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National Budget 2003/04: Mr Mbumba's Low Maintenance Garden

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Finance Minister Nangolo Mbumba presented his seventh national budget to Parliament on Thursday 6 March 2003. This budget is characterised by severe expenditure restraint as the Minister battles to meet his expenditure target of 30% of GDP and stabilise the stock of public debt. While Mr Mbumba should be congratulated for taking his fiscal targets seriously, there is a danger that important policy objectives such as fighting crime, delivering good primary and secondary education to the masses, improving access to health services and generally reducing inequality will not be achieved unless the budget process and the public sector is made vastly more efficient.

Amid much talk of treating the economy like a garden, Finance Minister Nangolo Mbumba presented his seventh main national budget to Parliament on Thursday 6 March. A constant feature of this government is that, however radical its rhetoric may often be, its actions are generally conservative, some would even say timid. The reason for this apparent paradox is not hard to find. On the one hand, SWAPO was born into a radical African nationalist tradition, fighting not only a moral and diplomatic but also an armed struggle against apartheid oppression. On the other hand, SWAPO has consistently displayed remarkable pragmatism, not least in its management of the economy since independence in 1990. While the party's heart may tell it to fight imperialists, reject capitalism and intervene in the economy, its head acknowledges that dangerous economic experiments elsewhere have turned potentially prosperous countries into economic wastelands. What we appear to be witnessing in this latest budget suggests that the conservative head is winning out over the radical heart to quite a large extent, perhaps too much.

Is he meeting his targets (and are they the right ones anyway)?

The Minister has on many occasions repeated his intention to pursue three important fiscal policy targets: to stabilised the stock of government debt at 25% of GDP, to limit the budget deficit to 3% of GDP, and to reduce the level of government spending to 30% of GDP. It has never been quite clear where these targets have come from and what they have been based on. In an interview with the IPPR conducted in 2001, the Minister argued that the 3% deficit target had simply been taken from the Maastricht Agreement of the European Union. Whatever the case, the IPPR welcomes these targets in principle as they have the potential to bolster fiscal discipline and enhance the economic credibility of Namibia.

Table 1 shows how government's estimates of revenue, expenditure and the budget deficit have changed since the first Medium Term Expenditure Framework (MTEF) was published in 2001/02. In 2001/02 it looked as if nothing very dramatic was set to happen on the revenue side of the budget while expenditure was set to fall modestly to push the deficit to below 3% of GDP. By 2002/03 the medium-term picture had changed somewhat. Revenues were forecast to fall significantly as a proportion of GDP while expenditure was to fall even more following the introduction of the 30% expenditure target. Within three years the budget deficit was to fall to 2.5%. The Minister now says the deficit is likely to fall to 3.1% of GDP.

Table 1: Medium Term Expenditure Framework Projections 2001/02-2003/04

	01/02	***02/03***	***03/04***	***04/05***	***05/06***
MTEF 2001/02					
Revenue	31.3%	31.0%	31.4%		
Expenditure	34.9%	33.9%	34.3%		
Deficit	3.6%	2.9%	2.9%		
MTEF 2002/03					
Revenue	32.3%	30.1%	28.1%	26.5%	
Expenditure	36.6%	34.5%	31.1%	29.0%	
Deficit	4.3%	4.4%	3.0%	2.5%	
MTEF 2003/04					
Revenue	32.3%	31.9%	30.4%	28.3%	26.7%
Expenditure	36.6%	35.7%	33.4%	31.6%	29.7%
Deficit	4.3%	3.8%	3.0%	3.3%	3.0%

Source: MTEF documents 2001/02-2003/04, Ministry of Finance
Note: Shaded areas denote actual as opposed to budgeted figures

This year revenues and expenditures are forecast to be higher than last year's forecast but the budget deficit is expected to remain the same at 3% of GDP. Last year the expenditure target was expected to be reached by 2004/05. This year the target will only be reached by 2005/06. Unusually, it now looks as if the budget deficit will rise next year to 3.3% despite significantly lower expenditure. This is because revenues are set to fall by more than 2% of GDP from next year. The MTEF document suggests this will come about due to a fall in revenues from the Southern African Customs Union (SACU) because of lower tariffs and a new revenue-sharing formula.

