

6. Public Finance

In the second half of 2012, growth of tax revenues decelerated relatively due to the slowdown in the economic activity and interest payments surged owing to the maturity structure of the debt stock, thus weighing on the budget performance. Tax revenues will continue to be collected as per the Law No. 6111 on the restructuring of public claims in 2012, albeit posting a year-on-year decline. SCT rate hikes to some products under the fiscal measures enforced in October 2011, as well as the expected decline in the quarterly rate of increase in interest payments in the subsequent months will contribute to the improvement in the budget performance in 2012. On the other hand, possible decline in tax revenues amid a potential slowdown in the economic activity in 2012 besides a lower-than-targeted privatization revenues and upside risks to public expenditures, especially to personnel expenditures, may adversely affect the budget performance. Thus, it should be emphasized that in order to ensure sustainability of the favorable fiscal outlook as well as the fiscal discipline, reinforcement of the fiscal framework through institutional and structural improvements envisaged in the MTP remains critical.

6.1. Budget Developments

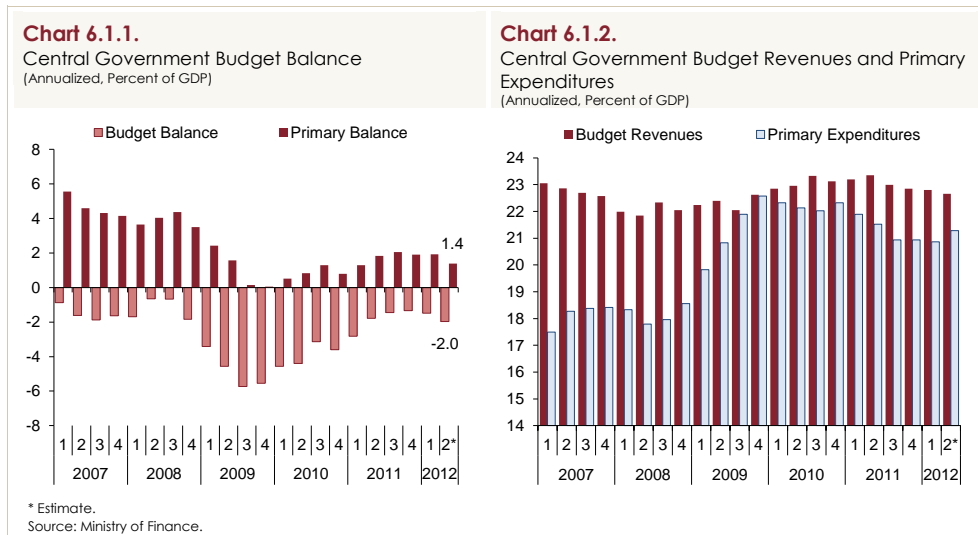
Central government budget posted a deficit of TL 6.7 billion, while primary balance recorded a surplus of TL 19.6 billion in the first half of 2012 (Table 6.1.1). The increase in interest expenditures by 17 percent was mainly influential on the year-on-year deterioration in the budget performance. Meanwhile, non-tax revenues surged owing to the profit transfer by the CBRT, thus compensating for the deterioration in the budget performance. On the other hand, the quarterly increase in interest expenditures is associated with the maturity structure of the debt stock, and is anticipated to slow down in the following months. Moreover, in the first half of the year, growth of tax revenues remained relatively subdued due to the deceleration in the economic activity, while primary budget revenues continued to increase mildly.

Table 6.1.1.
Central Government Budget Aggregates
(Billion TL)

	January-June 2011	January-June 2012	Rate of Increase (Percent)	Actual/Target (Percent)
Central Government Budget Expenditures	143.2	168.9	17.9	48.1
Interest Expenditures	22.4	26.3	17.0	52.3
Primary Expenditures	120.8	142.6	18.1	47.4
Central Government Budget Revenues	146.1	162.2	11.0	49.2
I. Tax Revenues	122.7	131.2	6.9	47.2
II. Non-Tax Revenues	18.5	24.9	35.1	56.6
Budget Balance	2.9	-6.7	-	31.8
Primary Balance	25.3	19.6	-22.7	67.1

Source: Ministry of Finance.

