



FISCAL STRESS TESTING MODEL AND ASSESSMENT OF FORWARD-LOOKING SCENARIOS

Ondra Kameník, Michal Kejak, David Vávra

November 2025
WWW.SYRI.CZ



Funded by
the European Union
NextGenerationEU



CZECH
RECOVERY PLAN



MINISTRY OF EDUCATION,
YOUTH AND SPORTS

SYRI STUDY / RG 8
ECONOMIC IMPACTS

FISCAL STRESS TESTING MODEL AND ASSESSMENT OF FORWARD-LOOKING SCENARIOS

Ondra Kameník¹, Michal Kejak^{2*}, David Vávra³

affiliation:

¹ OGREsearch

² CERGE-EI1

³ OGREsearch

*** Corresponding Author. Research assistance of Ngoc Nam Nguyen and Miroslav Hlousek is gratefully acknowledged.**

November 2025

WWW.SYRI.CZ

This study was prepared under the National Recovery Plan project, “The National Institute for Research on the Socioeconomic Impact of Diseases and Systemic Risks”, No. LX22NPO5101, funded by the European Union’s NextGenerationEU instrument (Ministry of Education, Youth and Sports, NRP’s EXCELES Programme)

Summary

This policy paper introduces a forward-looking, semi-structural macro-fiscal model developed to support fiscal policy analysis in the Czech Republic. The model fills a persistent gap in fiscal planning by providing a transparent and analytically tractable framework for assessing medium- and long-term fiscal sustainability under uncertainty.

The analysis focuses on three core scenarios:

1. A baseline scenario featuring unambitious consolidation, targeting a 50% debt-to-GDP ratio;
2. A comparative assessment of projections produced by the Czech Fiscal Council;
3. An ambitious alternative scenario exploring the feasibility and benefits of achieving a 30% debt-to-GDP target.

Policy Implications and Recommendations for the Czech Republic

The analysis underscores the risks associated with delayed fiscal consolidation, the shortcomings of overly optimistic projections, and the long-term advantages of maintaining lower debt levels—particularly through reduced interest costs and greater fiscal resilience. Failure to consolidate public finances may lead to unsustainable debt dynamics and increased vulnerability to macroeconomic shocks. Furthermore, reliance on internally inconsistent modeling frameworks that overlook key interactions can lead to misguided policy decisions and insufficient preparation for fiscal risks.

Main Characteristics and Innovations of the Model

The fiscal stress testing model is a forward-looking, semi-structural macro-fiscal tool designed to assess medium- and long-term fiscal sustainability under uncertainty. It ensures strict stock-flow consistency between government deficits, debt, and interest payments, and incorporates rational expectations to reflect the forward-looking behavior of economic agents. The model is estimated using Bayesian techniques, enabling a transparent integration of empirical evidence and expert judgment.

Analysis of Future Policy Scenarios

Three forward-looking scenarios illustrate the role of fiscal consolidation in ensuring long-term sustainability:

1. **Baseline (50% debt-to-GDP target):** Gradual, modest consolidation stabilizes debt levels but leaves the economy exposed to higher interest costs and elevated fiscal risks.
2. **Comparison with Czech Fiscal Council projections:** Reveals the dangers of relying on overly optimistic assumptions regarding growth, interest rates, and risk premia.
3. **Ambitious consolidation (30% debt-to-GDP target):** Demonstrates the long-term benefits of stronger consolidation, including lower debt-servicing costs and enhanced fiscal resilience.

1. Introduction

Debates on fiscal sustainability and the appropriate pace of consolidation have regained prominence in the wake of the global financial crisis. However, forward-looking analytical frameworks to inform these debates remain scarce. Fiscal consolidation strategies are often discussed in isolation, without sufficient consideration of their interactions with the broader macroeconomic environment (Leeper, 2010). As a result, fiscal policy tends to be reactive—responding to unfolding developments rather than shaping credible medium-term strategies.

In contrast to monetary policy, which has become increasingly forward-looking and systematic, fiscal policy remains largely backward-looking and focused on short-term issues rather than long-term sustainability. This discrepancy stems, in part, from the absence of adequate analytical tools and reliable data. As Leeper (2010) observes, “monetary policy making is increasingly a science, whereas fiscal policy remains closer to alchemy.” While central banks routinely publish interest rate and exchange rate projections and communicate their underlying assumptions, it is still difficult to obtain a transparent and official assessment of what constitutes a sustainable level of public debt under alternative macroeconomic conditions.

To help fill this gap, we developed a forward-looking fiscal stress-testing model tailored to the Czech Republic. We assembled relevant data, estimated the model parameters, designed policy scenarios, and performed stochastic simulations. The resulting framework is simple yet analytically rigorous. It enables systematic assessment of medium- and long-term fiscal sustainability, as well as stress-testing of alternative consolidation strategies.

A key focus of the model is debt management, particularly the maturity and currency composition of public liabilities—elements that are often overlooked despite their considerable influence on fiscal risks. The framework also facilitates the evaluation of alternative fiscal strategies across three core dimensions: potential output losses, political feasibility, and the probability of consolidation failure. These risks are visualized through fan charts representing the probability distributions of debt trajectories under uncertainty.

Relation to Existing Work

The model developed in this policy paper builds on a growing literature that applies forward-looking, semi-structural macroeconomic frameworks to fiscal policy analysis. These models are designed to combine theoretical consistency with empirical tractability, allowing policymakers to evaluate medium- and long-term fiscal developments while maintaining transparency and flexibility in implementation.

In contrast to fully specified DSGE models, semi-structural models abstract from microfoundations but retain essential behavioral and identity-based relationships—such as private consumption, investment, inflation dynamics, and fiscal rules. This makes them particularly suited for policy simulation, stress testing, and scenario analysis under conditions of uncertainty and data limitations.

A prominent example is the ECB's BASE model (Bańkowski et al., 2021, Bańkowski 2023), a semi-structural framework developed for the euro area that incorporates fiscal-monetary interactions, transmission lags, and institutional constraints, with particular attention to fiscal multipliers. The model has ability to produce internally consistent forecasts, simulate alternative policy paths, and support real-time fiscal monitoring.

This modeling approach improves upon the simpler frameworks used by institutions such as the IMF and the European Commission, whose debt sustainability analyses are often deterministic and highly aggregated. For instance, the IMF's work (e.g., Debrun and Kinda, 2017) develops forward-looking fiscal indicators but typically lacks explicit modeling of expectations, nonlinearities, or fiscal-monetary feedback effects. Similarly, in the Czech context, the Fiscal Council (Národní rozpočtová rada, NRR) produces medium-term projections based on exogenous assumptions, without employing a formal model of behavioral responses or general equilibrium interactions.¹

Our approach complements these tools by offering a **transparent, stock-flow-consistent**, and **stochastically simulated** framework that links fiscal consolidation strategies with macroeconomic variables and financial market conditions. The model explicitly captures the interaction between fiscal and monetary policy, embeds rational expectations, and incorporates debt structure by maturity and currency. These features make it well suited for forward-looking fiscal surveillance, consolidation planning, and risk-based policy evaluation.

Key Innovations

The model introduces several innovations compared to existing fiscal stress-testing tools:

- ▶ **Stock-flow consistency**, ensuring realistic and coherent debt and deficit dynamics;
- ▶ **Explicit modeling of debt structure**, including both maturity and currency composition;
- ▶ **Endogenous risk-premium dynamics**, where sovereign spreads respond to evolving fiscal and macroeconomic conditions;
- ▶ **Rational expectations**, reflecting the forward-looking behavior of economic agents; and
- ▶ **Stochastic simulation capabilities**, enabling the generation of probability distributions (fan charts) for debt trajectories and fiscal outcomes, rather than relying on single deterministic forecasts.

Together, these features make the model well-suited not only for assessing baseline fiscal sustainability but also for evaluating the credibility and risk profiles of alternative consolidation strategies.

