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THE 2023 BUDGET MAY END UP WITH A SURPRISE

EVALUATION NOTE

The budget data for January-May point to a significant deterioration compared to the same period of the previous year. As a matter of fact, the budget, which posted a surplus of 124.6 billion TRY in the first five months of 2022, has posted a deficit of 263.6 billion TRY in the same period of 2023. Moreover, the spending increases that will arise from the retirement age victims regulation, raising pensions to a minimum of 7,500 TRY, increasing the grants to be paid in Eid al-Fitr and Eid al-Adha, increasing the 3600 additional payment coefficient for the civil servants, providing free natural gas to residences, and raising the minimum wage, which were realized within the scope of election pledges, have not yet been reflected in the budget figures. Additionally, while the expenditures for aid and shelter for earthquake victims following the February 6 earthquakes have been partially covered in the budget, the fiscal impact of the budgetary transfers to the Disaster and Reconstruction Fund, established after the earthquake, for the construction of destroyed and damaged public buildings and infrastructure has not yet been fully revealed. On the other hand, a one-time earthquake tax was introduced in March on the earnings of corporations, except those in the earthquake zone, for the year 2022.

Mehmet Şimşek, the Minister of Treasury and Finance, who took office after the elections, made a statement to "return to rationality". Therefore under the conditions of high inflation, high deficit of the balance of payments, and the rapid deterioration in the budget performance compared to the previous year, the government's fiscal policy response has

¹https://www.tepav.org.tr/en/ekibimiz/s/1420/M.+Coskun+Cangoz_PhD

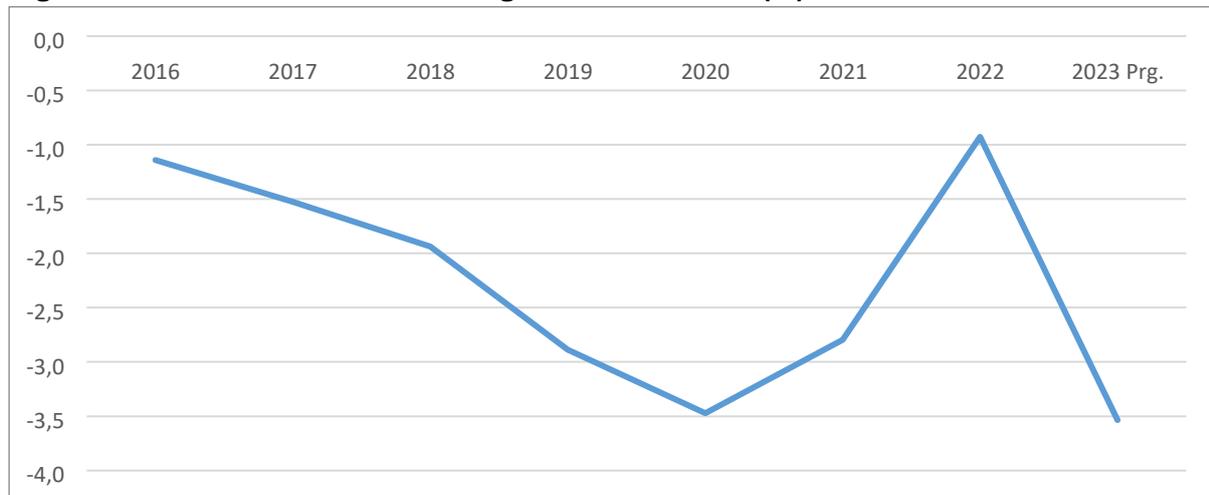
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become critical. In this context, the outlook for the budget and an assessment of what can (cannot) be done in the remainder of the year will provide clues to the answer to this question.

2023 Budget Outlook

The deficit in the central government budget increased starting from 2017 and was somewhat balanced in 2022. However, it was not due to the improvement in the structural budget, but to the increase in budget revenues beyond the projections in parallel with the increase in inflation and exchange rates. In fact, as discussed in the article titled "[Budget has no room for maneuver](#)" published in the TEPAV Blog, due to the rigidity in budget expenditures, the 2023 budget was programmed to run a deficit of 3.5 percent of GDP, in line with the upward trend of the previous years.

