EELARVENÕUKOGU
FISCAL COUNCIL

FISCAL COUNCIL OF ESTONIA
REPORT FOR 2017

April 2018

CONTENTS

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CHAIRMAN'S FOREWORD

The budgetary process in Estonia in 2017 allowed the Fiscal Council to produce its usual opinions in three publications, which were issued in spring, summer and autumn. The Fiscal Council assessed the official economic forecasts in spring and autumn and the outlooks in them for public finances, and in the summer it looked at whether the structural position of the previous year met the requirements of the State Budget Act.

In summary it can be said that the Fiscal Council found the assumptions for economic growth used in the forecasts of the Ministry of Finance in 2017 to be satisfactory, though it warned about the large number of planned tax changes and the risks associated with implementing them, which could leave the forecast errors for tax revenues larger than usual and mean the revenue forecasts are too optimistic.

The initial estimates for tax revenues in 2017 show that forecast errors for individual taxes are the largest they have been since the crisis. Less tax revenue than expected was received from excise and from corporate income tax. As stronger economic growth, investment and employment meant revenues from labour taxes and VAT were higher than expected, the overall tax receipts were in line with the predictions of the state budget. The uncertainty caused by the tax changes is certain to continue to surround tax receipts this year too.

The Fiscal Council also noted last spring that it did not agree with the estimate by the Ministry of Finance of the output gap, which was put at -0.8% of GDP for 2017 and -0.4% for 2018 in the spring forecast and which supported the desire of the new governing coalition to use fiscal policy to boost growth in the economy. The Fiscal Council already considered at that time that the economic indicators showed the cyclical position to be good. The Ministry of Finance changed its view of the economic cycle in the autumn and replaced its estimate of a negative output gap in its forecast with an estimate of a positive gap.

All the main institutions that analyse the Estonian economy are currently in agreement that the Estonian output gap in 2017 was positive. This means that for last year as a whole the total production of the economy exceeded its long-term sustainable level. Preliminary data show the nominal position of the government in 2017 was in deficit of -0.3% of GDP. A nominal deficit combined with a positive output gap points to a structural deficit.

Having a structural deficit would in earlier years have been a breach of the budget rules, but one important change was made to the State Budget Act in 2017 and to the rules in it for structural balance. The new rule allows the structural position in Estonia to be in deficit, but not by more than 0.5% of GDP, and under the condition that a structural surplus of the same size had previously been amassed. The calculation of the Ministry of Finance shows this requirement was met. The only remaining calculation is whether the structural deficit exceeded 0.5% of GDP or not and the Fiscal Council will soon be able to give its opinion on this.

A more detailed review of the activities and main messages of the Fiscal Council in 2017 is given in the following pages. The appendix to the report contains the opinions published during the year. All the opinions of the Fiscal Council together with longer explanatory letters are published on the website of the Fiscal Council.

Chairman of Fiscal Council
Raul Eamets
Tallinn, 13 April 2018

1. BRIEF INTRODUCTION TO THE FISCAL COUNCIL

The Fiscal Council of Estonia is an independent advisory council established in 2014 under the State Budget Act, whose function is to give opinions on the macroeconomic and fiscal forecasts on which Estonia's fiscal policy is based and to observe compliance with national fiscal rules. European Union law makes mandatory for members of the euro area to establish a fiscal council that performs similar functions. In Estonia, the legal basis for the establishment of the Fiscal Council and its functions is the State Budget Act adopted on 19 February 2014[1]. The statutes of the Fiscal Council were approved at the meeting of the Supervisory Board of Eesti Pank held on 9 April 2014[2]. Information is exchanged between the Fiscal Council and the Ministry of Finance under a cooperation agreement signed in February 2018[3].

Under the amendment to the State Budget Act of 2017, the Fiscal Council gives its opinion as follows:

- in April on the spring macroeconomic and fiscal forecast of the Ministry of Finance;
- in April on the achievement of the target for the structural budget position in the previous year and on the targets set out in the state budget strategy for subsequent years;
- in September on the summer macroeconomic and fiscal forecast of the Ministry of Finance.

