

# What is the Condition of the Croatian State Budget after as Many as Three Revisions?

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**Ott, Katarina**

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### **What is the Condition of the Croatian State Budget after as Many as Three Revisions?**

**Katarina Ott, PhD**

**Due to irresponsible fiscal behaviour of the previous Croatian governments in the years of economic prosperity and of the present government in the planning and revision of the 2009 budget, the Croatian state budget deficit has increased from 2.4 billion kuna projected at end-2008, to 9.3 billion kuna projected in August 2009.**

Budget revisions have been one of the most popular topics these days in Croatia, and the term has become commonly accepted. Even those who have hardly come across this term so far probably know that a budget revision means a change, i.e. a reduction and/or increase, in the amount of the budget relative to the budget plan adopted at the beginning of a calendar year. A budget revision occurs if it is established, during the budget year, that budget revenue estimates are unrealistic, or if unexpected expenditures arise during the year. Budget revisions can be due to unforeseen circumstances in the domestic or world economy, like, for example, the current global crisis. But they can also be the consequence of the government's inability to make realistic estimates of the budget revenue and expenditure what was the case in Croatia.

So, how does this change in budget amounts actually look like and what are its consequences? A table and a graph below provide a simplified presentation of the 2009 budget plan at the end of 2008, and as many as three revisions that followed - the first one in April, and the second and third in July 2009.

Specifically, even though it was obvious, that the world economy got into a recession which Croatia would not be spared from, in late 2008, the Government planned the 2009 budget too optimistically. At that time, the Government was already aware that public spending was unsustainably high and that the public debt of almost 11 billion kuna would become due in 2009 (represented by the solid curve on the graph, right-hand scale). The Government was supposed to know that further borrowing was irresponsible towards declining future generations which will have to repay this debt, and that excess government borrowing would hamper private sector development, as a result of both funding difficulties and an inevitable increase in tax burden. However, under the pressure of different interest groups, the 2009 budget plan was as optimistic as in the times of strongest economic growth, i.e. it envisaged an increase in revenue from 116.1 billion kuna to 124.6 billion kuna, an increase in expenditure from 118.4 to 127 billion kuna and a deficit of 2.4 billion kuna. However, such a budget plan soon proved to be unsustainable. Therefore, despite the introduction of new taxes and a VAT rate increase, in the budget revisions that followed the Government had to plan significant reductions in revenues (from 124.6 billion kuna planned in December to 112.2 billion kuna in July), because, due to recession, the revenues were simply not raised. Unfortunately, the Government was not strong enough to make any significant spending

cuts (although it did reduce spending from 127 billion kuna planned in December to 121 billion kuna in July this year). Instead, it decided to sharply increase borrowing (see the dashed curve on the graph, right-hand scale). As a consequence of such irresponsible fiscal behaviour of both the previous governments in the period of the 5-percent annual growth of GDP (2002-2007) and the present Government which planned and revised the 2009 budget, a state budget deficit of 2.4 billion kuna, projected at end-2008, grew to 9.3 billion kuna projected in August 2009 (see the vertical space between the solid and dashed curves, right-hand scale).

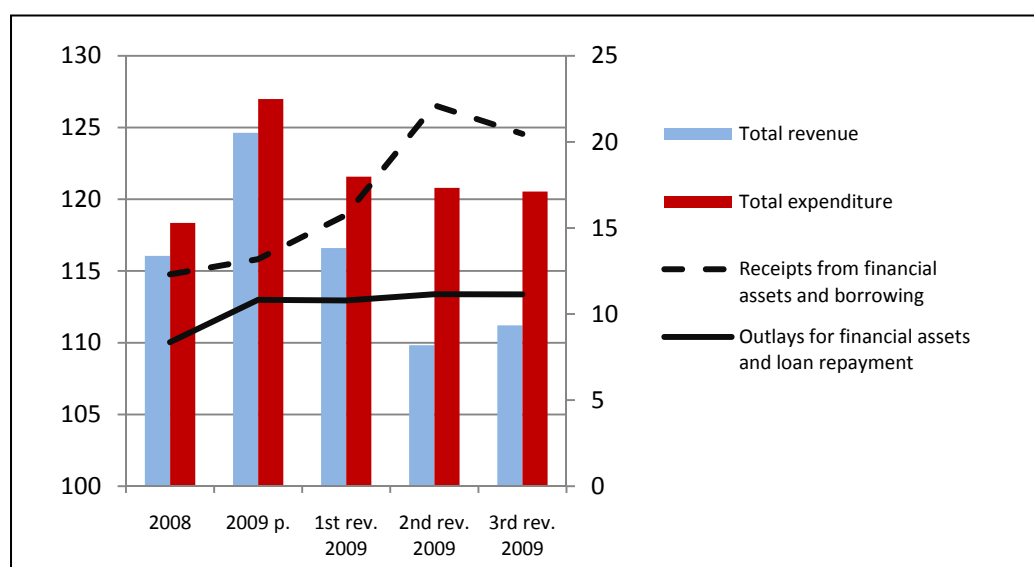
Time will show how realistic these three revisions of the Croatian budget, made in only seven months, were, how many more revisions will be made by the end of the year, and whether there will be any additional borrowing. And, let us not forget: the growth of the dashed curve (borrowing) in the current year will definitely lead to the growth of the solid curve (debt repayments and, of course, the interest increasing the debt) in the coming years.

**Table: Total revenue, expenditure and financing of the Croatian state budget (in million kuna)**

	Outturn 2008	Plan 2009	Revisions in 2009		
			I	II	III
<b>Income and expenditure account</b>					
Total revenue	116,059	124,637	116,603	109,824	111,211
Total expenditure	118,352	126,991	121,578	120,798	120,537
Surplus/deficit	-2,291	-2,355	-4,975	-10,975	-9,327
<b>Financing account</b>					
Receipts from financial assets and borrowing	12,308	13,183	15,763	22,129	20,471
Outlays for financial assets and loan repayment	8,360	10,828	10,788	11,155	11,144
Change in deposit balance	1,441	0	0	0	0
Net financing	2,508	2,355	4,975	10,975	9,327

Source: Ministry of Finance, 2009. Budget Revision: [<http://www.mfin.hr/hr/rebalans-proracuna-2009>].

**Graph: Total budget revenue and expenditure (left-hand scale), and budget financing (right-hand scale), in Croatia, in million kuna**



Source: Ministry of Finance, 2009. Budget Revision: [<http://www.mfin.hr/hr/rebalans-proracuna-2009>].