Overseas Development Institute

Social Protection and Fiscal Space:

From affordability to feasibility

Social Protection to Tackle Childhood Poverty: Lessons from West and Central Africa

ODI, 16th June 2009

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Overview

- What is fiscal space?
- Fiscal space for social protection?
- Fiscal space for social protection in the 5 case study countries.
- What does this mean in a crisis?

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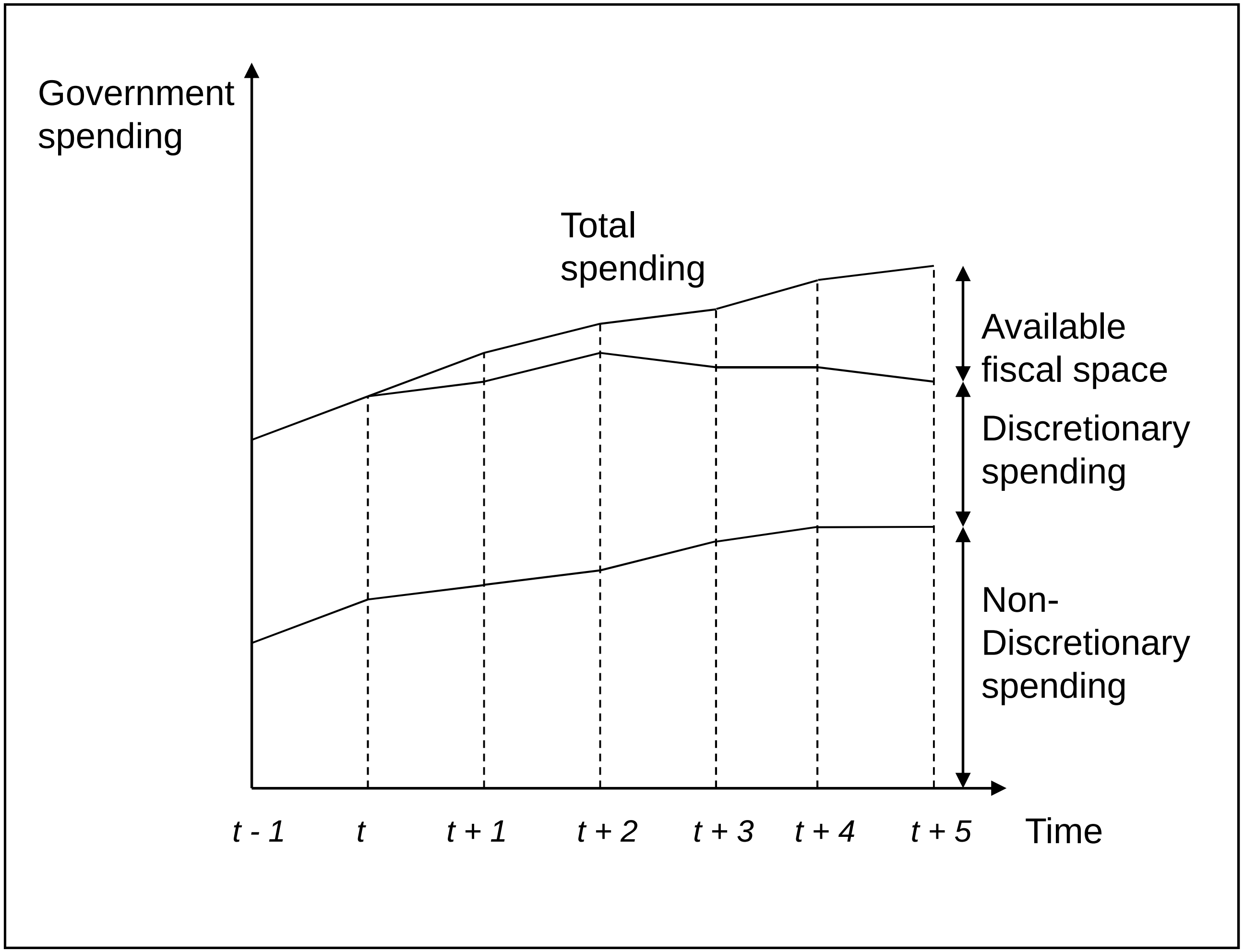
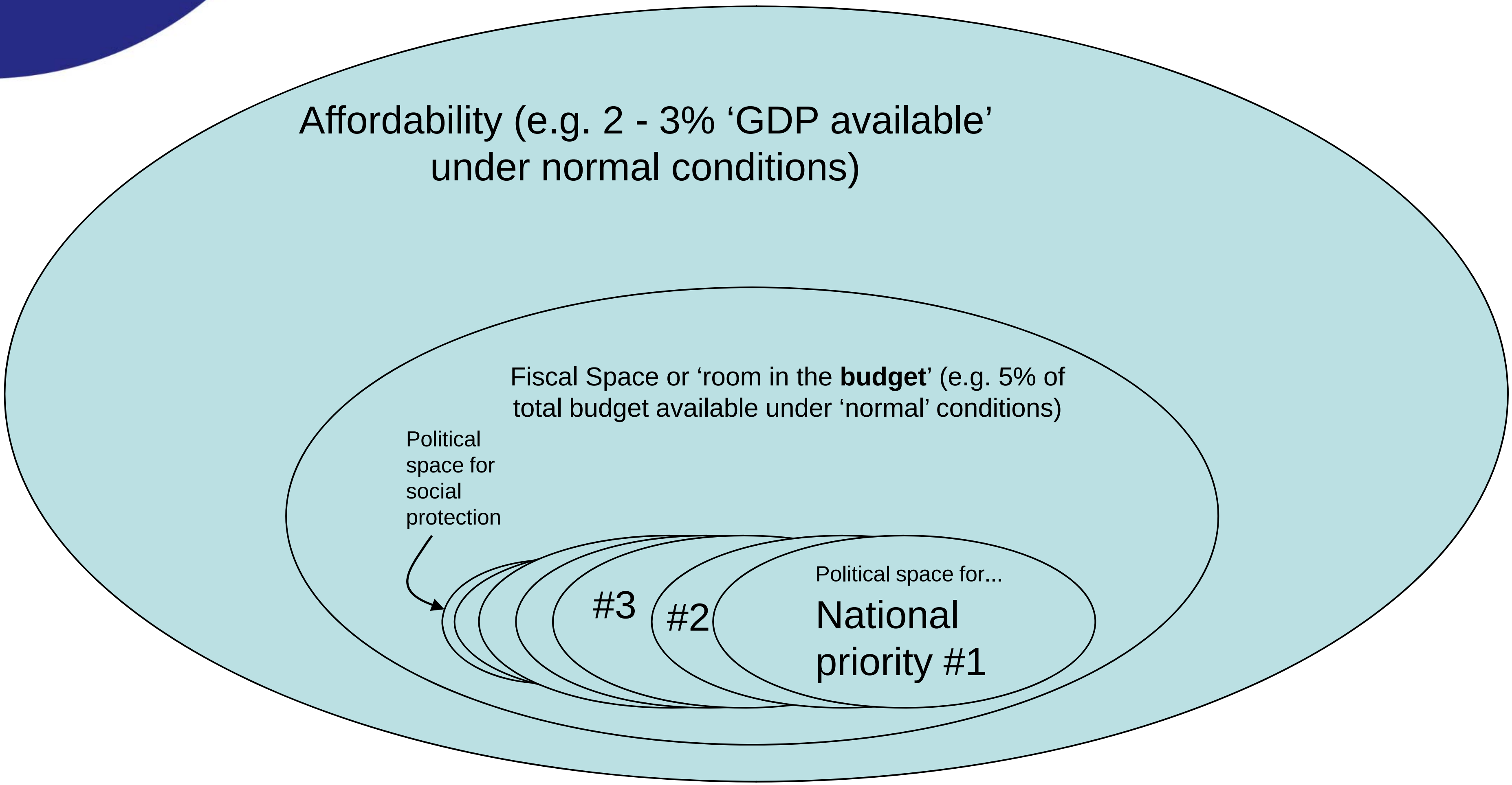
What is fiscal space?