Structure of the Policy Paper

The remainder of this policy paper is organized as follows. Section 2 outlines the model, summarizing its key equations, data sources, and estimation methods. Section 3 presents the baseline and alternative fiscal scenarios, including results from stochastic simulations. Section 4 compares our baseline projection with the Fiscal Council's (NRR) forecast,

¹ As of the 2023 Fiscal Council Report, Národní Rozpočtová Rada (2023).

highlighting the implications of embedding their assumptions into our forward-looking framework. Section 5 explores a more ambitious fiscal strategy aimed at reducing the debt-to-GDP ratio to 30%, and evaluates its impact on debt dynamics, interest costs, and output. Finally, Section 6 concludes with policy recommendations, emphasizing the importance of internally consistent fiscal assumptions, the benefits of early and credible consolidation, and the long-term advantages of maintaining lower public debt levels to strengthen fiscal and macroeconomic resilience.

2. Model Overview and Structure

This semi-structural macro-fiscal framework is designed to generate internally consistent trajectories of macroeconomic and fiscal variables while retaining the flexibility needed for real-time policy applications. Operating at an annual frequency, the model combines forward-looking stochastic dynamics, rational expectations, and both New-Keynesian and non-Ricardian elements. It has a non-linear structure and relies on Bayesian estimation of parameters, allowing for a realistic yet tractable assessment of fiscal risks under uncertainty.

2.1 Semi-Structural Approach and Key Features

The model ensures consistency between government deficits, interest payments, and debt accumulation, while abstracting from detailed microfoundations—such as how taxes are collected or specific expenditure programs are administered. This abstraction enables the model to remain manageable in complexity while still capturing the core fiscal-macro interactions.

Public debt is modelled with full stock-flow consistency. The framework tracks both the maturity structure and currency composition of government liabilities, which allows for realistic estimation of interest costs under changing yield curves and financial conditions. Domestic Treasury bonds and foreign-currency debt are both accounted for, and their shares evolve endogenously in response to market conditions and policy settings.

A fiscal rule governs the evolution of the primary balance and determines how deficits are financed—both in terms of maturity and currency mix. This fiscal block includes a behavioural reaction function linking the primary balance to the output gap and the level of public debt. In addition, a risk premium function increases with the level and trajectory of debt, feeding back into interest costs and macroeconomic variables.

Monetary policy is captured via a Taylor-type rule that adjusts nominal interest rates in response to inflation and the output gap. The uncovered interest parity (UIP) condition governs exchange rate dynamics, creating further macro-financial feedbacks. Inflation is determined by a New-Keynesian Phillips curve, while demand dynamics are captured through an IS equation with rational expectations.

The model incorporates several structural features relevant for fiscal stress testing:

- ▶ Non-Ricardian behaviour of agents
- ▶ Crowding-out of private capital from public debt accumulation
- ▶ Endogenous and debt-sensitive term and risk premia
- ▶ Asymmetric fiscal behaviour, with stronger adjustments of structural deficits at higher debt levels

Although it draws conceptually from dynamic stochastic general equilibrium (DSGE) models, the framework avoids their computational burdens and heavy data requirements. Instead, it offers a more malleable and transparent setup suitable for policy experiments, consistency checks, and stress testing in institutional settings.

2.2 Estimation and Simulation

Model parameters are estimated using Bayesian techniques, ensuring statistical coherence while incorporating prior knowledge and expert judgement. Once estimated, the model is used for stochastic simulations that generate full probability distributions of future fiscal outcomes, visualised through fan charts. These charts allow policymakers to assess the likelihood of adverse fiscal events—such as breaching legislated debt thresholds—and to compare alternative policy strategies under uncertainty.

3. Baseline Scenarios

In this section, we present our baseline long-term projection of an unambitious fiscal consolidation targeting a debt-to-GDP ratio of 50%—a level above the historical average—and discuss the projected trajectories of key fiscal variables.

3.1 Baseline Scenario: Assumptions and Setup

The baseline scenario represents an unambitious fiscal consolidation strategy that targets a debt-to-GDP ratio of around 50% by 2050, a level higher than the Czech Republic's historical average. The model is fully stock-flow consistent, with risk premia endogenously determined by the level of debt and the time value of money. The structure of public debt is decomposed by maturity—domestic bonds with one-, three- and ten-year maturities, and foreign-currency bonds with a five-year maturity—and by currency composition.² The projections are stochastic, generating probability distributions of future trajectories for all major macroeconomic and fiscal variables. Confidence intervals are presented as non-symmetric probability bands around the most likely, modal trajectories.

The projection incorporates as a given assumption the short-term (up until 2025 where available) projections of the Ministry of Finance from the August 2023 forecast for several of the main macroeconomic variables whose list can be found below. The projection is

² For compactness, the model works with three maturities of local currency debt: 1Y, 3Y, and 10Y, and one maturity of 5Y for the FCY debt.

also based on the forecast of several external variables up to 2027: the foreign output gap, inflation and interest rate.^{3,4}

3.2 Main Simulation Results

The debt-to-GDP ratio is projected to stabilize at approximately 50% by the middle of the century (see Fig. 1). This trajectory is consistent with an average budget deficit of 2–3% of GDP (see Fig. 2), which broadly aligns with the Czech Republic’s fiscal performance over the past two decades.

The government’s primary balance gradually improves over time (see Fig. 3), eventually turning into a modest surplus. However, the pace of adjustment remains relatively unambitious, especially considering the Czech Republic’s historical record of fiscal prudence.

The structural deficit (see Fig. 4) is expected to decline from its current level of around 4% of GDP—close to the historical peak—toward 2% of GDP, which is roughly in line with the historical average since 2005.

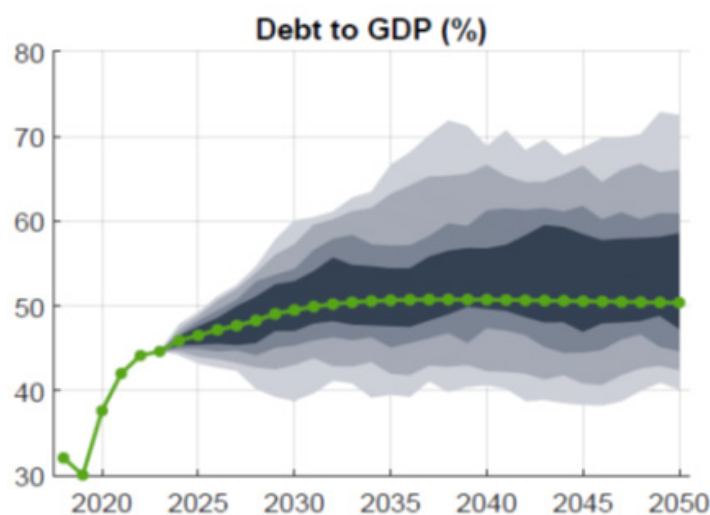


Figure 1: Debt to GDP Ratio [%]

3 The external assumptions come courtesy of the world economy forecast of the Global Projection Model Network.

4 Aside from those assumptions, the only other manual adjustment of the prediction consists of manually inserted values for the residuals in the output gap and exchange rate equations of the model during 2026–2028 and 2029, respectively. Those residuals decline over time; their purpose is to smooth the simulation transition from the Ministry of Finance projection to the model’s own endogenous mechanisms.