If the estimates contained in the 2003/04 budget turn out to be accurate, the Minister can rightly state that the latest budget takes him a significant way towards his targets. Looking back, however, analysts may be permitted a certain amount of scepticism that this will actually take place. Revenue, expenditure and the deficit in the first year of the first MTEF ended up 1.0%, 1.7%, and 0.7% higher than planned respectively. Revenue and expenditure in the first year of the second MTEF look like ending up 1.8% and 1.2% higher although, because growth in revenue has exceeded growth in expenditure, the expected deficit falls from 4.4% of GDP to 3.8%. In other words, the deficit has been lowered not by expenditure restraint (which had been planned) but by unexpectedly high revenues (which had not and which may not, therefore, have occurred).

Revenues up by only 8.8%…

The Minister estimates that revenues will increase from N$10.3 billion in the revised 2002/03 budget to N$11.2 billion in the latest 2003/04 budget, an increase of some 8.8%. At the same time inflation is expected to be 10% during 2003/04 and GDP to grow by 4.2%, the highest real increase since 1997. Nominal GDP is expected to grow by 14.2%. It is hard to believe revenues will increase by less than inflation when the economy is growing faster than it has done in the last five years and no major tax cuts have been announced. We suspect the Minister is making his usual conservative revenue forecasts. When he made extremely conservative estimates in the last main budget, revenue estimates ended up rising by an unprecedented 9% in the revised budget.

…points to a lower deficit later in the year?

If revenues rise with inflation we can expect an additional N$118 million to become available in the revised budget later in the year. If revenues rise with nominal GDP an additional N$549 million will be available. It will then be up to the Minister whether to increase expenditure (the traditional way of dealing with "unexpected" additional revenue), to reduce the deficit to below 3% of GDP (to as little as 1.5% of GDP) or to do a bit of both.

Some sensible tax measures have been announced…

The comprehensive tax review announced in the 2001/02 budget has still not been made public although, according to the Minister, it has now been approved by Cabinet. The Minister did announce some changes to individual income tax. The tax threshold will rise from N$20,000 (where it has stayed since 1999/00) to N$24,000 and the maximum marginal rate will fall from 36% to 35%. Further tax measures include the introduction of anti-avoidance rules, the reduction and simplification of transfer duties, and the introduction of a Tax Tribunal to handle smaller tax cases.

…but is the balance between taxes right?

The top marginal tax rate and the corporate tax rate have now been brought into line with each other at 35%. By international standards Namibia's top marginal tax rate is low (but less so when compared to other developing countries). On the other hand its corporate tax rate is high. Given the policy objectives of increasing growth and decreasing inequality, we would have expected the reverse to be desirable (a lower corporate tax rate and a higher top marginal tax rate). We look forward to finding out what the tax review concludes on this issue.

The mystery of the corporate tax take deepens

In recent budget speeches the Minister has stated that the Receiver of Revenue has performed its revenue collecting functions with ever greater effectiveness. In the case of income tax on individuals this assertion appears to be supported by healthy tax receipts well in excess of inflation. However, in the case of company taxes this does not appear to be the case. Company tax receipts from non-mining companies have generally been below inflation in the past few years. The 2003/04 budget estimates corporate tax revenues will be lower than all main budget estimates back to 1999/00. The budget forecast is lower than the actual revenue raised in 1998/99. We have pointed out in previous publications that non-mining tax revenues have consistently been overestimated in recent years. Perhaps the Ministry is trying to rectify this with a conservative estimate. Clearly something very strange is going on. Again, the comprehensive tax review should shed light on this but it could be the case that the Ministry has been focussing its tax effort more on individuals than companies. Changing focus might result in greater receipts for the same effort. A final point on revenues is that (non-diamond) mining tax receipts are expected to fall this year by some N$100 million. Clearly the new Skorpion mine is not expected to directly contribute to the government's tax take for some years to come.

He seems to be serious about expenditure restraint

Moving to the expenditure side of the budget, the Minister restated his intention to reduce spending to 30% of GDP although, judging by his latest projections, this will not be reached until 2005/06, still a politically safe distance away. Last year it was going to be reached next year. The IPPR had long argued for an expenditure target when it was announced in 2001. However, it is by no means clear government has chosen the right one. While a target of 30% of GDP will do much to reassure domestic and foreign investors (especially if it is reached), it is hard to believe that a country with such enormous public policy challenges can adequately address them without resorting to higher levels of public spending. It could be that Namibia is on the verge of a long-awaited "normalisation dividend". That is to say, the period during which the twin demands of national reconciliation and former fighters have stretched the budget is coming to an end, thus freeing up resources for economically productive public spending. If this is the case, lower public spending might still prove adequate. We are not convinced this is the case. Furthermore, unrealistic expenditure targets may simply encourage government to introduce taxes "through the back door", a trend we highlighted in the last January IJG Business Climate Monitor.