Figure 1 - Central Government Budget Balance / GDP (%)



Source: Ministry of Treasury and Finance

Compared to the same period of the previous year, expenditures for the January-May 2023 period recorded significant increases, especially in current transfers, interest expenditures, and personnel expenditures. Among goods and services expenditures, defense expenditures, which increased by 148.9 percent compared to the same period of the previous year, and health expenditures, which increased by 169.8 percent, mainly due to the earthquake, draw attention. In this context, health and social assistance expenditures under the current transfers' item increased by 93.4 percent compared to the same period of the previous year. Agricultural support payments, which were 50.3 percent of budget allocations in 2022, increased to 68.1 percent in January-May 2023 due to expansionary fiscal policies performed before the elections. Similarly, other transfers to households and social transfers also recorded significant increases compared to the same period of 2022 (117.5 percent and 97.2 percent, respectively). In this period, budget transfers for the Exchange-rate Protected Deposit (EPD) amounted to 4.4 billion TRY.

On the other hand, despite the surcharge in corporate tax rate, the realization rate of corporate income tax in the first five months of 2023 according to the budget targets was 45.3 percent, which is below the 51.1 percent level in the same period of 2022. On the other hand, indirect taxes on goods and services increased by 97 percent between January and May 2023. This increase was mainly driven by Special Consumption Tax (SCT) on motor vehicles, durable

goods and cola drinks. Compared to the same months of the previous year, these taxes increased by 176.7, 139.5 and 125.7 percent, respectively.

Table 1 - January - May Budget Realizations

(Million TRY)	January-May 2022	January-May 2023	% Change
BUDGET EXPENDITURES	959,773	1,875,715	95%
EX INTERESTS BUDGET EXPENDITURES	837,887	1,637,846	95%
I. Personnel Expenditures and SSI State Premiums	250,709	519,108	107%
II. Expenditures on Purchase of Goods and Services	66,426	135,631	104%
III. Interest Expenses	121,885	237,869	95%
IV. Current Transfer	383,398	790,144	106%
V. Capital Expenditures	46,568	107,966	132%
VI. Capital Transfer	4,110	45,170	999%
VII. Net Lending	86,677	39,827	-54%
BUDGET REVENUES	1,084,391	1,612,124	49%
I. Tax Revenues	881,156	1,371,153	56%
1. Taxes on Income and Profit	376,358	493,776	31%
a) Income Tax	116,979	213,083	82%
b) Corporate Income Tax	259,379	280,693	8%
2. Taxes Levied on Property	12,152	19,750	63%
3. Domestic Goods and Services Taxes	220,314	435,048	97%
a) Domestic Value Added Tax	65,652	128,694	96%
b) Special Consumption Tax	126,469	251,324	99%
c) Other	28,194	55,030	95%
4. Taxes on International Trade and Transactions	226,786	337,858	49%
5. Stamp Tax	15,102	30,288	101%
6. Fees	26,242	45,945	75%
7. Other Taxes Not Classified Elsewhere	4,200	8,489	102%
II. Non-Tax Revenues	203,235	240,971	19%
BUDGET BALANCE	124,618	-263,590	
PRIMARY BALANCE	246,504	-25,722	

Source: Ministry of Treasury and Finance

Overall, as a reflection of the fact that the increase in budget revenues remained below budget expenditures in the first five months of 2023, the budget balance, which was in surplus in January-May 2022, turned into a deficit.

End-2023 Scenarios

Following the rapid deterioration in the January-May 2023 compared to the same period of the previous year, how the budget balance will be shaped in the rest of the year will mostly depend on the policies to be implemented after the elections. However, expenditure-increasing regulations that come to the agenda during the election period must be considered in the estimation of all scenarios since they changed the budget's expenditure base. In this respect, potential budgetary impacts of expenditure increasing regulations are calculated based on the impact analyses presented during the parliamentary debate on the legislative regulations, and the reports prepared by the [Presidency of Strategy and Budget](#) and [TEPAV](#) in the aftermath of the earthquake are presented below.

Table 2 - Potential Budgetary Impacts of Expenditure Increasing Regulations

Expenditure Increasing Regulations	2023 Potential Budgetary Impacts (Billion TRY)
Earthquake Expenditures	483
Increase in current transfers (KKM, public-private partnership etc.)	200
Retirement age victims (EYT) regulation	85
Raising the minimum pension to 7,500TRY	65
Making the minimum civil servant wage 22,000TRY and gradual increase in pensions	65
Additional transfer to SSI due to EYT etc.	59
Free natural gas	37
Increasing the Eid al-Fitr and Eid al-Adha grants to 2000 TRY	25
Extending the coverage of 3600 additional payment coefficient	10
Increasing veterans' salaries	2

Source: TBMM minutes, Presidency of Strategy and Budget 2023 Kahramanmaraş and Hatay Earthquakes Report, TEPAV Kahramanmaraş Centered Earthquake Impacts and Policy Recommendations Evaluation Note, author's predictions and calculations.

