Macro note – Central Government Budget Balance

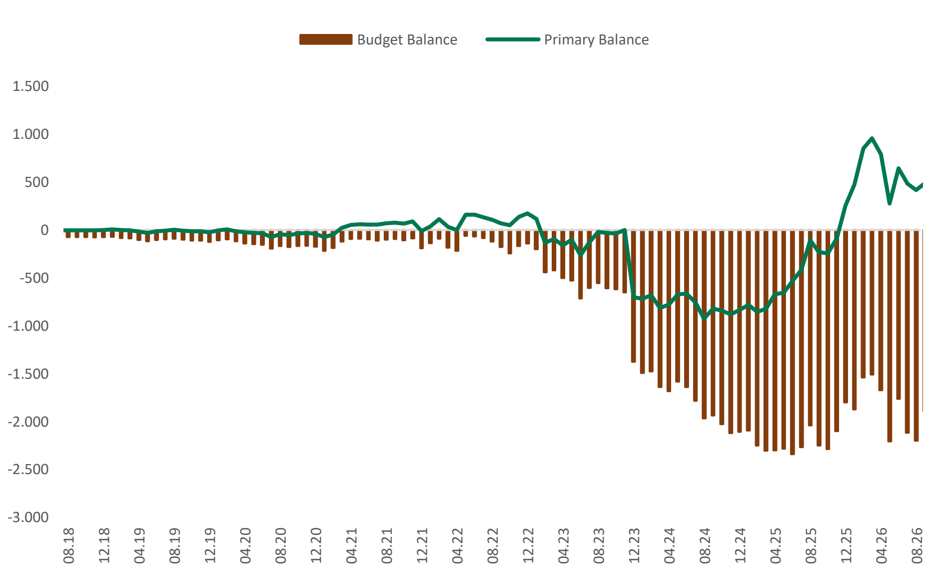
In August, the budget recorded a surplus of TRY 12.9 billion and the non-interest balance a surplus of TRY 209.9 billion. Whilst corporation tax is helping to shore up the budget, pressure from interest payments continues.

Abdulkadir DOGAN
Chief Economist
adogan@sekeryatirim.com.tr
(+90) 212 334 33 33/313

According to the central government budget figures for August published by the Ministry of Treasury and Finance, budget revenue stood at TRY 1,654.9 billion, whilst budget expenditure amounted to TRY 1,642 billion. During the same period, non-interest budget expenditure totaled TRY 1,144.5 billion. Based on these figures, the budget recorded a surplus of TRY 12.9 billion and the non-interest balance showed a surplus of TRY 209.9 billion. Whilst corporate tax was the key factor driving the budget surplus in August, expenditure items continued to trend at a near-flat level. Current transfers resulted in expenditure of TRY 600 billion due to a base effect, whilst tax revenues were sufficient to offset this increase. The rise in staff costs resulting from the inflation adjustment was an expected effect. Following this adjustment, we can state that staff costs will stabilize at around TRY 450 billion. However, when interest expenditure is excluded—with the exception of January and July—it has stabilized at an average of TRY 200 billion. There has been no significant increase in capital expenditure or transfers. When adjusted for the impact of interest rates, the performance of the core budget balance is consistent with the fiscal discipline anchor. In this context, we can say that the anchoring of inflation expectations and the decline in interest expenditure have been a prerequisite for the performance of the budget balance. The point we emphasize here is that there has been no deterioration in fiscal policy regarding tax collection or expenditure policies. However, the inflationary impact created by monetary policy—which increases expenditure by at least as much as inflation and generates high interest expenditure due to borrowing costs—is triggering the budget deficit. Therefore, as we have highlighted in our previous reports, positive developments in monetary policy and the disinflation process will also bring about improvements in fiscal policy. Revenue policy and collection continue to follow a flat trend. Despite a limited decline in tax revenues, there has been a broad-based improvement in revenue performance throughout the year. Consequently, the fundamental improvement that will restore fiscal discipline to the budget will result from improvements in expenditure items. We believe this will be achieved not so much through fiscal policy as through improvements in monetary policy and inflation expectations. Assuming the disinflation process continues resolutely in the second half of the year, several possibilities come to the fore. Foremost among these are the adjustments to administered/guided prices, as highlighted in the latest inflation report. Regulations in areas that regulate tax revenues—such as healthcare, transport and fuel—reflect the lagged effects of inflation. It is clear that this will have a positive impact on budget performance. The second possibility is that inflation will remain within the 28–30 per cent range by the end of the year, with no significant improvement from current levels. This effect necessitates that both monetary and fiscal policy maintain a tight stance for some time to come. The final and least likely scenario is a shift towards an ‘election economy’ and a one-off easing of fiscal policy. In this case, a marked rise in personnel and pension expenditure would be observed. To finance this, price increases and tax adjustments across expenditure categories may be introduced. Once these temporary effects are stripped out, we maintain our base scenario that the budget will converge towards the fiscal discipline benchmark in the 2027–2028 period, in line with the decline in inflation.

