

BUDGETARY SPACE FOR HEALTH IN UKRAINE

Policy document to support budget
preparation dialogue for 2021



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LIST OF ABBREVIATIONS

ACU	Accounting Chamber of Ukraine
COVID-19	novel coronavirus disease 2019-nCoV (COVID-19 virus)
CPI	consumer price index
EBRD	European Bank for Reconstruction and Development
EFF	Extended Fund Facility
GDP	gross domestic product
ICPC	International Classification of Primary Care
IMF	International Monetary Fund
LMIC	low- and middle-income country
MoEDTA	Ministry of Economic Development, Trade and Agriculture
NBU	National Bank of Ukraine
NHSU	National Health Service of Ukraine
OECD	Organisation for Economic Co-operation and Development
PBB	programme-based budgeting
PEFA	Public Expenditure and Financial Accountability
PFM	public financial management
PMG	Medical Guarantees Programme
UAH	Ukrainian hryvnia (currency)
UNICEF	United Nations Children's Fund
VAT	value-added tax
WHO	World Health Organization



INTRODUCTION

Ukraine is kick-starting dialogue on increasing funding for health care; a challenging task in the current macro-fiscal context, which is overshadowed globally by coronavirus disease (COVID-19). With the country's public spending on health care standing at 3.2% of gross domestic product (GDP) in 2019 – considerably behind its central European neighbours (OECD, 2020) – along with consistently declining levels of consolidated government spending on health, and the spotlight the global pandemic has placed on health system weaknesses and poor resourcing practices, the Government of Ukraine has restarted discussions on ways to better fund health. Despite the political will to find extra resources for health, in times of macro-fiscal turmoil this remains a political and technical challenge.

The idea of finding more funds – **or extending budgetary space** – for health has three dimensions (Barroy & Gupta, 2020):

1. Possibilities to **increase the overall public expenditure envelope defined by the existing fiscal space** depend on the country's macroeconomic performance and scope for additional public spending. The International Monetary Fund (IMF) defines fiscal space as “the room for undertaking discretionary fiscal policy relative to existing plans without endangering market access and debt sustainability” (IMF, 2018). Recent research for WHO and the Center for Global Development (Barroy & Gupta, 2020) shows that increasing overall expenditure envelopes is usually the main driver of higher allocations of funding for health, especially among low- and middle-income countries (LMICs) (which includes Ukraine, according to its income status).
2. The approach of **increasing the share of the expenditure envelope dedicated to health by reallocating funds away from other functions** was found to be relatively unusual among LMICs, according to Barroy & Gupta's multi-country research (compared to increases in the overall spending envelope achieved by new revenue, new borrowing or other financing sources) (Barroy & Gupta, 2020). While budget reprioritization remains an option, the WHO research shows that reallocation of funds towards health is not only a matter of political choice but also depends on the Ministry of Healthcare's capacity to prepare and negotiate budget proposals.
3. The third dimension involves **enabling increased spending on health by budgeting better**. Implementing more efficient rules in public financial management (PFM) by ensuring that health funding allocations are reliable, timely, flexible and strategic can enlarge the health sector's budgetary space, especially if accompanied by thorough planning and execution of health budgets by the Ministry of Healthcare (Barroy & Gupta, 2020).

This summary paper provides background on each of these dimensions of potential budgetary space for health in Ukraine, along with draft recommendations on how to enlarge that space in the medium term. Intended as a technical brief, it is based on the new methodology for budgetary space diagnostics proposed by Barroy & Gupta (2020), and uses health financing analysis undertaken for the upcoming World Bank public expenditure review (World Bank, 2020) to provide ideas for policy-makers working on extending and developing health and budgeting reforms in Ukraine, while also being useful for wider civil society and international observers.

BUDGETARY SPACE FOR HEALTH IN 2015–2020

Health spending per capita has increased in real terms (by 20% from 2015 to 2020), but this increase is partially explained by the decline in population size (2.9% across the period analysed), and was much slower than economic growth (Table 1). Moreover, consolidated health spending as a percentage of GDP significantly declined (from 3.6% to 3.0%, equating to almost 15%), which means government spending on health grew much slower than the economy. If this trend continues at the same rate (3%) into 2021, real health spending per capita is expected to decrease by 8.4%.

Health spending did not grow on a par with GDP because state spending overall was shrinking and, in the smaller budgetary envelope, health was not prioritized. Table 1 demonstrates the effect of the two major factors in the country not expanding budgetary space for health in line with economic growth during 2015–2020:

- i. To achieve recovery and enable longer term growth, the Government reduced overall state spending (from 34.2% to 32.9% of GDP), which meant that the overall size of the spending envelope had actually shrunk.
- ii. The Government also chose to reduce the share of the budget allocated to health (from 10.4% in 2015 to 9.2% in the 2020 plan).

Table 1. Changes in health financing, 2015–2020

	2015	2016	2017	2018	2019	2020 planned	2021 projected**	% change	
								2020 to 2015	2020 to 2021
Consolidated budget spending on health									
Real spending on health per capita (2015, UAH)*	1 657	1 553	1 850	1 897	1 959	1 988	1 848	20.2	-8.4
Real spending on health (2015, UAH)*	71.0	66.3	78.6	80.2	82.3	83.2	77.0	17.1	-8.7
Spending on health (% of GDP)	3.6	3.2	3.4	3.3	3.2	3.0	3.0	-14.8	0
Key drivers									
Population size (million)	42.8	42.7	42.5	42.3	42.0	41.8		-2.4	
Economic growth (% change, real GDP)	-9.8	2.4	2.5	3.4	3.2	3.7			
Consolidated spending (% of GDP)	34.2	35.0	35.4	35.1	34.5	32.9		-3.7	
Share of health in consolidated spending	10.4	9.0	9.7	9.3	9.4	9.2		-11.5	

* UAH: Ukrainian hryvnia. The real spending figures reflect adjustment for inflation based on the change in year-over-year consumer price index (CPI) (which measures price changes based on a specified basket of consumer goods and services). The real GDP growth rate reflects adjustment based on annual changes in the GDP deflator, which during 2015–2020 grew much faster than the CPI. As a result, deflator-adjusted real GDP growth depicts a slower dynamic compared to CPI-adjusted changes in real spending.

**Projection assumes: 2015–2020 average rate of change in population size; 2020 share of spending on health as % of GDP; GDP and price changes based on the median consensus forecast.

Sources: Consensus forecasts of the Ministry of Economic Development, Trade and Agriculture (MoEDTA, 2020c); State Treasury Service of Ukraine (2020b); State Statistics Service of Ukraine (2020a, 2020b, 2020c).

