FIRST CAPITAL
NAMIBIA

The 2011/12 Government of Namibia Budget
A Critical Analysis

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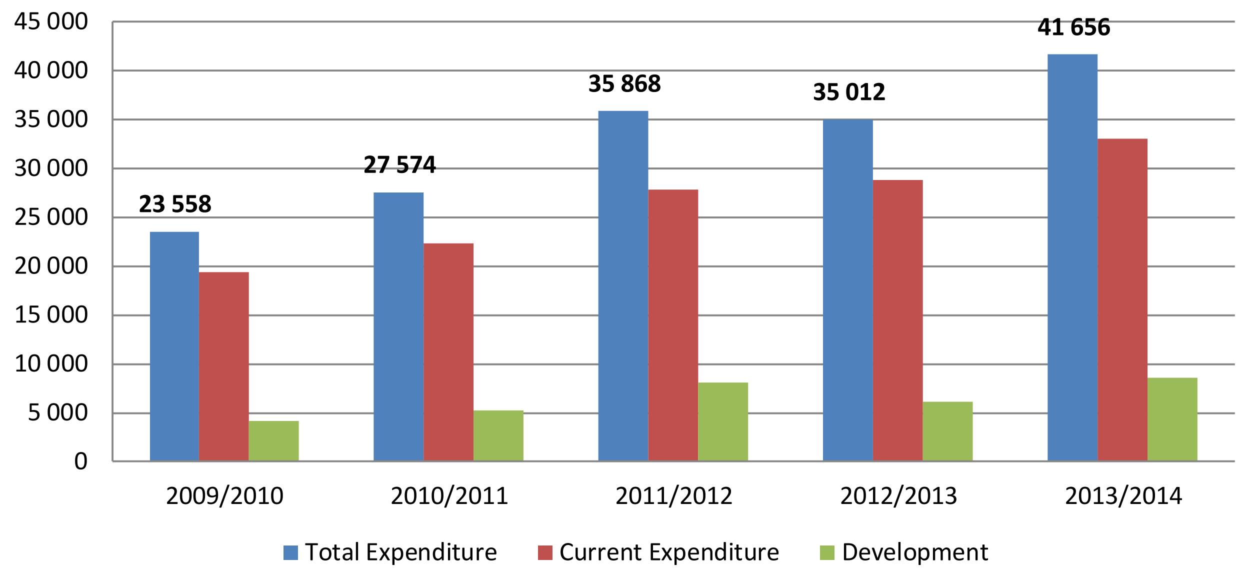
1. Introduction

Namibia's Minister of Finance Mrs Saara Kuugongelwa-Amadhila presented her 9th budget to the National Assembly on 09 March 2011. The Minister presented an expansionary budget with the aim of consolidating economic recovery, create jobs and improve the welfare conditions of Namibians while safeguarding macroeconomic sustainability. The government budget has two sides, namely government expenditure and government revenue, and if the two does not balance, a budget deficit or surplus is recorded and for the 2011/12 national budget, the minister announced a budget deficit of 9.8% of GDP, the highest since independence. In an effort to address the unemployment situation in the country, and stimulate economic growth, the Minister announced the introduction/implementation of a new program called Targeted Intervention Programme for Employment and Economic Growth (TIPEEG). TIPEEG is aimed specifically at addressing economic growth and fight the high unemployment through support to strategic priority growth sectors. The TIPEEG programme will focus on four key sectors, namely, agriculture, transport, tourism, housing and sanitation.

2. Expenditure Analysis

The overall government expenditure (excluding interest cost to service government debt) will increase by 30% to N$35.8 billion in 2011/12 from N$27.1 billion in 2010/12. The social, welfare, justice, administration and safety and security ministries accounts for about 80% (or N$28. 4 billion) of the total government expenditure, and the remaining 20% (or N$7.5 billion) is allocated to economic ministries such as mines, trade, land, agriculture, fisheries, transport, tourism and planning. The four largest spending ministries are Education, Finance, Health, and Defence, which in total accounted for over 51% (or N$18. 4 billion) of the total government expenditure in 2011/12. Finance ministry is the second largest spender because of the interest rate debt repayments on government debt and with the projected rise in deficit and debts; the Finance Ministry is likely to retain its position as the second biggest spender. The high spending on social sectors (education and health) and economic infrastructure (roads, transport and railways) means that the government is spending more for the future than for the past which augur well for the future of the country, in terms productivity gains. Figure 1 below shows total government expenditure breakdown, with current or operational expenditure accounting for close to 80% of total government spending.

