8. State Budget

Half-yearly state budget deficit remained deep, it however moderated in comparison to years 2020 as well as 2021.

The domestic state budget (SB)[1] recorded a deficit in the amount of 183 CZK bn for H1 2022, deficit was observed in this time period for the fifth year in a row. This year's deficit was however lower than the result from the first half of years 2020 and 2021. The easing of pressures on the extraordinary expenditures had an effect here (in connection with the ending of counter-pandemic restrictions) with simultaneous advancing recovery of the economy. It was yet with the contribution of the heightened geopolitical tension accompanied by unusually strong prices growth as well the need for unexpected expenditures linked to the refugee inflow from Ukraine. Despite the spring revival of a number of services (incl. tourism) the deficit significantly deepened in Q2 2022 compared to the previous quarter. The termination of the interim budget at the end of this year's March also played a role[2]. On the other hand, the economic revival as well as growth of prices caused the total tax collection[3] to overtake the record level from the comparable period before the onset of pandemics[4] for the first time this year in H1.

Total tax income overtook the pre-pandemic level for the first time.

Tax income grew mainly thanks to the VAT collection. Revenues from the EU budget dropped and stayed also behind the budget anticipations.

Total SB revenues exceeded the last year's level by one tenth (i.e. 74 CZK bn) in this year's H1. The considerable strengthening of all significant tax revenues contributed (mainly VAT and social security insurance), on the contrary the non-tax and capital revenues slightly decreased (by 6.3%, i.e. 6.2 CZK bn). Primarily the lower funds from the EU budget, whose volume did not reach even one third of the yearlong size anticipated by this year's budget[5], stood behind it. In addition last year's extraordinary yields from the frequency auction (in telecommunication) were not repeated any more (5.6 CZK bn).

Dynamic year-on-year growth of the VAT collection reflected the revived consumption as well as the notable acceleration of the growth of consumer prices.

162.6 CZK bn flowed in to the SB from the weight dominant tax – VAT – in H1, by 23% more year-on-year (the collection grew by similar pace also in Q1 2022 itself). It was connected to lower basis (the household consumption was still subdued by restrictions at the beginning of the last year) as well as the substantial price acceleration. The markedly revived consumption of non-residents could have already started to be evident (to a lesser extent), specifically due to the effect of spring recovery of arrival tourism as well as inflow of refugees from Ukraine. Waiver of value added tax on selected commodities (energies, vaccines, tests, respirators) in contrast affected the tax collection adversely.

Despite swift year-on-year growth, the state-wide collection of consumption taxes did not attain the level from H1 2019.

SB acquired by 16% more on consumption taxes year-on-year this year and the collection growth exceeded the budget anticipations so far. State wide collection of this tax however still slightly lagged behind (by 3%) the pre-pandemic period (H1 2019). Already only by 4.8% more of this tax flew into the SB year-on-year in June 2022 itself, since the collection of the most significant tax by volume – tax on mineral oils – stagnated. It could have been associated to the sharp spring rise of prices of motor fuels at petrol stations, to which both households and businesses presumably reacted by limiting their consumption (this was already indicated in May data related to retail sales for motor fuels). On the contrary the impact of temporary cut down of the tax rate[6] was not shown in the treasury fulfilment of the collection yet. Nevertheless the collection of tax on mineral oils went up by 12% in total for the whole this year's half-year, mainly due to the effect of low comparative basis (the counter-pandemic measures were culminating during Q1 2021 and the substantial restriction of the mobility of population between regions was reflected in the lowest collection of this tax in the

Tax on tobacco products contributed the most to the growth of collection.

