



Thematic  
analysis/diagnosis:  
**Public finances &  
fiscal policy**

## Executive Summary

**Significance of fiscal policy.** Prudent management of public finances ensures macro-financial sustainability, smooth performance of vital functions of the state, as well as efficient and successful implementation of strategic government priorities. By improving the quality and expanding the range of public services, successfully implementing properly selected investment projects, while simultaneously preserving the fiscal sustainability, the long-term development priorities can be realized. In that context, only the national development strategy, for whose implementation satisfactory (almost never, sufficient) budget funds have been allocated and appropriate tax reforms have been made, can enable inclusive and sustainable prosperity and raise the quality of life of the citizens.

**Obstacle or accelerator?** Fiscal policy can be an obstacle, but it can be also an accelerator of medium-term and long-term growth. If public debt exceeds 70% of GDP, which is currently considered a high-risk scenario, fiscal policy could become an obstacle for medium-term and long-term economic growth. That is why a cost-and-benefit analysis of new borrowing should be made. The purpose of the new borrowings is especially important, meaning it should be aimed at financing investment projects in priority areas: digitalization, green transition, strengthening of human capital, social cohesion, etc.

**Boosting the budget revenues.** The fiscal obligations are at a low level, one of the lowest in Europe, which leaves little fiscal space to finance public needs and deal with future crises. Almost without exception, all relevant international financial institutions recommend the elimination or drastic reduction of tax incentives and exemptions, as well as a gradual change in the structure of tax revenues in order to increase the share of direct taxes. The fiscal space is narrowed due to insufficient collection of projected revenues and insufficiently efficient tax administration.

**Unfavorable structure of budget expenditures.** The costs of salaries and remunerations are characterized by a low average salary, high wage compression between individual levels, and unevenly distributed number of public sector employees. Rationalization of budget expenditures is an important priority in the next 20 years. Under Wagner's law of continuous expansion of budget expenditures, budget users, public enterprises and institutions at the national and local levels find it difficult to relinquish acquired spending rights. Excessive institutionalization is a process of particular concern. Creation of institutions with partially or significantly overlapping competencies, justified under the guise of the need for European integration and harmonization with European legislation, distracts extensive budgetary resources from important long-term development priorities.

**Need for greater fiscal space.** In this sense, rationalization and rethinking of the public sector (through integration of institutions or agencies) would free up significant fiscal space to support long-term economic development. Furthermore, it would increase the level of discretionary budget expenditures for conducting more efficient fiscal policy in the short, medium and long term.

**The main challenge of the fiscal policy** in the context of NDS arises from a fundamental discrepancy. On one side, there are the low budget revenues, the result of the neoliberal tax system and tax evasion, itself the very fruit of shattered tax morality and insufficient capacity of the tax administration. On the other side, there are the inefficient and more extensive budget expenditures, in which government investments have a low share and they are underutilized, while corruption in public procurement and employment via political parties seriously erode the vital functions of the state. The hope of many previous governments has been that borrowed funds and inflows from occasional privatizations would have a positive multiplier effect on the economy, with accelerated growth reducing this fundamental discrepancy.

**Citizens' vision for personal income taxation.** The citizens who took part in the debates in the field of public finance and fiscal policy failed to reach a consensus on the issue of tax policy towards personal income in terms of maintaining a flat tax or transition to progressive taxation. However, the need was emphasized for fairer taxation that promotes social equality, i.e. the need for reducing the tax burden for poorer citizens. It is especially important that the participating citizens called for increased awareness of paying taxes (and significantly strengthened *tax morale*) as the basis for providing good public services, sanctioning tax evasion and the informal economy.

**Citizens' vision for the public debt.** Most participants believe that more prudent management of public debt and its reduction in the medium and long term is needed. The issue of debt is perceived as intergenerational solidarity, where future generations are unjustifiably burdened with debts incurred by current generations. Perhaps, as expected, there is no consensus on the need to introduce a progressive tax. If, however, there is a need for additional revenues in the budget, it is recommended that the threshold be set higher, i.e. to affect only high-income citizens. The participants largely believe that there is room for rationalization of budget expenditures, i.e. to be diligent in regard to the purposes for which public funds are being spent.

**Fiscal transparency.** Overall, fiscal transparency has improved significantly in recent years. Nevertheless, some analyzes in the context of the NDS would find there is lack of relevant data. Fiscal data are not yet fully in line with the international methodology (IMF Government Finance Statistics), and the definition of public debt is not yet fully in line with the methodology of the European statistical service Eurostat, which is used by the European Commission and The EU Delegation.

**Evidence-based policies.** Although seemingly drawing great budget resources in the short term, evidence-based economic policies and scientific/expert analysis of the costs and benefits of implementing many decisions and investment projects in the public sector are needed. Ultimately, the savings from well-established evidence-based policies are manifold in the long run. Such policies should also apply to the built-in ongoing programs that have been running through the budget for years, without a clear picture of their long-term effects on the economy.