Fiscal Policy Analysis
Budget allocation, Public Debt and Deficit since independence: Where are we coming from and where are we heading?

Introduction
Fiscal policy – like it is commonly defined – is a government policy used to influence a country’s economy through a change in government spending and/or taxes. Increasing taxes for example would cut down on people's disposable income and slow the economy in an effort to control macroeconomic variables such as high inflation. On the other hand, lowering taxes can give people more money to spend and thus induce a boom to the economy. Increasing government spending can give suppliers an incentive to increase production and thus an increase in income. The opposite holds when there is a reduction in government spending. Hence, fiscal policy can either be expansionary or contractionary depending on the state of the economy and the government’s objective(s). There are a number of challenges with fiscal policy, *Inter alia*: budget deficits which may be accompanied by high public debts, trade imbalances and/or fiscal instability.
Government policy for example is affected by its spending and when expenditures are greater than revenue, there will be a deficit. When the government is running a deficit, it cannot increase spending to stimulate the economy if there is a need to or if it wants to increase its spending while running a deficit. As such, it may need to borrow either internally or externally where borrowing will boost its debt level. Additionally, if the government reduces taxes, people’s income increase and they may tend to import more (this is true when applying the marginal propensity to import which says that a proportionate change in disposable income may cause a proportionate change in imports). Where there is too much importing, the economy risks running a trade deficit which in turn have negative impacts that fiscal policy is actually aimed to address. Therefore, it is important to understand fiscal policy as well as fiscal stabilisation as the effects of government expenditures, taxation, and debts on the economy are of immense importance. It is in light of the above that this policy brief aims to review Namibia’s expenditure/budget allocation since independence, public debts and deficit and ultimately look at what the future holds for Namibia in terms of fiscal option while maintaining fiscal stability.

**Government budget allocation since independence**

Namibia’s fiscal policy is countercyclical, implying that it is undertaken to support the economy during subdued economic environment. For the past few years the Namibian government maintained an expansionary fiscal policy (fiscal expansion undertaken since 2008/2009) which has been taken to cushion the economy against the global headwinds and address the structural challenges such as slow economic growth and high levels of unemployment. “This policy stance has served our country relatively well” – says the Minister of Finance in her 2013/2014 budget statement. For example, as a result of fiscal expansion, Namibia has witnessed a rebound in economic growth from -1.1% growth experienced in 2009 due to the effects of the global financial crisis. Since then, the economy though has not been growing positively each year, the average growth has been positive at about 4.3%. Estimates of the future economic outlook are also showing a positive growth expectation of about the same rate until 2020 (MacroABC projections).
Analysis of the budget allocation, Figure 1(a) and (b) below show that since independence, Education has been one of the votes that received the highest share of the government budget (about 23% of the total budget allocation on average).

Figure 1 (a): government budget allocation by votes, 1990 -2000

Source: Ministry of Finance Estimates of Revenue and Expenditure

Figure 1 (b): government budget allocation 2001 -2014

Source: Ministry of Finance Estimates of Revenue and Expenditure.
Another vote that has been receiving a giant share of the government budget is Finance with an average share of about 14%. This vote’s share has however reduced in the more recent years. For example, its share reduced from about 22% in 2006/2007 to about 12% in 2013/2014. However, compared to other votes such as Environment and Tourism, Mines and Energy, and Trade and Industry; its share remains significantly higher. The third highest receiver of the government budget has been the Health and Social Services vote, with an average share of about 12%. Therefore, from the above Figures, if we were to rank votes according to their share of the total budget, the top five (in the order of their share to the total budget) will be [1] Education [2] Finance, [3] Health and Social Services [4] Defence [5] Transports, Agriculture Water and Forestry. Looking at the trend of the budget allocation especially in Figure 1(a) while being mindful of the priority areas of the NDP 4 especially, the initial conclusion that we get from this Figure is that resources are not allocated accordingly. In other words, resources are not allocated according to the NDPs priority areas. With development budget being seen as the money allocated to the government’s productive spending, analysis of the development budget’s sectorial analysis (Figure 2 below) also indicate that there seem to be no distinct trend of how budget is allocated to various sectors during different time periods. Although it is clear from Figure 2 that most of the capital budget is allocated to the economic sector, the trends do not really bring out which periods we are prioritizing on either of the sectors. For example, the allocation to the economic sector for 2009/2010 to 2013/2014 and that of 1999/2000 to 2002/2003 financial years are similar that one would hardly indicate which of these years was the economic sector the priority area? From these observed budget allocation trends, it leaves a question mark on whether budget allocations are really in line with the National Development Plans and if not, why not?
Analysis of the execution rates\textsuperscript{ii} indicates that there seems to be a mismatch between the execution rates and the allocation of funds to different votes. Votes that are allocated more funds appear to have lower execution rates compared to those that have been allocated less funds. For example, Education, besides it being the highest allocated vote, it has an execution rate of only about 74% on average (from 1994/95 to 2010/2011). Given this low execution rate (lower than the rate for the votes such as Police, Defense and Works), one may wonder why this vote is allocated more funds when they cannot really utilize them all. The Police and the Defence are among other votes with higher execution rates, they have execution rate of more than 80%. Other votes with low execution rates include among others the Finance, Transport and the National Planning Commission which have execution rate of less than 70% on average. However, if compared to the execution rates for these recent years where the government has been carrying out expansionary fiscal policy, the rates are higher especially for votes such as Transport, Prison and Correctional Services, Trade and Industry, Defence Foreign Affairs and Police had execution rate of above 85% on average between 2005/06-2010/11. Regardless of the higher and/or low executional rates for some votes, the broad picture of the budget allocation indicates that the allocation seem to have been an “incremental exercise”, that is seemingly based merely on previous years’ budget estimates. As can be seen in Figure

