6. Public Finance

The central government budget balance posted a slight year-on-year deterioration in 2014, yet performed better than the target set in the budget period. This was mainly driven by tax revenues that are not a stable and permanent source of revenues. Tax revenues stood a little above the target, while primary expenditures maintained the high-rated increase that started in 2012 and increased above the target in 2014.

The MTP covering the 2015-2017 period envisages a fiscal policy that will reduce inflation as well as the current account deficit and raise domestic savings and growth potential in the upcoming period. Accordingly, it is projected that fiscal discipline led by tight fiscal policy practices will be sustained and the debt stock to GDP ratio will continue to taper off during the implementation of the MTP (Table 6.1). In addition, those policies, which may permanently raise the level of expenditures in the medium and long term by exploiting temporary sources of revenues, will be evaded. It is evaluated that the envisaged fiscal adjustment will be achieved, especially by keeping primary expenditures under control.

Table 6.1.
Central Government and General Government Budget Balance
(Percent of GDP)

	2013	2014*	2015**	2016**	2017**
Expenditures	26.1	25.4	24.3	23.6	22.8
Primary Expenditures	22.9	22.6	21.5	21.1	20.5
Interest Expenditures	3.2	2.8	2.8	2.5	2.3
Revenues	24.9	24.0	23.2	22.8	22.5
Tax Revenues	20.8	19.9	20..0	19.9	19.8
Other	4.1	4.1	3.2	2.9	2.8
Budget Balance	**-1.2**	**-1.4**	**-1.1**	**-0.7**	**-0.3**
Primary Balance	**2.0**	**1.5**	**1.7**	**1.8**	**2.0**
General Government Budget Balance	**-0.7**	**-0.8**	**-0.5**	**-0.2**	**0.1**
General Government Primary Balance	**2.6**	**2.2**	**2.4**	**2.4**	**2.5**
EU-Defined Nominal Debt Stock	**36.2**	**33.1**	**31.8**	**30.0**	**28.5**

* Estimate.
** MTP Target.
Source: MTP (2015-2017).

Efforts paid to achieve fiscal adjustment by slowing down primary expenditures during the implementation of the MTP are expected to underpin the CBRT's primary objective to maintain price stability and support macroeconomic stability. Thus, implementing fiscal policy in accordance with the MTP framework is critical. On the other hand, it should be emphasized that strengthening the fiscal framework by the institutional and structural improvements projected in the MTP remains to be of utmost importance for the sustainability of the fiscal discipline and the completion of the fiscal adjustment.

6.1. Budget Developments

The central government budget posted a deficit of 22.7 billion TL, while the primary budget balance registered a surplus of 27.2 billion TL in 2014 (Table 6.1.1). The central government primary budget surplus and the budget deficit posted a slight deterioration compared to 2013, but performed better than targeted in 2014. Although primary budget expenditures overshot the 2014 target, non-tax revenues turned out to be higher than the target. Also, by the contribution of the limited fall in interest expenditures, the central government budget deficit remained below the 2014 target by 10.6 billion TL.

Table 6.1.1.
Central Government Budget Aggregates
(Billion TL)

	2013	2014	Rate of Increase (Percent)	Actual/Target (Percent)	Target (Percent)
Central Government Budget Expenditures	408.2	448.4	9.8	102.7	7.0
Interest Expenditures	50.0	49.9	-0.2	96.0	4.0
Primary Expenditures	358.2	398.5	11.2	103.7	7.4
Central Government Budget Revenues	389.7	425.8	9.3	105.6	3.5
I. Tax Revenues	326.2	352.4	8.1	101.2	6.8
II. Non-Tax Revenues	49.4	56.8	14.9	127.2	-10.8
Budget Balance	**-18.5**	**-22.7**	**-**	**68.2**	**-**
Primary Balance	**31.4**	**27.2**	**-13.4**	**145.4**	**-**

Source: Ministry of Finance.

The central government budget deficit to the GDP ratio, which declined to 1.2 percent amid the favorable budget performance in 2013, is estimated to increase slightly to 1.3 percent in 2014 (Chart 6.1.1). Meanwhile, the primary budget surplus to the GDP ratio assumed an upward course and reached 2 percent at end-2013, after declining to 1.1 percent in the third quarter of 2012. On the other hand, the ratio is estimated to decline to 1.6 percent in 2014.

