Fiscal Space for Children: An Analysis of Options in Namibia

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Preface

This *Fiscal Space Analysis* is part of a series of country studies carried out by Ecorys for UNICEF between 2016 and 2018, in various sub-Saharan African economies. As such, it aims to provide a better understanding of the role of political economy factors in processes and decisions around the creation and use of fiscal space for investments in children in Namibia. It is published jointly with its sister publication *Namibia: Political Economy Analysis*.

The report was written by a team of Ecorys staff and consultants headed by Ecorys Project Director Ivo Gijsberts and including consultants Jonathan Wolsey and Corrado Minardi. It is based on literature review and a five-day fact-finding mission to Windhoek, Namibia carried out by Ronald Rateiwa and Mmamoletji Oniccah Thosago of DNA Economics – a South Africa-based consulting firm. However, due to timing and logistical constraints, they could not manage to meet with all the stakeholders they had planned to. Nonetheless, the writers are confident that the report captures a sufficient reflection of the current political economy processes and decisions around fiscal space for investments in children in Namibia.

The writers of this report wish to thank UNICEF Namibia Country Office staff in Windhoek, in particular Ernest Mbangula for their support. They also express gratitude to the various Government of Namibia officials and representatives of non-governmental entities for generously taking time to meet with the consultants.

The content of this report does not reflect the official position of UNICEF. Responsibility for the information and views expressed in the report lies entirely with the author(s).

List of abbreviations

AfDB:	African Development Bank
AIDS:	Acquired Immunodeficiency Syndrome
CIT:	Company Income Tax
CMA:	Common Monetary Area
CoE:	Compensation of Employees
DFI:	Development Finance Institution
ECD:	Early Childhood Development
FSA:	Fiscal Space Analysis
GDP:	Gross Domestic Product
HIV:	Human Immunodeficiency Virus
IMF:	International Monetary Fund
JSE:	Johannesburg Stock Exchange
MGECW:	Ministry of Gender Equity and Child Welfare
MoE:	Ministry of Education, Arts and Culture
MoF:	Ministry of Finance
MoHSS:	Ministry of Health and Social Services
MTEF:	Medium Term Economic Framework
NDP:	National Development Plan
NGO:	Non-Governmental Organisation
OECD:	Organisation for Economic Co-operation and Development
OVC:	Orphans and Vulnerable children
PIT:	Personal Income Tax
PHC:	Public Health Care
PTMC:	Prevention of Mother-To-Child Transmission
SACU:	Southern African Customs Union
SARS:	South African Revenue Services
SDGs:	Sustainable Development Goals
TB:	Tuberculosis
UNAIDS:	United Nations Programme on HIV/AIDS
UNESCO:	United Nations Educational, Scientific and Cultural Organization
UNICEF:	United Nations Children's Fund
USD:	United States Dollar
VAT:	Value-Added Tax
WEO:	World Economic Outlook

Executive Summary

The centrality of young people to the achievement of Sustainable Development Goals (SDGs) cannot be overemphasised, given that children under the age of 15 years make up more than 26%[1] of the world population. This global phenomenon is even more pertinent in Africa where 43%[2] of its population is under the age of 15 years[3]. In Namibia, the focus of this report, children under the age of 15 years make up 37% of the population[4]. A young population can both be an opportunity and a risk. **Therefore, effective, child-focussed programmes and policies must be prioritised**.

In this regard, UNICEF is playing a key role in advocating for and supporting the development of policies and programmes that enhance the wellbeing of children in Namibia. To advance this mission, **UNICEF has commissioned a fiscal space analysis (FSA) to understand past trends in expenditure on child-friendly priorities and estimate the future fiscal capacity needed to increase this type of priority expenditure in the education, health, and social welfare sectors**. The FSA has been carried out as a fiscal-projection exercise using historical data on government spending. Projections are formulated based on various assumptions that together constitute a "scenario" linked to the historical database. Scenarios are based on an analysis of the different policy options that influence the size of priority expenditure. In the case of the Namibia country study, priority expenditure was deemed to be equal to expenditure on education, health and social welfare in the absence of a detailed breakdown of historical budget data.

Economic growth in Namibia has slowed down following a decrease in the mining and other sectors around 2015. The decline in economic growth was coupled with a decrease transfers from the Southern African Customs Union (SACU), the country's largest source of revenue. These reductions in revenue, coupled with a weakening currency that is pegged to the struggling South African Rand, and an extended period of high rates of government spending increases has led to rising deficits and debt.

In response to these challenges, **the government has implemented a fiscal consolidation policy, expected to reduce non-priority expenditure while also ensuring efficiency expenditure towards priority sectors**. As a result**,** Namibia's budget is under pressure, including priority sectors.

In addition to an economic slowdown and constrained fiscal position, priority sectors are also faced with problems of allocative efficiency. With increasing demand for basic social services considering a rapidly rising population, there is an urgent need to increase the efficiency of spending to achieve better results with limited resources. Currently, the country's priority expenditure is higher in education and health, with social welfare being allocated less than 3.5% of total expenditure. It is advisable to both increase the proportion of total budget allocated towards priority sectors and enhance the effectiveness of priority spending. For instance, although the number of children enrolled in schools has increased, drop-out and repetition rates are still high in secondary education. The Namibian government is spending more towards secondary education learners, although low pass rates in secondary schools could be ascribed to low quality education

1 (World Bank, 2018a).
2 (World Bank, 2018a).
3 (United Nations, 2017).
4 (World Bank, 2018a).

provided at early childhood development and primary school. Similarly, a greater focus on primary, rather than curative, healthcare could also result in improved outcomes for the same level of spending.

In the short to medium term, Namibia's economic growth is not expected to be as high as prior to the slowdown, when GDP growth was frequently over 5%. The real-GDP average growth rate is assumed to be 2% over the projection period of 2016/17 to 2021/22 as per IMF's WEO forecast. Under the baseline status-quo scenario, assumptions would produce no significant changes in the fiscal structure as the real economy grows. Under a set of neutral, non-controversial assumptions, priority expenditure increases as a percentage of total expenditure, but decreases as a percentage of GDP. Per child priority expenditure would decrease slightly from US$1,541 in 2016/17 to US$1,482 in 2021/22. The average net internal debt flow would be 2.9 per cent of GDP, which indicates the Government could realize this scenario with moderate levels of internal borrowing. Overall, this would lead to sustained fiscal deficits, which would decline marginally from 7.5 per cent of GDP in 2016/17 to 7.1 per cent of GDP by 2021/22.

A promising option to reduce the fiscal gap in the country is to improve tax administration efficiency. Over the past few years, tax revenue has increased as a proportion of GDP. In 2009/10 tax revenue was recorded at 25.91% of GDP which then increased to 28.53% in 2015/16[5]. Nevertheless, the Namibian government believes that substantial improvements in the efficiency of tax collection can still be achieved. Namibia is currently in the process of establishing an independent revenue agency to further enhance tax administration and therefore collection. Assuming that, as planned, Namibia establishes a tax revenue agency, and this leads to growth in VAT, CIT and PIT collection rates. VAT, CIT and PIT would grow at the same rate as nominal GDP, and tax revenue would gradually increase over time from growing at the same rate as nominal GDP in 2016/2017 to growing 1.3 times faster (30%) by 2021/22.

Namibia's priority expenditure as well as its fiscal gap are heavily affected by the attained level of GDP growth. A scenario based on an assumption of Namibia increasing its economic growth is thus modelled. The scenario assumes increased GDP growth as a result of growth in the mining and construction sectors supported by government support and growth in global demand. The scenario assumes an average growth rate of 4.2% from 2016/17 to 2021/22, with growth rising incrementally to a high of 5.0% in 2021/22.

Attracting external grants to increase priority expenditure is unlikely for Namibia. Recently, donor grants have been declining, which is ascribed to Namibia being reclassified from a middle-income country to an upper middle-income country. Besides the country's income status affecting grants, another challenge is global economic conditions and political pressure in some developed nations to reduce international aid. These factors limit the chances that donors provide additional aid to middle-income countries such as Namibia.

Namibia's credit rating has recently been downgraded for multiple reasons, including its debt levels. Although extensive borrowing could potentially provide some relief in the short-term, in the long-run Namibia's increase in external debt could amplify negative economic shocks. Therefore, it is not suggested that the country should borrow extensively. The country is aware of these risks and it has sought to bring public debt on a sustainable path.

[5] (World Bank, 2018).

On average, about 30% of Namibia's revenue is from SACU transfers. Thus, a decrease in SACU transfers impacts Namibian revenue negatively. Namibia has raised its concerns on SACU transfers' fluctuations, with a decrease in transfers impacting the country's expenditure plans. A scenario shows the significant deteriorating effect of lower SACU revenue transfers on expenditure, budget deficits and the trajectory of debt. Priority expenditure would decrease from U$1,541 in 2016/17 to U$1,482 in 2021/22, while total government debt would increase by 3.7% in 2021/22.

Just as economic growth can drive fiscal space expansion, a decrease in GDP will drive a contraction. In addition to domestic issues, Namibia is very vulnerable to South Africa's economic performance; through SACU revenue and other mechanisms. With the current economic and political uncertainty in the country, lower GDP growth remains a legitimate concern in Namibia that requires contingency planning.

Fiscal space analysis is an important instrument available to UNICEF to influence decisions and protect funding in its priority sectors. UNICEF could interact with the government regarding resource allocation and balancing the composition of expenditures, particularly for prioritising children's health, education, and social welfare. In this regard, this report along with the quantitative tool provided can be an important tool to improve the effectiveness of the dialogue.

1 Introduction and methodology

1.1 The objective of the Fiscal Space Analysis (FSA)

UNICEF has commissioned a study to develop a methodological approach and carry out a projection exercise that UNICEF can use to inform its on-going dialogue with the government and other stakeholders regarding the "fiscal space" for expenditure essential for children. For this study, the fiscal-space concept simply means the flow of fiscal resources available for spending on children's needs. The concept is central in UNICEF's dialogue with the authorities: for the medium term, UNICEF would focus on ensuring as high a growth rate as possible for child-beneficial spending, subject, essentially, to two constraints: first, the need to ensure that the economy maintains sufficient capital formation to ensure sustained real-GDP growth; and, second, the need to ensure macroeconomic stability.

1.2 Methodology

1.2.1 Definition of priority expenditure

This report refers to expenditure categories regarded as beneficial to children as "priority" expenditure. For Namibia, such priority expenditure categories for children comprise the following three "institutional" expenditure categories: (i) education; (ii) health; and (iii) social welfare.

The composition of the government's priority expenditures for children is, inevitably, somewhat arbitrary. Government expenditure classified as "priority" includes aspects that are unrelated, or only loosely related, to children's welfare, such as gender equity, arts and culture. At the same time, some expenditure categories classified as non-priority are highly relevant to children, notably, for example, in the water and sanitation sector. This is especially important to bear in mind when considering possible scenarios to enhance priority expenditure by reducing non-priority expenditure. Future analyses of this kind may work with different definitions of priority expenditures for children. Even so, the methodological approach used in this study could work in the same way. That is, the methodological approach is the fundamental recommendation.

It is also important to bear in mind that fiscal space discussion concerns only expenditure carried out by government within its budget. Government expenditure on education and health plainly constitutes the bulk of the resources dedicated to education and public health in Namibia. Much of this expenditure is in categories that only the government carries out or could carry out. Nevertheless, non-governmental expenditure in these sectors is also significant. Especially in the health and social welfare sectors, some important programmes are funded by private and NGO entities, some of which receive donor support. These would not be included in the government budget. The present focus, however, is the expenditure flows in the priority sectors that flow through Namibia's fiscal accounts and hence are recorded "on budget."[6]

[6] While it would be possible to carry out the kind of analysis this chapter describes using an enhanced set of accounts going beyond the official budget accounts, it may prove challenging to identify and incorporate all relevant expenditure programs and funding sources.

A final note refers to one of the key measures used in the FSA to examine and compare both historical spending and the variation in priority expenditure under different scenarios, namely priority spending per child. This measure takes the total spending in the priority expenditure categories and divides this by the total number of children aged 19 or younger in Namibia. The figures on per-child priority spending obtained in this way are to be treated with caution since only a proportion of total expenditure at the institutional level benefits children directly.

1.2.2 Priority expenditure identity and analysis

Fiscal identity

Priority expenditure (Education, Health and Social Welfare)

=

Tax and non-tax revenue

+ External grants

+ External debt disbursements

+ Net internal financing flows

- External debt service

- Non-priority expenditure

- Internal interest expenditure

To analyse fiscal space for priority expenditure, the methodology first sets from the "identity" that governs the relationship of priority spending with its underlying fiscal space.

This identity states that total expenditure (comprising current, non-interest, interest, and capital expenditure) less the sum of total revenue and external grants is equal to the overall deficit, which is in turn equal to the net flow of external and internal financing. If total expenditure is broken down into the three categories of (1) priority and (2) non-priority non-interest expenditure and (3) interest expenditure, this identity can be rearranged for any year as shown in the box.

The "below-the-line" accounts taken together constitute fiscal space for the priority-expenditure flow. For a retrospective analysis – that is, for analysis of fiscal performance in historical years – this structure can be applied directly to show how the below-the-line flows (the retrospective fiscal space) combined to finance the priority expenditure flows. Section 2 describes the historical quantitative analysis for Namibia, for the years FY2011/12-FY2016/17.

For the projection analysis, the accounting identity is applied in a different way. For each projection year, the priority-expenditure flow is projected based on programming assumptions, encompassing the various determinants of recurrent and non-recurrent expenditure in the education, health, and social welfare categories. Similarly, the below-the-line accounts, except for the net internal financing flows, are projected based on programming assumptions. The total net internal financing flow for each year is then calculated residually, to ensure that the accounting identity is satisfied.

For any projection year, this net internal financing flow is the fiscal space "gap", that is, the difference between the projected priority-expenditure flow and the projected financing requirements. If this gap is "too large," then the programming assumptions, taken together, would be considered unfeasible. The criteria for "too large" include the limits on the government's capacity to borrow in domestic financial markets and the implied increase in the government's debt-GDP ratio. Policy-makers would presumably want to avoid having the net internal borrowing flow as a percentage of GDP exceed nominal GDP growth in coming years, to prevent the internal-debt stock from rising as a percentage of GDP.

The projection exercise is formulated by applying various assumptions, together constituting a "scenario" to the historical data base. The relatively simplified, illustrative projection exercise applies scenarios to historical data (as discussed in Appendix 1). Each scenario comprises programming assumptions for the years FY2017-18 to FY2021-22, covering:

- world economic conditions;
- basic Namibian macroeconomic variables;
- merchandise exports and imports;
- tax and non-tax revenue;
- external grants to the government;
- government expenditure in the priority and non-priority categories; and
- external and internal debt.

For each scenario, some of the assumptions are set as simple numbers (growth rates, percentages of GDP, etc.). Many of the assumptions, however, are constructed from other assumptions. For example, the growth rates of real GDP and of the price level are numbers that the analyst chooses based on projections by either the World Bank or IMF. It is straightforward to combine these assumptions into an assumed growth rate for nominal GDP.

1.2.3 Data description and limitations

This analysis is based on budgetary data covering actual figures (budget outturn) for the Fiscal Years (FY) 2011/12- 2016/17. The main data source is the Ministry of Finance (MoF). Additional data sources include the Namibian Bank, UNICEF, as well as the World Bank/IFC and the IMF. Despite a substantial data-collection effort, the quantitative analysis presented in the sections below is subjected to an important caveat. Namely, data on spending in the priority-expenditure categories is limited. Functional level breakdown of data was not available in more detail, in particular, associated expenditures classified under the economic budget classification could not be obtained. Thus, as noted before, for the modelling exercise, which investigates aspects such as increases in staff levels, priority expenditure categories were taken to be those of the main government institution responsible for the respective area. Since detailed data were not available for more detailed expenditure categories, it was not possible to produce more refined definitions and calculations for scenarios involving relevant sub-categories.

1.3 Organization of the FSA

The remainder of this report is organized as follows. Chapter 2 summarizes Namibia's present macroeconomic and fiscal circumstances. It also analyses the budgetary process and the general efficiency of the fiscal framework. Chapter 3 looks at the recent evolution of priority expenditure flows in the categories of priority expenditure and outlines some specific challenges in the various areas relevant for expenditure on children. Chapters 4 and 5 discuss various options available to policy makers to enhance fiscal space with an illustrative projection exercise for the priority expenditure flows and fiscal space that would fund them for the years FY2017/18-FY2021/22. The exercise consists of a base scenario (Chapter 4), comprising a broad range of macroeconomic and fiscal policy assumptions, and various alternative scenarios. Chapter 5 presents the main findings from the analysis. Further projection details are included in Appendix 1.

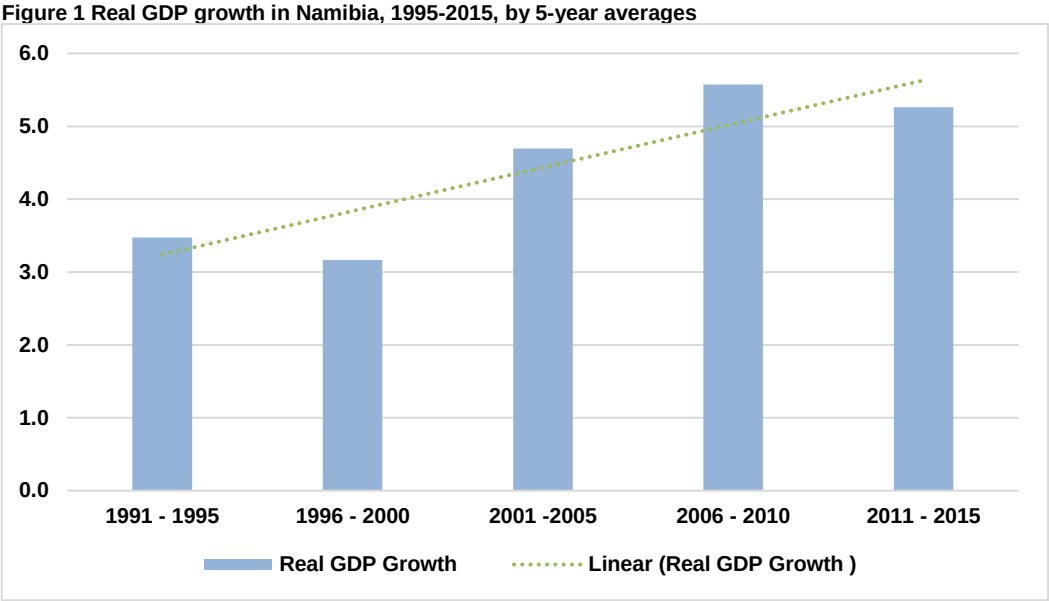
2 Namibia's macroeconomic and fiscal context

2.1 Longer-term national economic trends

2.1.1 Economic Growth

Figure 1 below shows Namibia's average growth trend in the 25 years leading to 2015[7]. It shows that **Namibia has experienced a growth trajectory, recording modest GDP growth in the pre-millennium period, followed by a period of accelerated growth**.

Figure 1 Real GDP growth in Namibia, 1995-2015, by 5-year averages



Source: World Bank (2018), WDI (2018).

