

Draft Budget Law for 2008 becomes even more socially oriented

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- On November 21 the Government approved the updated Draft State Budget for 2008.¹ The changes are mainly attributed to the revision of the forecast of key macroeconomic parameters, on which the budget is based. In particular, the forecast of nominal GDP was revised upwards by UAH 80 bn to UAH 890 bn, while the inflation of consumer prices is expected to be higher by 2.8 percentage points at 9.6%.

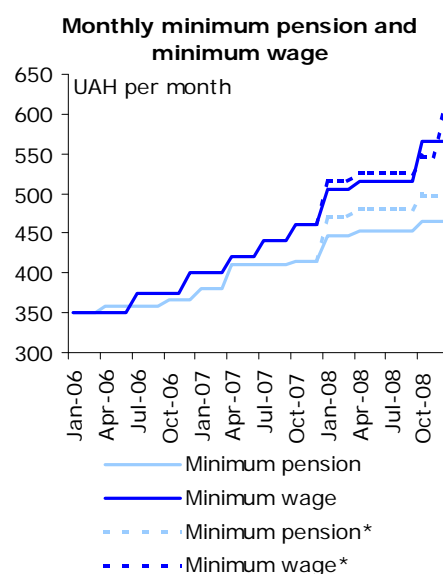
The adjustment of macroeconomic assumptions resulted in the upward revision of the consolidated fiscal revenues plan by UAH 19.3 bn to UAH 265.6 bn. Consequently the target of the consolidated fiscal expenditures has become higher by UAH 17 bn. Besides, it is foreseen to reduce the central fiscal deficit to UAH 16.5 bn (1.86% of GDP).

The major part of additional funds (UAH 16.2 bn) is traditionally planned for financing higher social payments. Therefore, the budget becomes even more socially oriented. First of all, the subsistence minimum, minimum wage and minimum pension would be further raised. Their growth rates are higher than in 2007 and exceed the forecasted inflation rate. Higher social standards, on the one hand, will contribute to higher real consumption, and, thus, the GDP. However, they will also add to the already high inflationary pressure.

In the updated Draft Law it is envisaged to change the principles of calculating pension payments. In particular, the value of a year of insurance record, which is used while estimating pension, is to be gradually increased from 1% to 1.35%. This measure, along with the previous initiative concerning increase of pension by 2% (instead of 1%) of due pension level for each year worked above the required working record (20 and 25 years for males and females respectively), are aimed at increasing pensions size as well as contributing to higher differentiation of pensions. At the same time, these initiatives would create significant pressure on the expenditure side of the Pension Fund budget. Though it is planned with zero deficit, the already substantial central fiscal transfer to the Pension Fund is to be increased by UAH 7.2 bn to UAH 33 bn (or 3.7% of GDP).

Other expenditures, in particular, financing of education, health care, science, culture and sport, are not planned to be significantly higher as compared to the previous version of the Draft State Budget. The exception are financing of the measures concerning the preparation and organization of the European Championship-2012, which are to be raised by 30% to UAH 3.9 bn. However, the absence of medium term budgeting in Ukraine makes questionable the efficiency of financing respective programs during next years.

Therefore, the State Budget for 2008 promises to be socially oriented. It is foreseen to increase substantially the current spending, in particular, wages and social payments. This is one of the threats of fiscal sustainability, as it is not possible to cut these expenditures if risks for budget execution are suddenly realised. This primarily concerns a slowdown of economic growth. Besides, high social spending diverts funds from financing capital outlays, which are essential for continuation of economic growth. It should be noted that in 2008 it is planned to finance large fraction of the capital outlays at the expense of unstable source, in particular, privatisation receipts, which is economically unjustified approach. This raises a question on their timely financing next year. It should be reminded that the privatisation plan has not been executed for several years in a row. The budget process promises to be difficult, while Budget approval by the end of 2007 requires tremendous efforts and coordination of activities of all authorities.



* according to the updated Draft State Budget
Source: State Budget Laws for 2006 and 2007, the Draft State Budget Law for 2008 (from September 14, 2007)

¹ According to the press-release of the Ministry of Finance from November 21, 2007 "The updated Draft Budget for 2008 is approved at the Government meeting". The first version of the Draft State Budget Law was submitted by the Cabinet of Ministers to the Verkhovna Rada on September 14, 2007.