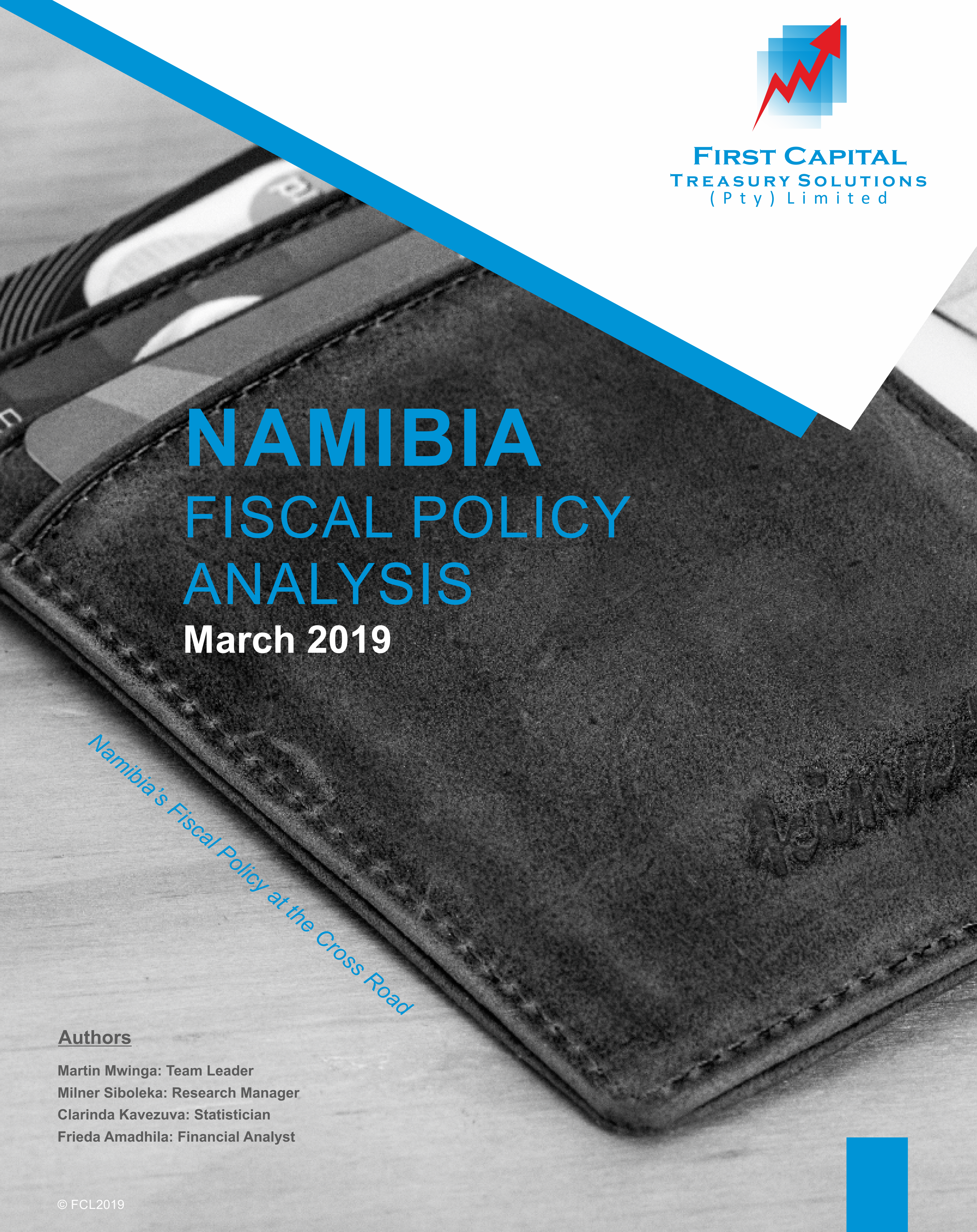

First Capital Treasury Solutions (Pty) Limited

NAMIBIA
FISCAL POLICY ANALYSIS
March 2019

Namibia's Fiscal Policy at the Cross Road

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Namibia’s Fiscal Policy Analysis
March 2019

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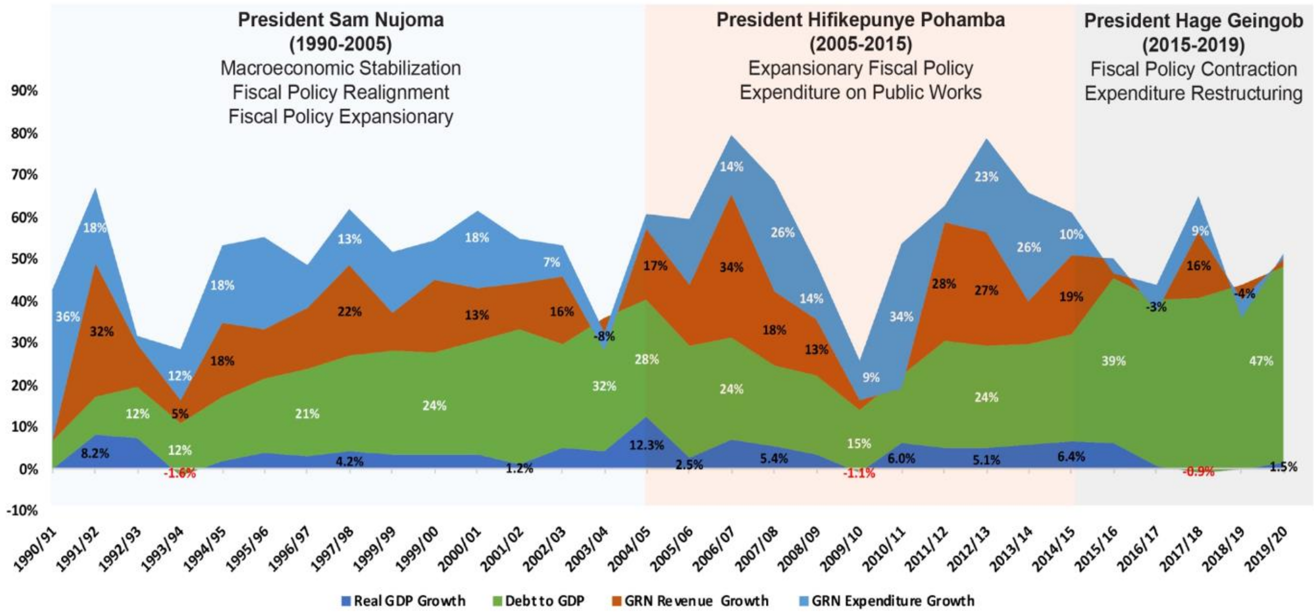
ACRONYMS

FC	: First Capital
GDP	: Gross Domestic Product
GRN	: Government of the Republic of Namibia
HPP	: Harambee Prosperity Plan
IMF	: International Monetary Fund
MoE	: Ministry of Education
MoF	: Ministry of Finance
MoHSS	: Ministry of Health and Social Services
MTEF	: Medium Term Expenditure Framework
NBC	: Namibia Broadcasting Corporation
NSA	: Namibia Statistics Agency
NUST	: Namibia University of Science and Technology
N$	: Namibian Dollar
SACU	: Southern Africa Customs Union
SADC	: Southern African Development Communities
SOEs	: State Owned Enterprises
STD	: Standard Deviation
TN	: Telecom Namibia
TB	: Treasury Bills
UNAM	: University of Namibia
USD	: United States Dollar
ZAR	: South African Rand

Table 1: Fiscal Policy Benchmark Targets and Outcomes

Fiscal Policy Benchmark Targets and Outcomes							
Indicator	**Benchmark %**	**2014/15**	**2015/16**	**2016/17**	**2017/18**	**2018/19**	**2019/20**
Total debt / GDP	**35%**	25%	39%	40%	42%	44%	47%
Domestic debt / GDP	**25%**	17%	21%	25%	27%	29%	31%
Foreign debt / GDP	**10%**	9%	18%	15%	15%	15%	16%
Foreign debt (excl. Rand) / GDP	**7%**	7%	15%	13%	12%	10%	9%
Total debt Service / Revenue	**10%**	5%	7%	9%	9%	12%	12%
Total debt Service / GDP	**3%**	2%	3%	3%	3%	4%	3%
Domestic debt / Total debt	**80%**	66%	54%	60%	65%	65%	66%
External debt / Total debt	**20%**	34%	46%	40%	35%	35%	34%
External debt (excl. Rand) / Total debt	**20%**	30%	42%	37%	35%	34%	33%
Debt falling due within 12 months	**30%**	29%	22%	21%	21%	22%	30%
TB as % of domestic debt	**40%**	43%	39%	36%	37%	36%	35%
Bonds as % of domestic debt	**60%**	57%	61%	64%	63%	64%	65%
Total Guarantees / GDP	**10%**	4%	4%	4%	7%	8%	8%

Source: MoF, BoN & First Capital Calculations



1. INTRODUCTION

Fiscal policy is the most effective policy instrument that the Namibian government employed over the past 29 years to influence and balance the economy, using taxes and spending. At the time of independence in 1990, the Namibian economy grew above 7 percent both in 1991 and 1992 before it registered negative growth of 1.6 percent in 1993. The new government was inheriting a huge infrastructure backlog especially in the areas of education, health, housing, water and electricity supply, roads and telecommunication infrastructure. In addition, poverty, unemployment and income inequality was very high and rising. To address some of these challenges, the new government under the SWAPO party had to make hard choices and design policies and programmes that was to address some of the identified challenges. To understand and appreciate fiscal policy in Namibia, one has to understand the economic challenges facing Namibia at the time of independence as these challenges shaped all new policies. Given the state of the economy at the time, policy makers in government agreed that the design and configuration of fiscal policy should incorporate both the fiscal stabilization, economic growth and social spending objectives.

To analyse fiscal policy in Namibia, we break our period of analysis into three periods, namely, Fiscal Policy under President Sam Nujoma (1990 to 2005), Fiscal Policy under President Hifikepunye Pohamba (2005 to 2015) and Fiscal Policy under President Hage Geingob (2015 to 2019). Based on data analysis, it is fair to conclude that the core focus of fiscal policy in Namibia over the past 29 years by the three presidents has been to use government expenditure to achieve sustained and inclusive economic growth, reduce unemployment; poverty and reduce income inequality while maintaining macroeconomic stability. As things stand, Namibia's fiscal policy stand at a crossroad. The country is at a difficult juncture when it comes to fiscal policy and the difficult task facing government is to strike the right balance between macroeconomic stabilization through fiscal consolidation and stabilization, stimulating aggregate demand to achieve economic growth objective while ensuring fiscal sustainability in the long-term. Why we believe Namibia's fiscal policy is at a cross road is because of the following:

- Total Government debts accumulated over the past 29 years reaching critical levels at 50% of GDP.
- Inelastic, non-progressive and volatile government tax revenue and narrow tax base.
- Default risk is on the rise by local authorities, private sector, state owned enterprises (SOEs) and households and may need bailouts.
- The economy is fragile and weak while many people are calling for additional fiscal stimulus to grow the economy and alleviate poverty.
- National savings levels are very low to support government while chances of foreign borrowings are diminishing.

At this juncture in Namibia's history, tough and unpopular decisions & choices are required towards the nation's redemption. In this report we present facts about Namibia's fiscal position and whether we can learn something from the past as a nation and chart a better sustainable future.

2. FISCAL POLICY OUTCOMES UNDER DIFFERENT PRESIDENTS

2.1. Fiscal Policy under President Sam Nujoma (1990 to 2005)

Analysts concur that in the first ten years of independence (1990 and 2000), fiscal policy in Namibia focused largely on the goal of macroeconomic stabilization, fiscal consolidation and spending to achieve social objectives while under-emphasizing the economic growth objective of fiscal policy. The assumption by policy makers at the time was that macroeconomic stabilization will lead to higher savings and investments and this will translate into higher economic growth, more jobs created, and poverty & income inequality reduced. Under President Nujoma the objectives and focus of fiscal policy was mainly on the following:

1. Macroeconomic stabilization (bringing down interest rate, inflation, government deficit and debt, etc);
2. Infrastructure Spending (education, health, roads, housing infrastructure, telecommunications etc);
3. Social spending (to reduce poverty and income inequality);
4. Human Resource/skills development.

The stance of fiscal policy under President Nujoma could only be classified as expansionary especially in the first five years where government expenditure increased annually by 17 percent. Despite such huge fiscal policy expansion, both deficit and debt levels remained relatively low helped much by unprecedented increase in government revenue. Was fiscal policy effective under the presidency of Sam Nujoma? Table 2 below shows the outcome of the impact of fiscal policy and other complimentary policies such as monetary policy.

GDP growth increased from an average of 1.1 percent during the period 1981 to 1989 to an average growth of 4.1 percent under president Nujoma's time in office (1990 to 2005). Both inflation and interest rate came down significantly from 11 and 16 to 5 and 9 percent respectively from 1990 to 2005. Despite high growth in government expenditure, government deficit as a percent of GDP remained relatively low at an average of 3 percent of GDP over Nujoma's presidency. The low deficit to GDP was achieved on account of high government revenue (*see table 2 below*). As per *table 2* below, President Nujoma achieved both macroeconomic stability objective, reduced the infrastructure backlog significantly especially in education and health through additional schools, clinics and hospitals built. In addition, infrastructure such as rural electrification, expansion of road network & telecommunication countrywide were successfully achieved through the use of fiscal policy as a policy instrument. However, unemployment, poverty and income inequality still remained stubbornly high due to the unchanged structure of the economy and limited and appropriate complimentary policies.

Table 2: Fiscal Policy & Economic Outcomes under President Nujoma (1990 to 2005)

Fiscal Policy Outcome under President Nujoma (1990 to 2005)			
Economic Indicator	Average (1990 - 1995)	Average (1996 -2000)	Average (2001 - 2005)
Interest Rate	17.0%	15.75%	9.5%
Inflation	13.9%	8.2%	6.9%
GDP Growth	3.5%	3.6%	5.2%
Growth in Total GRN Revenue	16%	15%	10%
Growth in GRN Tax Revenue	26%	17%	11%
Growth in GRN Expenditure	17%	16%	10%
Budget balance as % of GDP	-2%	-3%	-4%
Debt to GDP	11%	22%	29%
Foreign Debt to total Debt	49%	82%	55%
Unemployment Rate	19%	34%	31%
Poverty Incidence	37.8%	33.0%	27.6%
Gini-Coefficient	0.70	0.70	0.60
Education expenditure per learner (Thousand N$)	1,745	2,899	4,348
Literacy rate	76%	76%	76%
Health expenditure per Capita (Hundred N$)	233	364	564
Infant mortality Rate	57%	38%	48%

Source: BoN, NSA, MoF & First Capital Calculations

2.2. Fiscal Policy under President Hifikepunye Pohamba (2006 to 2015)

President Nujoma handed over an economy with budget balance to GDP of -3 percent and debt to GDP of 28 percent at the end of his term (2005) and it is fair to conclude that the bulk of infrastructure backlog was achieved, and macroeconomic stability was also achieved as highlighted in *table 1* above. Fiscal stimulus in the last five years of Sam Nujoma's rule also provided economic growth momentum with President Pohamba inheriting an economy growing at a peak of 12.3 percent in 2004. Under President Pohamba, the fiscal balance moved into surplus in 2006/7 to 2008/9. These budgetary surpluses were due to the rapid rise in government revenue and the cumulative effect of expenditure containment between 2003/4 to 2005/6. With such high government revenue, fiscal policy stance moved into an expansionary mode in 2011 and it can be concluded that under President Pohamba (2005 to 2015), fiscal policy in Namibia was expansionary with the aim of spurring economic growth and providing major infrastructure especially housing and road network. Under President Pohamba the objectives and focus of fiscal policy was mainly on the following:

1. Economic Growth through expansionary Fiscal Policy;
2. Infrastructure Spending (Roads and housing infrastructure);
3. Employment Creation through public works.

