The Czech Fiscal Council

REPORT ON THE LONG-TERM SUSTAINABILITY OF PUBLIC FINANCES

October 2025

Czech Fiscal Council

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Contents

Introduction and summary of the main trends

One of the key tasks of the Czech Fiscal Council (CFC or Council) under Act No. 23/2017 Coll., on the Rules of Budgetary Responsibility, as amended, (the Act) is to prepare a regular annual **Report on the Long-Term Sustainability of Public Finances** (the Long-Term Sustainability Report) and, in accordance with Section 21 of the Act, to submit it to the Chamber of Deputies of the Parliament of the Czech Republic for discussion.

As in previous Long-Term Sustainability Reports, this year CFC assesses the situation of Czech public finances primarily from a **medium- and long-term perspective**. In the first case, the key assessment indicator is the current and expected structural balance, and in the second, the projected development of public debt over a 50-year horizon, which provides a model approximation of the extent of the long-term fiscal imbalance.

In last year's Long-Term Sustainability Report, the CFC stated that in 2023 public finances found themselves at a crossroads between long-term unsustainability and a return to the more moderate fiscal policy that had been typical for Czechia before the COVID-19 pandemic. At the same time, it was noted that **the first signs of a gradual improvement in the fiscal imbalance could be seen during 2024.** At the time of publication of this Long-Term Sustainability Report (October 2025), with the benefit of a further year's hindsight, it is possible to confirm that the signs seen the year before last have translated into a noticeable move towards more sustainable public finances. This can be demonstrated by the fact that in 2024 **the overall general government deficit reached a value close to 2% of gross domestic product (GDP) and we expect a similar ratio this year. These are by far the best economic results since 2019 and also the lowest deficits in direct comparison with all of the Czech Republic's neighbouring countries**.

However, as was the case last year, it must be emphasised that a necessary prerequisite for continuing the favourable trend is to maintain the changes that were prepared and approved in 2023 and implemented in 2024, and not to worsen the fiscal trajectory with new inappropriate revenue or expenditure measures. And not only that – looking ahead to the coming years, it is already clear that in order to comply with national fiscal rules, any government emerging from this year's elections to the Chamber of Deputies of the Parliament of the Czech Republic will have to **present, at the latest in the draft state budget for 2027, further consolidation measures that will definitively return Czech public finances to a sustainable path.** Czech legislation defines this as a structural public finance deficit of no more than 1% of GDP, and **according to the current wording of the Act, the Czech Republic is to return to this level by 2028 at the latest.** The CFC is already fairly certain that without new consolidation measures, the Czech Republic will not be able to comply with national fiscal rules as early as 2027.

This will by no means be an easy task. Although the overall state of public finances has improved in recent years, the structural component of the general government deficit has improved less markedly, from over 3% of GDP during the COVID-19 pandemic to just under 2% of GDP. In other words, although the government's consolidation efforts between 2021 and 2025 were visible, they fell short of expectations and even of its own resolutions. As explained above, the CFC therefore still cannot consider the value of the general government´s structural balance under the Act to be such that **it would define public budgets as stable and healthy**, **especially from a medium-term perspective.**

Much greater progress has **been made in the long term. Here, the CFC views very positively the changes that have been made to the parameters of the pension system, which have become known as the "small pension reform" and the "great pension reform".** The "small pension reform" mainly tightened the conditions for granting early retirement pensions and slowed down the indexation of pensions to real wages (the contribution of real wage growth was reduced from half to one third, as was the case until 2017). The "great pension reform" then brought about a gradual increase in the retirement age (albeit capped at 67) and a reduction in the replacement rates for newly granted pensions. The overall impact of all the measures of the "great pension reform" is estimated to improve the negative balance of the pension system by approximately 2 pp in relation to GDP in the worst times, i.e. at the turn of the 1950s and 1960s. **In 2024, this reform also successfully passed the assessment of the Constitutional Court of the Czech Republic.** If all the reform measures of previous years were to be annulled, the pension system deficit in the period in question would reach almost 4% of GDP, while the sum of both reforms will, according to the current CFC projection, reduce this deficit to 1.5% of GDP (for more details, see subchapter 3.1).

Thanks to the changes in the pension system described above, accompanied by changes in the demographic projection by the Czech Statistical Office (CZSO), see chapter 2, this year's Long-Term Sustainability Report is significantly more optimistic in terms of the assessment of public finance

sustainability than the previous one. **In the baseline scenario, debt at the end of the projection fell from 217% of GDP to 178% of GDP. The moment of breaching the so-called debt brake threshold (general government debt-to-GDP ratio of 55%) has shifted only slightly compared to last year's Long-Term Sustainability Report**, from **the projected year of 2038** last year **to the currently projected year of 2037,** mainly as a result of expected higher defence costs, which in the CFC's baseline projection scenario will rise to 3% of GDP by 2030.

However, demographic factors will not only manifest themselves in the deepening imbalance of the pension system. **The ageing population will also require increased healthcare spending.** According to the current projection, public healthcare expenditure is expected to rise from the current 6.4% of GDP to 7.7% of GDP over the next 50 years. In this context, it should be noted that **the CFC has repeatedly drawn attention to the deteriorating balance of the health insurance system, which will gradually fall into deficit from 2023 onwards, despite the newly codified automatic indexation of payments for state insurees,** which came into effect for the first time last year.

The stability of public finances in the coming years will also be affected by two "new" types of expenditure. The first of these is the aforementioned defence expenditure, which currently stands at 2% of GDP. However, within the North Atlantic Treaty Organization (NATO), there has been agreement on the need to increase this to 5% of GDP. Increasing defence spending will also mean increasing general government deficits, as no decision has been made at the political level to reduce other spending or increase the tax burden in order to finance defence. **This fact has also been reflected in an amendment to national fiscal rules in the form of an exemption whereby defence spending exceeding 2% of GDP will no longer be included in the general government sector's expenditure frameworks.** The impact of increased defence spending on the general government deficit and debt is discussed in subchapter 5.3.

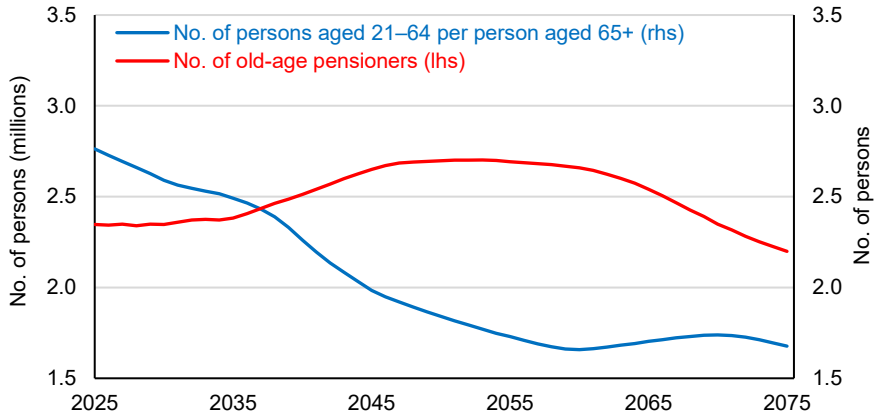
The second type of new expenditure is **the financing of the construction of nuclear reactors in Dukovany**. In this case, the situation is somewhat specific. The state will provide EDU II with a loan, which will be used to finance the construction of new reactors on an ongoing basis.

Once the nuclear facilities are operational and the electricity they produce is sold, EDU II will begin to repay the loan to the state, including interest. **While the provision of the loan by the state will be reflected in the cash balance of public budgets, the so-called Maastricht balance will not be affected. On the other hand, general government debt will increase during the provision of the loan for this purpose. However, between 2037 and 2066, when repayment is expected, this operation will have the opposite effect on debt.** At the end of the entire 50-year horizon, the general government debt will not be affected by the construction of new nuclear units in Dukovany (if the project runs according to the current schedule), see subchapter 5.5.

In connection with 2024, it is also necessary to mention the amendments to the fiscal rules of the European Union (EU). **Although their new form was approved in the first half of 2024, as we announced in last year's Long-Term Sustainability Report, EU Member States have already agreed on their partial relaxation. This is again due to the need to increase their defence capabilities and, at the same time, their unwillingness to give up other priorities, at least for a limited period.** The result is that new fiscal rules are in place, but the EU finds itself in a situation where the rules are less clear and predictable than in the past, are on average less binding on member state governments than the previous rules and are relaxed on an ad hoc basis or only partially applied right from the start. **This is happening at a time when a number of important EU countries have been struggling for many years with obvious over-indebtedness and exhausted fiscal capacity.** At the same time, there is a major fiscal turnaround in Germany, the EU's largest economy. The significant loosening of the German debt brake threatens to cause a rapid swing from a very moderate fiscal policy to an extremely loose one, and Germany is thus ceasing to be the last and largest safeguard against over-indebtedness within the entire club of eurozone and EU countries.

The CFC therefore not only continues to regard the maintenance of the stability of the Czech Republic's public finances and efforts to enforce fiscal rules as its fundamental mission but is also aware of something else this year: in terms of these statutory tasks, the coming years may bring even greater challenges than the often turbulent years of the past.

KEY FINDINGS in the baseline scenario

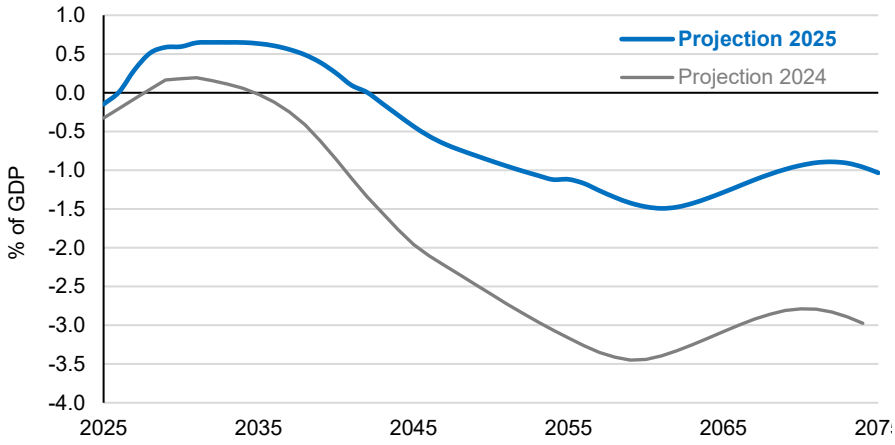


The number of old-age pensioners will peak around 2053 at about

2.7 million.

The number of 21–64 year olds per person aged 65+ will drop around 2060 to

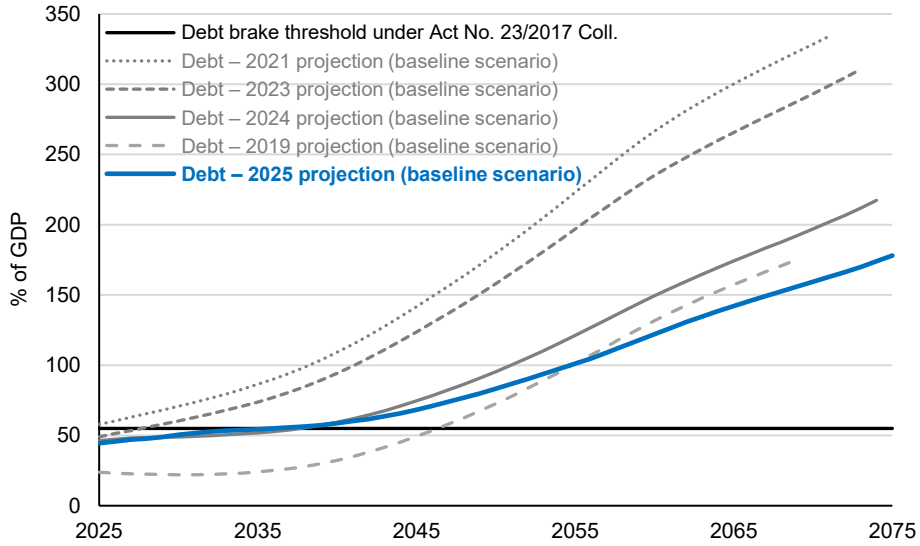
1.66.



The pension system balance will show surpluses in the medium term. In the long term, however, the system will run deficits. Nevertheless, mainly as a result of the pension system reforms, this deficit-to-GDP ratio will be up to

2 pp better

than in the previous projection during the worst times, i.e., at the turn of the 1950s and 1960s.



If the current tax and expenditure policies were maintained, the general government debt could reach

178% of GDP,

which is 39 pp less than in the 2024 projection.

According to the current projection, the debt brake threshold would probably be breached in

2037.

Public finance sustainability gap

2.88% of GDP

is the amount by which the primary structural balance would have to be better from 2025 until 2075 for the debt not to exceed the debt brake threshold (55% of GDP) in 2075.

1 Starting point

1.1 Development of the general government sector in 2024 and outlook for 2025

In 2024, year-on-year real GDP growth in the Czech Republic reached 1.2%.[1] Household final consumption expenditure contributed most to this growth (1.2 pp). In addition to a decline in the saving rate, this development reflected an increase in household disposable income, with average real gross wages rising by 4.7% in 2024 after two years of decline. The increase in real wages reflected high nominal wage growth (7.2% in 2024) and, above all, a significantly lower average inflation rate. After two years of very dynamic price developments (15.1% in 2022 and 10.7% in 2023), the average inflation rate reached 2.4% in 2024. The trade balance also had a positive impact on real GDP growth in 2024 (0.6 pp). Among other things, the geographical diversification of exports outside the euro area and exports of motor vehicles contributed to the positive balance. Although imports of goods were boosted by household demand, they were dampened by low domestic investment activity and lower imports of energy commodities. Government final consumption expenditure (0.6 pp), reflecting, among other things, expenditure related to the Recovery and Resilience Facility, also contributed to real GDP growth. The balance of services also had a slightly positive effect (0.1 pp) on real GDP growth. Gross capital formation significantly dampened year-on-year real GDP growth, with gross fixed capital formation contributing more to the decline (−0.8 pp) than changes in inventories (−0.5 pp). Investment (gross fixed capital formation) was negatively affected by the situation in the euro area, a decline in construction activity in the domestic economy and low capacity utilisation in industry. Investment activity was also weaker in the general government sector. The decline in inventories reflected a reduction in work in progress and a return to "normal" accumulation of production inputs after their accumulation during 2021–2023. From a business cycle point of view, the Czech economy was below its potential, with the output gap according to the Ministry of Finance of the Czech Republic (MF CR)[2] amounting to −1.8% of potential output.

The general government balance improved by approximately 1.5 pp compared to 2023, reaching a deficit of 2.2% of GDP (CZK 177.2 billion) in 2024.[3] This result was negatively affected by the deficit of central government institutions (2.6% of GDP) and social security funds (0.2% of GDP). On the other hand, the surplus of local government subsector (0.7% of GDP) had a positive effect on the overall balance of the sector.[4]

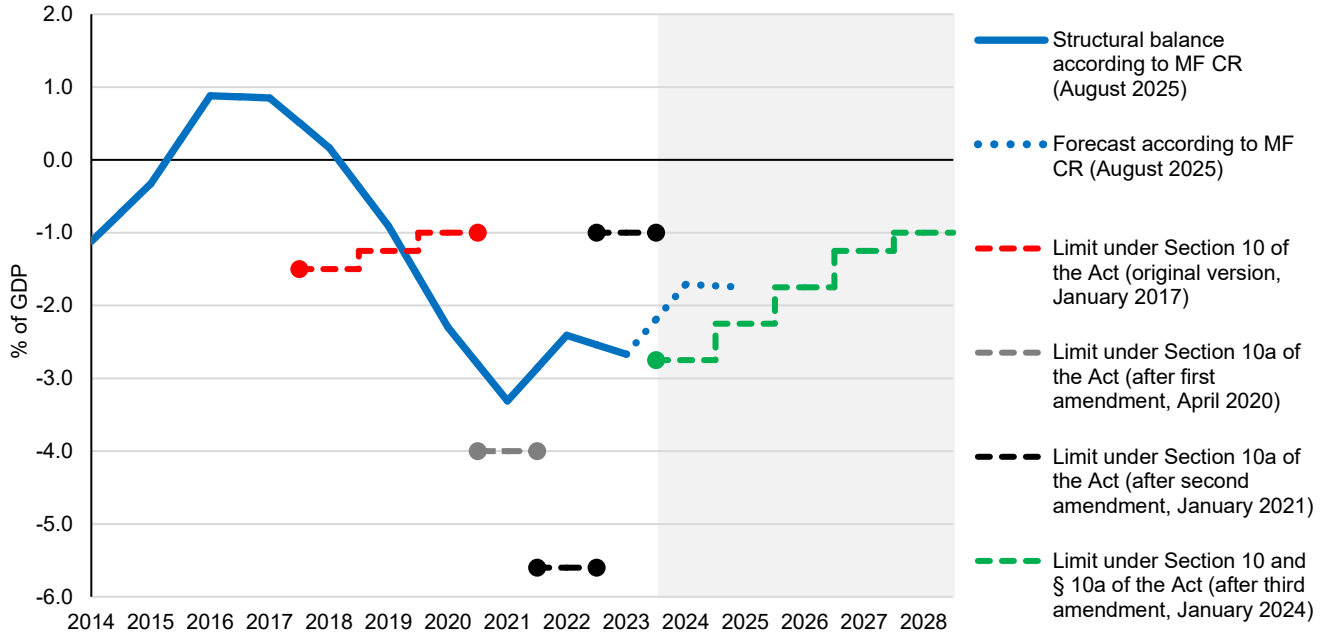
The general government structural balance reached −1.9% of GDP[5] in 2024. Compared to 2023, the structural balance improved by approximately 0.8 pp. The year 2024 was the first year for which the third amendment[6] to the Act set a structural balance limit (−2.75% of GDP) with an annual tightening of the limit by 0.5% of GDP in 2025–2027, see the green dashed line in Chart 1.1.1. In 2028, the 1% structural deficit limit specified in the original wording of the Act should be applied again.

According to the August macroeconomic forecast of the MF CR[7], the structural deficit should reach 1.7% of GDP in 2025 (see the dotted blue line in Chart 1.1.1). The high structural deficit for 2024 and 2025 clearly shows that even after the negative shocks of the COVID-19 pandemic, the energy crisis and the wave of inflation have subsided, it is still very difficult to change the structure of general

[1] CZSO (August 2025): Public database, MF CR (August 2025): Macroeconomic forecast of the Czech Republic.
[2] MF CR (August 2025): Macroeconomic Forecast of the Czech Republic.
[3] According to the MF CR (August 2025): Macroeconomic Forecast of the Czech Republic, the total balance of the general government sector for 2024 is CZK −161 billion (−2.0% of GDP). The improvement in the balance was due to higher revenues from personal and corporate income tax and windfall tax. However, these data have not yet been notified by Eurostat as part of the so-called second notification (the Czech Statistical Office will publish this on 21 October 2025), so we provide data confirmed by Eurostat as part of the so-called first notification (see https://csu.gov.cz/rychle-informace/notification-of-government-deficit-and-debt-2024-first-notification-data-notified-by-eurostat).
[4] CZSO (2025): Public database, Government finance statistics. The sum of the balances for individual subsectors is subject to inaccuracy due to rounding.
[5] The calculation of the structural balance for 2024 used the total balance of the general government sector according to the CZSO (2025): Notification of government deficit and debt - 2024 (First notification, data notified by Eurostat) published on 22 April 2025. The cyclical component of the balance and one-off and temporary measures were taken from the MF CR (August 2025): Macroeconomic forecast of the Czech Republic. Chart 1.1.1 (dotted blue line) shows the structural balance for 2024 according to the MF CR (August 2025): Macroeconomic Forecast of the Czech Republic. I.e. this structural balance is based on the overall balance of the general government sector, the amount of which has not yet been notified by Eurostat (as part of the second notification), and therefore the structural balance for 2024 is considered a forecast. See also the note below Chart 1.1.1.
[6] Box 2.1 in the 2022 Long-Term Sustainability Report describes the first two amendments to the Act of 2020 (implemented by Acts No. 207/2020 Coll. and No. 609/2020 Coll.). The third amendment to the Act (implemented by Act No. 349/2023 Coll.) is presented, for example, in the Office of the CFC (2024): Výroční zpráva za rok 2023 [Annual Report for 2023, available only in Czech], subchapter 4.1, and in the 2024 Long-Term Sustainability Report in subchapter 1.1.
[7] MF CR (August 2025): Macroeconomic Forecast of the Czech Republic.

government revenues and expenditures in the short term, despite efforts to consolidate public finances[8]. This fact has become particularly acute in the context of geopolitical development, which brings with it, among other things, increased defence spending and (future) expenditure related to demographic development (see, inter alia, chapter 3 and subchapters 5.2 and 5.3). In order to maintain the medium- and long-term sustainability of public finances, further consolidation measures are therefore needed to help comply with the expenditure fiscal rule (the structural balance rule) so that the structural deficit reaches a maximum of 1% of GDP in 2028, i.e. the limit set by the Act before its amendments.

Chart 1.1.1 General government structural balance



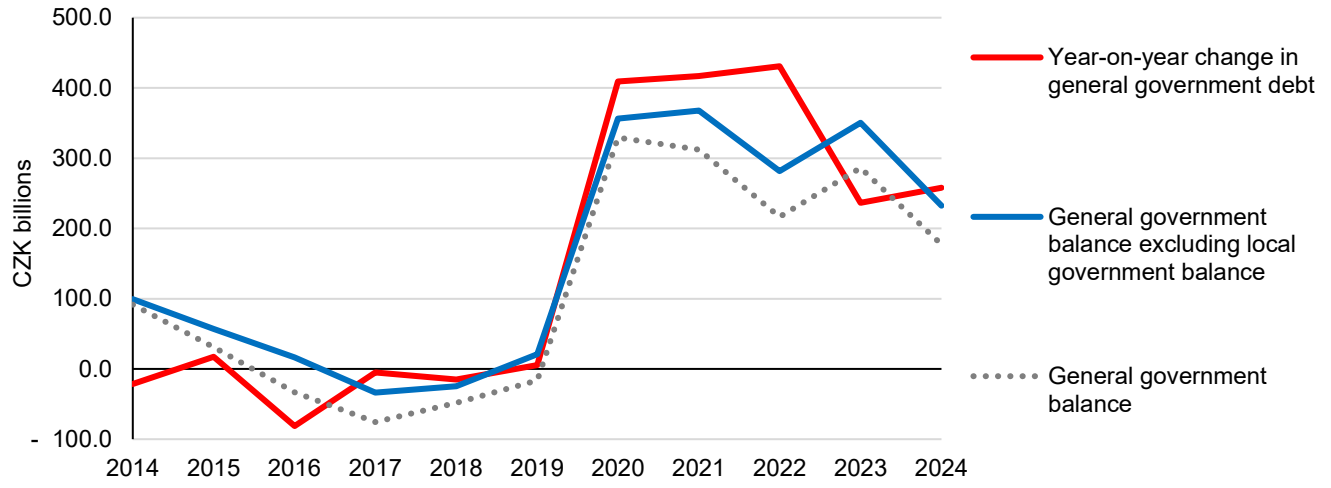
Source: MF CR (August 2024; August 2025): Macroeconomic Forecast of the Czech Republic, Act (various versions); CFC calculations.
Note: The first amendment to the Act (implemented by Act No. 207/2020 Coll.) set the structural balance limit for 2021 at −4.0% of GDP (see grey dashed line), with a subsequent year-on-year improvement of at least 0.5% of GDP in 2022–2027 (the trajectory for this period is not shown in Chart 1.1.1 for reasons of clarity). The legend of the graph shows the month and year of effect of the Act or its amendment. The structural balance for 2024 is derived from the total balance of the general government sector of −2.0% of GDP according to the MF CR (August 2025). This updated balance value for 2024 has not yet been confirmed by Eurostat in the second notification (the Czech Statistical Office will publish this information on 21 October 2025). Therefore, we consider the structural balance for 2024 shown in Chart 1.1.1 to be a prediction. In the text of the Long-Term Sustainability Report, we state the total balance of the sector for 2024 at −2.2% of GDP (according to the first notification from April 2025), or the structural balance derived from it according to the adjustments specified in footnote 5.

At the end of 2024, the debt of the general government sector reached CZK 3,491.9 billion.[9] Compared to the end of 2023, this is approximately CZK 257.8 billion more, see the red solid line in Chart 1.1.2. However, the negative balance of this sector for 2024 was “only” CZK 177.2 billion (see the grey dotted line in Chart 1.1.2), which is roughly CZK 80.6 billion less than the year-on-year change in debt. The difference between the change in the stock variable of debt and the flow variable of the balance is called the stock-flow adjustment (SFA). In 2024, the SFA reflected, among other things, the fact that the borrowing requirement of the general government sector was significantly affected by the deficit of the central government subsector (with the state budget deficit having a dominant influence), see the blue solid line in Chart 1.1.2. The surplus of the local government subsector (i.e. regions and municipalities) was not deposited in full at the Czech National Bank (CNB) in the state treasury system[10], where it could have been used, at least in part, to cover the financing need of the entire sector (the so-called cash-pooling system). The borrowing requirement of the general government sector thus had to

[8] The so-called consolidation package (Act No. 349/2023 Coll., amending certain acts in connection with the consolidation of public budgets, as amended) is presented in detail in the Office of the CFC (2024): Výroční zpráva za rok 2023 [Annual Report for 2023, available only in Czech], in subchapter 3.3.
[9] The general government debt has thus doubled from the end of 2019, when it stood at CZK 1,740.3 billion, to the end of 2024. The value of the debt at the end of 2024 (CZK 3,491.9 billion) is based on data from the Czech Statistical Office (August 2025): Government finance statistics.
[10] Regions and municipalities are not mandatory clients of the state treasury and are therefore not required to deposit their funds with the State Treasury. Instead, they may also deposit their financial resources with various other financial institutions.

be met on the financial market through the issuance of securities in a larger volume than would correspond to the balance of the entire sector. The impact of this situation on the long-term sustainability of public finances is discussed in one of the alternative scenarios in subchapter 5.4.

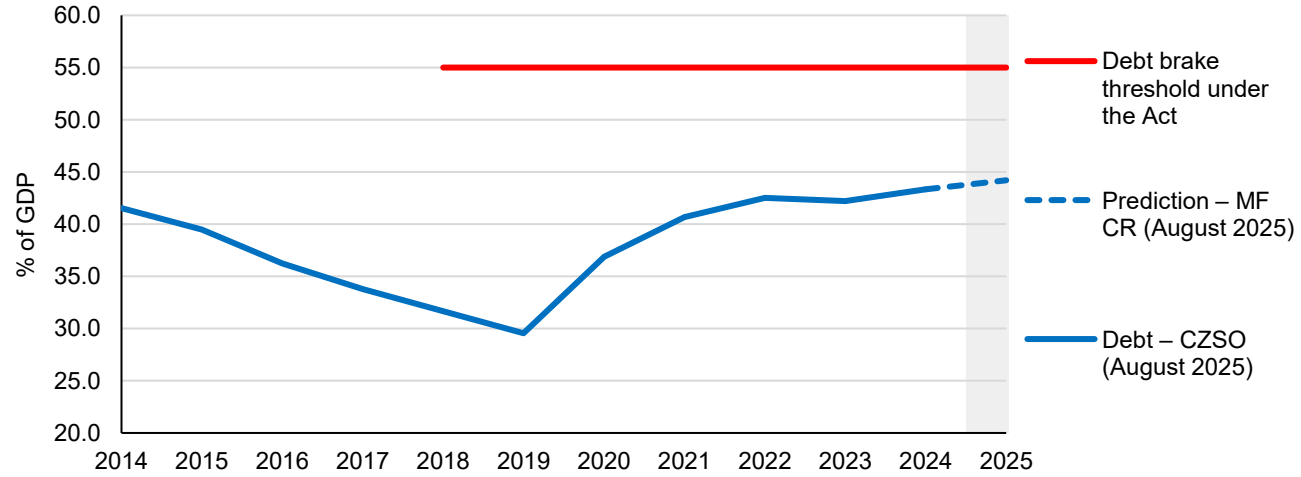
Chart 1.1.2 Total and adjusted balance and year-on-year change in debt of the general government sector



Source: CZSO (2025); CZC calculations.
Note: Balances are shown with the opposite sign, i.e. a numerical increase in the balance means a deterioration in the economic result (higher deficit). The general government balance consists of three subsectors (and their sub-balances): central government, local government (i.e. regions and municipalities) and social security funds. The solid blue time series shows the general government balance adjusted for the local government balance.

The ratio of general government debt to GDP rose by 1.1 pp year on year, reaching 43.3% at the end of 2024 (see Chart 1.1.3)[11]. The increase in the ratio was mainly driven by interest payments reflecting both the required securities yield and a significant increase in debt since the COVID-19 pandemic. The ratio also rose due to the SFA item, which was analysed earlier, and the primary deficit. Real GDP growth and changes in the price level had the opposite effect.[12] According to the MF CR[13] , the general government debt ratio is expected to be 44.2% in 2025.

Chart 1.1.3 General government debt minus the state debt financing reserve



Source: CZSO (2025), MF CR (August 2025): Macroeconomic Forecast of the Czech Republic; CFC calculations.

[11] MF CR (August 2025): Macroeconomic forecast of the Czech Republic.
[12] The application of the debt dynamics equation, which captures the factors influencing the change in the debt ratio, is provided, for example, by CFC (2025): Report on Compliance with the Rules of Budgetary Responsibility for 2024, Box 1.
[13] MF CR (August 2025): Macroeconomic Forecast of the Czech Republic.

From the perspective of the sustainability of public finances, the structure of debt holders is also important in addition to the level of debt. In other words, it also matters which entities buy and hold government debt securities (residents and non-residents). This perspective is important primarily because non-residents are more likely to sell Czech government bonds in case of increased risk aversion on financial markets. An increase in the share of debt held by non-residents leads to a change in the country's net investment position as there is an outflow of income abroad (interest payments), which has also a negative impact on the primary income balance.

Box 1.1 Revision of general government debt holdings 2021–2023

For 2021, 2022 and 2023, the government finance statistics have revised the data on Czech public debt holders. Public debt holders have been revised as part of the CNB's benchmark revision in connection with the revision of data in the Securities Holdings Database, which is managed by the CNB. Debt held by non-residents has been revised upwards for all three years, while debt held by residents has been revised downwards accordingly. The total amount of public debt for 2023 has also been revised upwards by CZK 5.7 billion (see Table B1.1.1).

