Highlights of the 2022/23 Federal Government Budget Proclamation

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TAKEAWAYS

- The total approved federal budget for the 2022/23 fiscal year (FY) is Ethiopian Birr (ETB) 786.6 billion. It shows a 40 per cent increase from the previous fiscal year. However, in real terms, the budget has increased by only 4.7 per cent due to high inflation in the country.

- Of the total approved budget, 71.6 per cent is allocated for federal government expenditure, 26.6 per cent for regional subsidies (general-purpose grants) and 1.8 per cent for capital projects towards achieving the Sustainable Development Goals (SDGs).

- The federal budget allocation between capital and recurrent expenditure has significantly moved away from previous trends. Compared to last year, the share allocated to capital expenditure has declined from 53 per cent to 39 per cent while the share of recurrent spending has increased from 47 per cent to 61 per cent. This is the lowest share of budget allocated for capital investments by the federal government in a decade. The decline in growth-promoting capital expenditures could have an adverse effect on the economy.

- The federal budget is financed from both domestic and external sources. Around 90 per cent of the approved budget is planned to be financed from domestic sources (56 per cent from domestic revenue and 34 per cent from domestic loans), while the remaining 10 per cent is to be financed from external assistance (5 per cent) and external loans (5 per cent).

- Compared to the last fiscal year, domestic borrowing has increased from ETB 66.8 billion to ETB 266.1 billion, which is close to a four-fold increase. The government is heavily relying on domestic borrowing to finance its budget deficit which may have negative implications for credit availability to the private sector, and it will be inflationary if there is direct financing from the central bank, the National Bank of Ethiopia.
- When comparing nominal budget shares allocated to different sectors, the significant shift this year is the increased budget allocation for debt servicing and national defence and the decline in the share of the budget for federal level implementation on the government priority sectors of education, health, road, water and energy, as well as agriculture and rural development.
- Around 34 per cent of the federal budget is allocated to what the government considers pro-poor sectors (namely education, health, road construction, water and energy, and agriculture) which shows a decline of 20.6 percentage points compared to its share in 2021/22. Although the federal government executes only a portion of the national budget allocated for these sectors, this is the first time that the nominal allocations for the federal government's education and health budgets have declined revealing the stress on government finances with concerning implications for social service delivery.
- Federal budget allocation for food security (safety net programmes) and job creation has increased from ETB 17.1 billion in 2021/22 to ETB 19.0 billion in 2022/23, corresponding to an 11.7 per cent increase in nominal terms and a 16.7 per cent decline in real terms. However, for the total federal budget on food security (safety net programmes) and job creation the government's treasury contribution has declined from 46.1 per cent in 2021/22 to 38.7 in 2022/23, with external assistance expected to finance 59.2 per cent in 2022/23. This is indicative of the budget constraint that the federal government is facing and has an adverse impact on the sustainability of social protection financing through domestic sources.

1. Background and Context

The federal government of Ethiopia approved a federal budget of Ethiopian Birr (ETB) 786.6 billion for the 2022/23 fiscal year (8 July 2022 to 7 July 2023). The budget consists of capital and recurrent expenditure for execution by the federal government, general-purpose grants (non-earmarked block grants) to sub-national regional governments, and additional capital budgets allocated to regions to help towards achieving the Sustainable Development Goals (SDGs). As a result of the conflict in the country, drought, the Russia-Ukraine war, and other shocks in different parts of the country, the performance of the economy was adversely affected in the 2021/22 fiscal year. Economic growth for 2021/22 is expected to be 6.6 per cent, and is lower than the projected 8.7 per cent.

The presentation of the federal budget for the fiscal year (FY) 2022/23 (which is the Ethiopian Fiscal Year (EFY) 2015) highlighted that the Ethiopian economy is currently facing multiple challenges that are affecting the country's macro-economic stability. Some of these are high inflation, foreign exchange shortage, high debt burden, and low domestic resource mobilization. The growing humanitarian need due to the drought, conflict, increased spending on defense, as well as other shocks have exacerbated the fiscal stress. The fiscal deficit has further widened due to a decline in foreign assistance and the challenge of increasing resources mobilized domestically.

The federal budget presentation outlined some assumptions on major macroeconomic indicators which are used as a basis for formulating the FY 2022/23 budget. The economic growth rate for 2022/23 is forecasted to be 9.2 per cent. While the average inflation rate for 2021/22 (July 2021-June 2022) was 33.7 per cent, through addressing structural and policy issues the plan is to bring the average inflation rate to 11.9 per cent in 2022/23. Nominal GDP is expected to increase by 22.2 per cent. The value of goods imported, which is taken as the main assumption for forecasting government revenue to be collected from customs duty and taxes, is forecasted to increase by 10.2 percent. With regards to fiscal policy, the government will follow the direction of fiscal consolidation to relieve the fiscal pressure. The priority for government expenditure will be focused on debt repayment, humanitarian aid, rehabilitation and strengthening the national defense.

2. FINANCING SOURCES OF THE BUDGET

The federal budget approved by the House of Peoples' Representatives of the Ethiopian parliament for FY 2022/23 is ETB 786.6 billion. It has increased by 40 per cent in nominal terms when compared with the budget approved for the FY 2021/22. With annual average inflation standing at 33.7 per cent in July 2022, the real value of the budget has increased by 4.7 per cent[1]. High inflation is significantly undermining the nominal budget increase and has become one of the most important sources of macro-economic instability that the country is committed to address in the coming fiscal year.

