

## **CHAPTER TWELVE: EXPLORING BEST PRACTICE IN PUBLIC BUDGET ALLOCATION**

### **12.1 Introduction**

This chapter seeks to link all the separate findings of Chapters 4-11, to find the governance indicators suited to finding the ideal budget allocation in the African context. The chapter is structured as follows: Section 12.2 discusses the criteria of an ideal budget allocation, Section 12.3 presents the public budget outcomes based on the criteria developed in Section 12.2 and Section 12.4 offers concluding remarks.

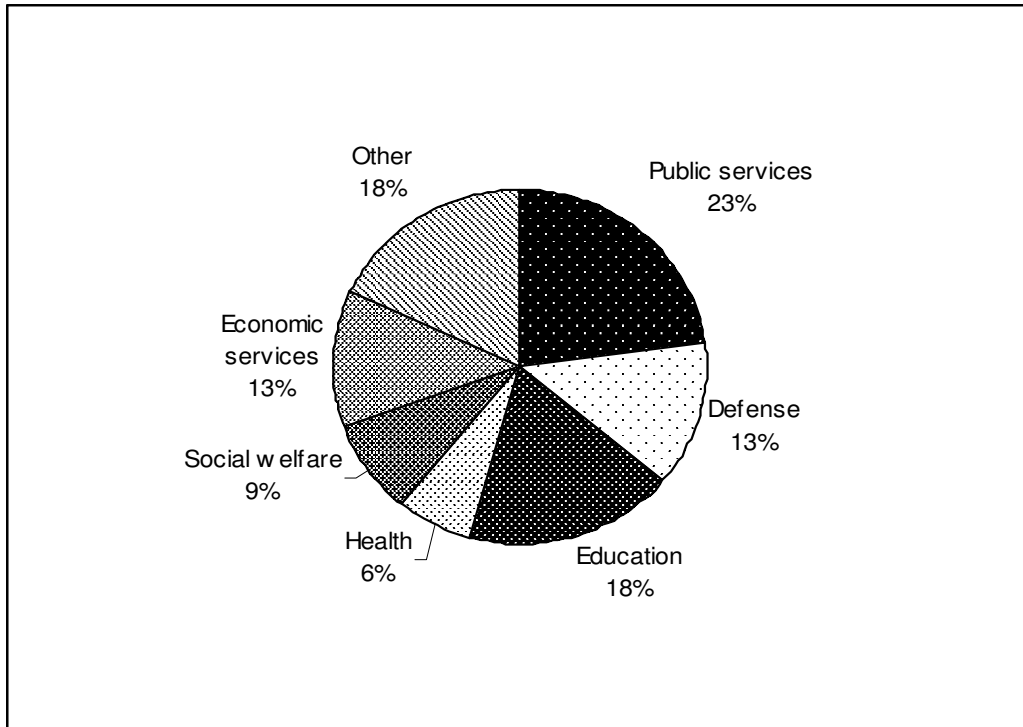
### **12.2 Criteria of public budget allocation**

This section identifies those budget allocation criteria best suited for use in finding optimal budget allocation strategies. The criteria are then used to outline a benchmark budget distribution that may be useful for budget analysis, especially in a NEPAD context.

#### **12.2.1 Corruption control**

The discussions in Chapters 4-11 have clearly shown that the prevalence of corruption plays a prominent role in the allocation of public resources. Based on the statistical significance of this variable in terms of budget allocation, the countries used in this study are stratified according to the extent to which they comply. It is assumed that the top 25% of the countries are the best performers. Their average budget allocations over the period 1995-2004 are then presented as the ideal mix of budget decision reflecting limited interference from corruption.

The best performing countries with regard to corruption criteria include Botswana, Lesotho, Mauritius, Namibia, Tunisia, Morocco and South Africa.