Table B1.1.1 Revision of Czech public debt holdings (difference from the figures in the previous Long-Term Sustainability Report, in CZK billions)

Year	Residents	of which:				Non-residents	Total debt
		banks	other financial institutions	CNB	other residents		
2021	-63.4	-37.9	-25.6	0.0	0.0	63.4	0.0
2022	-128.9	-82.6	-49.1	2.8	0.0	128.9	0.0
2023	-37.2	-30.0	-15.2	2.8	5.2	42.9	5.7

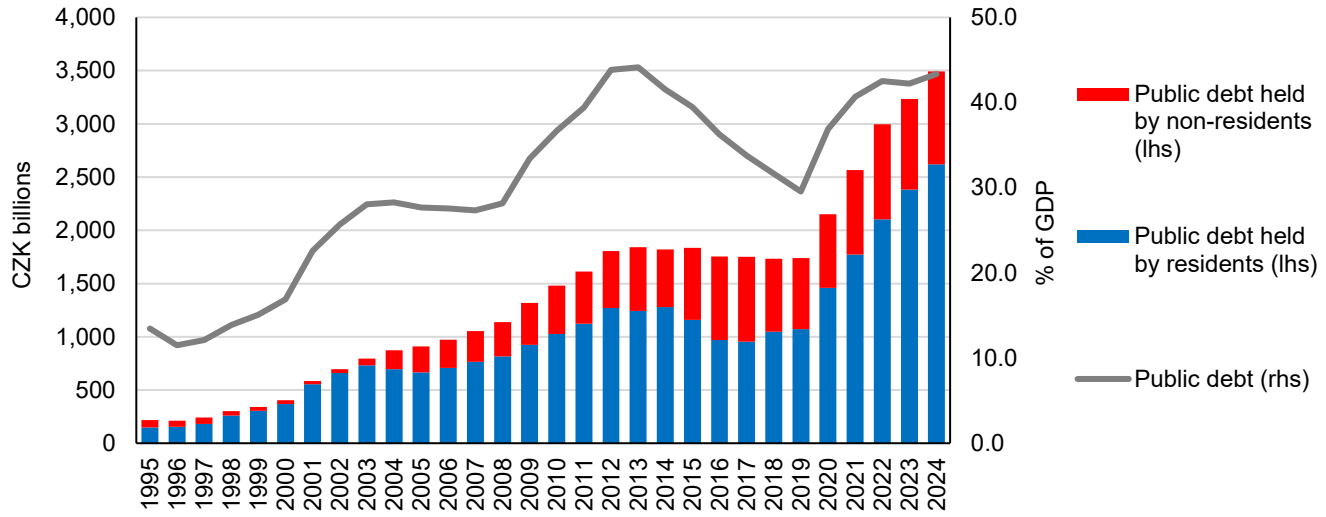
Source: CNB (2025); CFC calculations.

Despite this revision, the interpretation of public debt holders remains unchanged. Since 2020 we have observed a sharp increase in annual nominal gross borrowing requirement which has been covered by a significant increase in the share of domestic entities in public debt holdings. While residents held 61.6% of public debt at the end of 2019, this figure rose to 75.1% at the end of 2024. This is the highest level since 2004[14]. Within the resident sector, the domestic banking sector plays a key role in absorbing government bonds (see below).

At the end of 2024, residents held 75.1% of Czech public debt, with banks holding 46.2%, other financial institutions (e.g. pension funds, insurance companies) 22.4% and other entities (e.g. households) 6.5%. Non-residents thus held 24.9% of Czech public debt at the end of 2024. In line with international practice, the CNB considers 25.9% to be the critical threshold for foreign entities' holdings of public debt[15]. In terms of assessing the riskiness of the public debt structure, a massive sell-off of domestic debt by foreign investors would probably not only cause the exchange rate movements but would also increase the volatility of market prices for Czech government bonds. The 25.9% threshold has been consistently exceeded since our accession to the EU. After the revision, 2024 was the first year in which debt held by non-residents fell below this threshold, reaching the 24.9% (see Chart 1.1.4). The risk of external shocks spilling over to the domestic financial system thus decreased during 2024.

[14] Public debt held by residents in 2004 amounted to 79.5%.
[15] CNB (2022): Financial Stability Report – Spring 2022.

Chart 1.1.4 Public debt held by residents and non-residents

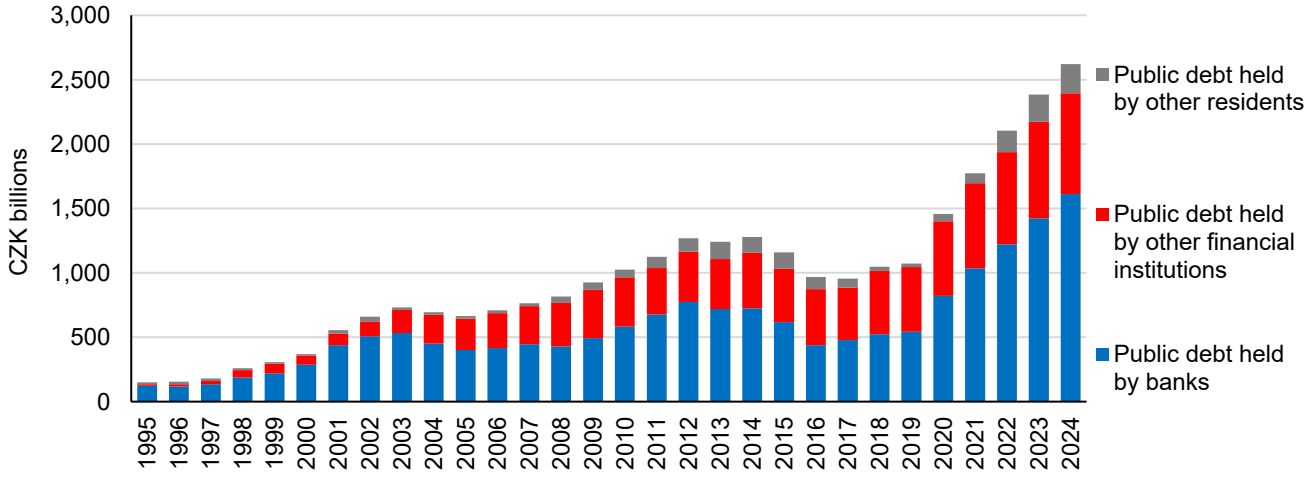


Source: CNB (2025); CFC calculations.

Public debt increased by CZK 257.8 billion in 2024, with residents absorbing CZK 236.7 billion. Of this, the domestic banking sector increased its holdings by CZK 189.7 billion and held CZK 1,612.6 billion (46.2% of total debt) at the end of 2024. Other domestic financial institutions (e.g. pension funds and insurance companies) increased their holdings by CZK 30.1 billion and held CZK 781.1 billion in debt at the end of 2024 (22.4% of total debt). Domestic financial institutions thus have a dominant share in public debt holdings.

As mentioned above, domestic banks held 46.2% of public debt at the end of 2024, which is 2.2 pp more than in 2023 and 15.0 pp more than in 2019. At the end of 2024, the ratio of public debt held by banks to banking sector assets was 15.2%, the highest since 2012, when the ratio was 16.2%. Given the relatively high and, since 2020, steadily growing share of government bonds in banks' balance sheets, an escalation of sovereign risk would have significant implications for the financial system. The CNB had already warned of the risks of sovereign exposure concentration at the end of 2020, when the value of government bonds on banks' balance sheets began to rise, accounting for 10.2% of domestic banks' total assets.

Chart 1.1.5 Public debt held by residents



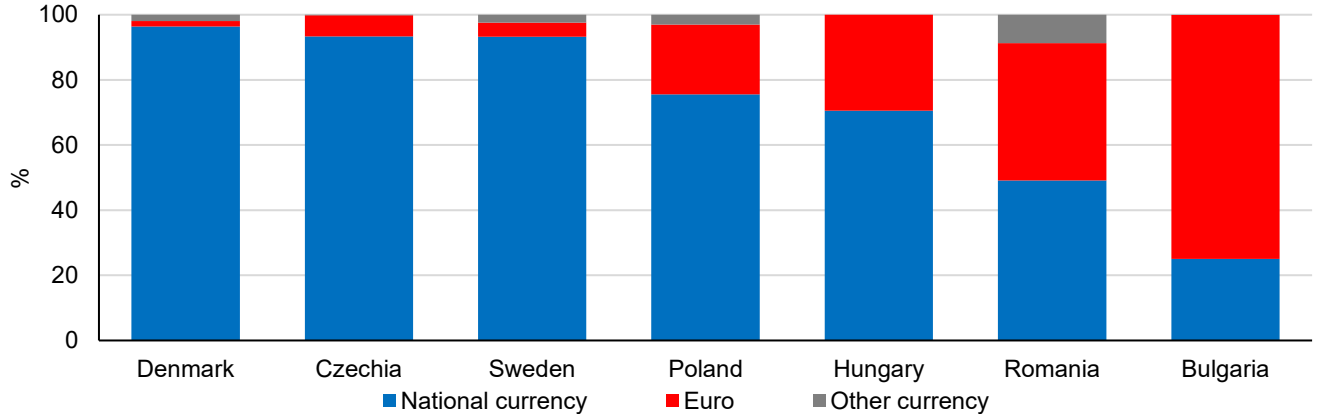
Source: CNB (2025); CFC calculations.

Public debt can also be viewed in terms of the currency in which it is issued and its residual maturity. Between 2011 and 2018, less than half of the total debt had a residual maturity of over 5 years, but since 2019 more than half of the total debt has had a residual maturity of over 5 years. At the end of 2024, this accounted for 54.7% of total debt.

Of the total public debt of CZK 3,491.9 billion (at the end of 2024), 93.2% of the debt was issued in

domestic currency and only 6.8% in foreign currency. This is the smallest share of foreign currency debt in total debt since 2003. Countries that are members of the EU but not part of the euro area issue their debt either in their national currency, the euro or another currency (Swiss franc, Japanese yen or US dollar). In Denmark, the Czech Republic and Sweden, the national currency dominates (more than 90% of debt is denominated in the national currency). Poland and Hungary have approximately 70–75% of their debt denominated in their currency, while Romania and Bulgaria have less than 50% of their public debt denominated in their currency.[16]

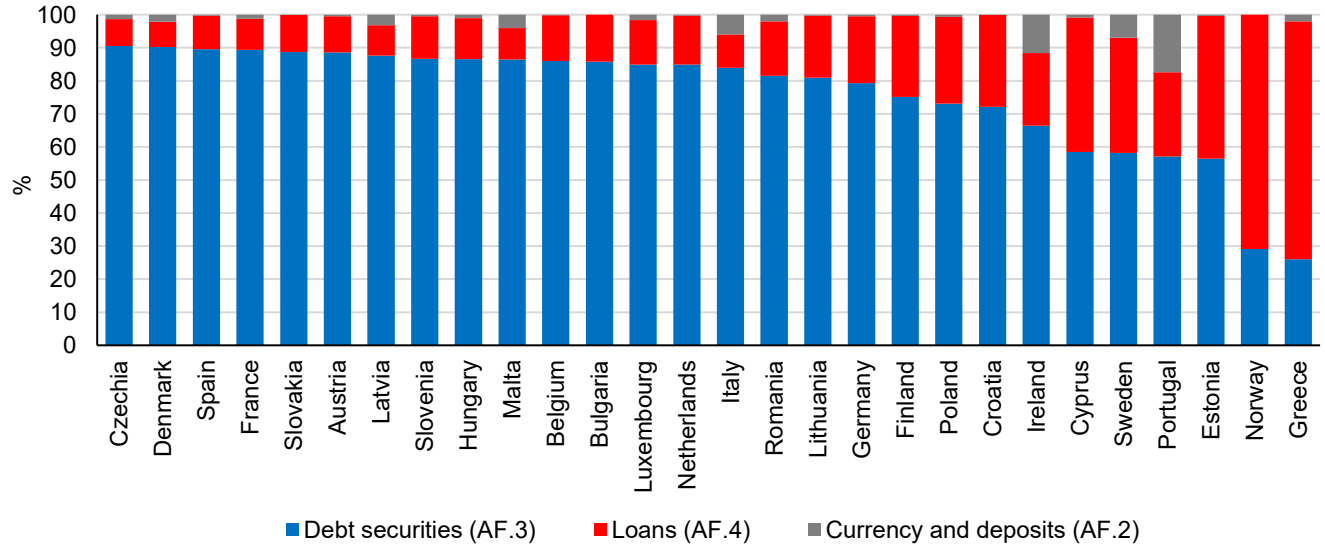
Chart 1.1.6 Central government debt structure by currency (2023)



Source: Eurostat (2025); CFC calculations.

Public debt consists of debt securities issued (statistical code AF.3), loans received (statistical code AF.4) and currency in circulation and deposits received (statistical code AF.2). The latter financial instrument (liability) is negligible in the case of the Czech Republic and consists of liabilities of the Czech Export Bank and the National Development Bank arising from their lending activities. The Czech Republic is the EU member state with the highest share of debt securities (90.5%) and, conversely, the second country with the lowest share of loans received in total debt (8.2%). Medium- and long-term government bonds issued in domestic currency thus play a key role in financing the government's gross borrowing requirement. In 2024, the average yield on newly sold fixed-rate government bonds fell to 3.95% p.a. This year, gross issuance of koruna-denominated government bonds is expected to total between CZK 350 and 450 billion. The Czech Republic has the highest credit rating of all Central and Eastern European countries and has been above the average credit rating of euro area member states for several years.

Chart 1.1.7 General government debt structure by financial instrument (2024, as % of total debt)



Source: Eurostat (2025); CFC calculations.

[16] In the case of Bulgaria, the currency board regime plays an important role.

1.2 Decomposition of fiscal effort

Fiscal effort represents the change in the structural balance between two periods. If it is negative, fiscal policy is eased; if it is positive, fiscal policy is tightened. The three basic factors influencing the level of fiscal effort are: autonomous developments (e.g. a higher share of wages and salaries in GDP leads to higher revenues for the general government sector due to higher taxation of the factor of production of labour compared to capital) discretionary government measures (intentional government measures) and factors depending on other determinants (e.g. municipal investment activity is partly dependent on the implementation of various operational programmes).

Table 1.2.1 shows the decomposition of fiscal effort for the period 2018–2024. The decomposition is carried out using the so-called indirect method, i.e. as a year-on-year change in the structural balance with subsequent decomposition. In 2024, fiscal effort reached 0.8 pp, i.e. stricter fiscal policy led to changes in the structure of general government sector revenues and expenditures, which resulted in a year-on-year improvement in the structural balance.

Table 1.2.1 Decomposition of fiscal effort (pp)

	2018	2019	2020	2021	2022	2023	2024
Taxes and social contributions	*0.4*	*-0.6*	*2.2*	*-1.4*	*-1.1*	*0.3*	*1.2*
Other revenue	*0.4*	*-0.1*	*0.1*	*-0.1*	*0.6*	*0.2*	*-0.3*
*in which one-off and temporary revenue-side measures**	*0.0*	*0.0*	*-0.7*	*0.5*	*0*	*0.6*	*0.1*
REVENUE	0.9	-0.8	2.9	-2.0	-0.5	-0.2	0.9
Compensation of employees and intermediate consumption	*-0.8*	*-0.1*	*-1.3*	*0.5*	*1.0*	*0.1*	*-0.2*
Social transfers and social transfers in kind	*0.1*	*-0.1*	*-2.6*	*0.5*	*0.6*	*-0.4*	*-0.1*
Interest	*0.0*	*0.0*	*-0.1*	*0.0*	*-0.4*	*-0.2*	*-0.1*
Investment	*-0.8*	*-0.2*	*-0.5*	*0.2*	*0.0*	*-0.3*	*0.2*
Other expenditures	*-0.1*	*0.1*	*-1.5*	*0*	*0.8*	*0.1*	*1.1*
*in which one-off and temporary expenditure-side measures**	*-0.1*	*0.1*	*-1.6*	*0.2*	*0.8*	*-0.6*	*1.1*
EXPENDITURE	-1.6	-0.3	-4.3	1.1	1.3	-0.1	-0.1
FISCAL EFFORT	-0.7	-1.1	-1.4	-0.9	0.8	-0.3	0.8

Source: CZSO (2025), MF CR (2019, 2021, 2022, 2023, 2024): Convergence Programme of the Czech Republic, MF CR (April 2025): Background for the CFC (regarding opinions on the derivation of expenditure frameworks for the state budget and state funds), MF CR (August 2025): Macroeconomic Forecast of the Czech Republic; CFC calculations.
Note: The item *Taxes and social contributions* was cyclically adjusted, other items were not. The cyclical component of the balance is taken from the MF CR (August 2025): Macroeconomic Forecast of the Czech Republic. Positive values of fiscal effort indicate a tightening of fiscal policy. The totals in the table may be subject to inaccuracies due to rounding. Fiscal effort in 2024 differs from the value published by the MF CR (August 2025), as the MF CR uses the Eurostat's as yet unconfirmed (in the second notification) general government balance for 2024 of −2.0% of GDP and the structural balance of −1.7% of GDP in its calculation of fiscal effort. The CZSO will publish the data notified (on the overall sector balance) by Eurostat on 21 October 2025. *One-off and temporary measures on the revenue and expenditure side are already included in the previous revenue and expenditure items, so they are entered into the calculation with the opposite sign.

Significant discretionary measures by the government affecting the structural balance in 2024 were mainly reflected on the government revenue side and were mostly presented as part of the so-called consolidation package.[17] The increase in personal income tax revenue, with a total effect of over CZK 8 billion, was influenced by a reduction in the threshold for applying the 23% tax rate, the abolition of the tax allowance for spouses who do not care for a child under three years of age, and the abolition of the tax allowance for placing a child in a pre-school facility. The 2 pp increase in the corporate income tax rate had an impact of CZK 21 billion. Higher taxation of tobacco products and the newly imposed taxation on tobacco alternatives resulted in an increase in revenue from this tax of CZK 4.2 billion. The year 2024 also brought increased revenue from real estate tax (CZK 10 billion) due to higher rates. The consolidation package increased revenues from social contributions by approximately CZK 18 billion (the reintroduction of sickness insurance for employees had a significant impact of CZK 13.4 billion, and an increase in contributions for self-employed persons had an effect of CZK 4.5 billion).[18]

[17] Act No. 349/2023 Coll., amending certain acts in connection with the consolidation of public budgets, as amended.
[18] Ministry of Finance of the Czech Republic (May 2025): Fiscal Forecast for the Czech Republic.

In addition to discretionary measures, Table 1.2.1 shows one-off and temporary measures on the revenue and expenditure side. These operations were widely used during the COVID-19 pandemic (2020–2021) and during the escalation of geopolitical tensions in 2022–2023 (the war between the Russian Federation and Ukraine), which triggered further increases in energy and food prices.

In 2024, one-off and temporary measures continued to include the windfall tax (CZK 40.9 billion) and extraordinary depreciation (CZK 1.3 billion) applied since the COVID crisis. On the government expenditure side, there was a significant year-on-year decline in the application of one-off and temporary measures. In 2024, humanitarian aid was provided for refugees, and a contribution was made towards their accommodation (CZK 9.7 billion). Another item included expenditure on flood damage (CZK 5.0 billion).[19]

[19] Act No. 609/2020 Coll., 65/2022 Coll., 66/2022 Coll., 198/2022 Coll., 366/2022 Coll., 75/2023 Coll.; Government Resolutions No. 207/2022, 235/2022, 689/2024, 714/2024, 733/2024, 734/2024, 736/2024, 755/2024, 798/2024, 799/2024, 823/2024, 837/2024, 850/2024, 875/2024, 876/2024, 985/2024, 990/2024. MF CR (April 2025): Background document for the CFC (regarding opinions on the derivation of expenditure frameworks for the state budget and state funds).

2 Long-term macroeconomic projection

Our long-term projection of general government expenditure, revenue and balance over a 50-year horizon is based on a projection of key relevant macroeconomic variables. The most important of these are GDP growth, employment trends, labour productivity and volume of wages.[20] We relate our fiscal projections to GDP and other variables in real terms. In contrast to the medium-term outlook, in the long-term projection we abstract from the business cycle. The estimated evolution of the economy is therefore a simulation of the evolution of potential GDP and other corresponding macroeconomic indicators. In previous periods, the Czech economy was initially negatively affected by the impacts of the COVID-19 pandemic and the anti-contagion measures in 2020 and 2021. This was followed by a negative supply shock related to the Russian Federation's invasion of Ukraine and rising energy and food prices in 2022 and 2023. In 2024, there was a partial recovery in economic activity, which should accelerate in the following years. The economic shocks mentioned above affected not only the cyclical position of the economy (negative output gap) but also estimates of current and past potential output growth in the Czech Republic and abroad.

The overall negative economic shock was very large, implying uncertainty about the starting point of our projections. This uncertainty about the starting point was also exacerbated by the large-scale revision of national accounts across EU countries in 2024. This revision meant an upward reassessment of historical GDP in the Czech Republic and affected the initial assumptions about the speed of economic convergence (see also Box 2.1).

2.1 Real convergence

As in previous years, our long-term macroeconomic projection assumes that the Czech economy is and will remain a converging economy. We continue to view Austria as the Czech economy's convergence target. Austria, like the Czech Republic, is a standard EU member state economy, and is similar to the Czech economy in size and structure.

We model the convergence process as convergence in GDP per worker, i.e. convergence of whole-economy labour productivity. We assume that the difference in labour productivity between the Czech Republic and Austria will shrink by a constant percentage each year. The gap between Austrian and Czech GDP per capita, which was estimated at 19.5% of the Austrian level in purchasing power parity in 2024[21], will thus narrow by an average of around 2.4% per year. This is in line with the speed of convergence over the last 20 years and with the usual empirical convergence results (see Chart 2.1.1). After convergence in output per worker came to a brief halt in 2022 in response to the aforementioned negative supply shock (see the small “dent” in Chart 2.1.1 at the grey line for 2022), it resumed in 2023–2024. The growth rate of labour productivity in the Czech Republic is also affected by the 2024 revision of the national accounts (see Box 2.1 for details), according to which historical data on national labour productivity have been revised towards the Austrian level.[22] The narrower initial productivity gap will mean that, at the current rate of convergence, GDP growth per worker will be slightly lower than it would have been before the revision.

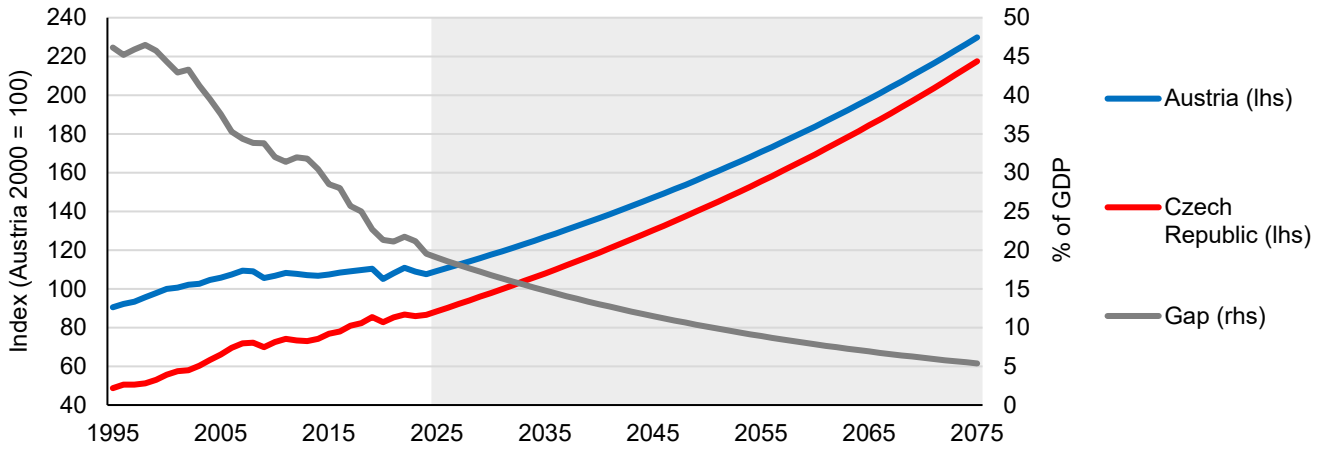
In addition to the convergence component of labour productivity growth, we also assume continuous autonomous technology growth (the growth rate of total factor productivity) of 1.5% per year. This is in line with the long-term average for developed countries if we exclude the effect of the financial crisis in 2008 and 2009, the COVID-19 pandemic crisis in 2020 and 2021, and the stagflation crisis related to the invasion of Ukraine by the Russian Federation (2022 and 2023). This technology growth is symmetrically reflected in the growth of the Austrian and the Czech economies. When estimating the long-term growth of the Czech economy, it is therefore necessary to add it to the convergence component of growth. It should be noted that over the last 17 years, the assumption of 1.5% growth in Austrian GDP per worker has not been fully realised (between 2007 and 2024, GDP per worker fell by 1.7%, corresponding to an annual decline of 0.1%), so lower growth in the common component of labour productivity growth is a risk factor for the projection (see also the alternative scenario in subchapter 5.1).

In our simulation, the growth rate of GDP per worker thus falls from 2.1% in 2025 to 1.7% at the end of the projection as a result of the convergence component of growth gradually being exhausted (see also Table

[20] A more detailed explanation of the methodology and the parameters used for the long-term macroeconomic projection is given in the Office of the CFC (2019): Dlouhodobá makroekonomická projekce ČR [Long-Term Macroeconomic Projection of the Czech Republic, available in Czech only].
[21] Thus, the initial labour productivity in the Czech Republic was 80.5% of the Austrian level (adjusted for the output gap). In 2024, GDP per worker fell in Austria (−1.8%), while it grew by 0.8% in the Czech Republic.
[22] While before the revision, the baseline labour productivity in the Czech Republic in 2023 was 75.2% of the Austrian level, after the revision in the same year it was 78.9%.

2.3.1). With the given parameter settings, this implies that whole-economy labour productivity could be at 94.6% of the future Austrian level in 2075. We then use the convergence of labour productivity and the projected evolution of the number of workers, which depends primarily on demographic change and the projected number of pensioners, to generate the overall GDP projection.

Chart 2.1.1 Convergence of output per worker to the Austrian level



Source: CZSO (2025), OECD (2025); CFC calculations.

Box 2.1 Impact of the revision of national accounts on convergence assumptions

At the end of June 2024, the CZSO published a revision of the national accounts, which significantly changed GDP, labour productivity and the share of compensation of workers in gross value added (GVA).[23] Given that the revision covered a relatively long period in history, it affects our considerations on economic convergence. However, the revision did not only concern Czech data but was carried out to varying degrees across EU countries, so it could have affected not only the starting point for the Czech Republic, but also the convergence target. In this box, we summarise the essence of the revision in the Czech Republic and in foreign economies and attempt to show how this revision has affected our assumptions about productivity growth and other economic parameters.

As part of the occasional revision, the CZSO and other statistical offices in the EU incorporated various methodological recommendations from Eurostat. The revision also reflected the findings of the 2021 Population and Housing Census. The change that had the greatest impact on the data in Czechia was a modification of provided lifetime period of individual fixed assets, which was reflected primarily in the estimate of housing services. There were two fundamental changes here. Firstly, the number and structure of dwellings was updated based on the results of the 2021 Census. Above all, however, the lifetime period of houses and flats were updated from the original 80 years for flats and 90 years for family houses to 70 years for both types of dwellings. This change had a direct impact on the increase in the use of the fixed capital (depreciation) and on the increase in the value of housing services. At the same time, a model was developed to estimate the share of self-builders in the construction of new family houses and in their renovation.

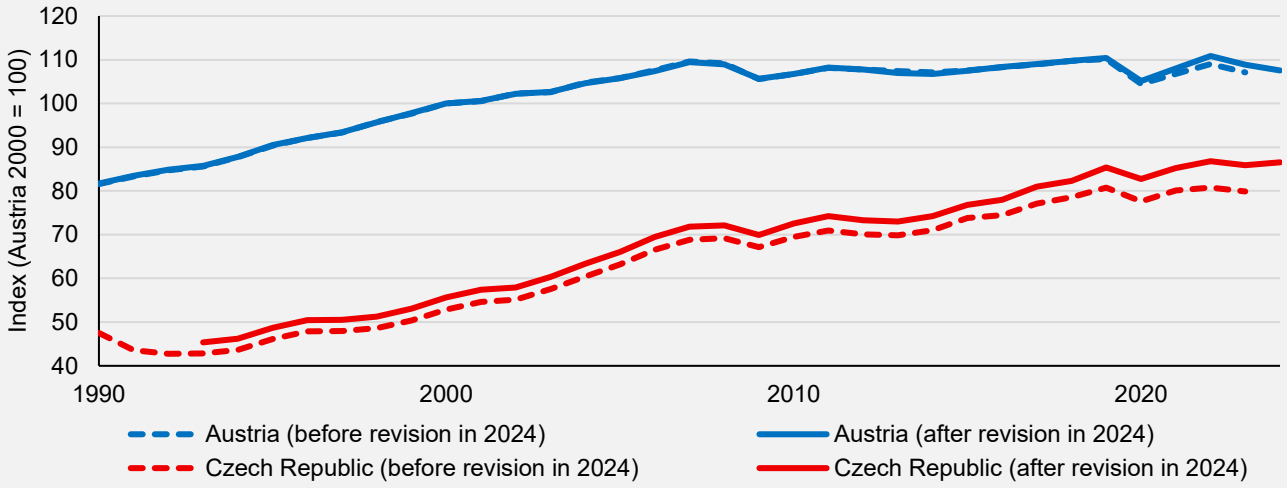
The revision also took into account other Eurostat recommendations, such as partial procedures for compiling the labour balance, incorporating new data into the estimate of subthreshold software, and estimates of the capitalisation of in-house software. Estimates of tips were also updated and the recording of payments for nuclear waste storage was changed. However, the quantitative impact of these changes was low compared to the change in the expected lifetime period of dwellings.

The above changes resulted in a relatively significant revision of historical GDP data. Czech nominal GDP was revised upwards by up to 3.9% (2022), which was reflected, among other things, in the interpretation of ratio indicators such as the ratio of public debt to GDP or deficits to GDP. There has also been a change in historical data on labour productivity compared with Austria according to OECD data.[24] As can be seen from Chart B2.1.1,

[23] For the sake of better international comparability, we work with the share of compensation of workers, which we define analogously to compensation of employees, except that we include an estimate of compensation of entrepreneurs (self-employed persons), at the same amount per self-employed person as the average per employee.
[24] Labour productivity is measured as GDP per person employed, calculated in real terms according to purchasing power parity (PPP). A certain complication in interpreting the new OECD data is that, in addition to the above-mentioned revision of GDP data, there has also been a change in the base year to which they are calculated. While older data calculated labour productivity according to constant prices from 2015, it is now calculated according to constant prices from 2020.

historical data on labour productivity for Austria are essentially similar to those before the revision. Labour productivity in the Czech Republic is, according to the new data, relatively closer to that of Austria. At the current rate of convergence, the narrower initial productivity gap will lead to slower productivity growth than before the revision.

