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L. P. SIDELNYKOVA,
Dsc in Economics, Professor,
Head of the Department of Finance, Accounting and Taxation,
Kherson National Technical University,
e-mail: sidelnykova.larysa@kntu.net.ua
ORCID ID: http://orcid.org/0000-0001-7182-2923

Transforming Budget Management within the Public Finance System under Fiscal Consolidation

The public finance system of Ukraine operates under unprecedented geopolitical and security challenges that have resulted in a substantial widening of fiscal imbalances. The rapid growth of defense expenditures amid a narrowing tax base undermines the effectiveness of traditional budget management instruments. Under these circumstances, an objective need for a radical transformation of domestic budget management, based on flexibility and anti-crisis response mechanisms, is required to ensure the state's overall fiscal sustainability.

The purpose of the study is to assess the transformation processes occurring within Ukraine's budget management system under fiscal consolidation and to substantiate managerial decisions aimed at strengthening long-term fiscal sustainability.

The article sets out the results of a comprehensive analysis of the architecture of public finances of Ukraine over ten years. It demonstrates that the classical tax-based model of budget formation has undergone a radical transformation, with the share of tax revenues contracted, and non-tax revenues and large-scale external assistance in the form of grants and concessional loans having become the main sources for fiscal support. Structural shifts in the expenditure side of the consolidated budget, resulting from the dominance of security and defense expenditures and reduced financing of human capital, were explored. Trends in the rapid accumulation of public debt driven by high levels of borrowing relative to gross domestic product were identified; changes in the structure of credit support, with particular emphasis on attracting long-term international financial resources, were analyzed.

It is substantiated that the hybrid financing model ensures short-term macro-financial stability while generating long-term debt and currency risks. The priority directions for improving budget management include strengthening fiscal consolidation through expenditure optimization, broadening the revenue base, reducing refinancing risks, and enhancing the institutional capacity

of the medium-term budget planning system.

Keywords: *public finances, fiscal consolidation, budget management, revenues, expenditures, budget deficit, public debt, fiscal sustainability.*

Л. П. СІДЕЛЬНИКОВА,
доктор економічних наук, професор,
завідувач кафедри фінансів, обліку та оподаткування,
Херсонський національний технічний університет,
e-mail: sidelnykova.larysa@kntu.net.ua
ORCID ID: http://orcid.org/0000-0001-7182-2923

Трансформація бюджетного менеджменту в системі публічних фінансів під впливом фіскальної консолідації

Система публічних фінансів України функціонує в умовах безпрецедентних геополітичних і безпекових викликів, які зумовили критичне розширення фіскальних розривів. Стрімке зростання видатків на оборону на тлі звуження податкової бази нівелює ефективність традиційного інструментарію управління бюджетними ресурсами. За цих обставин виникає об'єктивна потреба у кардинальній трансформації бюджетного менеджменту на засадах гнучкості та антикризового реагування з метою забезпечення загальної фіскальної стійкості держави.

У статті розкрито трансформаційні процеси у системі бюджетного менеджменту України під впливом фіскальної консолідації та обґрунтовано управлінські рішення для зміцнення довгострокової фіскальної стійкості.

Надано результати ґрунтовного аналізу архітектури публічних фінансів України за десятирічний період. Доведено факт глибокої деформації класичної податкової моделі формування бюджетних ресурсів, де частка податкових надходжень суттєво скоротилася, а основним фіскальним донором стали неподаткові доходи та масштабні обсяги зовнішньої допомоги у формі грантів і пільгових кредитів. Досліджено структурні зрушення у видатковій частині зведеного бюджету внаслідок домінування видатків на сектор безпеки й обмеження фінансування людського капіталу. Виявлено *тенденції стрімкого накопичення державного боргу, зумовлені високим рівнем запозичень відносно валового внутрішнього продукту; проаналізовано зміну структури кредитної підтримки з акцентом на залучення міжнародних довгострокових ресурсів.*

Обґрунтовано, що гібридна модель фінансування убезпечує короткострокову макрофінансову стабільність, але генерує довгострокові боргові та валютні ризики. Основними пріоритетами розвитку бюджетного менеджменту визначено посилення фіскальної консолідації шляхом оптимізації видатків, розширення дохідної бази, мінімізації ризиків рефінансування та підвищення інституційної спроможності системи середньострокового бюджетного планування.

Ключові слова: *публічні фінанси, фіскальна консолідація, бюджетний*

менеджмент, доходи, видатки, дефіцит бюджету, державний борг, фіскальна стійкість.