Beyond these three legally required opinions, the Fiscal Council is independent in setting its plan of work and may publish positions and research results on the Estonian economy or fiscal policy at its own discretion. The opinions of the Fiscal Council together with press releases, articles and background papers are published in Estonian and English on the website www.eelarvenoukogu.ee.

The Fiscal Council has six members and its work is led by the Chair and the Vice Chair (see Table 1). The inaugural Fiscal Council was appointed on 14 May 2014. The members of the Fiscal Council are appointed at the proposal of the Governor of Eesti Pank and with the approval of the Supervisory Board of Eesti Pank for a term of five years and can be reappointed.

Table 1. Members of Fiscal Council in 2017

Raul Eamets	Chairman	Dean of the Faculty of Social Sciences of the University of Tartu, Professor of Macroeconomics
Andrus Alber	Vice-Chairman	CEO of Finora Capital
Ülo Kaasik	Member	Deputy Governor of Eesti Pank
Martti Randveer	Member	Head of the Economics and Research Department of Eesti Pank
Urmas Varblane	Member	Professor of International Business at the University of Tartu
Andres Võrk	Member	Analyst at the Johan Skytte Institute of Political Studies at the University of Tartu

The members of the Fiscal Council are expected to have an impeccable reputation, a Master's degree or equivalent education in economics and the experience required for the performance of the Fiscal Council's functions. A member of the Fiscal Council may not be in a position or office or participate in activities that may have a negative impact on the independent performance of the Fiscal Council's functions. Foreign experts can also be members of the Fiscal Council.

The activities of the Fiscal Council are financed by Eesti Pank. The work of the Fiscal Council is supported by two economists from Eesti Pank, one of whom also performs the tasks of the secretary of the Fiscal

[1] https://www.riigiteataja.ee/en/eli/ee/504072014004/consolide/current
[2] http://eelarvenoukogu.ee/about-the-council/statutes
[3] http://eelarvenoukogu.ee/news/the-fiscal-council-and-the-ministry-of-finance-have-signed-a-cooperation-agreement

Council. The Fiscal Council also receives assistance from Eesti Pank in editing and translating published materials, website administration and other organisational issues.

2. ACTIVITY OVERVIEW

Meetings and opinions of the Fiscal Council

The statutes of the Fiscal Council require it to meet whenever necessary, but at least five times a year. In 2017 the Fiscal Council held five meetings on the premises of Eesti Pank. Two of the meetings were attended by all the members of the council, on two occasions five of the six members attended, and on one occasion four of the six members attended[4].

<u>17 April 2017</u>

At the first meeting of the year, the Fiscal Council discussed its opinion on the spring forecast 2017 of the Ministry of Finance.

<u>25 April 2017</u>

At its second meeting of the year, the Fiscal Council discussed its opinion and press release on the spring forecast 2017 of the Ministry of Finance and on the targets for the structural budget position reflected in the State Budget Strategy.

The opinion of the Fiscal Council on the spring forecast and on the targets for the structural budget position was published in a single document on 26 April (see Appendix 1).

The opinion of the Fiscal Council on the achievement of the target for the structural budget position for 2016 published on 25 July was produced after electronic consultations were held (see Appendix 2).

<u>8 September 2017</u>

At the third meeting of the Fiscal Council the Ministry of Finance presented its summer macroeconomic and fiscal forecast to the Fiscal Council.

The opinion of the Fiscal Council on the summer forecast was published on 27 September (see Appendix 3).

<u>9 October 2017</u>

The fourth meeting of the Fiscal Council discussed the topics for the upcoming meeting of the Network of EU Independent Fiscal Institutions, including the position of the network on the Five Presidents' Report, the participation of the Fiscal Council in the output gap working group, and the compilation for publication of the European Fiscal Monitor.

