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Executive Summary

Ukraine's fiscal position in the first half of 2025 remained resilient under wartime pressures. Strong revenue growth, bolstered by tax policy changes made at the end of 2024 and external grants, supported record defense spending. While expenditures expanded at a faster pace than revenues, decisive donor support and prudent debt management contained fiscal vulnerabilities. The overall deficit narrowed compared to last year, but sustainability still hinges on stable external financing and continued macroeconomic resilience.

- **Revenues expanded significantly, driven by strong tax performance and higher non-tax inflows.** Tax revenues rose by 14.5% y-o-y to $23.3 bn, underpinned by legislative changes to the military levy and excise rates, higher wages, and inflation. Non-tax revenues surged by 32.6% to $16.4 bn, largely from military assistance, while grant inflows reached $5.2 bn, underscoring the critical role of external support in sustaining fiscal stability.
- **Expenditures rose sharply, dominated by defense and security needs.** Total spending increased by 17.1% y-o-y to $58.1 bn, with defense outlays reaching $32.2 bn (+27.8%) and public order expenditures $8.5 bn (+15.2%). Social protection was the only major function to contract, falling by nearly 15%, mainly due to lower transfers to the Pension Fund and cuts to targeted assistance.
- **Mid-year budget amendments substantially revised key fiscal parameters.** In July, Parliament approved long-anticipated amendments to the budget[1], as the initial plan had underestimated defense needs during active hostilities. Revenues increased by $3.3 bn (+6.3%) to $55.1 bn, while the deficit ceiling was raised by $5.6 bn to $42.2 bn. Total expenditures grew by $8.9 bn (+10.2%) to $96.2 bn, reflecting the priority of sustaining defense financing through year-end.
- **The budget deficit narrowed in headline terms but remained structurally high.** Including grants, the deficit fell by 16.7% y-o-y to $13.1 bn, reflecting stronger revenue mobilization and external support. Excluding grants, however, the deficit widened to $18.3 bn (+8.9%), highlighting underlying fiscal pressures that are only partially offset by temporary inflows.
- **Financing relied on a mix of concessional external borrowing and moderate domestic issuance**. Gross external loans amounted to $15.6 bn, mainly via the ERA Initiative and the Ukraine Facility, complemented by IMF disbursements. Domestic bond issuance fell to $5.6 bn, though the government signaled greater reliance on this instrument in H2 2025. Transfers from the National Bank ($2 bn) also helped bridge gaps.
- **State debt rose markedly, underscoring growing reliance on external resources.** By end-H1 2025, state and state-guaranteed debt reached $184.4 bn (+21.4% y-o-y), with external debt comprising 72% of the total. Domestic debt growth was more moderate due to limited issuance and significant redemptions, while state-guaranteed debt declined slightly. Active debt management, including negotiations on GDP warrants, remains essential to contain risks.
- **Fiscal risks remain elevated, centered on external support, revenue volatility, and demographic pressures.** Any delay or shortfall in external financing could force greater reliance on limited domestic resources, complicating deficit management. Weak economic recovery, infrastructure destruction, and adverse weather may dampen tax and export revenues, while outward migration and labor shortages risk eroding the tax base and increasing social spending needs.