Was fiscal policy effective under the presidency of Hifikepunye Pohamba? Table 3 below shows the outcome of the impact of fiscal policy and other complimentary policies such as monetary policy.

Under President Pohamba, higher average GDP growth of 5.6 percent compared to 4.1 during Nujoma's presidency was achieved through high government spending. However, during the same period, debt to GDP increased after reaching a low of 15 percent in 2009/10 to 24 percent at the end of his term in 2014/15.

Table 3: Fiscal Policy & Economic Outcomes under President Pohamba (2005 to 2015)

Fiscal Policy Outcome under President Pohamba (2005 to 2015)			
Economic Indicator	**S. Nujoma Average (1990– 2005)**	**Average (2006 – 2010)**	**Average (2011– 2015)**
Interest Rate	14.0%	8.5%	6.0%
Inflation	9.6%	7.0%	5.2%
GDP Growth	4.1%	3.6%	5.6%
Growth in GRN Revenue	14%	17%	16%
Growth in GRN Tax Revenue	18%	17%	17%
Growth in GRN Expenditure	14%	15%	19%
Budget balance as % of GDP	-3%	-2%	-4%
Debt to GDP	21%	21%	23%
Foreign Debt to total Debt	62%	23%	31%
Unemployment Rate	28%	28%	29%
Poverty Incidence	32.8%	19.5%	17.4%
Gini-Coefficient	0.67	0.60	0.60
Education expenditure per learner (Thousand N$)	2,998	6,384	14,039
Literacy rate	76%	76%	88%
Health expenditure per Capita (Hundred N$)	564	743	1,903
Infant mortality Rate	48%	46%	39%

Source: BoN, NSA, MoF & First Capital Calculations

2.3. Fiscal Policy under President Hage Geingob (2015 to 2019)

President Hage Geingob took over an economy that was heading towards a slowdown due to a combination of many factors most notably the decline in commodity prices which resulted in the mining sector contraction as well as the weather induced agricultural sector slowdown. Beyond 2015, holding the status quo of massive government expenditure could have caused a worst economic situation than the current one, hence the Hage administration had to normalize and contain government expenditure. Both fiscal policy and the country were at a crossroad and the president and his team had to make difficult economic and fiscal choices confronting the country over the medium term. President Geingob had to choose either populist policies that appeals to the masses or rationale and painful policies that arrest high government expenditures to ensure sustainability of fiscal policy in coming years.

Although President Hage Geingob announced at the time of his takeover in 2015 that he will undertake expansionary fiscal policy to implement the Harambee Prosperity Plan (HPP) to help restructure the economy, achieve high economic growth, reduce unemployment and poverty, this position was reversed when the president realized that the economy was not generating enough revenue as expected. Unlike his predecessor who took over a booming economy and a government budget entering into a surplus, president Hage Geingob took over an economy with fiscal deficit at 6% while debt to GDP was at around 24%.

With such declining government revenue, fiscal policy stance moved from expansionary mode under the Pohamba era into a contraction and government expenditure re-prioritization. Under President Geingob the objectives and focus of fiscal policy was mainly on the following:

1. Fiscal Consolidation through contractionary Fiscal Policy;
2. Limited Targeted Infrastructure Spending (Roads and housing infrastructure);
3. Social Spending (education, health and social welfare cash transfers).

Was fiscal policy effective under the presidency of Hage Geingob? Although only a four-year period is used in this analysis, Table 3 below shows the outcome of the impact of fiscal policy under president Hage Geingob.

Both deficit to GDP and debt to GDP rose significantly under president Geingob with debt to GDP reaching 43 percent in 2018. It can be seen from table 4, that both government expenditure and government revenue declined significantly and the only way to ensure the government continue to provide service delivery to the population was to borrow. In addition, the economy contracted and entering a recession between 2017 and 2018. With the economy projected to recover over the coming years, a positive fiscal outlook is projected with both deficit and debt to GDP projected to decline to below targeted levels.

Table 4: Fiscal Policy & Economic Outcome under President Geingob (2015 to 2019)

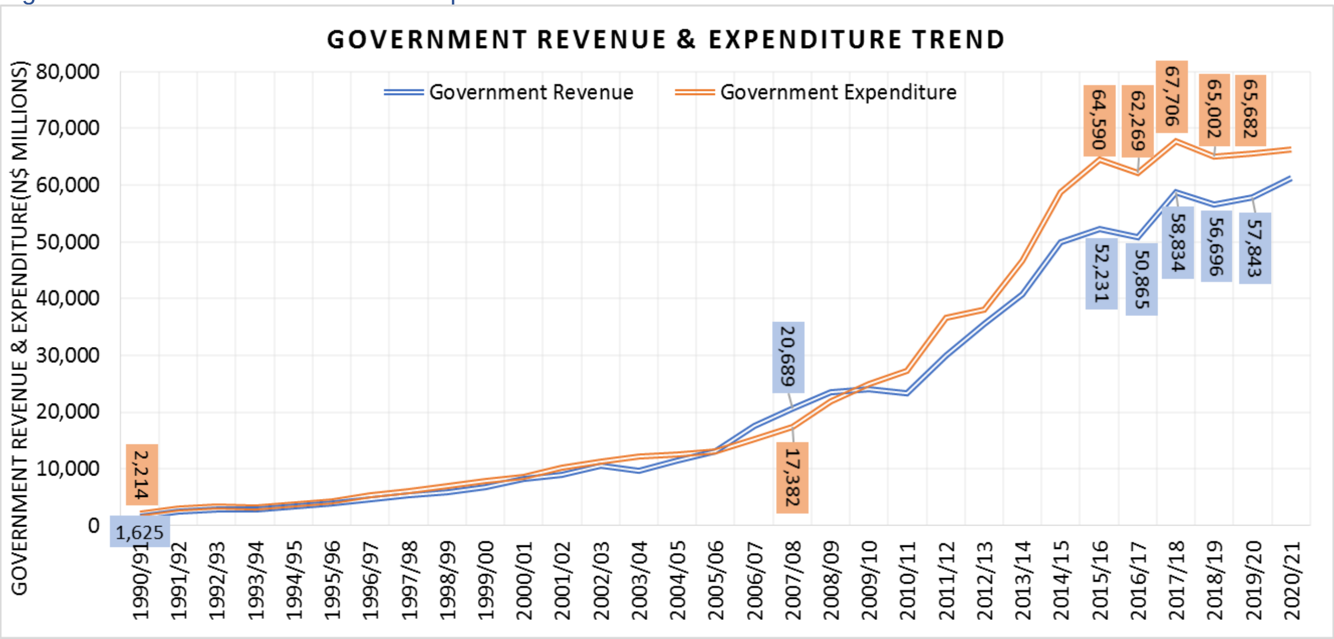
Fiscal Policy Outcome under President Geingob (2015 to 2019)			
Economic Indicator	**H.Pohamba Average (2005- 2015)**	**Average (2016 -2018)**	**Forecast (2019 –2023)**
Interest Rate	7.25%	6.75%	7.25%
Inflation	6.1%	5.7%	7%
GDP Growth	5.6%	1.4%	3%
Growth in Total GRN Revenue	16%	5%	7%
Growth in GRN Tax Revenue	17%	5%	7%
Growth in GRN Expenditure	17%	4%	6%
Budget balance as % of GDP	-3%	-7%	-9%
Debt to GDP	22%	42%	50%
Foreign Debt to total Debt	27%	40%	20%
Unemployment Rate	28%	34%	38%
Poverty Incidence	18.5%	17.0%	16.0%
Gini-Coefficient	0.60	0.56	0.52
Education expenditure per learner (Thousand N$)	10,211	18,317	18,588
Literacy rate	82%	89%	92%
Health expenditure per Capita (Hundred N$)	1,323	2,905	2,581
Infant mortality Rate	43%	45%	44%

Source: BoN, NSA, MoF & First Capital Calculations

3. REVENUE AND EXPENDITURE OVERVIEW

Namibia stands out in Africa and many parts of the world as a small open economy that does not depend on foreign donors to finance government budget. Since independence, the Namibian economy has generated and provided the necessary revenue required to support government expenditure. *Figure 1* below shows that there has been a strong positive correlation between government revenue and government expenditure. The high revenue generated by government ensured that Namibia's debt to GDP remain relatively low when compared with other countries. Government revenue and expenditure has increased from N$1.6 and N$2.2 billion respectively in 1990/91 to N$56.7 and N$65.0 billion respectively in 2018/19. The first ever government revenue decline was recorded in 2003/4 on the back of a major decline in mining tax revenue (*see figure 1*), which created the largest ever budget deficit recorded over the past 29 years. The 2003/4 revenue decline of 8 percent was short-lived as revenue increased by 17 percent a year after, a trend which lasted until 2008/9 when the economy contracted. Despite that revenue picked a year after the 2003/4 contraction, expenditure was contained for three consecutive years between 2004/5-2006/7. The cumulative effect of expenditure consolidation amid rising revenue created the first ever budget surpluses between 2006/7-2008/9. The surpluses recorded over the three years encouraged government to implement expansionary fiscal policy (increased expenditure). Based on the above analysis, it can be concluded that Namibia's fiscal policy is pro cyclical in nature meaning we spend more in good times and only contain our high spending appetite for a limited time when revenue performance slows. *Figure 4* shows that Namibia moved into a contraction phase of fiscal policy in response to slow growth in revenue since 2016/17. If this contraction in government expenditure continues for the next 3 years, it will help reduce both deficit and debt below target levels set by the government.

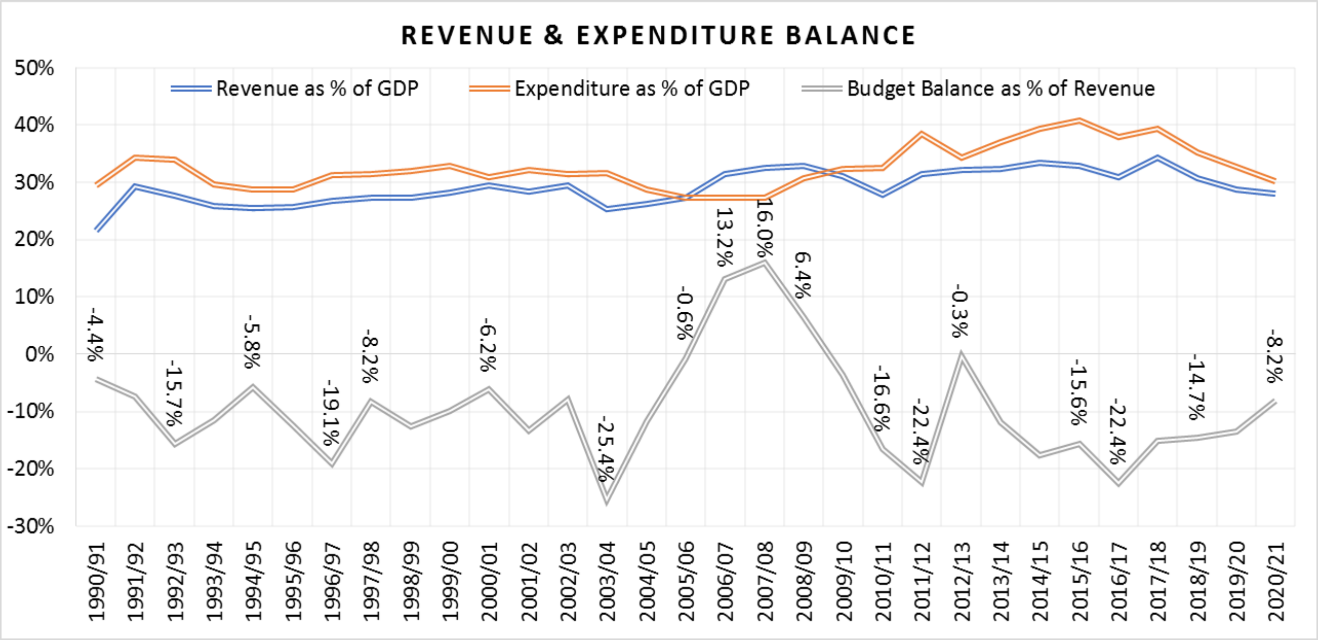
Figure 1: Government revenue and expenditure trend



Source: MoF

The proportion and share of both government revenue and expenditure to GDP remain stable and less volatile as is the case in many developing economies. According to figure 5 below, the size of government in the economy as measured by share of expenditure in GDP averaged 32.7 percentage over the past 29 years while revenue as percent of GDP averaged 29.1 percentage over the same period. In the extreme case, government expenditure of GDP as percentage was as high as 41 percentage. This demonstrates the fact that Namibia could be considered to be a welfare nation with high public spending, especially on education, health and transfer grants. With such high level of spending supported by high share of revenue to GDP, Namibia has managed to maintain a high level of welfare to counteract the negative effects of high unemployment and poverty.

