

## Ukraine's Consolidated Budget results through September 2012

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Based on Monthly Budget Execution reports of Ukraine's State Treasury

### Consolidated budget balance and financing

- Consolidated budget deficit increased as a result of decelerating revenues and accelerating expenditures.** After demonstrating a 1.5% GDP deficit in the second quarter (which was an improved result compared to 2011), Ukraine's Consolidated Budget balance deteriorated in the next two months. By the end of September, nominal consolidated deficit was almost seven times higher than in the same period of the previous year (see Table 1). As will be discussed further, the budget deficit grew as a result of decelerating revenues and accelerating spending. Moreover, while revenue growth in January-September was below schedule (total revenues 4.9% lower than baseline projection), expenditures grew at rates above growth levels planned for the year (16.2% real growth to same period of last year, compared to only 6.1% real annual growth in the annual Consolidated Budget).

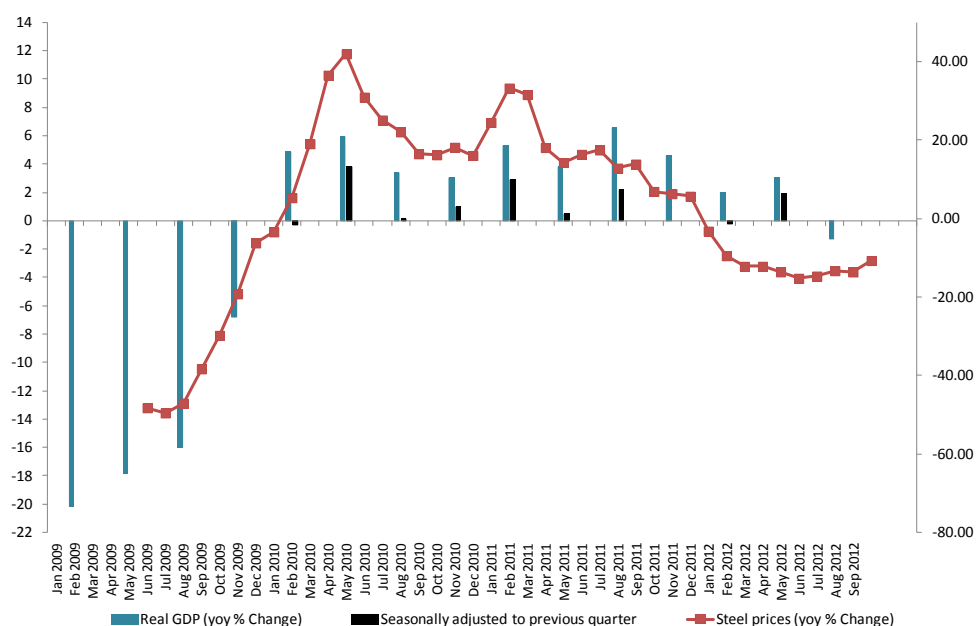
Table 1. Consolidated Budget Totals through January – September 2012 (UAH Millions)

	Annual budget plan*	Actual budget totals		Latest period for which GDP data is available and same period of the previous year	
		Jan-Sep	Jan-Sep	Q2	Q2
		2012	2011	2012	2011
<b>Latest budget totals</b>					
Expenditures	510,324	335,753	287,048		
Revenues	473,754	317,962	286,795		
Deficit (-) / surplus (+)	-35,643	-21,265	-3,123		
<b>Deficit as % of GDP</b>	<b>-2.37%</b>	<b>n/a</b>	<b>n/a</b>	<b>-1.5%</b>	<b>-1.9%</b>

