

6. Public Finance

As of the first half of 2014, the budget performance displayed a slight year-on-year deterioration, mostly due to the upsurge in primary expenditures and the slowdown in domestic demand driven tax revenues that became more significant in the second quarter. The favorable course of tax revenues in the first quarter is believed to be the result of early-2014 tax hikes, exchange rate and price movements and advance spending on consumption goods before the adoption of macroprudential measures to restrict domestic demand. On the other hand, the rate of increase in tax revenues slowed slightly in the second quarter. Meanwhile, the favorable performance of non-tax revenues is mainly attributed to temporary revenue items that are considered as one-offs.

With regard to the sustainability of the positive course of fiscal balances and to maintaining fiscal discipline on a permanent basis, it is critical that the fiscal policy be implemented in line with the MTP's framework and the primary expenditures be kept under control for the rest of the year.

6.1. Budget Developments

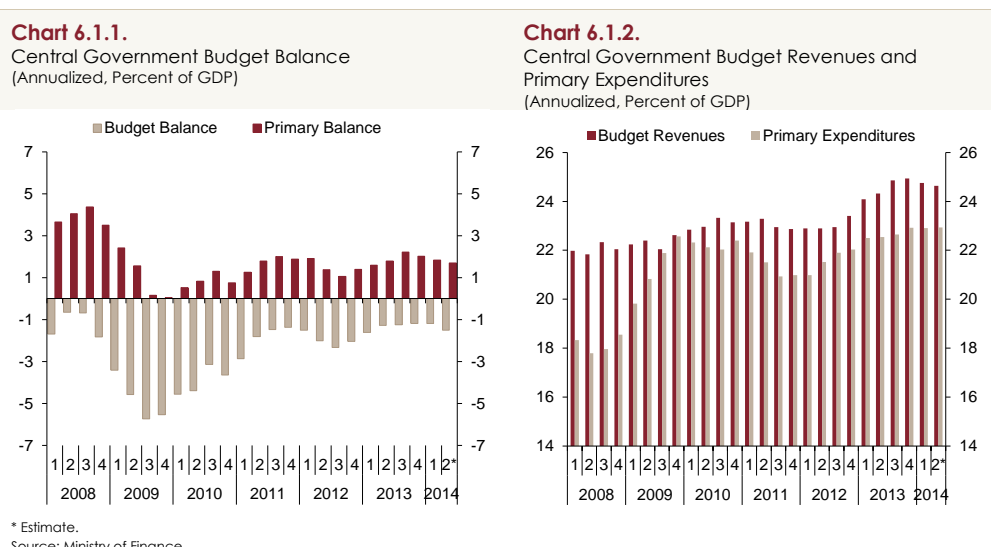
The central government budget posted a deficit of 3.4 billion TL, while the primary budget registered a surplus of 23.1 billion TL in the first half of 2014 (Table 6.1.1). Tax revenues were on track with the year-end target, while primary expenditures continued to rise dramatically.

Table 6.1.1.
Central Government Budget Aggregates
(Billion TL)

	January-June 2013	January-June 2014	Rate of Increase (Percent)	Actual/Target (Percent)	Targeted Annual Rate of Increase (Percent)
Central Government Budget Expenditures	187.9	213.9	13.8	49.0	7.0
Interest Expenditures	23.3	26.5	13.6	50.9	4.0
Primary Expenditures	164.6	187.4	13.9	48.7	7.4
Central Government Budget Revenues	190.9	210.5	10.2	52.2	3.5
I. Tax Revenues	158.4	168.1	6.1	48.3	6.8
II. Non-Tax Revenues	26.2	34.1	30.3	76.5	-10.8
Budget Balance	3.1	-3.4	-	10.1	-
Primary Balance	26.4	23.1	-12.4	123.2	-

Source: Ministry of Finance.

The central government budget deficit to GDP ratio, which declined to 1.2 percent in 2013 amid the favorable budget performance, is estimated to increase slightly to 1.5 percent in the first half of 2014 (Chart 6.1.1). Meanwhile, the primary budget surplus to GDP ratio assumed an upward course after declining to 1.1 percent in the third quarter of 2012. This ratio, which hit 2 percent at end-2013, is estimated to decline slightly to 1.7 percent in the first half of 2014.



