The Czech Fiscal Council

Office of the Czech Fiscal Council

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O P I N I O N

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on the development of general government finances and fiscal and budgetary policy

Pursuant to Section 21(2)(c) of Act No. 23/2017 Coll. on the Rules of Budgetary Responsibility (hereinafter "Act"), the Czech Fiscal Council (CFC) monitors general government finances. As part of this activity, it also seeks to identify risks that may negatively affect the stability of public finances in the short, medium and long term. Since September 2018, the CFC has been informing the public about its conclusions on a quarterly basis.

Initial economic situation

The Czech Republic's gross domestic product (GDP) grew by 2.8% year-on-year (y-o-y) and 0.8% quarter-on-quarter (q-o-q) in the third quarter of 2025. As in the previous two quarters, the preliminary data on economic performance were revised upwards again. Both domestic and foreign demand contributed to the growth. Household consumption grew by 3.0% (y-o-y) and gross capital formation (investment and inventories) by 3.3% (y-o-y). Exports of goods and services grew by 3.4% y-o-y, with exports (predominantly of services), which grew by 1.0% q-o-q, contributing most to GDP growth in q-o-q terms.

Economic growth is being driven by an increase in the number of hours worked and higher employment, while labour productivity is stagnating. Total employment rose by 1.0% y-o-y in the third quarter and the total number of hours worked by as much as 2.8%. Gross value added (GVA) showed similar dynamics to GDP in the third quarter, rising y-o-y mainly in construction (9.7%), trade, transportation, accommodation and food service (3.4%) and information and communication (7.5%). By contrast, it stagnated in manufacturing (+0.3%). This is reflected in the sectoral dynamics of growth in hours worked, employment and wages. Wages and salaries in the economy rose by 7.8% y-o-y. The inflation rate has been within the CNB's tolerance band for some time (2.5% in October), with a lower rate of growth in goods prices (1.3%) and a higher rate of growth in services prices (4.6%) persisting. This is also due to the impact of prices in the housing sector as rents rose by 5.8% y-o-y, while electricity prices fell by 3.6% and natural gas prices by 7.9% in y-o-y terms.

If the Czech economy stagnates in the last quarter of this year, it will achieve y-o-y growth of 2.4%, with growth expected to be around 2% again in 2026. Growth should be driven mainly by continuing recovery in household consumption as a result of the expected continued growth in real wages. Germany's fiscal policy may also have an impact on the growth of the Czech economy, with German public spending in 2026 expected to increase by 1 pp of GDP compared to 2025 as a result of the fiscal package[1] announced in March this year. The German general government deficit is expected to widen from 2.7% of GDP in 2024 to 3.1% of GDP in 2025 and then to 4.0% of GDP in 2026.

[1] The package includes an exemption for all defence spending above 1% of GDP, the creation of a €500 billion fund for infrastructure and climate investments and loosens expenditure rules for the federal states.

General government finances and fiscal policy settings for the coming years

The situation of Czech public finances did not change significantly at the end of November. The imbalance is mainly due to the state budget, which ended up with a cash deficit of CZK 232.4 billion at the end of November, although **the deficit adjusted for revenues and expenditures related to EU projects was significantly more favourable, at CZK 216.4 billion**. The revenue side of the state budget is significantly positively affected by the economic recovery. Tax revenues at the national level show a solid y-o-y increase of 8.2%, contributed to by both income taxes, as the growth in corporate income tax revenue (excluding windfall tax) is 12.8% and personal income tax paid by taxpayers is 11.2%. Value added tax also maintains solid growth (6.5%), reflecting growing consumer demand. The dynamic growth in nominal wages is also reflected in the y-o-y growth in social security contributions, which is 7.1% for pension insurance and state employment policy and 6.8% for public health insurance.

The expenditure side of the state budget is developing in line with expectations. Problems that have emerged because of the unrealistic recording of certain items – in particular subsidies for renewable energy sources and the financing of non-teaching staff in regional education from September 2025[2] – are being addressed through budgetary measures and the claims arising from unconsumed expenditure.