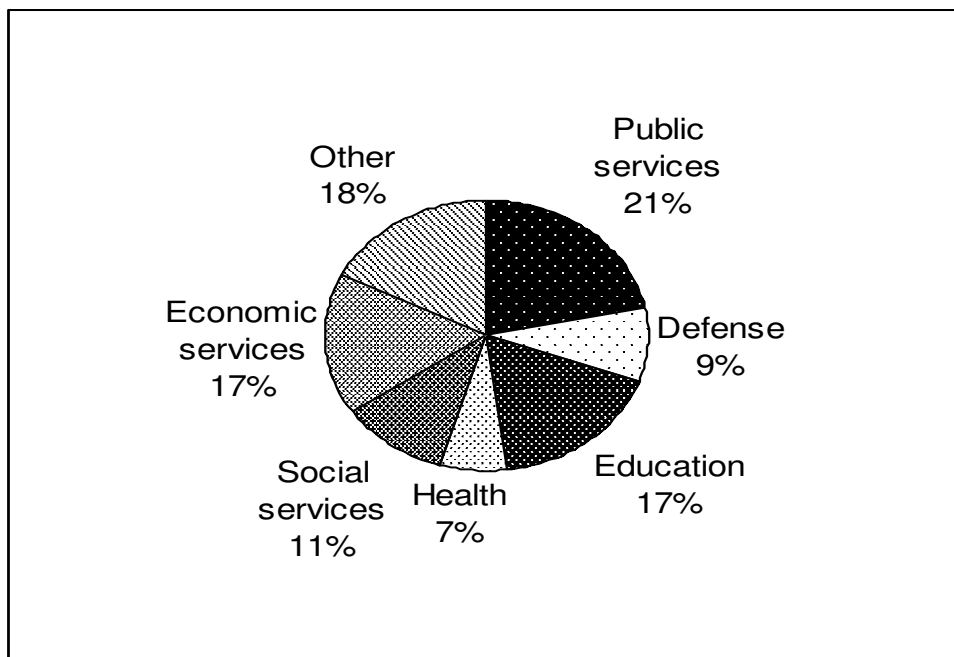
**Figure 57: Ideal public budget structure in Africa based on the corruption control criteria**

Analysis of the budget priorities of the countries in the sample show that, on average, the top 25% of the countries (characterised by corruption) allocate their public budgets in a manner shown in Figure 57. This suggests that, ignoring other governance indicators, the ideal public budget allocation to limit the impact of corruption would be to devote a maximum of 23% of the budget to public services, 13% to defence and 18% to 'other'. Expenditures on the latter categories should be regarded as the maximum levels since corrupt regimes tend to allocate more funds to defence and general public services. Any alteration of the public budget to allocate more than the proportions suggested in the structure will imply that the level of corruption in that country may be increasing and that urgent action should be taken to rectify the situation.

Minima of 18%, 6%, 9% and 13% for education, health, social welfare and economic services, respectively, are ideal in the African context. Thus, when expenditure priorities comply with these figures, corruption is probably limited.

### 12.2.2 Political stability

This criterion is analysed here as was the corruption-control index, and presented to reflect the spending behaviour of the top 25% best performers. Their priorities are then used as a basis for an 'ideal' budget structure. The top 25% include Botswana, Lesotho, Madagascar, Mauritius, Namibia, Tunisia and Mali. The ideal budget structure based on this criterion is presented in Figure 58.



