FISCAL SPACE ANALYSIS

2019

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Executive Summary

Economic growth in Mozambique has slowed significantly since 2015, with the slowdown exacerbated by the discovery of the large undisclosed loans. Growth started decelerating in 2015 as international commodity prices declined. This combined with the effects of the El Nino induced drought in the Southern part of the country drove inflation and the currency depreciated. The depreciation was further accelerated in the months following the discovery of the hidden debts. Foreign Direct Investment, especially in the non-megaproject economy, halved between 2015 and 2017. This affected activity of the private sector already faced with the high cost of credit as the monetary policy was tightened to respond to inflationary pressures. As a result, GDP growth slowed to a low of 3.8 percent in 2016 and 3.7 percent in 2017.

While the budget has been expanding in nominal terms, priority expenditures - defined as those that are directly beneficial to children in the sectors of education, health, social protection and water, sanitation and hygiene (WASH) - have declined in real terms in 2015 and 2016. Government spending on economic and social sectors, including the sectors mentioned above, declined to 48 percent of the total expenditure in 2016. On the other hand, debt servicing costs rose to 21 percent of the budget. According to the IMF's Article IV report, these costs are expected to increase further to 30 percent of the budget in the medium term. Slow growth in economic activity has implications for the growth in state revenues. The suspension of the IMF program in the country and general budget support by donors has also exerted pressure on the fiscal envelope. Moreover, rising debt servicing costs are crowding out priority expenditures.

The priority sectors are also faced with problems of allocative efficiency. With increasing demand for basic social services in the light of a rapidly rising population, there is urgent need to increase the efficiency of spending in order to achieve better results with limited resources. A comparison on spending and outcomes in sectors like education and health shows that Mozambique spends more compared to its peers to achieve similar results. Moreover, outcomes remain below expectations. For instance, despite significant investments in the sector, less than half of the children enrolled complete primary education. Progress in reducing infant and maternal mortality has been lagging. Social action programs have reached less than 20 percent of the targeted households. Similarly, about half the population still does not have access to clean drinking water while a relatively small proportion use improved sanitation facilities. Increase in spending in these sectors does not clearly reflect the needs on the ground. Spending is not equitable across provinces and does not target the poorest quintiles of the population effectively.

In a baseline status-quo scenario in which economic growth is averaging around 3.8 per cent, spending on priority sectors would increase but create a large financing gap (fiscal gap). 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 increase from US$97.6 in 2018 to US$103.5 in 2024. The average net internal debt flow would be 1.0 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 gradually decline from 4.7 per cent of GDP in 2018 to 1.1 per cent of GDP by 2024. At the same time, fiscal consolidation will lead to a moderate decrease in debt (both internal and external), reaching around 103% of GDP in 2024.

Mozambique's priority expenditure as well as fiscal gap is heavily affected by the attained level of GDP growth. Assuming an increase of GDP growth to average 4.4 per cent between 2018 and 2024 would lead to an increase in average priority expenditure per child from US$136.6 (base scenario) to US$138.4. The internal financing flow would decline to 0.8 per cent of GDP and debt stock would decrease to 98 per cent of GDP in 2024. Conversely, lower rates of GDP growth to average 3.3 per cent between 2018 and 2024 would lead to a decrease in average priority expenditure per child from $136.6 in the base scenario to $134.8. Moreover, internal debt flow would increase to 1.2 per cent of GDP, with the debt stock increasing to 108.4 per cent in 2024.

Attracting external grants would enable Mozambique to increase priority expenditure. Assuming Mozambique succeeds to obtain 1.6 per cent of GDP in grants by 2024, external debt would decline to 102.3 per cent and fiscal gap would be 0.9 per cent. Thus, external grants would enable the country to increase average per child priority expenditure, from US$136.6 in the base scenario to US$140 without further increasing the fiscal gap. On the other hand, if donor support for priority areas would decline to 0.5 per cent of GDP, Mozambique's average priority expenditure per child would decline by $4.6 to $132. Internal debt flow would increase to 1.1 per cent of GDP and the debt stock would also rise to 103.4 per cent of GDP by 2024.

A combination of higher GDP growth and higher donor support to priority areas would allow the country to realize the largest increase in priority expenditure. If Mozambique could simultaneously increase its GDP growth rate to an average of 4.4 per cent over the projection period, while also managing to attract external grants equivalent to 1 per cent of GDP by 2024, average per child priority expenditure could increase to $143.1 (higher than $136.6 in the base scenario). Furthermore, internal debt flow would decline to 0.8 per cent of GDP, causing the debt stock to decline to 98 per cent by 2024.

On the contrary, a combination of low GDP growth and a further decline in donor support to priority areas would lead to a substantial decrease in priority expenditure. A simultaneous decrease in the GDP growth rate to an average of 3.3 per cent over the projection period, and a parallel further withdrawal of external support in priority sectors, would lead to average per child priority expenditure decreasing to $130.3 (lower than $136.6 in the base

scenario). Furthermore, internal debt flow would rise to 1.3 per cent of GDP, causing the debt stock to increase to 108.7 per cent by 2024.

Mozambique could most effectively reduce the fiscal gap by improving VAT administration efficiency. Assuming an improvement of 30% in domestic VAT and import VAT collection efficiency over the projection period would allow Mozambique to close the fiscal gap by 2022, reaching an average positive flow of -0.8 per cent of GDP over the projection period, 1.8 percentage points lower than in the base scenario. Assuming that the country maintains average priority expenditure per child at $136.6 (similar to the base scenario), this would allow the country to use the additional resources to pay back debt, thus the debt stock would stand at 91.8 per cent of GDP by 2024.

Key Advocacy Messages while engaging with the MEF and other line Ministries

The analysis of the recent developments in the Mozambican economy shows that there is limited space to increase allocations to priority sectors in the next 5-6 years. Available literature also suggests that the efficiency of spending in these areas remains relatively low when compared to other countries. With increasing demand for the provision of basic social services to a rapidly rising population, there is an urgent need to improve allocative efficiency to attain better outcomes.

The scenarios in this study demonstrate that if the government does not resolve the current crisis and manage to stabilize growth and regain access to donor funding, the country's children will pay the price both in terms of lower spending on public services that will improve their skills and opportunities as they grow up but also in terms of inheriting a massive debt burden that they will have to repay. This is a strong message that UNICEF is in a key position to highlight. UNICEF must not shy away from pointing out that decision-makers are currently making choices that affects not themselves but Mozambique's children and future generations. They should be accountable to these decisions and the evidence produced in this report can be used effectively towards this end.

It is clear, for example, that accelerated economic growth will be key to reducing the financing gap and increasing spending in areas relevant to children. At the same time, increased donor spending has a greater impact in increasing per child spending though it may not directly help in reducing the country's debt burden. Thus, a combination of the two scenarios can bring significant improvements for spending on children. This would be possible if the current deadlock with the IMF and donors was resolved.

On the other hand, a deterioration in any of these factors can have severe impact on social spending for children. Even a scenario where GDP growth increases but donor financing reduces further can bring worse results as the loss from the latter outweighs the benefits from the former. Thus, this study provides UNICEF with objective evidence that resolving the current crisis should be utmost priority which it must communicate to the government. An important target of an influencing strategy would be the Ministry of Economy and Finance as it has the power to propose concrete steps towards this end. Another group to target are the donors as the evidence also demonstrates that they have a shared responsibility as despite concerns of fiduciary risks, donor funding into these areas incontrovertibly brings improvements in outcomes in these social sectors, and it would be crucial to continue this support to improve the lives of children in Mozambique. Finally, the creation of internal demand for accountability will be key to improve outcomes. From this perspective it would be essential to improve the capacity of the parliament and local assemblies in overseeing the budget and ensure that it reflects the local needs. Similarly, while civil society organisations have a platform where concerns over the budget are raised (e.g. through parliament), their capacity needs to be enhanced so that issues such as efficiency and equity are also raised and discussed. Same can be said of others like private sector organisations, religious institutions and the media.

Overall, all the scenarios summarised above first of foremost provide technically sound evidence that emphasizes and supports the recommended entry points presented in the Political Economy Analysis. UNICEF could consider making the findings more user friendly for example by using infographics or other comms tools that would make them more easily understood by decision-makers and stakeholders more broadly (including children and adolescents).

1. Introduction and methodology

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.

1.1. The objective of the Fiscal Space Analysis

The Fiscal Space Analysis (FSA) sets out by reviewing the recent evolution of the availability of financial resources within the government budget for expenditure flows directly relevant to children's welfare and development. It does this through a fiscal-space accounting framework, centered on the government budget and the identification of "priority" sectors considered most relevant for children's welfare.

The analysis also examines and evaluates options to increase overall fiscal space available in each economic area. The fiscal space accounting framework makes it possible to examine the consequences of sets of assumptions - "scenarios" - describing future macroeconomic conditions for fiscal space. Different scenarios produce different outcomes for fiscal space and have different implications for the government's capacity to fund its child-relevant expenditure. The scenarios described in this report are illustrative, in the sense that they are intended to show how UNICEF could apply the exercise to inform its discussions. Nevertheless, the options that are selected for the scenarios are based on discussions with the UNICEF country office and key stakeholders.

A projection exercise of this kind could help UNICEF engage in a technical dialogue with policymakers and other stakeholders to discuss different possible government policy approaches, to determine how and whether these policies would make it possible for the authorities to sustain and perhaps enhance the fiscal space for expenditure in sectors on which children depend. Thus, the point of the exercise as presented here is not so much to analyse specific assumptions and results, but rather to show how UNICEF could use this exercise in its dialogue with policymakers and other stakeholders.

1.2. Methodology

The analysis is carried out using an Excel-based projection exercise (MozFS.xlsm). Section 1.2.1 outlines the definition used for priority expenditure; section 1.2.2 describes the set-up of the fiscal space analysis, using a fiscal identity; and section 1.2.3 highlights some data limitations.

1.2.1. Priority expenditure categories for children

This report uses the term "priority expenditure" to refer to expenditure categories regarded as beneficial to children. This label does not imply that expenditures defined as "priority" should be "prioritized" at the expense of the non-priority ones. The rationale is rather to single out, from among all expenditure categories, those that are of specific interest to UNICEF's mandate to advocate for the protection of children's rights, to help meet their basic needs and to expand their opportunities to reach their full potential entrusted to it by United Nations General Assembly. For Mozambique, "priority" expenditure categories for children comprise the following "institutional" expenditure categories:

1. Education;
2. Health;
3. Social Action;
4. WASH (Water, Sanitation, and Hygiene)

Several points about the expression "priority expenditure" need to be clarified early on. First, the composition of the expenditure defined as such is inevitably somewhat arbitrary. Some expenditure in the categories listed above may not target or benefit children, directly or indirectly. On the other hand, expenditures not listed in the categories may benefit children, at least indirectly. Future analyses of this kind could work with different definitions of priority expenditure, although the methodology used in this study would still be applicable. Second, this fiscal space discussion concerns expenditure carried out by government within its budget.

1.2.2. Fiscal space 'identity' and analysis

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 (identically) equal to the overall deficit, which is in turn equal to the net flow of external and internal financing to the government. If total expenditure is broken down in 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.

FIGURE 1

Fiscal Identity
Priority Expenditure =

Tax and non-tax revenue
+ External grants
- Non-priority expenditure
- External debt service
- Internal interest expenditure
+ External debt disbursements
+ Net internal financing flows

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. Chapter 3 describes the historical evolution of priority expenditure for the Mozambique, for the years 2009-2016.

For the **projection analysis,** the accounting identity is applied in a different way. For each projection year, the priority-expenditure flow is projected on the basis of programming assumptions, encompassing the various determinants of recurrent and non-recurrent expenditure in the education and health 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 as a residual, 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 fiscal space. 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 database. The relatively simplified, illustrative projection exercise applies scenarios to historical data (as discussed in Appendix 1).

Each scenario comprises programming assumptions for the years 2017 to 2024, covering:

- world economic conditions;
- basic Mozambique 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 lines 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 for any given scenario. It is straightforward to combine these assumptions into an assumed growth rate for nominal GDP.

1.2.3. Data sources
Overall, severe data deficiencies across the board are a major impediment to the undertaking of this Fiscal Space Analysis.

The main data source for the retrospective analysis is the Ministry of Finance. Additional data sources include the World Bank/International Finance Corporation and the International Monetary Fund (International Financial Statistics and World Economic Outlook) and the United Nations Population Fund. The priority sectors are identified using the budget execution sector breakdown as reported by UNICEF in their anniversary report*, in order to maintain continuity across different reports. While data on expenditure for all sectors is available until 2016, data for 2017 was not available in time, which constrains the accuracy of our projections. Furthermore, the breakdown by economic category was not fully available for all sectors, therefore the staff and non-staff breakdowns are largely estimates.

Finally, the general government budget data reported by the Ministry of Finance also suffers from various inconsistencies. As a result, executed data for revenue collection and total expenditure is often inconsistent and likely incomplete.

The analysis of the composition of priority expenditure in chapter 3 draws on data presented in the UNICEF anniversary report, which in turn is based on data from previous general state accounts (Conta Geral do Estado, CGE). Other important sources include the recent sector public expenditure review, especially on education and health by the World Bank.

1.3. Organization of the FSA part
The remainder of this report is organized as follows. Chapter 2 summarizes the Mozambique's present macroeconomic context – in particular, its fiscal context. Chapter 3 analyses the recent evolution of the expenditure flows in the categories of priority expenditure and outlines some specific challenges in the various areas relevant for expenditure on children. Chapter 4 and 5 discusses various options available to policy makers to enhance fiscal space, using an illustrative projection exercise for the priority expenditure flows and fiscal space that would fund them for the years 2017-2024. The exercise is a sensitivity analysis, consisting of a base-scenario projection based on a broad range of macroeconomic and fiscal-policy assumptions, with various alternative scenarios based on changes to the base-scenario assumptions. Chapter 6 summarises the main findings from the analysis. Appendix 1 provides further details of the sensitivity analysis.

2. Mozambique's macroeconomic and fiscal context

This chapter will highlight some of the long-term trends and recent developments. Long term trends include economic growth, structure of the economy along with demographic trends and social development indicators like poverty. Recent developments refer to economic growth in the recent past, followed by developments in other macroeconomic indicators like external account, Overseas Development Assistance and Foreign Direct Investment, and fiscal performance.

2.1 Longer-term national economic trends

2.1.1 Real GDP growth

Mozambique experienced rapid economic growth in the two decades following the end of the civil war, albeit from a small base. With an average growth of 8 percent per annum it became one of the fastest growing economies in the world. The impact of the global financial crisis temporarily slowed growth to less than 7 percent in 2009 before it started recovering in subsequent years[1]. Large investments in the post-war reconstruction drove growth and agricultural production increased significantly as more displaced farmers returned, bringing more land under cultivation. However, gains in productivity remain low, limiting income generation for the sector. Other productive sectors like manufacturing, which can absorb the growing labour force, have stagnated as well. Growth is increasingly driven by the dynamic extractive industries sector which has received a lot of attention in recent years as Mozambique discovered huge reserves of natural gas in the North of the country, in Cabo Delgado. The country produces coal, heavy sands, aluminium and precious stones, and recently opened a graphite mine at the site of the largest deposit in the world.

2.1.2 Demographic trends

According to the 2017 census, there are now 28.9 million inhabitants in the country. The population has doubled since the end of the civil war, growing at an average annual rate of 3 percent. The country's population is the 12th largest in Africa[2]. At 57.6 years, life expectancy is among the lowest in the world. Fertility rate at 5.9 is among the highest in the world with a higher observed fertility than desired, indicating a need for increased family planning services[3]. Moreover, teenage pregnancies in the country remain among the highest in Sub-Saharan Africa[4]. A large young population (45 percent of the population is between the age of 0-14) implies a high dependency ratio whereby relatively few economically active people provide for those who are dependent, mainly children and the elderly. This can put a strain on the government's ability to provide basic goods and services. Coupled with the absence of measures to create enough employment opportunities, this can fester perceptions of exclusion among the growing youth bulge (the proportion of the population between 15 and 29 years of age) and be a significant driver of instability[5]. Youth unemployment increased from 24.7 percent in 1997 to 38.6 percent in 2009[6].

2.1.3 Structure and characteristics of the national economy

Growth patterns in the past two decades have not led to significant changes in the structure of the Mozambican economy. While agriculture remains the mainstay of the economy, employing about 70 percent of the population directly or indirectly, productivity remains well below its peers[7]. Most crop production is rain-fed and hence performance remains vulnerable to the vagaries of nature. Moreover, Mozambique is one of the countries most affected by climate change; floods in the North (including Zambeze basin) of the country are rampant while there have been instances of dry spells in the South. The country is also prone to cyclone activities in the coastal area with the Indian Ocean, Despite being a national development pillar identified in the country's long-term development strategy (Estratégia Nacional de Desenvolvimento, ENDE), investments in agriculture and rural development have been inconsistent and erratic[8]. With decelerating growth for a decade, the sector's contribution towards overall value-added in the economy has declined from about a third in 1993 to just under a quarter by 2016.

According to the data published by the National Institute of Statistics (Instituto Nacional de Estatísticas, INE), growth in manufacturing has been slow with its proportion in the total value added seeing a decline from 15 percent in the years following the war to single digits in recent years. Productivity remains a daunting challenge in this sector as pointed out by Jones and Tarp (2012). Not only has productivity growth in the secondary sector slowed over time, the productivity of manufacturing firms in Mozambique is well below its peers[9]. With an open economy, manufacturing firms are not able to compete with cheap imports. The sector is further strangled by the lack of access to finance and lengthy bureaucratic procedures. In the post war reconstruction, with building of infrastructures, the construction sector received an impetus. This continued with the discovery of natural resources which has required the building of railways, ports, roads as well as civil structures.

Data published by INE also show that services have steadily accounted for about half the overall value added in the economy. Dominant among these are trade and transport (together accounting for about 45 percent of the total value added in services). Public administration has seen significant increases in the value added, and services like education and health also contribute significantly towards the total value added (accounting for about 22 percent of the overall value added in services). Ironically, financial services have also been a fast-growing sector though high interest rates make it prohibitively expensive for small and medium enterprises (SMEs) to access credit. Despite being deemed a pillar of growth, the tourism sector has failed to bring in significant income in the country; the proportion of value added in the total has increased only slowly (averaging 4 percent of the total value added in services).

1. The impact on the trade balance was limited since the negative impact of reduced export prices, especially aluminium was somewhat offset by the reduced import values of oil and food. Moreover, the limited international integration of Mozambican financial market also meant that the shock of the crisis did not affect the country as much as neighbouring South Africa (Castel-Branco and Ossemane, 2010).
2. Porter et al. (2017).
3. DHS, 2011 and World Bank (2017c).
4. World Development Indicators (2014)
5. Porter et al. (2017).
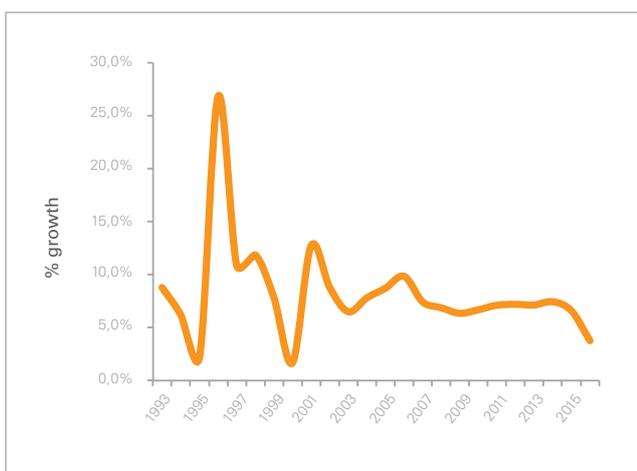6. World Bank (2016c).
7. World Bank (2016c)
8. Orre & Rønning (2017).
9. Jones and Tarp (2012)

The declining shares of the agriculture and manufacturing sectors have been substituted by an increase in the share of extractive industries. According to the published data by INE, this sector has seen rapid growth since the turn of the millennium averaging 20 percent per annum, though this hides the volatility in growth. Though from a small base, this sector is increasingly driving growth. Large investments for the so-called 'megaprojects' have come into the country. With little linkages with the rest of the economy, these capital-intensive projects depend mostly on imported goods and services to build their infrastructure and FDI to finance them. The nature of business in these industries means that gains increasingly accrue to the investors and those with high skills[10]. Moreover, these projects are also characterised by generous tax incentives, ostensibly to attract investments, thereby contributing little towards domestic revenue mobilisation.

FIGURE 2.1 Mozambique has seen rapid economic growth since the end of the civil war

Source: INE

FIGURE 2.2 But there are no signs of a structural transformation

Agriculture | Exctractive Indusries | Manufacturing | Utilities & Construction | Services
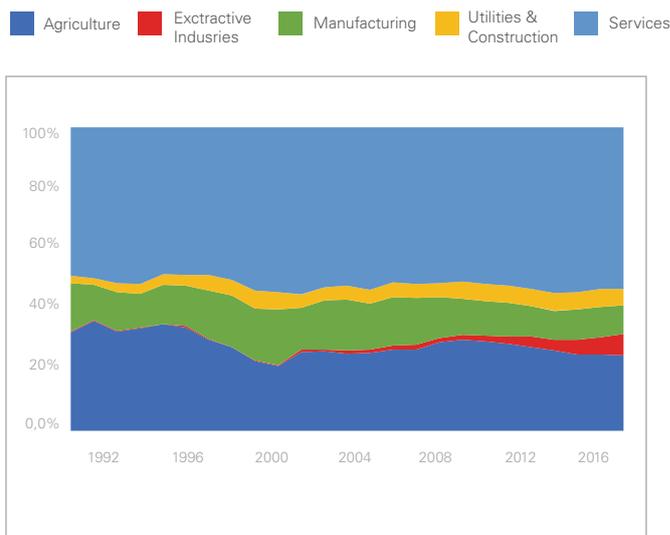
Source: INE

2.1.4 Poverty

The pattern of growth has also had implications on poverty reduction in the country. The overall poverty headcount declined from 68 percent in 1997 to 56 percent in 2003. Since then however, progress has been limited with the poverty incidence at 52 percent in 2009. Despite rapid economic expansion, every 1 percent increase in GDP per capita reduced poverty by 0.04 percentage points between 2003 and 2009 compared to 0.86 percentage points between 1997 and 2003[11]. This slowdown in progress has meant that average growth elasticity of poverty reduction in Mozambique between 1997 and 2009 was only about half that of the average in Sub-Saharan Africa (SSA)[12]. By 2015 the proportion of the poor in the country was down to 46 percent but at the cost of higher inequality (Gini Index increased from 0.4 in 1997 to 0.47 in 2015) which accelerated dramatically in recent years[13]. There are also significant regional disparities. For instance, while poverty between 2009 and 2015 declined rapidly in the South (by 18 percentage points), reduction in the Centre was less rapid (11 percentage points). Moreover, these gains were somewhat offset by an increase in the poverty headcount in the North (10 percentage points)[14]. Poverty reduction has not been rapid enough to outpace population growth and in 2015 there were more people in absolute poverty than in 1997.

The uneven progress in poverty reduction, with concentration of the poor in the centre and north, shows that even as the country experienced rapid growth, it has not been pro-poor. Per capita expenditures of the bottom 40 percent of the Mozambican population grew more slowly than the overall population between 2003 and 2009[15]. This lack of inclusiveness of the growth can explain the rise in inequality. Poorer households typically have lower human capital, lower quality jobs and higher dependency ratio. However, the isolation of households especially in rural Zambézia and Nampula has meant that returns to assets, especially education and land, are lower than in the rest of the country while inputs costs are higher further accentuating their poverty[16]. This is further exacerbated by the low productivity in agriculture thereby limiting its capacity to lift the rural population out of poverty.

10. Barma et al. (2012).
11. UNICEF (2014)
12. World Bank (2016c).
13. MEF (2016).
14. Ibid.
15. World Bank (2016c)
16. Ibid.

2.2 Recent Macroeconomic Developments

Mozambique's economy saw rapid expansion in the two decades following the civil war and significant discoveries of natural resources have put the country at the centre stage of mining and gas sectors and generated a lot of optimism. However, the decline in commodity prices slowed growth. Moreover, in April 2016, hidden debts worth US$ 1.4 billion came to the fore following the restructuring of the EMATUM bond, an already contentious loan amounting to US$ 0.8 billion. The discovery of these undisclosed debts set off a chain of events starting with an immediate suspension of an IMF loan to the already ailing economy. As donors also suspended General Budget Support (GBS), this left a large hole in the country's public finance amounting to about US$ 400 million equivalent to about 7 percent of the budget[17]. Moreover, the burden of debt servicing increased substantially, to 21 percent of the budget in 2016[18]. This has put government finances in a precarious position. Debt levels have reached unsustainable levels and Mozambique's credit rating by international agencies was downgraded as the government defaulted on some debt repayments. The already decelerating economic growth has come under substantial pressure from the ensuing crisis. Foreign Direct Investment (FDI) in the non-megaproject economy reduced significantly on account of diminished investor confidence. High inflation and depreciation of the currency have led to an erosion of real income. With limited resources to finance the growing fiscal deficit, the government has increasingly resorted to domestic financing through the central bank. The private sector, faced with depressed incomes and accumulating public arrears, is encountering severe challenges to survive further affecting growth. Thus, the country is caught in a vicious cycle.

Prospects for the economy have significantly changed. Economic growth is forecast to remain subdued by the IMF in the next few years[19]. While gas investments are expected to go through, massive inflows of revenues, once natural gas production commences by mid-next decade, will increasingly have to be used to repay the soaring debts rather than towards the welfare of the population. In the interim however, significant uncertainty remains. With depressed economic growth, domestic resource mobilisation will be affected. Moreover, the forensic audit report by Kroll to investigate the whereabouts of the large sums of money has yielded limited results, reflecting the reluctance on the part of the government for fiscal transparency and accountability and resulting in a continued deadlock in donor-government negotiations to unfreeze budget support.

2.2.1 Real GDP growth

Economic growth started decelerating in 2015 as low international prices of commodities like aluminium, coal, heavy sands as well as agricultural products like cashew reduced export earnings. Moreover, military tensions disrupted economic activity especially in the Centre of the country[20].

Floods in the North affected crop production bringing overall growth to 6.6 percent. By 2016, the negative effects of the El Nino induced drought, experienced in the wider Southern Africa region, became increasingly predominant in the Southern parts of Mozambique. Domestic food prices skyrocketed and drove up inflation. The discovery of the hidden debts, about a third of the national budget in 2016, exerted further downward pressure on economic activity. The currency depreciated significantly. In the absence of significant changes to the fiscal policy, the burden of adjustments happened increasingly through tightening the monetary policy. The resulting increase in the cost of credit negatively affected activity of the distressed private sector. As a result of these developments, real economic growth declined to 3.8 percent in 2016. While commodity prices are since recovering, resulting in strong performance of the megaprojects, this is not enough to offset the decline in growth of the private sector which is affected by low demand, reduced investment and high cost of credit[21]. Thus, economic growth in 2017 is estimated to have remained low at 3.7 percent. The divergent performance of the recovery and resilience of large businesses in the extractive industries especially megaprojects on the one hand and a further decline in other sectors of the economy on the other, has led some to characterise Mozambique as a two-speed economy[22].

