Ebony Center for Strategic Studies
ECSS
'Advancing critical thinking and innovation'
Customs Road, Zain Building Opp MTN, Juba - South Sudan
Tel: +211-954-090977
Email: ajakbol@ebonycenter.org
www.ebonycenter.org

Challenges and Opportunities for Fiscal Space in the FY2017/2018 Budget of Government of South Sudan

A paper prepared by Lual A. Deng[1] for DPF/TAF Event

24 February 2018
Quality Hotel

Abstract: The fundamental challenge for fiscal space in the FY2017/2018 budget of the Transitional Government of National Unity (TGoNU) of the Republic of South Sudan is the inherent indiscipline in the management of approved budgets. One of the root causes of this indiscipline is the lack of effective oversight from the legislative branch of government. The paper reviews the government's share of oil revenues during the first half of FY2017/2018 to show that there was a fiscal space during this period emanating from improved oil production and rising oil prices than the budgetary benchmarks. However, indiscipline in budgetary execution has not allowed TGoNU to make use of this opportunity. The paper, therefore, calls for enhanced oversight of the budgetary process through the establishment of a transparency and accountability forum (TAF) that will include all the stakeholders.

[1] Managing Director and founder of Ebony Center for Strategic Studies, Juba, South Sudan

I. The Context

…. we are reaping the fruits of indiscipline in years when our oil revenues were plentiful. Instead of moderating our expenditure and building up savings, we spent all that we had and more. We also neglected to develop our capacity to mobilize non-oil revenues. Hon. Stephen Dhieu Dau (2017)[2]

My choice of the above passage from the budget speech of the Minister of Finance and Planning (MoFP) is to convey the underlying pain a professional minister goes through when trying to explain how an economy – any economy, developed or developing – operates. In the context of South Sudan's economic policy management, one would think that John Maynard Keynes was addressing South Sudanese policymakers when he concluded:

We have involved ourselves in a colossal muddle, having blundered in the control of a delicate machine, the working of which we do not understand. The result is that our possibilities of wealth may run to waste for a time—perhaps for a long time[3].

There is almost a century (87 years to be exact) between the dates, the above two cited passages were made. Keynes was describing the underlined lack of understanding of the Great Slump of the 1930s, while Minister Dau was telling the legislative branch of our government about fiscal indiscipline as one of the drivers of economic crisis in 2017 in South Sudan. The two passages are complementary in their messaging. They are emphasizing the importance of sound economic policy in the process of wealth creation of nations. In this regard, South Sudan in her quest for wealth creation must guard against greed and selfishness on the one hand, and ignorance and arrogance on the other. This, however, assumes that there are efficient institutions of economic governance that would in turn ensure coherent public policy. That is, in an environment of weak institutions, predatory behaviors flourish. This would become apparent, in the case of South Sudan, when looking at some of the detrimental decisions made by our policymakers in the recent past.

South Sudan's economy is currently under a severe stress, precisely because we have embarked, since independence, on a path of political recklessness as illustrated by voluntary shutdown of oil production in January 2012. We are indeed reaping, to paraphrase Minister Dau, the fruits of our own political recklessness, evidenced by:

---

[2] From the FY2017/2018 Budget Speech to the Transitional National Legislature by Hon. Stephen Dhieu Dau, minister of Finance and Planning, TGoNU

[3]John Maynard Keynes, "The Great Slump of 1930," *The Nation &Athenæum*1 (December 1930): 1

a) Continued violent conflict that erupted on December 15, 2013**;**
b) High fiscal deficits; and
c) Triple digit inflation rate that has eroded the purchasing power of most ordinary citizens.

The purpose of this paper is to highlight some of the key challenges and opportunities for fiscal space in the financial year 2017/2018. I do this by first providing in Section Two of the paper, the meaning of fiscal space and illustrate it by using the approved FY2017/2018 budget. I then highlight in Section Three the challenges facing the execution of the FY2017/2018 budget and this is followed by opportunities in Section Four. Section Five concludes the paper.

II. Understanding Fiscal Space within the Framework of FY2017/2018

The point of departure here is to seek a common understanding of the fiscal space. In this regard, I would turn to Peter Heller who defines fiscal space as a:

… room in a government's budget that allows it to provide resources for a desired purpose without jeopardizing the sustainability of its financial position or the stability of the economy[4].