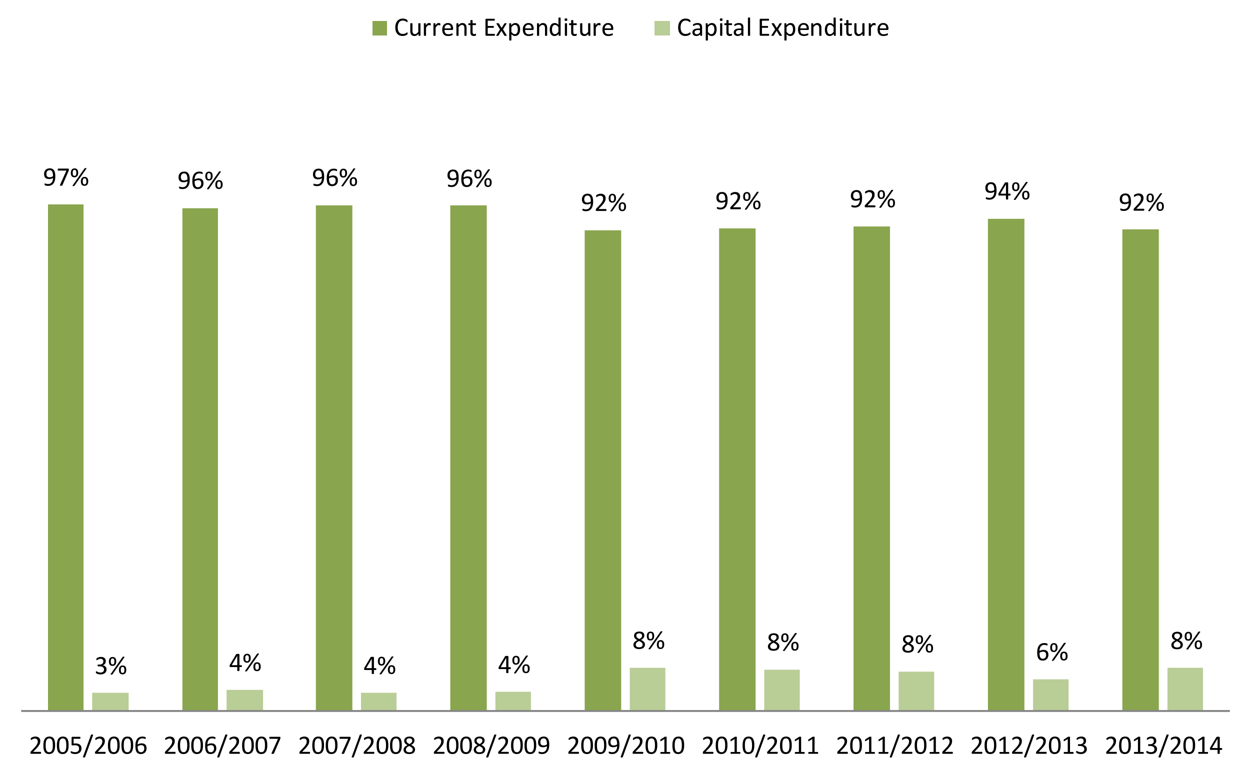
Figure 1: Expenditure Composition



3. Allocation to Education

Improving education is one of the priorities government has set itself to achieve over the coming years and government knows that for poverty and unemployment to be reduced, a country needs educated and skilled people. Since independence, education has received the largest share of our country's budget and this year is no different, with education receiving more than N$8.0 billion or 22% of total budget. When people are educated they are able to find work and improve the quality of their lives and the lives of their families. Although education receives the largest share of the national wealth, it spends more than 90% of its budget on consumption or current expenditure, and spending very little, less than 10% capital expenditures, explaining the reason why there is a still high shortage of schools, hostels, text books, school desks, etc. Figure 2 below shows the share of both current and capital expenditures in total education expenditure.

