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

Reducing the Resource Gap in the FY2019/2020 Proposed Budget Through Transparency and Accountability in the Management of Oil Revenues

(Draft for discussion)

By Lual A Deng[1]

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Abstract: The FY2019/2020 draft budget of the Government of Republic of South Sudan (GRSS), which is going through various stages of parliamentary reading at the Transitional National Legislature (TNL), has a huge resource gap of **SSP77 billion (or USD497 million**)! The central premise of this paper is that this gap could be reduced significantly through innovative approaches within the overall framework for transparent and accountable management of GRSS' share of oil revenues.

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[1] Managing Director of Ebony Center for Strategic Studies and member of the Transitional National Legislative Assembly (TNLA)

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I. Introduction

> ***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*[2].**

I consider budgeting of any kind and by any entity to be a process of wealth creation. In this sense, the public budget, which is about how resources of the country are mobilized and allocated by the government on behalf of the people to achieve desired public goods, is essentially a mirror of the social, political, and economic choices of the society. Budgeting is one of the four main components of the budget cycle. The other three components are: a) budget execution; b) monitoring, reporting, and auditing; and c) planning. Moreover, the government (i.e. state) finances its budget through taxes collected on the various economic activities in an economy. That is, the people are themselves the taxpayers who hold, through their elected representatives, the government accountable in the efficient management of these taxes. Hence, the popular phrase of "taxpayers money" we often hear in the politics of "matured democracies!"

The FY2019/2020 draft budget of the Government of Republic of South Sudan (GRSS) at the time of writing of this paper is going through the second reading before the Transitional National Legislature (TNL). The key characteristic of this budget is the huge resource gap of **SSP77 billion (or USD497 million at the exchange rate of SSP155/USD1.0 as stipulated in the budget speech of the Minister of Finance and Planning).** The gap constitutes 37% of the proposed FY2019/2020 budget. It is not normal, to the best of my knowledge, for an executive branch of government to present to the legislature a budget with such a huge resource gap without reasonable explanation on how to finance it. I would, therefore, venture into unpacking the abnormal nature of the decision of the executive or Council of Ministers (CoM) in presenting the FY2019/2020 proposed budget to the TNL as is!

The quoted passage, from some of my earlier analyses of previous budgets of GRSS, at the beginning of this section of the paper would provide partial explanation. It would seem to me that the "invisible hands" of greed & selfishness driven partly by forces of ignorance and arrogance have finally punched this huge hole in our treasury. Or what the Americans would say, this is "pouring our assets down the rat hole" of unproductive government spending!" This explanation would be complete, in my

[2] From "**Challenges and Opportunities for Fiscal Space in the FY2017/2018 Budget of Government of South Sudan**", a paper presented by Lual A Deng to the DPF/TAF discourse on 24 February 2018

view, if we make use of the scholarly work of Daniel Akec Thiong[3] on the "politics of fear," Majak D'Agoôt's[4] "gun class," and Alex de Waal's[5] kleptocracy. The Nuer concept of "*Hakuma mitoat*[6]," would also add value to our search for full explanatory variables of pervasive budgetary indiscipline in South Sudan.

The rest of the paper is divided into three sections. Chapter 2 provides a point of entry on how a budget is prepared. Chapter 3 is the analysis of the share of GRSS in the total oil revenues and Chapter 4 concludes the paper.

II. Understanding the Budget Cycle

A budget is an estimation of government's revenues and spending in a given period of time, which is usually 12 months. It has four phases of preparation, which determine the integrity and credibility of the budget process. The financial/fiscal year (FY) for GRSS runs from July 1st to June 30th. For instance, the FY2019/2020 is from 1 July 2019 to 30 June 2020. Other countries, such as Sudan do base their FYs on a calendar year (i.e. from January 1 through December 31). I use a modified Figure 1 below from: **A Handbook for the National Budget Planning and Preparation Process**, of the Ministry of Finance and Planning (MoFP), GRSS to briefly explain the budget cycle. This would help in understanding the budget process.

2.1 Phases of the budget cycle

The integrity of the budget is a function of the inherent fiscal discipline embedded in all its four phases. Most governments in the world derive their revenues from taxes, which they in turn spend to meet citizens' social, political, and economic choices. There are normally four types/sources of tax revenues: a) payroll taxes, which constitute about 36% of total resource envelope; b) individual income taxes, constituting half (50%) of total revenue; c) corporate income taxes (6%); and d) other taxes (e.g. excise taxes, estate & gift taxes, custom duties, remittances from central bank, miscellaneous fees and fines), which contributes about 8% of the total tax revenues of a country, such as the United States of America[7].

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3 Thiong, Daniel Akech. 2018. "How The Politics Of Fear Generated Chaos In South Sudan." African Affairs, 1–23. Published by Oxford University Press on behalf of Royal African Society.