Namibia's long-term growth trend is characterised by two phases. The first phase commences soon after Namibia gains independence from South Africa lasting for 10 years. The second phase sees Namibia move into a decade and a half of accelerated growth as investment into the mining and manufacturing sectors start paying economic dividends.

Phase 1: Namibia's economic growth performance in the pre-millennium period is often referred to as the post-independence adjustment period, following the country's formal independence from South African control in March 1990.[8] During the first 5 years of post-independence, real GDP growth averaged 3.5 percent. It then slowed in the subsequent period (between 1996 – 2000), averaging 3.2 percent – a trend ascribed to Namibia's structural make up as a commodity export driven economy[9]. The combination of weak global growth and a low commodity price cycle weighed significantly on growth performance.

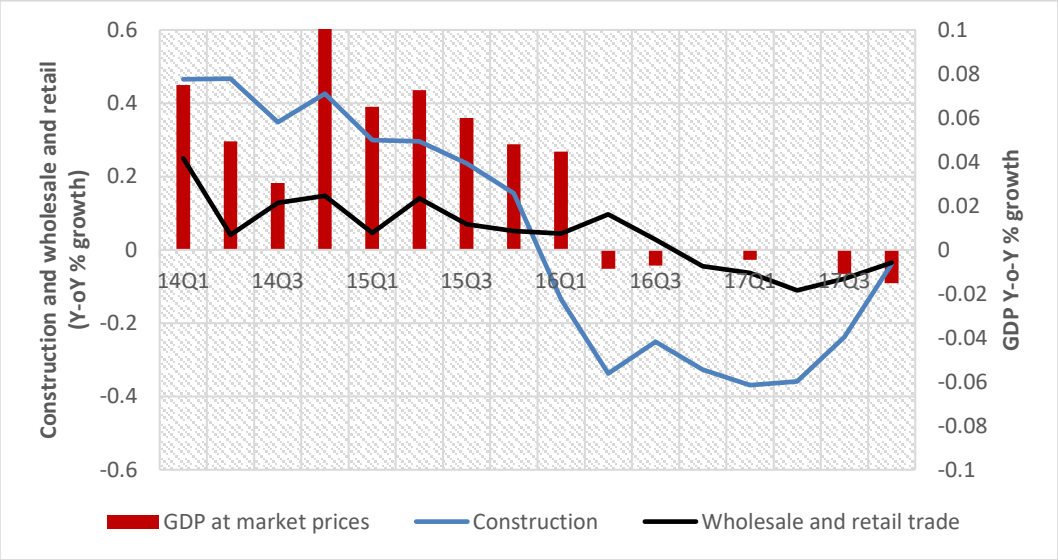
Phase 2: Rapid growth of the mining sector, including increased diamond and copper production volumes, higher commodity prices, as well as continued investment into new mining projects such as Anglo American's investment in the Skorpion zinc mine and refinery,[10] contributed to accelerated average growth of 5 percent between 2001 and 2005. The following period saw growth rise to an average of 6 percent, ascribed to the continued scale-up in mining production as well as robust

7 Averages calculated for the 5-year period to each plotted year (average growth 1991 – 1995, etc.).
8 (Republic of Namibia, 2016).
9 (Bank of Namibia, 2002).
1010 (Bank of Namibia, 2002).

manufacturing and agricultural activity.[11] The growth during this period was particularly impressive at it was achieved during a period in which the world economy was significantly constrained by the effects of the global economic crisis in 2008. Indeed, Namibian real GDP growth was as high as 5.3% between 2011 and 2015.

However, the country then experienced a severe economic slowdown, with real GDP growth recorded at 1.1% in 2016 and -1.2% in 2017. The economic decline resulted largely from a decline in commodity prices and hence mining activities, followed by declines in other sectors. Figure 2 shows that the significant decline in economic growth (using quarterly numbers) was associated with a significant deterioration in two of Namibia's most important sectors, i.e. construction and retail.

Figure 2 Quarterly real GDP growth (%) in Namibia and sectors year-on-year growth

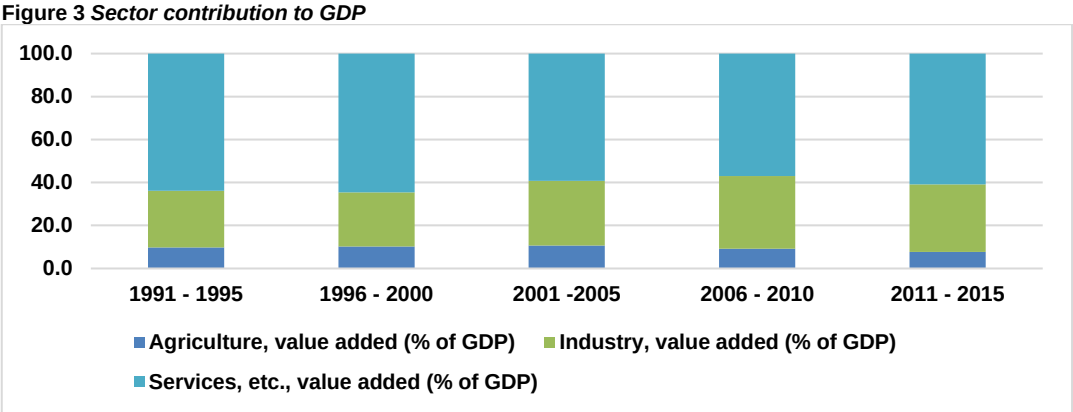


Source: Authors' own based on data from Namibian Statistics Agency.

2.1.2 *Structure and characteristics of the national economy*

The structure of Namibia's economy has seen limited transformation over the years, as shown in the chart below. The services sector has declined over the years, but only modestly. From as much as 64.6% of GDP from 1996 to 2000, its share reached 60.9% from 2011 to 2015.

Figure 3 *Sector contribution to GDP*



Source: World Bank, WDI.

[11] (Republic of Namibia, 2016).

As a percentage of GDP, industry's share has grown over the years, from a low of 25.1 percent (between 1996 and 2000) up to 33.7 percent (between 2006 and 2010), before declining somewhat to 31.5 percent (between 2011 and 2015). The government of Namibia has remained committed to growing this sector, manufacturing, considering its multiplier effects from an employment and value-addition perspectives. Apart from private and public sector investment, the government has over the years introduced packages of tax and non-tax incentives for new and existing manufacturing enterprises.[12] Indeed, while the government has sought to "*revolutionalise all aspects of the manufacturing process*"[13], this has not been without its challenges. In addition to ebbing foreign direct investment, the shortage of skills within the sector is among the issues faced within the sector.

Meanwhile agricultural output as a percentage of GDP has declined over the years, from a high of 10.7 percent (2001-2005) to 7.6 percent in the most recent period. While Namibia has a much lower proportion of subsistence farmers (40 percent), relative to a country like Swaziland where subsistence farming accounts for 70 percent, the risk of food insecurity remains pronounced.

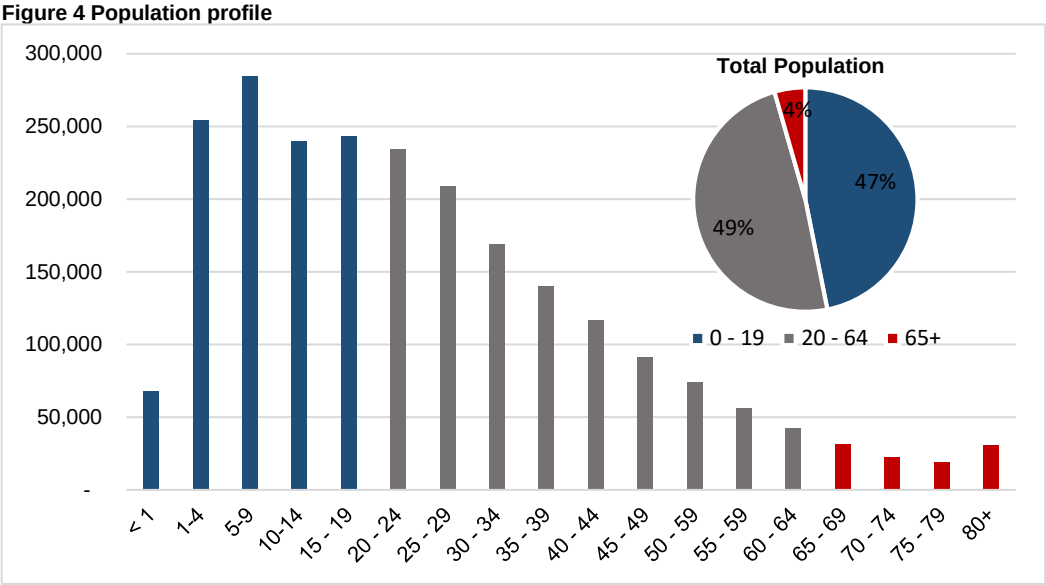
In response to the slowdown in growth and decreases in government revenue, the government decided to implement a fiscal consolidation strategy, as discussed in detail in section 2.3 below. Government itself acknowledges that it took difficult decisions to implement some of the deepest expenditure cuts since Independence, which may generate adverse effects on the economy[14]. A sharp contraction was also observed in wholesale and retail trade, the tourism sector and public administration, for this and other reasons. Other tertiary sector activities also registered a significant slow-down since 2016. The contraction in domestic demand also resulted in significant reduction of the credit and deposit growth, and hence financial intermediation generally. On the external front, an additional negative impact also emanated from the economic slow-down in Angola[15].

2.1.3 Demographic trends

Figure 4 below shows that amongst Namibia's population of 2.3 million, there is an almost equal split between the child population and the working age population. Using UNICEF's classification of children, which encompasses all individuals up to the age of 19 years, the child population is estimated at 47 percent, which is marginally lower than the labour force population of 49 percent. However, when using the standardised measure[16] of the working age population, this group is estimated at just under 60 percent of the population, while the child population is estimated at 36.4 percent. Nevertheless, the population structure clearly points to a high proportion of young adults that currently (and will continue) dominate the working age population, a trend the country could leverage to realise economic growth. There are, however, a number of structural issues that pose a risk to achieving this objective.

12 (Republic of Namibia (b), 2016).
13 National Planning Commission, n.d.
14 (Geingob, 2018).
15 (World Bank, 2018).
16 Using the classification where working age population constitutes all individuals between 15 years and 65 years.

Figure 4 Population profile



Source: Namibia Statistics Agency (2018).

2.1.4 Poverty, inequality and unemployment

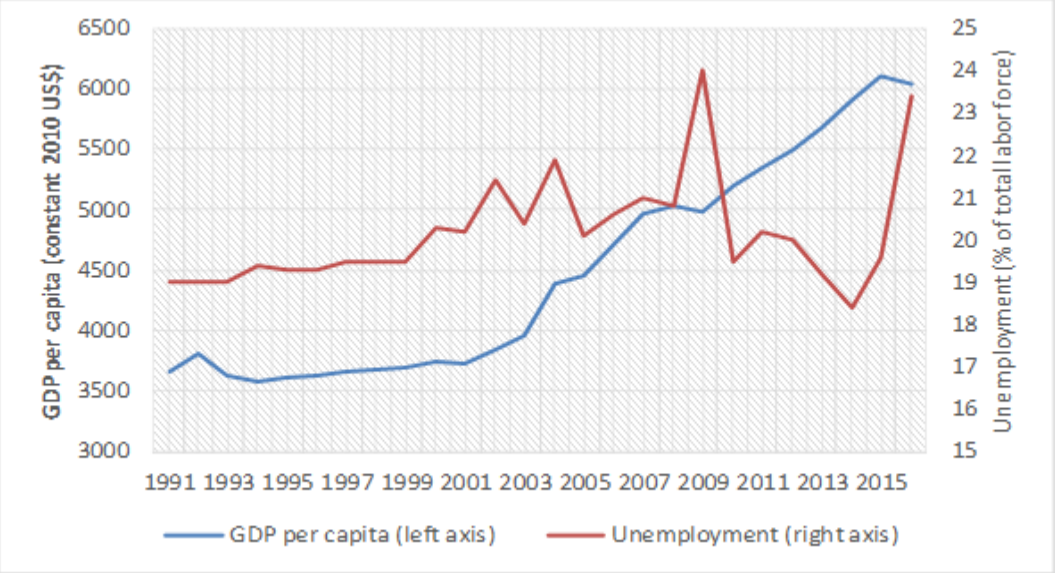
Unemployment in Namibia is high and has been rising recently and is one of the key economic challenges facing the country. Using the broad definition, Namibia's unemployment rate rose to 34% in 2016, from 27.9% in 2014.[17] The rate of unemployment is higher in rural areas (39.2%) relative to urban areas (just over 30%). This is significant given that more than half of Namibia's population dwells within rural areas.

Much like its neighbouring countries, Namibia is faced with high rates of inequality, unemployment, HIV incidence and poverty. If left unaddressed these social challenges are likely to undermine the country's growth potential. The government has consequently placed socio-economic transformation as one of the main pillars under the National Development Plan (NDP). Its main objective is to "build capable and healthy human resources"[18] While in some respects there is evident improvement in core indicators, there remains significant scope for further improvement.

Economic growth has also not been inclusive and has not generated sufficient jobs to meaningfully reduce inequality. Figure 5 below shows that while real per capita income almost doubled between 1991 and 2015, from US$3600 to more than US$6000, unemployment has also increased somewhat from 19% to 23%. One reason identified for this lack of inclusivity is that the structure of economic production and trade has remained heavily linked to extractive and related industries, with little transformation towards job-creating sectors or economic activities such as value-chain development.

[17] (Namibia Statistics Agency, 2016).
[18] (Republic of Namibia, 2017, p. 49).

Figure 5 Real per capita income vs unemployment



Source: Own analysis based on data from WDI (2017).

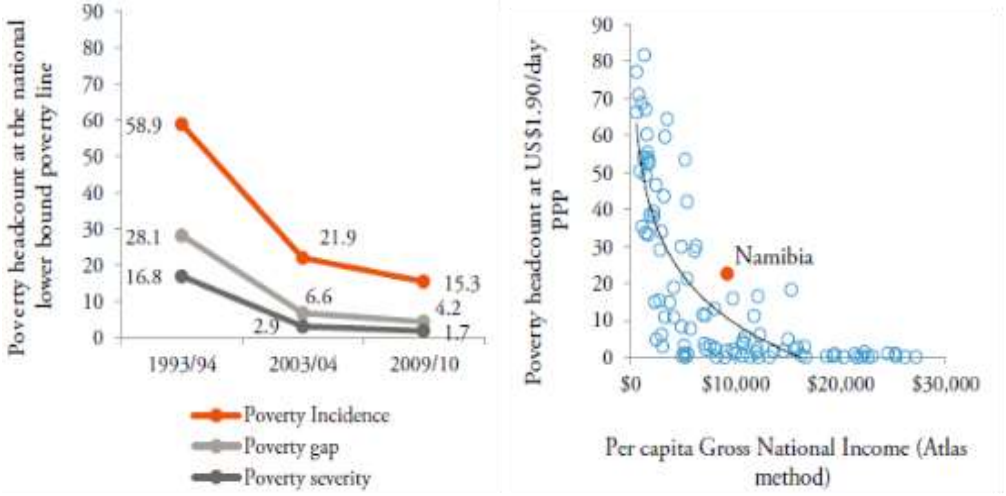
Among other factors, unemployment has a direct and pervasive effect on the level of poverty. National statistics show that poverty is particularly pronounced among children in Namibia. It is estimated that 34 percent of children live below the poverty line, when compared to the national average of 28.7 percent for the entire population.[19] This implies that children are likely to be disproportionately affected by Namibia's high unemployment rate.

While structural factors such as unemployment contribute to a lower quality of life among children, high rates of HIV also play a key role. While the national HIV prevalence has declined over the years, currently at 14 percent from 22 percent[20] in 2002, the high incidence rate and number of deaths among young adults remain high. This, consequently, contributes the high child dependency[21] (of 69.1 percent)[22] as well as the increasing the number of Orphans and Vulnerable children (OVC) (which stood at an estimated 153 745, 18 percent of the child population).

The combination of high unemployment and high HIV prevalence rates has exacerbated inequality. Figure 6 shows that although poverty incidence in Namibia has declined, the level of inequality is still very high compared to other countries with similar levels of per capita income. Namibia's Gini coefficient of 61.0% implies that the country has the second highest level of income inequality globally (see
Figure 7), with 10% of the population earning 51.8%[23] of national income. Furthermore, the decline in poverty has been principally the result of fiscal transfers rather than gains in employment. A recent study showed that only 30 percent of households in the bottom four income deciles depend on salary, wages, or a pension from previous employment as their primary source of income. Instead, their income comes mainly from subsistence farming or the receipt of social grants, drought relief, and/or private transfers[24].

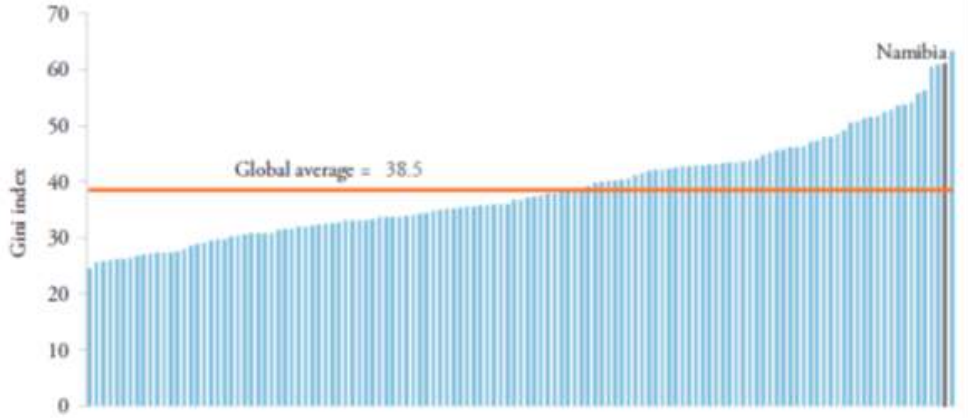
19 (OECD Namibia, p231 (p3).
20 (UNAIDS, 2018).
21 The dependency ratio is defined as the ratio of children aged 0-14 and persons aged 65 years and older per 100 persons in the age group of persons aged 15-64 years old (core working age group). (Namibia Statistics Agency, 2016, p. 28).
22 (Namibia Statistics Agency, 2016).
23 Accessed from http://wdi.worldbank.org/table/1.3 on 30 May 2018.
24 (World Bank, 2017:7).

Figure 6 Poverty incidence relative to per capita income



Source: (World Bank, 2017:5).

Figure 7 Inequality in Namibia is second highest in the world



Source: (World Bank, 2017:6).

2.2 Recent Macroeconomic Performance

2.2.1 Inflation and exchange rate

Namibia's economic performance has also been affected by its strong economic and historical association with South Africa – which has exposed it to a number of risks. Together with Lesotho, Swaziland, and South Africa, Namibia falls under the Common Monetary Area (CMA). Established in 1986[25], this monetary union was created primarily with the view of complementing the free trade mechanism throughout the Southern African Customs Union (SACU). As such, each of these respective economies have a fixed currency peg to the South African Rand, making their currencies susceptible to South Africa's exchange rate performance. The Rand has depreciated substantially against the dollar for a long period of time.

