An analysis of Government Budgets in South Sudan from a human development perspective

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Introduction

Government budgets are a principal channel of allocating financial resources and managing government expenditures to usher in economic growth and implement the development plans and programmes in the country. Budgets also are a financial mirror reflecting the prioritization of programmes and policies by the government, given the financial operating environment and the overall state of the economy. Thus, the dynamic links between the budgets and the development plans are a demonstration of the commitment of the government of the day to convert plans into an effective programme of action.

For this to hold, the budget should not have any significant exclusions on reported receipts and expenditures (estimates and actual), including on extraordinary security/defense related matters. Accurate recording of any significant expenditure on the latter count is an important aspect of understanding the overall direction of the budget and its pro-development orientation.

Fiscal deficits are an important marker of the policy stance, and have links to the overall macroeconomic stability in any country. External borrowing as a means of financing the fiscal deficit has specific macroeconomic consequences including on exchange rates, levels of current account deficits, and on the increase in foreign debt and decrease in foreign reserves. In the absence of developed financial markets and lack of private savings, domestic financing of deficits has its own limitations.

South Sudan, emerging after decades of conflict and devastation, faced a wide array of development challenges on all fronts which have unfortunately been exacerbated by the current conflict. Prior to the conflict, statistics showed some improvement but severe multi-dimensional deprivations with more than half of the population languishing below the poverty line, high rates of maternal and infant mortality, low literacy, poor access to sanitation and clean water sources. Also, it has been estimated that with the current crisis owing to looting, increased cattle raids and displacement of 1.5 million people (in excess of 20 percent of the population of the three conflict -affected states) has worsened poverty outcomes and increased inequalities. Food insecurity and malnutrition is widespread in the country. According to the Integrated Phase Classification (IPC) analysis of January 2014, the number of people in acute food insecurity and livelihood crisis (IPC phases 3, "Crisis" and 4, "Humanitarian Emergency") was estimated at about 3.7 million, almost four times the pre-crisis estimate of 1 million people. The areas most affected by food insecurity are Unity, Jonglei and Upper Nile States (FAO 2014/03).

The current budget needs to be analysed from this perspective and within the overall development country context. In general terms, for the budget to be able to respond adequately to the development plan the country needs to steadily diversify the structure of the economy, strengthen tax administration and security sector and contain spending leading to creation of the necessary fiscal space and flexibility to channel a higher level of resources towards development needs. Given the particular stage of development of South Sudan, with its near complete dependence on the oil sector revenues and the management thereof, the country is faced with a number of structural policy challenges, including vulnerability to resource shocks and well known 'Dutch disease effects' amongst others.1 Even though the budget is not the only policy instrument to address medium to longer term structural issues, it plays an important role in reinforcing the country's overall developmental vision.