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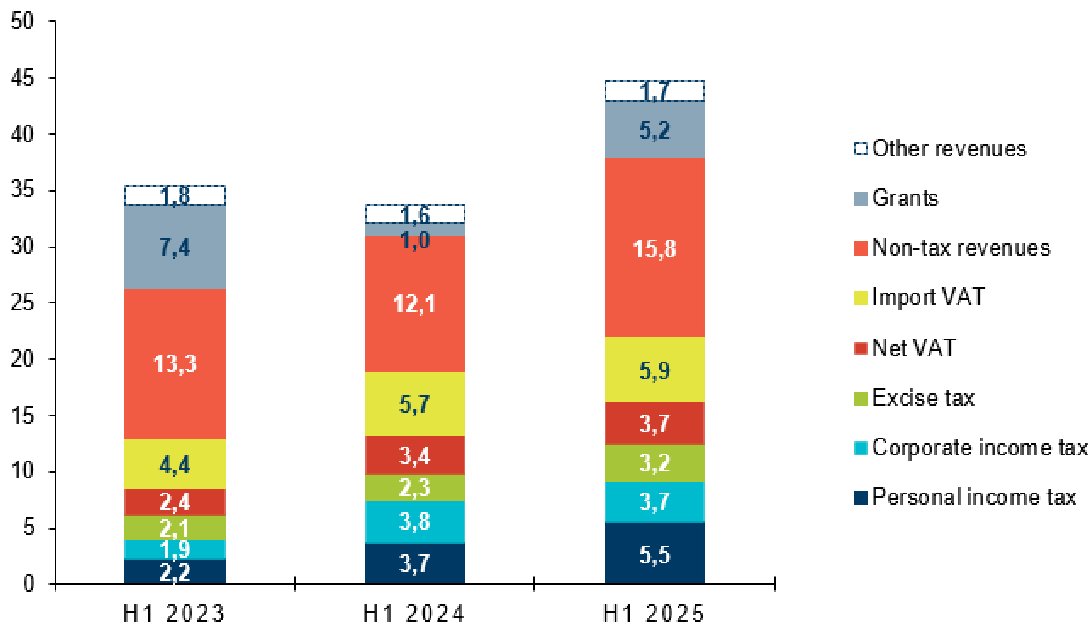
[1] *Here and after term "budget" is used for the central (state) level budget*

Budget Revenues

Taxes are the main source of revenues for the budget of Ukraine, accounting for **51.8%** of all budget revenues and, since the start of Russia's full-scale invasion, have remained a key resource for financing defense and security needs. Despite the challenging conditions faced by Ukraine's economy, taxpayers continue to fulfill their tax obligations, as evidenced by the volumes of taxes paid. In **H1 2025**, tax revenues increased by **14.5%** compared to the same period in 2024 – from **$20.3 bn** to **$23.3 bn**.

Figure 1. Structure of budget revenues in 2023-2025, $bn



Source: Ministry of Finance of Ukraine, Openbudget

Value Added Tax (VAT) remained the largest source of budget revenues in the H1 2025, accounting for 21.5% of all revenues. It was followed by **personal income tax (PIT)** and the **military levy**, which together accounted for **12.3%** of revenues. PIT and the military levy showed the strongest y-o-y growth: their revenues rose by **47.3%** compared to the same period in 2024 (**$5.5 bn** in H1 2025 vs **$3.7 bn** in H1 2024). This result was achieved thanks to changes in tax legislation adopted at the end of 2024 – namely, the increase in the military levy rate from **1.5%** to **5%** and its extension to sole proprietors operating under the simplified taxation system.

The increase in excise tax rates on tobacco products and fuel, aimed at gradually aligning them with EU levels, was the main driver of the sharp rise in excise revenues. As a result of these legislative changes, in H1 2025 excise tax revenues grew by 36.6% compared to the same period in 2024 – from $2.3 bn to $3.2 bn.

Key macroeconomic factors also contributed to higher revenues from PIT, excise tax, and VAT. In addition to legislative changes, these revenues were driven by rising inflation – the annual rate increased from **12%** in December 2024 to **15.9%** in May 2025 – and by growth in the average monthly wage, which rose from **$539** to **$600** over the same period.

The difficult security situation in the country, particularly in regions where Ukraine's main extraction capacities are located, as well Russia's destruction of gas production facilities, drove the decline in rent payments to the budget. As a result, their volume fell by 25% in H1 2025 compared to the same period last year – from $0.6 bn to $0.5 bn.

In H1 2025, the budget received 32.6% more non-tax revenues than in the same period in 2024 ($16.4 bn vs $12.4 bn). Their share of total budget revenues during this period was **36.7%**. The main source of such revenues was military assistance, which amounted to **$11 bn**, or **69.9%** of all non-tax revenues for the period. Of this amount, Ukraine received around **$2 bn (£1.5 bn)** in military financial assistance from the United Kingdom. These funds were provided under the ERA program, guaranteed by future proceeds from frozen Russian assets.

In H1 2025, Ukraine secured $5.2 bn in grant revenues (5x the H1 2024 figure), of which $4.7 bn came from the World Bank's PEACE in Ukraine program and $0.5 bn from the Ukraine Facility. Grants accounted for 11.5% of total budget revenues, highlighting their crucial role in maintaining financial stability. More than three years into the full-scale war, a steady inflow of grant financing remains vital for budgetary resilience, enabling Ukraine to cover priority expenditures without increasing state debt.