<u>20 December 2017</u>

The fifth meeting of the Fiscal Council discussed the research of how fiscal councils affect budget discipline. It also discussed matters related to travel and seminars for the Fiscal Council in 2018.

[4] A meeting of the Fiscal Council has a quorum if at least four members are present.

Other meetings and presentations

2 February 2017

Fiscal Council chairman Raul Eamets attended the sixth meeting of the EU Network of Independent Fiscal Institutions (EUNIFI) organised by the European Commission in Brussels. The meeting discussed cooperation between the European Fiscal Board and the national fiscal councils, the expenditure rule in the European fiscal framework, and the results of the Commission's annual survey on fiscal councils.

14 March 2017

Vice Chair of the Fiscal Council Andrus Alber and advisor Andres Saarniit attended a meeting organised by the French embassy in Tallinn where Estonian fiscal and tax policy and the planned policy measures of the new government were discussed.

6-7 April 2017

Vice Chair of the Fiscal Council Andrus Alber attended the annual meeting of parliamentary budget officials and independent fiscal institutions organised by the OECD in Edinburgh. New fiscal councils were presented and there were presentations and discussions on the state of public finances in OECD countries, the assessment of fiscal risk and fiscal sustainability, and public dissemination of the analysis and messages of fiscal councils.

7 April 2017

Members of the Fiscal Council met in Eesti Pank with staff of the Ministry of Finance, who presented the Ministry's economic forecast for spring 2017.

11 April 2017

Vice Chair of the Fiscal Council Andrus Alber, council member Urmas Varblane and advisor Andres Saarniit met representatives of the European Commission in Tallinn to discuss the views of the Council on Estonian economic growth, competitiveness and the labour market, and the experience so far of the Fiscal Council on its cooperation with the Ministry of Finance and Eesti Pank.

27 April 2017

Chair of the Fiscal Council Raul Eamets and advisor Andres Saarniit attended a meeting of the government to present the opinion of the Fiscal Council on the targets for the structural budget position in the state budget strategy.

5 May 2017

Chair of the Fiscal Council Raul Eamets attended the policy seminar 'Evolving fiscal policies in Europe' hosted by the International Monetary Fund (IMF) in Brussels. The seminar discussed the possible need for centralised management of euro area fiscal policy and the institutional form of it, the reasons the European Fiscal Board was set up and its mandate, the state of fiscal policy in Europe and the world, and the measurement of fiscal space.

8 May 2017

Chair of the Fiscal Council Raul Eamets and advisor Andres Saarniit attended a meeting of the Finance Committee of the Riigikogu to present the opinion of the Fiscal Council on the spring economic forecast of the Ministry of Finance and on the targets for the structural budget position for 2018−2021.

23 May 2017

Chair of the Fiscal Council Raul Eamets presented the report on the council's activities in 2016 to the Supervisory Board of Eesti Pank.

14 June 2017

Chair of the Fiscal Council Raul Eamets, Vice Chair Andrus Alber, and analyst Lauri Punga met a delegation from the International Monetary Fund (IMF) in Tallinn to discuss Estonia's new fiscal rules, the cyclical position of the Estonian economy, and the medium-term budget strategy of the new government.

15-16 June 2017

The meeting of the Baltic and Finnish fiscal councils organised by the Estonian Fiscal Council was held in Tallinn. Twenty fiscal council members and specialists from five different institutions attended the meeting. Fiscal Council analyst Lauri Punga gave a presentation to the meeting on Estonia's new budget rules. Chair of the Fiscal Council Raul Eamets gave an introductory presentation on endorsing economic forecasts.

27 September 2017

Chair of the Fiscal Council Raul Eamets and advisor Andres Saarniit attended a meeting of the government to present the opinion of the Fiscal Council on the summer economic forecast of the Ministry of Finance before the draft of the state budget for 2018 was approved.

9 October 2017

Chair of the Fiscal Council Raul Eamets and advisor Andres Saarniit attended a meeting of the Finance Committee of the Riigikogu to present the opinion of the Fiscal Council on the summer forecast of the Ministry of Finance.

