Fiscal Space for Children: An analysis of options in Rwanda
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### List of abbreviations

<table>
<thead>
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<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>CPI</td>
<td>Consumer price index</td>
</tr>
<tr>
<td>EDPRS</td>
<td>Economic Development and Poverty Reduction Strategy</td>
</tr>
<tr>
<td>FRW</td>
<td>Rwandan franc</td>
</tr>
<tr>
<td>FY</td>
<td>Fiscal year</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross domestic product</td>
</tr>
<tr>
<td>GFI</td>
<td>Global Financial Integrity</td>
</tr>
<tr>
<td>GNI</td>
<td>Gross national income</td>
</tr>
<tr>
<td>IFF</td>
<td>Illicit financial flows</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>LIC</td>
<td>Low income country</td>
</tr>
<tr>
<td>MIDIMAR</td>
<td>Ministry of Disaster Management and Refugees</td>
</tr>
<tr>
<td>MIGEPROF</td>
<td>Ministry of Gender and Family Promotion</td>
</tr>
<tr>
<td>MINALOC</td>
<td>Ministry of Local Government</td>
</tr>
<tr>
<td>MINECOFIN</td>
<td>Ministry of Finance and Economic Planning</td>
</tr>
<tr>
<td>MINEDUC</td>
<td>Ministry of Education</td>
</tr>
<tr>
<td>MININFRA</td>
<td>Ministry of Infrastructure</td>
</tr>
<tr>
<td>MINISANTE</td>
<td>Ministry of Health</td>
</tr>
<tr>
<td>n.e.c.</td>
<td>Not elsewhere classified</td>
</tr>
<tr>
<td>NER</td>
<td>Net enrolment rate</td>
</tr>
<tr>
<td>NISR</td>
<td>National Institute of Statistics of Rwanda</td>
</tr>
<tr>
<td>NST</td>
<td>National Strategy for Transformation</td>
</tr>
<tr>
<td>ODA</td>
<td>Official development assistance</td>
</tr>
<tr>
<td>R&amp;D</td>
<td>Research and development</td>
</tr>
<tr>
<td>RRA</td>
<td>Rwanda Revenue Authority</td>
</tr>
<tr>
<td>UNICEF</td>
<td>United Nations Children’s Fund</td>
</tr>
<tr>
<td>US$</td>
<td>United States dollar</td>
</tr>
<tr>
<td>VAT</td>
<td>Value added tax</td>
</tr>
<tr>
<td>WASH</td>
<td>Water, sanitation and hygiene</td>
</tr>
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</table>
This report is part of a series of country studies carried out by Ecorys and Associates for UNICEF in Eastern and Southern Africa. The project aims to strengthen UNICEF’s advocacy efforts through a better understanding of the role of political economy factors in processes and decisions around the creation and use of fiscal space for investments in children.

This report was written by Paul Beckerman, Gabriele Pinto, Andrea Dijkstra and Jonathan Wolsey.

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The findings, interpretations and conclusions expressed in this report are those of the authors and do not necessarily reflect the policies or views of UNICEF or the United Nations. The designations in this publication do not imply an opinion on legal status of any country or territory, or of its authorities, or the delimitation of frontiers.
Executive summary

This study investigated the options that are available to the Government of Rwanda to address the funding demands of priority sectors for children within a fiscally sustainable framework.

The macroeconomic and fiscal situation suggests that Rwanda will face difficulties finding much additional fiscal space in the short run to support greater investments in sectors that matter for children. In recent years, the government has achieved remarkable economic growth and has undertaken a relatively large public investment programme, especially in comparison to neighbouring economies. At the same time, high public investment flows have created a widening of the current account deficit. To reduce the pressure on the external balance, Rwanda has tightened its fiscal and monetary policies and scaled back some of its investment programme. As domestic revenues are not expected to increase much until at least 2020, the next two to three years will be guided by a policy of expenditure control and prudent borrowing.

Spending on ‘priority’ sectors has been uneven over the past years, but this may change in the future if the National Strategy for Transformation (NST1) places a renewed focus on these sectors. ‘Priority’ expenditure refers to recurrent and capital expenditure flows considered essential for children’s welfare. For the purposes of this study, priority expenditure is defined as spending on a number of sub-sectors of education, health, social protection and water supply (‘priority’ sectors). From FY2015/16–FY2016/17, total priority expenditure declined as a share of GDP from 6.4 per cent to 5.9 per cent. This trend can be explained in the context of the Economic Development and Poverty Reduction Strategy (EDPRS) II, which ran from 2013 to 2018, and prioritized areas related to economic growth. However, since social sectors are represented as a standalone pillar in the new NST1, this trend of public expenditure to social sectors could be reversed.

Given the development challenges faced in these child-friendly sectors, there is a clear case for increasing funding for priority sectors. Within the priority sectors, important policy challenges remain to be addressed. These are mainly related to improving the quality of service delivery and increasing the impact of policies towards alleviating poverty, which may indicate that – regardless of the high budget execution rate – Rwanda could make more optimal use of the funds spent. In addition, each sector has faced a financing gap, as all sectors were allocated less than they would need based on their sector plans. An increase in priority expenditure is thus necessary to address these challenges. While in some countries improvements in budget execution and increasing the efficiency of expenditure are options to deal with inadequate fiscal space, this is less likely for Rwanda, since the country appears to have relatively efficient expenditure management when compared to neighbouring countries.

In a baseline status quo scenario in which economic growth averages around 7 per cent, spending on priority sectors would increase without creating a financing gap. Under a set of neutral, non-controversial assumptions, priority expenditure would increase as a percentage of total expenditure and in terms of GDP. Per-child priority expenditure would increase from US$119 in FY2017/18 to US$186 in FY2023/24, which amounts to a 56 per cent increase. The average net internal debt flow would be 0.02 per cent of GDP, which indicates the government could realize this scenario without additional internal borrowing. The fiscal deficit would turn into a surplus of 0.34 per cent of GDP. This outcome is in line with the expected government policy of reducing capital expenditure, as this will free up resources to increase priority expenditure and reduce the fiscal deficit.

In addition to the positive changes foreseen under the baseline scenario, Rwanda could increase priority expenditure by an additional 2 per cent in a number of fiscally neutral ways. The selection of scenarios...
shows that increased value added tax (VAT) efficiency, increased grant revenue and reallocation of expenditures could fund this increase and at the same time decrease total debt.

**Alternative scenarios indicate that Rwanda could fund a small additional increase in priority expenditure through increased VAT efficiency.** Although the reform space in revenue collection is modest in the next two to three years, there is potential to increase efficiency in domestic revenue collections. In particular, the functioning of e-billing machines could be further improved and lead to more efficient VAT collection. If efficiency increases gradually from 20 per cent in FY2017/18 to 25 per cent in FY2023/24 and import VAT collection efficiency increases gradually from 42 per cent in FY2017/18 to 54 per cent in FY2023/24, average tax/non-tax revenue would increase by 0.37 per cent of GDP over the projection period. Government debt–GDP ratio would be reduced by 2.5 per cent in 2024 compared to the debt level in 2024 projected by the base scenario. When combined with a scenario in which priority expenditure would increase by 0.14 per cent of GDP and per-child expenditure would be US$191 in FY2023/24, compared to US$186 in the base scenario, the increase in average tax/non-tax revenue to GDP could fund the increase in priority expenditure and at the same time reduce government debt to a level below that of the base scenario.

**An alternative scenario in which social sectors attract additional external grant funding shows that this approach has the potential to both increase priority expenditure and to limit government indebtedness.** While Rwanda aims to reduce its aid dependency, specific grant proposals for social sectors could be successful in generating additional resources for the priority sectors. In a scenario where the external grants for both current and capital expenditure increase to 3 per cent of GDP in FY2023/24, totalling 6 per cent of GDP, the government could fund an increase in priority expenditure of 0.14 per cent of GDP. Total debt–GDP would decrease to 38.6 per cent in 2024.

**Attracting higher levels of private investments could lead to a scenario in which the private sector would fund ‘non-priority’ expenditure such as infrastructure, which would enable the government to reallocate funds to priority expenditure.** If non-priority recurrent and non-recurrent expenditure decreases respectively to 12 and 6 per cent of GDP in FY2023/24, priority expenditure could increase by 0.14 per cent of GDP. At the same time, this reallocation would lead to a decrease in external debt of 4.8 per cent. It should be noted that this scenario could turn out differently if private investments do not compensate for the loss of public investments due to lower GDP growth. This would have a negative effect on the increase in priority expenditure.

**A scenario of higher GDP growth, which could be realized by successfully attracting private funding, would also positively affect priority expenditure.** If GDP growth is higher than the base scenario (e.g. 8 per cent in FY2023/24 instead of 7.5 per cent), this would be beneficial for per-child expenditure. An increase of 0.5 per cent in GDP growth would increase per-child priority expenditure to US$188 and reduce government debt by 1.14 per cent of GDP.

At the same time, if private funding does not take off as expected, a scenario of lower GDP growth could be considered, which would have an exponentially negative impact on per-child expenditure. If GDP growth gradually declines from 5.7 per cent in FY2017/18 to 4.0 per cent in FY2023/24, per-child priority expenditure would still increase over the years, but less than in the base scenario: per-child expenditure would be US$168 in FY2023/24 (compared to US$186 in the baseline scenario). The debt–GDP ratio would increase to 53.4 per cent in FY2023/24, while the fiscal deficit would stand at 1.42 per cent of GDP. Under this scenario, Rwanda would also have a more significant fiscal gap, for which it would need to resort to internal borrowing.

**For the near future, improvement of expenditure efficiency and increasing local taxation are less likely scenarios to increase fiscal space.** While improving expenditure efficiency is always advisable, Rwanda already has relatively high expenditure outturn at both local and central level. Local governments have great potential
to increase their own revenues, but at the moment, the share of local government taxation as part of total tax collection is too small to have a significant effect on overall fiscal space. Financing a further increase in priority expenditure through additional external debt is not very likely in the short run, as Rwanda intends to achieve low debt distress status. Capturing illicit financing flows could also potentially increase fiscal space for priority sectors, but this scenario cannot be captured in the model.

Notwithstanding the modest scope for increasing fiscal space in the short term, the report concludes that there is a strong case for UNICEF to continue its dialogue on strategic resource allocation around children. Rwanda appears to be favourably placed to increase its priority expenditure over the medium term. The government’s upcoming strategy suggests a commitment to prioritize such expenditure. The present base scenario projects that Rwanda could increase per-child priority expenditure without creating a fiscal gap. Finding additional fiscal space beyond the flow projected in the base scenario is likely to be challenging for Rwanda, but not impossible. Increased VAT collection efficiency, additional external financing and some reprioritization of expenditure could increase priority expenditure by an additional 2 per cent in a fiscally neutral way.
1. Introduction and methodology

Like most countries in the Eastern and Southern Africa region, Rwanda is experiencing a demographic boom, which implies that the number of children will continue to grow rapidly in coming decades. This implies that the need for children’s services in health, education, sanitation, nutrition and protection will significantly increase. Meanwhile, Rwanda has been experiencing a change in the development financing landscape over the past decade. While official development assistance (ODA) remains an important source of funds for development, its relative importance has begun to slip. Future progress in children’s development will rely increasingly on funding from domestic sources.¹

In view of this reality, UNICEF has commissioned a study to develop a methodological approach and carry out a projection exercise that can be used to inform the ongoing dialogue with the government and other stakeholders regarding the ‘fiscal space’ for expenditure essential for children.

In this study, the fiscal space concept simply means the flow of fiscal resources available for spending on children’s needs. The concept is central in UNICEF’s dialogue with the authorities: in the medium term, UNICEF would focus on ensuring as high a growth rate as possible for child-friendly spending, subject essentially to two constraints: first, the need to ensure that the economy maintains sufficient infrastructure investment to ensure sustained real GDP growth; and, second, the need to ensure that the fiscal balance and government debt accumulation remain within prudent limits.

1.1 The objective of the Fiscal Space Analysis

The Fiscal Space Analysis sets out by reviewing the recent evolution of the availability of financial resources within the government budget for expenditure flows directly relevant to children’s welfare and development. It does this through a fiscal space accounting framework, centred around the government budget and the identification of ‘priority’ sectors considered most relevant for children’s welfare.

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

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

1.2 Methodology

The analysis is carried out using an Excel-based projection exercise (RwFS.xlsm). Section 1.2.1 outlines the structure of the fiscal space model; and Section 1.2.2 describes the approach used to populate the model, formulate alternative scenarios and run projections.

1.2.1 The model and key concepts

The model is a multiannual fiscal programming exercise, structured to indicate the evolution of the fiscal space under specified macroeconomic programming assumptions. This exercise produces multiannual fiscal accounts projections based on (1) historical data and (2) programming assumptions regarding macroeconomic conditions.

This report refers to expenditure considered beneficial to children as ‘priority’ expenditure. Making use of the government budget accounting ‘identity’, the analysis examines the effective financing and the potential for enhanced future growth of priority expenditure, given the recent and projected revenue and financial constraints as well as the evolution of non-priority expenditure. The projections can be analysed to compare, on the one hand, the evolution of real expenditure in sectors relevant to children and, on the other hand, the evolution of the rest of the fiscal accounts. The idea would be to determine whether any given set of assumptions, taken together, would produce projections in which the priority expenditure programme would be feasibly financed or, if not, how large the financing gap would be.

In this way, the analysis addresses the question of whether Rwanda’s government possesses and will continue to possess adequate ‘fiscal space’ to fund its ‘priority’ expenditure flow.