[1] Unless stated otherwise, all data related to the state budget stem from the data of the Ministry of Finance regarding the treasury fulfilment.
[2] It affected mainly the drawing of investment as well as possibilities to pre-finance some current transfers and also restricted further sources of funding at the beginning of the year (e.g. extra-budgetary resources – mainly the claims from the unused expenditures from the previous years).
[3] Here it is considered the tax collection at the level of all public budgets and not including the social security insurance.
[4] While the comparison with the beginning of year 2020 was by 2.9% lower still in Q1 2022, it already surpassed in total by 9.9% the level from H1 2019 in this year's half-year.
[5] Based on Act No. 57/2022 Coll., on the state budget, approved by the Chamber of Deputies of the Parliament of the CR on 10th March 2022.
[6] Effective as of 1st June until 30th September 2022, the consumer tax rate on petrol and diesel fuels is temporarily lowered by 1.50 CZK per litre.

last eight years at that time). Collection of tax on tobacco products, which expanded by one fifth besides other things thanks to the increase of the tax rate, contributed the most to higher collection of all consumption taxes this year. Growing collection of less significant categories of tax by weight also had a favourable effect, especially the tax on alcohol and also beer (its collection however still fell by more than 5% behind the peak from year 2019).

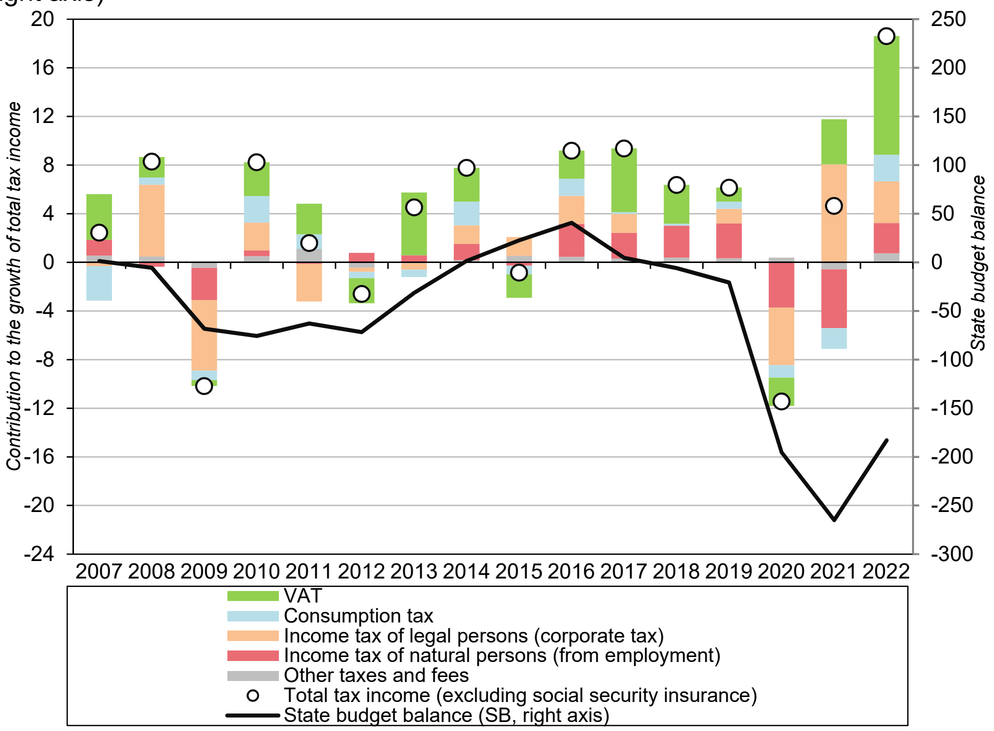
Collection of income tax of legal persons notably increased year-on-year thanks to high June payment.

SB revenue from the corporate tax briskly grew year-on-year (+16.8%), mainly thanks to the high June collection (including both quarter and half-yearly tax advance payments and part of the payment of tax for year 2021[7]). Collection for H1 appreciably exceeded the budget anticipations, because it reached nearly three quarters of the anticipated year-long volume and proved relatively good economic results of some large businesses (e.g. in the area of energetics or trade). Legislative amendments however also affected the size of the collection[8].

Swift growth of the collection of income tax of natural persons mirrored the fast recovery of the labour market. The collection however considerably fell behind the pre-pandemic level, mainly due to the influence of legislative amendments.