Chart 6.1.1.
Central Government Budget Balance
(Annualized, Percent of GDP)

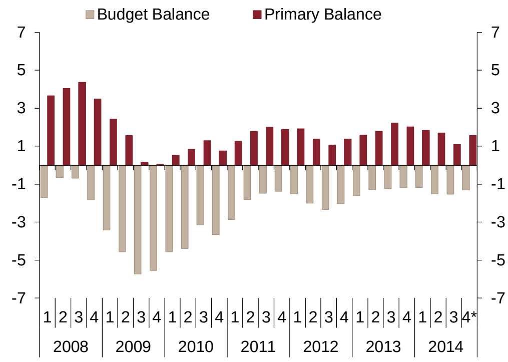
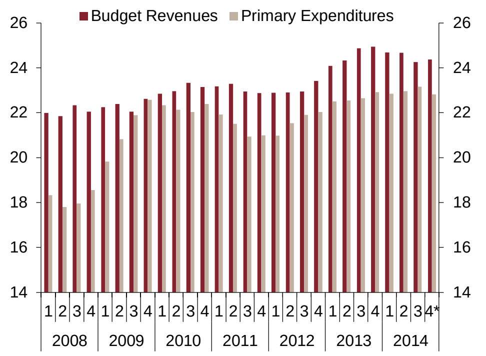


Chart 6.1.2.
Central Government Budget Revenues and Primary Expenditures
(Annualized, Percent of GDP)



* Estimate.
Source: Ministry of Finance.

Having surged since 2012 and reaching 22.9 percent at end-2013, the central government primary expenditures to the GDP ratio hit 23.2 percent in the third quarter of 2014, which is the highest level recorded since 2008. This ratio is expected to fall slightly to 22.8 percent in the last quarter of 2014 (Chart 6.1.2). On the other hand, the central government budget revenues to the 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. This ratio is estimated to drop to 24.4 percent in 2014, mainly due to slowing tax revenues based on domestic demand.

The central government primary budget expenditures, which have trended upwards since the second half of 2012, increased further in 2014. Accordingly, the central government primary budget expenditures registered a year-on-year increase of 11.2 percent in 2014 (Table 6.1.2).

In 2014, current transfers, personnel expenditures and purchase of goods and services, which are major items in primary expenditures, registered an increase of 9.1, 14.7 and 11.8 percent, respectively. Personnel expenditures and government premiums to SSI stand out as the main drivers of the surge in primary expenditures. On the other hand, expenditures on the purchase of goods and services, capital expenditures, capital transfers and lending items overshot the initial subsidies for 2014 to a sizeable extent and stood considerably above the target. 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)

	2013	2014	Rate of Increase (Percent)	Actual/Target (Percent)
Primary Expenditures	**358.2**	**398.5**	**11.2**	**103.7**
1. Personnel Expenditures	96.2	110.4	14.7	100.4
2. Government Premiums to SSI	16.3	18.9	16.1	100.3
3. Purchase of Goods and Services	36.4	40.7	11.8	108.2
4. Current Transfers	148.7	162.3	9.1	99.2
a) Duty Losses	4.1	3.8	-5.9	89.8
b) Health, Pension and Social Benefits	71.8	77.3	7.7	100.3
c) Agricultural Support	8.7	9.1	5.3	94.6
d) Shares Reserved from Revenues	39.9	47.3	18.8	100.3
5. Capital Expenditures	43.8	48.0	9.7	130.8
6. Capital Transfers	7.7	7.7	0.2	117.9
7. Lending	9.1	10.5	15.1	137.6

Source: Ministry of Finance.

In 2014, the central government general budget revenues recorded a year-on-year increase of 9 percent (Table 6.1.3). In this period, tax revenues and non-tax revenues increased by 8.1 and 14.9 percent, respectively. Tax revenues remained slightly above the target for 2014, while non-tax revenues increased considerably above the target.

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

	2013	2014	Rate of Increase (Percent)	Actual/Target (Percent)
General Budget Revenues	**375.6**	**409.2**	**9.0**	**104.1**
I-Tax Revenues	**326.2**	**352.4**	**8.1**	**101.2**
Income Tax	63.8	73.9	15.9	104.4
Corporate Tax	29.0	32.3	11.4	103.9
Domestic VAT	38.0	38.1	0.3	96.2
SCT	85.5	91.1	6.6	101.9
VAT on Imports	62.7	64.4	2.6	99.3
II-Non-Tax Revenues	**49.4**	**56.8**	**14.9**	**127.2**
Enterprises and Property Revenues	14.3	16.1	12.6	198.0
Interests, Shares and Fines	23.7	28.3	19.6	108.7
Capital Revenues	10.1	9.5	-5.5	109.1

Source: Ministry of Finance.