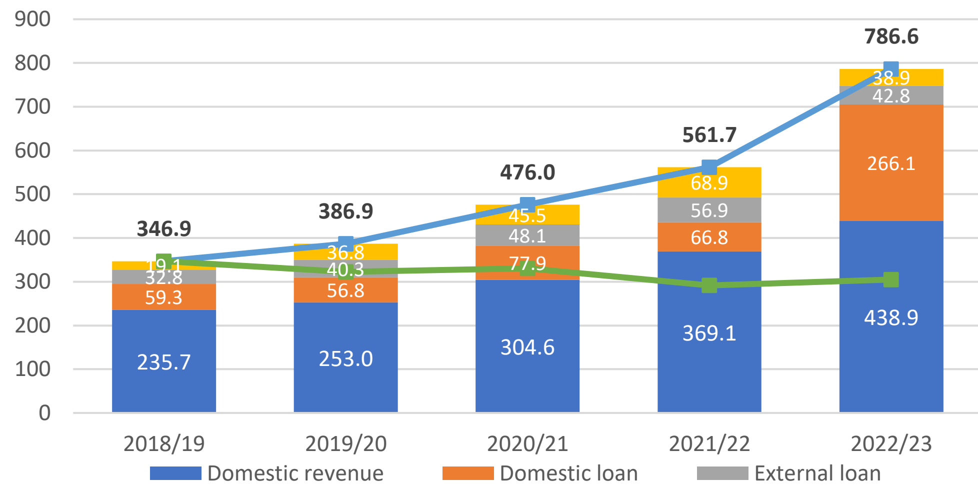
The approved federal budget is financed from both domestic and external sources. Domestic sources mainly comprise tax, non-tax, and capital revenue, while external sources are mainly borrowing and assistance in the form of grants from development partners. Around 89.6 per cent of the approved budget is to be financed from domestic sources, while the remaining 10.4 per cent is to be financed via external assistance and external loans.

- ETB 438.9 billion (55.8 per cent of the total budget) is planned to be mobilized from domestic revenue.
- ETB 266.1 billion (33.8 per cent of the total budget) is intended to be mobilized from domestic borrowing.
- ETB 42.8 billion (5.4 per cent of the total budget) is forecasted to be obtained from external sources in the form of loans.
- ETB 38.9 billion (4.9 per cent of the budget) is in the form of grants/assistance from bilateral and multilateral development partners.

Domestic revenue for 2022/23 is forecasted to increase by 19 per cent from what was budgeted in 2021/22. Compared to the 2021/22 FY, the share of budget to be financed from domestic revenue has declined from 66 per cent to 55.8 per cent. On the other hand, domestic borrowing has increased from ETB 66.8 billion to ETB 266.1 billion, which is close to a four-fold increase. The government is heavily relying on domestic borrowing to finance its budget deficit which may have negative implications for credit availability to the private sector, and it will be inflationary if there is direct financing from the central bank, the National Bank of Ethiopia. The government plans to reduce the inflationary pressure that could arise from increased domestic borrowing by avoiding direct financing from the National Bank of Ethiopia and relying on borrowing through issuing treasury bills. The amount of financing from external loan and external assistance has declined by 35 per cent from ETB 125.7 billion to ETB 81.7 billion.

[1] Real values are calculated using 2018/19 as a base year.

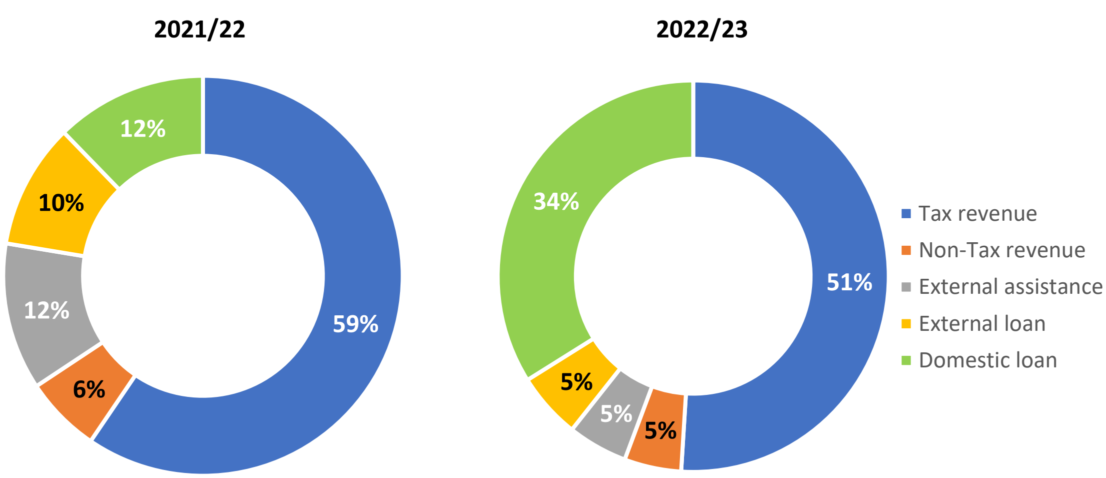
Figure 1: Sources of finance for the federal budget, 2018/19–2022/23 (in billion ETB)



Source: Data from the Ministry of Finance (MoF). Real values are calculated by the authors, with 2018/19 as the base year.

For the 2022/23 budget year, the share of tax revenue out of the total federal budget is 51 per cent, showing a decline of 8 percentage points from the previous fiscal year (Figure 2). The share of non-tax revenue has declined from 6 per cent to 5 percent. The share of total domestic revenue has declined from 65 per cent to 56 percent. On the other hand, the share of domestic loans out of total federal budget increased by 22 percentage points. The contribution of external assistance to the federal budget is expected to decline by 7 percentage points, while the share of external loans declines by 1 percentage point. It is important to note that the source of financing presented below applies to the federal budget only. In addition to the general-purpose grants (also referred to as non-earmarked block grants or subsidies) provided by the federal government to sub-national regional governments, regions also raise their own revenues and use the total resource envelope to plan their own budgets to be approved by their respective autonomous regional parliaments.