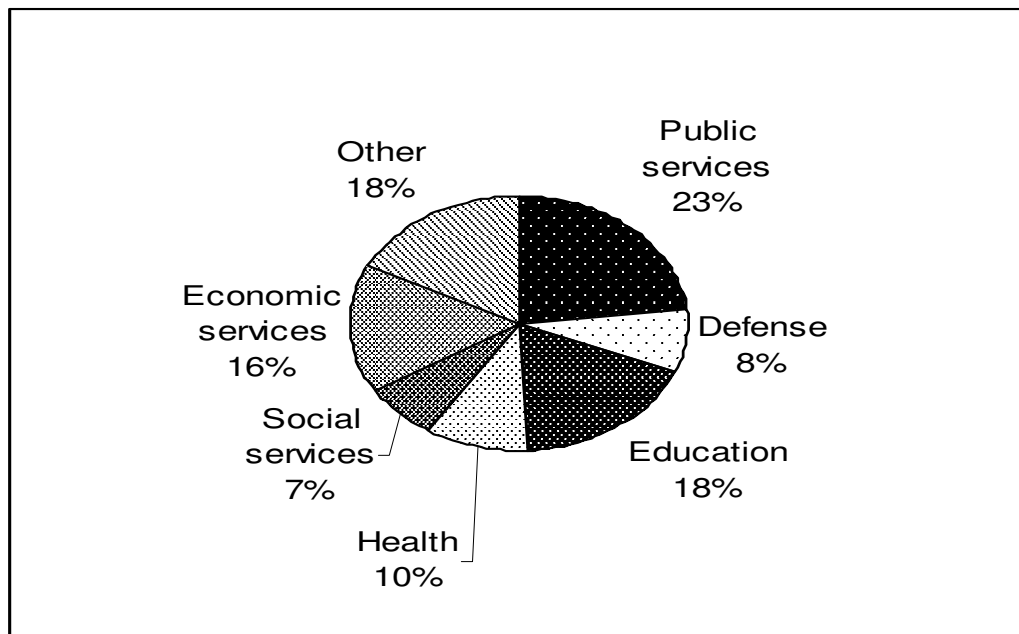
**Figure 58: Ideal public budget allocation in Africa based on political stability criteria**

The figure shows that spending on general public services, 'other' spending and defence should not exceed 21%, 18% and 9% of the budget, respectively. Any expenditure on these categories in excess of these figures may indicate political instability. The ideal allocation for education, health, social services and

economic services is at least 17%, 7%, 11% and 17%, respectively. To maintain these levels, political stability is a prerequisite.

### 12.2.3 Voice and accountability

Figure 59 portrays the effect of the voice and accountability index with the top performers in terms of this index determining the budget allocations to the different sectors. The top performers include Botswana, Lesotho, Madagascar, Mauritius, Namibia, South Africa and Mali.



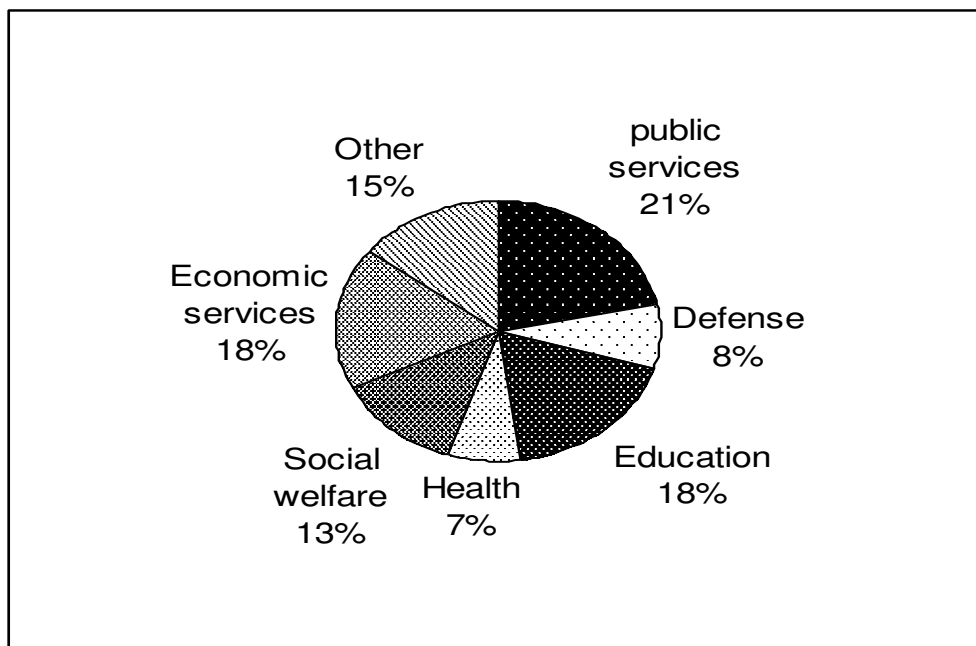
**Figure 59: Ideal public budget allocation in Africa based on the voice and accountability criteria**

Figure 59 clearly shows that a country with desirable levels of accountability and respect for the voice of its people should devote at least 18% of its budget to education, 10% to health, 7% to social services and 16% to economic services. A maximum of 23%, 8%, and 18% for general public services, defence and ‘other’ spending, respectively, is ideal.