A closer scrutiny of tax revenues reveals that income and corporate tax revenues displayed relatively high-rated increases in 2014, and the rate of increase in tax revenues declined from 9 percent to 5.5 percent when income and corporate tax revenues are excluded. This is largely attributed to the slowdown in tax collection based on domestic consumption. Among consumption-based tax revenues, the SCT and import VAT revenues rose by 6.6 and 2.6 percent, respectively, while domestic

VAT revenues increased merely by 0.3 percent. The details of SCT revenues show an increase by 21.6 and 8 percent in tax revenues on motor vehicles and tobacco products, respectively, whereas tax revenues on petroleum and natural gas products, which account for a large share of total SCT revenues, edged up by 1 percent.

The higher-than-targeted budget performance in 2014 was mainly driven by non-tax revenues. Non-tax revenues performed well as profit transfers from the CBRT and state banks to the budget as venture and ownership revenues remained above the target.

Having turned positive amid tax hikes in September 2012 as well as the base effect, the annual rate of change in real tax revenues started to slacken in the third quarter of 2013 and took negative values in the second quarter of 2014. Driven partly by the base effect and also by the relatively high collection in income and corporate taxes, real tax revenues increased slightly in the third quarter of 2014. However, real tax revenues remained unchanged on an annual basis in the last quarter (Chart 6.1.3). Among consumption-based tax revenues, domestic VAT and import VAT revenues receded by 9.7 and 6.6 percent in real terms, respectively, while the SCT revenues increased by 3.4 percent in the last quarter of 2014 (Chart 6.1.4).

Chart 6.1.3.
Real Tax Revenues
(Annual Percent Change)

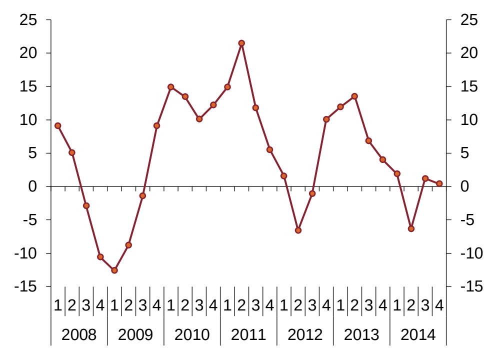
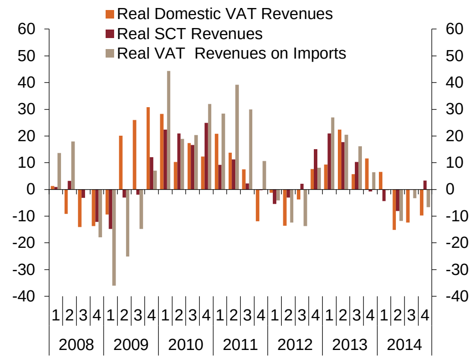


Chart 6.1.4.
Real VAT and SCT Revenues
(Annual Percent Change)



Source: Ministry of Finance.

6.2. Developments in the Public Debt Stock

Public debt stock indicators displayed a favorable outlook in 2014. The total public net debt stock and the EU-defined general government nominal debt stock continued to decline as a percentage of the GDP. The share of fixed-rate securities in the total debt stock increased, while the average maturity of the debt stock increased and the real cost of borrowing remained low in recent months.

The central government debt stock stood at 612 billion TL in 2014 (Chart 6.2.1). In the third quarter of 2014, the ratio of the total public net debt stock and the EU-defined general government nominal debt stock to GDP decreased by 2.2 and 2.1 points, respectively, compared to end-2013.

Chart 6.2.1.
Public Debt Stock Indicators

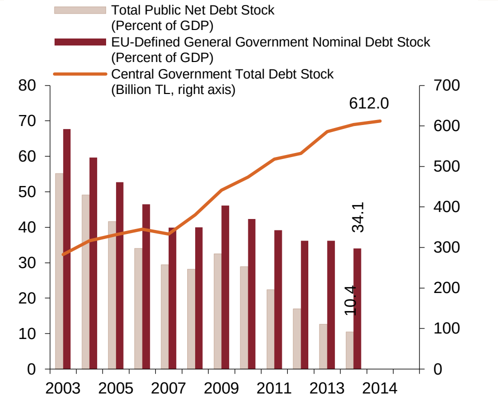
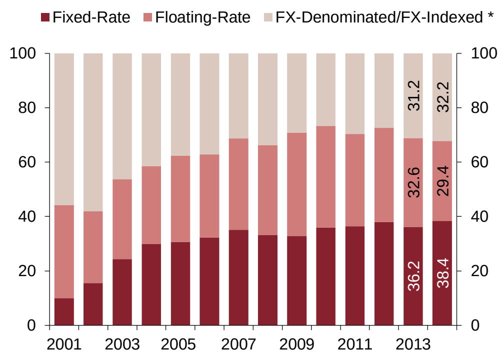


Chart 6.2.2.
Composition of the Central Government Debt Stock*
(Percent)



* FX-Denominated/FX-Indexed debt stock includes external debt stock and FX-denominated and FX-indexed domestic debt stock.
Source: Treasury.