Looking at the details of the rates of change in the budget's revenue/expenditure balance, budget expenditure in July increased by 37.8 per cent compared with the same period of the previous year. The highest proportional increases were observed in capital transfers (556.3 per cent) and lending expenditure (99.8 per cent), whilst the largest expenditure items were current transfers (TRY 624.7 billion) and staff costs (TRY 430 billion). The average annual increase in budget revenue stands at 28.5 per cent. The highest increases were observed in the revenue of regulatory and supervisory bodies (54 per cent) and stamp duty (50.6 per cent). The sub-categories contributing most significantly to budget revenue were income tax and corporation tax (TRY 351 billion and TRY 403 billion respectively).

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



In summary, the budget recorded a surplus of TRY 12.9 billion and the non-interest balance a surplus of TRY 209.9 billion in August. The increase in corporation tax contributed to the budget surplus. On the other hand, the persistently high level of borrowing costs is exerting significant negative pressure on budget performance beyond 2023. Any falls in nominal interest rates will have a markedly positive impact on fiscal discipline in the 2027–2028 period. As monetary policy works to achieve disinflation, falling interest rates will also contribute to fiscal discipline. The increased risks regarding the global debt burden and borrowing costs in recent times have once again highlighted the importance of efficiency in public finances. A shift in fiscal policy towards a tightening stance, in coordination with monetary policy, will contribute to fiscal discipline and price stability in the medium term. Policies aimed at enhancing the efficiency of tax revenues and restricting expenditure will also ensure the continuity of budgetary discipline. We would like to emphasize that the transitions involved in the normalization process of economic policy may bring about additional shocks and necessitate updates to our forecasts.

ŞEKER INVEST RESEARCH

Şeker Yatırım Menkul Değerler A.Ş.
Buyukdere Cad. No: 171 Metrocity
A Blok Kat 4-5 34330 SİSLİ /IST
TURKEY

TEL: +90 (212) 334 33 33
Fax: +90 (212) 334 33 34
E-mail: research@sekeryatirim.com
Web: http://www.sekeryatirim.com/english/index.aspx

For additional information, please contact:

Research

Kadir Tezeller	Head	+90 (212) 334 33 81	ktezeller@sekeryatirim.com.tr
Burak Demirbilek	Utilities	+90 (212) 334 33 33-128	bdemirbilek@sekeryatirim.com.tr
Atasav Can Tuglu	Food & Beverages, Automotive, Retail, Aviation	+90 (212) 334 33 33-334	atuglu@sekeryatirim.com.tr
Basak Kamber	Glass, Pharmaceutical, Defense, Telcos, Cons. Dur.	+90 (212) 334 33 33-251	bkamber@sekeryatirim.com.tr
M. Mucahid Yıldırım	Banking	+90 (212) 334 33 33-150	myildirim@sekeryatirim.com.tr
Yusuf Kemal Erdekli	Cement, Conglomerates, Real Estate	+90 (212) 334 33 33-115	yerdekli@sekeryatirim.com.tr
O. Furkan Ozdemir	Iron & Steel, Oil- Gas & Deriv.	+90 (212) 334 33 33-245	oozdemir@sekeryatirim.com.tr

Economy & Politics

Abdulkadir Dogan	Chief Economist	+90 (212) 334 91 04	adogan@sekeryatirim.com.tr

Institutional Sales

Deniz Keskin	Trader	+90 (212) 334 33 36	dkeskin@sekeryatirim.com.tr

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