Collection of income tax of natural persons (ITNP) grew by similar pace as the corporate tax collection year-on-year. It reflected the employment growth as well as the brisk nominal rise of average wages. The pay out of the compensatory bonus (to aid small businesses) still did influence the collection of ITNP adversely, but to a lesser extent than last year. In contrast other legislative amendments (ongoing increasing of tax rebate per taxpayer or higher tax deduction on children) curbed the pace of collection growth more intensively this year. While the state-wide collection of the corporate tax overtook the pre-pandemic level already last year, collection of this year's ITNP did not reach even the level from H1 2017. Last year's abolition of the "super gross wage" leading to a substantial lowering of the tax burden on labour played an essential role here. On the contrary the growth of the collection of ITNP levied by deduction (from capital gains) accelerated and was not significantly affected by the pandemic situation.

Chart 17 Contribution of constituent revenues to the growth of the state wide tax collection* (year-on-year in p. p.) **and state budget balance within H1** (in CZK bn, right axis)



* Includes tax income without the social security insurance. Source: MF CR

[7] It is the payment for payers, which have mandatory audit, or their tax return is processed and submitted by tax advisor.
[8] High year-on-year growth of the collection of the corporate tax was partially influenced by last year's shift of term for the payment of tax advance (based on the individual requests of companies) with negative impact on the income of this tax into the SB in the amount of 6.4 CZK bn (for H1 2021). Further it also contained the change in the taxation of the reserves of the health insurance companies.

Total SB outlays grew substantially in Q2 2022 compared to the beginning of the year. Termination of the interim budget as well as the need for exceptional expenditures related to high inflation and also the war in Ukraine had an effect.

Total SB outlays amounted to 970 CZK bn for H1 this year and mildly dropped year-on-year (by 0.8%), solely due to the effect of current expenditures. Their development however was more uneven during this year so far. If the regime of the interim budget[9] limited the expenditures in Q1, they were fundamentally influenced by the impacts of the racing inflation, which resulted in the need for the pension adjustment as well as other social benefits in the subsequent period. In addition, the need for extraordinary expenditures arose in connection to the war conflict in Ukraine (foreign aid, expenditures on the integration of refugees in the CR, crisis management in the area of state material reserves). In the opposite direction went the further reduction of the financial assistance related to the pandemics[10]. The total size of the SB current expenditures thus increased by 5.4% year-on-year in Q2 2022 itself, while it plummeted by 9.5% in the previous quarter.

Volume of current transfers to business entities returned to the level from year 2019.

More expenditures were directed to the non-investment purchases, the cost of servicing the growing state debt was however also rising.

The development of non-investment transfers to business entities, which attained only 40% of last year's level and plunged by 51 CZK bn, was decisive for the year-on-year fall of the current expenditures. It primarily reflected the decline of the emergency programmes for the affected businesses as well as whole branches, partially also the reduction of advance subsidies on renewable resources of energy (−3.8 CZK bn). Lower transfers to contributory as well as non-profit organisations were also connected to the decrease of the counter-pandemic help, their impact on current expenditures was however of smaller magnitude. Significant by volume current transfers towards regions and municipalities stagnated, because the mild growth of wage tariffs of teachers of primary and secondary schools (+2%) was compensated by reduction of funds in the area of social services or inpatient care (associated with the last year's extraordinary bonuses). Expenditures on wages in the organisational units of the state practically stagnated for the third year in a row. More funds were in contrast expended on the non-investment purchases year-on-year (+22.6%, i.e. 7.3 CZK bn), where the higher expenditures to bolsters up the state material reserves, growing prices consumed energies or higher need to purchase medicine and medical material were evident. The temporarily augmented payments for the so called state insured persons (+8.2 CZK bn)[11] also burdened the SB more this year. Expenditures on servicing the state debt also enlarged (to 23 CZK bn[12], nearly twofold in the last two years). The marked growth of interest rates on the bond marked as well as continuing strong growth of the size of the debt stood behind it. State debt totalled 2 708 CZK bn at the end of June this year by 12.1% more year-on-year. The debt climbed up by 242 bn since the beginning of this year, which was nevertheless less than in the preceding two years.

Growth of SB current expenditures was driven mostly by the paid out pensions, whose level was raised two times in H1. Pension account deficit deepened.

