	**311.5**	**334.8**	**367.2**	**388.6**	**419.0**	**448.0**	**481.3**
	prev.year=100	113.6	110.4	106.4	103.9	106.5	107.5	109.7	105.8	107.8	106.9	107.4
Employers' actual social contributions	*bill. CZK*	**167.6**	**185.0**	**197.0**	**204.6**	**216.9**	**233.2**	**255.9**	**270.7**	**289.8**	**308.7**	**332.3**
	prev.year=100	115.6	110.4	106.5	103.8	106.0	107.5	109.7	105.8	107.0	106.5	107.7
Employees' social contributions	*bill. CZK*	**59.9**	**65.9**	**70.2**	**73.0**	**77.3**	**82.7**	**89.6**	**94.9**	**101.3**	**108.3**	**116.6**
	prev.year=100	109.9	110.0	106.4	104.0	105.9	107.0	108.4	105.9	106.8	106.9	107.6
Social contributions by self- and non-employed persons	*bill. CZK*	**12.2**	**13.7**	**14.3**	**14.9**	**17.3**	**18.9**	**21.7**	**23.0**	**27.9**	**31.0**	**32.4**
	prev.year=100	105.1	112.5	104.4	104.3	115.9	109.1	114.9	106.1	121.2	111.1	104.6
Imputed social contributions	*bill. CZK*	**0.1**	**0.1**	**0.2**	**0.2**	**0.4**	**0.2**	**0.3**	**0.3**	**0.4**	**0.4**	**0.4**
	prev.year=100	69.9	95.3	197.6	124.7	209.4	57.9	102.4	117.5	136.6	98.5	106.5
Taxes on production and imports	*bill. CZK*	**203.6**	**208.8**	**218.9**	**240.3**	**247.9**	**258.0**	**266.7**	**285.4**	**326.8**	**344.0**	**352.2**
	prev.year=100	113.3	102.5	104.8	109.8	103.2	104.1	103.4	107.0	114.5	105.3	102.4
Taxes on products[1)]	*bill. CZK*	**190.4**	**197.0**	**206.8**	**227.0**	**234.2**	**244.9**	**253.6**	**271.7**	**313.1**	**330.4**	**338.1**
	prev.year=100	114.0	103.5	105.0	109.8	103.1	104.6	103.5	107.2	115.2	105.5	102.3
VAT	*bill. CZK*	**107.6**	**114.5**	**121.1**	**136.5**	**141.3**	**149.3**	**155.1**	**164.3**	**202.1**	**210.6**	**208.8**
	prev.year=100	117.3	106.4	105.8	112.8	103.5	105.6	103.9	105.9	123.0	104.2	99.2
Excises	*bill. CZK*	**58.0**	**60.9**	**64.4**	**71.4**	**71.4**	**76.8**	**79.5**	**87.5**	**99.2**	**110.5**	**119.5**
	prev.year=100	108.0	104.9	105.7	110.9	100.0	107.6	103.6	110.0	113.4	111.4	108.1
Other taxes on products[2)]	*bill. CZK*	**24.8**	**21.6**	**21.3**	**19.2**	**21.5**	**18.9**	**18.9**	**20.0**	**11.8**	**9.2**	**9.8**
	prev.year=100	114.9	87.2	98.8	89.8	111.9	88.0	100.2	105.7	59.1	78.2	106.5
Other taxes on production[3)]	*bill. CZK*	**13.2**	**11.8**	**12.1**	**13.2**	**13.7**	**13.1**	**13.1**	**13.7**	**13.7**	**13.7**	**14.0**
	prev.year=100	103.6	89.2	102.7	109.1	103.8	95.1	100.6	104.2	100.0	99.8	102.7
Capital taxes	*bill. CZK*	**0.5**	**0.6**	**0.6**	**0.5**	**0.6**	**0.7**	**0.7**	**0.9**	**0.6**	**0.7**	**0.7**
	prev.year=100	118.6	123.0	96.5	96.7	109.7	117.0	108.9	115.6	71.9	118.5	101.4

[1)] *Taxes that are payable per unit of some good or service produced or transacted.*

[2)] *This item contains for example customs duty, taxes from financial and capital transaction, payments from entertainment, lottery taxes and other.*

[3)] *All taxes that enterprises incur as a result of engaging in production, independently of the quantity or value of the goods and services produced or sold (real estate tax, road tax, etc.).*

Table 5-4: General government tax revenue and social contributions - ratios to GDP