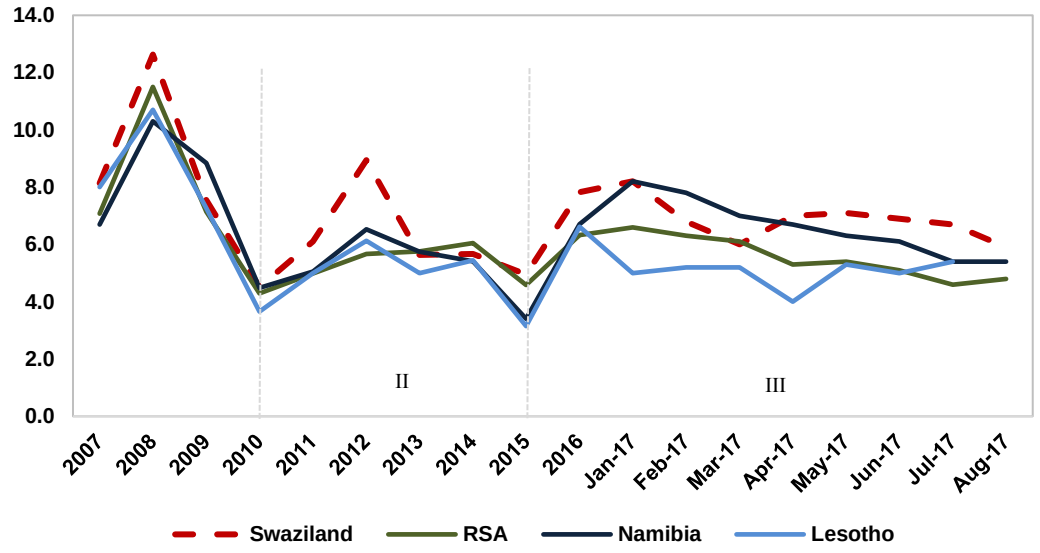
Given the currency arrangement within the Common Market Area (CMA), monetary policy is effectively guided by the South African Reserve Bank's (SARB) policy. Figure 8 below presents inflationary trends within the CMA. CMA Inflationary trends over the last decade can be summarised in 3 phases:

[25] The CMA has its roots established in the Rand Monetary Area (RMA) 1974, which was later revised in 1986, to form what is now known as the CMA (IMF, 2018).

- **Phase I (2007-2010):** Effects from the global financial crisis saw inflation within the region rise to heightened levels last seen in the early 2000s;
- **Phase II (2010-2015):** The period between 2010 and 2015 saw inflation peak at 9.6% in 2012, off the back of rising administered prices within the region. The initial oil price downturn in 2015 contributed to a moderation in inflation in the subsequent years;
- **Phase III (2016 – 2017):** The low oil price environment continued to provide some reprieve to oil importers. Effects of lower fuel prices, and the associated translation into the transport component of the CPI basket lowered inflationary pressures. Nevertheless, rising food prices, off the back of severe drought conditions, offset the disinflationary effects from the transport component to overall CPI, giving rise to higher inflation.

The SARB's monetary policy has been consistent with its objective of guiding and maintaining inflation within a 3 – 6% target band, and thus an interest rate hike cycle was instituted in Phase I. However, with the delicate balance of promoting economic growth – the SARB adopted an accommodative monetary policy stance in Phase II, followed by a tightening cycle in Phase III.

Figure 8 CMA inflation (2007 – 2017)

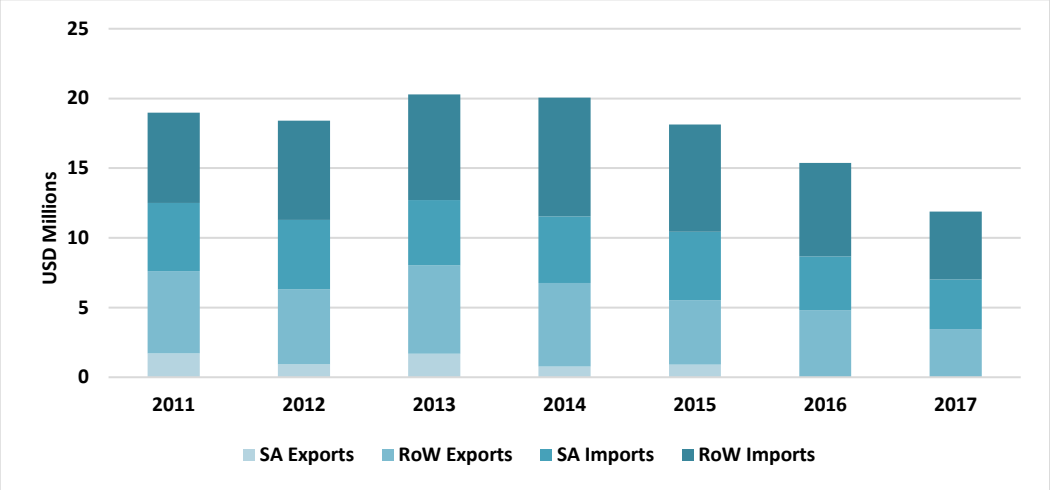


Source: World Bank, WDI.

2.2.2 *International Trade*

Figure 9 below presents a breakdown of Namibia's trade profile in terms of origin of exports, and destination of imports. It shows that South Africa remains Namibia's major trading partner: South Africa exports between 13% (2016) and 29% (2011) to Namibia and Namibia imports between 57% (2017) and 76% (2011) from South Africa. This is mainly due to the structural arrangement within the SACU, in which South Africa makes the largest economic contribution to the union (both in terms of imports and exports). The union's dependence on South Africa's large economic contribution consequently places the customs pool at risk of fluctuations associated with South Africa's growth performance. South Africa as the largest partner leads to other partners having significant dependence on South Africa. This presents economic risks, especially revenue risks, whenever South Africa's economic growth fluctuates

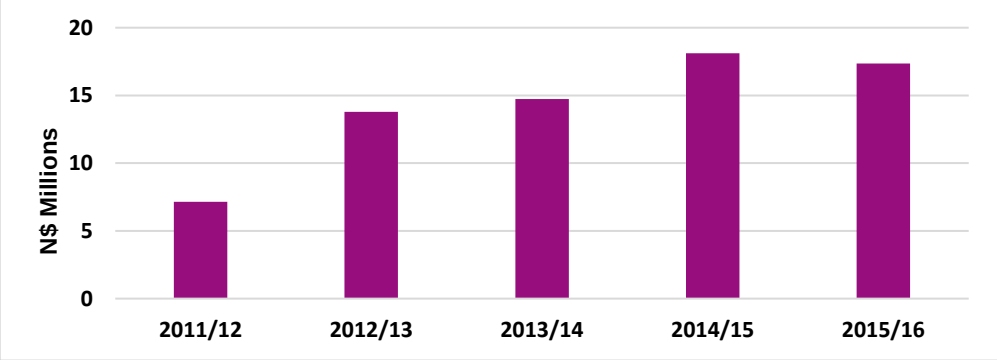
Figure 9 Trade profile (by source)



Source: Authors' own based on data from ITC – Trade Map.
Note: SA Exports – exports from SA to Namibia, RoW Exports – exports from the rest of the world to Namibia, SA Imports – Namibian exports to SA, RoW Imports – Namibian exports to the rest of the world.

Figure 10 presents Namibia's customs and other import duties, including SACU revenue for the period 2011/12 to 2015/16 financial years.

Figure 10 Customs and other import duties (SACU Revenue)



Source: Authors' own based on data from (Ministry of Finance, 2018).

2.3 Recent fiscal performance

Until recently, Namibia has been able to maintain a healthy fiscal position by generally balancing government expenditure and revenue. Although public debt as a percentage of GDP increased between 1995 and 2004 from 20.3 per cent to 29.4 per cent, through a series of budget surpluses, it recovered substantially over the next 6 years to reach 16.3 per cent in 2010.

Following this period, Namibia embarked on a period of expansionary fiscal policy which saw government expenditure increase substantially over the next 5 years. Although the policy boosted economic growth and resultantly, government revenue, the increase in revenue was not enough to avoid substantial budget deficits. During this period, public debt as a percentage of GDP more than doubled from 16.3 per cent in 2010 to 40.3 per cent in 2015. This sudden increase in public debt has brought with it substantial increases in the cost of debt service which is currently putting severe pressure on the government's budget. The sections below provide further discussion on the specific dynamics that have brought Namibia to its current position.

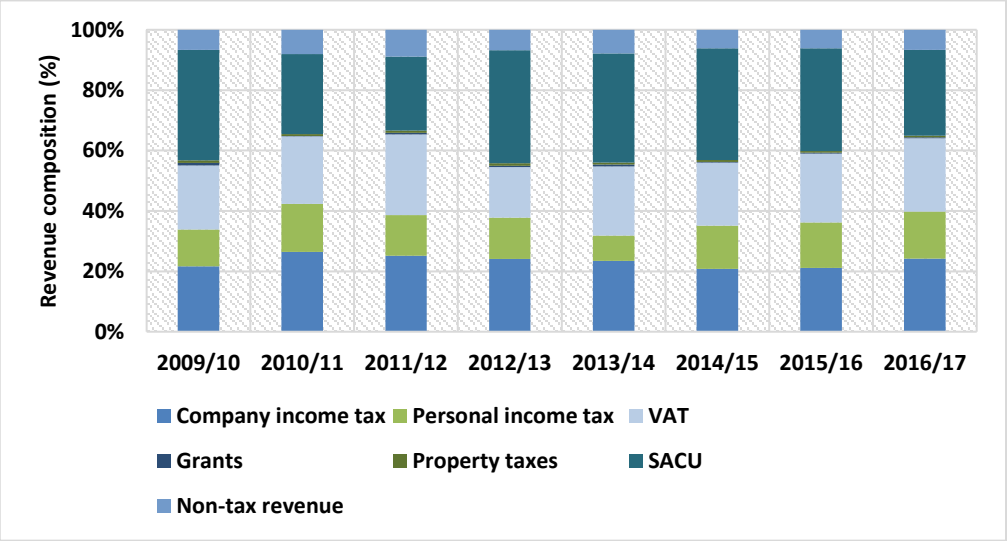
2.3.1 *Revenue performance*

Income from SACU remains Namibia's largest revenue source and contributed an average of 30% of total revenue between 2010 and 2017. As a result, whenever the SACU region in general, or South Africa as its largest economy, experiences economic slowdowns, Namibian revenue is meaningfully negatively impacted. Dependence on SACU revenues thus presents a risk to Namibian fiscal stability, as it does to the other smaller countries in the union. Currently, a stabilisation fund or reserve is being designed at the regional level to account for SACU revenue fluctuations impacting member states.

Besides SACU revenue, Company Income Tax (CIT), Value-Added Tax (VAT), and Personal Income Tax (PIT) are the most significant revenue sources for Namibia. Figure 11 presents the composition of Namibian government revenues for the period FY2009/10 to FY2016/17. In FY2016/17, CIT revenue was 24.3% (N$12 million), while that of VAT was 24,2% (N$11,9 million) and personal income tax contributed 15,6% (N$7,7 million). Over the past 5 financial years, the split between revenue contributors have been consistent, except for SACU transfers which decreased significantly in FY2015/16.

Other Namibian revenue sources are grants, property taxes, and non-tax revenue. Grants provided to Namibia decreased during the period under review. On the other hand, the contributions of property tax and non-tax revenue have increased. In FY2009/10, grants amounted to 1% of total revenue, which then decreased to 0,4% in FY2012/13 and 0,3% in FY2016/17. Namibia was recently re-classified from a lower-income country to an upper middle-income country. This improvement in classification tends to negatively impact external donors' contributions, who often want to focus support to the poorest countries. UNICEF Namibia specifically raised this as a concern in relation to the UN and other global donors[26].

Figure 11 Composition of government revenues



Source: (Ministry of Finance, 2018).

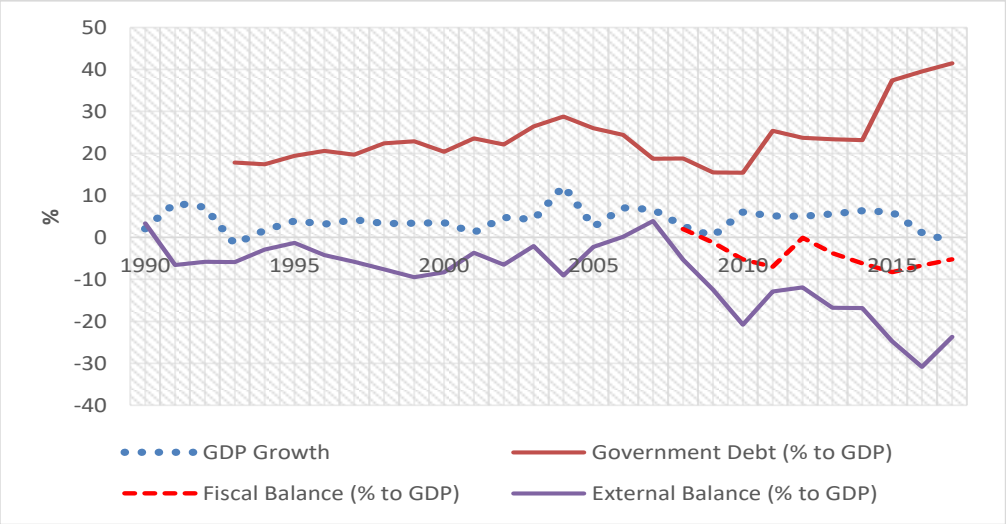
Tax revenue has typically increased at a higher rate than nominal GDP, with total revenue increased in all years up to FY2015/16, before declining y a 2.6% decline in FY2016/17. Namibia is currently in the process of establishing an independent revenue agency to further enhance tax administration and therefore collection. Assuming successful implementation, this is expected to increase especially the collection of CIT, PIT and VAT revenue.

[26] UNICEF Namibia interview held on 17th April 2018.

2.3.2 *Government debt (external, internal)*

Figure 12 shows how Namibia's reduced economic growth rates since 2015 have led to an increasingly negative fiscal balance and an increase in the debt stock as a percentage of GDP. The resultant increase in debt servicing cost is putting significant further pressure on the fiscus.

Figure 12 Worsening fiscal position in Namibia



Source: Own analysis based on data from WDI, MTEF 2018-21 and *https://tradingeconomics.com/namibia/government-budget*.

In general, government debt has been on the rise post-global financial crisis (see Figure 13 below), although initially debt was managed fairly well. A year after the global financial crisis, Namibia increased its foreign debt repayments/services. However, the spike in foreign debt servicing was once-off and the country thereafter stabilised its foreign debt repayments.

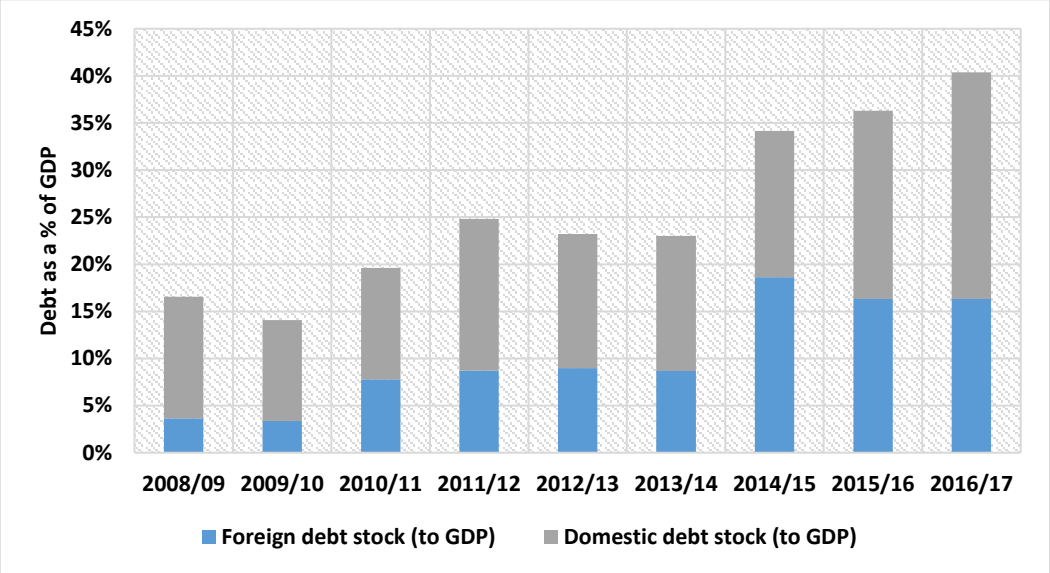
In response to the recent regional economic slowdown, deficits and debt increased substantially as revenues declined. Most significantly, lower SACU revenues resulted in a significant decline in overall revenues. Public debt stock increased from 23% to GDP in 2013/14 to 40% to GDP in 2016/17. High debt levels have led to Namibia's credit rating being downgraded by international agencies, creating further challenges for the Namibian fiscus as investor confidence decreased.

Both domestic and foreign debt has increased, although the increase in foreign debt is particularly concerning due to Namibia's currency peg to the South African rand and hence its inability to stabilise its own currency. By 2016/17, the amount of domestic debt was still 50% larger than foreign debt in 2016/17, but foreign debt had risen to 16% of GDP (with domestic debt at 24%). The foreign debt stock increased from 9% to 19% of GDP in one year from 2013/14 to 2014/15 due to the issuance of two Johannesburg Stock Exchange (JSE) bonds worth N$750 million[27]. In general, foreign debt comes largely through funding from the African Development Bank (AfDB)[28] and the bank is projected to keep funding Namibia through development loans designated for education and health.

[27] New Era. 2016. N$143 billion national debt… so what?

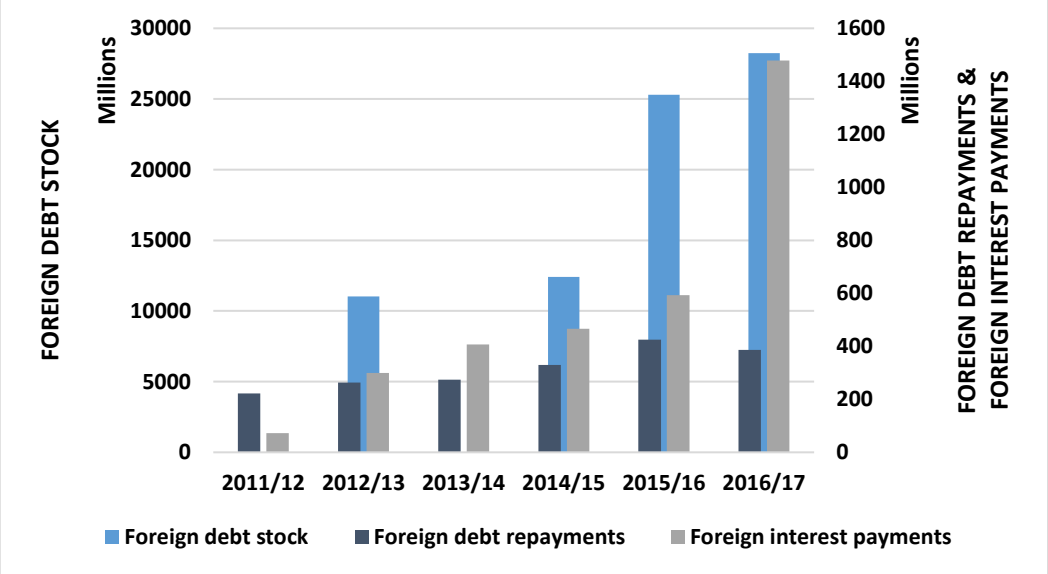
[28] Deloitte. 2018. Namibian Mid-Term Budget Review 2017/18 – 2019/20.