In the medium term, IMF forecasts economic activity to remain sluggish[23]. Despite anticipated investment inflows related to the natural gas projects in the North of the country, these are not forecast to lead to significant activity in the construction and related sectors. Activity in the non-megaproject economy will remain depressed unless the private sector is revitalised with financing (payment of arrears, reduction in the cost of finance, higher consumer demand) and business confidence is restored. These forecasts raise serious questions about real incomes in a population that has seen an average growth of over 3 percent in the last 10 years. However, these projections are contested by the government as overly pessimistic. According to the government, there are clear signs of recovery in the economy as inflation is brought under control, the currency has stabilised, and efforts are being made to resolve the debt crisis by taking concrete steps. According to the government, growth in 2018 is expected to reach 5.3 percent[24].

2.2.2 International trade

When looking at international trade and the external account it is important to make the distinction between megaprojects and the rest of the economy. In 2015, earnings from both megaprojects as well as traditional exports declined in line low international commodity prices. In 2016, megaproject exports recovered to US$ 2.4 billion (from US$ 2.0 billion in 2015), and even further to US$ 3.4 billion in 2017. Megaproject imports declined from US$ 0.9 billion to US$ 0.8 billion in 2016 as construction of on-going projects was completed and were expected to remain at this level in 2017.

17. Estimation of GBS per year before 2016
18. UNICEF (2018)
19. IMF (2018)
20. After several years of peace, soaring political tensions resulted in low-level conflict in the centre of the country. This came through targeted attacks on the main highway going North-South affecting transport services and the provision of goods and services, as well as people.

21. World Bank (2017b).
22. Ibid.
23. IMF (2018).
24. GoM (2017).

On the other hand, non-megaproject exports earnings declined from US$ 1.4 billion in 2015 to US$ 0.9 billion in 2016. This slide was expected to continue in 2017, with these exports amounting to US$ 0.8 billion. This can partly be explained by the negative effects of climate change related events on Mozambique's non-megaproject exports including cotton and cashew. Non-megaproject imports declined significantly from US$ 6.6 billion to US$ 4.0 billion in 2016 as inflation severely eroded real incomes and imports became too expensive. Imports were expected to remain around the same level in 2017. Thus, the overall current account deficit (including megaprojects) was brought down significantly from close to 40 percent of GDP in the recent past to 16-17 percent in 2017 though this is mostly due to developments in the megaprojects account. The large deficit in the non-megaproject account is unlikely to be sustainable, in the absence of megaproject activity.

In the medium term, according to projections by IMF, the narrowing of the current account deficit will continue before it starts expanding significantly from 2019, driven by developments in the megaprojects economy[25]. Large investments in natural gas in the North of the country will continue, necessitating capital-intensive imports which will be financed mainly through FDI in these projects.

2.2.3 Inflation and exchange rate
Inflation between 2012 and 2015 was in the low single digits. By the end of 2015 however, food prices started rising steeply as the negative effects of the El Nino induced drought became more prominent. Average food inflation in 2016 ran over 30 percent. This was further compounded by the depreciating currency which drove up the prices of food imports, already scarce as the drought had spread throughout the region. This increase in food prices drove up the overall inflation rate which averaged 20 percent in 2016. Overall inflation in 2017 remained over 15 percent as food prices continued to drive inflation in the first half of the year and prices in other segments like utilities also increased. High inflation rate in 2016 and 2017 has significantly hollowed out real incomes with increases in the average minimum wage well below the rate of inflation.

While the local currency remained at about MT 30/US$ between 2012 and 2014, by 2015, reduced export earnings put significant pressure on the exchange rate. The brief intervention by the Central Bank to defend the exchange rate further depleted already limited levels of international reserves without the intended effect as by the end of 2015, the currency had lost a third of its value against the US$ compared to 2014. By 2016, the effects of the drought compounded by the discovery of the hidden loans added immense pressure and by October 2016, the Metical exchanged for over 75 to the US$. On average the Metical lost just over half its value between 2014 (31.4 MT/US$) and 2016 (63.1 MT/US$). This had profound implications for the debt levels in the country since most of the debt is denominated in foreign currency. As is shown in section 2.4.6, debt levels have become unsustainable and debt servicing costs have soared significantly.

According to the data published by the national statistics office (INE), inflation in the first two months of 2018 declined to 3.4 percent. According to the IMF's projections inflation will be reined in over the medium term and remain well within the SADC inflation band. However, trends in the implied exchange rates show pressure on the local currency with a possible depreciation after 2019.

2.3 Recent trends in ODA and FDI
2.3.1 ODA
Overseas Development Assistance (ODA) dominated the overall resource envelope available to the government in the years following the civil war. Yearly inflows of ODA since the early 2000s have consistently been above US$ 1 billion. Between 2006 and 2013 flows grew from US$ 1.6 billion to US$ 2.3 billion before declining rapidly from 2014. By 2016, ODA flows were comparable to those observed in 2006. Nevertheless, ODA flows as a proportion of GDP have consistently been above 13 percent. However, the proportion of donor aid in the overall budget reduced from 40 percent in 2006 to about 7 percent in 2016 (though this does not include off-budget flows). This shows that donor resources as well as their significance in the budget have been declining in the past years, partly explained by the rapid increase of the overall budget. This decline can be attributed to both, domestic developments in donor countries which have generally developed a low tolerance towards the fiduciary risks involved in budget support as well as a deterioration in donor-government dialogue under the previous President. The precipitous drop in donor resources in the budget since 2016 (to about 4 percent in 2017)[26] is due to the halting of GBS following the discovery of the undisclosed loans. While support through sector common funds has continued, this involves comparatively low amounts of funding.

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25. IMF (2018).
26. According to data published in the Budget Execution Report (REO) in 2018

FIGURE 2.3 Bilateral aid is predominant in Mozambique, but has been declining

GBS Common Funds Projects
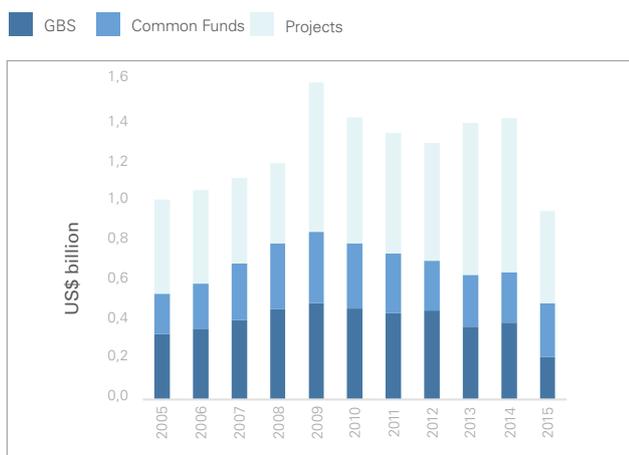
Note: Figures may not match with the data from MEF
Source: OECD

FIGURE 2.4 While the proportion of ODA in GDP remains high, ODA per capita is declining

ODA/GDP (%, left) ODA per capita (US$, right)

Source: OECD, INE, WDI

Information from the OECD DAC presents some insights into aid in Mozambique. Bilateral aid is predominant in Mozambique, accounting for around 60 percent of the ODA between 2014 and 2016. This includes the group of donors providing GBS through the Program Aid Partnership (PAP). Over 60 percent of bilateral aid is devoted to social sectors while about 17 percent is for economic infrastructure. The UK and EU institutions have traditionally devoted more resources towards GBS. The largest bilateral donor, the US, provides a significant amount of resources for health as well as other sectors like agriculture though this mostly remains outside the budget. Other important bilateral donors include Sweden, Germany, Netherlands and Norway. Multilateral organisations like the World Bank are among the largest contributors in the PAP. Other important agencies include African Development Bank, the IMF and the UN. In the health sector, apart from donors like the US (mostly through the President's Emergency Plan for AIDS Relief or PEPFAR), the Global Fund is an important player.

While significant donor resources come into the country, it is difficult to gather an accurate picture of the ODA. The complexity and inadequacy of information in the aid database, ODAMOZ, has illustrated the need for a more comprehensive system to capture donor resources flowing into the country. The Ministry of Economy and Finance (Ministério de Economia e Finanças, MEF) is currently embarking on the creation of a new database to capture external resources which would be linked to the e-SISTAFE (Mozambique's integrated financial management information system). Several studies have shown the lack of transparency and poor coordination of donor interventions which eventually affects aid performance as well as outcomes, especially in sectors like health where aid is particularly fragmented[27]. Figure 6 below shows that performance vis-à-vis aid effectiveness indicators identified in the Performance Assessment Framework (PAF), as measured by independent evaluations, has been declining.

FIGURE 2.5 More resources are devoted towards project support

DAC Countries Non-DAC Countries Multilateral Agencies
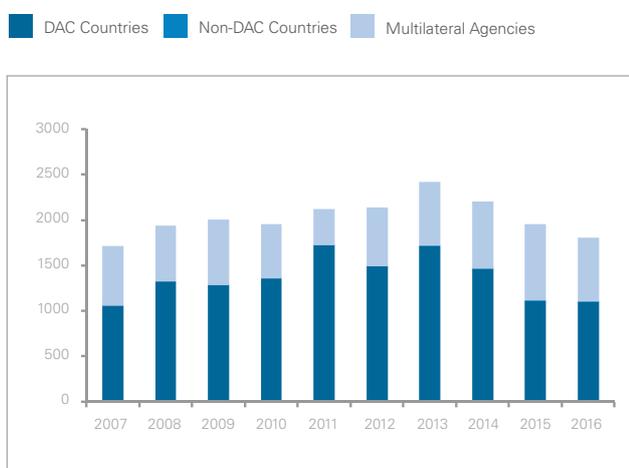
Source: MEF, ODAMOZ

FIGURE 2.6 Though aid effectiveness has not made much progress as shown by the PAF indicators scoring

Total number of indicators Achieved Not achieved but with progress Not achieved
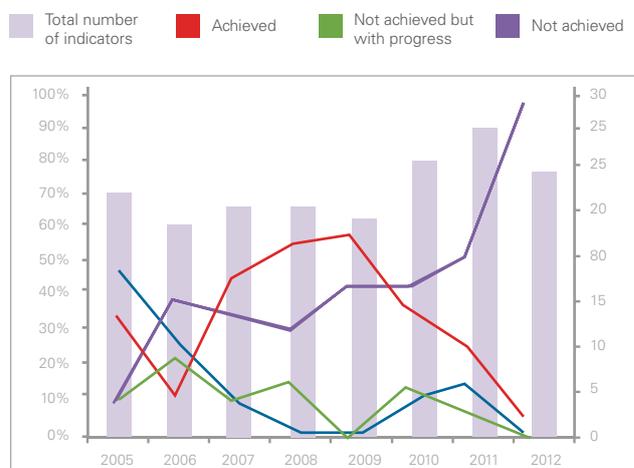
Source: ADE, ITAD, COWI (2014), p. 89

27. For instance, with increasing aid towards disease-specific vertical projects there remains a gap in horizontal financing to strengthen health systems thereby affecting outcomes (World Bank, 2016a). Moreover, with significant amount of resources going outside the single treasury account or even the budget, the overall resource envelope is not adequately known at the central level (Chilundo et al. 2015).

The broader issues related to the debt scandal creates significant uncertainty over ODA trends in the medium term. Support in the short term seems heavily dependent on transparency and accountability related to the hidden debts with the IMF acting as gate-keeper. At the same time, some donors are seeking to redirect support through different modalities to mitigate the impact on the poor. Consequently, aid through project support has seen increases[28]. It would be important to assess the impact of such diversion since it entails more than an increase in administrative costs of reporting by the government. Regardless, donor grants are forecast to continue a long-term downward trend[29].

2.3.2 FDI

While investments have been a big driver of growth in Mozambique, FDI inflows into the country really picked up pace towards the end of the 2000s following the discovery of substantial natural resources. Mozambique is richly endowed with non-renewable resources and large investments are required in the extractive industry sector to realise their huge potential. FDI between 2010 and 2013 increased from US$ 1 billion to US$ 6.2 billion mostly driven by megaprojects. These inflows were mainly used towards capital-intensive imports. With the end in the construction cycle of these projects, FDI inflows began to decline from 2014. Non-megaproject FDI inflows on the other hand peaked at US$ 2.6 billion in 2015. However, with the unfolding of the debt crisis and ensuing sluggish economic activity, these flows declined dramatically to about US$ 1.3 billion by 2017.

It is worth pointing out that even before 2010, the largest share of the FDI inflows went to the extractive industries. Other important beneficiaries of FDI include related industries of transport, real estate, construction and utilities. FDI to other productive and labour generating industries like agriculture, manufacturing and tourism peaked at US$ 588 million in 2012 but dropped to a paltry US$ 12 million in 2013. These investments have recovered somewhat, and by 2017 stood at US$ 201 million. The sheer scale of investments in the extractive industries dwarfs the inflows in other sectors. For instance, while manufacturing accounted for over 60 percent of the total FDI in 2002, its share in 2012 was as little as 7 percent, even though the level of investments in 2012 was higher (at US$ 391 million) compared to 2002 (US$ 263 million). Nevertheless, FDI in sectors like agriculture has been very volatile.

The top 10 investors in the country have remained mostly unchanged between 2010 and 2017. These are led by the United Arab Emirates, followed by Mauritius. Chinese FDI is concentrated in the construction sector while FDI from countries like Italy and Australia is linked to natural resources. Significant FDI inflows were received from the USA especially between 2012 and 2014. South African investments are relatively small compared to other countries but peaked in 2016. Other important players include Portugal and Brazil.

FIGURE 2.7   FDI increased significantly between 2010 and 2013, driven mainly by megaprojects

■ Megaproject   ■ Non-megaproject

Source: Banco de Moçambique

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28. See PEA for more discussions on this.
29. IMF (2018).

With major beneficiary being extractive industries and related sectors
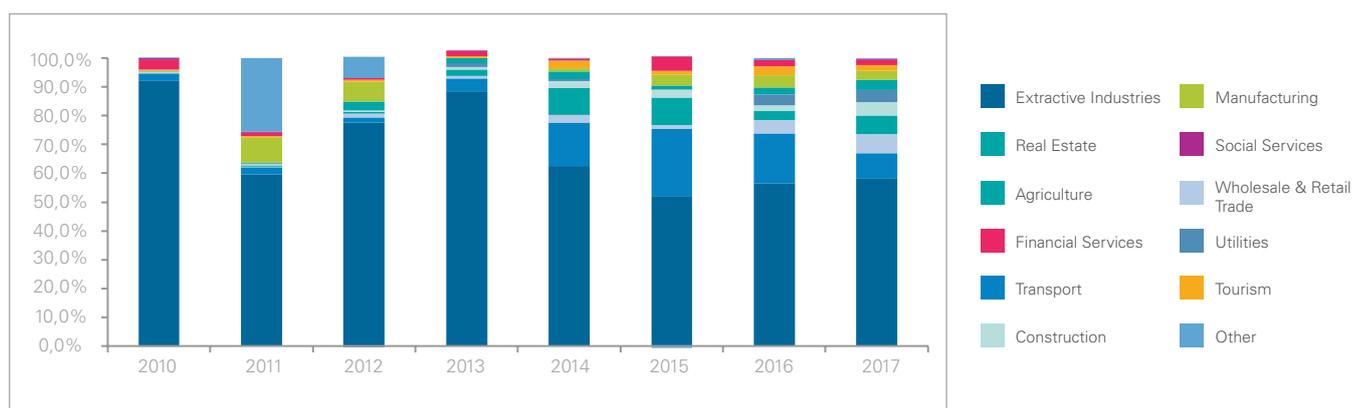
Source: Banco de Moçambique

In the medium term, according to projections by IMF, megaproject related FDI will continue to drop before picking up significantly in 2019 as investments in the big natural gas projects, worth several billion dollars, are expected to go ahead[30]. On the other hand, non-megaproject related FDI is forecast to continue its decline as economic activity remains weak[31].

FIGURE 2.9 Top investors in Mozambique account for almost all the FDI
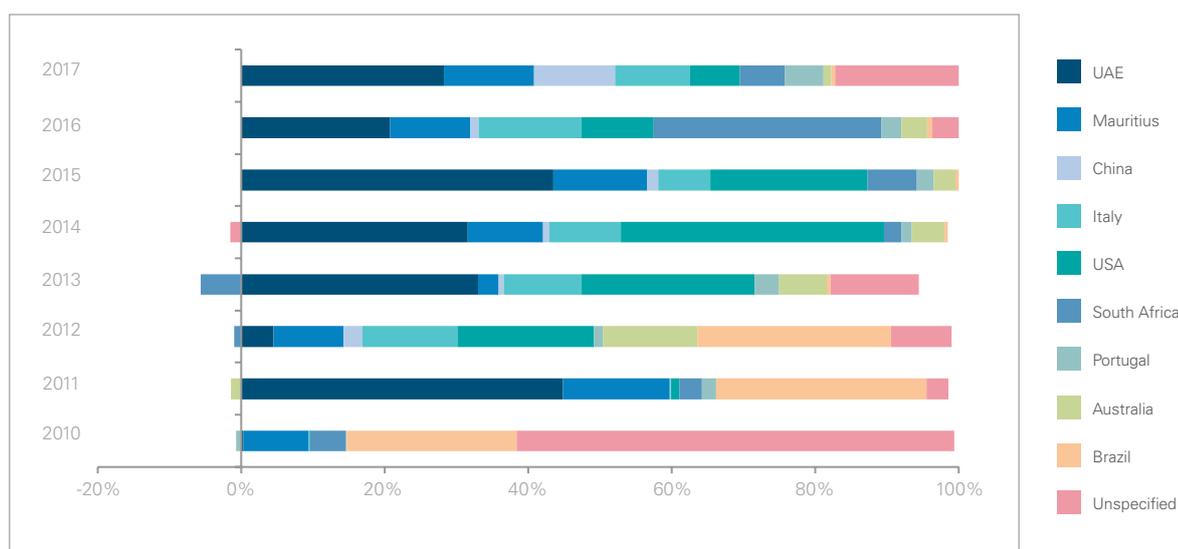
Source: Banco de Moçambique

2.4 Recent fiscal performance

2.4.1 Government financial performance

While domestic revenue collection has been well above 20 percent of GDP since 2012, total expenditures have consistently been above 30 percent of GDP and the government has increasingly resorted to financing the deficit by contracting debt. In 2014, the fiscal policy was expansionary with total expenditures reaching 40 percent of GDP. The fiscal deficit after grants widened from low single digits to over 10 percent of GDP. One-off events like the Presidential elections, and more importantly, the inclusion of EMATUM on the government books accounted for half on the fiscal loosening [32]. In 2015, expenditures were reined in to put them on a more sustainable path, declining by almost 5 percentage points of GDP. This also helped to bring down the fiscal deficit. The initially

approved budget for 2016 had to be revised after the discovery of the undisclosed loans as the landscape changed significantly. With the revised budget the total resource envelope saw a decline of 2.4 percentage points of GDP due to lower domestic revenues (1.5 percentage points) and donor support (0.9 percentage points) compared to the initially approved budget. Total expenditures on the other hand saw a nominal decline of just 0.4 percentage points. More specifically, current expenditures increased to accommodate the high interest payments while all other expenditure lines were reduced. Investment spending took the largest hit, declining more than 6 percent of GDP in 2016. Nevertheless, the fiscal deficit increased to 7.6 percent of GDP[33]. Fiscal policy in 2017 remained

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30. IMF (2018).
31. Ibid.
32. IMF (2015). EMATUM loan was part of the hidden debt, discovered in 2013 and was included in 2014 budget.
33. IMF (2018). This number is derived by calculating revenues net of verified VAT refund requests and expendituresbased on modified cash basis and including payment arrears.

loose in light of spending pressures. While the Capital Gains Tax (CGT) boosted domestic revenues by almost 2.7 percent of GDP, the fiscal deficit remained at 5.5 percent of GDP[34].

In nominal terms, recurrent expenditures have been rapidly increasing in the past years though this also includes interest payments. Investment spending took a significant hit in 2016 when these expenditures declined by almost 50 percent. The decline came from both internally financed investments, as domestic resources came under rising pressure, as well as externally financed investments as donor support declined. This decline will have an impact on infrastructure development. Moreover, with squeezed fiscal space, the maintenance of existing infrastructure

may also be affected, having implications for government's ability to provide basic services. The only way to mitigate such negative impacts is by finding efficiency gains through improved public investment management and better infrastructure governance. Some of the measures required to enhance the efficiency of public investments include the alignment of public investment programs to consider project feasibility, absorption capacity constraints and debt sustainability[35]. According to Public Investment Management Index, which captures ex-ante as well as ex-post dimensions of the various stages of the investment process, Mozambique scores below the median for Low-income countries (LICs) with particular weaknesses in project appraisals[36].

| FIGURE 2.10 | Expenditures outstripped domestic resources with the government resorting to deficit financing |

Domestic Revenues Grants Total Expenditures
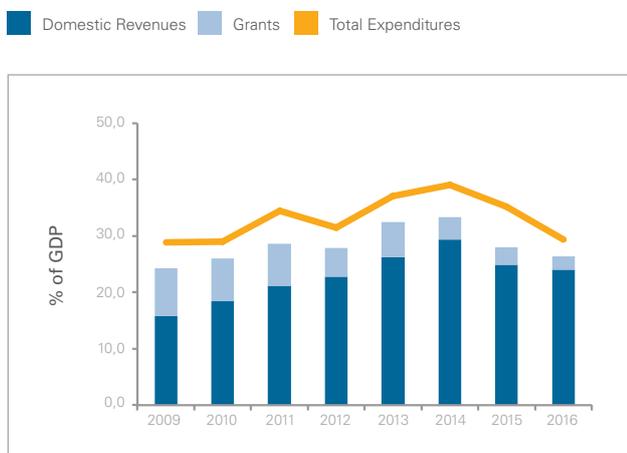
Source: GFS

| FIGURE 2.11 | Investment spending has borne the burden of fiscal adjustment |

Recurrent Investment
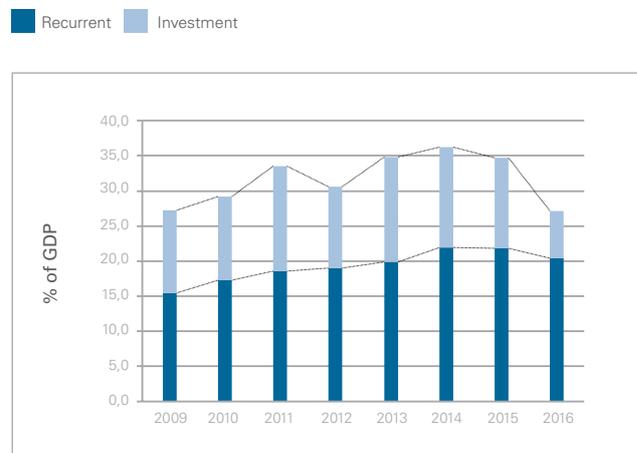
Source: GFS

Spending at deconcentrated levels has increased in the past years however most of this increase is for recurrent expenditures. Furthermore, as UNICEF budget briefs point out, there is a lack of correlation between this increased spending and the needs of the people as represented by vulnerability indicators, or geographic and spatial distribution of poverty, inequality and access. According to available data from the CGE, the proportion of the total recurrent spending at central level declined from 53 percent to 46 percent between 2009 and 2015. While spending at the district level

increased from 6 percent to 25 percent during the same period, this has been at the cost of spending at provincial level. 2016 saw some reversal in observed trends as spending at the centre increased. Investment spending remains concentrated at the central level; over 75 percent of the total investment spending (from all sources of financing) takes place at that level, with less than 10 percent at the district level. However, this may be underestimated since both central as well as provincial levels execute investment projects meant for the district level.

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34. Based on data in IMF (2018).
35. IMF (2018b)
36. Dabla-Norris et al. (2011).

FIGURE 2.12 Current expenditures have risen, while investment spending saw a steep decline in 2016

Legend: Wages, G&S, Interest, Transfers, Others, Internal, External

Source: GFS

FIGURE 2.13 Spending patterns at deconcentrated levels show mixed progress

Legend: Central, Provincial, District, Central, Provincial, District
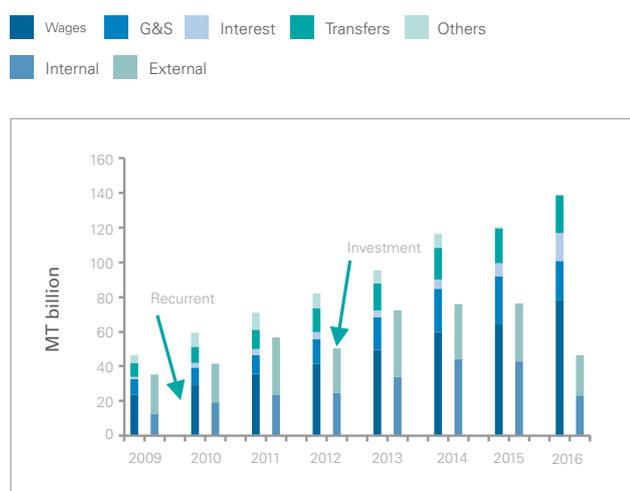
GFS, CGE and author's calculations

While expenditures have rapidly increased in recent years in response to the large spending needs in the country, this has come at the cost of heightened fiscal risks. The government embarked on a drive to increase public investments while increasingly resorting to borrowing through state owned enterprises (SOEs). However, in the absence of legal and regulatory framework, debt (in foreign denomination and on commercial terms) with public guarantee was increasingly contracted by corporations with weak performance. As borrowing became the main source of financing for these SOEs, they became the leading source of fiscal risk. The disclosure of large publicly guaranteed loans by three SOEs that led to the debt and aid crisis is a prime example of this. Moreover, with the depreciation of the exchange rate, servicing of the contracted debt (mostly denominated in foreign currency) has become expensive. With unsustainable costs of debt financing leading to the default, the scope for further external borrowing is eliminated.