I would define fiscal space in the context of South Sudan as a windfall that occurs during the budget execution and which does not get reflected in the budget equation. For example, an increase in either oil prices or production will generate more revenues for the GRSS, which were not anticipated at the time of budget preparation. Table 1 below gives the benchmarks used in the preparation of the FY2017/2018 budget. These are compared to actual values/levels (e.g. changes in oil prices and daily production) that are obtained during the implementation of the budget. The key assumption of the framework for fiscal space is to hold constant the total public expenditure, while allowing variations on the revenue side of the budget equation.

Table 1: A Framework for Fiscal Space In FY2017/2018 Budget

Variable	**Benchmark**	**Actual**	**Comments**
1. Oil production	**110,000** bbl./day Or **3,300,000** barrels/month or **39.6** million barrels for FY2017/2018	**127,000** bbl./day Or **3,810,000** barrels per month or **45,720,000** barrels for FY2017/2018	There is an increase of **17,000** bbl./day, which provides an important fiscal space that was not foreseen during the budget preparation
2. Price of Dar Crude	**$45**/bbl. of which Sudan takes **$24.1**/bbl. in lieu of transport, transit, & processing fees of	**$54.19**/bbl. during the first half of FY2017/2018 and of which Sudan takes **$24.1**/bbl. in lieu of	An increase of oil price by **$9.19**/bbl. gives additional revenues to the budget that was not foreseen

[4] See **Back to Basics** -- Fiscal Space: What It Is and How to Get It, by Peter Heller, Finance and Development, A Quarterly Magazine of the IMF, **June 2005, Volume 42, Number 2**

	$9.1/bbl. and **TFA** of **$15**/bbl.	transport, transit, & processing fees of **$9.1**/bbl. and **TFA** of **$15**/bbl. The price for the second half of FY2017/2018 is on average likely to be **$65/** barrel.	at the time of budget preparation. Moreover, the government should renegotiate the transitional financial arrangement/assistance (**TFA**) of **$15/barrel** being exported through Sudan and which was agreed upon at the time South Sudan was relatively better off compared to Sudan. South Sudan is now facing economic crisis and it would be mutually beneficial if the TFA were cancelled
3. Exchange Rate	**SSP155/$1.0**	**SSP165/$1.**0	Depreciation of the SSP against the US dollar by 6.5%; increases, other things remaining the same, the nominal income (i.e. oil revenues of the government, which are denominated in dollar) by the same percentage. It is, however, inflationary and reduces the purchasing power of those people with fixed income, since inflation-adjusted income and cost-inflation index are not used in South Sudan
4. GRSS share of oil production in barrels per day	42% of **110,000** bbl./day is equal to **46,200** barrels of which Sudan takes **28,000** bbl./day, leaving **18,200** bbl./day for GRSS. That means Sudan gets **60.6%** of GRSS' share of oil	54% of **127,000** barrels per day is equal to **68,580** barrels per day of which Sudan takes **28,000** bbl./day and **40,580** bbl./day for GRSS. That means Sudan gets **40.8%** of	There is a positive correlation between oil production and government-take (i.e. share in profit-oil). That is, whenever oil production declines, cost-oil increases (or profit-oil declines) bearing in minds that government-take is

	revenues, which is worse than **49%** under the CPA. The oil revenue sharing formula stipulated in the Wealth Sharing Protocol of CPA talks of **50/50** after **2%** payment to the oil producing States, which means it is **98%** that is being divided **50/50** and hence my assertion of **49%** to GONU and **49%** to GoSS.	GRSS' share of oil revenues, which is closer to **49%** under the CPA.	from the profit-oil. Hence, an increase of **12%** in the share of oil revenues for the government is a significant enhancement in the fiscal space, especially if used wisely.
5. GRSS share of oil revenues in FY2017/2018 budget	a) Gross oil revenues in FY2017/2018: **$820,851,613 or SSP127.232 billion for FY2017/2018** b) Payment to Sudan in FY2017/2018: **$453,600,000** c) Payment to Nilepet and suppliers of refined products in FY2017/2018: **$182,625,806** d) Payment to oil producing States & communities in FY2017/2018: **$18,361,290** e) Net oil revenues for GRSS to finance FY2017/2018: **$166,264,517 or SSP25.771 billion**	a) Gross oil revenues in FY2017/2018: **$1,471,452,480** b) Payment to Sudan in FY2017/2018: **$595,000,080** **c)** Payment to Nilepet and suppliers of refined products in FY2017/2018: **$182,625,806** d) Payment to oil producing States & communities in FY2017/2018: **$73,572,624** e) Net oil revenues for GRSS to finance FY2017/2018: **$620,253,970 or SSP96.14 billion**	i) When the benchmark price is **$45**/bbl. and daily production as **110,000** bbl./day, then Sudan takes **55.3%** of GRSS share of oil revenues due to the infamous TFA of **$15/b**bl., which is a huge burden on the fiscal sustainability of our budget. Arrogance and ignorance have not allowed the GRSS to assemble South Sudanese with experience and scarce skills to renegotiate the TFA. ii) Fuel subsidy takes **22.25%** of the total oil revenues for GRSS in FY2017/2018 when the benchmark price is **$45**/bbl. and daily production as **110,000** bbl./day iii) With improved oil production and prices, GRSS should be able to fully finance FY2017/2018 from its