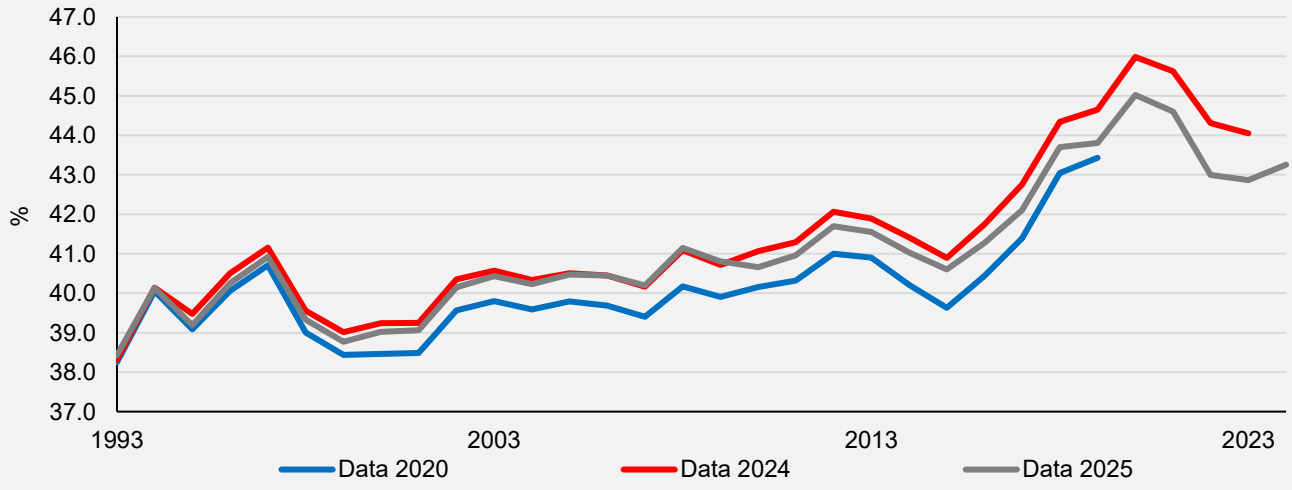
Chart B2.1.1 GDP per person employed (index, Austria 2000 = 100)



Source: CZSO (2025), OECD (2025); CFC calculations.
Note: Index based on GDP per person employed in USD according to purchasing power parity (PPP), in constant prices (for old data according to 2015, for new data according to 2020).

The revision of the national accounts also affected the second component of convergence, namely the convergence of the share of compensation of employees in GVA to the average for selected European countries. As can be seen from Chart B2.1.2 below, the initial indicator of the share of compensation of employees in GDP for the Czech Republic was revised downwards by up to 1.2 pp in 2023. Within the income approach to GDP calculation, the higher GDP driven by higher housing services is reflected in a higher operating surplus (of the household sector). The share of employee compensation in GDP thus logically declined as the operating surplus increased. It is worth noting that the share of employee compensation in the national accounts was already revised in 2021, when this share of GDP was revised upwards quite significantly. While in 2021 the change in the share was almost exclusively due to a reassessment of employee compensation, in 2024 employee compensation did not change much and the decline in the share can be attributed primarily to the aforementioned reassessment of GDP. Given that the convergence target for the share of compensation of employees in GVA in selected advanced economies has not changed significantly, the revision led to an increase in the convergence gap for this indicator. Again, given the constant rate of convergence, the initial increase in the gap will lead to slightly faster wage growth than before the revision. The two convergence effects (i.e. a lower initial gap in labour productivity and, conversely, a higher initial gap in the share of compensation of employees in GDP) will thus counteract each other and partially cancel each other out in terms of wage developments.

Chart B2.1.2 Compensation of employees as a share of GDP



Source: CZSO (2025); CFC calculations.

2.2 Demographic projection

The demographic projection is a key parameter for the long-term sustainability of public finances. It significantly affects both the expenditure side of public budgets, such as pensions, health care, education and social benefits, and the revenue side. Demographic projections are also one of the basic inputs for macroeconomic projections and intergenerational accounts. It is used as the basis for simulating the number of workers, which is affected by both the projected population count and the age structure of the population.

The long-term demographic projection is based on the demographic projection published by the CZSO in November 2023, which is drawn up in three variants: medium, high and low.[25]

For the baseline scenario of our projections, we have chosen the medium, i.e. most likely, variant of the demographic projection as the starting point.

As in previous years, we have updated the official demographic projection of the CZSO with new data. First, we replaced the age structure of the population as of 1 January 2025 with the observed reality. Subsequently, using the projected fertility, mortality and migration rates for 2024–2100 taken from the CZSO projection of 2023[26], we generated new projected population development including its age structure for each variant of the demographic projection.

The original demographic projection of the CZSO was based on the reality for the Czech Republic at the beginning of 2023. However, the actual development during the years 2023 to 2024 differed from this projection, which is discussed in more detail in Table 2.2.1. In recent years, population growth has been hampered mainly by a lower than projected birth rate, especially in 2024, when the number of births and, consequently, the birth rate was the lowest in the entire history of the survey for the Czech lands (i.e. since 1785). The reasons for the low birth rate are discussed in more detail in Box 2.2. In subchapter 5.2, we compile alternative scenarios that illustrate a sensitivity analysis with regard to the fertility rate. Contrary to the assumptions of the demographic projection, the higher mortality rate, which was still affected by the COVID-19 pandemic of 2020 and 2021, also contributed to the lower population count. Compared to 2020–2022, when higher mortality dominated the negative natural population growth, its relative impact is significantly reduced compared to low fertility.

Table 2.2.1 Materialisation of the CZSO's demographic projection in 2023–2024 (in ‰)

	2023			2024		
	projection	reality	difference	projection	reality	difference
Net migration	9,072	8,703	-0.369	2,240	3,384	1,145
Natural growth	-1.507	-1,990	-0.482	-1.741	-2.563	-0.822
gross mortality rate	*10.190*	*10.369*	*0.179*	*10.237*	*10,307*	*0.070*
gross birth rate	*8.682*	*8.379*	*-0.303*	*8.496*	*7.745*	*-0.752*
GROSS OVERALL GROWTH RATE	7.565	6,713	-0.852	0.499	0.822	0.323
Gross fertility rate	1.500	1.453	-0.047	1.500	1.368	-0.132

Source: CZSO (2024); CFC calculations.
Note: Values in the table may be subject to inaccuracies due to rounding.

However, the change in population count in recent years has been dominated by net migration, which is significantly related to the armed conflict in Ukraine and the granting of temporary protection to refugees. In 2022, net migration was significantly positive (an increase in the total population of approximately 300,000 people). The demographic projection of the CZSO assumed a continued influx of refugees in 2023 (total net migration of approximately 98,000 persons, of which 63,000 were refugees), and from 2024 onwards, it anticipates a partial outflow of these refugees over a period of four years (a total of 209,000 refugees in 2024–2027; however, "standard" net migration of 140,000 persons is anticipated for the same period). In 2023, net migration was lower than projected, while in 2024 the assumption of an incipient outflow of refugees was not met to any significant extent and the positive net

[25] CZSO (2023): Population projections of the Czech Republic 2023–2100.
[26] In our projections, we have slightly adjusted our fertility rate projection for the coming years due to the decline in the fertility rates in 2023 and 2024, which is significantly below the level of the demographic projection of the CZSO. In the medium variant of the demographic projection, we assume a gradual return of the fertility rate from the current 1.37 children per woman to the 1.5 children projected by the CZSO over the next five years. In the low variant, where the CZSO projects a gradual decline in the fertility rate to 1.25 children per woman, we assume a constant fertility rate of 1.37 until this downward trajectory reaches that value. This should occur in 2035.

migration outweighed the negative natural population growth. The fulfilment of assumptions regarding the outflow of refugees in the next years will probably be the most significant risk to the demographic projection.

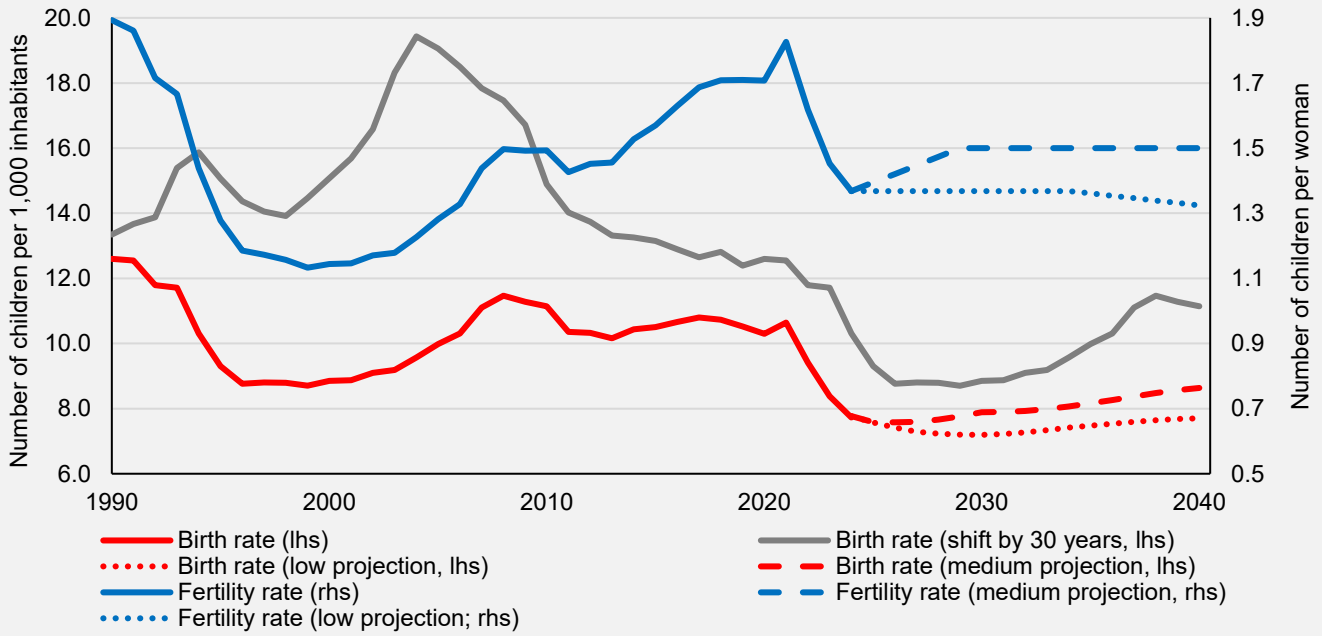
Overall, between 2022 and 2024, the population of the Czech Republic grew by 0.76%, which is 0.05 pp less than the original demographic projection from 2023. Even so, the population is at its highest since the end of World War II.

Using demographic projections, we estimated workforce growth as the population aged 21 and older minus the projected number of old-age pensioners and level 3 disability pensioners. We estimate the number of recipients of these pensions primarily based on the statutory retirement age.[27] In projecting the number of workers, we assume a stable labour force participation rate for each age group and a constant natural rate of unemployment. By linking the growth (or decline) rate of the labour force to the projection of GDP per worker, we obtain the growth trajectory of total GDP, from which we derive the growth rate of GDP per capita (see Table 2.3.1 in subchapter 2.3).

Box 2.2 Decline in fertility and birth rates in the Czech Republic

As already mentioned, the number of births and, consequently, the birth rate in the Czech Republic in 2024 were the lowest in recorded history (i.e. since 1785). As can be seen from Chart B2.2.1, the decline in the number of births was the result of two factors. Firstly, from its local maximum of 1.82 children per woman in 2021, the fertility rate fell to 1.37 in 2024.[28] The fertility rate is still above its historical minimum from 1999 (1.13 children per woman). The second significant factor is the decline in the number of women of reproductive age, which is related to the delayed effects of the record decline in fertility and birth rates in the 1990s. With a 30-year delay, which is the average age of mothers, the resemblance of the current decline in birth rates with the decline in birth rates in the second half of the 1990s (grey line in Chart B2.2.1) is evident. It is apparent that this effect will continue over the next five years.

Chart B2.2.1 Birth and fertility rates in 1990–2040



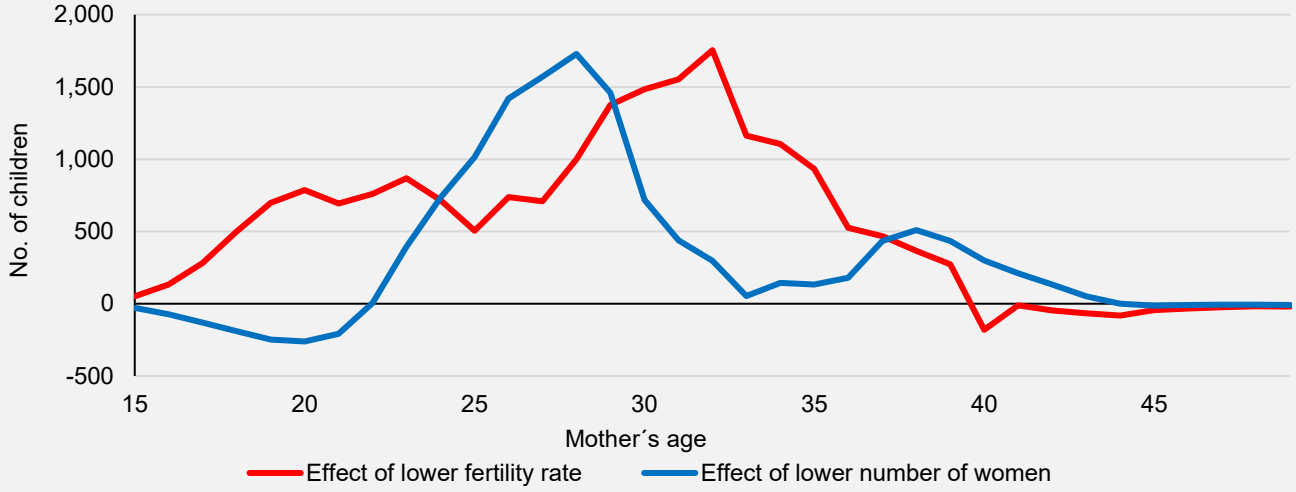
Source: CZSO (2024); CFC calculations.

The distribution of the decline in the number of births between declines in age-specific fertility rates and the decline in the number of women of various ages is shown in Chart B2.2.2. It shows the difference between 2017, when the number of live births reached its last local maximum (114.4 thousand children), and 2024, when the number of children was historically the lowest (84.3 thousand children, i.e. 26.3% less).[29] Of the approximately

[27] The methodology and projections for the number of pension beneficiaries are described in more detail in subchapter 3.1.
[28] The total fertility rate determines the number of children that would be born to each woman during her entire reproductive age (15–49 years) if the age-specific fertility rates of women did not change during this reproductive period. It is therefore the sum of age-specific fertility rates by age in a given year.
[29] In the calculation, we use the following breakdown according to age-specific fertility rates f_i:

30 thousand “missing” children, 18.9 thousand (62.8% of the decline) can be attributed to a decline in fertility across virtually all age categories of mothers, with the exception of mothers over 40, for whom fertility rates are rising slightly. The most significant decline in fertility is among mothers in the key age category of 28–33 years. A total of 11.2 thousand children (37.2% of the decline in the number of live births between 2017 and 2024) can be attributed to the lower number of potential mothers and thus to the aforementioned delayed effect of the low fertility rate of the second half of the 1990s. This effect mainly concerns women aged 25–30 but applies across all age categories between 21 and 44 years.

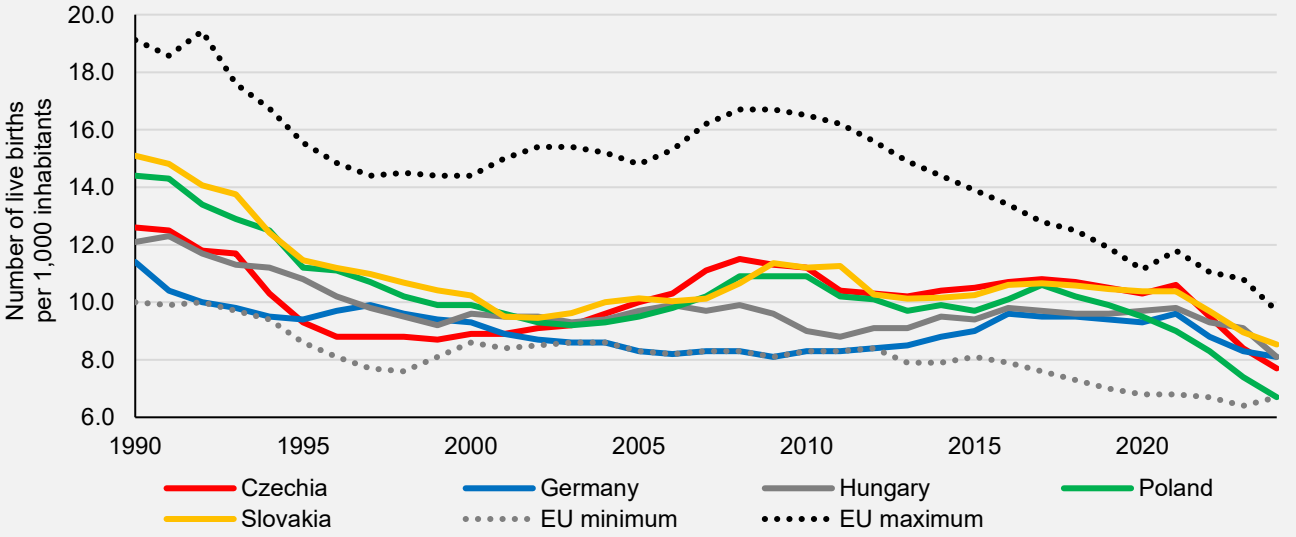
Chart B2.2.2 Decrease in the number of births in 2017–2024 by mother's age



Source: CZSO (2024); CFC calculations.

The decline in fertility rate in recent years can also be compared with other EU countries (Chart B2.2.3). This comparison shows that the decline in fertility rate in the Czech Republic over the last three years has corresponded to a simultaneous decline in fertility rate in other neighbouring countries. For example, the decline in fertility rate in Poland was dramatic. The decline in fertility rate across the EU varies in intensity from country to country. Within the EU, the initial fertility rate in the Czech Republic in 2021 was relatively high, with the Czech Republic having the second highest fertility rate in the EU that year. The decline in fertility rate in the Czech Republic is thus more pronounced because of the relatively high initial point.

Chart B2.2.3 Comparison of the decline in fertility rate across EU countries



Source: Eurostat (2024); CFC calculations.

$D_{2017} - D_{2024} = \sum_{i=15}^{49} Z_{i;2017} \cdot f_{i;2017} - \sum_{i=15}^{49} Z_{i;2024} \cdot f_{i;2024} = \sum_{i=15}^{49} \left[(Z_{i;2017} - Z_{i;2024}) \cdot f_{i;2017} + \left(f_{i;2017} - f_{i;2024}\right) \cdot Z_{i;2024} \right]$.
Thus, the decline in the number of children born between 2017 and 2024 (***D***) is due both to the contribution of a lower number of women aged 15 to 49 (***Z***$_i$) and to a decline in age-specific fertility rates (***f***$_i$). The lower index *i* indicates the age of the mother.

In addition to the aforementioned delayed effect of low fertility rate in the second half of the 1990s, several factors contributed to the decline in fertility rate. The first may be related to the relatively high international fertility rate during the COVID-19 pandemic. This higher fertility can be interpreted as some mothers bringing forward the timing of having a child. The current decline in fertility rate may thus be related to this "pre-stocking effect". Fertility rates increased most for the 25–30 age group between 2017 and 2021, while the subsequent decline in fertility between 2024 and 2021 was most pronounced for the 28–32 age group, which supports this hypothesis. The second reason may be the postponement of having children to a later age, as was the case in the 1990s. This would be suggested by the increasing age of mothers at the time of childbirth. The third explanation for the decline in fertility may be the impact of Ukrainian refugee migration. In addition to children, this wave saw a significant influx of women aged 15–49, which should lead to an increase in the number of children of Ukrainian nationality being born. This did indeed happen, and in 2024, approximately 4.5 thousand Ukrainian children were born in the Czech Republic, representing 5.4% of all births. The proportion of Ukrainian children born increased from 1.2% in 2021. However, as the number of Ukrainian women aged 15–49 increased much more significantly (approximately 3.5 times more) during the same period, the fertility rates of this group of women are significantly lower than those of the rest of the population. If Ukrainian women were to replicate the age-specific fertility rates of the total population, an estimated 3.5 thousand more children would have to be born in 2024. Another factor that may be contributing to lower fertility rate in the Czech Republic is the unfavourable socio-economic conditions for having children, e.g. with regard to the declining housing availability.

2.3 Real wages and the primary income distribution

Wage developments play a major role in projections for the pension system, education, health care and other areas. In our projection, we derive the evolution of real wages primarily from the long-term labour productivity projection, where real wages grow in the projection at least at the rate of GDP per worker (see subchapter 2.1). We nonetheless complement this convergence effect of real wage growth with the effect of the growth in the ratio of compensation of employees to gross value added (GVA).[30] This ratio was and to a large extent still is relatively low in the Czech economy compared to other countries. Thus, in our projection we assume that the convergence of the share of employees' compensation in GVA will continue at the same rate as for GDP per worker. This means that the difference between the share of workers' compensation in GVA in selected developed economies and the corresponding share in the Czech Republic narrows by 2.4% per year in our projection.[31]

The increasing ratio of compensation of workers to GVA in our projection means that real wages are growing faster than labour productivity. The volume of wages and salaries is likewise growing faster than GDP in the long term, at the expense of the gross operating surplus (profitability) of firms. The change in the distribution of GVA is meanwhile important for, among other things, the level and structure of future general government tax and insurance premium revenues.

The dynamics of real wages are also influenced by the assumption about the initial share of compensation to employees in GVA. In 2015–2019, there was a gradual increase (approximately 3.2 pp over four years), and in 2020 this share jumped by a significant 1.2 pp as a result of the slow response of wages to the sharp economic downturn. In the period of high inflation and falling real wages in 2021 and 2022, the share of compensation to workers on GVA declined (by 2.0 pp over two years), and the share also declined in 2023 (by approximately 0.1 pp), before rising by 0.4 pp in 2024. In addition to this relatively significant development, the initial share of compensation of employees in GDP was also affected by a revision of the national accounts, which led to a downward reassessment (see Box 2.1). In our projection, we consider the initial share of compensation of employees in GVA in 2024 to be an equilibrium. Overall, we expect real wages to grow by an average of 2.0% per annum (see Table 2.3.1), which is about 0.2 pp higher than the growth rate of GDP per worker. However, the difference between the two rates will narrow over time.

[30] It should be noted that, for reasons of better international comparability, we work with the share of compensation to workers, which we define analogously to compensation to employees, but with the difference that we also include an estimate of compensation to entrepreneurs (self-employed persons), at the same amount per self-employed person as the average per employee.
[31] The selected developed countries here are Austria, Germany, Sweden, Denmark, Belgium, the Netherlands and Finland. For details, see the Office of the CFC (2019): Dlouhodobá makroekonomická projekce ČR [Long-Term Macroeconomic Projection of the Czech Republic, available in Czech only].

Table 2.3.1 Average annual growth rates based on the long-term projection (%)

	2025–2035	2036–2045	2046–2055	2056–2065	2066–2075	Entire period
GDP per capita	2.4	1.6	1.4	1.7	1.8	1.8
GDP per worker	2.0	1.9	1.8	1.7	1.7	1.8
GDP total	2.2	1.6	1.3	1.5	1.6	1.6
Average real wage	2.5	2.1	1.9	1.8	1.8	2.0

Source: CZSO (2025), OECD (2025); CFC calculations.

Our projection of GDP growth, or GDP per capita, is influenced not only by assumptions about macroeconomic convergence, but also by demographic developments and changes in the retirement age. For a given population, a higher number of pensioners leads to a lower working-age population. This then means lower GDP for a given level of productivity. The projected number of pensioners is roughly stable or even declining slightly for the next five years. However, it will grow rapidly from 2030 onwards (see also subchapter 3.1). GDP dynamics are also influenced by changes in demographic projections, where higher migration in particular leads to a larger working population and higher GDP. Conversely, low fertility rates reduce the working population, but compared to migration, this effect occurs with a delay of about 20 years. Compared with last year's projections, total GDP around 2045 will be approximately 5.5% higher, and at the end of this year's projection horizon (2075), the total level of GDP will be 5.1% higher than last year. The higher GDP mainly reflects the higher initial GDP due to the latest historical revision of the national accounts, but also the lower projected number of pensioners (and thus higher number of workers) due to the expected extension of the retirement age.

The projection also includes an assumption about the rate of inflation. We assume that the rate of consumer price inflation is equal to the rate of growth of the GDP deflator, namely 2% a year. This rate of price level growth is in line with the CNB's current inflation target.

3 Expenditure and revenue in the long-term projection

This chapter presents a projection of general government expenditure and revenue based on the macroeconomic and demographic projections in the previous chapter. The projection of general government expenditure and revenue is calculated assuming un-changed revenue and expenditure policies. The projections are therefore not a forecast of what we would consider to be the most likely future outcomes. The results of these projections should be interpreted accordingly – they are all conditional on the existing policy settings and are designed to answer the question of what would happen if the current revenue and expenditure policies were left unchanged.

The baseline projection scenario reflects the government's austerity measures from previous years (the "consolidation package"), which affected both the revenue and expenditure sides of the public budget, as well as the approved changes to the pension system ("pension reform"). The pension system projection includes both those parts of the pension reform that were already incorporated into the baseline scenario last year (i.e. adjustments to early retirement pensions and changes to the indexation mechanism) and those parts that were not approved until the end of 2024 (in particular changes to the retirement age), which were included in the alternative scenarios in last year's Long-Term Sustainability Report.

Some revenues and expenditures are directly affected by demographic developments, while others are influenced by the long-term growth of the Czech economy and its convergence towards the level of developed countries, both in terms of GDP per capita and labour productivity and real wages. Demographic and convergence influences are intertwined. However, it can be said that demographic influences prevail in the pension system, education, health care, social benefits and long-term care, while convergence effects are more pronounced in the case of public investment spending, public employees' salaries and tax and insurance premium revenues.

3.1 Pension system

The pension system consists of old-age pensions, disability pensions and survivor (widows', widowers' and orphans') pensions. The system is managed and administered by the Czech Social Security Administration (CSSA), with the exception of pensions for the armed forces, for which the system is administered by the relevant ministries (the Ministry of the Interior, the Ministry of Defence and the Ministry of Justice). However, the conditions for the payment of pensions for the armed forces are essentially the same as those for insured persons under the CSSA, so we treat the entire pension system as a single entity in our projections.[32]

In previous years, the pension system as a whole has been significantly affected by price increases and several waves of regular and extraordinary pension indexation, as well as changes in legislation (in particular Act No. 155/1995 Coll., on Pension Insurance, as amended, the "Pension Insurance Act"[33]), most of which have recently been aimed at improving the sustainability of the pension system. Some of these legislative changes were already approved in 2023,[34] while others were approved in 2024.[35] The main component of the "great pension reform" is primarily an adjustment to the retirement age after 2030 above the current maximum level of 65 years, followed by measures aimed at slowing down the growth of newly granted pensions (reducing the level of earnings taken into account under the first reduction threshold from the current 100% to 90% and reducing the percentage per year of insurance from the current 1.5% to 1.45%).

On the expenditure side of the pension system, we first model the number of recipients of each type of pension and then the levels of these pensions. The revenue side of the system is modelled directly on the basis of our macroeconomic projection. Pension insurance contributions are, by their nature, a tax on labour income.

[32] There are some differences in the calculation of the pensions of the armed forces, for example in the amount of the pension granted in the event that the new pensioner has received a service allowance higher than the amount of the newly granted pension (the pension is then set at the amount of this service allowance). There also appears to be a higher proportion of men among military pensioners. In this Long-Term Sustainability Report we do not take these differences into account and assume that expenditure on armed forces' pensions will account for an average of 2.42% of pension expenditure paid by the CSSA, which is in line with the average over the last fifteen years.
[33] This Act mainly affects the so-called first pillar of the pension system. In addition, Act No. 462/2023 Coll. also amended the third pillar (amending Act No. 427/2011 Coll. on Supplementary Pension Savings, as amended).
[34] The so-called "small pension reform" is Act No. 270/2023 Coll., amending Act No. 155/1995 Coll., on Pension Insurance, effective from 1 October 2023. This amendment mainly included changes to the pension indexation mechanism (in particular, indexation by one third of real wage growth instead of the current half) and restrictions on early retirement.
[35] The so-called "great pension reform " is Act No. 417/2024 Coll., amending Act No. 155/1995 Coll., on Pension Insurance, and other related acts, with most of the amendments proposed to take effect on 1 January 2025. For more details, see Box 3.1 in this chapter and the Office of the CFC (2025): Dopady důchodové reformy na stabilitu a udržitelnost veřejných financí v dlouhém horizontu [Impacts of pension reform on the long-term stability and sustainability of public finances, available in Czech only].

3.1.1 Old-age pensions

Old-age pensions are quantitatively the most important component of the pension system. Around 2.35 million people are currently receiving them.[36] The number of old-age pensioners has been declining over the last five years (from the end of 2019 to the end of the first quarter of 2025 by 63.1 thousand people, thus approximately by 2.6 %). In 2020 and 2021, this was mainly due to the increased mortality among the elderly due to the COVID-19 pandemic. In 2023 and 2024, the inflow of newly granted pensions fell to approximately 40% of the long-term average, partly due to the continuing extension of the statutory retirement age and demographic influences (the generations born between 1960 and 1965 are relatively less numerous than the immediately older and younger generations), and partly due to the exhaustion of the effect of increased early retirement in response to the extraordinary pension indexation of 2022.[37]

The number of old-age pensioners will continue to be affected predominantly by demographic developments and changes in the statutory retirement age. The extension of the retirement age under current legislation (the Pension Insurance Act) will continue until 2030, when the retirement age for both men and most women should be 65 (for those born in 1965). Subsequently, the retirement age will increase by one month each year in accordance with the pension reform, starting with those born in 1966.[38] The retirement age will continue to increase in this way until those born in 1989, for whom the retirement age will be 67. For younger generations the retirement age should then be capped at 67. This statutory age is also included in the baseline scenario of our projection.