The fiscal identity

The analysis of the evolution of the fiscal space in the recent past and over coming years centres on the government budget accounting ‘identity.’ Over any accounting period, total priority expenditure must precisely equal the sum of all revenue and net financing flows less total non-priority expenditure. The net internal financing flows are a residual category. This required net internal financing flow is the ‘fiscal gap’.

For present purposes, the basic structure of the identity is as follows:

<table>
<thead>
<tr>
<th>Total priority non-interest expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Tax and non-tax, non-interest revenue (excluding external grants)</td>
</tr>
<tr>
<td>+ External and internal interest receipts</td>
</tr>
<tr>
<td>+ External grants</td>
</tr>
<tr>
<td>- Total non-priority, non-interest expenditure</td>
</tr>
<tr>
<td>+ External debt disbursements</td>
</tr>
<tr>
<td>- External debt service (repayment and interest)</td>
</tr>
<tr>
<td>- Internal interest</td>
</tr>
<tr>
<td>+ Net internal financing flows (= fiscal gap)</td>
</tr>
</tbody>
</table>

Examination of the account structure above makes it clear that this structure is a simple rearrangement of the accounts that constitute any government budget, and so, for recent years, this table can be readily constructed from government budget results. The aim is to show how the various fiscal space components could fund the projected priority expenditure flow. The size of the net internal financing flows or the fiscal gap indicate the financial feasibility of the projections.
Priority expenditure

For purposes of this study, ‘priority’ expenditure is defined as the recurrent and capital expenditure considered essential for children’s welfare. The expression ‘priority’ should not be taken to mean that such expenditure should always be ‘prioritized’ over other expenditure. Nor does it mean that this is how the Government of Rwanda defines ‘priority’. The point is simply to categorize expenditures of priority interest to children in general and to UNICEF. As such, the composition of ‘priority’ expenditure is chosen by UNICEF and the consultants.

For Rwanda, ‘priority’ expenditure categories for children comprise the ‘functional’ expenditure categories as shown in Table 1.1.

Table 1.1: Composition of ‘priority’ expenditure based on the functional budget classification

<table>
<thead>
<tr>
<th>Social sector</th>
<th>Budget categories identified as ‘priority expenditure’</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health</td>
<td>707 Health</td>
<td>The entire health sector was selected as priority expenditure because the sub-sectors changed from FY2015/16 to FY2016/17, which made it not possible to maintain a selection of sub-sectors.</td>
</tr>
<tr>
<td>Education</td>
<td>7091 Pre-primary and primary education</td>
<td>This excludes post-secondary education and research &amp; development (R&amp;D) in education, as these sub-sectors benefit older children.</td>
</tr>
<tr>
<td></td>
<td>7092 Secondary education</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7095 Education not definable by level</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7096 Subsidiary services to education</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7098 Education n.e.c. 2</td>
<td></td>
</tr>
<tr>
<td>Social protection</td>
<td>710 Social protection</td>
<td>The entire social protection sector was selected because the sub-sectors changed from FY2015/16 to FY2016/17.</td>
</tr>
<tr>
<td>WASH</td>
<td>7063 Water supply</td>
<td>This is a sub-category of 706: housing and community amenities.</td>
</tr>
</tbody>
</table>

All government expenditures not categorized as ‘priority’ would be ‘non-priority’.

It is important to recognize that there is a measure of arbitrariness in the priority/non-priority distinction. Some expenditure classified as priority for Rwanda may in fact not be directly beneficial for children (e.g. health expenditure specifically intended to benefit older people), while some expenditure classified as non-priority may in fact be highly beneficial to children (e.g. local expenditure on roads).3

In addition, it should be noted that while this report focuses on the fiscal space for government expenditure, there is also non-government expenditure. This includes off-budget expenditure executed by international agencies and non-government entities (including faith-based organizations). This study focuses on fiscal space for government expenditure, but expenditure relevant to children may also be funded outside the government.

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2 Not elsewhere classified.
3 Analysts may prefer tighter or broader priority-expenditure definitions, but the methodological approach described above would still be applicable.
1.2.2 Approach

The first phase of the present Fiscal Space Analysis consists of data compilation and a broad review of the recent evolution of the government budget generally, and priority expenditure in particular. The second phase consists of the formulation and implementation of an exercise in Excel to project the evolution of priority expenditure and its revenue and financing constraints. A base scenario is prepared, and this is then used as a base of comparison with alternative scenarios based on different policy approaches.

**Phase 1: Data collection**

The first phase consists mainly of the compilation of historical data and analysis of the recent data. The model, structured along the fiscal identity mentioned above, is populated with this data.

The analysis is based on data covering sector budget execution (‘functional classification’) for fiscal year (FY) 2015/16 and FY2016/17. The main data source has been the Ministry of Finance and Economic Planning (MINECOFIN) of Rwanda. Government finance statistics (GFS) have been provided directly by MINECOFIN, while revenue breakdown has been estimated using the latest Rwanda Revenue Authority (RRA) Annual Report (referred to as FY2015/16). Macroeconomic aggregates come from the national accounts of the MINECOFIN and the international financial statistics database of the IMF (International Monetary Fund). Data fed into the quantitative framework comprise the indicators presented in Table 1.2.

**Table 1.2: Data for the quantitative framework**

<table>
<thead>
<tr>
<th>Area</th>
<th>Indicators</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fiscal accounts</td>
<td>(1) Budget results from recent years (including main revenue flows, ODA flows, overall expenditure flows, and net financing flows).</td>
<td>Rwanda’s Ministry of Finance and Economic Planning (MINECOFIN).</td>
</tr>
<tr>
<td></td>
<td>(2) Sectoral expenditure flows in recent years (in sufficient detail to set out priority and non-priority flows).</td>
<td></td>
</tr>
<tr>
<td>Consumer prices, exchange rate</td>
<td>(4) Monthly consumer price index values.</td>
<td>IMF International Financial Statistics.</td>
</tr>
<tr>
<td></td>
<td>(5) Monthly average exchange rates.</td>
<td></td>
</tr>
<tr>
<td>Balance of payments and</td>
<td>(7) National expenditure accounts.</td>
<td></td>
</tr>
<tr>
<td>International investment position</td>
<td></td>
<td></td>
</tr>
<tr>
<td>International trade</td>
<td>(8) Merchandise exports by principal commodity and (I) imports by economic classification.</td>
<td>IMF International Financial Statistics (download) and ATLAS MIT.</td>
</tr>
<tr>
<td>External and internal</td>
<td>Year-end (10) external and (11) government internal debt stocks; External and government internal debt flows.</td>
<td>Rwanda’s Ministry of Finance and Economic Planning (MINECOFIN).</td>
</tr>
<tr>
<td>government debt</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

For Rwanda, an economic breakdown of government expenditure was not available at sector level. Therefore, the share of recurrent and non-recurrent expenditure for each priority sector has been estimated on the basis of several criteria.
1. Introduction and methodology

<table>
<thead>
<tr>
<th>Classification</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sector</td>
<td>Available</td>
</tr>
<tr>
<td>Sub-sector</td>
<td>Available</td>
</tr>
<tr>
<td>Economic function at sector level</td>
<td>Unavailable (set equal to aggregated share reported in GFS)</td>
</tr>
</tbody>
</table>

**Phase 2: The projection exercise**

The second phase of the analysis entails the formulation of a medium-term projection exercise describing possibilities for the evolution of priority expenditure over the coming seven years (at the request of the UNICEF Rwanda office, the projections have been extended to 2024, which is the end-date of the new medium-term strategy). The Rwanda Fiscal Space Analysis sets out from a set of projection assumptions, together constituting a ‘base scenario.’ The base scenario consists of a straightforward and non-controversial set of assumptions, to project fiscal space assuming ‘business as usual’. Chapter 4 (Section 4.1) describes the assumptions that make up this scenario and the projection results.

Subsequently, the study has looked at various alternative scenarios that would presumably enhance fiscal space. Determination of these scenarios has been based upon literature review and conducting interviews with key stakeholders, such as MINECOFIN, the IMF and the World Bank. The selected scenarios, or fiscal space enhancement strategies, have then been expressed quantitatively as programming assumptions for the projection model. The model then describes their consequences: first, for the evolution of the priority expenditure, and, second, for the overall financing requirement. Evolution of the priority expenditure can then be evaluated for its adequacy and the required financing requirement can be evaluated for its feasibility. Chapter 4 (Section 4.2) discusses the rationale behind the selected options and describes projection results for the alternative scenarios, each of which is almost the same as the base scenario but with one or more specific assumptions altered, to examine the consequences for the fiscal gap. The projection exercise helps evaluate their potential in quantitative terms.

**1.3 The structure of the Fiscal Space Analysis**

The remainder of the Fiscal Space Analysis report is organized as follows:

- Chapter 2 presents a review of Rwanda’s macroeconomic and fiscal context. The purpose of this chapter is to provide context to the Fiscal Space Analysis and the selection of options and alternative scenarios in Chapter 4.

- Chapter 3 provides a discussion of the recent evolution of Rwanda’s priority expenditure and policy challenges. The purpose of this chapter is to provide a detailed account of the spending profiles of the priority sectors, to provide context to the Fiscal Space Analysis and the evolution of priority spending in the future.

- Chapter 4 presents the projection results. Section 4.1 presents the base scenario assumptions and results. Section 4.2 presents the selected policy options to enhance fiscal space and presents the projection results for alternative scenarios. Section 4.3 presents other policy options and explains why these have not been converted to alternative scenarios.

- Chapter 5 offers conclusions from the discussion of the preceding chapters.
2. Rwanda’s macroeconomic and fiscal context

This chapter starts with a discussion of the main macroeconomic developments and trends in Rwanda. The second part of this chapter captures Rwanda’s fiscal performance and prospects. Overall, this chapter portrays the macroeconomic and fiscal context of the Fiscal Space Analysis.

2.1. Macroeconomic developments and trends

Recent selected economic indicators (Table 2.1) show that Rwanda has achieved an average annual real GDP growth of 7.4 per cent. This growth surpassed population growth, and therefore the real GDP per capita growth has been almost 5 per cent per year. The trade deficit rose to 18.7 per cent in FY2011/12, after which it has been declining. Financing of the trade deficit has led to increased borrowing and an increased fiscal deficit.

Table 2.1: Selected economic indicators for Rwanda

<table>
<thead>
<tr>
<th></th>
<th>FY2010/11</th>
<th>FY2011/12</th>
<th>FY2012/13</th>
<th>FY2013/14</th>
<th>FY2014/15</th>
<th>FY2015/16</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross domestic product (GDP)*</td>
<td>5,863</td>
<td>6,351</td>
<td>6,776</td>
<td>7,195</td>
<td>7,790</td>
<td>8,362</td>
</tr>
<tr>
<td>Real GDP growth (%)</td>
<td>7.5</td>
<td>8.3</td>
<td>6.7</td>
<td>6.2</td>
<td>8.3</td>
<td>7.3</td>
</tr>
<tr>
<td>GDP per capita (US$)**</td>
<td>550</td>
<td>581</td>
<td>605</td>
<td>626</td>
<td>662</td>
<td>702</td>
</tr>
<tr>
<td>Real GDP per capita growth (%)</td>
<td>4.8</td>
<td>5.6</td>
<td>4.0</td>
<td>3.6</td>
<td>5.6</td>
<td>6.0</td>
</tr>
<tr>
<td>Non-government consumption**</td>
<td>447</td>
<td>468</td>
<td>481</td>
<td>494</td>
<td>526</td>
<td>552</td>
</tr>
<tr>
<td>Non-government consumption growth rate (%)</td>
<td>4.4</td>
<td>4.8</td>
<td>2.7</td>
<td>2.6</td>
<td>6.6</td>
<td>5.0</td>
</tr>
<tr>
<td>Gross fixed capital formation (% of GDP)</td>
<td>22.5</td>
<td>23.9</td>
<td>25.2</td>
<td>24.9</td>
<td>25.2</td>
<td>25.7</td>
</tr>
<tr>
<td>Central government fiscal surplus (% of GDP)</td>
<td>–3.7</td>
<td>–1.4</td>
<td>–5.2</td>
<td>–4.2</td>
<td>–5.2</td>
<td>–3.6</td>
</tr>
<tr>
<td>Merchandise-trade surplus (% of GDP)</td>
<td>–16.1</td>
<td>–18.7</td>
<td>–17.9</td>
<td>–16.8</td>
<td>–16.1</td>
<td>–15.2</td>
</tr>
<tr>
<td>Consumer prices (December) growth rate (%)</td>
<td>5.8</td>
<td>5.9</td>
<td>3.7</td>
<td>1.4</td>
<td>2.8</td>
<td>5.5</td>
</tr>
<tr>
<td>Exchange rate (December) growth rate (%)</td>
<td>2.4</td>
<td>1.7</td>
<td>4.9</td>
<td>6.2</td>
<td>5.4</td>
<td>8.9</td>
</tr>
<tr>
<td>Population growth rate (%)</td>
<td>2.6</td>
<td>2.6</td>
<td>2.5</td>
<td>2.5</td>
<td>2.5</td>
<td>1.2</td>
</tr>
<tr>
<td>Population under 15 growth rate (%)</td>
<td>2.3</td>
<td>1.8</td>
<td>1.6</td>
<td>1.6</td>
<td>1.4</td>
<td>0.8</td>
</tr>
</tbody>
</table>

Source: IMF International Financial Statistics, World Bank World Development Indicators, MINECOFIN.
* US$ million at 2015 prices and exchange rate.
** US$ at 2015 prices and exchange rate.