			net oil revenues and will still have **$319.6** million to finance arrears and service the debt
6. Total Expenditure	FY2017/2018: **46.6** billion South Sudanese pounds or **$300,600,000**	FY2017/2018: **49.6** billion South Sudanese pounds or **$300,600,000**	This should be constant throughout the FY2017/2018 if no adjustments are made to the wage bill or change in the benchmarks setout in the budget
7. Financing gap/surplus if FY2017/2018 is funded only through net oil revenues	**There is a gap of $134,335,483 or SSP20.822 billion, which is closed through a combination of financing packages given under variable (parameter) 8 below**	There is estimated surplus of **$319,653,970**	GRSS could then improve the purchasing power of public sector employees without necessarily undermining its fiscal sustainability and macroeconomic stability. This could be done through the dollarization of the wage bill
8. Balancing the FY2017/2018 budget	a) Non-oil revenues of GRSS: **$90,967,742** or **SSP14.**1 billion b) External grants: **$2,645,161** or **SSP410** million c) External project loans: **$14,193,548** or **SSP2.2** billion d) Treasury Bills: **$4,468,085** or **SSP840** million e) Advanced oil Sales: **$22,060,947** or **SSP3.42** billion	a) Non-oil revenues of GRSS: **$90,967,742** or **SSP14.**1 billion b) External grants: **$2,645,161** or **SSP410** million c) External project loans: **$14,193,548** or **SSP2.2** billion d) Treasury Bills: **$4,468,085** or **SSP840** million e) Advanced oil Sales: **$22,060,947** or **SSP3.42** billion	GRSS should keep these budgetary items/variables as given in the approved budget (i.e. constant). The room for maneuver should be through the oil windfall

Source: **Constructed by the author from information contained in the Budget Speech of the Minister of Finance and from data provided by the Crude Oil Marketing Committee, Ministry of Petroleum, GRSS**

The analytical framework for fiscal space in the FY2017/2018 budget gives about $320 million, which GRSS could use to achieve desirable policy objectives "without jeopardizing the sustainability of its financial position or the stability of the economy" (Peter Heller, 2005). This would not be possible, however, given the nature and magnitude of indiscipline in the execution of the budget.

III. The Challenges Underpinning the Implementation of FY2017/2018 Budget

There are numerous challenges facing the fiscal space in FYI2017/2018, but I have chosen only four key ones. These are:

a) Ending the war and reaching peace agreement;

b) Indiscipline in the management of the approved budget;

c) Managing the exchange rate (ER) regime; and

d) Reorienting humanitarian assistance toward food security, livelihoods, and economic recovery.

3.1 Ending the current violence is imperative for fiscal sustainability and economic recovery

According to the World Bank, the security sector in South Sudan takes 60% of the total annual expenditure of the GRSS[5]. This is absolutely not fiscally sustainable, for it undermines our quest for sustained peace, economic growth, and poverty eradication. Moreover, preliminary findings of a research project the Ebony Center is conducting with funding from the African Economic Research Consortium (AERC) shows that:

The process of capital (physical, human, and social) formation in South Sudan has been undermined by the current civil war that broke out in December 2013. Stated differently, violence has affected investment in public goods, such as roads, electricity, education, public health, water/ sanitation, security[6], and so forth. It has consequently resulted in low private investment on the one hand, and reduced social interaction on the other. Social capital has been eroded and mistrust has risen among communities that used to coexist peacefully.[7]

Ending the war is, therefore, a necessary, though not a sufficient condition in ensuring fiscal sustainability in the Republic of South Sudan.

3.2 Indiscipline in the management of the approved budget

This challenge is at the core of the public financial management (PFM) in the Republic of South Sudan. I would once more turn to the Minister of Finance to give an insider view of some of the difficulties facing the execution of the budget:

Rt. Hon. Speaker, indiscipline is still a feature of our budget management. We have

---

[5] See Country Engagement Note (CEN) for the Republic of South Sudan, Report No. 120369-SS of The World Bank published on 7 November 2017

[6] It is paradoxical to say that resources have been geared toward the security sector, yet there is high level of insecurity in the country!