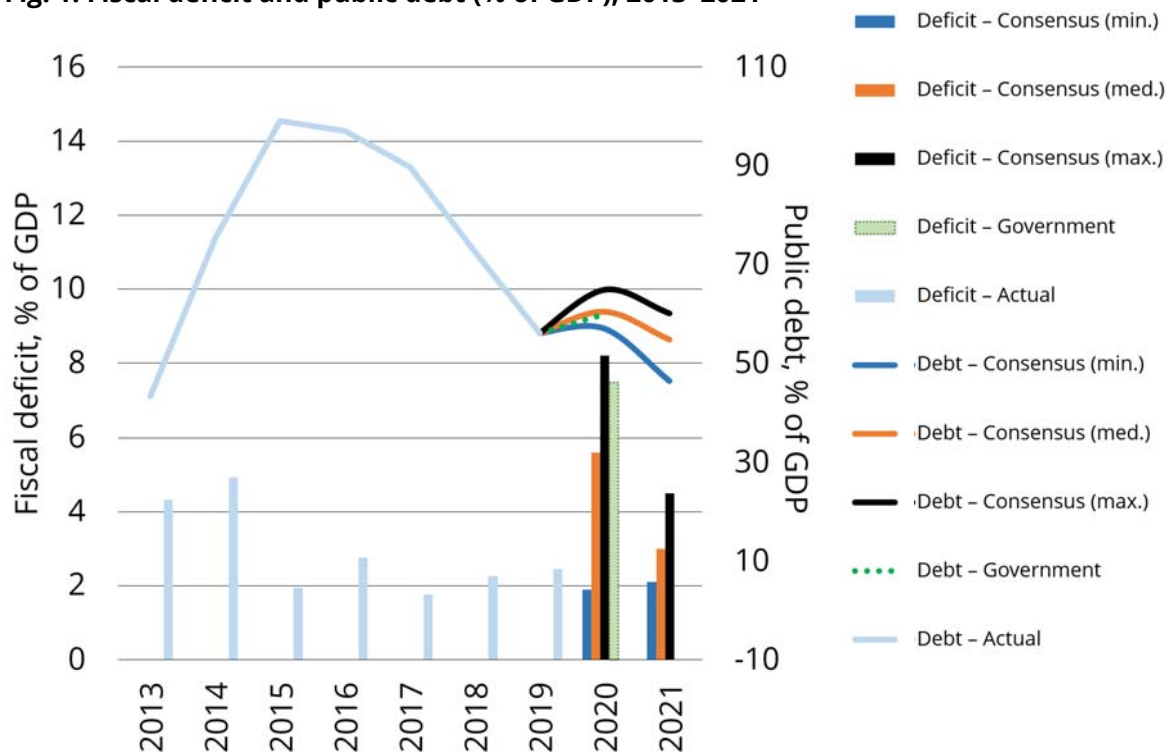
ASSESSMENT BY COMPONENT

1 | Overall public expenditure

During 2014–2016, Ukraine managed to eradicate persistent quasi-fiscal deficits, weathering the economic crisis through bold structural reforms and earnest fiscal consolidation in order to remove macro-fiscal imbalances and reduce public debt (from 4.9% of GDP in 2014 to 1.8% in 2017)¹ (see Fig. 1). By 2016, growth was restored, inflation significantly reduced and international reserves partly recovered (see Fig. 2). These developments were supported by an IMF Extended Fund Facility (EFF) designed to support macroeconomic stabilization and the anti-corruption reform agenda in the post-Maidan Revolution context (IMF, 2019).

Prudent fiscal policies kept the economy stable, but it remained vulnerable because of slow growth (in international comparison), political uncertainty, and uneven business, judiciary and anti-corruption reforms. The IMF raised concerns about this evidence of Ukraine's sustained economic vulnerability to risk (including a large proportion of foreign currency debt, increasing vulnerability to variation in exchange rate) and advised the country to operate tighter fiscal policy aiming to help keep the public debt under control (with a primary surplus of 1.0–1.5% of GDP). The recommended approach also included resisting populist policy, avoiding tax cuts, and improving revenue administration (IMF, 2019).

Fig. 1. Fiscal deficit and public debt (% of GDP), 2013–2021



Sources: Consensus forecasts of the MoEDTA (2020c); 2020 State Budget Law (Verkhovna Rada of Ukraine, 2020).

The Ukrainian economy had started to contract before the COVID-19 crisis, with economic growth declining in the second half of 2019.² Currency appreciation impaired trading terms, and global slowdown reduced prices for key export items; simultaneously, government spending declined, reflecting deteriorating revenue performance and lower expenditure on energy subsidies. Industrial output started to contract, responding to lower demand and growing competition. From January 2020, Ukraine's GDP began to fall (down by 0.5% compared to January 2019) (MoEDTA, 2020a).

Anticipating and reacting to COVID-19 and the ensuing economic uncertainty, the Ukrainian Government downgraded its 2020 macroeconomic forecast, lowered GDP growth expectations, increased inflation and unemployment projections (Fig. 2), and revised mid-term planning to a one-year limit. The Budget Code was amended, suspending the requirement for the Government to develop a three-year budget declaration until 1 Jan 2021 (Verkhovna Rada of Ukraine, 2020).

Projections by Ukrainian and international partners are gloomy in the longer term.

- The latest consensus forecast³ covers the period 2020–2021 (MoEDTA, 2020c), with the projections predicting a significant deficit in the current account into 2021, in contrast to the Ukrainian Government's expectation of a 1.7% surplus (see Fig. 2 for details).
- The IMF forecasts a much deeper recession for Ukraine for the year 2020, and a slower recovery in 2021, with economic growth resuming (by 3.0%) in 2022; however, the Fund supports the expectation of continued current account deficits, and believes the surge in unemployment will be more pronounced and protracted.

In 2020 the Ukrainian Government intends to increase its deficit to 7.5% of GDP through substantial new borrowing. In April 2020, the law on amending the annual state budget was changed to accommodate revenue shortfall and new spending pressures resulting from COVID-19 (Verkhovna Rada of Ukraine, 2020) (see Table 2).⁴ The Government would cover about half of the new financing needs through additional foreign loans, and borrow the rest domestically (with the public debt growing to 59.9% of GDP).