Overall, however, expenditure restraint has been severe with total spending rising by a mere 6.8%. Only eight out of thirty votes have received allocations above the expected rate of inflation of 10%: the National Assembly, Civic Affairs, Finance, Health, Lands, the National Planning Commission, Higher Education and the Electoral Commission. The Office of the Prime Minister, Defence, Labour, Works, and Transport have all suffered nominal cuts. The Office of the President, Police, Basic Education, Agriculture, Prisons, and Fisheries have received very small increases indeed.

Is underspending being tackled?

One notable feature of this budget is the relatively low allocation to so-called development spending. This year's development budget is a mere N$1.177 billion compared to N$1.188 billion in 2002/03. We have criticised the Ministry in the past for allocating more to the development budget than ministries had the capacity to spend. The low 2003/04 allocation may be in recognition of this problem. The Minister did not make such an argument explicitly but this might have simply been out of a desire to avoid political flak since most parliamentarians continue to view development spending as "good" and operational spending as "bad". He did, however, mention underspending as a problem, a sentiment with which we entirely agree.

A longer-term view of public pay

A further issue of importance is that of public pay. The Minister announced that N$303 million has been set aside for salary increases during 2003/04. This amounts to almost 6% of the total allocation to remuneration. There are encouraging signs that government is taking a longer-term view of public pay with the latest settlement being part of a three-year pay deal according to recent press statements. This is to be welcomed and is certainly in the spirit of the MTEF.

Expenditure highlights by vote…

The following paragraphs highlight what we believe to be the issues of most importance in each of the expenditure votes contained in the budget document. In examining expenditure allocations, readers should bear in mind that overall spending increased by only 6.8% and that inflation is expected to average 10% during this financial year. Any activity allocated more than 6.8% is receiving more than the average. Any activity allocated more than 10% is receiving a real as opposed to a nominal increase in resources (ie. an increase exceeding the rate of inflation).

Vote 01 Office of the President

The ***National Intelligence Security Agency*** receives N$46.6 million, an increase of over 13%. Since 1994/95 the NISA has been awarded average increases of 11% a year. It is not clear whether anyone anywhere is in a position to assess whether these expenditures have been effective.

Vote 02 Office of the Prime Minister

The ***National Emergency Disaster Fund*** receives N$3 million compared to last year's N$58 million. The current policy is probably to reallocate money from the Contingency Fund (see below) if and when an emergency takes place.

The ***President's Economic Advisory Council (PEAC)*** receives 17% more despite the lack of any apparent activity pending the implementation of recommendations of a report by NEPRU. As in last year's budget, N$17,000 is allocated for furniture and office equipment. According to our calculations, to date PEAC has been allocated N$92,838 for furniture and office equipment. One wonders how a Main Division with only two people can consistently receive such high allocations. The importance here is not so much PEAC itself but what the allocations say about the budget process as a whole.

Table 2: Furniture and office equipment allocation for PEAC

N$	***'99/00***	***'00/01***	***'01/02***	***'02/03****	***'03/04****
Furniture and office equipment	55,638	1,200	2,000	17,000	17,000

*budgeted not actual expenditure

Vote 05 Civic Affairs

Civil Registration receives a sizeable allocation of N$21.25 million for new equipment.

Vote 06 Police

The Minister stated that more resources are to be devoted to ***combating crime*** and, indeed, Main Division 02 Combatting of Crime receives a healthy 11% increase. Our comment last year, however, still holds. This allocation of N$284 million is almost exactly the same as the combined allocation to VIP Security (N$88 million) and the Special Field Force (N$194 million). There appear to be 2,930 posts filled for Combatting of Crime compared to 2,311 in VIP Security and 5,010 in the Special Field Force. Remarkably, more constables are employed protecting VIPs (2,084) than combating crime (1,679). When Main Division 07 VIP Security was introduced under that name in 2001/02, the ratio of VIP Security spending to spending on Combatting of Crime was 18%. It is now 31%. Expenditure on the Special Field Force has been cut from N$267 million although there seems to be as many posts filled as last year.

Vote 08 Defence

The total allocation to the ***Ministry of Defence*** is exactly N$56 million lower this year compared to last year. This is part of a longer-term trend which has seen defence spending decline since its peak in 1999/00 when defence spending hit 3.7% of GDP, a high number by historical and international standards.

Vote 09 Finance

The allocation to ***pensions for members of the National Assembly*** increases from N$42 million to N$43 million.