As the rising debt servicing costs squeeze government finances, there are increasing cashflow challenges. During the budget execution, disbursements to spending units are delayed and there is a rationing of appropriation requests sent to MEF. The treasury releases funds according to availability of resources and based on priorities (though these are not always clearly defined)[37]. This can lead to significant disparity between initial allocation and actual spending. However, lower levels of execution may be misleading since it does not take into account commitments, which have in fact increased. A result of this is the rapid accumulation of arrears. In the absence of real time recording of commitment and verification in the e-SISTAFE, these arrears are not properly recorded. Thus, the budget deficit is potentially much higher[38]. Rising domestic arrears to suppliers, which were estimated at about 3.7 percent of GDP by the end of 2016, have mounted significant pressure on the private sector, directly impacting growth. Arrears on defaulted external loans amounted to over US$ 700 million by the end of 2017.
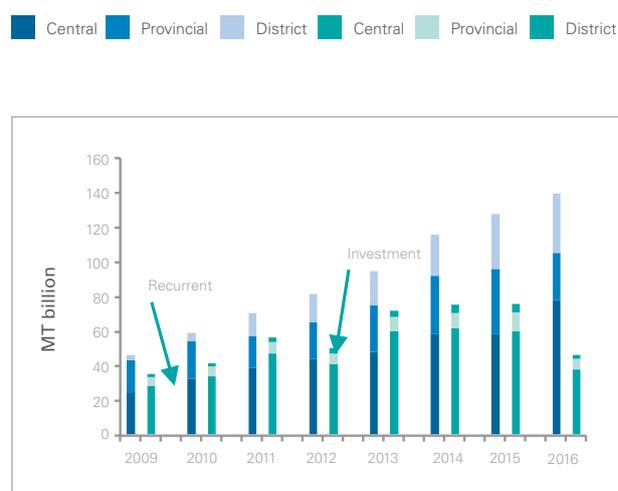
Another issue with the current PFM system is that of rolling balances. According to a note published by the Mozambican think tank, IESE (Instituto de Estudos Socias e Económicos), there are large cash balances at the end of the year that are delinked from the single treasury account (Conta Unico de Tesouro, CUT). These cash balances amounted to about 25 percent of the total resources available to the government in 2016 and averaged US$ 1.9 billion in 2013-2015, almost equivalent to the average resource allocations to education, health, WASH and social protection during that time. According to the same source, these balances amounted to about US$ 1.2 billion in 2016. The continued existence of these balances without adequate explanation can impact future fiscal space including for priority spending for children. The MEF, in a recent response to a query raised in parliament, stated that these rolling balances include balances with entities that do not form part of the central government (municipalities, institutes, other funds and SOEs) and hence also remain outside the CUT and are consequently not reported in the CGE.

2.4.2 Revenue performance

There has been a rapid increase in domestic revenue collection in the past decade. Since the revenue authority was established in 2006, domestic revenues increased from less than 16 percent of GDP to over 25 percent in 2017. Mozambique's tax-to-GDP ratio remains relatively high compared to its peers. Total collections, including non-tax revenues, peaked at over 29 percent in 2014. Significant amounts of CGT, though one-off, further boosted revenues in 2012-2014, amounting to as much as 3 percent of GDP in 2014. In the absence of CGT, revenue collection in 2015 declined slightly compared to 2014. In 2016, the revenue target was revised downward as the macroeconomic environment had an impact of overall collection. Collection in 2017 was once again boosted by one-off CGT received by the government[39].

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37. According to Weimer (2017), priorities include debt repayments, salaries and pensions, and indispensable spending including hospitals and security.
38. This is reflected in the figures by IMF (2018).
39. ENI, major investor in the Coral South natural gas field, sold 50 percent of its stake to Exxon Mobil triggering a CGT of about US$ 353 million, or 2.8 percent of the GDP.

The single largest source of revenue to the government is Value Added Tax (VAT). This is followed by taxes on corporations, including one-off CGT. In 2013-2014 for instance, about 70 percent of the direct taxes were collected from corporations. Of these, CGT amounted to almost 30 percent while the rest was corporate income tax (CIT). Personal income tax (PIT), until 2009, brought the state more revenues than CIT. Growth of the PIT in recent years is a result of rising real government wages and an increase in the number of highly paid expatriates[40].

While VAT is a regressive tax in which poorer households are burden more than the well-off since they spend a high proportion of their income on consumption, it is applied for its effectiveness in revenue mobilisation. Given this equity-efficiency trade-off, it is important to complement VAT with progressive income tax system as well as pro-poor expenditures in order to address the challenges of equity[41]. While VAT collections can help channel funds for such pro-poor expenditures, this tax should not replace income taxes. Contributions from CIT are gradually accounting of a higher proportion of the overall revenues compared to PIT. It would be essential to maintain this trend. Removal of tax exemptions to megaprojects can provide a significant boost to collections under this category.

| FIGURE 2.14 | Tax-to-GDP ratio in Mozambique is high compared to other low-income countries |

Direct   Indirect
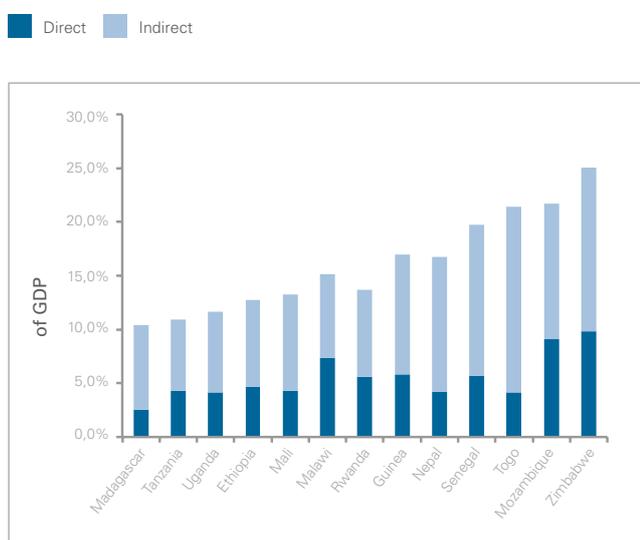
Source: ICTD Government Revenue Dataset, UNU Wider

| FIGURE 2.15 | VAT is the largest contributor despite boosts from CGT in direct taxes |

CIT   CGT   PIT   VAT   Int. Trade   Other Taxes

Source: CGE

The tax base in Mozambique remains narrow, and combined with high statutory rates, this poses a significant burden on the current taxpayers. This is further aggravated by VAT non-repayments by the government; in 2015 these arrears amounted to as much as 4 percent of GDP . Coupled with depressed growth, accumulating public arrears and high cost of finance, the private sector is disproportionately affected by the current crisis. On the other hand, contributions from large businesses, megaprojects in the extractive industries in particular, to overall tax revenues remain fairly small compared to the scale of their operations and export earnings. This paradoxical situation, where government on the one hand is accumulating arrears in VAT repayments and on the other sanctioning generous benefits to large businesses, has increased the perceptions of unfairness of the current tax system. The unfavourable macroeconomic environment poses the risk of increasing the informalisation of the economy potentially reversing the positive achievements of the past as reflected in the tax-to-GDP ratio[43].

According to the IMF, revenue performance over the medium term will be under pressure and growth observed in the past will be difficult to sustain considering the slowdown in economic activity due to the economic crisis. Thus, the proportion of overall domestic revenues in GDP is forecast to decline.

40. Swistak et al. (2017).
41. Minh Le (2003)
42. Ibid.
43. According to the last national survey of the informal sector (2004) informal sector accounted for over 40 percent of the GDP and is not entirely accounted for in the national accounts (Swistak et al., 2017).

2.4.3 Current expenditure performance

Current expenditure has increased rapidly in line with the expanding budget. Fluctuation in this type of expenditure has been smoother than in investment expenditure which has absorbed most of the volatility of the government budget. Current expenditure increased from 15 percent of GDP in 2009 to 22 percent in 2014. Despite the fiscal adjustments which took place after the expansionary budget in 2014, the level of current expenditure remained at over 20 percent. While it accounted for little less than 60 percent of the total expenditure between 2009 and 2015, by 2016 this proportion increased to 70 percent.

The wage bill, which is the largest component of current spending, increased from 8 percent of GDP in 2009 to a little over 11 percent since 2014. While other lines of expenditure can be adjusted downward (or arrears can be accumulated through deferred payments), wages and salaries cannot.

Spending on the public payroll is also not necessarily advisable, when the low ratio of service providers in education (e.g. pupil teacher ratio) and health (e.g. health worker to population ratio) is considered. Despite increases in nominal terms, real income in the civil service has significantly eroded as the minimum wage rose more slowly than the price level and the US Dollar value of the currency. In dollar terms, the minimum wage among the civil service has declined by almost a third since its peak in 2014[44]. This could potentially have negative implications for the quality of public services as teacher and health worker absenteeism and other challenges might increase.

Transfers are another sticky line in current expenditures, accounting for about 10 percent of total expenditure between 2009 and 2016. Interest payment and debt service have gained a lot of significance in the total as these rose steeply to 21 percent of expenditure in 2016, crowding out spending in other areas, including social sectors. Finally, after seeing steep rises between 2011 and 2013, expenditures on goods and services have been adjusted sharply downwards declining almost 1.5 percentage points of GDP between 2014 and 2016.

Given these expenditure items which are contingent and (politically) difficult to adjust drastically downwards, current expenditure can only be adjusted at a slower pace. Moreover, given the very recurrent nature of these expenditures execution rate of these expenditures tends to be high, close to 100 percent, with over spending in some years, especially in the wage bill. In 2016, considering the fiscal challenges faced by the government, execution of expenditures on goods and services declined to a little over 90 percent.

According to the IMF, in the medium term, despite persistent and serious challenges to government finances, current expenditures will remain at over 20 percent of GDP[45]. In the nearer term, given the upcoming elections later in 2018 and 2019, spending pressures are expected to rise significantly, although there is less space to increase these expenditures at the pace observed in 2014. The decentralisation bill currently being discussed may also result in changes in the pattern of expenditures with a larger shift to deconcentrated levels.

2.4.4 Investment expenditure performance

Public investment has been an important component of public expenditure in Mozambique, especially in the post-war context, and accounted for about 10 percent of GDP between 2000 and 2008. The discovery of significant natural resources gave a further impetus to this type of expenditure. As the government embarked on a public investment drive, expenditure increased to 14-15 percent between 2011 and 2014. This ratio is high not only compared to peer countries like Uganda and Tanzania that are also expecting revenue streams from natural resources but also compared to those with established streams like Angola and Botswana[46]. In 2015 in response to the necessity to rein in expenditures, investment expenditure declined slightly to 13 percent of GDP. In 2016 however, these expenditures took a large hit and declined to under 7 percent of GDP. The recent trend in investment expenditures in real terms shows a sobering picture. While these expenditures grew in double digits in some years, growth since 2013 has been on a downward trend with a severe contraction in 2016. It is worth pointing out that while domestically financed investments have experienced a smooth rise until 2014 bringing about a generally rising trend in total investment expenditures, externally funded investment spending has been volatile with average growth over the period (2009-2016) of -3 percent.

The evolution of the resource envelope for investment expenditure shows that domestic resources have gained significance. In 2004-2009, domestic resources accounted for about third of total expenditure on public investment; it then increased to 46 percent between 2010 and 2013 as donor assistance in the global resource envelope started declining. In 2014 and 2015 domestic resources accounted for almost 60 percent of total public investment expenditure before declining to 50 percent in 2016.

The execution of domestically financed investment expenditure has been high, with overspending in some cases. On the other hand, execution of externally financed investment expenditures has been volatile, averaging around 70 percent. Thus, execution of overall investment expenditure has been lower, averaging about 84 percent between 2009 and 2014. By 2015, the execution rate dropped to 77 percent. In 2016, despite a downward revision in the revised budget, overall execution of investment spending was low at 66 percent. Once again, execution of domestically financed investment (82 percent) was high while that of externally financed investments plummeted (to 57 percent).

44. http://www.open.ac.uk/technology/mozambique/sites/www.open.ac.uk.technology.mozambique/files/files/Mozambique 409-wage_&_exchange_rate_supplement_2018.pdf
45. IMF (2018).
46. World Bank (2016c).
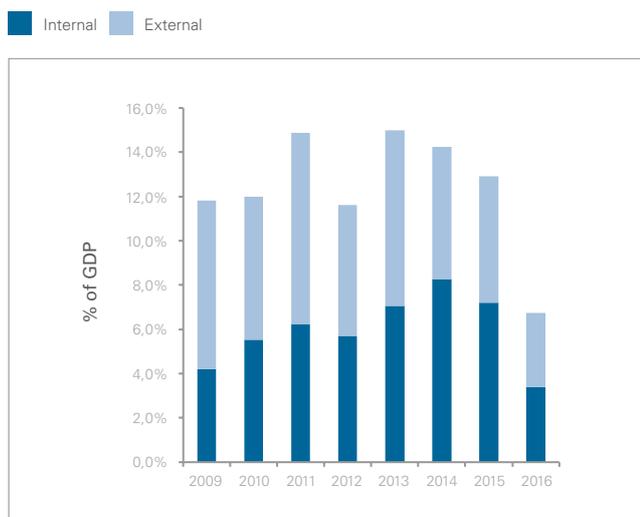
Source: GFS

Source: GFS

Investment expenditure are the first to be adjusted in times of crises. With the current condition of public finances there will be limited space to increase public investment in the medium term. Domestic resources will be under severe pressure, while reduced donor assistance limits the scope to raise finances through this mechanism. With the downgrading in Mozambique's credit rating and continued suspension in the IMF program, borrowing in the international market will be prohibitively expensive.

2.4.5 State enterprises

The state has stakes in several companies that serve a social objective or for commercial objective to finance the state budget. There are currently 13 state owned enterprises i.e. with 100 percent stake by the state. These include strategic sectors for public services like utilities (Electricidade de Moçambique, EDM), communications (Rádio de Moçambique, RM), transport (rail passenger operations of Caminhos de Ferro de Moçambique, CFM), including others like agricultural development (Ragadio do Baixo Limpopo, RBL), infrastructure development (Maputo Sul). Commercial interests of the state are represented in airports (Aeroportos de Moçambique - Mozambique Airports), transport (CFM), oil (Empresa Nacional de Hidrocarbonetos, ENH). Apart from this the state has stakes in several other entities, 109 companies, that may or may not be majority state owned. These include strategic or social objectives for instance, the stake in Petromoc which could be justified for provision of fuel in remote areas where private entities may not enter, or commercial interests such as the stake in Coca-Cola.

A recent report by the World Bank lays out some of the major fiscal risks arising from public corporations. Apart from the five-year plan (Programa Quinquenal do Governo - PQG) there is no clear documentation to set out the role that public enterprises should play (participation or regulation) and in what sector[47]. With a lack of proper regulatory framework, enterprises which exercise monopoly for instance in utility provision (EDM) also act as the regulator, which can be a source of conflicts of interest. According to government published data, of the 13 SOEs, only two, CFM and ENH, have shown profits while others have been running losses[48]. In some cases, this has been a result of mismanagement. For instance, political interference and freeze in tariffs meant that companies had to absorb the high costs of production thereby running losses[49]. Moreover, subsidies from government are relatively limited, and in many cases face delays.
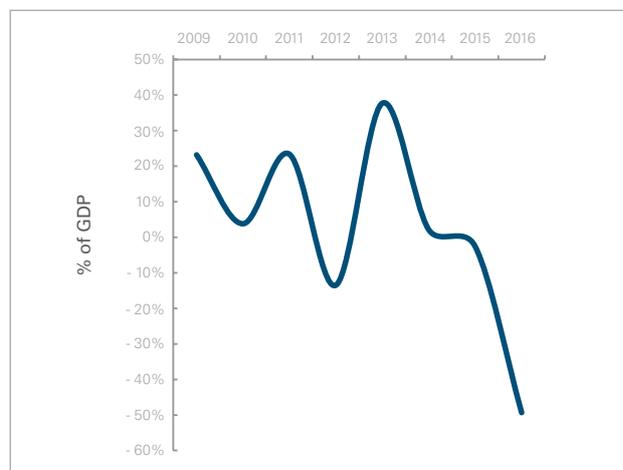
As the government embarked on the public investment drive, state enterprises were used as a vehicle to implement several investment projects. On-lending is the largest source of financing to these companies, especially for construction, but repayments remain low[50]. Sometimes debt is directly raised by these companies, increasingly on non-concessional terms, with government guarantees but their consolidated debt position is not known. Guarantees to public corporations in 2013 and 2014 exceeded the legislated limit[51]. More worrying still is the fact that debt with public guarantees was increasingly from public corporations with poor financial record or no record at all, as is shown by the fact that the three public corporations which contracted large debts were created shortly before the loans were taken. This shows that public corporations are a source of significant fiscal risk to government finances and it is a matter of urgency to monitor these risks by moving towards greater fiscal transparency and accounting for liabilities in the government books.

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47. World Bank (2016b).
48. Ibid.
49. This was especially the case with EDM. Electricity prices were frozen between 2010 and 2015 in reaction to riots in September 2010 and so the company could not raise tariffs.
50. World Bank (2016b).
51. Ibid.

2.4.6 Government debt (external, internal)

Expenditure has been expansionary and procyclical without the necessary financing from domestically mobilized revenue in recent years. Donor support was not sufficient to cover the financing gap, and thus the government increasingly resorted to borrowing. According to the data by the central bank, the external-debt stock increased 2.5 times between 2009 and 2017. Bilateral loans have dominated the overall debt, especially since 2014, which include a mix of concessional and non-concessional loans. Accumulation of debt on commercial terms has led to sharp increases in debt servicing costs. For instance, multilateral loans were equivalent to 41 percent of the total debt in 2016, with debt servicing costs of about 18 percent (of the total debt servicing costs) given their concessional terms. Bilateral loans stood at about 42 percent of the total in 2016 and accounted for representing the same amount in debt service. Commercial loans on the other hand, about 17 percent of the total debt, accounted for 40 percent of the total debt servicing costs[52]. The discovery of the undisclosed loans, equivalent to 10 percent of GDP in 2015, pushed the external debt levels from

66 percent to 76 percent of GDP in 2016[53]. However, the resulting depreciation of the currency pushed these proportions even further since most of the debt is denominated in US$. Moreover, the non-concessional terms of the loans meant that the debt servicing costs soared. By the end of 2016 external debt stock was equivalent to 104 percent of GDP[54]. By 2017, this proportion came down somewhat as the currency stabilised, but debt levels remain untenable. According to the IMF, Mozambique's debt is in distress.

Government domestic borrowing domestically is also substantial. Domestic debt was in single digits as a proportion of GDP until 2015. However, with the revelations of the large external debts, government finances received a sudden shock - economic activity slowed considerably, donor support was halted, external financing became difficult. Thus, the government borrowed internally, and this proportion increased to 25 percent by 2016[55]. By December 2017, the stock of domestic debt stood at over MT 100 billion.

| **FIGURE 2.18** | External debt increased rapidly, dominated by bilateral debt which includes a mix of concessional and non-concessional loans |

■ Multilateral ■ Bilateral

Note: These figures may not match with those from IMF
Source: Banco de Moçambique

| **FIGURE 2.19** | Domestic debt increased sharply in recent years |
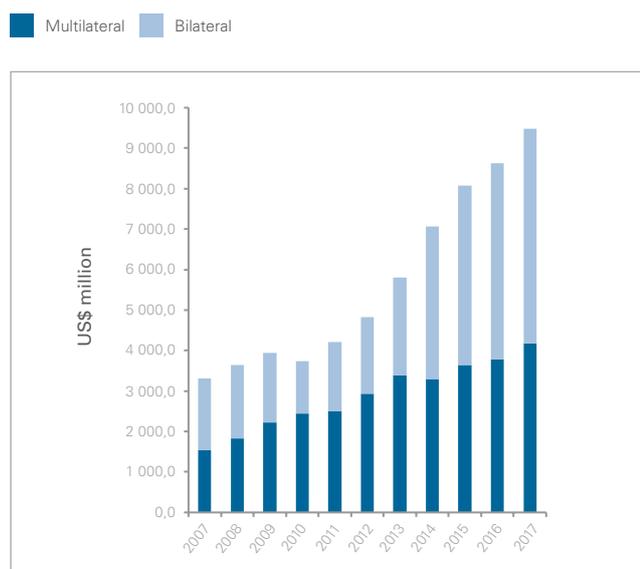
Note: These figures may not match with those from IMF
Source: Banco de Moçambique

The government has essentially been in default on its payments since 2016 when it missed the payment on the undisclosed loans on the companies (MAM). In January 2017, it defaulted on the sovereign bond interest repayment which had been swapped for the debts of another public corporation (EMATUM)[56]. The debt servicing costs reached 26.5 percent of the total revenue in 2016[57]. These costs include both external and domestic debt and are expected to increase further. This situation has highly significant implications for fiscal space to increase spending on social priority sectors in the medium term.

While shocking to many, it is worth noting that the loans contracted in 2013 (and then discovered in 2016) took place in a very different context. In 2013 commodity prices were high, the economy was awash with foreign investments and the anticipation of the massive gas revenues created high expectations about the future, leading to an unrealistic picture of the state of the economy. This misled perception led to imprudent decision-making including borrowing at commercial rates for projects that were rushed through and not subject to sufficient scrutiny and appraisals. This seems to have been the common story for most of the government decisions in

52. AfDB (2017).
53. World Bank (2017b).
54. IMF (2018).

55. Ibid.
56. AfDB (2017).
57. UNICEF (2018).

that period (focus on extractives instead of other productive sectors, on economic rather than social infrastructure, on conspicuous consumption and imports rather than production through local industries, borrowing on commercial rather than on concessional terms etc.). The narrative of an overheated economy and significant fiscal risk mainly as a result of a lack of fiscal transparency is by no means exclusive to Mozambique but a small, developing economy will be more exposed than larger and more advanced economies.

2.5 Prospects

Prospects for imminent recovery of the economy are bleak although this is contested by the authorities. While growth had already started decelerating in 2015, the discovery of the hidden loans has plunged the economy into a deep crisis. The economic growth trajectory has shifted from an average of 7 percent to less than 4 percent in 2016 and 2017. According to the IMF, the annual economic growth will remain subdued in the medium term. This view is contested by the authorities. Significant uncertainty remains over the future trend of ODA though it is safe to assume that no surge in these flows should be expected. The combination of reduced growth and declining donor support will continue to exert pressure on the budget. Moreover, without a resolution of the deadlock over accountability over the hidden debts, injection of FDI in the non-megaproject economy may be a distant possibility, as investor decisions hinge on IMF's resumption of its program. Rising debt servicing costs will crowd out expenditures on priority sectors relevant for children that are subject to ever increasing demand from a growing population. Spending pressures with upcoming elections if not handled prudently could lead to a further deterioration of the government's fiscal position. Debt levels are likely to remain at over 100 percent of GDP for the foreseeable future. With the rising cost of servicing the existing debt, the scope for increased external borrowing will be limited. Increased internal borrowing will come not only at the cost of increased difficulties of servicing the debt which will have to offer increased interest rates but also at the cost of crowding out the private sector, further exacerbating the downward pressure on growth.

Revenue from natural gas can be seen as a dim light at the end of a very long tunnel. Large anticipated capital-intensive imports to build infrastructure for these megaprojects will be financed by increased inflows of FDI. As these projects become operational, the estimated revenue stream is expected to have the potential to relieve the government of some of the pressures faced currently but only in a decade from now. The non-megaproject economy however is not expected to recover unless active steps are taken to improve the business environment and resuscitate the private sector. The divergent performance of the megaproject compared to the non-megaproject economy may become even starker in the medium term.

The government is aware that the gas reserves would bring little to the economy if they are simply exported and hence it is also looking at local content development. According to the Natural Gas Master Plan, as gas production commences, about 25 percent of the produce is expected to be diverted for domestic use in order to stimulate economic activity in the production of fertilizers, chemical and plastic. However, development of currently non-existing industries will take time and require very much improved governance to ensure efficiency in the production which is necessary to spur growth and generate employment.

Abundant natural resources alone cannot ensure sustainable and inclusive growth unless urgent steps are taken to improve access to basic services, and to reduce poverty and inequality in the context of a burgeoning population. An analysis of the current state of these services and their financing can help identify areas that can be further strengthened to achieve better results and build critical human and social capital.

2.6 Conclusion

This chapter demonstrates that while Mozambique has experienced rapid economic expansion in past two decades, the country has failed to translate this growth into better standard of living for its population. Rather than a broad-based growth, economic activity is increasingly driven by megaprojects in the extractive industries. In light of the recent crisis triggered by the discovery of undisclosed debts, confidence of donors and investors in the country has severely eroded. With reduced ODA, public finances have come under increasing pressure and there is limited scope to borrow in the international market given the high costs involved. As the government resorts to domestic debt, this crowds out the private sector, already being stifled by growing public arrears and low FDI and depressed demand. In the absence of significant adjustments in the fiscal policy, the burden of adjustment is taken by adjusting the monetary policy, further impacting the growth of the private sector.

The fiscal policy remains loose. As domestic resources increasingly substitute donor contributions, these go more towards recurrent spending rather than for investments. As the government increasing resorted to financing the deficit through borrowing, debt levels quickly rose to unsustainable levels. This may not be possible going forward. Rising debt servicing costs will squeeze the fiscal space available to increase spending on social sectors. Moreover, with subdued growth, revenue generation may not continue of the rapid growth path it had in the past. These developments point to limited scope to substantially increase spending in child-friendly areas.

3. Priority expenditure trends and policy challenges

This chapter highlights the evolution of priority expenditures over the past years (2009-2016) looking specifically at their growth over time, the composition of expenditures and sources of financing. It also looks at the specific issues observed within each priority sector for UNICEF.

3.1 Priority-expenditure composition and recent evolution

Government spending on social and economic sectors:
Expenditure in social and economic sectors deemed priority by the government increased in recent years in both nominal as well as real terms. As a proportion of total expenditure, this spending (as defined by the government, including sectors for human development like education, health, water and sanitation as well as sectors for economic prosperity like agriculture, infrastructure and social protection) has not always been in line with the target of 60 percent and in 2016 dropped to 48 percent[58]. This is because non-

discretionary spending i.e. debt servicing and financial operations have been high. As a proportion of discretionary expenditures though, spending on these sectors does account for 60 percent of the total[59]. Although as a proportion of GDP, these expenditures have been declining. Fast growth in domestic revenues has meant that more expenditures are financed through internal resources.

On the other hand, the significance of donor resources, especially grants, is declining. The following analysis uses data from the general state accounts (CGE) and the recent UNICEF report on trends in priority expenditures[60]. It is important to note that the current analysis only looks at expenditures that are on budget and reported in the CGE, and do not include off-budget spending from donors. This is especially important in the case of health where significant resources are channelled towards the sector outside the government budget.

| FIGURE 3.1 | Government priority spending has been at or above 60% of discretionary spending |
| FIGURE 3.2 | But as a proportion of GDP these expenditures are declining |

Legend: Education | Health | WASH | Social Action | Infrastructure | Agriculture | Defence | Other priority | Non-priority

CGE and author's calculations

CGE and author's calculations

Growth in spending on priority social and economic sectors defined by the government has been slower compared to overall expenditures. Average growth in priority spending between 2009 and 2016 stood at 6 percent, albeit with significant declines in 2015 and 2016. Current expenditure has increased much faster than investment spending. However, this increase in spending has failed to bring significant results. For instance, while the wage bill has risen, most of the increase in spending goes towards salary adjustments of the existing staff than towards recruiting new staff. This suggests that while efforts are made to retain and motivate existing staff, the need to recruit more staff for service delivery may not be addressed[61]. The proportion of social workers continues to remain low as shown by the teacher-pupil ratio as well as health workers to population ratio.

Spending on social and economic sectors in 2015 and 2016 contracted sharply in real terms as the total resource envelope shrank on the one hand and non-discretionary spending increased on the other thereby crowding out these expenditures. In the context of the crisis, public investment expenditure has been cut across the board. Reduced investment spending has implications for the quality of service delivery. However, expenditure analysis shows varying trends for individual sectors. The following analysis focuses on priority sectors as defined by UNICEF, which include education, health, water and sanitation (WASH) and social action, and delve further into each of the individual sectors.