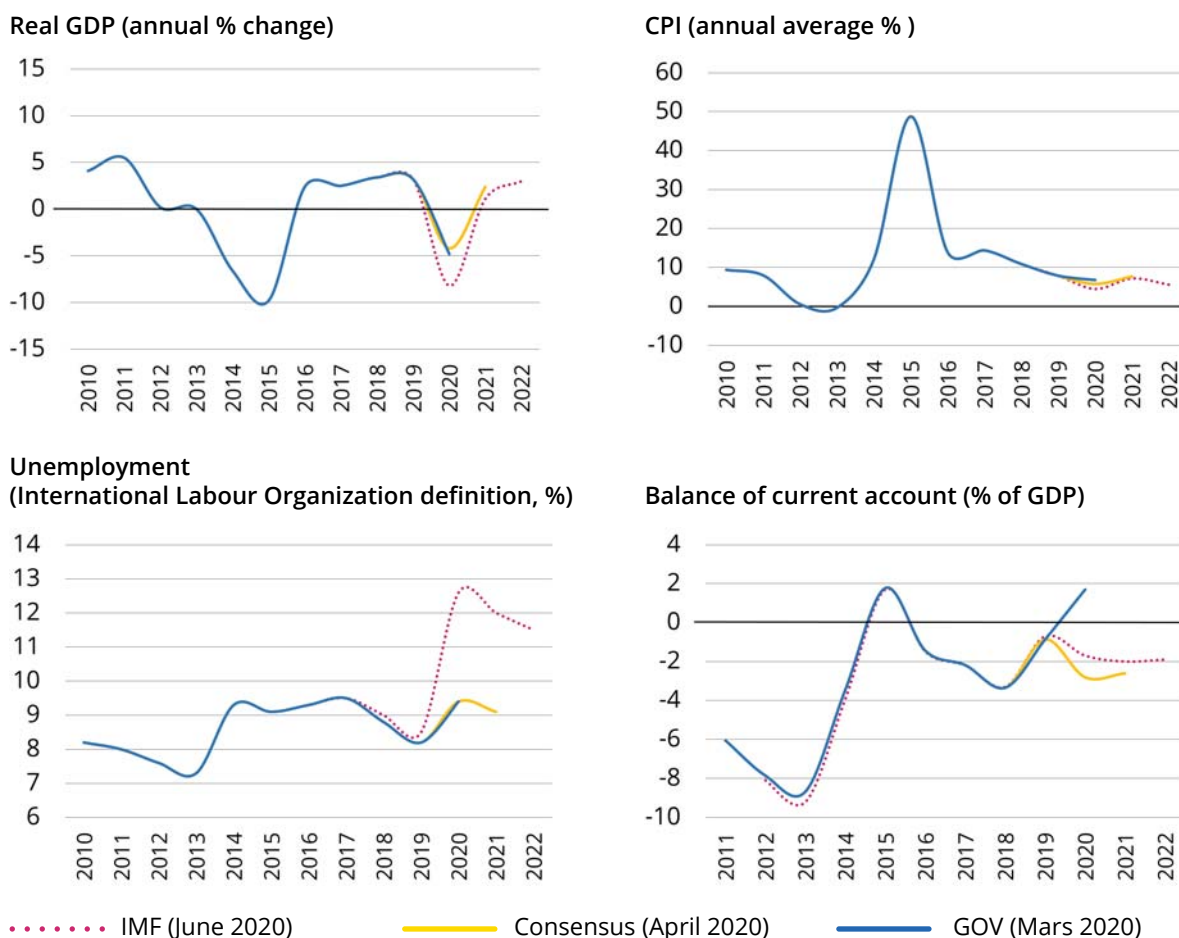
Macro-fiscal feasibility of the new deficit financing plans depends on the prospects of cooperating with the IMF. The mainstream expectation is that the bulk of Ukraine's external financing would originate from a new IMF programme, agreed by the IMF Executive Board in June 2020 following Ukraine's completion of certain required actions (including land reform and changes to banking regulations to insure against denationalization). Execution of the programme is also contingent on a range of structural benchmarks reflecting continued reforms, as the IMF believes that the risks to the programme are "very large", in terms of both global turbulence and uncertainty about the direction of economic policies in Ukraine.

² For more details (in Ukrainian), see the MoEDTA review on the final quarter of 2019 (MoEDTA, 2020b).

³ Macroeconomic projections are compiled by the MoEDTA and the United Nations Children's Fund (UNICEF), based on a survey of experts representing the Ministry of Finance, the National Bank of Ukraine (NBU), state research institutions, independent think-tanks and private investment companies (MoEDTA, 2020c).

⁴ The central government deficit is approved annually within the Budget Law, but without any overarching national regulation to impose limits. Stand-by arrangements can be made in cooperation with the IMF, limiting the budget deficit as a share of GDP (IMF 2019, 2020). In June 2020, the IMF approved a new stand-by arrangement for Ukraine, relaxing deficit ceilings in view of COVID-19 pressures (7.7% of GDP in 2020, but reducing to 5.3% in 2021 and 3.5% in 2022).

Fig. 2. Key macroeconomic totals, 2010 (or latest available year) to 2022 (predicted)



Sources: IMF (2020b); State Statistics Service of Ukraine (2020a, 2020b); NBU (2019a, 2019b); MoEDTA (2020c).

Table 2. Amendments to the 2020 State Budget Law resulting from COVID-19, April 2020

	Thousand UAH				% of GDP		
	Initial	Amended	Change (thousand UAH)	Change (%)	Initial	Amended	Change
Revenues	1 095 580 446	975 833 650	-119 746 796	-10.9	27.5	24.5	-3
Expenditure	1 199 231 214	1 281 624 506	82 393 292	6.9	30.1	32.2	2.1
Lending	-7 375 047	-7 386 547	-11.500	0.2	-0.2	-0.2	0
Deficit	96 275 720	298 404 308	202 128 588	209.9	2.4	7.5	5.1