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Taxes and social contributions	*in % GDP*	**34.7**	**35.0**	**33.4**	**34.1**	**33.9**	**34.0**	**34.8**	**35.8**	**36.6**	**36.0**	**34.8**
Current taxes on income, wealth, etc.	*in % GDP*	8.3	8.8	8.3	8.5	8.3	8.8	9.1	9.6	9.7	9.3	8.8
Tax on individual or household income incl. holding gains	*in % GDP*	**4.8**	**4.8**	**4.7**	**4.5**	**4.6**	**4.5**	**4.7**	**4.9**	**4.8**	**4.6**	**4.3**
Taxes on the income or profits of corporations incl. holding gains	*in % GDP*	3.4	3.8	3.4	3.8	3.5	4.1	4.3	4.6	4.7	4.5	4.3
Levy on lottery revenue	*in % GDP*	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**0.0**	**0.0**	**0.0**	**0.0**
Other current taxes	*in % GDP*	0.2	0.2	0.2	0.2	0.3	0.2	0.1	0.1	0.1	0.1	0.1
Social contributions	*in % GDP*	**14.2**	**14.6**	**14.1**	**14.1**	**14.2**	**14.2**	**14.9**	**15.1**	**15.1**	**15.1**	**15.0**
Actual social contributions	*in % GDP*	14.2	14.6	14.1	14.1	14.2	14.2	14.9	15.1	15.1	15.1	15.0
Employers' actual social contributions	*in % GDP*	**10.0**	**10.2**	**9.9**	**9.8**	**9.9**	**9.9**	**10.4**	**10.5**	**10.4**	**10.4**	**10.4**
Employees' social contributions	*in % GDP*	3.6	3.6	3.5	3.5	3.5	3.5	3.6	3.7	3.6	3.6	3.6
Social contributions by self- and non-employed persons	*in % GDP*	**0.7**	**0.8**	**0.7**	**0.7**	**0.8**	**0.8**	**0.9**	**0.9**	**1.0**	**1.0**	**1.0**
Imputed social contributions	*in % GDP*	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Taxes on production and imports	*in % GDP*	**12.1**	**11.5**	**11.0**	**11.5**	**11.3**	**11.0**	**10.8**	**11.1**	**11.7**	**11.6**	**11.0**
Taxes on products	*in % GDP*	11.3	10.9	10.4	10.9	10.7	10.4	10.3	10.5	11.3	11.1	10.6
VAT	*in % GDP*	**6.4**	**6.3**	**6.1**	**6.6**	**6.5**	**6.3**	**6.3**	**6.4**	**7.3**	**7.1**	**6.5**
Excise taxes	*in % GDP*	3.4	3.4	3.2	3.4	3.3	3.3	3.2	3.4	3.6	3.7	3.7
Other taxes on products	*in % GDP*	**1.5**	**1.2**	**1.1**	**0.9**	**1.0**	**0.8**	**0.8**	**0.8**	**0.4**	**0.3**	**0.3**
Other taxes on production	*in % GDP*	0.8	0.7	0.6	0.6	0.6	0.6	0.5	0.5	0.5	0.5	0.4
Capital taxes	*in % GDP*	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

Table 5-5: Central government revenue

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total revenue	*bill. CZK*	**486.3**	**519.5**	**547.2**	**581.7**	**605.3**	**675.1**	**702.2**	**750.0**	**830.7**	**839.9**	**884.9**
	prev.year=100	108.6	106.8	105.3	106.3	104.1	111.5	104.0	106.8	110.8	101.1	105.3
Current taxes on income, wealth, etc.	*bill. CZK*	**77.1**	**88.6**	**91.3**	**93.8**	**98.5**	**154.1**	**160.1**	**176.9**	**194.3**	**183.1**	**187.3**
	prev.year=100	95.6	115.0	103.0	102.8	105.0	156.4	103.9	110.5	109.8	94.2	102.3
Social contributions	*bill. CZK*	**170.7**	**189.3**	**201.5**	**208.9**	**221.8**	**241.1**	**262.9**	**277.2**	**300.1**	**318.7**	**342.6**
	prev.year=100	112.9	110.9	106.4	103.7	106.2	108.7	109.0	105.5	108.3	106.2	107.5
Taxes on production and imports	*bill. CZK*	**198.7**	**203.7**	**213.5**	**234.9**	**242.0**	**221.5**	**224.2**	**240.3**	**271.8**	**274.0**	**282.4**
	prev.year=100	113.5	102.5	104.8	110.0	103.0	91.5	101.2	107.2	113.1	100.8	103.1
Capital taxes	*bill. CZK*	**0.5**	**0.6**	**0.6**	**0.5**	**0.6**	**0.7**	**0.7**	**0.9**	**0.6**	**0.7**	**0.7**
	prev.year=100	118.6	123.0	96.3	96.9	109.7	117.0	108.9	115.0	71.3	118.8	102.1
Property income	*bill. CZK*	**10.7**	**11.7**	**10.7**	**7.9**	**13.5**	**22.0**	**22.6**	**17.4**	**15.0**	**14.5**	**18.4**
	prev.year=100	78.2	108.8	92.1	73.2	171.3	163.0	102.9	77.2	86.1	96.4	126.9
Sales	*bill. CZK*	**17.4**	**14.6**	**14.6**	**17.6**	**18.1**	**21.2**	**22.2**	**25.7**	**25.0**	**26.5**	**27.6**
	prev.year=100	111.2	83.9	99.5	121.1	102.8	117.2	104.6	115.5	97.4	105.9	104.4
Other revenue	*bill. CZK*	**11.3**	**11.0**	**15.1**	**18.1**	**10.9**	**14.6**	**9.5**	**11.6**	**23.8**	**22.5**	**25.9**
	prev.year=100	101.3	97.4	137.3	120.2	60.1	134.2	65.2	122.0	205.2	94.5	114.9

Table 5-6: Local government revenue

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total revenue	*bill. CZK*	**245.0**	**166.1**	**203.0**	**192.1**	**200.1**	**228.3**	**260.0**	**328.7**	**350.3**	**351.9**	**365.6**
	prev.year=100	145.8	67.8	122.2	94.6	104.2	114.1	113.9	126.4	106.6	100.4	103.9
Current taxes on income, wealth, etc	*bill. CZK*	**63.4**	**71.5**	**74.4**	**82.2**	**82.9**	**52.7**	**63.8**	**70.5**	**76.6**	**91.7**	**93.6**
	prev.year=100	106.3	112.8	104.0	110.6	100.9	63.5	121.1	110.5	108.8	119.6	102.1
Social contributions	*bill. CZK*	**0.0**	**0.0**	**0.1**	**0.1**	**0.0**	**0.1**	**0.0**	**0.1**	**0.1**	**0.1**	**0.1**
	prev.year=100	95.8	73.9	197.1	100.0	62.7	190.5	60.0	104.2	120.0	121.7	86.3
Taxes on production and imports	*bill. CZK*	**4.9**	**5.0**	**5.3**	**5.3**	**5.9**	**36.5**	**42.5**	**45.1**	**55.0**	**70.0**	**69.8**
	prev.year=100	105.6	102.5	105.9	100.0	110.1	620.0	116.3	106.2	121.8	127.4	99.7
Capital taxes	*bill. CZK*	**-**	**-**	**0.0**	**-**	**-**	**-**	**-**	**0.0**	**0.0**	**0.0**	**0.0**
	prev.year=100	x	x	x	0.0	x	x	x	x	180.0	100.0	44.4
Property income	*bill. CZK*	**2.8**	**3.6**	**4.5**	**4.7**	**4.5**	**3.7**	**6.9**	**6.8**	**8.0**	**6.5**	**7.0**
	prev.year=100	148.5	126.7	125.9	102.8	95.9	82.0	187.2	99.7	116.6	82.2	107.5
Sales	*bill. CZK*	**29.6**	**32.4**	**43.5**	**38.7**	**40.1**	**41.3**	**44.1**	**49.6**	**50.1**	**50.9**	**51.8**
	prev.year=100	113.7	109.5	134.0	88.9	103.8	103.0	106.6	112.5	101.0	101.7	101.8
Other revenue	*bill. CZK*	**144.2**	**53.5**	**75.2**	**61.1**	**66.7**	**94.0**	**102.8**	**156.6**	**160.6**	**132.6**	**143.2**
	prev.year=100	190.5	37.1	140.7	81.2	109.1	141.0	109.4	152.3	102.5	82.6	108.0