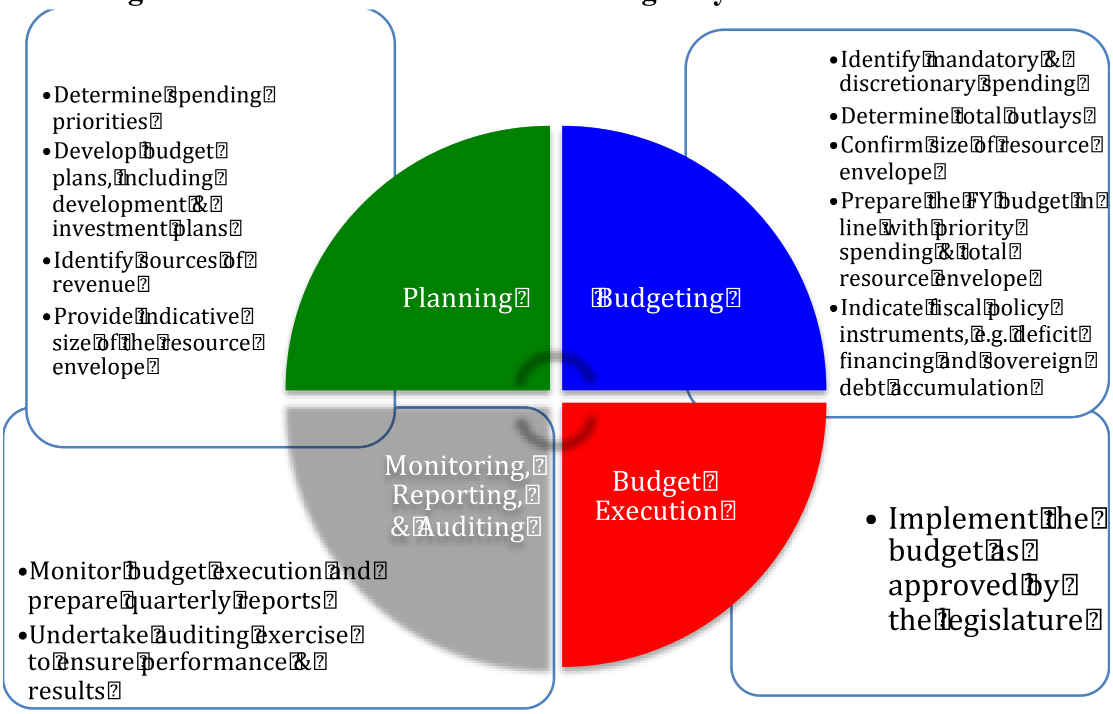
4 "Taming the Dominant Gun Class in South Sudan." SPECIAL REPORT NO. 4: ENVISIONING A STABLE SOUTH SUDAN (May 29, 2018). See https://africacenter.org/spotlight/taming-the-dominant-gun-class-in-south-sudan/

5 De Waal, Alex. 2014. "When Kleptocracy Becomes Insolvent: Brute Causes of The Civil War In South Sudan." African Affairs, 113/452, 347–369. Published by Oxford University Press on behalf of Royal African Society

6 A government managed by a small group of smart individuals who understand themselves perfectly and who have decided to use public resources for their own individual and collective welfare without regard to the rest of the society

7 I derived these percentages from 2018 Federal Budget of the United States of America

Figure One: Schematic View of the Budget Cycle



There are, however, countries with natural resource endowments (e.g. oil) that derive larger percentage of their total revenues from state-owned businesses. South Sudan falls in this category of countries. The share of oil revenues in the GRSS' resource envelope for FY2019/2020 draft budget is about 78%. It is, therefore, imperative that a robust system of transparency and accountability is put in place to manage the oil and gas sector of the South Sudanese economy. But, let us first briefly look at each of the phases of the budget cycle.

2.1.1 Planning phase

This is the first and critical phase in which priority areas for spending are determined within the overall public policy objectives of the government of the day. For instance, the overarching objectives of the FY2019/2020 draft budget are to consolidate peace and stabilize the economy. Budget planners are, therefore, expected to have had identified spending priorities with respect to consolidating peace on the one hand, and stabilizing the economy on the other. Spending priorities toward achieving these two objectives would be interlinked and reinforcing each other given their nature of being pre-conditions for sustainable peace, economic growth, and poverty eradication.

The Revitalized Agreement on the Resolution of Conflict in the Republic of South Sudan (R-ARCSS) is an important framework for identifying spending priorities, which would in turn constitute, in my view, what is called "**mandatory**

spending." There is no, to the best of my knowledge, classification of the budget outlays of GRSS into **mandatory and discretionary spending**. There is now an opportunity, in my view, to introduce such a system in the light of R-ARCSS. I would use the agreement to identify what I think to be mandatory spending in the context of consolidating peace, which is a precondition for macroeconomic stability and delivery of basic services by the South Sudanese State. I present in Table 1 below the priority areas for mandatory spending, which could have guided the preparation (i.e. phase 2) of the FY2019/2020 draft budget.

Table 1: Suggested Priority Areas for Mandatory Spending in R-ARCSS

Chapter of R-ARCSS	**Priority Area for Mandatory Spending**
1. R-TGoNU	a) Expanded presidency b) Expanded Cabinet c) Expanded Transitional National Legislative Assembly (TNLA)
2. Permanent Ceasefire & Transitional Security Arrangement	a) Establishment of Cantonment/Assembly areas b) Reunification of forces c) DDR
3. Humanitarian Assistance & Reconstruction	a) Returning, Resettlement, Rehabilitation, Relief, & Re-integration (5Rs) of refugees, IDPs, & POCs b) Special Reconstruction Fund (SRF)
4. Resource, Economic and Financial Management Arrangements	a) Institutional Reform b) Fiscal and Financial Allocation Monitoring Commission (FFAMC) c) Economic and Financial Management Authority (EFMA)
5. Transitional Justice, Accountability, Reconciliation & Healing	a) Commission for Truth, Reconciliation and Healing (CTRH) b) Hybrid Court for South Sudan (HCSS)
6. Parameters for Permanent Constitution	**Discretionary spending**
7. JMEC	Funded by donors
8. Procedures for the amendment of R-ARCSS	**Discretionary spending (if any)**

The second overarching objective is to stabilize the economy. There are two critical spending priorities in the FY2019/2020 proposed budget. These are provision of basic services (e.g. education, health, water, rule of law) and infrastructure. Provision of basic services is premised on efficient and effective institutions that are managed by highly motivated and relatively well-remunerated employees. Wages and salaries of the public sector will have to be reviewed with the aim of improving the conditions of employees in this critical area of spending. As for infrastructure, the

President has already identified roads and bridges as a top spending priority area in the FY2019/2020 draft budget. This is known as the capital budget or expenditure in the annual budget of a government. The budget planners must implement the directives of the President with respect to the infrastructure development within the framework of a medium-term strategy.

