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PRESS RELEASE

The meaning and purpose of macroeconomic and fiscal policy guidelines in Croatia

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This article aims to clarify the meaning and purpose of macroeconomic and fiscal policy guidelines, which are the basis for drawing up and adopting a national budget, to outline the generally accepted good practice standards and to briefly comment on the "Proposal of Measures and Guidelines for Drawing up a 2012 Croatian Budget".

The Croatian Government has published its Proposal of Measures and Guidelines for Drawing up a 2012 Croatian Budget[1], pursuant to which the Ministry of Finance will deliver instructions to other ministries and state bodies of the first level of the organisational classification (e.g. Parliament, Office of the President, Constitutional Court and government agencies and bureaus), as well as to extra-budgetary users (such as the Croatian Water Resources Management and Croatia Roads) for the preparation of their 2012 budget proposals. Pursuant to these instructions, budgetary and extra-budgetary users will draw up their budget proposals and submit them to the relevant ministries and other state bodies of the first level of the organisational classification for harmonization and delivery to the Ministry of Finance. The Ministry of Finance will then reconcile the received budget proposals with the estimated revenues and will submit its own 2012 budget proposal, along with projections for 2013-2014, to the Government. The Government determines the proposals of the budgets and financial plans of extra-budgetary users for 2012, as well as projections for 2013-2014, and submits them to Parliament for debate. After their adoption, the budget execution process sets in. This time, exceptionally, the deadline is set at 1 April (due to the change of Government during the first three months in 2012, temporary financing is in effect), but normally, the entire process is completed by January 1.

The Guidelines represent a document that shapes the financial destiny of the state in the year to which it relates, but also in the years to come. This is why the Croatian Budget Act clearly defines the content of the Guidelines. The situation is similar in almost all countries in the world, where the Guidelines are issued under different names (pre-budget statement, fiscal strategy, budget strategy, budgetary framework, etc.), but with the more or less same content. Although the practices and procedures differ from country to country, it is generally accepted as good practice to discuss this document in the parliament as well (thus, for example, the US Congress rejected the Obama Administration's fiscal policy proposals), and to present a simplified version of the guidelines to the public. So far, however, this has not been the practice in Croatia.

[1] Vlada RH, 2012. *Prijedlog mjera i smjernice za izradu proračna za 2012. godinu* [online]. Available from: [http://www.vlada.hr/hr/naslovnica/sjednice_i_odluke_vlade_rh/2012/5_sjednica_vlade_republike_hrvatske].

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The purpose of the Guidelines is to spark off debate on budgetary figures placed in the context of the country's economic position, so that everyone knows what can be expected from the budget and what the relationship is between the Government's policies and the allocation of budget resources.

The Guidelines must show the Government's perception of the relationship between fiscal policy and economic environment, and its budgetary priorities in the following years, but without going into details, which the Government will provide in the budget proposal. The Guidelines must reflect the Government's initial positions regarding the next year and make clear that the final budget proposal can turn out different, because it will have to take into account developments during the formulation of the proposal, as well as feedbacks received within the Government, from Parliament, civil society organisations and the public.

According to the generally accepted good practice standards[2], the Guidelines should lay out:

1. the Government's perspective on the evolution of macroeconomic conditions, including the rationale for its basic assumptions about domestic and external macroeconomic indicators over the medium term, such as the real GDP growth, composition of its growth, and movements in employment, prices, the current account and interest rates;
2. the Government's clear long-term objectives and economic and fiscal policy intentions for the forthcoming budget year and the following two years; the total level of revenue, expenditure, deficit/surplus and debt; the role of the fiscal policy in the context of overall macroeconomic policy; the sensitivity of budget aggregates to macroeconomic conditions over the medium term; and estimates of the net borrowing requirement and assumptions concerning debt-servicing costs;
3. strategic measures envisaged for different sectors, providing a perspective on how different sectors will fare in terms of budget allocations and how these allocations might be influenced by any new government policy measures. This would include aggregate estimates of current outlays and investment by sector, information on the different elements of expenditure on a functional classification basis (e.g. spending on health care, education and defence) and on an economic classification basis (e.g. compensation of employees, subsidies and social welfare benefits); an update of the estimates issued in the previous year by sector; and anticipated changes in the roles of sectors;
4. expectations for tax and revenue, taking into account the revenue collections in the previous periods and anticipated developments in the economy that might influence revenue collections in the coming periods; and
5. estimated costs of any new policy measures to be undertaken in the coming year, including how such measures will affect the budget over the medium term and, possibly, the long term.

It is essential that the guidelines be published on time, so that the Parliament and the public can discuss them and come up with suggestions, which can help the Government formulate a budget proposal in a more efficient way. The best publication time frame for the guidelines would be April or May of a budget year, within the first stage of the budgeting process for the next year.