19 October 2017

Chair of the Fiscal Council Raul Eamets attended the joint seminar of fiscal councils and central banks in Frankfurt titled 'Fiscal governance in the euro area: Current challenges and future outlook'. The meeting discussed the fiscal position of the euro area, the future of the economic and monetary union, a review of the fiscal compact, and the impact of discretionary tax measures on revenue elasticities.

31 October 2017

Vice Chair of the Fiscal Council Andrus Alber presented the council's activities and main messages in the past half year to the Supervisory Board of Eesti Pank.

7 November 2017

Vice Chair of the Fiscal Council Andrus Alber attended a meeting of the Network of EU Independent Fiscal Institutions in Madrid. The meeting discussed proposed changes to the European fiscal framework, the annual report of the European Fiscal Board, the work of the working groups of the network, and the next edition of the European Fiscal Monitor.[5]

[5] The European Fiscal Monitor, published at the initiative of the Network of EU Independent Fiscal Institutions and including a chapter on Estonia written by the Fiscal Council, can be found at: http://www.euifis.eu/eng/fiscal/174/european-fiscal-monitor

1 December 2017

Vice Chair of the Fiscal Council Andrus Alber, advisor Andres Saarniit and analyst Lauri Punga met a delegation from the International Monetary Fund (IMF) in Tallinn to discuss Estonia's new fiscal rules and the fiscal policy measures of the new government.

19 December 2017

Vice Chair of the Fiscal Council Andrus Alber attended the discussion on the future of Estonian and European finances at the Estonian representation of the European Commission. Experts from the Ministry of Finance and the Estonian representation of the European Commission discussed the condition of the Estonian state budget and the proposals of the European Commission for deepening the economic and monetary union.

Opinion articles

28 April 2017

The opinion piece 'Now is not the time to be putting the state budget in deficit' by Raul Eamets was published in the newspaper Postimees[6].

The Fiscal Council considers that the economic forecast describes the expected development of the key economic indicators accurately enough, is cautious enough, and is quite well in line with several other forecasts. The world around us is relatively unstable and it is better to be safe than sorry as they say. Where there is a difference, and what is worth disputing, is the Ministry of Finance's assessment of the position of the economic cycle.

/.../

Overall this means that the impact of the measures that are intended to revive the economy will not be felt at the most appropriate moment. Of course the Fiscal Council is not opposed to the use of investment to reinvigorate the economy, the debate is about the timing. The fire is burning with quite a strong flame and we are pouring more petrol onto it.

1 June 2017

The opinion piece 'The new look of Estonian fiscal policy' by Urmas Varblane was published in the newspaper Äripäev[7].

Estonian fiscal policy had earlier already been run for a long time on the principle of a balanced budget, and in 2014 this was written into the State Budget Act. To take better account of the economic cycle and its impact on tax revenues, the requirement for the annual budget balance was set in structural terms. Now, after only three budgets have been passed following this requirement, successfully it would appear, the new government coalition is changing the fiscal rules. The new rules will permit the general government a structural deficit if structural surpluses have previously been built up.

/.../

The fiscal forecast is less certain than usual this year because the details of several of the planned tax changes are not yet sufficiently clear. From observing the current discussion in the government coalition

[6] Full article: http://eelarvenoukogu.ee/news/now-is-not-the-time-to-be-putting-the-state-budget-in-deficit

[7] Full article: http://eelarvenoukogu.ee/news/the-new-look-of-estonian-fiscal-policy

about the tax changes, it is not certain whether all the drafts proposed will come into force at the intended time and in the form proposed. In sum, the Fiscal Council considers that the structural deficit of the general government could be larger in 2018 than the government is planning for.

The planned changes to the fiscal rules have also been prepared in a very short time. The reputational risk caused by the volatility and unpredictability of the procedures for setting the fiscal rules and tax policy is a serious problem. If the government decides to loosen the fiscal rules but is at real risk of not meeting them in their very first year, it will understandably not have a positive impact on the credibility of those rules or of the whole of fiscal policy.