I would like to point out at this juncture that spending on infrastructure, which is an integral part of capital budget, is normally spread over a medium-term period of say, three years. Hence, the most appropriate tool that the budget planners could use is Public Investment Program (PIP). This is especially relevant in the context of South Sudan National Development Strategy (July 2018 – June 2021). That is, the PIP is a critical instrument for determining spending priorities in the context of capital budget in which a certain rate of economic growth of the economy is targeted. A good example is the planned 400-kilometer highway to be constructed by a Chinese company and for which USD 602.3 million is being squeezed out of a single financial year. This should not be the case, given other competing priorities brought about by R-ARCSS. Moreover, the Chinese construction company cannot complete the planned highway in the FY2019/2020. Evidence-based planning is imperative here.

The conventional way of planning for capital budgeting is to look at the level of investment in the economy against desired rate of economic growth. This relationship is captured by capital-output ratio, which is the amount of capital required to produce a unit of output. The most important factor here is the productivity of this capital. Hence, the starting point at the planning phase of the budget cycle is a simple equation: **I=S, which states saving and investment are equal in ex-ante as well as ex-post sense.** This simple equation should be qualified in the context of South Sudan where oil constitutes about two-thirds of the gross national product (GDP), 98% of exports, and 92.6% of total government revenues in the FY2019/2020. It is, therefore, assumed in this paper that private investment is insignificant and what matters is government capital expenditure (i.e. investment). This assumption would be relaxed as economy is stabilized and quality of data is improved.

The next step is to decide on the rate of economic growth, which I denote as **G**. This is determined by another simple equation: **G=S/V**, where **S** is the propensity to save expressed as saving-output (i.e. income) ratio or total savings in the economy as a percentage of gross domestic product (GDP). And **V** is capita-output ration, which measures the productivity of investment. For developed economies a small amount of capital is required to produce one unit of output (i.e. GDP), while for developing economies where productivity of investment is low a large amount of capital is normally required. The capital-output ratio for developed economies is now empirically established to be 3, which would normally guide budget planners in a developing economy setting.

I would, for the purposes of capital budget in the FY2019/2020, derive a capital-output ratio for South Sudan from the World Bank's Country Engagement Note on South Sudan issued in November 2017 (Annex 2 page 29). The World Bank projected then a growth rate of South Sudan's economy to be 1.2% in FY2018/19. Moreover, the average Gross Fixed Capital Formation (GFCF)[8] for South Sudan during the period 2008 – 2015 is given as 11.3% of GDP. The National Development Strategy (NDS) document (graph 1 page 37) gives an average of 10% during the period 2012 – 2015. I would use GFCF to represent saving-output ration (**S**) to get the capital-output ratio (**V)** for South Sudan. It should be stated once more that the quality of data being used here is of low quality, but they provide important trends in our analysis of the planning process.

The calculation is: **G=S/V** or **1.2=11.3/V!** Stated differently: **1.2V=11.3**, leading to **V=11.3/1.2. The capital-output ratio for South Sudan is 9.4.** Suppose the Ministry of Finance and Planning is targeting in the Fy2019/2020 draft budget an economic growth rate (**G**) of 10%. This would require investment rate (or GFCF) of: **10=S/9.4= S= 94%!** This is not realistic for investment rate to be at such a high level, but it conveys a powerful message to policymakers in South Sudan that they will have to allocate more resources toward both physical and human capitals formation in order for the country to embark on the path to sustainable peace, economic growth, and poverty eradication. The good news is that the Ministry of Finance and Planning is targeting an economic growth rate of 3.5%. Using this rate, then we get: **3.5=S/9.4 or S=3.5 x 9.4=32.9%**. A comparative look at the GFCF for Ethiopia during the period 2012 – 2015, shows an investment rate of 38% corresponding to a growth rate of 10.3% and a capital-output ratio of 3.7 or approximately 4.0.

Once spending priorities and plans for achieving them have been identified, the next step in the planning phase is to determine sources of funding. This is the stage at which tax rates could be raised and/or new taxes levied. The final point at this planning phase is to provide indicative size of the resource envelope within which the identified spending priorities and associated plans will be funded.

2.1.2 Budgeting phase

The Ministry of Finance and Planning would under ideal situation send out, at the beginning of the third quarter of the Fiscal Year (i.e. January in the case of GRSS), a circular to all the public sector spending units. The circular advises the spending units

[8] Gross fixed capital formation (GFCF) is a macroeconomic concept used in official national accounts. GFCF is a component of the expenditure on gross domestic product (GDP), and thus shows something about how much of the new value added in the economy is invested rather than consumed. It is assumed in this paper and for lack of accurate data that GFCF is equivalent to S.

to begin preparation of the new budget within given parameters. The R-ARCSS is a good example of some of the binding parameters in the FY2019/2020 draft budget. Moreover, improving the living conditions (**i.e. indexation of their salaries to protect the purchasing power of their income**) of public sector employees should have been included in the draft budget as one of key elements of mandatory spending. That is, raising wages and salaries, for instance, of the staff of our public universities should have been included in the FY2019/2020 draft budget. The CoM instead approved the raise after the draft budget was presented to the TNL! It should nevertheless be included in this year's spending priorities through supplementary budget procedures of the TNL.

The challenging policy decision to index wages and salaries of public sector employees to inflation would normally be taken at this stage of budgeting phase. That is, cost-of-living allowance (COLA) is the conventional way of indexing wages/salaries to inflation so as to protect the purchasing power of wages and salaries, in our case, of government employees during high-inflation periods. South Sudan has been through periods of high inflation since the failed attempts to realign the official and parallel market exchange rates in December 2015. There are, however, genuine practical difficulties in applying indexation of wages and salaries to what is clearly exchange rate-induced inflation. Lack of technical capacity is one of the elements underpinning such genuine difficulties in South Sudan.