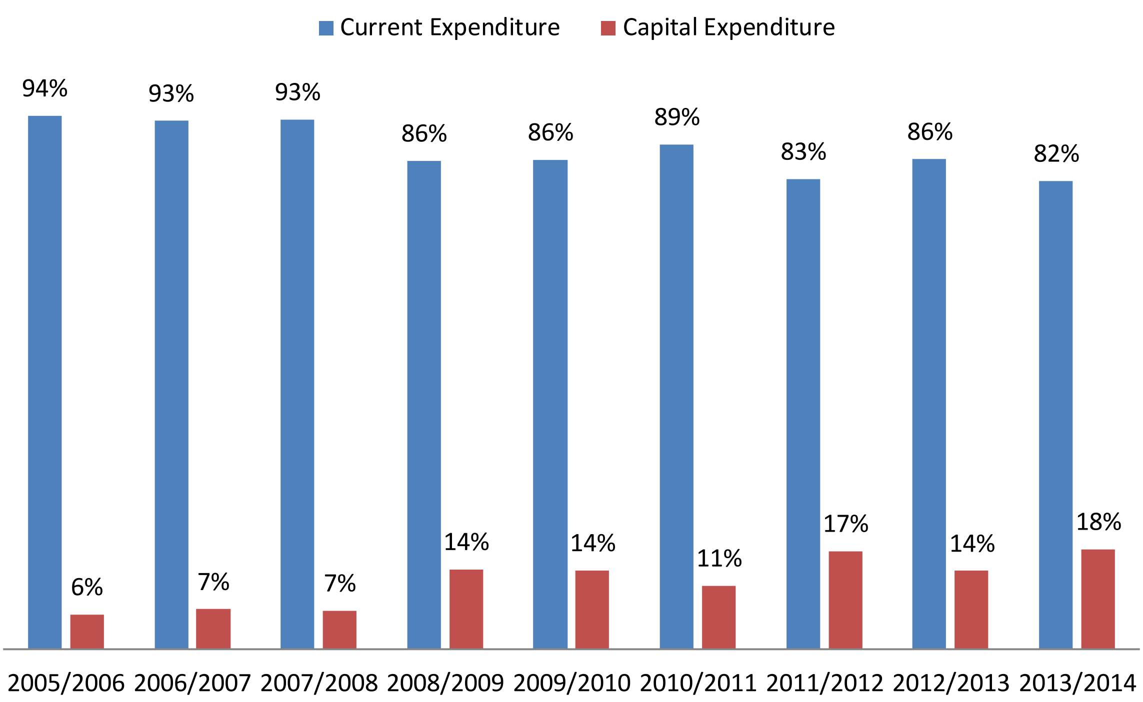
Figure 2: Education Expenditure Allocation



4. Budget Allocation to Health Services

The Ministry of Health and Social Services is the principal institution charged with protecting the health of all Namibians and providing essential health services. The 2011/12 Budget includes N$3.3 billion allocation to support Ministry of Health's mission. A closer look at the composition of health expenditure reveals that more than 80% of the Ministry's budget goes into current expenditure (see figure 3 below). It is encouraging to see that capital/development expenditure has been increasing rising from 7% in 2007 to 17% of total expenditure in 2011, indicating that the Ministry has been investing more in health infrastructure such as hospitals, clinics, medications and equipments and if this trend continues Namibia will not only provide quality health to its people, but the country is likely to become an exporter of world class medical services to the world.

Figure 3: Health Expenditure Allocations



5. Revenue Analysis

On the revenue side, the government continues to depend heavily on indirect taxes. In 2011/12, 94 percent of the government revenue is expected to accrue from tax revenue (N$26.3 billion out of total government revenue of N$28. 1 billion). Out of the total tax revenue 51% (or N$ 13. 6 billion) is expected from indirect taxes, that is taxes on goods and services and taxes on imports – SACU, and 48% (N$12. 2) from direct taxes (taxes on income and profits). Direct taxes (income and profit tax, etc) are deemed to be progressive and indirect taxes (taxes on expenditure on goods and services such as VAT, levies, import/export duties, excise duty, stamp duty, motor vehicle tax, etc) are regressive, because direct taxes are on income but indirect taxes are on consumption / expenditure, and affects the low income and the poor the most. Higher income earners pay greater direct taxes and therefore progressive, but indirect taxes are the same irrespective of the income level of the consumer and therefore regressive. Indirect taxes are one of the main causes of inflation, because these taxes are passed on to the consumers by way of increasing the price of goods and services. Therefore, attempts should be made to increase the share of direct taxes in the total tax revenue in order to contain the rising cost of living. The 2011/12 budget makes no tax adjustment to benefit the low income group and with such a regressive tax system, the poor who spend more than 70% of their income on food will remain poor and income inequality will remain high.