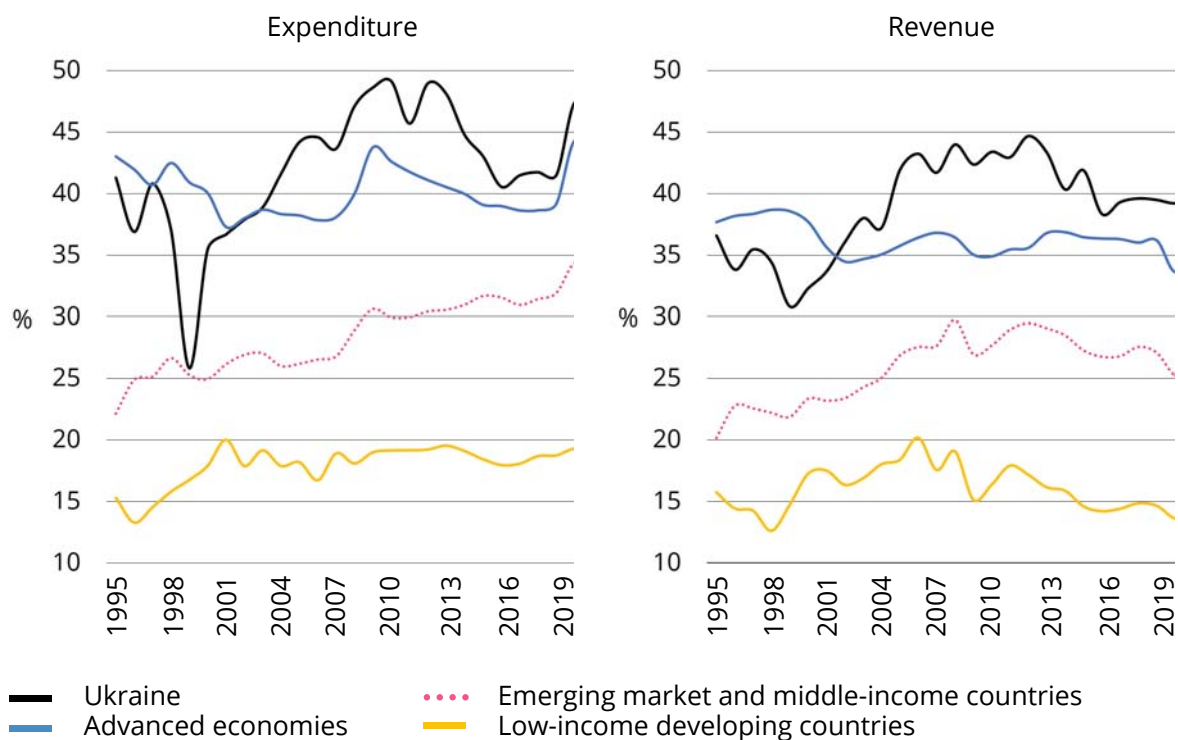
Source: Explanatory tables to the draft supplementary 2020 State Budget Law (Verkhovna Rada of Ukraine, 2020).

Disruption in cooperation with the IMF could sharply increase borrowing costs for the country, immediately undermining longer term debt sustainability. Alternative methods exist to finance the deficit but none of the existing forecasts seem to analyse the potential macro-fiscal effects of these, including any resulting inflationary pressures.

Increased spending on health in 2020 as part of the COVID-19 response will support recovery but the timing and extent of this effect is hard to quantify. A significant part of new spending approved in the supplementary budget in April 2020 is expected to go to health care. This includes an increase in the allocation to Ukraine's National Health Service (NHSU) (UAH 15.8 billion or about 0.4% of GDP) and a potentially significant share of the new COVID-19 Response Fund (UAH 64.7 billion or 1.6% of GDP), which is expected to cover extra medical costs as well as additional social protection measures. Such investment will naturally help to strengthen confidence, stimulate consumption through stronger financial protection, and minimize the health impact of the epidemic on Ukraine's labour force. However, the macro-fiscal benefit of this additional expenditure and its possible timing could not be quantified without additional research.

Ukraine's public expenditure as a share of GDP is high in global comparison (ranking 11th in the world in 2012 at 48.97%), so further increases in tax rates are not feasible (see Fig. 3). Even after a period of significant spending reduction, in 2019 it was still well above average for advanced economies, at 41.51% of GDP, with a share of 47.41% expected at the end of 2020. Government revenue as a share of GDP has also been very high traditionally, and – unlike in most advanced and emerging economies – the Government does not expect a decrease in 2020 (Fig. 3). Ukraine redistributes a significant amount of the GDP through the Government, yet state institutions remain weak and are not trusted by the population. If the quality of public services is not improved, further increases in taxes rates to expand the overall budget envelope are not advisable for Ukraine.

Fig. 3. Government expenditure and revenue as a % of GDP, 1995–2019



Notes. Totals refer to general government expenditure and revenue, covering central government, local governments, and social security funds.

Source: IMF Fiscal Monitor (IMF, 2020a).

Both immediately and in the longer term, the key potential source of extra fiscal space – to expand overall expenditure – is improved revenue administration. Ukraine’s revenue administration, referred to by the IMF as the “Achilles heel of Ukraine’s fiscal framework” (IMF, 2019), suffers from gaps in organization, management and oversight of the tax and customs systems, which undermine their fairness, enable corruption, and compromise government revenue. After the Revolution of Dignity in 2014, the Government proclaimed structural reforms in this area, including functional reorganization, improved audit and more efficient collection processes. Major improvements followed in revenue administration in 2015–2018 (notably in value-added tax (VAT) administration), and functional reorganization of the revenue service significantly intensified during 2019–2020, including transformations in the structure, transparency and collection processes for improved efficiency, compliance and fraud reduction. Unfortunately, these changes coincided with steep currency appreciation (affecting customs and VAT proceeds), a political wrestle with the tobacco industry (slowing down excise collections) and, most recently, the onset of the COVID-19 crisis, obfuscating the revenue impact of the improved administration.

| INTERMEDIATE CONCLUSION |

Expanding overall fiscal space by accumulating additional debt or new taxes would jeopardize Ukraine’s macro-fiscal stability. Despite eventually recovering from the 2014–2015 financial crisis, reducing debt and regaining market access through painful adjustment, the economy has not grown fast enough to ensure ongoing resilience, remaining highly vulnerable to changes in external market conditions. In the longer term, key potential sources of extra fiscal space are: (1) economic growth through a better business climate and stronger human capital; and (2) enhanced revenue administration. The unfolding COVID-19 crisis will hit Ukraine’s in areas in which it is already vulnerable: terms of trade, and exchange rate. The Government should therefore prepare to adjust macro-fiscal parameters again once the global economy stabilizes, likely entailing fiscal consolidation. It is therefore critical to access crisis-related borrowing in order to support recovery and stimulate growth in the longer term.

2 | Budget share for health

Since 2015, consolidated health-care expenditure has declined as a share of GDP and as a percentage of the consolidated budget (Table 3). Much of Ukraine's public expenditure contraction from 2012 to 2019 was due to a decrease in the expenditures of the Pension Fund; consolidated overall spending by central and local governments remained virtually unchanged. The amount of funds allocated to health care has declined over these years, both as a share of GDP and as a percentage of consolidated expenditure.

In consolidated spending (all tiers of government), health spending has been gradually crowded out by investment in economic infrastructure, education and security, across five key priority areas supported by the public sector at various levels of government: (1) economic activities (e.g. roads); (2) security and judiciary; (3) education; (4) housing and utilities; and (5) defence. See Table 3 for detailed data on the local and central government weighting for these investment areas.

Unlike consolidated spending, central government expenditure reduced significantly since the 2014–2015 crisis. Nonetheless, the share of central spending on economic activities, security, judiciary and defence was expanded, while the shares of health, education and social protection programmes decreased. Specifically, the share of central health spending (including earmarked transfers) was reduced from 11.0% to 9.6% across the period 2015–2020 (Table 4).