- ‘room in a government’s budget that allows it to provide resources for a desired purpose without jeopardising the sustainability of its financial position or the stability of the economy’ (Heller, 2005).

What is fiscal space? (2)



What is fiscal space? (3)



Fiscal space for social protection?

- Recurrent in nature ⇨
  - ideally financed through the recurrent part of budget by increased taxes or reallocation
- Aid rarely finances recurrent part of budget…
- What if government and donor preferences differ (as is often the case)
- …How about aid financed projects in the investment/development budget?
  - Question marks over sustainability and full ownership (‘we know best’ ethos vs domestic resource allocation)?
  - Impact on broader public sector reforms rarely considered (PSR)
  - = contingent liability by stealth?
  - i.e. Off-budget Pilot ⇨on-budget project ⇨step away (crisis?)

Fiscal space for social protection in 5 case study countries

Key points regarding fiscal space for social protection in the 5 case study countries:

Congo:

- Significant potential fiscal space due to oil revenues.
- Sustained economic and revenue growth, but with a very low non-oil tax to GDP ratio.
- Key macroeconomic and fiscal aggregates suggest that a universal child benefit would be affordable, costing 2.0% of GDP compared with an overall fiscal surplus of 11.1% of GDP in 2007.
- The very low levels of health (2.2%) and education (1.2%) spending suggest weak government commitment to use fiscal space for improved social service provision.
- Poor performance suggests that managing social protection expenditures and programme delivery may prove challenging.

Fiscal space for social protection in 5 case study countries

Equatorial Guinea

- As a result of vast oil wealth, strong potential to finance social protection.
- The economy has grown significantly, but is strongly dependent on oil. Although it has the highest non-oil deficit in sub-Saharan Africa, there is potential for additional expenditures.
- Estimated costs of social protection are relatively low for Equatorial Guinea when expressed as a proportion of GDP: a universal child benefit and universal social pension could cost around 1% of GDP, while the overall fiscal surplus in 2007 exceeded 22% of GDP.
- However, It is not clear whether sufficient organisational capacity exists to develop and administer social protection programmes
- Thus social protection is affordable for Equatorial Guinea, but the feasibility of undertaking the associated institutional reform required to deliver social transfer programmes is highly complex.

Fiscal space for social protection in 5 case study countries

Ghana

- In the short term, it has limited fiscal space to spend on social protection, notwithstanding possible future growth and revenues due to exploitation of recently discovered oil reserves.
- Revenue and total expenditure are already high as a proportion of GDP. Ghana has showed willingness to spend on social protection, with the addition of 2.5% to the value-added tax (VAT) rate in 2004 to finance the new national health insurance scheme (NHIL).
- It has relatively high scores on institutional quality measures suggesting it would be spent relatively well
- A child benefit, even if targeted to children in households below the poverty line, would be difficult to afford,
- An option might be to expand of the recently launched LEAP cash transfer programme to cover all extreme poor households (currently planned to reach one sixth of extreme poor households in five years)

Fiscal space for social protection in 5 case study countries

Mali

- Economic and revenue performance in recent years has been good,but fiscal constraints are still significant.
- The revenue yield (tax revenue to GDP ratio) was 15.8% in 2005, suggesting some room for an increase when compared with levels in the region.
- Non-discretionary expenditures comprise a relatively small share, compared with discretionary expenditure, which suggests there may be some scope for reallocation.
- Estimates suggest that a targeted child benefit would cost around 3.2% of GDP, which is unlikely to be affordable,
- Only a more modest scheme (perhaps targeting the extreme poor with a lower benefit level) would be feasible in the short to medium term.

Fiscal space for social protection in 5 case study countries

Senegal

- Economic and revenue performance in recent years has been good, but with a relatively low tax level and revenue yields already relatively high there is limited scope for creation of fiscal space.
- The overall size of the public sector in relation to the economy as a whole is also relatively high, as total spending averaged 24.8% of GDP.
- Reallocation may be an area where fiscal space could be created, as discretionary spending stood at 17.8% of GDP in 2007.
- Estimates suggest that social protection would be relatively expensive for Senegal. A targeted child benefit would cost around 3.7% of GDP which would be much higher than total public health spending, so a more modest option would need to be found.

Fiscal space for social protection in 5 case study countries

The overall picture is therefore one of two broad country groups:

- First, the oil-rich countries of the Gulf of Guinea (e.g. Congo and Equatorial Guinea) which as a result of soaring global oil prices and rich oil reserves, have substantial available resources, with large overall fiscal surpluses.
- They thus have ample resources to finance additional expenditures on social protection
- However, these countries have the lowest proportions of public spending on the social sectors and the lowest measures of institutional quality
- The main barriers are political and institutional as evidenced by very low scores on measures of institutional quality.

Fiscal space for social protection in 5 case study countries

- In case of the three aid-dependent economies (Ghana, Mali and Senegal) affordability is more of a problem.
- These countries spend a larger share of public resources on the social sectors, but tax yields and public spending are close to the limits of ‘recommended’ thresholds for fiscal and macroeconomic sustainability.
- Measures of institutional quality are higher than in the oil-dependent countries although still low by international standards.
- It may prove possible to generate sustainable fiscal space.

Key points for fiscal space in a crisis

- Fiscal space likely to contract (likely less scope for anti-cyclical fiscal policy in LDCs)
- Will aid commitments hold? (Bad time for LDCs to have to pick up legacy entitlements!)
- Social protection not a strong candidate for a one-off stimulus (target groups small and poor, perceived as permanent)
- Crisis = opportunity for change in political priorities?