The central government budget balance to GDP, which displayed a year-on-year improvement in 2011 on the back of the favorable budget outturn, deteriorated moderately in the first half of 2012 due to falling budget revenues amid the slowdown in economic activity. Having worsened in the last quarter of 2011 amid rapidly soaring primary expenditures, the central government primary balance to GDP deteriorated further in the second quarter of 2012 (Chart 6.1.1). Central government budget revenues posted a modest year-on-year decline in 2011 and remained virtually unchanged from end-2011 in the second quarter of 2012, while central government primary expenditures to GDP has edged up since end-2011 (Chart 6.1.2).



Central government primary expenditures posted a year-on-year growth by 18.1 percent in the January-June period of 2012. Current transfers and personnel expenditures, which are major components of the primary expenditures, were up 21.3 percent and 19 percent, respectively, while expenditures on goods and services declined by 0.4 percent, mainly on the back of the dramatic fall in health expenditures due to the coverage of green

card holders under the general health insurance plan. Meanwhile, expenditures within the general health insurance plan are a component of current transfers, not a sub-item of the purchases of goods and services. Accordingly, health, pension and social benefits, the major component of current transfers, went up by 26.5 percent following the amendment to the coverage of the health insurance, contributing to the increase in current transfer expenditures. The rise in personnel expenditures in the first half of 2012 was mainly driven by the surge in salaries and severance pay. Capital expenditures increased relatively mildly by 6.1 percent, whereas capital transfers went down by 36.3 percent due to the decline in infrastructural rural support project and other capital transfer items (Table 6.1.2).

Table 6.1.2.
Central Government Primary Expenditures
(Billion TL)

	January-June 2011	January-June 2012	Rate of Increase (Percent)	Actual/Target (Percent)
Primary Expenditures	120.8	142.6	18.1	47.4
1. Personnel Expenditures	36.8	43.8	19.0	53.6
2. Government Premiums to SSI	6.3	7.3	15.3	51.3
3. Purchase of Goods and Services	12.4	12.3	-0.4	42.8
a) Defense and Security	3.5	3.8	8.4	35.9
b) Health Expenditures	2.6	0.4	-85.0	42.4
4. Current Transfers	55.0	66.7	21.3	51.2
a) Duty Losses	0.9	0.9	1.0	19.9
b) Health, Pension and Social Benefits	27.2	34.4	26.5	49.7
c) Agricultural Support	5.5	6.3	13.1	87.1
d) Shares Reserved from Revenues	14.6	16.7	14.3	49.3
5. Capital Expenditures	6.8	7.2	6.1	25.9
6. Capital Transfers	1.7	1.1	-36.3	26.0

Source: Ministry of Finance.

Central government general budget revenues posted a year-on-year increase by 10.6 percent in the first half of 2012. Meanwhile, tax revenues and non-tax revenues soared by 6.9 percent and 35.1 percent, respectively due to the profit transfer by the CBRT (Table 6.1.3). Corporate taxes surged in the first five months of 2012 amid soaring profits owing to high growth in 2011, while increasing only mildly in the first half of the year by 3.8 percent owing to the base effect in June due to the Law No. 6111 on the restructuring of public claims. The income tax revenues increased by 15.7 percent on the back of the ongoing increase in registered employment. This has partially compensated for the deceleration in total tax revenues amid the relative slowdown in the growth of indirect taxes. On the other hand, the rate of increase in consumption-based taxes went down due to the slowdown in economic activity. In the first half of 2012, SCT revenues increased by 4.5 percent, while domestic VAT revenues edged up by 1.7 percent. The slowdown in the growth of SCT revenues mainly

stemmed from the year-on-year decline in SCT collection on oil and natural gas products, as well motor vehicles. In the meantime, amid the slowdown in domestic demand, VAT revenues on imports registered a decline by 0.3 percent, remaining well below the growth rate by 34.5 percent in 2011.