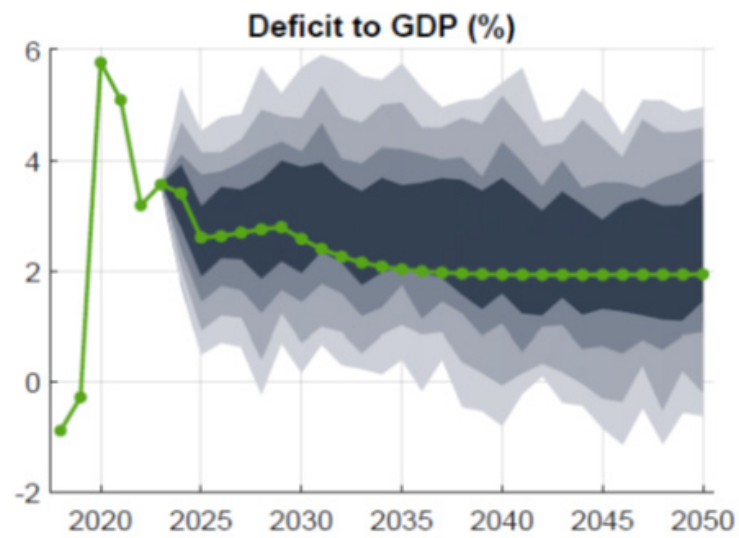


Figure 2: Deficit to GDP Ratio [%]

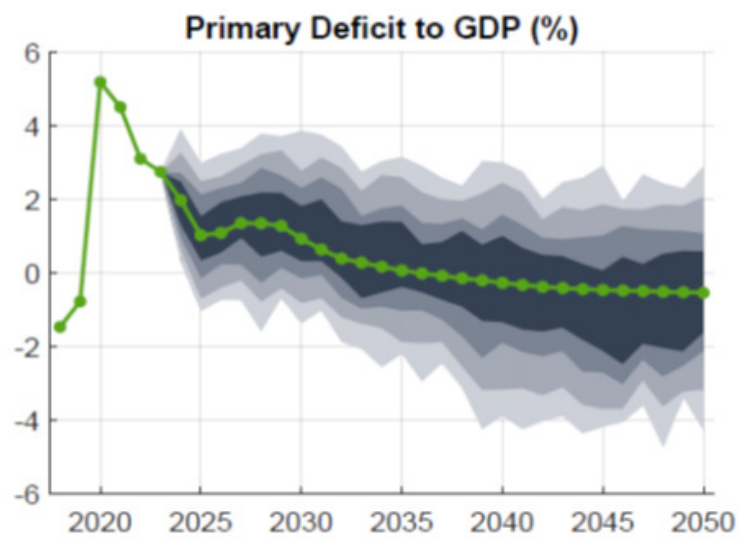


Figure 3: Primary Deficit to GDP Ratio [%]

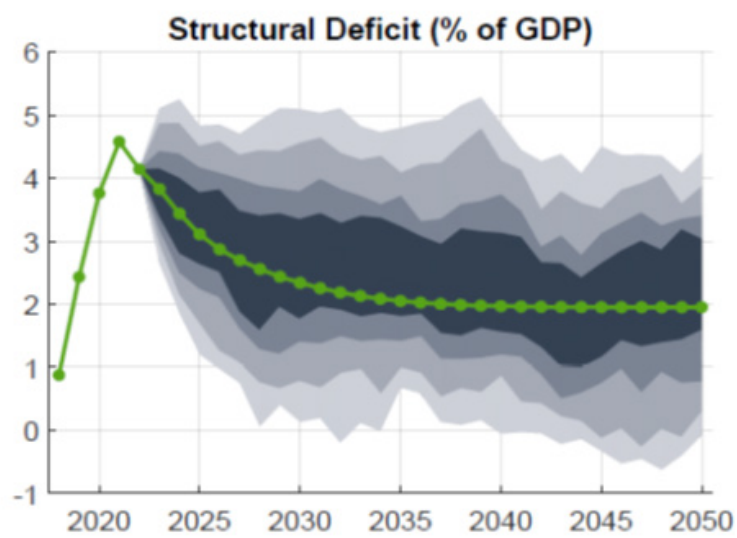


Figure 4: Structural Deficit to GDP Ratio [%]

Interest costs and debt-servicing expenditures are projected to rise gradually (see Fig. 5), driven by both the increasing stock of public debt and a normalization of interest rates from the historically low levels observed between 2010 and 2019. The probability distribution of future interest costs is skewed to the upside, reflecting risks associated with higher debt levels and potential adverse interest rate shocks.

Government bond yields are expected to increase relative to their 10-year historical average, and the yield curve is projected to revert to a standard upward-sloping shape with a positive term premium. Country and currency risk premia are assumed to remain broadly in line with their historical averages.

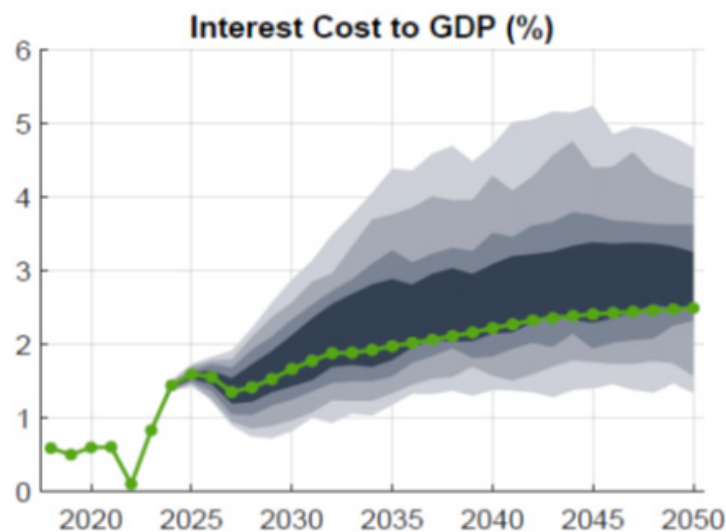


Figure 5: Interest Cost to GDP Ratio [%]

The macroeconomic outlook remains stable and broadly aligned with long-term fundamentals. Real GDP growth (see Fig. 6) is projected to average around 2% annually, while nominal GDP growth (Fig. 7) is expected to hover near 4%, consistent with stable inflation anchored at the Czech National Bank's official target. The nominal exchange rate (Fig. 8) is anticipated to appreciate by approximately 1.7% per year over the long run, supported by productivity growth comparable to that observed over the past two decades.

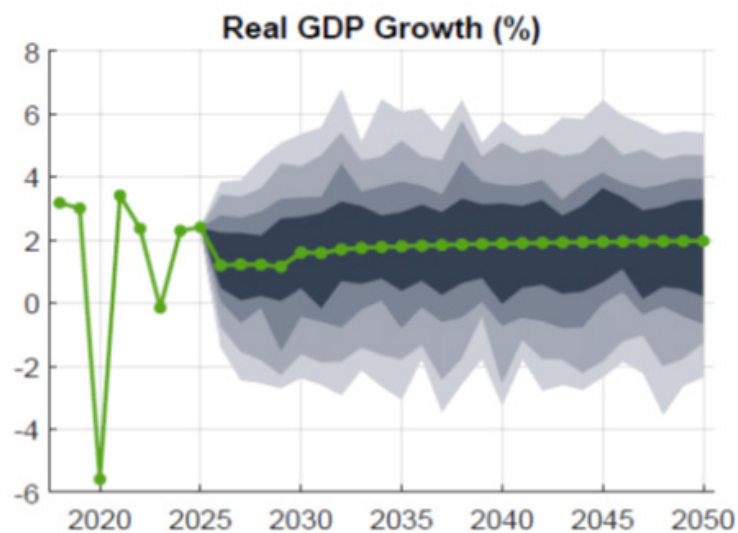


Figure 6: Real GDP Growth Rate [%]

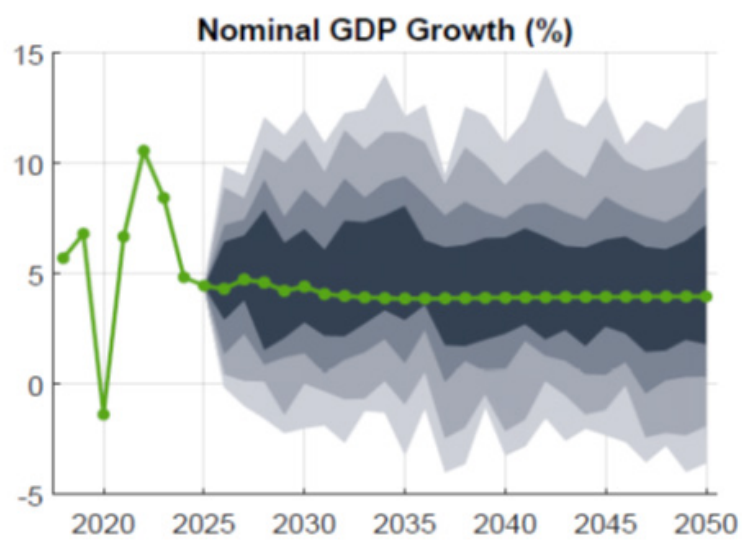


Figure 7: Nominal GDP Growth Rate [%]