3. BUDGET

The Fiscal Council of Estonia works with an annual budget approved by the Governor of Eesti Pank. The activities of the Fiscal Council are financed by Eesti Pank from its budget on the principle that the funds allocated must be sufficient for the Fiscal Council to be able to perform its functions independently[8]. An overview of the expenses of the Fiscal Council in 2017 is given in Table 2[9].

Table 2. Fiscal Council expenditure in 2017 (euros)

Remuneration of members	54,862
Business trips	3,681
Seminars and events	3,218
IT expenditure	164
Total expenditure	61,925

Total expenses for 2017 were 90% of the amount budgeted. Salaries of the members accounted for around 89% of the spending of the Fiscal Council, costs of travel for 6%, and other costs 5%. The Chair of the Fiscal Council receives a monthly salary of 793 euros, and members a salary of 529 euros.

The budget planned for the Fiscal Council for 2018 is 70,800 euros (see Figure 1). The budget allows for the usual number of business trips for participation in the work of the networks of the independent fiscal institutions and the amendments that will apply from 2018 to the law on salaries for senior civil servants, which also affects the level of pay of members of the Fiscal Council.

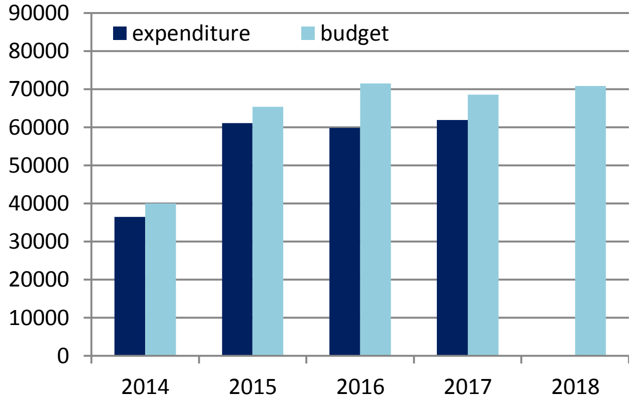

Figure 1. Fiscal Council budget and expenditure (euros)

[8] The Government of the Republic compensates Eesti Pank for the direct expenses incurred due to the work of the Fiscal Council at the request of Eesti Pank. The central bank has not yet exercised this right.

[9] Table 2 does not contain the costs of the pay of the Eesti Pank economists working to support the Fiscal Council.

APPENDIX 1. Opinion on the spring forecast 2017 of the Ministry of Finance and on the targets for the structural budget position for 2018−2021

Opinion

Under the State Budget Act, the Fiscal Council must give an assessment of the macroeconomic and fiscal forecasts of the Ministry of Finance, and of the structural budget position planned for the general government in the state budget strategy. This year there was a very short gap between the releases of these documents, and so the Fiscal Council has put both its opinions together in one publication.

External demand started to rise in 2016 and the Estonian exporting sector was able to benefit from this. The spring forecast of the Ministry of Finance expects GDP growth of 2.4% in 2017 and 3.1% next year, which is very close to the outlooks from other forecasters. The views of forecasters on changes in consumer prices are also relatively similar.

In the longer run the Fiscal Council sees that there is more of a danger of slower growth. Firstly, maintaining such growth requires labour costs to rise more slowly, and only the first signs of this have been apparent so far. Secondly there is no evidence of the expected increase in investment activity that should help keep economic growth at close to 3%. Thirdly, growth in our main trading partners may indeed have picked up, but the hardening of protectionist positions is a cause for concern, as it could harm the potential for growth in the Estonian economy. This makes it reasonable that the Ministry of Finance has slightly reduced its forecasts for the sustainable growth of the main economic indicators.

The new government plans to introduce several important changes to fiscal policy. The Fiscal Council recommends that when writing forecasts and budget plans in future, the government should more clearly state the effect that its planned expenditure and tax policy measures will have on economic growth.

