Ukraine | Research
Economy
Desk Note

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State budget 2013

Cost cutting plan eases hryvnia and sovereign risk

The state spending plan proposed for 2013, approved by Ukraine's parliament on Dec. 6, gives the impression that authorities are preparing to face 2013 challenges without reliance on IMF funding. The budget's 7% yoy revenue growth plan looks feasible and its targeted general deficit (including a Naftogaz subsidy) of 4.5% of planned GDP is manageable. Against this backdrop, external funding is critical but looks achievable. Moreover, it is set to keep external public debt/GDP as low as 0.2x and points to some easing of pressure on the local currency in 2013.

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State budget stats, UAH bln

	2012E	2013 plan	yoy
Revenues	338.3	361.5	6.9%
Spending	413.6	410.7	-0.7%
Deficit	75.3	49.2	-34.7%
% of GDP	5.3%	3.1%	-2.2pp

Public debt, year-end, UAH bln*

	2012E	2013 plan	yoy
Total	511.3	565.8	10.7%
% of GDP	35.8%	35.9%	+0.1pp
External	310.3	317.4	2.3%
Internal	201.0	248.4	23.6%

**At constant UAH/USD rate*
Source: Verkhovna Rada, Concorde Capital estimates

2013 budget revenue up only 6.9% yoy, social initiatives broadly ignored

The Finance Ministry expects just a 6.9% yoy budget revenue increase in 2013, which looks quite realistic (we expect nearly 8% growth for this year) even if Ukraine experiences economic hardships further on. The government was quite brave to cut the ruling party's pre-election social initiatives, which look up to date. In particular, we did not find any plans to repay the lost deposits of Soviet Savings Bank in the bill, and minimum social standards have been frozen: the subsistence level is up just 6.8% yoy and minimum wages are just 5.0% higher yoy.

Budget-to-GDP ratio is reduced, but fiscal pressure on is unlikely to relax

The modest revenue target presumes that the general budget's share of GDP will fall to 29.4% in 2013 from this year's 33.1% target. In our view, this is not a move towards easing tax pressure but acknowledgment of the fact that the tax base has been deteriorating. All key revenue streams have been marked for reduction in 2013 except personal income tax, import duties and direct NBU funding, which are expected to grow 11%, 19% and 51% from the official 2012 plan, respectively. In addition, against the backdrop of an anticipated enterprise profit tax rate reduction by 10% (to 19% in 2013 from 21% currently), the profit tax collection plan is left almost flat at only a 1.8% decline - business shouldn't expect any relaxed tax pressure.

Pension Fund deficit increase marked for 2013

The bad news is that the Pension Fund subsidy from the budget is growing (up to 5.3% of GDP from 4.5% in 2012). In view of the painful pension age increases starting 2011, which targeted a narrowing Pension Fund deficit, the outcome is utterly disappointing. Apparently, the pre-election generosity will not be reversed here.

Naftogaz subsidizing continues

More disappointing news is that gas and heating tariffs are not set to grow in 2013: the budget is based on UAH 727/tcm gas tariff for heating enterprises, which is a current rate. Naftogaz (NAFTO) is still expected to be subsidized for tariff differences, while the subsidy is somewhat lower than in 2012 (UAH 8.0 bln vs. UAH 12 bln targeted last year). The state plans to resume T-bill contributions to Naftogaz's statutory fund for this support. State banks, or the NBU through intermediary commercial banks, are seen as the main buyers of the securities that will imply further growth of exposure to "related parties" for two state flagships, Oschadbank (OSCHAD) and UkrExim Bank (EXIMUK). Note that the banks' exposure to T-bills increased to 52% and 48% of equity as of end-1H12 from 36% and 37% as of end-2011, respectively.

General fiscal gap at 4.5% of GDP

Though budget cuts indeed will happen in 2013, the central budget deficit is targeted to be quite solid at 3.1% GDP (3.6% counting Naftogaz). The number could have been acceptable for the IMF unless we have a look at the general fiscal gap, which is promised to reach 4.0% (4.5% counting Naftogaz). The aggressive deficit target apparently will raise extra issues during talks with the IMF.