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58. UNICEF (2018). According to UNICEF's Budget Memo for the fiscal year 2018, the proportion of spending on priority sectors in the overall budget increased slightly to 53 percent in 2017 before dropping to 49 percent in 2018 (UNICEF, 2017b).
59. UNICEF (2017b)
60. UNICEF (2018)
61. World Bank (2014).

3.1.1 Recent evolution of priority expenditure for children

Between 2009 and 2016, expenditure on the four priority sectors for the purposes of the analysis increased significantly in both nominal and real terms. In nominal terms, spending on priority sectors increased from MT 28 billion in 2009 to MT 79 billion in 2016, representing an average increase of 16 percent a year. Real expenditures on the other hand increased much slower by 7 percent a year on average, though performance between different years remains varied. Significant increases were observed in 2012 and 2013 while spending remained flat in 2014 when pressures of the election year meant spending was focused in other areas. Rapidly rising inflation in 2016 meant that even as spending in these sectors increased 12 percent in nominal terms, these expenditures shrank in real terms.

Between 2009 and 2016, as a proportion of the government spending, priority sector expenditures have accounted for over

30 percent of the total, declining temporarily in 2014. However, not all sectors are equally well financed. Education for instance is the largest sector accounting for 56 percent of the total priority expenditures, followed by health at about 27 percent and WASH at 14 percent. Spending on social protection, though it has increased during this time, remains relatively small at less than 4 percent of the priority expenditures.

A comparison of initial allocations to these sectors and actual expenditures shows that execution rate is high, over 90 percent on average though this hides significant disparities between sectors as shown below. Years 2012 and 2013 again stand out with actual spending higher than initial allocations. This was also observed in 2016.

FIGURE 3.3	Spending on priority sectors increased rapidly, though growth in real terms is more modest

Source: CGE and author's calculations

FIGURE 3.4	These sectors account for a significant proportion of total government expenditures
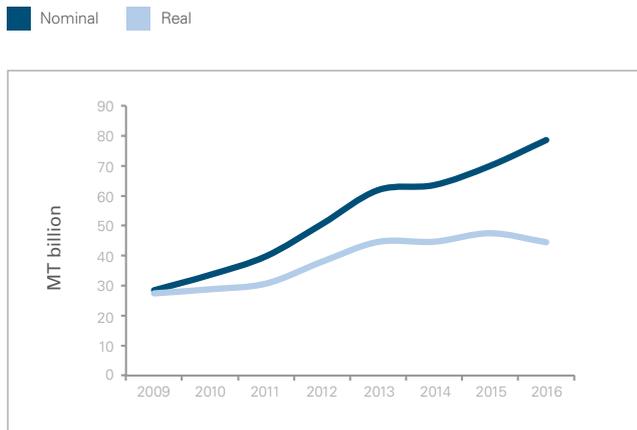
Source: CGE and author's calculations

As a source of funding for priority expenditure, domestic revenues have become more significant compared to a few years ago. In 2009, domestic resources financed about 57 percent of the total expenditures on priority sectors. By 2015 this proportion had increased to 82 percent before declining to 77 percent in 2016. The increase in expenditures from domestic revenues however is overwhelmingly going towards recurrent spending which increased from 48 percent in 2009 to 72 percent in 2016. While recurrent spending in real terms increased on average by 12 percent per year between 2009 and 2016, investment increased just over 2 percent.

These expenditures have seen declines since 2014. It is worth noting that investments in priority expenditures have increased much slower compared to other (economic) sectors. Investment spending in priority sectors remains dominantly supported by external resources which have on average financed over 80 percent of these expenditures, except in 2014 and 2015 when their share declined to about 62 percent. Moreover, external resources tend to be more volatile than internal. Support from common funds at the sector level has also declined. This has severe implications for the consistency of service delivery.

FIGURE 3.5 Significance of internal resources has increased over the years

Legend: Nominal, Real
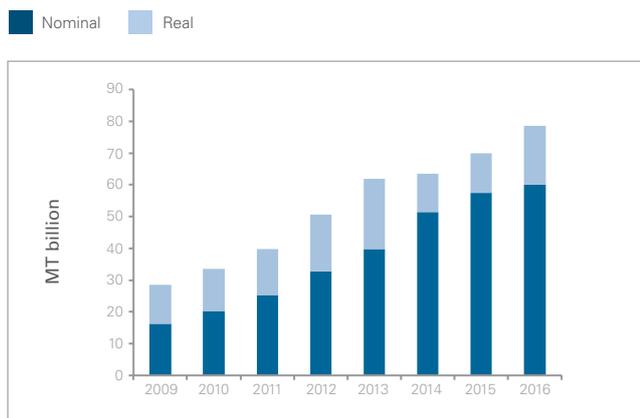
FIGURE 3.6 However, the increase in channelled more towards recurrent spending

Legend: Current, Investment
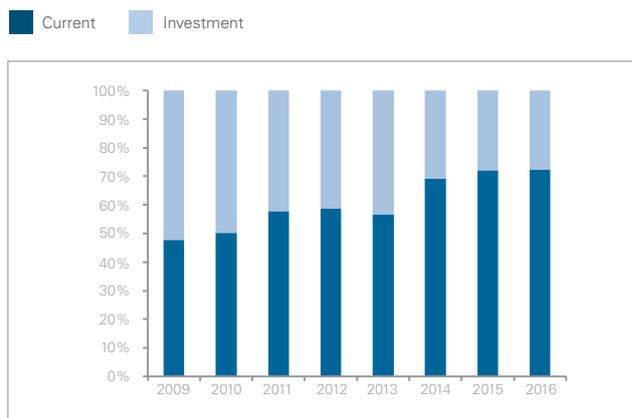
FIGURE 3.7 External recourses dominate investments

Legend: Internal, External
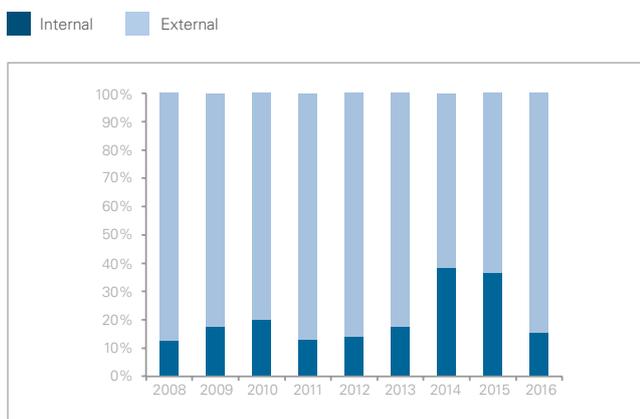
FIGURE 3.8 Known to be volatile

Legend: Internal, External
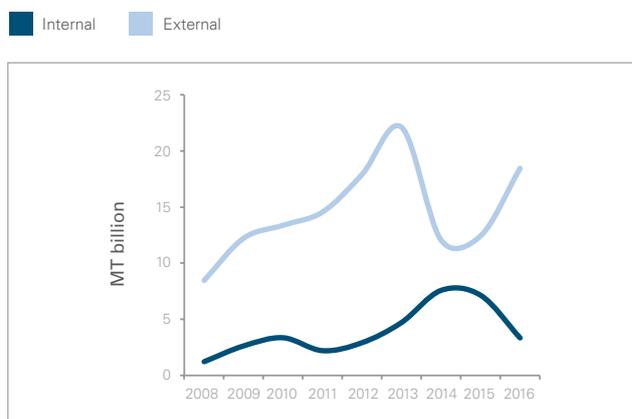
FIGURE 3.9 Donor Support in terms of Sector Common Funds is also declining

Legend: FASE, Education Total, PROSAUDE, Health Total, PRONASAR/ASAS, WASH Total
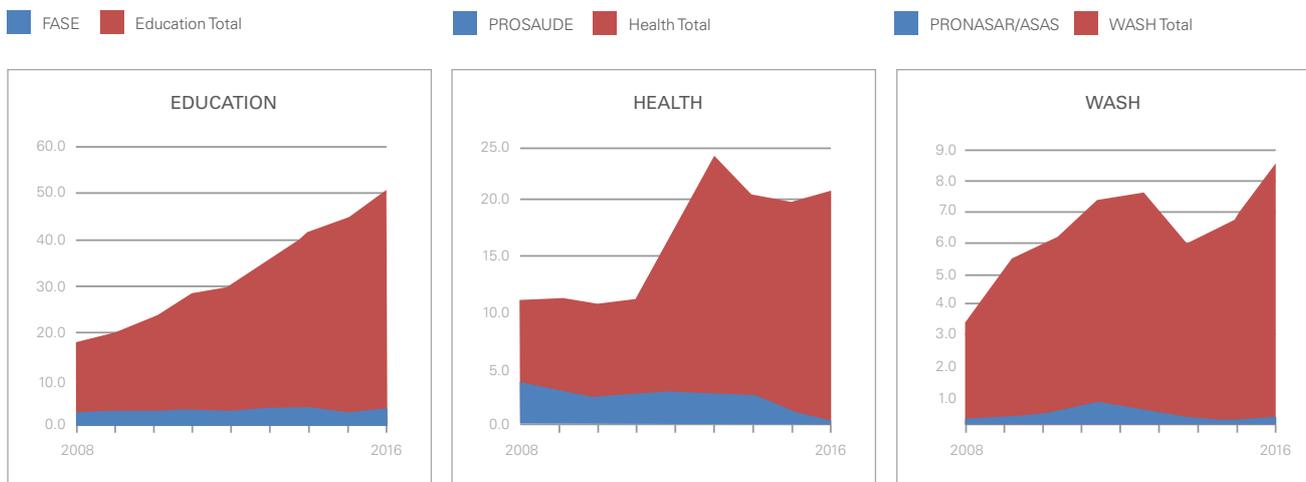
Author's calculations based on CGE and UNICEF

1.1.1 Efficiency of priority expenditure:

The level of priority expenditure has increased significantly in the past years and the country has made progress in outcome indicators like primary and secondary education enrolment rates, mortality rates, access to improved water and sanitation. However, increased expenditures have not yielded the desired results. Mozambique still remains behind its peers in several development indicators. Moreover, the recent census reveals that the population is higher than previously anticipated, thereby affecting the existing ratios that determine progress. The fact that the country spends more than other countries in sectors like education to achieve average results shows there is room for significant improvements through efficiency gains[62]. On the other hand, in sectors like health, the country spends less compared to its peers and hence progress in achieving desired outcomes in less than optimal. At the same time, there are other countries that have attained better outcomes given similar levels of spending suggesting that there is scope for improving efficiency. While there are limited studies with in-depth analysis of spending efficiency, anecdotal evidence suggests that efficiency is low in Mozambique. The following section looks at individual sectors.

1.2 Sectoral issues in priority expenditure

1.2.1 Education

Spending: Education is a priority sector for the government and this is evident from the spending in the past years. Education spending as a proportion of GDP has consistently been high, at 6-7 percent. This is high compared to an average of 4 percent in SSA[63]. Spending as a proportion of total expenditures has fluctuated somewhat, from 20 percent in 2009 to a little over 16 percent in 2014 before rising again to reach 21 percent by 2016. Nevertheless, on average,

spending on education as a proportion of total government spending is around 19 percent, also high compared to average in SSA at 14 percent[64]. In nominal terms education spending increased from MT 17 billion in 2009 to MT 47 billion in 2016. Real growth between 2009 and 2015 has been positive, averaging 9 percent. However, growth in 2016 was negative and the level of expenditure in real terms has stagnated since.

Most of the resources in the sector come from internal sources which have increased from 70 percent of the total education spending in 2009 to almost 90 percent in 2015-2017. However, most of the expenditures are towards recurrent costs, mainly salaries[66]. Over time, the proportion of investment spending in the sector declined from 35 percent in 2009 to 15 percent in 2016. Funding from common fund to channel external resources to the sector, called FASE, has also declined from 20 percent to 8 percent of total funding for the sector. Given the high level of current expenditures, execution rate is high at 92 percent compared to 87 percent for overall government expenditures. While execution of domestic expenditures is almost 100 percent, it is dragged down somewhat by lower execution of external resources which are spent more on capital expenditures as well as goods and services. The declining share of external funds has implications for the investments and acquisition of goods and services in the sector. Spending is quite decentralised with almost 57 percent of the total being executed at the district level, in part due to the high level of current spending. However, internal investment budget is small providing limited scope to respond to local priorities . External resources on the other hand, remain quite centralised[67].

| FIGURE 3.10 | Real spending has increased smoothly in recent years |

■ Real spending (MT billion, left) ■ of total govt expenditure (%, right)
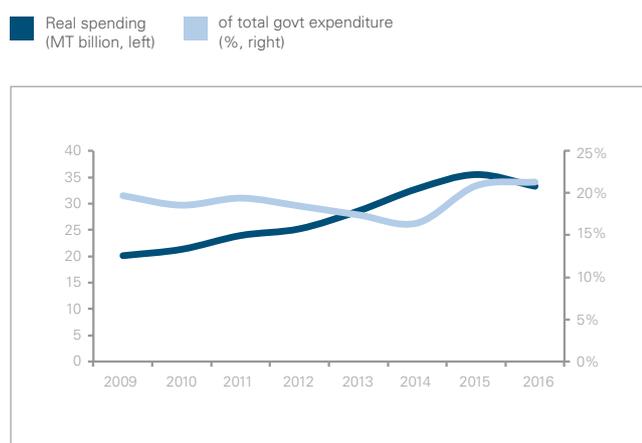
Source: Based on UNICEF data from CGE

| FIGURE 3.11 | Though per capita expenditures (in US$) has declined |

■ Nominal ■ Real
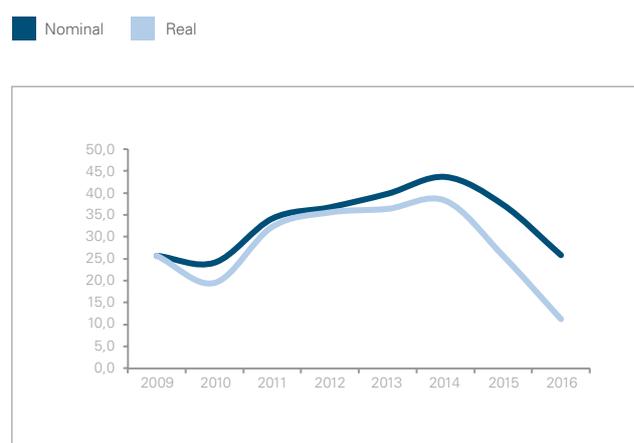
Source: CGE, WDI and author's calculations

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62. World Bank (2017a).
63. UNICEF (2018).
64. Ibid.
65. Between 2009 and 2014, 93 percent of the increase in education spending was on labour followed by 5 percent for investments and 2 percent for goods and services (World Bank 2017a).
66. Ibid.
67. UNICEF (2018)

Outputs: Increased spending in education has brought positive results. According to the Public Expenditure Review on Education (E-PER) from 2017, the number of teachers nearly doubled between 2004 and 2016 (from 67,940 to 134,919) which helped reduced the pupil-teacher ratio from 76 in 2006 to 62 in 2016 though this ratio is still high compared to the SSA average of 41. Given budget constraints, sustaining the past trend of contracting on average 8,000 new primary school teachers per year will be challenging. According to the 2018 budget, this number was down to 5,000[68]. Thus, it seems unlikely that the targeted ratio of 57 by 2019 will be achieved. There are significant gaps in teachers' knowledge and teaching ability as shown by low scores in assessments like World

Bank survey on Service Delivery Indicators. Moreover, supervision and support mechanisms tend to be limited. Investments in these areas, which show tangible results only in the medium term, tend to be overlooked and instead projects with high visibility like building of schools and acquisition of benches are prioritised. For instance, teacher absenteeism was high at 56 percent in a recent survey with teachers either not in school or not teaching in the class when they were supposed to[69]. This is more pronounced in the Centre and North of the country. More recently, a new supervision mechanism led by districts has been put in place since 2017. This will help track teacher and student performance and minimise absenteeism.

FIGURE 3.12	The number of teachers has grown

■ EP1　■ EP2　■ ESG1　■ ESG2

Source: World Bank (2017a), pg 53

FIGURE 3.13	But teacher skills remain low

■ South　■ Centre　■ North

Source: World Bank (2017a), pg 55

Heavy investments in building new schools and acquiring better inputs has also shown results especially in reducing the distance travelled to schools. However there still remain significant disparities between regions. Many students are still taught in schools made of nonconventional materials, and about one third continue to sit on the floor. While the cost of textbooks production has been brought down significantly, their distribution is still expensive, and many are siphoned off to be sold illegally. Once again, given budget constraints, these expenditures are likely to be affected going forward.

While nominal spending per student increased by a factor of 3.5 between 2008 and 2016 on average, spending in the sector has not been equitable[70]. Tete, Nampula, Cabo Delgado and Zambézia have consistently been under funded compared to their needs and size. Zambézia has been the least funded province throughout this period with spending levels at about half of the per-student spending in Maputo in 2016[71]. While the benefits of primary education are equally shared among the poor and rich as well as boys and girls alike, this is not true of secondary and tertiary education which disproportionately benefits the least poor and boys (especially in tertiary education)[72].

68. MINEDH.
69. World Bank (2015).
70. UNICEF (2018).
71. Ibid. This is an improvement compared to the fact that spending per student in the province was one third of the level in Maputo in 2008.
72. Ibid.

FIGURE 3.14 Spending among provinces is not equitable
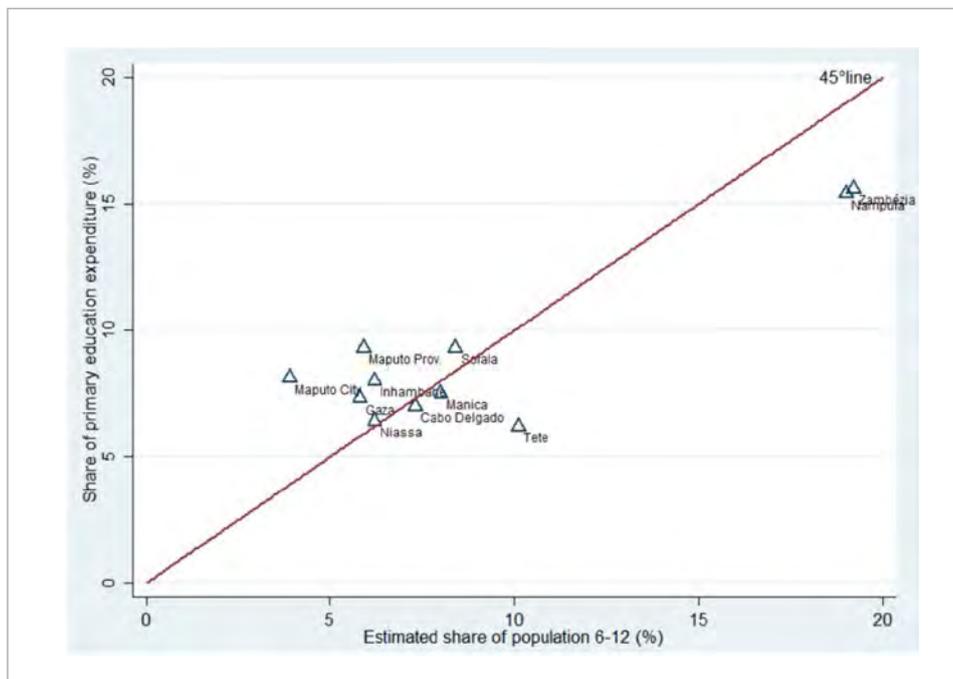
Source: World Bank (2017a), pg 42

Outcomes: According to the E-PER, Mozambique has made significant progress in education particularly in terms of enrolment rates. Lower primary enrolments increased by 63 percent between 2004 (when school fees were abolished) and 2016 while those for upper primary increased by 88.5 percent in the same period. However, according to the same source, of those enrolled at the primary level, less than half successfully completed their education in 2014, compared to 69 percent in SSA. While enrolment at lower secondary level increased to 41 percent in 2016, only 22 percent completed their education. This is much lower than in SSA on average where enrolment is 32 percent, while completion rate is 41 percent. Similarly, enrolment at upper secondary level of 23 percent is lower compared to 32 percent in SSA with a completion rate of only 9.5 percent. Low completion rates are caused by high repetition rates and dropouts. Repetition rates, though reduced over the last decade, still remain high. Based on data from the Ministry of Education (MINEDH), the E-PER also shows that only 26 percent of pupils who enrol in Grade 1 complete Grade 6 without repeating. Moreover, dropout rates at Grade 1 are 17 percent, and by Grade 4 reach as much as 20 percent. This shows that while progress has been made in increasing enrolment, student achievements are lower and the education system is not able to retain students[73].

FIGURE 3.15 Primary completion rates remain below the regional average
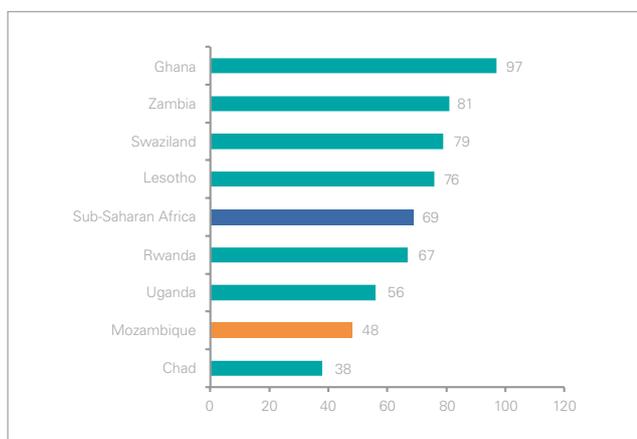
Source: UIS

FIGURE 3.16 With a large gap in secondary education completion
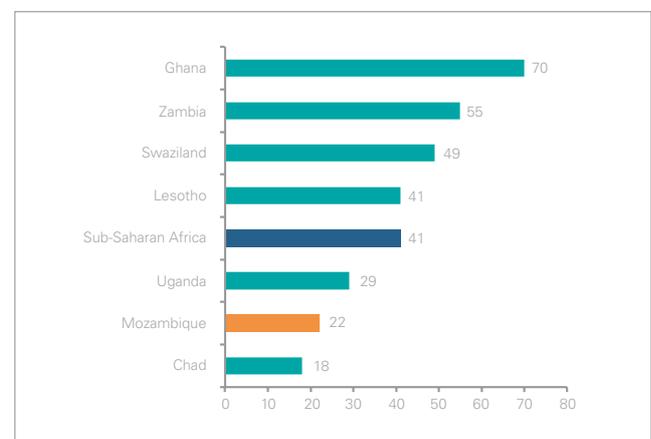
Source: UIS

73. Ibid.

Access remains a concern. According to the Demographics and Health Survey (DHS) from 2011, 49 percent of the children aged six had never been to school, further increasing to 56 percent in rural areas. Absenteeism of students is high in the North (65 percent) and Centre (61 percent) compared to the South (20 percent), with economic constraints being sighted most often even though school fees have been abolished. Gender disparities are also higher in the Centre and North of the country.

Learning outcomes are also low. The first national learning assessment in 2013 concluded that only 6.3 percent of Grade 3 pupils had the requisite reading competencies. This achievement is also low when compared to other countries, for instance the 2014 Service Delivery Indicator Survey showed that of the 6 countries in SSA with comparable data, Mozambique had the lowest score in terms of pupil competencies and spent more in terms of government expenditures.

FIGURE 3.17 Access remains a concern

At school   Dropout   Neverbeen at school

Source: World Bank (2017a), pg 24

FIGURE 3.18 Learning outcomes remain low

Language   Mathematics   Nonverbal reasoning
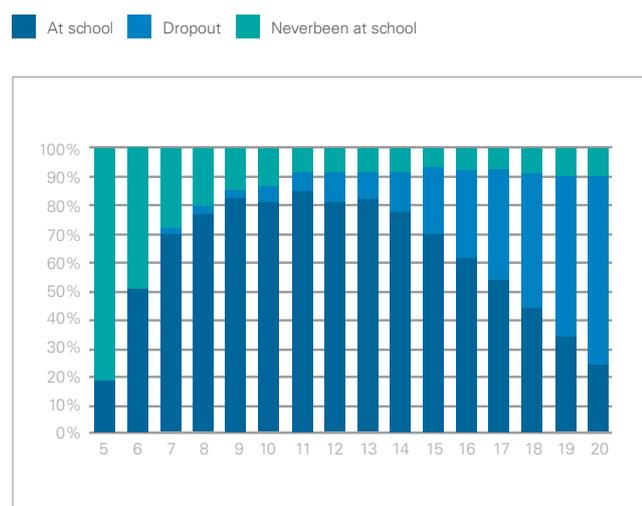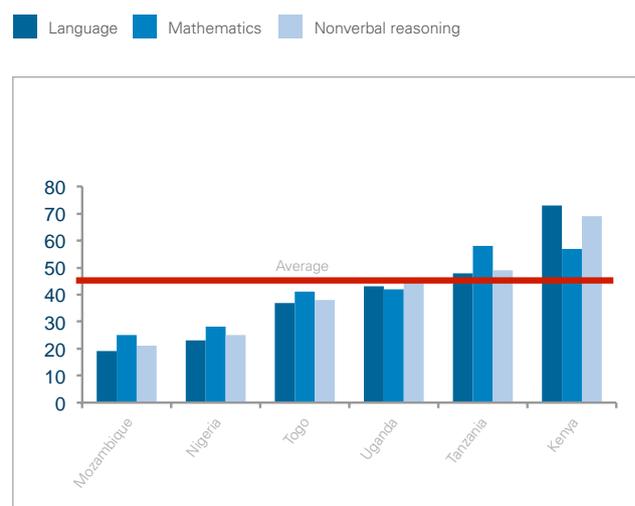
Source: Based on World Bank (2017a), pg 27

3.1.2 Health

Spending: Health spending as a proportion of GDP has averaged 3 percent between 2009 and 2016 but has fluctuated significantly. From its peak in 2013, when it reached 4.3 percent of GDP, health expenditure has to its average level of 3 percent in recent years. Similar trends are observed when considering health spending as a proportion of the total government expenditures. After peaking at 11 percent in 2013, these expenditures approached their average of 9 percent (observed between 2009 and 2016). This is comparable to other low-income countries (LIC) in the region and slightly lower than in SSA. Nevertheless, it remains well below the share of 15 percent committed under the Abuja Declaration and the country remains far from achieving the goals set out in the five-year plan or the 2030 SDG heath target. Mozambique is estimated to have a financing gap of US$ 53 per capita to attain an essential service delivery in health[74].

Between 2009 and 2017, growth in real terms has averaged 7 percent, though quite volatile. For instance, spending in the sector grew from MT 8 billion in 2009 to MT 16 billion in 2012 and further to MT 21 billion in 2013, mainly as a result of donor funds, driven in part, by the introduction of new commodities, such as vaccines. This translated into high real growth in health spending. In the absence of large donor funds, growth was negative in 2014. Since then, spending in nominal terms has been on a slowly increasing trend (from MT 17 billion in 2015 to MT 21 billion in 2016), though in real terms spending declined in 2016 given high inflation.