In contrast to the state budget deficit, municipalities and regions (local government subsector) reported a cash surplus of CZK 23.4 billion at the end of October, which is less than in previous years (in October 2024, the surplus was CZK 51.6 billion, and in October 2023, it was as high as CZK 63.4 billion).[3] In the case of public health insurance companies (social security funds subsector), the slight deficit continues to deepen, amounting to CZK 4.1 billion in cash terms at the end of October.

Based on current data, it can be estimated that the accrual total general government balance for this year will be around −2% of GDP. **In terms of assessing the cash balance of the state budget, the CFC again points out that the comparable figure to the balance approved in the state budget act (CZK –241 billion) is the balance adjusted for revenues and expenditures related to EU projects**. As mentioned above, this amounted to CZK −216.4 billion at the end of November. It cannot therefore be ruled out that the final state budget balance will be around the value approved in the state budget act. The shortfall in revenues from the sale of emission allowances, where the budget had expected CZK 30 billion, but the state had only received CZK 11.7 billion at the end of November, is offset by significantly higher than expected growth in tax revenues and social security contributions. On the expenditure side, in addition to the drawdown of investment expenditure in the last month of the year, the key factor will also be the rate of use of claims arising from unconsumed expenditure, which is currently showing higher growth than in the previous year.

The development of public finances in the coming years will be significantly influenced by the form of the state budget for 2026. Its draft, submitted by the outgoing government, was returned by the Chamber of Deputies of the Parliament of the Czech Republic (PSP CR) to the government for revision on 26th November 2025. In this context, the CFC notes that the process of approving the state budget for 2026 creates another situation for which there is no comparable precedent in the history of the Czech Republic (following the discussion on resubmitting the draft state budget to the Chamber of Deputies after the elections). So far, there has never been a case where the incoming government majority returned a proposal for revision to the outgoing government, which in the meantime lost its majority in the PSP CR.[4] This has certain implications for the budgetary process. The CFC comments on some of them below:

a) In line with the CFC´s expectations presented in its Statement on 16th October 2025, the Czech Republic is heading for a provisional budget again after four years. The CFC expects that the

[2] See CFC´s Statement on the Draft State Budget for 2025.

[3] The significant y-o-y decline in the balance of local government subsector in October 2025 is mainly due to a y-o-y increase in municipal and regional expenditure on non-investment transfers to subsidised organisations in the field of education.

[4] The situation in 2012, when the budget was also returned to the government for revision, cannot be used as a precedent for this situation, as it was done with the consent of the ruling finance minister and with the support of most of the ruling coalition.

incoming government will want to ensure that the provisional budget is only as long as necessary. However, given that a provisional budget will be in place, the CFC would recommend the time available to be used for bringing the draft state budget into line with the budgetary responsibility rules enshrined in the Act. As the CFC has already stated (see Statement and Opinion), the outgoing government's draft is not in compliance with the Act as it stands. The most important issue to be resolved remains the discrepancy between the proposed expenditure of the State Transport Infrastructure Fund (SFDI) and the planned subsidy to this fund from the state budget. This discrepancy can be resolved either by reducing the fund's expenditure, by finding expenditure in other chapters of the state budget at the expense of which a higher subsidy to the fund would be realised, or by the rapid and credible creation of additional new tax revenues (e.g. as a result of changes in tax law) which would cover the higher subsidy from the state budget at the latest from the moment of approval of the state budget for 2026. According to the CFC, other solutions would only mean a violation of the current wording of the Act. In this context, the CFC points out that the new draft state budget act cannot differ in key parameters from the draft submitted if it is not to deviate from the requirements of the Act.[5]

b) Although the short-term provisional budget is more of an administrative than an economic complication, political representatives should aim to approve the regular budget as quickly as possible. Its approval by the PSP CR gives the government the legitimacy to spend taxpayers' money in the declared structure and at the same time opens space for new investment and subsidy programmes. It should be emphasised that for several organisations in the general government sector, subsidy revenues from the state budget represent part of their income, and uncertainty about their amount complicates their activities during a prolonged provisional period.