\* Based on the latest Treasury Report and MinEcon GDP forecast

- Deteriorating budget totals mirror worsening macroeconomic outlook, as global steel prices continue to decline and Ukraine's terms of trade weaken. (See Figure 1). Economic growth was further jeopardized in August-September by rising tensions in trade relations with Russia which affected performance of Ukraine's machine building industry. Although the latest absolute GDP numbers are available only for the 2<sup>nd</sup> quarter of the year (which makes it impossible to produce more up-to-date comparisons of the deficit figures to GDP), the State Statistics Committee has just published its estimate of GDP year-over-year real change for the 3<sup>rd</sup> quarter, which revealed a 1.3% decline.
- Consolidated budget deficit figures include local and state budget balance but exclude other quasi-fiscal obligations such as the deficit of NJSN Naftogas and the deficits of the country's social funds. At the same time, these latter deficits are included into the IMF estimates of the General Government Deficit thresholds. In 2011, Ukraine has broken the agreed benchmark for the Naftogas deficit, which was supposed to be in balance by end of last year. Macro-fiscal risks of using public funds for covering financial risks of Naftogas related to growing price differentials between import of gas and its further sales to households and utility companies have been at the core of Ukraine's negotiations with the IMF since the outset of the global economic crisis in 2008. During September 2012, the Government has developed amendments to the 2012 Budget (approved later this year) and a separate Cabinet of Ministers Resolution (No 5308 of 02.10.2012) which allocates UAH 3.9 billion for compensation of the gas price differentials to Naftogas.

Figure 1. Ukraine's GDP and Global Steel Prices (Jan 2009 - Sep 2012)



## Consolidated budget receipts

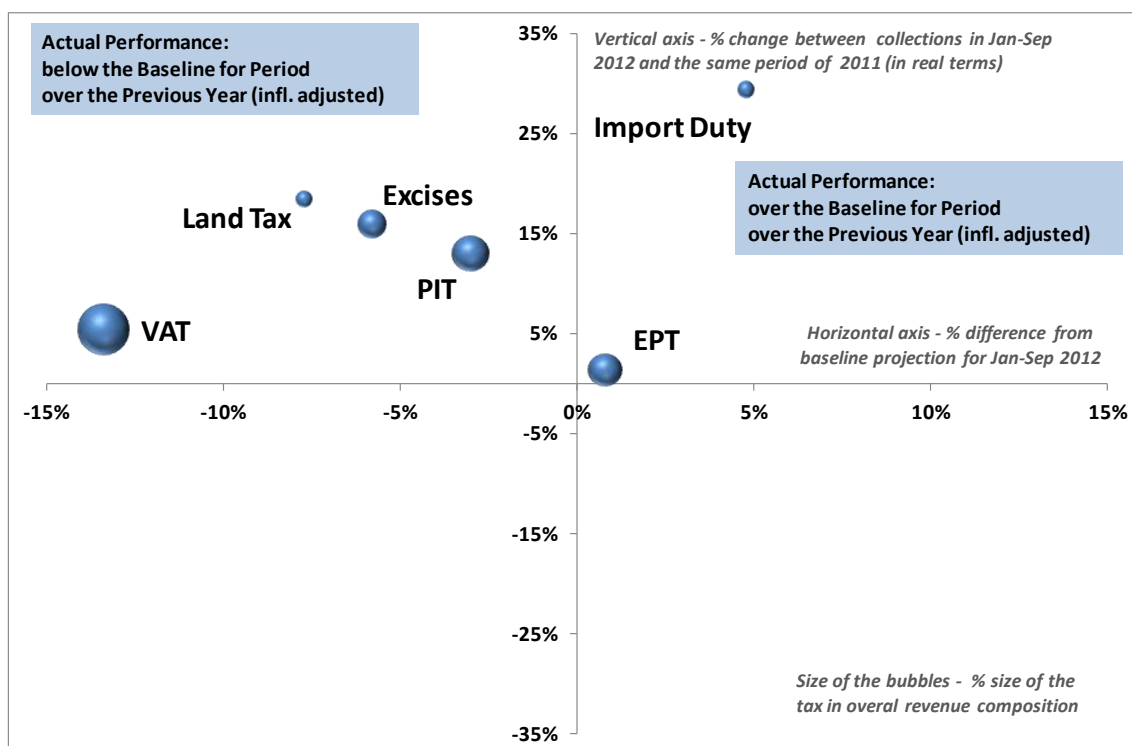
- In January-September 2012, consolidated revenues grew strongly compared to last year (by 10.1% in real terms), but still remained 4.9% below the period baseline projection.** As illustrated in Table 2 and Figure 2, all key taxes were collected above last year's levels, in real terms. At the same time, only two revenue sources – Import Duties and the EPT – were also exceeding period baseline projections for this period, with Import Duties collected 4.9% above the projection, and EPT being almost equal to the projection (only 0.6% higher). All other taxes remained behind schedule, with the poorest performance of VAT, Ukraine's largest revenue source (as illustrated in Figure 2).