Figure 2: Revenue, Expenditure and Budget Balance



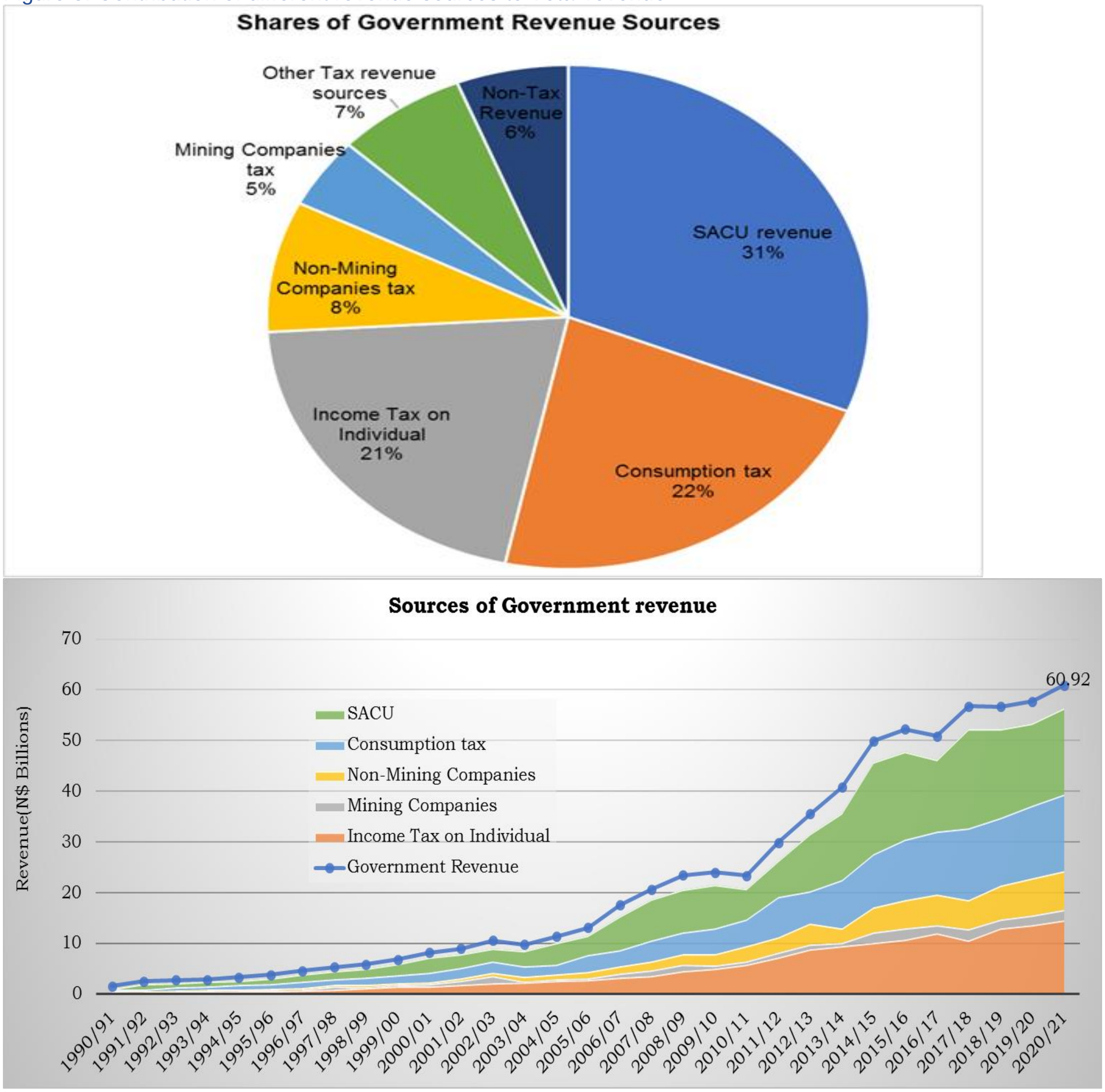
Source: MoF

4. REVENUE ANALYSIS

4.1. Sources of Government Revenue

Government revenues in Namibia are generated largely from direct taxes, taxes on international trade (SACU) and indirect taxes. The sources of these taxes are therefore linked to growth of income and expenditure growth in the economy. With the increased economic activities and rising economic growth since 1990, Namibia has experienced steady revenue growth coming from diversified sources with tax revenue accounting for 94 percent of total revenue (*see table figure 3 below*). Over the past 29 years, SACU revenue has contributed on average 31 percent to total government revenue, while taxes on the consumption of goods and services accounted for 22 percent followed by taxes on individual incomes accounting for 20 percent. Corporate tax constituted 13 percent while 6 percent was derived from Non-tax revenue sources

Figure 3: Contribution of different revenue sources to Total revenue

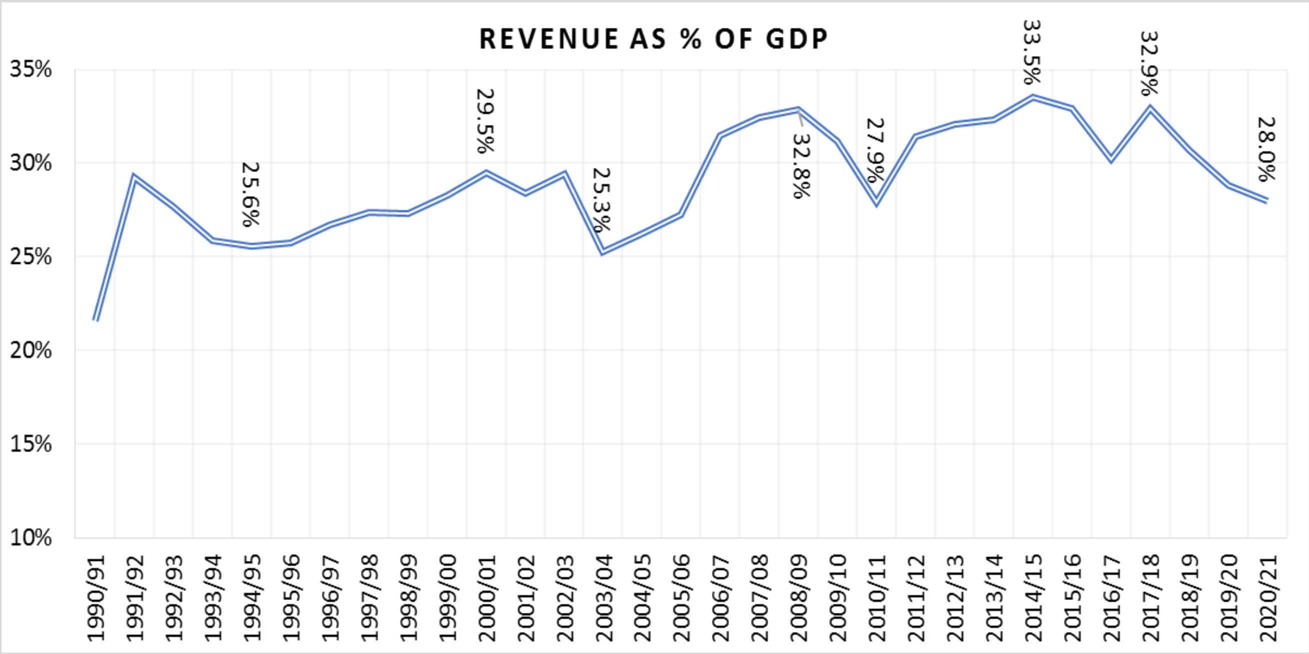


Source: MoF

4.2. Revenue performance over time

Government revenue at the time of independence in 1990 was about 22 percent of GDP. It rapidly increased throughout the 1990s and 2000s, reaching about 30% percent of GDP by 2010, rising further to 33% percent of GDP in 2018 (see figure 4 below). Since independence, government revenue to GDP averaged 30 percent. The ratio of revenue to GDP has been increasing gradually, an indication associated with improvement in the efficiency of revenue collections especially in instances where no major tax reforms were adopted. Revenue to GDP ratio declined from 33 percent in 2017/18 to 31 percent in 2018/19. This trend is expected to continue in 2019/20 with revenue to GDP dropping further to 29 percent. The recent declining revenue to GDP ratio is suggesting that our rate of collection falls below the average trend when the economy slows down.

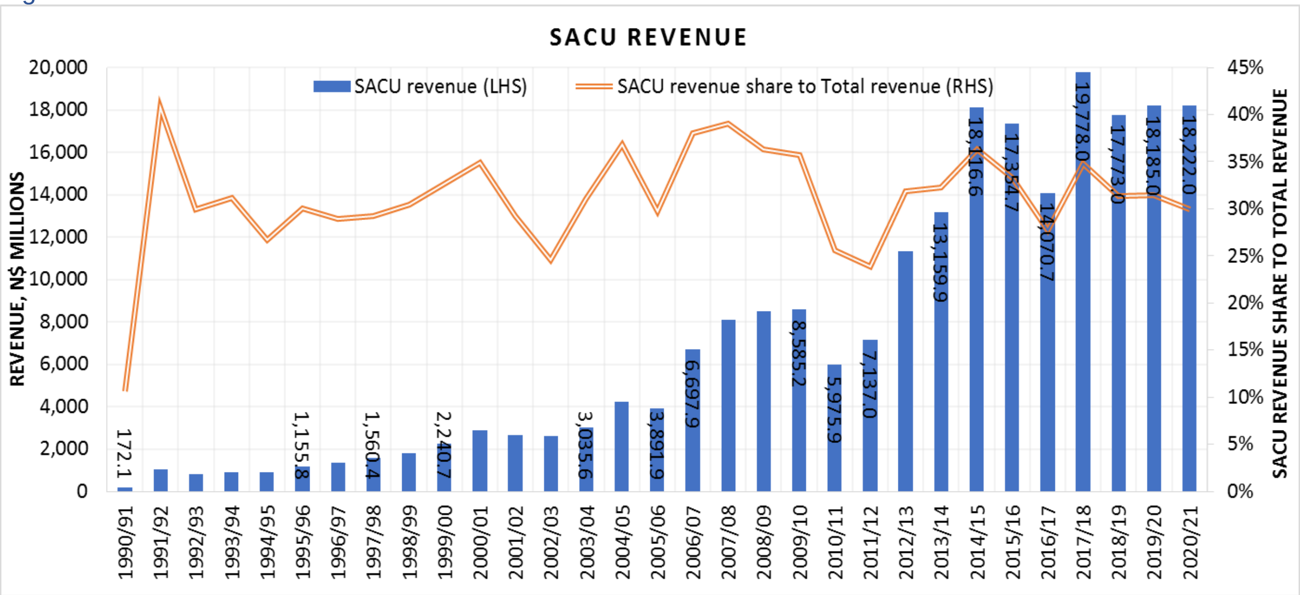
Figure 4: Revenue as % of GDP



Source: MoF

SACU revenue remains a significant contributor to the total government revenue. On average over the past 29 years it has contributed 31 percent to total revenue (see figure 5). Given its significant contribution to government revenue, instability in SACU revenue places the government's revenue in an unstable position. Most notably, in 2014/15 SACU revenue increased by 38 percent translating into an increase of 22 percent in government revenue. In addition, between 2017/18 to 2018/19 SACU revenue declined by 5 percent while government revenue declined slightly by 0.2 percent. SACU revenue are projected to decline by 2 percent in 2019/20(Y/Y) while total revenue would rise by 2 percent.

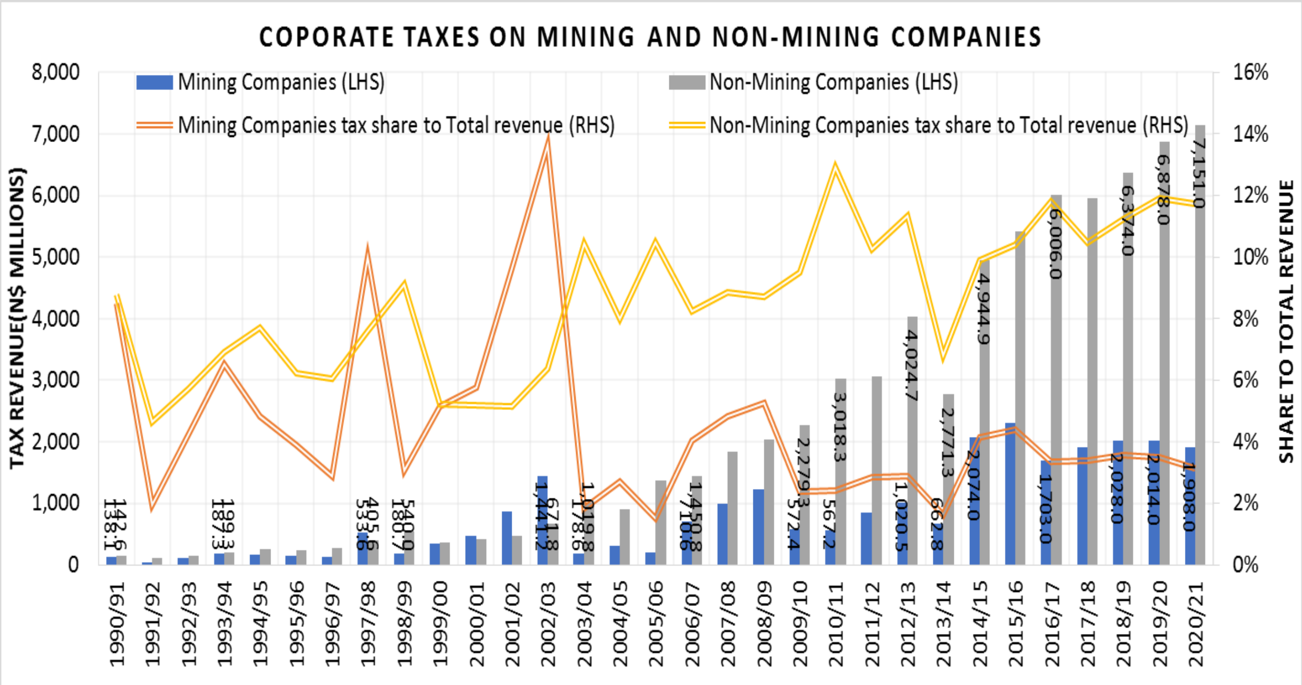
Figure 5: SACU Revenue



Source: MoF

Corporate taxes which are levied on company revenues forms another important component of government revenue. Consistently over time, there has been a rising trend of the contribution to total revenue from non-mining companies' corporate taxes while mining companies tax contribution to total revenue has been highly volatile over the past 29 years (see figure 6 below).

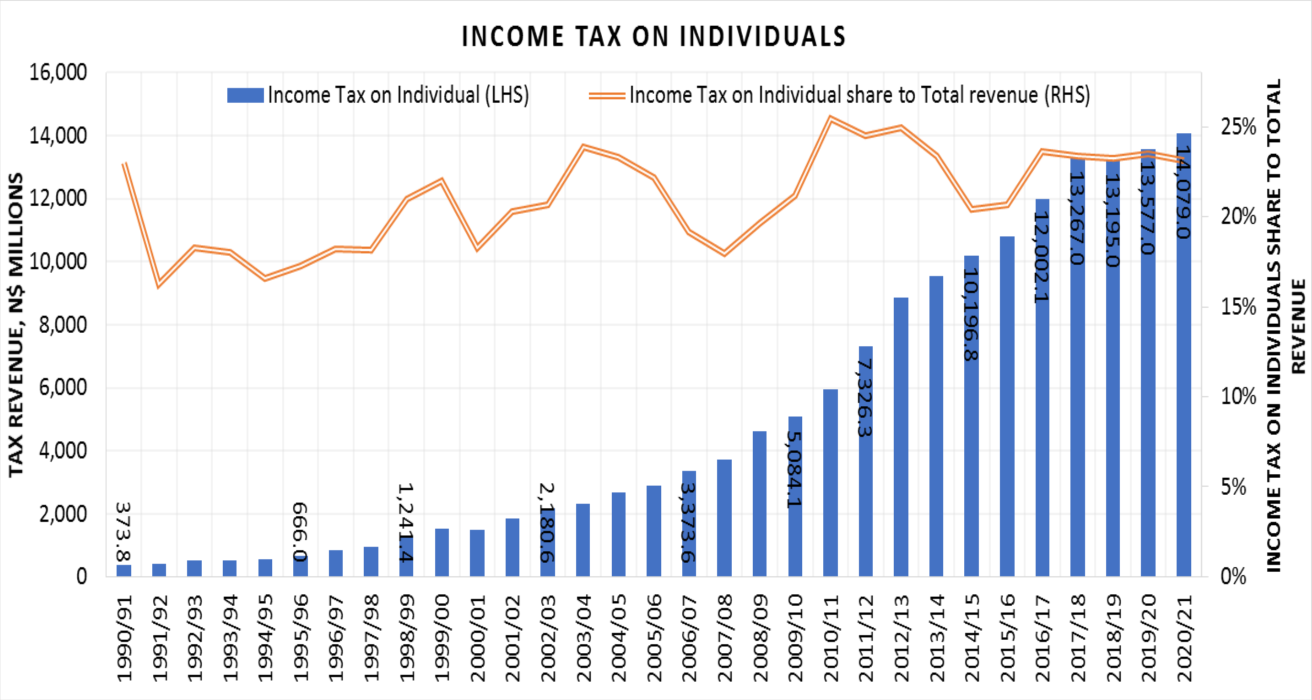
Figure 6: Corporate Taxes on Mining and Non-mining companies



Source: MoF

According to Figure 7 below, income tax revenue on individuals has been rising in line with increase in number of people employed and rising individual income levels. In 1990 only N$373 million was generated from income tax on individuals and this has increased to more than N$12 billion by 2018. Income tax revenue on individuals' contribution to revenue since 1990 averaged 21 percent up to date. The percentage of income tax contribution was 24 percent in 1990/91 and was at a peak in 2010/11 at 26 percent.