Budget Expenditures

In H1 2025, defense and security expenditures continued to dominate the budget, accounting for 70.1% ($40.7 bn) of total spending, while socio-economic expenditures received only 29.9%. Overall budget expenditures increased by 17% y-o-y, reaching $58.1 bn. The primary driver of this increase remains the defense and security sectors, with funding rising by 27.7% and 15.2%, respectively.

The Ministry of Defense received $31.4 bn, or 51.4% of total expenditures, which is 30.1% more than in H1 2024. Although there were some funding issues in January, they turned out to be minor and did not significantly impact the overall situation, unlike in 2024. Furthermore, overall funding levels increased notably: the average monthly funding rose from $4 bn in 2024 to $5.2 bn in 2025.

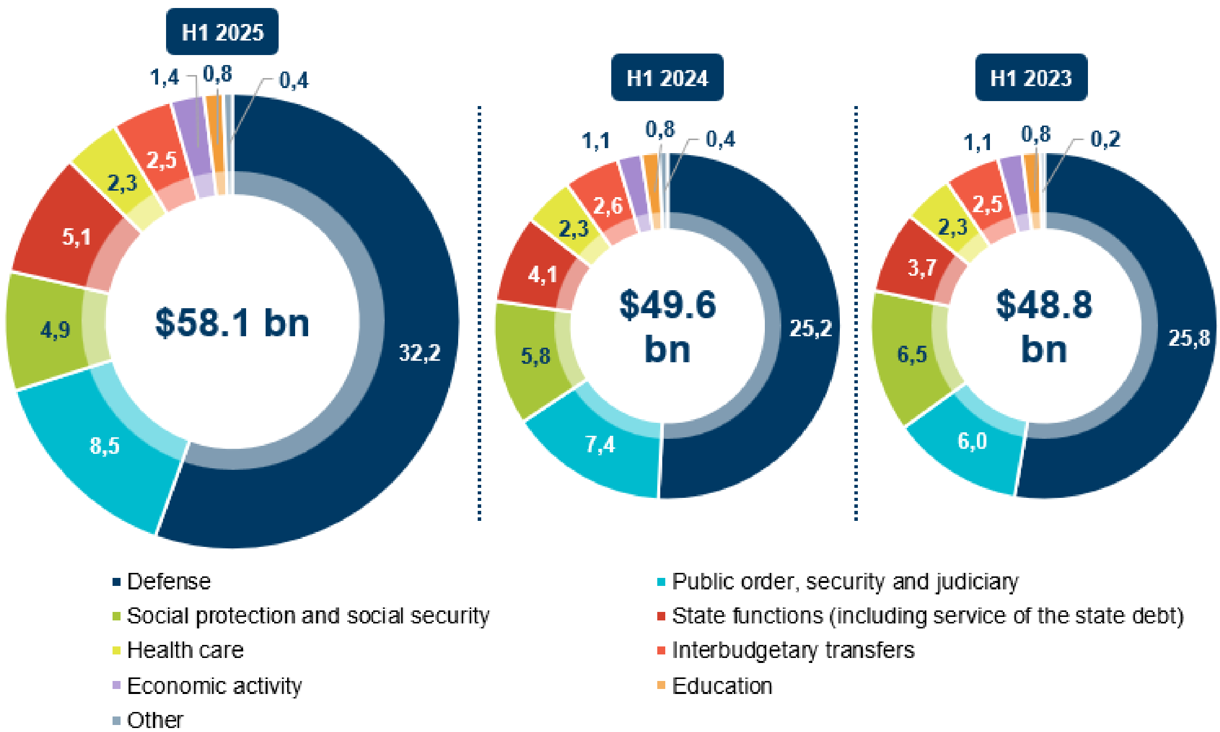
Despite stable funding throughout H1 2025, actual expenditures significantly exceeded the amounts projected in the budget, which could have led to a substantial year-end deficit of around $20 bn. This posed a threat to the financing of defense and security, particularly military salaries and equipment procurement. As in 2024, the government opted to amend the budget and, in July, approved an additional $10 bn in expenditures to cover the needs of the defense and security sectors. These additional funds are expected to come from higher tax revenues in certain categories, reduced spending on domestic debt servicing, and transfers from the National Bank of Ukraine. The remaining $10 bn in the forecasted deficit is expected to be covered by international partners in the form of military equipment and weapons.