Expenditures on social benefits traditionally form part of the SB current expenditures – it presented 41.4% in H1 2022. Their weight strengthened year-on-year for the first time in the comparable period in the last six years (+3 p.p.) and these benefits at the same time had the most pro-growth effect on the development of all current expenditures (+21.3 CZK bn) so far this year. This year's expanded volume of social benefits was from more than 85% driven by higher expenditures on pensions – these strengthened by 6.8% year-on-year thanks to January adjustment as well as the exceptional June one. The number of pension recipients worked in the opposite direction, significantly affected by higher mortality. It shrank by 1.7% compared to June 2020. Good condition of the labour market was reflected in the ongoing

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[9] Total of the monthly expenditures of all organisational units of the state thus could reach maximum of one twelfth of total SB expenditures set according to the approved Act on SB from year 2021. This led among other things to the postponement of the non-essential operating expenditures as well as investment.

[10] This aid culminated last year in Q2 when it comprised of 64 CZK bn (101 bn in total for the entire H1). It mainly consisted of compensation of part of wages and mandatory transfers (within the Antivirus A, A+ and B programme), special programmes to directly support the hit sectors of the economy (e.g. COVID Rent, COVID Uncovered costs), higher outlays in healthcare (especially increase of the state payment per so called state insured person, raised personal costs of employees in health and social works, purchases of protective equipment) and finally also the increased expenditures on some social benefits (care benefits, extraordinary contribution for employee in quarantine or isolation).

[11] Monthly payments by state increased from 1767 CZK to 1967 CZK per person as of 1st January 2022. According to the amendment to the Act on public health insurance approved later however the payment fell to 1567 CZK as of 1st July 2022. The average monthly payment for the whole year 2022 will total 1 767 CZK and it will thus be maintained at the level from year 2021.

[12] It corresponds to the balance of the budget chapter State debt.

growth of pension insurance revenues (+5.9%). Pension account deficit[13] however still deepened to 8.6 CZK bn year-on-year and recorded a deficit for a third year in a row.

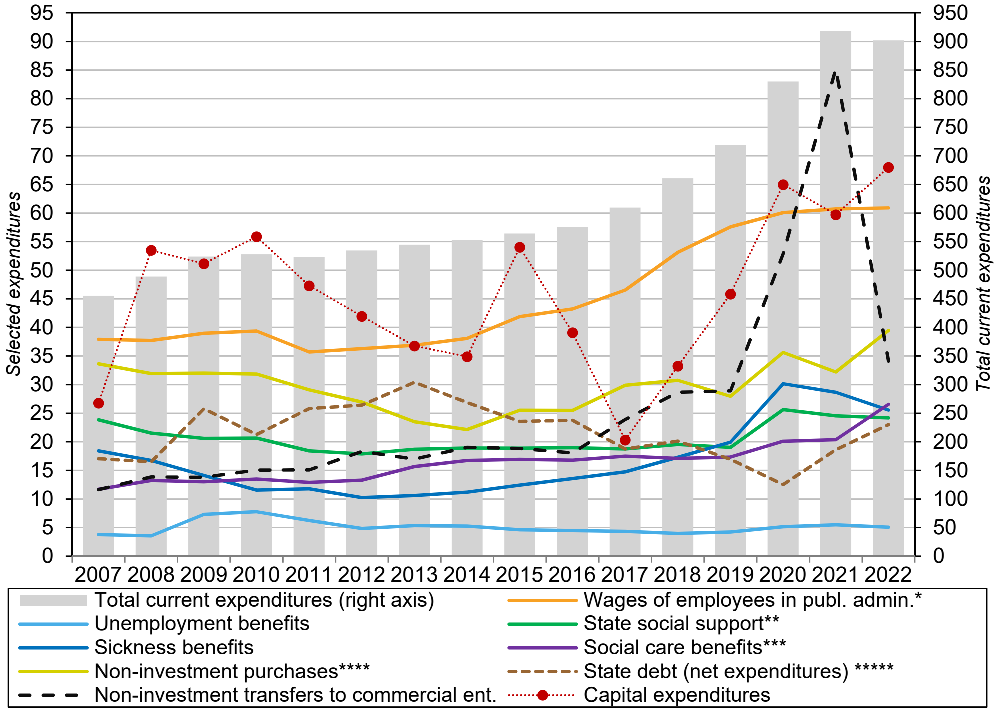
Volume of majority of non-pension social benefits fell due to the retreat of pandemics as well as good condition of the labour market. The payment of the humanitarian benefit however was significant, expenditures on care also strengthened.