I have been advocating, though in vain, for alternative type of indexation, which I believe would not only protect the purchasing power of the wages and salaries of public sector employees, but also stabilize the economy of South Sudan. This alternative is the exchange rate indexation on the argument that the economy of South Sudan is highly dollarized by IMF standard. That is, our economy is at the stage in which economic agents think in terms of United States of America dollar (USD) and prices in South Sudanese pound (SSP) are indexed to the daily SSP/USD exchange rate.

I would like to revisit the idea of indexing wages and salaries to the U.S. dollar. South Sudanese policymakers in general and members of the TNL in particular should invest time and efforts to understand when does the unofficial dollarization take place. The following long passage from Kurt Schuler could enhance such an understanding:

Unofficial dollarization often occurs in stages that correspond to the textbook functions of money as a store of value, means of payment, and unit of account. In the first stage, which economists sometimes call "asset substitution," people hold foreign bonds and deposits abroad as stores of value. They do so because they want to protect against losing wealth through inflation in the domestic currency or through the outright confiscations that some countries have made. In the second stage of unofficial dollarization, which economists sometimes call "currency substitution," people hold large amounts of foreign-currency deposits in the

domestic banking system (if permitted), and later foreign notes, both as a means of payment and as stores of value. Wages, taxes, and everyday expenses such as groceries and electric bills continue to be paid in domestic currency, but expensive items such as automobiles and houses are often paid in foreign currency. In the final stage of unofficial dollarization, people think in terms of foreign currency, and prices in domestic currency become indexed to the exchange rate[9].

How do we quantitatively measure the phenomenon of unofficial dollarization described in the passage quoted above? The literature on dollarization gives two indicators[10]: a) **share of foreign currency deposits in the money supply (or total liquidity, which includes foreign currency deposits);** and b) **share of foreign currency deposits in total bank deposits**. I assume, in the case of South Sudan economy and for ease of analysis, total money supply to be more or less equal to total bank deposits. According to the IMF (1995) an economy is considered highly dollarized if the share of foreign currency deposits in the money supply is equal to or greater than 30% and moderately dollarized if it is below 30%, but more than 16.4%. It is on the basis of these indicators that researchers have been able to determine the extent of which countries have dollarized, partially or fully (or officially and unofficially). Countries that allow a foreign currency to circulate together with a local currency are considered to be in what is called a "**bi-monetary system**!"

I have three years ago (i.e. 2016) estimated the foreign currency deposits in the money supply to be about 61.8%, which confirmed then that South Sudan economy fell within the category of economies that are highly dollarized. Such a picture has serious implications to the design, application, and management of monetary policy. This is because SSP, on which monetary policy in South Sudan is anchored on, constitutes only 32% of the money supply. That situation continues up to the time the TNL is deliberating on the FY2019/2020 draft budget.

In the light of the picture depicted in the preceding paragraphs, MoFP should have taken the issue of wage indexation into account when preparing the FY2019/2020 draft budget. This is because budgeting is the phase where the actual costing of public sector activities (capital and operating expenditures) is performed by each and every spending unit. It is ideally a process in which negotiations on respective allocations take place between the national planning authority and those responsible for the budget and planning units in all the spending agencies of the government. In some countries, agencies are given indicative figure (i.e. money to spend) within which to determine their own spending priorities. This figure is normally based on historical patterns of spending by the agencies.

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[9] See Kurt Schuler (2000): Basics of Dollarization - Global Policy Forum

[10] For more on this, see for instance - Adam Bennett (1999): Monetary Policy in Dollarized Economies; Impact of Dollarization; Kurt Schuler (2005): Some Theory and History of Dollarization; Bonga and Dhoro (2015): Currency Substitution, Dollarisation and Possibility of De-dollarisation in Zimbabwe; Myriam Quispe-Agnoli (2002): Costs and Benefits of Dollarization

The planning arm of MoFP coordinates budgeting process through various stages. Technical staff of the agencies drives the preparatory stage, while the negotiation point involves senior public sector personnel at the level of undersecretaries and agency heads. I would like to illustrate this point, for the sake of clarity for our policymakers, using the federal government budget process of the United States of America. MoFP is, with respect to budget preparation, analogous to the Office of Management and Budget (OMB) as shown in Box 1 below. I am not suggesting in anyway that the MoFP should necessarily follow the budget process of the United States of America. The example is being given as by way of explaining the process of budgeting to the general public as well as policy community in the Republic of South Sudan.

A comparative analysis of the budgeting process would be in the context of similar conditions, such as the East African countries. This paper is not, however, about comparative analysis of budgets; it is about how to reduce the huge resource gap in FY2019/2020 draft budget.

The initial drafts of the budget are subjected to the clusters of the CoM (i.e. Cabinet) to deliberate upon. The Minister of Finance and Planning would then present what I call a "pooled draft" to the CoM, which should really be around April or May of every year. Once the Cabinet approves the draft, the Minister of Finance would then table it before the Transitional National Legislature (TNL) in what is known as the First Reading. The TNL should receive the draft budget in May in order for it to be approved by June 30th! The GRSS has, since independence, never presented the budget to the TNL before June 30th. For instance, the current draft budget (i.e. FY2019/2020) was presented to the TNL on Monday 8 July 2019. The government would have shutdown if this were in other countries where it would be unconstitutional for a government to operate without approved budget or without "continuing resolution" by the TNL. But, this is South Sudan.

Box 1: The US Budget Process

The budget process lasts 18 months. Here's the schedule for the FY 2020 budget, the third one to be submitted by President Trump.

