

8. State Budget

State budget ended in deficit in H1, which deepened year-on-year. Brisk growth of current as well as capital expenditures stood in the background, together with mild slowdown of economic growth.

Insurance receipts as well as higher tax collection positively affected the growth of total revenues, moderate decrease of revenues from the EU budget then negatively.

Collection of VAT strengthened during the half-year, but lagged behind both the budget anticipations and final consumption dynamics of government as well as households.

Growth of income tax of natural persons from dependent activity stopped accelerating, its pace still overtook the level of business cycle peak in the last decade.

State budget (SB)¹ ended in deficit of 20,7 bn in H1 2019. Budget balance worsened year-on-year for the third time in a row and thus moved into deficit similarly to the last year. While total SB revenues strengthened by 8.1% year-on-year and expenditures by 10.2%, their rates of growth perceptibly exceeded the annual budget anticipations. SB balance, which presents a dominant item of the budget deficit or surplus of the government institutions sector, attained -0.8% in relation to the nominal GDP in H1 (-0.2% a year ago). Deeper deficit reflected this year's brisk growth of weight significant current expenditures, as well as the acceleration of the investment activity. Moderate slowdown of the economic performance also played a role, since the dynamics of total tax incomes (including insurance) eased its pace to the four-year minimum (+5.9%, +6.2% a year ago).

Year-on-year growth of total SB revenues (by 55.8 CZK bn) was by nearly three quarters pulled by higher tax incomes (including insurance). Non-tax and capital revenues also had a favourable impact (by one sixth higher year-on-year), since the moderate decrease of revenues from the EU budget (by one tenth, resp. 6.6 CZK bn)² was offset by a onetime transfer of 18.0 CZK bn from the privatization account. Mainly higher collection of insurance on social security (+20.8 CZK bn) contributed to the stronger all tax incomes (similarly to year 2018), total tax collection enjoyed only slightly weaker effect.

SB raised on the weight dominant tax – VAT – by 3.0% more year-on-year in H1, and even though the growth rate strengthened during the year³, it still lagged behind the budget anticipations. Pace of VAT collection was slowing already third year in a row and did not approach the growth dynamics of final consumption expenditure of households (5.7%) or government institutions (8.5%)⁴ so far. Collection of all consumption taxes rose by 3.9% due to higher collection of all main types of tax. For the most significant tax by volume on mineral oils, it strengthened by 2.3%⁵ and managed to stay on the level of budget anticipations thanks to higher dynamics in Q2 itself. Collection of tax on tobacco products recorded higher rate of growth despite the fact, that the rates were not raised this year (for the first time since 2011). Its collection however fluctuates during the year, mainly for the reasons of frequent prestocking.

Income tax of natural persons from dependent activity (employment) further added the most to the growth of the state-wide collection of direct taxes. It strengthened by 13.3% year-on-year, slightly below the level of budget anticipations. Despite the pace of collection not strengthening any more in contrast to years 2016 till 2018, it still exceeded the dynamics from the business cycle peak period in the last decade. Record number of working persons and further also the brisk growth of average earnings, especially in services was also instrumental in this. Tax on capital income also recorded a double-digit growth exceeding the budget anticipation. Collection of income tax of natural persons associated mainly with the volume of sales flowing from small businesses enlarged as well. The swift growth of the domestic demand was still evident here, widening of tax rebates and tax benefits (e.g. on children) had the opposite effect. State-wide collection of the

¹ Unless stated otherwise, all data related to the state budget stem from the data of the Ministry of Finance regarding the cash fulfilment.

² These revenues also contain the revenues from so called Financial mechanisms (*EEA and Norway Funds, Swiss – Czech Cooperation Programme*). Their decrease in H1 2019 was affected by exceptionally high last year basis – SB acquired part of final payments related to the already concluded programme period 2007 to 2013 (in the amount of 20.4 CZK bn) in H1 2018.