Table 5-7: Social security funds revenue

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total revenue	*bill. CZK*	**85.8**	**95.1**	**104.9**	**112.5**	**119.4**	**127.4**	**138.4**	**149.1**	**161.6**	**171.8**	**188.4**
	prev.year=100	116.3	110.8	110.3	107.3	106.1	106.7	108.6	107.8	108.3	106.4	109.7
Current taxes on income, wealth, etc	*bill. CZK*	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
	prev.year=100	x	x	x	x	x	x	x	x	x	x	x
Social contributions	*bill. CZK*	**69.0**	**75.4**	**80.1**	**83.8**	**90.1**	**93.9**	**104.5**	**111.7**	**119.2**	**129.7**	**139.1**
	prev.year=100	115.1	109.2	106.3	104.5	107.6	104.2	111.3	106.8	106.8	108.7	107.3
Taxes on production and imports	*bill. CZK*	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
	prev.year=100	x	x	x	x	x	x	x	x	x	x	x
Capital taxes	*bill. CZK*	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
	prev.year=100	x	x	x	x	x	x	x	x	x	x	x
Property income	*bill. CZK*	**0.3**	**0.4**	**0.5**	**0.3**	**0.4**	**0.6**	**0.4**	**0.3**	**0.3**	**0.3**	**0.5**
	prev.year=100	113.2	135.8	147.8	54.9	147.9	128.2	74.9	73.7	95.1	106.5	157.1
Sales	*bill. CZK*	**0.0**	**0.1**	**0.1**	**0.1**	**0.1**	**0.4**	**0.1**	**0.1**	**0.2**	**0.2**	**0.2**
	prev.year=100	20.1	245.2	108.7	58.9	100.0	609.1	34.8	75.7	145.3	110.4	101.2
Other revenue	*bill. CZK*	**16.5**	**19.2**	**24.1**	**28.4**	**28.7**	**32.5**	**33.3**	**37.1**	**41.9**	**41.7**	**48.7**
	prev.year=100	123.6	116.7	125.4	117.9	101.2	113.2	102.3	111.3	113.0	99.5	116.9

5.2 Expenditures

Table 5-8: General government expenditure

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total expenditure	*bill. CZK*	**716.6**	**782.5**	**861.7**	**879.6**	**915.4**	**1046.5**	**1141.2**	**1219.5**	**1235.1**	**1306.0**	**1361.1**
	prev.year=100	89.7	109.2	110.1	102.1	104.1	114.3	109.1	106.9	101.3	105.7	104.2
Final consumption expenditure	*bill. CZK*	**340.4**	**379.3**	**399.7**	**440.6**	**460.9**	**496.7**	**549.5**	**603.2**	**624.2**	**661.3**	**687.7**
	prev.year=100	111.1	111.4	105.4	110.2	104.6	107.8	110.6	109.8	103.5	105.9	104.0
Collective consumption[1)]	*bill. CZK*	**157.0**	**181.4**	**187.4**	**217.3**	**232.1**	**241.7**	**271.2**	**305.6**	**299.1**	**333.7**	**345.0**
	prev.year=100	107.2	115.5	103.3	116.0	106.8	104.2	112.2	112.7	97.9	111.5	103.4
Individual consumption	*bill. CZK*	**183.4**	**198.0**	**212.3**	**223.3**	**228.9**	**254.9**	**278.3**	**297.6**	**325.1**	**327.6**	**342.7**
	prev.year=100	114.7	107.9	107.3	105.2	102.5	111.4	109.2	106.9	109.2	100.8	104.6
Social transfers in kind[2)]	*bill. CZK*	**88.4**	**95.2**	**104.8**	**111.1**	**115.4**	**127.5**	**142.1**	**150.2**	**160.7**	**167.4**	**171.2**
	prev.year=100	118.0	107.7	110.1	106.0	103.9	110.4	111.5	105.7	107.0	104.2	102.3
Transfers of individual non-market goods or services[3)]	*bill. CZK*	**95.1**	**102.8**	**107.6**	**112.2**	**113.5**	**127.5**	**136.2**	**147.3**	**164.3**	**160.2**	**171.5**
	prev.year=100	111.8	108.1	104.7	104.3	101.1	112.3	106.9	108.2	111.5	97.5	107.0
Social benefits other than social transfers in kind	*bill. CZK*	**183.3**	**208.1**	**225.6**	**243.8**	**263.9**	**280.5**	**305.1**	**315.6**	**328.5**	**342.7**	**364.4**
	prev.year=100	116.3	113.5	108.4	108.0	108.3	106.3	108.8	103.4	104.1	104.3	106.4
Interest	*bill. CZK*	**20.4**	**20.3**	**23.2**	**21.2**	**18.4**	**23.8**	**30.5**	**29.3**	**32.6**	**34.4**	**35.4**
	prev.year=100	134.4	99.7	114.1	91.6	86.7	129.5	128.2	95.9	111.2	105.6	102.9
Subsidies	*bill. CZK*	**40.6**	**49.3**	**57.9**	**61.1**	**61.0**	**65.4**	**56.6**	**68.2**	**59.0**	**55.2**	**62.0**
	prev.year=100	96.7	121.5	117.5	105.5	99.8	107.3	86.5	120.6	86.5	93.6	112.3
Gross fixed capital formation	*bill. CZK*	**76.7**	**77.3**	**83.8**	**67.7**	**79.1**	**83.4**	**95.2**	**117.2**	**136.4**	**146.5**	**162.0**
	prev.year=100	99.5	100.8	108.4	80.8	116.9	105.4	114.2	123.1	116.4	107.4	110.6
Other expenditures	*bill. CZK*	**55.3**	**48.2**	**71.6**	**45.2**	**32.1**	**96.7**	**104.3**	**86.0**	**54.4**	**66.0**	**49.6**
	prev.year=100	27.6	87.2	148.5	63.2	71.0	301.0	107.8	82.4	63.3	121.2	75.2