Budget 2014/15: Key issues and trends from a human development perspective

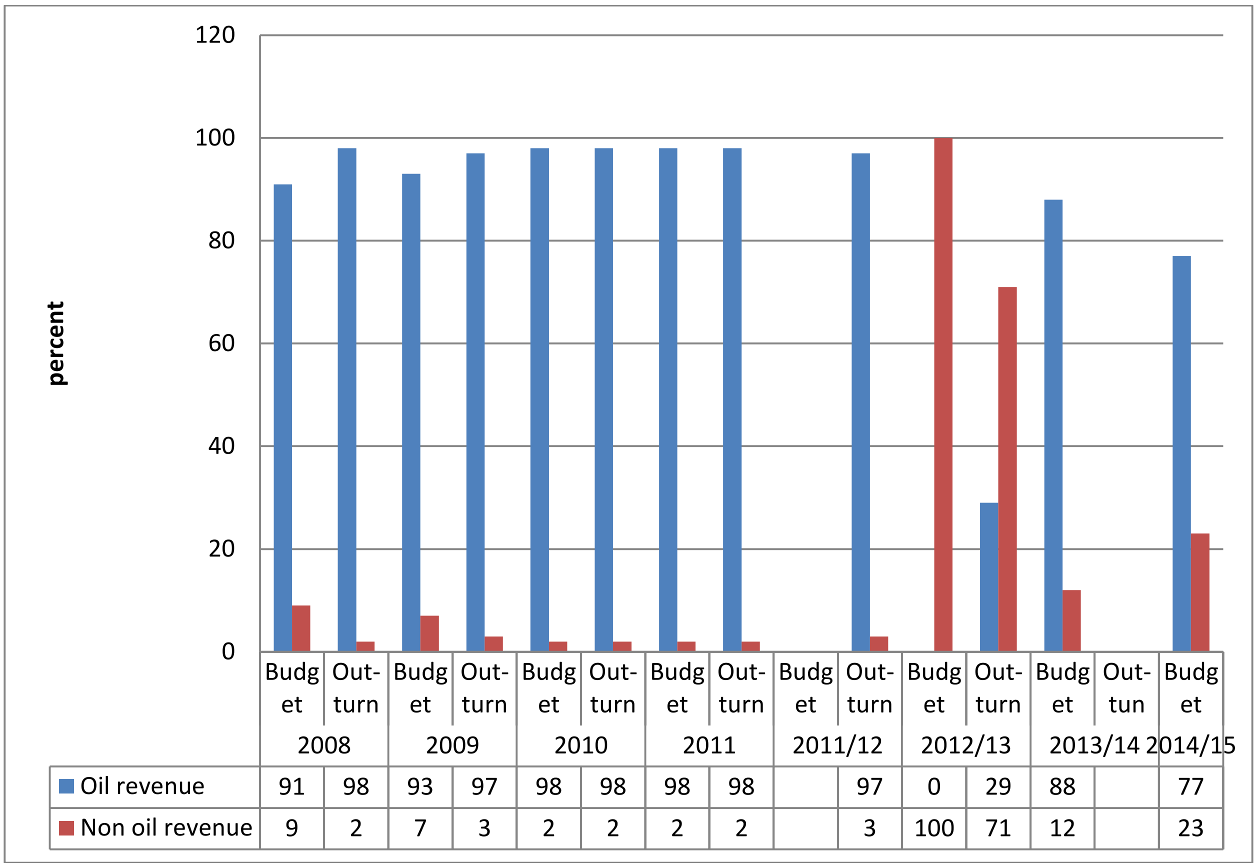
On 1 July 2014, the Finance Minister for the Government of South Sudan presented the draft budget for the 2014/2015 fiscal year featuring expenditures of 11.278 billion South Sudanese Pound (SSP), which is expected to be endorsed by the National Legislative Assembly in due course The budget has been presented against the backdrop of a prolonged period of austerity followed by an unforeseen and still ongoing internal conflict. The budget has a stated three-pronged focus on maintaining security, keeping the government running and providing core services to the people.

While the entire current budget document is not yet accessible, some early trends are discernable and being highlighted in this preliminary analysis as per below:

- In nominal terms, the 2014/15 budgeted represents a 35percent reduction in outlays when compared with the 17.3 billion SSP budgeted in the previous financial year (but a much smaller drop compared with projected actual spending).
- On the revenue side, budgets over the years since independence, continue to show wide fluctuations in estimates including on the non-oil side. Oil continues to be the major source of revenue with the government expecting it to finance nearly 80percent of the overall budget. However, there are uncertainties in oil revenue levels in the light of the ongoing conflict, particularly in the oil producing states.
- A number of structural issues affecting the planned strengthening of non-oil revenue include a narrow tax base and systemic weaknesses in tax administration which is not harmonized across the ten states. Historical trends on oil and non-oil revenues are depicted below in Figure 1. They show that the budgeted level of non-oil revenue is highly ambitious.
- The economic diversification imperatives are urgent, given current budgetary projections featuring a significant dip in oil production by 2020. While regional integration especially the East African Community (EAC), is a policy priority highlighted in the budget, there are particular challenges to note, owing to the fact that integration would in effect mean raising of tariffs (relative to current levels) , which in the absence of off-setting policy changes, would worsen the anti-export bias in the economy and imply trade diversion effects. This is because EAC has higher rates of tariff protection in several sectors, which the country would need to adopt as part of the Common External Tariff arrangement in EAC. The effect on weighted average tariffs on all trades world be offset in part by the diminished tariffs vis-à-vis EAC countries. There could be substantial potential revenue gains, and efficiency losses could be avoided with supporting policy changes. A full cost-benefit analysis would be useful to decide the way forward.