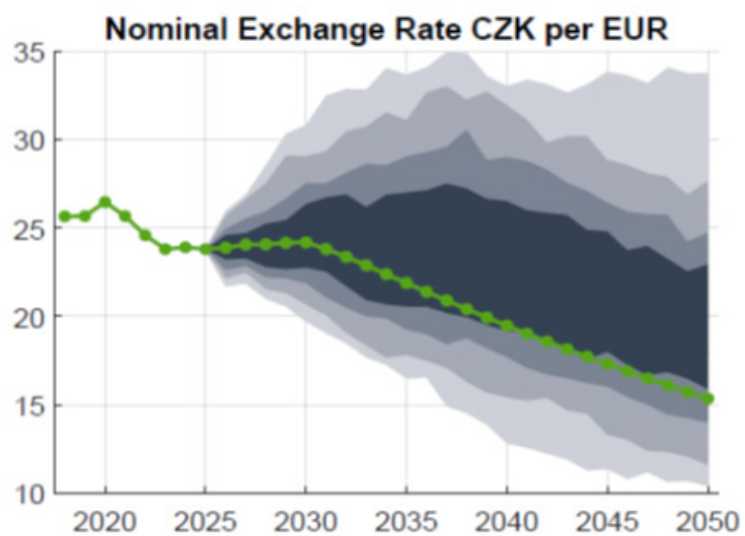


Figure 8: Nominal Exchange Rate [CZK/EUR]

We expect interest rates on government securities (see Fig. 9) to remain elevated compared to the average observed over the past decade, reflecting the anticipated normalization of global monetary conditions. These higher interest rates are likely to significantly influence the future composition of public debt, altering the patterns observed in recent years. The government yield curve is projected to revert to a conventional upward-sloping shape with a positive term premium. Both the country risk premium and the currency risk premium are assumed to remain close to their historical averages.

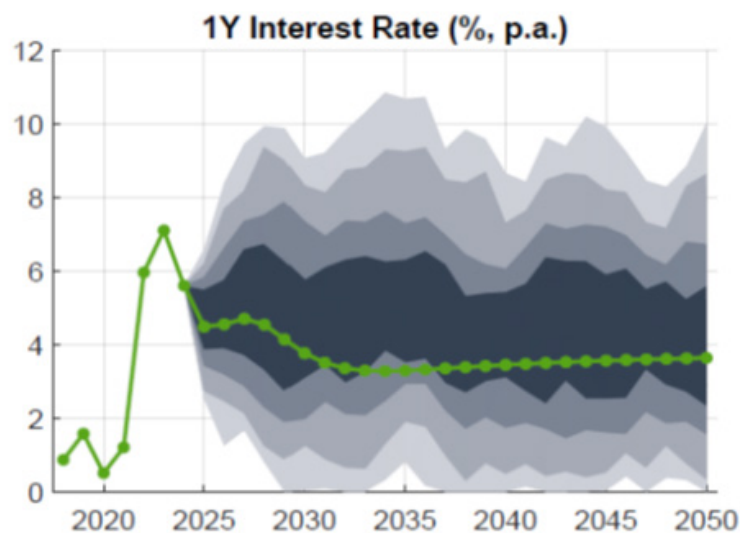


Figure 9: 1Y Interest Rate on Government Bonds [% p.a.]

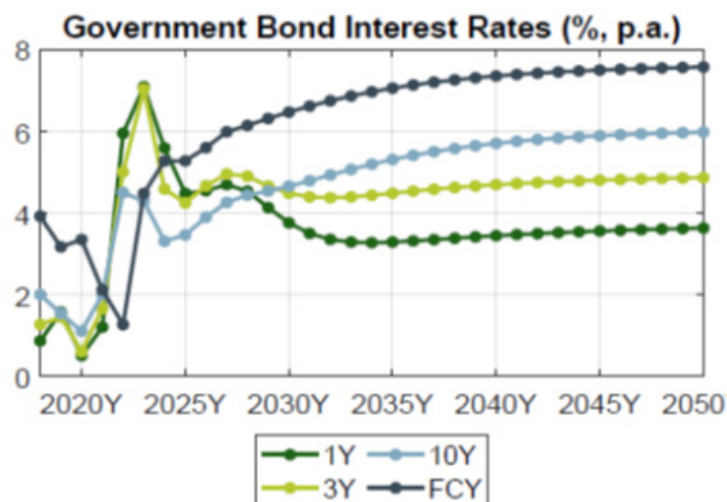


Figure 10: Government Bonds Interest rates [% p.a.]

Given the relatively high initial cost of foreign-currency (FCY) debt, domestic Treasury bonds are expected to remain the primary instrument for public debt financing. In the early years of the projection, lower yields on short-term (1Y–3Y) domestic bonds (see Fig. 10) are likely to increase their share in the overall debt structure. Over the longer term, gradual appreciation of the koruna is expected to reduce the effective cost of FCY

borrowing, leading to a moderate rise in the share of FCY-denominated debt toward the end of the projection horizon (see Fig. 11).

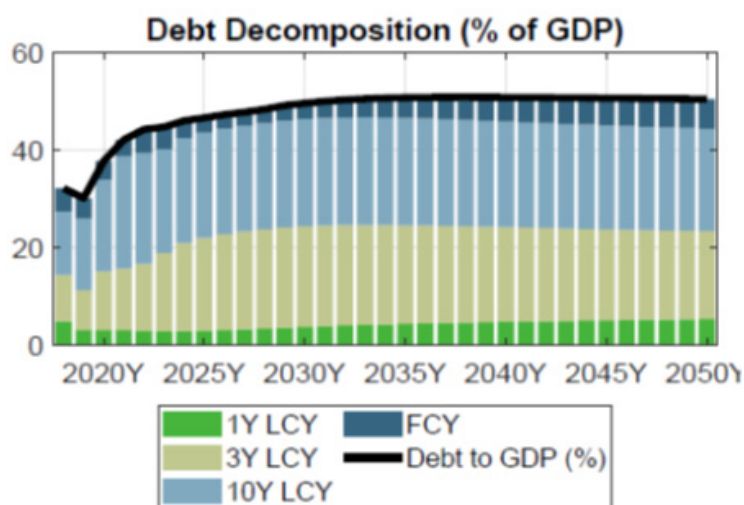


Figure 11: Debt Decomposition to GDP Ratio [%]

4. Baseline Scenario: Implications of Unambitious Fiscal Consolidation and Comparison with the Czech Fiscal Council Scenario

This section compares our baseline projection with the forecast of the Czech Fiscal Council (NRR) and analyzes the differences in the projected trajectories of key fiscal variables. The objective is twofold. First, we highlight how reliance on ad hoc exogenous assumptions—such as fixed interest rates or risk premia—can result in internally inconsistent predictions. Concretely, while our baseline scenario assumes a relatively neutral and unambitious consolidation path, and the NRR projection anticipates a much more adverse debt trajectory, the projected government interest costs remain nearly identical in both scenarios up to 2040.

Second, we replicate the sharp deterioration in the primary balance assumed in the NRR baseline by embedding it within our model framework. We show that this path can be generated endogenously through two distinct mechanisms: (i) as a result of ad hoc fiscal shocks to the actual government deficit, or (ii) as the consequence of a persistent structural shift in fiscal policy, reflected in the structural deficit. In both cases, the internally consistent structure of our model reveals that the resulting government interest costs—determined endogenously through market responses—exceed those in the NRR projection. Moreover, these higher interest costs are accompanied by broader macroeconomic instability, including persistently higher inflation and exchange rate depreciation.

4.1 Comparing the Baseline with Czech Fiscal Council (NRR) Scenarios

Our model's baseline assumes a moderate consolidation path, resulting in the stabilization of public debt at around 50% of GDP. In contrast, the Czech Fiscal Council's (NRR) forecast projects an exponential increase in public debt over the long term – see Figure 12. This divergence is primarily driven by significantly different assumptions regarding the evolution of the government's primary balance after 2030 – see Figure 13. While the NRR anticipates a steady deterioration of the primary balance, our model-based projection implies a gradual improvement, returning to levels observed in the post-financial crisis period – see Figure 14.