³ Volume of VAT collection stagnated year-on-year in Q1 2019, it grew by 5.9% in Q2. Slower pace was partially also connected to the year-on-year lower volume of retained excessive deductions by Financial Administration at the beginning of the year. The most up-to-date data so far also proved the dynamism of the VAT collection during this year – VAT collection strengthened in total for the first eight months of the year by 5.2% year-on-year.

⁴ Both values express the year-on-year rate of growth of the nominal not-seasonally adjusted consumption for H1 2019.

⁵ It also corresponds to the more detailed CZSO data related to the natural consumption of oil products. Consumption of diesel fuel (+2.4%) as well as kerosene (+3.6%) increased year-on-year, decrease occurred on the contrary for petrol (-0.2%) during the first five months of year 2019.

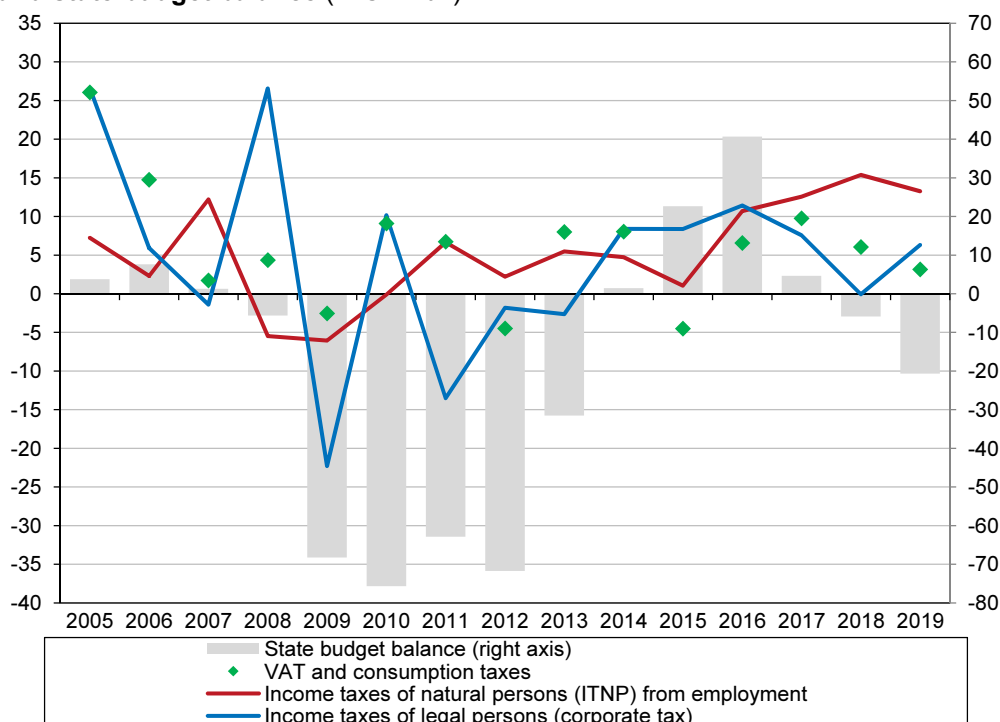


corporate tax rose by 6.3% and reflected the decreasing profitability of businesses, mainly because of intensifying wage costs, but also relatively weaker last year's basis of this tax.

Positive net position of the CR towards the EU budget hiked to the three year maximum in H1.

Even though a moderate decrease of SB revenues from the EU budget occurred this year compared to H1 2018 (including financial mechanisms), this drop was not related to the current programme period (2014–2020). It is also proved by the net position of the CR towards the EU budget. It attained +24,4 CZK bn in H1 and it was the highest for the last three years in this time period. Considerable increase of revenues (from 32.9 to 53.9 CZK bn) was exclusively behind the strengthening of the net position this year. Size of payments of the CR into the EU budget expanded year-on-year (by nearly one third to 29.6 bn.)⁶. Stronger revenues mirrored faster drawing especially from structural and cohesion funds (+17.5 CZK bn) and also in the programmes aimed at rural development.