[1] For a budget to transcend its narrow bookkeeping function, it ought to have a sound functional institutional structure and capacity particularly at the state level, which is a significant challenge in South Sudan.

Figure 1: **Performance of oil and non-oil Revenue during the period the 2008-2014/15, South Sudan**[2]



	2008 Budget	2008 Out-turn	2009 Budget	2009 Out-turn	2010 Budget	2010 Out-turn	2011 Budget	2011 Out-turn	2011/12 Budget	2011/12 Out-turn	2012/13 Budget	2012/13 Out-turn	2013/14 Budget	2013/14 Out-tun	2014/15 Budget
Oil revenue	91	98	93	97	98	98	98	98		97	0	29	88		77
Non oil revenue	9	2	7	3	2	2	2	2		3	100	71	12		23

- On the expenditure side, the 2014/15 budget has allocated 3.97 billion SSP representing 35percent of the national budget to the security/defence sector.[3] The country stands to gain from t significant peace dividends if the current peace agreement is successfully negotiated.
- As Figure 1 shows, this marks a sharp year on year increase in total central government security sector bill reversing the decline noticed in 2013/14 **(2012/2013 28percent, 2013/2014-**

[2] The oil revenue budget was nil in 2012/2013FY because of shutdown of the oil pipeline as result of brief arm confrontation between South Sudan and Sudan. Government new tax policy of centralization of major non-oil revenue resources led to significant increased in non-oil revenue.

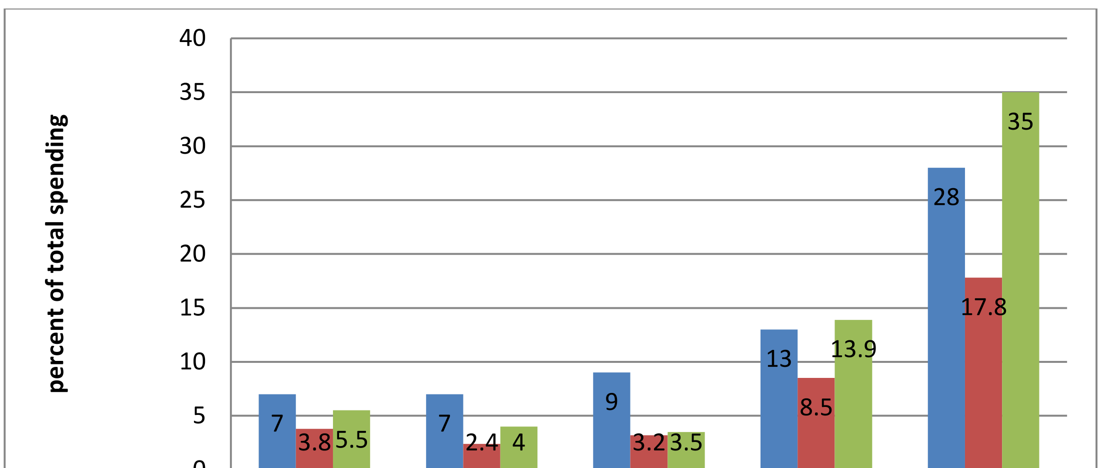
[3] The allocation to security sector excludes allowances and others cost of police, wildlife protection, prisons, fire brigade and states security spending from local revenues

17.8percent, 2014/2015- 35percent). The average of central government spending on security is **26.9percent** of the total government spending in the fiscal years 2012/2013, 2013/2014 and 2014/2015.