Figure 13 Namibian foreign and domestic debt stock



Source: (Ministry of Finance, 2018).

Figure 14 Namibian foreign debt stock and foreign debt repayments



Source: (Ministry of Finance, 2018).

2.3.3 *Expenditure performance*

The Namibian government sought to resolve their fiscal constraints by implementing a medium-term fiscal consolidation plan. Government authorities implemented reductions in non-priority expenditure, particularly non-wage expenses and capital outlays. The consolidation programme is intended to be '*growth-friendly*' with the objective to reduce the budget deficit and public debt, while increasing the capital budget. The increased capital budget is envisaged as the mechanism through which growth will be achieved despite the contractionary fiscal policy.[29]

It is hoped that, in the years following implementation of a consolidation plan, the economy will improve and then allow less austere fiscal policy. Growth expectations are centred on an increase in mining activities, drought recovery in the country and region, increase in construction activities and manufacturing recovery[30]. Despite these expectations, government authorities are

[29] Deloitte. 2018. Namibian Mid-Term Budget Review 2017/18 – 2019/20.

[30] (International Monetary Fund, 2018).

wary that the fiscal deficit should be contained within budget projections to avoid further arrears accumulation[31].

According to the fiscal strategy for the Medium-Term Economic Framework (MTEF) 2018-21, fiscal consolidation is expected to be achieved by doing the following:

- Stabilizing growth in public debt at about 42 percent of GDP, through a combination of reduction in the budget deficit, leveraging alternative forms of financing and implementing structural policy reforms;
- Gradually reducing the budget deficit from the excess of 8.3 percent of GDP in FY2015/16 to 6.3 percent FY2016/17 and further achieving a steep reduction to 3.6 percent of GDP in FY2017/18 with the expressed objective of reaching budget balance by FY2019/20; Average budget deficit was projected to 2.3 percent of GDP over the FY2017/18 – 2019/20 MTEF;
- Targeting expenditure reduction on non-core operational expenditure items such as overtime allocation, furniture, office equipment and vehicles, material supplies and subsistence travel for reallocation and postponement of non-productive capital expenditure, especially the expenditure allocations for office buildings for which no contractual obligations have been set;
- Leveraging alternative forms of financing to support infrastructure development and capital formation through sovereign guarantee to Public Enterprises, Development Finance Institutions (DFIs), and through Public, Private Partnerships; and
- Promoting private sector development through structural policy reforms and financing by DFIs.

Table 1 Total government expenditure FY2009/10 to FY2016/17

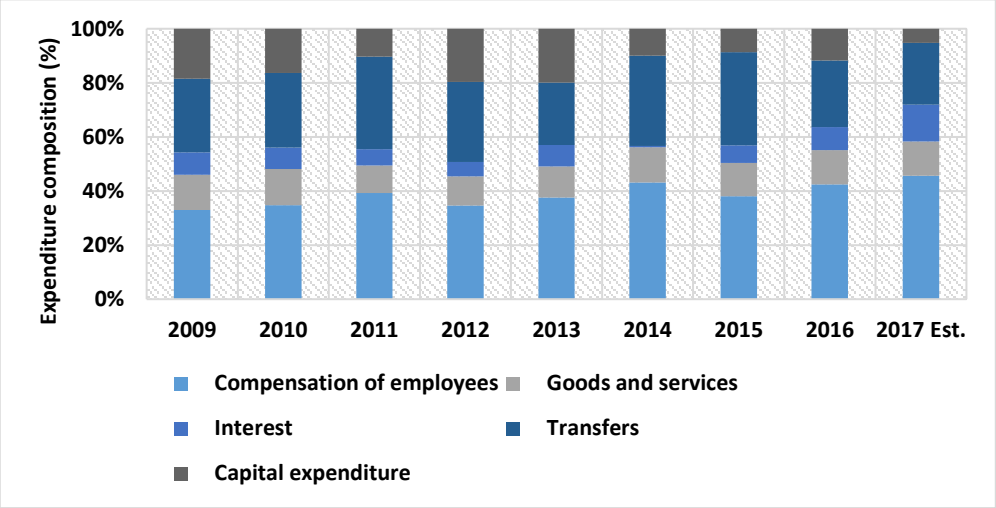
Fiscal year	09-10	10-11	11-12	12-13	13-14	14-15	15-16	16-17
Total government non-interest expenditure (NAD billions)	24.9	27.3	35.5	36.4	45.0	53.8	62.0	57.8
Growth rate year on year (%)		9.4%	30.2%	2.6%	23.6%	19.7%	15.2%	-6.8%

Source: (Ministry of Finance, 2018).

As shown in Figure 15, decreasing total expenditure has led to substantial changes in the composition of expenditure since 2015. As expenditure decreased, compensation of employees (CoE) increased as a share of total expenditure. This is common in times of fiscal consolidation, as it is not easy or even possible to reduce CoE in the short to medium term. Capital expenditure and transfers have seen the greatest reductions. These reductions risk having a potential negative impact on growth rates and delays in providing important infrastructure for the social sectors, but it is not clear whether reductions have yet had meaningful impacts in this regard.

[31] (International Monetary Fund, 2018).

Figure 15 Composition of government expenditure



Source: (Ministry of Finance, 2018).

As would be expected, interest payments have also increased due to increased debt level. Interest spending has increased significantly from 7% of total expenditure in 2015 to 14% in 2017. The economic downturn has constrained tax revenue and increased the borrowing requirement. The increased borrowing has been further exacerbated by a depreciating currency over the period (largely outside the country's control), leading to increased debt servicing costs. This has put further pressure on expenditure which in turn, may lead to increased borrowing.

Breaking out of this vicious cycle is the key fiscal challenge facing the country. Declining SACU revenues coupled with a persistent fiscal deficit, government resources being extensively dedicated to personnel, downgrades ('junk status' ratings), growing government debt and constrained fiscal space present government with the need to introduce stringent public expenditure prioritisation to maintain Namibian fiscal sustainability.

2.4 Looking forward

The above sections have outlined several fiscal challenges. The first is that as much as 30% of Namibia's revenue is from SACU transfers. This exposes the country to SACU fluctuations and the economic performance of the larger member states. Mitigating SACU transfer risks would require the country to lower expenditure when SACU transfers are low and increasing savings when they are high. According to interviews conducted with the MoF, the country is planning to implement a stabilisation fund or reserve for SACU transfers.

The second challenge is the reduction in donor grants. While donor funding has never been particularly large in recent times, the country will still have to find alternative revenues to replace grants. Additionally, these grants would have to be earmarked for priority sectors.

The third challenge is that of returning to higher levels of economic growth. The Namibian government has sought to reduce inefficient expenditure, prevent a further credit downgrade, reduce public debt, and improve economic growth by introducing a fiscal consolidation policy. The policy however seems to have brought forth the unintended consequence of reduced economic activity.[32] The FY2017/18 Appropriation Amendment Act was implemented to redress government

[32] (Tralac, 2018).

spending arrears without compromising budget implementation.[33] The country's GDP could however increase in the future if key economic sectors were to be revived, in particular the mining sector. Therefore, once the economy is stabilised, and these sectors start to once again contribute meaningfully to economic activity, an economic recovery is possible.

A key revenue reform being implemented is the introduction of a tax administration agency. The establishment of that agency aims to improve tax administration efficiency and consequently tax revenue and overall government revenue.

[33] (Tralac, 2018).

3 Priority expenditure trends and policy challenges

This chapter highlights the evolution of priority expenditure looking specifically at growth over time, and the composition of expenditure. It also looks at the specific issues observed within each priority sector for UNICEF.

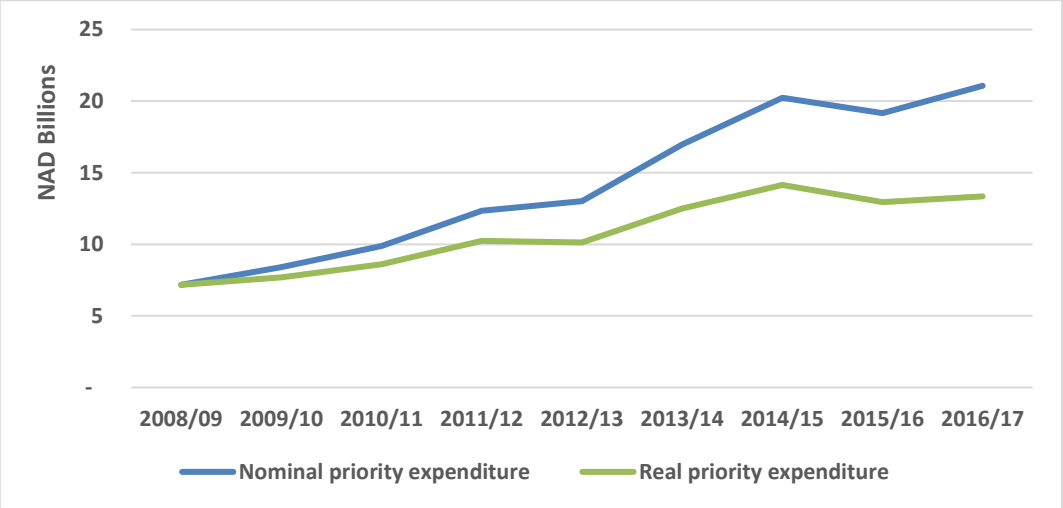
This report defines to priority sectors as categories for children which comprise the following three activities: (i) education; (ii) health; and (iii) social welfare. In practice, this means that all expenditure within the Ministry of Ministry of Education, Arts and Culture (MoEAC)[34], the Ministry of Health and Social Services (MoHSS) and Ministry of Gender Equity and Child Welfare (MoGECW) will be defined as priority expenditure. Note that not all this expenditure focuses on children, but available data does not make it possible to only isolate child related expenditure.

3.1 Priority expenditure in recent years

3.1.1 Recent evolution of priority expenditure

During the period 2008/09 to 2016/17 priority expenditure increased in both nominal and real terms, as shown in Figure 16. In real terms, priority expenditure increased from R7,1 billion in 2008/09 to R13,3 billion in 2016/17 (in 2008/09 prices), an average annual real growth rate of 8.1%. Priority expenditure did however decline in 2015/16, as a result of the national economic slowdown, increasing debt and deficit levels and of the contractionary fiscal policy being then implemented.

Figure 16 Priority spending increased over the period under review (2008/09 – 2016/17)



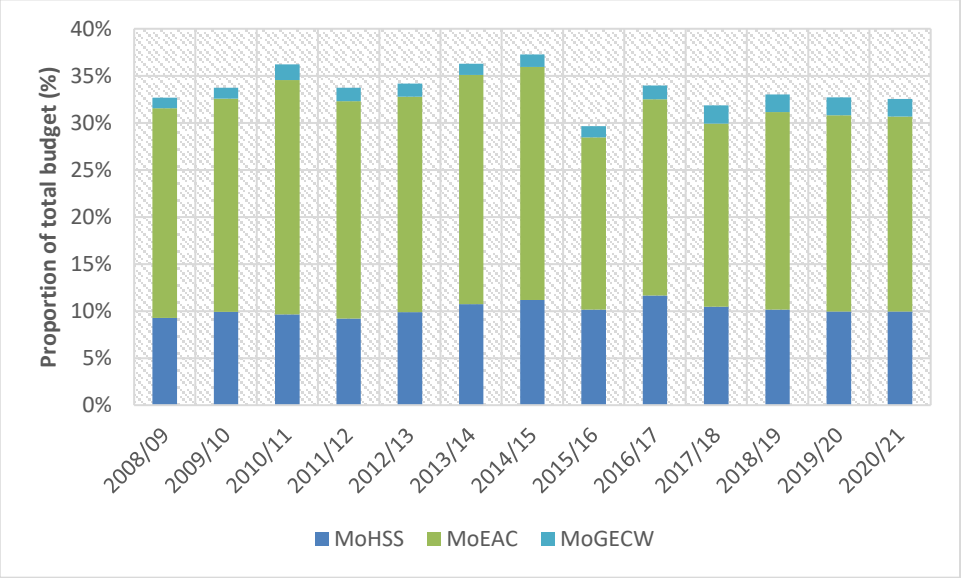
Source: Authors' own calculations based on data obtained from MoF.

The share of priority expenditure has remained relatively constant as a proportion of government expenditure in recent years. As shown in Figure 17, total priority expenditure, as a percentage of government expenditure, increased from 32% to 37% between 2008/09 and 2014/15, then declined significantly to slightly below 30% in 2015/16, before stabilising at around 32% in the most recent years (including the most recent MTEF budget). The priority expenditure reduction in

[34] Note that the Ministry of Higher Education Training and Innovation is not included in this estimate, and hence the focus here is on basic education.

2015/16 was largely a result of the reduction in the MoEAC budget, the largest priority sector, in which transfers and subsidies were reduced significantly in response to budgetary pressures.[35]

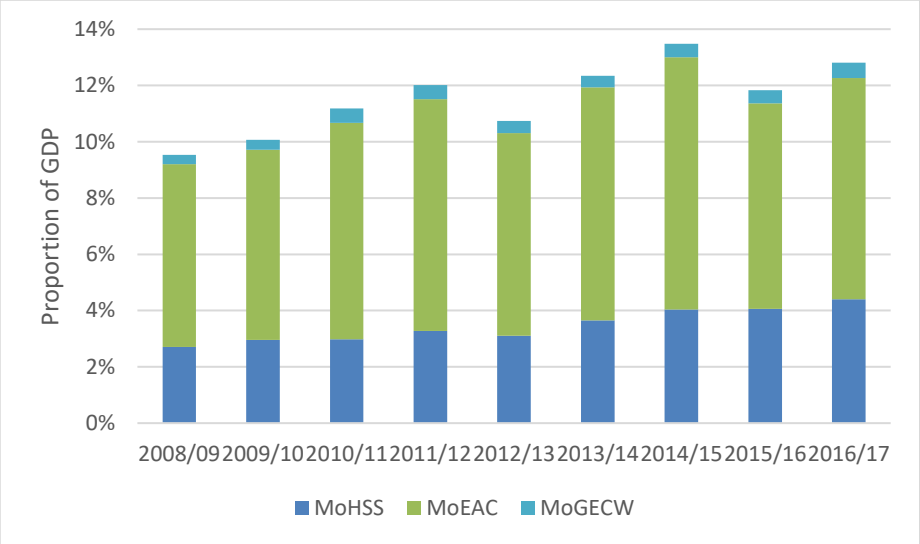
Figure 17 Government priority expenditure has been between 30% and 37% of government spending



Source: Authors' own calculations based on data obtained from MoF.

Priority expenditure also rose significantly as a percentage of GDP, from about 9.5% in 2008/09 to 12.2% in 2016/17. This increase is largely the result of increasing overall government expenditure as a percentage of GDP, rather than a specific focus on increasing priority expenditure. Between 2008/09 and 2016/17 overall government expenditure grew at 7.6% in real terms, compared to a similar 8.1% real growth rate in priority sectors. As the government continues its fiscal consolidation strategy in the coming years, it will be important to monitor the extent to which the government is able to maintain priority expenditure as a proportion of GDP.

Figure 18 Priority sectors as a percentage of GDP



Source: Authors' own calculations based on data obtained from MoF.

The UNESCO Dakar Framework for Education for All recommends that 9% of GDP be spent on education. Although Namibia was able to achieve an education allocation of 9.3% of GDP in

[35] The absence of programme level data means that it is not clear what proportion of these reductions were seen in Education relative to Arts and Culture.

FY2014/15, this has decreased since on reaching 7.7% of GDP in FY2017/18[36]. The country's education budget allocation therefore almost meets the target. Nonetheless, there are concerns about budget allocations within education, as discussed in section 3.2.1 below.

Namibia's health expenditure as a percentage of GDP is also substantially below the Abuja Declaration in which the African Union countries pledged to spend at least 15% of their total expenditure on health care. Since 2012/13 Namibia has typically been spending slightly more than 10% of its total budget on health, up slightly from earlier years.

3.1.2 Fiscal space in recent years

This section briefly contextualises priority spending within the broader fiscal environment in the country. To this end, the table below summarises the trends in priority expenditure between FY2011/12 and FY2016/17 - expressed as a percentage of GDP. It essentially summarises the available fiscal space by showing how other components of revenue and expenditure influence (or are influenced by) priority expenditure.

The following can be inferred from the table on how priority expenditure has been financed:

- **Tax and non-tax revenue (excluding external grants) has been relatively stable over the period as a percentage of GDP**, although it declined somewhat in the most recent years as a result of declines in SACU revenues and the wider economic slowdown. This revenue decline should be interpreted considering the significantly decline in GDP growth in these years (see section 2.2 above), with the aggregate effect of these two factors being a significant decline in real tax revenues;
- **External grants account for a small proportion of financing** (only approximately 0.1% in most years), implying that external funding does little to stabilise or offset changes in government revenues. It is unlikely that there will be a significant rise in grants going forward, since the country recently acquired middle-upper income status, which limits the country's grant financing options;
- **Total non-priority expenditure has also been stable as a percentage of GDP** but will likely need to be reduced in the coming years if priority expenditure is to be maintained in the current fiscal climate;
- **Net external financial flows increased significantly to 7.6% in 2015/16**, showing the significant increase in external debt that was required to maintain spending levels.

Table 2 Priority expenditure for children and its fiscal space FY2012/13 to FY2016/17 (% of GDP)

Fiscal year	FY11/12	FY12/13	FY13/14	FY14/15	FY15/16	FY16/17
Per cent of GDP						
Total priority expenditures for children	**12.0%**	**10.7%**	**12.3%**	**13.5%**	**11.8%**	**12.8%**
Total education (MoEAC) expenditure	8.2%	7.2%	8.3%	9.0%	7.3%	7.9%
Total health (MoHSS) expenditure	3.3%	3.1%	3.7%	4.0%	4.1%	4.4%
Total social development (MoGECW) expenditure	0.5%	0.4%	0.4%	0.5%	0.5%	0.5%
Overall fiscal space	**12.0%**	**10.7%**	**12.3%**	**13.5%**	**11.8%**	**12.8%**
Tax and non-tax revenue (excl. external grants) (+)	28.9%	31.2%	30.6%	33.2%	32.2%	30.8%

[36] (UNICEF Namibia, 2017).

Fiscal year	FY11/12	FY12/13	FY13/14	FY14/15	FY15/16	FY16/17
Per cent of GDP						
External grants (+)	0.2%	0.1%	0.2%	0.1%	0.1%	0.1%
Total non-priority non-interest expenditure (-)	-22.5%	-19.3%	-20.4%	-22.4%	-26.5%	-22.3%
Net external financial flows (incl. external interest) (+)	0.4%	2.7%	-0.2%	0.5%	7.6%	0.9%
Net internal financial flows (incl. internal interest) (+)	**5.0%**	**-4.0%**	**2.1%**	**2.1%**	**-1.6%**	**3.3%**

Source: Authors' own calculations based on data obtained from MoF.

3.2 Overview priority sector successes and challenges

This section discusses the key spending and performance issues in each of the priority sectors in turn.