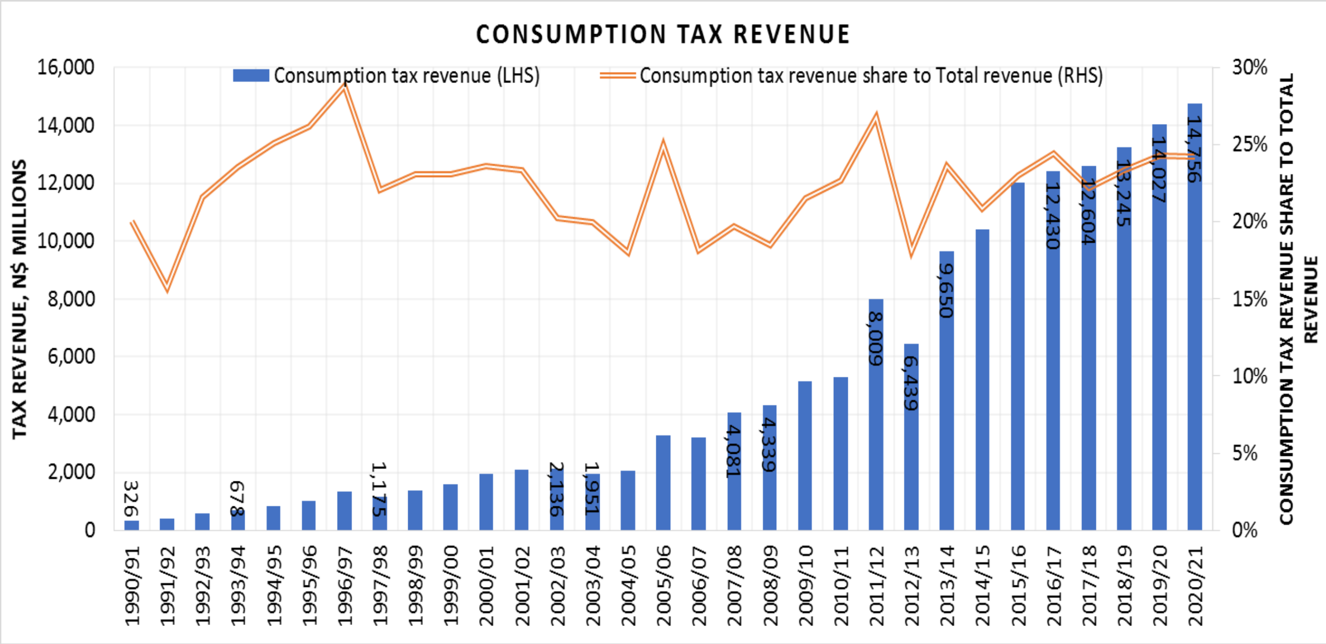
Figure 7: Income Tax on Individuals



Source: MoF

With rising expenditure and income in the economy, consumption has risen significantly and its contribution to total revenue since 1990 averaged at 22 percent. Consumption tax revenue was 20 percent in 1990/91 rising to 28 percent by 1996/7 (see figure 8 below). Consumption tax revenue currently stands at 24 percent and it is projected to reach 25 percent of total revenue by 2019/20.

Figure 8: Consumption Tax Revenue



Source: MoF

4.3. Revenue volatility

Rising volatility in Namibia's tax collections has made it difficult for the government to accurately forecast revenues. Namibia being a natural resource-dependent economy means that swings in commodity prices over the past 29 years have contributed to greater tax revenue volatility. Table 5 below shows the standard deviation (a measure of volatility) for each component of government revenue with SACU revenue being the most volatile revenue component followed by consumption tax revenue. Individual income tax revenue and non-mining tax revenue are the most stable revenue components. Tax revenue fluctuations often creates unpredictability that can confound policy makers' efforts to balance budgets. Over the past three years from 2016 to 2018, Namibia faced the greatest tax revenue volatility due to poor economic growth and this eventually led to fast rising deficit and debt to finance the revenue gap.

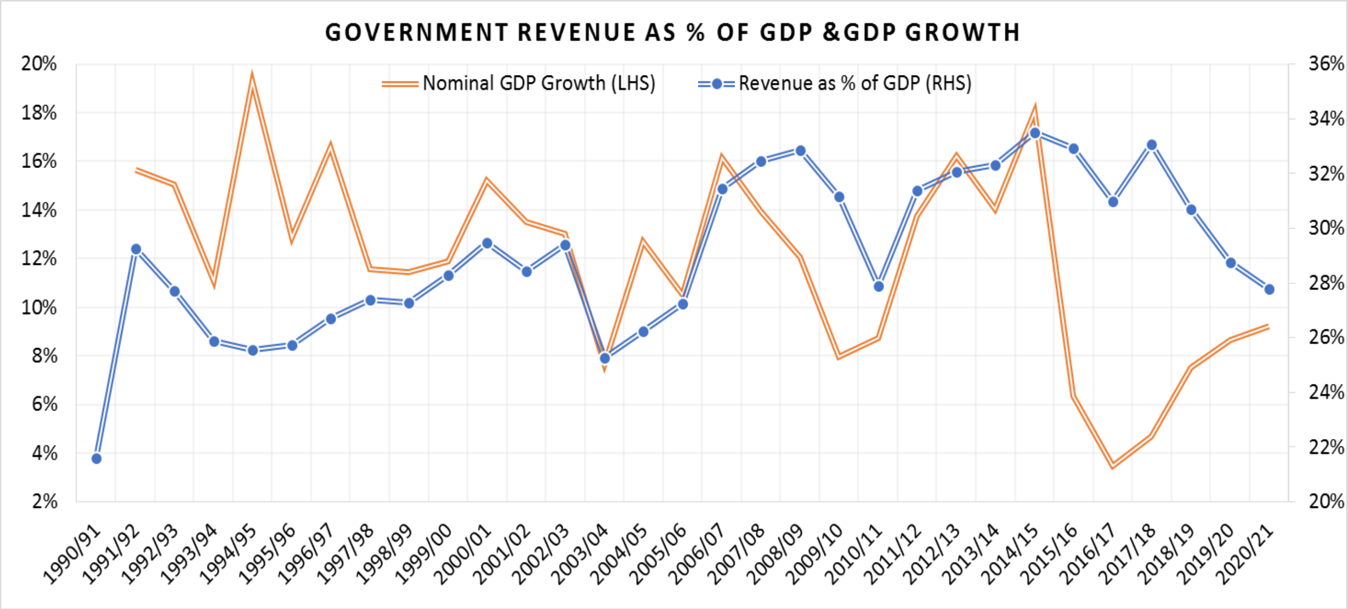
Table 5: Revenue volatilities

STD of revenue source share to Total Government Revenue	
SACU revenue	0.058
Consumption tax	0.030
Mining Companies tax	0.028
Income Tax on Individual	0.026
Non-Mining Companies tax	0.023

Source: MoF, First Capital Calculations

Figure 9 below shows the relationship between government revenue and GDP. Total revenue tends to grow as the country's GDP grows. Conversely, when there is an economic downturn, revenues usually decrease. Fluctuations in GDP growth will automatically be reflected in fluctuations in government revenue. In comparison to the GDP growth, there is an observed co-movement between government revenue to GDP ratio and GDP growth. In a usual case the ratio of revenue to GDP should remain constant as revenue changes should change with the level of economic activity. As seen in figure 9 below the ratio of revenue to GDP increases with the increase of the GDP growth and falls when GDP growth falls. This trend is more telling for policy making. The trend suggests that the marginal revenue increases with the increase in the GDP growth meaning that the proportional revenue collection increases when the economy is growing faster.

Figure 9: Government revenue as % of GDP & GDP growth



Source: MoF & NSA

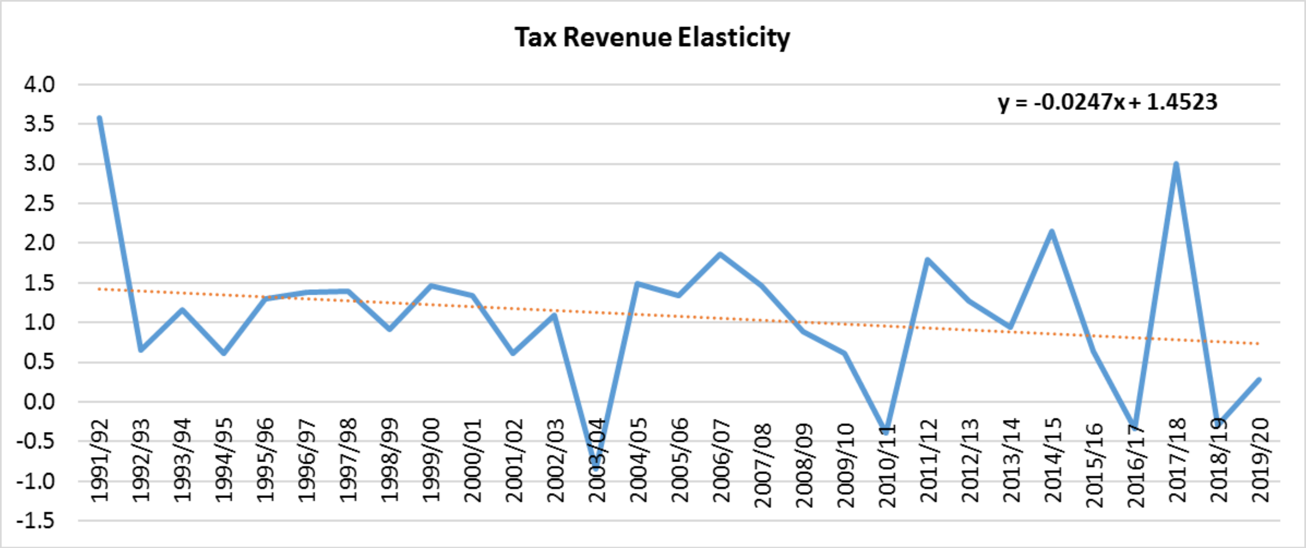
4.4. Tax Revenue elasticity of Growth

In this section we look at the responsiveness (elasticity) of income tax revenue to changes in income (GDP) and how this is related to the structure of the tax system and the distribution of income. The lower the responsiveness of revenue to a change in income or GDP, the less volatile the tax revenue from this source becomes, but this also implies lower progressivity of the income tax system.

Over the last three decades since 1990, Namibia's tax revenue has been subject to significant fluctuations. As tax revenue is the largest source of revenue for government, accounting for over 90 per cent of the total revenue, fluctuations in this source of revenue have a significant bearing on the total government revenue. Using readily available administrative data and parameters from the government budgets income tax revenue elasticities are calculated for the period 1990–2019.

The tax revenue elasticity coefficient for Namibia of 1.08 was calculated. This elasticity ratio implies that when the GDP increase by 1 percent, tax revenue increases by 1.08 and vice-versa when GDP falls by a percentage. The revenue elasticity ratio of 1.08 appears to be very low compared to other countries where the ratio tends to be above 1.5 to 2.0. This lower ratio suggest that Namibia's tax revenue is less responsive to a change in income or GDP and implies lower progressivity of the income tax system. Figure 10 below shows the trend in Namibia's tax revenue elasticities since 1990.

Figure 10: Tax Revenue Elasticity



Source: MoF, NSA & First Capital Calculations

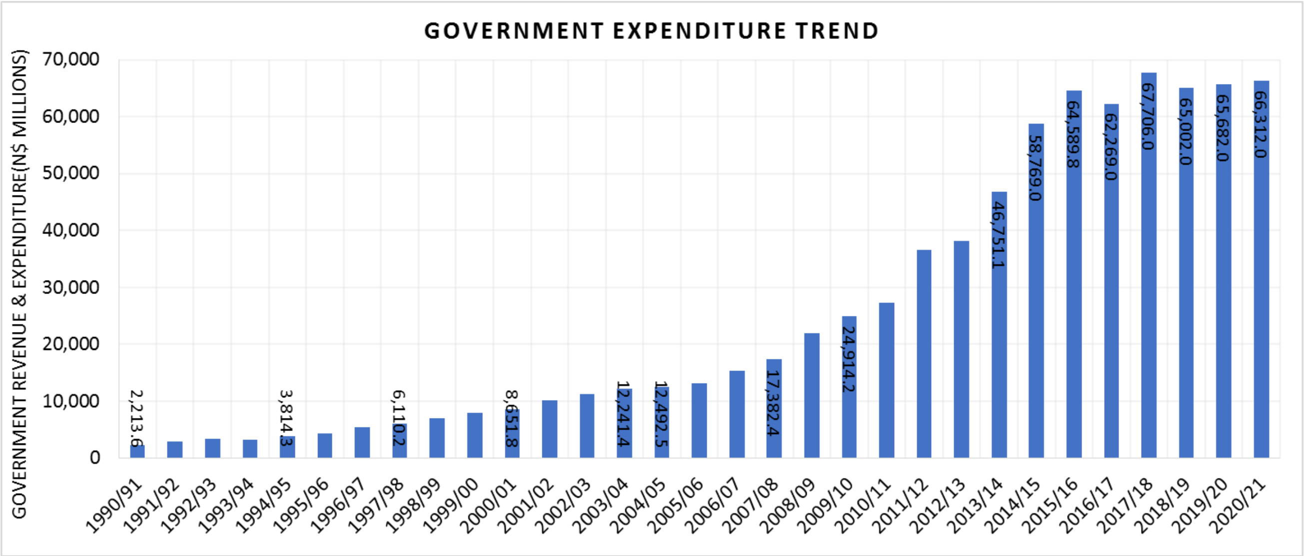
5. EXPENDITURE ANALYSIS

In Namibia, government spending is classified as current expenditure and capital expenditure. Current expenditure comprises of compensation to employees, purchases of goods and services, current transfers and subsidies and debt servicing. Capital expenditure on the contrary is composed of acquisition of non-financial assets and capital transfers to government entities. There has been a far-reaching increase in all public expenditure components between 1990 and 2018. This was as a result of increase in current/operational expenditures, especially in wages of civil servants, expenditure on subsidies, grants and transfers. On average, government spending stands at 38.4 percent of GDP in 2017/2018 compared to 29.4 percent in 1990/91.