[7] See **Identifying Binding Constraints on Growth in the Context of Fragility: The Case of South Sudan**. A collaborative Research Project funded by AERC

weak procurement practices, expenditures are poorly prioritized, and some agencies are able to disregard their budget while others receive nothing. The costs of indiscipline are immediate and real. When scarce resources are diverted to unplanned operating expenditures, we cannot pay salary and wages to about half a million employees on the government payroll.[8]

Salaries for November 2017 of the members of the TNLA are being paid now (mid-February 2018). This is at the time when GRSS should have about $150 million as windfall from half-year oil revenues that were not anticipated at the time of the approval of FY2017/2018 budget. If the salaries of members of the National Legislature were three months behind (i.e. in arrears) what would be the situation for other spending units, including the states, counties, and Payams? But, what evidence do we need more than what the Minister of Finance has provided in the above passage?

3.3 Managing the exchange rate (ER) regime

Monetary authorities in South Sudan have not been able to provide professional leadership in this area. The economy of South Sudan is highly dollarized[9] and yet the Central Bank of South Sudan (BSS/BoSS) would seem not to be taking into account this reality. In fact, ordinary economic agents have understood how a dollarized economy operates and have subsequently adopted measures to protect their assets from a volatile exchange rate regime, which is driving triple double budget inflation that is eroding the purchasing power of ordinary citizens. Hence, management of the exchange rate regime continues to be one of the key challenges facing the implementation of the approved FY2017/2018 budget.

3.4 Reorienting humanitarian assistance toward food security, livelihoods, and economic recovery

About two-thirds (63.8%) of the population of South Sudan is food insecure[10]. I have excluded, in calculating the percentage of food insecure, Internally Displaced Persons (IDPs – 1.9 million persons) and refugees (2.4 million people), from the total population of South Sudan, which is estimated to be 12.3 million people. The UN agencies and Non-governmental Organizations (NGOs) provide “life-saving food assistance and emergency livelihoods support to 5.1 million South Sudanese[11]” or 63.8% of the total population. The humanitarian relief supplies are not taxed and therefore reduce the amount of non-oil revenues to GRSS that would have accrued to the treasury. Hence, the challenge here is how to redirect humanitarian assistance toward food security, livelihoods, and recovery.

IV Opportunity For Fiscal Space in the FY2017/2018

I highlight the following opportunities:

---

[8] From the FY2017/2018 Budget Speech to the Transitional National Legislature by Hon. Stephen Dhieu Dau, minister of Finance and Planning, TGoNU

[9] For farther analysis, see Protecting Purchasing Power From Skyrocketing Prices In South Sudan Through Partial Dollarization, by Lual A. Deng (2016)

[10] See Humanitarian Bulletin. Issue No. 02 of February 20, 2018

[11] Ditto

a) IGAD-High Level Revitalization Forum (HLRF);
b) Enhanced Transparency and Accountability; and
c) Improved Oil Production and Prices.

4.1 The HLRF

The high-level revitalization forum provides an opportunity to take urgent measures to immediately restore macroeconomic stability. That is, a revitalized Agreement on the Resolution of Conflict in the Republic of South Sudan (ARCISS/ARCSS) would create, other things being equal, a binding constraint on GRSS' expenditures in general, and security sector spending in particular. Holding security sector spending at the FY2017/2018 budget level would create a fiscal space for reducing fiscal deficit, which would in turn lead to stabilizing the exchange rate on the one hand, and to lowering the triple digit inflation on the other.

But, a revitalized HLRF will definitely enable the economic agents, especially the households, to reverse the findings of the Ebony Center's AERC funded research project, which concludes that:

V***iolence affects private investment … through low returns to economic activity, which in turn discourages both saving and investment. This is due to the fact that the GRSS (or TGoNU) is fighting various armed groups in the countryside. Both GRSS/TGoNU and rebels compete over household resources (e.g. labor, land, and livestock), especially in the rural areas, for use in the power struggle among the elites, a struggle that is underpinned by violence. In such an environment, the government's role of protecting household savings, labor, and property (e.g. livestock and farm land) and combating corruption had taken a backseat***[12].

I would, therefore, argue in the light of the above findings that peace is both a necessary and sufficient condition for embarking on path to economic recovery. The non-oil revenues of GRSS would then be increased as taxable economic activity returns to normalcy. Moreover, peace dividends would have additional positive multiplier effects on the proximate determinants of growth – saving, investment, education, productivity, and infrastructure.