### 12.2.4 Comprehensive criteria of budget allocation in Africa

The three preceding sections analyse the budgets of the best performing countries on the basis of three governance criteria in isolation. This section attempts to improve on the optimal budget allocations suggested in Sections 12.2.1-3 by using all three indicators jointly. The first step involves the selection the 25% best performing countries in each category. Then, based on this selection, those countries that perform best in all three criteria are selected. Third, those countries that comply with at least two of the conditions are selected. Fourth, the average budget allocations of these best performing countries in order are analysed and used to revise the optimal budget allocation.

The budget allocation based on the comprehensive criteria is shown in Figure 60.



**Figure 60: Ideal public budget allocation in Africa based on the comprehensive criteria**

The figure shows that combining the criteria causes the budget allocation to shift drastically in the case of some spending categories. The maximum budget

allocation to general public services should not exceed 21%, which accords with the result when political stability alone is considered but which contradicts the results for both corruption control and voice and accountability. In the case of defence spending, the ideal margin for the combined criteria is 8% compared to 13% and 9% for corruption control and political stability, respectively, when considered separately. 'Other' expenditure is set at 15% by the analysis for the combined criteria, compared to 18% for all three criteria considered independently. The 'ideal' public budget should spend at least 18%, 7%, 13% and 18% on education, health, social welfare and economic services, respectively.

### **12.3 Summary of findings**

The purpose of this chapter was to devise a 'template' for an 'ideal' budget distribution based on the most successful countries in Africa. The findings are that the ideal budget in the African context should not allocate more than 21% of the public budget to general public services; 8% to defence and 18% to 'other' spending. Instead, a minimum of 18% should be allocated to education; 10% to health; 11% to social welfare and 18% to economic services.

## **CHAPTER THIRTEEN: CONCLUSION AND POLICY RECOMMENDATIONS**

### **13.1 Introduction**

The purpose of this chapter is to offer policy recommendations based on the research results discussed in the preceding chapters. It is structured as follows: Section 13.2 summarises the conclusions related to the major findings of the study, Section 13.3 outlines some policy recommendations, Section 13.4 explains the limitations of the study and offers suggestions for further research in the same or related fields and, finally, Section 13.3 concludes the study.

### **13.2 Conclusions**

The purpose of this study was to identify and investigate the determinants of the structure of public budgets in Africa. The analysis was carried out within a panel econometric framework at two levels. First, each of the functional categories of government spending is analysed using a single equation approach, with the dependent variables the functional categories of government spending expressed as shares of the total public budget and of the GDP (Chapters 4-10). Second, further estimations are conducted in Chapter 11 using an ITSUR systems approach.

These analyses yield the following important observations. Firstly the role of corruption in the allocation of the public budget is prominent in a number of functional categories. Most significantly, countries with lower levels of corruption tend to allocate larger shares of their budgets to the education, health and social welfare categories, while those that are corrupt tend to allocate a larger share of their budgets to defence and general public services categories.

Secondly, political stability is also shown to be important in determining public budget allocations across all the different categories. High levels of instability are

found to result in budget allocations that are biased towards general public services and defence, while greater stability are associated with higher allocations to education, health, social welfare and economic services.

Thirdly, improving the level of democracy in a country as reflected in the significance of the voice and accountability index, is found to improve the allocation of budget resources to the social and economic expenditure categories at the expense of defence spending.

Fourthly, the example set by neighbouring countries in their expenditure on defence plays an important role in the allocation of budget expenditure to defence. Large allocations to defence then cause further heightening of tension rather than ensuring peace in the region.

Fifthly, the role of IMF programmes is instrumental in the budget allocation process. Countries that have implemented IMF programmes tend to allocate fewer resources to defence and instead devote more to social and economic categories.

These findings about the role of corruption, political instability and lack of voice and accountability in budget allocation suggest an 'ideal' budget in which specific maximum shares are assigned to those spending categories that are negatively related to the governance indicators and specific minimum shares to those spending categories that are positively related to the indicators.