Overall the Fiscal Council finds that the spring forecast of the Ministry of Finance describes the outlook for economic growth and inflation in Estonia accurately enough. The Fiscal Council does not agree, however, with the Ministry of Finance's estimate of the position of the economic cycle. This is because labour market indicators, among them rapid wage growth, low unemployment and high employment, indicate the economy is in a good cyclical position, which contradicts the opinion of the Ministry of Finance that there are still unused production resources in the economy.

As well as giving an opinion on the spring forecast of the Ministry of Finance, the Fiscal Council needs to assess whether the planned structural budget position of the general government satisfies the fiscal rules or needs adjustment. The state budget strategy for 2018−2021 puts the structural budget position for the general government in deficit over the next three years, by as much as 0.5% of GDP in 2018 and 2019. The Fiscal Council finds this to be in breach of the State Budget Act as it stands.

The Fiscal Council is aware that the government plans to change the fiscal rules in the State Budget Act so that a structural budget deficit of up to 0.5% of GDP can be permitted against the earlier structural surplus that was built up. Even assuming that this change is made in the State Budget Act, the Fiscal Council sees a danger that the general government structural budget deficit for 2018 will be larger than 0.5% of GDP.

The calculation of this size of deficit is based on the assumption that the output gap in 2018 in Estonia is negative by 0.4% of GDP. Measuring the structural budget position using the estimate of the output gap by the European Commission or the International Monetary Fund puts the actual structural deficit even bigger by up to 0.2 percentage point of GDP.

This makes it possible that the impact of the measures that are intended to revive the economy will not be felt at the most appropriate moment in the economic cycle. Excessive growth in budget spending may make it harder to keep the growth in wages in the private sector in check, and may make it harder to find the labour resources needed for an expansion of production. Equally, it is not impossible that growth in domestic demand may outstrip that in supply in some sectors.

Keeping the general government fiscal position at the targeted level also depends on the passage of several tax changes that had not yet been fully specified or approved by the Riigikogu at the time this Fiscal Council opinion was written. The revenue increasing impact of those changes is estimated at up to 1% of GDP depending on the year. In the assessment of the Fiscal Council the large number of planned tax changes and the complexity of introducing them, partly because of the disputes at the Supreme Court over the changes to the tax laws, will increase the potential for forecasting errors and increase the risk that the forecast for tax revenues is too optimistic.

Meeting the government targets assumes changes in the State Budget Act as well as in various tax laws. The planned changes to the fiscal rules have been prepared in a very short time and represent a fundamental shift from the act that has been in force for only three years in the direction of a looser fiscal policy. It is recommended that in future such frequent changes should be avoided so that the credibility of fiscal rules may be maintained.

Chairman of Fiscal Council
Raul Eamets
Tallinn, 26 April 2017

The extended letter of explanation that accompanies the opinion can be found at: http://eelarvenoukogu.ee/news/despite-the-reliable-economic-forecast-the-planned-budget-policy-is-not-in-accordance-with-the-law

APPENDIX 2. Opinion on the achievement of the general government structural budget position target in 2016

Opinion

Under the State Budget Act, the Fiscal Council must issue its opinion on the achievement of the target for the structural budget position after the government's consolidated report on the financial year has been published. According to fiscal rules, the general government budget has to be at least in structural balance.

When the state budget strategy for 2016–2019 was prepared, the structural budget position target was set at a surplus of 0.6% of GDP. The target remained the same when the 2016 state budget was passed. In the state budget, it was also assumed that the budgets of both central and local governments, and the budget for the whole general government would be in a small nominal deficit.

Under the European system of accounts (ESA 2010), which is the basis for the fiscal rules in Estonia and the European Union, the revenues of the general government exceeded spending by an amount that was equal to 0.3% of GDP. The nominal surplus was mostly due to tax revenues being stronger and investment expenditure being smaller than expected. Despite GDP growth being relatively slow, labour taxes caused the tax income of the general government to rise nearly 6% in a year, which allowed increasing the general government current expenditure at the same rate.