Figure 2: Share of financing sources of the total federal budget for 2021/22 and 2022/23 (per cent)

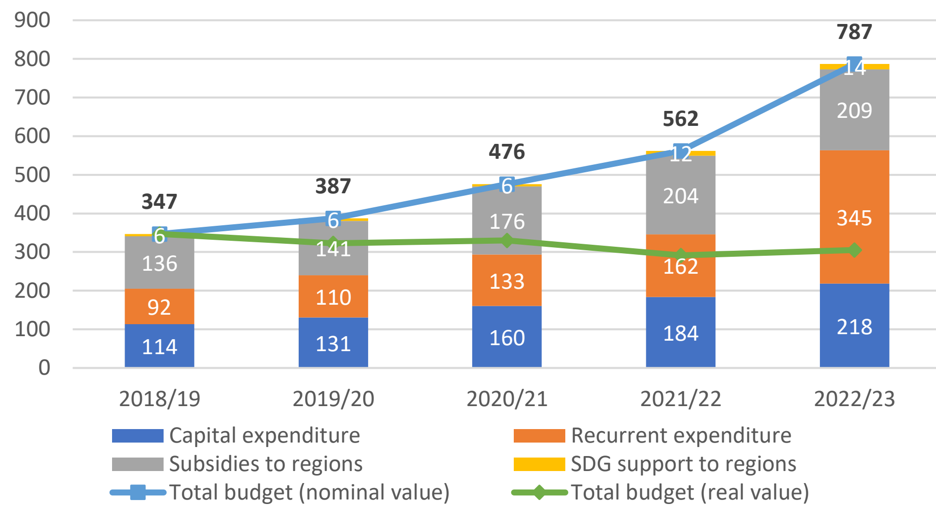


Source: Data from MoF.

3. Federal Budget Allocation

Of the total approved budget of ETB 786.6 billion, 71.6 per cent is allocated for federal government expenditure (ETB 563.2 billion), 26.6 per cent (ETB 209.0 billion) for regional governments responsible for sub-national budget allocation, and 1.8 per cent (ETB 14 billion) is earmarked for supporting capital projects towards the achievement of Sustainable Development Goals (SDGs) at the sub-national level. The nominal budget allocated for federal government spending has increased by 62.7 per cent compared to 2021/22 (Figure 3). Block grants to regional governments have also shown a 2.7 per cent increase compared to last year. The budget for supporting the achievement of SDGs at the sub-national level has increased by 16.6 per cent from ETB 12 billion to ETB 14 billion. However, when accounting for inflation, the total value of the federal budget has increased by only 4.7 per cent[2] (versus a 40 per cent increase in nominal terms). For the budget increase to be realized in real terms, the government should take strong measures to control the inflation rate.

Figure 3: Federal budget allocation trends, 2018/19–2022/23 (in billion ETB)



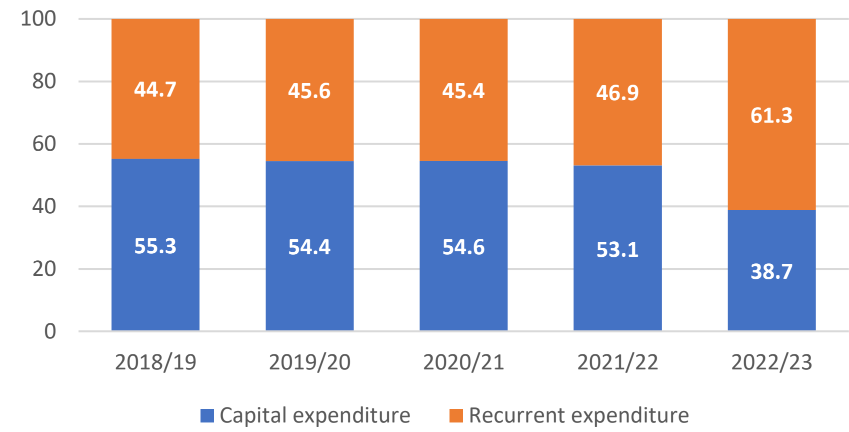
Source: Data from MoF. Real values are calculated by the authors, with 2018/19 as the base year.

3.1. Federal Government Budget

Out of the total federal budget, ETB 562.2 billion are allocated to be executed by the federal government, a 63 per cent increase from the 2021/22 budget. Out of this, ETB 345 billion (61.3 per cent) are budgeted for federal recurrent expenditure and ETB 218 billion (38.7 per cent) for federal capital spending. Compared to 2021/22, the recurrent and capital budgets for the federal government have increased by 112.8 per cent and 18.8 per cent, respectively. The high increase in the recurrent budget is driven by increased allocation to debt servicing, transfers/subsidies, and increased recurrent spending on national defence. Compared to last year's budget (2021/22), the share of capital spending has declined from 53 per cent to 39 per cent while the share of recurrent spending has increased from 47 per cent to 61 per cent. This is the lowest share of budget allocated for capital investments by the federal government in a decade. The decline in growth-promoting capital expenditures could have a negative effect on the economy.

[2] Using 2018/19 as a base year and 2021/22 fiscal year's annual moving average inflation of 33.7 per cent.