6. Economic Growth & Job Creation Impact of the 2011/12 Budget

For expanded government expenditure programme to force the economy onto a sustainable path, sufficient growth must be generated to offset the otherwise negative effect of the high budget deficit, and increased government investment must raise private sector aggregate demand through associated multiplier and accelerator effects. Namibia is to embark on a targeted broad economic growth framework, namely the **Targeted Intervention Programme for Employment and Economic Growth (TIPEEG)** in a bid to create around 104 000 jobs over the next three years from 2011 to 2014. The announcement was made by the Minister of Finance when she tabled the 2011/12 national budget. The Minister informed the national assembly that TIPEEG is aimed at addressing unemployment, inequality and poverty by unlocking employment opportunities in different sectors of the Namibian economy. The TIPEEG growth framework identifies four growth sectors and prioritises efforts to support employment creation in the following four key sectors:

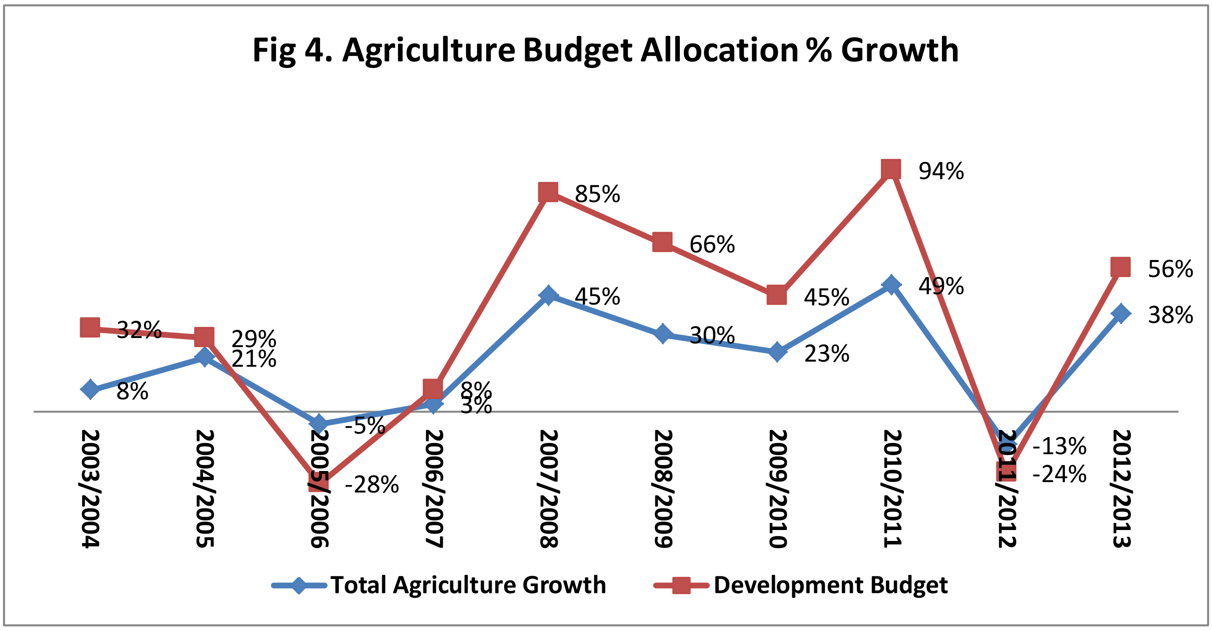
- the agriculture sector
- the tourism sector
- transport
- housing & sanitation