In estimating pension expenditure, we start by estimating the future number of old-age pension beneficiaries. We base this estimate on demographic projection and the statutory retirement age, but we also take into account the option of early retirement or, conversely, the option of working beyond retirement age and thus supplementing one's old-age pension.

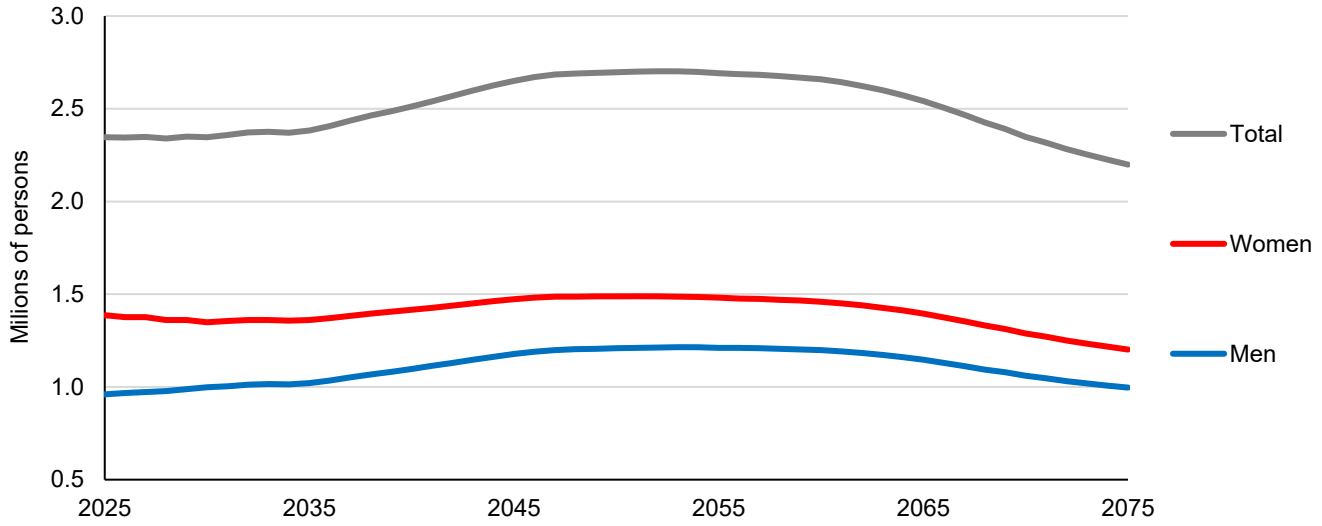
For these reasons, we use the so-called "rates of retirement", i.e. the proportions of the number of pensioners in the total number of people of a certain age cohort, to project the number of old-age pensioners. In projecting them, we also take into account that the number of old-age pension beneficiaries interacts with disability pensions, as the payment of both types of pensions is mutually exclusive. For these reasons, we work with rates of retirement that do not refer to the whole population of a given age, but only to that part of the population that does not receive a disability pension (see subchapter 3.1.2 for the projection of the number of disability pensioners). We construct rates of retirement on the basis of time to the statutory retirement age This is the main determinant of the decision of the elderly in the Czech Republic about when to retire. The rates of retirement used in the projection of the number of old-age pensioners were derived separately for men and women as the average of the empirical retirement rates recorded in reality.[39]

In the baseline scenario of the projection, the number of old-age pensioners will remain stable at roughly the current level for the next five years (see Chart 3.1.1). While the number of female old-age pensioners will decline slightly (by 2.7% between 2025 and 2030), mainly due to the extension of their retirement age, the number of male pensioners will increase (by 4% over the same period). After 2030, the large cohorts born in the 1970s will gradually retire. Despite the extension of the retirement age above 65 as part of the pension reform, which will significantly dampen the growth in the number of old-age pensioners, this demographic development will result in a steady increase in the number of old-age pensioners. This will peak around 2053, when there should be approximately 2.7 million old-age pensioners, i.e. roughly 15.2% more than today.

[36] Data according to the Czech Social Security Administration, i.e. excluding pensioners from the armed forces.
[37] By the end of 2022, the incentive to apply for an early pension has increased, as all pensions awarded in 2022 would automatically be indexed by all extraordinary indexations made in 2022. Due to the sharp increase in early retirement applications, the total number of applications for pension assessment rose from the usual annual figure of around 100,000 to 180,000. However, a significant proportion of these pensions were only assessed, with the individuals concerned continuing to work and just "freezing" their future pensions at a higher level. The wave of early pension applications at the end of 2022 thus complicates estimates of the number and size of pensions to be paid in the coming years.
[38] For a description of the reforms and their impacts, see Box 3.1 in this Long-Term Sustainability Report and also the Office of the CFC (2025): Dopady důchodové reformy na stabilitu a udržitelnost veřejných financí v dlouhém horizontu [Impacts of pension reform on the long-term stability and sustainability of public finances, available in Czech only].
[39] For women, only a single retirement rate was considered. The model scenario involved a woman with two children as the model situation. We set the projected retirement rates according to their average for the years 2013–2023. For a more detailed description and discussion of the rates of retirement and modifications thereof as a result of different rates of increase in the retirement age, see the Office of the CFC (2019): Projekce důchodového systému [Projection of the Pension System, available in Czech only].

In addition to the change in the number of pensioners, there will also be a change in the gender structure, as the equalisation of the statutory retirement ages for men and women will lead to an increase in the proportion of men in the total number of old-age pensioners from the present level of 40.9% to 45.4% in 2075. The increase in the male share of total pensioners will also reflect the convergence of life expectancy of men and women.

Chart 3.1.1 Projection of the number of old-age pensioners (medium variant of the demographic projection)



Source: CZSO (2025), CSSA (2025); CFC calculations.

The projection of expenditure on old-age pensions also includes an estimate of the average old-age pension. This is affected, on the one hand, by the starting level of existing pensions granted in the various times in the past. The level of these pensions is then also conditional on their history of indexation (statutory and extraordinary). The second component of the average old-age pension is the amount and number of newly granted pensions. The average pension is then a weighted average of these two types of pensions. Usually, newly granted pensions are higher than those granted in the past, as they are linked to nominal wages in the year when the pension is granted. Older pensions are indexed fully to inflation and only partly to real wage growth. It is this therefore the case that the value of older pensions relative to the average wage gradually decreases with increasing distance from the time of pension granted.[40] The change in the average pension then reflects the evolution of existing pensions, the number and amount of newly granted pensions and, finally, the number and amount of pensions that have been terminated (pensions that have terminated are usually lower than the average pension). If the proportion of newly granted pensions increases, the overall replacement rate tends to increase.

The level of newly granted pensions consists first of a basic flat-rate part, which we assume will stay at 10% of the average wage. This flat rate is the same for all pensioners. The second component of the pension is the so-called earnings-related part, which is derived from the insured person's past earnings indexed to the past trend in average wages and the number of years of contributions (including non-work validated periods).[41] The calculation also includes two reduction thresholds, which represent an element of redistribution and dampen differences in newly assessed pensions.[42]

We simulate the amount of newly granted pensions in relation to the average wage. As the starting point for our projection of the level of newly granted pensions we used the latest known figures, according to which the level of new pensions was 45.5% of the average gross wage for men and 40.6% for

[40] When real wages rise, old-age pensions rise more slowly than nominal wages. Thus, the pension-wage ratio decreases with increasing age (or the time since the old-age pension was granted). An exception is the one-off increase in pensions on reaching a certain age (according to the provisions of Section 67a(1) of the Pension Insurance Act, the pension increases by CZK 1,000 on reaching the age of 85 and by CZK 2,000 on reaching the age of 100).

[41] The minimum earnings-related part of the pension pursuant to Section 33(2) of Act No. 155/1995 Coll. will also be at least 10% of the average nominal wage from 2026. The current minimum earnings-related part is CZK 770 per month. The minimum pension will thus amount to 20% of the wage, an increase of approximately CZK 3,890 (i.e. 71.6% when using the flat rate part for 2025).

[42] For a more detailed description, see the study of the Office of the CFC (2019): Projekce důchodového systému [Pension System Projection, available in Czech only].

women.[43] The lower newly assessed pensions for women are due to their lower average wages and their lower statutory retirement age, and thus shorter coverage period. Following the equalisation of the statutory retirement ages for men and women (i.e. after 2030), the coverage period for women will increase and the difference between men's and women's newly granted pensions will therefore decrease.

After 2025, we will link the replacement rate of new pensions to the estimated coverage period.[44] Until 2030, the coverage period will grow faster for women than for men in connection with the extension of the retirement age for women. After 2030 and after the equalisation of the retirement ages for men and women, the coverage period will grow at the same rate for both and more slowly. The impact of the extension of the retirement age on the coverage period will cease in 2056 due to its cap at 67 years. However, the coverage period will be reduced even earlier due to the gradual restriction on counting studies as a non-work validated period between 2045 and 2055.

In addition to the projected coverage period, the replacement rate of newly granted pensions will also be affected by another pension reform measure, namely a change in the parameters for calculating newly granted pensions. From 2026, there will be a gradual reduction in accounting for income below the first reduction threshold from the current 100% to 90% and a reduction in the crediting of pensions for each year of insurance from the current 1.5% to 1.45%. Both changes should take place gradually between 2026 and 2035. This adjustment significantly reduces the estimated replacement rates of newly granted pensions during this period.

For both men and women, we project a decline in the ratio of newly granted pensions to average wages more or less throughout the entire projection horizon. For men, this ratio will fall to 41% and for women to 38.5% of the average wage at the end of the projection horizon (i.e. in 2075). The difference between the amount of newly granted pensions for men and women will thus persist even after 2030 and after the retirement ages are equalised due to their different wage levels.

In order to calculate the total average pension, it is also necessary to model the evolution of pensions granted in the past. In 2022 and 2023, the ratio of these pensions to wages increased quite significantly due to waves of regular and extraordinary indexations during this period (in June 2022, September 2022 and June 2023) and a simultaneous significant decline in real wages. Overall, the average pension increased by CZK 5,208 between December 2021 and January 2024, i.e. by about one third, because of indexation. The total replacement rate rose from 40.2% at the end of 2021 to 46.9% in 2023. In 2024, real wages resumed growth and the total replacement rate fell to 45%, with this decline continuing in subsequent years (to 43% in 2025 and 41.6% in 2026).

In our projection, we assume that the indexation scheme will be followed in the future. In accordance with Section 67 of the Pension Insurance Act, we therefore assume that existing pensions will be indexed by one-third of real wage growth[45] and by the full rate of inflation. The inflation rate is considered to be the cost-of-living index for pensioner households. In our projection, we assume that the cost-of-living index for pensioners will grow by 0.3 pp more than the inflation rate according to the consumer price index.[46] In the long term, it will grow in line with the CNB's 2% inflation target.

The development of the average old-age pension will also be affected by other changes in the pension system, such as the introduction of the so-called "child-rearing bonus" (from 1 January 2023, an increase in the old-age pension for each child raised by CZK 500 per month) and its partial replacement by the so-called fictitious assessment base.[47]

[43] We use the average ratio of new pensions to the average monthly wage for the last three years, i.e. for 2022–2024. It should be noted that the wave of applications for early retirement pensions at the end of 2022 significantly disrupted the time series of replacement rates from newly granted pensions (a jump in 2022, a decline in 2023 and a correction in 2024), which makes these initial replacement rates a significant element of uncertainty.

[44] For more details, see Box 5.1 in subchapter 5.3 of last year's Long-Term Sustainability Report, as well as the study of the Office of the CFC (2022): Odhad náhradového poměru dávek důchodového pojištění [Estimation of the replacement rates of pension insurance benefits, available in Czech only].

[45] Pensions are indexed to real wage growth only in the statutory indexation period and with a delay. The last time pensions were indexed to real wages was in January 2023, based on real wage growth in 2021. As real wages fell in 2022 and 2023, pensions will only be indexed to real wage growth again when real wages exceed their 2021 level. According to estimates based on the macroeconomic forecast of the MF CR (August 2025), this should happen in 2027, so indexation to real wages will start in January 2029.

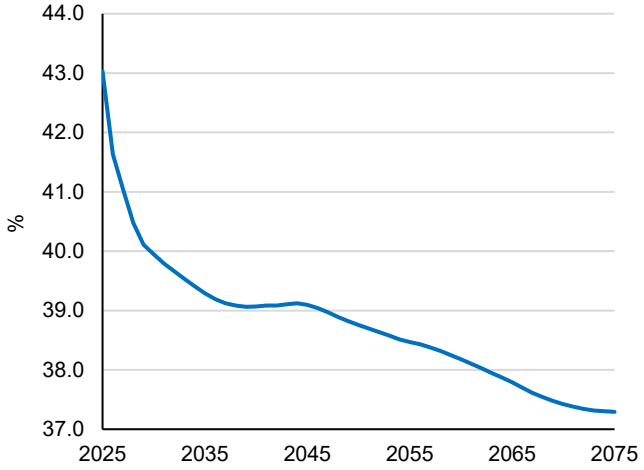
[46] Over the period 2008 to 2024, the annual growth in the pensioners' cost of living index was, on average, around 0.4 pp higher than the growth of the standard consumer price index. The difference between the annual growth of the two indices was higher in periods of relatively high price growth, when the higher weight of food, energy prices and health care prices in the pensioners' cost of living index was reflected.

[47] The change in the parameters for calculating the child-rearing bonus is another part of the pension reform. These changes do not affect the child-rearing bonus already granted in 2023 and 2024, but there will be a change in the determination of the child-rearing bonus for newly granted pensions after 2026. The calculation of the child-rearing bonus according to the current settings will remain for the third and subsequent children in the family. Care for the first and second child should now be rewarded in the form of so-called "fictitious assessment bases",

The combination of all these assumptions with the demographic projection implies the development of average old-age pension. After the strong increases in 2022 and 2023, the ratio of average old-age pension to average wage will fall quite rapidly to 39.1% around 2038 (Chart 3.1.2). This will reflect the "switch-off" of pension indexation to real wages by 2029, lower pension indexation after that date (one-third of real wage growth instead of half) and a decline in the replacement rate from newly granted pensions. The decline in the replacement rate will then stop in connection with the increase in the number of new pensioners with higher pensions and will remain roughly stable until 2045, subsequently falling below 37.3% at the end of the projection horizon.

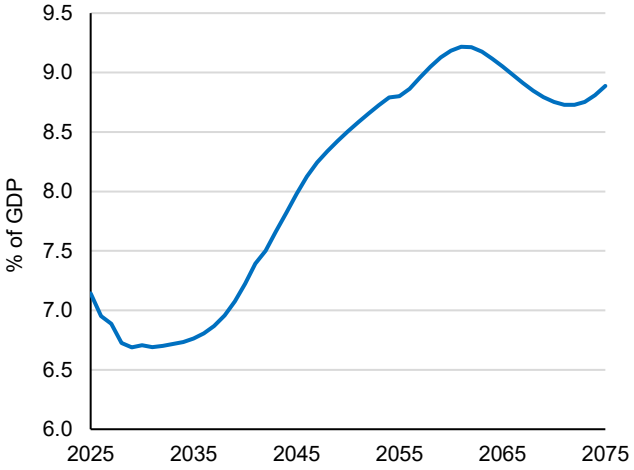
The evolution of old-age pension expenditure as a share of GDP can be derived from the number of old-age pensioners and the evolution of the ratio of pension to average wage. Expenditure peaks around 2060 at 9.0% of GDP (see Chart 3.1.3). The increase in expenditure compared to the present is mainly driven by the growth in the number of pensioners. Compared to the estimated level of old-age pension expenditure in the previous Long-Term Sustainability Report, the maximum share of expenditure in GDP is significantly lower. This is mainly due to the impact of the pension reform. The impact of the individual parts of the pension reform is described in Box 3.1 below.

Chart 3.1.2 Ratio of average old-age pension to average wage (in %)



Source: CZSO (2025), CSSA (2025); CFC calculations.

Chart 3.1.3 Ratio of old-age pension expenditure to GDP (in %)



Source: CZSO (2025), CSSA (2025); CFC calculations.

Box 3.1 Pension reform

The pension system projections in this year's Long-Term Sustainability Report were significantly influenced by the pension reforms implemented in 2023 (Act No. 270/2023 Coll.) and 2024 (Act No. 417/2024 Coll.), which amend Act No. 155/1995 Coll. on Pension Insurance. This box provides a brief overview of the main parts of the pension reform[48] and also calculates the impacts of their individual effects.

The main component of the pension reform is primarily an adjustment to the retirement age above the current maximum level of 65 years after 2030. Compared to the government's proposal and current legislation, the linking of the retirement age to life expectancy or probability of death was abolished. For generations born after 1965, the retirement age will automatically increase above 65 by one month for each subsequent year of birth. At the same time, the retirement age has been capped at 67 for all generations born after 1989. As can be seen from Chart B3.1.1, the impact of the higher retirement age will only begin to be felt from 2031, but in the longer term it will improve the balance most significantly of all factors (by around 1.4% of GDP in 2060) and by as much as 2.1% of GDP at the end of the projection horizon in 2075 (the difference between the blue and grey lines in Chart B3.1.1).

Another fundamental change in the pension reform is the reduction in the crediting of earnings in the calculation of newly granted pensions. Starting in 2026, the earnings taken into account up to the first reduction limit (i.e. 26% of wages) will be gradually reduced from 100% of the personal assessment base in 2026 to 90% from 2035. The

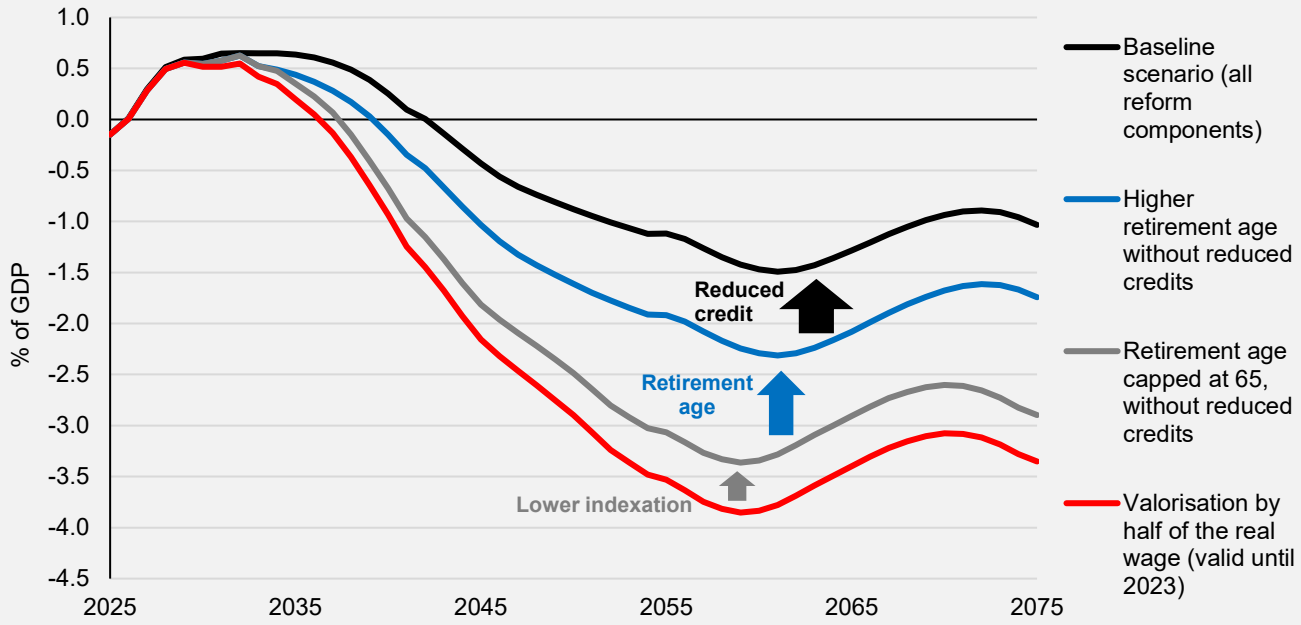
which will be derived from the general assessment base ("average wage"). For women with lower incomes in particular, the fictitious assessment base will mean a higher newly granted pension, but the increase in this pension will be lower than CZK 500 (i.e. compared to the child-rearing bonus under the current rules).

[48] For more details, see also the Office of the CFC (2025): Dopady důchodové reformy na stabilitu a udržitelnost veřejných financí v dlouhém horizontu [Impacts of pension reform on the long-term stability and sustainability of public finances, available in Czech only].

crediting rate for each year of insurance will also be reduced (from 1.5% to 1.45% of the calculation base). Both changes are effective from 2026 but will only be phased in gradually until 2035. At the same time, these changes only apply to newly granted pensions and will not affect pensions granted in the past. Given this, the impact of these changes will be relatively weak at first. The maximum impact of the reduced credits will again be felt around 2060 and will amount to approximately 0.8% of GDP (see the comparison of the blue and black lines in Chart B3.1.1).

From around 2029, the impact of the reduced indexation of existing pensions by one third instead of the current half of real wage growth will take effect. Although the change in the indexation mechanism was approved in 2023 and has been in effect since the beginning of 2024, indexation based on real wage growth will only start when real wages, which fell significantly in 2022 and 2023, exceed their 2021 level. According to estimates, this should happen in 2027, with indexation based on real wages then starting in January 2029 due to delays. From that year onwards, the impact of lower indexation will be felt relatively quickly (compare the grey and red lines in Chart B3.1.1) as it affects all pensions awarded. We project the maximum impact of lower indexation after 2060 to be approximately 0.5% of GDP.[49]

Chart B3.1.1 Pension system balances according to different parts of the pension reform



Source: CZSO (2025), CSSA (2025); CFC calculations.

The pension reform also includes other changes, some of which are aimed at increasing the stability of the pension system, while others have the opposite effect. For example, increasing the minimum earnings-related part of the old-age pension to 10% of the average wage (from the current CZK 770) will contribute to higher pension spending, with an impact on the pension system balance of approximately 0.1% of GDP. Another important change is the possibility for spouses and registered partners to voluntarily share the calculation base by mutual agreement. The impact of this change may again lead to higher pension system expenditure of around 0.2% of GDP. Higher expenditure (impact of approximately 0.1% of GDP) will also result from the extension of the pool of people in so-called demanding occupations, whereby people in these occupations could retire up to five years before their official retirement age without a reduction in pensions.[50]

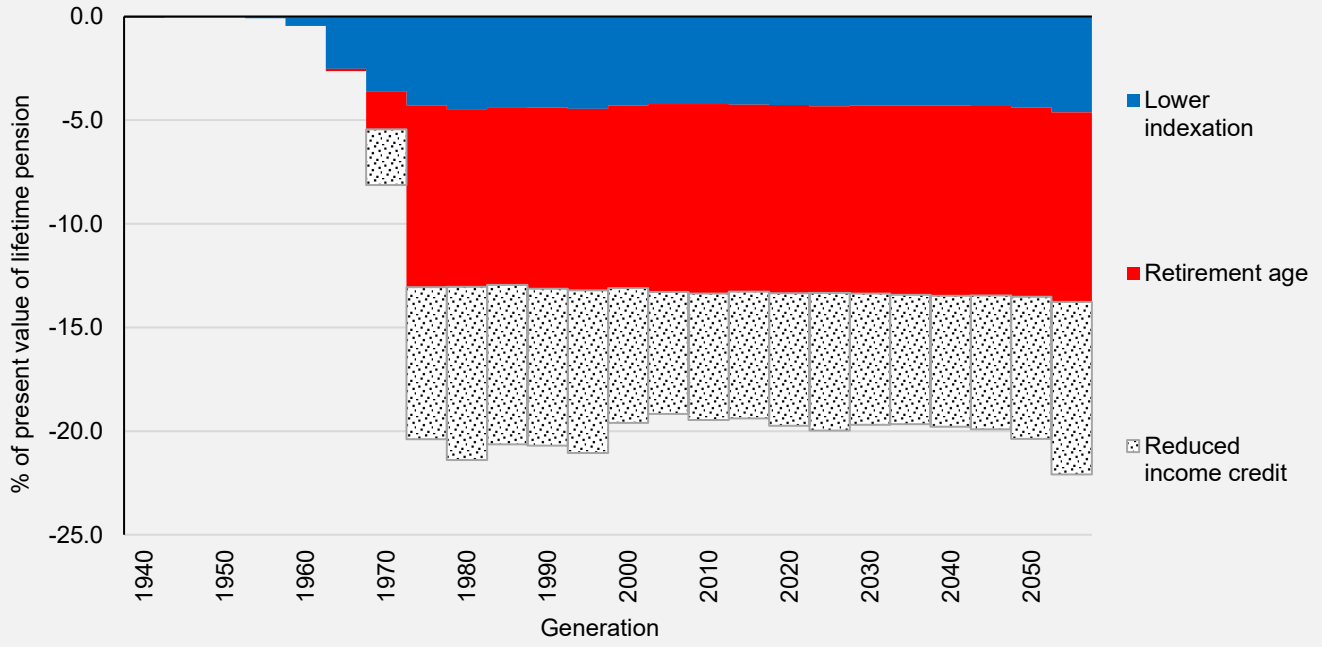
[49] The relative impact of the individual parts of the pension reform also depends on the order in which they are calculated. Given the history of the approval of the individual parts, in Chart B3.1.1 we have first calculated the impact of the change in the indexation formula, then the impact of the retirement age, and finally the impact of reduced income credits in the calculation of newly granted pensions. This order relatively increases the impact of indexation compared to the impact of reduced credits, as it takes into account a higher number of pensioners (before the increase in the retirement age). If the individual steps of the pension reform were ordered differently (and also if their various components were cancelled), the partial impacts could be slightly different. However, the overall impact must be the same.

[50] The classification of "demanding occupations" is linked to the job classification register and covers all workers in the fourth job category, i.e. approximately 12,000 people. According to the original government proposal, "demanding occupations" were also to cover part of the third job category, approximately another 108,000 people, but this group was excluded. The situation of the employees concerned in these occupations should be addressed through a mandatory contribution by their employers to "old-age savings products" of up to 4% of their wages, from which these employees could finance their living expenses in the form of a so-called pre-retirement pension.

On the other hand, the reduction of the so-called "child-rearing bonus " for newly granted pensions will lead to lower costs and greater stability of the pension system. Instead of the child-rearing bonus, care for the first and second child should now be rewarded in the form of so-called "fictitious assessment bases," which will be derived from the general assessment base ("average wage"). Overall, the change in the area of child-rearing bonuses could mean lower pension system expenditures of approximately 0.1 to 0.2% of GDP. The bill also contains a number of other changes, such as recognition of doctoral studies as non-work validated period of insurance, recognition of widow's/widower's pensions for registered partners, easing the conditions for recognising pensions when the minimum insurance period of 35 years is not met, a more modest reduction of the pension in the case of early retirement upon obtaining 45 years of insurance, an extension of the time limit for renewing entitlement to a widow's/widower's pension from two years to five years, and some administrative changes. However, compared to the changes mentioned above, the overall impact of these changes will be negligible.

The impact of the main parts of the reform on different generations is shown in Chart B3.1.2. The chart clearly shows that for generations born before 1965, the effect of the pension reform will be relatively limited and will mainly be related to the change in the indexation mechanism. A substantial part of the reform will then be “paid for” by the generation of the so-called “Husák children”, i.e. the generation from the second half of the 1970s and all younger generations. In relative terms (i.e. as a percentage of lifetime pensions earned before the reform), the impact on generations after 1975 will be essentially uniform.

Chart B3.1.2 Impact of pension reform on individual generations



Source: CSSA (2025), CZSO (2025); CFC calculations.
Note: total impacts for the period 2000–2150, real terms in 2024 prices, discounted at a real interest rate of 1%. The x-axis shows individual generations according to five-year periods of their birth. For generations after 2055, the entire period of their expected pension drawdown is not covered, so they are not included.

3.1.2 Disability pensions

As with old-age pensions, we first project the number of beneficiaries and then the average disability pension. The projection of the number of disability pensioners is based on assumptions about the proportion of people receiving a disability pension in each age cohort (the rate of disability). As with the retirement rate, we distinguish between the rates for men and women.[51] The rate of disability increases with age, peaking in the past between 60 and 63 years for men and 56 and 60 years for women. The peaks of the age-specific disability rate curve are currently lower than they were in the past, especially for men. This is primarily a manifestation of the healthy ageing hypothesis.[52]

[51] For a more detailed description of how the number of disabled pensioners is projected, see the study of the Office of the CFC (2019): Projekce důchodového systému [Pension System Projection, available in Czech only].
[52] See subchapter 3.2 of this Long-Term Sustainability Report and CFC (2021): Report on the Long-Term Sustainability of Public Finances, Box 4.3.

Close to retirement age, disability rates are mainly influenced by the conversion of some disability pensions to old-age pensions. Disability rates fall here because some of those receiving disability pensions opt for old-age pensions and are thus removed from the disability pensioner register. Some disability pensioners with higher disability pensions draw this pension until the age of 65, when their disability pension is automatically converted to an old-age pension and the disability rate drops to zero.

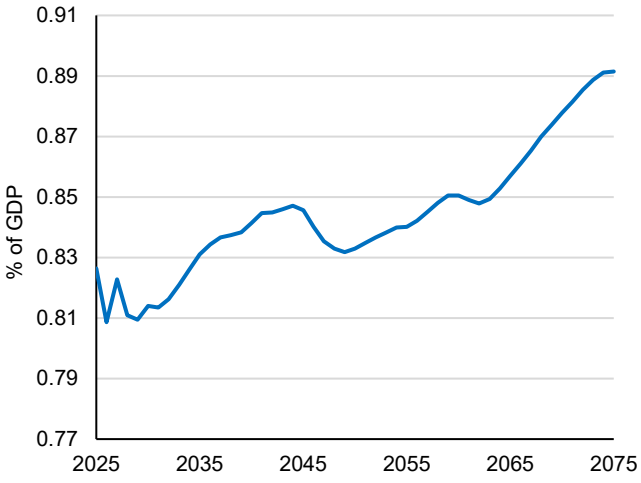
In our projection of age-specific disability rates, we take the rising retirement age into account. For the population under 55, we assume the same disability rates as in the past. We also assume that the disability rate curve will peak two years before retirement age. The disability rate will thus rise steadily to this peak from the age of 55. We again assume an even decline in the disability rate from its peak until retirement age. After reaching the statutory retirement age, we assume a zero disability rate.

