

RUSSIA'S STATE BUDGET IN JANUARY–MAY 2015

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According to the recent data released by the Federal Treasury, within January–May 2015 the federal budget revenues contracted by 2.2 p.p. of GDP, and the expenses went up by 3.3 p.p. of GDP on the same period of the previous year. Revenues and expenses of the consolidated budget of the subjects of the Russian Federation over January–April 2015 went up 1.1 and 0.3 p.p. of GDP, respectively. The amount of the federal budget deficit for the first five months of 2015 constituted 3.7% of GDP, while the consolidated budget of RF subjects over January–April of 2015 has been executed with a surplus of 2.4% of GDP. On 25 June 2015, The RF Government approved in principle basic parameters of the 2016 Federal Budget and planned period of 2017–2018 taking account of latest trends in the GDP movement and oil prices, long-term risks and challenges including linked to structural and demographic imbalances in the economy.

The preliminary estimates of the federal budget execution in January–May 2015

Over January–May 2015, the federal budget revenues amounted to 19.0% of GDP (Rb 5,359.7bn) down 2.2 p.p. of GDP from the same period 2014 (Table 1); in absolute terms the federal budget revenues over five months of 2015 against the same period of 2014 shrank by Rb 522.9bn or by 8.8% in nominal terms. Oil and gas revenues continued falling and by five months-end 2015 and their volume came to 8.8% of GDP (Rb 2,471bn) down 2.5 p.p. of GDP or Rb 677.3bn below the volume of oil and gas revenue against corresponding period 2014. At the same time. Oil and gas revenues over January–May 2015 went up by 0.3 p.p. of GDP on the five months 2014 to 10.2% of GDP (Rb 2,888.3bn).

Over the first five months 2015, the volume of the federal budget expenditure reached 22.7% of GDP up 3.3 p.p. of GDP on the same period 2014. When taken in absolute terms, the federal budget expenditure went up by Rb 1,001.5bn or by 18.6% in nominal terms. By the end of January–May 2015, the federal budget was executed with the deficit of 3.7% of GDP

(Rb 1,048.2bn) down 5.4 p.p. of GDP against the surplus balance of the federal budget for the same period 2014. Oil and gas deficit also went up to 12.5% of GDP up 2.9 p.p. of GDP against January–May 2014.

Over five months 2015, the federal budget revenues in terms of share of GDP demonstrated different movement in comparison with the same period 2014 (Table 2). Revenues from the foreign economic activity shank by 3.5 p.p. of GDP on the same period 2014 to 4.6% of GDP or by 42.6% in nominal terms.

Over January–May 2015, receipts from the Mineral Extraction Tax (MET) went up by 0.4 p.p. of GDP on the corresponding period 2014 to 4.8% of GDP. In nominal terms, growth constituted 10.7%. Proceeds to the revenue part of the federal budget over five months 2015 from domestic VAT increased by 0.4 p.p. of GDP and from import VAT shrank by 0.1 p.p. of GDP on five months 2014. In nominal terms, revenues generated from domestic VAT grew by 13.1% and from import VAT down by 3.4%. In January–May 2015 on five months 2014, the federal budget revenues in terms of share of GDP generated from domestic excises remained unchanged and came to 0.7% of GDP (increase 5.5%

Table 1

MAIN PARAMETERS OF THE FEDERAL BUDGET FOR JANUARY–MAY 2014 AND JANUARY–MAY 2015

	January–May 2015		January–May 2014		Changes	
	bn Rb	% of GDP	bn Rb	% of GDP	bn Rb	p.p. of GDP
Revenues, of which:	5,359.7	19.0	5,882.6	21.2	522.9	-2.2
Oil and gas revenues	2,471.4	8.8	3,148.7	11.3	677.3	-2.5
Non-oil and gas revenues	2,888.3	10.2	2,233.9	9.9	649.4	0.3
Expenditures, of which:	6,407.9	22.7	5,406.4	19.4	1,001.5	3.3
Interest	210.0	0.7	165.0	0.6	45.0	0.1
Non-interest	6,197.9	22.0	5,241.4	18.8	956.5	3.2
Surplus (deficit) of the federal budget	-1,048.2	-3.7	476.2	1.7	-1,524.4	-5.4
Non-oil and gas deficit	-3,519.6	-12.5	-2,672.5	-9.6	-847.1	-2.9
GDP estimations	28137		27728			

Sources: RF Federal Treasury, Ministry of Finance, Gaidar Institute calculations.