In non-military sectors, notable increases were observed in state functions (including debt servicing), which rose by 25.8% or $1 bn, primarily due to higher debt servicing costs. The economic activity sector also saw growth, increasing from $1.1 bn in H1 2024 to $1.4 bn in H1 2025 (a 24.1% increase). Meanwhile, funding for social protection declined by 14.7%, falling from $5.8 bn to $4.9 bn, although a significant portion of social protection sector funding still goes toward pensions and social payments.

Expenditures on social protection decreased by 18.8% compared to H1 2024 due to a reduction in the budget transfer to the Pension Fund of Ukraine. Total social protection expenditures in H1 2025 amounted to $4.6 bn, down from $5.7 bn in H1 2024. The decline was driven primarily by a reduction in deficit coverage for the Pension Fund of Ukraine, which decreased by $783 mn, or 22.3%. In addition, funding for support to persons in difficult life circumstances fell by 20.2%, or $199 mn. Expenditures in other areas remained virtually unchanged, indicating that current social sector reforms are being implemented within the framework of existing expenditures, without attracting or cutting additional resources in the social sphere.

In June 2025, the government approved a new one-time "resettlement" allowance for children returning from temporarily occupied territories or from deportation and/or forced relocation, with the aim of creating appropriate conditions for their reintegration and adaptation. The allowance amounts to $1,201 per child. The total funding for 2025 is set at $1.2 mn, which will allow assistance to be provided to approximately 1,000 children. The Ministry of Social Policy plans to cover 5.1% of the returned children, out of the confirmed 19,546 deported and/or forcibly relocated children[2].

Figure 2. Structure of budget expenditures in 2023-2025, $bn[3]



Source: Ministry of Finance of Ukraine, Openbudget

Table 1. Actual expenditures on social payments in Q1 2023-2025, $bn

Indicator	H1 2023	H1 2024	H1 2025	Change (%, h-o-h, 2025 vs 2024)
Pension Fund funding for pension payments & covering deficit	3.7	3.5	2.7	(22.3)
Support for vulnerable citizens	1.4	1.0	0.8	(20.2)
Support for low-income families (including housing and utility subsidies)	0.8	0.2	0.2	(13.6)
Support for children & families	0.3	0.3	0.3	(12.7)
Support for persons with disabilities	0.03	0.05	0.05	14.5

Source: Ministry of Finance of Ukraine, KSE Institute

[2] *"Children of War" portal*

[3] *The state functions sector includes the state debt servicing*

Budget Financing

In H1 2025, a substantial increase in defense spending drove up Ukraine's budget expenditures at a pace that outstripped revenue growth, resulting in a wider budget deficit. Nevertheless, the proactive strategy of attracting significant international grant support has helped keep the situation manageable. The overall deficit, including $5.2 bn in grants, amounted to $13.1 bn, which is 16.7% lower compared to the deficit incl. grants y-o-y. Excluding grants, the deficit reached $18.3 bn, reflecting an 8.9% increase y-o-y (compared to the deficit excl. grants).

Budget deficit financing, similar to prior periods, relies on a mix of domestic sources – such as government bonds and privatization revenues – and external financial assistance. These tools have remained essential in maintaining Ukraine's financial stability throughout 2025. Domestic debt is not the most effective instrument in 2025, with gross domestic bond issuance declined from $6.2 bn in H1 2024 to $5.6 bn in H1 2025. However, according to the amendments to the budget made in June 2025, the government plans to expand the use of this instrument in the coming periods of the year.

Table 2. Budget funding sources (revenues and gross financing) in 2023-2025, $bn

Resources	H1 2023	H1 2024	H1 2025	Change (%, h-o-h, 2025 vs 2024)
Internal budget resources	**22.2**	**26.5**	**28.8**	**8.7**
Domestic government bonds	7.8	6.2	5.6	(10.2)
Own budget revenues (without grant)	14.4	20.3	23.3	14.5
Share of internal budget resources	48.4%	65.1%	58.1%	x
External budget resources	**23.7**	**14.2**	**20.8**	**46.3**
External loans	16.3	13.2	15.6	18.6
Grants	7.4	1.0	5.2	397.3
Share of external budget resources	51.6%	34.9%	41.9%	x

Source: Ministry of Finance of Ukraine, KSE calculations

External financing continues to play a key role in 2025. The government continues to attract external loans and borrowings to fund the budget deficit, with most of them on concessional terms. For H1 2025, gross external loans amounted to $15.6 bn (compared to $13.2 bn for the H1 2024). The majority of external loans for the budget – $11.8 bn (inc. $7.4 bn from EU and $3.4 bn from Canada and $1 bn from UK) – were received through the ERA Initiative, which is backed by future revenues from frozen Russian assets. Another significant portion ($3.4 bn) was received from the European Union under the Ukraine Facility program. The IMF provided an additional $400 mn in the eighth tranche of EFF program.