Introduction. The public finance system of Ukraine operates under synergistic pressure of geopolitical, macroeconomic and security challenges, which increase its vulnerability and necessitate adaptive transformations. The widening fiscal gap, driven by underutilized tax capacity amid a dramatic increase in national security and defense expenditures, highlights the need to implement a stringent fiscal consolidation policy. A considerable state budget deficit and a rapid accumulation of public debt undermine the effectiveness of traditional approaches to budget resource management. Under such conditions, there is an objective need to transform the budget management system by strengthening its flexibility, adaptability, and crisis-response capacity, which involves improving the mechanisms for managing revenues, expenditures, and public borrowing, enhancing the efficiency of the use of budget resources, and ensuring long-term fiscal sustainability of the state as a prerequisite for macroeconomic stability.

Literature review. Issues of theory, methodology and practice of budget management remain the focus of sustained attention among Ukrainian scholars. O. Irshak, A. Faliuta, and I. Irshak substantiate the theoretical foundations of budget management and propose their own definition as a continuous process associated with the planning, control, and management of public financial resources aimed at achieving strategic objectives [1]. I. Hruzina examines the essence, main components, and functions of budget management, identifies its distinctive features, and demonstrates the advantages of its application [2]. O. Horbunov clarifies the role of budget management within the regulatory system through a synthesis of the concepts of budget policy, budget mechanism, budget process, budget system, and budgetary structure [3]. A. Kozenko and L. Kravtsov shift the focus of research on the theoretical and organizational foundations of budget management to the local level [4]. In contrast, B. Huzar investigates the practical aspects of budget management by analyzing its current state and trends in Ukraine [5]. Considering the primary objective of budget management as ensuring effective and efficient management of financial resources within the budgetary sphere, O. Martyniuk substantiates the need to develop an advanced model of budget management, aimed at improving the efficiency of the budget process, enhancing the transparency in budget management, and adapting the budget system to contemporary socio-economic challenges [6], a conclusion that is highly relevant in the current socio-economic context.

V. Kudriashov emphasizes that the deepening fiscal imbalances under wartime conditions, the growing state budget deficit, and the increasing debt burden on the public finance system intensify the need to balance the state budget and assess the impact of budget-balancing mechanisms on the financial stability of the country [7]. Ukrainian scholars have extensively examined fiscal consolidation as a tool for public finance stabilization [8], its conceptual foundations [9], the effectiveness of its instruments [10], implementation challenges under martial law [11], and the efficiency of budget expenditures in this context [12]. These studies provide a theoretical and methodological foundation for further research into the transformation of budget management under the pressure of increasing fiscal imbalances and the need to strengthen long-term fiscal sustainability.

Despite significant scholarly contributions to the study of budget management under fiscal consolidation, issues of transformation of public finance management under conditions of wartime fiscal destabilization still remain out of focus.

The research purpose is to assess the transformation processes within Ukraine's budget management system under fiscal consolidation and to substantiate managerial decisions aimed at strengthening long-term fiscal sustainability.

Research results. The fiscal environment of Ukraine is currently characterized by a high level of uncertainty and systemic transformations under the influence of destructive factors, which require strict fiscal consolidation. Budget management is undergoing fundamental changes due to the need to adapt to the narrowing of the tax base, the loss of production capacities, and the rapid growth of defense expenditures. The current situation is aggravated by the cumulative effect of the disrupted logistics links, the uncontrolled migration, and the unprecedented reliance on external financial assistance, which highlights the need to develop new approaches to the budget management as a prerequisite for maintaining the fiscal sustainability of the state.

These adverse trends give a grasp of the problems in the fiscal field. However, the sound assessment of their impact requires a quantitative analysis of actual indicators to estimate the depth of destabilization processes and the imbalance of the public finance system.

Table 1 presents the structure of revenues of the consolidated budget of Ukraine by component over the past ten years.