Chart 17 State wide collection of selected tax incomes (year-on-year in %) and state budget balance (in CZK bn) in H1



Source: MF CR

Faster drawing of funds from the EU budget stood behind the strengthened investment activity of the state.

Total SB expenditures increased by one tenth year-on-year in H1, similarly to the same period of year 2018. Both current (+58.1 CZK bn) and capital expenditures (+12.5 bn) added to the growth this year. More than 70% of investment was aimed at the common CR and EU projects⁷, their volume expanded by nearly 10 CZK bn year-on-year. Investment drawing has been only 36% of the annual planned budgeted amount at the end of June this year (similarly to last year), mainly because of slower onset of solely national investment (17%). Proportion of investment on all SB expenditures was rising already second year in a row and amounted to 6.0% (average for the whole decade was 6.6%).

Growth of current SB expenditures accelerated mostly due to the effect of higher expenditures on

Rate of growth of current SB expenditures strengthened within H1 already third year in a row. It climbed to 8.8% this year, the most in the last thirteen years. Higher expenditures on social benefits shared in it by nearly one third (growth of 22 CZK bn). Expenditures on wages in the regional education (+13.7 bn) also added significantly as well as the wages in

⁶ For the most part a varying timing of mandatory payments of the CR within this year stood behind this development, which was connected to the prepared exit of the Great Britain from the EU.

⁷ Total expenditures (incl. current) to finance common EU and CR programmes summed 65.8 CZK bn in H1, by 15.2 CZK bn more year-on-year.

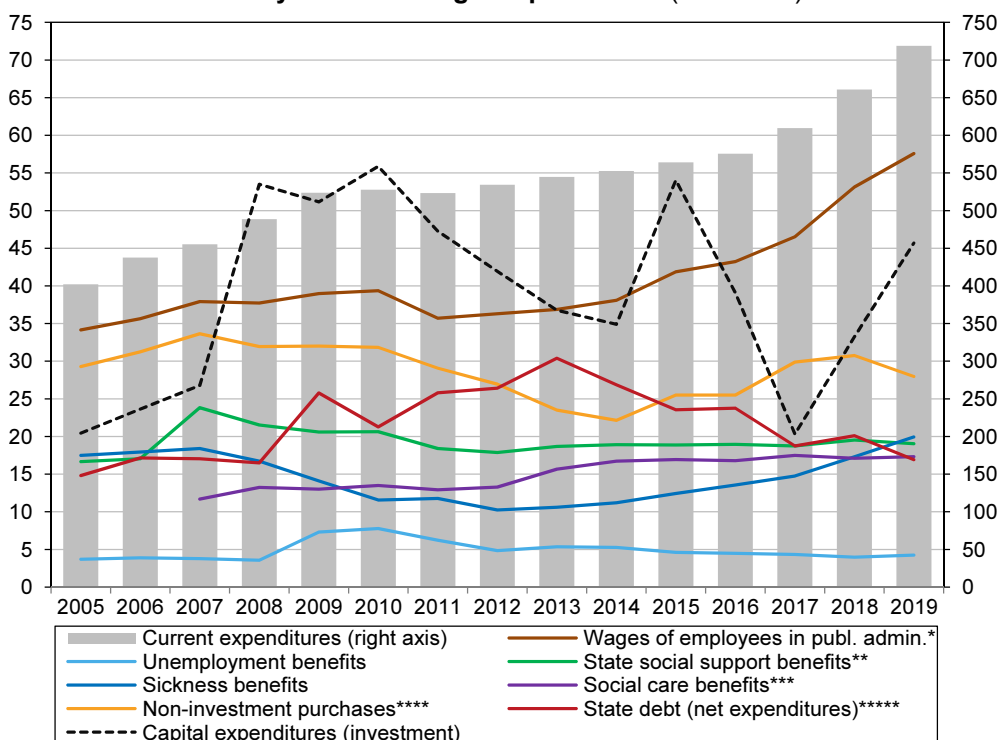
pensions and wages of employees in the budget sphere.

the central government institutions including the armed and police forces (+4.4 bn) and further then the non-investment transfers to state funds as well as higher compulsory payments into the EU budget.