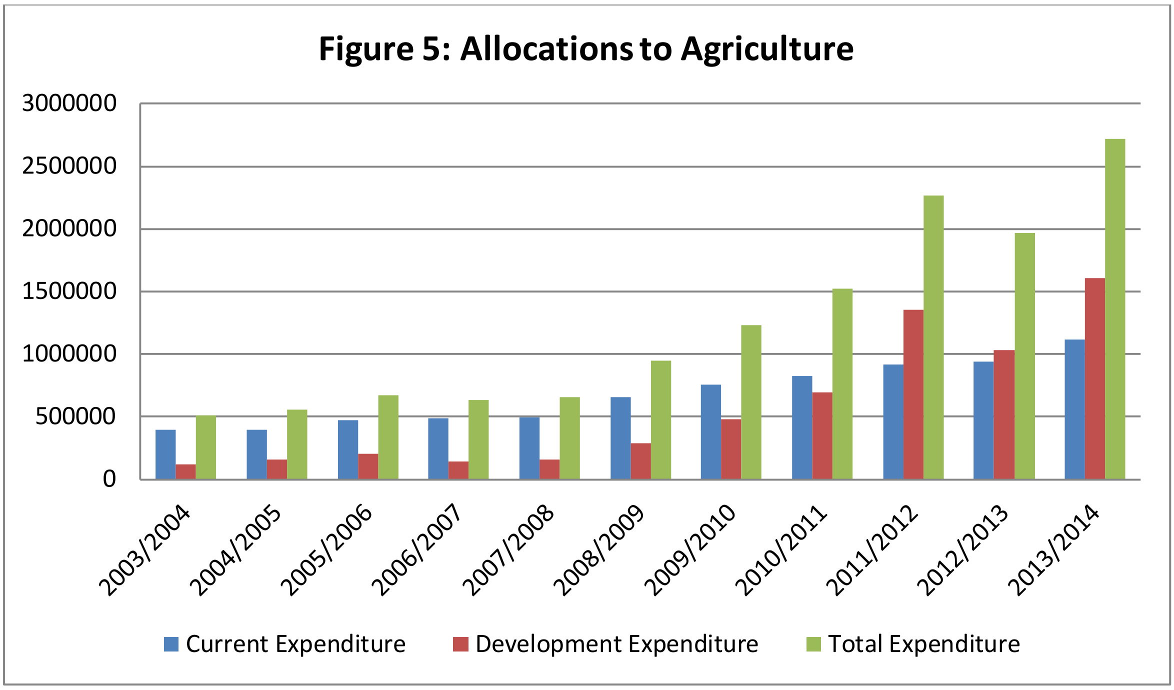
Although TIPEEG identifies key sectors where employment creation is possible, the Minister was silent on the policies and institutional developments required to ensure the effective implementation of the new intervention strategy. Namibia has mass unemployment which is structural in nature, and cannot therefore be addressed by once off expansionary government expenditure. Direct government expenditure cannot create permanent jobs in the short run (1-3 years), but government can provide effective inducements to private investment in targeted sectors principally by providing funds and other incentives to boost production. Below we present a brief analysis on why we do not believe the 2011/12 budget contains enough measures to achieve high economic growth and create 104 000 jobs.

6.1 TIPEEG Job Driver Number 1: Agriculture Sector

Agriculture sector has the capacity to generate more jobs as it is highly labour intensive and additional investment in the sector by private sector will substantially boost production and create more jobs. For agriculture to create more jobs it requires well designed policy package that support both communal and commercial farmers, but we do not believe government ownership of farms is the solution to boost production in the agricultural sector. Although agriculture expenditure rises by 94% (see figure 4 below) in 2011/12, budget allocation to the sector is projected to growth by negative