2018

- Early fall: Federal agencies submit budget requests to OMB.
- November: OMB sends its comments back to the agencies.
- December: Agencies submit the final budget request to OMB.

2019

- January: OMB submits the budget to president.
- February: President submits the budget to Congress. Trump did so in March.
- April 15: Congress prepares its Budget Resolution.
- June 10: Congress creates Appropriation Bills.
- June 30: House approves all bills and submits them to the President.
- September 30: All bills must be signed into law.

Source: https://www.thebalance.com/what-is-the-federal-budget-3306305

2.1.3 Budget execution phase

Law in the form of appropriation act governs the implementation of the approved budget. That is, the appropriation act is approved by the legislature (i.e. TNL in our case) together with the budget. In this regard, any alteration of approved budget items is a violation of law. For instance, spending units that spend more than what have been allocated to them in the approved budget; do in fact violate the appropriation act. This violation of the appropriation is known as indiscipline in the jargon of public financial management (PFM). There is, in fact, pervasive indiscipline with respect to budget execution in South Sudan. This challenge is at the core of the public financial management in the Republic of South Sudan. I would like to illustrate this point by quoting one of the courageous Ministers of Finance of South Sudan, who gave 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

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.[11]

The Minister was presenting the FY2017/2018 draft budget in August 2017. He was subsequently proven right. For instance, salaries for November 2017 of the members of the TNLA were paid in mid-February 2018. And this was at the time when GRSS had received 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 former Minister of Finance has provided in the above passage? The culture of fiscal indiscipline continues unabated.

2.1.4 Monitoring, reporting, and audit phase

This is the fourth and final phase of the budget cycle. The performance of the budget execution is assessed through quarterly reporting and annual audit reports. MoFP is required by law to send to the TNL quarterly reports on the implementation of the budget. The planning phase of the budget cycle would normally draw lessons of experience in the execution of the budget from reports generated here. But, it would seem to me that in the case of South Sudan, it is business as usual since the reports of the Auditor General (AG) of the Republic are not taken into account in the preparation of the annual budgets. Moreover, the policymakers would seem not to be interested in any system that restrain their own behavior, a point to which I turn to the former Minister of Finance for articulation:

> ***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[12].***

Minister Dau was dismissed from the Cabinet before he could complete the implementation of the FY2017/2018 at which he made the above cited passage. I am certain that people with legal training would deduce from this statement: "**In doing so,**

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

[12] Ditto

I encountered considerable resistance from a number of quarters," the people who have been instrumental in the dismissal of the minister. Resistance from a number of quarters has become another "unknown gunmen" in our Daniel Akec Thiong's "politics of fear." The quarters referred to by the Minister are the drivers of the "politics of fear" or the self-interested elites of Majak D'Agoôt's "gun-class," which is captured by the following:

> ***South Sudan's proclivity for violence and conflict and its inability to acquire institutional depth is broad and deep. In part, this is attributed to age-old militarization of all facets of life and society stretching back to slavery and colonialism. Self-interested elites have held sway because of the utility of violence. In the past, native servicemen provided military clout to the extractive colonial enterprise and plunder. Afterward, similar arrangements were utilized by the indigenes to purge the homeland from foreign occupation—particularly from Sudanese Jalaba colonialism***.[13]

2.2 A call for classification of outlays by mandatory and discretionary spending

The TNL could introduce a budget control bill that would enhance the role of the legislature in the budget process. The bill could initiate two key innovations with respect to budgeting in South Sudan, though such practices are the norms in many countries. The first is the preparation of the budget to begin on July 1, which is the very day the new fiscal year, begins. The second is the new presentation of the outlays (i.e. total expenditure) by mandatory and discretionary spending. Moreover, this new presentation could either be by spending blocks as was practiced during the time of Hon. Aggrey Tisa Sabuni when he was Minister of Finance (2013 – 2015) or into the following:

a) A Capital budget (i.e. PIP);
b) A Core Staff budget for the essential core of each government agency; and
c) Annual operating budget for programs.

I have discussed the capital budget in the planning phase section of this paper. On the core staff, the thought would be to remove core staff from any discretionary activity and lock it in as part of mandatory spending (i.e. entitlement arrangement)[14]. That is, like Social Security program in those countries that have such a system. In this way, the core staff of the government is protected. They can still be dismissed, but their salaries are not in doubt and should be paid on time. With this endowment effect in place, it would be essential to index their salaries. Then, in the operational (program) budget, GRSS could have staffing levels for those individuals necessary to

[13] "Taming the Dominant Gun Class in South Sudan." SPECIAL REPORT NO. 4: ENVISIONING A STABLE SOUTH SUDAN (May 29, 2018). See https://africacenter.org/spotlight/taming-the-dominant-gun-class-in-south-sudan/

[14] I am grateful to Prof. (emeritus) Daniel W. Bromley of the University of Wisconsin-Madison for this paragraph in which he encouraged me to be forthright with some of my ideas on how to improve the budgeting process in South Sudan

carry out specific programs and initiatives. The main purpose here is to figure out how to protect the core "civil service" employees so that they make a commitment to the government in return for a commitment to them. What is needed is their devotion and commitment to the service of the people of South Sudan. It is hard to get that when they go months without pay.

III. Transparency and Accountability: A tool for ensuring the integrity of FY2019/2020 budget

> ***Thanks for the reminder. I now remember going through this informative paper. It speaks the core of our problem, the incoherent fiscal discipline possibly birthed by unfettered access to windfalls from oil. The germane literature is littered with the evidence that governments that depend largely on natural resources for their fiscal obligations tend to be fiscally irresponsible. Natural resources are a source of free money, which the state spends as it wishes. Result? Usually poor governance. Good governance, it seems, is closely associated with taxes as a major source of state income***[15].