2.1.1 Structure and characteristics of the national economy

The Government of Rwanda is undergoing a structural transformation of its economy, to move from a traditional agriculture-based economy to a diversified economy. Within the last two decades, the government has steadily invested in developing economic activities. In its two decades of economic growth, public investment accounted for half or more of all investments in Rwanda. The government invested in infrastructure, including the national airline RwandAir, electricity, telecommunications and later the internet backbone. More recent investments in increasing
the electrical grid and building a large convention centre are meant to stimulate private sector development and attract MICE (meetings, incentives, conferences and events) business tourism.\(^4\)

As a result, the contribution of the agricultural sector to the GDP has decreased from 40 per cent in 2000 to 27 per cent in 2016, although the sector still employs about three quarters of Rwanda’s economically active population. Main products in this sector are maize, cassava, Irish potatoes, sorghum and rice. Contributions of the service and industry sectors to the GDP have increased from 50 per cent in 2000 to 65 per cent in 2016, mainly on account of the service sector, which has increased its contribution from 38 per cent to the GDP to 48 per cent (see Figure 2.1). Growth in the industry sector has been driven by construction, whereas in the service sector growth has been based on trade, transport and real estate activities, notably hospitality and tourism.

In addition to adjusting the composition of the GDP, the Government of Rwanda has put many efforts into increasing economic productivity in each of the sectors. Total factor productivity expresses the contribution of increased productivity to GDP growth. Figure 2.2 demonstrates that growth in total factor productivity has been uneven, and the increase in productivity was lower between 2010 and 2014 as compared to 2000 to 2010 – meaning that in the last five years Rwanda’s technological progress has contributed to a lesser extent to GDP growth than increases in inputs (capital and labour).\(^5\)

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\(^5\) International Monetary Fund (IMF), Rwanda Selected Issues, July 2017.
The industrial sector has the highest value added, but is a relatively difficult sector to develop, partly because of Rwanda’s small scale and landlocked geography. The government is trying to stimulate growth in this sector, notably in manufacturing. Compared to its neighbours, Rwanda is relatively safe and politically stable. This has enabled it to attract investment in infrastructure, information and communication technology, business and tourism. The high level of infrastructure investment has stimulated the development of the service sector and decreased the reliance on agriculture as share of the GDP.

Agriculture is the least productive sector, but remains a key sector for employment. The agricultural sector employs 45.9 per cent of the work force, as opposed to industry and services, which employ 14.3 per cent and 39.7 per cent respectively. When subsistence farmers are included, the percentage of the population employed in agriculture is 68.3 per cent, compared to 8.4 per cent in industry and 23.3 per cent in the service sector. Therefore, Rwanda’s economic strategy maintains a heavy focus on improving agricultural productivity, through developments such as improved irrigation systems, use of fertilizers, crop intensification and use of improved seeds.

2.1.2 Demographic trends

Rwanda has – and will continue to have – a large proportion of youth population, which requires a gradual increase in child-friendly spending if the government is to maintain its priority expenditure per child. Population growth is in line with regional trends (Figure 2.3). The United Nations estimated Rwanda’s population at 11.6 million in 2015. As this population lives on an area of 26,000 square kilometres, Rwanda is Africa’s most densely populated country (26th in the world).
2. Rwanda’s macroeconomic and fiscal context

In 2015, about 42 per cent of the total population was under 14 years of age. The share of the population under 14 years of age has stabilized in recent years, although with population still growing at a relatively high rate, the number of children will continue to grow. In 2025, the population is expected to grow to 14.5 million. While the share of children (0–14) will be smaller as compared to 2015 (36 per cent), the absolute number of children will be higher (5.2 million vs. 4.7 million in 2015).

Rwanda’s population growth is both an opportunity and a challenge. On the one hand, the demographic dividend offers great potential to attain high levels of economic growth. On the other hand, it underscores the urgency of achieving economic growth and employment opportunities to avoid many young people entering the job market without any prospects. Figure 2.4 illustrates a growing group of youth and adults (55 per cent in 2015 and 61 per cent in 2035), i.e. an increased labour force vis-à-vis dependent groups such as children and elderly people.

2.1.3 Poverty and inequality

The sustained growth of the last decade has enabled Rwanda to increase its per capita purchasing power, which now stands at about US$1,900. This figure is now about the same as the figures for neighbouring Uganda, although it is still well below the figures for Tanzania and Kenya (Figure 2.5).
The figures from the National Institute of Statistics of Rwanda (NISR) show a significant decline in poverty levels, from 46.0 per cent (FY2010/11) to 39.1 per cent (FY2013/14). The number of people living in extreme poverty fell from 21.8 per cent to 16.3 per cent. The decline in poverty appears to be explained by three main developments: (1) a shift from farm to non-farm employment leading to higher wages; (2) increased agricultural productivity – although the sector could still benefit from higher productivity, its output has increased by about 5 per cent in terms of food crop production since 2007; and (3) private sector development – the number of private establishments increased, as well as the number of corresponding jobs. The NISR also reports progress in decreasing inequality, as it finds a lower Gini coefficient – from 0.490 in FY2010/11 to 0.448 in FY2013/14.

The United Nations Development Programme measures multidimensional poverty, which complements monetary measures of poverty with deprivations suffered by individuals with respect to education (measuring indicators such as years of schooling and children enrolled), health (taking into account indicators on nutrition and child mortality) and living conditions (considering access to basic provisions such as cooking fuel, toilets, electricity). Rwanda’s report for FY2014/15 indicates that 53.9 per cent of the population are multidimensionally poor. This is much lower than the 86.5 per cent recorded in 2005, but it still means that about half of Rwanda’s 11 million people live in multidimensional poverty. In terms of the contribution of deprivation to overall poverty, living standards constitute the largest contribution to multidimensional poverty (53 per cent), followed by education (28.6 per cent) and health (18.4 per cent) – meaning deprivation in living standards (no access to cooking fuel, toilets, electricity) is higher compared to deprivation in health or education. Compared to previous years, the relative contribution of education to multidimensional poverty has increased, while that of health has decreased.

Poverty eradication is one of the priority areas in the new National Strategy for Transformation. The NST targets eradication of extreme poverty by 2024. Scaling up and improving social protection interventions are mentioned as key strategic interventions to reach this objective.

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10 Ibid.
11 Ibid. The Gini coefficient ranges from 0 (perfect equality) to 1 (perfect inequality).
13 United Nations Development Programme, Human Development Index, Table 6A: Multidimensional Poverty Index: changes over time.
2.1.4 Real GDP growth

In the last two decades, Rwanda has achieved continued and sustained growth. Between 2002 and 2016, the average annual real growth rate was 7.8 per cent of GDP.\(^{14}\) While this is well below the assumptions of Vision 2020 (which aimed for an ambitious annual average real GDP growth of 11.5 per cent), it is one of the highest rates in the region. Using 2010 as the base year, Rwanda’s real growth rate exceeded those of its neighbouring countries (Figure 2.6).

\[\text{Figure 2.6: Real GDP growth (index, 2010 = 100)}\]

Source: International Monetary Fund, World Economic Outlook Database, October 2017.

Despite its strong growth, Rwanda remains one of the world’s poorest countries, ranking 171th among 193 countries, according to IMF country ranking by GDP (at purchasing power parity per capita 2017 estimates).\(^{15}\) The trend in GDP per capita growth reflects Rwanda’s above average growth performance, but the size of its GDP per capita also demonstrates the gap in relation to neighbouring Tanzania and Kenya (in current US$, Figure 2.7).

\[\text{Figure 2.7: GDP per capita (current US$)}\]

Source: International Monetary Fund, World Economic Outlook Database, October 2017.

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\(^{15}\) Ibid.
Real GDP grew by 5.9 per cent in 2016, compared with 8.9 per cent in 2015. Several presumable one-time events contributed to this slowdown, including a severe drought (affecting agriculture and power generation), conclusion of some large public investment projects, and fiscal tightening. GDP growth is predicted to recover from the drop in 2016, as weather conditions should allow for a better harvest and recovery of the agriculture sector, while larger public investment, notably in tourism, is expected to lead to increased service exports (Figure 2.8). However, keeping in mind the process of structural transformation and the need to increase productivity, only time will tell whether the 2016 decline in real GDP growth was a temporary downfall or the beginning of a period of somewhat slower growth. In addition, the level of GDP growth will depend on various external factors. These include persisting aid dependence, uncertain weather conditions, commodity price volatility, and regional tensions centred on neighbouring countries. More importantly, private sector investment may not materialize as planned. As the World Bank puts it in its Economic Update 2017: "Overall, medium to long term outlook will depend on the extent to which the private sector will move to invest in the tradable sectors with higher growth and productivity potential."

Sustaining high GDP growth, despite tightening financing constraints, remains a key priority for the government. The government is now developing its Vision 2050 and its third medium-term implementation strategy. The new National Strategy for Transformation (NST1) covers seven years, aligned with the presidential term that began in 2017. The key objective is attainment of an upper-middle (and eventually high) income status – therefore GDP growth will be the central focus. Strategic priorities include export diversification, cheaper and more accessible energy, higher agricultural productivity, better matching of skills and employment, increased private savings, and improved public project management. Efforts to attract private investment will continue and be intensified. Rwanda’s participation in the G20 Compact for Africa is intended to signal its strong interest in private-sector development.

2.1.5 International trade and the current account

Traditionally, Rwanda has imported more than it exported, being a small and landlocked country with few natural resources. Over the years, its export earnings have increased and exports have become more diversified. Minerals,
agriculture and manufacturing export earnings increased from US$4 million in 2007 to US$155 million in 2016.\(^{21}\) Traditional export products such as coffee, tea and minerals still account for about half of the export earnings.

Figure 2.9: Rwanda export/import composition, US$ million

Like most non-oil developing economies, Rwanda runs a deficit on its current account, but the deficit has swollen in recent years, in part because of adverse commodity export price movements, but also because merchandise imports rose with Rwanda’s ambitious public investment programmes, such as the Kigali Convention Centre, the Kivu-Watt Project and the reconstruction of Kigali International Airport. Figure 2.10 illustrates the increasing current account deficit between 2013 and 2016, both in terms of US$ millions and in percentage of GDP.

Figure 2.10: Current account deficit 2010–22 in US$ millions and in percentage of GDP
Source: International Monetary Fund, World Economic Outlook Database, October 2017.

\(^{21}\) Ibid.

\(^{22}\) The Atlas of Economic Complexity data from the MIT is collected by customs offices, therefore it includes only goods and not services. This is an important drawback, as services are becoming a rising share of international trade.
Ideally, Rwanda would have financed its current account deficit mainly with direct foreign investment, as it must limit the growth of external debt and as its foreign exchange reserves are limited. However, foreign grants have been declining, which forced Rwanda to draw from its foreign exchange reserves to finance the deficit, which created an unsustainable situation, with reserves dropping from US$1,050 million at the end of 2011 to US$738 million by mid 2015 (equal to approximately 3.5 months of imports).\(^{23}\) In 2016, the government secured an IMF standby credit facility, intended to help reduce the deficit and relieve pressure on the current account and its foreign exchange reserves. The IMF programme relies on exchange rate depreciation and fiscal tightening to reduce import demand.

In this context, policymakers have shifted their focus from stimulating infrastructure investment to reducing imports and increasing exports. The government is promoting locally made products through a ‘Made in Rwanda’ policy and has taken steps to diversify exports. The government has continued to promote Rwanda as an attractive location for national and international business, even though Rwanda itself is not the largest market in its area. It has continued to court investors by setting up special economic zones with low-cost energy and tax exemptions. Rwanda has become an especially enthusiastic promoter of public-private partnerships to increase access to private financing for public services.

### 2.1.6 Inflation and exchange rate

Inflation rates have been relatively stable and below 6 per cent since 2010. Inflationary pressure revived somewhat in 2016, partly because of higher food prices caused by drought conditions and partly as a consequence of exchange-rate depreciation, which the authorities allowed in order to help control the current account deficit. In early 2017, headline inflation peaked at 8.1 per cent as a result of a spike in food price inflation.\(^{24}\) In its latest assessment, IMF staff said that the real exchange rate is ‘broadly’ in line with fundamentals,\(^{25}\) but the authorities are well aware that they cannot take a complacent approach to inflation. It should be noted that urban and rural inflation rates differ, with the latter being higher.

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\(^{23}\) International Monetary Fund, Staff Report for the 2017 Article IV Consultation, Seventh Review under the Policy Support Instrument and Second Review under the Standby Credit Facility, June 2017.

\(^{24}\) Ibid.

\(^{25}\) Ibid.
2. Fiscal performance and policy

Rwanda’s fiscal deficit has ranged in recent years from 3 to 5 per cent. This was partly the result of the government investment projects under the Economic Development and Poverty Reduction Strategy II (EDPRS II), which required increased capital expenditure. Following the increasing current account deficit and the resulting pressures on the external balance, the government’s fiscal policy has moved from a more expansionary policy to fiscal consolidation and a prudent borrowing policy.

The government states in its April 2017 Budget Framework Paper that its fiscal policies for the coming years aim to achieve:

- fiscal and debt sustainability with progress toward the East African Community macroeconomic convergence criteria – the fiscal deficit norm is 3 per cent of GDP;
- a reduction in the current account deficit and the concomitant reliance on external financing; and
- further improvement in prioritization and efficiency of public expenditure, in support of growth, poverty reduction and structural current account improvement.

The government will therefore try to slowly reduce the deficit to an average of 3.5 to 4 per cent of GDP over the coming three years. It also aims to maintain its debt at a sustainable level, and reduce its reliance on external financing. In the next few paragraphs, the effect of these policies on government revenues and expenditures will be discussed.

