# Macro note – Central Government Budget Balance

**In February, budget and primary balance post a deficit of TRY 310.1 billion and TRY 170.4 billion, respectively. Personnel expenditures and current transfers remain flat compared to the previous month, while procurement of goods and capital expenditures increase significantly.**

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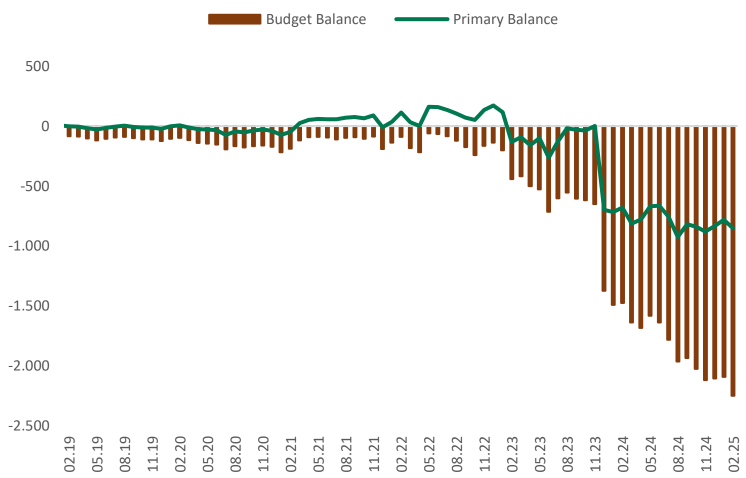
According to the February central government budget data released by the Ministry of Treasury and Finance, budget revenues and budget expenditures were realized as TRY 723.4 billion and TRY 1,033.5 billion, respectively. In the same period, non-interest budget expenditures were realized as TRY 893.8 billion. Accordingly, THE budget deficit was realized as TRY 310.1 billion while the primary balance posted a deficit of TRY 170.4 billion. The first thing that strikes the eye in February's figures is that austerity policies have fallen short of the desired level. Expenditures for the purchase of goods and services increased by TRY 14 billion compared to January.  On the other hand, the monthly increase in capital expenditures is TRY 37 billion and TRY 26.5 billion in capital transfers. These increases were overshadowed by the TRY 12 billion in lending expenditures, which in turn was overshadowed by the calm course of personnel and current expenditures in February. Transfers to the Electricity Generation Co. amounted to TRY 22.9 billion in February (TRY 14.1 billion in the previous month). The coordination of monetary and fiscal policies in the fight against inflation was emphasized. We estimate that the contribution of monetary policy to disinflation has been limited and fiscal policy has a greater role to play. In particular, the additional contribution to inflation from public expenditures makes the job of monetary policy more difficult. Regulations from administered prices have a sticky effect on inflation. If budget revenues are not increased, which means additional taxes, the budget deficit could spiral out of control. On the other hand, these measures have the potential to create new inflationary pressure. It is a double dilemma and a vicious circle. The most reasonable way to control the budget without fueling inflation seems to be to cut expenditures. The changes in the pension system, the earthquake disaster and continued high inflation are the key items limiting the budget recovery. We remind readers that fiscal policy has yet to reach the desired level of tightness, and additional pressure on inflation may come from the budget deficit. We believe that monetary policy alone will take time to bring price stability in the current conjuncture and fiscal policy should be emphasized. Budget expenditures increased by 49.8% yoy. The highest proportional increases were recorded in capital transfers (1,398%) and interest expenditures (154.8%), while current transfers (TRY 111 billion) and interest expenditures (TRY 85 billion) posted the highest increases. The average annual increase in budget revenues was 34.9%. The highest increases were recorded in income tax (89.2%) and bank/insurance transaction tax (101.9%). Income tax and SCT made the highest contribution to budget revenues (TRY 131.5 billion and TRY 126 billion, respectively). When the rates of increase are evaluated together, the chronic course of the budget deficit, regardless of the amount, can be easily seen.

**Graph 1: Budget and Primary Balance (12m rolling, Billion TL)**




Deviation of the budget balance from the 2% budget deficit/GDP target, the anchor of fiscal discipline, is a consequence of external shocks as well as elections. To achieve the pre-2022 performance, some structural transformations seem imperative. A revenues policy that can compensate for the increase in expenditures triggered by inflation and the earthquake disaster has not yet been established. In our previous reports we have noted that fiscal policy has additional duties in an environment where monetary policy has been tight for a long time. While some expenditure-cutting measures have been taken, the rhetoric that the fiscal discipline anchor will be effectively implemented keeps expectations about medium-term targets alive. In this sense, we find the recent fiscal measures limitedly positive. Personnel expenditures, which have increased especially due to inflation, cannot be compensated without cuts in other budget items. Another alternative is to generate additional tax revenues, and these practices have increased recently. It was inevitable that the deteriorating inflation outlook, especially as a result of monetary policy, would eventually spill over into other macro indicators. Fiscal discipline has long had a negative outlook due to both inflation and high expenditures. Although tax collections have improved due to seasonal effects, the overall trend continues to deteriorate. In this context, the decisive implementation of the recent austerity measures is critical for the stability of fiscal policy. Although the inflation level has been brought down to 30% thanks to monetary policy, the structural breaks after this point will require additional measures beyond monetary policy. In this context, fiscal policy has a serious role to play. If revenue collection remains weak, the year-end budget deficit may exceed forecasts. Although monetary policy-induced pressures on the budget have eased, the impact of inflation will persist for some time. We anticipate that the budget performance and fiscal discipline outlook of the pre-Covid period can be achieved by 2025-2026.

In sum, the budget posted a deficit of TRY 310.1 billion and the primary balance TRY 170.4 billion in February. Despite the calm course in personnel and current expenditures, capital and goods expenditures fueled the budget deficit. When the increase in the purchase of goods and services and the expenditures item are evaluated together, we see that the austerity measures in the public sector are not at the targeted level. We are going through a period in which past preferences in monetary policy have hindered the discipline in public finance. Considering the current realizations, we estimate that the budget deficit/GDP level will be realized at around 4.8%. Under the anchor of fiscal discipline, this deficit has hovered around 1.5-2.5%. A tightening of fiscal policy in coordination with monetary policy will contribute to fiscal discipline and price stability in the medium term. Policies to increase the efficiency of tax revenues and to restrict expenditures will bring about sustainability in budget discipline. We continue to expect that the budget outlook will gradually reach levels consistent with price stability starting from 2025. We underline that transitions in the normalization process in economic policies may bring additional shocks and updates to our forecasts.

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