In 2017, Ukraine launched a major health financing reform which included centralizing spending on the essential benefits package under a national single payer – the NHSU (involving all primary care expenditure from 2018 and the entire package including specialized and emergency care from April 2020). The reform relieved local governments of their responsibility for financing essential services (except utility payments and capital costs), thus allowing them to redirect funds away from health. To compensate, the central Government substantially increased health funding in nominal terms during 2018–2020; however, the health allocation at the central level remained unchanged as a share of GDP (2.5%). See Table 4 for details of the health spending distribution in relation to other sectors throughout the period analysed.

In parallel, the Government gradually expanded its fiscal equalization scheme during 2015–2020, supporting economically deprived communities with unconditional revenue top-ups and indirectly benefiting health facilities. However, while the core (base) grant – allocated by a transparent formula – grew in nominal terms, it remains insufficient to sustainably cover delegated spending at the level of individual communities (Levitas & Djikic, 2019). The two other major block grants, defined without formula and allocated via regional administrations (not directly to local government budgets) were introduced as a temporary measure to address the uneven capacities of communities to adjust to reforms. These are a “stabilization” grant established in 2015, and an additional block grant from 2017 to maintain health and education facilities. Combined, they soon outstripped the base grant by almost UAH 5 billion.

Table 3. Consolidated spending priorities (all government tiers), 2015–2020

	Expenditure as a % of GDP						Expenditure as a % of total consolidated budget					
	2015	2016	2017	2018	2019	2020 planned	2015	2016	2017	2018	2019	2020 planned
Public administration	5.9	5.6	5.6	5.4	5.1	5.1	17.3	16.1	15.7	15.3	14.8	15.5
Incl. debt servicing	4.3	4.0	3.7	3.3	3.0	3.1	12.7	11.5	10.5	9.3	8.8	9.6
Defence	2.6	2.5	2.5	2.7	2.7	2.6	7.7	7.1	7.0	7.8	7.8	8.0
Security and judiciary	2.8	3.0	3.0	3.3	3.6	3.3	8.1	8.6	8.4	9.4	10.5	10.1
Economic activities	2.8	2.8	3.4	4.0	3.9	4.1	8.3	7.9	9.7	11.3	11.2	12.5
Environment	0.3	0.3	0.2	0.2	0.2	0.2	0.8	0.7	0.7	0.7	0.7	0.7
Housing and utilities	0.8	0.7	0.9	0.9	0.9	0.7	2.3	2.1	2.6	2.4	2.5	2.1
Health care	3.6	3.2	3.4	3.3	3.2	3.0	10.4	9.0	9.7	9.3	9.4	9.2
Culture and sports	0.8	0.7	0.8	0.8	0.8	0.8	2.4	2.0	2.3	2.3	2.3	2.5
Education	5.7	5.4	6.0	5.9	6.0	5.9	16.8	15.5	16.8	16.8	17.4	17.8
Social protection	8.9	10.8	9.6	8.7	8.1	7.1	25.9	30.9	27.0	24.7	23.4	21.4
Total	34.2	35.0	35.4	35.1	34.5	32.9	100.0	100.0	100.0	100.0	100.0	100.0

Sources: State Treasury Service of Ukraine (2020b); State Statistics Service of Ukraine (2020a).

Table 4. Spending priorities of the Ukrainian central Government (including transfers), 2015–2020

	Expenditure as a % of GDP						Expenditure as a % of total state budget (incl. transfers)					
	2015	2016	2017	2018	2019	2020 planned	2015	2016	2017	2018	2019	2020 planned
Public administration	5.2	5.0	4.8	4.6	4.3	4.3	18.1	17.4	17.2	16.7	15.9	16.4
Incl. debt servicing	4.2	4.0	3.7	3.2	3.0	3.1	14.6	14.0	13.2	11.7	11.1	11.9
Defence	2.6	2.5	2.5	2.7	2.7	2.6	9.0	8.7	8.9	9.8	9.9	10.0
Security and judiciary	2.7	3.0	2.9	3.3	3.6	3.3	9.5	10.5	10.5	11.9	13.2	12.6
Economic activities	1.9	1.5	1.8	2.3	2.3	2.7	6.6	5.1	6.3	8.2	8.4	10.3
Environment	0.2	0.2	0.2	0.2	0.2	0.2	0.7	0.7	0.6	0.5	0.6	0.7
Housing and utilities	0	0	0.1	0	0	0	0	0	0.2	0	0	0
Health care	3.2	2.4	2.6	2.5	2.5	2.5	11.0	8.4	9.4	8.9	9.1	9.6
Culture and sports	0.3	0.2	0.3	0.3	0.3	0.3	1.2	0.7	0.9	1.0	1.0	1.2
Education	3.7	3.3	3.1	3.0	3.1	3.2	12.9	11.6	11.1	10.8	11.6	12.3
Social protection	8.7	10.3	9.1	8.2	7.5	6.6	29.8	36.0	32.4	29.6	27.8	25.1
Block grants	0.4	0.3	0.7	0.7	0.7	0.5	1.3	1.0	2.6	2.6	2.4	1.8
Total	29.0	28.7	28.1	27.7	27.1	26.2	100.0	100.0	100.0	100.0	100.0	100.0

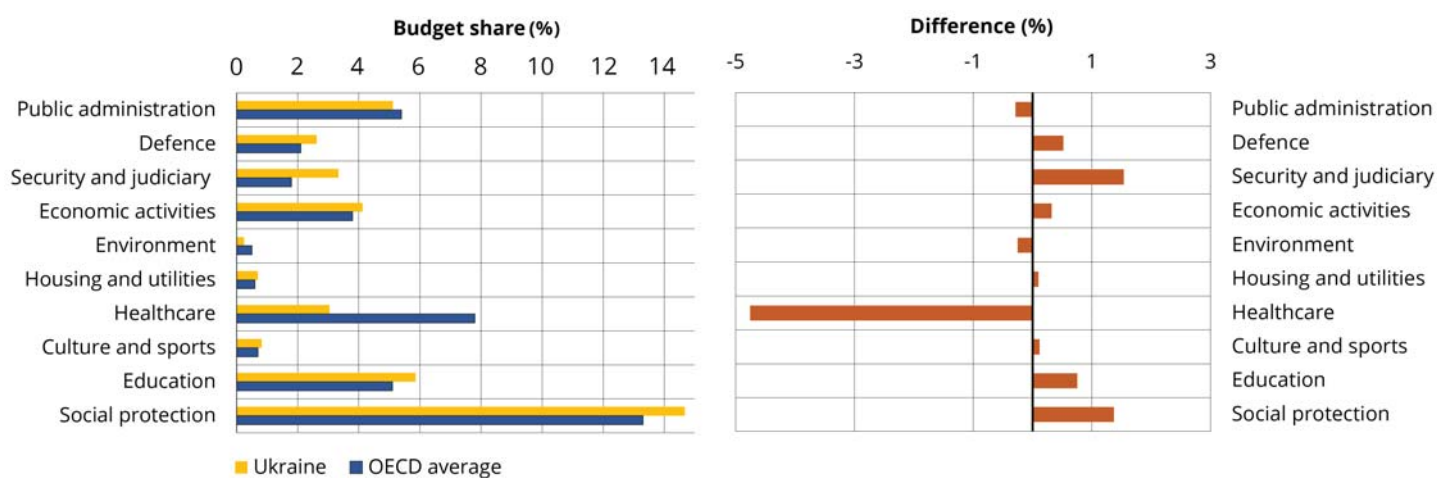
Sources: State Treasury Service of Ukraine (2020b); State Statistics Service of Ukraine (2020a).