\textit{Source: Development budget estimates of expenditure, National Planning Commission.}
below, Namibia has indeed been carrying out an expansionary fiscal policy. The total budget allocation has been following an upward trend.

Figure 3: Total budget allocated since independence

![Graph showing total budget allocation since independence](image)

Source: Ministry of Finance Estimates of Revenue and Expenditure, MacroABC Model.

The total budget allocation almost doubled from about N$18.0 billion in 2007/08 to N$47.0 billion in 2013/14. Needless to say, the increase in the government expenditure over these periods may be attributed by the desire to achieve the NDP3 and the NDP 4 goals (however, allocation seemed to be not directed to the right votes and/or sectors). The increase in the total allocation in 2006/07 and 2011/2012 when the growth in budget allocation peaked to 18.4% and 28.4% respectively, may be an indication of the desire to increase the expenditure on the priority areas of the NDP3 which if the goals are met may ultimately lead to higher economic growth and the goals of the Targeted Intervention Program for Employment and Economic Growth (TIPEEG) which was introduced in 2011. When looking at the disaggregation of government expenditure in terms of operational and capital spending, they vary from year to year (Figure 4 below).
Figure 3: Operational and Development expenditure as a percentage of GDP.

![Graph showing Operational and Development expenditure as a percentage of GDP.](image)

Source: Ministry of Finance Estimates of Revenue and Expenditure.

Figure 4 shows development budget, as indicated by the ratio of the development budget to GDP, is small, implying that our government expenditure is highly overwhelmed by operational expenditure (which appears to be mostly personnel expenditure and other operations of the government institutions). The operational budget reached a highest rate of 35% in 1992/1993 and the lowest rate of about 21% percent in 2006/2007. The higher operational expenditure in 1992/1993 may be attributed to the recruitment of the former freedom fighters. Development expenditure as percentage of GDP on the other hand is very low, having the highest peak of about 7% in 2011/2012, a year when TIPEEG was introduced. Despite the seemingly low development expenditure as indicated by the low development expenditure as a percentage of GDP, execution of the development budget seems to be a challenge. Since 1994, the execution rate has never reached 100% on average (Figure 5). The highest execution rate is recorded in 2000/2001 when the rate reached 96%. In the first year of TIPEEG (2011/2012) the execution rate stood at 92%. With development expenditure being the productive spending of the government, it is necessary that the money allocated for development expenditure is utilized to the maximum.
While it remains too early to comment on whether it was worth spending so much money on programmes such as TIPEEG, since it is a programme that led to total allocation to increase to a highest peak ever (expenditure grew by 28.4% as seen in Figure 2 above), it is imperative to assess the effects of higher government expenditure both in the short-run and the long-run. It is against this latter statement that we now look at Namibia’s fiscal stance.

Namibia’s fiscal stance

There seems to be no standard definition of fiscal stance, although some measures of fiscal balance may be typically involved in measuring fiscal stance. However, in a simpler version, one may define fiscal stance as “the state of Public Finance”. The measures of fiscal stance basically are attempting to convey a sense of the impact of fiscal policy on domestic demand and financial resources. The indicators of fiscal stance are to a larger extent are related to how the fiscal deficit affects the macro-economy. Thus, the macroeconomic impact of fiscal deficit and how it is financed is important since it affects among others; (i) aggregate demand, and hence output, inflation and/or relative prices (ii) the balance of payments and (iii) the domestic financial
markets including interest rates and private sector borrowing. A commonly used indicator to assess the fiscal stance is the overall balance, which is defined as revenue and grants minus expenditures and net lending. The primary balance which measures the difference between total government revenue and total expenditure on goods and services during a fiscal year but excluding the debt service costs (mainly interest rate payments) may also be used as a measure of fiscal stance. The primary balance shows the extent to which revenue covers expenditures before taking into account finance costs. Therefore, one would say that the primary balance measures the current effects of a discretionary budget policy. As a starting point of analysis, Figure 5 below plots the time path of revenue, government spending and the revenue-expenditure gap for Namibia since independence.