1) Value of all services provided to all members of society or to specific groups, i.e. expenditure for public services, defence, security, justice, health protection, environment protection, research and development, infrastructure development.

2) Social benefits in kind are social transfers in kind intended to relieve the households from the financial burden of social risks or needs, i.e. payments from insurance enterprises to health care institution for services provided to households.

3) Goods or services provided to individual households free or at prices which are not economically significant, by non-market producers (education, health service, housing, culture, sport, etc.).

Table 5-9: General government expenditure - ratios to GDP

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total expenditure	*(in % GDP)*	42.6	43.2	43.2	42.3	41.8	44.5	46.3	47.3	44.4	44.0	42.5
Final consumption expenditure	*(in % GDP)*	20.2	20.9	20.0	21.2	21.1	21.1	22.3	23.4	22.4	22.3	21.5
Collective consumption	*(in % GDP)*	9.3	10.0	9.4	10.4	10.6	10.3	11.0	11.9	10.8	11.2	10.8
Individual consumption	*(in % GDP)*	10.9	10.9	10.6	10.7	10.5	10.8	11.3	11.5	11.7	11.0	10.7
Social transfers in kind	*(in % GDP)*	5.2	5.3	5.2	5.3	5.3	5.4	5.8	5.8	5.8	5.6	5.3
Transfers of individual non-market goods or services	*(in % GDP)*	5.6	5.7	5.4	5.4	5.2	5.4	5.5	5.7	5.9	5.4	5.4
Social benefits other than social transfers in kind	*(in % GDP)*	10.9	11.5	11.3	11.7	12.1	11.9	12.4	12.2	11.8	11.5	11.4
Interest	*(in % GDP)*	1.2	1.1	1.2	1.0	0.8	1.0	1.2	1.1	1.2	1.2	1.1
Subsidies	*(in % GDP)*	2.4	2.7	2.9	2.9	2.8	2.8	2.3	2.6	2.1	1.9	1.9
Gross fixed capital formation	*(in % GDP)*	4.6	4.3	4.2	3.3	3.6	3.5	3.9	4.5	4.9	4.9	5.1
Other expenditures	*(in % GDP)*	3.3	2.7	3.6	2.2	1.5	4.1	4.2	3.3	2.0	2.2	1.5

Table 5-10: General government expenditure

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total expenditure	*bill. CZK*	**716.6**	**782.5**	**861.7**	**879.6**	**915.4**	**1046.5**	**1141.2**	**1219.5**	**1235.1**	**1306.0**	**1361.1**
	prev.year=100	89.7	109.2	110.1	102.1	104.1	114.3	109.1	106.9	101.3	105.7	104.2
Compensation of employees	*bill. CZK*	**126.7**	**133.9**	**135.0**	**151.4**	**154.7**	**172.9**	**191.6**	**214.2**	**222.1**	**236.7**	**250.6**
	prev.year=100	117.6	105.6	100.9	112.1	102.2	111.8	110.8	111.8	103.7	106.6	105.9
Intermediate consumption	*bill. CZK*	**95.8**	**113.1**	**115.1**	**132.7**	**144.0**	**152.9**	**173.6**	**196.0**	**193.5**	**208.2**	**213.5**
	prev.year=100	98.9	118.1	101.8	115.3	108.5	106.2	113.5	112.9	98.7	107.6	102.5
Social benefits other than social transfers in kind[1]	*bill. CZK*	**183.3**	**208.1**	**225.6**	**243.8**	**263.9**	**280.5**	**305.1**	**315.6**	**328.5**	**342.7**	**364.4**
	prev.year=100	116.3	113.5	108.4	108.0	108.3	106.3	108.8	103.4	104.1	104.3	106.4
Social benefits in kind	*bill. CZK*	**88.4**	**95.2**	**104.8**	**111.1**	**115.4**	**127.5**	**142.1**	**150.2**	**160.7**	**167.4**	**171.2**
	prev.year=100	118.0	107.7	110.1	106.0	103.9	110.4	111.5	105.7	107.0	104.2	102.3
Property income	*bill. CZK*	**20.4**	**20.3**	**23.2**	**21.2**	**18.4**	**23.9**	**30.6**	**29.3**	**32.6**	**34.4**	**35.5**
	prev.year=100	134.4	99.8	114.1	91.6	86.8	129.3	128.2	95.9	111.2	105.6	103.0
Interest	*bill. CZK*	**20.4**	**20.3**	**23.2**	**21.2**	**18.4**	**23.8**	**30.5**	**29.3**	**32.6**	**34.4**	**35.4**
	prev.year=100	134.4	99.7	114.1	91.6	86.7	129.5	128.2	95.9	111.2	105.6	102.9
Other property income	*bill. CZK*	**-**	**0.0**	**0.0**	**0.0**	**0.1**	**0.0**	**0.1**	**0.0**	**0.1**	**0.1**	**0.1**
	prev.year=100	-	-	-	-	-	80.8	-	74.6	-	100.0	100.0
Subsidies	*bill. CZK*	**40.6**	**49.3**	**57.9**	**61.1**	**61.0**	**65.4**	**56.6**	**68.2**	**59.0**	**55.2**	**62.0**
	prev.year=100	96.7	121.5	117.5	105.5	99.8	107.3	86.5	120.6	86.5	93.6	112.3
Gross fixed capital formation	*bill. CZK*	**76.7**	**77.3**	**83.8**	**67.7**	**79.1**	**83.4**	**95.2**	**117.2**	**136.4**	**146.5**	**162.0**
	prev.year=100	99.5	100.8	108.4	80.8	116.9	105.4	114.2	123.1	116.4	107.4	110.6
Capital transfers[2]	*bill. CZK*	**50.1**	**72.4**	**92.8**	**77.7**	**57.6**	**127.5**	**120.2**	**98.4**	**70.5**	**71.1**	**56.9**
	prev.year=100	23.2	144.6	128.2	83.7	74.2	221.3	94.3	81.8	71.6	100.9	80.1
Investment grants[3]	*bill. CZK*	**18.9**	**18.7**	**19.1**	**22.4**	**25.9**	**27.5**	**36.9**	**35.2**	**35.1**	**33.8**	**36.8**
	prev.year=100	76.2	98.7	102.1	117.8	115.6	105.8	134.5	95.2	99.9	96.3	108.7
Other capital transfers	*bill. CZK*	**31.2**	**53.8**	**73.8**	**55.2**	**31.7**	**100.0**	**83.3**	**63.2**	**35.3**	**37.2**	**20.2**
	prev.year=100	16.3	172.5	137.3	74.8	57.4	315.8	83.2	75.9	55.9	105.4	54.1
Other expenditure	*bill. CZK*	**34.8**	**13.0**	**23.5**	**13.0**	**21.3**	**12.5**	**26.3**	**30.3**	**31.8**	**43.8**	**44.9**
	prev.year=100	301.1	37.3	181.5	55.1	164.3	58.9	209.5	115.4	104.8	137.9	102.6