Having surged significantly since 2012 and reaching 22.9 percent at end-2013, the central government primary expenditures to GDP ratio is estimated to remain elevated also in the first half of 2014 (Chart 6.1.2). On the other hand, the central government budget revenues to GDP ratio increased upon robust economic activity as well as tax adjustments in September 2012 and January 2013, reaching 24.9 percent at end-2013. The ratio is estimated to decline to 24.6 percent in the first half of 2014, mainly due to slowing tax revenues based on domestic demand.

The central government primary budget expenditures, which started to surge as of the second half of 2012, increased further in the first half of 2014. Accordingly, the central government primary budget expenditures registered a year-on-year increase of 13.9 percent in this period (Table 6.1.2).

During January-June 2014, current transfers, personnel expenditures and purchase of goods and services, which are major items in primary expenditures, registered an increase of 10.1, 16.5 and 14 percent, respectively. The relatively smaller increase in current transfers restricted the rise in primary budget expenditures to some degree. Personnel expenditures and public investment expenditures (capital expenditures and transfers) were the main drivers of the rapid increase in primary expenditures. On the other hand, most of the upsurge in lending resulted from the rise in loans extended to SEEs.

Table 6.1.2.

Central Government Primary Expenditures (Billion TL)

	January-June 2013	January-June 2014	Rate of Increase (Percent)	Actual/Target (Percent)
Primary Expenditures	164.6	187.4	13.9	48.7
1. Personnel Expenditures	49.0	57.0	16.5	51.9
2. Government Premiums to SSI	8.1	9.6	18.7	50.8
3. Purchase of Goods and Services	13.3	15.2	14.0	40.5
4. Current Transfers	75.3	83.0	10.1	50.7
a) Duty Losses	1.4	1.5	6.5	35.4
b) Health, Pension and Social Benefits	36.5	39.9	9.2	51.8
c) Agricultural Support	6.8	6.8	0.9	70.5
d) Shares Reserved from Revenues	19.6	22.8	16.7	48.4
5. Capital Expenditures	12.0	13.9	16.2	37.9
6. Capital Transfers	2.2	2.7	22.7	41.5
7. Lending	4.7	6.0	27.6	78.3

Source: Ministry of Finance.

In the first half of 2014, the central government general budget revenues recorded a year-on-year increase of 9.6 percent (Table 6.1.3). In this period, tax revenues and non-tax revenues increased by 6.1 and 30.3 percent, respectively.

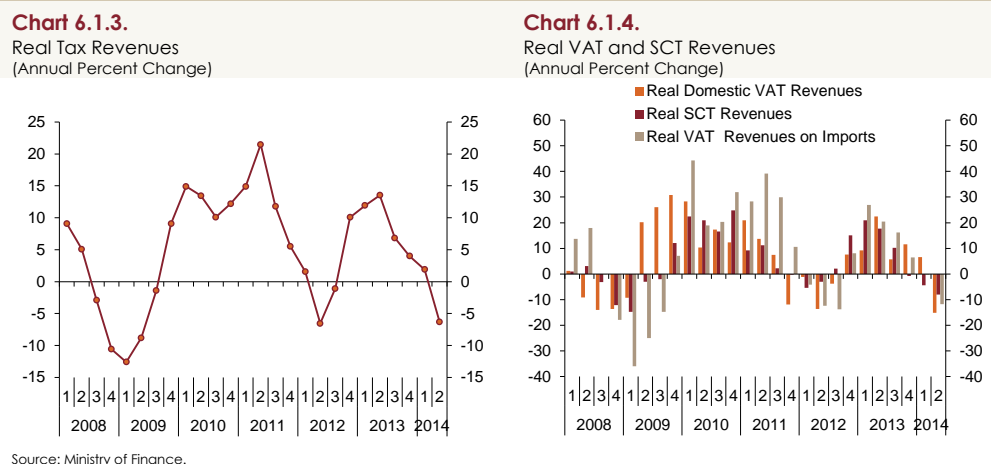
Table 6.1.3.
Central Government General Budget Revenues
(Billion TL)

	January-June 2013	January-June 2014	Rate of Increase (Percent)	Actual/Target (Percent)
General Budget Revenues	184.5	202.2	9.6	51.5
I-Tax Revenues	158.4	168.1	6.1	48.3
Income Tax	29.5	34.9	18.1	49.3
Corporate Tax	15.4	15.4	0.0	49.5
Domestic VAT	19.0	19.7	3.7	49.8
SCT	40.0	40.7	1.8	45.5
VAT on Imports	30.9	31.5	1.8	48.5
II-Non-Tax Revenues	26.2	34.1	30.3	76.5
Enterprises and Property Revenues	7.5	8.8	17.7	107.8
Interests, Shares and Fines	12.2	17.0	39.9	65.5
Capital Revenues	5.4	6.4	18.3	72.8

Source: Ministry of Finance.