In our projection, the number of disability pensioners rises steadily and peaks in 2037, when it will be 11.4% higher than now. The growth in the number of disability pensioners is linked on the one hand with population ageing and on the other hand with the rising of the statutory retirement age. In the period 2038–2062, the number of disability pensioners will decline as they retire on old-age pensions. In 2062, the number of disability pensioners will be roughly the same as it is now (or 1.2% higher than in 2024). Subsequently, the number of disability pensioners will increase over the projection horizon.

We project the average disability pension by assuming a constant ratio between the average disability pension of a given level and the average old-age pension. The dynamics of the average disability pension thus follows the growth in old-age pensions.

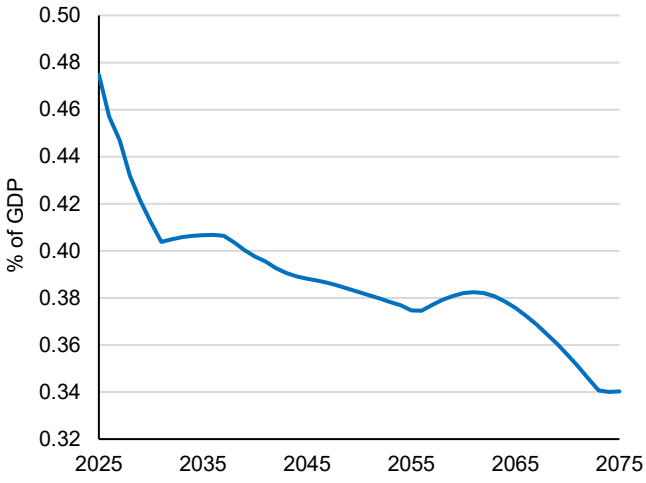
Overall, our projection of the share of disability pension expenditure to GDP fluctuates around 0.8% and then gradually increases towards 0.9% (see Chart 3.1.4 and Table 3.1.1).

Chart 3.1.4 Ratio of expenditure on disability pensions to GDP (in %)



Source: CSSA (2025); CFC calculations.

Chart 3.1.5 Ratio of expenditure on survivors' pensions to GDP (in %)



Source: CSSA (2025); CFC calculations.

3.1.3 Survivors' pensions

Survivors' pensions include widows', widowers' and orphans' pensions. Again, we first simulate the number of recipients of each type of pension. For orphans' pensions, we assume that the proportion of beneficiaries in the population aged 0 to 25 remains stable.[53]

In the case of widow's and widower's pensions, it is necessary to distinguish between pensions paid individually (solo) and pensions paid out concurrently, i.e. in combination with old-age (or disability) pension. For solo widow's and widower's pensions we assume an approximately constant share in the part of the adult population (i.e. for our purposes, people aged over 21) not receiving an old-age or disability pension.

Both the number of recipients of orphans' pensions and the number of recipients of solo widow/widower pensions are projected to decline slightly, as both demographic groups used as the basis for the projection are shrinking despite the increase of the

[53] An orphan's pension can be drawn by a beneficiary up to the age of 26 (if studying at university).

retirement age. For orphans' pensions, this is mainly due to lower projected fertility rate and therefore a lower number of children.

We use a more comprehensive approach to project the number of widow's and widower's pensions paid in combination with old-age or disability pensions. For the projection, we use age-specific rates of receipt of widow's (and, by analogy, widowers') pensions, which show what proportion of women (or men) of a given age receive this type of pension. The curve of these age-specific rates increases with age. We adjust the age-specific rates of receipt of the survivors' concurrent pensions in the projection for the extension of the statutory retirement age and the extension of life expectancy.[54] The increase in the statutory retirement age reduces the number of people entitled to a combination survivor's pension, as, ceteris paribus, it reduces number of pensioners. If life expectancy rises, or if male and female life expectancy converges, the event of widowhood moves to a higher age on average. So, despite the increasing number of senior citizens in the population, there is a slight decline in the number of concurrent survivors' pensions paid in our projection.

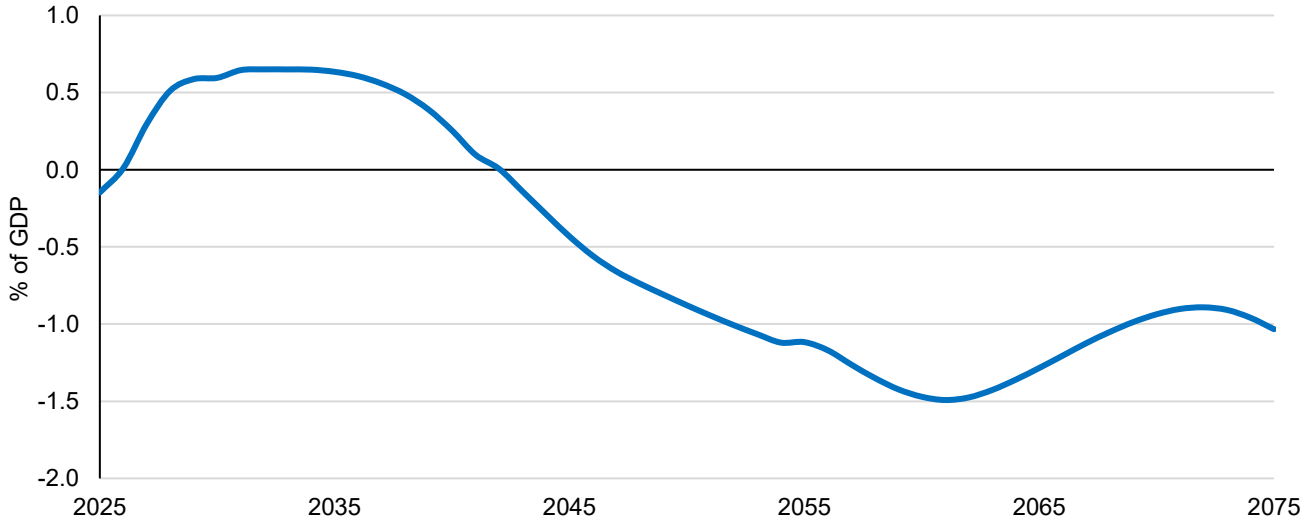
We again model the level of survivor s' pensions as a fixed ratio to the old-age pension. Overall, the projection of survivors' pensions shows a relatively modest development, falling from 0.47% to 0.34% of GDP at the end of the projection horizon, mainly due to a decline in the number of widows'/widowers' pensions paid concurrently (impact of the extension of the retirement age; see Chart 3.1.5 and Table 3.1.1).

3.1.4 Total revenue, expenditure and balance of the pension system

We model pension system revenue on the basis of the expected evolution of compensation of workers. In our macroeconomic projection, we expect the ratio of such compensation to GDP to increase as a result of convergence (see subchapter 2.3). The ratio of pension system revenue to GDP will thus rise proportionally as well. Overall, the revenue of the system will thus go up from 8.6% of GDP (in 2025) to approximately 9.3% of GDP at the end of the projection. However, such an increase in revenues to the system cannot be sufficient to cover the increase in expenditure, especially on old-age pensions, described above.

The pension system as a whole is projected to improve over the next few years, with deficits initially declining and even modest surpluses thereafter (maximum to 0.65% of GDP in 2032). This will mainly reflect the postponement of pension indexation to real wages until 2029 and the growth in real wages. However, after 2040, due to the increase in the number of pensioners, the system will start to move into deficits, peaking around 2061, when they are projected to reach approximately 1.5% of GDP per year (see Chart 3.1.6). The subsequent decline in expenditure and improvement in the pension system balance will be driven by a reduction in the number of old-age pensioners.

Chart 3.1.6 Annual balances of the pension system



Source: CZSO (2025), CSSA (2025); CFC calculations.

[54] For details, again, see the study of the Office of the CFC (2019): Projekce důchodového systému [Pension System Projection, available in Czech only].

Table 3.1.1 Summary of pension system projections for selected years (% of GDP)

	2025	2035	2045	2055	2065	2075
Old-age pensions	*7.3*	*7.0*	*8.2*	*9.0*	*9.3*	*9.1*
Disability pensions	*0.8*	*0.8*	*0.8*	*0.8*	*0.9*	*0.9*
Survivors' pensions	*0.5*	*0.4*	*0.4*	*0.4*	*0.4*	*0.3*
Total expenditure	8.6	8.2	9.4	10.3	10.5	10.4
Total revenue	8.6	8.8	9.0	9.1	9.2	9.3
BALANCE	-0.1	0.6	-0.4	-1.1	-1.3	-1.0

Source: CZSO (2025), CSSA (2025); CFC calculations.
Note: Old-age pensions include pensions for members of the armed forces. The totals in the table may not add up due to rounding.

3.2 Health care

In the Czech Republic, health care expenditure has long been covered primarily by public funds, which account for around 85% of funding. The largest share of healthcare expenditure is covered directly by health insurance companies, which account for approximately 70% of total healthcare expenditure.[55] It is this part of expenditure that we focus on in our projection. On the revenue side, we also focus only on the public health insurance system.

The basis for the projection of the expenditure side is the profile of health expenditure per capita for a given age, distinguishing separately age-specific health expenditure for men and women. We assume that these costs are sufficiently stable over time. Despite the assumption of stability of the cost curve, it may change over the projection period. For example, the cost curve may change in line with the concept of healthy ageing or the morbidity effect.[56]

In our macroeconomic projection, we assume that real wages will grow faster than labour productivity or GDP per capita (see subchapter 2.3). If we assume that wages in health care maintain their current level relative to the average wage, growth in the share of wages in GDP will lead, ceteris paribus, to an upward shift in the health care cost curve, because wage costs are a significant part of health care expenditure.

On the other hand, the relative price of some non-wage cost items (such as imported medicines and medical equipment) may fall precisely because of real convergence. In fact, real convergence causes, among other things, the convergence of the domestic price level to the foreign price level, and thus the appreciation of the real exchange rate, which may in turn hamper the growth of health spending. Given the aforementioned uncertainty about the direction in which the age-specific health care cost curve will change, in our simulation we use a stable curve derived empirically as the average of the relevant curves for the period 2010–2021, using separate curves for men and women. Unlike in previous projections, we have also included the latest available data for 2020 and 2021, i.e. the COVID-19 pandemic period, in the average. Contrary to our original expectations, health care costs did not return to pre-pandemic levels and remain higher even now. In the long term, we therefore expect costs to remain at higher level.

A stable cost curve over time assumes that health care costs per person of a given age change in proportion to GDP per capita. So, if there were no change in the demographic structure, health care expenditure would increase proportionately to the growth of the economy. All changes in the share of health care expenditure are thus solely a result of the changing age structure of the population. Given the shape of the curve, which shows increasing costs covered by health insurance with age, population ageing implies a gradual increase in total healthcare expenditure (see Chart 3.2.1).

Health insurance expenditure currently stands at 6.4% of GDP. If the medium variant of the demographic projection were to materialise, the total costs covered by public health insurance would gradually rise to around 7.7% of GDP at the end of our projection horizon in 2075, i.e. an increase of 1.3 pp. Compared to our 2024 projection, expenditure has increased by approximately 0.7 pp. This is due to the aforementioned abandonment of the assumption that health insurance companies' expenditure will return to pre-pandemic levels (see Chart 3.2.2).

The revenue side of the public health insurance system relies on contributions paid by employees, employers and the self-employed and individuals with no taxable income and on contributions paid by the state for “state insurees”, i.e. children, students, old-age and disability pensioners, the unemployed etc. However, payments for state insurees are budget neutral from the perspective of the overall general government deficit, because they constitute revenue to one public budget component – health insurance companies – on the one hand, and expenditure of

[55] See CZSO (2024): Health Accounts of the Czech Republic 2010–2022.
[56] See CFC (2021): Report on the Long-Term Sustainability of Public Finances, Box 4.3.

another public budget component – central government – of an equal amount on the other hand.

We estimate the contributions collected from the first group as a constant ratio to compensation of workers. Here we project slight growth in contributions collected, due to the assumed rise in the ratio of wages and salaries to GDP.

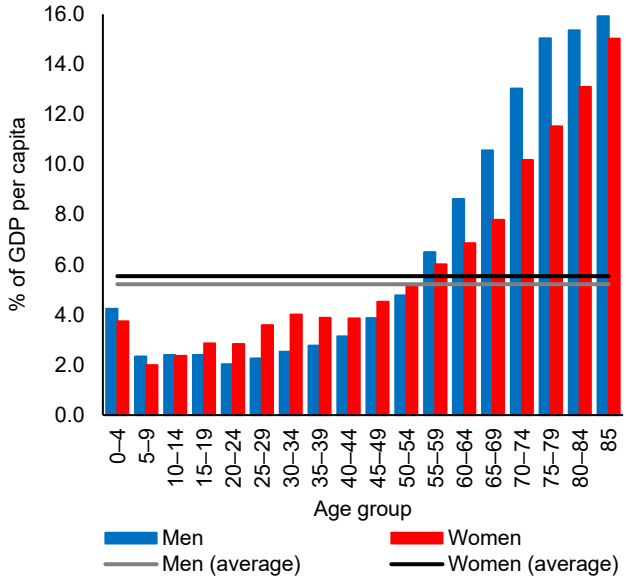
For the period after 2023, a mechanism of automatic indexation of payments for state insurees has been adopted. According to the automatic valorisation under amendment No. 592/1992 Coll. to the Czech National Council Act on Public Health Insurance Premiums, as amended (the "Premiums Act"), from 2024 the payments for state insurees will automatically be indexed to the consumer price index and to half of the growth in real wages.[57] We therefore take this indexation into account in our projection.

We therefore assume that the reference base will automatically increase in line with the indexation mechanism. Inflation is assumed to be at the inflation target level, i.e. 2%. Nevertheless, over the projection period, health insurance revenue for state insurees will fall from around 1.9% today to 1.3% of GDP in 2075. This is due to the indexation mechanism itself, which guarantees lower growth than nominal GDP growth. This decline will thus compensate for the previous excessive growth in revenue for state insurees in the context of the COVID-19 pandemic (see above).

Total revenue to the health insurance system, which will reach 6.3% of GDP this year, will gradually decline to 6.1% of GDP at the end of the projection horizon, assuming automatic indexation of the reference base for payments for state insurees.

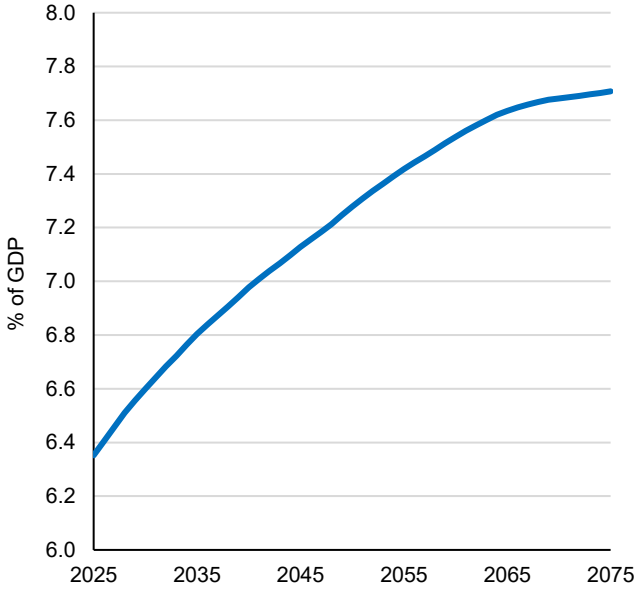
Under the medium variant of the demographic projection, the public health insurance system will be in deficit throughout the projection horizon. In this scenario, the public health insurance system balance will increase from the current slight deficit of 0.02% of GDP to 1.6% of GDP in 2075.[58]

Chart 3.2.1 Costs covered by the health insurance by age group



Source: CZSO (2025); CFC calculations.

Chart 3.2.2 Ratio of public health care expenditure to GDP (%)



Source: CZSO (2025); CFC calculations.

3.3 Non-pension social benefits in cash and long-term care

Other expenditure items include spending on non-pension social benefits in cash and long-term care. In the model, we first simulate benefits that are fiscally significant, amounting to more than 0.1% of GDP. At the same time, these benefits must meanwhile be identifiably linked to demographic change. Expenditure on maternity benefit, parental allowance, care allowance and housing allowance meet these two criteria. Tax advantage for dependent children is also included among these non-

[57] See the Premiums Act.

[58] Technically, however, it is not possible for the healthcare system to be permanently in deficit. The deficits of health insurance companies will therefore have to be covered, and there will probably be an increase in the state budget's contribution, e.g. an increase in payments for state insurees. However, in this Long-Term Sustainability Report, we model the balance of the entire general government sector, so these deficits will in any case be reflected in the overall general government deficit regardless of where they arose.

pension social benefits in cash.[59] We then project other benefits, which we assume maintain a constant percentage of GDP at the current level. Other benefits comprise unemployment benefit, child allowance, foster care allowances, birth and funeral grants, sickness benefits and social assistance/needs benefits.

We simulate expenditure on fiscally significant social benefits separately and use their link to demographic change for the simulation. In the case of housing allowance, we have verified the link to demographic change on the basis of past trends. For some benefits, such as maternity benefit and parental allowance, the link to demographic change follows from the design of the benefit itself. For the simulation, we use our modified CZSO demographic projection. At the same time, we assume that the ratio of the average benefit amount to the average wage is maintained and that the current non-take-up rates of some benefits are maintained.

We base our simulation of **maternity benefit** on the construction of that benefit. We use a constant ratio of the average benefit amount to the average wage multiplied by the duration of receipt of the benefit as the basis. We link the projection of this benefit to the projection of the number of new births.

The projection of **parental allowance** expenditure is linked to the development of the number of children up to the age of three. This is a change from the projections until 2023, as the length of parental leave has been reduced from four to three years. The simulation is based on data on the structure of parental allowance recipients by age of child, the number of parental allowance payments and the number of terminations by age of child at the time of termination. We then calculated the proportion of recipients in each age cohort and their average monthly parental allowance amount. In the simulation, we assume that this share, together with the ratio of the average monthly benefit to the average wage, is constant over time. The current parental allowance is CZK 350,000.[60]

To estimate the **care allowance**, we use the shares of individuals receiving an allowance in the given age categories and in the given dependence category in the years 2014–2023.[61] Under the assumption of a constant share of the number of individuals of a given age drawing the allowance, we then use the demographic projection to determine the total number of individuals drawing the allowance in the various dependence categories. The care allowance amount is determined by approved legislation.[62] While there has been an increase in the amount of the allowance for persons in the 2nd to 4th level of dependency since 1 July 2024 (the highest increase being in the highest level of dependency in home care, by CZK 7,800, i.e. 40.6%), the amount of the allowance in the 1st level has not changed. From 1 January 2026, there will be an increase in the care allowance amount for dependency levels 1 and 2 (approximately 10% for level 2 and 48% for level 1). The care allowance amount for persons in the highest degree of dependency using residential social services remains lower than for persons in home care.[63] From 2027 onwards, we assume a stable ratio of the amount of the allowance to the average wage.

The projection of **the housing allowance** is also linked to demographic change. We simulate the allowance according to past trends based on CZSO data. This shows that approximately 25% of the number of housing allowance payments are made to people over 65 years of age.[64] The remaining three quarters of beneficiaries are between 18 and 64 years old.

Child benefits, housing benefits, living allowances and housing supplements will be merged into a single benefit, known **as state social assistance benefit**, from October 2025. The first benefits under the new rules will be paid out from April 2026.[65]

[59] The reason for this is the national accounts methodology, whereby tax advantage for child is included in social benefits (i.e. an increase in public budget expenditure), while at the same time personal income tax revenue is reported at a level that does not take this institution into account. See subchapter 3.6 of this Long-Term Sustainability Report.
[60] For parents of two or more children born at the same time, the total amount of the benefit is CZK 525,000. However, in the model, we simulate a uniform parental allowance of CZK 350,000 for all children. According to the CZSO data, the share of multiple births in all births was only 1.3% in the period 2018–2022 and fell to 1.2% in 2023.
[61] The share of people receiving care allowance increases significantly after the age of 75. In our calculation, we combine data from the Czech Labour Office and the Ministry of Labour and Social Affairs of the Czech Republic (MoLSA). For a detailed description of the calculation method, see the underlying study by the Office of the CFC (2019): Odhady nákladů příspěvku na péči v návaznosti na stárnutí populace [Estimates of the Costs of Care Allowance as the Population Ageing, available in Czech only].
[62] Section 11 of Act No. 108/2006 Coll., on Social Services, as amended. The amendment took place in 2024 (Act No. 164/2024 Coll.) with effect from 1 July 2024, and in June 2025, the allowance for the level 1 and 2 dependency category was increased, effective from 1 July 2026 (amendment to Act No. 323/2025 Coll., on the Uniform Monthly Reporting by Employers, as amended). From 1 January 2026, the monthly care allowance for persons over 18 years of age will range from CZK 1,300 in the lowest level 1 dependency category to CZK 27,000 in the highest level 4 category. The allowance in the level 1–3 is higher for persons under 18 years of age.
[63] The care allowance is usually used as part of the client's payment for the social service. For persons in levels 1 to 3 of dependency, the amount of the allowance does not depend on whether the care is provided at home or in a residential social service, but in the highest level 4, the allowance for residential social services is CZK 4,000 (i.e. 14.8%) lower than for clients in home care.
[64] We also verified this figure with EU-SILC data for the Czech Republic for 2022, according to which the share of people aged 65+ receiving housing allowance is approximately one-third of the total and their share of total expenditure on housing allowance is 20.3%.
[65] See Act No. 151/2025 Coll., on State Social Assistance Benefits, as amended.

However, in this year's projection, we are currently projecting these benefits individually.

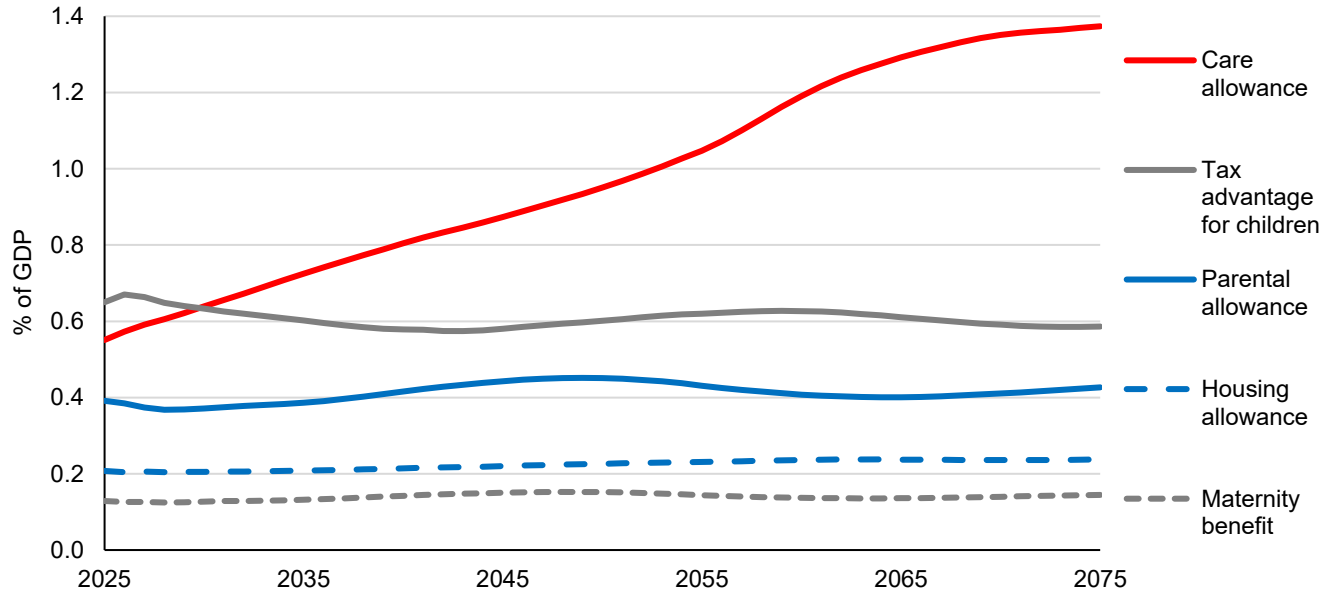
The evolution of the **tax advantage for children** is linked to the evolution of the number of children and higher education students. Minors under the age of 18 are eligible for the benefit. It also applies to people under 26 who have student status or who, for health reasons, are unable to undertake continuous training for future occupation or to engage in a continuous gainful activity. In 2025, the annual amount of the tax benefit is CZK 15,204 for the first child, CZK 22,320 for the second child and CZK 27,840 for the third and each subsequent child. In the simulation we use the average of the values of the benefits for the first and second child, i.e. CZK 18,762. We assume that the amount of the tax advantage for children will increase in line with the average wage.

Projections of expenditure on individual benefits as a ratio to GDP are shown in Chart 3.3.1. Due to the ageing of the population, expenditure on care allowance will grow the fastest among social benefits, rising from 0.5% of GDP today to almost 1.4% of GDP in 2075.

Expenditure on parental allowance will decrease until around 2030, then increase until the early 2050s, after which it will alternate between a period of slight decrease and a period of slight increase. This is due to the expected evolution of the number of children under the age of three. The amount of tax advantage for children will fluctuate around 0.6% of GDP. Total social benefits other than pensions will increase from 2.8% to 3.7% of GDP over the entire period under review. The volume of non-pension social benefits will increase mainly as a result of rising expenditure on care allowances. From the early 1960s onwards, total expenditure will grow more slowly.

Owing to population ageing, we expect not only an increase in care allowances but also an increase in **other long-term care expenditure**. Part of these expenditures is financed from the public health insurance system and is thus recorded under health care expenditure. Part is financed directly by clients of social services through their own contributions or from their care allowances and thus does not enter the general government expenditures. The remainder, however, is financed from other public funds (the state budget and local budgets). In the case of these expenditures, the same sensitivity to demographic developments is assumed as for the care allowance, so we assume that these expenditures will develop in parallel with the care allowance. By 2075, there will be an increase in long-term care expenditures of approximately 0.5 pp of GDP compared to the present.

Chart 3.3.1 Projections of non-pension social benefits in cash



Source: CZSO (2025), MoLSA CR (2025); CFC calculations.

3.4 Education

The ratio of education expenditure relative to GDP was around 4.5% in 2024, with the largest part of it being financed through the Ministry of Education, Youth and Sports of the Czech Republic (MEYS CR). More than three quarters of the expenditure of its budget are transfers to local public budgets. Besides the MEYS CR, municipalities and regions, which are responsible for establishing and administering educational establishments from pre-schools to

vocational colleges, also contribute to education expenditure.

Wage costs in regional education account for the largest part of public education spending. Their projection is linked to wage growth in the economy and to the number of staff, which is directly related to the number of pupils. In the projection of education expenditure shown in Chart 3.4.1, we assume that the ratio of teaching and non-teaching staff per thousand pupils in each type of school remains unchanged over the projection horizon. The share of pupils in each age category is also kept at the level of the average actual shares over the period 2015–2024 in the projection. After an initial increase, expenditure on public education as a percentage of GDP will decline, particularly in the 2030s, due to demographic developments, when fewer teaching and non-teaching staff will be needed in the education system due to fewer pupils.

The growth in total education expenditure is mainly influenced by the dynamics of salaries of teaching and non-teaching staff. In our projection, we assume the same dynamics as the average wage in the economy for all employees in regional education except teachers. For teachers, the projection assumes a guaranteed salary level so that, on average, the salary per full-time equivalent is 130% of the average monthly nominal wage in the calendar year before last.[66]

Another significant part of the expenditure of the MEYS CR consists of payments to universities for their current activities and for research and development (R&D). In particular, payments to universities show the opposite trend to transfers to local public budgets. Their share of the ministry's total expenditure is decreasing. While in 2013, expenditure on universities accounted for almost one third of the total expenditure of the MEYS CR, in 2024 it was only 20%, although there was a slight increase of around 1 pp compared to 2023. Going forward, however, we project that spending on universities will stop declining, mainly because of rising wage costs. The share of university students aged 18 to 26 in the total population in the same age group is comparable to the level of this indicator in Austria. For this reason, we leave the share of students in the total population in the same age group at the level of the ten-year average (i.e. the actual shares from 2015 to 2024) for the purposes of the projection. Given the demographic projection, an increase in the number of students can thus also be expected, with a peak at the end of the 2030s. Thereafter, the number of university students will decline until around the mid-2050s, when the number of university students should start increasing slightly. However, we expect another decline at the end of the 2060s.

In universities' operating costs, wage growth will be reflected in growth of the compensation of academic workers, whose number is also largely dependent on the number of students. Given demographic trends, the number of university students will continue to grow for less than a decade and, after a slight decline, will grow in the second half of the 2030s until 2039, when it will peak. This is reflected in the need to expand the capacity and equipment of universities. Thus, the bulk of the operating costs of public universities in our model depends on demographic trends, while we expect the remaining part of these costs (40% of operating costs) to grow in line with GDP growth.

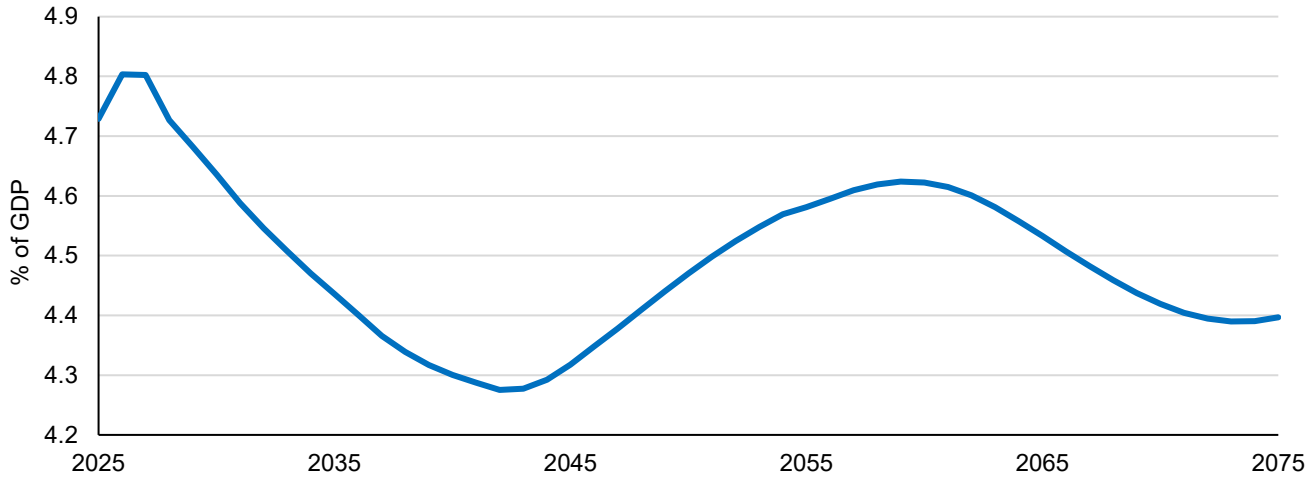
We also expect universities' R&D spending to increase in real terms over the long term. We assume that 60% of R&D spending is affected by the growth of salaries in education, while 40% of the costs grows in line with GDP.[67]

We incorporate a further 1.4% of GDP of education spending into our projection to cover, for example, capital expenditure and other current expenditure, which we assume will grow in line with GDP.