Table 2

RECEIPTS FROM THE MAIN TAXES IN THE FEDERAL BUDGET IN JANUARY–MAY 2014 AND JANUARY–MAY 2015

	January–May 2015		January–May 2014		Changes in p.p. of GDP
	bn Rb	% of GDP	bn Rb	% of GDP	
Tax receipts, total, of which:	4,764.7	16.9	5,417.1	19.5	-2.6
Corporate income tax	236.9	0.8	159.5	0.6	0.2
VAT on goods sold in RF	1019.6	3.6	901.8	3.2	0.4
VAT on goods produced in RF	645.5	2.3	667.4	2.4	-0.1
VAT on goods produced in RF	211.8	0.7	200.0	0.7	0.0
Excises on goods produced in RF	18.1	0.06	27.3	0.1	-0.04
Mineral extraction tax	1,343.4	4.8	1,214.5	4.4	0.4
Revenues from the foreign economic activity	1,289.4	4.6	2,246.7	8.1	-3.5

Sources: RF Federal Treasury, Gaidar Institute calculations.

Table 3

FEDERAL BUDGET EXPENDITURE FOR JANUARY–MAY 2014 AND JANUARY–MAY 2015

	January–May 2015		January–May 2014		Changes in p.p. of GDP
	bn Rb	% of GDP	bn Rb	% of GDP	
Expenditure, total, of which:	6,407.9	22.7	5,406.4	19.4	3.3
Nationwide issues	388.4	1.4	343.3	1.2	0.2
National defense	1,846.8	6.6	1,297.5	4.7	1.9
National security and law-enforcement activity	735.3	2.6	737.7	2.7	-0.1
National economy	658.3	2.3	608.0	2.2	0.1
Housing and utilities sector	46.9	0.2	38.8	0.1	0.1
Environment protection	25.9	0.09	16.5	0.06	0.03
Education	275.8	1.0	273.0	1.0	0.0
Culture and cinema	32.3	0.1	29.2	0.1	0.0
Health care system	186.1	0.7	177.2	0.6	0.1
Social policy	1,657.0	5.9	1,341.5	4.8	1.1
Physical culture and sports	29.2	0.1	12.8	0.05	0.05
Mass media	32.2	0.1	30.8	0.1	0.0
Public debt servicing	210.0	0.7	165.0	0.6	0.1
Interbudgetary transfers	283.5	1.0	335.0	1.2	-0.2

Sources: RF Ministry of Finance, Gaidar Institute calculations.

in nominal terms), meanwhile, proceeds from import excises declined by 0.04 p.p. of GDP (reduction by 33.7% in nominal terms). In January–May 2015, proceeds generated from the corporate profit tax in terms of share of GDP up 0.2 p.p. of GDP or 48.6% in nominal terms against the same period 2014.

Over the first five months 2015 against January–May 2014, the volume of federal budget expenditure (Table 3) in terms of share of GDP demonstrated the following changes:

- expenditure on the national defense up 1.9 p.p. of GDP or up 1.4 times in nominal terms;
- expenditure under the item 'Social policy' up 1.1 p.p. of GDP or up 23.6% in nominal terms;
- expenditure under the item 'National security and law-enforcement activity' in term of share of GDP down 0.1 p.p. of GDP; in absolute terms contraction constituted Rb 2.4bn.;
- expenditure under the item 'National economy' and 'Nationwide issues' in terms of share of GDP up 0.1 and 0.2 p.p. of GDP, respectively; in nominal terms growth constituted 8.3 and 13.2%, respectively;
- expenditures under the item 'Interbudgetary transfers' in terms of share of GDP down 0.2 p.p. of GDP or by 15.3% in nominal terms;
- expenditure on education in terms of share of GDP stayed unchanged and constituted 1.0% of GDP, in absolute terms expenditure on education went up by Rb 2.8bn;
- expenditure of health care system in terms of share of GDP up 0.1 p.p. of GDP and Rb 8.9 bn;
- expenditures on government debt servicing up 0.1 p.p. of GDP to 0.7% of GDP or up 27.3% in absolute terms;
- the corresponding indices for the other federal budget expenditure items change only slightly in terms of share of GDP, and in the range between 0.03–0.05 p.p. of GDP.