5.1. Total Government expenditure Trend

Government expenditure has increased significantly from N$2.2 billion in 1990/91 to N$65 billion in 2018/19 representing an average annual increase of 12 percent *(See figure 11 below)*. This is in line with the nominal GDP growth which also averages at 12 percent per annum during the similar period. After growing by 36 percent in 1991/92, government expenditure maintained an average growth 11 percent between 1992/93 and 2005/6. From 2006/07 to 2015/16, government expenditure growth averaged 18 percent while it remained flat from 2016/17 to 2018/19. Since 2016/17, government expenditure has stabilized with two years recording first ever declines in expenditures of 4 percent and 8 percent for 2016/17 and 2018/19. The same trend to contain expenditure is projected over the MTEF period of 2018/19-2020/21. Should this trend be sustained, significant fiscal policy outcome benefits will start showing in 5 years' time with a budget surplus and significant decline in debt and debt serving cost as much of the government debt matures over time.

Figure 11: Government Expenditure Trend

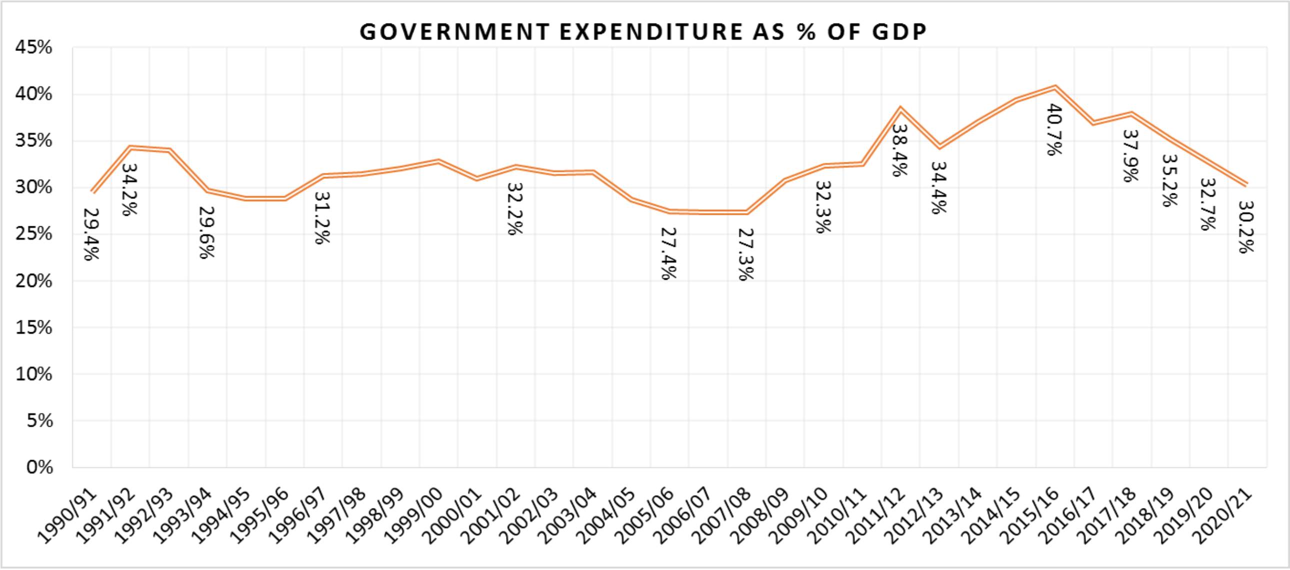


Source: MoF

5.2. Government expenditure as % of GDP

Government expenditure as a percentage of GDP increased from 29.4 percent in 1990/91 and reached a peak of 40.7 percent in 2015/16 *(refer to figure 12 below)*. This indicates that the government is significant player in the economy and changes in government expenditure will have a significant impact on the economy. For instance, the economic contraction experienced between 2016/17 to 2018/19, is mainly attributed to contraction in government expenditure that affected mainly the construction sector and the purchasing power of government.

Figure 12: Government Expenditure as percentage of GDP

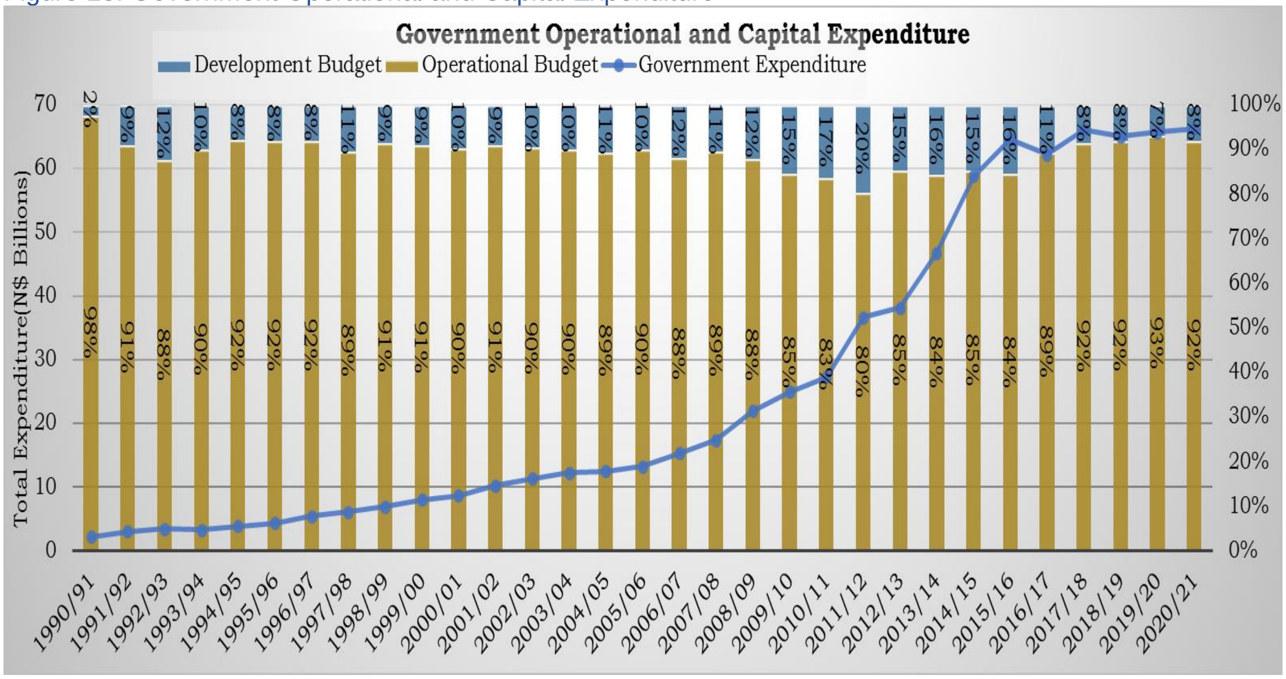


Source: MoF

5.3. Operational and Capital Expenditure allocations

Overall since 1990, government's capital expenditure allocations averaged 10 percent compared to 90 percent on operational expenses. The highest proportional allocation for capital expenditure was in 2011/12 when 20 percent of the budget was channeled to fund capital projects (*see figure 13 below*). High capital expenditure allocations in 2011/12 were as a result of the government's drive to solve the unemployment challenge through massive infrastructure spending under the TIPEG. During the same period, the government also committed resources to address the housing challenges through the Mass Housing Project. Since 2016/17 capital expenditure allocation has declined from 16 percent of total expenditure in 2015/16 to 11 and 8 percent in 2016/17 and 2017/18 respectively. The 2018/19 expenditure allocations also show that only 8 percent was allocated for capital expenditure, a trend to be maintained during the MTEF period ending 2020/21. The biggest contributors to operation expenditure allocations are the governments wage bill which takes 45 percent of total government expenditure as well as social sectors expenditure allocations which takes 48 percent of the total expenditure of government.

Figure 13: Government Operational and Capital Expenditure



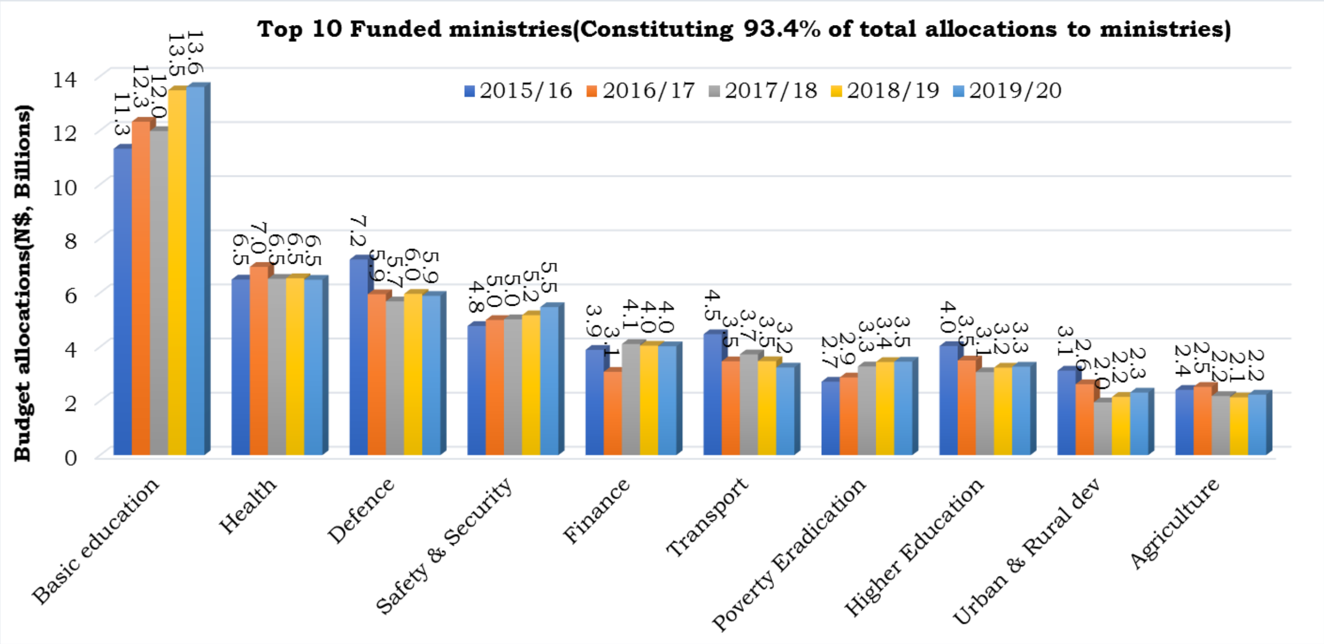
Source: MoF

5.4. Government expenditure by ministry

Basic Education expenditure still remains the priority by government. In 2018/19, Ministry of Basic education received the highest budget allocation of N$13.5 billion (21 percent of total government expenditure). At N$13.5 billion, the Ministry of Basic Education's allocation was increased by 13 percent compared to the expenditure allocation the previous year. The expenditure boost in education is meant to cover for the free primary and secondary education program. During the same year, the Ministry of Health & Social Services received the second allocation of

N$6.5 billion (Half of what the Ministry of Basic education receives). The Ministries of Defense and Safe & Security received the third and four highest ministerial budget allocations respectively. The combined allocations to these security service ministries accounts for 19 percent of the total budget allocations to ministries. The top ten funded ministries as shown in figure 14 below accounts for 93.4 percent of total expenditure allocations to ministries.

Figure 14: Top 10 Funded Ministries

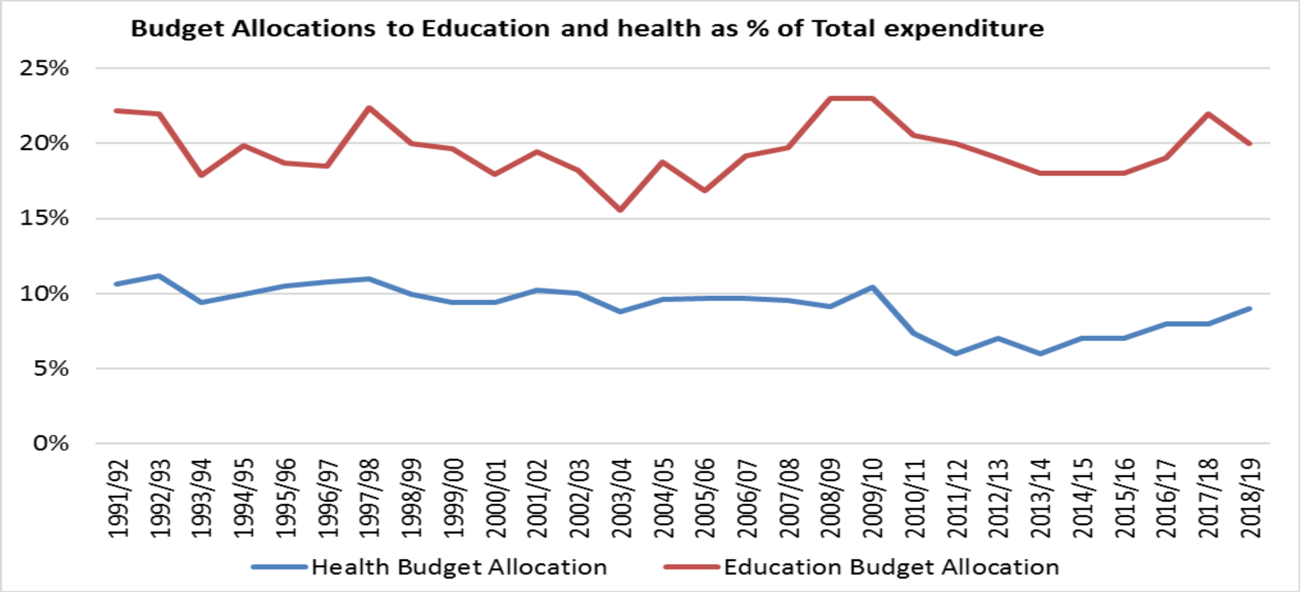


Source: MoF

5.5. Budget allocations to education and Health Ministries

Government expenditure to education and health ministries averaged 18 and 9 percent respectively over the past 29 years. Education and health sectors account for 29 percent of the national budget allocation. Most notably as a percentage of total expenditure, Health allocation has declined over time from 11 percent in 1991/92 to 6 percent in 2013/14 before marginally rising to 8 percent in 2018/19. Despite the pressure on public sector health services due to the rising population, the improvement in income levels of most individuals has eased this burden as some choose private health care services. However, the rising prevalence of diseases mostly chronic diseases requires that the government increases its expenditure allocation on health. From the graph below it becomes clear that the government's priority spending at the time of independence was education and health as their share out of the total government expenditure was highest compared to recent periods. Government expenditure on basic education received a share of 22 percent in 1990/91. At that time access to private education was limited and most households relied on public schools for their education hence government spending was high on education.