Total education expenditure in real terms will increase over the entire projection period. In relation to GDP, it will increase in the early years only until 2026 due to the growth in wage costs. Thereafter, education expenditure in relation to GDP will decline due to demographic developments as the number of pupils in public schools (excluding universities) declines. In the mid-2040s, however, public education expenditure relative to GDP will start to rise again, reaching 4.6% of GDP at the turn of the 2050s and 2060s. Over the next 13 years, the ratio of public education expenditure in GDP will decline again due to demographic developments, but in 2074, the penultimate year of our projection, it will begin to rise slightly again (see Chart 3.4.1).

[66] See Act No. 563/2004 Coll., on Teaching Staff and on Amendments to Certain Acts, as amended, and the press conference of the MEYS CR of 3 October 2023 (https://msmt.gov.cz/ministerstvo/novinar/do-skolstvi-pujde-ze-statniho-rozpoctu-o-4-mld-vic-nez-letos, available in Czech only).
[67] This assumption is based on Eurostat statistics, according to which, given a five-year average, payments to employees account for about 60% of total expenditure on tertiary education.

Chart 3.4.1 Ratio of public education expenditure to GDP (%)



Source: MEYS CR (2025), CZSO (2025); CFC calculations.

3.5 Expenditure associated with convergence effects and other expenditure

Above, we discussed expenditure that we expect to be more or less linked to demographic changes. We could assume that the remaining expenditure of the general government will remain roughly stable as a share of GDP. However, regardless of demographic developments, the very fact that the Czech economy is a converging economy will also have a systematic long-term impact on certain other types of expenditure. Our aim, however, is not to simulate in detail the shares and development of individual expenditure categories. Rather, we are concerned with capturing the systematic and long-term changes that will result from convergence[68]. For this reason, we focus on the contribution of convergence effects to the growth or decline in total expenditure (expressed as a percentage of GDP).

The baseline level of this expenditure, which we do not project separately, is 17.0% of GDP. This figure corresponds to the 10-year average of general government expenditure not being projected separately adjusted for one-off and temporary measures and position in the business cycle.

The first group of expenditure where convergence effects may occur is **public investment**. In this case, a gradual decline in its share of GDP is expected. This relationship is based on our analysis of EU countries, which shows an inversely proportional relationship between a country's economic development and the share of public investment in GDP. Less developed countries tend to spend a larger percentage of GDP on public investment. There are probably several reasons for this. Less developed (but converging) countries are trying to eliminate inadequate infrastructure (motorways, railways, regional infrastructure, etc.), which results in a higher level of public investment. Another possible reason is the higher relative price level of investment goods in less developed countries, which directly leads to a higher share of investment in GDP. Higher relative price level of investment may be due to economic laws (differences in the endowment of less developed economies with capital, labour and technology), but also to the lower quality of public administration, as indicated, for example, by governance quality indices.[69] The CFC projection anticipates that these effects will fade as the Czech Republic's economic development increases, leading to a decline in public investment of 0.3 pp of GDP over the projection horizon (see Table 3.5.1).

The convergence of the Czech economy will also be reflected in **the remuneration** of general government **sector employees**, which will represent further expenditure pressures. This is due to the assumption of a gradual increase in the cost of activities provided by general government sector organisations. Growth in labour productivity and growth in the share of compensation of employees in the private sector will cause wage pressures, which will inevitably spill over into the general government sector. However, activities in this sector are mostly service-oriented, and moreover, it is not possible to fully compensate for wage growth with labour productivity growth (public administration, justice, internal security, etc.). As a result, costs will rise even if the same level of services is maintained by general government sector employees, and the relative share of this expenditure

[68] In the case of defence, the change in expenditure as a percentage of GDP is not the result of economic convergence, but of political decisions in response to the geopolitical situation.
[69] See, for example, World Economic Forum (2020): The Global Competitiveness Report 2020.

in GDP will therefore also increase. This is a manifestation of the so-called Baumol-Bowen effect: goods whose production does not see long-term growth in labour productivity (if they are to be provided in the same quality) inevitably become relatively more expensive as a result of wage growth in other sectors. This subchapter does not simulate the impacts of the Baumol-Bowen effect on expenditure on healthcare, education and defence[70], as these are already included in the partial projections presented in previous subchapters of the Long-Term Sustainability Report. In the remaining areas, our projection assumes that this effect will gradually increase and will represent an additional 0.4 pp of GDP on the expenditure side at the end of the projection period.

There is a change from the previous Long-Term Sustainability Report in **defence expenditure**. We assumed last year that, starting in 2024, the Czech Republic would fulfil its commitments to the North Atlantic Treaty Organisation (NATO) and spend a constant 2% of GDP on defence over the projection horizon. However, this year's projection assumes in its baseline scenario that defence spending will increase by 0.2% of GDP per year from 2026 until it reaches 3% of GDP in 2030. After 2030 there will be a gradual reduction in defence spending back to 2% of GDP in 2034. We then maintain this share of GDP at a constant level. Our baseline scenario is thus based on both the current wording of national legislation and the political declaration to the European Union. The amendment to the domestic budgetary rules[71] allows for an increase in total state budget expenditure for the 2026 to 2033 by the amount of expenditure on the defence that exceeds 2% of nominal GDP. The European Council document[72] which allows the Czech Republic to activate the national escape clause for defence expenditure[73] explicitly states that the Czech government expects to increase defence spending by at least 0.2% of GDP per year and to reach 3% of GDP for defence in 2030 according to NATO methodology. In our long-term debt projection, we can disregard the fact that the Classification of the functions of government (COFOG) in the national accounts and the NATO methodology differ in terms of the timing of defence expenditure. In 2025, according to the national accounts methodology, defence expenditure will most likely amount to 1.3% of GDP, and according to the NATO methodology, 2% of GDP. This is due, for example, to the effect of advance payments as this kind of expenditure is recorded in the national accounts as expenditure only when it is settled (e.g. delivery of an aircraft). However, different accounting of expenditure over time does not affect the general government's borrowing requirement and therefore does not affect our debt projection. In other words, we disregard the difference between the cash and accrual principles here. One of our alternative scenarios (subchapter 5.3) assumes an increase in military expenditure after 2034 to 3.5% of GDP, in line with the agreement reached at the NATO summit in The Hague in June 2025.

In addition to convergence effects, we also consider **the increase in payments to EU**. The approval of the Multiannual Financial Framework for 2021–2027 has, among other things, led to a permanent increase in the ceiling for payments to 1.40% of the EU's gross national income (GNI).[74] However, annual payments to the EU in the previous programming period 2014–2020 did not reach the ceiling in force at the time (with the exception of 2020). As in previous Long-Term Sustainability Reports, we expect (compared to the current situation) an increase in payments to the EU of 0.1 pp of GDP from 2028 onwards.

For **other expenditure**, we do not anticipate any sensitivity to demographic developments, convergence or other effects, and we therefore keep their level constant until the end of the projection horizon.

[70] In the case of defence spending on salaries, an increase can also be expected, but we do not anticipate the set share of defence spending in GDP being exceeded in the period under review.
[71] Parliamentary Press 856: Amendment to Act No. 218/2000 Coll., on Budgetary Rules and on Amendments to Certain Related Acts, as amended, provision of Section 8, paragraph 3.
[72] Council Recommendation: Allowing Czechia to deviate from the maximum growth rates of net expenditure as set by the Council under Regulation (EU) 2024/1263 (Activation of the national escape clause); Article (9): *"Czechia envisages increases by at least 0.2 percentage points every year, with the objective that total public expenditure on defence reaches 3 per cent of GDP in 2030 using the NATO definition."*
[73] See also NRR (2025): Report on compliance with fiscal responsibility rules for 2024, box 3. Among other things, the box discusses the impact of the activation of the national escape clause by some EU members on compliance with the fiscal rule on net expenditure.
[74] Council Decision (EU, Euratom) 2020/2053 of 14 December 2020 on the system of own resources of the European Union and repealing Decision 2014/335/EU, Euratom.

Table 3.5.1 Ratio of expenditure associated with convergence effects and other expenditure to GDP (%)

	2025	2035	2045	2055	2065	2075
Other expenditure - baseline scenario	17.0	17.0	17.0	17.0	17.0	17.0
Convergence-related changes in other expenditure	0.0	0.1	0.1	0.1	0.2	0.2
public investment	*0.0*	*-0.1*	*-0.2*	*-0.3*	*-0.3*	*-0.3*
growth in general government costs	*0.0*	*0.1*	*0.2*	*0.3*	*0.3*	*0.4*
defence expenditure	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
growth in payments to EU	*0.0*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*
OTHER EXPENDITURE INCLUDING CHANGES	17.0	17.1	17.1	17.1	17.2	17.2

Source: CFC calculations.
Note: The data in the table may be subject to inaccuracies due to rounding.

3.6 Revenue in the long-term projection

For general government revenue projection, we use the cyclically adjusted revenue categories in 2025 while the subsequent long-term projection depends on demographic and convergence effects. For the purposes of this Long-Term Sustainability Report, general government revenues are divided into the following categories: revenue from personal and corporate income tax, statutory social security contributions, revenue from consumption tax and other revenue (e.g. property income, revenue from sales of goods and services, revenue from the EU).

When projecting **personal income tax** (PIT) revenue, we assume that it depends primarily on compensation of employees. According to our estimates, the share of compensation of employees in GDP will gradually increase due to the convergence effect (see subchapter 2.3), and the ratio of this tax to GDP will also grow proportionally. This effect will outweigh the fact that the share of workers in the total population will decline for demographic reasons. According to our macroeconomic projection, wages will grow fast enough to more than offset the decline in the number of workers.[75]

Compared to the previous Long-Term Sustainability Report, the baseline value of this tax has increased by 0.1 pp (from 3.9% to 4.0% of GDP). This is mainly a consequence of the relatively strong growth in nominal wages and salaries in 2024 and 2025. The revision of the output gap and the greater importance of withholding tax in the total revenue from this tax category also play a role. The expected growth in PIT revenue from the current 4.0% of GDP to 4.3% of GDP at the end of the projection is merely a consequence of convergence (see Table 3.6.1).

Corporate income tax (CIT) revenue is highly sensitive to the economic cycle and therefore fluctuates over time. The structure of the tax base also makes this tax difficult to predict. However, we disregard cyclical influences in the long-term projection and, for the sake of consistency, project its revenue based on the development of the net operating surplus. This should explain the development of this tax revenue better than GDP development, as the net operating surplus is the macroeconomic counterpart of net operating profits before tax.[76] As in the case of personal income tax, a convergence effect will also be evident here, but it will have the opposite effect. Growth in the share compensation of employees in GDP will necessarily lead to a decline in the share of gross operating surplus in GDP. The share of net operating surplus in GDP will then decline even more as we assume that the share of fixed capital consumption in GDP will remain unchanged. As a result, the share of corporate income tax revenue in GDP will fall from 3.9% at the beginning of the projection to 2.9% at the end.

Compared to the previous Long-Term Sustainability Report, there has been no change in the baseline value of this tax at the start of the projection (still 3.9% of GDP).

For **other current taxes (e.g. administrative fees)**, we assume a fixed share of GDP, as this has been stable in the long term in the past and, given the current tax policy settings, there are no reasons for us to change this assumption.

Mandatory social security contributions include pension contributions (including the systems of the Ministry of Defence, the Ministry of the Interior, the

[75] It should be noted that we deviate in part from carrying out the projection strictly in accordance with current legislation. Tax regulations often include deductions and discounts or thresholds in nominal terms. Thus, growth in nominal wages and other incomes can lead to an increase in the average tax rate, all other things being equal. This means that without a change in legislation, there is, for example, an erosion of the real value of deductibles and discounts, a shift to higher tax bands and the associated taxation at a higher tax rate, etc. In our projection, however, we do not work with these and similar effects and assume that, for example, the real value of deductible items and discounts will be constant relative to the average wage and that the average tax rate will therefore remain the same.
[76] Again, we disregard the effects caused by inflation (which would be particularly evident in the erosion of the real value of tax depreciation of companies' fixed capital or in the valuation of inventories).

Ministry of Justice and the Ministry of Finance), public health insurance contributions excluding state insurees, payments for state insurees and other mandatory social security contributions (sickness insurance and state employment policy contributions). Due to their structure, all these payments are linked to compensation of employees in our projection in a similar way as PIT. The convergence effect is evident here again and the share on GDP increases proportionally with the increase in the share of compensation of employees. Compared to the previous Long-Term Sustainability Report, the baseline value of mandatory social security contributions at the start of the projection has been reduced by 0.3 pp (from 16.7% of GDP to 16.3% of GDP). This is a consequence of the revision of nominal GDP, implying a lower ratio of insurance revenue and payments for state insurees to GDP, and an updated estimate of the output gap.

In the case of the revenue projection for so-called state insurees, we considered the demographic evolution of the groups to which state insurees belong (for more details, see subchapter 3.2). It should be noted that in the general government sector, payments for state insurees are both revenue (for health insurance companies) and expenditure (for the state budget). They therefore have no impact on the general government balance, but we report them separately because they affect the data on the structure and size of the general government sector.

Consumption taxes (**taxes on production and imports**) mainly include revenue from value added tax and selective excise duties. The revenue from these taxes is simulated according to the share of household final consumption expenditure in GDP, which represents an approximation of the most significant part of the tax base for consumption taxes. According to our macroeconomic projection, this ratio will remain unchanged (a change in the structure of income in favour of compensation of employees does not necessarily translate into a change in the structure of household spending), so consumption tax revenue will also maintain a constant share of GDP.[77] Compared to the previous Long-Term Sustainability Report, there has been a decrease of 0.4 pp (from 11.4% to 11.0% of GDP), mainly as a result of a structural (rather than merely temporary) reduction in selective excise duty revenue.

Property income mainly includes dividends and shares in the profits of state-owned enterprises. It also includes interest income from the placement of surplus liquidity in the State Treasury. Again, we assume a stable share of GDP in the long term. At the same time, we work with a scenario in which the state does not change its share in the major companies it (co-)owns. Overall, we therefore assume that the share of property income in GDP will remain constant at 0.6% in the long term.

Other revenue mainly include revenue from the sale of goods and services and revenue from the EU. The share of revenue from the sale of goods and services in GDP is essentially stable, so it is fixed for the long-term projection. We also assume that revenue from the EU will constitute a constant percentage of GDP. However, the development of this revenue is subject to a considerable degree of uncertainty, which makes it difficult to quantify. Although there has been a short-term increase in this revenue due to the energy and geopolitical situation, there is no specific information about any structural change in the long term. It should also be noted that our projection only includes general government income from the EU, not total EU revenue for all entities in the Czech Republic, which is likely to decline in the future due to convergence to advanced economies.

Table 3.6.1 shows the development of total general government sector revenues, including individual revenue categories (as a percentage of GDP). Although total revenues are constant in our projection, this is only a consequence of the decline in payments for state insurees from 1.9% to 1.3% of GDP over the projection horizon (see subchapter 3.2). If we exclude payments for state insurees from general government revenues, total revenues would rise from 38.9% of GDP to 39.5% of GDP over the projection horizon, mainly as a result of economic convergence and an increase in the share of wages and salaries in GDP.

[77] Here again, we deviate slightly from strict compliance with legislation, as some excise duty rates are constructed as a nominal amount per unit of goods. We therefore assume that legislation will change in the long term in such a way that the revenue from this group of taxes will develop as if they were all constructed as *ad valorem* taxes.

Table 3.6.1 General government revenue in selected years (% of GDP)

	2025	2035	2045	2055	2065	2075
Personal income taxes	4.0	4.1	4.2	4.3	4.3	4.3
Corporate income taxes	3.9	3.6	3.4	3.2	3.0	2.9
Other current taxes	0.2	0.2	0.2	0.2	0.2	0.2
Social security contributions	16.3	16.4	16.6	16.8	16.9	16.9
pension insurance	*8.6*	*8.8*	*9.0*	*9.1*	*9.2*	*9.3*
public health insurance (excluding SIs)	*4.4*	*4.5*	*4.6*	*4.7*	*4.7*	*4.8*
payment for state insurees (SIs)	*1.9*	*1.6*	*1.5*	*1.5*	*1.4*	*1.3*
other	*1.4*	*1.4*	*1.5*	*1.5*	*1.5*	*1.5*
Taxes on production and imports	11.0	11	11	11	11.0	11.0
Property income	0.6	0.6	0.6	0.6	0.6	0.6
Other revenue	4.8	4.8	4.8	4.8	4.8	4.8
TOTAL REVENUE	40.8	40.7	40.8	40.9	40.8	40.8

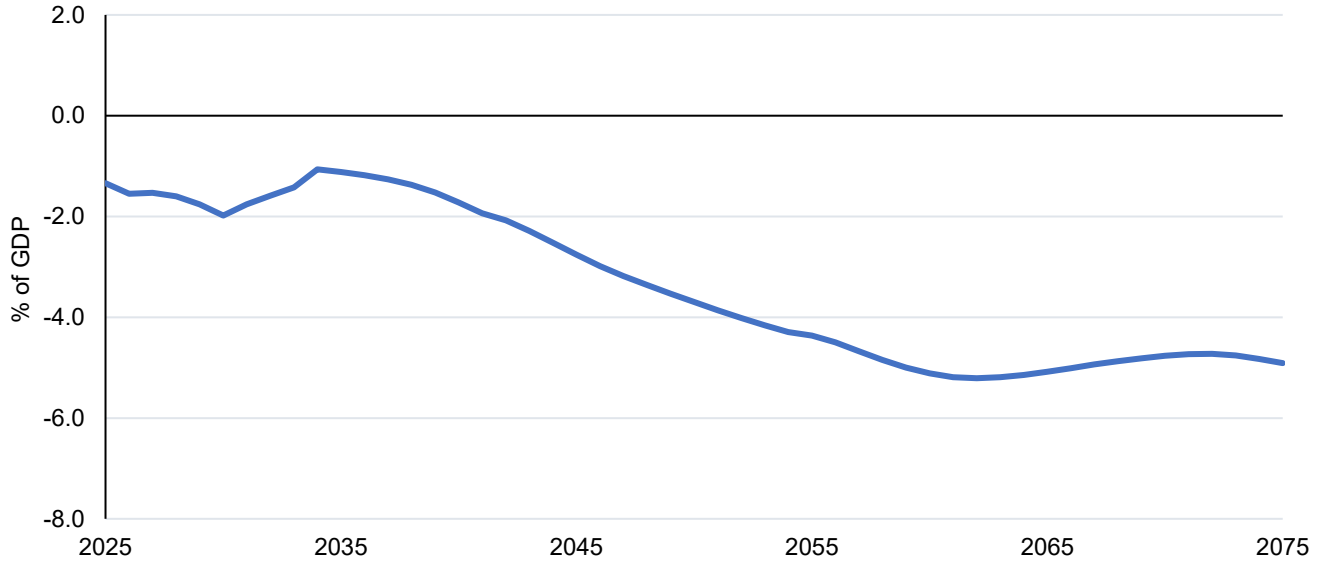
Source: CFC calculations.
Note: The totals in the table may be subject to inaccuracies due to rounding.

4 General government balance and debt

4.1 Primary balance

The projections of individual revenue and expenditure items allow us to produce a projection of the primary general government balance (see Chart 4.1.1), which shows negative values throughout the period under review. The first deterioration in primary balances occurs between 2026 and 2030 because of increased defence spending. In our baseline scenario (see subchapter 3.5), we assume that defence expenditure will increase by 0.2% of GDP per year from 2% to 3% of GDP between 2026 and 2030 and will gradually decline back to 2% of GDP between 2031 and 2034. From 2034 to 2075, we then keep it constant at 2% of GDP. This scenario is in line with the national budgetary rules.[78] The second deepening of primary deficits occurs from 2035 to 2060. This is due to demographics and the associated increase in expenditure (particularly on pensions, healthcare and care allowance). According to the projection, negative primary balances will stabilise after 2060, as smaller cohorts will start to reach retirement age at that time. Nevertheless, primary deficits will remain significant (around 5% of GDP) until the end of the projection period. The revenue side will remain broadly stable in the period under review (growing by 0.6% of GDP as a result of convergence, see subchapter 3.6), and will therefore not contribute significantly to offsetting rising expenditure.

Chart 4.1.1 Primary general government balance



Source: CFC calculations.

4.2 Interest costs

To obtain a comprehensive picture of the development of the general government balance, we need to supplement the trajectory of primary balances with interest expenditure associated with general government debt. Until now, we have expressed both expenditure and revenue items as a percentage of GDP, and the inflation rate was therefore not relevant for them in this expression. However, this is not possible in the case of interest costs. Interest costs are generally determined by the nominal interest rate, which takes inflation into account. The nominal interest rate is an approximate sum of the real interest rate and the inflation rate, with the real interest rate itself being determined by real factors (marginal productivity of capital or the time preferences of economic agents). The long-term inflation rate thus has an impact, via nominal interest rates, on the share of interest costs in GDP and therefore also on the overall size of the share of general government expenditure in GDP. In our projection of nominal interest

[78] Total state budget expenditure can only be increased for the 2026 to 2033 budget years by defence expenditure exceeding 2% of GDP. In other words, defence expenditure (above 2% of GDP) is exempt until 2033, and there is an implicit assumption that after 2033, either defence expenditure will be reduced back to 2% of GDP, or other expenditure will be reduced proportionally, or revenue will be increased. However, the chosen option does not matter for the projection of the state's borrowing requirement and thus for the projection of debt dynamics.

expenditure, we assume 2% inflation, which is in line with the CNB's inflation target.

In our context, the general government debt consists mainly of state debt (more than 90% in the long term), and we focus on this in our projection. We assume that the interest costs on the remaining part of the general government debt (e.g. municipal debt) behaves similarly. In reality, general government debt is financed by a whole range of instruments, from non-marketable loans to a wide variety of debt securities with different maturities, coupon yields and denominations.[79] In our projection, we simplify and divide the entire debt into two parts: short-term debt (i.e. debt maturing within one year) and long-term debt. We assume that the short-term part of the debt is financed at a short-term rate[80] and must be refinanced each year at the current rate. In contrast, we assume that the long-term part of the debt is financed by bonds with an original maturity of ten years and a coupon corresponding to the yield on a basket of government bonds with an average residual maturity of ten years (a ten-year maturity was chosen because it is the longest maturity for which we have a sufficiently long time series that is also internationally comparable). We keep the shares of short-term and long-term debt in total debt constant at 10% and 90%.[81]

We model total interest costs as the product of the general government debt and the so-called implicit nominal interest rate, which is the weighted average of the nominal interest rates paid on the short-term and long-term parts of the debt. The weight of the short-term interest rate in the implicit interest rate is equal to the share of short-term debt, i.e. 10%. In our projection, we consider the short-term interest rate to be constant at 1.8% p.a., as the expected real short-term interest rate of −0.2% p.a. is adjusted for 2% inflation.[82] The interest rate on the long-term portion of the debt has a 90% weight in the implicit interest rate. However, for the sake of simplicity, we assume that the interest rate on the long-term portion of the debt is equal to the 10-year moving average of 10-year interest rates in individual years. This approach considers the fact that the current interest rate is not relevant for servicing costs of ten-year bonds already issued, but rather the interest rate at the time of issue. We also assume that the 10-year nominal interest rate will converge to 2.8% p.a. in the baseline scenario, as we assume a real interest rate of 0.8% p.a. and the rest is the expected inflation rate.

Overall, the selected assumptions lead to the modelled implicit interest rate on general government debt gradually increasing to 3.3% p.a. by 2031 (mainly due to higher interest rates in 2022 to 2025). The interest rate then falls to an equilibrium level of 2.71% p.a.

4.3 Debt

Interest costs are included on the expenditure side in the calculation of the general government balance, thereby exacerbating annual deficits. These accumulate in general government debt, and the growing debt generates a further increase in interest costs (see Table 4.3.1 for selected years). General government debt is heading towards 178% of GDP in 2075 over a 50-year horizon (the baseline scenario). The debt will breach the debt brake threshold in 2037. This course is mainly due to the development of primary balances, not our interest cost model. Even if we were to assume (unrealistically) that long-term real interest rates would be zero throughout the projection period, debt would still head towards around 152% of GDP (see Chart 4.3.1).

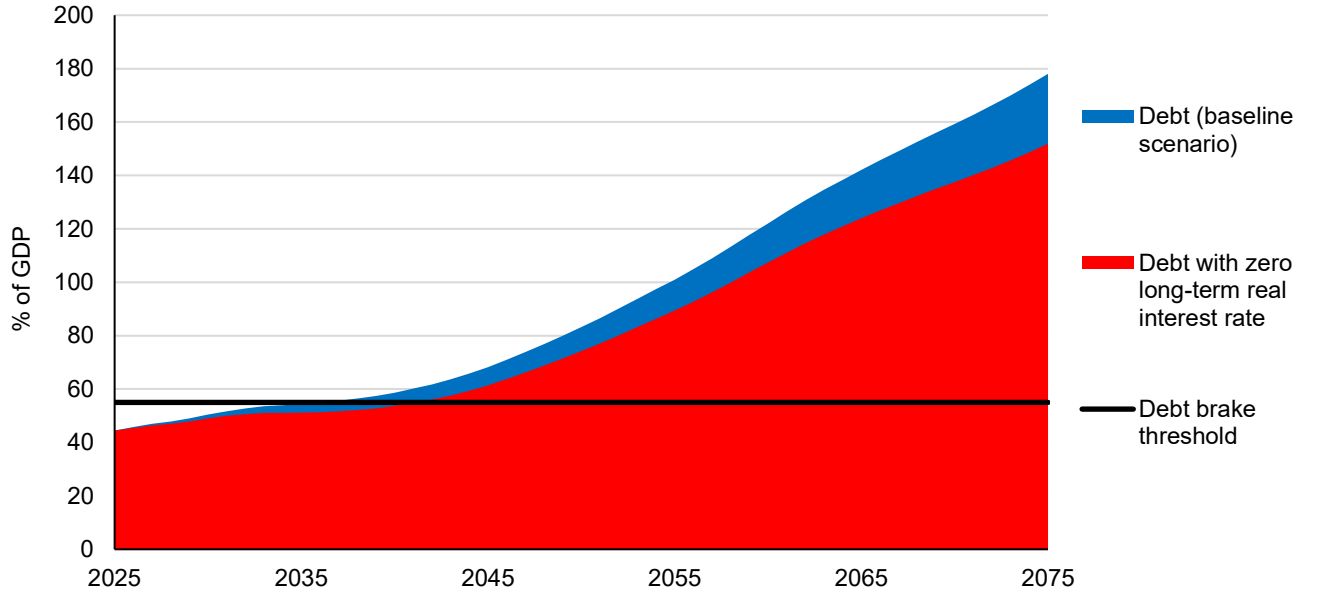
In the previous Long-Term Sustainability Report, the debt brake was projected to be breached in 2038, but in this year's Long-Term Sustainability Report it has been shifted to 2037. The reason for this is that while the parametric adjustments to the pension system affect primary balances and debt dynamics in the medium and long term, increased defence spending above 2% of GDP between 2026 and 2033 will worsen primary balances and debt dynamics in the short and medium term. Breaching the debt brake in 2037 is thus a logical consequence of higher borrowing requirements over the next ten years in the absence of adequate adjustments to the expenditure or revenue side.

In addition to this version of the interest expenditure projection, we also perform an alternative simulation with financial market feedback on interest rates, in which we take into account the relationship between the level of debt relative to GDP on the one hand and the level of interest rates on the other. In the simulation, we assume that each percentage point of debt-to-GDP ratio above the 55% threshold increases the current 10-year real interest rate by 0.039 pp.[83]

[79] For more details, see MF CR (2025): Report on the Management of the Czech Republic's Public Debt in 2024.
[80] Annual average of the 3-month PRIBOR.
[81] The average share of short-term debt of the general government sector in the last six years (2019–2024) was 10.9%, falling to 10.1% in 2024.
[82] The source of historical nominal interest rate data is the CNB (2025), the conversion to real interest rates was made using the GDP deflator (CZSO, 2025).
[83] For an estimate of the risk premium, see Tománková (2020): The Effect of General Government Debt on Government Interest Rates.

Under these assumptions, from 2037, when according to our projection the debt will exceed the debt brake threshold, debt growth would accelerate compared to the baseline scenario. Around 2056, the debt would become unsustainable, and the Czech Republic would fall into a debt trap, as the effective interest rate would exceed the nominal GDP growth rate.

Chart 4.3.1 General government debt



Source: CFC calculations.

Table 4.3.1 Interest costs and total balance (% of GDP) in selected years

	2025	2035	2045	2055	2065	2075
Interest costs (baseline scenario)	1.4	1.5	1.8	2.6	3.7	4.6
Total balance (baseline scenario)	-2.7	-2.6	-4.5	-7.0	-8.8	-9.6

Source: CFC calculations.

4.4 Public finance sustainability indicator

Indicator S1 is used as an overall indicator of the sustainability or unsustainability of public finances. It is generally defined as the percentage of GDP by which the primary structural balance must change (by the same percentage of GDP each year) over the entire forward-looking period for the debt to reach a predetermined value at the end of that period.[84]

In our case, we will choose a 50-year period (2025–2075) and ask by what percentage of GDP the primary balance would have to be better than our projection each year for the general government debt to be at 55% of GDP, i.e. at the debt brake level, at the end of the projection period. The S1 indicator constructed in this way captures the sustainability gap in public finances. However, it should be emphasised that this is an indicator whose purpose is primarily to enable a quick comparison of whether the sustainability of public finances is improving or deteriorating. It is not a recommendation that the balance should actually improve by a given amount each year.

According to our simulation, the public finance sustainability gap is currently 2.88 (last year's value was 3.78 and the year before that 6.22). This means that if the primary deficit were to be 2.88% of GDP better than the baseline scenario every year from 2025 onwards throughout the projection period, debt would be heading towards 55% of GDP in 2075. Given that in such a case the debt trajectory would never exceed the debt brake, there would be no feedback between interest and debt.