The FY2019/2020 draft budget indicates total outlays of **SSP208.2** billion and a resource envelope (i.e. total revenues) of **SSP131.2 billion**. The difference between the proposed total outlays and total revenues is what is being referred to here as the **resource gap**. This resource gap is equivalent to **SSP77 billion** or **USD497 million** in terms of the United States of America dollars. The challenge before us is how to close this gap. I intend, in the rest of this chapter of the paper, to show how the TNL could go about in closing or eliminating all together the gap.

3.1 Reducing the resource gap

There are usually two broad ways of closing the resource gap. The first method is to reduce planned spending with the view to realigning expenditures with revenues, so that there is a balanced budget. The other approach would be either to raise revenues through borrowing from domestic and external sources or/and to increase taxes. Borrowing from domestic sources would mainly be from the Bank of South Sudan (BoSS) through what is known as deficit financing (i.e. printing more pounds). But, it should be recalled that deficit financing is inflationary and its consequences in South Sudan have been detrimental to macroeconomic stability as well as to the living standards of the population.

3.1.1 Recalculating the allocation of GRSS' share of oil revenues

[15] From a rejoinder made by Prof. Augustino Ting Mayai of University of Juba and Sudd Institute on a thread announcing the DPF/TAF discourse on the subject of this paper

I would like to provide alternative approach to closing the resource gap in the FY2019/2020 draft budget[16]. The Minister of Petroleum together with the First Deputy Governor of Bank of South Sudan and their teams have aided this effort through credible information they provided to the Economy, Development, and Finance Committee of the TNLA[17]. I do focus on GRSS' oil revenues, which constitutes **92.6%** of total revenues (i.e. resource envelope). The share of GRSS in total oil production is derived from two types of crude oil – the Dar blend (from blocks 3 and 7) and Nile blend (from blocks 1, 2, and 4). The share of GRSS from the Dar blend is given as **44%** and from the Nile blend is **39.5%**. The share of **the Nilepet Corporation,** which is **8%,** is not part of the GRSS[18]**.**

The new facts are made use of to reduce the gap through: a) savings from the amount that have been given to Nilepet in the draft budget; b) price differential, since the Nile blend is priced at the same price of London Brent, which is higher than the budget benchmark price of USD55/bbl. for Dar blend; and c) exchange rate differential of SSP6/bbl. Table 2 below is used in the recalculation of the share of GRSS' oil revenues in the FY2019/2020 draft budget. The total oil production is given in the budget to be 170,000 barrels per day (bpd). This figure has been corrected by the Minister of Petroleum to be 173,000 bpd[19] (**130,000 from blocks 3 and 7; while 43,000 from blocks 1, 2, and 4**).

The share of GRSS from oil production in blocks 3 and 7 (i.e. the Dar blend) is, therefore, **57,200 bpd** (i.e. 0.44 x 130,000=57,200), which gives a projected total of **20,878,000 barrels (or bbl.**) in FY2019/2020. The share of GRSS from blocks 1, 2, and 4 (Nile blend) is 16,985 bpd (i.e. 0.395 x 43,000=16,985), which is **6,199,525 bbl**. in FY2019/2020. We now have the combined total share of GRSS from the Dar and Nile blends as **27,077,525 bbl**., which is higher than what has been given in the draft budget by **1,016,525 bbl**. It should now be obvious why transparency with respect to how cost- and profit-oil are calculated is imperative to have a correct size of the resource envelope.

[16] Prof. Augustino Ting Mayai makes the following comments on this point when reviewing the draft of the paper: "**You realize that the resource gap is always closed. In the end, the government often spends above the budget. So, in a way, I won't worry about that. What I would worry about is the fact that the money isn't spent on priorities. This is why, even after an a whooping expenditure of nearly $600M in the first 3 quarters of the just ending fiscal year, the salaries remain unpaid**."
[17] This was on 15 August 2019
[18] The Minister of Petroleum and his team have confirmed on 15 August 2019 before the Economy, Finance, and Development Committee of the TNLA the authenticity of these percentages and arrangements
[19] The Minister of Petroleum gave a figure of daily production ranging between 43,000 and 47,000 bpd, but I have decided to be conservative on these figures

Table 2: Distribution of GRSS' Share of oil Revenues as proposed by MoFP

Stakeholders	**Share of stakeholders expressed in Barrels of Crude oil/year**	**Share of stakeholders expressed in monetary terms/year**	**My Comments**
1. GRSS of which: Sudan, Oil producing States & communities and take from	**26,061,000 bbl. Based on new information: 27,077,525, which is composed of 20,878,000 bbl. from block 3 & 7; and 6,199,525 bbl. from blocks 1, 2, & 4**	**USD1.433 billion or SSP222.2 billion (or SSP235.5 billion as stated in the budget speech) Based on new information: USD1,148,290,000 from Dar blend and USD371,971,500 from Nile blend, which all add up to a total of USD1.5 billion**	**If we use the real exchange rate of SSP250/$1.0 determined by the parallel market rate then it is SSP375 billion**
2. Sudan takes 28,000 bpd in lieu of TFA, processing, transport, & transit fees. These barrels are to taken from the Dar blend	**10,220,000 bbl.**	**USD562.1 mn or SSP87.1 bn**	The allocation to Sudan should not be calculated in SSP, since it is paid directly in USD.
3. GRSS' share after payment to Sudan	Based on new information: 10,658,000 bbl. from Dar blend & 6,199,525 bbl. from Nile blend or a total of **16,857,525** bbl.	Based on new information: **USD958,161,500** or **SSP154.3 billion**	The working figure is therefore **SSP154.3 billion**
4. Oil producing states & communities take 5% of 74,185=3,709 bpd	**1,353,785 bbl.**	**USD74,458,175 or SSP12.0 billion**	It is given in the budget speech as **SSP6.6 bn**! MoFP calculates 5% of what has remained after Sudan is paid, which is not correct. If the **GRSS deducts**