Table 3. Sources and amounts of external loans to Ukraine in 2025

Foreign loans received in 2025	$ bn
ERA	11.8
European Union	*7.4*
Canada	*3.4*
United Kingdom	*1.0*
EU (Ukraine Facility)	3.4
IMF	0.4

Source: Ministry of Finance of Ukraine

As forecasted in the KSE Institute's Macroeconomic Handbook, a total of $41.7 bn in external loans is planned to be received in 2025. Accordingly, an increased level of external borrowing is anticipated in H2 2025. This is also attributable to the disbursement of funds under the Ukraine Facility program, which, according to the established schedule, were expected in the first half of the year but have not been received.

State Debt and State-Guaranteed Debt

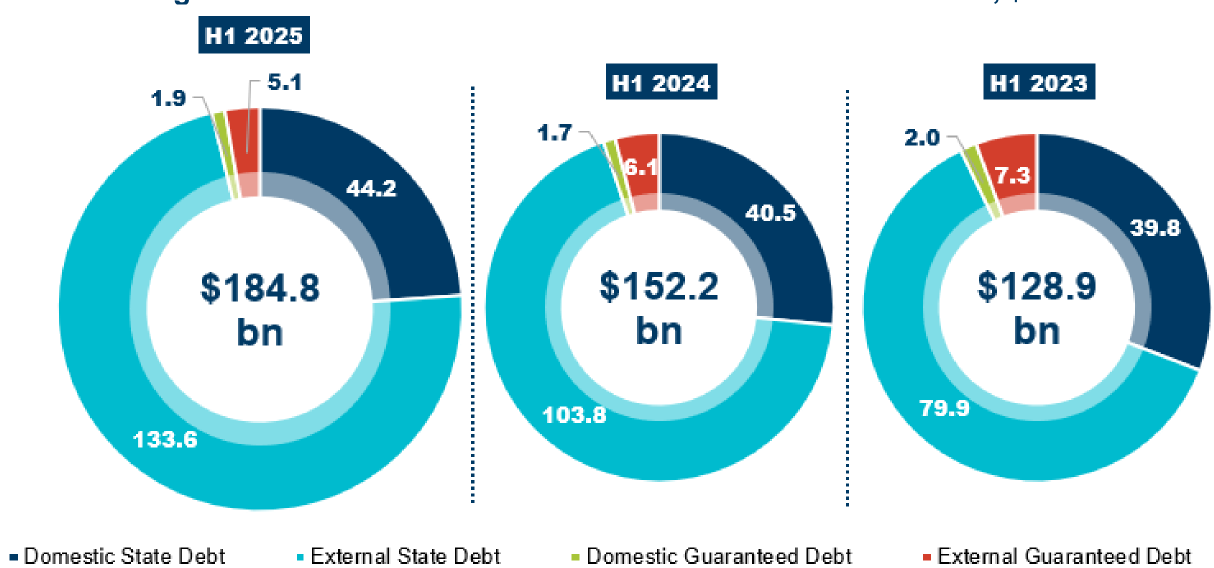
Ukraine's state debt increased significantly in H1 2025, fueled by greater borrowing requirements stemming from budget deficits and dependence on international financial aid. By the end of H1 2025, total state and state-guaranteed debt reached $184.4 bn, marking a 21.4% rise compared to the end of H1 2024.

Active borrowing of international credit resources to support the economy and cover the budget deficit, as well as currency fluctuations, have driven the rapid growth of external state debt. Ukraine's external state debt increased by 28.7% compared to the end of H1 2024, reaching $133.6 bn, which accounts for 72.3% of total state debt. Such rapid growth rates are expected to continue in the next half-year due to active external financing.