Table 2. Consolidated Revenues in January - September 2012 (UAH Millions)

	Nominal actual revenues (Jan - Sep 2012)	Comparisons to plan		Comparisons to baseline		Comparisons to same period of 2011		Budget 2012 to Budget 2011 (% Change in real terms)
		Annual plan (Jan-Dec 2012)	Actual revenues as % of annual plan	Baseline projection (Jan - Sep 2012)	% Difference of actual over baseline	Nominal actual revenues (Jan - Sep 2011)	% Change in real terms	
<b>Total Revenues</b>	<b>317,962.31</b>	<b>473,754.26</b>	<b>67.12%</b>	<b>334,270.07</b>	<b>-4.9%</b>	<b>286,794.57</b>	<b>10.1%</b>	<b>10.5%</b>
VAT	100,992.03	163,380.24	61.81%	116,740.45	-13.5%	95,191.80	5.3%	17.9%
PIT	49,186.72	70,294.05	69.97%	50,697.75	-3.0%	43,275.66	12.9%	6.5%
EPT	39,797.55	58,210.84	68.37%	39,566.81	0.6%	39,057.31	1.2%	12.5%
Excises	29,204.19	42,741.40	68.33%	30,970.17	-5.7%	25,018.13	15.9%	5.4%
<i>Excise internal</i>	<i>21,793.34</i>	<i>32,457.40</i>	<i>67.14%</i>	<i>23,547.73</i>	<i>-7.5%</i>	<i>19,515.01</i>	<i>10.9%</i>	<i>-4.9%</i>
<i>Excise import</i>	<i>7,410.86</i>	<i>10,284.00</i>	<i>72.06%</i>	<i>7,422.44</i>	<i>-0.2%</i>	<i>5,503.12</i>	<i>33.8%</i>	<i>60.2%</i>
Land Tax	9,518.35	14,028.06	67.85%	10,314.31	-7.7%	7,988.82	18.3%	10.2%
Import Duty	9,610.15	12,694.36	75.70%	9,159.07	4.9%	7,386.54	29.3%	14.9%

Source: Treasury Budget Execution Report.

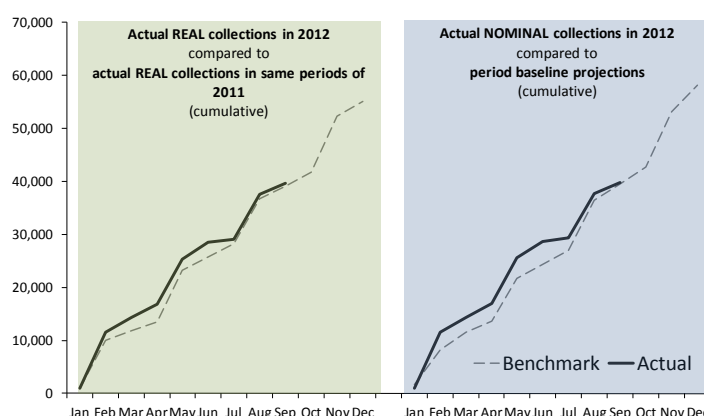
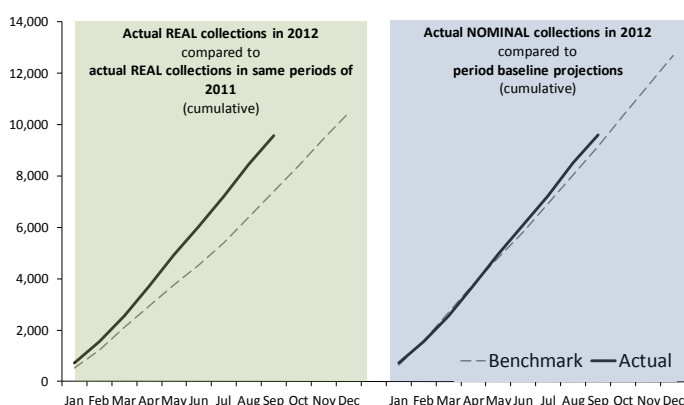
Figure 2. Performance of key taxes in January-September 2012