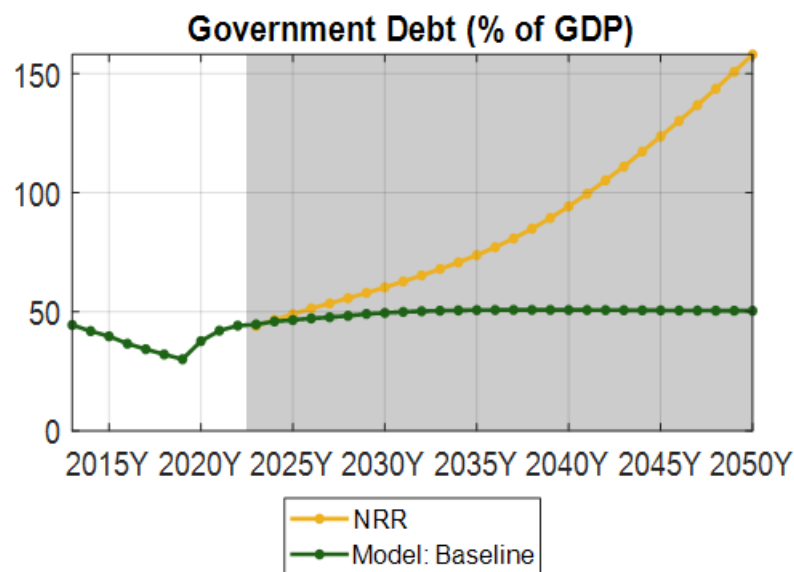


Figure 12: Government Debt to GDP Ratio [%]

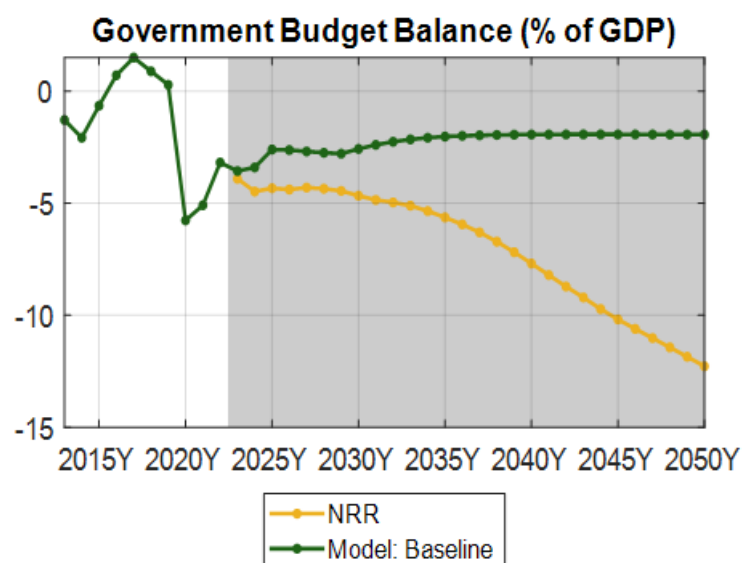


Figure 13: Government Budget Balance to GDP Ratio [%]

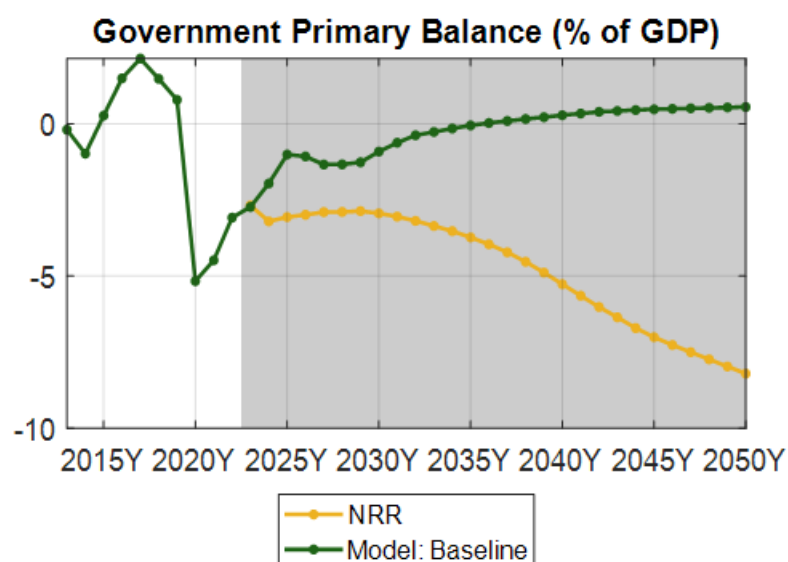


Figure 14: Government Primary Deficit to GDP Ratio [%]

Although the NRR expects significantly higher primary deficits starting as early as 2024, the corresponding increase in interest costs is delayed in their forecast and becomes pronounced only after 2040 – see Figure 15. This implies an implicit assumption that the risk premium on Czech sovereign debt will remain low despite deteriorating fiscal fundamentals. In contrast, our model—which endogenizes the risk premium—shows that maintaining such high primary deficits would result in a sharp and earlier increase in interest costs over time.

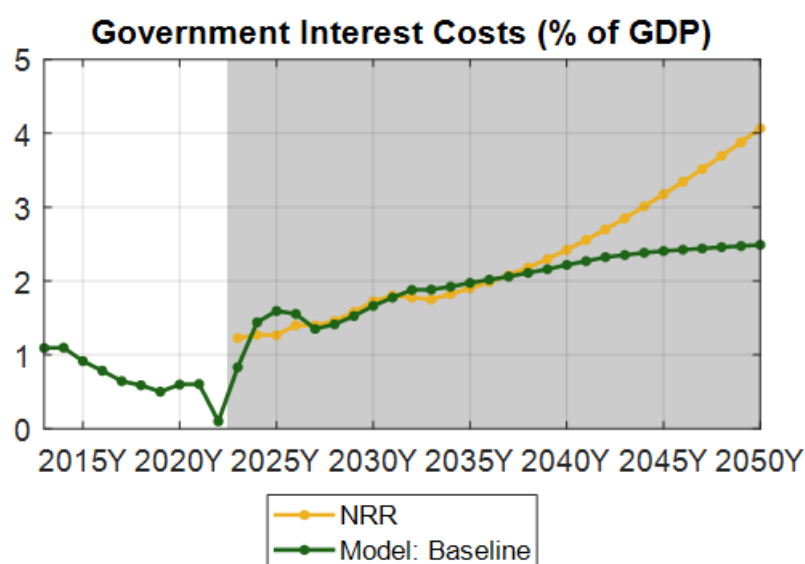


Figure 15: Government Interests Costs to GDP Ratio [%]

The discrepancy between the two projections becomes evident when examining the total budget balances: our model indicates a more stable fiscal trajectory, while the NRR baseline scenario implies unsustainable deficits in the absence of structural adjustments or improved financing conditions. Our projections also show modestly higher long-term

real and nominal GDP growth, partly reflecting greater macroeconomic stability and lower risk premia – see Figures 16 and 17.

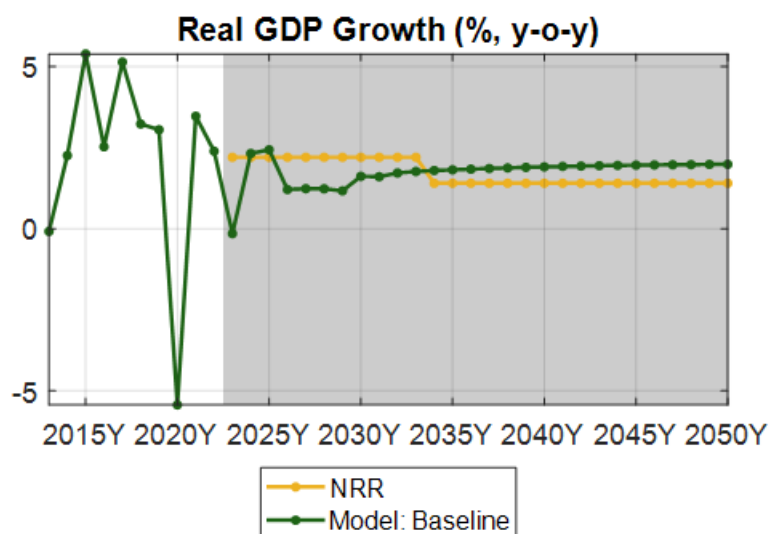


Figure 16: Real GDP Growth Rate [%]