Figure 15: Budget Allocations to Education & Health as % of Total Expenditure

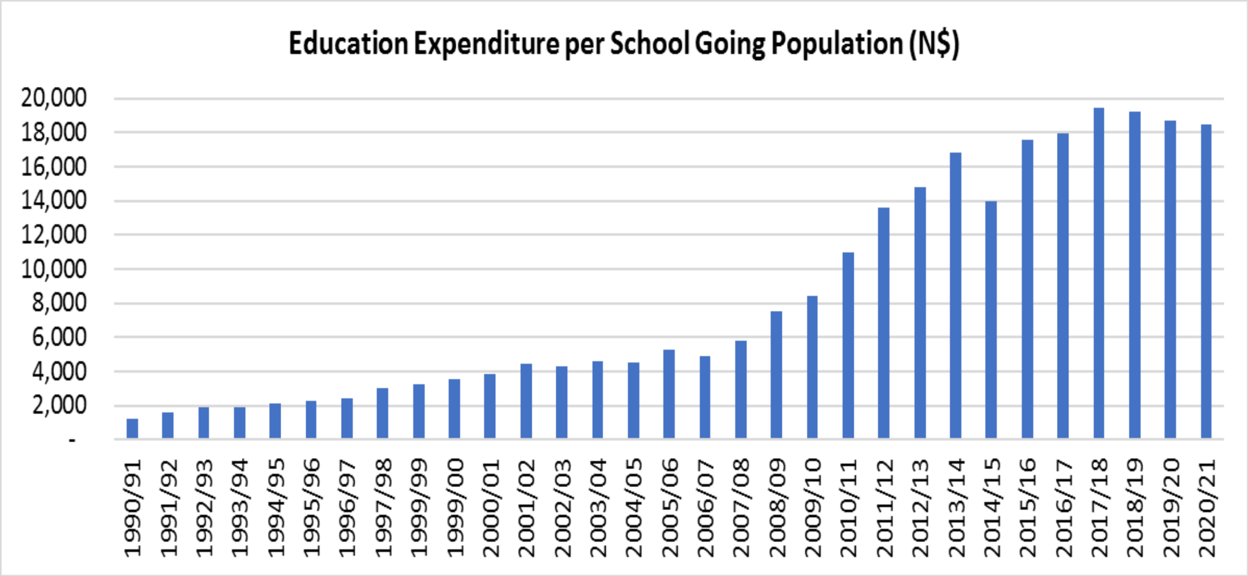


Source: MoF

5.6. Education budget allocation per student enrollment

Since 1990, the education budget per student enrolment has been gradually rising form N$ 1,231 in 1990/91 to N$ 19,236 projected in 2018/19 (*see figure 16*). This indicates that more money is allocated per learner now that before.

Figure 16: Education Expenditure per School Going Population

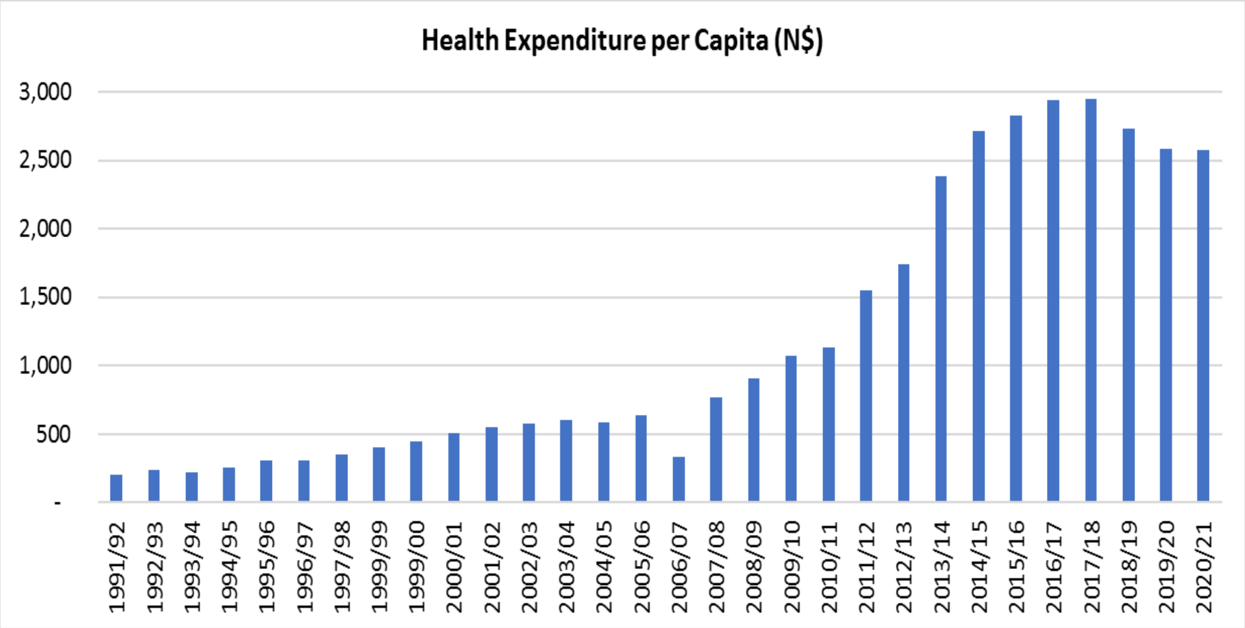


Source: MoF, NSA & First Capital Calculations

5.7. Health Budget Allocation per Capita

Health budget allocation per capita has been increasing over the years from N$ 208 per capita in 1991/92 to N$ 2,729 in 2018/19 *(see figure 16).* This implies that the budget allocation is increasing faster than population growth.

Figure 17: Health Expenditure per Capita

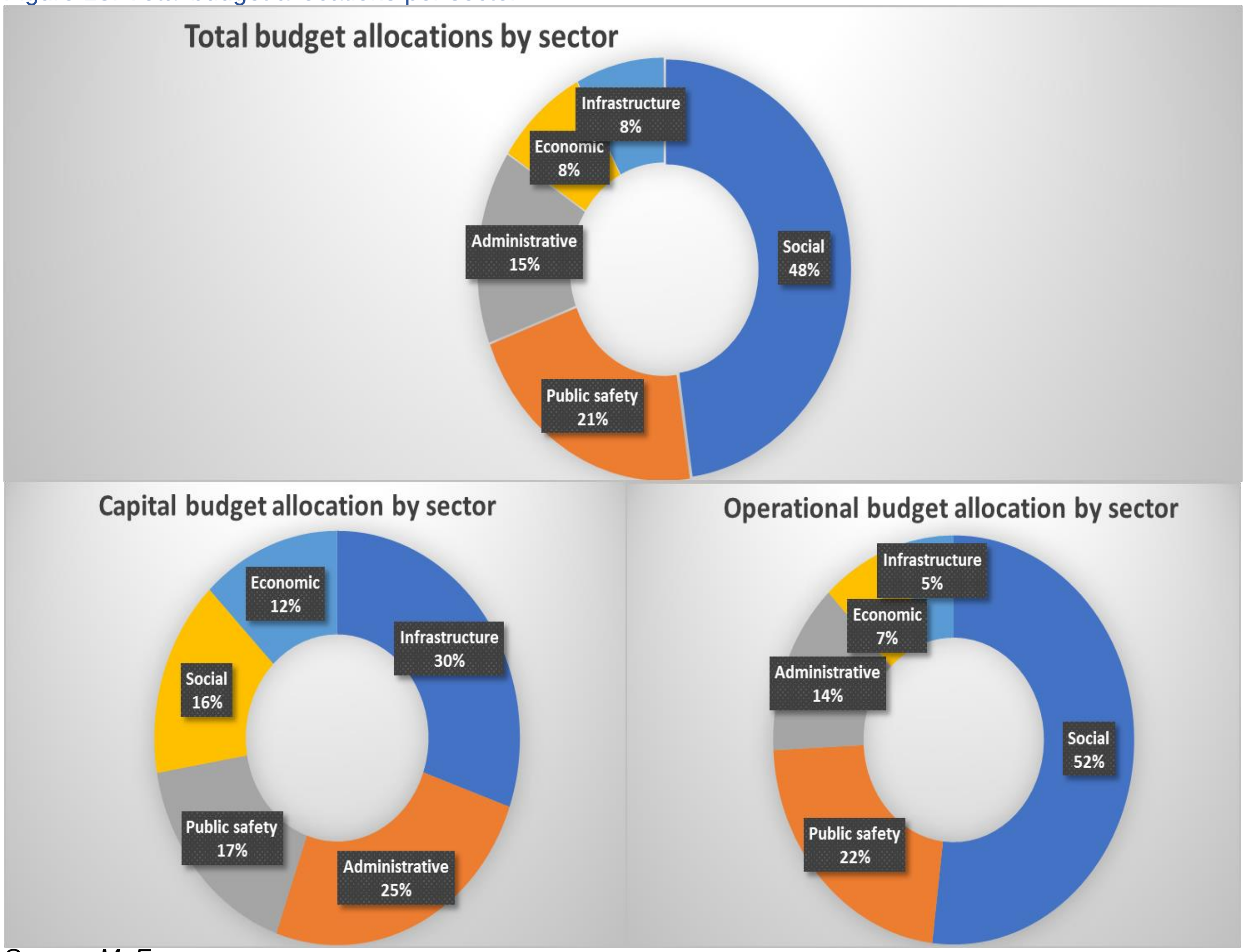


Source: MoF, NSA & First Capital Calculations

5.8. Budget Expenditure allocations by sector

Over the past 5 years, nearly half (48 percent) of the budget was allocated for social expenditure, which includes education, health and welfare services. Public safety expenditure which includes budget allocations to the ministry of defence and safety & security among others accounts for 21 percent of the total budget (*see figure 18).* The economic and infrastructure sectors receive lowest 8 percent each from the budget allocations.

Figure 18: Total budget allocations per sector

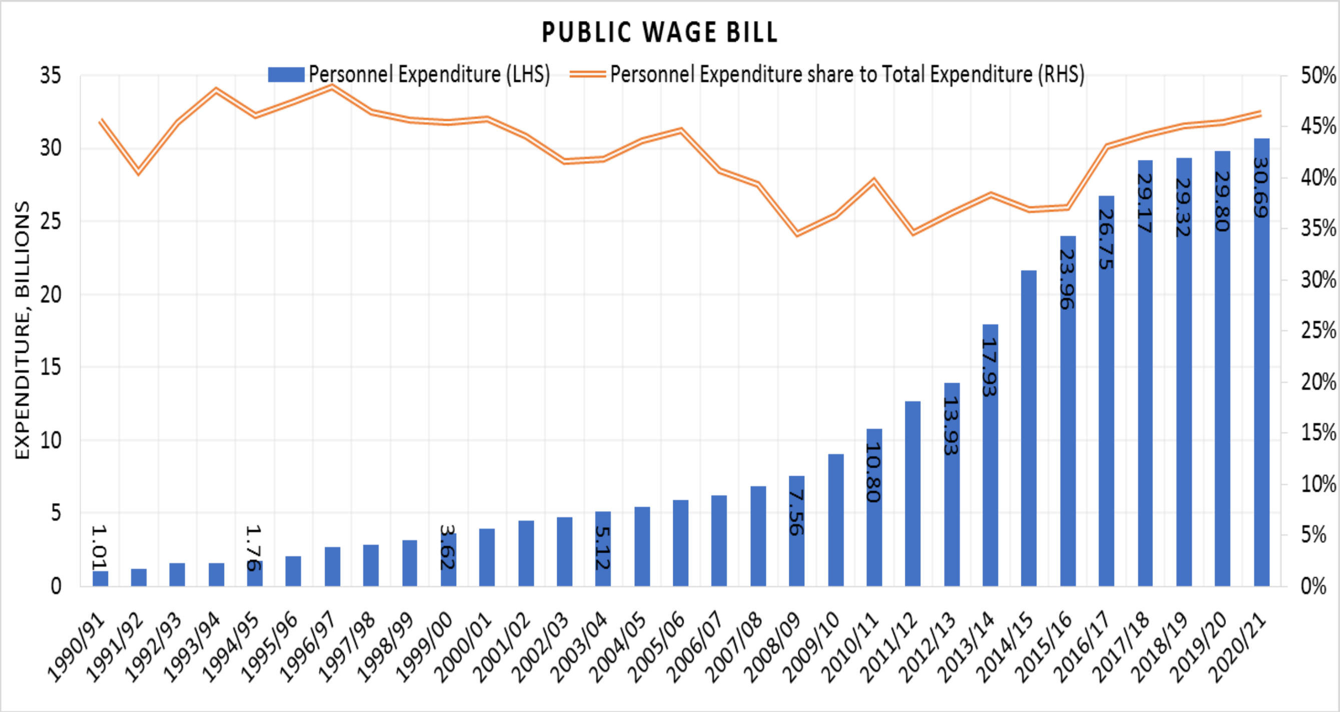


Source: MoF

5.9. Government Wage Bill

The government wage bill increased from N$ 1 billion in 1990/91 to N$ 29 billion in 2018/19.This represents an annual average growth of 12 percent. The main driver of the rising government wage bill was increase in the number of government employees and salary increases and employment benefits. On average the government spends 45 percent of its total expenditure on public servants per year. The proportion of personnel expenditure to total expenditure was at its all-time high in 1996/7 at 49 percent. In 2018/19 the wage bill stood at 42 percent of total expenditure which is expected to reach 45 percent in 2019/20 (*see figure 19).*