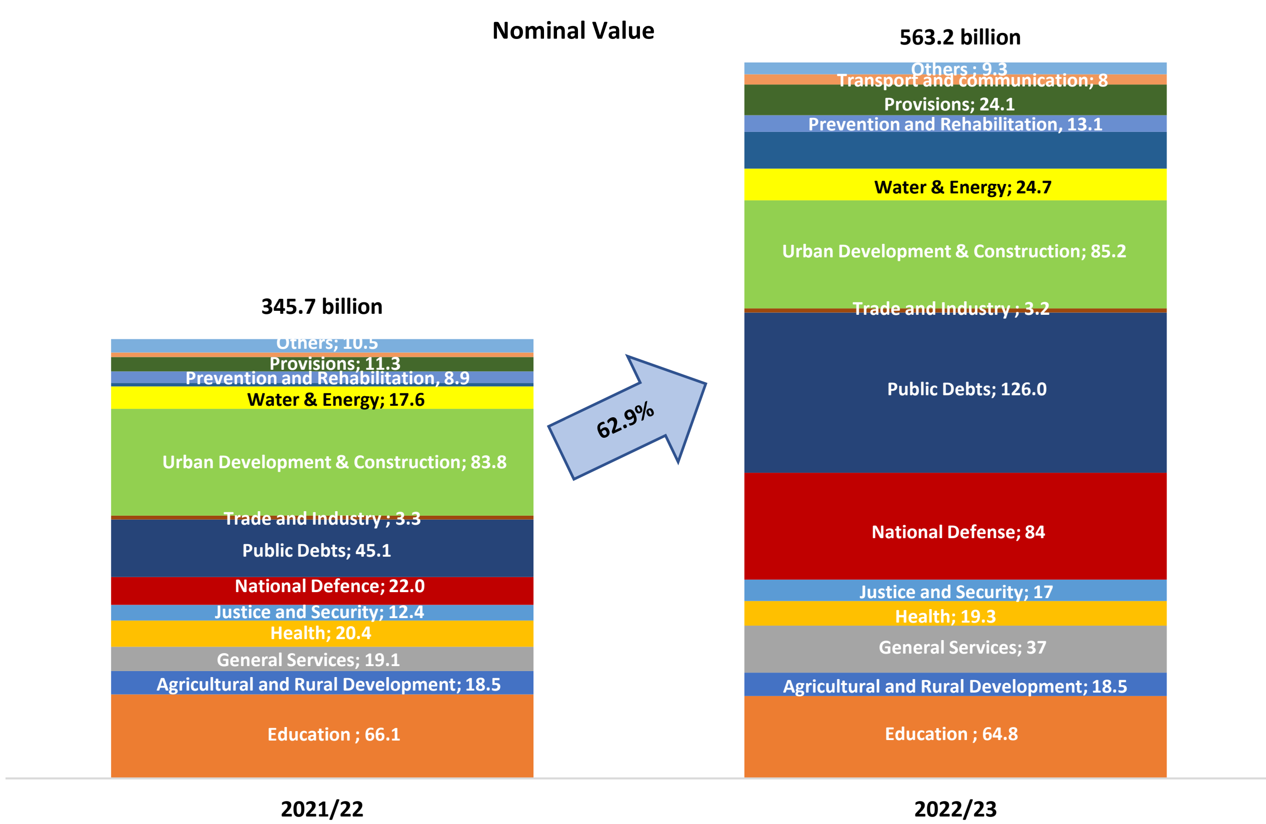
Figure 4: Federal government budget by capital and recurrent expenditures (per cent)

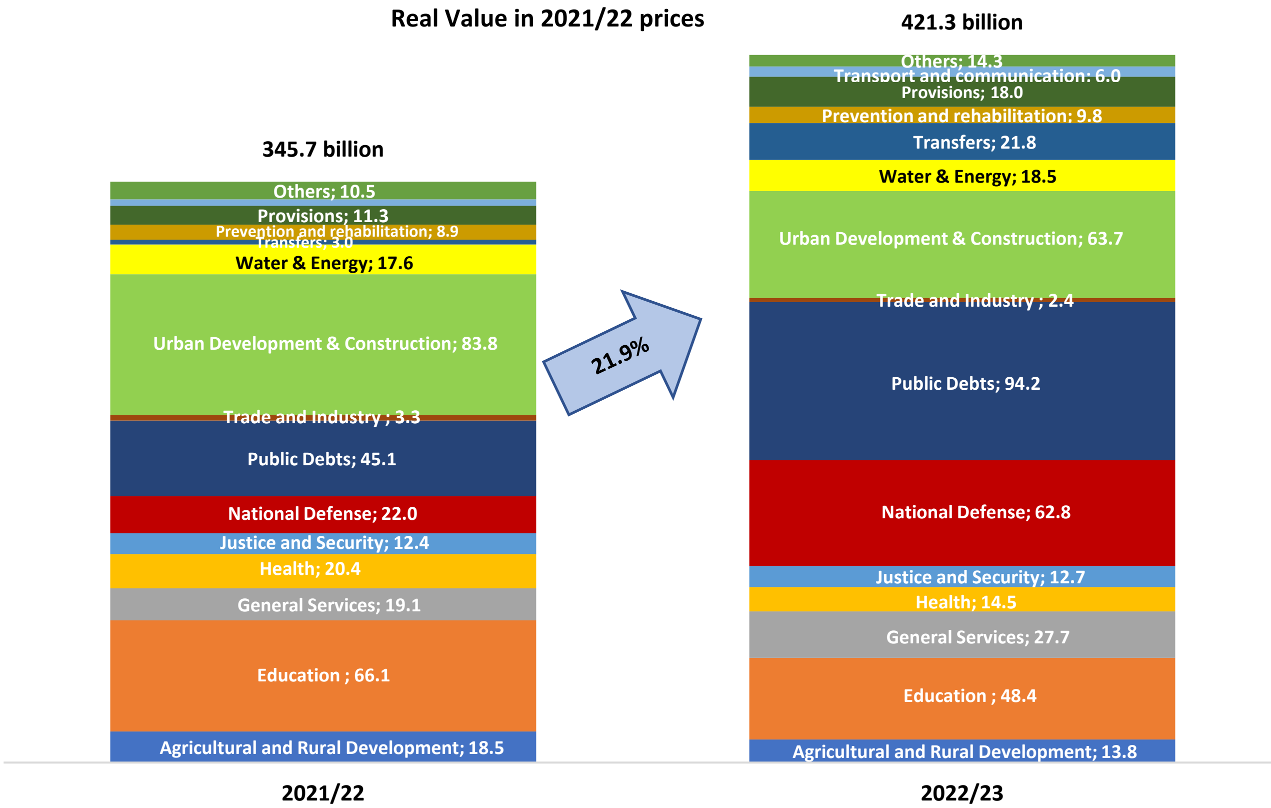


Source: Data from MoF.

The significant shift in this year's federal budget is the increased allocation for debt servicing and national defense and the decline in the federal budget for government priority sectors of education, health, road, water and energy, as well as agriculture and rural development. Compared to the federal budget in 2021/22, the budget allocated for national defense has increased by 281 per cent while allocation for public debts has increased by 179 per cent (Figure 5). Allocation for transfers/subsidies has also increased by more than eight-fold.