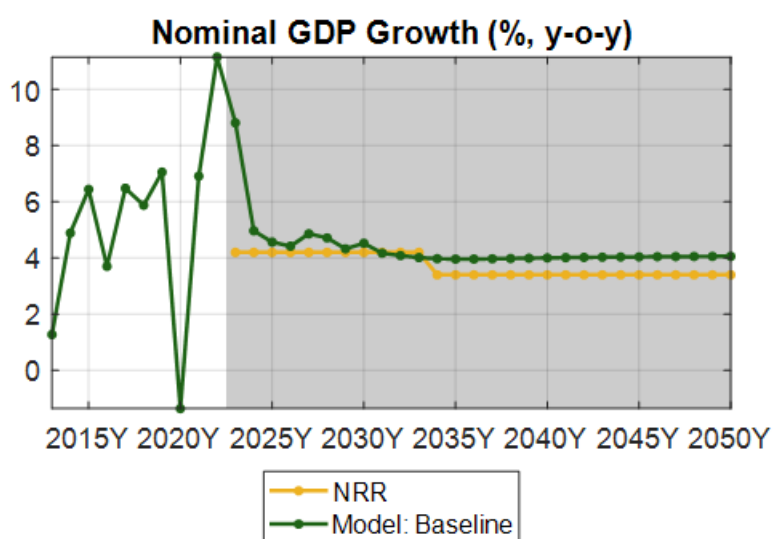


Figure 17: Nominal GDP Growth Rate [%]

4.2 Implications of Czech Fiscal Council Scenarios Through the Lens of Our Model

To assess the internal consistency of the NRR scenario, we simulate two additional cases in which the primary balance is exogenously fixed to follow the path projected by the Czech Fiscal Council. In the first case, we interpret this trajectory as the result of discretionary changes to the overall government deficit. In the second, we attribute it to persistent shifts in structural budget policy. Both scenarios are evaluated using our stock-flow-consistent macro-fiscal model – see Figure 18.

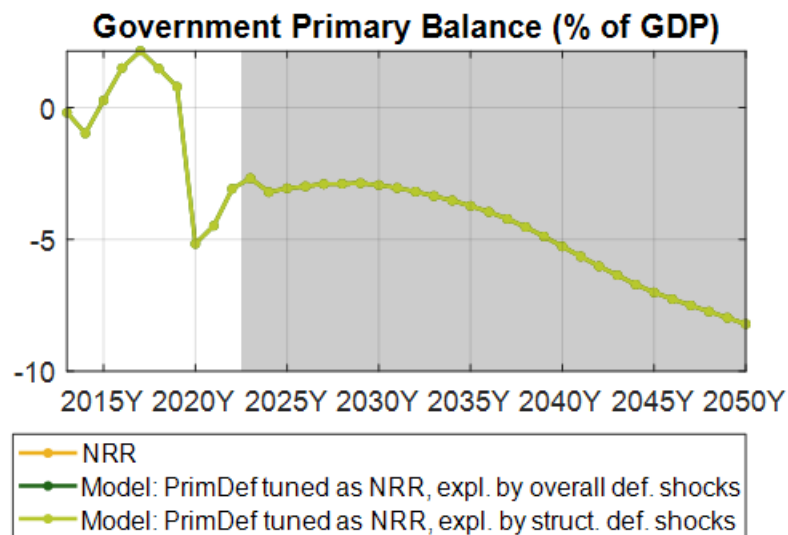


Figure 18: Government Primary Balance to GDP Ratio [%]

In both model-consistent simulations, the large primary deficits lead to an explosive path for public debt, surpassing 100% of GDP by 2050 – Figure 19. Importantly, these scenarios also generate unsustainable interest costs—well above those shown in the NRR baseline—unless one assumes an improbable, permanent drop in the country risk premium – Figure 20. Under either interpretation, the NRR scenario appears fiscally untenable when evaluated through a forward-looking, general equilibrium framework.

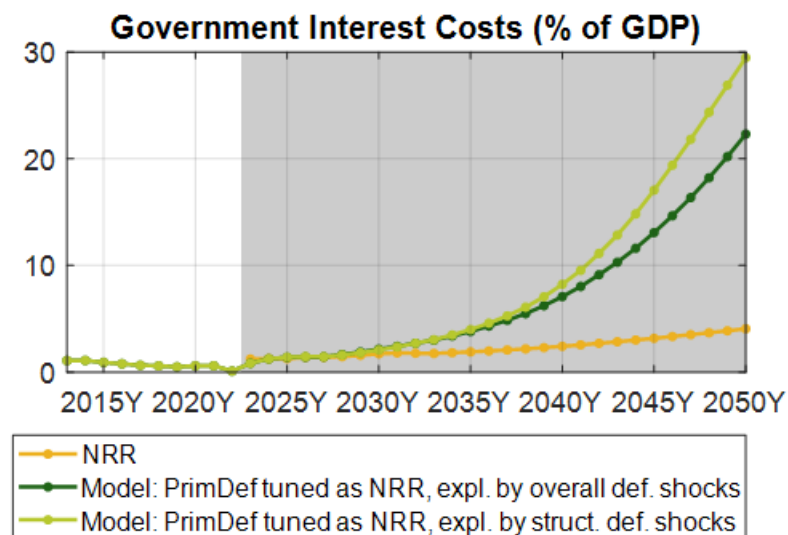


Figure 19: Government Interest Costs to GDP Ratio [%]

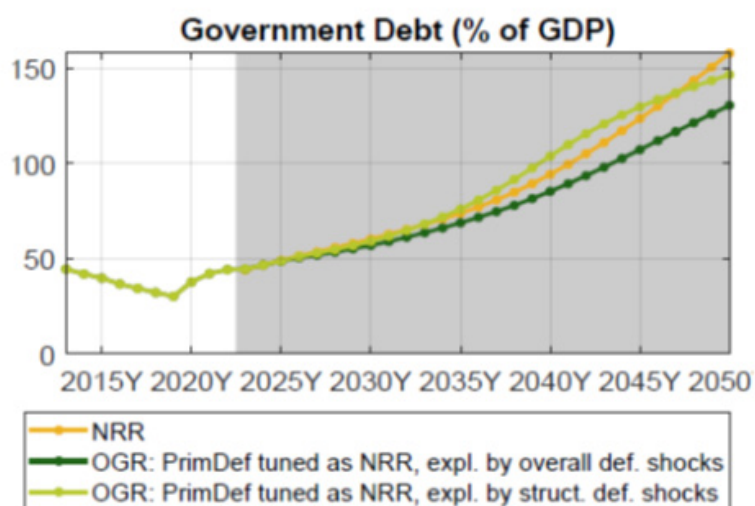


Figure 20: Government Debt to GDP Ratio [%]

Such large interest rate costs would push the total budget balance to unsustainable levels even further than the NRR forecast, represent a major threat to macroeconomic stability – see Figure 21. Our simulations show inflation persistently rising, exceeding 20% by 2050 – see Figure 22. Moreover, the exchange rate depreciates substantially in contrast to the baseline scenario, which assumes a mild appreciation driven by real productivity gains – Figure 23.