The reduction of new government bond issuance and significant repayments on previously issued bonds (especially in Q1 2025) ensured moderate growth of domestic debt. Ukraine's domestic state debt increased by 9.1% compared to the end of H1 2024 to $44.2 bn, accounting for 23.9% of total state debt. According to the NBU Depository, in H1 2025, the government of Ukraine raised $5.6 bn from offering domestic government debt securities through auctions and allocated $5.9 bn for redemption of domestic government debt securities.

The government adheres to a policy of reducing the issuance of guarantees, which leads to a gradual decrease in state-guaranteed debt. State-guaranteed debt for the period from the end of H1 2024 to the end of H1 2025 decreased by 10.3% from $7.8 bn to $7 bn. However, state-guaranteed domestic debt increased by 3.2%, from $1.7 bn to $1.9 bn, while state-guaranteed external debt decreased by 19.6%, from $6.1 bn to $5.1 bn. The increase in domestic state-guaranteed debt is due to a slight rise in liabilities to banks and other financial institutions, including JSC "State Export-Import Bank of Ukraine," JSC "State Savings Bank of Ukraine," as well as portfolio guarantees.

Figure 3. State Debt and State-Guaranteed Debt in 2023-2025, $bn



Source: Ministry of Finance of Ukraine, KSE calculations

The resolution of obligations related to GDP warrants is the main event of the state debt management in H1 2025. In 2015, Ukraine completed a successful sovereign debt restructuring totaling $15 bn, which included a partial (20%) debt write-off. As part of this transaction, GDP-linked warrants were issued – debt instruments with payments contingent on the country's economic growth rates. The Ministry of Finance initiated negotiations on the restructuring of payments under the GDP warrants issued in 2015 but no agreement with creditors had been reached by the end of H1 2025. A payment was scheduled for June 2, 2025, based on economic growth performance in 2023. Nevertheless, a moratorium on payments related to these warrants has been imposed and will remain in effect until the completion of the restructuring process. Consequently, a technical default has been declared on this type of debt obligation. The further resolution of this issue will have a significant impact on Ukraine's state debt.

Key Risks for 2025

- **Delays or shortfalls in external financing** could pose significant fiscal risks, as covering the deficit would require mobilizing domestic resources. Given the already elevated expenditure plans, the scope for additional compensatory measures remains limited, increasing fiscal vulnerabilities.
- **Weak economic recovery** amid destruction of productive capacity, damage to critical infrastructure, and adverse weather conditions could reduce tax revenues and foreign exchange inflows from exports. Revenue overperformance—driven by last year's underestimation of tax-raising measures—is observed and expected to continue through year-end, but its scale may be smaller than it would have been in the absence of these adverse factors.
- **Intensifying outward migration and labor shortages** could weaken labor tax revenues and increase pressures on social spending. Combined with the ongoing uncertainty regarding the duration of hostilities, this creates additional risks to budgetary sustainability.

Table 4. Ukrainian budget, $bn

Indicators	H1 2023	H1 2024	H1 2025	Change (%, h-o-h, 2025 vs 2024)
Total revenues	**35.6**	**33.8**	**44.9**	**32.9**
Grants	7.4	1.0	5.2	397.3
Non-tax and other revenues	**21.2**	**13.4**	**21.6**	**60.8**
Tax revenues	**14.4**	**20.3**	**23.3**	**14.5**
PIT	2.2	3.7	5.5	47.3
Corporate income tax	1.9	3.8	3.7	(1.1)
Rent for the use of subsoil	0.8	0.6	0.5	(25.0)
Excise tax	2.1	2.3	3.2	36.6
Domestic VAT (net)	2.4	3.4	3.7	10.8
Import VAT	4.4	5.7	5.9	2.6
Import and export duty	0.5	0.6	0.6	(1.1)
Total Expenditures	**48.8**	**49.6**	**58.1**	**17.1**
Defence	25.8	25.2	32.2	27.8
Deficit	**(13.1)**	**(15.8)**	**(13.1)**	**(16.7)**
Deficit (net of grants)	**(20.4)**	**(16.8)**	**(18.3)**	**8.9**
Net borrowings	17.4	12.7	13.5	5.6
Loans	24.1	19.4	21.2	9.4
Repayments	(6.7)	(6.6)	(7.7)	16.6

Source: Ministry of Finance of Ukraine, KSE calculations

Prepared by the Center of Public Finance and Governance at the Kyiv School of Economics

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