- The best performance during January-September was again registered among taxes whose collection is, in principle, most vulnerable to administrative manipulation (EPT and Import Duties). As in 2011, both of these sources outpace period projections. Collections of Import Duties in January-September 2012 were 4.9% above schedule, and also 29.3% higher compared to the same period of last year (see Figure 3). The Enterprise Profit Tax collections in January-September were only 0.6% above baseline, and 12.5% higher than in the same period of 2011. It is notable, however, that while EPT still remained ahead of schedule by end of September, the percentage of overperformance steadily decreased throughout the year (see Figure 4). The EPT also demonstrates the lowest rate of real growth compared to same period of 2011 (only 1.2%).

Figure 3. Import Duties performance in January-September 2012

Figure 4. EPT performance in January-September 2012

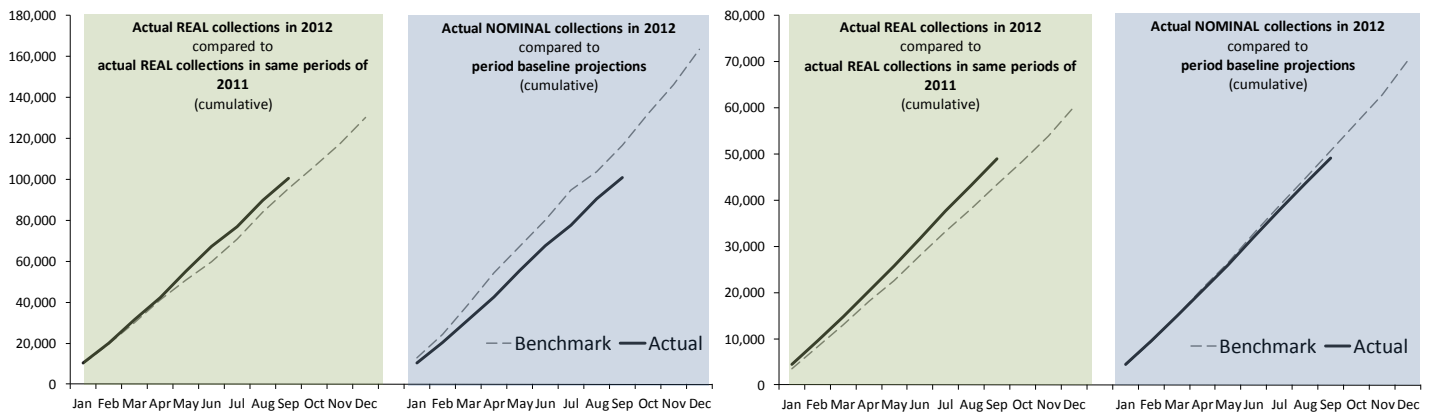


- The VAT remained to be Ukraine's worst performing tax, growing slowly against last year and falling furthest behind schedule. In the 2012 Annual Budget, the Value Added Tax was supposed to bring in one of the highest increases of all taxes compared to last year (17.9% in nominal terms, as showed in Table 2). This forecast was consistent with the VAT's robust performance throughout 2011 (it was collected slightly above plan and 40% above 2010 level, in real terms). In January-September 2012, however, VAT proceeds were 5.3% higher than last year, in real terms, and throughout this period the proceeds fell increasingly behind schedule, as illustrated in Figure 5. By end of September, collections were 13.5% lower than projected for the period, making VAT the worst performing tax in Ukraine's consolidated budget so far.