2.2.1 Government revenue

Revenue generation has been a priority for Rwandan economic authorities for decades, and steep challenges have been overcome to improve revenue collection. One motive has been to reduce dependence on external assistance. From FY2011/12–FY2015/15, total revenue has increased from 21.95 per cent of GDP to 24.15 per cent of GDP, mainly due to an increase in tax and non-tax revenues, which overcompensated the decrease of on-budget external grants.

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In recent years, the authorities have redoubled their efforts to increase revenue generation, undertaking various reforms. A series of studies have been undertaken to inform these reforms. The IMF Policy Support Instrument programme, which started in 2013, specifically focused on increasing domestic revenues. The Office of the Auditor General conducted a series of performance audits of the tax system and made a range of recommendations. Rwanda undertook a TADAT (tax administration diagnostic assessment tool) assessment, which also yielded some reforms in strengthening taxpayer registries and electronic filing, and reduced outstanding stock of arrears more efficiently.  

The most important improvements were made with regard to tax administration. Responsibility for collection of local taxes was transferred to the Rwanda Revenue Authority (RRA). Auditing procedures have undergone continuing improvement, and a system of large taxpayer administration was developed. The RRA has been implementing various reforms to improve tax registries and electronic filing, such as enhanced use of electronic billing (e-billing) machines, e-tax enhancements and electronic cargo tracking systems. Tax policy reforms included increased value added tax (VAT) on mobile airtime, royalty taxes on mining and taxes for special petroleum and infrastructure funds. These changes followed IMF technical assistance recommendations. In mid 2017, Parliament approved a revised fixed asset tax. The government plans to consider several excise taxes, but the anticipated changes are expected to be small and will not significantly increase revenue. As a result of the above-mentioned reforms, notably the improvements made towards tax administration, tax and non-tax revenue (excluding grants) rose from 12.4 per cent of GDP in FY2011/12 to 18.3 per cent in FY2015/16, which is among the higher ratios in sub-Saharan Africa. Total tax revenue rose from 11.7 per cent of GDP in FY2011/12 to 15.7 per cent in FY2015/16.

The largest tax-revenue components are income tax (PAYE), contributing 23.3 per cent of total tax; domestic VAT (21.7 per cent); and company/profit tax (16.1 per cent). On the external sector side, VAT on imported products, excise customs and import duties add up to 25 per cent of total tax revenue.

Non-tax revenue is relatively small. Among its most important components are earnings for United Nations peacekeeping operations carried out by Rwandan troops, which are of course largely offset by expenditure on carrying out these operations. Non-tax revenue also includes a variety of administrative fees and charges.

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27 IMF, Staff Report for the 2017 Article IV Consultation, June 2017, p. 7.
28 Ibid.
29 Ibid.
30 Calculations by the author based on the MINECOFIN macroeconomic framework.
Table 2.2: Rwanda, tax revenue breakdown

<table>
<thead>
<tr>
<th>Tax type</th>
<th>Actual FY2015/16 (in billion FRW)</th>
<th>Share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>PAYE</td>
<td>229.7</td>
<td>23.3</td>
</tr>
<tr>
<td>Profit tax (company income tax (CIT), personal income tax (PIT) and withholding (WHT))</td>
<td>159.3</td>
<td>16.1</td>
</tr>
<tr>
<td>VAT</td>
<td>323.2</td>
<td>32.8</td>
</tr>
<tr>
<td>VAT customs</td>
<td>109.1</td>
<td>11.1</td>
</tr>
<tr>
<td>VAT domestic</td>
<td>214.1</td>
<td>21.7</td>
</tr>
<tr>
<td>Excise duties</td>
<td>138.1</td>
<td>14.0</td>
</tr>
<tr>
<td>Excise customs</td>
<td>67.5</td>
<td>6.8</td>
</tr>
<tr>
<td>Excise domestic</td>
<td>70.5</td>
<td>7.1</td>
</tr>
<tr>
<td>Mining royalties</td>
<td>3</td>
<td>0.3</td>
</tr>
<tr>
<td>Import duties</td>
<td>72.9</td>
<td>7.4</td>
</tr>
<tr>
<td>Road fund</td>
<td>37.3</td>
<td>3.8</td>
</tr>
<tr>
<td>SR levy</td>
<td>8.7</td>
<td>0.9</td>
</tr>
<tr>
<td>ID levy</td>
<td>8.8</td>
<td>0.9</td>
</tr>
<tr>
<td>Other taxes</td>
<td>57.4</td>
<td>5.8</td>
</tr>
<tr>
<td>Total</td>
<td>986.7</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Source: Rwanda Revenue Authority Annual Report FY2015/16.

Rwanda has potential to broaden its tax base. Several improvements can still be made to increase coverage. The most likely short-term improvements in revenue collection would come from reforms in tax administration. The tax payer register is currently being updated to improve its quality, and there is scope to increase tax collection from the rural areas. Tax collection efficiency can be further improved. A specific opportunity is in recently introduced electronic billing (e-billing) machines to improve VAT compliance. These machines have been put in place, but are not yet functioning optimally. In the long run, Rwanda could benefit from additional revenue gains when the economy becomes less cash-based and more taxpayers in the rural areas can be reached, such as subsistence farmers and people living in very remote areas.

Tax policy options present fewer possibilities for improvement in the near future. The authorities have not indicated that they plan to consider changes in tax policy apart from the revision of the fixed asset tax. The additional revenue generation of this tax will depend on the threshold set for companies to pay. The IMF believes the threshold is set too high, and that this will limit revenue collection. The latest IMF estimates (July 2017), which generally foresee a reduction in overall revenue as a percentage of the GDP, do not take into account the effects of the property tax law. In the medium to longer term, possibilities exist to gradually lower the threshold on the property tax and adjust the tax incentives for international companies. However, the extent to which this will take place will be influenced by the debate on whether Rwanda needs low taxation in order to attract investments.

The potential for improved local government revenue performance is not clear. Since 2014, the RRA has been collecting local taxes, which comprise two main taxes (on fixed assets and on rental income) as well as a wide range of fees. The overall revenue generated from local taxation is small: according to Budget Framework Paper estimates, local government accounts for only 0.4 per cent of all of Rwanda’s direct taxation. The RRA has made
an effort to enhance local taxation collection by introducing declarations made via mobile telephones and by outsourcing collection (to a single company). Further reforms are planned, including implementation of a geographic information system and a mobile app to collect fees. The RRA has also tried to reach more people by setting up new revenue collection centres. Some interviewees believe the RRA could do more to increase the local-level tax base, e.g. investing in tax education. Nevertheless, the RRA takes the view that just about all feasible policy changes to enhance local tax collection are already in place, and that further revenue enhancement would have to come through improved administration.

The policies of export promotion for attracting private sector financing have implications for revenue generation, since these policies include tax incentives. The IMF and the government are carrying out a tax expenditure analysis to determine to what extent the tax incentives are in proportion to the expected investments they would generate. There is a difference of opinion as to what extent tax incentives are effective, with a fear that Rwanda may be prone to aggressive external parties taking advantage of its tax and investment regime. The RRA noted that the investment promotion law is undergoing revision as well, with the aim of setting up a monitoring and evaluation system to monitor the investments approved by the Rwanda Development Board. In summary, investment promotion measures are under scrutiny, but are nevertheless expected to affect revenue collection, at least in the short term.

All in all, major increases in revenue collection appear unlikely in the short run, as many reforms have already been implemented, and increasing tax expenditures have shifted the authorities’ focus to protecting rather than increasing revenue collection. The current IMF programme still includes elements to support improvement of tax collection, but its focus has shifted towards export promotion and exchange rate management. The Budget Framework Paper for FY2017/18–FY2019/20 expects tax revenue to decline as a percentage of GDP from the estimated 15.6 per cent in 2016/17 to 15.3 per cent in 2017/18 and 14.9 per cent in FY2018/19–FY2019/20.

External aid

In the last decade, official development assistance (ODA) has increased in monetary value but has declined as a percentage of gross national income (GNI) (see Figure 2.14).

![Figure 2.14: Rwanda, ODA received 2000–2015](https://data.worldbank.org/data-catalog/world-development-indicators).

The share of grants in overall revenue has been diminishing accordingly. Rwanda used to rely heavily on donor financing: until FY2012/13, grants accounted for over 40 per cent of total government revenue, but this number...
declined to around 24 per cent in FY2015/16. This partly reflects an increase in Rwanda’s own revenue collection, and a reduced dependence on aid. It is important to note, however, that some in-kind grants are not recorded in the budget and would be difficult to value.\textsuperscript{31} On-budget foreign aid is presented in the budget laws, but data from the executed budget provide no information on the actual foreign financing that was disbursed. According to the ODA Report FY2015/16, in that fiscal year 82.7 per cent of traditional ODA was recorded on-budget.\textsuperscript{32} This means it is estimated that 17.3 per cent of traditional ODA is provided off-budget.\textsuperscript{33}

Rwanda – like some other sub-Saharan economies – has secured an increased flow of concessional loans, with a high grant component. This partly compensates for the reduced foreign-grants inflow.

Figure 2.15: Share of grants in total government revenue

\textit{Source: MINECOFIN Macro-Fiscal Framework, July 2017.}

Although the share of grants in total revenue has been declining, Rwanda remains a favoured destination for aid, compared to other countries in the region. Specific donors have increased their support to Rwanda. The Ministry of Health, in particular, mentioned that specific grant proposals are being prepared to fill funding gaps in sector plans. For coming years, an increased grants flow would not be a completely unrealistic possibility. Over the longer term, especially if Rwanda succeeds in achieving middle-income status, ODA is set to decline significantly.

2.2.2 Government expenditure

Current expenditure remained at about 14.5 per cent of the GDP between FY2010/11 and FY2015/16. A modest increase in the wage component (from 3.3 to 3.8 per cent of the GDP) and interest payments (from 0.4 to 0.9 per cent of the GDP) has been compensated for by decreases in goods and services purchases (from 3.4 to 2.8 per cent) and overall transfers (from 5.3 to 4.8).
The government’s capital expenditure declined from 12.0 per cent of GDP in FY2010/11 to 11.3 per cent of GDP in FY2015/16. Foreign-financed capital expenditure dropped from 6 to 4.3 per cent of GDP, and this was not fully offset by the increase of domestic capital expenditure from 6 to 7 per cent of GDP.

Rwanda’s expenditure outturn is high, meaning most allocated resources are indeed spent. The latest Public Expenditure and Financial Accountability (PEFA) Assessment (2016) found aggregate expenditure outturn was 109.8 per cent in FY2011/12; 112.1 per cent in FY2012/13; and 110.9 per cent in FY2013/14 (Figure 2.18).  
34 Compared to neighbouring countries such as Kenya, where actual expenditures are significantly lower than the original and revised budgets, 35 and Tanzania and Uganda, which in the majority of budget years also face negative expenditure deviations, 36 Rwanda’s expenditure credibility is quite good and its expenditure outturn high.

---

In line with its fiscal consolidation strategy to decrease the current account deficit, the government aims to control its expenditures in the next couple of years. The government has committed itself to keeping the growth rate of current expenditure and net lending below the GDP growth rate, which means the ratio of current expenditure to GDP will decline.37 For FY2017/18, the government aims to focus capital expenditure on completing ongoing and pipeline projects. It plans to limit capital spending to 9.5 per cent of GDP for FY2017/18–FY2019/20, reflecting the reality of reduced availability of external assistance, but also to help reduce the fiscal deficit to the 3 per cent East African Community norm. This approach is intended to be consistent with the present prudent fiscal policy and with the government’s general policy aim of increasing the ratio of private to public investment.

2.2.3 Public debt

In 2005, Rwanda received debt relief under the Heavily Indebted Poor Countries Initiative and the Multilateral Debt Relief Initiative, which reduced the ratio of its government external debt-to-GDP to 25 per cent in 2005. Since that period, Rwanda’s public debt has increased, as can be seen in Figure 2.19.

---

Debt-to-GDP has risen significantly since 2014. The government took on debt to finance large investment projects, such as the expansion of RwandAir, the Kigali Convention Centre and the Bugesera International Airport. The declining availability of project grants has meant that the government also has had to contract (concessional) loans for smaller projects.

The government aims, as a matter of policy, to finance its fiscal deficit mainly with concessional external loans. Over the FY2017/18–FY2019/20 period, net domestic financing is planned to be close to zero, which would reduce the internal debt stock as percentage of GDP. External public debt would still grow, from 29.8 per cent of GDP to about 38 per cent of GDP in 2020. Since the financing would be concessional, the net present value would be only 26.9 per cent in 2020, below the East African Community norm of 50 per cent. A debt sustainability analysis carried out by the IMF in 2016 shows that, except from the year 2023 when Rwanda’s Eurobond must be refinanced, the baseline sustainability indicators will remain below the danger thresholds. IMF staff rated the risk of debt distress for Rwanda as ‘low’, as more than half (58 per cent) of Rwanda’s external debt is concessional. Another positive aspect is that Rwanda’s debt definition takes into account contingent liabilities related to large public (-private) sector investments, such as the new airport in Bugesera.

Figure 2.19 shows Rwanda’s public debt consists largely of external debt. The debt flow contributes to financing the current account deficit. From this perspective, Rwanda may face some risk if it falls short of meeting its objective of reducing its trade deficit, especially in view of the fact that it cannot rely on grants. Therefore, the government aims to maximize concessional funding and to develop a domestic capital market capable of taking on more of the government’s financing needs. Policymakers also hope to find ways to lengthen domestic debt maturities. In addition, policymakers will continue to search for ways to stimulate greater direct investment flow.