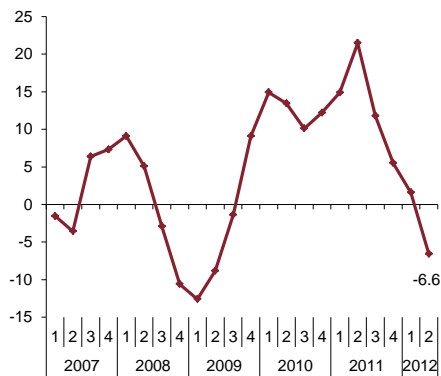
Table 6.1.3.
Central Government General Budget Revenues
(Billion TL)

	January-June 2011	January-June 2012	Rate of Increase (Percent)	Actual/Target (Percent)
General Budget Revenues	141,2	156,1	10,6	48,5
I-Tax Revenues	122,7	131,2	6,9	47,2
Income Tax	23,2	26,8	15,7	49,8
Corporate Tax	13,9	14,4	3,8	53,0
Domestic VAT	15,1	15,4	1,7	45,8
SCT	29,8	31,3	5,4	44,4
VAT on Imports	23,3	23,3	0,3	43,3
II-Non-Tax Revenues	18,5	24,9	35,1	56,6
Enterprises and Property Revenues	6,0	10,9	82,2	117,9
Interests, Shares and Fines	9,9	10,2	3,7	46,7
Capital Revenues	1,8	1,4	-24,7	12,2

Source: Ministry of Finance.

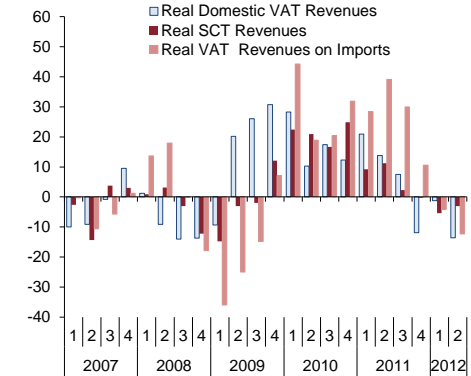
Having decelerated since the third quarter of 2011, annual growth of real tax revenues turned negative for first time in a 10-quarter period amid the slowdown in the economic activity as well as the base effect, and posted a 6.6 percent decline in the second quarter of 2012 (Chart 6.1.3). Consumption-based tax revenues are the primary tax revenue items which are adversely affected by the slowdown in the economic activity. Accordingly, in the second quarter of 2012, SCT revenues, a major component of the tax revenues, fell by 3.1 percent year-on-year in real terms, while domestic VAT revenues and VAT revenues on imports posted a year-on-year decline by 13.6 percent and 12.3 percent, respectively, in real terms (Chart 6.1.4).

Chart 6.1.3.
Real Tax Revenues
(Annual Percent Change)



Source: Ministry of Finance.

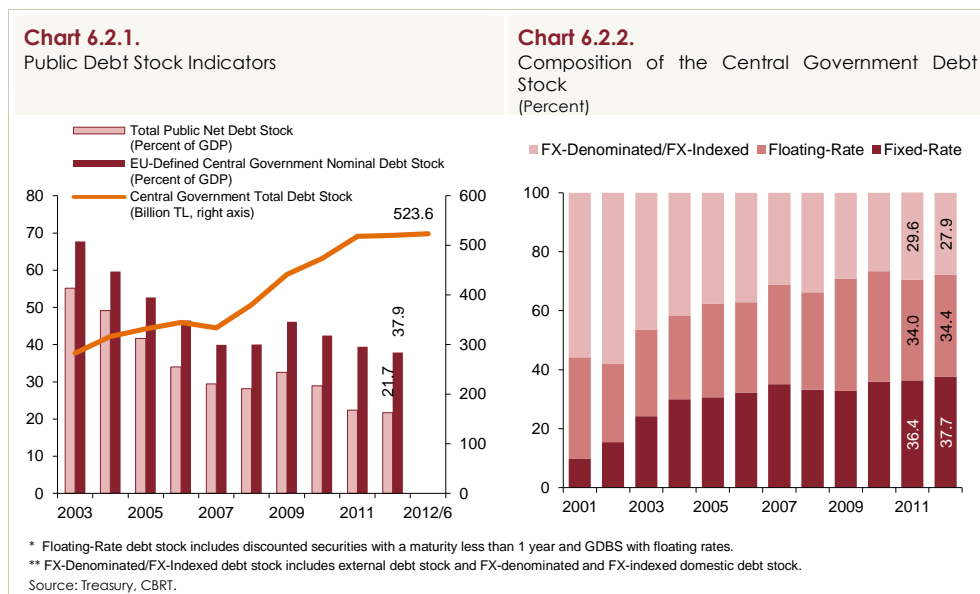
Chart 6.1.4.
Real VAT and SCT Revenues
(Annual Percent Change)



6.2. Developments in the Debt Stock

Public debt stock indicators improved further in the second quarter of 2012. Public debt rates continued to decrease and the real cost of borrowing remained low. Meanwhile, the average maturity of the debt stock was extended, the share of interest and exchange-rate-sensitive securities in the debt stock declined and domestic debt rollover ratio went down.