The share of fixed-rate securities in the total debt stock increased slightly from end-2013 (Chart 6.2.2). An analysis of the interest and exchange rate structure of domestic borrowing suggests that the share of fixed-rate borrowing registered a year-on-year increase in the first eleven months of 2014. The ratio of public deposits to average monthly debt service stands at 278.9 percent. The average term-to-maturity of the domestic debt stock rose to 55 months (Chart 6.2.3). Meanwhile, external borrowing by bond issues amounted to 6.3 billion USD, with the average maturity standing at 14.8 years (Chart 6.2.4).

Chart 6.2.3.
Average Maturity of the Domestic Cash Borrowing and Term-to-Maturity of the Domestic Debt Stock
(Month)

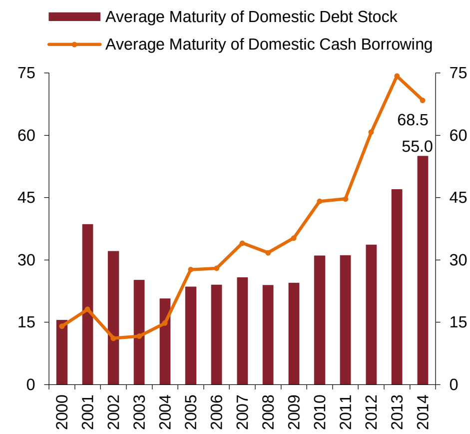
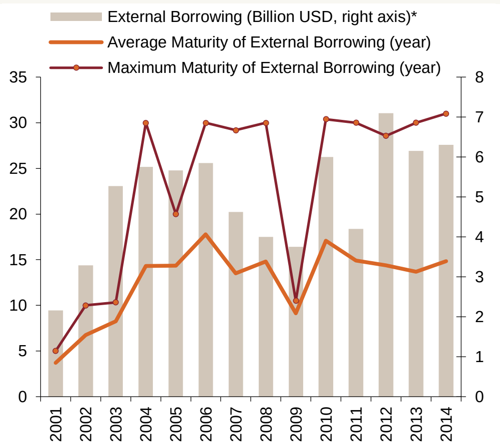


Chart 6.2.4.
Borrowing By Bond Issue



Source: Treasury.

The domestic debt rollover ratio stood at 81.3 percent as of November 2014 (Chart 6.2.5). Having plummeted from early 2009 to early 2011, the average real interest rate[1], which rose in the second half of 2013 due to global financial fluctuations and the cautious monetary policy stance, has recently recorded low levels (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).

Chart 6.2.5.
Total Domestic Debt Rollover Ratio
(Percent)

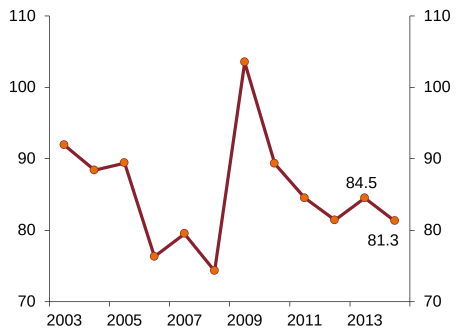
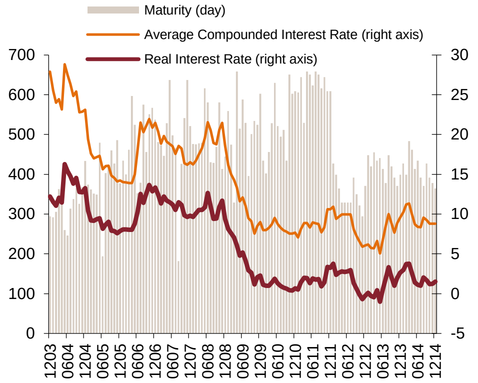


Chart 6.2.6.
Average Maturity and Interest Rates of Borrowing at Discount Auctions



Source: Treasury, CBRT.