Deficit funding still hanging on external loans, but debt/GDP won't grow

We see no surprise with the means of proposed deficit funding: a routine privatization revenue target (UAH 10.9 bln), near USD 5.2 bln of external loans and UAH 92.7 bln of local T-bills. The plan is quite realistic assuming availability of external funding will not worsen: this year the Finance Ministry raised USD 3.85 bln from abroad, excluding the rollover of a USD 1.0 bln VTB loan, and USD 2.8 bln internally through foreign currency T-bills. And the plan will not hurt government's leverage – public debt/GDP will remain broadly flat at 0.36x and external debt/GDP will be about 0.20x in 2013, we estimate. Next year, the government will have to repay a USD 1.0 bln Eurobond in June and USD 2.5 bln during the year to the IMF (also the NBU will have to repay USD 3.0 bln), pointing to available external funding as being critical.

Low social spending ease pressure on hryvnia

The suggested spending plan increases confidence in the national currency even without cooperation with the IMF. One of the major risks that we saw for 2013 was "protected" social liabilities, which would require a solid UAH emission. A large part of social initiatives have been dropped, suggesting the authorities will be able to cover liabilities without printing money above the targeted level (T-bills purchase by the NBU and a planned UAH 16.0 bln direct transfer from the NBU). This outlay allows for conducting a controlled devaluation in 2013 and reducing the risks for a shock scenario for the local currency.

Key budget stats

Revenues and expenditures, UAH bln

	Target 2012	2012 Expected	Target 2013	2013 Target / 2012E
State budget revenues	374.0	338.3	361.5	6.9%
% of GDP	26.2%	23.7%	22.9%	-0.8pp
State budget spending	413.6	413.6	410.7	-0.7%
% of GDP	28.9%	28.9%	26.1%	-2.8pp
State budget deficit	39.6	75.3	49.2	-34.7%
% of GDP	2.8%	5.3%	3.1%	-2.2pp
General budget revenues	473.8	438.8	463.1	5.5%
% of GDP	33.1%	30.7%	29.4%	-1.3pp
General budget spending	510.3	516.9	525.6	1.7%
% of GDP	35.7%	36.1%	33.3%	-2.8pp
General budget deficit	36.6	78.2	62.5	-20.1%
% of GDP	2.6%	5.5%	4.0%	-1.5pp
Pension Fund subsidy	57.5	64.5	83.2	29.0%
% of GDP	4.0%	4.5%	5.3%	0.8pp
Incl. Pension Fund deficit coverage	9.7	15.3	21.8	42.5%
% of GDP	0.7%	1.1%	1.4%	0.3pp

Source: Verkhovna Rada, Concorde Capital estimates

Deficit financing, UAH bln

	2012E	Target 2013	yoy
State budget deficit	75.3	49.2	-34.7%
State loans	3.4	1.2	-64.7%
Total deficit to cover	78.7	50.4	-36.0%
% of GDP	5.5%	3.2%	-2.3pp
External funding, net*	10.9	7.1	-34.9%
- New loans	42.1	42.7	1.4%
- Repayments	-31.2	-35.6	14.1%
Internal funding (net)	27.3	47.4	73.6%
- New loans	63.4	92.9	46.5%
- Repayments	36.1	45.5	26.0%
Privatization proceeds	6.0	10.9	81.7%
Change in state deposits and securities invested	-34.5	14.9	n/m
Public debt, year-end*	511.3	565.8	10.7%
% of GDP	35.8%	35.9%	0.1pp
External debt, year-end*	310.3	317.4	2.3%
% of GDP	21.7%	20.1%	-1.6pp
Internal debt, year-end	201.0	248.4	23.6%
% of GDP	14.1%	15.8%	1.7pp

**At current UAH/USD exchange rate; Source: Verkhovna Rada, Concorde Capital estimates*

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