3.2.1 Education

Since attaining independence in 1990, Namibia has made great strides in ensuring that education is accessible to all. Enrolment increased by 59% from 462,350 in 1992 to 733,603 learners in 2017. However, despite this achievement, the sector still faces a number of problems, some of which are heightened under the current contractionary fiscal policy. One of the systemic problems raised by the Ministry of Education, Arts and Culture (MoEAC) during interviews is that the presence of critical present challenges makes it difficult to proactively plan for inevitable future challenges. The MoEAC therefore find that budget proposals for proactive preventative policies and plans are often rejected by Treasury as the available funding is primarily absorbed by more time-sensitive current problems in the sector. This problem is clearly illustrated by the lack of a formalised school infrastructure maintenance plan. Consequently, repairs are by default favoured over maintenance, resulting in many environments not conducive to learning.

Learner performance remains a concern, particularly in maths and science. For instance, in 2015, only 45% of Grade 5 students achieved the expected proficiency level in English while 63% of Grade 5 students achieved proficiency in Mathematics. Grade 7 learners fared even worse with just 48% and 41% achieving proficiency in English and Mathematics respectively. At the secondary level, 30% of the students repeat the grade and more than one-third of all students drop out by Grade 10. The transition from secondary to higher education is very low currently estimated at 19% of the grade 12 cohorts. In the most remote, rural areas, drop-out rates are an area of concern. Only 49% of first graders in extremely remote areas still attend school in Grade 5.[37]

The challenges confronting the education sector in Namibia can be grouped into three categories, namely quality, funding and access.

a. Quality

Interviewees suggested that many teachers are not sufficiently trained and capacitated, with more than 20% of teachers having no teaching qualification[38]. UNICEF is currently assisting the Ministry of Education with the development of National Standards and Performance Indicators for schools[39]. This programme intends to make schools more accountable for outcomes. Some

[37] (Patriot, 2018).
[38] (Republic of Namibia, 2017).
[39] Interview with the MoEAC on 20 April 2018 in Windhoek, Namibia.

believe that performance and accountability is not demanded from educators, so there is not sufficient pressure to improve. Teacher absenteeism is also said to be widespread[40]. This programme has faced resource constraints in the past but, according to UNICEF, is currently back on track. This programme is essential as the prevalence of unqualified and underqualified[41] teachers at early stages of learning (Early Childhood Development, Pre-Primary and Primary) has also led to repetition and drop-out rates increasing exponentially as learners proceed to higher grades.

b. Education Funding

In terms of funding, Table 3 shows that primary education takes the biggest proportion, followed by secondary education.

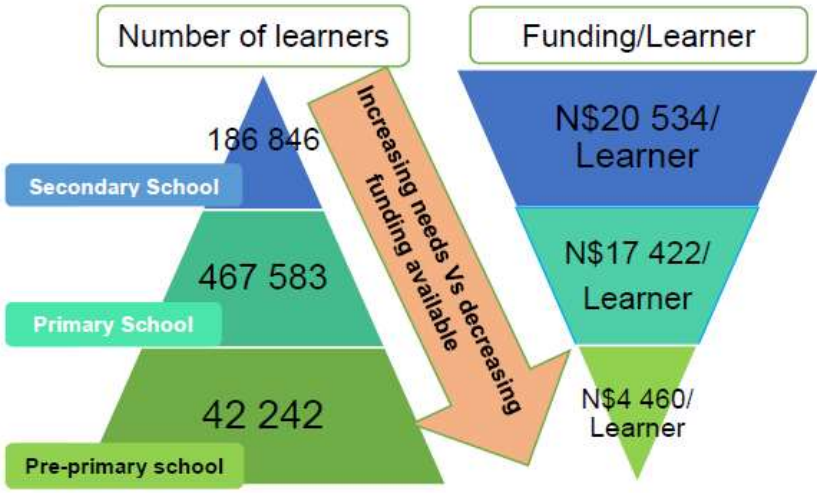
Table 3 Allocation of funds to education programmes

	2017	2018	2019	2020	2021
Programme Quality Assurance	0.1%	0.2%	0.2%	0.4%	0.1%
Primary Education[42]	63.0%	64.3%	61.8%	62.5%	63.0%
Secondary Education[43]	29.6%	28.2%	30.4%	29.8%	29.3%
HIV and Aids Monitoring Unit	0.0%	0.0%	0.0%	0.0%	0.0%
Pre-Primary	1.5%	1.2%	1.5%	1.5%	1.6%
Building and Infrastructure	0.7%	0.5%	1.0%	0.5%	0.8%
Others	5.1%	5.5%	5.1%	5.3%	5.2%

Source: MTEF 2018-21.

However, when these allocations are compared to the number of learners at the respective levels, primary education appears relatively less well funded, as shown in Figure 19. Analysis suggests that the current funding model for Namibia is potentially inversely related to the needs of the sector. One of the major challenges raised is that the pre-primary and primary phases of education in Namibia are not strong, resulting in poor outcomes at secondary and tertiary levels. However, the current budget ceilings per learner at secondary school is double that of those at primary, and eight times more than those in pre-primary school.

Figure 19 Structure of enrolment relative to government expenditure[44]



Source: Own analysis based on data from MTEF 2018-21 and UNICEF.

[40] Interview with Klaus Schade on 18 April 2018 in Windhoek, Namibia.
[41] Primary school qualified teachers were moved to secondary schools without upgrading their qualifications and skills set.
[42] Grades 1-7.
[43] Grades 8-13.
[44] Spending per learner was calculated using 2017 MTEF estimates and projected 2017 enrolment numbers. 2017 enrolment number were obtained by projecting 2016 figures by the past 10-year average enrolment growth rates.

Figure 19 shows that while there are about 186 000 secondary school learners, which account for about 27% of total enrolment, each learner is allocated more than 48% of total funds available for all learners at pre-primary, primary and secondary. At the same time, primary school learners who account for more than 67% of total enrolment, are allocated only about 41% of funds available for all learners at pre-primary, primary and secondary. Such an inverse relationship between funding and the number of learners compromises the education outcomes especially at secondary level where drop-out rates are very high because learners are not prepared for secondary school due to low quality primary school. Government has added an additional grade (Grade 13) with the hope of mitigating the effects of poor primary education by increasing the time available for completing secondary education. Such an intervention does however not address the potential root cause of poor education outcomes, which is a weak primary phase.

Improving Early Childhood Development (ECD) has not been a spending priority within the MoEAC and recent budget increases have largely focused on personnel salary and wages in primary and secondary phases. In aggregate, wages accounted for 87% of MoEAC expenditure in FY2017/18.[45] Personnel remuneration being dominant in overall expenditure is not unique to Namibia, with other regional countries like South Africa and Swaziland experiencing similar challenging in controlling the growth of these items.

c. Access to education

Given Namibia's geographically sparsely populated nature, a challenge faced by the education sector is to attain the minimum threshold enrolment in each school without having to force learners to travel very long distances. The dispersed population requires that more resources are needed per child as government either must build more schools or expand the hostel system to accommodate children that live in remote areas. This is complicated by the fact that learner numbers have increased significantly from 462 350 in 1992 to 733,603 learners in 2017, yet the budget has not increased. Schools are resultantly often under-resourced with specific shortages in the areas of infrastructure maintenance and investment. Table 3 above shows that infrastructure is allocated less than 1% of the department's annual budget. In addition, because of bureaucracy and corruption, infrastructure costs are often inflated, resulting in only a small proportion reaching the ground for actual construction.

3.2.2 Health

Namibia has significantly reduced maternal and neonatal mortality. Both infant and under five mortalities have declined. HIV/AIDS rates in pregnant women have reduced from a peak of 22% in 2002 to 16.9% in 2014. Antenatal services are available in all health facilities in the country, resulting in 87% of all births occurring in health facilities and 88% attended to by skilled birth attendants. Immunization coverage has improved substantially throughout the NDP4 period (2013-2017).[46]

A national nutrition programme has helped lower the prevalence of stunting from 29% in 2006 to 24% in 2014. The percentage of mothers who feed their infants through breastfeeding has grown to 48% in 2013 from 23% in 2006. Prevalence of iron deficiency anaemia is 22% in women and 48% among children. While there has been success in fighting communicable diseases, such as TB and Malaria, non-communicable diseases accounted for 43% of the 14,000 total deaths in 2012. As of 2015, Namibians had a Health Adjusted Life Expectancy of 58 years.[47]

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45 Comment based on stakeholders' interviews.
46 (Republic of Namibia, 2017).
47 (Republic of Namibia, 2017).

Despite these success stories, a number of challenges still exist in the health sector in Namibia. These are discussed further below and include:

- Financing for preventative and curative expenditures;
- Quality of service;
- Expenditure efficiency; and
- Access.

Table 4 below provides an overview of programme expenditure by the MoHSS over the Medium-Term Expenditure Framework (MTEF). **Analysis of expenditure shows that less than 1% is directly allocated to primary (largely preventative) healthcare services**. This is very small compared to what is allocated to curative services, although this report takes note that referral and regional health services may include primary healthcare components/activities as well, although it is likely be a relatively small proportion. This issue was further confirmed by the MoHSS which indicated that on average, the department spends 60% of its budget allocation towards curative healthcare. The preventative allocation is said to be approximately 5% in total, despite the health priority needs in primary health care. At the time of writing this report, the ministry had trained 1 200 healthcare providers that could render community health education and campaigns, however, 649 of these are not deployed due to budget constraints. This misalignment between national priorities and the financing framework is likely to adversely affect health outcomes and the lack of primary health care (PHC) expenditure is likely to negatively impact the efficiency of total expenditure.

Table 4 Programme expenditure MoHSS

	2017	2018	2019	2020	2021
Referral Hospital Services[48]	27.7%	25.0%	30.0%	30.0%	29.8%
Regional Health and Social Welfare Services[49]	39.5%	38.4%	41.5%	42.0%	41.8%
Primary Health Care Services[50]	0.8%	0.8%	0.5%	0.5%	0.5%
Others	32.0%	35.8%	28.0%	27.5%	27.9%

Source: MTEF 2018-2021.

A second challenge is expenditure inefficiencies that result from uncoordinated programmes. The MoHSS interviewees stated that there is little, or no vertical integration of programmes designed to benefit the same patient. For instance, Prevention of Mother-To-Child Transmission (PTMC), immunisation, nutrition and family planning may be administered by different programmes, yet they are targeting the same mother and child. This increases programme overheads, leaving fewer resources for the actual programme delivery.

Access to health facilities is a third challenge. Ease of health access in Namibia varies between urban and rural areas, with rural residents often lacking access due to longer distances to their nearest health facilities. According to the MoHSS, there are 280 physical clinics in the country, and within every 25km there should be a physical clinic. However, due to the low number of households in remote rural areas (especially in southern regions), clinics in rural areas being further apart than the ideal 25km. The MoHSS provides mobile clinics which visit remote rural areas at least every 2 to 4 weeks. Although this alternative model should significantly improve access to health services, current budget constraints present transportation constraints for

[48] To provide curative and specialised services to patients referred from regional and district hospitals and to develop and strengthen the skills and knowledge of health workers through clinical training.

[49] To improve the quality of life by rendering services through programs in the field of Family Health, Epidemiology, Public and environmental health, disability prevention and rehabilitation as well as information, education and communication.

[50] Development of strategies to prevent and manage diseases, injuries and other health conditions through surveillance of cases and promotion of healthy behaviours. To ensure that Namibia has an efficient public health system with programs aimed at reducing incidences of disease outbreaks.

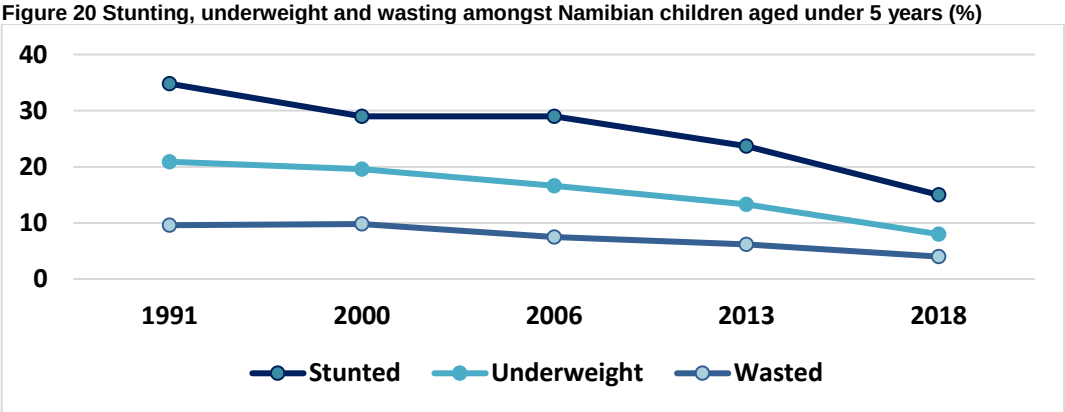
nurses and doctors. As a result, outreach campaigns have recently been reduced to only once a month, thus eliminating the initial strategy of visiting villages once every 2 weeks.

Finally, lower than desired quality of service affects health outcomes. Typically, every clinic is serviced by at least one registered nurse and two enrolled nurses. However, in most cases clinics are serviced by only one enrolled nurse with no registered nurses on site. There are no allowance or incentives provided to registered nurses deployed in rural areas, which results in most of them declining placement in such areas. This affects the quality of healthcare services provided to rural patients.

Paradoxically, Namibia has an oversupply of nurses, although these nurses cannot be deployed due to budget constraints and the implementation of the moratorium on the government wage bill[51]. In FY2018/19, approximately 343 qualified nurses and 169 recent nurse graduates were not deployed due to budgetary issues[52]. Additionally, availability of essential drugs is affected by lack of appropriate infrastructure to store cold medicine due to the unavailability of electricity in rural areas and a tedious procurement processes. Lastly, medical referrals from all regions are made to Windhoek, putting resource constraints on Windhoek and negatively impacting healthcare quality.

Nutrition indicators in Namibia are concerning, with 15% of children under the age of 5 being stunted and 4% are wasted, i.e. too thin for their age, in 2018[53]. There was a consensus among UNICEF Namibia interviewees[54] that new born and infant feeding practices impact on the child's wellbeing and nutritional status of children remains a concern in the country, despite the progress shown in Figure 20.

Figure 20 Stunting, underweight and wasting amongst Namibian children aged under 5 years (%)



Source: (Namibia, UNICEF, 2017).

Breastfeeding is closely related to and possibly influences stunting and malnutrition in children. Exclusive breastfeeding from birth to at least six months is encouraged by the Namibian Ministry of Health and Social Services. According to a recent study,[55] Namibia experienced a decline in early initiation of breastfeeding (EIBF) rate between 2000 and 2013. Findings of the study indicates that weighted percentage of babies who were breastfed within one hour of birth decreased significantly from 82.5% in 2000 to 74.9% in 2013. This shows that there a need for improvement on these indicators, given their direct impact on the wellbeing of the child.

51 Interview with the Ministry of Health and Social Services on 18 May 2018 via Skype in Pretoria, South Africa (Windhoek, Namibia).
52 (Africa, All, 2018).
53 (UNICEF, 2018).
54 UNICEF Namibia interview held on the 17th April 2018.
55 (M. N. Ndirangu, 2018).

UNICEF Namibia interviewees[56] mentioned that there appears to be limited and contradictory knowledge on child feeding practices which are linked to an introduction of weaning earlier than medically recommended. Mothers' level of education also influences a child's level of wellbeing, including feeding practises. The government used to have a door-to-door screening programme meant to educate parents on nutrition; the programme was terminated due to fiscal constraints experienced as of FY2014/15. UNICEF and Namibia University of Science and Technology implemented a nutritionist course in 2018, the programme is intended to reduce child malnutrition overtime.

3.2.3 Social Welfare

The HIV/AIDS epidemic has led to a rapid increase in the number of vulnerable children and orphans. UNICEF estimated that by 2012 Namibia would have had an orphan population of over 250 000 out of a child population of approximately 1 million (i.e. one in three children would be an orphan). The MoHSS sought to address the vulnerability of poor children and orphans by implementing child safety nets through the provision of child grants in 2002. The child grants programme was transferred from MoHSS to Ministry of Gender Equity and Child Welfare (MGECW) in 2004, and the MGECW has established a Child Welfare Division to fulfil the mandate of rendering child welfare and protection services in Namibia[57].

Namibia's comprehensive social safety net is funded by the government. The social safety net is comprised of *unconditional* social grants offered to poor and vulnerable Namibian citizens or permanent residents including children. Unconditional social grants do not require grant beneficiaries to employ certain behaviours or achieve certain outcomes. The unconditional social grants offered are Basic State Grants, War Veteran Grants and Child Welfare Grants. Most relevant to this report, Child Welfare Grants are provided to orphans and vulnerable children. There are primarily four Child Welfare Grants:

1. The Child Maintenance Grant is received by biological parent(s) of a child younger than 18 years whose spouse has died or sentenced to imprisonment for at least six months, or a child whose parent receives an old-age pension or disability grant. The grant therefore provides financial support for care of children and is received by biological parent(s) on behalf of their children;
2. The Foster Care Grant is provided in accordance with the Namibian Children's Act 33 of 1960. The grant is means-tested and provided to poor foster parents who care for a child placed under their custody;
3. The Places of Safety Allowance is provided to any individual or place which takes care of a child under the age of 18. The individual or place should be taking care of the child as per the commissioner of Child Welfare in terms of Section 33 of the Namibian Children's Act of 1960;
4. The Special Maintenance Grant is specifically targeted at Namibian children under the age of 16 with disabilities.

Table 5 below shows the different types and size of grants that children in Namibia are currently receiving. Foster Care Grant for the first foster child is N$200 and N$100 for subsequent children. The same principle applies for the Child Maintenance Grant, where by N$250 is provided for the first child and N$200 for subsequent children.

Table 5 Grant disbursement monetary value

Child welfare grant type	Monetary value (N$) FY2017/18
Child Maintenance Grant	250 per month

[56] UNICEF Namibia interview held on 17th April 2018.

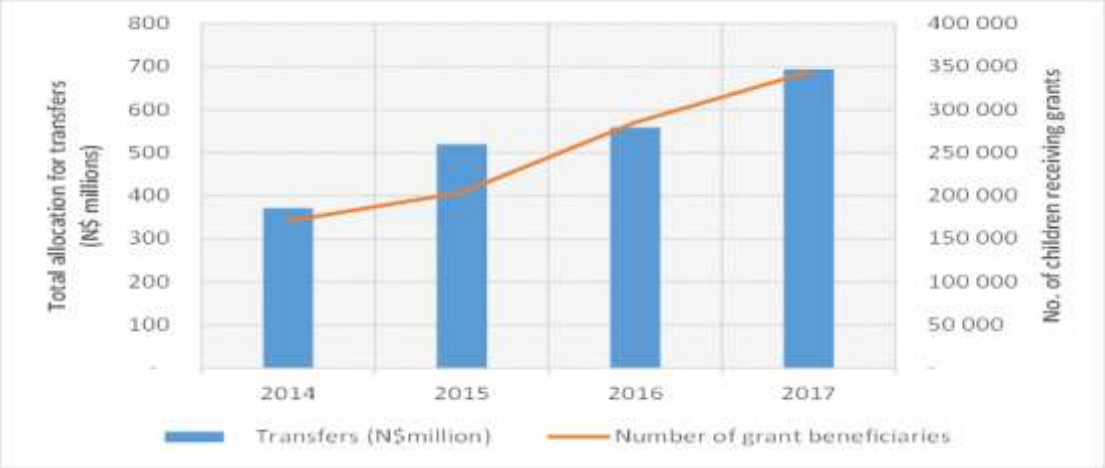
[57] (UNICEF, 2015).