The government has actively courted private-sector investment, emphasizing public-private partnerships. While main contingent liabilities of large (public-private) projects are incorporated in debt forecasts, the investments in the electricity sector may create a future liability for the government. Rwanda has long recognized that energy, and especially electrical power, is fundamentally important for development. Private investors depend on steady, reliable power. For this reason, Rwanda has invested heavily in the sector. Thus far, however, demand for power has fallen short of what Rwanda can now provide. The shortfall of demand implies that Rwanda may have overinvested in the sector. The World Bank is currently designing a project to support sustainable financing in the energy sector.

Rwanda has also undertaken an initiative to enable sub-national government entities to borrow funds themselves, introducing regulations to enable such entities to secure credit ratings. Guidelines were published in 2017, and it is hoped that the first sub-national bond issues will soon take place. Still, the prospect that municipal bonds will serve as a viable funding source remains limited. Administrative capacity and the ‘private-sector’ mindset are yet to be introduced at the local level. Furthermore, there is some concern about the prospect of Rwanda accumulating more debt, even at sub-national levels.

2.3 Implications for the Fiscal Space Analysis

Rwanda’s macroeconomic context has led to a change in fiscal policy. Over the past quarter century, Rwanda has been one of Africa’s most ambitious reformers and one of its fastest growing economies. The government is extremely committed to lift Rwanda to a higher income status. In recent years, in furtherance of this policy approach, Rwanda has invested heavily in its economic growth. Partly for this reason, Rwanda is now facing a
situation in which it must carefully control its current account deficit, at least over the next few years. This means that the coming years could be years of slower growth and tighter fiscal constraints.

**This leaves the government with limited options to increase fiscal space.** Rwanda’s fiscal policy has, as a result of these developments, shifted from a rather expansionary approach to a more prudent policy, aiming at reducing the fiscal deficit and maintaining debt sustainability. Since the government is also facing a reduced inflow of external grants, and is not expecting a large increase in its own tax and non-tax revenue, this means Rwanda needs to control its expenditure to realize a lower fiscal deficit.

**This context needs to be taken into account for the projection exercise and when advocating for increased expenditure on behalf of Rwanda’s children.** It may mean priority expenditure can only be increased up to a certain level, to ensure that sufficient resources are available to enable the country to sustain its growth.
3. Priority expenditure

This chapter describes in more detail which functional items of the budget were selected as ‘priority’ expenditure for the purposes of this exercise, and analyses how this ‘priority’ expenditure has evolved over the past years. The chapter subsequently discusses the policy context to priority expenditure, and analyses budget allocations, spending profiles and sector-specific challenges for each of the selected priority sectors.

3.1 Priority-expenditure composition and recent evolution

3.1.1 Composition of priority expenditure

As explained in Section 1.2 of Chapter 1, this analysis defines ‘priority expenditure’ as spending which is particularly relevant to children. The point is simply to categorize expenditures of priority interest to children, and as such, the composition of ‘priority’ expenditure has been chosen by UNICEF and the consultants.

For Rwanda, ‘priority’ expenditure categories for children comprise the ‘functional’ expenditure categories. Since FY2015/16, the Government of Rwanda has published annexes of its budget execution reports, which incorporate tables that show executed budget data in functional (i.e. per sector) and programme (i.e. per programme and sub-programme) classifications. The Fiscal Space Analysis works better using these types of classifications, because they make it easier to classify expenditure into more and less child-friendly categories in comparison to an ‘institutional’ classification. Still, even with a functional classification, the selection of ‘child-friendly’ (sub-)sectors is somewhat arbitrary, subject to choices made by the consultants and UNICEF. It is important to remember that the ‘child-sector’ character of a given kind of expenditure is more a matter of degree: in principle, almost all kinds of expenditure are likely to be somewhat beneficial for children. Nevertheless, the sectors selected are surely relevant to children and increasing spending in these sectors is relevant for children’s development and contributes to overall socioeconomic growth.

For Rwanda, the following functional categories of expenditure were selected as benefiting children and are hence ‘priority’ in character.

**Table 3.1: Composition of ‘priority’ expenditure**

<table>
<thead>
<tr>
<th>Social sector</th>
<th>Code</th>
<th>Title</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health</td>
<td>707</td>
<td>Health</td>
<td>The entire health sector was selected as priority expenditure because the sub-sectors changed from FY2015/16 to FY2016/17, which made it not possible to maintain a selection of sub-sectors.</td>
</tr>
<tr>
<td>Education</td>
<td>7091</td>
<td>Pre-primary and primary education</td>
<td>This excludes post-secondary education and research and development (R&amp;D) in education, as these sub-sectors do not directly benefit children.</td>
</tr>
<tr>
<td></td>
<td>7092</td>
<td>Secondary education</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7095</td>
<td>Education not definable by level</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7096</td>
<td>Subsidiary services to education</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7098</td>
<td>Education n.e.c.</td>
<td></td>
</tr>
</tbody>
</table>
3. Priority expenditure

<table>
<thead>
<tr>
<th>Social sector</th>
<th>Code</th>
<th>Title</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Social protection</td>
<td>710</td>
<td>Social protection</td>
<td>The entire social protection sector was selected because the sub-sectors changed from FY2015/16 to FY2016/17.</td>
</tr>
<tr>
<td>WASH</td>
<td>7063</td>
<td>Water supply</td>
<td>This is a sub-category of 706 housing and community amenities.</td>
</tr>
</tbody>
</table>

Figure 3.1 shows the composition of priority expenditure. The bulk of the priority expenditure consists of spending on health and education.

![Figure 3.1: Composition of priority expenditure, US$ million (2015 prices)](source: MINECOFIN, Budget Execution Reports FY2015/16–FY2016/17.)

3.1.2 Evolution of priority expenditure

Budget execution data reported by functional classification is available only for the last two budget years (see Figure 3.1). To describe the evolution of priority expenditure, data from the revised budget laws have been used for the period FY2011/12–FY2014/15. While this is technically not actual expenditure data, the previous chapter has found budget execution rates are relatively high in Rwanda, and therefore using the revised budget data can give some indication of the recent trend in priority spending.

Figure 3.2 demonstrates the different functional categories of priority expenditure as share of total expenditure (as reported for FY2015/16 and FY2016/17) and as share of the total revised budget (for FY2011/12 to FY2014/15). The trend appears to be uneven, with fluctuating shares per category. The total of priority expenditure as share of total functional expenditure increased to 26.8 per cent in FY2015/16, but dropped again in FY2016/17 to 24.5 per cent.
Figure 3.2: Evolution of priority expenditure, as percentage of total expenditure
Note: the functional category of water supply was negligible in FY2011/12 and not included in the revised budget law for FY2012/13.

Figure 3.3 converts the revised budget allocations (FY2011/12–FY2014/15) and the actual expenditures (FY2015/16–FY2016/17) expressed in current FRW to constant US dollars (2017 prices) to demonstrate real changes in absolute allocations. In real terms, the only category which visibly received additional funding was social protection. Health and education spending has fluctuated over the past six years, but has not increased in real terms when comparing FY2011/12 to FY2016/17.

Figure 3.3: Evolution of priority expenditure, constant US$ million (2017 prices)
Note: The functional category of water supply was negligible in FY2011/12 and not included in the revised budget law for FY2012/13.

3.1.3 Benchmarking of priority expenditure against international benchmarks

Countries and international organizations have tried to formulate certain international benchmarks, targets or floors regarding social sector spending. These benchmarks provide some guidance to countries on what would be appropriate to spend on various social sectors. Below, Rwanda is compared to some of these benchmarks, as well as to some other countries with higher incomes. While this puts Rwanda’s spending levels into context, it does not mean Rwanda’s results are below average, nor should Rwanda aim for a certain level of spending. It should be emphasized that global benchmarks for social sector spending should be used for guidance as they are not
adequate measures of adequacy of spending in themselves. There are many country-specific factors that should be considered to determine the appropriate amount of funding to be spent. In addition, the quality of services cannot be expressed by spending levels. A country that spends more on education does not necessarily obtain better results in this sector than a country that spends less on education. Efficiency and effectiveness of spending greatly influence its impact.

UNESCO has set two benchmarks for spending on education. Governments should spend between 15 per cent and 20 per cent of their national budgets on education (countries furthest from the targets will need to aim for the higher end of this range), and low and lower-middle income countries in particular should spend at least 3.4 per cent of GDP on pre-primary, primary and lower secondary education or 5.4 per cent of GDP across all education levels. Figure 3.4 shows Rwanda is slightly below both benchmarks.

Figure 3.4: Rwanda’s education expenditure against international benchmarks
Source: MINECOFIN Revised Budget Finance Laws FY2011/12–FY2014/15; MINECOFIN, Budget Execution Reports FY2015/16–FY2016/17. This figure reflects the entire education expenditure (not only the selected categories mentioned in Table 3.1).

Figure 3.5 shows results from upper- and lower-middle-income countries and from a selection of high-income countries which were mentioned in the Vision 2050 blueprint as leading examples. It appears that Rwanda’s share of spending as percentage of total expenditure is at similar levels as Estonia and Finland, but below that of Israel and a great deal below that of Singapore. It should be noted that spending is very country-specific, and by no means should Rwanda mirror itself to spending similar amounts as high-income countries. These numbers merely present how Rwanda’s spending rate relates to other countries. High income countries may already have attained a certain level of quality in their education system, which allows them to spend less on this sector. What may be more relevant is the fact that upper- and lower-middle-income countries, on average, spend more than 15 per cent of their budget on education. Rwanda may want to aim at reaching at least the 15 per cent benchmark as part of its desire to attain middle-income status.

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In the Abuja Declaration on HIV/AIDS, Tuberculosis and other Related Infectious Diseases, African Union countries set a target of allocating at least 15 per cent of their annual budget to the health sector. In addition, research points at a spending target of 5 per cent of GDP on health. Figure 3.6 shows that Rwanda does not meet both targets. The increasing gap between the target of the Abuja Declaration and the money spent on health in FY2016/17 may be of concern.

Figure 3.7 shows Rwanda is, by far, not the only country with government expenditure of less than 15 per cent of total expenditure on health. The five high-income countries mentioned in the Vision 2050 blueprint all spend less than 15 per cent on health – but all more than Rwanda. Interestingly, the gap for lower-middle income countries is quite significant – these countries spent approximately 7 per cent of their budget on health. In that respect, Rwanda is already spending more than the average of lower-middle income countries.

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47 Data on upper-middle income countries was not available.
Social protection spending is to a large extent dependent on the country context. Still, some international benchmarks have been set. In 2008, at the African Union Windhoek Conference, African governments committed to a basic social protection floor, the cost of which was determined at 4.5 per cent of GDP. In addition, the International Labour Organization and others have estimated the level of government spending needed to provide basic social protection at between 2.9 per cent and 5.2 per cent of GDP. Rwanda’s spending on social protection is below these targets (see Figure 3.8).

However, it may be that these targets are not very realistic. A World Bank study found that low-income and middle-income countries spend 1.5 per cent and 1.6 per cent of GDP respectively on social safety nets. Higher-income countries spend 1.9 per cent of GDP on social protection. In this respect, Rwanda’s average expenditure of 1.2 per cent of GDP is still below average, but the gap is not as big as when compared to the international benchmarks in Figure 3.8. The study also found considerable variation across countries (e.g. with 4.8 per cent of GDP).
GDP, Sierra Leone spends more on social safety than Croatia, with 3.6 per cent). This indicates levels of social protection are very country-specific, and one should look at the results in addition to monetary benchmarks.

With regard to water supply, a target of 0.5 or 1 per cent of GDP could be used. This is based on two components. First, the commitment made at the 2008 African Union eThekwini meeting by several African ministers of health and/or water,\(^{50}\) to spend 0.5 per cent of GDP on sanitation and hygiene. Second, a 1 per cent benchmark suggested by the 2006 Human Development Report for low-income countries to be spent on water supply and sanitation together.\(^{51}\) Rwanda’s average expenditure on water supply between FY2013/14 and FY2015/16 was 0.5 per cent of GDP.

3.1.4 The position of priority expenditure in past and current strategies

The evolution of priority expenditure should be seen in a broader policy context. Vision 2020 has been further operationalized through medium-term strategies, which have been increasingly focused on economic development. The first implementation strategy was the Poverty Reduction Strategy (PRSP), which covered the period 2002–2006. The government concluded that under the PRSP “the social sectors (particularly health and education) had been well addressed, but the real economy, i.e. the sectors dealing with the production of goods and services, did significantly deliver on the specified targets.”\(^{52}\) At the same time, while non-income poverty indicators improved, the poverty rate only decreased by 2.2 per cent. This caused a policy shift in the approach to development. The second five-year plan to implement Vision 2020 was therefore rebranded as the Economic Development and Poverty Reduction Strategy (EDPRS) and put economic growth at the core of its policy, along with further decentralization to promote citizens’ involvement. It included three flagship programmes: Sustainable Growth for Jobs and Exports, Vision 2020 Umurenge Programme (integrated rural development programme to eradicate extreme poverty) and Good Governance.\(^{53}\) EDPRS I succeeded in achieving both economic growth and poverty reduction, as poverty decreased from 57 per cent in 2006 to 45 per cent in 2011, measured along the national poverty line.\(^{54}\)

The development approach in EDPRS II is similar to its predecessor. Under EDPRS II, the largest sectors under the definition of ‘priority’ expenditure, i.e. education and health, do not belong to the four thematic priority areas. While social protection is defined under one of the EDPRS II core thematic areas, education and health can be found under the ‘foundational issues’ that “reflect long-term ongoing priorities where, in many cases, significant progress has already been made during EDPRS I. These shall be of continued focus for the nation in order to lay a firm foundation for the emerging priorities designed and implemented under the thematic areas.”\(^{55}\)

The EDPRS II is costed, and spending targets have been set for allocation to health, education and social protection. Education takes the largest share of the budget allocated to thematic area ‘productivity and youth employment’. Health and education are the largest sectors under the foundational issues. The subsequent sections discuss in more detail to what extent these spending targets have been adhered to.