- Personal Income Tax increased considerably in real terms, but still remained below the schedule.** Considerably higher collections of PIT in comparison to 2011 (12.9% increase in real terms in January-September 2012 compared to same period of previous year) allowed the Government to stay just near the baseline projections for this tax, falling behind by 3.0% (see Figure 6). Notably, PIT performance against baseline steadily deteriorated during the year (as also visible from Figure 6).

Figure 5. VAT performance in January-September 2012

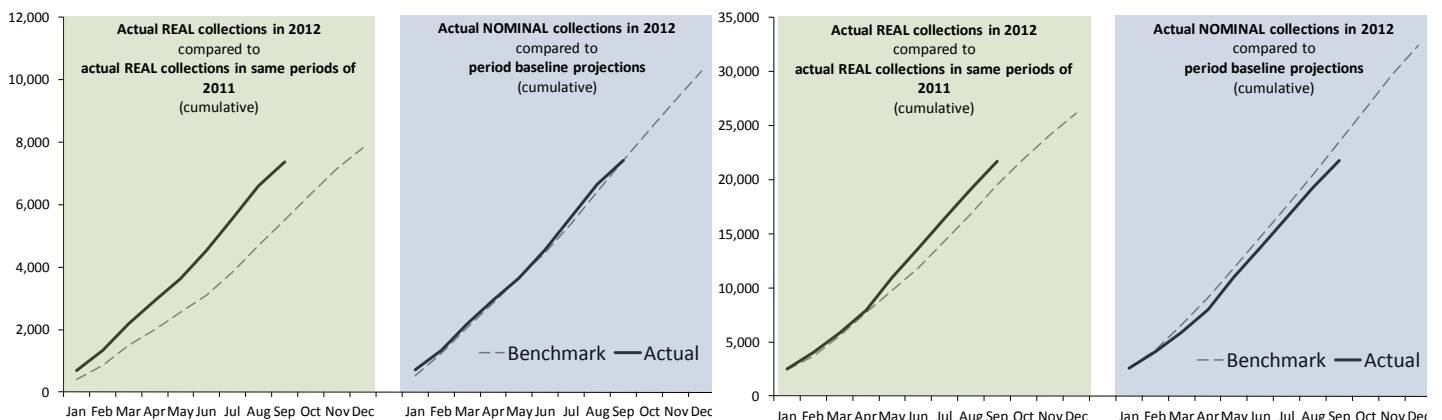
Figure 6. PIT performance in January-September 2012



- Excise taxes grew strongly compared to last year but still fell behind schedule.** The 2012 Budget predicted a striking 60.2% real growth in excises on imported goods, while the annual forecast of internal excise collection implied a 4.9% real contraction (it was the only tax which was expected to be raised at levels lower than last year). In January-September 2012, both groups of excise taxes grew strongly in comparison to the same period of 2011, in real terms (by 33.8% and 10.9% respectively), but both remained below schedule (by 0.2% and 7.5%, respectively). As illustrated in Figure 7 and Figure 8, foreign excises remained just above baseline during most of the months but fell below projections by September, while collections of the domestic excises have diverged further away from schedule during the entire year.

Figure 7. Performance of Excises on Imported Goods in January-September 2012

Figure 8. Performance of Excises on Domestic Goods in January-September 2012



## Consolidated budget spending

- Real consolidated expenditures in January-September 2012 increased compared to last year at rates considerably higher than was predicted by the 2012 annual budget.** During January-September, consolidated budget expenditures grew by 16.2% in real terms compared to the same period of last year, considerably outpacing the 6.1% change rate expected annually for this year (see Table 3). By the end of September, this allowed the Government to spend 65.8% of its total annual commitment.