Table 1

Structure of revenues of the consolidated budget of Ukraine, 2016–2025, billion UAH

Indicators	Years										2025/ 2016 pp
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	
Tax revenues	83,13	81,44	83,28	82,98	82,57	87,46	61,16	52,77	58,21	58,10	-25,03
Non-tax revenues	16,03	15,20	16,27	16,51	17,03	12,18	16,77	33,12	28,37	29,06	+13,03
Income from capital transacttions	0,20	0,22	0,24	0,24	0,26	0,23	0,13	0,12	0,14	0,15	-0,05
From the European Union, foreign governments, international organizations, donor agencies	0,54	0,16	0,14	0,09	0,09	0,08	21,91	13,97	13,25	12,66	+12,12

Continuation of Table 1

Trust funds	0,10	2,99	0,08	0,19	0,06	0,05	0,02	0,03	0,03	0,03	-0,07
Total	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	-

Source: compiled by the author based on data from [13]

The data in Table 1 indicate a significant restructuring of the state budget components during the period of full-scale Russian aggression. Before 2022, more than 80% of the budget revenues at all levels were generated through tax revenues, which is characteristic of a balanced market economy. In 2021, this share reached 87.46%.

The sharp decline in the share of tax revenues in 2022 (to 61.16%) and its further reduction (by the total of 25.03 pp over the analyzed period) indicate that the tax system has ceased to be the main source of financing public expenditures. Instead, there has been a considerable increase in the share of external financial assistance from international partners and financial institutions. Its share rose from nearly zero before the escalation of military aggression to 21.91% at its onset, and subsequently stabilized at slightly higher than 12%. In addition, the share of non-tax revenues nearly doubled, indicating the forced mobilization of alternative, often quasi-fiscal, domestic resources.

Hence, the classical tax-based model of the state budget formation has undergone a substantial transformation. Whereas the stability of the public finance system was based on the domestic economic activity, it has now shifted towards hybrid financing, with tax revenues covering only part of the most essential public needs. The growing share of non-tax revenues and foreign grants gives evidence of the depleted traditional fiscal reserves and the forced transition to emergency mobilization of resources, making the revenue side of the budget extremely vulnerable to external political and economic pressures.

Table 2 shows the structure of expenditures of the consolidated budget of Ukraine.

Table 2

Structure of expenditures of the consolidated budget of Ukraine, 2016–2025, billion UAH

Indicators	Years										2025/ 2016 pp
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	
National functions	16,05	15,73	15,32	14,82	12,84	13,70	8,16	7,86	8,82	8,54	-7,51
Defense	7,11	7,04	7,76	7,78	7,55	6,91	37,55	47,23	46,61	51,17	+44,06
Public order, security and judiciary	8,63	8,37	9,44	10,33	10,00	9,55	14,93	13,32	14,42	13,95	+5,32
Economic activity	7,92	9,74	11,26	11,25	16,47	15,91	5,14	5,57	5,26	4,30	-3,62
Environmental protection	0,75	0,69	0,66	0,71	0,57	0,57	0,17	0,14	0,21	0,20	-0,55

Continuation of Table 2

Housing and communal services	2,09	2,57	2,43	2,52	2,02	3,09	1,35	1,59	1,34	1,52	-0,57
Healthcare	9,02	9,69	9,27	9,37	11,02	11,04	7,07	4,90	4,83	4,37	-4,65
Spiritual and physical development	2,02	2,30	2,32	2,30	1,99	2,35	1,11	0,87	0,92	0,81	-1,21
Education	15,49	16,82	16,80	17,43	15,82	16,96	9,55	6,95	7,05	6,57	-8,92
Social protection and social security	30,91	27,04	24,75	23,49	21,73	19,92	14,96	11,58	10,56	8,58	-22,33
Total	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	-

Source: compiled by the author based on data from [13]

The data in Table 2 indicate significant structural changes in the public expenditures. The priority of the security and defense sector, which accounted for 65.12% of the total state budget appropriations in 2025, resulted in a significant reduction in the share of social expenditures compared with 2016, including social protection and social security (by 22.33 pp), education (by 8.92 pp), and healthcare (by 4.65 pp).

Before the full-scale Russian invasion, the structure of the consolidated budget of Ukraine was balanced, but once the martial law was imposed, the security-related expenditures have absorbed a vast share of the budget, thus putting constraints on spending for human capital development. The transformation of budget management towards a survival-oriented budget model creates additional risks for fiscal sustainability by increasing the dependence on external borrowing to finance deficits in socially important expenditure categories (Fig. 1).