			USD9.1 on 1,353,785 bbl., then this will be equal to USD12.32 mn or SSP2.0 billion
5. GRSS' share after payment to oil producing states & communities	**15,503,740 (9,304,215 bbl. Dar blend and 6,199,525, bbl. Nile blend)**	Based on new information: **USD883,703,325 or SSP142.3 billion**	I add to this figure what GRSS pays to Sudan (i.e. USD9.1/barrel exported through Sudan) on behalf of oil producing States & communities, which is equivalent to SSP2.0 billion, I get
6. Net oil revenues of GRSS in SSP of which 30,000 bpd is allocated to infrastructure development	15,503,740 bbl. less 10,950,000 bbl. in favor of Chinese Construction Company	SSP144.3 billion of which SSP93.4 billion is allocated to infrastructure development	Total outlays are given as SSP208.2 billion. But, capital expenditure is overestimated by SSP64.4 billion! Hence, total outlays would be SSP143.8 And if we add revenue from taxes (i.e. non-oil) of SSP29.9 billion to oil revenues of SSP144.3, we get SSP174.2 billion. There is, therefore, a surplus of SSP29.0 billion

3.1.2 Closing the resource gap through transparency

The resource gap is based on the assumption that **SSP93.4 billion will be spent on roads in the FY2019/2020.** This is, however, not true. I have challenged this assumption in Table 2 above by updating information obtained from the Minister of Petroleum and First Deputy Government of BoSS to re-examine the proposed spending on infrastructure. A careful look at the components of the proposed capital expenditure would, however, reveal that there are serious issues with this allocation. One of these is that a Chinese construction company has been awarded a contract to build a **400-kilometer (km) long highway** with the proceeds from the sales of 10,950,000 bbl. In fact, the Chinese construction company will not be able to complete the building of 400 km highway in the FY2019/2020.

Let us assume that the company would be able to construct 100 km during the FY2019/2020 at a cost of **USD1.8 mn/km** or a total cost of **USD180.0 million.** This means that the amount of USD602.3 million (i.e. SSP93.4 bn) appearing as spending for road in the total outlays of SSP208.3 billion is, according to my calculations, USD180.0 million (or SSP29.0 bn). Stated differently, the budgeted total outlays of **SSP208.2 billion** would now be, by my calculations, **SSP143.8 billion**. The transparency, demonstrated by these two senior officials, in providing accurate information has also facilitated the recalculation of the share of GRSS' oil revenues. The recalculation has yielded projected total oil revenue to increase from SSP100.9 billion given in the FY2019/2020 draft budget to **SSP144.3 billion, which leads to a total GRSS' revenues of SSP174.2 billion** (i.e. 144.3 bn from oil revenues + 29.9 bn non-oil revenues).

Hence, the difference between total outlays and total revenues would yield a surplus of **SSP30.4 (i.e. 174.2 – 143.8) billion** (or **USD188.8 million at the exchange rate of SSP161/USD1.0**). The TNL could then allocate this amount of SSP30.4 billion to priority spending areas (e.g. public universities and other core institutions) that were left out in the draft budget. This surplus, in terms of crude oil, is equivalent to 10,000 bpd or 3650,000 bbl. in the FY2019/2020.

3.1.3 Managing the infrastructure fund

The point of departure for the TNL is a careful analysis of the infrastructure development fund, which has been allocated 30,000 bpd or 10,950,000 bbl. per year (i.e. **USD602.3 million**) in the draft budget. The GRSS should be commended for taking such a visionary steps toward the development of South Sudan by creating such a facility. The problem, however, arises when the proceeds are deposited monthly into a **<u>zero-interest earning account at a Chinese bank</u>**! This would be appropriate and good public policy if these proceeds were used as a collateral. Moreover, the allocation should be reduced from 30,000 bpd to 20,000 bpd, so that the difference (i.e. 10,000 bpd) arising from this reduction should be used toward improving the living conditions of employees in the core institutions of GRSS.

I would recommend that the proceeds from the yearly sales of 7,300,000 bbl. (i.e. 20,000 x 365) **be deposited into an interest-earning escrow account or a Special Purpose Vehicle (SPV) under the management of Bank of South Sudan with an international bank**. Alternatively, MoFP could seek the services of an independent transaction adviser to provide options for the utilization of resources made available under this noble initiative of establishing Infrastructure Development Fund. Moreover, the Government of Norway could assist in the management of the Infrastructure Development Fund. I have sought in the course of preparing this paper an expert opinion from Dr. Peter J. Middlebrook, CEO, Geopolicity Inc. His initial views are presented in Table 3 below, which he has also shared with Dr. David Nailo Mayo, Chairman of the Economy, Development, and Finance Committee, Transitional National Legislative Assembly (TNLA). Dr. Middlebrook stated his views in the following passage:

> ***A transaction advisory firm would normally seek to (i) put in place the most optimal terms and conditions for the deal including contract term, procurement arrangements (i.e. local content), oil price fluctuations, risks and mitigation measures (ii) establish cost benefit calculations including net present value and rate of return analysis (iii) undertake market testing (iv) outline the best options for ringfencing the infrastructure investment perhaps as a Special Purpose Vehicle (SPV) to improve performance monitoring and value for money (v) and establish key performance indicators for the procurement process. The contract should be pegged to the USD given ongoing devaluation and the infrastructure to be built, must be planned and overseen by sector Ministries. Ideally, a joint procurement committee has oversight of all procurement under the contract, to maximize the benefits to local works, services and technical assistance providers. Feasibility studies would be undertaken, independently, to secure optimal investment mixes (i.e. roads, power, fiber optic, water, storage etc.).***