**MAIN PARAMETERS OF THE CONSOLIDATED BUDGET OF RF SUBJECTS FOR JANUARY–APRIL 2014
AND JANUARY–APRIL 2015**

	January–April 2015		January–April 2014		Changes in p.p. of GDP
	bn Rb	% of GDP	bn Rb	% of GDP	
Revenue, of which:	3,163.8	14.1	2,840.5	13.0	1.1
Corporate profit tax	955.7	4.3	763.4	3.5	0.8
personal income tax	806.0	3.6	776.1	3.5	0.1
excises of goods produce in RF	155.2	0.7	152.4	0.7	0.0
tax on aggregate income	157.2	0.7	144.3	0.7	0.0
property tax	347.1	1.5	321.5	1.5	0.0
transfers from other budgets of the RF budgetary system	510.1	2.3	528.4	2.4	-0.1
Expenditure	2,615.4	11.7	2,501.7	11.4	0.3
Surplus (deficit) of consolidated budget	548.5	2.4	338.8	1.6	0.8
GDP estimates	22,404		21,843		

Sources: RF Federal Treasury, Gaidar Institute calculations.

End of June 2015, the RF Government adopted basic parameters of the 2016 federal budget and for subsequent 2017–2018, envisaging downward adjustment of planned indices for 2016–2017¹ on the so-called undistributed conditionally approved expenditure and gradual reduction of the federal budget deficit from 2.4% of GDP in 2016 to 0.7% of GDP in 2018. According the Ministry of Finance and the Government commission of budget projections, 2016–2018 budgets envisage reduction of budget outlays for public programs by 10% at the expense of reduction of inefficient expenses of their optimization.

Issues of pension indexation, social payouts and benefits remain open for debate. The Ministry of Finance propositions about maintaining indexation at the level adopted in the formation of the current budget for 2015–2017 in the volume of 5.5% in 2016 or 4.5% in 2017² is not supported by Olga Golodets, the deputy chairperson of the RF Government, who declared that “she intends to defend indexation of pensions and social payments in 2016–2018 to the full extent”³. The Ministry of Finance justified its position of limiting the size of pensions’ indexation and other social payments by the risk of the Pension Fund budget imbalancing which will result in additional increase of budget expenditure, decrease of wages growth rates, and need to check the inflation, meanwhile arguments of the vice premier about increasing the size of indexation are unknown yet.

In June 2015, the Government submitted to the State Duma a draft law on introducing changes in the

federal budget for 2015–2017⁴ with proposition to increase budgetary provisions on financing measures aimed at ensuring sustainable economic development and social stability in the amount of Rb 20.1bn. Part of additionally allocated funds for support of the economy in terms of contributions and subsidies to JSC and federal unitary enterprises⁵. It is envisaged to increase also the volume of subsidies to strategic organizations of the military-industrial complex. Not contesting expediency of additional budget expenditure, it is necessary to note, that in their activity these organizations ‘erode’ budget funds which leads to their non-target use and often direct stealing and one can expect that along with proposition to allocate additional funds, the Government will develop a packet of normative and legislative acts aimed at strengthening control over their use and measures to increase their efficiency.

**Analysis of the main parameters
of the consolidated budget execution
by RF subjects in January–April 2015**

As reported by the RF Federal Treasury, the *consolidated budget revenue of RF subjects* over the first four of 2015 amounted to Rb 3,163.8bn or 14.1% of GDP, which is by 1.1 pp. of GDP, or by 11.4% in nominal terms, higher than the same index for January–April 2014. The consolidated budget expenditure of RF subjects over the first four month of 2015, in terms of share of GDP, went up on the corresponding index for the same period of 2014 by 0.3 pp. of GDP to 11.7 % of GDP, or Rb 2,615.4bn (*Table 4*).

1 Included in adopted budget for 2015–2017.

2 In 2018, it is proposed to index expenditure by target inflation rate -4%.

3 <http://www.forbes.ru/news/292443-golodets-pobeshchala-otstavit-indeksatsiyu-pensii-v-polnom-obeme>

4 <http://government.ru/activities/18448/>

5 FSUE “Headquarters of special construction in Far Eastern Federal okrug under the Federal Agency of special construction,” JSC “Corporation of Far Eastern Development”, “Deposits Insurance Agency”.

By the end of January–April 2015, the *consolidated budget revenues of RF subjects* over the first four of 2015 was executed with a surplus at 2.4% of GDP (Rb 5,485bn) up 0.8 p.p. of GDP against budget surplus of the same period of 2014.

An analysis of the structure and movement of the consolidated budget (tax-generated and non-tax) revenue items of RF subjects for January–April of 2015 and January–April of 2014 revealed the following trends:

- profit tax receipts up 0.8 p.p. of GDP to 4.3% of GDP or by 25.2% in nominal terms; at the same time, growth of proceeds generated by the profit tax from organizations engaged in production sharing agreements¹ from Rb 61.2 to Rb 125,4bn (4 months of 2014 and 4 months of 2015);
- personal income tax (PIT) receipts up 0.1 p.p. of GDP to 3.6% of GDP or by 3.8% in nominal terms. Across PIT revenues structure there is a growth:
 - up 2.3-fold (from Rb 2.2 to 5.0bn) receipts in terms of fixed advance payments from income obtained by individuals who are foreign citizens and holding patents;
 - up 10.7% (from Rb 2.4 to 2.6bn) proceeds from the income generated by economic activity of individuals².