Pension account balance slightly decreased, but remained in surplus.

Proportion of social benefits in all SB expenditures totalled 39.2% and it was falling for the second year in a row. Increase of the volume of social benefits was from 86% pulled by the resources on pensions. Their growth rate doubled compared to the beginning of the last year (to 8.8%) and reached a ten-year maximum at the same time. Given the stagnation of the number of persons receiving pensions, the effect of the legislative amendments fully showed⁸. Expenditures on pensions overtook the rate of growth of the collected insurance (+7,8%)⁹ for the first time since year 2013. Pension account balance¹⁰ thus mildly worsened, still it remained positive already second year in a row (+7.7 CZK bn).

Chart 18 Selected half-year state budget expenditures (in CZK bn)



*Cover expenditures on salaries in central government institutions (including armed and police forces). Do 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).
 **** 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

Growth of expenditures on non-pension social benefits was driven by higher drawing of sickness benefits.

Expenditures on other social benefits (excluding pensions) amounted to 64.9 CZK bn in H1, they increased by 4.8% year-on-year. Their growth rate was expanding already fourth year in a row. This development was considerably affected by the sickness insurance benefits, whose drawing deepened by 15.3%¹¹ and nearly doubled in the last seven years.

⁸ It included the increase of the basic pension assessment from 9% to 10% of the average wage, percentage pension assessment by 3.4% and further the increase of 1 000 CZK for pension recipients, who reached the age of 85 years. Pension adjustment mechanism further fully reflects the impact of the consumer price growth (altern. the growth of the living costs of pensioners) since year 2018 and one half of the growth of real wages in the economy is also taken into account.

⁹ Rate of year-on-year growth of levied insurance on pensions slowed this year for the first time after five preceding years. It jumped to record +10.7% in H1 2018. This development corresponded to the moderate slowdown of employment growth in the economy as well as likely peak of average wage dynamics achieved last year.

¹⁰ Expressed as the difference between revenues and expenditures on pensions from the SB. Expenditures on administration of the pension insurance system are not included (they arrived at 6.4 CZK bn according to the MF data for the whole year 2018).

¹¹ Continuing growth of the temporary incapacity for work stood behind it (based on the MLSA data, the number of reimbursed days of sickness leaves increased by 6.7% in H1). Daily assessment basis of this benefit also increased (derived among other things from the