The budgetary space acquired by transforming temporary non-formula grants could help to increase health spending as well, as it could also be used for stronger fiscal equalization. The temporary (non-formula) equalization grants could be viewed as a possible extension to the budgetary space for certain key functions, including health; however, as the central Government was consolidating resources in 2020 to cover the recently centralized responsibility for funding the essential benefits package, in reality it halved the additional block grant (intended for maintaining health and education facilities), and the redistributive consequences of this change are yet to be clearly established. That said, the transparently allocated component of the key fiscal equalization scheme is arguably very narrow. Since 2015, Ukraine's unfolding decentralization reform has resulted in a range of communities not having enough taxable employment to cover their delegated spending. Discretionary block grants could be redirected into making the core fiscal equalization system more robust (Levitas & Djikic, 2019).

One potential option would be for Ukraine to expand health financing by absorbing budgetary space released from declining debt repayment and servicing obligations as they start to clear away after 2020. The debt servicing pressures created by Ukraine's substantial new debt accumulated during 2013–2016 (Fig. 1) started to increase through 2018 and peaked in 2019–2020 (IMF, 2019). However, as a result of the economic growth, debt interest payments fell as a share of both GDP and the budget; so debt servicing has not thus far served to divert any budgetary space from other sectors. However, capitalizing on this potential new space for other expenditures would require Ukraine's debt to continue to decline, which is unlikely, given the need to borrow for the COVID-19 response.

Compared to the average for member countries of the Organisation for Economic Co-operation and Development (OECD), Ukraine allocates a much smaller budget share to health than to security and judiciary, social protection, and education. The functional composition of Ukraine's general government spending differs substantially from the OECD average (see Fig. 4), with the biggest divergence seen in health, which does not feature among the country's top five functional priorities. The proportion of general budget expenditure allocated to health is almost 5% lower than in the OECD countries.

Fig. 4. Functional composition of general government spending, Ukraine and OECD average, 2019



Sources: OECD Government at a Glance (OECD, 2019); State Treasury Service of Ukraine (2020a).

INTERMEDIATE CONCLUSION

In recent years no extra budgetary space has been created for health care resulting from reallocation of budget shares from other sectors. To the contrary; health financing has contracted in comparison to investment in economic infrastructure, education, and security, with no extra priority afforded to the health sector by the central Government, even when health financing reforms were initiated, reallocating spending responsibility to the national purchaser. This lack of prioritization of health in comparison to other sectors is a matter of political choice. Discretionary block grants, which are opaque, inefficient, and do not target health directly, remain a potential small addition to the health budget. However, this resource might be better used to improve Ukraine's fiscal equalization system. More promisingly, extra budget space could be leveraged from debt servicing payments, once the country's public debt is reduced, and consideration should be given to aligning the functional composition of general government spending with the OECD average (given the current exceptionally high share spent on security and judiciary).

3 | PFM

Historically, Ukraine's PFM system has been assessed as centralized and "rigid and control-oriented" (PEFA Secretariat, 2016), ensuring discipline but obstructing efficiency in public services provision and policy orientation of spending. A solid treasury system and strict budget execution controls proved beneficial during the 2014–2015 crisis, helping the Government to minimize arrears despite dramatic revenue shortfalls. However, the system lacked flexibility and focus on results, remaining vulnerable to fiscal risks from poor management of state enterprises and public assets (all of which have materialized again, during this latest crisis) (PEFA Secretariat, 2016).

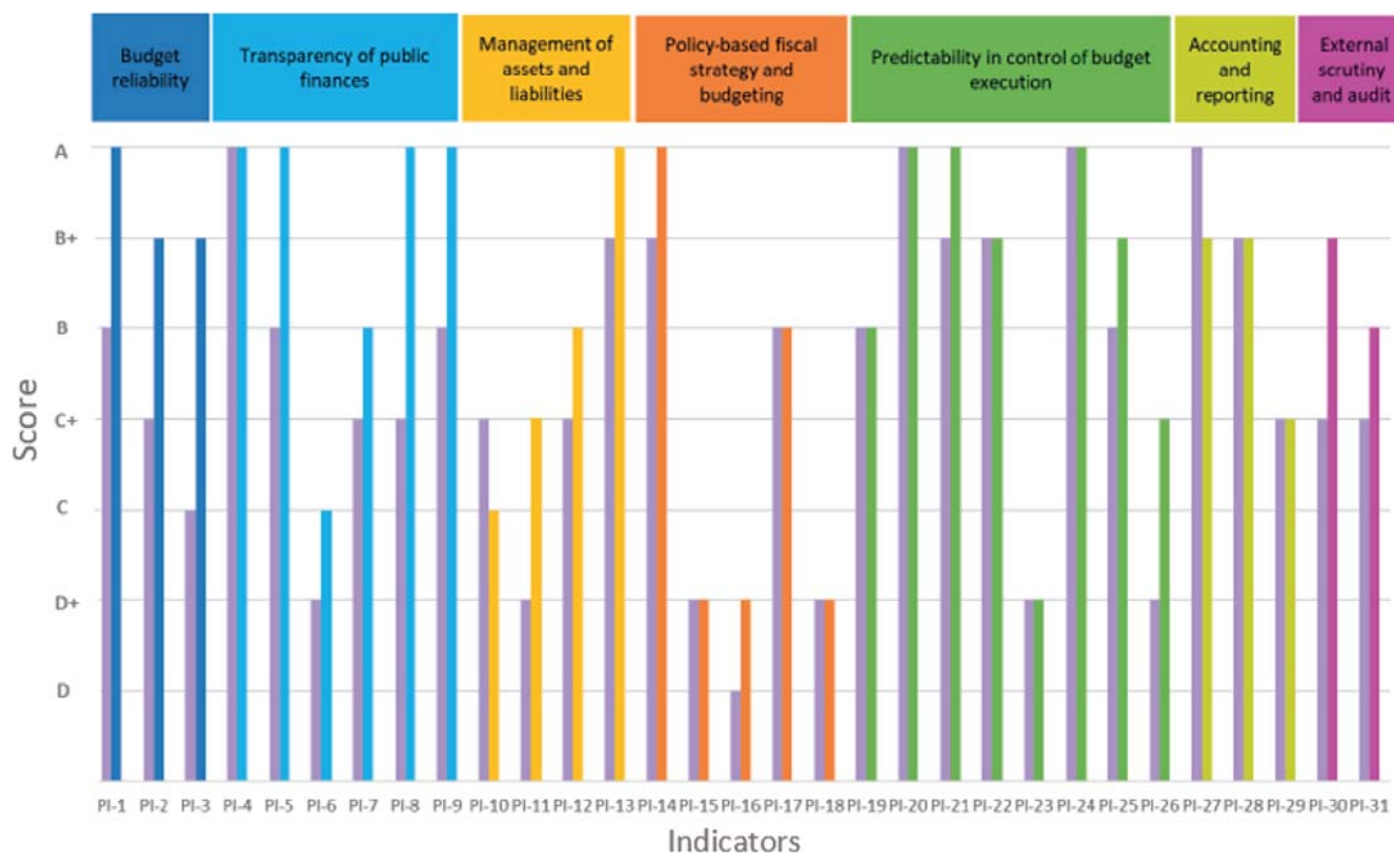
Since 2014, Ukraine has worked to make PFM rules more flexible and strategic, starting significant PFM reforms under the new Government in 2014 to fundamentally improve transparency, reliability, and external scrutiny of budget allocations. In 2017 a new PFM reform strategy was approved, aiming to modernize PFM to enable effective accumulation and allocation of resources, enhancing quality of public services and supporting mid- and long-term state policy priorities (Cabinet of Ministers of Ukraine, 2017). Some core achievements included the introduction of a wide range of budget transparency mechanisms and medium-term budgeting tools, and improved macroeconomic and budget forecasting (Shcherbyna et al., 2020). Improvements can be charted through the positive changes in assessment scores under the Public Expenditure and Financial Accountability (PEFA) framework between 2016 (covering the period 2011–2015) and 2019 (covering 2015–2018), as depicted in Fig. 5. Strategic budgeting remains an important area of focus in Ukraine, in which vast improvements could be made.