A closer analysis of tax revenues reveals that income tax revenues displayed high-rated rises in the first half of 2014, and the rate of increase in tax revenues declined to 3.4 percent from 6.1 percent after excluding income tax. This is largely attributed to the slowdown in consumption-based tax collection. Among consumption-based tax revenues, domestic VAT revenues increased by 3.7 percent, while the rate of increase in SCT and import VAT revenues was merely 1.8 percent. The details of SCT revenues show a 13.3 and 8.4 percent increase in tax revenues on tobacco products and motor vehicles, respectively. On the other hand, tax revenues on petroleum and natural gas products, which account for a large share of SCT revenues, decreased by 5.2 percent.

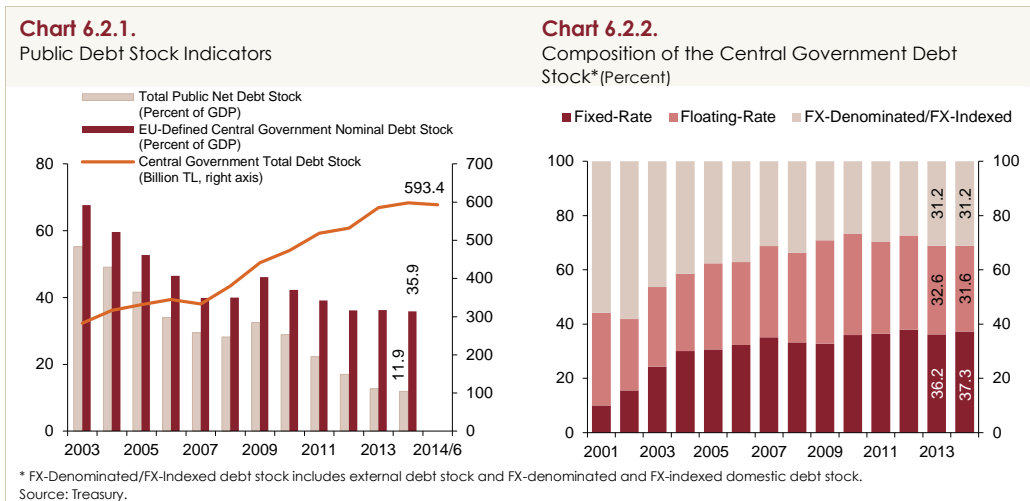
Having turned positive amid tax hikes in September 2012 as well as the base effect, the annual rate of increase in real tax revenues started to slacken in the second half of 2013. Real tax revenues dropped by 6.3 percent in the first half of 2014 due to the marked slowdown in domestic demand driven tax revenues (Chart 6.1.3). Among consumption-based tax revenues, domestic VAT, SCT and import VAT revenues decreased by 15.2, 8 and 11.8 percent in real terms, respectively, in the first half of 2014 (Chart 6.1.4).



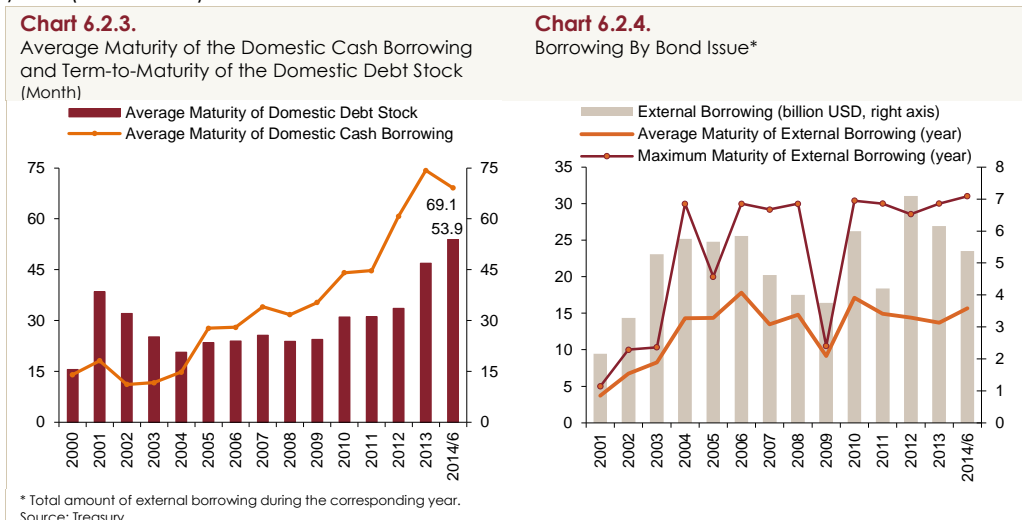
6.2. Developments in the Public Debt Stock