<p>Improvement of the financial situation of households was reflected in the lower SB expenditure on both material deprivation assistance benefits and state social support benefits.</p>	<p>They thus became the most significant group of social benefits by weight for the first time after year 2008 when they replaced the state social support benefits (SSS) in this role. Their drawing on the contrary decreased by 2.5% this year, the most in the last seven years. Among SSS sub-benefits, only foster care benefits strengthened. All income-tested benefits (e.g. child allowances) and weight dominant parental allowances (−0.8%) went down. Reduction of expenditures on material deprivation assistance benefits (by 21% year-on-year, by 60% in five years) also emphasised more favourable financial situation of households. The shrinking of expenditures on unemployment benefits on the contrary halted after five years, besides other things also due to high proportion of its friction component and growth of the size of average monthly benefit (derived from previous job earnings of the job applicant)¹².</p>
<p>Size of the state debt remained stable. Borrowing need was realised via issue of medium and long-term bonds on the domestic market.</p>	<p>State debt reached the size of 1 712.6 CZK bn at the end of June 2019. Year-on-year it nearly did not change, it mildly fell compared to the preceding quarter (by 1.1%). State kept realising its borrowing need exclusively on the domestic market. CZK value of the foreign debt thus narrowed year-o-year (by 38.6 bn) and the share of external debt in total indebtedness arrived at 12.6%, which was the least since the end of 2004. State issued medium- and long-term bonds in the amount of 200.6 CZK bn during H1, more than three fifths of them had maturity above 10 years. State used the opportunity of favourable conditions on the domestic financial market (yield of state bonds along the longer end of the yield curve hit the lowest level since the end of year 2017). Non-residents prevailed among the owners of CZK bonds (42.3%), their proportion mildly grew since the beginning of year 2018. Trend of cutting the net outlays on the state debt servicing continued. These costs were 16.9 CZK bn for H1 and decreased by nearly one sixth year-on-year, by nearly one half in the last six years.</p>
<p>Trend of decrease of net expenditures on state debt continued.</p>	<p>Consolidated debt of the whole government institutions sector¹³ totalled 1 837 CZK bn according to the CZSO data at the end of Q1 2019 and was raised quarter-on-quarter (+102 CZK bn). Indebtedness rate was 34.0% of GDP, it fell by 1.8 p.p. year-on-year, solely thanks to the brisk growth of the nominal GDP. Government institution sector attained a very mild budget deficit in the amount of 2.3 CZK bn¹⁴ in the CR in Q1, it showed nearly balanced budget also in the same period of the last year. Balance of central government institutions budget worsened by 9.6 CZK bn year-on-year and finished in 26.1 bn deficit, while the local government institutions budgeted with a surplus of 20.4 CZK bn (higher by 6.0 bn year-on-year). Budget of the social security funds (health insurance companies) did not change year-on-year and reached a surplus of 3.4 CZK bn.</p>
<p>Indebtedness rate of the government institution sector shrank year-on-year. Budget was in practice balanced, local government institutions attained surplus.</p>	<p>The Czech Republic ranked the fourth relatively least indebted EU state at the end of Q1 2019. Only small economies of Estonia (8.1%) and Luxembourg (21.3%) recorded markedly favourable figures. Further five countries reached a similar indebtedness level as the CR. Indebtedness of the whole Union was 80.7% of GDP and did not reduce quarter-on-quarter for the first time since the beginning of year 2017. Small positive shift at the level of the whole Union is the result of prevailing high indebtedness of the majority of significant EU economies (apart from Germany). Indebtedness slightly enlarged in five EU countries year-on-year, beside others in Italy (to 134.0%), France (99.7%) and Greece (181.9%). Only less than half of the euro area members complied with the Maastricht deficit criterion at the level of 60% of GDP at the beginning of the year, only the Netherlands among the</p>
<p>The CR still maintained the position of fourth relatively least indebted EU economy.</p>	<p>Only less than half of the euro area members complied with the Maastricht deficit criterion at the level of 60% of GDP at the beginning of the year, only the Netherlands among the</p>
<p>Lowering of the indebtedness rate manifests only very slowly in EU, despite</p>	<p>Only less than half of the euro area members complied with the Maastricht deficit criterion at the level of 60% of GDP at the beginning of the year, only the Netherlands among the</p>

size of previous earnings). Growth of the volume of paid out sickness benefits was also affected by higher drawing of maternity benefits (+7.5%).

¹² 34.7% of all registered job applicants were eligible for the unemployment benefits at the end of June 2019, 29.7% the year before. The average monthly size of the benefit amounted to 8 011 CZK in June 019, 7 382 CZK in the same time period of the last year.

¹³ Preliminary data regarding the debt and deficit of the government institution sector for Q2 2019 will be published by CZSO on 2nd October 2019, by Eurostat then on 22nd October 2019.

¹⁴ Balance of budget of government institutions adjusted for seasonal and calendar effects finished in surplus of 15.7 CZK bn for Q1, which constituted 1.1% of GDP. The adjusted surplus increased by 4.2 CZK bn against Q4 of the last year.

persisting economic growth as well as considerable reduction of budget deficit.

larger economies. Enduring economic growth was favourably reflected in the balance of the government institutions sector budget in the Union. It totalled (after adjustment for seasonal and calendar effects) only a shallow deficit (–0.6% of GDP) in Q1 and moved at the level of the business cycle peak from years 2007 and 2008 already second year in a row. Twelve union members reported surplus this year, five recorded deficit in the excess of 3% of GDP – Italy, France, Belgium and Romania like in the Q1 2018, Greece also joined this year.