\(^{50}\) For Rwanda, the declaration was signed by the Minister of State in Charge of Water and Mines.


\(^{52}\) Economic Development and Poverty Reduction Strategy (EDPRS) II.

\(^{53}\) Economic Development and Poverty Reduction Strategy (EDPRS) I.


\(^{55}\) Ibid.
The position of the health and education sector could change in the next seven-year implementation plan. The National Strategy for Transformation (NST1) is expected to have a dedicated social pillar, of which the key objectives are said to be:

1. Enhancing graduation from poverty and extreme poverty and promoting resilience. This includes upgrading and improving of quality of social protection programmes.

2. Eradicating malnutrition. Nutrition is one of the five key areas under the social pillar, and thus gets a more prominent place, when compared to EDPRS II, where it was one of eight foundational sectors.

3. Quality health care.

4. Quality education. Whereas in EDPRS II, the focus of education was on technical vocational education and training, the outline now seems to be more balanced, with renewed attention to pre-primary and basic education.

5. Basic infrastructure. This includes access to water and sanitation.

After years of investing heavily in much needed infrastructure, the government plans – partly because of the macroeconomic situation as described in the previous chapter – to lower public investment to these sectors. This may lead to a renewed focus on the social sectors in the government’s strategy for the coming years. At the time of writing (2017), the NST1 has not yet been costed – so it is not possible to say if these sectors will also be prioritized in terms of budget allocations. The layout of the plan is however promising in terms of priority-setting towards child-friendly sectors.

### 3.2 Sector-specific profiles

This section provides an aggregate overview of the spending profile of each sector. It first briefly assesses the main achievements and outstanding reform challenges in the sector, continues with an assessment of the financing needs and the level of external financing, and finally looks at its fiscal performance with regard to budget execution rate, the level of decentralization and the recurrent development expenditure ratio.

#### 3.2.1 Education

**Achievements and key policy challenges**

With regard to the selected expenditure categories under the education sector (pre-primary, primary and secondary education), remarkable progress has been made in increasing the enrolment rates in primary and secondary
education. All children are entitled to 12 years free education, and education is compulsory between the ages of 7 to 16. The primary net enrolment rate (NER) was 97.3 per cent (girls 98 per cent) in 2015. However, quality in education has now been placed at the forefront as a challenge, which requires reform. The graduation rate at the end of primary school is below the sub-Saharan low income countries’ (LIC) average of 70 per cent. The lower secondary school enrolment rate is also below the LIC average of 39.6 per cent and far below that of leaders in sub-Saharan Africa, such as Kenya. Of particular concern are the inequalities between urban–rural and high–low income households, a high teacher-to-pupil ratio at primary level (58:1 in 2015), and little access to pre-primary education with a NER of 14.2 per cent.

**Financing needs in the education sector: higher than the actual funds spent**

The costed FY2013/14–FY2017/18 Education Sector Plan includes planned funding to the sector and financing needs based on its plan, and projected a financing gap. Actual spending in the education sector has been about 80 per cent of the planned funding, and around 72 per cent of funds that would be needed to fully implement the education sector plan. Funding to the sector is thus lower than planned in the EDPRS II, and lower than the sectors’ indicated needs. Especially in FY2015/16 and FY2016/17, actual expenditure is well below the funds projected to be needed to execute the sector plan.

**Table 3.3: Executed budget compared to planned needs and available funds in the Education Sector Plan**

<table>
<thead>
<tr>
<th></th>
<th>FY2012/13</th>
<th>FY2013/14</th>
<th>FY2014/15</th>
<th>FY2015/16</th>
<th>FY2016/17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expenditure</td>
<td>207.7</td>
<td>234.3</td>
<td>214.4</td>
<td>204.8</td>
<td>213.9</td>
</tr>
<tr>
<td>Funds projected to be available</td>
<td>232.3</td>
<td>265.5</td>
<td>269.1</td>
<td>285.7</td>
<td>307.7</td>
</tr>
<tr>
<td>As percentage of expenditure</td>
<td>89%</td>
<td>88%</td>
<td>80%</td>
<td>72%</td>
<td>70%</td>
</tr>
<tr>
<td>Funds projected to be needed</td>
<td>232.3</td>
<td>302.8</td>
<td>289.0</td>
<td>317.8</td>
<td>355.6</td>
</tr>
<tr>
<td>As percentage of expenditure</td>
<td>89%</td>
<td>77%</td>
<td>74%</td>
<td>64%</td>
<td>60%</td>
</tr>
</tbody>
</table>

Source: MINECOFIN, Revised Budget Finance Laws FY2011/12–FY2014/15; MINECOFIN, Budget Execution Reports FY2015/16–FY2016/17; Republic of Rwanda Ministry of Education, Education Sector Strategic Plan 2013/14–2017/18, October 2013. This figure reflects the entire education expenditure (not only the selected categories mentioned in Table 3.1).

**Execution rates: high**

The sub-sectors (highlighted in blue) of the education sector, which were selected as ‘priority’ expenditure, present over three quarters of total education expenditure. In FY2016/17, 83 per cent of the executed education budget was in the categories defined as priority.

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56 International Monetary Fund, Rwanda Selected Issues, July 2017.
Table 3.4: Composition of the education budget

<table>
<thead>
<tr>
<th>Budget code</th>
<th>Category</th>
<th>FY2015/16</th>
<th>FY2016/17</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Expenditure (FRW billion)</td>
<td>Share in total education budget</td>
<td>Expenditure (FRW billion)</td>
</tr>
<tr>
<td>709</td>
<td>Education</td>
<td>204.8</td>
<td>213.9</td>
</tr>
<tr>
<td>7091</td>
<td>Pre-primary and primary education</td>
<td>71.8</td>
<td>35%</td>
</tr>
<tr>
<td>7092</td>
<td>Secondary education</td>
<td>64.7</td>
<td>32%</td>
</tr>
<tr>
<td>7093</td>
<td>Post-secondary non-tertiary education</td>
<td>3.0</td>
<td>1%</td>
</tr>
<tr>
<td>7094</td>
<td>Tertiary education</td>
<td>40.1</td>
<td>20%</td>
</tr>
<tr>
<td>7095</td>
<td>Education not definable by level</td>
<td>6.7</td>
<td>3%</td>
</tr>
<tr>
<td>7096</td>
<td>Subsidiary services to education</td>
<td>1.5</td>
<td>1%</td>
</tr>
<tr>
<td>7097</td>
<td>R&amp;D education</td>
<td>1.2</td>
<td>1%</td>
</tr>
<tr>
<td>7098</td>
<td>Education n.e.c.</td>
<td>15.8</td>
<td>8%</td>
</tr>
<tr>
<td>Priority spending</td>
<td></td>
<td>160.4</td>
<td>78%</td>
</tr>
<tr>
<td>Other education</td>
<td></td>
<td>44.3</td>
<td>22%</td>
</tr>
</tbody>
</table>


Execution rates are close to 100 per cent, and very little reallocation takes place among sub-sectors in the execution process (except for the category of ‘education not definable by level’, which is intended to be reallocated as execution proceeds). Tables 3.5 and 3.6 show high execution rates against the revised budget in pre-primary and primary, and secondary education, for FY2015/16 and FY2016/17.

Table 3.5: Budget outturn FY2015/16 in education priority sectors (FRW billion)

<table>
<thead>
<tr>
<th>Budget code</th>
<th>Category</th>
<th>Original budget</th>
<th>Revised budget</th>
<th>Executed budget</th>
<th>% spent of original budget</th>
<th>% spent of revised budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>7091</td>
<td>Pre-primary and primary education</td>
<td>61.3</td>
<td>73.0</td>
<td>71.8</td>
<td>117%</td>
<td>98%</td>
</tr>
<tr>
<td>7092</td>
<td>Secondary education</td>
<td>62.9</td>
<td>66.9</td>
<td>64.7</td>
<td>103%</td>
<td>97%</td>
</tr>
<tr>
<td>7095</td>
<td>Education not definable by level</td>
<td>24.2</td>
<td>6.7</td>
<td>6.7</td>
<td>28%</td>
<td>100%</td>
</tr>
<tr>
<td>7096</td>
<td>Subsidiary services to education</td>
<td>3.1</td>
<td>1.7</td>
<td>1.5</td>
<td>49%</td>
<td>87%</td>
</tr>
<tr>
<td>7098</td>
<td>Education n.e.c.</td>
<td>16.2</td>
<td>16.3</td>
<td>15.8</td>
<td>98%</td>
<td>97%</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>167.6</td>
<td>164.6</td>
<td>160.4</td>
<td>96%</td>
<td>97%</td>
</tr>
</tbody>
</table>

Source: State Law FY2015/16; MINECOFIN, Budget Execution Report FY2015/16.
Table 3.6: Budget outturn FY2016/17 in education priority sectors (FRW billion)

<table>
<thead>
<tr>
<th>Budget code</th>
<th>Category</th>
<th>Original budget</th>
<th>Revised budget</th>
<th>Executed budget</th>
<th>% spent of original budget</th>
<th>% spent of revised budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>7091</td>
<td>Pre-primary and primary education</td>
<td>83.8</td>
<td>90.3</td>
<td>95.1</td>
<td>114%</td>
<td>105%</td>
</tr>
<tr>
<td>7092</td>
<td>Secondary education</td>
<td>53.2</td>
<td>50.8</td>
<td>47.0</td>
<td>88%</td>
<td>93%</td>
</tr>
<tr>
<td>7095</td>
<td>Education not definable by level</td>
<td>18.0</td>
<td>17.3</td>
<td>8.4</td>
<td>47%</td>
<td>47%</td>
</tr>
<tr>
<td>7096</td>
<td>Subsidiary services to education</td>
<td>1.8</td>
<td>1.9</td>
<td>2.5</td>
<td>140%</td>
<td>131%</td>
</tr>
<tr>
<td>7098</td>
<td>Education n.e.c.</td>
<td>27.7</td>
<td>25.0</td>
<td>24.8</td>
<td>90%</td>
<td>99%</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>184.5</td>
<td>185.7</td>
<td>177.8</td>
<td>96%</td>
<td>96%</td>
</tr>
</tbody>
</table>


External financing: 4.2 per cent of total education budget

The on-budget external financing constitutes 4.2 per cent of the overall education budget allocations in FY2016/17, and flows almost entirely to the Ministry of Education. The UNICEF Budget Brief on Education identifies a decreasing trend: external financing fell from 6.7 per cent of the education budget in FY2015/16 to 2.5 per cent in FY2017/18.

Level of decentralization: largest of the social sectors (53 per cent of funds executed by local government)

The programme budget presents expenditure on education as part of the Ministry of Education (MINEDUC) and the districts. According to the budget execution report, districts spent 53.3 per cent of the overall education sector budget in FY2016/17, compared with 56 per cent in FY2015/16. Pre-primary, primary and secondary education expenditure is ‘priority’ – i.e. child-beneficial – expenditure, and districts accounted for 70.6 per cent of education priority expenditure. District expenditure on education was about the same in FY2016/17 (FRW 114 billion) as in FY2015/16 (FRW 114.7 billion). When adjusted for inflation, the amount spent by districts in FY2016/17 is slightly lower.

Districts spent FRW 114.7 billion on education in FY2015/16, or about 98 per cent of their allocated budget. The execution rate (compared with the revised budget) was 95 per cent in FY2016/17, a bit lower than in the previous fiscal year. The programme budget does not include a further breakdown in levels of education.

Recurrent vs. development spending: 82 per cent vs. 18 per cent

The executed budget data available provides no economic classification, and so it is not possible to report on performance on recurrent and development spending. The budget allocations per programme and sub-programme reveal that education funds are allocated to MINEDUC (which reallocates part of the funds to various implementation agencies) and the districts. Together, 82.3 per cent of the budget is allocated to recurrent expenditure, leaving 17.7 per cent to be spent on development expenditure, 4.2 per cent of which is set to be externally financed. Districts allocated 93.6 per cent of their education budget to recurrent expenditure, compared with 68.4 per cent for MINEDUC expenditure. The development budget is thus allocated primarily to the central level.

The UNICEF Budget Brief on Education found that budget allocations showed an increase in recurrent compared to development expenditure from FY2012/13 to FY2017/18.\(^{61}\)
3.2.2 Health

Achievements and key policy challenges

The health sector has made impressive progress in reaching almost universal health care. Health insurance coverage of 91 per cent and community-based health care ensure nearly universal access to basic health care. Child mortality has reduced steadily and immunization coverage is above 95 per cent. Maternal mortality has declined to 210 per 100,000 in 2015 compared to 1,071 in 2000.62 The infant mortality rate stands at 32 deaths per 1,000 live births, while the under-five mortality rate is 50 deaths per 1,000 live births.63

Important reform challenges are still ahead, such as combating undernourishment. The Demographic and Health Survey (DHS) 2014/15 found that 38 per cent of children are stunted, and 14 per cent are severely stunted.64 Inequalities persist in access to health services between rich and poor, e.g. the DHS 2014/15 reports 63.3 per cent of women living in rural areas indicated that they faced at least one problem accessing health care, against 39 per cent of women living in urban areas.65 Other challenges are inadequate quality of services and a shortage of skilled health providers, equipment and supplies.