[1] *Transfers to households, in cash or in kind, intended to relieve them from the financial burden of a number of risks or needs (for example sickness, disability, old age, unemployment, family etc.).*

[2] *Transactions of capital distribution, both in cash and in kind, which have no influence either on beneficiary´s ordinary income or these transaction´s payer but amount of their net property.*

[3] *Capital transfers in cash or in kind made by governments to other institutional units to finance all or part of the costs of their acquiring fixed assets.*

Table 5-11: General government expenditure - ratios to GDP

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total expenditure	*(in % GDP)*	42.6	43.2	43.2	42.3	41.8	44.5	46.3	47.3	44.4	44.0	42.5
Compensation of employees	*(in % GDP)*	7.5	7.4	6.8	7.3	7.1	7.4	7.8	8.3	8.0	8.0	7.8
Intermediate consumption	*(in % GDP)*	5.7	6.2	5.8	6.4	6.6	6.5	7.0	7.6	7.0	7.0	6.7
Social benefits other than social transfers in kind	*(in % GDP)*	10.9	11.5	11.3	11.7	12.1	11.9	12.4	12.2	11.8	11.5	11.4
Social benefits in kind	*(in % GDP)*	5.2	5.3	5.2	5.3	5.3	5.4	5.8	5.8	5.8	5.6	5.3
Property income	*(in % GDP)*	1.2	1.1	1.2	1.0	0.8	1.0	1.2	1.1	1.2	1.2	1.1
Interest	*(in % GDP)*	1.2	1.1	1.2	1.0	0.8	1.0	1.2	1.1	1.2	1.2	1.1
Other property income	*(in % GDP)*	-	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Subsidies	*(in % GDP)*	2.4	2.7	2.9	2.9	2.8	2.8	2.3	2.6	2.1	1.9	1.9
Gross fixed capital formation	*(in % GDP)*	4.6	4.3	4.2	3.3	3.6	3.5	3.9	4.5	4.9	4.9	5.1
Capital transfers	*(in % GDP)*	3.0	4.0	4.7	3.7	2.6	5.4	4.9	3.8	2.5	2.4	1.8
Investment grants	*(in % GDP)*	1.1	1.0	1.0	1.1	1.2	1.2	1.5	1.4	1.3	1.1	1.1
Other capital transfers	*(in % GDP)*	1.9	3.0	3.7	2.7	1.4	4.3	3.4	2.5	1.3	1.3	0.6
Other expenditure	*(in % GDP)*	2.1	0.7	1.2	0.6	1.0	0.5	1.1	1.2	1.1	1.5	1.4

