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Fiscal Policy Commission

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**11th Position paper of the Fiscal Policy Commission on the State Budget
Amendments for the Republic of Croatia year 2016 and
projections for 2017 and 2018**

At its 16th meeting held on 22nd November 2016, the Fiscal Policy Commission reconsidered the Amendments of the State Budget of the Republic of Croatia and projections for 2017 and 2018 submitted by the Croatian Government to the Speaker of the Croatian Parliament by the Act on 21st November 2016.

Proposed amendments to the Budget are submitted primarily due to organizational changes within the ministries, having established the new 14th Government of the Republic of Croatia. In addition to the technical changes favourable fiscal situation has been established enabling, in the year 2016, significant reduction in the budget deficit of general Government in relation to the originally planned (from -2.7% to -1.7 GDP, that is one percentage point). Namely, due to the favourable macroeconomic indicators in 2016 Ministry of Finance expects an increase in budget revenues by about 1.5 billion kuna, primarily due to growth in revenues from income taxes (1.2 one billion kuna), special taxes and levies (for about 0.7 billion kuna) and property income (0.6 billion kuna). Besides, according to the proposed Amendments the largest deficit reduction is recorded in the state budget (from -2.2% to -1.6% of GDP) and in the local and regional self-governments (from -0.1% to 0.2% GDP).

Unlike the previous amendments to the Budget, this time there are no plans to increase expenditure affecting the deficit, but it is suggested to reduce expenditures that are financed from their own resources or specific revenues or donations by 0.7 billion kuna. The largest amount has been saved on interest expenses due to reduced debt intensity and lower borrowing costs especially in the domestic market. Reducing expenditures from sources financed from the EU budget indicates weakness within the system. Therefore, the Commission

reiterates the necessary need to strengthen the system within the state administration with the task to withdraw EU funds for projects in Croatia, particularly with regard to education at all levels (from ministries to municipalities), and the implementation of staff retention policy within the system.

The decision of the Croatian Government to direct the total amount of increased revenues into reduction of the budget deficit, the Commission considers positive and in line with its previous recommendations. Such a decision, according to the Ministry of Finance assessment, will result, as already mentioned earlier, in reducing general Government budget deficit from the planned -2.7% of GDP to -1.7% of GDP. It is expected for the nominal deficit to be reduced by 3.5 billion kuna, or slightly more than 1% of the GDP. In order to increase the sustainability of public finances, Fiscal Policy Commission suggests the drafting of the budget for 2017 to be based on the lower deficit than estimated for 2016 in order to achieve faster reduction of public debt to GDP. The Commission believes that such a direction will increase the possibility for Croatia to abrogate the excessive deficit procedure (EDP) in 2017. In addition, the Commission reiterates the need for stronger fiscal consolidation on the expenditure side of the budget.