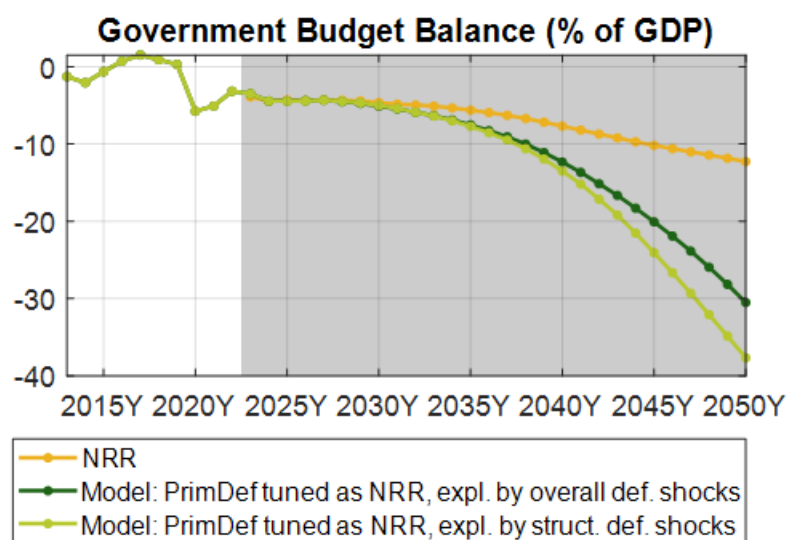


Figure 21: Government Budget Balance to GDP Ratio [%]

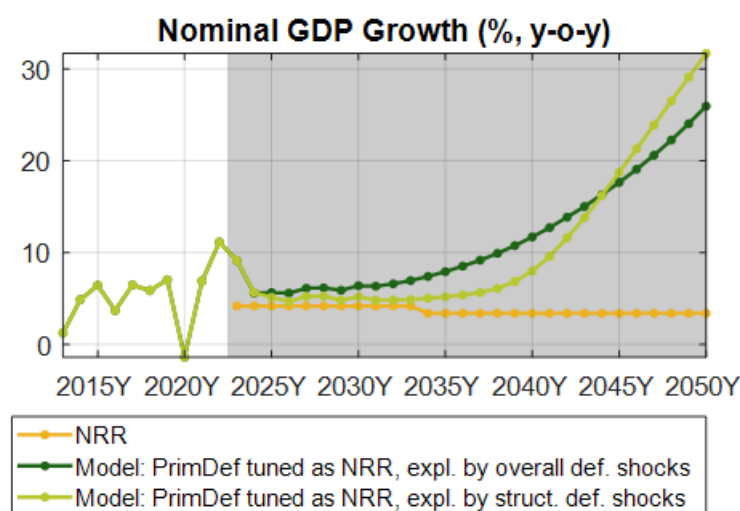


Figure 22: Nominal GDP Growth rate [%]

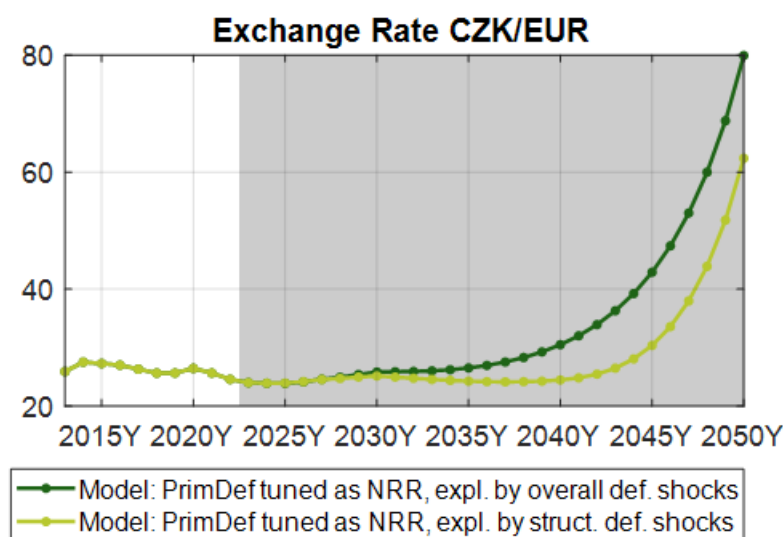


Figure 23: Exchange Rate [CZK/Euro]

These results underscore the importance of using internally consistent models to evaluate the consequences of fiscal policy choices. By failing to account for endogenous responses in interest rates and risk premia, deterministic projections—such as those by the NRR—may significantly understate the risks associated with prolonged fiscal imbalances.

5. Seemingly Overambitious Consolidation Toward a 30% Debt Target

This section presents an alternative scenario that explores the macro-fiscal implications of pursuing a more ambitious fiscal consolidation strategy—one that gradually reduces the government debt-to-GDP ratio to 30%, compared to the 50% target in the baseline (see Figure 24). This target roughly corresponds to the Czech Republic’s historical average and

reflects a return to debt levels consistent with prudent fiscal policy prior to the post-2020 debt accumulation.

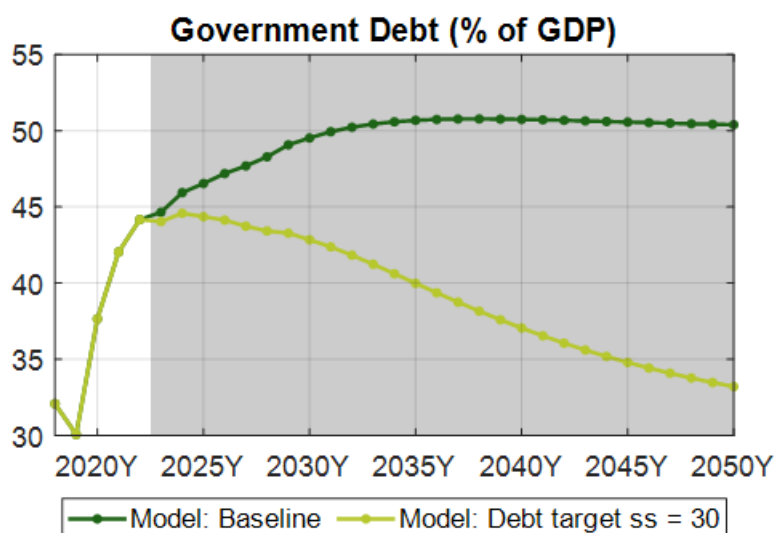


Figure 24: Government Debt to GDP Ratio [%]

The primary objective of this exercise is to assess whether more ambitious consolidation would necessarily come at the cost of lower output growth. Simulations demonstrate that such a consolidation strategy does not necessarily lead to lower output growth. On the contrary, lower debt levels reduce sovereign risk premia and interest costs, thereby supporting long-term macroeconomic stability and allowing real GDP growth to remain unaffected or even slightly improved.

The 30% debt target scenario assumes an immediate improvement in fiscal discipline, with the primary deficit narrowing relative to the baseline – see Figure 25. This is achieved through a gradual adjustment in the structural balance over the next ten years, returning to the average levels observed prior to the COVID-19 pandemic – see Figure 26. The resulting budget balance improves by approximately 1 percentage point of GDP compared to the baseline, while maintaining realistic assumptions about revenue and expenditure dynamics – Figure 27.

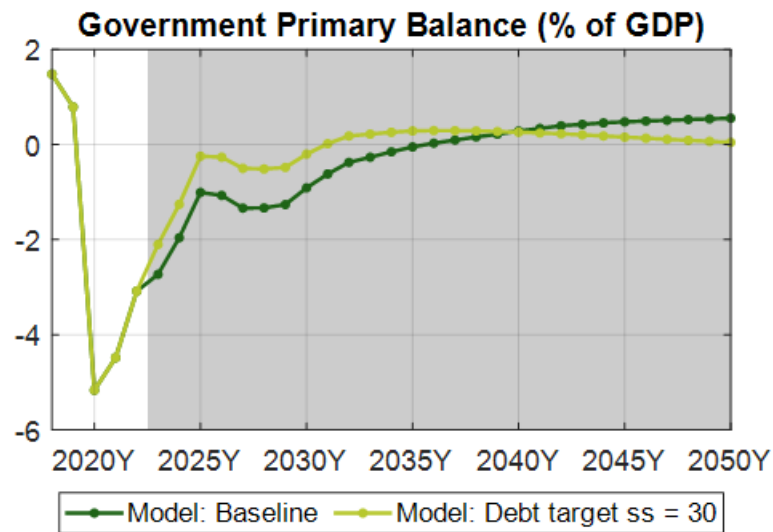


Figure 25: Government Primary Balance to GDP Ratio [%]