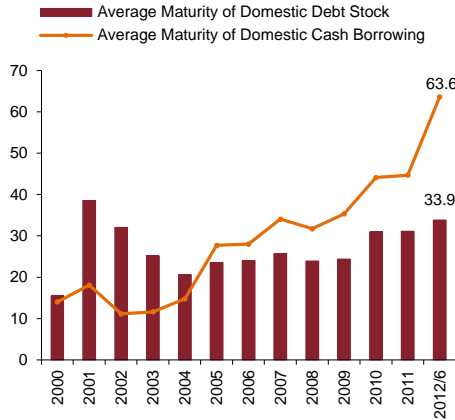
The ratio of total public net debt stock and EU-defined general government nominal debt stock to GDP posted a year-on-year decline by 0.7 points and 1.5 percentage points, to 21.7 percent and 37.9 percent, respectively, in the first quarter of 2012 (Chart 6.2.1). Meanwhile, the central government debt stock remained unchanged in June 2012 from end-2011 (Chart 6.2.1).



As of June 2012, the Treasury has maintained its borrowing strategy to alleviate the sensitivity of the debt stock to liquidity, interest rate and exchange rate. Accordingly, the share of fixed-rate securities increased in the total debt stock (Chart 6.2.2). The ratio of public deposits to the average monthly debt service reached 249.7 percent. Term-to-maturity of the domestic debt stock hit 33.9 months amid the marked year-on-year increase in the average maturity of the domestic cash borrowing (Chart 6.2.3). External borrowing by bond issues amounted to USD 4.6 billion, with the average maturity remaining unchanged since 2011 (Chart 6.2.4).

Chart 6.2.3.

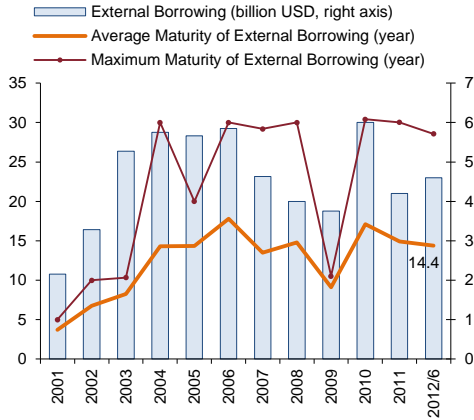
Average Maturity of Domestic Cash Borrowing and Term-to-Maturity of the Domestic Debt Stock (Month)



Source: Treasury, CBRT.

Chart 6.2.4.

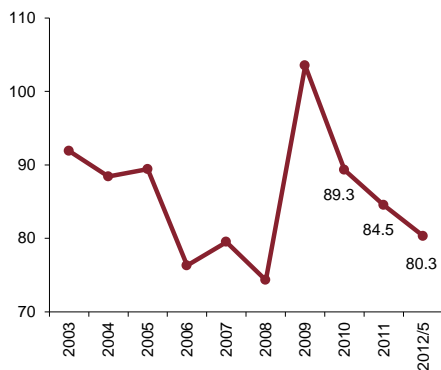
Borrowing By Bond Issue



Domestic debt rollover ratio stood at 80.3 percent at the end of the first five months of 2012 (Chart 6.2.5). However, according to the Treasury's announced strategy on domestic borrowing for July-September 2012 period, domestic debt rollover ratio is envisioned to reach 81.3 percent by end-September. Having plunged from early 2009 to the start of 2011, the average real interest rates at discount auctions remain currently low (Chart 6.2.6).

Chart 6.2.5.

Total Domestic Debt Rollover Ratio (Percent)



Source: Treasury, CBRT.

Chart 6.2.6.

Average Maturity of Borrowing and Interest Rates at Discount Auctions