"Non-pension" social benefits, considerably expanded during the pandemics, grew slower in H1 (by 3.6% year-on-year). Had there not been the exceptional immediate aid (consisting mainly of the humanitarian assistance to refugees from Ukraine in the amount of 4.3 CZK bn), the total volume of non-pension benefits would decrease. Since due to the major improvement of the epidemic situation, significant savings manifested in the pay out of care benefits in comparison to the last year's H1 (by 40%, i.e. 2.7 CZK bn), the volume of sickness benefits also reduced for the first time after year 2012 (by 4%, 0.7 bn). Lowering of the disbursed unemployment support (−7.6%) or state social support benefits including foster care (−1.5%)[14] had a smaller impact. On the contrary, the SB expended by one tenth more (+1.7 CZK bn) on care benefits (long-term sickness benefit).

Half-yearly volume of investment hiked up to record level thanks to the spring acceleration in spending.

Even though this year's drawing of capital outlays notably accelerated following the ending of the interim budget in Q2, SB spent only one third of the annual anticipated volume for the whole half year[15]. The investment amount still expanded by considerable 13.9% year-on-year (to record 68 CZK bn), from the major part due to the strengthening of flows into the state funds (on transport infrastructure as well as the environment). Total investment formed even 7% of all budget expenditures, which corresponded to the long-term average.

Chart 18 Selected expenditures of the state budget within H1 (in CZK bn)



* Covers expenditures on salaries in central government institutions. Does not include e.g. wage costs of regional education.
**Also includes the foster care benefits. ***Includes Material deprivation assistance benefits, Benefits for people with disabilities, Care benefits based on Act on State Social Support. Humanitarian aid provided for citizens of Ukraine are also included here.
****Contains mainly expenditures on purchase of services, materials, energies or other services (e.g. expenditures on repairs and maintenance). *****Corresponds to the balance of the budget chapter State debt.
Source: MF CR, MLSA

[13] It is expressed as the difference between revenues and expenditure on pensions form the SB. Expenditures do not contain the costs of administration of the pension insurance system.
[14] Lower expenditures on the weight significant parental allowances (−7.2%) mainly stood in the background, in contrast the income tested benefit experienced growth – housing allowance (+10.2%) and child allowance (+56.5%). For the last mentioned item, the impact of legislative changes in force since last year's July (especially increase of the limit of the relevant income establishing the right to the child allowance from 2.7 to 3.4multiple of the minimum subsistence amount and increase of the child allowance amount by 26%).
[15] Similar half-yearly "run-up" of investment was however apparent also last year or in years 2018 and 2019.

Half-yearly positive SB balance towards the EU budget was under the effect of weaker revenues the lowest in the last four years.

Despite stronger year-on-year decrease of the majority of revenue types the CR remained towards the EU budget the net recipient in H1 2022. The structural funds preserved the position of the most significant revenue channel (17.7 CZK bn), even though these flows into the CR reduced by more than one half against H1 2020 (the similar was also valid for the cohesion funds). The volume of otherwise fairly stable in the long-term direct payments in agriculture decreased substantially slower (to 17.1 bn). 6.1 CZK bn was allocated to the rural development (incl. the area of fishing). It represented the only revenue title, where the CR gained more year-on-year. Half-yearly total domestic payments into the Union budget practically stagnated similarly to the previous two years (32.5 CZK bn). The CR thus acquired from the EU budget net 15.9 CZK bn so far this year (the least since H1 2018). If revenue from the EU tool Recovery and Resilience Facility[16] were also included, the positive balance would be 23.5 bn.

Budget deficit of the government institutions sector shrank nearly by one half in the CR year-on-year, still it remained deep.