Figure 5. Federal government budget in nominal and real terms (2021/22 and 2022/23)





Source: Data from Ministry of Finance. **Notes:** 'Others' is composed of budget for Organs of State; Culture and Sport; Transport and Communication; Mining; and Labour and Social Affairs. Real values for 2022/23 are calculated using the 2021/22 average inflation rate of 33.7 per cent.

The three budget lines with the highest allocation are public debts, national defense, and roads accounting for ETB 126 billion (22.4 per cent), ETB 85.2 billion (14.9 per cent), and ETB 66.2 billion (11.8 per cent) of the federal government's budget respectively (Table 1). Together, public debt servicing and national defense make up around 37 per cent of the federal budget. The share of debt financing from the federal budget increased from 13 per cent to 22.4 per cent between 2021/22 and 2022/23. Budget required for debt financing is increasing due to a widening fiscal deficit caused by increased expenditure for defense and emergency response/humanitarian assistance for populations affected by conflict, drought, and other shocks. This increasing expenditure burden has resulted in increased borrowing, pushing the economy into a high risk of debt distress.

Table 1: Allocation and share of the federal government budget by sector

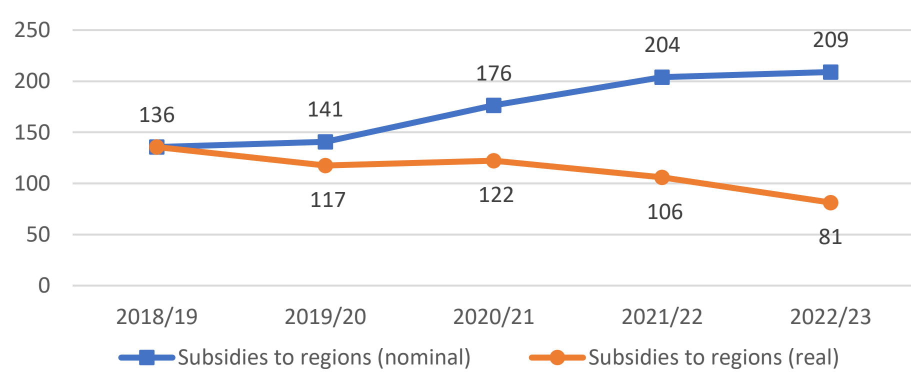
	Budget allocated for 2022/23 (ETB billion)	Share of budget for 2022/23 (per cent)	Share of budget for 2021/22 (per cent)	Change in the share of budget allocated between 2022/23 and 2021/22
Public Debts	126.0	22.4	13.0	9.3
National Defense	84.0	14.9	6.4	8.6
Roads *	66.2	11.8	19.5	-7.7
Education	64.7	11.5	19.1	-7.6
General Services	37.0	6.6	5.5	1.0
Transfer	29.1	5.2	0.9	4.3
Water & Energy	24.7	4.4	5.1	-0.7
Provisions	24.1	4.3	3.3	1.0
Health	19.3	5.9	3.4	-2.5
Urban Development *	18.9	3.3	4.7	1.4
Agriculture and rural development	18.5	5.4	3.3	-2.1
Justice and Security	17.0	3.6	3.0	-0.6
Prevention and Rehabilitation	13.1	2.6	2.3	-0.3
Others **	22.2	5.0	3.6	-1.4

Source: Data from Ministry of Finance. **Notes:** * "Roads" and "urban development" are jointly categorized as "urban development and construction" in the federal government budget classification. ** "Others" is composed of budget for Organs of State; Culture and Sport; Transport and Communication; Mining; and Labour and Social Affairs. Real values for 2022/23 are calculated using the 2021/22 average inflation rate of 33.7 per cent.

3.2. Federal Subsidies (non-earmarked block grants) to Regional Governments

Every fiscal year, the federal government allocates budget subsidies for regional governments based on a formula developed by the House of Federation. Looking at the trend in recent years, the nominal value of the budget allocated to regions has increased by 53.7 per cent between 2018/19 and 2022/23 (Figure 6). For the fiscal year 2022/23, this corresponds to ETB 209 billion, an increase of 2.5 per cent from its value in 2021/22. However, in real terms, the value of the budget has declined by 23.2 per cent due to high inflation.

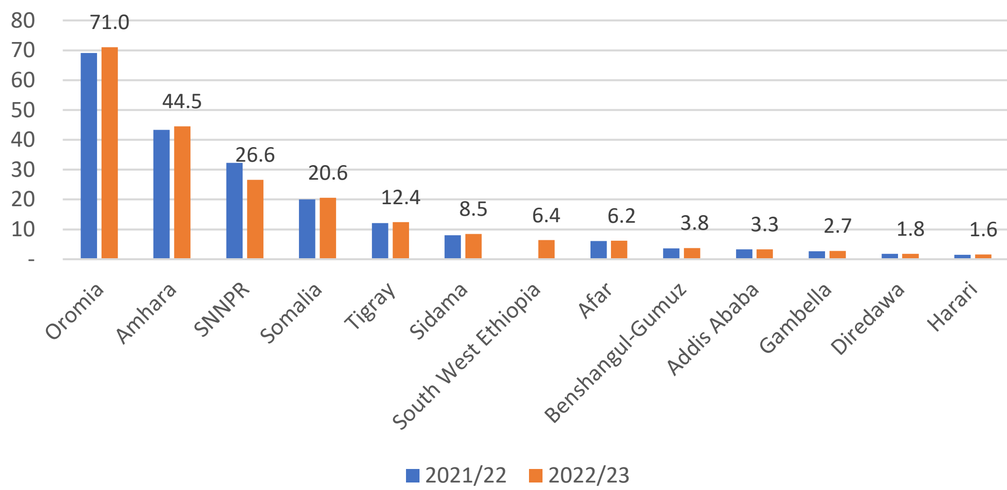
Figure 6. Federal government subsidies to regions in nominal and real terms, 2018/19–2022/23 (in billion ETB)



Source: Data from MoF. Real values are calculated by the authors, with 2018/19 as the base year.