### **13.3 Policy recommendations**

The findings of this study suggest that fiscal policy makers should take note of the following:



Firstly, for an ideal budget allocation to be achieved in the African context, measures must be put in place to control corruption. These may include the following:

- Anti-corruption legislation: countries that have anti-corruption laws should ensure that they enforce these laws.
- Public officers' ethics law: countries that have not legislated about codes of ethics for public officials are recommended to do so. Such laws should *inter alia* require public officers to declare their wealth and disclose any interests that they may have in private investments and their links with government.
- Anti-corruption institutions such as parliamentary committees on public finance and investment: these must be strengthened if they exist and established where they are lacking. Such institutions must be entrenched in the constitutions of their countries.

Secondly, to ensure optimal public choice, reflecting the preferences of citizens, governments should ensure that political stability is a high priority on its development agenda. Governments can address instability by establishing early warning systems so that they can address any problems before they degenerate into civil unrest and war. This may involve bringing together all the parties involved in a conflict in order to dialogue. At the continental level, peace efforts under the African Union (AU) should be encouraged to ensure that problems on the continent can be resolved by leaders without recourse to outside support.

Thirdly, voice and accountability must be held vital in internal budget allocation. Governments must embrace true accountability to citizens, being simultaneously transparent and informed about collective and individual needs. This can be achieved through:

- Openness with regard to fiscal policies;
- Establishment of information and communication offices where anyone seeking information about public matters can find assistance; and

- Provision of retraining for police and other security personnel on matters related to public relations, since in Africa many offences against human rights are committed by police.

Fourthly, in the spirit of greater economic and political integration, ideal budget allocation criteria must be devised to measure the extent of fiscal convergence of the member countries of existing regional blocs.

### **13.3 Limitations of the study**

Although the objectives of this study were achieved, the research was constrained by the following limitations.

Firstly, although an attempt was made to obtain data for as many countries as possible, the required data could not be found for all the countries in Africa. Aggravating this problem, even for those countries for which data could be obtained, often time series were not sufficiently long for rigorous panel econometrics. For example, due to the short time nature of the data, it was not possible to conduct panel cointegration estimations.

Secondly, the data used in this study to proxy corruption, political instability and accountability have been compiled using highly subjective methods. Bias arising from the data collected may have influenced the results substantially.

### **13.4 Suggestions for future studies**

Future research on this topic could focus on the following outstanding issues:

- The impact on the structure of the public budget of changes in the tax rate and base, which in this study are assumed to be stable, could be investigated, since it is possible that expenditure priorities change with

- changing levels of tax rate and base. Furthermore, such an analysis could focus on the sensitivity of expenditure priorities to changes in the tax base.
- The link between expenditure priorities and their socio-economic outcomes could be studied. While this study focuses on the role of governance in the priorities of government expenditure, it does not attempt to link priorities with the efficiency (cost-benefit) of these expenditures. Future research could explore whether these priorities impact positively or negatively on, for example, enrolment rates, literacy, infant mortality rate and life expectancy.
  - The ballooning effect of corruption on the size of the budget requires further exploration. In this study the ways in which governance indicators such as corruption impact on the size of the public budget are not explicitly investigated. The possibility should be explored of using frameworks which endogenise total government expenditure in a model so that the effect of high levels of corruption on the total budget (the ballooning effect) is investigated.
  - Governance indicators should be endogenised. Instead of treating corruption, political stability and human rights only as exogenous, further studies should endogenise these variables since, for example, endogenising corruption may unveil the factors that cause corruption in the public sector and show how these factors can be linked indirectly to the structure of the public budget.
  - Expenditure priorities should be linked to macroeconomic outcomes. Theoretical and empirical evidence link optimal budget allocation to desirable macroeconomic outcomes. However, this approach was not followed in this study, as it was not part of the objectives. Due to the importance of the role of optimal budget allocation in macroeconomic performance, research could empirically test the role of budget allocation on macroeconomic outcomes in Africa.
  - Lastly, when data becomes available, researchers interested in this area should conduct more analyses within the panel econometrics framework.

This includes *inter alia* panel analysis using a two-way error component model; dynamic panel data models; testing for panel unit roots; and cointegration analysis. These analyses would validate the findings of this research.