If measures to reduce the long-term imbalance in public finances are delayed, the scope of adjustments in tax and expenditure policies to ensure that the debt brake limit (55% of GDP) is not exceeded in 2075 will have to be more significant. The sustainability gap indicator presented above will therefore

[84] For a more detailed description, see, for example, European Commission (2025): Debt Sustainability Monitor 2024.

have to be even higher. If solutions are postponed until the debt brake limit is reached (according to the projection, by 2037), the indicator will increase to 3.59.[85]

It should be noted that a similar indicator constructed by the European Commission, which, however, works with an infinitely long horizon instead of a 50-year projection period and expresses the fiscal effort necessary to balance discounted revenues and expenditures (this is the S2 indicator), gives a value of 5.4 for the Czech Republic in 2024[86]. Given the requirement to balance expenditure and revenue, the S2 indicator is significantly stricter than the sustainability gap calculated by us when using the same data.

[85] So, for the debt to head towards 55% of GDP in 2075, the primary deficit would have to be 3,59% of GDP lower from 2038 to 2075.
[86] European Commission (2025): Debt Sustainability Monitor 2024.

5 Alternative scenarios and additional analyses

The baseline scenario of our projection used in the previous chapters was calculated on the assumptions that the adjusted medium variant of the CZSO's demographic projection will materialise and that the current tax and expenditure policies will be maintained. To at least partly illustrate potential uncertainties and deviations from our baseline scenario, which can generally be significant in long-term projections, we prepared a set of alternative scenarios described in more detail below. The first of the alternative scenarios drawn up for the medium variant of the demographic projection, whereby we consider a more pessimistic assumption regarding the long-term growth of the economy. In the second scenario, we consider alternative parameters of the demographic projection, specifically assuming a different fertility rate trend. On the one hand, we consider a scenario in which the fertility rate will increase over the next 10 years from the current 1.37 to 2.46 children per woman. This fertility rate corresponds to that of the 1970s[87], when fertility was at its highest since the late 1950s. On the other hand, there is a low fertility scenario, where fertility rate will remain at the current 1.37 children per woman and then decline according to the low variant of the CZSO demographic projection. In other alternative scenarios, we simulate different assumptions regarding the extent of increased defence spending, a scenario with the state's annual borrowing requirement affected by persistent local government surpluses, and a scenario with the construction of two nuclear power plant in Dukovany.

5.1 Slowdown in productivity growth

In the first alternative scenario, we examine the sensitivity of the projection to alternative assumptions regarding labour productivity growth. In the baseline scenario of the projection, in addition to the convergence component of labour productivity growth, we also assume continued autonomous technology growth of 1.5% per annum (both in the Czech Republic and Austria). This assumption is based on average productivity growth in developed countries over a longer period, but there is no guarantee that this pace will be maintained in the future. Whereas in previous years we compiled a technological acceleration scenario, in which we assumed higher productivity growth than in the baseline scenario, this year we are analysing the sensitivity of the projection to the opposite situation. This is partly in response to low productivity growth in the chosen convergence target (Austria), where labour productivity has essentially stagnated over the last 17 years. There is therefore a risk that this trend will continue in the long term.

To assess this risk, we are compiling a scenario in which labour productivity would grow 1 pp slower each year than in the baseline scenario, both in advanced economies and in the Czech Republic.[88]

Other parameters, such as the pace of convergence of the Czech economy with other countries and the increase in the share of compensation of workers to gross value added, remain the same in the technological deceleration scenario as in the baseline scenario.

The result of the above is lower GDP growth per worker and thus lower real wage growth (compared to the baseline scenario). However, the number of workers remains unchanged. We therefore do not anticipate any changes in structural unemployment or labour market participation rates.

The revenue side of the budget, expressed as a percentage of GDP, is not affected, because real income and GDP slowdown in parallel. On the expenditure side, the deterioration will mainly affect pension expenditure. Permanently lower real wage growth will cause pensions granted in previous years to grow faster (or decline more slowly) in relation to real wages than in the baseline scenario. This is because the statutory indexation of pensions covers only one-third of real wage growth, so that as wages rise, the ratio of pensions to wages falls. Due to lower GDP growth in this scenario, the size of the debt carried over from previous years in relation to GDP will also be higher, as will debt servicing. Overall, general government debt is up to 92.8 pp higher than in the baseline scenario (see Chart 5.2.1).

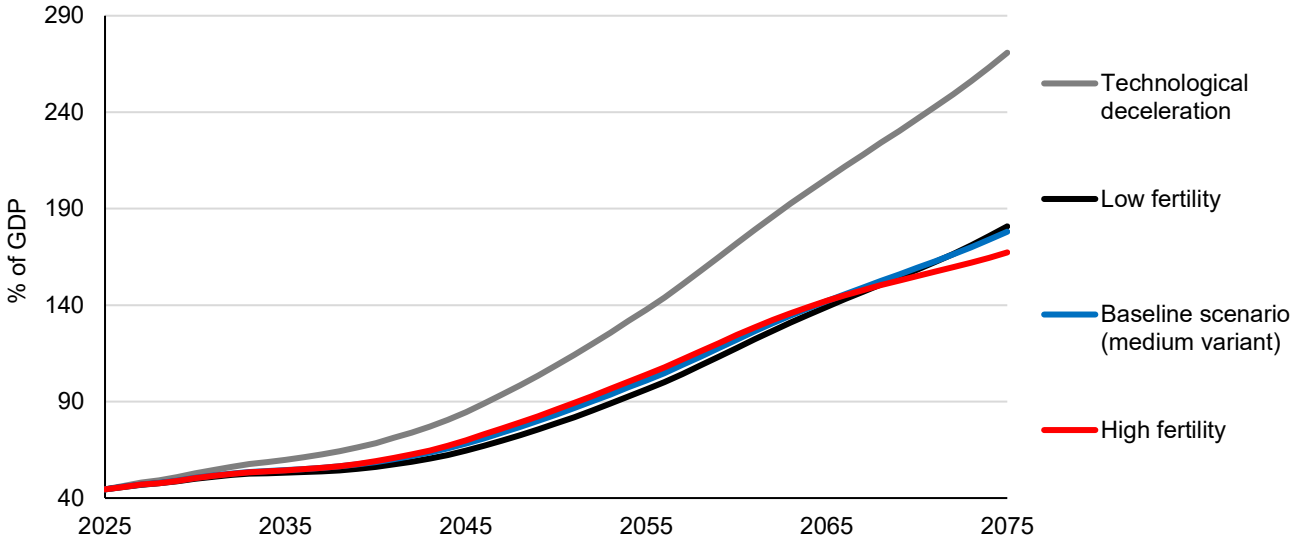
5.2 Different variants of demographic projections

Another scenario analyses the sensitivity of the baseline scenario to different assumptions about demographic development. Here, it would be possible to use the demographic development scenarios compiled by the Czech Statistical Office (high and low variants of the demographic projection). The different demographic scenarios differ from each other

[87] Data according to the World Bank database (2025).
[88] See Chapter 2. We assume a symmetrical impact on both the Czech Republic and Austria (convergence target). The speed at which the labour productivity gap between the Czech Republic and Austria is closed will therefore not be affected.

mainly in terms of different population sizes[89], but are very similar in terms of the projected age structure of the population. The ratio between the number of people of working age (for our purposes, aged 21 to 64) and the number of people aged 65 and over is essentially the same in all scenarios differing only at the very end of the projection horizon. The similarity in the population structure for the demographic scenarios mentioned is due to opposing mechanisms within each demographic scenario. For example, in the high demographic scenario, compared with the medium demographic scenario, higher fertility and higher migration rates cause the ratio of people of working-age population to the population 65 and over to increase, but lower mortality and higher life expectancy reduce this ratio. As a result, the medium, high and low demographic scenarios generate similar projections of the debt-to-GDP ratio.

Chart 5.2.1 General government debt – comparison of alternative scenarios (slower productivity growth and different demographic projections) with the baseline scenario



Source: CZSO (2025), CSSA (2025); CFC calculations.

Given this similarity between the official demographic variants and the relatively significant developments in the area of birth rates and fertility in recent years (see subchapter 2.2 and its Box 2.2), we have constructed two demographic sensitivity scenarios focused separately on different fertility rates.[90] The first of these – the scenario labelled “high fertility” – responds to some frequently heard claims that an appropriate pro-population policy can be sufficient to make the pension system sustainable. Therefore, we consider a scenario in which the fertility rate rises from the current 1.37 to 2.46 children per woman over the next 10 years and remains at this level until the end of the projection. This fertility rate corresponds to the 1970s, when fertility was at its highest since the late 1950s (the so-called "Husák's children"). The other assumptions of the projection (mortality and migration rates) are identical to those of the medium variant. The main result of this sensitivity analysis is that even an extremely favourable combination of demographic parameters will not ensure the stability of the pension system. Although the pension system deficits are 0.2 to 0.7% of GDP lower in 2065–2075 than in the baseline scenario, their decline comes gradually and too late, after 2055, when new births start to enter the labour market. Until then, the pension system deficits are even petty worse than in the baseline scenario (by a maximum of 0.1% of GDP due to higher expenditure on orphan’s and disability pensions). At the same time, however, the higher fertility during this period leads to significantly higher expenditure outside the pension system (education, social benefits, healthcare). In this scenario, these increased expenditures then lead to higher primary deficits and faster debt growth (see Chart 5.2.1). The above-mentioned improvements in pension system deficits only become apparent at the end of the projection horizon (a 10.7% lower debt-to-GDP ratio in 2075).

Symmetrically to the high fertility scenario, we construct a scenario in which the fertility rate will initially remain constant at the current low level of 1.37

[89] While in the adjusted medium variant of the demographic projection, the population remains basically stable at around 10.7 million and then declines from 2050 to 10.2 million in 2075, in the low variant it declines to 8.7 million inhabitants and in the high variant it rises to 11.5 million inhabitants in the same year.

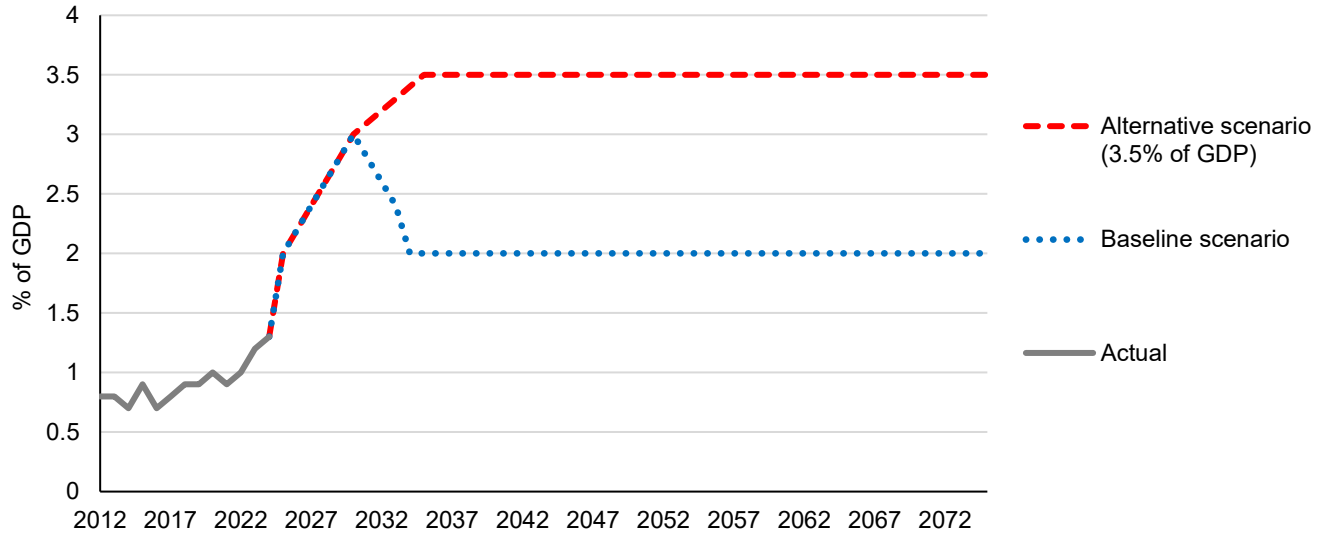
[90] For a more detailed description of the development of these sensitivity demographic scenarios, see the study of the Office of the CFC (2021): Alternativní demografické projekce [Alternative Demographic Projections, available in Czech only].

children per woman until 2035 and then continue to decline in line with the low scenario of the CZSO demographic projection to 1.25 children per woman. In this variant, the deficits of the pension system are initially slightly lower than in the medium variant (lower expenditure on orphan's and disability pensions), and expenditure on social security, education, social benefits and healthcare is also lower due to the lower number of children. This is reflected in a lower increase in debt. In the longer term, the effect of a lower number of workers and lower GDP will begin to take effect, which will be reflected, among other things, in higher pension system deficits and an increase in debt, which will be 2.8% of GDP higher in 2075 than in the medium variant (see Chart 5.2.1). Overall, both variants with different fertility rates show relatively low sensitivity of projected debt to this demographic parameter.

5.3 Permanently increased defence expenditure according to The Hague summit

In our projection of general government debt in the baseline scenario, we assume that defence expenditure will rise to 3% of GDP between 2026 and 2030, before falling and remaining at 2% of GDP between 2034 and 2075.[91] However, at the NATO summit in The Hague in June 2025, the leaders of the NATO member states agreed to increase defence expenditure to 5% of GDP. By 2035, all member states of the alliance must reach the level of 5% of GDP, with states allocating 3.5% of GDP to so-called "core defence" expenditure and the remaining 1.5% of GDP covering other security-related areas (e.g. cybersecurity, critical infrastructure, industrial base, civil preparedness).[92] In this alternative scenario, defence expenditure will increase from 3% of GDP to 3.5% of GDP between 2030 and 2035, and we will then maintain this level until 2075 (see Chart 5.3.1).

Chart 5.3.1 Defence expenditure

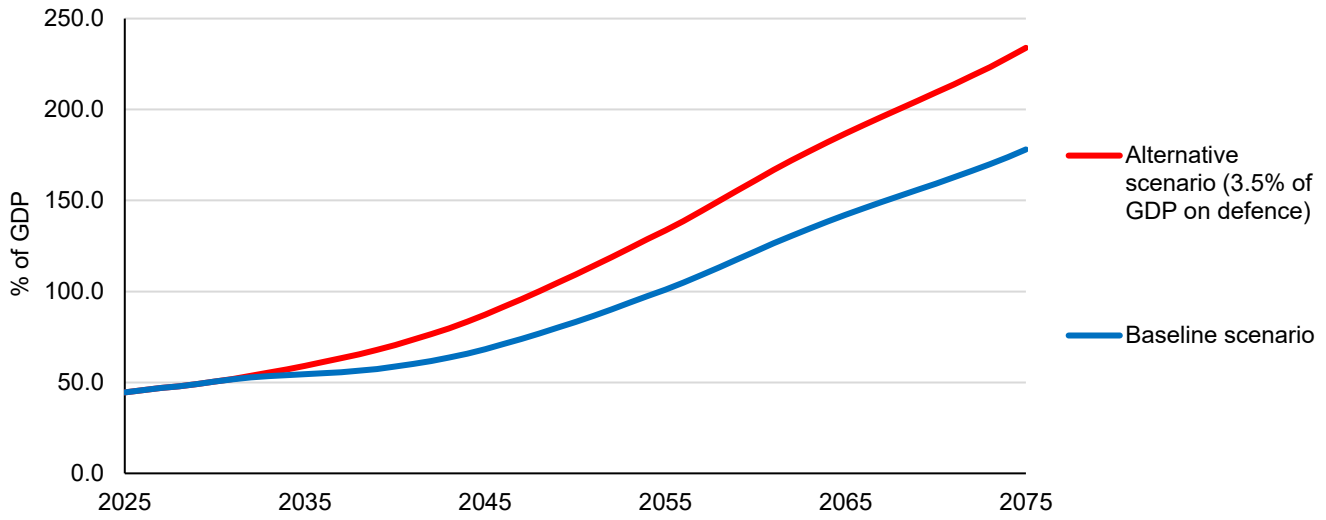


Source: CZSO (2025), European Commission (2025); CFC calculations.

In the alternative scenario, debt begins to grow significantly faster from 2031 onwards, and while in the baseline scenario the debt brake is projected to be breached in 2037, in the alternative scenario this occurs as early as 2033. The total debt of the general government sector is then 66% of GDP worse at the end of the projection and is heading towards 244% of GDP (see Chart 5.3.2). The projection thus shows that without significant measures on the expenditure or revenue side, the commitment made at The Hague summit cannot be met without a dramatic increase in debt. It should be added that this scenario is based on a defence spending commitment of only 3.5%, with the remaining 1.5% of GDP assumed to be covered by current public expenditure.

[91] For a description and explanation of the assumption of defence expenditure development in the baseline scenario, see subchapter 3.5.
[92] See https://www.nato.int/cps/en/natohq/official_texts_236705.htm.

Chart 5.3.2 General government debt in the baseline and alternative scenario with higher defence expenditure



Source: CFC calculations.

5.4 The borrowing requirements of the general government sector according to the state budget balance

In our debt projection, the general government annual borrowing requirement is based on the total deficit of the general government sector[93]. In the case of the Czech Republic, however, due to the systemic surpluses of local government subsector (i.e. regions and municipalities), this assumption leads to an underestimation of borrowing requirements and thus also to an underestimation of debt growth in our projection. This is because the overall balance of the general government sector is consistently significantly better than the balance of the central government subsector, which is predominantly influenced by the state budget, see also subchapter 1.1 and Chart 1.1.2. A more accurate debt projection for the Czech Republic would not be based on the projection of the balances of the entire general government sector, but on the projection of the deficits of central government institutions (which are significantly influenced by the aforementioned state budget deficits), which in the case of the Czech Republic are systematically worse than the balance of the entire sector. This is precisely the result of structural and permanent surpluses in the local government subsector (regions and municipalities) resulting from the budgetary allocation of taxes.

In this alternative scenario, we therefore assume that the government's borrowing requirement will be 0.7% of GDP higher each year than our projected balance for the general government sector in 2025–2075. The figure of 0.7% of GDP represents the 10-year average of local government subsector surpluses (see Table 5.4.1).

We therefore implicitly assume structural surpluses for municipalities and regions at this level throughout the projection. Debt dynamics are less favourable in this scenario. The debt brake threshold would be breached in 2031, i.e. six years earlier than in the baseline scenario. At the end of the projection, general government debt is 29% of GDP higher, rising from 178% of GDP to 207% of GDP (see Chart 5.4.1).

This scenario highlights the fact that, unless the budgetary allocation of taxes is adjusted, general government debt will tend to grow faster than the overall general government deficits.

An alternative option for reducing borrowing requirements arising predominantly from state budget deficits (i.e., the balance of central government) would be to place local government surpluses to a greater extent in their accounts held in the CNB (the state treasury system). The MF CR can cover borrowing requirements by using the balances of other government sector entities that hold their funds in accounts in the central bank.

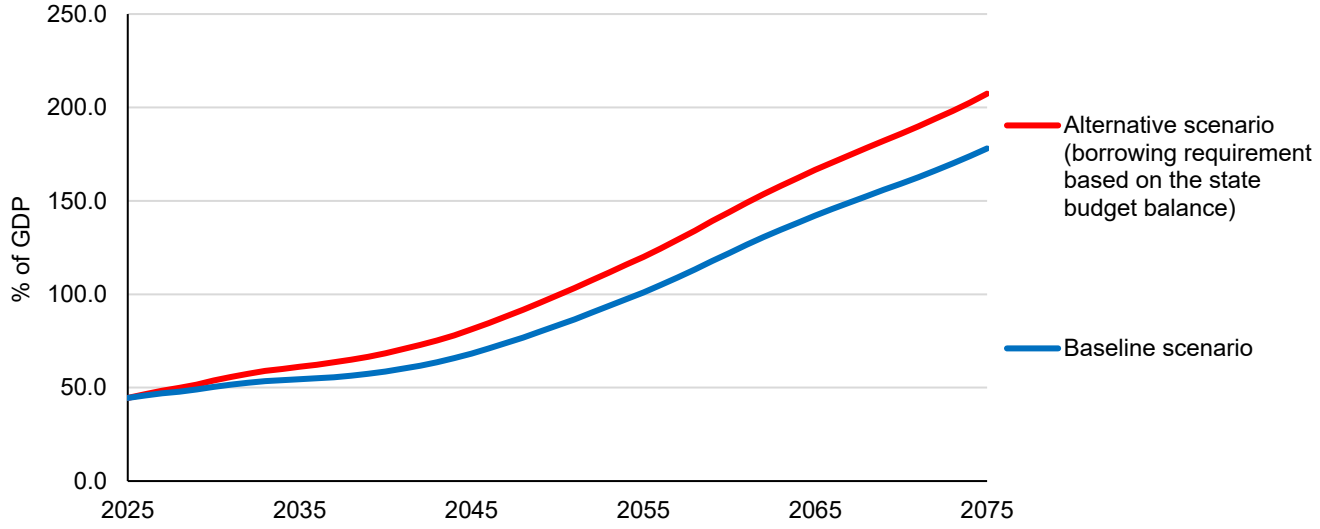
[93] The balance of the general government sector consists of three subsectors (and their sub-balances): central government, local government (i.e. regions and municipalities) and social security funds. The balance of social security funds has the least impact on the overall balance of the sector, which is why we do not explicitly mention this subsector in the text to maintain the clarity of the alternative scenario.

Table 5.4.1 Balance of the central government and local government subsectors (% of GDP, 2015–2024)

	Central government	Local government	General government
2015	-1.3	0.6	-0.7
2016	-0.4	1.0	0.7
2017	0.5	0.8	1.5
2018	0.1	0.4	0.9
2019	-0.5	0.6	0.3
2020	-5.9	0.5	-5.6
2021	-5.7	0.9	-5.0
2022	-4.0	0.9	-3.1
2023	-4.5	0.8	-3.7
2024	-2.6	0.7	-2.2

Source: CZSO (2025); CFC calculations.
Note: Data for 2024 are based on the first notification from the CZSO approved by Eurostat (April 2025).

Chart 5.4.1 General government debt in the baseline and alternative scenario with the government borrowing requirement according to the state budget balance (% of GDP)



Source: CFC calculations.

5.5 Construction of nuclear power plant in Dukovany

In this alternative scenario, we attempt to analyse the impact of the method of financing the construction of new nuclear power plants in Dukovany on general government debt. Our initial assumption is the construction of two units worth CZK 400 billion (4.4% of GDP at 2024 prices).[94] In our simulation, we assume that the state will begin to raise funds in line with current market conditions from 2026 onwards. These funds will be lent to Elektrárna Dukovany II, a. s. (“EDU II, a. s.”) during the construction period (2026–2036). In our projection, we assume a linear increase in the state's borrowing requirement of 0.4% of GDP per annum over these eleven years compared to the baseline scenario.[95]

As can be seen in Chart 5.5.1, the general government debt will thus increase by 4.4% of GDP by 2036 compared to the baseline scenario. This is because we do not take into account the impact of

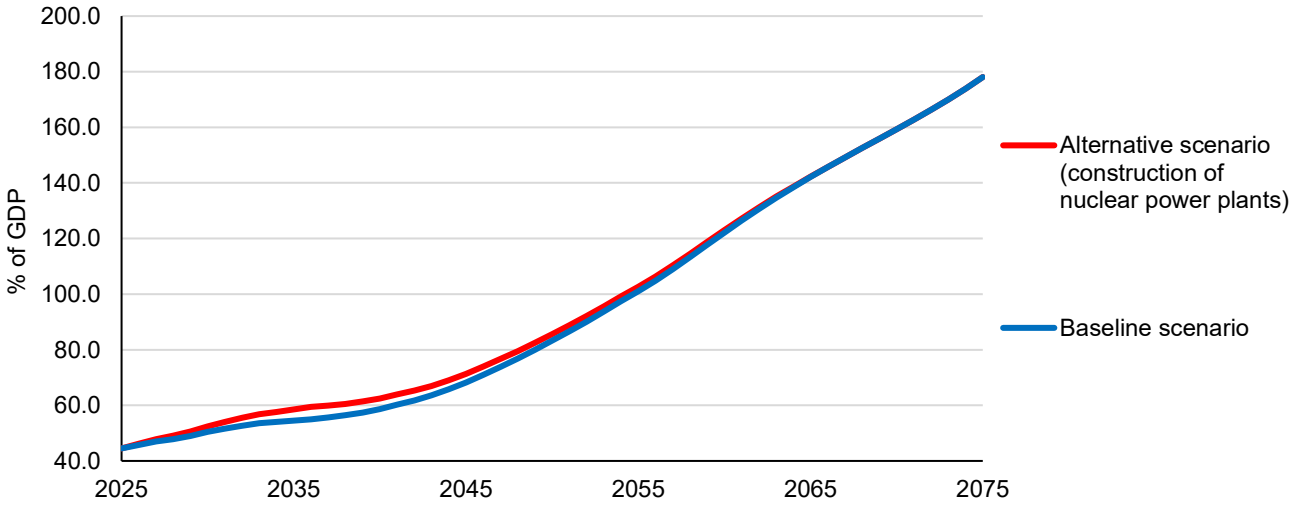
[94] See also: https://www.mfcr.cz/cs/ministerstvo/media/tiskove-zpravy/2025/stat-kupuje-80-podil-ve-spolecnosti-elektrarna-duk-59336 (available in Czech only), https://ec.europa.eu/commission/presscorner/detail/en/ip_24_2366. Details of the contracts are available at: https://smlouvy.gov.cz/ (available in Czech only).
[95] However, it should be noted that the implementation of such a large-scale project is associated with a number of risks. The presented scenario assumes that construction will be completed on schedule and that the price of electricity produced will enable EDU II, a.s. to repay the repayable financial assistance.

construction on GDP growth (through the involvement of Czech companies and the multiplier effect).

Between 2037 and 2066, EDU II, a. s. will subsequently repay the principal and interest to the state. In our simulation, we assume that the state will use these principal repayments to repay the principal of its debt. However, this will essentially be a "standard" state budget revenue, which can be used for purposes other than repaying the principal of the debt. We do not include interest payments on this additional debt in our projection. These would slightly increase total state budget expenditure (and increase the debt ratio) until 2036, and after 2037 they would constitute state budget revenue (reducing the debt ratio).

The result of the alternative scenario is that financing the construction of nuclear power plants in the chosen and notified manner will increase the debt ratio in the short term by the amount of funds that the state will have to borrow (by 4.4% of GDP), but this increase can be eliminated after the loan is repaid.

Chart 5.5.1 General government debt in the baseline and alternative scenarios with the construction of nuclear power plants



Source: CFC calculations.

5.6 Generational accounts in the pension system

5.6.1 Generation-specific revenue and expenditure

In this subchapter, we examine generation-specific expenditure and revenue in individual years. These show how the fiscal burden is distributed across generations.[96] The largest generation-specific item is the revenue and expenditure of the pension system, which we analyse in more detail in the following subchapter. However, population ageing and the entry of baby-bust cohorts into the labour market affect not only the pension system itself, but also healthcare expenditure and generation-specific social benefits. We consider around 44.2% and 44.1% of total government revenue and expenditure in 2024, respectively, to be generation-specific.

Chart 5.6.1 depicts the age profile of revenue and expenditure per person of a given age. It is clear that children in the first three years of life are net recipients, mainly because of maternity and parental leave payments and increased healthcare costs. Education benefits follow from the age of two years up, dominating until around the age of 18. Child/student-linked personal income tax discounts, which are also considered to be a social benefit and which we assign to children, are also significant.

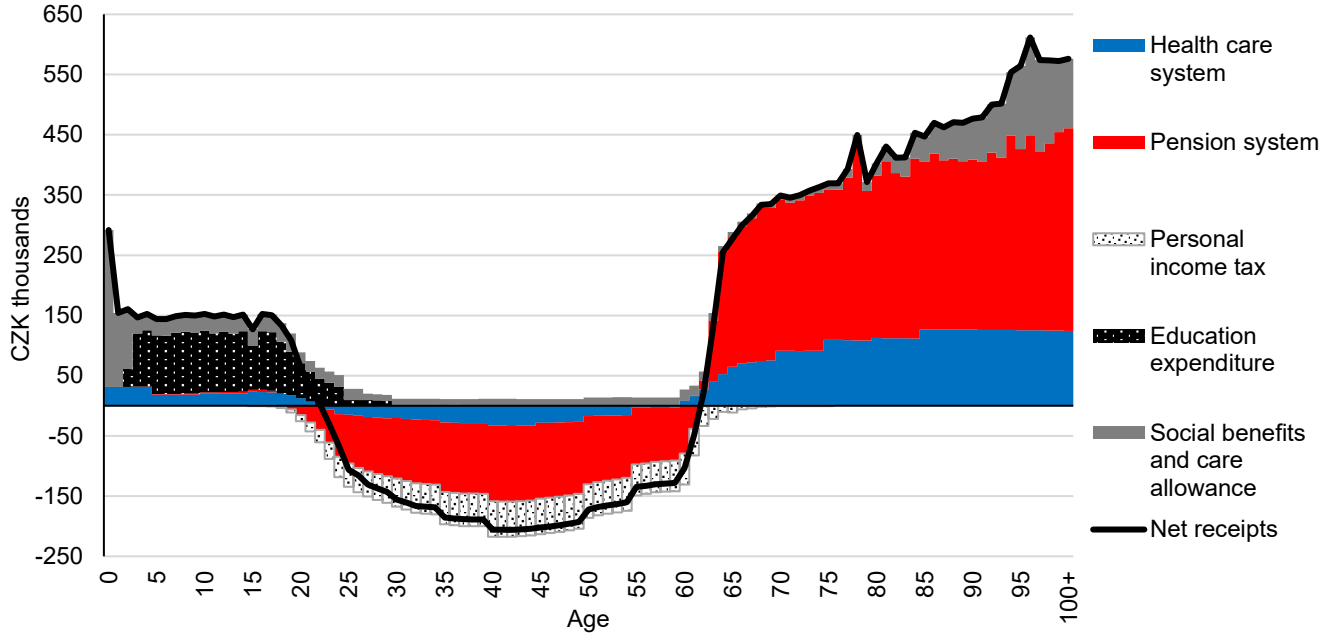
Conversely, people of working age are on average net contributors, as their contributions to the system in the form of income tax and health and social security contributions exceeded the benefits that these generations receive from the system. Post-working-age generations are again net beneficiaries, benefiting most from the pension and health care systems and from social benefits (care allowance). On average, a person between 23 and 61 years is therefore a net contributor to public budgets at present.