- A dominant part of the allocation is used to pay the salaries of the army and veterans with some provisions for operating costs and new capital expenditures. The same is true of the Rule of Law sector where the 1.573 billion SSP is being used to pay salaries to police, prison and fire services.

- Proportionately, in contrast, social sector allocations and outlays on rebuilding infrastructure in the country are pegged at less than 20percent of the current budget and have shown a decline relative to 2012/13, the year of independence of the country. This trend needs to be reversed urgently as South Sudan faces some of the worst deprivations on vital human development indicators[4]. Also, the state of infrastructure is extremely poor, with South Sudan having one of the lowest road densities in Africa and most of it being gravel roads which are not suitable for all weather transportation. Moreover, only around 1 per cent of the population has access to electricity, mostly generated by off-grid private diesel fuelled plants or generators to run businesses and households. The tariff for electricity charged to the lucky few with access to central electricity supplies in selected towns is one of the highest in Africa. Similarly, the key river ports including of Juba, Mongalla, Bor, Adok, Malakkal and Renk are in poor condition[5]. Finally, the crisis has brought wide ranging destruction of infrastructure, notably of hospitals, schools, bridges as well as private and government buildings.

Figure 2



	Education	Health	Infrastructure	RoL	Security
2012/2013FY	7	7	9	13	28
2013/2014FY	3.8	2.4	3.2	8.5	17.8
2014/2015FY	5.5	4	3.5	13.9	35

[4] For details see, South Sudan, MDG Status Report, 2012 available at http://www.ss.undp.org/content/dam/southsudan/library/Reports/MDGpercent20Reportpercent202012.pdf

[5] UNDP, 2014, The Diagnostic Trade Integration Study, 2014, forthcoming

- Over the years, budgetary allocations to the security sector have remained relatively high, whereas the resource allocation to development has been fluctuating. In 2012/2013 FY, resources allocated to education, health and infrastructure averaged 7.6 percent whereas a whopping 28percent of the total budget was allocated to the armed services sector, (not counting the large proportion of state transfers that is spent on this sectoral at the state level). The disproportionate resource allocation between development sectors and security is a major bottleneck in the socio-economic development agenda of the country. FY 2013/2014 saw a further reduction in budgetary allocation to the development sectors from 7.6 percent to 3.1 on average, when compared with a reduction in security sector budget from 28percent to 17.8percent due to austerity measures (which a subsequenced budget revision raised again).
- In average terms, as can be seen in the pie-charts below, (Chart 1,2 and 3) the total resources budgeted for allocation to the core development sectors viz. education, health and infrastructure, increased marginally from 3.1 percent in 2013/14 to 4.3 percent in 2014/15. When compared to the allocations made to the security sector, it is evident that the government continues to disproportionately restrict resource allocation for development which in turn is a binding constraint on its ability to delivery basic social service to the citizens.

The government has earmarked 7 percent and 2.3 percent of the total budget for arrears fund and interest payment on outstanding debt, respectively. While unavoidable, this creates considerable strains in a country that did not inherit any external debt post independence. This trend, if it persists, will lead to further crowding out of investment in sectors vital to economic growth and development in the country.

The debt challenge the country is facing also affects the ability of the private sector to grow and create jobs, and therefore the ability to diversify revenues to non-oil gets constrained. In the budget, 87.3 percent of 7.8 billion SSP of outstanding loans, as of June 2014, is from domestic sources. This borrowing has the potential to crowd out the private sector. In the previous financial year, the domestic outstanding debt was 70 percent of the total.