Out of the total budget allocated to the regions, ETB 71 billion is allocated to Oromia regional state (Figure 7). Amhara, SNNP, Somali, Tigray, and Sidama regions receive ETB 44.5 billion, 26.6 billion, 20.6 billion, 12.4 billion and 8.5 billion, respectively. South West Ethiopia Peoples' Region is a new regional state in southwestern Ethiopia which split from the Southern Nations, Nationalities, and Peoples' region (SNNPR) in November 2021. The decline in the budget allocated for SNNPR compared to its 2021/22 budget is due to a shift of some of the budget to the newly established South West Ethiopia Peoples' region. In 2022/23, ETB 6.4 billion is allocated to South West Ethiopia Peoples' region. Afar, Benshangul-Gumuz, Addis Ababa, Gambella, Dire Dawa and Harari receive ETB 6.2 billion, 3.8 billion, 3.3 billion, 2.7 billion, 1.8 billion and 1.6 billion, respectively.

Figure 7: Trends of federal subsidies across regions, 2021/22–2022/23 (in billion ETB)



Source: Data from MoF.

3.3. Support for SDG Implementation in Regions

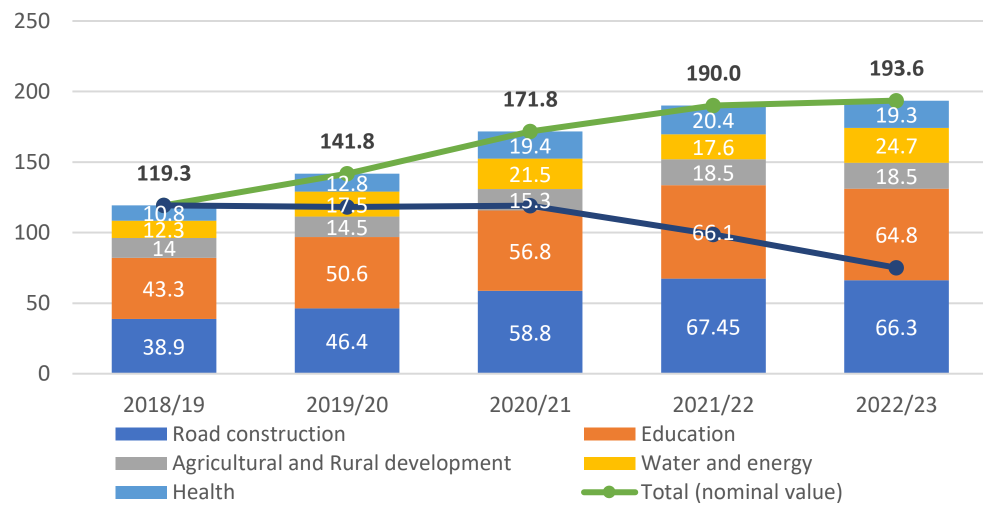
The federal government has been providing budgetary support to regions to help achieve the Sustainable Development Goals (SDGs). According to the 2011/12 FY proclamation, this support for capital expenditure is to be utilized for financing specific sectors that are determined in agreement between the Ministry of Finance and regional governments. The budget is intended to be allocated to poor and vulnerable groups in society, to ensure equitable service delivery and access to productive resources. In 2022/23, ETB 14 billion is to be transferred to regional states as per the grant formula for implementation of the Sustainable Development Goals (SDGs), which is 16.7 per cent higher than the amount allocated in 2021/22.

4. Federal Allocations to Sectors of Focus

The federal budget only shows the resources that are allocated across sectors at the federal government level. At the regional level, the resource envelope encompasses federal subsidies and resources mobilized within the regions. The total regional budget is then allocated between sectors by the regions themselves for sub-national level implementation. The sector budget analysis in this section focuses on the budget to be implemented by the federal government only. This understates the overall budget allocated for each sector as the sub-national governments also allocate and execute budgets for these sectors.

The federal government budget allocation for selected sectors – education, health, water and energy, agricultural and rural development, and road construction – has shown an increasing trend over the years in nominal terms (Figure 8). Compared to 2021/22, the budget allocated to these sectors increased by only 2 per cent in nominal terms in 2022/23. In real terms however, the budget allocation has declined by 23.8 per cent. The sectoral level allocation indicates that nominal budgets for education and health have declined by 2 per cent and 5 per cent while in real terms the decline is 26 per cent and 29 per cent, respectively. The nominal allocation for water and energy increased by 40 per cent which is a 5 per cent increase in real terms.

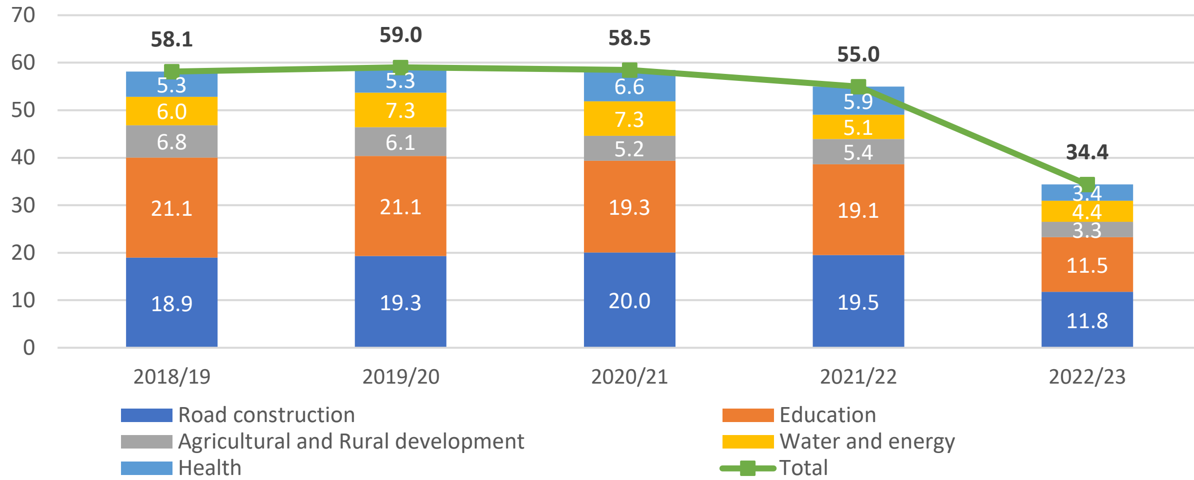
Figure 8: Federal budget allocation to selected sectors, 2018/19–2022/23 (in billion ETB)



Source: Data from MoF. Real values are calculated by the authors, with 2018/19 as the base year.