The ***contingency fund*** receives N$150 million under Main Division 10. This allocation has fallen from a peak of N$204 million in 2001/02.

Air Namibia receives N$400 million under Main Division 11. We have already commented at length on this issue. According to *The Namibia Economist* of 4 April 2003, the company is attempting to lease its Boeing 747 and appears to have appointed a new CEO from Swiss-based company ExecuJet which is set to become a shareholder.

The ***Namibia Development Bank (NDB)*** receives N$125 million, the same allocation as last year. Although its board has now been appointed, it is unclear when the NDB will actually commence operations. We remain to be convinced of the need for a Namibian Development Bank to finance infrastructure. It is hard to believe it could do this more cheaply than existing institutions and arrangements. That does not mean, however, that there is no useful function it could serve.

The Ministry of Finance is allocated N$77 million under Main Division 13 for information technology, presumably for the new ***Integrated Financial Management Information System and Payroll Deduction Management System*** mentioned in the budget speech.

Repayments of principal on foreign loans rise from N$33 million last year to N$52 million this year as the grace periods end on concessional foreign loans. Interest payments on foreign loans rise from N$25 million to N$48 million. The allocation to ***loan guarantees*** rises from N$103 million to N$170 million. The Minister has, as promised, been admirably open about the state of government loan guarantees, providing a breakdown in the accompanying MTEF document between guarantees given to domestic and foreign institutions (Table 10 p20). As mentioned in our ***IJG*** Business Climate Monitor for January 2003, the Bank of Namibia had already started to publish information on loan guarantees earlier in the year. It remains difficult for outsiders to assess the risks associated with such guarantees since it remains unclear for which institutions they have been granted. The Minister assures the public they are awarded to “financially sound companies” and therefore have a “low default risk”. The hope is new guarantees are now rigorously assessed following the experiences of the past few years.

Vote 10 Basic Education, Culture and Sport

The total allocation to Vote 10 increases by a mere 2.2% although the Minister’s office receives 6.5%. The allocations to ***primary education (Main Division 04) and secondary education (Main Division 05)*** rise by 3% and 0% respectively. Hostels (Main Division 11) receive 8% more (N$220 million), precisely half of the entire allocation to secondary education. These exceptionally low increases may partly be explained by the fact that the main budget has traditionally excluded important donor contributions to primary education and other activities. These are generally included in the revised budget later in the year. However, there is a strong suspicion that the availability of donor funds has allowed government to allocate less to primary and secondary education than it otherwise would have. Since no one yet believes we have succeeded in providing quality primary (let alone secondary) education to the entire population, this is of serious concern.

Vote 13 Health and Social Services

Within the Ministry of Health and Social Services the allocations to Administration, Hospital Management, Regional Health and Social Welfare, and Primary Health Care are N$52 million, N$434 million, N$637 million and N$20 million respectively. That ***Primary Health Care (PHC)*** receives the equivalent of half of the administration budget and a lower allocation than in 2001/02 appears remarkable since PHC is generally regarded as the main means of bringing preventative health services to the poorest in society. It is difficult to identify the additional resources government says it is putting into HIV/AIDS from the budget document.

The allocation to ***social pensions*** under Main Division 06 rises from N$332 million to N$415 million. The Minister stated that an additional N$117 million had been made available to clear the backlog of more than 17,000 applicants which had built up. It is not clear where this money has been allocated. Neither is it clear that the fundamental cause of the backlog is being addressed. South Africa recently raised its social pension to R700 a month. On an income-for-income comparison (income per capita of US$3,020 in South Africa compared to US$2,030 in Namibia in 2000 according to the World Bank World Development Indicators 2002), Namibia's pension would now be N$470 per month rather than the present N$250. Namibia's social pension has not even kept pace with inflation since 1990. We estimate that if the N$92 pension had risen in line with inflation it would now be just under N$290 a month. If it had risen in line with nominal GDP it would be over N$550 a month.

Vote 16 Justice

The ***Office of the Ombudsman*** receives N$91,000 less than last year. Government is on the verge of creating an additional and hugely expensive Anti-Corruption Agency when there are strong arguments that a beefed up Ombudsman could do the job equally well.

Vote 17 Regional and Local Government and Housing

The allocations under ***Main Division 07 (Regional Offices)*** appear to have been moved to Main Division 03 (Regional, Local Government and Traditional Authority Coordination).

Vote 18 Environment and Tourism

The ***Namibia Tourism Board*** receives N$30 million under Main Division 05. This is probably due to the delay in implementing the tourism levy on the tourism industry which was supposed to take place at the beginning of this financial year.