Chart 1: South Sudan National Budgets 2012/13 FY; Allocations to the security viz allocations to Infrastructure, Health and Education

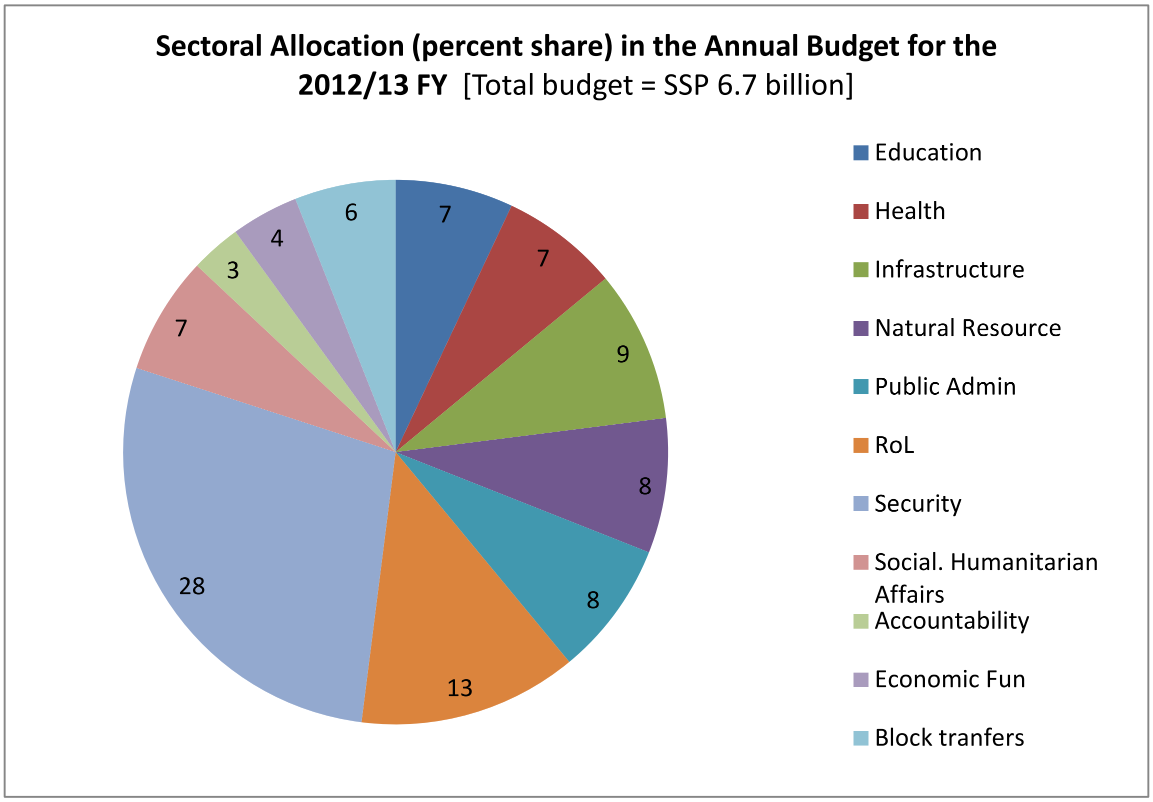


Chart 2: South Sudan National Budgets 2013/14 FY; Allocations to the security viz allocations to Infrastructure, Health and Education.