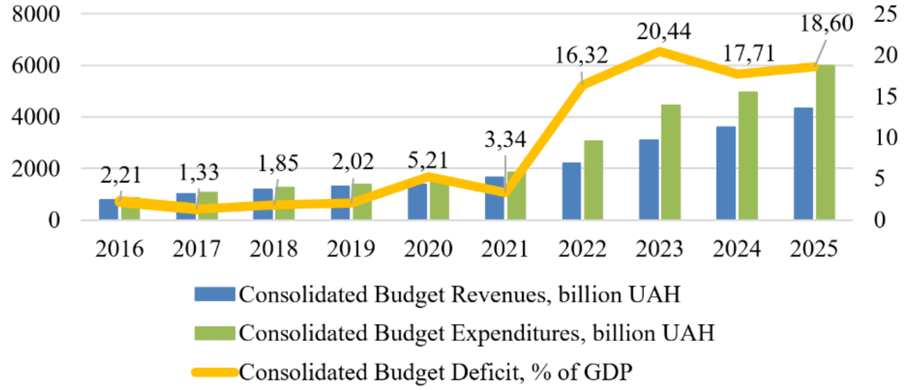

Fig. 1. Revenues and expenditures of the consolidated budget of Ukraine and the budget deficit, 2016–2025

Source: compiled by the author based on data from [13, 14]

The deficit of budget resources generated by the national economy has entailed a critical dependence of the public finance system on external and domestic sources. This has boosted the public debt and weakened the fiscal sustainability of the state due to the growing external debt burden, while creating additional pressure on the monetary market by crowding out private investments with domestic public borrowing.

Fig. 2 illustrates the indicators of debt operations of the consolidated budget of Ukraine and the ratio of public borrowing to GDP.

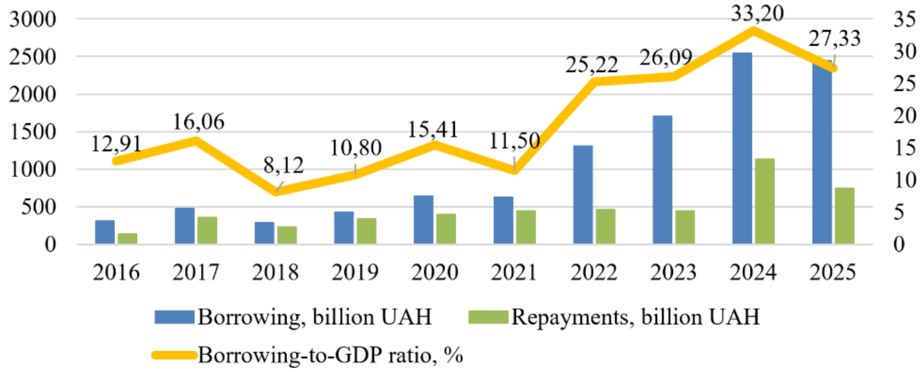

Fig. 2. Debt operations of the consolidated budget of Ukraine and borrowing-to-GDP ratio, 2016–2025

Source: compiled by the author based on data from [13, 14]

The data in Fig. 2 demonstrate the gradual increase in the debt financing of public expenditures since 2019. In 2021, the situation improved in a way due to the gradual recovery of the economy after the pandemic, but the full-scale Russian aggression radically changed the architecture of debt operations. The peak value of funds borrowed by Ukraine was recorded in 2024 (2,542.4 billion UAH); The peak value of the net financing of debt operations – in 2025 (1,692.4 billion UAH).

The analysis of net financing for debt operations shows its nearly tenfold increase over the studied period, suggesting that the borrowed capital turned into a key source for the country's fiscal sustainability. 2024 was the most challenging year in terms of debt servicing, as the repayment exceeded 1.1 trillion UAH. The 2025 indicators confirm the continued high dependence of the budget system on external and internal borrowing (2,441.3 billion UAH), although the structure of net financing shows a stabilization of the debt burden due to attracting mainly preferential long-term resources from international partners.

Emphasis should be placed on the ratio of public borrowing to GDP, allowing for an assessment of the intensity of debt pressure on the economy. As shown in Figure 2, before the full-scale invasion, the public borrowing was moderate, averaging 12.47% of GDP. However, since 2022, this indicator has rapidly increased. It was record high in 2024 (33.20% of GDP), as the resources generated by the national economy were almost entirely absorbed by the security and defense sector, while borrowing became the main source of financing for the rest of budget expenditures. The 2025 figure (27.33% of GDP) shows a relative decline in the intensity of public borrowing, with the persisting high dependence on debt financing of public needs.

An assessment of fiscal risks will not be sound unless it covers not only the total public debt obligations, but also their structural analysis. The balance between internal and external sources of financing determines not only the current liquidity of the budget, but also the cost of debt servicing in the future. Since the terms for raising funds in the domestic market (through domestic government bonds, OVDP) and from international partners strongly differ, it is advisable to analyze the dynamics of each segment and assess the ratio of external credit resources to GDP (Fig. 3).