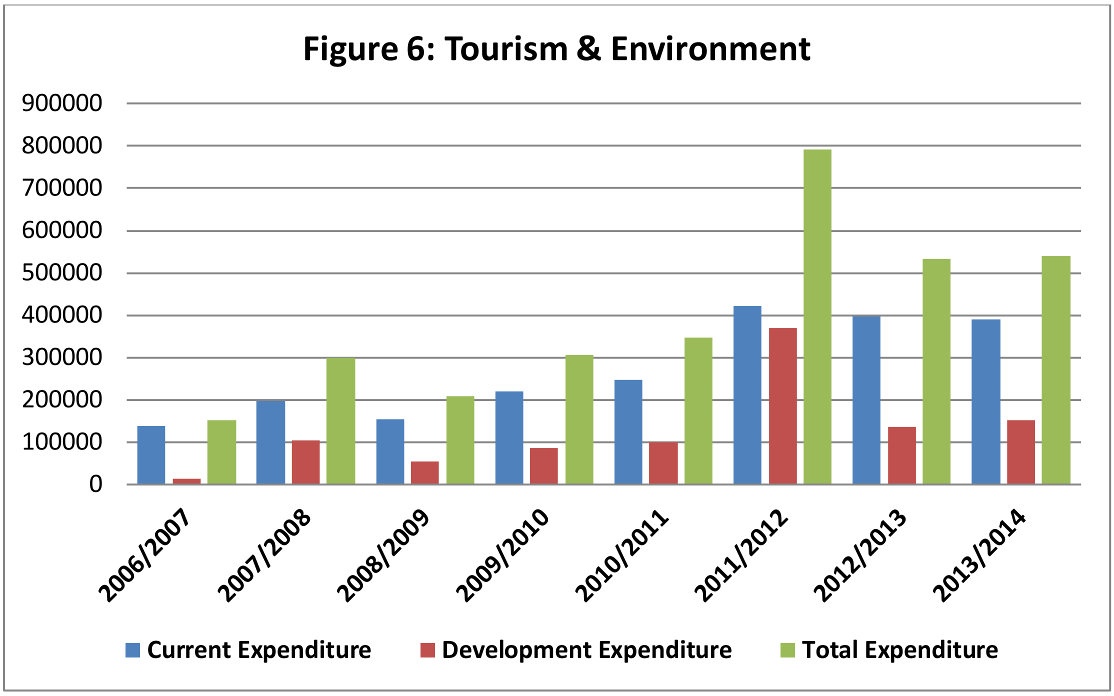
13% in 2012/13, before rising by 58% in 2012/13, representing average expenditure growth of 42% over a three year period from 2011 to 2013, much lower than the average growth in agriculture budget expenditure of 65% over 2008/9 to 2010/11. The question is "how many jobs were created over this period (2008 -2010) when budget allocation to agriculture grew on average by 65%? Our position is that the current allocation will have very little job creation on the sector, and we do not foresee significant jobs being created in the sector based on what we see in the 2011/12 budget. Figure 5 below shows a breakdown of allocations to the Ministry of Agriculture, with development budget accounting for more than 50% of total budget allocated to the ministry, a very encouraging trend and something absent in many ministries who spends the bulk of their budget allocations on consumptions/current expenditure.