In absolute terms proceeds growth from these taxes is insignificant, however, this trend testifies about the stability of profit obtained by private entrepreneurs in the wake of economic slowdown as well as increased quality of PIT administration, on the whole;

- proceeds from domestic excises in shares of GDP remained unchanged and came to 0.7% of GDP and went up by 1.9% in nominal terms;
- proceeds from taxes on aggregate income and property tax in terms of shares of GDP remained unchanged and constituted 0.7 and 1.5 p.p. of GDP, respectively with growth by 9.1 and 8.0% in nominal terms respectively;
- contraction of revenues from uncompensated receipts from other budgets of the RF budgetary system by 0.1 p.p. of GDP to 2.3% of GDP or by 3.4% nominal terms.

Proper revenues of the consolidated budget of the RF subjects constituted Rb 2,653.7bn (11.9% of GDP) up Rb 341.6bn and up 1.3 p.p. of GDP against the

same period 2014. Nevertheless, the issue of ability of regional budgets to fully and timely meet obligations on public debt servicing remains open. According to the RBC data³, the first Russian region late with interest payment (default by Standard & Poors⁴ definition) was the Novgorod region and feasibility that other RF subjects will face the issue of liquidity shortage for redeeming or refinancing debt.

The fact that makes matters worse is that despite the surplus of the RF consolidated budget drawn during January–April 2015, as of 1 May 2015 the vast majority of regions (about 70) had a zero balance of budget funds on credit institutions' accounts while total volume of balance of funds of RF subjects totaled Rb 156.2mn.⁵ Thus, main burden for cutting risks of non-payments by regional budgets will be transferred to the federal level. There are several options: increasing volumes of interbudgetary transfers in order to raise the level of budgetary provision of the RF subjects and/or increasing volumes of budgetary loans as replacement of more expensive bank credits and/or strengthening measures of administrative character.

Regarding interbudgetary transfers from the federal center to regions, the trend demonstrates their contraction in terms of share of GDP over last two years. Only during January–April 2015, subsidies to the budgets of RF subjects and municipalities shank by 0.2 p.p. of GDP or by 16.5% in volume terms against the same period of 2014 (Table 5), including biggest contraction (twofold) is observed on subsidies to budgets aimed at ensuring budget balance. A number of experts consider that this situation significantly affects the budget sustainability of RF subjects. Nevertheless, not everything is so clear.

Over January–April 2015 against the same period of 2014, movement of revenues of the consolidated budgets of RF subjects demonstrates an increase in the volume of transfers directed at assisting socio-economic development in long-term perspective; in particular, went up:

- over threefold (from Rb 3.6 to 11.2bn) amounts of subsidies directed at cofounding of capital investment in the projects of public (municipal) property;
- sums of subsidies directed at refund of part of interest rate on short-term credits obtained for horticulture development (by Rb 2.2bn);

1 Signed prior to come into effect FZ of 30 December 1995 № 225-FZ "On agreements of production sharing" and not envisaging special tax rates for transfer to the federal budget and budget of RF subjects.

2 Individuals registered as self-employed entrepreneurs, notary officers engaged in private practice, lawyers setting their offices and other individuals engaged in private practice in compliance with article 227 of RF Tax Code.

3 Information as of 1 June 2015 <http://top.rbc.ru/economics/09/06/2015/557706719a794772e63bd6b2>.

4 S&P considers situation as a default when "borrower failed to meet debt obligations on time and in full" and not only failing to meet obligations on bonds. In more detail see RBC. <http://top.rbc.ru/economics/09/06/2015/557706719a794772e63bd6b2>

5 CB data: <http://www.cbr.ru/statistics/UDStat.aspx?Month=05&Year=2015&TbID=302-25>

Table 5

STRUCTURE OF THE CONSOLIDATED BUDGET REVENUES OF THE RF SUBJECTS ACROSS INTERBUDGETARY TRANSFERS FOR JANUARY–APRIL 2014 AND JANUARY–APRIL 2015