Figure 19: Public Wage Bill

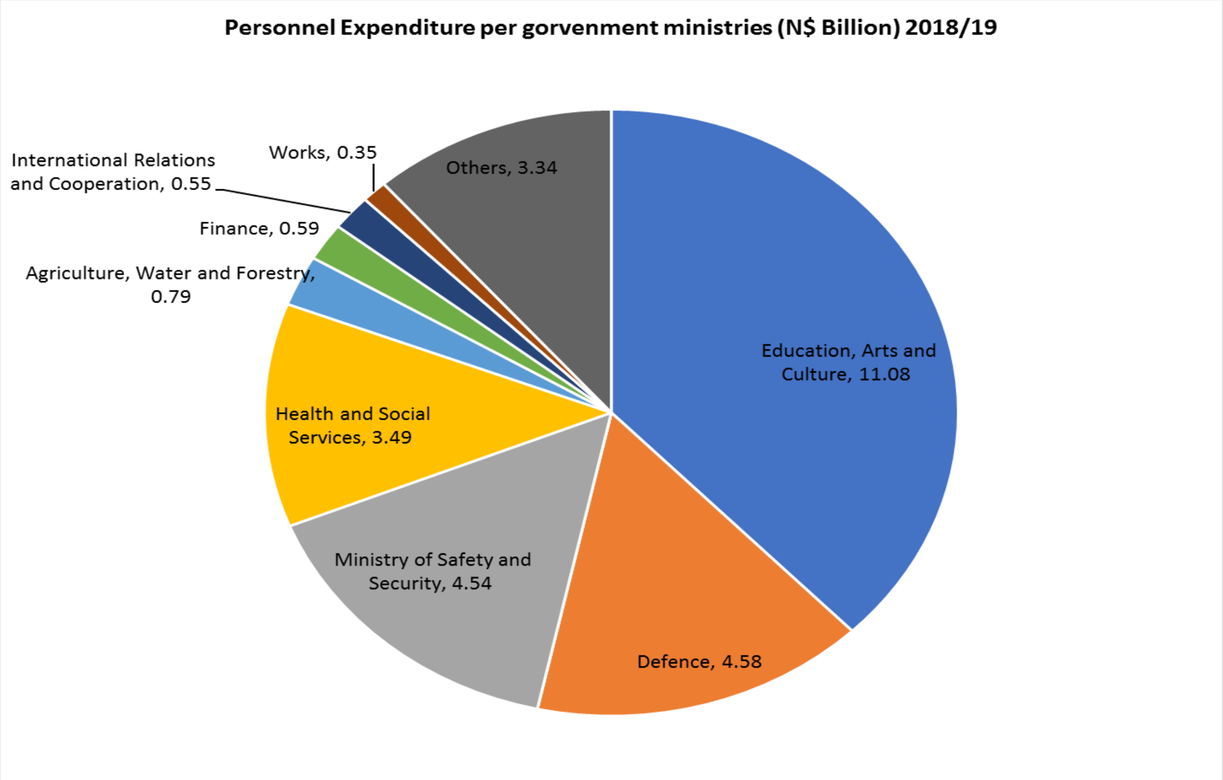


Source: MoF

5.10. Personnel expenditure per government ministries

The Ministry of basic Education, Arts & Culture has the highest wage bill of N$ 11. 1 billion which accounts for 38 percent of the total government wage bill (*see figure 20*). Ministry of Defence and Safety & Security spends N$ 4.6 (16 percent of the total government wage bill) and N$ 4.5 billion (15 percent of the total government wage bill) on wages and salaries of the staff respectively. The top four ministries with high wage bills (Ministry of Education, Defence, Safety & Security and Health & Social Services) accounts for 81 percent of the total government wage bill.

Figure 20: Personnel Expenditure Per Government Ministry



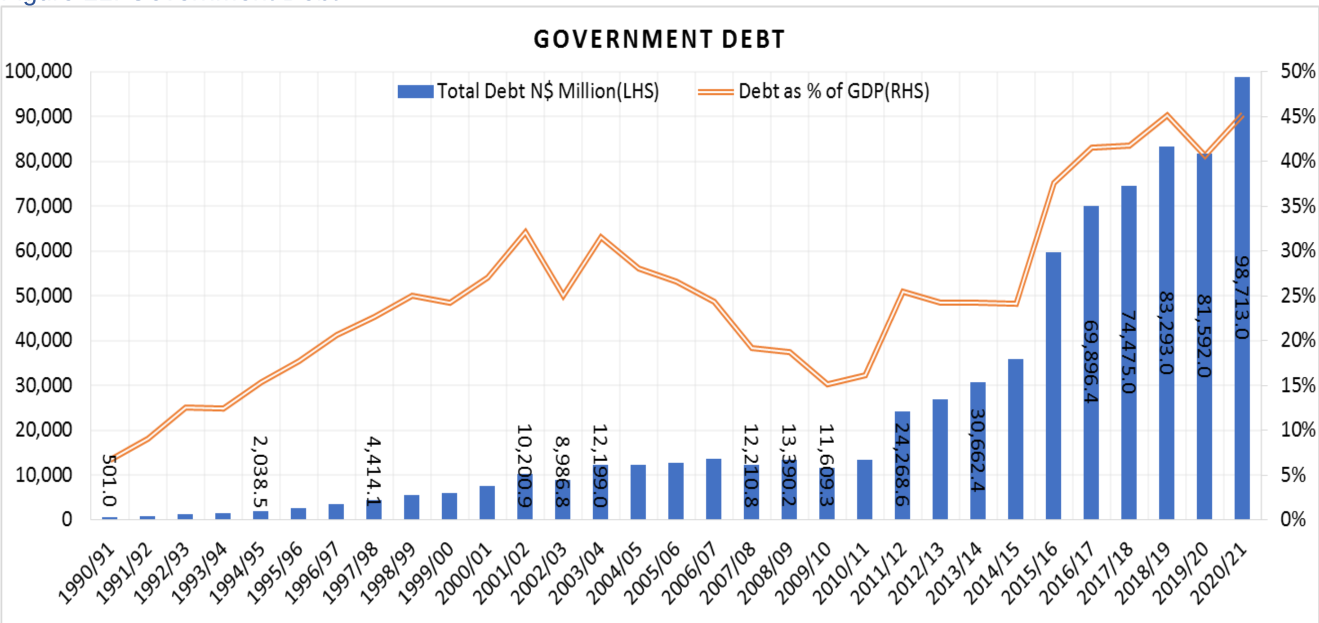
Source: MoF

6. DEBT ANALYSIS

6.1. Debt stock over time

Namibia have been sleepwalking its way into troublesome debt-to-GDP ratios that has increased from 7% of GDP in 1990/91 to 45% to GDP in 2018/19. Although debt to GDP rose to 32% in 2003/4, it was reduced by half to 15% by 2009/10 thanks to temporary budgetary surpluses recorded in prior years. The government debt stock has increased from N$501 million (7 percent of GDP) in 1990/91 to N$83.7 billion (45 percent of GDP) in 2018/19 and is expected to rise to 92.7 billion in 2019/20 (46 percent of GDP) *(see figure 21).* Since 2015/16 the government debt increased at an average rate of 26 percent per annum. The total debt to GDP surpassed the 35 percent benchmark 2015/16. This inability to keep debt under control over the years has led to the need for large government expenditure cuts with significant macroeconomic consequences with the economy stuck in an economic recession for most parts of 2017 and 2018.

Figure 21: Government Debt

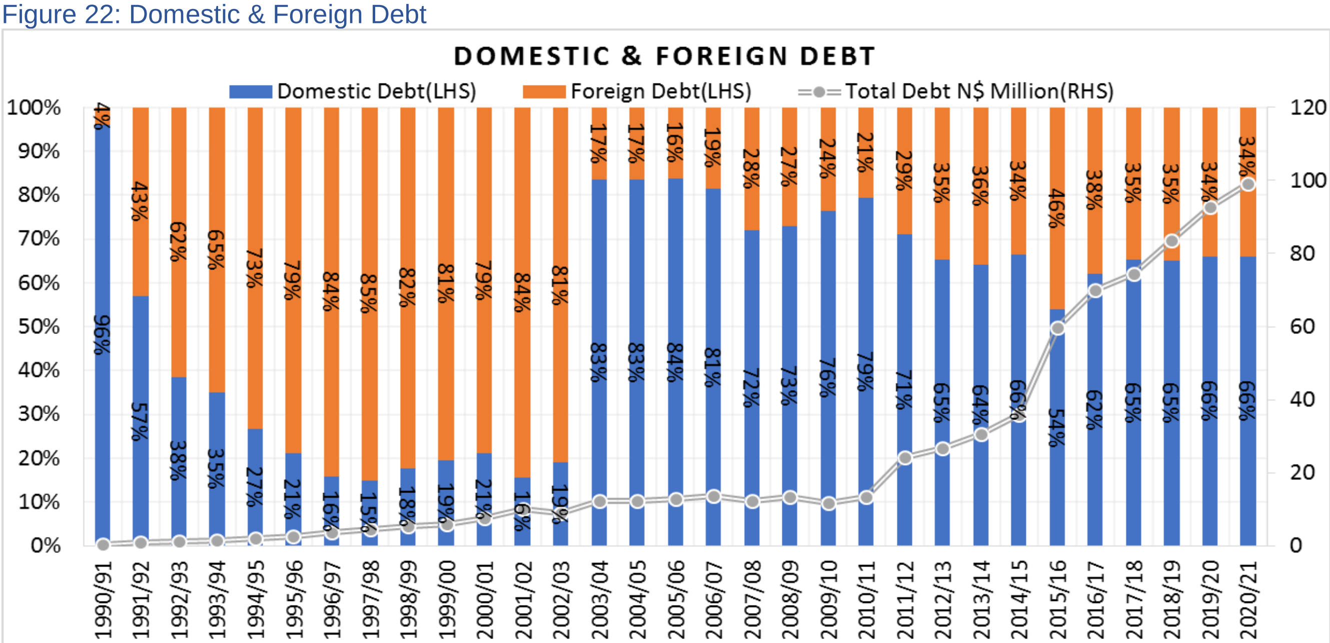


Source: MoF

6.2. Domestic and Foreign Debt

The total government debt has been increasing due to cumulative government deficit. Government debt is expected to reach N$ 92 billion by the end of 2019/20 composing of 65 and 35 percent of domestic and foreign debt respectively (*see figure 22*). A larger portion of public debt remains concentrated in domestic debt issue mainly in debt securities such as treasury bills and bonds.

Figure 22: Domestic & Foreign Debt

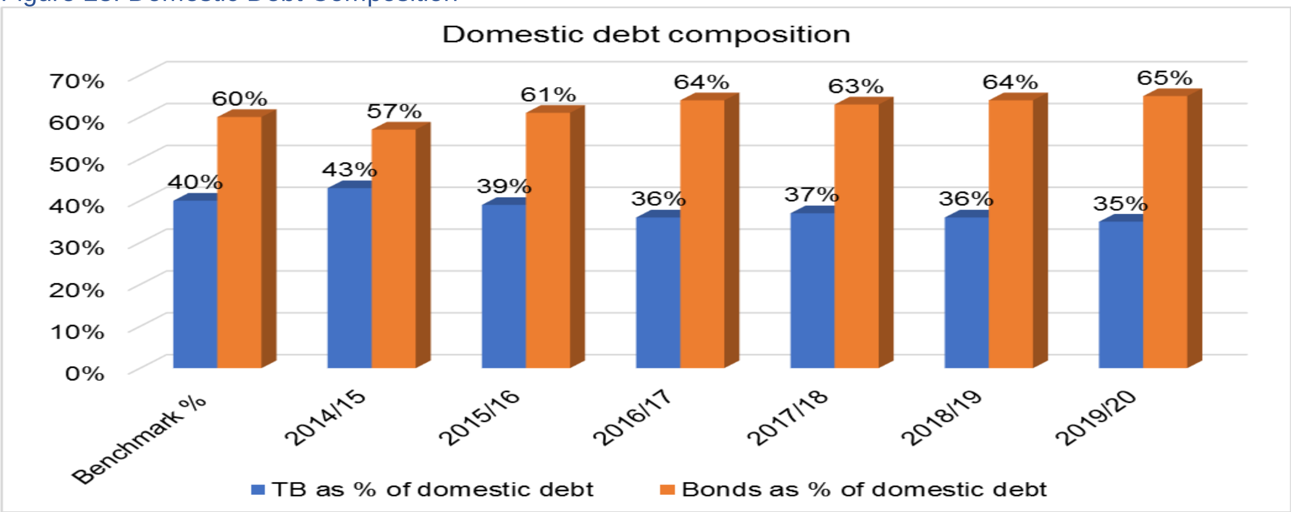


Source: MoF

6.3. Domestic Debt Composition

The total domestic debt stock held by the public is mostly concentrated in debt securities, of which long term securities make up 44 percent while short term securities composed 34 percent of total debt in 2018. *Figure 23 below* shows an increase in debt securities which is in line with the trend observed in domestic debt profile. The total debt stock in 2018 exceeded the threshold rate of 40 percent in treasury bills and 60 percent in bonds.

Figure 23: Domestic Debt Composition

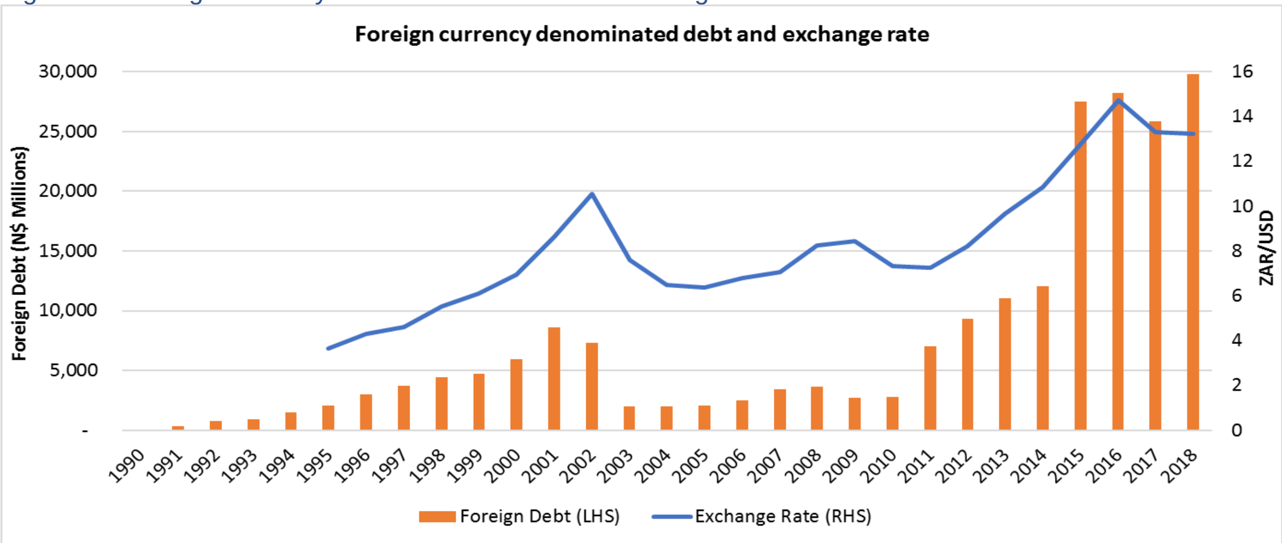


Source: BoN

6.4. Foreign Debt and Exchange Rate

Foreign debt accumulated on account of the currency depreciation of ZAR/USD and continued foreign borrowing by government. Foreign debt increased by 128 percent between 2014 to 2015 rising from N$ 12 billion to N$ 27 billion (see figure 24).