Financing needs: a reality

The Health Sector Plan, covering the period of EDPRS II (FY2013/14–FY2017/18), contains an extensive costing and funding gap analysis. A financing gap was widely anticipated in the sector plan. The projected available funding was in line with actual expenditures, suggesting a realistic approach in budgeting for the health sector. Still, health expenditure fell short of the funds projected to be needed to implement the Health Sector Plan.

Table 3.7: Executed budget compared to planned needs and available funds in the Health Sector Plan

<table>
<thead>
<tr>
<th></th>
<th>FY2013/14</th>
<th>FY2014/15</th>
<th>FY2015/16</th>
<th>FY2016/17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expenditure</td>
<td>154</td>
<td>200.3</td>
<td>153.8</td>
<td>145.9</td>
</tr>
<tr>
<td>Funds projected to be available</td>
<td>190.2</td>
<td>133.4</td>
<td>138.9</td>
<td>144.8</td>
</tr>
<tr>
<td>As percentage of expenditure</td>
<td>81%</td>
<td>150%</td>
<td>111%</td>
<td>101%</td>
</tr>
<tr>
<td>Funds projected to be needed</td>
<td>205.9</td>
<td>204.6</td>
<td>208.1</td>
<td>226.3</td>
</tr>
<tr>
<td>As percentage of expenditure</td>
<td>75%</td>
<td>98%</td>
<td>74%</td>
<td>84%</td>
</tr>
</tbody>
</table>


External financing: 20 per cent of total health budget

Funds projected to be available included estimates of donor contributions. The sector plan anticipated that donor projects would account for around 31 per cent of the health budget, and that contributions would amount to a steady FRW 62 billion a year. In reality, the budget for FY2016/17 indicates that 20 per cent of the health budget is financed by external grants. The UNICEF Budget Brief on Health for FY2017/18 notes that the share of externally financed funds to the health budget has been declining compared to FY2013/14, when more than half of the entire health budget was funded externally.66 Still, compared to the education sector, health is a key recipient of aid as one fifth of its entire budget and one third of its development budget depend on external financing. In addition, it

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64 Ibid.
is important to remember that these numbers include none of the off-budget external funding to the health sector. The Health Financing Sustainability Policy noted a large amount is still not included in the budget.67

**Budget execution rates: high, but a drop in FY2016/17**

Data on actual spending are available by sector for FY2015/16 and FY2016/17. The sub-sectors of health were differently classified in FY2016/17, moving from six sub-sectors to three; hence, it is impossible to compare spending trends within the sub-sectors.

Health sector execution rates fell sharply in FY2016/17, when 77 per cent of the budget was spent, well below the comparable education sector indicator. This may reflect, at least in part, the difficulty of finding qualified health workers willing and able to fill the sector’s positions, as well as some fundamental differences in the nature of health expenditure compared with education – the health sector has a higher share of development expenditure, which is generally more difficult to spend compared to recurrent expenditure.

**Table 3.8: Budget outturn FY2015/16 and FY2016/17 in health sector (FRW billion)**

<table>
<thead>
<tr>
<th>Health sector</th>
<th>Original budget</th>
<th>Revised budget</th>
<th>Executed budget</th>
<th>% spent of original budget</th>
<th>% spent of revised budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2015/16</td>
<td>154.5</td>
<td>178.6</td>
<td>153.8</td>
<td>100%</td>
<td>86%</td>
</tr>
<tr>
<td>FY2016/17</td>
<td>188.6</td>
<td>189.3</td>
<td>145.9</td>
<td>77%</td>
<td>77%</td>
</tr>
</tbody>
</table>

Source: State Law FY2015/16 and FY2016/17; MINECOFIN, Budget Execution Reports FY2015/16 and FY2016/17.

**Level of decentralization: 18.2 per cent of health budget is executed by local government**

The share of spending by local government is much lower in the health sector than in the education sector. In FY2016/17, 18.2 per cent of total funds was allocated to the district level. The budget execution rate at district level was higher (94.7 per cent of the revised budget allocation) than that of the Ministry of Health (MINISANTE, 73.2 per cent). In FY2015/16, the district execution rate was 99.6 per cent compared with 83 per cent in MINISANTE. The drop in the budget execution rates overall for the health sector in FY2016/17 to 77 per cent was caused by lower outturn at MINISANTE; execution rates at district level remained high.

**Figure 3.11: Share MINISANTE and districts in the health sector**


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**Recurrent vs. development spending: 39 per cent vs. 61 per cent**

The composition of recurrent and development expenditures in the health sector is significantly different from the education sector. In the Budget Law FY2016/17, 61.3 per cent of health sector expenditure is allocated to development expenditure. These funds are almost entirely managed at the central level, with 19.5 per cent funded externally. Districts allocated 91.9 per cent of their budgets to recurrent expenditure. The fact that recurrent expenditure is generally easier to spend (e.g. paying salaries and bills) undoubtedly helps explain the higher district-level execution rate.

![Figure 3.12: Budget allocation to health (economic classification) FY2016/17 (FRW billion)](source: State Law 2016/17.)

### 3.2.3 Social protection

**Achievements and key policy challenges**

Social protection services are crucial, as 39 per cent and 16 per cent of Rwandans still live under the general and extreme poverty line respectively, and health statistics indicate the need for investments in nutrition programmes for the poor. In addition, social protection is crucial in addressing the needs of persons with disabilities and genocide survivors. In parallel with developing comprehensive social protection programmes to address poverty and vulnerability of its populations, the Government of Rwanda has taken up these challenges through a series of homegrown solutions – which are cultural practices translated into development programmes – including the ‘one-cow-per-poor-family’ (Girinka) programme.

According to the World Bank, Rwanda is “among global leaders in building an integrated social protection system in a low income environment that is closely tied to national goals of poverty reduction.”

A flagship intervention is Rwanda’s Vision 2020 Umurenge Programme, which is a large-scale social protection programme comprising cash transfers, public works and financial services. While the results under the social protection programmes have been impressive, further progress is needed in the extension of coverage to all poor households and strengthening the impact of the support to accelerate graduation from poverty. The government is currently working on development of a more comprehensive set of social protection programmes, to increase their impact on communities.

Given that all social protection sub-sectors are arguably relevant for children, the entire social protection sector is defined as ‘priority’ spending for this study.

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Financing needs: envisaged increases did not take place

The Social Protection Strategic Plan includes a summary of the social protection cost projections over the period FY2013/14–FY2017/18. For FY2013/14 and FY2014/15, the revised budget included an amount higher than the costs anticipated in the strategic plan, which indicates a certain priority given to social protection (which would be in line with its position within one of the thematic areas in the EDPRS II). FY2015/16 and FY2016/17 indicate a gap between total estimated costs and the actual spending reported in the executed budget.

Table 3.9: Executed budget compared to planned needs in the Social Protection Sector Strategic Plan

<table>
<thead>
<tr>
<th>Social protection</th>
<th>FY2013/14</th>
<th>FY2014/15</th>
<th>FY2015/16</th>
<th>FY2016/17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total cost estimated in the Social Protection Sector Strategic Plan (FRW billion)</td>
<td>54.8</td>
<td>64.9</td>
<td>73.5</td>
<td>74.5</td>
</tr>
<tr>
<td>Actual spending (FRW billion)</td>
<td>73.2</td>
<td>78.3</td>
<td>61</td>
<td>61.1</td>
</tr>
<tr>
<td>% of costs budgeted in the Social Protection Sector Strategic Plan</td>
<td>133%</td>
<td>121%</td>
<td>83%</td>
<td>82%</td>
</tr>
</tbody>
</table>


External financing: 20 per cent of social protection budget

From the overall social protection portfolio, 20 per cent is externally financed. The UNICEF Budget Brief on Social Protection found a fluctuating trend in external funding to social protection, ranging from 24.6 per cent in FY2013/14 to 12.1 per cent in FY2015/16 and 19.7 per cent in FY2017/18.

Budget execution rates: high, but a drop in FY2016/17

In FY2015/16, the social protection sector comprised six sub-sectors. The largest share of social protection expenditure was allocated to ‘unspecified’ social protection, and about one third was allocated to the budget line 7103 (‘genocide survivors’). The sub-sector categories in the budget for FY2016/17 are different. Unemployment and R&D disappeared, most probably having been integrated into other sub-sectors because of their small sizes.

In FY2015/16 budget execution rates as compared to the revised budget allocation were high for all programmes, although somewhat lower when compared with the original budget, since the revised budget cut almost 20 per cent of the original budget allocated to social protection (FY2015/16, see Table 3.10).

Table 3.10: Composition and performance of the social protection budget FY2015/16 (FRW billion)

<table>
<thead>
<tr>
<th>Budget code</th>
<th>Category</th>
<th>Original budget</th>
<th>Revised budget</th>
<th>Executed budget</th>
<th>% spent of original budget</th>
<th>% spent of revised budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>710</td>
<td>Social protection</td>
<td>75.5</td>
<td>61.5</td>
<td>61.0</td>
<td>81%</td>
<td>99%</td>
</tr>
<tr>
<td>7101</td>
<td>Sickness and disability</td>
<td>0.5</td>
<td>0.8</td>
<td>0.8</td>
<td>157%</td>
<td>99%</td>
</tr>
<tr>
<td>7103</td>
<td>Genocide survivors</td>
<td>27.6</td>
<td>27.6</td>
<td>27.6</td>
<td>100%</td>
<td>100%</td>
</tr>
<tr>
<td>7104</td>
<td>Family and children</td>
<td>5.6</td>
<td>3.7</td>
<td>3.5</td>
<td>62%</td>
<td>94%</td>
</tr>
<tr>
<td>7105</td>
<td>Unemployment</td>
<td>0.5</td>
<td>0.6</td>
<td>0.5</td>
<td>99%</td>
<td>87%</td>
</tr>
<tr>
<td>7108</td>
<td>R&amp;D social protection</td>
<td>0.7</td>
<td>0.1</td>
<td>0.1</td>
<td>17%</td>
<td>94%</td>
</tr>
<tr>
<td>7109</td>
<td>Social protection n.e.c.</td>
<td>40.5</td>
<td>28.7</td>
<td>28.5</td>
<td>70%</td>
<td>99%</td>
</tr>
</tbody>
</table>

Source: State Law FY2015/16; MINECOFIN, Budget Execution Report FY2015/16.

In contrast with FY2015/16, the revised FY2016/17 budget increased the social protection budget. The execution rate was lower in FY2016/17 when compared to the previous fiscal year: 77 per cent of the original budget and 74 per cent of the revised budget.

Table 3.11: Composition and performance of the social protection budget, FY2016/17 (FRW billion)

<table>
<thead>
<tr>
<th>Budget code</th>
<th>Category</th>
<th>Original budget</th>
<th>Revised budget</th>
<th>Executed budget</th>
<th>% spent of original budget</th>
<th>% spent of revised budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>710</td>
<td>Social protection</td>
<td>79.4</td>
<td>82.3</td>
<td>61.1</td>
<td>77%</td>
<td>74%</td>
</tr>
<tr>
<td>7101</td>
<td>Sickness and disability</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>98%</td>
<td>99%</td>
</tr>
<tr>
<td>7103</td>
<td>Genocide survivors</td>
<td>9.4</td>
<td>11.7</td>
<td>11.3</td>
<td>120%</td>
<td>97%</td>
</tr>
<tr>
<td>7104</td>
<td>Family and children</td>
<td>2.8</td>
<td>6.2</td>
<td>1.2</td>
<td>42%</td>
<td>19%</td>
</tr>
<tr>
<td>7109</td>
<td>Social protection</td>
<td>66.8</td>
<td>64.0</td>
<td>48.3</td>
<td>72%</td>
<td>75%</td>
</tr>
</tbody>
</table>


Level of decentralization: districts implement about 50 per cent of the social protection budget

The social protection budget is executed by various ministries, according to their mandate (e.g. school feeding, health insurance). The ministry overseeing social protection programmes is the Ministry of Local Government (MINALOC). Other ministries involved are the Ministry of Disaster Management and Refugees (MIDIMAR) and the Ministry of Gender and Family Promotion (MIGEPROF). The Ministry of Agriculture and Animal Resources (MINAGRI) also provides a programme addressing nutrition and household vulnerabilities. Table 3.12 presents an overview of the main implementers and programmes in social protection, based on (sub-) programme titles in the executed programme budget.

Table 3.12: Social protection by programme FY2016/17 (FRW billion)

<table>
<thead>
<tr>
<th>FY2016/17</th>
<th>Revised</th>
<th>Executed</th>
<th>Execution rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>MINALOC Social protection</td>
<td>20.9</td>
<td>19.2</td>
<td>92%</td>
</tr>
<tr>
<td>Demobilisation, reintegration and reinsertion coordination</td>
<td>5.7</td>
<td>4.5</td>
<td>79%</td>
</tr>
<tr>
<td>Persons with disabilities inclusion and advocacy</td>
<td>0.3</td>
<td>0.3</td>
<td>98%</td>
</tr>
<tr>
<td>MIDIMAR Returnees and refugees management</td>
<td>3.4</td>
<td>0.1</td>
<td>4%</td>
</tr>
<tr>
<td>Disaster management</td>
<td>2.0</td>
<td>0.7</td>
<td>36%</td>
</tr>
<tr>
<td>MIGEPROF Women empowerment</td>
<td>0.1</td>
<td>0.1</td>
<td>77%</td>
</tr>
<tr>
<td>Child rights protection and promotion</td>
<td>2.3</td>
<td>2.1</td>
<td>90%</td>
</tr>
<tr>
<td>Districts Social protection</td>
<td>34.3</td>
<td>27.3</td>
<td>80%</td>
</tr>
<tr>
<td>Undefined</td>
<td>13.2</td>
<td>6.8</td>
<td>51%</td>
</tr>
</tbody>
</table>


Districts also record a relatively high execution rate of the social protection budget (80 per cent), although performance is weaker when compared with the districts’ high levels of execution in education and health. Social protection activities which are ‘undefined’ significantly affect the overall budget turnout.