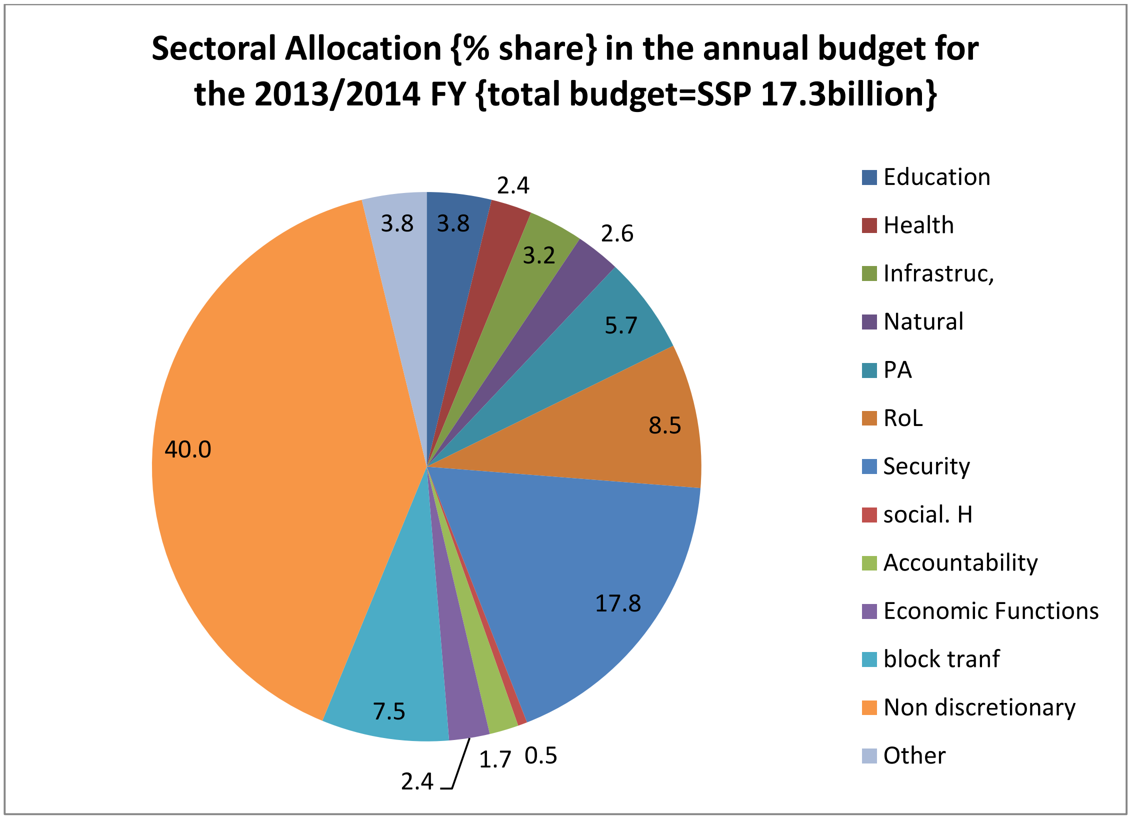
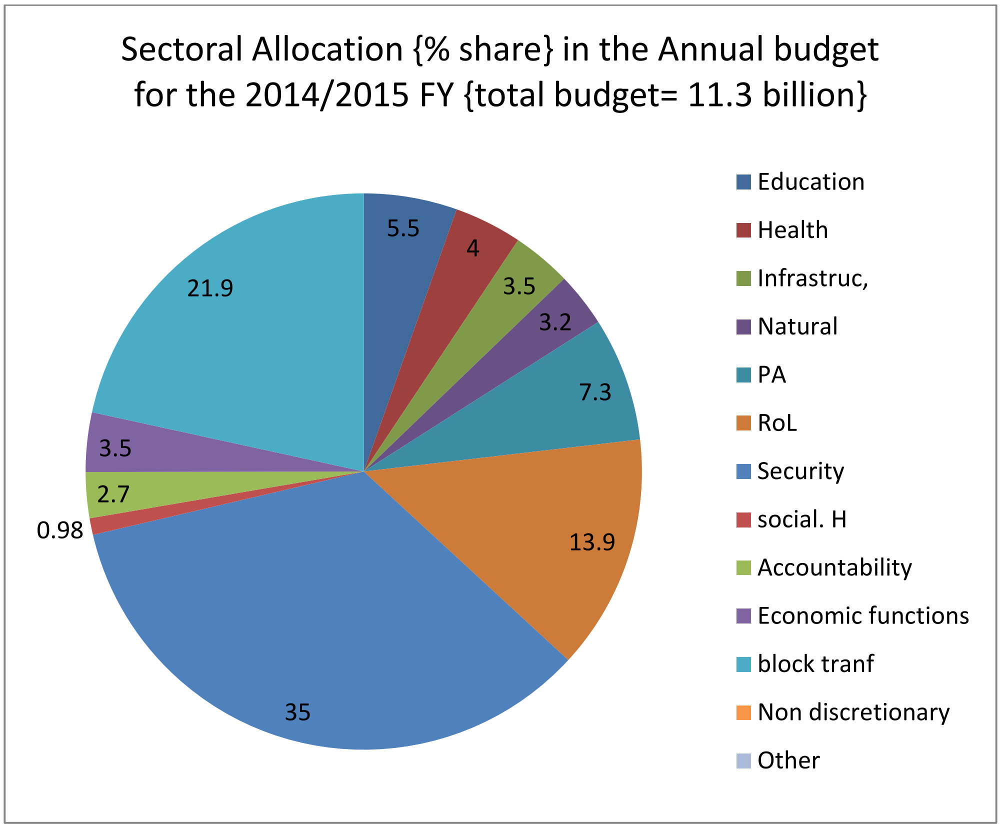