Around 34 per cent of the federal budget is allocated to what the government considers pro-poor sectors, namely education, health, road construction, water and energy, and agriculture (figure 9). This has shown a decline of 20.6 percentage points compared to its share in 2021/22. The share of the 2022/23 federal budget allocated to these sectors at the federal level is 11.8 per cent for road construction, 11.5 per cent for education, 3.3 per cent for agriculture, 4.4 per cent for water resources and energy, and 3.4 per cent for health (Figure 9). Compared to the approved budget for 2021/22, the budget share for education, health, and water and energy has declined by 7.6, 2.5 and 0.7 percentage points, respectively. The total share allocated to these priority sectors has declined from 55 per cent in 2021/22 to 34.4 per cent in 2022/23. It should be noted that the analysis in this section understates the overall budget allocated for each sector at national level, especially for education and health, as the sub-national governments execute most of Ethiopia's education and health budgets and the federal government is mainly responsible for higher education and tertiary health services. Regardless, this is the first time that the nominal allocations for the federal government education and health budgets have declined revealing the stress on government finances with concerning implications for social service delivery.

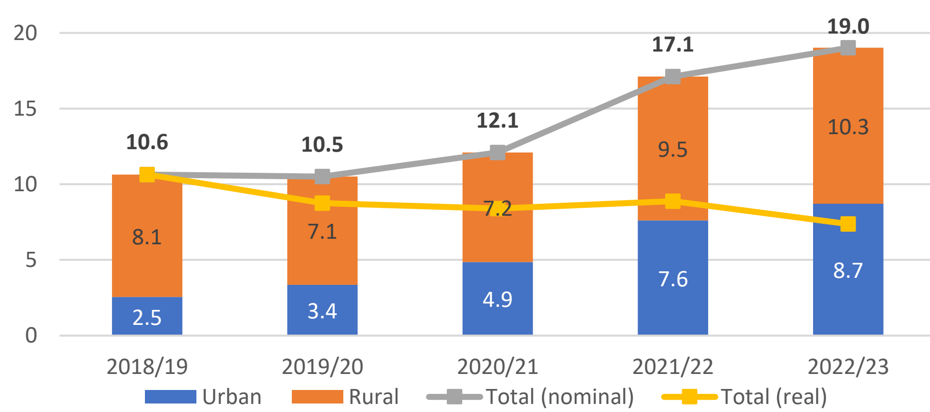
Figure 9: Share of the federal budget allocated to selected sectors, 2018/19–2022/23 (per cent of budget for the federal government)



Source: Data from MoF.

The federal budget allocated to social protection has been increasing over the years, particularly for food security and job creation. It rose from ETB 17.1 billion in 2021/22 to ETB 19.0 billion in 2022/23, which is a 11.7 per cent increase in nominal terms (Figure 10). The increase in the nominal budget allocation mainly came from the urban food security and job creation component, which increased by 14 per cent, while the rural component increased by 8 per cent in nominal terms. In real terms, the budget for food security (mainly for safety net programmes) and job creation has declined by 16.7 per cent, corresponding to a budget share decline from 4.9 per cent to 3.5 per cent.

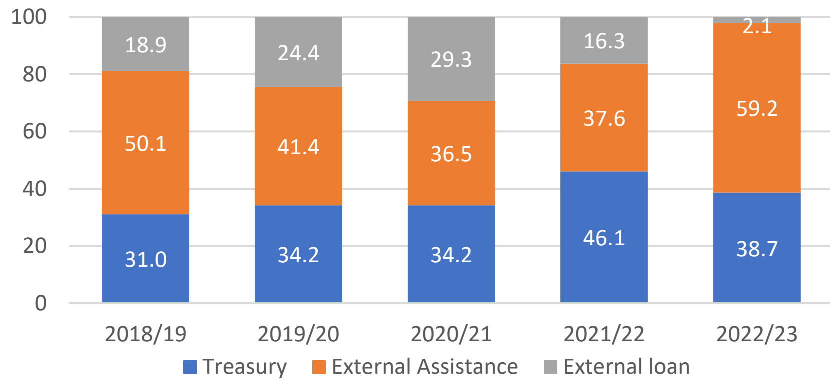
Figure 10: Share of the federal budget allocated to food security and job creation (in billion ETB)



Source: Data from MoF.

The increase in the nominal budget allocation for social protection is to be mainly financed from external assistance. The contribution from foreign assistance is expected to increase from 37.6 per cent to 59.2 per cent. As can be seen from Figure 11, the government treasury contribution to safety net programmes and job creation declined from 46.1 per cent to 38.7 per cent. Not only the share, but the contribution from treasury has also declined in absolute terms by 6.7 per cent. On the other hand, the financing from external assistance and loans has increased by 26.4 per cent while its share increased by 7.4 percentage points. The decline in contribution from the federal treasury is indicative of the budget constraint that the federal government is facing. This has an adverse impact on the sustainability of social protection financing through domestic sources.