| BUDGET FORMULATION |

Ukraine has operated programme-based budgeting (PBB) for annual budget laws since 2002 at the central level, and for most local governments since 2017 (except sub-rayon communities, for which it was extended in 2019) (Verkhovna Rada of Ukraine, 2010). Each programme includes result indicators formulated by the key spending unit, agreed with the Ministry of Finance, and transparently declared. In this way, the PBB method of budget formulation is intended to break all expenditures down based on intent rather than expected inputs.

While the PBB mechanism formally attaches spending to programmes, in many sectors, including health, there is a delay in linking expenditure to results. Spending units have commonly been constrained by additional sector-level requirements relating to economic classification (such as numbers of personnel or salary levels). A World Bank assessment of Ukraine's health system governance in 2013 concluded that these rigid input-based spending norms in health made it impossible to use PBB in a meaningful way (Belli, Dzhygyr & Maynzyuk, 2015).

Fig. 5. Changes in Ukraine's PEFA scores between 2016 and 2019



Notes. Score scale: A = high; D = low. PI: performance indicator. PEFA is a methodology for assessing PFM performance. It identifies 94 characteristics (dimensions) across 31 key PFM components (indicators) in 7 broad areas of activity (pillars).

Source: PEFA 2019 performance assessment report (Shcherbyna et al., 2020).

The 2017–2020 health financing reform has removed centrally mandated, input-based constraints, opening the way for programme-based orientation of health spending. With the NHSU administering the essential benefits package as the single national purchaser of health service contracts from 2020 onwards, and the legal status of many health care providers changing to public non-profit-making enterprises, one overarching budget programme can now operate: Ukraine's Medical Guarantees Programme (PMG), covering primary, specialized, and emergency care. However, effective operation of the PMG is constrained by the quality of data available for costing its strategic purchasing. The reform assumes that the NHSU will gradually switch to using a new e-health data system to compile most of the necessary statistics to support its PMG operations, moving away from its current reliance on historical data collected through highly unreliable paper-based systems that lead to inefficiencies. This should make it possible to avoid miscalculations of expected levels of service utilization, which impact contracting decisions, including pricing mechanisms for payment of service providers.

| BUDGET NEGOTIATION AND APPROVAL |

Policy orientation of the budgeting process, including PFM tools to keep a strategic focus during budget preparation and legislative scrutiny, are the weakest areas of Ukraine's PFM system, with low scores (D and D+) attributed in some areas in the two latest PEFA assessments (2015 and 2019). See Fig. 5 for the progression or stagnation of various budget indicators across the period analysed.

In December 2018, Ukraine significantly amended the Budget Code to introduce medium-term budget planning (Verkhovna Rada of Ukraine, 2019), allowing a three-year budget declaration to be considered by the Verkhovna Rada (the Ukrainian Parliament) and used for developing annual budgets. In early 2019, the Ministry of Finance prepared the first draft Budget Declaration 2020–2022 under these new rules, with three-year policy proposals and related spending projections for the health sector. However, the Cabinet of Ministers did not approve the draft Budget Declaration 2020–2020 prepared in 2019 (coincidentally amid parliamentary election preparation) and, following the onset of COVID-19 and its ensuing macroeconomic uncertainties, the Government suspended medium-term budgeting for one year (Verkhovna Rada of Ukraine, 2020).

One reason for Ukraine scoring low in terms of quality of budget preparation guidance (Fig. 5) is that the spending ceilings provided to line ministries by the Ministry of Finance (to inform budget preparation) are not required in Ukrainian law to be approved by the Government. The PEFA analysis identifies a risk in this approach of last-minute changes in budget proposals, recommending instead that political leadership should engage actively in priority-setting during the early stages of the budget preparation process (PEFA Secretariat, 2019).

Ukraine's Ministry of Finance uses detailed guidelines and templates to help line ministries to prepare technical documentation for their proposals (Ministry of Finance of Ukraine, 2012), requiring spending units to provide comprehensive information on the financing of every requested programme in the previous years, the detailed structure of programme inputs (including staffing and payroll data), and the expected result indicators. However, it is not clear to what extent this information is used in the negotiation process.