Child welfare grant type	Monetary value (N$) FY2017/18
Foster Care Grant	200 per month
Places of Safety Allowance	10 per day
Special Maintenance Grant	200 per month

Source: (Welfare, Ministry of Gender Equity and Child, 2018).

Since the transfer of the child grant programme from MoHSS to MGECW in 2004, the number of child grant beneficiaries has increased from 9 000 in September 2002 to 181 033 in June 2015.[58] Figure 21 represents the growth in the number of children receiving grants in Namibia and the funds allocated for such purposes. Child grant beneficiaries have almost doubled from 170 816 in 2014/15 to 344 055 in 2017/18, in line with the increase in budgetary allocations for transfers. MGECW interviewees explained that their strategy is to keep the grant amount the same and increase coverage, rather than increasing the amount of the grant per child, because a number of children still remain uncovered. Besides fiscal constraints, many eligible children cannot receive the grant because of lack of national documents such as birth certificates.

Figure 21 Total number of child grant beneficiaries vs budgetary allocation for transfers



Source: (Ministry of Gender Equity and Child Welfare, 2018).

Estimated child poverty headcount rate was 43.4% in 2010[59] **and in 2015 34% of children lived in poverty, of which 18% lived in severe poverty**. 37.4% of rural children lived in poverty compared to 14.6% of urban children.[60] These statistics echo that although the number of beneficiaries increased extensively, child poverty is prevalent in the country especially in rural areas.

Therefore, although child grants prevent beneficiaries from being further below the poverty line, the country's child poverty remains stubbornly high. This might be due to the barriers to accessing grants. Firstly, child grants are not universally offered to poor households with children because qualifying households need to have an annual income no more than N$1 000. Secondly, children and their parents or guardians need to have Namibian identity documents which poor people often do not possess. The universal grant proposal was supported by the National Household and Income Expenditure Survey of 2009/10 which indicated that should child welfare grants become universal and be provided to all children under 18, child poverty would be reduced from 34% to 9% and extreme child poverty would be eliminated entirely.[61]

58 (UNICEF, 2015).
59 (Roberts, 2010).
60 (UNICEF, 2015).
61 (UNICEF, 2015).

3.2.4 *Cross-cutting issue: Sanitation*

While the country made progress in outcome indicators in the priority sector, low levels of sanitation remain a significant issue. The country's sanitation level has been stagnant at 24% since 2006, making Namibia one of the African countries with the lowest levels of sanitation. Sanitation facilities, including running water provided at schools, are directly linked to child welfare. Approximately 23 per cent of the 1,641 schools in the country do not have toilets.[62]

Lack of sanitation is also prominent in rural areas and some urban areas due to high urbanisation. The national rate of open defecation was 52 per cent in 2010, the second highest in Eastern and Southern African countries after Somalia (53 per cent)[63]. In 2015/16, 74% and 21% of rural and urban dwellers practised open defection, respectively: a practice that is unsanitary and harmful to health. Cholera, typhoid, hepatitis, polio, diarrhoea, worm infestation, reduced physical growth, impaired cognitive function and malnutrition could be linked or further influenced by open defection. Approximately, 17 per cent of children under 5 suffered from diarrhoea in 2015/16 and repeated episodes of diarrhoea contribute to the country's high levels of childhood stunting, which is at 15%.[64].

Sanitation provision requires significant coordination in the country as it falls under four ministries: Agriculture, Water and Forestry, Urban and Rural Development, Health and Social Services, and Education, Acts and Culture. UNICEF Namibia coordinates these ministries to identify and find solutions for sanitation challenges. One of identified challenges is schools being expanded without sanitation facilities. Resolving sanitation challenges in environment where there is pressure on the capital budget will require significant advocacy and likely require budget reprioritisation.

62 (Namibia, UNICEF, 2018).
63 (Namibia, UNICEF, 2018).
64 (Namibia, UNICEF, 2017).

4 The base scenario

Chapter 4 and 5 set out the fiscal projection exercise. Chapter 4 describes the base scenario, chapter 5 discusses options to increase fiscal space, presents several alternative scenarios, and compares the results of those to the base scenario. While each option takes account of Namibia's specific circumstances, it is important to remember that the projection results are based on specified, quantitative programming assumptions. In no case should the results be regarded as forecasts.

4.1 Base scenario assumptions

The projection analysis is carried out first with a "base scenario", a straightforward and relatively non-controversial set of assumptions covering the years 2017-2022. The goal of this scenario is to illustrate how much fiscal space will be available for the Namibian government in the coming years if the economy evolves in ways that extend recent trends while still limiting the growth in public debt levels in line with government's objectives.

This scenario centres on several key assumptions, including the growth rates of GDP, the exchange rate, and population growth rates. The evolution of other economic variables depends significantly on these key assumptions[65]. Table A3 in Appendix 1 extensively lists the base-scenario assumptions and provides brief explanations for them. Key base-scenario assumptions are listed in Table 6.

Table 6 Key assumptions in the base scenario

Growth rates (%)	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Real GDP	-1.2	1.2	3.3	3.8	3.5
Consumer price index	5.5	5.2	5.7	5.4	5.2
Population growth	2.3	2.3	2.3	2.3	2.3

These assumptions reflect the following view of Namibia's future economic performance: The growth rate of real GDP is set to increase gradually from -1.2% in FY17-18 to 3.5% by FY21-22, as the economy is expected to recover slowly after recent declines. Consumer-price inflation is assumed to remain constant, averaging 5.4% over the projection period. The population growth rate is also expected to be stable at 2.3% throughout.

As discussed in section 2, Namibia is planning to consolidate fiscally due to the current trajectory of the ratio of public debt to GDP. For the baseline scenario, to incorporate this policy decision, current expenditure in priority sectors are assumed to be determined by the collaborative effects of inflation and population growth. This allows for expenditure to remain relatively consistent with the status quo while allowing any economic growth more than inflation to contribute to fiscal consolidation.

[65] Thus, for example, certain variables are assumed to grow at the same rate as the nominal GDP – that is, they are assumed to grow at the "combined" rates of real GDP and the GDP deflator.

4.2 Base scenario and fiscal space "mapping"

Table 7 shows some of the key projection results for the financial years 2017/18 to 2021/22, based on the base scenario assumptions. **Taken together, the programming assumptions would imply rough stability in the evolution of the economy's key ratios**. **Under these assumptions, priority expenditure would be decreasing in terms of per child expenditure and as a percentage of GDP due to the fiscal consolidation assumptions.** Priority expenditure as a percentage of total expenditure will however be increasing as it is assumed that these sectors would be somewhat protected relative to the other sectors. The relatively slower growth in expenditure relative to GDP and therefore government revenue also allows the fiscal deficit to decrease gradually over time from 8.2% in FY18-19 to 7.1% FY21-22. Although still high, the baseline scenario assumes a gradual decrease in the fiscal deficit over the projection period as the cost from a more drastic decrease might be outweighed by its costs. The net internal financing flow (the resources needed to finance priority expenditure) would resultantly follow the same pattern as the fiscal deficit decreasing over time as a percentage of total expenditure and as a percentage of GDP.

Table 7 Namibia Key projection results for the base scenario

	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Priority expenditure					
Per cent of total expenditure	36.6%	36.8%	36.9%	37.0%	37.2%
Per cent of GDP	13.0%	13.0%	12.6%	12.2%	11.9%
Per child in US$ at 2016 exchange rate and prices	$1528.93	$1517.05	$1505.42	$1493.99	$1482.81
Net internal financing gap (fiscal gap)					
Per cent of total expenditure	8.8%	9.5%	8.5%	6.7%	5.0%
Per cent of GDP	3.1%	3.3%	2.9%	2.2%	1.6%
Fiscal Deficit (surplus/deficit)					
Per cent of GDP	-7.6%	-8.2%	-8.0%	-7.5%	-7.1%

The base scenario thus suggests that, to restrain Namibia's current debt trajectory, Namibia's priority expenditure will decrease slightly from US$1 528.93 per child to US$1 482.81 per child. This will create an average fiscal gap of 2.6% of GDP, which will result in a debt-to-GDP ratio of 63.7 per cent in FY21-22. This means that the Government of Namibia could somewhat restrain its current debt trajectory while still providing relative protection to the priority sectors. It is however worth mentioning that, given the relative volatility of the macroeconomic and fiscal variables used as inputs into these projections, accurate predictions over the projection period are difficult. Nevertheless, the parameter values used are aligned with the projection of the IMF in the February 2018 Country Report where the debt-to-GDP ratio is projected to reach 69.7 per cent in 2022[66].

According to IMF[67] given that Namibia's headline inflation has decreased from 7.3% in 2016 to 5.2% in 2017 and the economy has reached a GDP turning point from experiencing substantial growth until 2015/16 when the construction and mining sectors' growth declined significantly. A key policy decision to compact the decline was brought forth in the form of establishing fiscal consolidation. It would take a while before the country fully recovers, primarily because Namibia has high fiscal deficits, moreover, the economy is strongly interlinked to the South African economy

66 (IMF, 2018).
67 (IMF, 2018).

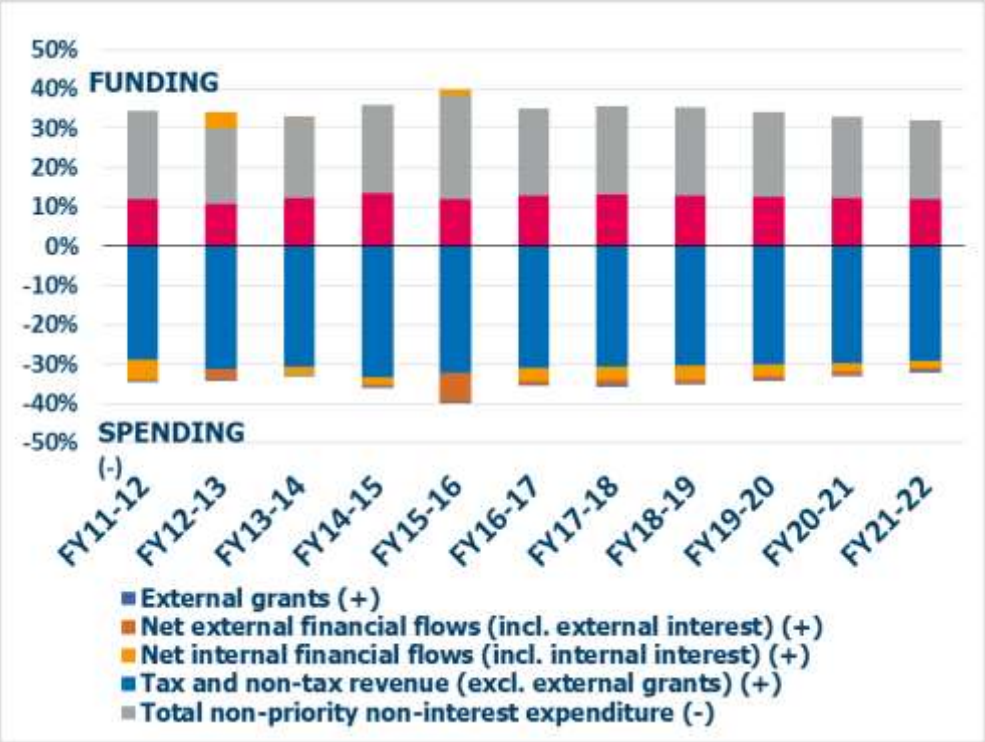
which is in experiencing a recession. Therefore, a base scenario in this case is that over the next few years, Namibia's priority expenditure would be declining as the country is consolidating.

Table 8 Results for the other elements of the fiscal account

Results	Base Scenario
Average tax and non-tax revenue/GDP, FY17-18 – FY21-22	30.0%
Average priority expenditure/GDP, FY17-18 – FY21-22	12.5%
Average priority expenditure per child (USD at 2015 prices & exchange rate), FY17-18 – FY21-22	$1505.65
Net internal debt flow/GDP, FY17-18 – FY21-22	2.6%
Total government debt/GDP, FY21-22	**69.9%**

Figure 22 shows a fiscal-mapping chart for FY11-12 to FY21-22, with projections from the base scenario. All projections are shown as a percentage of GDP. In the "stacked-bar" presentation, funding sources are above and expenditure flows below the horizontal axis: in effect, the sum of everything above the horizontal axis effectively funds everything below. For each year, the sum of all flows above the horizontal axis is precisely equal to the sum of all flows below the horizontal axis. Stated differently, the tax and non-tax revenue, the external grants, and net external financial flows, shown above the horizontal axis, together fund the priority expenditure, the non-interest non-priority expenditure, and the (negative) internal financing flow including internal interest. The net internal financing flows include the interest on the internal debt.

Figure 22 Fiscal space and its components over the historical and projection period in the base scenario (FY11/12 - FY21/22) as a % of GDP



The projection exercise can be used to evaluate different policy approaches involving priority expenditure and its fiscal space. In general, if a scenario is proposed that involves an increase in the priority-expenditure flow relative to what is in the base scenario, the "fiscal gap" would presumably increase. The exercise would show an increase in the net internal financing flow to the government compared with the base scenario. On the other hand, if a scenario is proposed involving an enhancement through one or more elements of fiscal space, the exercise would show

a reduction in the net internal financing flow to the government compared with the base scenario. Naturally, combined scenarios are possible, in which both the priority-expenditure and the fiscal-space flows are increased. The idea would be to determine the net consequence of the two changes. The exercise shows the multiannual internal financing flows for the whole projection period and accumulates these flows so that the exercise shows the government's total debt at the end of the projection period.

Since these results are quantitative, they can be discussed in terms of their feasibility: Would the net internal financing flow be likely to exceed the capacity of internal financial markets and would the government's total debt stock rise too high too quickly as a percentage of GDP?

5 Alternative scenarios

The projection exercise is set up to carry out sensitivity analysis. The procedure consists of calculating projections based on alternative scenarios, which are set out in this chapter. The assumptions of each alternative scenario are kept the same as those of the base scenario except that one or two assumptions are changed. Keeping the scenarios relatively straightforward makes results easier to interpret and more useful. Comparison of each alternative scenario with the base scenario would indicate the order-of-magnitude consequences for the fiscal accounts of the changed assumptions, given the exercise's other assumptions.

Section 5.1 describes possible approaches for increasing fiscal space. Section 5.2 then describes some illustrative alternative scenarios and describes how results compare with those of the base scenario. Finally, Section 5.3 considers the potential impact of key risks facing fiscal space in the country through a number of alternative scenarios.

5.1 Options to increase fiscal space

In principle, policy-makers have the following general options for enhancing fiscal space for priority expenditure:

(1.) Increasing tax and non-tax revenue; and possibly earmarking some of this for priority expenditure;
(2.) Increasing external grants for budget support and projects;
(3.) Reducing non-priority expenditures;
(4.) Reducing external debt service through agreements with creditors;
(5.) Increasing external debt disbursements; and
(6.) Increasing net internal borrowing flows.

Apart from government policy choices, changes in the macroeconomic context also affect the fiscal space. For example, increased GDP growth would increase the fiscal space by increasing tax revenue.

Namibia is currently in a precarious position. The recent sharp increase in public debt has brought with it a substantial increase in the cost of debt service. **If substantial changes to its fiscal approach are not made, the resulting increasing fiscal deficit will continue to put upward pressure on public debt and this unsustainable debt cycle will continue.** Increasing debt levels will further increase non-discretionary spending (debt-service costs) which will put downward pressure on discretionary. This is important to remember as the base scenario and most of the alternative scenarios project a downward trend in expenditure per child over the projection period. This represents the likely trade-off between the maintenance or increase of current spending levels and long-term fiscal sustainability.

Financing priority sectors through debt financing is therefore unlikely or sustainable. This leaves improved macroeconomic performance, increased tax revenues, and reprioritisation as the only viable options for increasing fiscal space for the priority sectors. Financing through increased donor funding is also unlikely given the current downward trend which is mostly due to Namibia's income level being reclassified, as discussed in section 2.

The evaluation of the alternative-scenario results therefore suggests that the best policy approaches to securing *sustained* increases in fiscal space for priority-expenditure appear to lie with improved tax administration and increased economic growth. Of course, other pathways to achieving improvements in fiscal space are possible as well, most notably in terms of improving allocative and cost-efficiency in the priority expenditure categories. In all priority sectors there appear to be opportunities for significantly improving efficiency and effectiveness. It is thus plausible to assume that significant resources could be freed up through improving decision-making and management through the continuous use and analysis of performance information, monitoring and evaluation in conjunction with budgetary allocation information.

5.2 Alternative scenarios and projections compared with the base scenario

5.2.1 Scenario 1: Increasing tax and non-tax revenue

Namibia is currently finalising the legislative framework, referred to as the Namibian Revenue Authority Bill, for the establishment of an independent institution dedicated to the collection of tax revenue. It is envisaged that the establishment of a well-capacitated independent institution, similar to South African Revenue Services (SARS), would improve revenue collection. The assumption is that a dedicated independent revenue collection agency would be able to collect more tax revenue even if economic activity remains unchanged.

Between 2011/12 and 2016/17, PIT and CIT revenue in Namibia grew at an average nominal annual rate of 14.6% and 10.5% respectively. This is meaningfully higher than nominal GDP growth during this same period. Although past performance over such a short time horizon cannot be used to accurately predict future performance, this, along with the introduction of an independent revenue authority, might indicate overly pessimistic assumptions regarding the relationship between tax revenue growth and GDP growth in the baseline. **There is therefore potential for more significant growth in tax revenue over the projection period than what is presented in the baseline.**

The IMF also suggests that there is space to increase tax revenue through the following measures[68]:

- Improving the progressivity of PIT by adjusting rates;
- Strengthening CIT;
- Closing loopholes under CIT and VAT;
- Broadening the VAT base by eliminating zero rating and exemptions on real estate, telecommunications and fuel products.

The first "alternative" scenario, Scenario 1, therefore suggests that these improvements in the tax system could bring about expansion in fiscal space. The assumptions of Scenario 1 (summarised in Table 9 below) are the same as those for the base scenario, except that instead of VAT, CIT and PIT revenue growing at the same rate as nominal GDP, it gradually increases over time from growing at the same rate as nominal GDP in FY16-17 to growing 1.3 times faster (30%) by FY20-21.

Table 9 Key assumptions for Scenario 1

Growth rates	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Real GDP	-4.4%	-1.2%	1.2%	3.3%	3.8%	3.5%
Consumer price index	3.9%	5.5%	5.2%	5.7%	5.4%	5.2%

[68] (IMF, 2018).