Figure 11: Share of the federal budget allocated to food security and job creation (per cent)

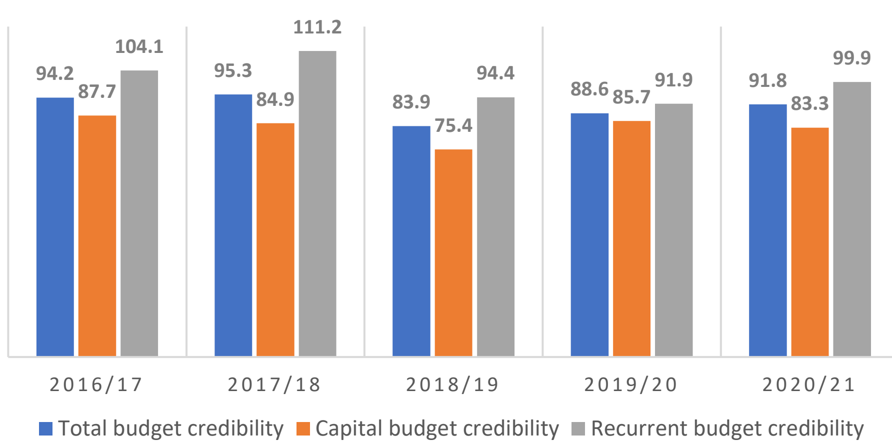


Source: Data from MoF.

5. Federal Government Budget Credibility

Budget credibility is measured as the proportion of actual expenditure at the end of the fiscal year out of the budget that was approved at the start of the fiscal year. For a budget to be an effective instrument, it needs to be credible. In this regard, budget credibility analysis for the period 2016/17-2020/21 reveals that the variation between the total amount of federal expenditure and the total federal budget that was originally approved was on average around 9.3 per cent (Figure 12). For 2020/21, the budget credibility was 91.8 per cent. In analysing the budget credibility disaggregated by budget components, there appears to be lower budget credibility for capital expenditure at 83 per cent compared to 100 per cent for the recurrent budget. Recurrent budget credibility remains higher than capital budget credibility since a greater share of the recurrent budget is salary expense and is therefore more predictable. Some of the main reasons for lower capital budget credibility are delays in procurement, lack of project management capacity, and the shortage of foreign currency to acquire goods required to make capital investments.

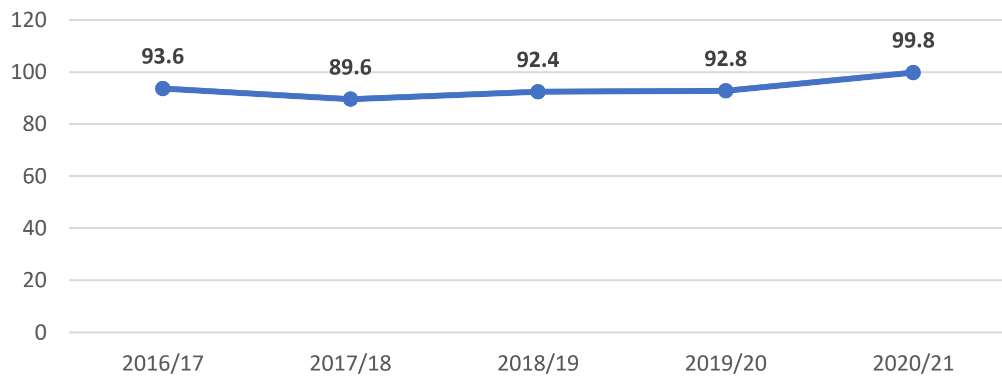
Figure 12: Federal government budget credibility (per cent)



Source: Data from MoF.

As part of the budget credibility assessment, planned federal domestic revenue is compared to the actual domestic revenue collected by the federal government. During the period 2016/17 to 2020/21, on average 93.7 per cent of the planned federal domestic revenue was collected by the end of the fiscal year (Figure 13). The implementation of various tax reforms, with their increased focus on improving tax administration, has contributed to the improvement of domestic revenue budget credibility. Federal domestic revenue performance was 99.8 per cent of the budgeted amount for 2021/22. Since tax comprises around 80 per cent of overall federal domestic revenue, maintaining an effective tax policy and further improving its implementation along with tax compliance and tax administration is essential to maintain the improvement in federal domestic revenue mobilization.

Figure 13: Performance of the federal government domestic revenue: actual federal domestic revenue collected as a percentage of planned federal domestic revenue



Source: Data from MoF.

Annex 1: Timeline for the State Budget Process in EFY 2015 (2022/23)

Planning/Budgeting cycle	Ethiopian Fiscal Year	Gregorian Calendar
Planning cycle		
1. Macro-Economic and Fiscal Framework (MEFF)	By Tahisas 30	By 08 January
1.1 MEFF preparation	Until Hidar 30	Until 09 December
1.2 MEFF approval	By Tahisas 30	By 08 January
3. Notification of the three-year subsidy estimates	By Tir 01	By 09 January
4. Preparation of the annual fiscal plan	By Tir 15	By 23 January
Budgeting cycle		
A. Pre-preparation of budget by public bodies		
1. Pre-preparation of budget	Before Yekatit 01	Before 08 February
2. Notification of annual subsidy	By Yekatit 01	By 08 February
3. Issuing the budget call	By Yekatit 01	By 08 February
4. Budget requests	By Megabit 15	By 24 March
5. Preparation of the draft recommended budget	Megabit 15–Ginbot 15	24 March–23 May
6. Review of the recommended budget by the Council of Ministers	Ginbot 16–Ginbot 25	24 May–02 June
B. Budget approval		
7. Legislative approval and appropriation of the budget	Sene 01–Sene 30	08 June–07 July
C. Implementation		
8. Notification of approved budget	Hamle 01–Hamle 07	08 July–14 July
9. Accepting the approved budget and action plan preparation	Hamle 08–Hamle 30	15 July–06 August
10. Implementing the approved budget	Hamle 01–Sene 30	08 July 2022 –07July 2023

This federal government level budget brief was produced by Fanaye Tadesse Techane ftechane@unicef.org with guidance and contributions provided by Zeleka Paulos zpaulos@unicef.org. The main objective of this budget brief is to synthesize complex budget and expenditure information so that it is easily understood by stakeholders, to foster discourse and to inform policy and financial decision-making processes. The analysis presents budget and expenditure that are recorded on-budget by the Ministry of Finance. UNICEF's work on Public Finance for Children is undertaken under the leadership of Samson Muradzikwa.

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