4.2 Enhanced Transparency and Accountability in the Management of Oil Revenues

Transparent and accountable management of oil revenues would in turn help in formulating a strategy for sustained peace, economic growth, and poverty eradication. Moreover, the Minister of Finance would be able to achieve what he had expressed below in his budget speech to the Transitional National Legislature:

Rt. Hon. Speaker, we are continuing with reforms. Although they are painful, and will meet resistance, there is no other way. Without reforms, we will not place our country on the road to prosperity, towards fulfilling the hope that many people had for South Sudan at independence. With the help of this House, I believe there are a number of initiatives we can implement in the coming fiscal year to lay the

[12] See **Identifying Binding Constraints on Growth in the Context of Fragility: The Case of South Sudan**. A collaborative Research Project funded by AERC

foundations for stronger budget management and greater fiscal sustainability. These measures build on the Economic and Fiscal Stabilization and Recovery Action Plan that I submitted to you last year[13].

4.3 Improved Oil Production and Prices

I have discussed in Section Two of this paper the assumptions on which the FY2017/2018 budget was based. There have been increases of 27% and 20.4% in production and price of the Dar crude, respectively. Such a windfall should have created sufficient fiscal space for GRSS to, at least, pay salaries and wages of public sector employees. This is not the case, however, for the GRSS is in arrears ranging from three to six months of non-payment of salaries and wages. We do not need to go far to find the answer to the inability of the GRSS to effectively and efficiently utilize the windfall generated by improved oil production and prices. It is the inherent indiscipline in the management of the approved budget as, once more, illustrated by the Minister of Finance:

Rt. Hon. Speaker, this fiscal year, I introduced measures to limit non-priority operating expenditures and improve our cash management. I established a Cash Management Committee, I cancelled outstanding cheques, I closed Government bank accounts held in commercial banks, and I placed limits on medical and travel claims. In doing so, I encountered considerable resistance from a number of quarters. Although everyone complains about the current economic situation, few people want to accept economic stabilization reforms that will limit their own individual opportunity to access State resources[14].

V. Conclusion

I have identified in this paper four challenges and three opportunities for a fiscal space in the FY2017/2018 approved budget of the GRSS. Indiscipline in the management of approved budgets is the fundamental challenge that policymakers in South Sudan must address with urgency if they were to achieve the triple objectives of sustained peace, economic growth, and poverty eradication. The first half of the FY2017/2018 witnessed a windfall from oil revenues to the tune of $150 million, which was not anticipated at the time of the budget approval. Yet, GRSS continues to face difficulties in paying salaries and wages to its employees. This is because in the words of the Minister of Finance, "few people want to accept economic stabilization reforms that will limit their own individual opportunity to access State resources." The Minister was essentially appealing to the National Legislature to exercise its oversight function.

I would, therefore, recommend in the light of the inherent indiscipline in the management of our financial resources and the failure of the legislature to exercise its oversight function, that a Transparency and Accountability Forum (TAF) be established. The main purpose of TAF is to ensure the integrity and credibility of the budgeting process – preparation and execution. The TAF membership should include all the stakeholders, such as the civil society and the development partners.

---

[13] From the FY2017/2018 Budget Speech to the Transitional National Legislature by Hon. Stephen Dhieu Dau, minister of Finance and Planning, TGoNU

[14] Ditto

1-Since the total shut down in oil production in Jan. 2012, at a time when there was nothing put aside for rainy days, subsequent RSS national budgets have always catered for core government functions only. This basically meant catering for salaries and minimum operating allocations at the national level, and seriously compromised state transfers. The whole idea being to guarantee security and rule of law. So no allocations for capital expenditure (infrastructure, creation of public goods, general welfare promotion or maintenance, etc). Yet these budgets in themselves have always carried deficits i.e. shortfalls to cover CORE government functions. I think this is quite consistent with the definition of fiscal or budgetary deficit provided in the presentation.

2-All things said and done, the presentation has identified a problem, and a solution. Merging the problem with the suggested solution, is where the fireworks begin, in my view. As mentioned, the problem is INHERENT indiscipline. The word inherent can also mean in-built, deep rooted, fundamental, etc. This being the case, it means the problem is quite pervasive and runs right across the board. Issues of deficits in capacity, rule of law, requisite mental attitudes, bringing on board the sense of impunity, all come to bear.

3- By all means the TNLA comes to mind as a major culprit to blame for lack of effective oversight. But by doing so are we not deflecting the blame from other perpetrators of fiscal indiscipline, allowing them to take a back seat as the TNLA bears the brunt of the blame?

4- The suggested solution is also problematic. To put it bluntly, it is like replacing a poorly functioning system with one that does not work at all.