Growth rates	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Population growth	2.3%	2.3%	2.3%	2.3%	2.3%	2.3%
Alternative assumptions						
Elasticity of company-tax revenue with respect to nominal GDP	1.0	1.1	1.1	1.2	1.2	1.3
Elasticity of personal income tax revenue with respect to nominal GDP	1.0	1.1	1.1	1.2	1.2	1.3
Elasticity of value added tax revenue with respect to nominal GDP	1.0	1.1	1.1	1.2	1.2	1.3

This scenario assumes a strengthened tax collection system and that all increased revenues will be allocated to the servicing of debt. Table 10 provides a summary of the projection results using the assumptions above. As a result, although there is increased fiscal space, priority expenditure does not increase the net-effect of improving the debt position in the short- to medium-term will serve priority expenditure in the long-term.

Table 10 Key projection results in scenario 1

	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Priority expenditure						
Per cent of total expenditure	36.5%	36.6%	36.8%	36.9%	37.0%	37.2%
Per cent of GDP	12.8%	13.0%	13.0%	12.6%	12.2%	11.9%
Per child in USD at 2016 exchange rate and prices	$1541.05	$1528.96	$1517.07	$1505.42	$1494.00	$1482.81
Net internal financing gap (fiscal gap)						
Per cent of total expenditure	9.4%	8.6%	9.0%	7.3%	4.4%	1.4%
Per cent of GDP	3.3	3.1	3.2	2.5	1.5	0.5
Fiscal Deficit (surplus/deficit)						
Per cent of GDP	-7.5	-7.6	-8.0	-7.6	-6.7	-5.8

As shown in Box A, the projection exercise suggests that this would lead to a 0.5 percentage-points increase in average tax revenue as a percentage of GDP over the projection period, 0.6 percentage-point decrease in net internal debt flow as a percentage of GDP, and a reduction in the average government debt stock as a percentage of GDP from 63.7% to 62.7%. Priority expenditure would remain unchanged because, as discussed, the increase in revenue is allocated to the servicing of debt.

Box A: Enhanced VAT, CIT and PIT collection

Results	Scenario 0	Scenario 1	Variation
Average tax revenue/GDP, FY2017-2021	30,0%	30,5%	0.5%
Average priority expenditure/GDP, FY2017-2021	12,5%	12,5%	0%
Average priority expenditure per child (USD at 2016 prices and exchange rate), FY2017-2021	$1505.65	$1505.65	$0
Net internal debt flow/GDP, FY2017-2021	2,6%	2,0%	-0.6%
Total government debt/GDP, FY21-22	**69.9%**	**67.4%**	**-2.5%**

5.2.2 *Scenario 2: Enhanced economic growth*

Scenario 2 models an increase in economic growth. Interviews[69] with the Namibian MoF revealed that the government is planning to increase expenditure towards infrastructure and support mining activities. Construction (infrastructure) and mining have previously been identified as sectors that have significant potential to increase GDP growth for Namibia. Respondents mentioned government intervention in gold mining projects as an area that the government would consider. Therefore, this scenario is modelled on the assumption of increased GDP growth as a result of enhanced mining and construction due to government support. The scenario assumes an average growth rate of 4.2% over the projection period: with growth rising incrementally to a high of 5.0% in FY2021-22. Table 11 provides a summary of the projection assumptions, while Table 12 shows the projection results.

Table 11 Key assumptions for Scenario 2

Growth rates	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Real GDP	**-4.4%**	**0.3%**	**2.7%**	**4.8%**	**5.3%**	**5.0%**
Consumer price index	3.9%	5.5%	5.2%	5.7%	5.4%	5.2%
Population growth	2.3%	2.3%	2.3%	2.3%	2.3%	2.3%

Table 12 Key projection results for Scenario 2

	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Priority expenditure						
Per cent of total expenditure	36.5%	36.2%	36.0%	36.0%	35.9%	35.9%
Per cent of GDP	12.8%	12.8%	12.6%	12.1%	11.5%	11.1%
Per child in USD at 2016 exchange rate and prices	$1541.05	$1528.96	$1517.08	$1505.43	$1494.01	$1482.82
Net internal financing gap (fiscal gap)						
Per cent of total expenditure	9.4%	8.8%	9.2%	7.6%	5.1%	2.7%
Per cent of GDP	3.3%	3.1%	3.2%	2.5%	1.7%	0.8%
Fiscal Deficit (surplus/deficit)						
Per cent of GDP	-7.5%	-7.6%	-8.0%	-7.5%	-6.8%	-6.1%

Box B shows the differential outcomes between the base scenario and scenario 2. Average tax revenue decreases by 0.4 percentage point from the baseline scenario. This is due to the fact that, although the bulk of tax revenue increases as a result of the increased economic activity, SACU revenues are more likely to be affected by regional economic activity. In this scenario therefore, SACU revenue is exogenously assumed to continue growing at 3.3% in nominal terms which is the same as the baseline assumption. Resultantly, average revenue as a percentage of GDP, excluding SACU revenue, in this scenario does not differ from the baseline.

Priority expenditure also decreases as a percentage of GDP as it has been assumed that, to consolidate fiscally, expenditure is not affected by real growth, but only increases as a result of population growth and inflation. In this scenario therefore, the increased fiscal space created by the increased GDP growth is harnessed to control the fiscal deficit and slow down public debt accumulation while protecting the current levels of priority expenditure. Average net internal debt flow and total government debt as a percentage of GDP therefore decrease by 0.4 and 3.1 percentage points respectively.

[69] Interview with Ministry of Finance held on 19 April 2018 (Windhoek, Namibia).

Box B: Enhanced economic growth

Results	Scenario 0	Scenario 2	Variation
Average tax revenue/GDP, FY2017-2021	30.0%	29.6%	-0.4%
Average priority expenditure/GDP, FY2017-2021	12.5%	11.9%	-0.6%
Average priority expenditure per child (USD at 2016 prices and exchange rate), FY2017-2021	$1505.65	$1505.65	$0
Net internal debt flow/GDP, FY2017-2021	2.6%	2.2%	-0.4%
Total government debt/GDP, FY2021	69.9%	64.2%	-5.7%

5.2.3 *Scenario 3: Higher priority expenditure with economic growth and improved tax collection*

The previous scenarios illustrated the effects on public debt of improved tax collection and economic growth. **Scenario 3 assumes that Namibia can achieve both simultaneously and therefore has fiscal space available to continue consolidating their fiscal position but also increase expenditure in the priority sectors**. Although Namibia currently faces substantial fiscal risk, expenditure in the priority sectors are still lower than the ideal. Health and Education expenditure are both below their targets set by the Abuja Declaration and the UNESCO Dakar Framework for Education respectively. Furthermore, as discussed 2.1.3, Namibia's population consists of a high proportion of Orphans and Vulnerable Children (OVC) requiring substantial social protection and social support from government. Therefore, if fiscal space is created that is sufficient to both meaningfully address debt levels and increase priority expenditure, such a policy option should certainly be considered.

Scenario 3 provides the potential effects of such an option. Table 13 provides a summary of the projection assumptions above, while Table 14 shows the projection results. In this scenario, it is assumed the economy grows at an average annual real rate of 2.9 per cent[70] and the elasticities of VAT, PIT and CIT revenue to nominal GDP increases from growing at the same rate as nominal GDP in FY16-17 to growing 12.5% faster[71] by FY21-22. Furthermore, it is assumed that the staff numbers in the priority sectors would increase 4.75 times faster than the child population to address the current staff shortages. Non-staff operational expenditure also increases to compensate for the increased human resources.

Table 13 Key assumptions for Scenario 3

Growth rates	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Real GDP	-4.4%	-0.4%	2.0%	4.1%	4.6%	4.3%
Consumer price index	3.9%	5.5%	5.2%	5.7%	5.4%	5.2%
Population growth	2.3%	2.3%	2.3%	2.3%	2.3%	2.3%
Alternative assumptions						
Elasticity of education staff size with respect to child population	1.0	1.0	4.75	4.75	4.75	4.75
Elasticity of health staff size with respect to child population	1.0	1.0	4.75	4.75	4.75	4.75
Elasticity of social protection staff size with respect to child population	1.0	1.0	4.75	4.75	4.75	4.75
Elasticity of VAT revenue to nominal GDP	1.0	1.025	1.05	1.075	1.100	1.125

[70] The middle point between the real GDP growth assumption in scenario 2 and the baseline.

[71] The middle point between the elasticities assumed in scenario 1 and the baseline.

Growth rates	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Elasticity of PIT revenue to nominal GDP	1.0	1.025	1.05	1.075	1.100	1.125
Elasticity of CIT revenue to nominal GDP	1.0	1.025	1.05	1.075	1.100	1.125

Table 14 provides a summary of the projection results using the assumptions above.

Table 14 Key projection results for Scenario 3

	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Priority expenditure						
Per cent of total expenditure	36.5%	36.4%	36.8%	37.2%	37.7%	38.2%
Per cent of GDP	12.8%	12.9%	13.0%	12.8%	12.5%	12.3%
Per child in USD at 2016 exchange rate and prices	$1541.05	$1528.96	$1541.49	$1556.57	$1574.40	$1595.21
Net internal financing gap (fiscal gap)						
Per cent of total expenditure	9.4%	8.7%	9.6%	8.5%	6.5%	4.6%
Per cent of GDP	3.3%	3.1%	3.4%	2.9%	2.2%	1.5%
Fiscal Deficit (surplus/deficit)						
Per cent of GDP	-7.5%	-7.6%	-8.2%	-8.0%	-7.4%	-6.9%

As shown in Box C, the projection exercise suggests that, **given the assumptions of this admittedly optimistic scenario, it would be possible to both increase expenditure in the priority sectors while still constraining the current public debt trajectory**. Public debt as a percentage of GDP could decrease by 1.2 percentage points while priority expenditure per child would increase by 3.4% per year on average.

Box C: Increased GDP growth due to recovery in construction activities: allocated to servicing debt

Results	Scenario 0	Scenario 3	Variation
Average tax revenue/GDP, FY2017-2021	30.0%	30.1%	0.1%
Average priority expenditure/GDP, FY2017-2021	12.5%	12.7%	0.2%
Average priority expenditure per child (USD at 2016 prices and exchange rate), FY2017-2021	$1505.65	$1559.33	$53.67
Net internal debt flow/GDP, FY2017-2021	2.6%	2.5%	-0.1%
Total government debt/GDP, FY2021	69.9%	67.8%	**-2.1%**

5.2.4 Scenario 4: Reprioritisation from non-priority to priority expenditure

The next scenario, **Scenario 4**, **presents the assumption of reprioritising expenditure from non-priority to priority sectors**. The baseline scenario assumes non-priority expenditure grows at approximately the rate of inflation even though it also assumes real growth in the economy. This is, as discussed, to constrain the current trajectory of government debt.

The projection model suggests that government could reprioritise non-priority expenditure towards priority expenditure and improve child health, education and social welfare while still achieving the intended outcomes of debt consolidation. By decreasing the elasticity of non-priority expenditure to nominal GDP growth by 5 per cent, it is possible to increase priority expenditure meaningfully without affecting debt-levels. Ideally, the decrease in non-priority sectors, as defined by this report,

should not occur at the expense of the government's political priorities. It is therefore essential that this is achieved through fiscal discipline and increased spending efficiency. The IMF has also suggested that spending efficiency in Namibia could be improved by improved budget formulation and tightened expenditure controls[72]. Table 15 provides a summary of the projection assumptions in which staff size in the priority sectors are assumed to increase at a much greater rate than the relevant populations. Staff costs are the major cost driver in these sectors. The model therefore automatically increases non-staff operational expenditure in the respective sectors in alignment with the growth in staff numbers, inflation and real economic growth.

Table 15 Key assumptions for Scenario 4

Growth rates	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Real GDP	-4.4%	-1.2%	1.2%	3.3%	3.8%	3.5%
Consumer price index	3.9%	5.5%	5.2%	5.7%	5.4%	5.2%
Population growth	2.3%	2.3%	2.3%	2.3%	2.3%	2.3%
Alternative assumptions						
Elasticity of education staff size with respect to child population	1.0	1.0	2.0	3.0	4.0	5.0
Elasticity of health staff size with respect to child population	1.0	1.0	2.0	3.0	4.0	5.0
Elasticity of social protection staff size to child population	1.0	1.0	2.0	3.0	4.0	5.0
Elasticity of non-priority expenditure to nominal GDP	1.0	1.28	0.72	0.56	0.52	0.52

Table 16 provides a summary of the projection results under the assumptions listed above. It shows that, even though the fiscal deficit as a percentage of GDP is decreasing over the projection period, priority expenditure per child is still increasing slightly as a result of the increase in the proportion of total expenditure being allocated to the priority sectors.

Table 16 Key projection results for Scenario 4

	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Priority expenditure						
Per cent of total expenditure	36.5%	36.6%	37.0%	37.4%	38.0%	38.8%
Per cent of GDP	12.8%	13.0%	13.0%	12.8%	12.6%	12.5%
Per child in USD at 2016 exchange rate and prices	$1541.05	$1528.96	$1523.58	$1525.36	$1535.16	$1554.35
Net internal financing gap (fiscal gap)						
Per cent of total expenditure	9.4%	8.8%	9.3%	8.3%	6.7%	5.5%
Per cent of GDP	3.3%	3.1%	3.3%	2.8%	2.2%	1.8%
Fiscal Deficit (surplus/deficit)						
Per cent of GDP	-7.5%	-7.6%	-8.1%	-7.9%	-7.5%	-7.3%

Box D below show that tax revenue would remain at an average of 30.0 percent of GDP over the projection period, while the average spending on priority expenditure per child would increase

[72] (IMF, 2018).

meaningfully by 1.8% or $27.83 per child per annum. These increases could therefore occur while keeping public debt on the same trajectory as assumed in the baseline.

Box D: Increased GDP growth due to recovery in mining and construction activities; allocated to priority expenditure

Results	Scenario 0	Scenario 4	Variation
Average tax revenue/GDP, FY2017-2021	30.0%	30.0%	0.0%
Average priority expenditure/GDP, FY2017-2021	12.5%	12.8%	0.3%
Average priority expenditure per child (USD at 2016 prices and exchange rate), FY2017-2021	$1505.65	$1533.48	$27.83
Net internal debt flow/GDP, FY2017-2021	2.6%	2.6%	0.0%
Total government debt/GDP, FY2021	69.9%	71.5%	1.6%

5.2.5 Other options for enhancing the fiscal space

Increasing external grants for budget support and projects

Grants' contribution to Namibian revenue is limited, at 1% in 2009/10 before decreasing to 0.3% in 2016/17. **The option of increasing grants as a potential source for additional revenue to enhance fiscal space is unlikely for Namibia.** Besides the country's upper-middle income status, another challenge is global economic conditions. Politically some Western economies are under political pressure to reduce international support and economic growth is still weak in some countries, thus limiting the chances that donors provide additional aid to middle-income countries such as Namibia.

Increasing external-debt disbursements

In general, macroeconomic policy specialists concur that it is not advisable to use commercial external debt to fund education, health, or social-development expenditure. The reasoning is straightforward: eventual returns to education and health expenditure are realized over decades, but debt service on commercial external debt is generally due within a decade. Concessional debt, with multi-decade terms and near-zero interest rate, is more realistic for such purposes. As mentioned previously, Namibia's credit rating was downgraded for multiple reasons, including its level of debt financing. Although extensive borrowing could potentially relieve severe fiscal constraints in the short-term, in the long-run Namibia's increase in external debt would amplify negative economic shocks. The country is aware of these risks and it has sought to bring public debt on a sustainable path.

5.3 Risks to fiscal space and their impact

5.3.1 Scenario 5: Decrease in SACU revenue transfers

Section 2 highlighted Namibia's dependence on SACU in terms of trade and revenue, with on average about 30% of Namibia's revenue coming from SACU transfers in recent years**. Scenario 5 models the impact of a decrease in SACU revenues for Namibia**. Namibia has raised its concerns on SACU transfers' fluctuations, with a decrease in transfers impacting the country's expenditure plans. Historically, SACU transfers have also proven to be a volatile source of funding which increases fiscal risks and the ability to accurately plan future spending. Hence, the projection exercise shows the significant deteriorating effect of lower SACU revenue transfers on expenditure, budget deficits and the trajectory of debt.

There was an upward trend in SACU revenue between FY11-12 and FY15-16 increasing at an average nominal rate of 24.9%. This trend was broken by a decrease of 4.2% in FY17-18. Although

there was a small uptick in the following fiscal year, this does indicate that these revenues are vulnerable to external influences. Table 17 shows the assumptions of Scenario 5 which assumes that, over the projection period, SACU revenues would decrease at the same annual rate as it did in FY17-18.

Table 17 Key assumptions for Scenario 5

Growth rates	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Real GDP	-4.4%	-1.2%	1.2%	3.3%	3.8%	3.5%
Consumer price index	3.9%	5.5%	5.2%	5.7%	5.4%	5.2%
Population growth	2.3%	2.3%	2.3%	2.3%	2.3%	2.3%
Alternative scenarios						
SACU transfer growth rate	3.3%	-4.2%	-4.2%	-4.2%	-4.2%	-4.2%

Table 18 shows the effects of a gradual decrease in SACU revenue over the projection period. As SACU revenues do not influence expenditure through model assumptions, priority expenditure remains the same as the baseline in relative and absolute terms. **However, the decrease in revenue results in a much higher need for debt financing which is shown by the increase in the fiscal deficit presented below.**

Table 18 Key projection results for Scenario 5

	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Priority expenditure						
Per cent of total expenditure	36.5%	36.6%	36.8%	36.9%	37.0%	37.2%
Per cent of GDP	12.8%	13.0%	13.0%	12.6%	12.2%	11.9%
Per child in USD at 2016 exchange rate and prices	$1541.05	$1528.96	$1517.07	$1505.42	$1494.00	$1482.81
Net internal financing gap (fiscal gap)						
Per cent of total expenditure	9.4%	10.5%	12.7%	13.1%	12.5%	11.8%
Per cent of GDP	3.3%	3.7%	4.5%	4.5%	4.1%	3.8%
Fiscal Deficit (surplus/deficit)						
Per cent of GDP	-7.5%	-8.2%	-9.4%	-9.7%	-9.7%	-9.7%

On average over the projection period, **Scenario 5** (Box E) assumptions result in no variation from the baseline in terms of priority expenditure for reasons discussed. **However, the decrease in SACU revenue of 1.5 percentage points and the resulting decrease in total government revenue results in a 4-percentage point increase in the average debt-to-GDP ratio and a 1.6 percentage point increase in the net internal financing requirement**. Therefore, reserves for SACU transfers would help overcoming plausible transfer shortfalls. The increases in the financing requirement could be mitigated by a contractionary fiscal policy, however, given the volatility of SACU revenues, it will remain a challenge to adjust spending plans accordingly.

Box E: Decrease in SACU transfers

Results	Scenario 0	Scenario 5	Variation
Average tax revenue/GDP, FY2017-2021	30.0%	28.4%	-1.6%
SACU transfer/GDP, FY2016–2021	7.8%	6.3%	-1.5%
Average priority expenditure/GDP, FY2017-2021	12.5%	12.5%	0.0%
Average priority expenditure per child (USD at 2016 prices and exchange rate), FY2017-2021	$1505.65	$1505.65	$0.00

Results	Scenario 0	Scenario 5	Variation
Net internal debt flow/GDP, FY2017-2021	2.6%	4.1%	1.6%
Total government debt/GDP, FY2021	69.9%	76.1%	6.2%

5.3.2 *Scenario 6: Lower GDP growth*

Global growth is off the back foot, with advanced economies expected to experience higher growth over the medium term. Although Namibia experienced remarkable economic growth up until FY15-16, and it is generally expected that the recent contraction would only be temporary, **the economy still faces significant downside risk**. Contractionary fiscal policy, the protracted low-growth environment in South Africa, uncertainty related to the sustainability of public debt, lower than expected demand for exports, and slower than expected recovery in the mining and construction sectors could all lead to a more modest economic growth outlook. Given the importance of economic growth for the creation of fiscal space, the final scenario, scenario 6, illustrates the potential consequences of lower economic growth.