**Figure 5: Revenue verses government spending**

![Graph showing the time path of revenue, government spending, and the revenue-expenditure gap for Namibia since independence.](image)

*Source: Ministry of Finance Fiscal data and MTEF projections.*

The revenue line has mostly been below the expenditure line, an indication of a gap between the two fiscal indicators. The revenue-expenditure line has been mostly negative, pointing to a budget deficit that the Namibian government has been experiencing. This negative gap is not surprising having learned from the preceding discussions that fiscal policy has been expansionary since 2008/09. The revenue-expenditure gap widened in 2011/2012 when it increased to more than
N$7 billion. This huge deficit is also not surprising given that this is the period when the government undertook TIPEEG; hence the fiscal expansion in 2011/2012 widened the deficit that was witnessed this year. Figure 6 below goes one step further in explaining the fiscal stance. It depicts the evolution of the primary balance, overall balance, revenue and public debt GDP ratio where the public debts includes both domestically and externally acquired funds. The primary balance and the overall balance follow the same trend; however, the overall balance is lower than the primary balance. This makes sense since the primary balance excludes finance costs while the overall balance is finance cost inclusive. Ideally, overall balance is the best measure of the fiscal stance. Fiscal rules suggest that, when the deficit is increasing, public debts are expected to go up. The rationale behind the fiscal rules is that; when deficits mount, more funds may be needed to finance it, hence, ceteris peribus; borrowing will increase to finance the deficit. This could be the reason we are seeing that when the deficit widened in 2011/2012, the debt GDP ratio (Figure 6) also increased from 16.2% in 2010/2011 to 26.4% in 2011/2012.

**Figure 6: Evolution of the primary balance, overall balance, revenue and public debt GDP ratio**

![Graph showing the evolution of the primary balance, overall balance, revenue and public debt GDP ratio between 2009/2010 and 2015/2016.](source)

*Source: Namibia MacroABC model and own calculation.*

**What do these numbers mean for Namibia?**

Well, a widening fiscal deficit that results from a fiscal expansion would mean that public debts are likely to increase. This is
because; the relationship between deficit and debts is like a vicious circle. Meaning that, if there is an increase in deficits for example, borrowings increase in an attempt to finance higher expenditure which actually led to the deficit. This simply means that one is solving a problem with another problem. An increase in borrowing leads to an increase in debts which may in turn increase interest payments (which forms part of total government spending) and therefore the end results will be a widening deficit. The sketch below (Figure 7) illustrates the just explained relationship between the deficit and the debt. The relationship is indeed a vicious circle.

Figure 7: Vicious circle of deficit and debt.

Comments on the fiscal stance and fiscal sustainability
The question that now begs for an answer is: what is Namibia’s fiscal position? Is our fiscal policy sustainable? In answering these questions we need to look at two things, namely, the size of our deficit and debt and compare them with our set thresholds. As a result of the ongoing fiscal expansion, the following adjustments have been made to the fiscal rules (Fiscal Policy Frame Work, 2013/14-2015/16): (i) Public expenditure as a percentage of GDP revised from a ceiling of 30% to a ceiling of 40% (ii) budget deficit as a percentage of
GDP revised from a ceiling of 5% to a ceiling 7% (iii) debt as a percentage of GDP revised from a threshold of 25% -30% to a limit of now 35%. Currently, the 2013/14 outlook shows an expected public expenditure of about 35% of GDP, a budget deficit of about 6% of GDP and public debt of about 28%. All these numbers are below the set limits; however, the deficit GDP ratio is almost hitting the set limit which may not be a good sign especially when one thinks about the relationship between the deficit and debts. In that case it implies that the government may need to look at the avenues that can increase its current revenue so that when it increases its expenditure it may not necessarily need to borrow though for now we are looking at a sustainable debt. With the recently announced tax relief, the implications are that reduced tax revenue resulting from the tax relief may worsen the budget deficit. As such, government may opt for borrowing to finance the deficit, and may ultimately worsen the fiscal stance and put the debt sustainability at risk. Thus, while it might also not be the best option of them all, the government should attempt increasing its revenue – this can be both tax and non-tax revenue. There are three ways in which the government can increase its tax revenue; it can introduce a new tax i.e. exploiting a new tax base, it can increase the rate of an existing tax or it can enlarge its tax base. One way to increase the tax base may be to tax the “zero rated tax products”. Though this may be seen as something that may put heavy burdens on the poor and as such may increase poverty, it is well a known fact that this zero rated VAT incentives are more beneficial to the non-poor than the poor. Another alternative may be to increase excise tax (this is tax on products like alcohol and tobacco. While increasing excise tax may increase the tax incidence, proponents of such tax practice argue that increase of tax on price inelastic products such as alcohol and tobacco may not have significant negative effects on these products consumption, but may lead to significant changes in revenue collected. A common consensus among tax experts is that the best tax practice is the one where the tax revenue-to-GDP ratio is above 20%, the excise taxes are 3.5% of GDP or VAT of at least 35% of total tax.

