16 October 2020

Assessment of budget documents for 2021 and 2022

In the current uncertain conditions, expansionary fiscal policy is counter-cyclical and, as such, appropriate in the light of available forecasts. However, the planned expenditure of the general government sector in the coming years is high and therefore exposed to significant risks, especially related to their effectiveness. At the same time, the current situation should not be exploited for implementing measures that structurally worsen the public finance position. The envisaged accelerated investment activity should strengthen long-term economic potential as much as possible. This would ensure that the burden of significantly increased government debt during the crisis will not be too heavy in the future. Otherwise, when the crisis is over, the room for manoeuvre in the context of future reversals of the business cycle will be reduced and it will be difficult to ensure the long-term sustainability of public finances.

The Fiscal Council notes that the conditions set out in the Fiscal Rule Act that enable exceptional circumstances to be enforced, given the available data at the time of drafting this assessment are fulfilled this year and next, while for 2022 this cannot be unequivocally confirmed.

The fiscal projections in the proposed budget documents continue to be significantly marked by the effects of measures to limit the consequences of the COVID-19 epidemic. As early as in March 2020, the Fiscal Council noted that the conditions stipulated by the Fiscal Rule Act for a temporary deviation from achieving medium-term fiscal sustainability were met, and that, in these circumstances, it would pay special attention to fiscal developments excluding the direct effects of COVID-19 measures. Such an analysis of the given fiscal projections shows that the general government deficit will increase significantly next year due to expenditure growth almost doubling. The increase in investment expenditure is expected to be particularly pronounced and the growth in other expenditure is also expected to be much higher than the growth of the long-term economic potential.

According to the Fiscal Council, the proposed scope and structure of fiscal incentives are optimistic, while their actual implementation could entail a number of risks. In the event of a projected significant increase in investment, risks relate to their efficiency and thus to the actual short-term and especially long-term effect on economic activity. The projected high growth of other expenditure not related to COVID-19 measures poses a risk to the structural position of public finances. In addition to the uncertainties associated with the forecasts of macroeconomic and fiscal aggregates, the Fiscal Council also explicitly highlights the risks arising from economic policy measures. Some discretionary measures already adopted and announced that are not directly related to the epidemic may worsen the structural situation of public finances.

As in most other countries, the general government debt is expected to increase significantly in the crisis and temporarily exceed 80% of GDP. An increase in debt during a period of low interest rates and the expected recovery in economic growth may still be acceptable. However, it becomes risky if debt before the interest rate are normalised again is not used mainly to increase economic potential. It is therefore essential that all funds earmarked for financing the projected expenditure, both grants and loans, are spent effectively in finding solutions that will have the highest multiplying effect and enable the sustainable growth and development of the economy.