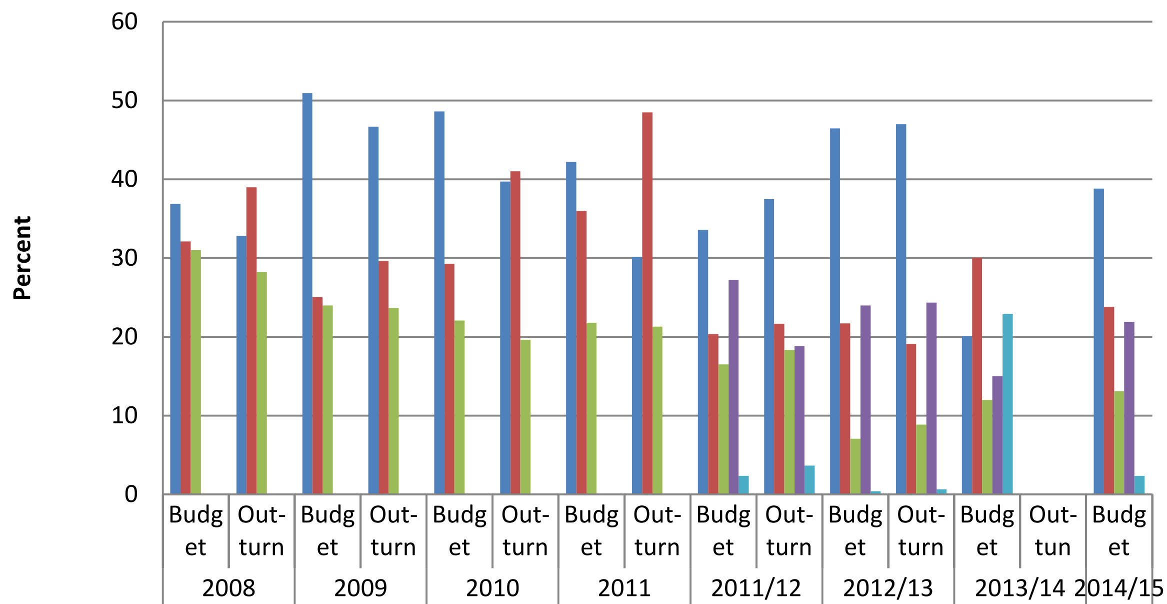
Chart 3: South Sudan National Budgets 2014/2015 FY; Allocations to the security viz. allocations to Infrastructure, Health and Education.



- A key concern on the expenditure side relates to the excessive size of the public sector wage bill, a condition South Sudan has historically inherited since its independence. Government is a major employer in South Sudan. The disproportionate size of the public sector wage bill is a having significant adverse impact on government expenditure since it crowds out other necessary spending. Ironically, the salaries paid are low and coupled with the poor conditions of service, lead to low productivity.
- Since pre-independence years, between 2008 and FY 2013l2014 the national government wages bill averaged 40percent of the total government expenditure, and over 73percent of the

total wage bill was disbursed to meet the salaries and wages of Defense and Veterans Affairs between 2008 and 2012/2013. The Defense & Veterans Affairs wage bill increased from 34 percent of the wage bill in FY 2008 to 84 percent of the wage bill in FY 2011/2012 and fell back to 70 percent in FY 2012/2013. This is an indication that government wage bill for all other sectors combined, relative to the security sector does not constitute a significant component of the general wage bill.