Public debt stock indicators displayed a favorable outlook in the first half of 2014. The total public net debt stock and the EU-defined nominal debt stock to GDP ratios continued to decline, the share of fixed-rate securities in the total debt stock increased, the average maturity of the debt stock extended and the real cost of borrowing remained low over the past three months.

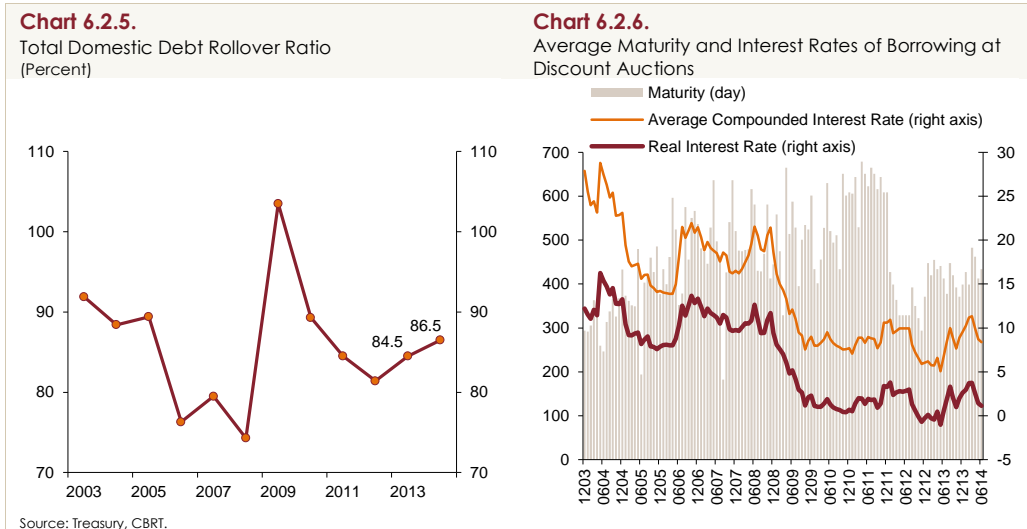
The central government debt stock stood at 593.4 billion TL as of end-June 2014 (Chart 6.2.1). In the first quarter of 2014, the total public net debt stock and the EU-defined nominal debt stock to GDP ratios decreased by 0.8 and 0.4 points, respectively, compared to end-2013 figures (Chart 6.2.1).



The share of fixed-rate securities in the total debt stock increased slightly from end-2013 (Chart 6.2.2). As for the interest and exchange rate structure of domestic borrowing, the share of fixed-rate borrowing registered a year-on-year decline in the first five months of 2014. The ratio of public deposits to average monthly debt service stands at 170.3 percent. The average term-to-maturity of the domestic debt stock rose to 53.9 months (Chart 6.2.3). Meanwhile, in the first six months of 2014, external borrowing by bond issues amounted to 5.4 billion USD, with the average maturity standing at 15.7 years (Chart 6.2.4).



The domestic debt rollover ratio stood at 86.5 percent at end-May 2014 (Chart 6.2.5). Having plummeted from early 2009 to early 2011, the average real interest rate¹ that had recently been on the rise due to global financial fluctuations and the cautious monetary policy stance recorded low levels in the past three months (Chart 6.2.6).



¹ Real interest rates are calculated by subtracting the 12-month-ahead CPI expectation of the CBRT Survey of Expectations from nominal interest rates (average annual compounded interest rate at the Treasury's TL-denominated zero-coupon securities auction).