It is important to note that these expenditures do not include off-budget financing which is typically high, between one-quarter and one-third of the total sector spending.

There is a consistent mismatch between budget allocations and actual expenditure. This is mainly due to the difficulty in tracking external donor resources, a substantial proportion of which is off the single treasury account (Conta Unica de Tesouro, CUT) and even off the budget. The lack of timely reporting on donor resources that are included in the budget but remain off-CUT distorts the execution rate. On the other hand, the execution rate of domestic resources allocated to health is very high. The proportion of donor funding has been volatile and followed a declining trend over past years from 52 percent in 2009 to only 27 percent of the total health budget in 2016. Mirroring tendencies from other sectors this has resulted in a significant decline in investment expenditures from 61 percent of total sector expenditure to 32 percent during the same period. The common fund PROSAUDE has also seen its resources decline over the years from 52 percent of the total spending in the sector in 2008 to just 2 percent in 2016. This is currently being replaced, in part by a new World Bank performance-based programme financed by the IDA, Global Financing Facility Trust fund, and a multi-donor trust fund and project specific support. Internal investments are increasingly supporting the building of care facilities and others essential spending, e.g. on medicines, as external resources coming from PROSAUDE and other sources decline. District spending has risen somewhat as districts execute mostly current expenditures. Investment spending from external sources on the other hand remains heavily concentrated at the central level.

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74. World Bank (2016a).
75. For instance, total spending on health as reported in the CGE is about MT 21 billion, however actual spending was as high as MT 32 billion according to the Health Public Expenditure Review from 2016. This also means that donor resources in the sector were much higher at 70 percent, compared to what is reported in the CGE (55 percent).
76. World Bank (2016a).

FIGURE 3.19 Spending has been volatile and Mozambique is far from achieving the Abuja Declaration

Real spending (MT billion, left) ■ of total govt expenditure (%, right)

Source: Based on UNICEF data from CGE

FIGURE 3.20 As a result per capita expenditures (in US$) fall short of an essential healthcare package

Nominal Real

Source: : HNPStats and World Bank (2016a

Output: Despite increases in recurrent expenditures, there has been little progress in improving the ratio of physicians and nurses to the population, which remains below Mozambique's peers. According to the Health Public Expenditure Review (H-PER) Mozambique is identified as one of the 52 countries with a severe shortage of health workers with a ratio 4.5 workers to every 10,000 people, far below the suggested minimum ratio of 23 by WHO (2006). Despite efforts to engage community health workers through a dedicated program, the progress in improving outreach remains low compared to other countries like Ethiopia, Malawi and Niger which have similar or lower per capita expenditures compared to Mozambique. Moreover, the ratio of administrative to health workers remains high and workload between provinces is unequal leading to inefficiencies. While increasing domestic resources for investments go towards care facilities (primary, secondary etc.), it has come at the cost of spending on administrative and institutional support. While intermediate indicators like distributions of ARVs show some progress thanks to substantial funding from vertical programs, progress remains below government targets. For instance, the country is behind its target of at least 80 percent of adults and children coverage of ARV treatment; the ratio in 2016 was 64 percent and 69 percent respectively. Nevertheless, there are improvements in institutional births and immunisation coverage. Health workers and their skills are also an issue. In an unannounced

visit in 2014, it was found that a quarter of health care providers were absent; of those present, only half could properly diagnose common health conditions and only a third could follow clinical guidelines for treatment[77]. Moreover, only a third of the facilities had running water, electricity and sanitation facilities and just two-in-five had all medicines in stock[78].

While nominal per-capita spending has increased substantially between 2008 and 2016, the picture has been distorted by the high spending in Maputo province. Here too there are vast regional disparities. Zambézia records the lowest per capita spending among the provinces. Only 57 percent of the households in the province use health facilities. On the other hand, access to facilities is the lowest in Cabo Delgado with only 39 percent of the households having a health facility within 30 minutes' walk from their residence. This is in stark contrast to regions with highest access like Maputo province at 96 percent, and to regions with the highest utilisation rate like Inhambane at 81 percent . This can be a possible source of inefficiency increasing the cost of delivery of services and strongly underlines the need to use investment spending proactively to improve access to and quality of social services[80]. Finally, health spending tends to benefit the least poor more than the relatively poor[81].

77. UNICEF (2017)
78. Ibid.
79. UNICEF (2018).
80. World Bank (2016a). According to the same source, possible gains in efficiency through a more equitable distribution of resources could contribute to bridge the financing gap by at least 7 percent.

81. UNICEF (2018).
82. UNICEF (2014).
83. UNICEF (2018).

FIGURE 3.21	Other countries with per capita expenditure levels similar to Mozambique perform better

Source: World Bank (2016a), pg 13

FIGURE 3.22	Spending across provinces is not equitable

Population Share, 2012   Expenditure Share, 2012
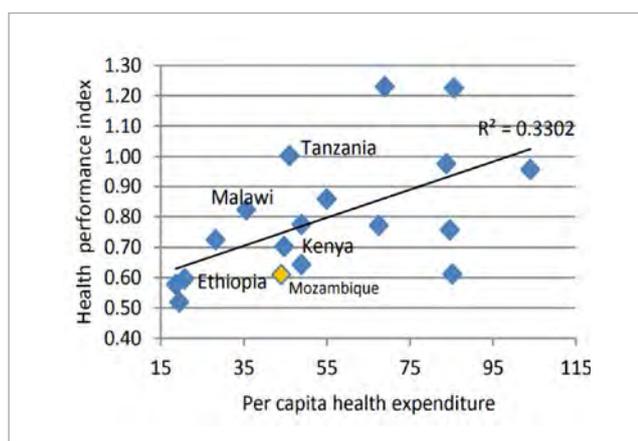
Source: World Bank (2016a), pg 23

Outcomes: Substantial improvements have been made in reducing child and maternal mortality. Under-5 mortality declined to 71.3 per thousand live births in 2016 from 220 in 1993 while maternal mortality rates have declined by nearly a third to 408 per 100,000 live births from 1000[82]. However, the country lags behind its peers in terms of other indicators like prevalence of HIV/AIDS, Malaria, TB and nutrition. Life expectancy at 55 also remains below its regional as well as below income peers (low income countries). Over the years, increase in spending has not brought desired results, and the country remains far from achieving the 2030 SDG health target of neo-natal mortality rate of less than 12[83].

3.1.3 Social Action

Spending: Spending on social action[84] has increased several fold and its significance in total government spending more than doubled between 2009 and 2016 from 0.8 percent in 2009 to 1.6 percent in 2016. As a proportion of GDP, this remains negligible, accounting for about 0.4 percent of GDP in 2016. In nominal terms this spending increased from MT 0.7 billion in 2009 to MT 3.5 billion in 2016. In real terms, spending on social action programs increased by an average of 40 percent between 2011 and 2014. However, these expenditures declined by 15 percent in 2016.

Spending has been predominantly domestically funded, increasing from 54 percent in 2009 to as high as 94 percent in 2014. However, since this peak domestic funding has been declining and reached 87 percent in 2016.

Given the nature of this spending which includes mainly cash transfers, recurrent spending in predominant. As a result, recurrent spending steadily increased from around 45 percent in 2009 to close to 90 percent between 2012 and 2016. Higher investment spending
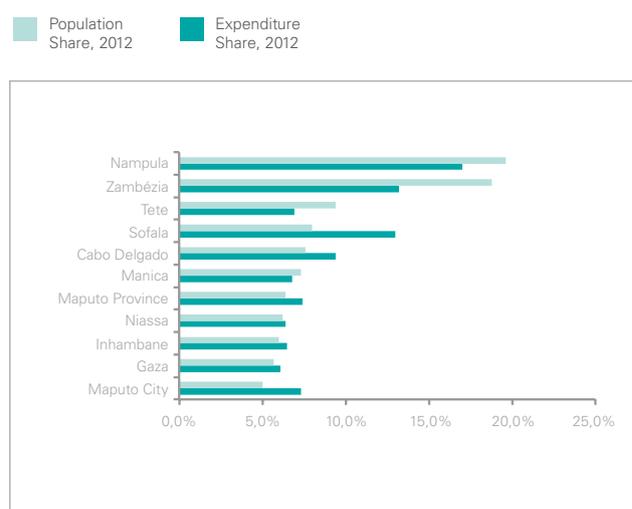
in the early years can be associated with the setting up of the social protection systems. Declining investment spending is again a result of reduced donor financing in this sector. As a result of the high recurrent spending, observed execution rate of these expenditures is also high, averaging 87 percent between 2009 and 2016.

Spending is highly decentralised to the provincial level mainly by provincial institutions of the Ministry of Gender, Children and Social Action (Ministério do Género, Criança e Acção Social MGCAS), and the National Institute of Social Action (Instituto Nacional de Acção Social, INAS)[85]. The proportion of central spending declined from 53 percent in 2009 to 12 percent in 2016. In 2017, this proportion is expected to rise to 22 percent as more donor resources support the sector and these remain concentrated at the central level.

Outcomes: Like all other social sectors, spending in social protection is not equally spread across the country. Per capita spending on the poor is low in the provinces of Zambézia and Nampula which account for the most number of poorest people in the country. Spending is also low in the provinces of Sofala and Inhambane. There is little relationship between the geographical distribution of social protection programs of INAS and the poverty in the provinces. This could lead to a worsening of inequalities in the country if not addressed in time.

The coverage of targeted households in the social protection programs remains low. By 2016, the coverage was at 17 percent, below and too far from the target of 25 percent by 2019 according to the five-year plan. Similarly, the number of vulnerable children benefitting from social action programs was at about 310,000 compared to the target of 350,000 by 2019.

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82. UNICEF (2014).
83. UNICEF (2018).
84. Though Social Action and Labour have been merged into one priority sector according to the state budget, the definition used is the same as UNICEF (2018) i.e. it is guided by the National Basic Social Security Strategy (ENSSB II) and includes allocations to Ministry of Gender, Children, and Social Action (MGCAS) and the National Institute of Social Action (INAS), and excludes the components of Labour and social subsidies.
85. Budget for District Services for Health, Women's Affairs and Social Action (SDSMAS) is accounted for under the health sector (UNICEF, 2018)

3.1.4 Water, sanitation and hygiene (WASH)

Spending: Overall spending on WASH has fluctuated between 1 and 1.5 percent of GDP between 2009 and 2016. An overwhelming majority of these resources go towards water supply. According to a study by the World Bank on water and sanitation programs (WSP) in Africa in 2011, Mozambique spends less than 0.1 percent of GDP towards sanitation and hygiene programs, lower than the commitment of at least 0.5 percent made in the the eThekwin Declaration signed in 2008 during the AfricaSan II summit. It is difficult to calculate the level of expenditures based on the current classification of the data presented in the CGE. Based on data from the CGE, as a proportion of total government spending, this sector as a whole (water and sanitation) accounts for less than 5 percent[86]. Overall spending for WASH increased from MT 3 billion in 2009 to just over MT 8 billion by 2016. In real terms, spending in this sector increased by an average of 11 percent. However, given budget constraints, this growth is unlikely to be sustained. Steep declines in real spending can be expected from the lower allocations in subsequent years.

WASH is an investment intensive sector given the heavy infrastructure needed to supply water and build sanitation facilities. Consequently, spending tilts heavily towards investment expenditures, which range between 80 percent and 90 percent of the total. At the same time, relatively small allocations towards recurrent expenditures and limited human capacity can be a constraint towards the maintenance of existing infrastructure. Moreover, heavy donor presence in investment spending makes the sector especially vulnerable to volatility. On average, internal resource to this sector have been around 20 percent, though this proportion increased to over 30 percent in 2014 and 2015. Since 2016 however the proportion of internal resources to the sector have dropped significantly to 12 percent in 2016 and further to an expected 7 percent in 2017. Several projects in the sectors have been stalled due to lack of funding from the government, contributing to a low execution rate in 2017[87]. Donor resources to the two basket funds in the sector have also significantly declined from their peak in 2011. Inconsistent reporting of these donor-funded projects and delays drag down the overall execution rate of the sector, which averaged 75 percent between 2009 and 2017. Given the large dependence on donor funding for this sector, in a context of declining donor support, there are serious concerns over the sustainability of the sector's financing. Finally, given the nature of spending in the sector, expenditures remain fairly centralised.

Outcomes: Mozambique has made significant progress in increasing access to water from improved sources, from 41 percent in 2000 to 51 percent in 2015[88]. However, this remains below the average of LIC at 66 percent and 68 percent in SSA[89]. In 2011, as much as 39 percent of the population had to walk over 30 minutes to collect water, while this proportion is expected to have declined, it still remains high. Moreover, the country is only halfway to achieving the 2030 target of universal access.

Progress in improved sanitation facilities are much more modest with the proportion of the population with access to improved facilities increasing from a 14 percent in 2000 to 21 percent in 2015. This is low compared to LIC and SSA at 28 percent and 30 percent respectively. About 39 percent of the population still practice open defecation, one of the highest ratios in the world. Significant improvements are needed in this area in order to attain the 2030 SDG target of universal coverage. Studies have shown that Mozambique loses about US$ 130 million a year or 1.2% of GDP due to lack of proper sanitation and hygiene facilities[90]. Lack of facilities can incur direct costs in terms of time lost to access facilities, and contraction and subsequent treatment of diseases, as well as indirect costs in terms of loss of productivity and employment. Higher investments in improved facilities in that area can thus bring huge returns.

Inequalities in access between the provinces mask the progress in both areas. Clearly, benefits on improved sources has not benefitted those most in need. Access to these basic services is much higher in the urban than the rural areas. Moreover, spending has benefitted the relative less poor in the upper quintiles than the lower ones. When comparing spending across provinces, central and northern provinces of Zambézia, Nampula, Niassa, Cabo Delgado and Tete have the lowest access to improved facilities.

3.2 Implications for Fiscal Space

From the above analysis, important inferences can be drawn in order to gauge fiscal space going forward. These are explained briefly below.

Limited space to substantially increase funding for priority sectors.

While domestic revenues grew rapidly in the past decade, there is little indication that this growth can be sustained going forward. Debt servicing costs which reached 21 percent of total expenditures in 2016 and are forecast to reach around 30 percent in the medium term, will squeeze the fiscal space for increasing allocations to social spending. With the ongoing economic crisis, there may be limited scope to substantially increase revenues unless steps are taken to improve revenue administration. Donor support through GBS has been halted since 2016 and financing through different sector basket funds has also experienced significant declines. Resumption of support hinges on accountability over the hidden debts. While project support has increased in the meantime, a significant share is channeled outside the government system. In the absence of proper recording and coordination of these interventions, substantial information gaps can lead to fragmented decision-making and ultimately affect performance in the sector as is shown in the case of health. Moreover, volatility of these funds given delays in donor disbursements can severely affect effective planning. As business confidence runs low and resumption of IMF program is not yet in sight, it also does not seem very likely that the non-megaproject economy will see an injection of investments, which may free some resources for social spending. A continued deadlock in IMF/donor-government negotiations could lead to a perpetuation of the downward spiral in growth.

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86. UNICEF (2018)
87. While the exact number of projects stalled at the national level is not known, according to AIAS, as many as 8 of their projects have been stalled.
88. UNICEF (2014).
89. UNICEF (2018).
90. FMO (2016), Nweti (2017), WSP (2011) among others.
91. For instance, according to World Bank (2016a), while there may be increased focus on spending on vertical disease funds by donors, horizontal funding to strengthen health systems remains low.

Strategic allocation and increased efficiency

While spending on priority sectors has increased, resources are not allocated to areas most in need. For instance, the foregoing analysis showed that the increase in resources for priority sectors has gone more towards recurrent spending and the proportion of current spending to investments has declined. Investment spending will be important to support the necessary infrastructure to provide services but also to create the demand for services by increasing absorption. At the same time, considerations of absorptive capacity and accompanying investment in creating a skilled force of service providers will also be essential. For instance, while the overall number of visits to a health facility in Zambézia may be low, this is more an outcome of the fewer health facilities in the province than an outcome of lower demand. An increase in the number of facilities and presence of skilled health workers will lead to a higher number of visits. The formula introduced to increase investment spending in lagging provinces to harmonise outcomes is not being adequately used.

Sectoral expenditure analysis (based on PERs etc.) suggests that there is substantial room for efficiency gains in the education sector as can be seen from the fact that unit costs in the sector are considerably higher for the predicted results compared to other countries. The same can be said about health where countries like Ethiopia have a lower per capita health expenditure while achieving better results in terms of infant mortality rate, and countries like Niger have a rate comparable with Mozambique but with much lower per capita expenditure. This suggests that improving outcomes in these sectors may have more to do with increasing efficiency than increasing resources, though the health sector does need more resources in other areas[91]. Thus, an increase in efficiency would mean better outcomes even with limited resources. On the other hand, sectors like WASH and social protection need more resources overall in order to achieve the set targets.

FIGURE 3.23 Efficiency of spending in Mozambique remains low

Source: World Bank (2017a), pg 12
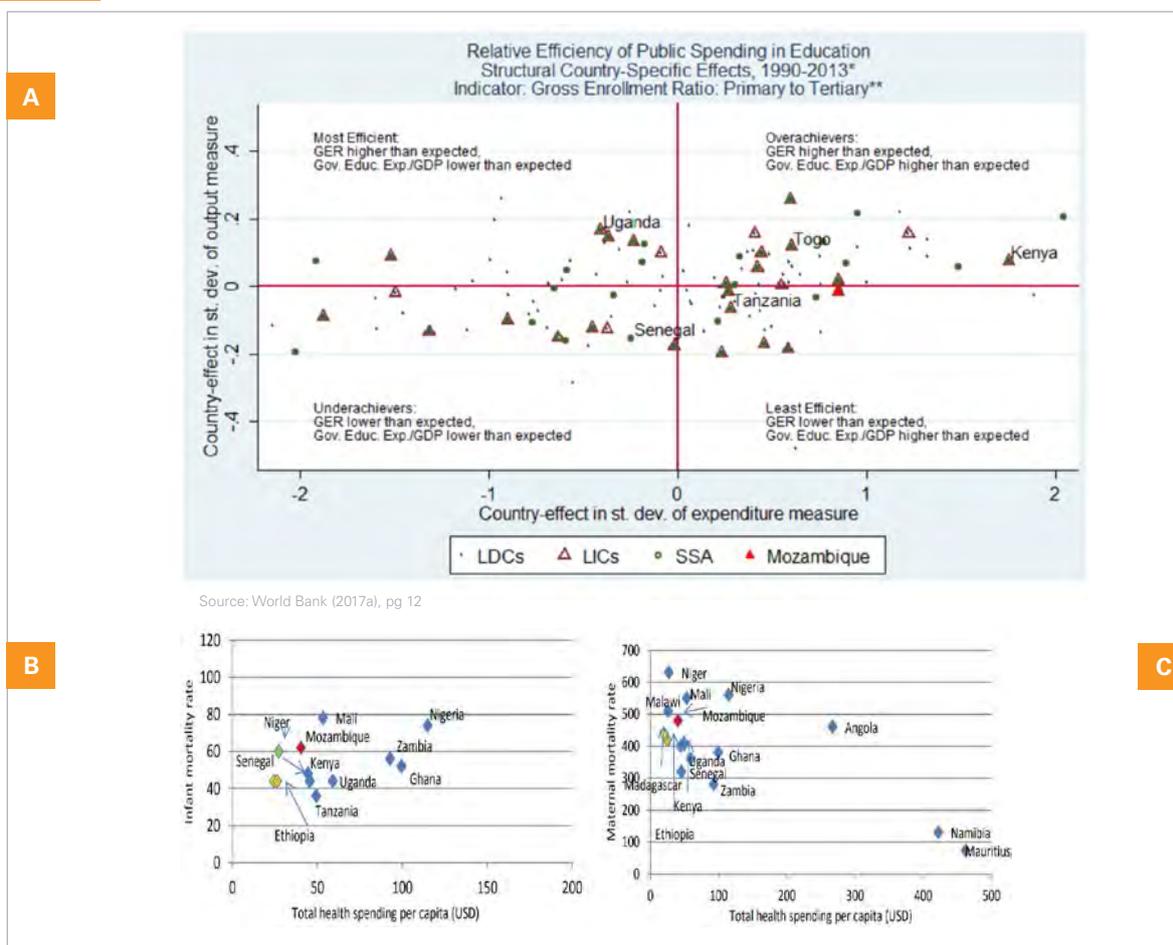
Source: World Bank (2016a) pg 28

It will be also important to ensure equity among provinces so that spending is directed to provinces where it is most needed to increase efficiency. For instance, expenditure data for all sectors show disparities in per capita expenditures in the different provinces with especially low per capita spending in the provinces in the

Centre and North especially Zambézia, Tete, Nampula and Cabo Delgado. On the other hand, most spending has been concentrated in the South especially Maputo[92]. Consequently, outcomes in these regions are also divergent.

91. For instance, according to World Bank (2016a), while there may be increased focus on spending on vertical disease funds by donors, horizontal funding to strengthen health systems remains low.
92. UNICEF (2018).

4. The base scenario

This chapter will highlight some of the long-term trends and recent developments. Long term trends include economic growth, structure of the economy along with demographic trends and social development indicators like poverty. Recent developments refer to economic growth in the recent past, followed by developments in other macroeconomic indicators like external account, Overseas Development Assistance and Foreign Direct Investment, and fiscal performance.

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 2017-2024. The goal of this scenario is to illustrate how much fiscal space will be available for the Mozambican government in the coming years if the economy evolves in ways that extend recent trends.

This scenario centres on several key assumptions, including the growth rates of GDP, the exchange rate, and population. Assumptions regarding many other economic variables depend on these key assumptions[93]. Table 30 in Appendix 1 lists the base-scenario assumptions and provides brief explanations for them. Key base-scenario assumptions include the following:

| TABLE 1 | Key assumptions in the base scenario |

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.6	3.0	3.3	3.6	4.0	4.3	4.7	5.0
Consumer price index (% growth)	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8

Table 31 in Appendix 1 lists the numerical values of the base-scenario assumptions.
These assumptions reflect the following view of Mozambique's future economic performance. The growth rate of real GDP is set to increase gradually from 2.6% in 2017 to 5% by 2024. Consumer-price inflation is assumed to decline gradually from 21.2% to 5.5% over the projection period. The population growth rate is assumed to decline modestly from 2.9 to 2.8 per cent.

4.2 Base-scenario projection results

Table 2 shows some of the key projection results for the years 2017-2024, based on the base scenario assumptions:

| TABLE 2 | Key Projection results for the base scenario |

	2017	2018	2019	2020	2021	2022	2023	2024
Priority expenditure								
Per cent of total expenditure	37.3	37.9	38.2	38.6	39.2	40.1	40.9	41.7
Per cent of GDP	11.3	11.4	11.3	11.2	11.1	11.0	10.9	10.8
Per child in US$ at 2016 exchange rate and prices	132.4	134.3	134.5	135.1	136.2	137.8	139.9	142.4
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	9.7	9.2	7.1	5.0	2.4	0.2	-2.2	-5.0
Per cent of GDP	2.9	2.8	2.1	1.5	0.7	0.0	-0.6	-1.3
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.7	-4.7	-4.0	-3.4	-2.7	-2.2	-1.7	-1.1

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93. 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.

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 increasing in terms of per child expenditure but will decline as a percentage of GDP. As the growth rate would remain high, the fiscal deficit would grow because expenditure would rise faster than revenues. The net internal financing flow (the resources needed to finance priority expenditure) would increase accordingly, both as a percentage of total expenditure and as a percentage of GDP.

The base scenario thus suggests that Mozambique can realize an increase in priority expenditure (from US$132.4 per child to US$142.4 per child), creating an average fiscal gap of 1% of GDP, while the debt-to-GDP ratio would be 103.1 per cent in 2024. In essence, this means that the Government of Mozambique could sustain its current levels of expenditure (at the expense of higher debt) in priority sectors if the economy were to achieve its expected performance and if no special measures were taken to create additional fiscal space.

TABLE 3	Results for the other elements of the fiscal account

Results	Base Scenario
Average tax and non-tax revenue/GDP, 2017-2024	19.2
Average priority expenditure/GDP, 2017-2024	11.2
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2017-2024	136.6
Net internal debt flow/GDP, 2017-2024	1.0
Total government debt/GDP, 2024	103.1

Table 32 in Appendix 1 shows the full projection results, based on the base-scenario assumptions.

Base-scenario and fiscal-space "mapping"

The "mapping" of the government's funding sources to its expenditure programs, and its priority expenditure, can be characterized straightforwardly by the government's overall funding flows.

As explained in chapter 1, the funding flows (i.e. how the Government funds its expenditure) broadly comprise the following:
1. tax and non-tax revenue;
2. external grants; and
3. the net (external and internal) financing of the fiscal deficit.

Over any time interval, total funding flows are equal to the total expenditure flows, which comprise the three broad categories of:
1. priority expenditure (as defined in chapter 1);
2. non-priority expenditure (expenditure on all other sectors, excluding interest);
3. interest expenditure.

With only a few exceptions, no category of expenditure can be said to be directly linked with any specific funding source, and no funding source can be said to be linked with any specific expenditure. The exceptions are that certain grants and loan disbursements are provided to fund specific project expenditures, and these would be in specific sectors. Apart from these exceptions, all expenditures can be funded by all types of funding flows (e.g. expenditure in the priority sectors can be financed by taxation, but also by external grants or loans).

FIGURE 4.1   Mozambique, Fiscal mapping chart

Figure 4.1 is a fiscal-mapping chart, with 2017-24 projections according to the base scenario. The projections are shown as percentages of GDP. In the "stacked-bar" presentation, funding sources are above and expenditure flows below the horizontal axis. The sum of everything shown above the horizontal axis effectively funds everything shown below. By definition, the sum of the net external and internal financing flows is the same as the overall fiscal deficit.

For the base scenario, the expenditure flows would imply a negative net internal government debt flow. Under the base scenario, the government deficit would decrease from 4.7 per cent per cent of GDP in 2017 to 1 per cent per cent in 2024, while the net internal debt flow would decrease from 2.9 per cent of GDP in 2017 to -1.3 per cent in 2024.

5. Alternative scenarios

5.1 Options to increase the 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 – e.g. increased tax revenue will be set aside to be spent on a priority sector such as education, instead of a non-priority sector, such as defence;
2. increasing external financing, i.e. attracting more development aid;
3. reducing spending in priority sectors, possibly by increasing expenditure efficiency;
4. reducing non-priority expenditure;
5. reducing external debt service, presumably through agreements with creditors;
6. increasing external debt disbursements; and
7. increasing net internal borrowing flows.

Apart from government policy choices, changes in the macroeconomic context can affect fiscal space. For example, higher GDP growth would lead to an increase in fiscal space by generating higher tax revenue.

From the analysis in chapter 2, Mozambique's options to increase fiscal space within the next seven years are constrained. Mozambique must maintain a prudent fiscal policy, as the country is in the middle of a debt crisis and thus needs to maintain its external debt under control.

Although options to increase fiscal space are not as evident as for other countries, Mozambique may find some room to manoeuvre. The scenarios we present are mainly broken down between an upside case and a downside case, which allows us to illustrate how different degrees of positive and negative economic conditions would affect fiscal space in Mozambique.

