The Czech Fiscal Council

Eva Zamrazilová
Chairwoman

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Main Points

- Legislative Framework
- Institutional Framework
- Key Tasks
- Conclusions

Legislative Framework

Budget Responsibility Act: adopted in January 2017

- **National fiscal rules**
  - **Limit on total expenditure of public sector (E)**
    - E = R + 1 % of nominal GDP
      - R - Projected total consolidated revenues of the public sector adjusted for the impact of the business cycle
  - **Limit on public debt (adjusted for Treasury reserves) - 55 % of GDP**
    - Hitting this limit is automatically followed by adoption of measures leading to stabilization
    - The government approves and submits new stabilizing budget
  - **Escape clauses**
    - Status of war, emergency or similar threats
    - Strong deterioration of economic conditions
      - 2 % q/q decline of GDP or 3% y/y decline of GDP

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Institutional Framework

The Czech Fiscal Council (CFC): established in January 2018

- Independent Fiscal Institution
- 3 board members approved by parliament
  - Chairman suggested by government
  - Members suggested by:
    - Czech National Bank
    - Senate
- The Office of the Czech Fiscal Council
  - Small institution (12 employees, budget approx. 800 000 €/year)

Committee for Budgetary Forecasts (CFB): established in May 2018

- Experts from both private and public companies which publish full-fledged publicly disposable macroeconomic forecasts on regular basis (mostly quarterly)
- At present 10 experts (honorary function)

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Main tasks of CFC and CFB

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- Long-term public finance sustainability report - published (and submitted to the Parliament) every year
- Evaluation of the 3 years fiscal framework
  - Compliance with methodology (approved jointly with The Ministry of Finance) and thus numerical correctness
  - Recommendations – does the fiscal framework comply with long-term sustainability ?

Committee for Budgetary Forecasts

- Evaluation of macroeconomic forecast upon which the public finance outlook is based
- Evaluation of the fiscal forecast
- 3 degrees : optimistic, realistic, prudential

- The statements of NFC and CFB are released both on the NFC website and the Ministry of Finance website

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Our first steps

- **Statement (April 2018)**
  - As for methodical issues, fiscal framework is based on appropriate background

HOWEVER…

- **Recommendation**
  - Set the public expenditures at levels lower than the fiscal framework allows
  - Full utilization would lead to fiscal expansion which is not desirable given the current state of the economic cycle
  - In the case of unexpected deterioration of the economy, there will be space for active fiscal policy, if necessary

WHY?

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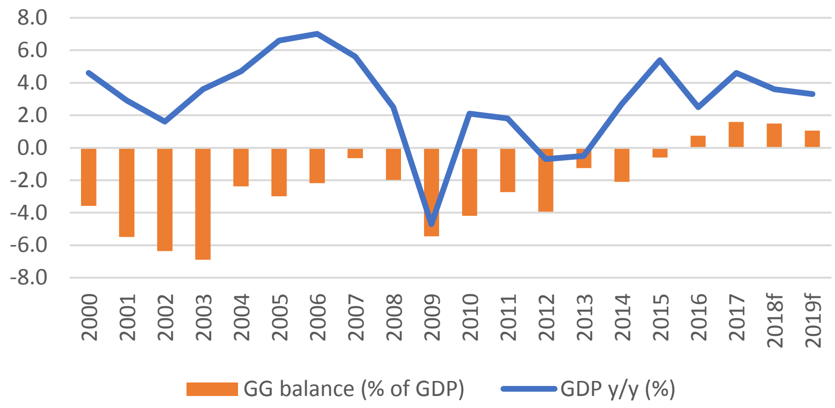
Experience from the crisis



	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Public debt (% of GDP)	27.9	27.7	27.5	**28.3**	**33.6**	**37.4**	**39.8**	**44.5**	44.9	42.2	39.9	36.8	34.6
Primary balance (% of GDP)	-1.9	-1.1	0.4	-1.0	-4.2	-2.9	-1.4	-2.5	0.1	-0.8	0.5	1.6	2.3

- Fiscal policy has been strongly procyclical before the crisis
- Public finance produced deficits under strong growth of GDP
- Even though there were no expenditures to help banks, the public debt to GDP ratio increased by 17 pp in 2009-2012 period
- It was painful to consolidate public finance to present shape
- Small open economy needs to create buffers for bad times
- Stress tests indicate vulnerability of public finance to similar economic downturn
- Fiscal expansion is not desirable as imbalances would deepen (labour market strongly overheated)

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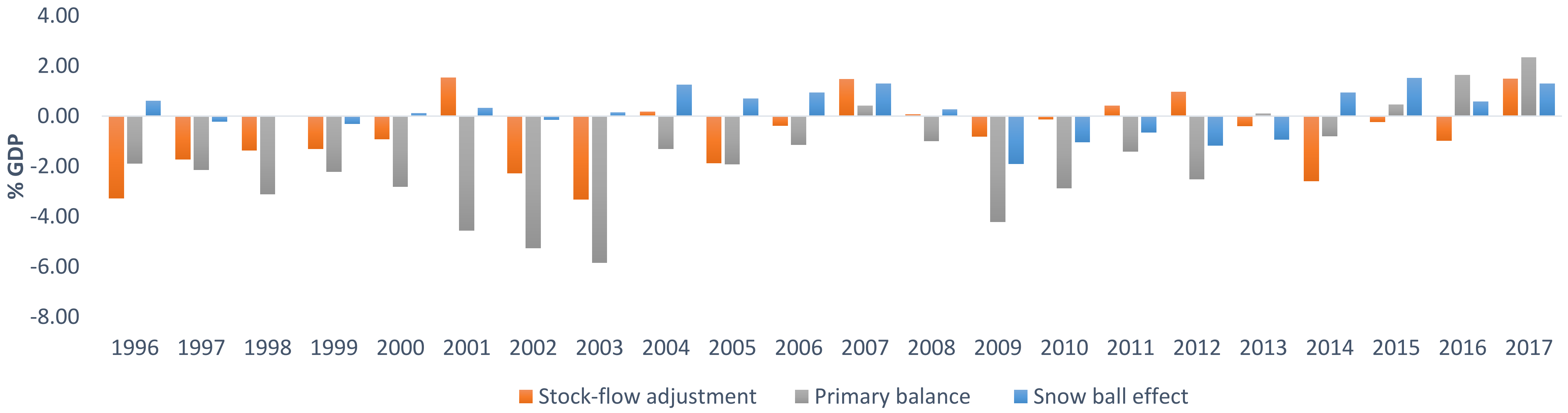
Public debt dynamics



- The „snow ball effect“ has been positive since 2014 due to low interest rates (partly effect of previous consolidation) and strong GDP growth
- However, this consolidation was mostly based on cutting expenditures approved in good times (2005-2007)
- Present good times are tempting for politicians to make the same mistakes

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Conclusions

- Lesson from the crisis: fiscal policy needs some space to support domestic demand in case of weakening foreign demand or imbalances in other sectors

- Structural weaknesses in public finance persist

- Main goal of CFC: to put pressure on public authorities to consolidate public finance in long-term perspective

- Public discussion of short-term and long-term priorities

- Fiscal brake should never be stepped on

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Thank you for your attention

eva.zamrazilova@unrr.cz

@EZamrazilova