Macro note – Central Government Budget Balance

In October, budget and primary balance posts a deficit of 186.3 billion and 50 billion TRY, respectively. Despite the strong increase in personnel expenditures and current transfers, tax collections remains relatively low, triggering the negative trend in the budget deficit...

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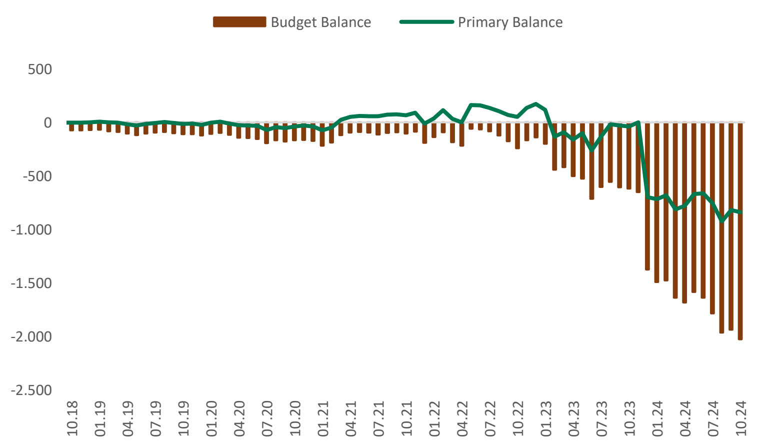
According to the October central government budget data released by the Ministry of Treasury and Finance, budget revenues and budget expenditures were realized as 769.3 billion TRY and 955.5 billion TRY, respectively. In the same period, non-interest budget expenditures were realized as 819.3 billion TRY. Accordingly, the budget deficit was realized as 1,86.3 billion TRY while the primary balance posted a deficit of 50 billion TRY. Considering the course of current transfers over the past three years, current levels indicate a 300% increase. The impact of inflation on the budget should not be overlooked here. However, if this trend continues, it will be almost impossible to maintain fiscal discipline in the budget. A tax collection policy that can cover the increase in personnel expenses and current transfers will be one of the most vital issues on the 2025 agenda. Changes to the pension system, the earthquake disaster and persistent inflation are adding to budgetary pressures. The twelve-month cumulative budget deficit has exceeded two trillion liras, about nine times the average of the past decade. The rigidity in budget expenditures despite the adjustments in tax collection, and increasing expenditures despite the measures taken have evolved into a chronic budget deficit. We would like to remind that the desired level of tightness in fiscal policy has not yet been achieved and additional pressure on inflation may come from the budget deficit. Having focused on monetary policy, the economic administration has recently increased its fiscal policy measures. 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 67.9% yoy. The highest proportional increases were in lending (123%) and interest (104%) expenditures, while the highest items were current transfers (350 billion TRY) and personnel expenditures (242 billion TRY). The average annual increase in budget revenues was 62.4%. The highest increases were in income tax (121%) and banking and insurance transactions tax (155%). Income and special consumption taxes made the highest contribution to budget revenues (160 billion TRY and 139 billion TRY, respectively).

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



When the ten months of the year are evaluated together, we see that fiscal policy has moved away from the long-standing anchor of fiscal discipline. A revenue policy that can compensate for the increase in expenditures triggered by inflation and the earthquake disaster has not yet been established. We have stated in our previous reports 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 past this point will need 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 the 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 186.3 billion TRY in October. The high course of personnel expenditures and current transfers points to a significant deficit in the budget when seasonal revenues are adjusted. We are going through a period in which past preferences in monetary policy have undermined the discipline in public finance. The year-end budget deficit will deviate significantly from the 2013-2023 averages. In the last quarter of the year, and especially in December, we may see a very high budget deficit due to the closure of accounting periods. 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 continuity in budget discipline. We continue to expect the budget outlook to gradually reach levels consistent with price stability starting from 2025. We underline here that transitions in the normalization process in economic policies may bring additional shocks and updates to our forecasts.

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