---

1 Price inelastic products are those products which a change (increase or decrease) in theirs prices does not really affect their consumptions. One such an example is addictive products such as cigarettes.
Table 1: Tax and VAT revenues in percentages

<table>
<thead>
<tr>
<th>Year</th>
<th>Tax revenue as % of GDP</th>
<th>VAT as % of total tax revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999/00</td>
<td>29%</td>
<td>23%</td>
</tr>
<tr>
<td>2000/01</td>
<td>27%</td>
<td>24%</td>
</tr>
<tr>
<td>2001/02</td>
<td>25%</td>
<td>24%</td>
</tr>
<tr>
<td>2002/03</td>
<td>26%</td>
<td>22%</td>
</tr>
<tr>
<td>2003/04</td>
<td>23%</td>
<td>22%</td>
</tr>
<tr>
<td>2004/05</td>
<td>24%</td>
<td>20%</td>
</tr>
<tr>
<td>2005/06</td>
<td>25%</td>
<td>27%</td>
</tr>
<tr>
<td>2006/07</td>
<td>28%</td>
<td>20%</td>
</tr>
<tr>
<td>2007/08</td>
<td>29%</td>
<td>20%</td>
</tr>
<tr>
<td>2008/09</td>
<td>29%</td>
<td>19%</td>
</tr>
<tr>
<td>2009/10</td>
<td>29%</td>
<td>22%</td>
</tr>
<tr>
<td>2010/11</td>
<td>26%</td>
<td>24%</td>
</tr>
<tr>
<td>2011/12</td>
<td>29%</td>
<td>29%</td>
</tr>
<tr>
<td>2012/13</td>
<td>32%</td>
<td>20%</td>
</tr>
<tr>
<td>2013/14</td>
<td>32%</td>
<td>21%</td>
</tr>
<tr>
<td>2015/16</td>
<td>32%</td>
<td>22%</td>
</tr>
<tr>
<td>2016/17</td>
<td>31%</td>
<td>24%</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance fiscal data.

Table 1 above shows that Namibia has been doing relatively well in terms of tax revenue-to-GDP ratio. The ratio has been above 20% since independence and this is commendable. However, the VAT as a percentage of GDP has been a bit volatile year by year hovering around 23% on average. This shows that Namibia ranks far from the best tax practices in terms of VAT, hence in this case taxing the zero rated products for example may be one of the alternatives that the government can opt for not only to increase VAT revenue but also to raise much revenue in aggregate.

Table 2: Fiscal stance in the SACU region

<table>
<thead>
<tr>
<th>Countries</th>
<th>Debts (% of GDP)</th>
<th>Overall balance (% of GDP)</th>
<th>tax revenue (% of GDP)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>09/10</td>
<td>10/11</td>
<td>11/12</td>
</tr>
<tr>
<td>SA</td>
<td>33.0</td>
<td>36</td>
<td>39.6</td>
</tr>
<tr>
<td>Botswana</td>
<td>16.3</td>
<td>17.4</td>
<td>16.3</td>
</tr>
<tr>
<td>Lesotho</td>
<td>-</td>
<td>35.2</td>
<td>39.6</td>
</tr>
<tr>
<td>Swaziland</td>
<td>13.7</td>
<td>17.4</td>
<td>19.9</td>
</tr>
<tr>
<td>Namibia</td>
<td>15.6</td>
<td>16.1</td>
<td>26.5</td>
</tr>
</tbody>
</table>

Source: IMF article IV country report and own calculation.