In the base scenario, real GDP growth is assumed to average 2 per cent between FY17/18 and FY 21/22. In this scenario, **it is assumed that real GDP growth only grows at an average of 0.6% over the period, 1.5 percentage points less**. Table 19 provides a summary of the key assumptions for scenario 6, while Table 20 shows the projection results.

Table 19 *Key assumptions for Scenario 6*

Growth rates	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Real GDP	-4.4%	-2.7%	-0.3%	1.8%	2.3%	2.0%
Consumer price index	3.9%	5.5%	5.2%	5.7%	5.4%	5.2%
Population growth	2.3%	2.3%	2.3%	2.3%	2.3%	2.3%

Table 20 provides a summary of the projection results using the assumptions above. It illustrates how the decrease in the fiscal deficit and the net internal financing gap decreases at a much lower rate than in the baseline scenario.

Table 20 Key projection results for Scenario 6

	FY16-17	FY17-18	FY18-19	FY19-20	FY20-21	FY21-22
Priority expenditure						
Per cent of total expenditure	36.5%	37.1%	37.5%	37.9%	38.2%	38.6%
Per cent of GDP	12.8%	13.2%	13.4%	13.2%	13.0%	12.8%
Per child in USD at 2016 exchange rate and prices	$1541.05	$1528.96	$1517.07	$1505.42	$1494.00	$1482.80
Net internal financing gap (fiscal gap)						
Per cent of total expenditure	9.4%	8.7%	9.8%	9.5%	8.2%	7.2%
Per cent of GDP	3.3%	3.1%	3.5%	3.3%	2.8%	2.4%
Fiscal Deficit (surplus/deficit)						
Per cent of GDP	-7.5%	-7.7%	-8.4%	-8.5%	-8.3%	-8.2%

Box F shows the differential outcomes between the base scenario and scenario 6. If fiscal spending adjustments are not made to adjust to the lower growth environment, this scenario's projection

exercise shows a 0.4 percentage point increase in internal debt flow, and an increase of 7.4 percentage point the government debt-to-GDP ratio.

Box F: Lower economic growth

Results	Scenario 0	Scenario 6	Variation
Average tax revenue/GDP, FY2017-2021	30.0%	30.3%	0.3%
Average priority expenditure/GDP, FY2017-2021	12.5%	13.1%	0.6%
Average priority expenditure per child (USD at 2016 prices and exchange rate), FY2017-2021	$1505.65	$1505.65	$0.00
Net internal debt flow/GDP, FY2017-2021	2.6%	3.0%	0.4%
Total government debt/GDP, FY2021	**69.9%**	**77.3%**	**7.4%**

6 Conclusion

This report has highlighted fiscal challenges faced by the government of Namibia in increasing allocations to child-focussed priorities. Given the sluggish economic performance, high debt levels, low donor grants, and decline in SACU transfers, the government will find it difficult to raise domestic revenues. Without increased domestic revenue, fiscal consolidation should be supported as the long-term consequences of continuing the current debt path will be devastating to UNICEF's priority sectors. Thus, this report's central recommendation is that, given the current fiscal environment in Namibia, **UNICEF's focus should be on the protection of expenditure in priority sectors, and the efficiency and effectiveness of this expenditure rather than advocating for increases**. Debt-servicing costs are currently increasing at a faster rate than tax revenue implying that the amount of funding available for discretionary expenditure (non-debt related expenditure) decreases each year. This implies that substantial real economic and tax revenue growth will be required even if the goal is just to maintain the current levels of expenditure per child.

An increase in economic and revenue growth are anticipated to result in an increase in priority sectors' expenditure. An assumption is that these increases would be in staff numbers which would be faster than the child population to address the current staff shortages. Non-staff operational expenditure would also increase to compensate for the increased human resources. **Therefore, these assumptions could be used when UNICEF is advocating for expenditure protection across child priority sectors. Moreover, UNICEF as an organisation for child priorities should use these and other quantitative projections in its dialogue with the Namibian government and other stakeholders to ensure that evidence-based decisions can be made**. These projections should not only cover future expenditure needs in education, health, social development and other sectors relevant for children, but should also encompass the main components of "fiscal space" that provides the funding for such expenditure.

The analysis of this report is intended to be essentially illustrative, to show how the methodology it recommends can be used to address the relevant policy issues. But certain tentative conclusions regarding the substantive issues do emerge, including the following:

1. Given Namibia's demographic profile and the high number of Orphans and Vulnerable Children (OVC) in the country, it is critical that both the total amount **currently allocated towards priority sectors is protected** during a time of fiscal constraints. Additionally, the **effectiveness of priority spending must be enhanced**. Effective investment across all sectors including priority sectors at this level is essential if the country is to move onto a longer-term growth and development trajectory;
2. Namibian debt levels increased significantly during the period of economic slowdown, which has raised debt-servicing costs substantially. As these costs are mostly non-discretionary, **efforts to bring down debt levels meaningfully are required, otherwise there might be long- and medium-term consequences** for funding available for discretionary allocations, such as to priority sectors;
3. Education expenditure is considered to be inverse to the number of children, with secondary school having less learners than primary school; however, more funds are allocated towards secondary schools than primary schools. Primary school learners account for 67% of total enrolments and only 29% of available funds are allocated to primary education. Such an inverse relationship between funding and the number of learners can compromise the education outcomes especially at secondary level where drop-out rates are very high because learners are not prepared for secondary school due to low quality primary school. **Effective**

and improved strategic allocation could be achieved by re-aligning education expenditure towards critical primary schooling to reduce secondary school dropouts and repetition rates;

4. Effective allocation of social welfare transfers (prioritising the most vulnerable children), targeted towards children, would not only support education (and health) outcomes in the country, but also directly benefit those facing the most extreme levels of poverty;
5. Naturally, effective investments in priority expenditure would need to be sustainably funded through increased tax revenue. Both personal and company income tax increased between FY2015/16 and FY2016/17 from 15% to 16% and 21% to 24%, respectively. More growth could be expected once a revenue services agency is established. The report modelled the impact of enhanced tax administration, an **improvement in tax collection would have a positive impact towards overall revenue and potentially increases in priority sector spending in the longer term**;
6. On average, about 30% of Namibia's revenue is from SACU transfers. However, recently SACU revenues have been unstable and has declined in a number of years, posing revenue risks for Namibia. The projection exercise shows the significant deteriorating effect of lower SACU revenue transfers on expenditure, budget deficits and the trajectory of debt. **Therefore, reserves for SACU transfers would assist in overcoming plausible transfer shortfalls**;
7. **External grants are likely to decrease rather than increase over time, thus implicating revenue**. A global economic slowdown and Namibia improving its status to an Upper-Middle Income Country are the main contributors to this trend;
8. The country has pursued a contractionary fiscal policy in recent years impacting overall government expenditure, including priority expenditure. **The projection model suggests that government could reprioritise non-priority expenditure towards priority expenditure and improve child health, education and social-protection**. Fiscal discipline and spending efficiency are required to reduce the national deficit to sustainable levels while ensuring that investment in priority areas is protected to achieve the country's longer-term growth and social development objectives;
9. **The potential for the strengthening of the mining sector**, as a result of government support for mining projects, including gold, represents a potential opportunity for the country that would lead to an increase in GDP and hence increased tax revenue;
10. On the other side of the argument, just as economic growth can drive fiscal space expansion, a decrease in GDP will drive a contraction. In addition to domestic issues, Namibia is very vulnerable to South Africa's economic performance; through SACU revenue and other mechanisms. **With the current economic and political uncertainty in the country, lower GDP growth remains a legitimate concern in Namibia**.

UNICEF could interact with the government regarding resource allocation and balancing the composition of expenditures, particularly for prioritising children's health, education, and social welfare. In this regard, this report can be an important instrument to improve the effectiveness of the dialogue. Moreover, this quantitative tool can also help in determining the importance of the various parameters like economic growth vis-à-vis others like establishing a tax administration agency which can help shape effective and valuable dialogue with the government.

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Appendix 1: Fiscal space projections

This Appendix describes the details of the base-scenario projection exercise discussed above, and then describes the results of a sensitivity analysis.

The base-scenario programming assumptions are intended to be relatively simplified, to make the calculation relatively easy to carry out and to understand. The following general explanatory points are noted:

1. The assumptions are "programming" assumptions. They are not intended, and should not be understood, as *forecasts*, but rather as plausible possibilities for planning purposes. The growth rates of government expenditure are intended as plausible policy settings;
2. In general, the aim for the base scenario is to set programming assumptions that are "neutral." The elasticities that help determine the government's revenue performance are taken to be somewhat higher than one in the initial projection year, and then to decline gradually toward one over the projection period. In general, it is inadvisable to apply econometric point estimates based on historical data for these values, for at least two reasons. The first is that future elasticities are likely to differ from historical elasticities. The second is that, say, if the elasticity of a given revenue line with respect to nominal GDP is assumed always to exceed (be less than) one, the projected revenue flow would rise (diminish) indefinitely as a percentage of GDP;
3. It is straightforward to set programming assumptions that adjust gradually over the projection period, using ("geometric") adjustment formulas. This is useful for several different assumption lines. For example, a large proportion of the assumptions are set as growth rates. These can be assumed to rise or diminish gradually from their initial projection values toward their final projection values. Another way to use a gradual adjustment would be for the elasticity of a given revenue line with respect to nominal GDP to take on an initial value somewhat different from one, but then gradually adjust toward a long-term value of one.

For the base scenario, the programming assumptions are as follows:

A 1: Projection results for the fiscal-space projection exercise (base scenario)

GENERAL GOVERNMNET FINANCIAL ACCOUNTS:	FY16-17	Average: FY17-18-FY21-22	FY21-22
Per cent of GDP			
(A) Total priority non-interest expenditure:	**12.8**	**12.9**	**12.7**
Total education expenditure	**7.9**	**7.8**	**7.8**
Total health expenditure	**4.4**	**4.5**	**4.4**
Total social-protection expenditure	**0.5**	**0.6**	**0.5**
Priority recurrent expenditure:	**12.8**	**12.9**	**12.7**
Recurrent education expenditure:	**7.9**	**7.8**	**7.8**
Expenditure on education staff	6.0	6.0	6.0
Non-staff recurrent education expenditure:	1.8	1.8	1.7
Recurrent education expenditure on goods and services	0.5	0.5	0.5
Other non-staff recurrent education expenditure	1.3	1.3	1.2
Recurrent health expenditure:	**4.4**	**4.5**	**4.4**
Expenditure on health staff	2.1	2.1	2.1
Non-staff recurrent health expenditure:	2.3	2.4	2.3

GENERAL GOVERNMNET FINANCIAL ACCOUNTS:	FY16-17	Average: FY17-18-FY21-22	FY21-22
Recurrent health expenditure on goods and services	2.1	2.2	2.1
Other non-staff recurrent health expenditure	0.2	0.2	0.2
Social-welfare expenditure	**0.5**	**0.6**	**0.5**
Expenditure on social welfare staff	0.1	0.1	0.1
Non-staff recurrent social welfare expenditure:	0.5	0.5	0.5
Recurrent social welfare expenditure on goods and services	0.0	0.0	0.0
Other non-staff recurrent social welfare expenditure	0.4	0.4	0.4
Priority non-recurrent expenditure:	**0.0**	**0.0**	**0.0**
Non-recurrent education expenditure	0.0	0.0	0.0
Non-recurrent health expenditure	0.0	0.0	0.0
Non-recurrent social welfare expenditure	0.0	0.0	0.0
(B) Tax and non-tax revenue (excl. external grants) (+):	**30.8**	**30.1**	**29.4**
Tax revenue:			
Income tax:	**12.0**	**12.0**	**12.0**
Company income tax	7.3	7.3	7.3
Personal income tax	4.7	4.7	4.7
Other income tax:	0.0	0.0	0.0
Taxes of international trade and transactions	**8.6**	**7.9**	**7.2**
Customs and other import duties (SACU)	8.6	7.9	7.2
Excises	0.0	0.0	0.0
Domestic taxes on goods and services	**7.3**	**7.3**	**7.3**
Value-added tax on internal transactions	7.3	7.3	7.3
Non-tax revenue (excl. external grants) (+):	**2.0**	**2.0**	**2.0**
(C) External grants (+):	**0.1**	**0.4**	**0.4**
Total government non-interest expenditure	35.1	35.2	35.0
(D) Total non-priority non-interest expenditure (-):	**-22.3**	**-22.3**	**-22.3**
(E) External-debt disbursements (+):	**0.9**	**0.9**	**0.9**
(G) Net internal financial flows (incl. internal interest) (+):	**3.3**	**3.8**	**4.3**
Net internal financial flows (excl. internal interest) (+):	5.8	6.6	7.8
Internal interest expenditure (-)	1.7	2.8	3.5

A 2: Projected priority expenditure (US dollars per child and exchange rate FY2016/17)

GENERAL GOVERNMNET FINANCIAL ACCOUNTS:	FY16-17	Average: FY17-18-FY21-22	FY21-22
US$ per child at prices and exchange rate of 2016			
(A) Total priority non-interest expenditure:	**$1 541.1**	**$1 679.5**	**$1 817.2**
Total education expenditure	**$946.3**	**$1 023.5**	**$1 107.4**
Total health expenditure	**$529.3**	**$583.2**	**$631.5**

GENERAL GOVERNMNET FINANCIAL ACCOUNTS:	FY16-17	Average: FY17-18-FY21-22	FY21-22
Total social-protection expenditure	**$65.4**	**$72.8**	**$78.3**
Priority recurrent expenditure:	**$1 541.0**	**$1 679.5**	**$1 817.2**
Recurrent education expenditure:	**$946.3**	**$1 023.5**	**$1 107.4**
Expenditure on education staff	$**725.4**	**$583.2**	$**631.5**
Non-staff recurrent education expenditure:	$220.9	$72.8	$**78.3**
Recurrent education expenditure on goods and services	$62.1	$**1 679.4**	$**1 817.0**
Other non-staff recurrent education expenditure	$158.8	$**1 023.4**	$**1 107.3**
Recurrent health expenditure:	**$529.3**	**$787.4**	**$861.1**
Expenditure on health staff	**$253.5**	$236.0	$246.2
Non-staff recurrent health expenditure:	$275.7	$66.4	$69.2
Recurrent health expenditure on goods and services	$255.9	$169.6	$176.9
Other non-staff recurrent health expenditure	$19.8	$583.2	$631.4
Social-welfare expenditure	**$65.4**	**$275.2**	**$300.9**
Expenditure on social welfare staff	**$9.7**	$308.0	$330.5
Non-staff recurrent social welfare expenditure:	**$55.7**	$285.9	$306.7
Recurrent social welfare expenditure on goods and services	**$4.9**	$22.1	$23.7
Other non-staff recurrent social welfare expenditure	**$50.8**	$72.8	$78.3
Priority non-recurrent expenditure:	**$0.1**	**$10.5**	**$11.5**
Non-recurrent education expenditure	$0.0	$**62.2**	**$66.8**
Non-recurrent health expenditure	$0.04	$**5.5**	$**5.9**
Non-recurrent social welfare expenditure	$0.0	$**56.7**	$**60.9**

A 3: Additional sensitivity analysis for the fiscal space projection exercise - enhanced expenditure on child protection

Scenario:	0	1	2	3	4	5	6
Assumptions that vary with scenarios:							
Real GDP growth rate (National currency)	Growth rate remains unchanged at 3.5% over the projection period.	Growth rate remains unchanged at 3.5% over the projection period.	**Growth rate gradually rises over the projection period; from 0.3% in FY2017/18 to 5.0% in FY21/22**	Growth rate remains unchanged at 3.5% over the projection period.	Growth rate remains unchanged at 3.5% over the projection period.	**Growth rate gradually over the projection period; from -2.7% in FY2017/18 to 2.0% in FY21/22**	Growth rate remains unchanged at 3.5% over the projection period
Elasticity of company-tax revenue with respect to nominal GDP	Remains at 1 over the projection period.	**Gradually increases over the projection period; from 1.0 in FY16/17 to 1.3 in FY21/22**	Remains at 1 over the projection period.	Remains at 1 over the projection period	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.
Elasticity of personal income tax revenue with respect to nominal GDP	Remains at 1 over the projection period.	**Gradually increases over the projection period; from 1.0 in FY16/17 to 1.3 in FY21/22**	Remains at 1 over the projection period	Remains at 1 over the projection period	Remains at 1 over the projection period	Remains at 1 over the projection period	Remains at 1 over the projection period.
Elasticity of value added tax revenue with respect to nominal GDP	Remains at 1 over the projection period.	**Gradually increases over the projection period; from 1.0 in FY16/17 to 1.3 in FY21/22**	Remains at 1 over the projection period	Remains at 1 over the projection period	Remains at 1 over the projection period	Remains at 1 over the projection period	Remains at 1 over the projection period.

Scenario:	0	1	2	3	4	5	6
Elasticity of education staff size with respect to child population	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.	**Gradually increases over the projection period; from 1.1 in FY17/18 to 1.5 in FY21/22.**	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.
Elasticity of health staff size with respect to total population	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.	**Gradually increases over the projection period; from 1.1 in FY17/18 to 1.5 in FY21/22.**	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.
Elasticity of social protection expenditure to child population	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.	**Gradually increases over the projection period; from 1.1 in FY17/18 to 1.5 in FY21/22.**	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.
Elasticity of non-priority recurrent expenditure to nominal GDP growth	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.	Remains at 1 over the projection period.	**Gradually decreases over the projection period; from 0.95 in FY17/18 to 0.75 in FY21/22.**	Remains at 1 over the projection period.	Remains at 1 over the projection period
SACU transfer growth rate	Remains at 3.3 over the projection period.	Remains at 3.3 over the projection period.	Remains at 3.3 over the projection period.	Remains at 3.3 over the projection period.	Remains at 3.3 over the projection period.	Remains at 3.3 over the projection period.	**Decreases from 3.3% in FY16/17 to -4.2% in FY21/22**
Average tax revenue/GDP. FY2016–2021	30.1%	30.6%	30.1%	30.1%	30.1%	30.5%	28.6%

Scenario:	0	1	2	3	4	5	6
Average priority expenditure/GDP. FY2016–2021	12.9%	12.9%	12.9%	12.9%	12.9%	13.1%	12.9%
Average priority expenditure per child (US$ at FY2016 prices and exchange rate). FY2016–2021	$1.679.5	$1.679.5	$1.684.7	$1.684.7	$1.684.7	$1.631.4	$1.679.5
Net internal debt flow/GDP. FY2016–2021	2.8%	2.8%	2.8%	2.8%	2.8%	36%	3.0%
Total government debt/GDP. FY2021	64.0%	63.1%	64.1%	63.1%	63.1%	66.2%	67.7%

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