Calculations by the Ministry of Finance put the general government structural budget surplus at 0.7% of GDP in 2016, which exceeds the target for 2016. Assessments by other institutions also indicate a fiscal position that is in structural balance or in surplus. Only the disaggregated method used by the Fiscal Council indicates that a structural deficit is also possible.

The Fiscal Council finds that based on the current estimate, the general government structural budget position for 2016 is in line with the State Budget Act. However, experience has shown that the estimates of output gap and the structural balance can later change significantly. This means that when planning fiscal policies, the estimate concerning the size of the structural surplus given in the consolidated report on the state financial year cannot be considered final.

Chairman of Fiscal Council
Raul Eamets
Tallinn, 25 July 2017

The extended letter of explanation that accompanies the opinion can be found at: http://eelarvenoukogu.ee/news/the-general-government-budget-for-2016-is-in-nominal-and-structural-surplus

APPENDIX 3. Opinion on the summer forecast 2017 of the Ministry of Finance

Opinion

It is the job of the Fiscal Council to observe that the budgetary rules are followed and to publish opinions on the state macroeconomic and fiscal forecasts, which the Ministry of Finance produces twice a year. Under the updated state budget act the spring economic forecast is used as the basis for drafting the state budget strategy and the state budget for the next year, which is then amended if necessary after the summer economic forecast is published. For this reason the Fiscal Council focuses primarily in its assessment on the outlook for 2018.

The summer economic forecast of the Ministry of Finance for 2017 expects that the Estonian economy will grow faster in 2018 than was previously forecast and with support from more branches of the economy. The economy will grow by 3.3% at constant prices and 6.9% at current prices. Although this is faster than the estimated long-term sustainable growth rate, the Fiscal Council considers that the risks to the forecast that could make growth faster or slower, stemming for example from slower growth in investment or faster growth in wages, are in balance in 2018.

In other words, the Estonian economy will grow at above its sustainable rate next year. The estimate of the Ministry of Finance puts the gap between actual GDP and the potential level, or the output gap, at 0.5% of GDP. The estimate of the Fiscal Council of the position in the economic cycle is almost the same. Other economic indicators that are easier to measure, such as rapid wage growth, rising employment, a rise in the vacancy rate, and an increase in reports from companies of labour shortages restricting growth, indicate that the Estonian economy is operating at above its sustainable level. Overall, the Fiscal Council finds that it is reasonable for the GDP growth forecast to be corrected upwards for the near term, and that the forecast of the Ministry of Finance is accurate enough in its description of the future development of the Estonian economy.

Like in the spring however, the Fiscal Council does not agree fully with the Ministry of Finance’s forecast for tax revenues in 2018. Amendments to the corporate income tax system, which encourage regular distribution of dividends through a lower tax rate, will enter into force from next year, and the Ministry of Finance assumes that almost half as much will be taken out in dividends in 2018 as was taken in 2017. This assumption means that tax revenues will again grow by more than the economy as a whole, at a rate of 8%. The Fiscal Council considers this assumption to be too optimistic.

Despite the very rapid growth in revenues, the general government budget is expected by the summer forecast to be in nominal and structural deficit in 2018. The structural deficit is forecast to be 0.4% of GDP, which is above but close to the legally permitted limit. Given the possible errors in the forecasting of tax revenues and the difficulty of estimating the position in the economic cycle, the structural deficit may turn out to be bigger than this though.

For this reason, the Fiscal Council welcomes the government decision of 14 September to draft the state budget for 2018 with a smaller structural deficit than was expected in the summer forecast. Given the position of the economic cycle, the Fiscal Council recommends that the state budget should have a small surplus to ensure that the structural fiscal position remains within the legal limits.

Chairman of Fiscal Council
Raul Eamets

Tallinn, 27 September 2017

The extended letter of explanation that accompanies the opinion can be found at: http://eelarvenoukogu.ee/news/rapid-economic-growth-demands-a-budget-surplus