The generational accounts also reveal that the average individual born in 2000–2004 (i.e. the first generation for which we capture their entire life cycle in the projection) will receive CZK 8.5 million more from

[96] For a description of the generational accounting methodology, see the Office of the CFC (2021): Metodika mezigeneračních účtů [Generational Accounting Methodology, available in Czech only]. See also Box 6.1 in the 2021 Long-Term Sustainability Report.

public budgets over their lifetime than they will contribute to them. If policies remain unchanged, each member of the generation born fifty years later will receive CZK 7.7 million more than they contribute.[97]

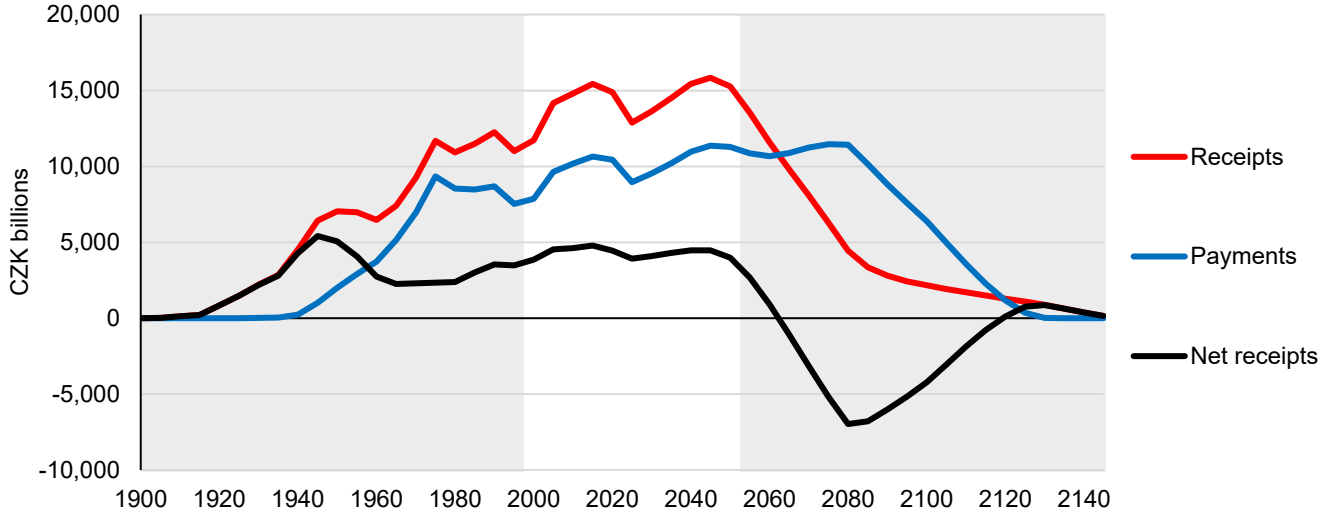
Chart 5.6.1 Payments and receipts per person of a given age in 2024



Source: CZSO (2025), CSSA (2025); CFC calculations.

As Chart 5.6.2 shows, generations born up to 2065 are net beneficiaries in the public finance system in our projection. Generations born later are still economically active in our defined period, but their entire retirement period is not captured. They are therefore net contributors overall. However, in the long term, beyond 2150, these generations will also become net beneficiaries under unchanged policies

Chart 5.6.2 Public budget payments and receipts of a given generation[98]



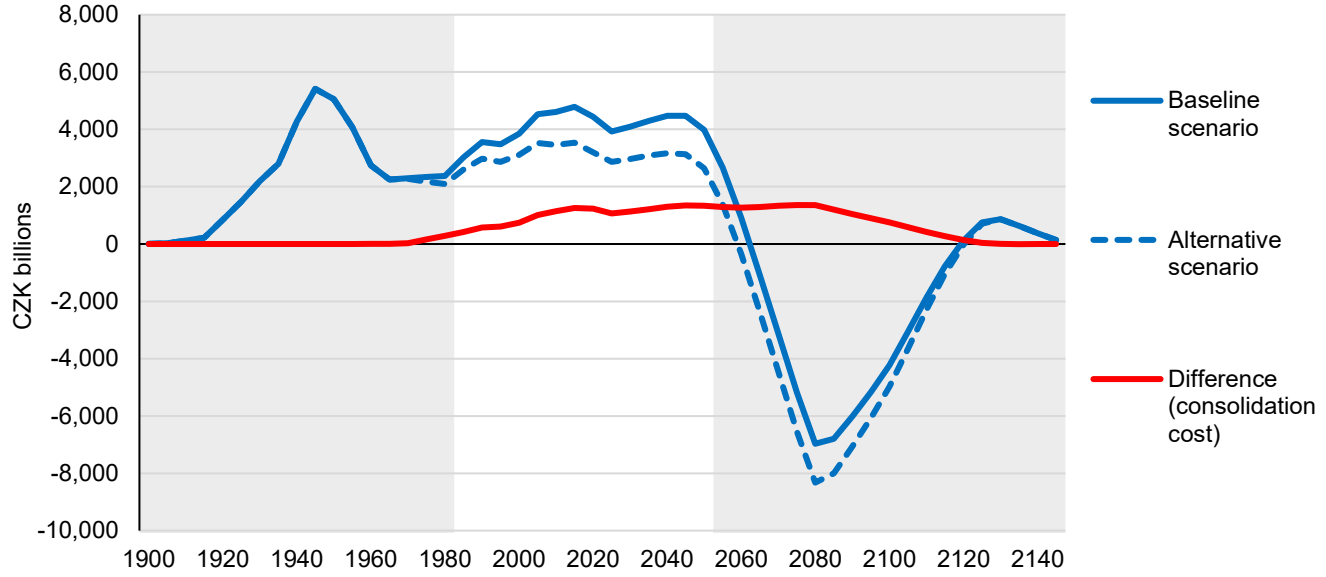
Source: CZSO (2025), CSSA (2025); CFC calculations.

[97] Revenues and expenditures are expressed in real terms at 2024 prices and are discounted by real interest rate of 1%. This roughly corresponds to the so-called natural interest rate estimated, for example, in Hlédik and Vlček (2018): Quantifying the Natural Rate of Interest in a Small Open Economy – The Czech Case, Working Papers 2018/7, Czech National Bank.

[98] The data in the graphs in subchapter 5.6.1 and 5.6.2 covering the period 1900–2150 (or 1950–2100) are in 2024 prices, discounted at a real interest rate of 1%. The x-axis shows individual generations according to five-year periods of their birth. Generations for which either their entire working career is not included or the entire period of their pension drawdown is not covered are highlighted in grey.

Chart 5.6.3 shows how the net receipts of each generation would change if we assume higher taxation at a rate at which the general goverment debt would stay at the debt brake level (55% of GDP) until 2075. We assume that the tax burden is increased from 2038, i.e. one year after the debt brake is reached. In this case, net receipts would rise for all generations from 1950, while the burden would increase for generations born after 1990. The overall increase in the tax burden would be around 12%. Comparing the baseline no-change scenario with the alternative sustainable finance scenario, it is clear that the future generations will bear the greatest burden (Chart 5.6.3).

Chart 5.6.3 Net receipts of each generation, baseline and alternative scenario[98]



Source: CZSO (2025), CSSA (2025); CFC calculations.

5.6.2 Generational accounts and the pension system

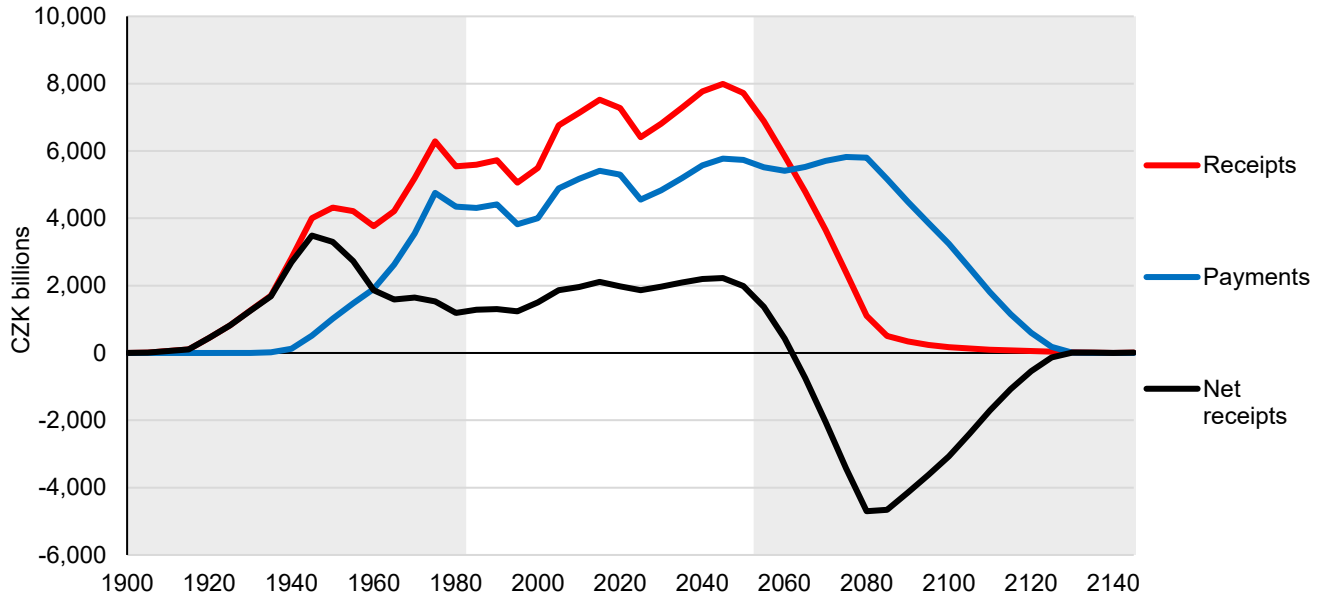
In the previous subchapter, generational accounts were compiled for the widest possible range of generation-specific household revenues and expenditures. To discuss the impacts of pension reform on various different generations, it is appropriate to examine specific pension system revenues and expenditures in the framework of these generational accounts.

The Czech pension system is largely based on intergenerational solidarity, with social security contributions paid by the economically active generation being used directly to pay existing pensions (pay-as-you-go pension system). In the generational accounts model, we therefore include the pension insurance contributions of the working population (i.e. the pension system revenue), which we then compare with the expenditure on pensions paid to the economically inactive population. In the projection of pension expenditure of individual generations, we use the expenditure calculation method presented in subchapter 3.1 of this Long-Term Sustainability Report.[99] We consider expenditure on old-age, disability, widows', widowers' and orphans' pensions. For the projection of pension system revenue decomposed into generations, we begin with the method used to calculate such revenue for the pension system as a whole (see subchapter 3.6 of this Long-Term Sustainability Report). We then divide these contributions to the pension system by generation on the basis of the volume of wages paid. We leave the ratio of the wage of a generation of a particular age to the average wage in the economy, as well as the participation rates and cyclically adjusted unemployment rates of each cohort, constant over time. In the baseline scenario, we assume the same pension system parameters as in our projections described in subchapter 3.1. Here, we calculate how much each generation will pay into the pension system in total in the period 2000–2150 and how much they will receive in old-age, disability and other pensions (see Chart 5.6.4).[100] The net amount received (pensions paid out minus social security contributions paid in) for each generation is thus determined by the pension per pensioner, but also reflects the

[99] See also the Office of the CFC (2019): Projekce důchodového systému [Pension System Projection, available in Czech only] and the Office of the CFC (2022): Odhad náhradového poměru dávek důchodového pojištění [An Estimate of the Replacement Rate of Pensions, available in Czech only].
[100] Revenue and expenditure are expressed in real terms (2024 prices; indexed by the GDP deflator) and are discounted by a real interest rate of 1%.

generation's relative size, its life expectancy and retirement age. In the period 2000–2150, the current older generations no longer contribute to the system and merely draw pensions (left-hand grey part of Chart 5.6.4). Conversely, the youngest generations, who are yet to be born and do not reach retirement age in our projection horizon, merely contribute to the system (except for disability and orphans' pensions), see the right-hand grey side of Chart 5.6.4.

Chart 5.6.4 Pension system payments and receipts of individual generations[98]



Source: CZSO (2025), CSSA (2025); CFC calculations.

The generations whose entire working and retirement cycles we cover start with the one born in 1980 and end with the one born in 2050. All these generations receive more from the pension system than they pay into it. Relatively younger generations will receive more, owing mainly to a combination of higher life expectancy and capping of the retirement age at 67 years. The calculation presented in Chart 5.6.4 already takes into account the application of the pension reform, which is why the net receipts for most generations are lower than we assumed last year (see also Chart B3.1.2 from Box 3.1 illustrating the impact of different parts of the pension reform on different generations). Even after the implementation of this reform, however, the pension system's settings will generate deficits in the long term, which will contribute to an escalation of the general government debt, as described in chapter 4. If these deficits are to be eliminated in the future and further changes are to be made to the pension system, the question arises as to which generations will bear the brunt of this reform.

We therefore prepared a set of simple possible alternatives, which we construct in such a way that the accumulated pension system balance is zero in 2075. There are several ways of achieving this. One can change the revenue side of the pension system (raise the social security contribution rate) or change the expenditure side (reduce the replacement rate and hence reduce pensions), or do a combination of both. Another option is to further raise the retirement age above 67, which has a similar impact as reducing the replacement rate. Below, we consider two options separately: firstly, a situation where only the social security contribution rate rises and pensions stay the same relative to the average wage as in the baseline scenario (see Chart 5.6.5); secondly, the situation where, on the contrary, the contribution rate stays unchanged and pensions fall relative to wages, i.e. the replacement rate decreases (see Chart 5.6.6).

In both variants, we consider various alternative changes. In alternative 1, we assume that the pension system is balanced every year. For each year, we therefore calculate the insurance contribution rate (or replacement rate) that balances the pension system's revenue and expenditure. In this alternative, the central authorities opportunistically use temporary surpluses in the pension account, so that pension insurance rates fall from the current 28% to 25.9% of income in 2032. However, due to the increase in the number of pensioners, they will subsequently rise to 32.5% in 2061. This means that in 2061, the economically active generation would face a pension burden that is 4.5 pp higher than that of the currently working generation, which would already be receiving pensions.

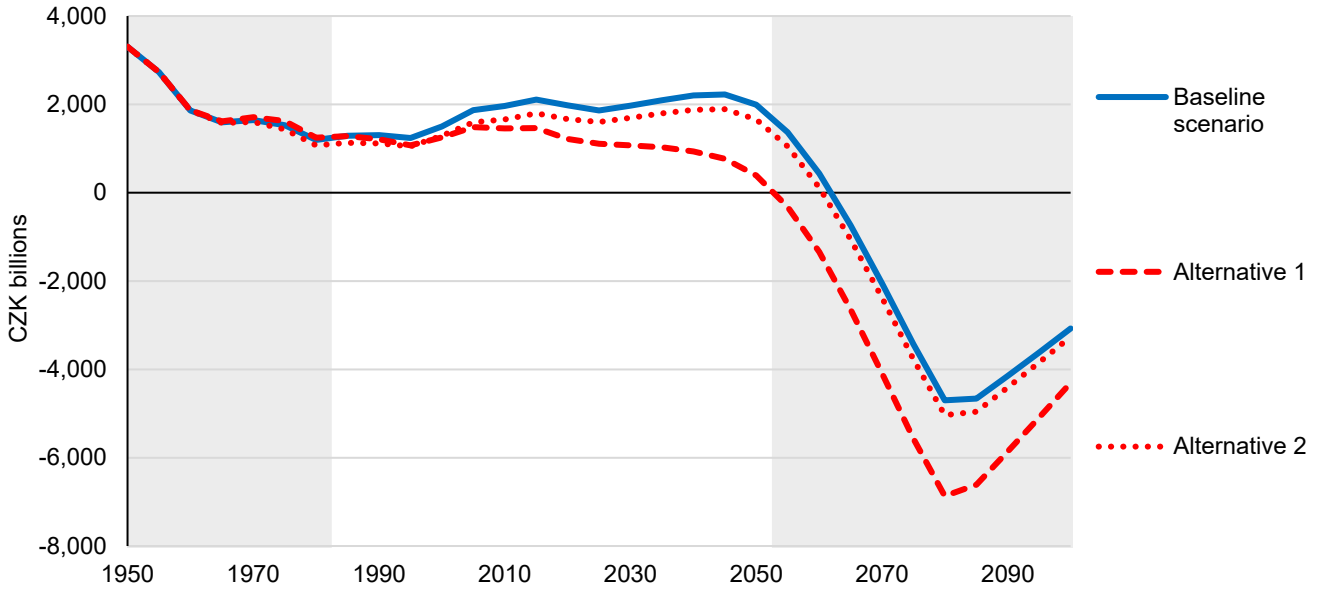
Conversely, maintaining the current pension insurance rate would mean that pensions would have to

be reduced from the current level of around 45.1% of the average wage to 36.9% in 2062. In this case, the burden of debt sustainability would be borne by the current economically active generation, which would receive relatively lower pensions than current pensioners.

In other alternatives, we raise the pension insurance rate or lower the replacement rate so that the pension system is cumulatively in equilibrium by 2075.[101] The impact on each generation depends on the point in time at which the pension rate increases or the replacement rate decreases. In alternative 2, we consider an increase in the rate starting in 2038, i.e. one year after the debt brake threshold is reached. Needless to say, the greater the delay in raising the insurance rate, the bigger the response required. In alternative 2, the insurance rate increases from the current 28% of income to 30%.

Chart 5.6.5 shows that an increase in pension insurance rate would mainly burden younger generations, especially those born recently and future generations. Earlier rates increases are slightly more equitable across generations than the other alternatives as they spread the costs of stabilising the pension system across more generations.

Chart 5.6.5 Rising insurance rate scenario (net balances)[98]



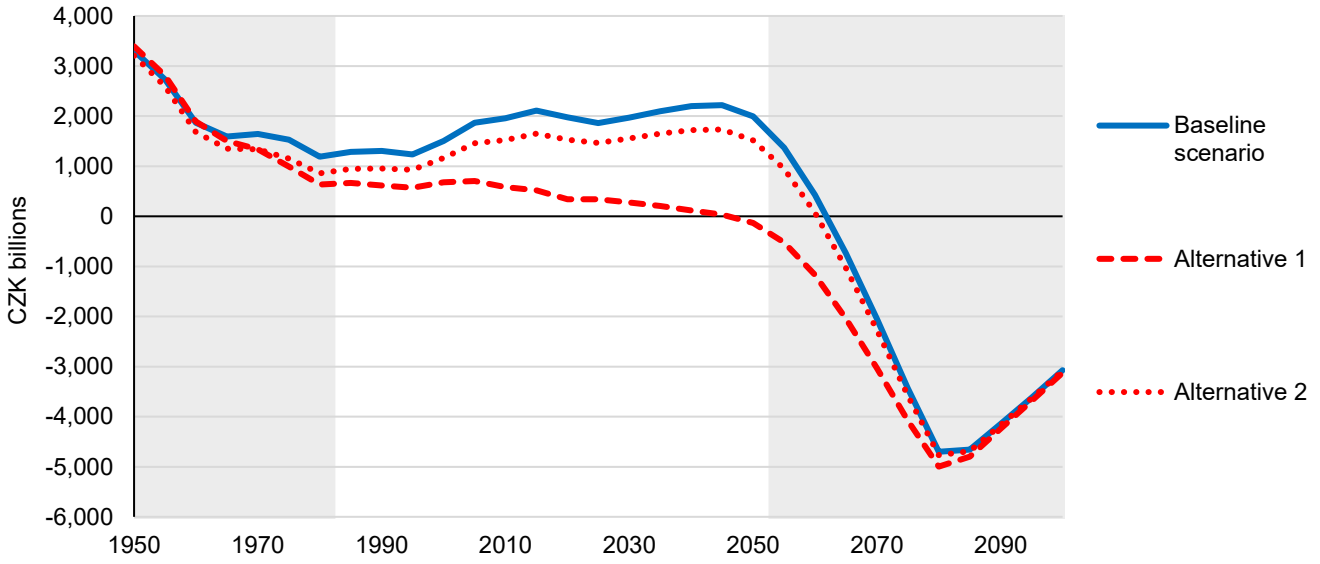
Source: CZSO (2025), CSSA (2025); CFC calculations.
Note: In each alternative, the pension insurance rate is increased in such a way that the pension system is balanced in 2075. In alternative 1, this is achieved by balancing the pension system every year; in alternative 2 we consider an increase in the rate starting in 2038 (i.e. the year after the debt brake threshold is reached).

If we assume that the pension insurance rate will remain at the current level of 28% in the future and that the retirement age does not change either, it will be necessary to lower the replacement rate to achieve a balanced pension system. Chart 5.6.6 shows that both the older generation (starting with those born in the 1960s) and younger ones will be worse off in the event of a reduction in pensions, so the effects of consolidating the pension system will be distributed more evenly across the generations by comparison with an increase in the pension contribution rate at the same point in time. Again, if the reduction in pensions takes place earlier, the burden will be shared more evenly across the generations. Conversely, if the reduction in pensions is delayed, the impact on older cohorts will be smaller at the expense of the younger generations.

Our projection of changes to the pension system is simplified in many respects, but it is clear that postponing parametric changes to the pension system will asymmetrically burden the younger generations born after the turn of the millennium. At the same time, it is evident that adjustments to the pension system settings that focus on the expenditure side produce a more even distribution of the impact across generations than adjustments to the revenue side and can be perceived as "fairer".

[101] These alternatives are therefore designed in such a way that the net present value of pension income over the period 2021–2075 is equal to the net present value of pension expenditure over the same period. Unlike alternative 1, where the pension system is stable over the entire 2025–2150 horizon, in alternative 2 the pension system may not necessarily be stable after 2075.

Chart 5.6.6 Falling replacement rate scenario (net balances)[98]



Source: CZSO (2025), CSSA (2025); CFC calculations.
Note: In each alternative, the replacement rate is reduced in such a way that the pension system is balanced in 2075. In alternative 1, this is achieved by balancing the pension system each year; while in alternative 2 the reduction in the replacement rate starts in 2038 (i.e. the year after the debt brake threshold is reached).

5.7 Comparison with the previous Long-Term Sustainability Report

Compared with the Long-Term Sustainability Report published in 2024, the current edition is relatively more optimistic in terms of the assessment of the sustainability of public finances. Debt at the end of the projection is reduced from 217% of GDP to 178% of GDP in the baseline scenario. The main reason for this improvement is the impact of the pension reform, which was only included in alternative scenarios in last year's Long-Term Sustainability Report.

On the other hand, however, the impact on the debt brake has been brought forward (to 2037 instead of 2038). The reason for this is that while parametric adjustments to the pension system affect primary balances and debt dynamics mainly in the long term, increased defence spending above 2% of GDP between 2026 and 2033 will worsen primary balances and debt dynamics in the coming years. Bringing forward the debt brake to 2037 is therefore a logical consequence of higher borrowing requirements over the next ten years in the absence of adequate adjustments to the expenditure or revenue side.

The debt projection was also affected by the extensive revision of national accounts across EU countries in 2024. This revision meant an upward reassessment of historical GDP in the Czech Republic (by up to 3.9%) and affected the initial assumptions about the speed of economic convergence. The projection of future GDP has shifted upwards, reducing the projected share of general government expenditure in GDP. Compared with last year's projection, total GDP at the end of the projection horizon (in 2075) will be approximately 5% higher than last year.

The projections for expenditure and GDP were also influenced by the fulfilment of the assumptions of the CZSO's demographic projection from 2023. Compared to this projection, population growth in recent years has been hampered mainly by lower birth rates, with the number of births in the Czech lands in 2024 being the lowest in recorded history (i.e. since 1785). On the other hand, net migration has had a positive effect on population growth, with the assumption of an incipient outflow of refugees not materialising in 2024 and positive net migration outweighing the negative natural population growth. Given that net migration is mostly directed towards the working population, while the reduced fertility rate reduces the working population with a delay of at least 20 years, these changes will lead to higher GDP overall in the medium term.

On the expenditure side of the general government sector, lower spending on education and other cash social benefits (mainly parental allowance and tax credit for children) contributed to a slower increase in debt compared to the 2024 Long-Term Sustainability Report. The decline in the projection for these expenditures was mainly due to lower fertility rates (fewer births). Conversely, healthcare expenditure is higher in relation to GDP than in last year's projection. Between 2026 and 2033, our projection for defence expenditure is rising, increasing by up to

1% of GDP compared to last year's projection of 2% of GDP.

Pension expenditure is also lower than we anticipated last year across the entire projection horizon. This reflects, among other things, the approval of a further part of the pension reform, which has a significantly positive impact on improving the balance. In the longer term, pension expenditure, like healthcare expenditure, is mainly influenced by demographic developments. The higher projected number of pensioners in the longer term of the projection reflects a reduction in the expected mortality rate and an increase in life expectancy. In the shorter term, on the other hand, higher net migration has a positive effect, improving the ratio of the working-age population to the population aged 65 and over. At the end of the projection horizon, however, this ratio deteriorates due to lower fertility.

As already mentioned, the primary deficit projection suggests that the debt brake will be breached in 2037, one year earlier than assumed in the previous edition of the Long-Term Sustainability Report. Given the evolution of projected primary structural deficits, interest costs and debt, the so-called sustainability gap in public finances has narrowed from last year’s 3.78% of GDP to 2.88% this year. The sustainability gap shows how much better the primary structural balance would have to be each year from 2025 to 2075 in order for debt not to exceed the debt brake threshold in 2075.

Conclusion

The current Long-Term Sustainability Report shows a significant improvement in the long-term sustainability of Czech public finances compared to last year´s projection. Projected public debt falls from last year's 217% of GDP to 178% of GDP at the end of the projection. This is mainly due to the approved parametric adjustments within the first pillar of the pension system. These adjustments include a change in the pension indexation mechanism in 2023 (indexation by one-third of real wage growth instead of the previous half) and a restriction on early retirement. In 2024, this was followed by an adjustment of the retirement age after 2030 above the current maximum level of 65 years of age and a gradual reduction in the replacement rate for newly granted pensions. In the following years, the pension system should be in surplus, and in the worst demographic years (around 2060), its annual balance should improve by 2.5 pp (from −4.0% of GDP to −1.5% of GDP) compared to the situation before the above-mentioned adjustments adopted in 2023 and 2024.

Our projection, including the outlook for the pension system, is affected by demographic and macroeconomic projections. In 2024, the assumption of an incipient outflow of Ukrainian refugees did not materialise to any significant extent, and positive net migration outweighed negative natural population growth. Overall, between 2022 and 2024, the population of the Czech Republic grew by 0.76%, the highest rate since the end of World War II. Compared to the previous Long-Term Sustainability Report, the macroeconomic projection is also influenced by the revision of the national accounts by European statistical offices in June 2024. This revision meant a reassessment of historical GDP in the Czech Republic and affected the initial assumptions about the speed of our economic convergence.

However, the projected moment of breaching the so-called debt brake has moved closer by one year (to 2037), which is a consequence of increased defence spending, which in the baseline scenario of our projection will grow to 3% of GDP by 2030. This shows that while parametric adjustments to the pension system have a dominant impact on debt dynamics in the long term, increasing defence spending between 2026 and 2033 has an impact in the short and medium term. Breaching the debt brake already in 2037 is therefore a logical consequence of higher borrowing requirements over the next ten years in the absence of adequate adjustments on the expenditure or revenue side.

The CFC appreciates the shift towards improving the long-term sustainability of public finances but draws attention to the risks in the medium term arising from the situation where the structural balance has not yet returned to a sustainable level while witnessing efforts to pursue several fiscally very demanding priorities simultaneously without adequate adjustments on the revenue side.

Appendices

Table D.1 Summary of general government revenue and expenditure in selected years (% of GDP) – medium variant of demographic projection

	2025	2035	2045	2055	2065	2075
REVENUE						
Personal income tax	4.0	4.1	4.2	4.3	4.3	4.3
Corporate income tax	3.9	3.6	3.4	3.2	3.0	2.9
Other current taxes	0.2	0.2	0.2	0.2	0.2	0.2
Social security contributions	16.3	16.4	16.6	16.8	16.9	16.9
pension insurance	*8.6*	*8.8*	*9.0*	*9.1*	*9.2*	*9.3*
public health insurance (excluding state insurees)	*4.4*	*4.5*	*4.6*	*4.7*	*4.7*	*4.8*
payment for state insurees	*1.9*	*1.6*	*1.5*	*1.5*	*1.4*	*1.3*
other	*1.4*	*1.4*	*1.5*	*1.5*	*1.5*	*1.5*
Taxes on production and imports	11.0	11	11	11	11.0	11.0
Property income	0.6	0.6	0.6	0.6	0.6	0.6
Other revenue	4.8	4.8	4.8	4.8	4.8	4.8
TOTAL REVENUE	40.8	40.7	40.8	40.9	40.8	40.8
EXPENDITURE						
Pensions	8.7	8.2	9.4	10.3	10.5	10.4
Health care (public health insurance system only)	6.4	6.8	7.1	7.4	7.6	7.7
Other social benefits in cash	2.8	3.0	3.2	3.4	3.6	3.7
Payments for state insurees	1.9	1.6	1.5	1.5	1.4	1.3
Long-term care outside the public health insurance system	0.6	0.7	0.8	0.9	1.1	1.1
Education	4.7	4.4	4.3	4.6	4.5	4.4
Other expenditure – baseline scenario	17.0	17	17	17	17	17.0
Changes related to convergence	0.0	0.1	0.1	0.1	0.2	0.2
public investment	*0.0*	*-0.1*	*-0.2*	*-0.2*	*-0.3*	*-0.3*
defence expenditure	*0*	*0*	*0*	*0*	*0*	*0.0*
growth in general government costs (wage)	*0.0*	*0.1*	*0.2*	*0.3*	*0.3*	*0.4*
growth in payments to EU	*0.0*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*
Total expenditure excluding interest	42.1	41.8	43.5	45.2	45.9	45.7
Primary structural balance	-1.3	-1.1	-2.8	-4.4	-5.1	-4.9
Interest (no interest rate feedback)	1.4	1.5	1.8	2.6	3.7	4.6
TOTAL EXPENDITURE (no interest rate feedback)	43.4	43.3	45.3	47.8	49.6	50.3
TOTAL BALANCE (no interest rate feedback)	-2.7	-2.6	-4.5	-7.0	-8.8	-9.6
DEBT (no interest rate feedback)	44.5	54.5	68.2	101.0	142.1	178.1

Source: CFC calculations.
Note: The totals in the table may be subject to inaccuracies due to rounding.