6.2 TIPEEG Job Driver Number 2: Tourism Sector

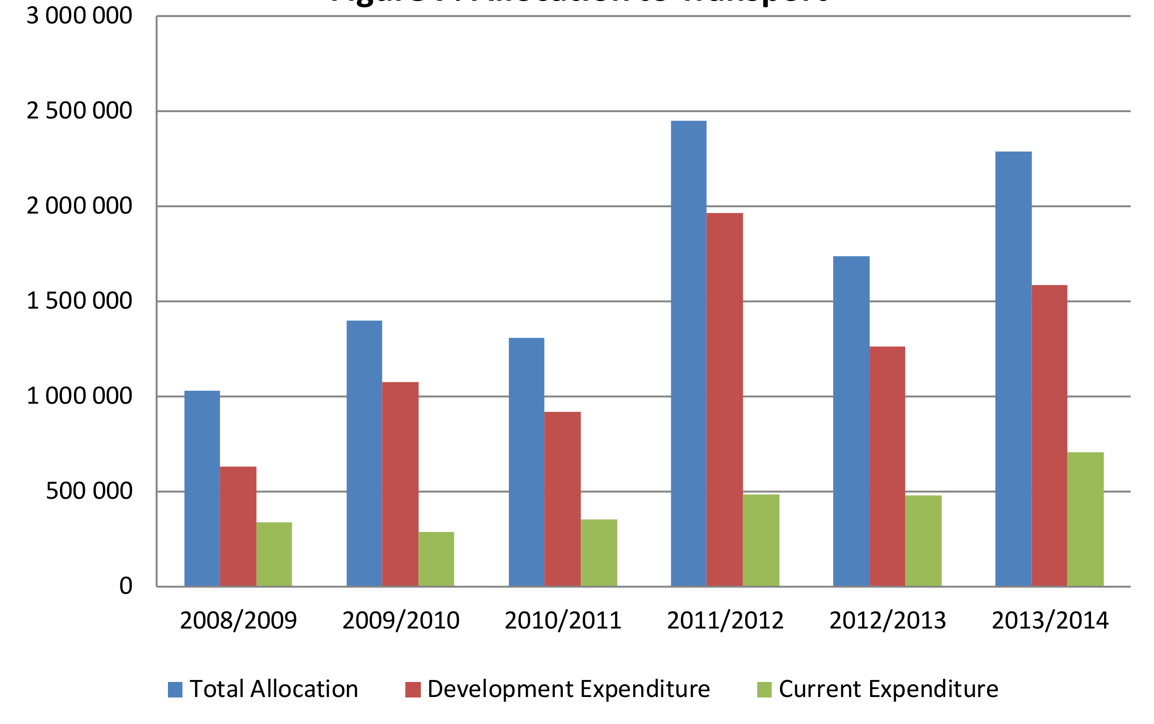
Jobs in tourism is linked to the growth in number of tourists visiting Namibia and depends on many factors other than a once of government expenditure to the tourism sector. Figure 6 below shows that government allocated around N$791 million to the Ministry of Tourism sector, with close to N$436 million of this going into development expenditure of the tourism sector. A further breakdown of the development budget allocation shows that N$266 million goes to Namibia Wild Life Resort (NWR), N$70 million goes to Namibia Tourism Board. As figure 6 shows more than 50% of the budget allocation to the Ministry of Environment & Tourism goes into operational expenditure. Based on expenditure analysis in figure 6 below, we do not believe the 2011/12 tourism budget expenditure will have multiplier effect on the tourism sector & the economy and we do not think the sector will generate envisaged jobs. Jobs creation in the sector will only come once the private sector starts expanding its investments in the sector.



6.3 TIPEEG Job Driver Number 3: Transport Sector

Namibia will spend more than N$2.4 billion on transport infrastructure, with N$1.9 billion earmarked for development expenditure on new roads, road rehabilitation and railway refurbishment. As figure 7 below shows most of the allocation to transport sector goes to the development budget, and very little to operational expenditure and this has been the tradition since independence. Unfortunately this is a once off expenditure, and allocations to transport declines substantially in 2012/13. The high budget allocation to the transport sector should also be seen as a response by government to the collapse of the country's road and railway network due to the heavy rains received in the first quarter of 2011. Although jobs will be created during the construction phase, we do not think this will be significant and most of these jobs will be temporary and linked to the length of the tender.

Figure 7: Allocation to Transport



6.4 TIPEEG Job Driver Number 4: Housing & Sanitation

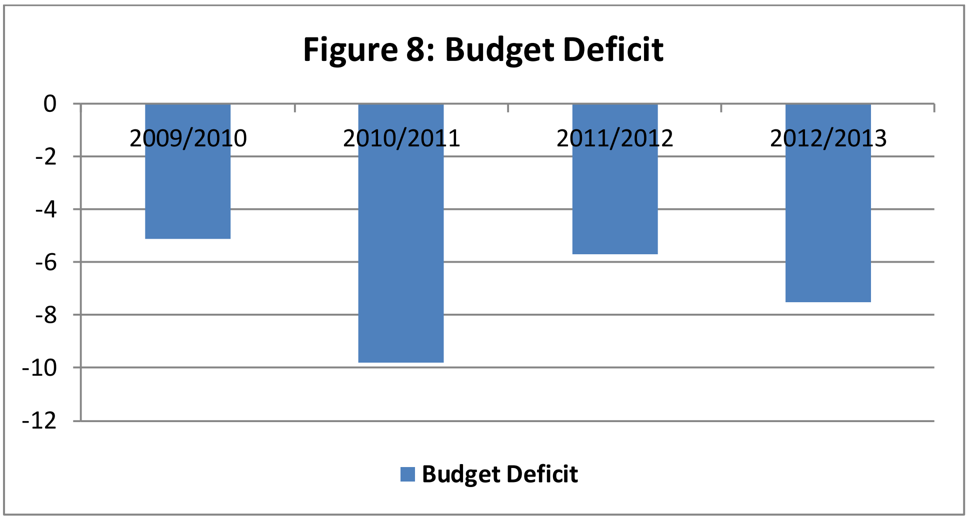
TIPEEG identifies housing and sanitation as a growth priority sector that has a potential to stimulate economic growth and create jobs. The Budget allocates a total amount of N$2.8 billion over three years (2011/12 to 2013/14) for land servicing, construction of low cost housing as well as construction of urban and rural sanitation facilities. In our view this sector should not form part of a list of priority sector requiring government intervention to stimulate economic growth and create jobs, but should form part of the social safety net strategy with indirect benefit to the economy.