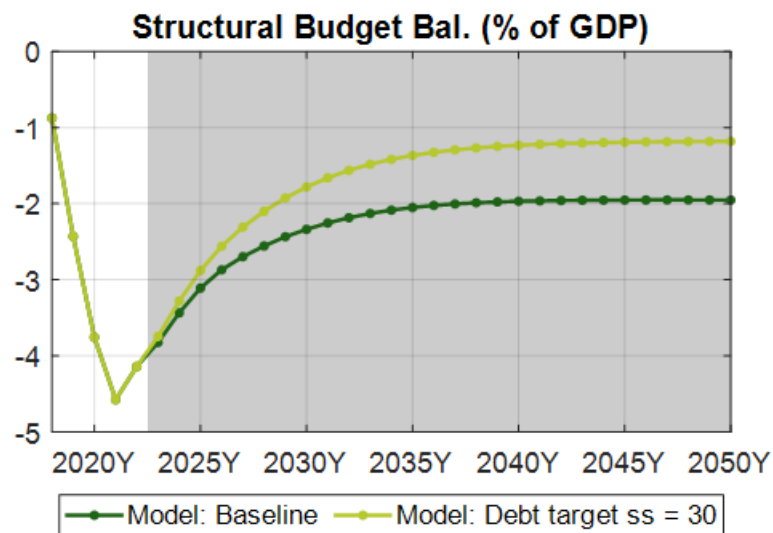


Figure 26: Structural Budget Balance to GDP Ratio [%]

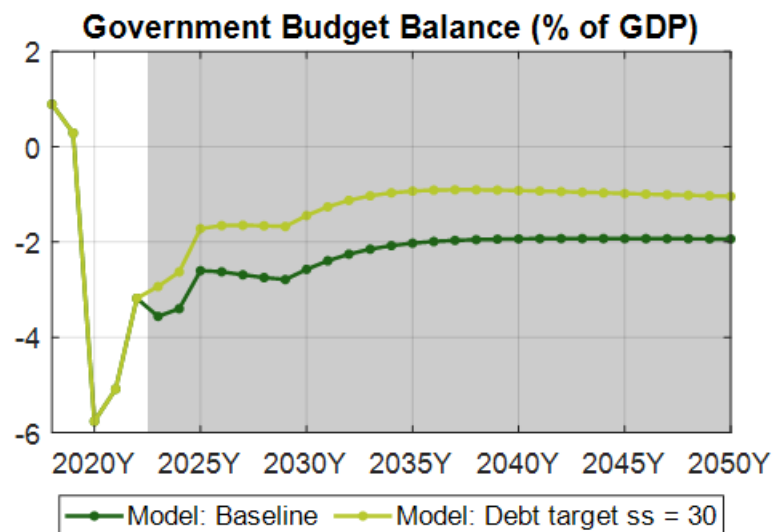


Figure 27: Government Budget Balance to GDP Ratio [%]

Despite the more aggressive fiscal consolidation, the model shows no adverse effects on GDP growth—see Figure 28. Lower debt burdens reduce interest costs from an average of 2% of GDP in the baseline to just 1.2% of GDP in the 30% debt target scenario—see Figure 29. These savings translate into a more favorable budgetary position and lower fiscal stress indicators, including a reduced probability of breaching the 55% debt ceiling and a smaller cumulative output loss relative to trend.

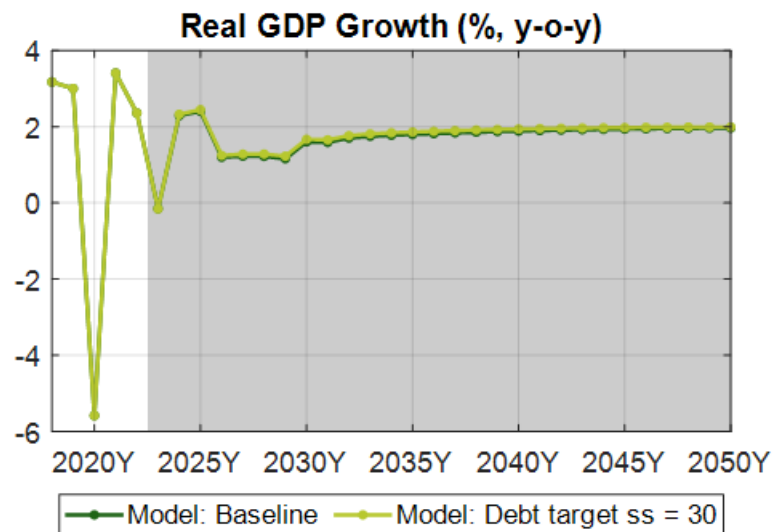


Figure 28: Real GDP Growth Rate [%]

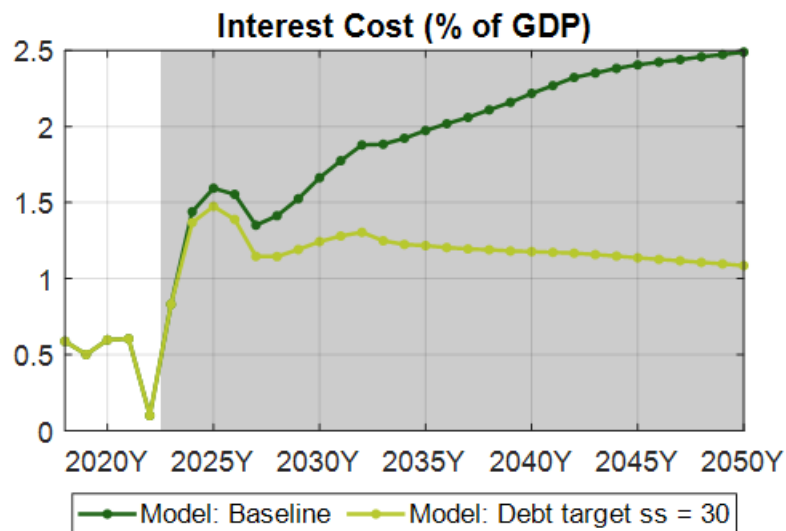


Figure 29: Government Interest Costs to GDP Ratio [%]

In summary, the results suggest that ambitious consolidation, if implemented gradually and credibly, can deliver fiscal sustainability gains without compromising economic growth. It improves resilience to future shocks and lowers the structural risks associated with high public debt levels—ultimately enabling a more stable macroeconomic environment.

6. Conclusion and Policy Implications

The first key conclusion highlights the importance of the model's general equilibrium structure. By design, all simulated variables are jointly consistent with macroeconomic identities, external projections, and the behavioral responses of key economic agents. This internal consistency is essential for evaluating the feasibility and risks of alternative fiscal consolidation strategies under uncertainty, as it avoids the internally inconsistent assumptions often found in deterministic frameworks.

We also show that projections which disregard the inevitable link between persistent primary deficits and rising interest costs can lead to misleading conclusions. Maintaining such deficits would detach debt-servicing costs from sustainable levels—unless one assumes a substantial and permanent structural decline in the country risk premium. In the current environment of tightening global financial conditions, such an assumption is implausible. Our model, through its endogenous treatment of risk premia and interest rates, captures these dynamics explicitly and demonstrates that such fiscal paths would lead to unsustainable debt trajectories.

Overall, the results underscore the need for realistic fiscal assumptions and highlight the advantages of forward-looking, stock-flow-consistent models for policy analysis. Overly optimistic scenarios that assume benign financing conditions despite deteriorating fiscal fundamentals risk providing misleading policy guidance. By contrast, timely and credible fiscal consolidation reduces sovereign risk premia, stabilizes debt dynamics, and enhances fiscal resilience.

References:

- Bańkowski, K. (2023). *Fiscal Policy in the Semi-Structural Model ECB-BASE*. ECB Working Paper Series No. 2802, European Central Bank.
- Bankowski, K., Christoffel, K., & Faria, T. (2021). *Assessing the Fiscal-Monetary Policy Mix in the Euro Area*. ECB Working Paper Series No. 2623, European Central Bank.
- Debrun, X., & Kinda, T. (2017). *Strengthening Post-Crisis Fiscal Credibility: Fiscal Councils on the Rise – A New Dataset*. *Fiscal Studies*, 38(4).
- Kameník, O., Šmídová, Z., Tůma, Z., & Vávra, D. (2013). *A Simple Fiscal Stress Testing Model: Case Studies of Austrian, Czech and German Economies*. OECD Working Paper No. 1074.
- Leeper, E. M. (2010). *Monetary Science, Fiscal Alchemy*. NBER Working Paper No. 16510, National Bureau of Economic Research.
- Národní rozpočtová rada (2024). *Zpráva o dlouhodobé udržitelnosti veřejných finance 2023*. Fiscal Council Report.