Table 5-12: Central government expenditure

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total expenditure	*bill. CZK*	**577.9**	**574.7**	**652.9**	**660.5**	**681.5**	**799.8**	**853.1**	**904.3**	**908.3**	**946.3**	**984.6**
	prev.year=100	86.1	99.4	113.6	101.2	103.2	117.4	106.7	106.0	100.4	104.2	104.0
Compensation of employees	*bill. CZK*	**92.3**	**95.4**	**94.8**	**106.0**	**107.2**	**106.4**	**117.0**	**108.8**	**110.8**	**120.6**	**127.5**
	prev.year=100	114.0	103.4	99.4	111.8	101.1	99.3	109.9	93.0	101.9	108.8	105.7
Intermediate consumption	*bill. CZK*	**45.9**	**58.1**	**53.9**	**65.3**	**74.8**	**74.2**	**86.7**	**96.9**	**93.5**	**105.3**	**102.0**
	prev.year=100	88.6	126.7	92.7	121.3	114.4	99.3	116.8	111.8	96.5	112.6	96.9
Social benefits other than social transfers in kind	*bill. CZK*	**153.4**	**204.3**	**220.5**	**236.2**	**254.6**	**271.5**	**294.9**	**303.8**	**316.7**	**331.0**	**352.5**
	prev.year=100	100.4	133.2	107.9	107.1	107.8	106.6	108.6	103.0	104.2	104.5	106.5
Social benefits in kind	*bill. CZK*	**1.3**	**1.4**	**1.6**	**1.8**	**1.9**	**3.1**	**3.3**	**2.2**	**1.9**	**0.9**	**0.9**
	prev.year=100	793.8	108.8	116.4	110.0	105.3	164.8	107.1	67.2	84.0	50.5	92.4
Interest	*bill. CZK*	**18.4**	**18.6**	**20.4**	**18.6**	**16.7**	**21.9**	**28.5**	**26.9**	**29.6**	**32.3**	**33.1**
	prev.year=100	131.1	100.9	110.0	90.9	89.7	131.3	130.5	94.4	109.9	109.0	102.5
Subsidies	*bill. CZK*	**33.4**	**36.6**	**44.0**	**45.6**	**43.7**	**48.8**	**38.3**	**38.9**	**32.7**	**25.9**	**30.8**
	prev.year=100	97.9	109.6	120.2	103.7	95.9	111.5	78.6	101.5	84.0	79.2	119.0
Gross fixed capital formation	*bill. CZK*	**18.0**	**24.7**	**26.3**	**31.7**	**36.8**	**34.5**	**33.7**	**46.9**	**62.0**	**76.9**	**86.8**
	prev.year=100	43.3	136.9	106.8	120.2	116.4	93.7	97.6	139.1	132.2	124.1	112.9
Capital transfers	*bill. CZK*	**119.8**	**85.3**	**119.4**	**79.7**	**64.8**	**133.2**	**129.3**	**109.0**	**87.1**	**83.4**	**63.1**
	prev.year=100	46.2	71.2	140.1	66.7	81.4	205.6	97.1	84.3	79.9	95.8	75.6
Other expenditure	*bill. CZK*	**95.5**	**50.5**	**71.9**	**75.7**	**81.0**	**106.2**	**121.4**	**170.8**	**174.1**	**170.0**	**187.9**
	prev.year=100	258.9	52.8	142.4	105.3	107.1	131.0	114.3	140.7	101.9	97.6	110.5

Table 5-13: Local government expenditure

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total expenditure	*bill. CZK*	**204.8**	**178.6**	**196.2**	**191.2**	**209.3**	**238.4**	**271.7**	**342.8**	**352.9**	**352.1**	**375.0**
	prev.year=100	149.6	87.2	109.9	97.4	109.5	113.9	114.0	126.1	103.0	99.8	106.5
Compensation of employees	*bill. CZK*	**32.8**	**36.7**	**38.4**	**43.4**	**45.5**	**64.2**	**72.1**	**102.8**	**108.6**	**113.2**	**120.1**
	prev.year=100	129.8	111.9	104.5	113.0	104.7	141.3	112.2	142.6	105.7	104.3	106.1
Intermediate consumption	*bill. CZK*	**48.3**	**53.8**	**60.0**	**66.2**	**68.1**	**77.3**	**85.5**	**97.3**	**98.1**	**100.9**	**109.7**
	prev.year=100	110.4	111.3	111.5	110.4	102.9	113.5	110.6	113.9	100.8	102.9	108.7
Social benefits other than social transfers in kind	*bill. CZK*	**29.9**	**3.8**	**5.1**	**7.5**	**9.3**	**9.0**	**10.2**	**11.8**	**11.9**	**11.7**	**11.9**
	prev.year=100	629.7	12.6	135.0	146.9	124.2	96.6	113.4	115.6	100.6	98.6	102.1
Social benefits in kind	*bill. CZK*	**1.0**	**1.4**	**1.6**	**1.8**	**2.0**	**1.2**	**1.4**	**2.4**	**2.5**	**2.6**	**2.8**
	prev.year=100	164.5	145.4	111.1	114.3	109.1	61.1	115.6	169.9	104.5	102.4	108.9
Interest	*bill. CZK*	**1.9**	**1.6**	**2.6**	**2.6**	**1.7**	**1.9**	**2.0**	**2.4**	**3.0**	**2.2**	**2.4**
	prev.year=100	180.3	85.3	160.6	99.4	67.6	110.3	104.5	118.9	126.8	72.9	108.1
Subsidies	*bill. CZK*	**7.2**	**12.7**	**13.9**	**15.5**	**17.2**	**16.6**	**18.2**	**29.3**	**26.3**	**29.3**	**31.2**
	prev.year=100	91.8	176.8	109.7	111.4	111.3	96.6	109.6	160.7	89.8	111.6	106.3
Gross fixed capital formation	*bill. CZK*	**58.1**	**51.9**	**56.5**	**35.2**	**41.6**	**48.3**	**60.7**	**69.7**	**73.8**	**68.9**	**74.7**
	prev.year=100	168.9	89.3	108.8	62.3	118.0	116.2	125.6	114.9	105.9	93.3	108.5
Capital transfers	*bill. CZK*	**12.3**	**11.5**	**8.5**	**14.9**	**13.3**	**14.2**	**11.9**	**16.4**	**19.2**	**12.4**	**12.8**
	prev.year=100	121.1	93.6	73.9	176.0	89.4	106.7	83.4	138.2	117.3	64.4	103.6
Other expenditure	*bill. CZK*	**13.3**	**5.2**	**9.7**	**4.0**	**10.5**	**5.5**	**9.8**	**10.7**	**9.5**	**10.9**	**9.4**
	prev.year=100	146.4	39.0	186.7	41.6	262.3	52.3	178.5	108.9	88.7	115.0	85.8