Compared to other countries in the Southern African Customs Union (SACU), Namibia’s debt level is lower than that of South African and Lesotho (Table 2).
Although we are not scoring well in terms of deficit to GDP ratio, the tax revenue to GDP ratio shows that Namibia has the highest tax revenue in the SACU region. On average, Namibia's tax revenue to GDP ratio is about 29.0%, while other SACU members have a ratio of about 23% on average. From the statistics in Table 2 above, the initial conclusion that can be drawn is that Namibia has higher expenditure compared to other countries, thus higher deficits. Also, it may be that other countries have higher non-tax revenues than Namibia, hence their lower overall balance.

**Conclusion, recommendations and policy implications**

The above discussions and statistics tell us that Namibia's fiscal policy has been expansionary for the past few years and the fiscal stance is found to be sustainable, at least for now and the near future. The estimates for the next five years show a good fiscal stance for the country. While this is true, the observed relationship between deficits and debts tells us that a continuous fiscal deficit fuels the debt level which if debts stock continue to be high, it may go beyond the set limits and hence unsustainability of public debts. The deficit which is now very close to the set limit calls for alternative ways of raising more funds in terms of revenue or perhaps spending efficiently. One example that Namibia can probably copy from is Botswana whose expenditure policy is linked to the National Development Plan priorities. Implying that government budget allocation is highly allocated to the NDP(s) priority areas and as such the government may spend *efficiently* – the so called productive spending. This policy has served Botswana well, and might as well serve us well if used in Namibia. Using this expenditure policy, Botswana managed to reduce its primary deficit from 11.6% of GDP in 2009/10 to 1.4% in 2012/13 and estimates are showing that the surplus is likely to be maintained for the next few years, reaching a surplus of about 2.4% in 2016/17. In addition to controlling its expenditure, the government of Namibia may attempt to enlarge its tax base or increase existing tax rates (taxes on alcohol and tobacco as stated earlier) to raise additional revenue in order to impact the deficit. Public sector deficit has long term macroeconomic impacts depending on how the deficit is financed. It is commonly known that deficit is financed through exhausting the net assets/equity that was accumulated in the boom years or by increasing debts (i.e. borrowing). The latter lead to crowding out of private sector investment and this is a contradiction of the initial intention of the government, which was to support the economy. Namibia borrows more domestically than it borrows externally, which is not a bad idea, however, higher debts means higher interest payments, and higher
interest payments reduces the potential for government spending. Another feature of debts is “intergenerational transfer” which means that if current spending is financed by debts, then there is a transfer of the economic burden to the next generation as they will be the ones to pay back the money borrowed. Of course, this is only true if the money borrowed is used for current spending and not on investment in things such as infrastructure which the future generation may use to their advantage. Basically, the message we are getting from the macroeconomic impact of deficits and debts is that, it is best to borrow for investment (i.e. borrow for capital spending) and not operational spending. Also, domestic borrowing if not well controlled, may lead to crowding out of private sector which is not an ideal situation to our economy, Namibia. While it may not be the best option, this brief recommends that our government look at avenues to increase revenue as a strategy to curb higher deficit which is likely to have negative effects to the economy. In fact the endogenous growth theory postulates that revenue collected from VAT are non-distortionary, hence if we are proponents of endogenous theory, we (Namibia) can increase VAT as an alternative to raise additional revenue.

Summary conclusions on budget allocation
Our budget is based on inconsistent macroeconomic assumptions and budget classifications. There seems to be no clear distinction of the sectors which our budget is aimed for, more specially our development budget. As such, our sector allocations are not in line with our priority areas. In short, one would say that our priorities as they appear in the NDPs are mostly not budgeted for. As already mentioned above, we need to review our budget allocation strategies because currently they appear to be just an incremental exercise based on past budget allocations.

Summary recommendation
The number one recommendation is that expenditures be aligned to the NDPs. And secondly, Namibia must look for avenues to increase revenue and spend productively (i.e. a redirection in expenditure is recommended).

Written by Evelina Niishinda (enishinda@npc.gov.na). Directed and supervised by: Manongwa Sikanda (msikanda@npc.gov.na)
References

International Monetary Fund. (2013). “Namibia 2012 Article IV Consultation.” 
IMF Country Report No 13/43

IMF Country Report No 12/234


____________________

i The reported statistics are limited to the availability of data

ii Note that the execution rates referred to here are the capital expenditure execution rate.

iii 2012/2013 - 2015/16 are estimates.

iv Note that the reported statistics are limited to the availability of data.

v The reported statistics are limited to the availability of data.

vi Using this expenditure policy, Botswana managed to run a fiscal surplus.

vii See for example Rademacher (2011)