We present three upside scenarios to illustrate how additional fiscal space could be created:

- **Alternative scenario 1** assumes that the government takes steps to resolve the deadlock with the IMF, so that the program is resumed, and is thus able to attract investments in the non-resource sector as confidence is restored, thereby increasing real GDP growth;
- **Alternative scenario 2** considers how a potential increase in donor support could finance priority expenditure;
- **Alternative scenario 3** if scenario 1 happens, most likely scenario 2 will also happen. Scenario 3 combines scenarios 1 and 2, producing a best case scenario with higher GDP growth, as well as higher donor support in priority areas.

We present three downside scenarios to illustrate how fiscal space would decrease under negative economic conditions:

- **Alternative scenario 4** assuming that gas investments are further delayed leading to lower GDP growth than assumed in the base scenario.
- **Alternative scenario 5** mirrors scenario 2, assuming a decline in donor support in priority areas
- **Alternative scenario 6** combines scenarios 4 and 5 producing a worst case scenario where Mozambique fails to achieve higher economic growth and also faces a decline in donor support.

Other potential alternatives are also considered to show the effect of different economic and political conditions.
Alternative scenario 7 presents a combination of higher economic growth and lower donor support to priority areas;
Alternative scenario 8 calculates the result of increased effectiveness of tax collection.

We present three downside scenarios to illustrate how fiscal space would decrease under negative economic conditions:
- **Alternative scenario 4** assuming that gas investments are further delayed leading to lower GDP growth than assumed in the base scenario.
- **Alternative scenario 5** mirrors scenario 2, assuming a decline in donor support in priority areas
- **Alternative scenario 6** combines scenarios 4 and 5 producing a worst case scenario where Mozambique fails to achieve higher economic growth and also faces a decline in donor support.

5.2 Alternative scenarios and projections compared with the base scenario

5.2.1 Alternative scenario 1: higher GDP growth

One of the key challenges for Mozambique is creating and sustaining high GDP growth. If the government succeeds in resolving the deadlock with the IMF, and creates a more attractive investment climate in the non-megaproject sector, achieving a higher GDP growth than assumed in the base scenario would be possible. The resumption of the IMF program will help restore some confidence in the economy thereby attracting more investors.

Scenario 1 uses the same assumptions as the baseline scenario with the only difference that the real growth rate is now moderately higher (gradually increasing from 2.8 per cent in 2017 to 6 per cent in 2024) than the growth assumed in the base scenario. This alternative assumption is highlighted in Table 4

TABLE 4   Key assumptions in scenario 1

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.8	3.2	3.7	4.1	4.6	5.1	5.5	6.0
Consumer price index (% growth)	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8

Table 5 shows the projection results using the assumption of a higher GDP growth than in the base scenario. Higher real GDP growth will result in higher government revenues and higher expenditure. As a result, per child expenditure in priority sectors would be positively affected and increase by 11 per cent over the projection period.

TABLE 5   Key projection results in scenario 1

	2017	2018	2019	2020	2021	2022	2023	2024
Priority expenditure								
Per cent of total expenditure	37.3	37.9	38.2	38.7	39.4	40.3	41.1	42.1
Per cent of GDP	11.3	11.4	11.3	11.2	11.1	11.0	10.8	10.7
Per child in US$ at 2016 exchange rate and prices	132.5	134.7	135.2	136.2	138.0	140.4	143.4	147.1
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	9.6	9.1	6.8	4.5	1.6	-1.0	-3.8	-7.1
Per cent of GDP	2.9	2.7	2.0	1.3	0.5	-0.3	-1.0	-1.8
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.7	-4.6	-3.9	-3.2	-2.5	-1.9	-1.4	-0.7

Table 6 compares the projection results of this scenario with those of the base scenario. Average priority spending per child would increase to US$147.7 from US$132.5. The average net internal debt flow would be 0.8 per cent of GDP (compared with 1 per cent of GDP in the base scenario). The total (external and internal) government debt stock would amount in 2024 to 98 per cent of GDP (compared with 103.1 per cent in the base scenario).

TABLE 6   Results from scenario 1

Results	Base Scenario	Scenario 1	Variation
Average tax and non-tax revenue/GDP, 2017-2024	19.2	19.2	0.0[94]
Average priority expenditure/GDP, 2017-2024	11.2	11.1	-0.1
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2017-2024	136.6	138.4	1.8
Net internal debt flow/GDP, 2017-2024	1.0	0.8	-0.2
Total government debt/GDP, 2024	103.1	98.0	-5.0

94. The difference is very small at -0.01.

5.2.2 Alternative scenario 2: higher donor support in priority areas

The prospects for increased donor grants in priority sectors appear relatively limited in Mozambique. Nevertheless, if the government were to successfully resolve the deadlock with the IMF which mostly depends on further transparency and accountability over the hidden debts, there might be scope for raising more funding through external grants. However, given the current state of donor-government dialogue and trends in donor grants in the previous years, it is unlikely that donor grants will see a steep rise.

Scenario 2 considers an increase of external grants to fund priority expenditure. In this particular scenario, an increase in priority expenditure resulting from grants aimed at increasing capital expenditure in each priority sector by 20 per cent over the projected period is assumed. This would effectively increase the size of external grants as a percentage of GDP modelled for the base scenario, allowing the government to slowly increase capital expenditure in priority sectors from 1 per cent of GDP to 4.4 per cent of GDP over the projection period. Table 7 lists the standard and alternative assumptions used to project this scenario.

TABLE 7	Key assumptions for scenario 2

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.6	3.0	3.3	3.6	4.0	4.3	4.7	5.0
Consumer price index	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8
Alternative assumptions								
Total Priority non-recurrent expenditure	3.2	3.4	3.5	3.6	3.7	3.8	3.8	3.9
Central-government external grants for capital expenditure (projects)	1.0	1.2	1.6	2.0	2.5	3.1	3.7	4.4

Table 8 summarizes the projection results using these assumptions. Priority expenditure will grow at a faster pace than that projected in the base scenario, but the net internal financing gap and fiscal deficit will remain virtually the same as the additional funds will be provided by external sources instead of the government's own revenues.

TABLE 8	Key projection results in scenario 2

	2017	2018	2019	2020	2021	2022	2023	2024
Priority expenditure								
Per cent of total expenditure	37.2	38.0	38.5	39.2	40.0	41.0	42.0	43.1
Per cent of GDP	11.3	11.5	11.5	11.5	11.4	11.4	11.4	11.4
Per child in USD at 2015 exchange rate and prices	131.9	135.1	136.2	137.8	140.1	142.8	146.0	149.8
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	9.3	8.8	6.7	4.5	1.9	-0.4	-2.8	-5.6
Per cent of GDP	2.8	2.7	2.0	1.3	0.5	-0.1	-0.8	-1.5
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.6	-4.5	-3.9	-3.3	-2.5	-2.1	-1.6	-0.9

Table 9 shows that, with these assumptions, the average net internal debt flow would be lower than in the base scenario over the projection period (2017-2024). The total (external and internal) government debt stock would also be lower. Grants could thus fund an increase in priority expenditure without causing an increase in government debt or widening the fiscal deficit.

TABLE 9   Results from scenario 2

Results	Base Scenario	Scenario 2	Variation
Average tax and non-tax revenue/GDP, 2017-2024	19.2	19.2	=
Average priority expenditure/GDP, 2017-2024	11.2	11.4	-0.3
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2017-2024	136.6	140.0	3.4
Net internal debt flow/GDP, 2017-2024	1.0	0.9	-0.1
Total government debt/GDP, 2024	103.1	102.3	-0.8

5.2.3 Alternative scenario 3: higher GDP growth + donor support in priority areas
If the Government of Mozambique were to succeed in resolving the deadlock with the IMF and donors over the hidden debts, while also demonstrating progress in improving socio-economic indicators by attracting more investments in the non-megaproject sector, it might be able to create a best case scenario where fiscal space is maximized.

Scenario 3 considers a combination of scenarios 1 and 2, effectively illustrating a best case scenario for Mozambique.

Table 10 shows the key assumptions with regard to consumer price index (CPI) and population growth stay the same, while the assumption regarding GDP growth is the same as that of scenario 1 and those concerning external grants and capital expenditure in priority sectors are the same as those in scenario 2.

TABLE 10   Key assumptions for scenario 3

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.8	3.2	3.7	4.1	4.6	5.1	5.5	6.0
Consumer price index	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8
Alternative assumptions								
Total Priority non-recurrent expenditure	3.2	3.4	3.5	3.6	3.7	3.8	3.8	3.9
Central-government external grants for capital expenditure (projects)	1.0	1.2	1.6	2.0	2.6	3.2	3.9	4.6

Table 11 shows the projection results when using the alternative assumptions on tax collection efficiency. The projection results show that increased tax collection efficiency would lead to a decrease of the fiscal deficit over the projection period from 4.6 percent of GDP to 0.6 percent by 2024. There are several measures to improve the overall efficiency of tax collection in Mozambique. These include not just simplifying and modernising the VAT collection system, and stronger oversight on the border flows to curb the leakage in excise, but also introducing simpler measures like tax credit instead of income deductions to enhance revenue generation through tax collection. Removal of tax exemptions for megaprojects is another significant avenue to increase tax revenues as is the expansion of the tax net in the country.

TABLE 11	Key projection results for scenario 3							
	2017	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Priority expenditure								
Per cent of total expenditure	37.4	38.2	38.8	39.4	40.2	41.3	42.4	43.5
Per cent of GDP	11.4	11.6	11.6	11.5	11.5	11.4	11.4	11.4
Per child in USD at 2015 exchange rate and prices	133.1	136.6	138.1	140.2	143.1	146.7	151.0	156.1
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	9.5	9.0	6.7	4.4	1.5	-1.0	-3.8	-7.0
Per cent of GDP	2.9	2.7	2.0	1.3	0.4	-0.3	-1.0	-1.8
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.6	-4.6	-3.9	-3.2	-2.5	-1.9	-1.3	-0.6

Table 12 compares the results from alternative scenario 3 with the results from the base scenario. With the assumptions of scenario 3, the average priority expenditure per child would increase by an average of US$ 6.5 over the projection period, compared to the base scenario. The net internal debt flow would be 0.8 per cent of GDP (compared with 1 per cent of GDP in the base scenario). The total (external and internal) government debt stock would amount in 2024 to 98 per cent of GDP (compared with 103.1 per cent in the base scenario), meaning that overall the government finances would be in better shape as the increased revenues allow the government to pay back its debt.

TABLE 12	Results from scenario 3 compared to the base scenario			
Results		**Base Scenario**	**Scenario 3**	**Variation**
Average tax and non-tax revenue/GDP, 2017-2024		19.2	19.2	0.0[95]
Average priority expenditure/GDP, 2017-2024		11.2	11.5	0.3
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2017-2024		136.6	143.1	6.5
Net internal debt flow/GDP, 2017-2024		1.0	0.8	-0.2
Total government debt/GDP, 2024		103.1	98.0	-5.1

5.2.4 Alternative Scenario 4: lower GDP growth

Mozambique could also be facing more challenging economic situations, including the further delay of gas investments or external shocks, such as commodity price volatility, which would negatively affect its economic growth. This scenario therefore considers a GDP growth lower than that of the base scenario. A significant risk to current gas investment plans could be seen in terms of numerous attacks by so-called terrorist elements in the North of the country. These attacks can create significant instability in the region with a potential risk of delaying multi-billion dollar gas investments.

Scenario 4 uses the same assumptions as the baseline scenario with the only difference that the real growth rate gradually increases from 2.5 per cent in 2017 to 4.0 per cent in 2024, a slower increase than in the base scenario. This alternative assumption is highlighted in Table 13.

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95. The difference is very small at -0.01.

TABLE 13	Key assumptions for scenario 4

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.5	2.7	2.9	3.1	3.4	3.6	3.8	4.0
Consumer price index (%)	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth (%)	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8

Table 14 shows the projection results for this scenario. Unlike the previous scenario, lower GDP growth would result in a smaller increase in the percentage of total expenditure spent on priority sectors from 37.3 per cent in 2017 to 41.4 per cent in 2024. Per child expenditure would increase to US$138 in 2024, instead of US$142.4 in the base scenario.

TABLE 14	Key projection results for scenario 4

	2017	2018	2019	2020	2021	2022	2023	2024
Priority expenditure								
Per cent of total expenditure	37.3	37.8	38.2	38.6	39.1	39.9	40.6	41.4
Per cent of GDP	11.3	11.4	11.4	11.3	11.2	11.1	11.0	10.9
Per child in USD at 2015 exchange rate and prices	132.3	134.0	133.8	133.9	134.4	135.3	136.5	138.0
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	9.7	9.4	7.4	5.5	3.2	-1.3	-0.6	-2.9
Per cent of GDP	3.0	2.8	2.2	1.6	0.9	-0.4	-0.2	-0.8
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.7	-4.7	-4.1	-3.5	-2.9	-2.5	-2.1	-1.6

Table 15 compares the projection results with those of the base scenario. The average internal debt flow would be 1.2 per cent of GDP (compared with 1 per cent of GDP in the base scenario). The total (external and internal) government debt stock would amount in 2024 to 108.4 per cent of GDP (compared with 103.1 per cent in base scenario). This scenario also highlights the fragility of the Mozambican economy as a slower gradual increase of the rate of GDP growth already leads to a 5.3 per cent increase in government debt compared to the base scenario.

TABLE 15	Results from scenario 4

Results	Base Scenario	Scenario 4	Variation
Average tax and non-tax revenue/GDP, 2017-2024	19.2	19.2	0.0[96]
Average priority expenditure/GDP, 2017-2024	11.2	11.2	0.1
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2017-2024	136.6	134.8	-1.8
Net internal debt flow/GDP, 2017-2024	1.0	1.2	-0.2
Total government debt/GDP, 2024	103.1	108.4	-5.3

96. The difference is very small at 0.01

5.2.5 Alternative scenario 5: lower donor support in priority areas

As highlighted in scenario 2, the prospects for increased donor grants in priority sectors appear relatively limited. While donor support had already declined over past years, the debt crisis has accentuated this decline. In the absence of steps towards showing government commitment in terms of improved transparency and accountability of the hidden debts, donors might be under pressure to withdraw their existing support to priority sectors even further.

Scenario 5 considers a decrease of external grants to fund priority expenditure. In this particular scenario, a decrease in priority capital expenditure of 20% over the projected period is assumed. This would effectively decrease the size of external grants as a percentage of GDP modelled for the base scenario, effectively cutting central government capital expenditure in priority sectors from 0.8 per cent of GDP to 0.5 per cent of GDP over the projection period. Table 16 lists the standard and alternative assumptions used to project this scenario.

TABLE 16   Key assumptions in scenario 5

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.6	3.0	3.3	3.6	4.0	4.3	4.7	5.0
Consumer price index	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8
Alternative assumptions								
Total Priority non-recurrent expenditure	3.1	3.1	3.0	2.9	2.9	2.8	2.7	2.6
Central-government external grants for capital expenditure (projects)	0.8	0.8	0.8	0.9	0.8	0.8	0.7	0.5

Table 17 summarizes the projection results, using these assumptions. Priority expenditure will grow at a slower pace than that projected in the base scenario, resulting in overall lower per-child expenditure over the projection period. Net internal financing gap and total government debt would remain relatively stable as only externally-financed expenditure would decrease.

TABLE 17   Key projection results in scenario 5

	2017	2018	2019	2020	2021	2022	2023	2024
Priority expenditure								
Per cent of total expenditure	37.2	37.5	37.7	37.9	38.3	39.0	39.6	40.2
Per cent of GDP	11.3	11.3	11.1	10.9	10.7	10.5	10.4	10.2
Per child in USD at 2015 exchange rate and prices	131.8	132.4	131.6	131.1	131.2	131.7	132.6	133.8
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	9.8	9.4	7.3	5.2	2.6	0.4	-2.0	-4.7
Per cent of GDP	3.0	2.8	2.1	1.5	0.7	-0.1	-0.5	-1.2
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.7	-4.7	-4.0	-3.4	-2.7	-2.3	-1.8	-1.2

Table 18 shows that, with these assumptions, the average net internal debt flow would be slightly lower than in the base scenario over the projection period (2017-2024). The total (external and internal) government debt stock would be higher, and per-child expenditure would be on average US$ 4.6 lower. A reduction of grants could thus lead to a significant reduction in priority expenditure.

TABLE 18   Results from scenario 5

Results	Base Scenario	Scenario 5	Variation
Average tax and non-tax revenue/GDP, 2017-2024	19.2	19.2	=
Average priority expenditure/GDP, 2017-2024	11.2	10.8	-0.4
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2017-2024	136.6	132.0	-4.6
Net internal debt flow/GDP, 2017-2024	1.0	1.1	0.1
Total government debt/GDP, 2024	103.1	103.4	0.3

5.2.6 Alternative scenario 6: lower GDP growth + lower donor support in priority areas

Opposite of the situation considered in scenario 3, a worst case scenario can result from delays in gas investments and the failure of the Mozambican government to resolve the deadlock with the IMF and donors, leading simultaneously to lower GDP growth and the withdrawal of external support in priority sectors.

Scenario 6 considers a combination of scenarios 4 and 5, illustrating a potential worst case scenario for Mozambique.

Table 19 shows that the key assumptions with regard to consumer price index (CPI) and population growth stay the same as in the base scenario, while the assumption regarding GDP growth is the same as that of scenario 4 and those concerning external grants and capital expenditure in priority sectors are the same as those in scenario 5.

TABLE 19   Key assumptions for scenario 6

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.5	2.7	2.9	3.1	3.4	3.6	3.8	4.0
Consumer price index	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8
Alternative assumptions								
Total Priority non-recurrent expenditure	3.1	3.1	3.0	2.9	2.9	2.8	2.7	2.6
Central-government external grants for capital expenditure (projects)	0.8	0.8	0.8	0.8	0.8	0.8	0.6	0.5

Table 20 shows the projection results when using these alternative assumptions. The projection results show that lower GDP growth combined with lower donor support would lead to the largest decrease in per child expenditures relative to the base scenario (US$ 129.7 by 2024 compared to US$ 142.4 in the base scenario).

TABLE 20 Key projection results for scenario 6

	2017	2018	2019	2020	2021	2022	2023	2024
Priority expenditure								
Per cent of total expenditure	37.2	37.5	37.6	37.9	38.2	38.8	39.3	39.9
Per cent of GDP	11.3	11.3	11.1	10.9	10.8	10.6	10.4	10.3
Per child in USD at 2015 exchange rate and prices	131.7	132.1	130.9	130.0	129.5	129.3	129.4	129.7
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	9.9	9.5	7.6	5.8	3.5	1.6	-0.4	-2.6
Per cent of GDP	3.0	2.9	2.2	1.7	1.0	0.4	-0.1	-0.7
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.7	-4.7	-4.1	-3.6	-2.9	-2.6	-2.2	-1.7

Table 21 compares the results from alternative scenario 6 with the results from the base scenario. With the assumptions of scenario 6, the average tax and non-tax revenue collection would be virtually the same as in the base scenario. The net internal debt flow would be 1.3 per cent of GDP (compared with 1 per cent of GDP in the base scenario). The total (external and internal) government debt stock would amount in 2024 to 108.7 per cent of GDP (compared with 103.1 per cent in the base scenario), meaning that overall the government finances would be in worse shape as debt-to-GDP would remain at dangerous levels.

TABLE 21 Results from scenario 6 compared to the base scenario

Results	Base Scenario	Scenario 6	Variation
Average tax and non-tax revenue/GDP, 2017-2024	19.2	19.2	0.0[97]
Average priority expenditure/GDP, 2017-2024	11.2	10.8	-0.3
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2017-2024	136.6	130.3	-6.3
Net internal debt flow/GDP, 2017-2024	1.0	1.3	0.3
Total government debt/GDP, 2024	103.1	108.7	5.7

5.2.7 Alternative scenario 7: higher GDP growth + lower donor support in priority areas

It is also possible that the Mozambican government will succeed in attracting additional investment to the non-resource sector, but donor support might nonetheless continue its downward trend.

Scenario 7 considers a combination of scenarios 1 and 5 in order to illustrate a "middle ground" scenario for Mozambique.

Table 22 shows that the key assumptions with regard to consumer price index (CPI) and population growth stay the same as in the base scenario, while the assumption regarding GDP growth is the same as that of scenario 1, while those concerning external grants and capital expenditure in priority sectors are the same as those in scenario 5.

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97. The difference is very small at 0.01.

TABLE 22	Key assumptions for scenario 7							

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.8	3.2	3.7	4.1	4.6	5.1	5.5	6.0
Consumer price index (% growth)	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8
Alternative assumptions								
Total Priority non-recurrent expenditure	3.1	3.1	3.0	2.9	2.9	2.8	2.7	2.6
Central-government external grants for capital expenditure (projects)	0.8	0.8	0.8	0.9	0.8	0.8	0.7	0.5

Table 23 shows the projection results when using the alternative assumptions on tax collection efficiency. The projection results show that, in the absence of donor support, per-child expenditure would decline relative to the base scenario, despite higher levels of GDP growth. Moreover, priority expenditure would be lower than in the base scenario, both as a percentage of GDP and as a percentage of total expenditure.

TABLE 23	Key projection results for scenario 7							

	2017	2018	2019	2020	2021	2022	2023	2024
Priority expenditure								
Per cent of total expenditure	37.2	37.5	37.7	38.0	38.4	39.1	39.8	40.5
Per cent of GDP	11.3	11.3	11.1	10.9	10.7	10.5	10.3	10.0
Per child in USD at 2015 exchange rate and prices	131.9	132.8	132.2	132.2	132.9	134.1	135.8	138.1
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	9.8	9.2	7.0	4.7	1.8	-0.7	-3.5	-6.9
Per cent of GDP	3.0	2.8	2.0	1.3	0.5	-0.2	-0.9	-1.7
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.7	-4.6	-3.9	-3.3	-2.5	-2.0	-1.4	-0.8

Table 24 compares the results from alternative scenario 7 with the results from the base scenario. With the assumptions of scenario 7, net internal debt flow would be 0.9 per cent of GDP (compared with 1 per cent of GDP in the base scenario). The total (external and internal) government debt stock would amount in 2024 to 98.4 percent of GDP (compared with 103.1 per cent in the base scenario), meaning that overall the government finances would be in better shape thanks mainly to the higher levels of growth. Nonetheless, priority expenditure would be on average US$ 2.8 lower, highlighting the importance of donor support for priority sectors in Mozambique.

TABLE 24	Results from scenario 7 compared to the base scenario		

Results	Base Scenario	Scenario 7	Variation
Average tax and non-tax revenue/GDP, 2017-2024	19.2	19.2	0.0[98]
Average priority expenditure/GDP, 2017-2024	11.2	10.7	-0.4
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2017-2024	136.6	133.7	-2.8
Net internal debt flow/GDP, 2017-2024	1.0	0.9	-0.2
Total government debt/GDP, 2024	103.1	98.4	-4.7

98. The difference is very small at -0.01.

5.2.8 Alternative scenario 8: improved VAT administration

Another possible option through which the government of Mozambique could create more fiscal space would be the improvement in revenue collection. Several measures can be taken to increase overall revenue. These mainly include increasing the efficiency of the current tax system rather than increasing tax rates. Some steps are being taken in an effort to enhance domestic resource mobilisation. For instance, recently, the government announced the abolition of the old system of customs collection (TIMS), a step long awaited since the single electronic window to collect customs duties was rolled out in 2012[99]. This is an important step in preventing a leak in revenue collections. Similarly, the Prime Minister recently announced the rolling out of the e-taxation platform that simplifies procedures for paying taxes through the banking system rather than having to queue at regional tax authority offices[100].This system can also increase transparency and help reduce corrupt practices involved in direct cash payments to the tax officials. However, there have been significant delays in the implementation of the system.

An IMF mission in 2016 conducted an extensive review of the current tax system to identify entry points for further revenue generation[101]. Revenue generation through VAT can increased by simplifying and modernising the regime and broadening its base. However, such discussions cannot happen without due consideration to the clearing of VAT repayments. Recently, the revenue authority announced that all donor funded-projects will be exempt from paying VAT, which could result in large potential losses of VAT collections[102]. Excise is another area where revenues can be boosted. Stronger control of the borders, especially with South Africa can significantly improve revenues from this source[103]. With regards to taxes on incomes, tax credit rather than income deduction can not only improve the progressivity in the average

tax rate but also bring more revenues. The introduction of a wealth tax can also bring more revenues however this may be politically difficult to achieve[104]. Finally, revenues can also be increased by the removal of benefits on megaprojects. As exemptions on certain coal mining concessions are coming to an end, these contracts can be renegotiated, and exemptions removed[105]. While there may be pressures not to renegotiate these contracts given the political economy considerations explained in the PEA, benefits through accelerated depreciation can incentivise further investments and increase production[106].

Scenario 8 considers an improvement in tax collection effectiveness. Table 25 shows that the key assumptions with regard to GDP, consumer price index (CPI) and population growth stay the same. Two assumptions related to tax collection efficiency have been altered as compared to the base scenario ("alternative assumptions").

The assumptions altered concern two main types of taxes: domestic VAT and import VAT. These are two fundamental types of taxes as they represent roughly 30 per cent of the government's total fiscal revenues. Without increasing the tax rate (the average tax rate of both taxes is 20 per cent and 17 percent respectively), the government could increase the efficiency of collection, thus leading to an increase in revenue and therefore creating additional fiscal space. In practical terms, this could be achieved through a decrease in exemptions, which could reduce the losses in revenue.

In this scenario, an assumption is made that domestic VAT collection efficiency increases gradually from 30.1 per cent in 2017 to 37.7 per cent in 2024, while import VAT collection efficiency increases gradually from 60.4 per cent in 2017 to 75.8 per cent in 2024.

TABLE 25   Key assumptions for scenario 8

Growth rates	2017	2018	2019	2020	2021	2022	2023	2024
Real GDP	2.6	3.0	3.3	3.6	4.0	4.3	4.7	5.0
Consumer price index	21.2	18.9	16.5	14.2	12.0	9.8	7.6	5.5
Population growth	2.9	2.9	2.9	2.9	2.8	2.8	2.8	2.8
Alternative assumptions								
Domestic VAT collection effiency (%)	30.1	31.2	32.2	33.3	34.4	35.5	36.6	37.7
Import VAT collection efficiency	60.4	62.5	64.6	66.8	69.0	71.2	73.5	75.8

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99.   About 30 percent of the total customs duties continued to be collected through the old system with allegations of corrupt practices.
100. http://www.rm.co.mz/index.php/component/k2/item/712-governo-introduz-pagamento-de-imposto-via-sistema-bancario.html
101. Swistak et al. (2017).
102. http://clubofmozambique.com/news/projects-funded-by-international-partners-are-now-exempt-from-vat-in-mozambique/
103. Swistak et al. (2017). Trade statistics between Mozambique and South Africa shows significant disparities in excisable goods, mainly under-reporting on the Mozambican side.
104. Based on interviews.
105. Based on interviews.
106. Swistak et al. (2017).