7.0 TIPEEG Vs NDP 3 (National Development Plan 3)

The Namibian economy faces complex challenges (high structural unemployment, rising poverty, unbalanced economic growth, income inequality) and temptations to respond to these challenges in an emotional, ad-hoc and fragmented way can be quite strong and damaging. There can be enormous risks and dangers in ad-hoc solutions which are not thought through, as their effect on the economy and the population can be quite damaging, and may require painful policy adjustment in future in the form of higher taxes, cut in government expenditure, etc. Namibia already has a long-term national development plan (NDP 3), adopted by Parliament in June 2008, which attempt to translate Vision 2030 objectives into concrete policies and actions. Its main theme is "Accelerated Economic Growth and Deepening Rural Development". More specifically, NDP 3 seeks to achieve the medium term objectives of sustainable growth, employment creation, reduction of poverty and inequality in income distribution across the various regions, environmental sustainability, gender equality and important reductions in HIV/AIDS prevalence and specifies policies and programmes that need to be implemented to achieve the targets in NDP 3. While TIPEEG excludes sectors such as manufacturing, fishing, infrastructure such as power, rural water supply, small business enterprises, NDP 3 puts these at the forefront as prerequisite for economic growth and job creation. Do we now have two competing programs? Is TIPEEG derived from NDP 3, and if so on what basis were the priority sectors in NDP 3 excluded in this intervention package? Is TIPEEG trying to address weaknesses in NDP 3? If so how? The national budgets are there to finance programs and projects identified in NDP 3 and TIPEEG only becomes relevant if it addresses weakness in NDP 3, which based on our 2011/12 budget analysis is not the case.

8.0 Budget Deficit

The budget deficit at 9.8% and debt to GDP approaching 30% raises questions about sustainability of fiscal policy going forward, in light of revenue constraints & high expenditure that cannot be reduced. Fiscal risk emanating from this year's high budget deficit of 9.8% to GDP and debt to GDP approaching 30% by 2012 makes Namibia's fiscal position vulnerable and could over time bring down Namibia's credit ratings, which will make cost of borrowing by both government SOEs much higher.



Namibia's ability to absorb fiscal risks is still satisfactory, given the strength of past fiscal policy outcomes, with Namibia running low debt and deficits. The question is what will be the government's capacity to respond to the realization of fiscal risks in the future? The structure of government expenditure is rigid. At around average 36 percent of GDP over the coming three years, government expenditures are dominated by social outlays such as health, education, social protection programs, infrastructure maintenance, debt service, and wages that cannot just be reduced. In addition, Namibia is becoming prone to natural disasters such as floods and droughts that will put financial pressure on government spending in future. Coupled with this, pressure is mounting on government to find other sources of revenue to replace the projected decline in revenue from the SACU revenue.

9.0 Conclusion

Over the past 20 years, rising government expenditure has not translated to meaningful job creation, and economic growth, as Namibia still ranks among the countries with highest unemployment at 51%, highest income inequality at 0.6 and rising poverty. If government expenditure could not halt unemployment rising from 37% in 2000 to 51% in 2008, what has significantly changed in the components of government expenditure to enable the 2011/12 budget create 104 000 jobs over the next three, translating into 35000 jobs created annually from 2011. We view the new intervention economic programme TIPEEG as very weak in its current form and we do not foresee any tangible employment created by allocations to the programme in the 2011/12 budget. We believe that fragmented policy and uncoordinated decision making in government can lead to duplication of effort, wastage of financial resources, wasted time and contradictory outcomes.

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