c) In addition to harmonising the new draft state budget with the Act, the CFC points out that, in accordance with the resolution (available in Czech only) of the Committee on the Budget of the PSP CR, the government may update its fiscal revenue forecast with new information that has emerged since the draft state budget was approved in September this year. The CFC would consider such a step to be in line with the Act, provided that the new forecast is verified in a timely manner by the Committee on Budgetary Forecasts (Committee). **However, the CFC points out that the expected improvement in the macroeconomic situation in 2026 has already been taken into account in the increase in general government revenues approved by the Committee at its meeting on October 30, 2025 (see Committee Opinion; available in Czech only) and which is already reflected in the existing draft state budget, which the PSP CR has returned for revision. Expectations of massive new revenues from this source are therefore unrealistic.**

d) Regarding the discussion on the possible state budget balance, the CFC points out that its amount is calculated based on the parameters contained in the current version of the Act and cannot be deviated from. The Act contains a trajectory for the y-o-y reduction of the general government structural balance, which is nothing new in the Czech legal system, although this is often misinterpreted in the public. **The Act in its current wording has been in force since 2023, and the budgets for 2024 and 2025 have already been drawn up based on its principles. The year 2026 should be the third in a row to respect the logic and quantitative requirements of the Act.** At the same time, the CFC points out that when this part of Czech legislation was approved as part of the so-called consolidation package, no one on the political scene protested, no amendments were tabled, and there was not even a strong political debate on the floor of the PSP CR. The CFC concluded that this trajectory is considered acceptable and even desirable by both the ruling and opposition political parties. Moreover, the path of improving the structural balance is only intended to return Czech public finances to the trajectory that was defined by the Act as sustainable even before the onset of the Covid-19 pandemic.

[5] In accordance with the Act, it is possible to consider that strictly earmarked expenditure for the repayable financial assistance to company “EDU II”, which is responsible for the construction of a new nuclear power plant in Dukovany, could be removed from expenditure if there is a realistic assumption that the European Commission will not issue a notification of the extension of public support in next year and that alternative private financing has been secured for the time being.

e) The CFC also points out that the setting of Czech public finances is also influenced by the current fiscal rules of the European Union, particularly the so-called net expenditure path. The calculation of this path, presented in the Fiscal-Structural Plan of the Czech Republic for 2025–2028 period, assumes a similar development of general government structural deficits as the current wording of the Act.

f) Furthermore, in connection with the discussion on the general government deficit, it is also necessary to mention the macroeconomic aspect. According to the CFC, it is not easy to justify why the Czech Republic should require a fiscal impulse in the current macroeconomic situation, i.e. an effort to push the economy very likely above its potential through debt-financed government expenditure. According to the current macroeconomic forecast, the Czech economy is in an upward phase of the cycle and is heading towards closing the negative output gap in the second half of next year.

g) The CFC also believes that the Czech Republic should not lose its advantage in the form of relatively low general government debt and a declining deficit trajectory. There are several countries in the EU that find themselves in a difficult situation characterised by a combination of high fiscal deficits and low economic growth. Among post-socialist countries, this applies in particular to Romania, whose general government deficit is expected to reach 8.4% of GDP this year and, despite improvements, will remain around 6% of GDP in 2026 and 2027.[6] All this is accompanied by very weak economic growth, which will come close to 1% this year and next. A serious situation can also be observed, for example in France, whose general government deficit will reach of 5.5% of GDP this year, with the deficit improving only marginally in 2026 and 2027. All this with general government debt close to 120% of GDP and the burden of political instability.

h) As it has done many times in the past, the CFC also points out that Czech public finances should create sufficient space for the pressure that demographic change will bring from the middle of the next decade, particularly in the pension and health care systems, as well as in long-term care expenditure.[7]

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[6] However, all our neighbours also report general government deficits. According to the European Commission's autumn forecast, the deficit in Poland should reach 6.8% of GDP this year, 5.0% of GDP in Slovakia and 4.4% of GDP in Austria. Even Germany, which until recently had been fiscally responsible, is likely to exceed the Maastricht 3% limit this year, as well as in 2026 and 2027. Countries such as Hungary (this year's deficit is estimated at 5.1% of GDP) and Bulgaria (3.0%) are in no better shape.

[7] For more details, see CFC (2025): Report on the Long-Term Sustainability of Public Finances 2025 (coming soon in English, currently only available in Czech).