	January–April 2015		January–April 2014		Changes, p.p. of GDP	Changes in volume terms, %
	bn Rb	% of GDP	bn Rb	% of GDP		
Uncompensated receipts from other budgets of the RF budgetary system, of which:	510.1	2.3	528.4	2.4	-0.1	-0.1
1) Subsidies to the budgets of the subjects of the Russian Federation and municipalities, of which:	227.0	1.0	271.9	1.2	-0.2	-16.5
subsidies for leveling-off budgetary maintenance	195.3	0.9	211.5	1.0	-0.1	-7.7
subsidies to budgets aimed at ensuring budgets balance	27.2	0.1	54.4	0.2	-0.1	-50.0
2) Subsidies to budgets of the RF budgetary system	62.2	0.3	54.4	0.3	0.0	14.4
3) Subventions to budgets of RF subjects and municipalities	147.3	0.7	136.8	0.6	0.1	7.7
4) Other interbudgetary transfers	73.6	0.3	65.3	0.3	0.0	12.7

- amount of subventions (by 7.7%) including for support of least protected groups of population regarding housing payment and unemployment benefits will permit to sustain the level of consumer demand.

Relatively viable mechanism of ensuring regional budgets sustainability concentrates in the center's policy aimed at replacement of more expensive commercial credits and public bonds of the RF subjects with the public budget loans at the rate of 0.1% annual. However, for whatever reason, the process of replacement is a slow one: over four months 2015 in the total volume of public debt of the RF subjects the share of public budget loans went up insignificantly from 31.0% to 35.9%. However, efficiency of this approach

is directly dependent on the sustainability of the trend aimed at increasing tax revenues of the regions (first of all, from the profit tax). However, due to unclear state of the prospects of the Russian economy recovery, sustainability of this trend is in doubt.

Looking back at the issue of arrears in payment of credit liabilities of the Novgorod region, it is necessary to specify that according to the data of RBC "the region was unlucky regarding the dates because in the wake of the crisis not a single bank submitted entry for an auction at the start of the year because all considered the rate of 23.63% too low". The situation when a region allows arrears in payment due to internal reasons speaks for a low quality of financial management and as a result about the need to cor-

Table 6

CONSOLIDATED BUDGET EXPENDITURE FOR JANUARY–APRIL 2014 AND JANUARY–APRIL 2015

	January–April 2015		January–April 2014		Changes, p.p. of GDP
	bn Rb	% of GDP	bn Rb	% of GDP	
Expenditure, total:	2,615.4	11.7	2,501.7	11.4	0.3
Of which:					
Nationwide issues	170.8	0.8	162.9	0.7	0.1
National security and law-enforcement activity	28.1	0.1	25.3	0.1	0.0
National economy	393.3	1.7	366.8	1.7	0.0
Housing and utilities sector	187.8	0.8	192.6	0.8	0.0
Environment protection	6.3	0.03	5.3	0.03	0.0
Education	745.3	3.3	742.5	3.4	-0.1
Culture and cinema	94.0	0.4	88.5	0.4	0.0
Health care	400.7	1.8	372.4	1.7	0.1
Social policy	480.8	2.1	448.0	2.0	0.1
Physical culture and sports	49.8	0.2	47.7	0.2	0.0
Mass media	13.0	0.06	12.4	0.06	0.0
Government and municipal debt servicing	44.1	0.2	33.1	0.1	0.1

Sources: RF Federal Treasury; Gaidar Institute calculations.

rect steps of administrative/supervisory nature in the sphere of management of the RF subjects' obligations. Otherwise, neither increase of grants to the regions nor the policy of replacement of bank credits will not ensure budget system sustainability in the long-term.

The consolidated budget expenditure of the RF subjects (*Table 6*) as of the end of January–April 2015 across the majority of lines in terms of the share of GDP and in absolute terms changed insignificantly or remained at the level of corresponding level of 2014.

Cash execution of the regional budgets' expenditure for January–April 2015 comes to 27.2% which is comparable with the level of execution of the subjects' consolidated budgets for the same period of 2014 – 26.3%. Over January–April 2015, evenness of cash execution of regional budgets across function costs items is also observed, except expenses in budget item 'general interbudgetary transfers' where

cash execution constitutes 1.5% or Rb 309.5bn while approved annual budgetary appropriations constitute Rb 21.0bn. Thus, municipalities become 'hostages' of austerity regional policy. Taking account sensitivity of budget revenues of municipalities from the state of the economy and from the volume of local authorities' obligations for financing educational institutions and health care organizations, the state of grants to municipal budgets should become the focus of constant federal monitoring.

On the whole, in near-term the state of the budgetary system does not raise fears. Main risks in mid-term are determined by selection of the budgetary system deficit balance, expenditure on support of economic growth and financing of social and defense costs. Long-term risks of the budgetary system sustainability are linked with the quality of public finance management. ●