Vote 20 Agriculture, Water and Rural Development

There appears to be little sign that the ***N$1 billion*** mentioned in a Cabinet press release last year has been made available to the Ministry of Agriculture. Perhaps the N$1 billion was simply a reassurance that the Ministry of Agriculture would continue to receive an annual allocation of around N$500 million over the coming years.

Vote 25 Lands, Resettlement and Rehabilitation

The Minister announced that the allocation for land purchases under the ***land reform programme*** was to increase from N$20 million to N$50 million under Main Division 10 (Land Use Planning and Allocation). This is approximately what is spent on the National Intelligence Security Agency and one eighth of the allocation to Air Namibia. It does now look as if the capacity to spend these allocations has improved over time. No mention of the land tax was made in the budget speech which, according to *The Namibia Economist* of 4 April, is indeed set to be introduced on 1 April and raise some N$30 million a year over the medium term.

Vote 27 Higher Education, Training and Employment Creation

The Ministry of Higher Education is one of the big winners from this budget, increasing its allocation by N$74 million or almost 15%. Subsidies to the ***University of Namibia and the Polytechnic of Namibia*** rise from N$123 million to N$154 million (25%) and N$68 million to N$79 million (16%) respectively. This compares to the 3% and 0% increases for primary and secondary education respectively already mentioned.

The Minister made no mention of the ***National Centre for Innovation, Entrepreneurship and Technology or the Council on Employment Creation*** announced in the 2001/02 budget speech.

Vote 30 Information and Broadcasting

Information and Broadcasting is back in its own ministry with its own vote but very little else appears to have changed. The NBC receives N$104 million in subsidies, down from N$111 million last year. ***NAMPA and New Era*** plod further along the long and winding road to commercialisation but continue to receive the same subsidies as last year. Last year's budget included revenue estimates for sales and advertisements of *New Era*. This year's budget excludes these estimates.

Doing more with less…

In setting such an ambitious expenditure target, the Minister of Finance is setting the government's budgeting system an enormous challenge. Namibia will have to address its immense inequalities and social problems with more limited public spending. That means relatively more public services will have to be delivered with relatively fewer resources. For this to be successful Namibia's budget system will have to improve its capacity to identify priorities and eliminate wasteful spending. It will have to incorporate incentives so that good performers are rewarded and poor performers effectively reformed.

Some belt-tightening is apparent

There are signs that a certain amount of belt-tightening is taking place. The total allocation to the offices of office bearers increased from N$89.4 million to N$94.7 million, an increase of some 5.9%, less than overall spending and less than inflation. This average figure hides large differences in individual office bearers. The offices of the Minister of Home Affairs, the Minister for Women Affairs, the Minister for Health, the Minister of Regional and Local Government and

Housing, the Minister of Fisheries, the Minister of Higher Education, and the Attorney General all receive allocations above the expected rate of inflation. The total allocation to administration is set to rise by 7.2%, faster than total spending, from N$780.6 million to N$836.5 million. The proportion spent on offices and administration is 7.6% of total spending, exactly the same as last year. Whether good performers are being rewarded and poor performers reformed is open to question. Certainly, Air Namibia, UNAM and the NBC continue to receive large subsidies yet have all been subject to investigations, enquiries or restructuring.

Does Mr Mbumba have the gardening skills?

Can inequality be significantly reduced if spending declines to 30% of GDP? Maybe. Simply put, those countries which have most successfully reduced inequality have done so by stimulating economic growth and thereby creating jobs for the poor. If fiscal restraint has the effect of encouraging investment and growth to the extent that jobs are created for the unskilled, this will be a major step towards reducing inequalities. However, if spending is skewed towards the better-off and the anticipated investment and jobs do not materialise, inequality will worsen.

There are worrying signs that the new path the Minister appears to be charting will increase rather than decrease inequality. Although the Minister speaks of “notable progress being achieved” on poverty, we do not know what evidence the Minister has to back this up. Our analysis of the budget shows that the poor come off particularly badly in the services they require most – policing, primary and secondary education, primary health care, and social pensions. Indeed, in so many ways the budget appears to be skewed in favour of those who already have – from VIP security, to parliamentary pensions, subsidies to parastatals, tertiary health care, and higher education. If inequality is to be seriously addressed through the budget, Mr Mbumba will have to make sure his gardening skills equal those of other successful Namibian gardeners who achieve minor miracles with only limited inputs.