Table 26 shows the projection results when using the alternative assumptions on tax collection efficiency. The projection results show that increased tax collection efficiency would lead to Mozambique realising a fiscal surplus by 2022, reaching 2.3% by 2024, as opposed to a -1.1 percent deficit in the base scenario.

TABLE 26   Key projection results for scenario 8

	2017	2018	2019	2020	2021	2022	2023	2024
Priority expenditure								
Per cent of total expenditure	37.3	37.9	38.3	38.9	39.7	40.8	41.9	43.2
Per cent of GDP	11.3	11.4	11.3	11.2	11.1	11.0	10.9	10.8
Per child in USD at 2015 exchange rate and prices	134.4	134.3	134.5	135.1	136.2	137.8	139.9	142.4
Net internal financing gap (fiscal gap)								
Per cent of total expenditure	8.6	6.9	3.3	-0.3	-4.8	-8.9	-13.5	-18.9
Per cent of GDP	2.6	2.1	1.0	-0.1	-1.4	-2.4	-3.5	-4.7
Fiscal Deficit (surplus/deficit)								
Per cent of GDP	-4.4	-4.0	-2.9	-1.8	-0.6	0.2	1.2	2.3

Table 27 compares the results from alternative scenario 8 with the results from the base scenario. With the assumptions of scenario 8, the average tax and non-tax revenue collection would increase by an average of 1.5 per cent of GDP over the projection period, compared to the base scenario. The net internal debt flow would be -0.8 per cent of GDP (compared with 1 per cent of GDP in the base scenario) – which means Mozambique could effectively close the fiscal gap. The total (external and internal) government debt stock would amount in 2024 to 91.8 per cent of GDP (compared with 103.1 per cent in the base scenario), meaning that overall the government finances would be in better shape as the increased revenues allow the government to pay back some of its debt.

TABLE 27   Results from scenario 8 compared to the base scenario

Results	Base Scenario	Scenario 8	Variation
Average tax and non-tax revenue/GDP, 2018-2024	19.2	20.7	1.5
Average priority expenditure/GDP, 2018-2024	11.2	11.2	=
Average priority expenditure per child (USD at 2015 prices & exchange rate), 2018-2024	136.6	136.6	=
Net internal debt flow/GDP, 2018-2024	1.0	-0.8	-1.8
Total government debt/GDP, 2024	103.1	91.8	-11.3

In this particular scenario, we only model an increase in revenues without an increase in priority expenditure. However, it is possible to envision a scenario where the government uses fiscal space created through improved tax collection efficiency to increase priority (or non-priority) expenditure instead of paying back its debt.

5.2.9 Summary of Scenario Results

The impact on fiscal space of the scenario considered, are summarized in Table 28.

TABLE 28 Summary of scenario results			
	Gov. debt 2024	**Priority Spending per child (in USD, average 2017-2024)**	**Percentage Change compared to the base scenario**
Base scenario	103.1	136.6	=
Higher GDP growth	98.0	138.4	1.4%
Higher donor support in priority areas	102.3	140.0	2.5%
Higher GDP growth + higher donor support	98.0	143.1	4.8%
Lower GDP growth	108.4	134.8	-1.3%
Lower donor support in priority areas	103.4	132.0	-3.3%
Lower GDP growth and lower donor support	108.7	130.3	-4.6%
Higher GDP growth + Lower donor support	98.4	133.7	-2.1%
Improved VAT administration	91.8	136.6	=

The projection exercise has produced illustrative results that show alternative means of creating enhanced fiscal space that can be used to finance priority spending, as well as how fiscal space could decrease as a result of adverse conditions. These scenarios show the effect of different economic growth and donor support scenarios, as well as how increase in priority spending could be financed in a number of different ways. We have explored how the Government could seek to create fiscal space through:

- An increase of external grants (Scenarios 2 and 3);
- A gradual increase in the efficiency of tax administration (Scenario8).

Scenario 3 and 6 demonstrate the potential effect of the most drastically positive and negative economic conditions. Should the deadlock with the IMF be resolved and the program resumed, resulting in economic growth that is higher than anticipated and an increase in donor support, priority spending per child would increase by almost 5 per cent and at the same time lead to a decrease in debt to 98 per cent of GDP. It should be noted that this positive scenario places these parameters (i.e. economic growth and level of donor support) to levels similar to those observed before the hidden debts were discovered. Should growth be lower (and decline to 4 per cent by 2024), and should donors further withdraw their support in priority areas, this would lead to a decrease of 4.6 per cent in priority spending per child as compared to the base scenario. Debt levels would then rise to 108.7 per cent of GDP.

Figure 5.1, Figure 5.2 and Figure 5.3 once again summarize the effects of the different scenarios on Mozambique's fiscal surplus/deficit, total government debt as a percentage of GDP and child priority expenditure in constant US dollars.

FIGURE 5.1 Mozambique, Fiscal deficit/surplus as percentage of GDP
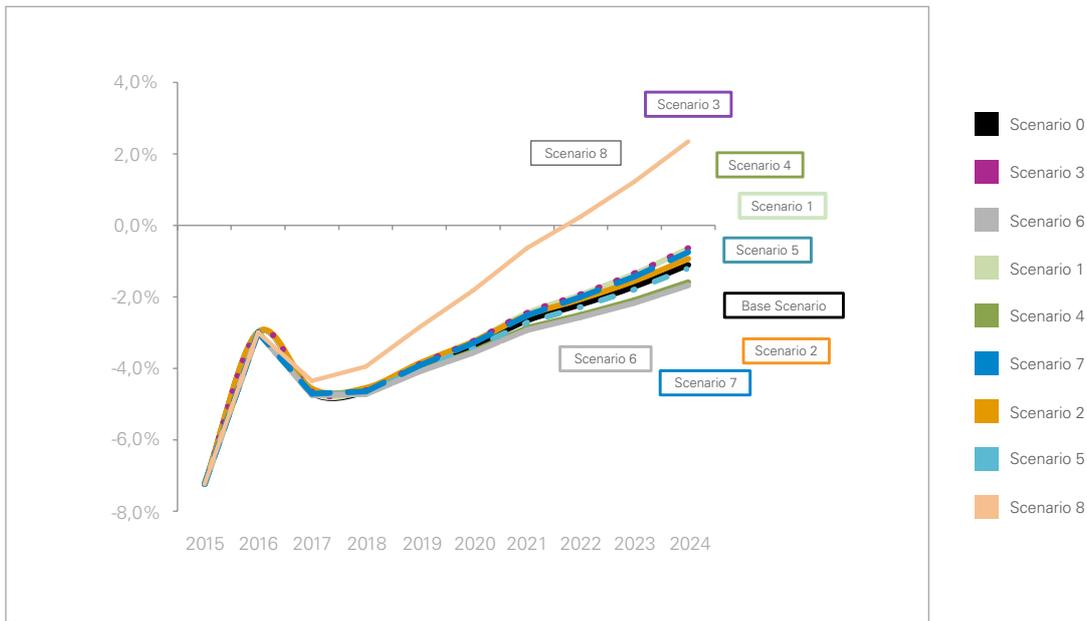
FIGURE 5.2 Mozambique, Total government debt stock as percentage of GDP
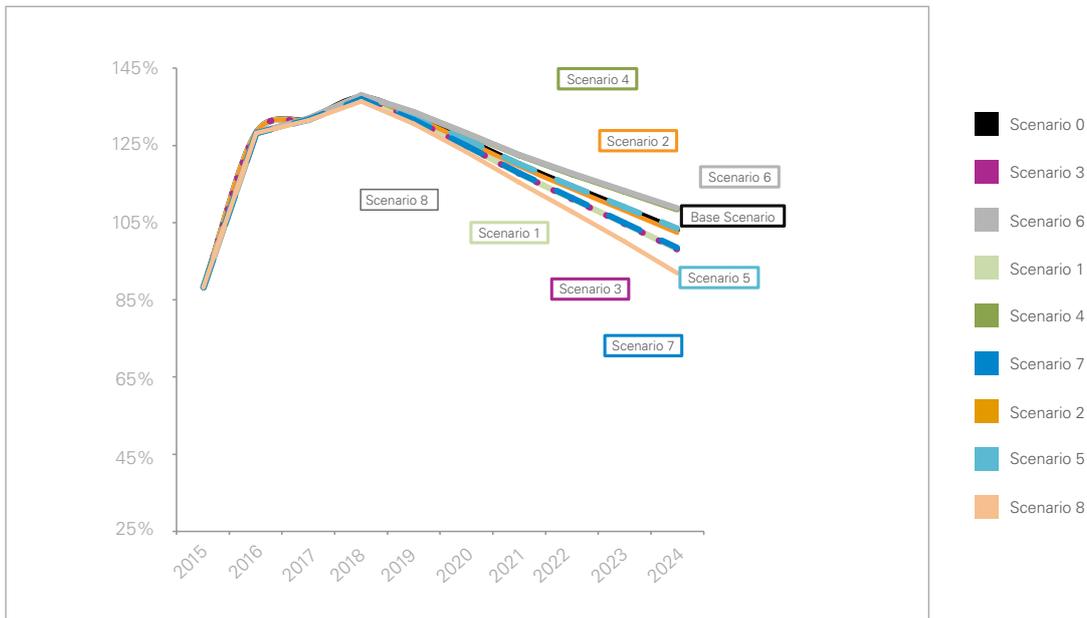
FIGURE 5.3 Mozambique, Per child priority expenditure, USD 2016 price and exchange rate
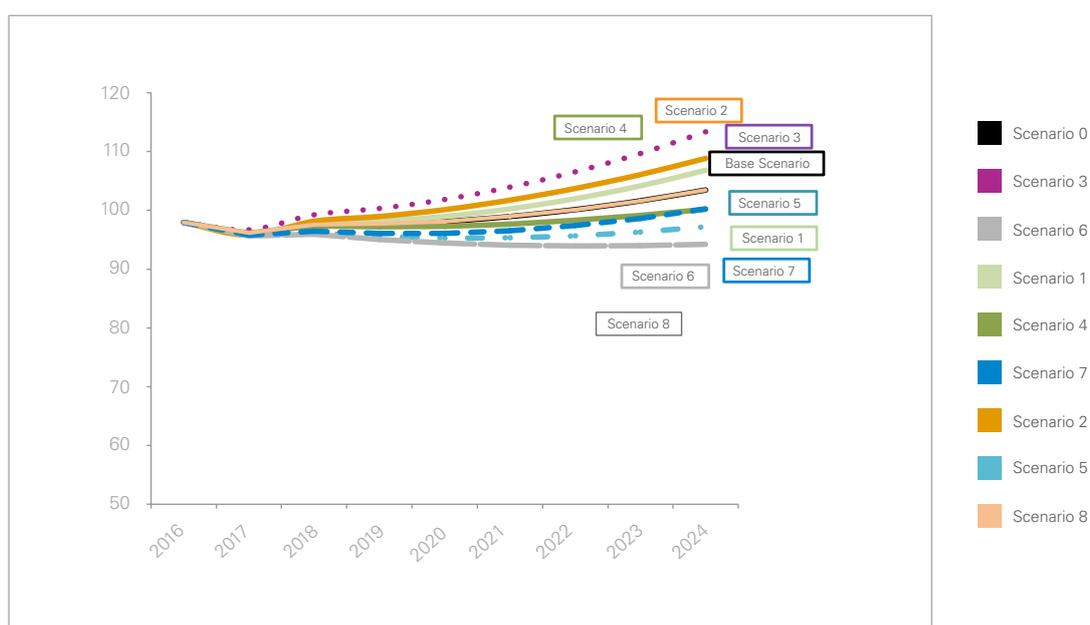
Meanwhile, the table below summarizes the effect of each scenario per sector. The table shows clearly how the government could potentially increase average per-child expenditure in critical sectors like education and health. Mozambique could create fiscal space for priority expenditure by increasing its GDP growth (scenario 1), obtaining external grants (scenario 2) or improving its tax administration (scenario 8). As highlighted in the table below, these strategies would not lead to an increase in debt, and would even allow the government to pay back a significant part of its debt

thus further expanding its future fiscal space by lowering interest payments.

On the other hand, scenario 4, 5, and 6 highlight show how adverse economic and political conditions could negatively affect priority expenditure and also lead to a higher debt stock. Finally, scenario 7 illustrates how a mixed set of economic and political conditions could still reduce Mozambique's fiscal space for priority expenditure, but would not necessarily lead to a substantial increase in debt.

TABLE 29 Summary of scenario results per sector

	Gov. debt 2024	Education	Health	Social Action	WASH	Total
Base scenario	103.1	80.9	36.2	5.2	14.2	136.6
Higher GDP growth	98.0	82.0	36.7	5.3	14.4	138.4
Higher donor support in priority areas	102.3	81.2	37.6	5.4	15.8	140.0
Higher GDP growth + higher donor support	98.0	83.4	38.1	5.5	16.1	143.1
Lower GDP growth	108.4	79.9	35.7	5.2	13.9	134.8
Lower donor support in priority areas	103.4	79.5	34.9	5.0	12.6	132.0
Lower GDP growth and lower donor support	108.7	78.5	34.4	5.0	12.4	130.3
Higher GDP growth + Lower donor support	98.4	80.5	35.4	5.0	12.8	133.7
Improved VAT administration	91.8	80.9	36.2	5.2	14.2	136.6

5.3 Other possibilities for enhancing the fiscal space

This section mentions other options to increase fiscal space that have not been used for the above-mentioned scenarios. These options have not been included in the set illustrative alternative scenarios, as the model does not provide ways to quantify the effect of these scenarios.

5.3.1 Tax policy measures

Advocacy and broadening of the tax net

The tax base in Mozambique remains limited and the informal economy is large; in the absence of latest estimates, the best guess is around 40 percent of GDP[107]. The current economic crisis is also pushing several firms out of business and it is not unreasonable to assume that in formalisation may increase. This issue, apart from capacity, also relates to the willingness to pay. The weak social contract between the government and citizens and a lack of confidence in the system to use the contributed resources prudently can explain why a large section of the economically active remain outside the tax net. The disclosure of the hidden debts may have further entrenched this view. Moreover, the current context where large businesses, especially megaprojects, enjoy generous tax exemptions and benefits while others are expected to pay taxes at high statutory rates even as large arrears in VAT refunds are run by the government, perpetuates the feeling on unfairness of the tax system. These challenges need to be addresses before efforts to increase the tax net.

Revenue generation at the municipal level

While municipalities are decentralised and have the mandate to collect their own revenue, the base remains extremely limited. Property tax could generate significant revenues, however lack of implementation has meant that revenue generating capacity through this source is limited. Other taxes include vehicle tax, however it is contested whether this tax can bring substantial revenues given that vehicle concentration is mainly in the South of the country[108]. As a result of the limited tax collections at this level, most municipalities depend heavily on intergovernmental transfers.

Revenue generation at decentralised level

The current decentralisation bill does not make reference to revenue mobilisation at decentralised levels. However, such a step can increase potential for local revenue generation and strengthen fiscal autonomy. While the ability to manage and utilise these generated resources could improve service delivery to the local population, it would be important to put in place the necessary institutional set up before such a step.

5.1.1 Improving the business environment:

Any discussion of improving tax administration cannot happen in isolation. Improvement in fiscal policy and administration that is conducive to the growth of the small and medium enterprises (SME), which can become an engine of growth, will be essential. This would involve not only addressing issues of tax burden and fairness, but also increasing the country's access to finance and attracting further investments in an effort to make this sector competitive.

5.3.2 Efficiency of expenditures

The analysis of priority sector shows that significant gains can be made from efficiency of spending. Moreover, given the limited resource envelope strategic allocation of resources will also be essential. For instance, foregoing analysis shows that in education, more gains can be made by improving efficiency than simply increasing allocations to the sector. Equity in spending should also be an important consideration.

5.3.3 Rolling balances

Chapter 2 highlighted the continued presence of rolling balances as observed by a civil society organisation in Mozambique, IESE. The inadequate explanation for the non-inclusion of these large balances will have an implication for the available fiscal space to increase spending in areas relevant for children.

5.3.4 Reducing illicit financing flows

While not included in the model, another (unquantifiable) option to free up resources is to improve capturing illicit financial flows. Illicit financial flows (IFFs) are illegal movements of money or capital from one country to another. The latest report of Global Financial Integrity (GFI) has investigated these IFFs, using two sources: (1) deliberate misinvoicing in merchandise trade (the source of GFI's low and high estimates), and (2) leakages in the balance of payments (also known as "hot money flows"). [109]The GFI report provides low estimates, which are based on trade between Mozambique and advanced economies only; and high estimates, which also take into account trade between developing countries. Naturally, measurements of illicit financial flows are identified indirectly and hence data on IFFs is imprecise. Figure 5.4 illustrates that the estimates of IFFs in Mozambique significantly differ. When taking into account IFFs between Mozambique and all countries, the estimates suggest an increase up to 2010, after which the IFFs have been somewhat decreased.

107. Ibid.
108. Based on interviews.
109. Global Financial Integrity (GFI), Illicit Financial Flows to and from Developing Countries: 2005-2014, April 2017, http://www.gfintegrity.org/wp-content/uploads/2017/05/GFI-IFF-Report-2017_final.pdf.

FIGURE 5.4   Mozambique Illicit Financial Flows 2005-2014 (in US$ millions)

■ Total Illicit Flows (low)   ■ Total Illicit Financial Flows (high)

MOZAMBIQUE: Illicit Financial Flows

Source: Global Financial Integrity, http://www.gfintegrity.org.
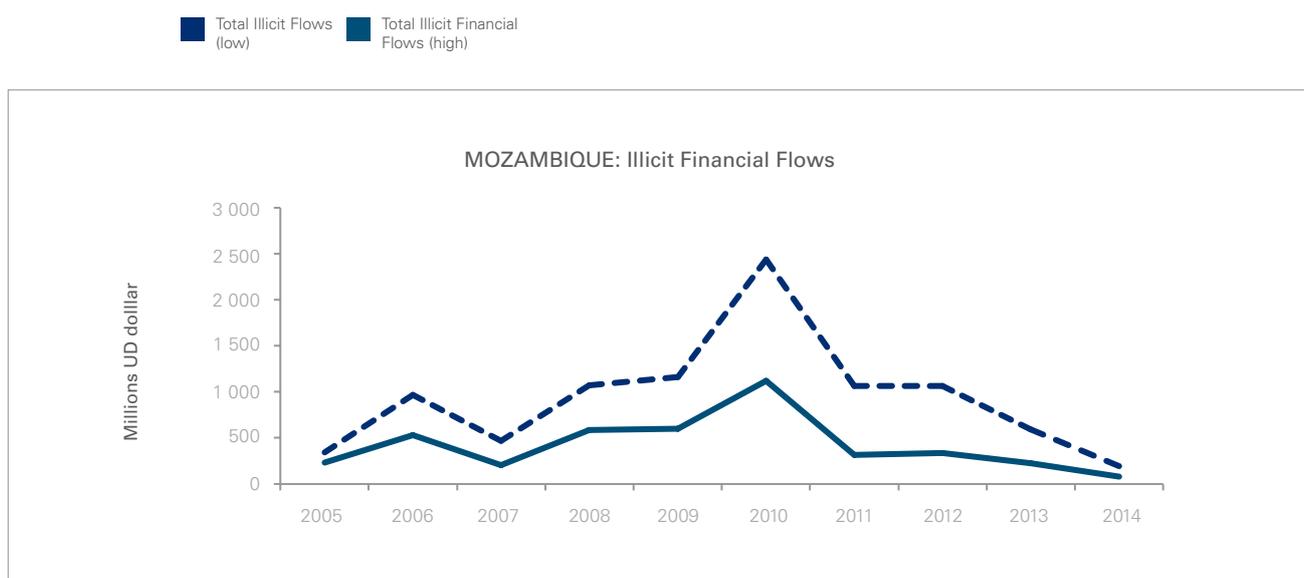
Figure 5.5 demonstrates illicit financial inflows and outflows as percentage of total trade. Illicit financial outflows are estimated at 2 to 3 per cent of Mozambique's total merchandise trade, and inflows at 3 to 7 per cent of Mozambique's total trade. While illicit inflows and outflows in Mozambique are below the average in the region, if the government of Mozambique were able to more effectively address trade mispricing practices, significant resources could be potentially captured and directed toward priority sectors.

FIGURE 5.5   Illicit Financial Flows, 2005-2014 average (as percentage of total trade)

■ Mozambique   ■ Sub-Saharan Africa

Source: Global Financial Integrity, http://www.gfintegrity.org.
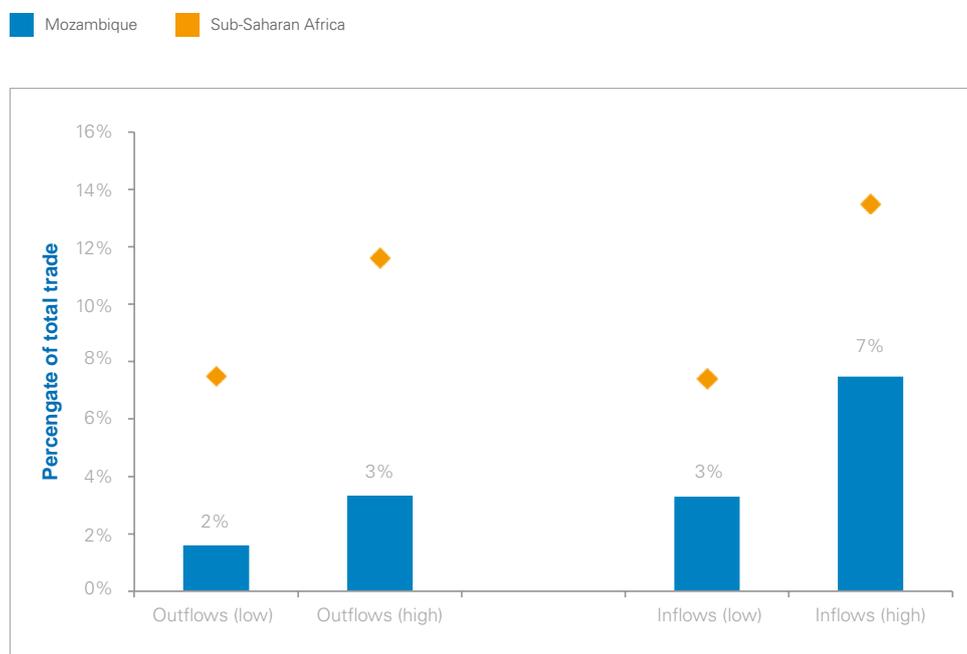
6. Conclusions

The current report highlights significant challenges faced by the government of Mozambique in increasing allocations in child-friendly areas. Given the sluggish economic performance and in the absence of one-off capital gains tax, the government will face difficulty in raising domestic revenues. Moreover, unless there are perceived efforts by the government to improve transparency and accountability over the hidden debts, it seems unlikely that donor support will increase to cushion the resource envelope. On the expenditure side, as more resources are devoted towards debt servicing, the costs of which increased steeply to 21 percent of the total government spending in 2016, fiscal space for expenditures relevant for children will be squeezed. Moreover, the continued prioritization of increasing recurrent spending means that there are limited resources for investments. Even within investment spending, expenditures on economic infrastructures seem to be growing faster than on social infrastructures thus significantly impacting the wellbeing of children. The ongoing deadlock with the IMF is hurting the economy by eroding confidence. The resolution of the deadlock can bring in much-needed relief in the form of increased donor assistance and boost further investments in the non-megaproject economy.

The report then went on to demonstrate how fiscal space for expenditures beneficial to children can be increased by looking at economic growth and donor support.

Some of the key takeaways from these scenarios are summarised below:

1. Increasing economic activity can have a positive impact on domestic resource mobilisation. In such a scenario however, commitment to use the increased fiscal space towards investments will be important to bring about desired results. On the other hand, lower growth than anticipated can have a negative impact by reducing the available resources. While effect of changes in economic growth on average spending per child in priority areas seems positive, its impact on the debt burden seems larger.

2. Changes in resources from donor assistance has a larger impact on per child spending in priority areas. These changes can have a significant impact on investment spending in these areas. However, this scenario does not have a significant impact on the burden of debt.

3. The combined effect of increase/decrease in economic activity along with an increase/decrease in donor assistance therefore will have the largest impact. Economic growth will impact domestic resource mobilisation while donor assistance will bring about changes in investment spending. In such a scenario, both average per child spending as well as the debt burden will be positively/negatively affected.

4. Further, in order to show that both parameters, economic growth as well as donor assistance, are important, a scenario whereby economic growth accelerates but donor assistance reduces is also shown. In such a scenario, the benefits of higher growth are more than offset by the negative effects of reduced donor assistance. This shows that even as the significance of donor assistance in the previous years may have declined, it is not completely inconsequential.

5. Improved VAT administration can have a significantly positive impact on domestic resource mobilisation. Additionally, other aspects of the tax policy and administration that could not be modelled are also discussed as they can be expected to have a significant impact on domestic resource mobilisation.

6. Improving the efficiency of public expenditures will be essential in creating further fiscal space for spending in areas relevant to the wellbeing of children. This includes reducing unit costs as well as ensuring equity in spending among the different provinces.

7. In the continued presence of rolling balances, created fiscal space may not be used effectively. Thus, it would be important to address this issue. Another important area of increasing fiscal space include the elimination of illicit financial flows.

UNICEF is at the forefront of the debates with the government regarding resource allocation and balancing the composition of expenditures. In this regard, the FSA can be an important instrument to improve the effectiveness of the dialogue. Moreover, such a quantitative exercise can also help in determining the importance of the various parameters like economic growth vis-à-vis others like donor assistance which can help shape the dialogue with the government.

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APPENDIX 1
Fiscal space projections

Programming assumptions base scenario

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. In particular, the growth rates of government expenditure are intended as plausible policy settings;

2. In general, the aim for Scenario 0 is to set programming assumptions that are "neutral" in character. For example, Mozambique`s merchandise export volumes are assumed to grow at the same rates as the world trade volume, so Mozambique's exports maintain the same share of the world trade volume. The volume of Mozambique' merchandise imports is assumed to grow at the same rates as real GDP, so merchandise imports would tend to maintain the same percentage of GDP. For recurrent expenditure, the assumption that staff sizes will grow at the same rate as the population would be neutral in a similar sense. So is the assumption that government wage rates would grow at the same rate as per-capita nominal GDP;

3. The elasticities that help determine the government's revenue performance are taken to be unitary for Scenario 0. This is also a "neutral" assumption. (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 of tax revenue with respect to their underlying determinants 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 to exceed (be less than) one, the projected revenue flow would rise (diminish) indefinitely as a percentage of GDP;

4. 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.