Table 5-14: Social security fund expenditure

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total expenditure	*bill. CZK*	**90.2**	**96.2**	**106.0**	**112.0**	**115.5**	**127.7**	**142.6**	**150.8**	**161.7**	**169.9**	**173.3**
	prev.year=100	115.5	106.6	110.2	105.7	103.1	110.6	111.6	105.8	107.2	105.0	102.0
Compensation of employees	*bill. CZK*	**1.6**	**1.8**	**1.8**	**2.0**	**2.1**	**2.3**	**2.5**	**2.7**	**2.7**	**2.9**	**3.0**
	prev.year=100	107.2	108.8	104.1	111.0	101.9	109.5	111.1	105.4	102.7	106.2	105.0
Intermediate consumption	*bill. CZK*	**1.6**	**1.2**	**1.3**	**1.2**	**1.1**	**1.4**	**1.5**	**1.9**	**1.9**	**2.0**	**1.8**
	prev.year=100	118.6	76.1	105.5	92.9	94.8	127.3	105.3	123.4	102.1	105.7	90.4
Social benefits other than social transfers in kind	*bill. CZK*	**-**	**-**	**-**	**0.0**	**-**	**-**	**-**	**-**	**-**	**0.0**	**-**
	prev.year=100	x	x	x	x	0.0	x	x	x	x	x	0.0
Social benefits in kind	*bill. CZK*	**86.1**	**92.4**	**101.5**	**107.5**	**111.5**	**123.2**	**137.4**	**145.6**	**156.3**	**163.9**	**167.5**
	prev.year=100	116.1	107.3	109.9	105.8	103.8	110.4	111.6	106.0	107.4	104.8	102.2
Interest	*bill. CZK*	**0.1**	**0.1**	**0.2**	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
	prev.year=100	89.5	215.7	168.2	42.2	23.1	77.8	50.0	85.7	100.0	16.7	100.0
Subsidies	*bill. CZK*	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
	prev.year=100	x	x	x	x	x	x	x	x	x	x	x
Gross fixed capital formation	*bill. CZK*	**0.5**	**0.7**	**0.9**	**0.8**	**0.7**	**0.6**	**0.9**	**0.6**	**0.7**	**0.8**	**0.5**
	prev.year=100	50.7	140.7	129.4	85.8	84.0	84.0	154.6	69.5	111.1	119.1	64.0
Capital transfers	*bill. CZK*	**-**	**-**	**-**	**0.1**	**0.0**	**-**	**0.0**	**0.0**	**0.1**	**-**	**-**
	prev.year=100	x	x	x	x	6.6	0.0	x	81.4	174.3	0.0	x
Other expenditure	*bill. CZK*	**0.4**	**0.1**	**0.2**	**0.3**	**0.1**	**0.3**	**0.2**	**0.1**	**0.0**	**0.3**	**0.4**
	prev.year=100	427.0	13.7	455.8	108.4	31.5	332.1	82.2	29.4	64.6	661.9	146.0

5.3 Balance

Table 5-15: General government net lending/net borrowing by subsectors

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
General government net lending (+)/net borrowing (-)	*bill. CZK*	**-55.8**	**-68.8**	**-100.1**	**-77.3**	**-81.5**	**-135.0**	**-166.8**	**-170.0**	**-80.4**	**-104.6**	**-94.0**
Central government net lending (+) /net borrowing (-)	*bill. CZK*	**-91.6**	**-55.2**	**-105.7**	**-78.7**	**-76.2**	**-124.6**	**-150.9**	**-154.3**	**-77.6**	**-106.3**	**-99.7**
Local government net lending (+) /net borrowing (-)	*bill. CZK*	**40.2**	**-12.5**	**6.8**	**0.9**	**-9.2**	**-10.1**	**-11.7**	**-14.1**	**-2.6**	**-0.3**	**-9.4**
Social security funds net lending (+) /net borrowing (-)	*bill. CZK*	**-4.4**	**-1.2**	**-1.1**	**0.5**	**3.9**	**-0.3**	**-4.2**	**-1.7**	**-0.2**	**2.0**	**15.1**

Table 5-16: General government net lending/net borrowing by subsectors - ratios to GDP

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
General government net lending (+)/net borrowing (-)	*(in % GDP)*	-3.3	-3.8	-5.0	-3.7	-3.7	-5.7	-6.8	-6.6	-2.9	-3.5	-2.9
Central government net lending (+) /net borrowing (-)	*(in % GDP)*	-5.4	-3.0	-5.3	-3.8	-3.5	-5.3	-6.1	-6.0	-2.8	-3.6	-3.1
Local government net lending (+) /net borrowing (-)	*(in % GDP)*	2.4	-0.7	0.3	0.0	-0.4	-0.4	-0.5	-0.5	-0.1	0.0	-0.3
Social security funds net lending (+) /net borrowing (-)	*(in % GDP)*	-0.3	-0.1	-0.1	0.0	0.2	0.0	-0.2	-0.1	0.0	0.1	0.5