Table 3: Options for the use of resources allocated to infrastructure development

Base Option	**Optimal Options**
- Assess and Improve Terms and Conditions (i.e. local content, performance monitoring, feasibility design) - Strengthen Local Content Arrangements (i.e. 60% local contractors and labor) - Asset evaluation / contractor taxation	- Calculate Net Present Value of the Deal - Undertake Feasibility Studies including VfM - Appoint Independent Transaction Advisors - Identify Alternative Structures (SPV, KPIs, VfM) -
- Appoint Independent Transaction Advisor and identify most optimal options from an economic standpoint, including market testing, for YR1, YR3, YR5 timeframe - Consider market-based sales and sovereign management and contracting - Establish Five Year Infrastructure Investment plan, around which investments (anchor, ancillary and spinoff are made) - Explore SPV and matching infrastructure with donor funds - Support competitive procurement and transparent award - Build in operations and maintenance financing to sustain.	- Market testing to identify alternative VfM options - Appoint Independent Transaction Advisors - Establish joint Government / Partner Special Purpose Vehicle to manage project. - Establish options for hedging against exchange, oil price and other risks. - Links to ancillary investments (Special Economic Zones) and Small to Medium Enterprises. - Consider Joint Ventures - Explore options for leveraging

3.2 Improving the living conditions of core public sector employees

There is, in my view and based on the brief analysis of the share of GRSS' oil revenues, a fiscal space to address the lingering question of how to improve the living conditions of employees in the core public sector institutions. I have mentioned earlier in this paper that the FY2019/2020 budget is underpinned by two overriding objectives – consolidating peace and stabilizing the economy. I have in chapter 2 of the paper highlighted some areas stipulated in the R-ARCSS to constitute what I thought to be mandatory spending if the GRSS were to consolidate peace. I do appreciate the allocation of SSP10.0 billion (or USD64.5 mn) for the implementation of R-ARCSS and SSP93.4 billion (or USD602.3 mn) for infrastructure development.

The draft budget has, however, ignored an important fact that stabilizing the economy requires effective institutions, which are managed by highly motivated and remunerated employees[20]. For instance, the role of our public universities in human capital formation, which is one of the fundamental determinants of economic growth, cannot be over emphasized. Yet, employees of these institutions are among the poorly paid individuals in South Sudan. Hence, I would recommend that some of the savings (**i.e. USD200.8 mn**) from my analysis of the proposed infrastructure development fund could be used toward raising wages and salaries of employees in core institutions, such as universities, schools, hospitals, rule of law, and security sector. The total cost of the proposed new structure of wages and salaries for the five public universities is estimated to be **SSP9.4 billion (or USD58.4 mn**).

The TNL could allocate 10,000 bpd toward improving living conditions of the core staff in the public sector. This would be, in terms of crude oil, **3,650,000 bbl**., which is equivalent to **USD200,750,000 (or USD200.8 million**) at the benchmark price of USD55/barrel of Dar blend. I would venture in Table 4 below to allocate this amount to be paid in support of wages and salaries indexation to exchange rate to the following categories:

Table 4: Improving living conditions through exchange rate indexing of wages and salaries to staff of core institutions

Category	**Number of persons**	**Amount in USD**	**Comment**
1. Public Universities	Details about the number of the staff (academic and non-academic) are with the administration of these universities	58.4 million	The Cabinet approved pay raise for a total cost of **SSP9.4 billion** after the budget was presented to the TNL. This should not wait for supplementary budget, since this raise is within total outlays of the

[20] The TNL has just approved today 21 August 2019 the FY2019/2020 budget. I still hold the main arguments advanced in this paper

			FY2019/2020 draft budget
2. National Legislature		12.0 million	This figure is for members of the two houses and their staff. The assumption here is that the payroll of the national legislature is about USD1.0/month, which would make the TNL more efficient
3. Core Institutions	12,000	144.0 million	It is assumed here that 12,000 highly qualified South Sudanese in the civil service would each be paid USD1,000/month. For instance, the capacity of the Presidency would be enhanced through reassignment of 36 highly qualified South Sudanese as follows: 10 staff to the office of the President, 6 staff to the office of FVP, and 5 staff to each of the four VPs
Total estimated cost		**214.4 million**	This amount is slightly higher than the realized savings, but there are envisaged improvements in both production and price of our crude oil. The daily production is projected to be around 195,000 bpd at end-December 2019

IV. Conclusion and Recommendations

In conclusion, I would think that the TNL has for the first time an opportunity to turn the misdiagnosed resource gap in the FY2019/2020 draft budget into a tool for ensuring integrity of the budgeting process. Transparency and accountability are the foundation of public budget integrity. It is through accurate information obtained from reliable sources and my own knowledge about the oil and gas sector of the two Sudans that I have been able to show some pockets of fiscal space in the FY2019/2020 draft budget. I am convinced beyond doubt that the FY2019/2020 draft budget would be able to accommodate the recently proposed raise of the salaries of the staff of our public universities. I would support any supplementary budget aimed at raising the salaries of our universities, which should pave the way for a generalized salary raise for all the public sector employees.

I would urge the Council of Ministers of the Revitalized Transitional Government of National Unity (R-TGoNU) to initiate a process of supplementary budget to be presented to the TNL in January 2020. The envisaged supplementary budget is based on projected additional 22,000 bpd of which the share of GRSS is 9,240 bpd. The proceeds from these additional earnings from oil would be used toward the implementation of R-ARCSS (e.g. security sector reform, reconstruction fund, enterprise development fund, and so forth). My focus on the implementation of R-ARCSS is informed by the fact that peace is a necessary, though not a sufficient condition for economic growth and poverty eradication.