Table 3. Consolidated spending in January-September 2012 (UAH millions)

	Nominal actual expenditures (Jan - Sep 2012)	Comparisons to plan		Comparisons to same period of 2011		Budget 2012 to Budget 2011 (% Change in real terms)
		Annual plan (Jan-Dec 2012)	Actual expenditures as % of annual plan	Nominal actual expenditures (Jan - Sep 2011)	% Change in real terms	
<b>Total Expenditures</b>	<b>335,752.87</b>	<b>510,324.40</b>	<b>65.8%</b>	<b>287,047.81</b>	<b>16.2%</b>	<b>6.1%</b>
Public Administration	37,248.51	62,857.78	59.3%	34,721.43	6.6%	12.0%
Defence	10,007.05	17,373.61	57.6%	8,868.00	12.1%	11.1%
Civil Order, Security & Judiciary	24,691.00	37,502.37	65.8%	21,892.89	12.0%	3.6%
Economic Activities	39,974.71	67,699.09	59.0%	34,784.59	14.4%	-12.5%
Environment Protection	3,099.41	9,591.89	32.3%	2,119.40	45.6%	39.9%
Housing and Utilities	6,853.63	13,489.02	50.8%	6,211.41	10.2%	10.7%
Healthcare	40,016.44	58,495.54	68.4%	31,983.05	24.3%	10.4%
Culture and Sports	9,210.78	14,855.01	62.0%	6,900.50	32.6%	21.3%
Education	72,680.43	101,474.37	71.6%	60,346.94	19.6%	6.0%
Social Protection & Social Care	91,970.91	126,985.73	72.4%	79,219.60	15.3%	10.0%

Source: Treasury Budget Execution Report.

- **Most active spending was registered in Social Protection, Education, Healthcare and Civil Order & Judiciary.** In all social sectors with wage-intensive budgets, consolidated expenditures increased compared to last year at rates which were considerably higher than annual increase rates budgeted for 2012. Respectively, in these four sectors, spending in January-September covered the highest percentage of the annual commitment (see Table 3).
  - **In Social Protection and Social Care,** real consolidated spending in January-September 2012 grew by 15.3% compared to the same period of the previous year, representing 72.4% of the annual budget for this sector. Real annual increase of expenditures on Social Protection for the entire year was planned at 10.0%.
  - **In Education,** consolidated expenditures in the first nine months of 2012 were 19.6% higher than in the same period of 2011, in real terms, and represented 71.6% of the annual budget for this sector. Real annual increase of the education budget for 2012 was planned at only 6%.
  - **In Healthcare,** consolidated expenditures in January-September 2012 increased by 24.3% in real terms compared to the previous year, covering 68.4% of the annual commitment. Real annual increase of consolidated expenditures on Healthcare was budgeted at 10.4%.
  - **In Civil Order and Judiciary,** real spending grew by 12% compared to the previous year, with actual expenditures for January-September covering 65.8% of the annual plan. Annual expenditures for this sector are supposed to increase by only 3.6% in real terms compared to 2011.
- **Spending on Economic Activities was considerably increased and directed mostly on support to Coal Mining and other Extracting Industries.** Economic Activities was the only function of the consolidated budget which was reduced in the 2012 Budget compared to the 2011 Budget, in real terms (by 12.5%). Nevertheless, real consolidated spending on Economic Activities in January-September 2012 increased by 14.4%. Most of the increase was related to growing expenditures on Coal Industry and Other Solid Fuel Extraction Industries, while spending on Agriculture actually decreased in real terms.

- **Expenditures Housing and Utilities grew according to plan but the composition of the increasing spending is not easily identifiable.** A relatively modest increase in Housing and Utilities sector (10.2% of real growth which corresponds almost exactly to the 10.7% real increase budgeted for the 2012) was linked mostly to the growing spending classified as “Other activities in Housing and Utilities sector”. At the same time, expenditures on Utilities decreased in real terms (compared to the same period of 2011).
- **The lowest real increase compared to last year was registered in Public Administration and Defense.** Real consolidated expenditures on Public Administration increased by 6.6% in January-September 2012 compared to same period of the previous year, and represented a comparatively modest 59.3% of the annual commitment. Expenditures on Defense were 12.1% higher than in the first nine months of 2011 (in real terms) and equal to 57.6% of the annual budget for this sector.
- **The lowest rate of annual expenditure execution is registered for Environment Protection.** Spending on this category during January-September 2012 represented only 32.3% of the annual commitment. At the same time, these expenditures grew by impressive 45.6% in real terms, compared to the same period of 2011. The bulk of the increase was registered in sub-category related to Protection and Reasonable Use of Natural Resources.