5.4 Debt

Table 5-17: General government debt by subsectors and instruments

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
General government debt by instruments	*bill. CZK*	**209.9**	**236.7**	**299.8**	**340.5**	**405.4**	**591.5**	**702.3**	**775.0**	**855.1**	**903.5**	**973.0**
	prev.year=100	97.9	112.8	126.7	113.6	119.1	145.9	118.7	110.3	110.3	105.7	107.7
Currency and deposits	*bill. CZK*	**-**	**-**	**-**	**-**	**-**	**7.2**	**24.4**	**4.0**	**2.8**	**0.6**	**0.0**
	prev.year=100	x	x	x	x	x	x	340.9	16.2	71.4	21.7	3.7
Securities other than shares	*bill. CZK*	**147.7**	**160.3**	**196.4**	**232.1**	**275.6**	**354.8**	**427.4**	**528.4**	**633.8**	**704.6**	**801.3**
	prev.year=100	111.2	108.6	122.5	118.2	118.7	128.7	120.5	123.6	119.9	111.2	113.7
Loans	*bill. CZK*	**62.2**	**76.4**	**103.4**	**108.4**	**129.8**	**229.5**	**250.5**	**242.6**	**218.5**	**198.3**	**171.7**
	prev.year=100	76.2	122.8	135.3	104.8	119.7	176.9	109.2	96.8	90.0	90.8	86.6
Central government debt	*bill. CZK*	**187.5**	**211.2**	**271.7**	**314.6**	**378.3**	**559.8**	**660.6**	**725.6**	**790.4**	**830.9**	**891.7**
	prev.year=100	94.8	112.7	128.7	115.8	120.2	148.0	118.0	109.8	108.9	105.1	107.3
Currency and deposits	*bill. CZK*	**-**	**-**	**-**	**-**	**-**	**7.2**	**24.4**	**4.0**	**2.8**	**0.6**	**0.0**
	prev.year=100	x	x	x	x	x	x	340.9	16.2	71.4	21.7	3.7
Securities other than shares	*bill. CZK*	**135.9**	**145.7**	**185.0**	**222.4**	**267.9**	**347.8**	**415.4**	**517.4**	**611.5**	**681.1**	**778.5**
	prev.year=100	109.4	107.2	126.9	120.2	120.5	129.8	119.4	124.6	118.2	111.4	114.3
Loans	*bill. CZK*	**51.6**	**65.4**	**86.7**	**92.2**	**110.4**	**204.8**	**220.8**	**204.2**	**176.0**	**149.2**	**113.2**
	prev.year=100	70.1	126.9	132.5	106.4	119.7	185.5	107.8	92.5	86.2	84.7	75.9
Local government debt	*bill. CZK*	**27.2**	**31.9**	**36.0**	**34.5**	**35.8**	**40.3**	**50.0**	**59.0**	**72.0**	**79.1**	**86.7**
	prev.year=100	136.8	117.3	112.7	95.7	103.9	112.7	124.0	118.0	122.1	109.8	109.6
Currency and deposits	*bill. CZK*	-	-	-	-	-	-	-	-	-	-	-
	prev.year=100	x	x	x	x	x	x	x	x	x	x	x
Securities other than shares	*bill. CZK*	**11.8**	**14.7**	**12.0**	**10.1**	**8.2**	**7.1**	**12.3**	**11.9**	**22.6**	**24.0**	**23.3**
	prev.year=100	138.0	124.1	81.9	83.9	81.5	86.8	172.4	96.6	190.7	105.8	97.3
Loans	*bill. CZK*	**15.4**	**17.3**	**24.0**	**24.4**	**27.6**	**33.2**	**37.7**	**47.1**	**49.4**	**55.1**	**63.4**
	prev.year=100	135.9	112.1	138.9	101.6	113.1	120.4	113.6	125.0	104.8	111.6	115.0
Social security funds debt	*bill. CZK*	**1.9**	**2.4**	**1.7**	**1.2**	**0.7**	**0.5**	**0.4**	**0.3**	**0.2**	**0.3**	**0.2**
	prev.year=100	323.9	127.7	71.8	67.8	61.9	64.9	84.6	79.5	74.5	117.5	68.0
Currency and deposits	*bill. CZK*	-	-	-	-	-	-	-	-	-	-	-
	prev.year=100	x	x	x	x	x	x	x	x	x	x	x
Securities other than shares	*bill. CZK*	-	-	-	-	-	-	-	-	-	-	-
	prev.year=100	x	x	x	x	x	x	x	x	x	x	x
Loans	*bill. CZK*	**1.9**	**2.4**	**1.7**	**1.2**	**0.7**	**0.5**	**0.4**	**0.3**	**0.2**	**0.3**	**0.2**
	prev.year=100	323.9	127.7	71.8	67.8	61.9	64.9	84.6	79.5	74.5	117.5	68.0

Note: Government debt consists of following financial instruments: currency and deposits, securities issued other than shares excluding financial derivatives and loans. Government debt means total gross debt at nominal value outstanding at the end of the year and consolidated between and within the sectors of general government. The nominal value is considered equivalent to the face value of liabilities. It is therefore equal to the amount that the government will have to refund to creditors at maturity.

Table 5-18: General government debt by subsectors and instruments - ratios to GDP

		1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
General government debt based on instruments	*(in % GDP)*	12.5	13.1	15.0	16.4	18.5	25.1	28.5	30.1	30.7	30.4	30.4
Currency and deposits	*(in % GDP)*	-	-	-	-	-	0.3	1.0	0.2	0.1	0.0	0.0
Securities other than shares	*(in % GDP)*	8.8	8.9	9.8	11.2	12.6	15.1	17.3	20.5	22.8	23.7	25.0
Loans	*(in % GDP)*	3.7	4.2	5.2	5.2	5.9	9.8	10.2	9.4	7.9	6.7	5.4
Central government debt	*(in % GDP)*	11.1	11.7	13.6	15.1	17.3	23.8	26.8	28.2	28.4	28.0	27.8
Currency and deposits	*(in % GDP)*	-	-	-	-	-	0.3	1.0	0.2	0.1	0.0	0.0
Securities other than shares, exclusive of financial derivatives	*(in % GDP)*	8.1	8.0	9.3	10.7	12.2	14.8	16.9	20.1	22.0	22.9	24.3
Loans	*(in % GDP)*	3.1	3.6	4.3	4.4	5.0	8.7	9.0	7.9	6.3	5.0	3.5
Local government debt	*(in % GDP)*	1.6	1.8	1.8	1.7	1.6	1.7	2.0	2.3	2.6	2.7	2.7
Currency and deposits	*(in % GDP)*	-	-	-	-	-	-	-	-	-	-	-
Securities other than shares	*(in % GDP)*	0.7	0.8	0.6	0.5	0.4	0.3	0.5	0.5	0.8	0.8	0.7
Loans	*(in % GDP)*	0.9	1.0	1.2	1.2	1.3	1.4	1.5	1.8	1.8	1.9	2.0
Social security funds debt	*(in % GDP)*	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	*(in % GDP)*	-	-	-	-	-	-	-	-	-	-	-
Securities other than shares	*(in % GDP)*	-	-	-	-	-	-	-	-	-	-	-
Loans	*(in % GDP)*	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0