The budget forecast for 2023 is based on three different scenarios, taking into account the budget performance in the January-May period and the possible effects of expenditure-increasing regulations on the budget.

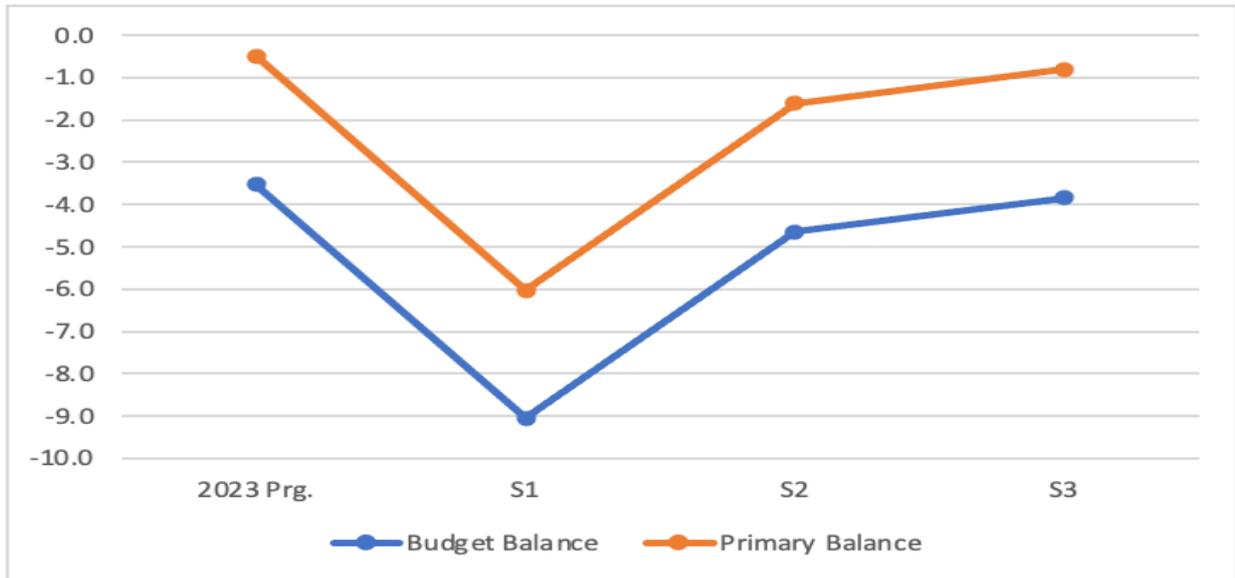
S1 - The Lost Year 2023 Scenario: Based on the article titled "[Budget has no room for maneuver](#)" published in TEPAV Blog and media reports² citing Treasury and Finance Minister Mehmet Şimşek, it is foreseen that no measures will be implemented on the expenditure side of the budget until the end of the year and no tax adjustments will be made before the local elections in March 2024.

² <https://www.gazetepencere.com/mehmet-simsekin-yakinlarina-soyledikleri-ortaya-cikti-yukse-butce-aciklari-kabusu-oldu/>

S2 - Better lose the saddle than the horse scenario: It is envisaged that expenditure-increasing promises made during the election period will be realized, other budget expenditures that increased in the first 6 months will be cut in the second half of the year, and some rate increases in indirect taxes that do not require a legislative amendment will be made in order to limit the budget deficit.

S3 - "Back to Rational" Scenario: An economic program that includes expenditure savings and reprioritization as well as tax adjustments is envisaged. However, since the Parliament will go into recess on July 1, it is highly improbable that reforms requiring expenditure consolidation and tax adjustments will be implemented in 2023. Moreover, even if legal arrangements are made, their financial impact will be seen in the 2024 budget at the earliest.

Figure 2 - Budget Balance and Primary Balance Forecasts under Different Scenarios



Projections based on the scenarios indicate that the budget deficit could reach 9.1 percent of GDP in the case that expenditure-increasing measures are fully implemented, while no measures are taken on either the expenditure or revenue side (S1).³ The budget deficit, however, decreases to 4.6 percent if expenditure measures are implemented and revenue-raising measures, particularly taxes on goods and services, are implemented (S2). Under the scenario of stronger fiscal consolidation (S3), the budget deficit is estimated at 3.8 percent, significantly converging to the level envisaged under the program.

To sum up, depending on the degree to which fiscal consolidation will be prioritized in the economic policies to be implemented in the second half of 2023, the budget deficit may be realized at historically high levels or in line with the MTP (medium-term program) projections.

³ Based on the GDP data of 18,654 billion TL used in official statistics