Government institution sector (VI) budget in the CR ended in deficit of 75.3 CZK bn in Q1 2022[17]. Even though it represented a deficit by nearly one half lower year-on-year, it was simultaneously the second worse result achieved within Q1 in the history of the independent CR. Substantial slowdown of growth of total expenditures VI (to 1.2% year-on-year), which was mainly associated with the termination of majority of support programmes for the entities impacted by the plunge of demand during the pandemics, contributed to the deficit moderation in Q1. Parallelly, the acceleration of the revenue growth occurred (to 13.6%) – both under the influence of the total revival of the economy and impact of the high price growth. Revenue VI from the product taxes (+27 CZK bn, i.e. +20%) as well as from net social contributions of both employers and workers themselves (+21 bn, +9%) thus grew swiftly. In both cases it concerned revenues substantially exceeding their pre-crisis maximum. Budget deficit fell solely to the central VI, since regional VI as well as health insurance companies recorded mild budget surplus (similarly to the beginning of last year). Gross consolidated debt of the sector VI rose to 2 683 CZK bn, year-on-year by 6.8% this year in March. The size of the debt grew continuously since half of year 2019, this year's increase was however the lowest since the beginning of pandemics so far.

Growth of the consolidated government institution debt slowed down in the CR.

Budget deficit of the government institution sector in the EU dropped for the fifth quarter in a row, specifically to the lowest value since the onset of pandemics.

Post crisis revival of the economy together with strong reduction of the extraordinary public expenditures tied to the pandemics are gradually reflected in the improved budget of the government institutions sector in the EU countries. Sector VI budget deficit[18] decreased for the fifth time in a row in the Union quarter-on-quarter and it amounted to 2.2% of GDP at the beginning of this year (the least since the end of year 2019). The relative deficit was thus lower than in the CR (−3.5% of GDP) or Spain (−4.4%) and France (−3.8%), the deepest deficits troubled Italy and Malta. Hungary (−6.9% of GDP) and Slovakia (−3.7%) were hit the most within the Central Europe (similarly to the whole last year), in contrast Poland (−1.2%) and Germany (−0.4%) headed towards the balanced budget this year so far. In comparison to Q1 2021, when a number of states proceeded with counter pandemic restriction, the balance of sector VI budget improved in the vast majority of Union members this year. Only Bulgaria and also Denmark (whose budget still ended in mild surplus) experienced an apparent deterioration.

The indebtedness rate in the EU started mildly decreasing following the last year's absolute peak.

The indebtedness of sector VI, which ascended to the historically highest level at the beginning of the last year, arrived at 87.8% of GDP (res. 95.6% in the euro area) in the EU at the end of Q1 2022. All member states reported a year-on-year reduction of the indebtedness (whole EU by 4.5 p.p., the CR by 1.1 p.p.), apart from Romania, Slovakia

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[16] It funds mainly the investment and reform projects of the EU member states via the national restoration plans. The CR started to draw on it for the first time this year.

[17] Data regarding the budget of government institutions for Q2 2022 will be published by the CZSO on 3rd October 2022, Eurostat then on 21st October 2022. More detailed assessment of the development for this year's Q1 is contained in the publication Analysis of the sector accounts:
https://www.czso.cz/csu/czso/cri/analyza-ctvrtletnich-sektorovych-uctu-1-ctvrtleti-2022

[18] Unless stated otherwise, data given below regarding the budget of sector VI are expressed after seasonal adjustment.

Nearly all member states recorded a positive shift.

and Malta (where a mild increase manifested). The debt in the Union was nevertheless higher by 10 p.p. compared to the lowest indebtedness level from the year of the pre-pandemic boom (period 2014 till 2019), by nearly 20 p. p. (+13 p.p. in the CR) in the most affected states (Greece, Italy, Spain, France). On the contrary only Ireland fared considerably better than before the pandemics (−4 p.p.). This year's indebtedness corresponded to the level from the end of year 2019 in Denmark and Sweden and both countries thus solidified their position among the least indebted economies. The indebtedness rate arrived at 42.8% of GDP in the CR, which marked the eighth lowest value in the Union and at the same time still sovereign best position among the Central European states.