Figure 24: Foreign currency denominated debt and exchange rate

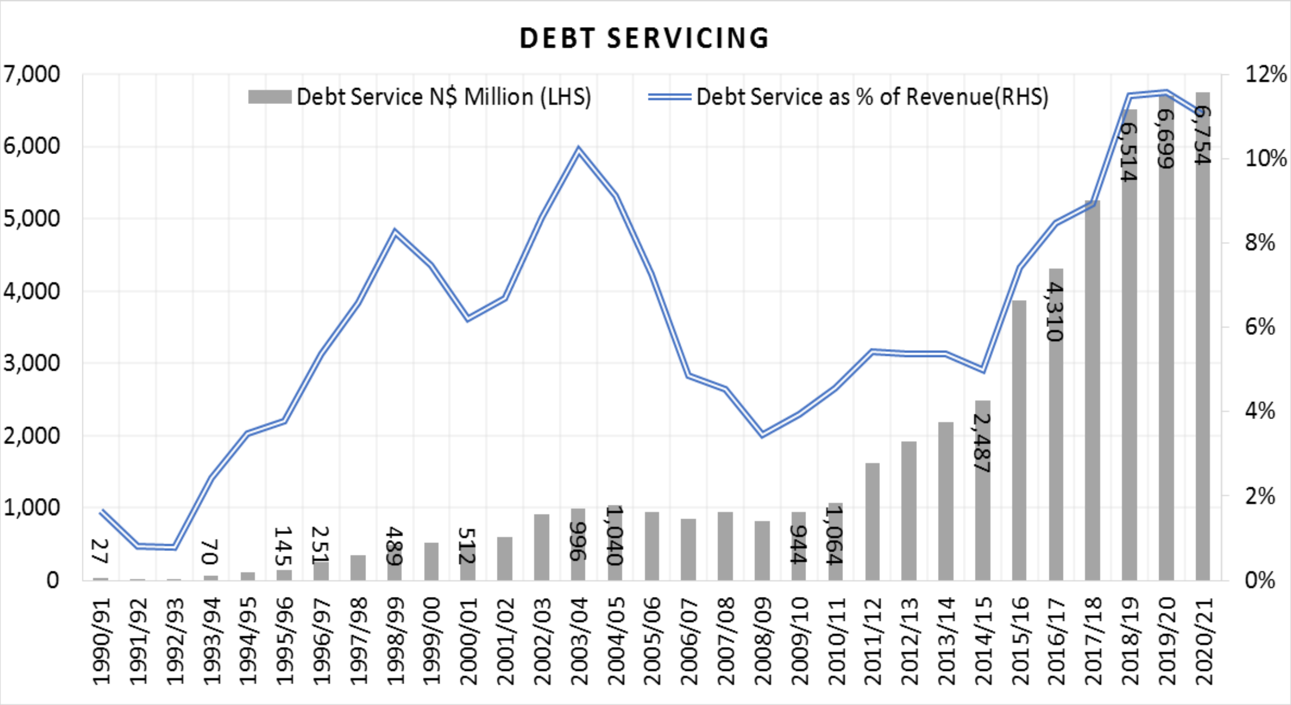


Source: BoN

6.3. Public debt servicing cost

The cost of servicing the public debt increased from N$ 200 million (2 percent as a percentage of revenue) in 1990/91 to N$ 6.5 billion in 2018/19 (11 percent as a percentage of GDP) (see figure 25). Debt servicing cost is rising in correspondence to public debt. Debt servicing cost to revenue surpassed the benchmark of 10 percent in 2018 as it reached 11 percent. Part of the increase in foreign denominated debt servicing cost is as a result of exchange rate depreciation of the domestic currency in relation to the US$ and other major currencies. Furthermore, the increasing interest payments is also a result of rising bond yields on government bonds which is linked to weak sovereign rating making the cost of borrowing expensive.

Figure 25: Debt Servicing

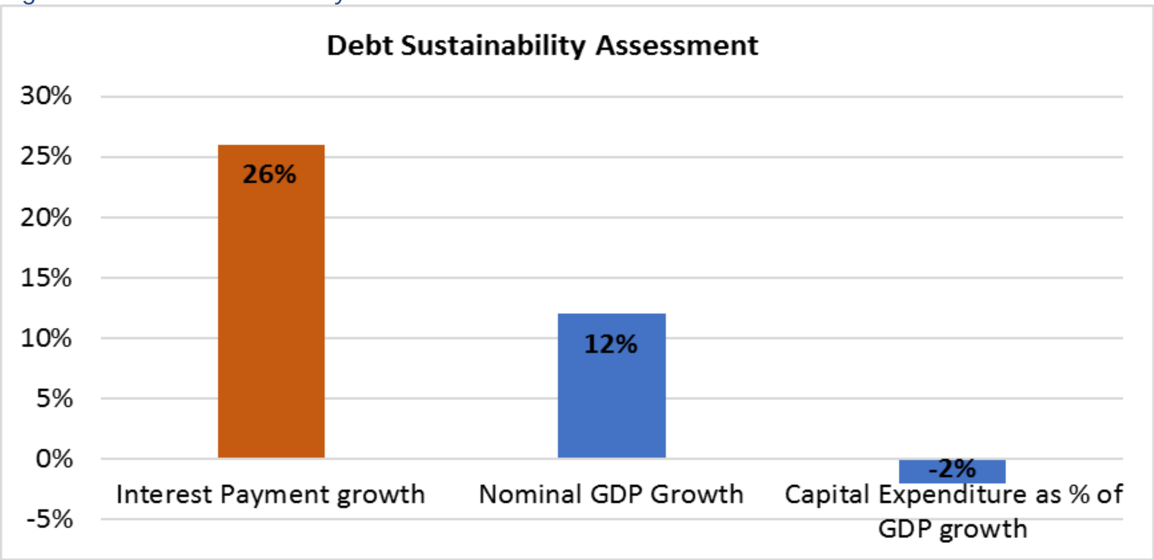


Source: MoF

6.4. Debt Sustainability Assessment

Over the past 29 years, interest payments have increased at a rate of 26 percent on average per annum. The nominal GDP growth increased by 12 percent while capital expenditure to GDP growth declined by 2 percent on average per annum (see figure 26). If this trend continues a significant portion of government revenue will be channeled to service debt in the medium term which will reduce the governments ability to fund and provide other essential services.

Figure 26: Debt Sustainability Assessment

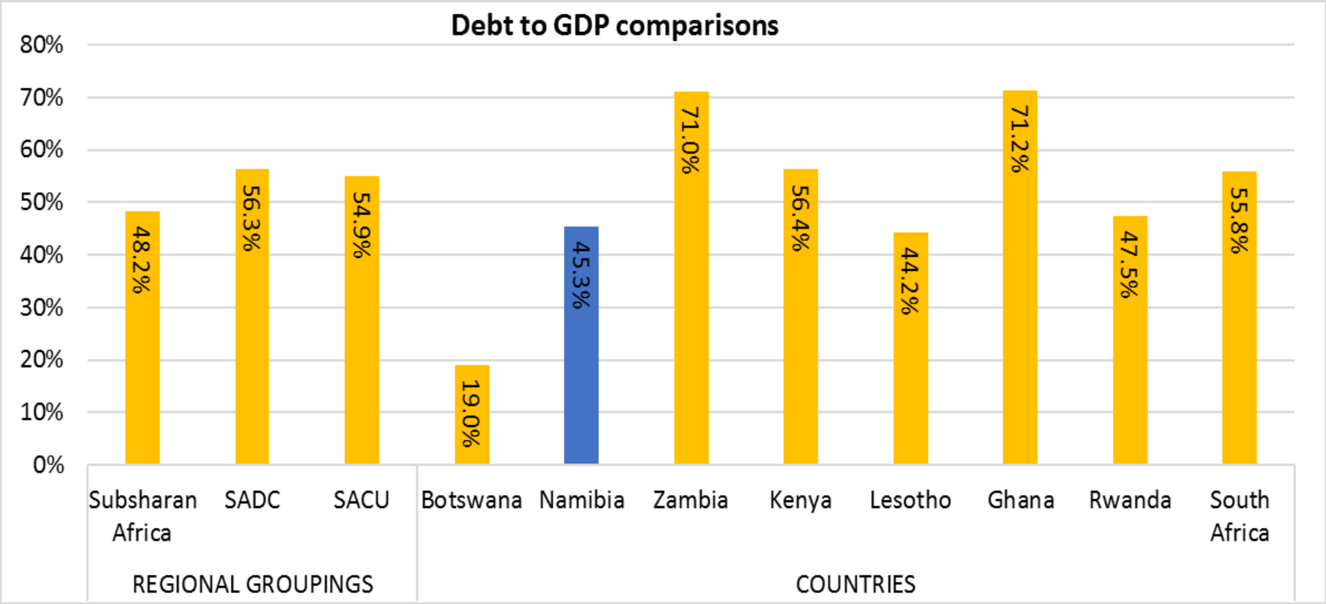


Source: MoF, NSA & First Capital Calculations

6.5. Debt stock comparisons by countries

Namibia's debt stock compares favorable with most countries on the continent. At 45 percent Namibia's debt to GDP ratio remains lower than the average of countries making up SACU (55 percent), SADC (56 percent) and Sub-Saharan Africa (48 percent). By countries Namibia's debt is lower than that of Zambia, Kenya, Ghana, Rwanda and South Africa *(*see figure 27*).* However, Namibia's debt is higher than that of Botswana which stands at 19 percent.

Figure 27: Debt to GDP Comparison



Source: IMF & MoF

6.6. The impact of introducing an early retirement for Civil servants

The civil service has a staff composition of 91,295 as of April 2018. Six percent or 5,478 of the total number of civil servants are aged between 55-59 years. The government spends $29.3 billion on personnel related expenditures of 91,295 civil servants which translates to an average N$306,000 cost to government for each civil servant (*see table 6*). Of the 5,478 civil servants aged 55-59 years, any retirement that would attract at least 40 percent of this group would save government at least N$670.5 million in personnel related expenditure equivalent to 3 percent of the wage bill. On the other hand, the same situation would cost the government pension fund N$1.62 billion in pension payouts.

Table 6: Impact of Early Retirement

The Impact of early retirement for civil servants	
Total Public sector Wage bill	N$29.3 Billion
Average cost per civil servant	N$306,000
Average pension payouts per beneficiary	N$740,000
Number of Civil servants aged 55-59 Years	5,478(or 6% of total Civil service)
Cost to Gov of Civil servants Aged 55-59 Years	N$1.67 Billion
Should 40% of aged 55-59 years take early retirement	
Government would save	670.5 Million
The cost to pension payouts	N$1.62 Billion

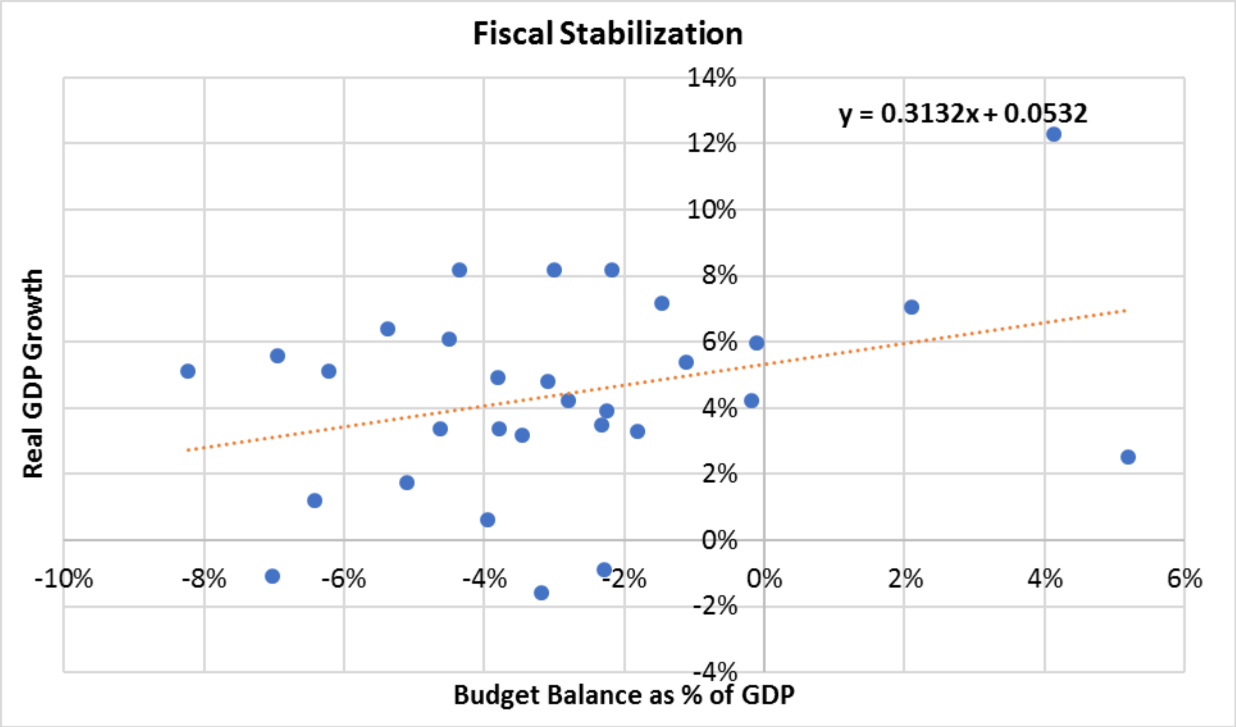
Source: MoF, GIPF & First Capital Calculations

If the government is to implement this measure, the government would be able to reduce about 8 percent of its budget deficit. On the other hand, saving N$ 670.5 would help reduce the government debt by at least 4 percent. In the long run, this measure combined with other measures will place Namibia at a sustainable fiscal position to contain expenditure and reduce debt.

6.7. Fiscal Stabilization Assessment

The fiscal stabilization coefficient measures the relationship between GDP growth and budget balance to GDP growth. This relationship gives an indication of how economic agents or the economy in general responds to fiscal policy. The variable budget balance has been lagged for two years. As shown in figure 28 below, an improvement in the budget balance (from deficit towards a surplus) is associated with higher GDP growth. This means that economic agents consider the path of fiscal policy before making investment decisions.

Figure 28: Fiscal Stabilization



Source: MoF & First Capital Calculations

7. CONCLUSION

There is a saying that today's problems come from yesterday's solutions, and the fiscal policy challenges and problems government faces today is linked to efforts by government in seeking solutions to solve the unemployment situation, poverty and spending on social and welfare programs. Government can't now change the past, but if policy makers don't learn from it, the country will be trapped into recreating it and falling further in debts and end up in a debt trap. The Namibian economy is projected to emerge from the recession in 2019 with low GDP growth numbers compared to past growth rates. As the economy starts to register positive real GDP growth rates government revenue is equally expected to gradually increase. Revenue improvement that is expected at the back of improved economic activities would be a huge test for our fiscal policy management to maintain the current spending trend of fiscal consolidation. Rather than rising expenditure, efficiency should be increased on the current expenditure levels to increase the output with similar resource allocations.

ABOUT US

First Capital Namibia is a financial services company specialized in providing treasury and asset (investment) management services. Established in July 2009, First Capital have in-depth, personal knowledge of the Namibian capital markets and the resulting insight enables us to manage Namibian assets across different spectrum including cash management, equity, fixed income, specialist agriculture and property mandates. We are licensed to manage money for private investors, pension funds, insurance groups, public (government) sector, and charities. Our credibility as asset managers is tightly governed by the Namibia Financial Institutions Supervisory Authority (NAMFISA). We are a Namibian based investment team and focus exclusively on the Namibian market and we add value to portfolios through offering specialized Namibian mandates.

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