TABLE 30 Assumptions notes for the Base Scenario

(A) WORLD ECONOMIC CONDITIONS (1-3):
(1) The growth rate of the world trade volume decreases gradually from its estimated 2017 value of 5.9 per cent to 2024 value of 5 per cent.
(2) The growth rate of the U.S.-dollar world price level declines gradually from its estimated 2017 value of 3.7 per cent to a 2024 value of 2 per cent.
(3) The London Interbank Offer Rate rises gradually from its 2017 value of 2.4 per cent to a 2024 value of 3 per cent.
(B) BASIC MOZAMBIQUE MACROECONOMIC VARIABLES (4 10):
(4) The growth rate of real GDP gradually increases from 2.6 per cent in 2017 to 5 per cent in 2024
(5) The GDP deflator grows at the same rate as the year-average consumer price index.
(6) The December-December growth rate of the consumer price index (CPI) declines gradually from 21.2 per cent in 2017 to 5.5 per cent in 2024.
(7) The December-December growth rate of the U.S. dollar exchange rate grows at a rate (approximately) equal to the differential of the Rwanda and the world U.S.-dollar inflation rates.
(8) The overall population growth rate slowly decreases from 2.9 in 2017 to 2.8 per cent in2024
(9) The population under fifteen growth rate remains stable at 2.1 per cent over the projection period
(10) The headcount poverty incidence declines gradually from 55.6 per cent in 2017 to 50 per cent in 2024.
Exports and imports of goods and non-factor services (11 17):
(11) The export volume grows at the same rate as the world trade volume.
(12) Export prices grow at the same rate as the world U.S.-dollar price level.
(13) The import volume grows at the same rate as real GDP.
(14) Import prices grow at the same rate as the world U.S.-dollar price level.

(15) Non-factor service exports grow at a rate equal to the combined growth rates of world trade volume and the world US$ price level.

(16) Non-factor service imports excluding insurance and freight charges for merchandise imports grow at a rate equal to the combined growth rates of world trade volume and the world US$ price level.

(17) Insurance and freight charges remain stable at 12 per cent of the value of merchandise imports over the projection period.

National-expenditure accounts (18 20):

(18) Consumption expenditure by government entities outside the central government remains at -15.3 per cent of GDP over the projection period.

(19) Gross fixed capital formation remains stable through the projection period.

(20) The net increase in inventory stocks remains at 0 per cent over the projection period.

(C) TAX AND NON-TAX REVENUE (21 31):

(21) The elasticity of personal income tax with respect to nominal GDP remains stable at 0.8 through the projection period.

(22) The elasticity of company-tax revenue with respect to nominal GDP remains stable at 0.8 through the projection period.

(23) The elasticity of other income-tax revenue with respect to nominal GDP remains stable at 0.8 through the projection period.

(24) The elasticity of customs revenue with respect to merchandise-imports value will remain at the value of 0.9 over the projection years

(25) The elasticity of excise revenue with respect to nominal GDP will remain at the value of 0.9 over the projection years

(26) The elasticity of export-duty revenue with respect to export value increases from 0.3 in 2018 to 0.3 in 2024.

(27) The internal value-added tax rate remains unchanged at 17 per cent.

(28) The internal value-added tax collection efficiency remains unchanged at 29 per cent.

(29) The import-based value-added tax rate remains at 20 per cent.

(30) The import-based value-added tax collection efficiency remains unchanged at 20 per cent.

(31) The elasticity of central-government non-tax revenue with respect to nominal GDP remains at 1 over the projected years.

(D) EXTERNAL GRANTS TO THE GOVERNMENT (32 33):

(32) Central-government external grants for current expenditure remain stable at 1.5 per cent of GDP over the projection period

(33) Central-government external grants for capital expenditure slowly decline from 0.9 per cent of GDP in 2017 to 0.9 per cent of GDP in 2024

(E) GOVERNMENT EXPENDITURE IN THE PRIORITY AND NON-PRIORITY CATEGORIES (34 55):

(E.1) For non-interest recurrent expenditure,

(E.1.a) In the education sector,

(34) The staff size grows at the same rate as the number of children.

(35) Staff salaries grow at a rate equal to the growth rate of per-capita nominal GDP.

(36) Expenditure on current goods and services grows at a rate equal to the combined growth rates of the year-average CPI and the sectoral staff size.

(37) Expenditure on non-staff recurrent expenditure excluding current goods and services grows at a rate equal to the combined growth rates of the year-average CPI and the number of children.

(E.1.b) In the health sector,

(38) The staff size grows at the same rate as the population.

(39) Staff salaries grow at a rate equal to the growth rate of per-capita nominal GDP.

(40) Expenditure on current goods and services grows at a rate equal to the combined growth rates of the year-average CPI and the sectoral staff size.

(41) Expenditure on non-staff recurrent expenditure excluding current goods and services grows at a rate equal to the combined growth rates of the year-average CPI and the population growth rate.

(E.1.c) In the social-protection sector,

(42) Central-government recurrent expenditure grows at a rate equal to the combined growth rates of the year-average CPI and the population.

(E.1.d) In the WASH sector,

(43) The staff size grows at the same rate as the number of children.

(44) Staff salaries grow at a rate equal to the growth rate of per-capita nominal GDP

(45) Expenditure on current goods and services grows at a rate equal to the combined growth rates of the year-average CPI and the sectoral staff size.

(46) Expenditure on non-staff recurrent expenditure excluding current goods and services grows at a rate equal to the combined growth rates of the year-average CPI and the population growth rate.

(E.1.f) In the non-priority expenditure sectors,

(47) The staff size grow at the same rate as the population.

(48) Staff salaries grow at a rate equal to the growth rate of per-capita nominal GDP

(49) Expenditure on current goods and services grows at a rate equal to the combined growth rates of the year-average CPI and the sectoral staff size.

(50) Expenditure on non-staff recurrent expenditure excluding current goods and services grows at a rate equal to the combined growth rates of the year-average CPI and the population growth rate.

(E.2) For non-recurrent expenditure, over the projection years,

(51) Education non-recurrent central-government expenditure remain at the 2017 value of 1 over the projection years.

(52) Health non-recurrent central-government expenditure remain at the 2017 value of 1 per cent of GDP over the projection years.

(53) Social-protection non-recurrent central-government expenditure remain at the 2017 value of 0.2 per cent of GDP over the projection years.

(54) Non-recurrent Water and Environment expenditure remain at the 2017 value of 1.2 per cent of GDP over the projection years.

(55) Non-priority non-recurrent central government expenditure increases gradually from the 2017 value of 3.8 per cent of GDP to a 2024 value of 7 per cent of GDP.

(F) FOR EXTERNAL AND INTERNAL DEBT (56 60):

(56) Average interest rates on the previous year's year-end external debt stock increase (decrease) with LIBOR.

(57) Average interest rates on the previous year's year-end internal debt stock remains stable at 11.2 per cent over the projection period.

(58) External debt disbursements remain stable at 11.2 per cent over the projection period.

(59) External-debt repayments remain stable at 3.7 per cent of GDP over the projection period.

(60) External-debt disbursements in each projection year amount to 55.1 per cent of total non-recurrent expenditure.

TABLE 31   Assumptions for the Base Scenario

	2017	2018	2019	2020	2021	2022	2023	2024
(A) EXTERNAL 'STATE-OF-THE-WORLD' VARIABLES:								
Growth rates:								
*World trade volume	0.06	0.06	0.06	0.06	0.05	0.05	0.05	0.05
**World U.S.-dollar price level	0.04	0.03	0.03	0.03	0.03	0.02	0.02	0.02
Average world U.S.-dollar oil price (US$/bbl.)	-0.14	0.03	0.03	0.03	0.03	0.02	0.02	0.02
Interest rates:								
London Interbank Offer Rate (LIBOR)	0.02	0.03	0.03	0.03	0.03	0.03	0.03	0.03
(B) BASIC MACROECONOMIC VARIABLES:								
Growth rates:								
Gross domestic product (national currency - millions)	0.17	0.14	0.20	0.19	0.17	0.16	0.14	0.12
Gross domestic product at 216 prices and exchange rate (US$ million)	0.03	0.03	0.03	0.04	0.04	0.04	0.05	0.05
GDP deflator	0.14	0.10	0.17	0.15	0.13	0.11	0.09	0.06
Consumer prices (year-average)	0.14	0.10	0.17	0.15	0.13	0.11	0.09	0.06
Consumer prices (December)	0.21	0.19	0.17	0.14	0.12	0.10	0.08	0.06
Exchange rate (year-average)	0.00	0.03	0.16	0.12	0.10	0.00	0.00	0.00
Exchange rate (December)	0.17	0.15	0.13	0.11	0.10	0.06	0.04	0.03
Population (millions)	0.03	0.03	0.03	0.03	0.03	0.03	0.03	0.03
Population under fifteen (millions)	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Population in poverty	0.13	0.11	0.09	0.07	0.10	0.06	0.04	0.03
Headcount poverty incidence	0.56	0.54	0.52	0.50	0.50	0.50	0.50	0.50
Growth rates (US$ million):								
Merchandise exports:	-0.09	0.09	0.09	0.08	0.08	0.08	0.08	0.08
Unit value	-0.14	0.03	0.03	0.03	0.03	0.02	0.02	0.02
Volume	0.06	0.06	0.06	0.05	0.05	0.06	0.06	0.05
Copper exports:	-0.09	0.09	0.09	0.08	0.08	0.08	0.08	0.08
Unit value	-0.14	0.03	0.03	0.03	0.03	0.02	0.02	0.02
Volume	0.06	0.06	0.06	0.05	0.05	0.06	0.06	0.05
Non-copper exports:	0.10	0.09	0.09	0.08	0.07	0.10	0.10	0.08
Unit value	0.04	0.03	0.03	0.03	0.02	0.04	0.04	0.03
Volume	0.06	0.06	0.06	0.05	0.05	0.06	0.06	0.05
Merchandise imports:	-0.20	0.06	0.07	0.07	0.06	0.06	0.05	0.05

	2017	2018	2019	2020	2021	2022	2023	2024
Unit value	-0.14	0.03	0.03	0.03	0.03	0.02	0.02	0.02
Volume	0.06	0.06	0.06	0.05	0.05	0.06	0.06	0.05
Oil imports:	-0.12	0.06	0.07	0.07	0.07	0.07	0.07	0.07
Unit value	-0.14	0.03	0.03	0.03	0.03	0.02	0.02	0.02
Volume	0.03	0.03	0.03	0.04	0.04	0.04	0.05	0.05
Non-oil imports:	0.06	0.06	0.07	0.06	0.06	0.08	0.08	0.08
Unit value	0.04	0.03	0.03	0.03	0.02	0.04	0.04	0.03
Volume	0.03	0.03	0.03	0.04	0.04	0.04	0.05	0.05
Growth rates:								
Non-factor services receipts	0.10	0.09	0.09	0.08	0.08	0.07	0.07	0.07
Non-factor services payments, excluding merchandise-imports insurance and freight	0.06	0.06	0.07	0.06	0.07	0.07	0.07	0.07
Ratios:								
Ratio, insurance and freight costs/merchandise imports value	0.12	0.12	0.12	0.12	0.12	0.12	0.12	0.12
Incremental capital-output ratio	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Per cent of GDP:								
Consumption expenditure by governments excl. central government	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15
GENERAL-GOVERNMENT FINANCIAL ACCOUNTS:								
Tax and non-tax revenue (excl. external grants) (+):								
(C) TAX REVENUE:								
Central government:								
Elasticities of...								
personal income tax with respect to nominal GDP	0.80	0.80	0.80	0.80	0.80	0.80	0.80	0.80
company-tax revenue with respect to nominal GDP	0.80	0.80	0.80	0.80	0.80	0.80	0.80	0.80
other income-tax revenue with respect to nominal GDP	0.80	0.80	0.80	0.80	0.80	0.80	0.80	0.80
customs revenue with respect to merchandise-imports value	0.89	0.87	0.86	0.85	0.84	0.82	0.81	0.80
excise revenue with respect to nominal GDP	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90
export-duty revenue with respect to export value	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30
internal VAT revenue with respect to nominal GDP	0.27	0.27	0.27	0.27	0.27	0.27	0.27	0.27
VAT revenue from imports with respect to the value of merchandise imports	0.27	0.27	0.27	0.27	0.27	0.27	0.27	0.27

	2017	2018	2019	2020	2021	2022	2023	2024
Consumption taks:								
Internal VAT:								
Internal VAT rate	0.17	0.17	0.17	0.17	0.17	0.17	0.17	0.17
Internal VAT collection efficiency	0.29	0.29	0.29	0.29	0.29	0.29	0.29	0.29
VAT revenue from imports:								
External VAT rate	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
External VAT collection efficiency	0.58	0.58	0.58	0.58	0.58	0.58	0.58	0.58
NON-TAX REVENUE:								
Elasticities of...								
central-government non-tax revenue with respect to nominal GDP	0.87	0.87	0.87	0.87	0.87	0.87	0.87	0.87
(D)EXTERNAL GRANTS (+):								
Per cent of GDP:								
Central-government external grants for current expenditure	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Central-government external grants for capital expenditure (projects)	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01
(E) CENTRAL-GOVERNMENT EXPENDITURE:								
Growth rates:								
Recurrent education expenditure:	0.16	0.13	0.20	0.19	0.17	0.16	0.14	0.12
Central-government recurrent education expenditure:								
Education staff	0.02	0.03	0.03	0.03	0.03	0.04	0.04	0.04
Education remuneration rates	0.14	0.10	0.17	0.16	0.14	0.12	0.11	0.09
Non-staff recurrent education expenditure:	0.17	0.13	0.20	0.18	0.16	0.14	0.12	0.10
Recurrent education expenditure on goods and services	0.17	0.13	0.20	0.19	0.17	0.15	0.13	0.11
Other non-staff recurrent education expenditure	0.16	0.13	0.19	0.18	0.15	0.13	0.11	0.09
Recurrent health expenditure:	0.17	0.14	0.21	0.20	0.18	0.17	0.15	0.14
Central-government recurrent health expenditure:	0.17	0.14	0.21	0.20	0.18	0.17	0.15	0.14
Health staff	0.03	0.03	0.04	0.04	0.04	0.05	0.05	0.06
Health remuneration rates	0.14	0.10	0.17	0.16	0.14	0.12	0.11	0.09
Non-staff recurrent health expenditure:	0.17	0.14	0.20	0.19	0.17	0.15	0.13	0.11
Recurrent health expenditure on goods and services	0.18	0.14	0.21	0.20	0.18	0.16	0.14	0.12
Other non-staff recurrent health expenditure	0.17	0.14	0.20	0.19	0.16	0.14	0.12	0.09
Non-priority recurrent expenditure:	0.03	0.03	0.04	0.04	0.04	0.05	0.05	0.06

	2017	2018	2019	2020	2021	2022	2023	2024
Central-government non-priority recurrent expenditure	0.03	0.03	0.04	0.04	0.04	0.05	0.05	0.06
Non-priority staff	0.14	0.10	0.17	0.15	0.13	0.11	0.09	0.06
Remuneration rates in non-priority sectors	0.18	0.15	0.22	0.21	0.19	0.17	0.15	0.13
Non-staff recurrent non-priority expenditure	0.03	0.03	0.03	0.03	0.03	0.03	0.03	0.03
Recurrent non-priority expenditure on goods and services	0.14	0.10	0.17	0.16	0.14	0.12	0.11	0.09
Other non-staff recurrent non-priority expenditure	0.11	0.10	0.14	0.14	0.12	0.11	0.09	0.08
Per cent of GDP:								
Non-recurrent education expenditure	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01
Central government non-recurrent education expenditure:	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01
Non-recurrent health expenditure	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01
Central government non-recurrent health expenditure:	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01
Non-recurrent social action expenditure	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Central government non-recurrent social action expenditure:	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Non-priority non-recurrent expenditure	0.04	0.04	0.05	0.05	0.05	0.06	0.06	0.07
Central-government non-priority non-recurrent expenditure	0.04	0.04	0.05	0.05	0.05	0.06	0.06	0.07
(F) EXTERNAL AND INTERNAL DEBT:								
Average interest rates (applied to preceding year-end debt stock):								
Average interest rates on external debt	0.02	0.02	0.03	0.03	0.03	0.03	0.03	0.03
Average interest rates on internal debt	0.11	0.11	0.11	0.11	0.11	0.11	0.11	0.11
Per cent of preceding year-end debt stock:								
External-debt repayments (-)	-0.03	-0.03	-0.03	-0.03	-0.03	-0.03	-0.03	-0.03
Per cent of GDP:								
External-debt disbursements (+):	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04
External-debt disbursements/total non-recurrent expenditure	0.55	0.55	0.55	0.55	0.55	0.55	0.55	0.55
External-debt repayments (-)	-0.02	-0.02	-0.02	-0.02	-0.02	-0.02	-0.02	-0.02
Net internal-debt flow (+):	0.04	0.05	0.05	0.06	0.07	0.07	0.08	0.10

Projection results Base Scenario

Table 32 shows the projections results for the base scenario (i.e. using the assumptions mentioned the preceding tables).

TABLE 32   Project results for the base scenario

	2018	2019	2020	2021	2022	2023	2024
(A) TOTAL PRIORITY NON-INTEREST EXPENDITURE	**11.58**	**11.58**	**11.60**	**11.63**	**11.69**	**11.76**	**11.86**
Total education expenditure	6.80	6.80	6.81	6.82	6.83	6.85	6.88
Total health expenditure	3.02	3.05	3.09	3.12	3.16	3.21	3.26
Total social action expenditure	0.56	0.52	0.49	0.47	0.45	0.45	0.45
Total WASH expenditure	1.20	1.21	1.22	1.23	1.24	1.25	1.27
Priority recurrent expenditure:	8.20	8.15	8.12	8.09	8.09	8.11	8.16
Recurrent education expenditure:	5.77	5.76	5.76	5.75	5.75	5.76	5.78
Central government recurrent education expenditure:	5.77	5.76	5.76	5.75	5.75	5.76	5.78
Expenditure on education staff	3.67	3.67	3.69	3.71	3.73	3.77	3.83
Non-staff recurrent education expenditure:	2.10	2.09	2.07	2.05	2.02	1.99	1.95
Recurrent education expenditure on goods and services	1.08	1.07	1.07	1.06	1.06	1.05	1.04
Other non-staff recurrent education expenditure	1.02	1.01	1.00	0.98	0.96	0.94	0.91
Recurrent health expenditure:	2.03	2.04	2.06	2.08	2.10	2.12	2.16
Central government recurrent health expenditure:	2.03	2.04	2.06	2.08	2.10	2.12	2.16
Expenditure on health staff	1.29	1.30	1.32	1.34	1.36	1.40	1.43
Non-staff recurrent health expenditure:	0.74	0.74	0.74	0.74	0.73	0.73	0.72
Recurrent health expenditure on goods and services	0.38	0.38	0.38	0.38	0.39	0.39	0.39
Other non-staff recurrent health expenditure	0.36	0.36	0.36	0.35	0.35	0.34	0.33
Recurrent social action expenditure:	0.38	0.33	0.28	0.25	0.23	0.21	0.20
Central government recurrent social action expenditure:	0.38	0.33	0.28	0.25	0.23	0.21	0.20
Recurrent WASH expenditure:	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Central government recurrent WASH expenditure:	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Expenditure on WASH staff	0.01	0.01	0.01	0.01	0.01	0.01	0.01
Non-staff recurrent WASH expenditure:	0.01	0.01	0.01	0.00	0.00	0.00	0.00
Recurrent WASH expenditure on goods and services	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Other non-staff recurrent WASH expenditure	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Priority non-recurrent expenditure:	3.38	3.43	3.49	3.54	3.59	3.65	3.70
Non-recurrent education expenditure:	1.03	1.04	1.05	1.06	1.08	1.09	1.10

	2018	2019	2020	2021	2022	2023	2024
Central government non-recurrent education expenditure:	1.03	1.04	1.05	1.06	1.08	1.09	1.10
Non-recurrent health expenditure:	0.99	1.01	1.03	1.05	1.06	1.08	1.10
Central government non-recurrent health expenditure:	0.99	1.01	1.03	1.05	1.06	1.08	1.10
Non-recurrent social action expenditure	0.18	0.19	0.20	0.21	0.23	0.24	0.25
Central government non-recurrent social action expenditure:	0.18	0.19	0.20	0.21	0.23	0.24	0.25
Non-recurrent WASH expenditure:	1.18	1.19	1.21	1.22	1.23	1.24	1.25
Central government non-recurrent WASH expenditure:	1.18	1.19	1.21	1.22	1.23	1.24	1.25
(B) TAX AND NON-TAX REVENUE (EXCL. EXTERNAL GRANTS) (+):	**22.61**	**22.28**	**21.86**	**21.48**	**20.87**	**20.40**	**20.02**
Tax revenue:	18.81	18.56	18.21	17.91	17.35	16.93	16.60
Central government tax revenue:	18.81	18.56	18.21	17.91	17.35	16.93	16.60
Income tax:	8.84	8.54	8.26	8.01	7.80	7.61	7.45
Personal income tax	3.71	3.59	3.47	3.37	3.28	3.20	3.13
Company tax:	5.09	4.91	4.75	4.61	4.49	4.38	4.29
Other income tax	0.04	0.03	0.03	0.03	0.03	0.03	0.03
Value-added tax:	9.37	9.48	9.47	9.45	9.16	8.97	8.83
Value-added tax on internal transactions	4.94	4.94	4.94	4.94	4.94	4.94	4.94
Value-added tax on imports	4.43	4.54	4.53	4.52	4.23	4.04	3.89
Customs and excise duties:	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Customs duties	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Excises	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Export duties	0.61	0.54	0.49	0.44	0.39	0.35	0.32
Non-tax revenue (excl. external grants) (+):	3.80	3.72	3.65	3.58	3.52	3.47	3.42
Central government non-tax revenue:	3.80	3.72	3.65	3.58	3.52	3.47	3.42
(C) EXTERNAL GRANTS (+):	**2.39**	**2.39**	**2.39**	**2.39**	**2.40**	**2.40**	**2.40**
External grants for current expenditure:	1.51	1.51	1.50	1.50	1.50	1.50	1.50
Central government external grants for current expenditure:	1.51	1.51	1.50	1.50	1.50	1.50	1.50
External grants for capital expenditure (projects):	0.88	0.88	0.89	0.89	0.89	0.90	0.90
Central government external grants for capital expenditure (projects):	0.88	0.88	0.89	0.89	0.89	0.90	0.90
(D) TOTAL NON-PRIORITY NON-INTEREST EXPENDITURE (-):	**-15.67**	**-15.78**	**-15.97**	**-16.22**	**-16.55**	**-16.94**	**-17.40**
Non-priority recurrent expenditure:	-11.55	-11.28	-11.05	-10.85	-10.68	-10.53	-10.40

	2018	2019	2020	2021	2022	2023	2024
Central government non-priority recurrent expenditure:	-11.55	-11.28	-11.05	-10.85	-10.68	-10.53	-10.40
Non-priority expenditure on staff	-6.62	-6.62	-6.62	-6.62	-6.62	-6.62	-6.62
Non-staff recurrent non-priority expenditure:	-4.93	-4.66	-4.43	-4.23	-4.06	-3.91	-3.78
Recurrent non-priority expenditure on goods and services	-1.79	-1.54	-1.33	-1.17	-1.04	-0.95	-0.87
Other non-staff recurrent non-priority expenditure	-3.14	-3.12	-3.10	-3.07	-3.02	-2.97	-2.91
Non-priority non-recurrent expenditure:	-4.12	-4.50	-4.92	-5.37	-5.87	-6.41	-7.00
Central government non-priority non-recurrent expenditure:	-4.12	-4.50	-4.92	-5.37	-5.87	-6.41	-7.00
(E) EXTERNAL-DEBT DISBURSEMENTS (+):	**3.70**	**3.70**	**3.70**	**3.70**	**3.70**	**3.70**	**3.70**
External-debt disbursements (+) (US$ millions):	522.56	543.44	579.35	616.40	712.33	809.63	905.07
(F) EXTERNAL DEBT SERVICE (-):	**-3.57**	**-3.67**	**-3.68**	**-3.56**	**-3.18**	**-2.90**	**-2.66**
External interest expenditure (-)	-1.76	-1.88	-1.96	-1.89	-1.69	-1.54	-1.39
External interest expenditure (-) (US$ million)	-247.68	-276.17	-306.23	-315.03	-324.65	-336.75	-340.17
External debt repayments (-)	-1.81	-1.79	-1.72	-1.67	-1.49	-1.36	-1.27
External debt repayments (-) (US$ million)	-256.01	-262.68	-269.70	-277.44	-285.91	-296.57	-309.40
(G) NET INTERNAL FINANCIAL FLOWS (INCL. INTERNAL INTEREST) (+):	2.11	2.66	3.30	3.84	4.44	5.10	5.79
Net internal-debt flow (+):	4.54	5.10	5.81	6.53	7.40	8.43	9.61
Internal-debt disbursements (+)							0.00
Internal debt repayments (-)							0.00
Internal interest expenditure (-)	-2.43	-2.44	-2.52	-2.69	-2.96	-3.33	-3.82
Discrepancy (+)	0.00	0.00	0.00	0.00	0.00	0.00	0.00

TABLE 33 Summary of projection results per scenario

Scenario	1	2	3	4	5	6	7	8
AVERAGE OVER PROJECTED YEARS								
US$ per child priority expenditures at 2016 prices and exchange rate								
Total priority non-interest expenditure:	142.677	146.700	142.944	148.388	140.722	135.144	133.377	138.777
Total education expenditure	83.64	85.87	83.07	86.67	82.56	81.57	80.54	83.69
Total health expenditure	38.20	39.33	38.53	39.68	37.65	35.84	35.35	36.85
Total social action expenditure	6.04	6.15	5.57	5.65	5.99	5.14	5.11	5.20
Per cent of GDP								
Central government surplus:	-8.47	-8.11	-8.02	-7.81	-8.65	-8.23	-8.42	-7.88
Central government primary surplus	-3.92	-3.75	-3.56	-3.50	-4.01	-3.73	-3.81	-3.56
Tax revenue	17.95	17.89	17.95	17.89	17.98	17.95	17.98	17.89
Other revenue	3.63	3.61	3.63	3.61	3.63	3.63	3.63	3.61
External grants	2.39	2.39	2.77	2.77	2.39	1.98	1.98	1.98
Total non-interest expenditure (-)	-27.89	-27.65	-27.91	-27.77	-28.02	-27.29	-27.41	-27.04
Central government external and internal interest	-4.55	-4.36	-4.46	-4.31	-4.65	-4.51	-4.61	-4.32
Total priority non-interest expenditure:	11.64	11.53	11.66	11.66	11.69	11.03	11.09	10.93
Total education expenditure	6.82	6.75	6.78	6.81	6.86	6.66	6.69	6.59
Total health expenditure	3.11	3.09	3.14	3.11	3.13	2.92	2.94	2.90
Total social action expenditure	0.49	0.49	0.46	0.45	0.50	0.42	0.43	0.41
Net financing (gross of interest):	8.47	8.11	8.02	7.81	8.65	8.23	8.42	7.88
Net external financing	2.07	2.12	2.07	2.12	2.05	2.07	2.05	2.12
Net internal financing	6.39	5.99	5.95	5.69	6.61	6.16	6.37	5.76
Final-year central-government debt stock:	129.09	119.12	126.46	117.32	134.49	127.63	133.00	117.70
Final-year central-government external-debt stock	85.21	79.55	85.21	79.55	88.25	85.21	88.25	79.55
Final-year central-government internal-debt stock	43.88	39.56	41.25	37.76	46.24	42.42	44.75	38.15

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