The Croatian Budget Act[3] mainly complies with the generally accepted good practice standards. According to this Act, the Ministry of Finance is obliged to draw up economic and fiscal policy guidelines for a three-year period and propose them to the Government by the end of May. The Government must adopt them by mid-June. According to Article 25 of the said Act, the guidelines must contain:

1. strategic economic and fiscal policy goals;
2. basic macroeconomic indicators;
3. basic fiscal policy indicators;
4. an estimate of revenue and expenditure and receipts and expenses for all levels of the general budget;

[2] Ramkumar, V. and Shapiro, I. (eds.), 2010. *Guide to Transparency in Government Budget Reports: Why are Budget Reports Important, and What Should They Include?* [online]. Available from: [http://internationalbudget.org/wp-content/uploads/Guide-to-Transparency-in-Government-Budget-Reports-Why-are-Budget-Reports-Important-and-What-Should-They-Include-English.pdf].
[3] Zakon o proračunu, NN 87/08. Available from: [http://narodne-novine.nn.hr/clanci/sluzbeni/340390.html].

5. a proposal for the financial plan amount broken down by users of the first level of the organisational classification, which includes the financial plan amounts for the previous budget year and for the current budget year, as well as a proposal for the financial plan amount for the next budget year and for the following two years; and
6. anticipated changes in public debt and a public debt management strategy.

While the legal framework is satisfactory, the problem lies in the fact that governments in Croatia have often failed to comply with the Act, with respect to both the timely issuance of guidelines and their mandatory content. No government so far has issued guidelines in mid-June, but only in autumn, except last year when they appeared in July. The content of the guidelines has so far been more or less in accordance with law, which has made it possible to assess whether they are credible or not. However, the Guidelines from July 2011[4] were an exception, as they did not contain (for election purposes?) a great number of tables with actual data items and levels of the organisational classification, which were included in all the previous guidelines. Therefore, it was impossible to see how the planned spending cuts would be implemented. These guidelines did not even include "a proposal for the financial plan amount by users of the first level of the organisational classification, consisting of the financial plan amount for the previous budget year and for the current budget year, as well as a proposal for the financial plan amount for the next budget year and for the following two years", so that it was impossible to establish how much particular budget users spent in 2010 and how much they were expected to spend in the 2011-14 period.

Despite being issued in a timely manner, the latest January 2012 Guidelines are incomplete. Instead of detailed tables they are supposed to include pursuant to the Budget Act, there is only one two-row table of expenditure (total expenditure and expenditure as a percent of GDP)!

Given the absence of actual data tables, it is impossible to assess the feasibility of goals set out in the descriptive part of the Guidelines. Those interested, which should be all of us, can only discuss such issues as the baby food definition or a potential increase vs. decrease in net wages. At the same time, it is not clear why the estimated growth of revenues from corporate income tax or personal income tax is going to be exactly 35% or 21% respectively, relative to the previous year. These estimates would probably be clearer if not only the budget plan, but also its outturns for 2011 were presented, which is unfortunately not the case.

It is even more difficult to understand how the economic growth would be achieved on the basis of a boost in gross investment of public enterprises[5], knowing that the net deficit accumulated by these enterprises, i.e. companies of special national interest, totalled 3.5 billion kuna in 2009. Owing to the previous Government's decision, providing that these companies' business reports are no more submitted to Parliament, those interested must seek up-to-date information on the websites of the companies, the Fina and Zagreb Stock Exchange. Based on such information it can be concluded that in 2010, the companies recorded a net surplus of 2-3 billion kuna, primarily owing to HEP (Croatian Electricity Company) and INA. It is therefore questionable whether they would be able to „generate a minimum increase of 8 billion kuna in investments relative to 2011." As the estimates of GDP growth in 2012 are mainly based on the growth of public sector investments, and a projection of expenditure cuts has not been elaborated, it would be good to wait for a budget proposal before drawing any conclusions to this effect.

One should hope that, after these Guidelines, prepared, under the circumstances, at such short notice, this government will be the first in the history of Croatia to pleasantly surprise the public by issuing high-quality macroeconomic and fiscal policy guidelines for the 2013-15 period in mid-June 2012, providing a brief explanation of these guidelines for citizens and submitting them to Parliament.

By sticking to the time schedule laid down in the Budget Act, as well as to the content of all budgetary documents (economic and fiscal policy guidelines, the Government' budget proposal, the voted budget, intra-year reports, mid-year and year-end reports and the state audit report), while at the

[4] Ott, K., 2011. "Commentary on the Croatian Government's Economic and Fiscal Policy Guidelines for the 2011-14 Period" [online]. *Press Release,* No. 30. Available from: [http://www.ijf.hr/eng/releases/30.pdf].
[5] Bajo, A., 2010. "Companies of Special National Interest in Croatia" [online]. *Press Release,* No. 30. Available from: [http://www.ijf.hr/eng/releases/25.pdf].

same time publishing simplified versions of these documents for citizens, the Government would significantly improve fiscal transparency. Higher fiscal transparency might help in curbing corruption, increasing public sector efficiency, defining and implementing more effective public policies, attracting investment and boosting confidence in the Government. In this way Croatia would finally improve its Open Budget Index [6]score and move to the group of countries with much more transparent budgets. After all, Croatia has joined the Open Government Partnership[7], and hopes are that it will fulfil the commitments assumed under that Partnership in all its activities, not just to promote its international image but to consolidate its public sector, stimulate economic growth and development and thus improve the well-being of its citizens.

[6] Urban, I. and Bađun, M., 2010. "Croatia's Score on Open Budget Index 2010" [online]. *Press Release,* No. 26. Available from: [http://www.ijf.hr/eng/releases/26.pdf].
[7] Vlada RH, Ured za udruge. Available from: [http://www.uzuvrh.hr/stranica.aspx?pageID=198].