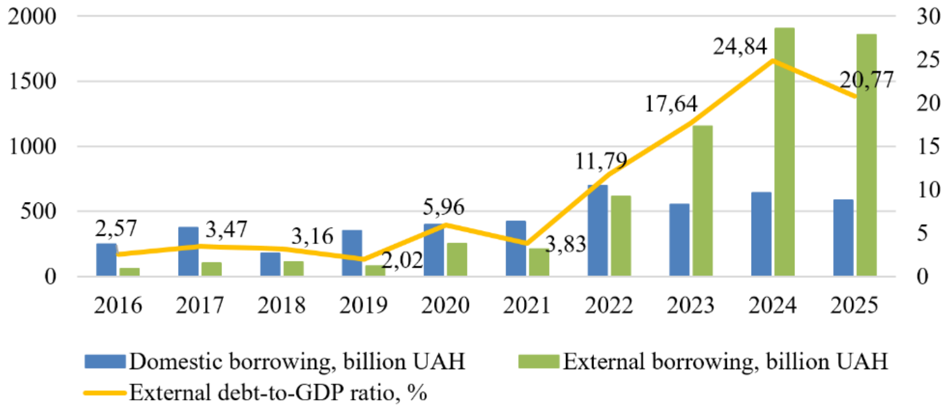

Fig. 3. Internal and external borrowing and external debt-to-GDP ratio, 2016–2025

Source: compiled by the author based on data from [13, 14]

The data in Figure 3 show a substantial restructuring in the sources of budget deficit financing. In 2016–2021, the state debt policy relied on the domestic credit market: the share of internal borrowing steadily dominated and was record high in 2016 and 2019 (80.08% and 81.30%, respectively). This allowed for minimizing currency risks, while maintaining the relative autonomy of the budget system.

Subsequently, the share of external borrowing was speedily up to reach 75– 76% in 2024–2025, while domestic sources of debt financing of public expenditures declined to 24–25%, respectively. This differentiation of sources of debt financing signals the transition to a model in which external support has become the main guarantor of fiscal security. Although Ukraine currently attracts international capital predominantly on concessional terms, including low interest rates and longer maturities, such a high share of external borrowing increases the dependence on the geopolitical stability of its partners and currency fluctuations. Given that Ukraine receives more than 75% of its new loans in foreign currency, any depreciation of UAH will automatically increase future debt- servicing costs, creating additional pressure on foreign exchange reserves.

Besides that, obtaining large scopes of external financing creates a significant refinancing risk that may lead to further debt accumulation in the coming years. If the rate of economic recovery remains lower than the rate of debt accumulation, the government may be forced to take on additional debt only to service interest payments on existing obligations.

Also, a high share of external financing links the Ukraine's fiscal resilience to political developments and budgetary processes of donor countries, where any delay in external funding limits the government's ability to finance public expenditures. Although such external credit expansion is a forced reaction to martial law, it remains exceptionally high by international standards and requires setting up a strategy for the gradual reinstatement of the dominant role of domestic sources for public purpose financing.

Conclusions and recommendations. The public finance system in Ukraine is undergoing a radical transformation amidst the uncertainty and increased security challenges caused by the Russian military aggression. It shows in the growing dependence on debt, structural refocus to external sources of financing, and the increasing role of international financial assistance in balancing the budget system. This structure of financial resources–contributes to the maintenance of the short-term macro-financial stability. But it creates systemic risks for the fiscal sustainability in the medium- and long-term, which necessitates further modernization of budget management based on fiscal consolidation, improved efficiency of mobilization and use of domestic budget resources, and the gradual restoration of a balanced structure of sources for financing public expenditures.

The main improvements in state budget management amidst high uncertainty are as follows:

- strengthening fiscal consolidation by optimizing budget expenditures, increasing their effectiveness and reducing inefficient expenditures;
- expanding and strengthening the revenue base of the budget through improved tax administration, reduced shadow economy, and minimized tax losses;
- optimizing the debt management policy aimed at reducing currency risks, extending borrowing terms, and gradually reinstating the dominance of domestic sources of financing;
- enhancing the institutional capacity of budget management by improving the medium-term budget planning, increasing the transparence of the budget process and implementing the risk-oriented approach in public financial management.

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