Results frameworks are not yet well developed in the health-care sector, lacking underlying service delivery concepts and robust data. The 2017 health financing reform represented a breakthrough, requiring (but not mandating legislatively) national health priorities to be issued, to guide the design of the essential benefits package (Ministry of Healthcare of Ukraine, 2019). The 2020 PMG was the first attempt to link health spending to explicitly outlined health priorities, and service delivery concepts for (integration of) various types of care are under development within the essential benefits package. As already mentioned, as a result of system inefficiencies, health outcomes data are also unreliable (in particular the mortality statistics) (Ukrainian Center for Social Data, 2019).

| BUDGET EXECUTION |

Since 2015, Ukraine's budget appropriations have become much more reliable, including in health. The 2019 PEFA assessment noted significant improvement in reliability of the budget (as shown in Fig. 5). Moreover, the difference between approved and actual expenditures has been significantly reduced over time, with less reallocation between functions in the budget execution process. In particular, the country performed well in terms of keeping expenditure outturn deviation below the 5% threshold (2016–2018) and, within the health function, decreasing under-execution of consolidated health allocation (2015–2019). Predictability has grown across most health sub-functions, reaching the maximum score for key budget forecasting indicators, and revenue collections have become much more aligned with approved projections. Budget arrears were minor and decreasing at the time of the assessment and the Government had strong control systems in place for non-salary expenditures and compliance with payment rules and procedures.

Ukraine's major reforms since the 2014 Revolution of Dignity included a new progressive Law "on Public Procurement" (in 2015), and ProZorro – an award-winning, innovative centralized electronic procurement system, heralded by the European Bank for Reconstruction and Development (EBRD) as an exceptional example of public e-procurement. Other innovative approaches to creating a transparent and efficient health procurement system include temporarily outsourcing centralized procurement of medications to reputable international organizations. The Government created a domestic centralized procurement agency, which is expected to start taking over this function during 2020.

| BUDGET MONITORING AND EVALUATION |

In recent years, Ukraine's central system for external scrutiny and audit has been significantly strengthened (as depicted in Fig. 5). The country's chief audit institution, the Accounting Chamber of Ukraine (ACU) has been upgrading its standards and methodologies, improving systems to track implementation of follow-up (PEFA Secretariat, 2019). As the health reform centralizes the bulk of health financing within the essential benefits package under the NHSU, the independent audit coverage for health spending will respectively increase.

New data collection and analysis tools will also allow the NHSU to produce much stronger evidence for extra allocations in health based on performance and contract-related financial data from health service providers. Up-to-date statistics on provider facilities are being made available for analysis via modern analytical dashboards at the NHSU website; the volume and composition of these data will increase as the e-health system expands, primary health care providers begin

to fully utilize the International Classification of Primary Care (ICPC) electronic coding methodology, and hospitals begin to report on their case mix. At the same time, it is critical for Ukraine to develop a full set of institutional leverages to oversee NHSU activities. In particular, the Law “on state financial guarantees for public medical services” requires the Government to set up an independent civil control board to review NHSU analysis and recommendations. Once this body becomes operational, it can improve reliability and quality of data analysis, including performance monitoring.

In 2019, Ukraine implemented the first set of spending reviews, including two reviews of programmes in the health sector (medical education, and health-care facility management under the Ministry of Finance). This methodology was introduced as part of the medium-term budgeting reform, as a tool to improve spending efficiency and policy orientation. In 2020, the Government intends to carry out a spending review of the programme for centralized procurement of medical goods (Cabinet of Ministers of Ukraine, 2020). Frequent changes in Ukraine’s political landscape meant that the 2019 reviews were not taken into consideration by the Ministry of Healthcare; however, a large body of evidence was collected on the efficiency of spending, facilitating the formulation of bold proposals for change.

| INTERMEDIATE CONCLUSION |

Historically, budget execution in Ukraine is predictable and well controlled, which helps the country’s largely progressive PFM system to maximize budgetary space within the current allocation system. Several important PFM improvements in the health sector took place in 2017–2019, largely linked to the health financing reform and introduction of the new NHSU financing methods. Shifting to output-oriented health financing methods enshrined within the PMG concept is key, making available additional budgetary space for health by tailoring funding channels according to need, to maximize service provision efficiency in health care facilities. Improved accumulation of data by the NHSU will also contribute to efficiency gains, incorporating performance-oriented elements into provider contracts.

An evidence-based results framework could be used to underpin budget proposals, enabling the Ministry of Healthcare to further enlarge budgetary space. Policies and costings drawn up on the basis of sound reasoning would be easier to implement on the basis of a medium-term budgeting framework, with ceilings approved earlier in the process. For these reasons it is critical to maintain the momentum for medium-term budgeting reforms launched in 2018, in light of new macro-fiscal uncertainties, and to revive the spending review processes initiated in 2019.

CONCLUSIONS AND RECOMMENDATIONS



In 2021, the economy is expected to contract as a result of COVID-19 impacts. If the GDP allocation to health remains at 3%, real health spending per capita is expected to decrease by 8.4%.

- To keep real per-capita spending on health at the 2020 level in 2021, the Ukrainian Government will need to increase funding to 3.3% of GDP (up from 3.0% in 2020).

It is possible to extend the overall expenditure envelope, but this would require reforms to ensure economic growth and better revenue administration. New debt from borrowing, and new taxes would be a high risk for the country.

- Key potential sources of extra fiscal space are: (1) economic growth through a better business climate and stronger human capital; and (2) enhanced revenue administration. The unfolding COVID-19 crisis will hit Ukraine's economy in areas in which it is already vulnerable, so the Government should prepare to adjust macro-fiscal parameters, including fiscal consolidation measures. Crisis-related borrowing mechanisms should be utilized to support recovery and create growth after the crisis, through investment in human capital and increased transparency.

It is possible to reallocate resources from other sectors to enlarge budgetary space – this is a question of active policy choices.

- The Government should consider the position health occupies in terms of prioritization (e.g. in comparison with economic infrastructure, education and security). If debt continues to shrink, the health sector can also benefit from funds that are currently used to repay public debt.

Budget execution in Ukraine is historically predictable and well controlled, helping to maximize space within the current PFM allocation system. Health financing reform and introduction of the new NHSU financing methods have contributed to improvements in the system. However, budgetary space for health could be further extended through various PFM improvements.

- Preserving and extending new financing mechanisms attached to the country's single overarching budget programme (the PMG) – as well as resuming medium-term budgeting reforms (currently on hold) – could extend budgetary space for health.
- Shifting to output-oriented health financing methods within the PMG makes it easier for the NHSU to allocate funding according to need. Efficiency can also be further increased by improvements in data collection and analysis, and introducing performance-related elements into contracts.
- The Ministry of Healthcare could consider implementing a better quality, evidence-based results framework (with a medium-term focus) as the basis for budget proposals.



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The WHO Regional Office for Europe

The World Health Organization (WHO) is a specialized agency of the United Nations created in 1948 with the primary responsibility for international health matters and public health. The WHO Regional Office for Europe is one of six regional offices throughout the world, each with its own programme geared to the particular health conditions of the countries it serves.

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