Figure 3



	2008		2009		2010		2011		2011/12		2012/13		2013/14		2014/15
	Budget	Out-turn	Budget	Out-turn	Budget	Out-turn	Budget	Out-turn	Budget	Out-turn	Budget	Out-turn	Budget	Out-tun	Budget
Salaries	37	33	51	47	49	40	42	30	34	37	46	47	20		39
Operating	32	39	25	30	29	41	36	49	20	22	22	19	30		24
Capital	31	28	24	24	22	20	22	21	17	18	7	9	12		13
Transfers		0	0	0	0	0	0	0	27	19	24	24	15		22
Other									2	4	0	1	23		2

[6]

Conclusion

The most pressing objective for macroeconomic policy, particularly fiscal policy, is rapidly restoring the economy to full health in an inclusive and equitable manner. The pace of economic growth since South Sudan's independence has been sluggish and insufficient to restore the economy to a sustainable growth path bringing substantial growth, closer to the country's potential. In addition, new significant downside risks were introduced due to persistent conflict, and adoption of a contractionary fiscal policy stance, which, however, was not a choice, rather, a necessity stemming from binding constraints on revenue and financing.

[6] Other expenditures from 2008 to 2011 were zero during the pre-independence periods, and the sharp fall in salaries from budgeted 47 percent to actual 20 percent in FY 2013/2014 is thus, misleading. Some component of actual spending on salaries for the period might have been included in 23 percent (actual) for other expenditures.

The assessment of revenue developments and performance should focus on revenues as a proportion of GDP in the light of revenues-to-GDP ratios in countries with similar levels of economic development. When the fiscal deficit needs to be reduced, the economic cost of raising taxes must be weighed against the costs of reducing public spending. A relatively easy solution would be to sharply curtail "private taxes" associated with roadblocks and corruption, leaving room for higher taxes flowing to the Treasury with no increase in the burden on the private sector. On the expenditure side, government should develop clear and unambiguous expenditure regulatory frameworks, and allocate resources in accordance with its expenditure policies to ensure that budget execution and expenditure management are in conformity with expenditure policies.

Sectoral shares of expenditures need a careful review with a human development orientation. As highlighted earlier, the 2014/15 budget has apportioned the largest share of the budget to security presumably on the understanding that security is a precondition for development. It is, however, also important to note that sustained investments in development are equally critical for security as a fragile peace takes hold. For instance, roads can be seen from the twin lens of being indispensable for an effective and timely response to any security threat and for increasing the connectivity between centres of economic activity and creating opportunities for commerce. Similarly, in the current budget priorities ought to have also focused on instituting enabling conditions for early recovery and creating social protection mechanisms including for the Internally Displaced Persons (IDPs) which number over 1.1 million as of July 2014. A significant proportion of the South Sudanese, particularly the IDPs have lost their livelihoods in the aftermath of the current unrest which has also been confirmed by the current UNDP assessment. Prior to the conflict the IDPs were engaged in various livelihoods activities such as farming, fishing, raising livestock , and in various types of businesses including running local restraurants, shops, charcoal making, firewoods and local construction materials as key income sources. In preparation for restoring a lost livelihood and eventual return to the communities of origin the IDPs would need rehabilitation support in their areas of origin as well in the IDP shelter sites.

References:

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2. Republic of South Sudan, Approved Budget 2012/2013
3. The Government of South Sudan, Approved Budget 2011
4. The Government of South Sudan, Approved Budget 2010
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6. The Government of South Sudan, Approved Budget 2008
7. 2014/2015 budget speech