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71 This is a separate intervention in the Executed Budget by Programme FY2015/16, and most probably included in the functional category of social protection.
**Recurrent vs. development expenditure: 48 per cent vs. 52 per cent**

The executed budget provides no data on the performance of recurrent and development expenditure. The allocations in the Budget Law FY2016/17 suggest that districts are primarily responsible for development expenditure (which may explain why the execution rate is lower than districts’ rates in health and education, in which district budgets are primarily made up of recurrent expenditure). Taken together, 27 per cent of the district budgets consist of recurrent expenditure, with the remaining 73 per cent allocated to development expenditure. Of the development expenditure, 20 per cent is externally financed.

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![Budget allocation to social protection programmes (economic classification) FY2016/17](image)

*Source: State Law 2016/17.*

**3.2.4 Water supply**

**Achievements and key policy challenges**

The National Demographic Health Survey 2014/15 found 73 per cent of households have access to an improved source of drinking water. The most common source is protected springs. Only 10 per cent of households have running water on their premises. Twenty-seven per cent of households use unprotected sources of water, which increases the risk of waterborne diseases. The difference between urban and rural households is quite significant, with 9 per cent of urban households using unsafe water, against 31 per cent of rural households.

According to the FY2017/18 Forward Looking Sector Review Report for the water and sanitation sector, key implementation challenges include a funding gap; sustainability of water and sanitation services (e.g. maintenance); deficits in water production and insufficient mechanisms to treat wastewater; regulation issues, including viability of water tariffs; and a lack of harmonization in the sector.

**Water supply financing needs: very high**

The Water and Sanitation Strategic Plan FY2013/14–FY2017/18 estimated that its five-year plan would require FRW 475.7 billion to implement the activities in water supply, but only FRW 59 billion was available. The sanitation budget was estimated at FRW 54 billion, for which no funds were available. The sector and its stakeholders

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73 Ibid.
have thus faced an enormous financing gap from the outset of the EDPRS II. According to the budget included in the Strategic Plan, the sector would need to spend over FRW 100 billion a year to cover all needs in water and sanitation. The current budget represents only about a quarter of this need.

**Budget execution rate: Drop in FY2016/17**

Available budget data show a decline of both the allocated and the executed budget in FY2016/17 as compared to FY2015/16.

**Table 3.13 Performance of the water supply budget FY 2015/16 and FY2016/17**

<table>
<thead>
<tr>
<th>Water supply</th>
<th>Original budget</th>
<th>Revised budget</th>
<th>Executed budget</th>
<th>% spent of original budget</th>
<th>% spent of revised budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2015/16</td>
<td>35.2</td>
<td>25.3</td>
<td>25.1</td>
<td>71%</td>
<td>99%</td>
</tr>
<tr>
<td>FY2016/17</td>
<td>27.3</td>
<td>27.4</td>
<td>17.6</td>
<td>65%</td>
<td>64%</td>
</tr>
</tbody>
</table>

Source: State Law FY2015/16 and FY2016/17; MINECOFIN, Budget Execution Reports FY2015/16 and FY2016/17.

**Level of decentralization: 35 per cent of water supply budget**

According to the Water and Sanitation Sector Plan, districts carry primary responsibility for water and sanitation services. The programme budget defines ‘water and sanitation’ programmes under the Ministry of Infrastructure (MININFRA) through the Water and Sanitation Authority (WASAC) for each district. Together, these programmes add up to a budget which is slightly higher than the budget specified for the water supply sector. These programmes probably include additional activities, which do not fit the sector definition. The districts are responsible for 35.2 per cent of this budget.

**Recurrent vs. development expenditure: only development, which is one-third externally financed**

Water and sanitation expenditure includes only development expenditure. One third of the funding for water and sanitation is provided by external sources.
3.3 Implications for the Fiscal Space Analysis

The above assessment of priority expenditure reveals some findings which are relevant for the Fiscal Space Analysis.

The National Strategy for Transformation could support an increase in priority expenditure, after years of uneven spending trends. Analysis of previous years shows uneven spending trends in the priority sectors. These trends can be placed in the context of the EDPRS II, which puts more emphasis on other areas. With the new National Strategy for Transformation, in which the social sectors constitute a separate pillar, this trend may be reversed.

The priority sectors are in need of more funding based on their outstanding challenges. Within the sectors, a number of policy challenges remain to be addressed. These seem to be mainly related to improving quality (e.g. in education, enrolment rates are impressive, but quality of education has not evolved at the same pace) and effectiveness (e.g. Rwanda is a pioneer in social protection programmes, but the government is now assessing how to improve targeting), which may indicate that – regardless of the high budget execution rate – Rwanda could make more optimal use of the money being spent. In addition, each sector faces a financing gap, as all sectors received less than they needed based on their sector plans. An increase in priority expenditure is thus necessary to address these challenges.

Compared to other countries, increasing expenditure efficiency (i.e. realizing higher budget execution rates) within the priority sectors is a less likely scenario to generate much fiscal space in Rwanda. Budget execution rates are high in each of the sectors, although all sectors except education recorded lower execution rates in FY2016/17 when compared with the previous fiscal year. This may be related to the fact that these sectors – health, social protection and water supply – have higher levels of development expenditure and higher levels of external financing. While the level of decentralization differs per sector, this does not seem to impact performance of spending. For each sector, district execution rates were reported to be high.

Increased availability of executed budget data, e.g. broken down in recurrent and development expenditure, and offering more information on the execution of foreign aid, would provide more insight in adjustments to be made if Rwanda wants to further improve expenditure efficiency.
4. Fiscal space scenarios

This chapter focuses on options to create fiscal space, and uses the projections of the fiscal space model to calculate what these options would mean in monetary terms.

Section 4.1 sets out the base scenario. It discusses the assumptions used to set the base scenario, and the projection results of running the model based on these assumptions. Section 4.2 presents projections based on a set of illustrative alternative scenarios. The assumptions of each alternative scenario are the same as those of the base scenario, except that one or two assumption lines are changed. The changed assumptions are different per alternative scenario, and are introduced in the first table accompanying each alternative scenario section. Outcomes of each alternative scenario were compared with the outcomes of the base scenario, and each fiscal space option indicates the possible changes in priority allocation per capita and its implication for public debt.

4.1 The base scenario

Assumptions

The projection analysis is carried out first with a ‘base scenario’, a straightforward and non-controversial set of assumptions covering the fiscal years 2017 to 2024. This scenario is based on several key assumptions, such as the growth rates of GDP, the exchange rate and population growth. Other assumptions depend on these key assumptions. Table A.1 in Appendix 1 lists the base scenario assumptions and provides brief explanations for them. Key base scenario assumptions include the following:

Table 4.1: Key assumptions in the base scenario

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<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>6.3</td>
<td>6.5</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.3</td>
<td>7.5</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Population growth</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
<td>2.1</td>
</tr>
</tbody>
</table>

The growth rate of the exchange rate (national currency per US$) would be equal to the differential of the Rwandan and international (US$) inflation rates. Table A.2 in Appendix 1 lists the numerical values of the base scenario assumptions.

These assumptions reflect the following view of Rwanda’s future economic performance:

- The real GDP growth rate is assumed to rise gradually to a 7.5 per cent annual rate in the final projection year.
- Consumer price inflation is assumed to persist at about 4 per cent.
- The population growth rate is assumed to decline gradually.
- The exchange rate assumption reflects the view that the real effective exchange rate is, as the IMF says, basically sustainable, and that further changes in the nominal rate would respond, essentially through market forces, to the evolution of the inflation differential.

76 Thus, for example, certain variables are assumed to grow at the same rate as the nominal GDP – that is, they are assumed to grow at the ‘combined’ rates of real GDP and the GDP deflator.
**Base scenario projection results**

Table 4.2 shows some of the key projection results for the fiscal years 2017 to 2024, based on the base scenario assumptions.

**Table 4.2: Key projection results for the base scenario**

<table>
<thead>
<tr>
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</tr>
</thead>
<tbody>
<tr>
<td><strong>Priority expenditure</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>20.08</td>
<td>20.79</td>
<td>21.56</td>
<td>22.31</td>
<td>23.11</td>
<td>23.99</td>
<td>24.91</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>5.89</td>
<td>5.98</td>
<td>6.07</td>
<td>6.16</td>
<td>6.25</td>
<td>6.35</td>
<td>6.45</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>119.47</td>
<td>127.35</td>
<td>136.45</td>
<td>146.85</td>
<td>158.51</td>
<td>171.44</td>
<td>185.81</td>
</tr>
<tr>
<td><strong>Net internal financing gap (fiscal gap)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>9.30</td>
<td>5.37</td>
<td>1.40</td>
<td>–2.16</td>
<td>–5.58</td>
<td>–8.78</td>
<td>–11.72</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>2.73</td>
<td>1.55</td>
<td>0.39</td>
<td>–0.60</td>
<td>–1.51</td>
<td>–2.33</td>
<td>–3.03</td>
</tr>
<tr>
<td><strong>Fiscal deficit (surplus/deficit)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>–5.45</td>
<td>–4.39</td>
<td>–3.28</td>
<td>–2.31</td>
<td>–1.37</td>
<td>–0.48</td>
<td>0.34</td>
</tr>
</tbody>
</table>

Taken together, the programming assumptions would imply rough stability in the evolution of the economy’s key ratios. Under these assumptions, priority expenditure would be increasing. As the growth rate would remain high, the fiscal deficit would narrow because revenue would rise faster than expenditure. The net internal financing flow would diminish accordingly, both as a percentage of total expenditure and as a percentage of GDP.

The base scenario thus suggests that Rwanda can realize an increase in priority expenditure (from US$119.47 per child to US$185.81 per child), without creating a fiscal gap. Table 4.3 shows that, on average, the overall net internal financing gap would be around zero over the projection period. Government debt-to-GDP ratio would be 42.19 per cent in 2024.

**Table 4.3: Results for the other elements of the fiscal account**

<table>
<thead>
<tr>
<th>Results</th>
<th>Base scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average tax and non-tax revenue/GDP, 2017–2024</td>
<td>17.79</td>
</tr>
<tr>
<td>Average priority expenditure/GDP, 2017–2024</td>
<td>6.16</td>
</tr>
<tr>
<td>Average priority expenditure per child (US$ at 2015 prices and exchange rate), 2017–2024</td>
<td>149.41</td>
</tr>
<tr>
<td>Net internal debt flow/GDP, 2017–2024</td>
<td>0.02</td>
</tr>
<tr>
<td>Total government debt/GDP, 2024</td>
<td>42.19</td>
</tr>
</tbody>
</table>

Table A.3 in Appendix 1 shows the full projection results, based on the base scenario assumptions.

**Base scenario and fiscal space ‘mapping’**

The ‘mapping’ of the government’s funding sources to its expenditure programmes, and its priority expenditure, can be characterized straightforwardly by the government’s overall funding flows. As explained in Chapter 1, the funding flows (i.e. how the government funds its expenditure) broadly comprise the following:
1. Tax and non-tax revenue;
2. External grants; and
3. The net (external and internal) financing of the fiscal deficit.

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

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

Figure 4.1: Rwanda, fiscal mapping chart
Source: RwFS.xlsx.

Figure 4.1 presents a fiscal mapping chart, with FY2017 to 2024 projections according to the base scenario. The projections are shown as percentages of GDP. In the ‘stacked-bar’ presentation, funding sources are above and expenditure flows below the horizontal axis. The sum of everything shown above the horizontal axis effectively funds everything shown below. By definition, the sum of the net external and internal financing flows is the same as the overall fiscal deficit.

For the base scenario, the expenditure flows would imply a negative net internal government debt flow. Under the base scenario, the government deficit would decrease from 5.45 per cent of GDP in FY2017/18 to a surplus of 0.34 per cent in FY2023/24, while the net internal debt flow would decrease from 2.73 per cent of GDP in FY2017/18 to –3.03 per cent in FY2023/24.
4.2 Alternative scenarios

In principle, policymakers have the following general options for enhancing the fiscal space for priority expenditure:

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

Apart from government policy choices, changes in the macroeconomic context can affect the fiscal space. For example, increased GDP growth would increase the fiscal space by increasing tax revenue.

The analysis in Chapter 2 indicated that Rwanda’s options to increase fiscal space within the next seven years are constrained. Rwanda must maintain a prudent fiscal policy, because it cannot afford a drop in foreign reserves and needs to control its external debt. While increasing the tax base is definitely a long-term priority for the government, options to further increase revenue collection will not have significant effects over the projection period, also considering that revenue income is affected by tax expenditures. In addition, external financing is decreasing in relative terms. Much will depend on the success of Rwanda’s policy to attract more foreign investment and private capital. Although options to increase fiscal space are not as evident as for other countries, Rwanda may find some room to manoeuvre.

One possibility would be to increase revenue from own taxation and from external sources. For this reason, the first four alternative scenarios attempt to model changes in revenue collection (efficiency of VAT collection) and grant financing, in order for Rwanda to increase fiscal space:

- Alternative Scenario 1 calculates the result of increased efficiency in VAT collection.
- Alternative Scenario 2 models an increase in priority expenditure.
- Alternative Scenario 3 brings Scenarios 1 and 2 together, and shows to what extent increased VAT collection efficiency could fund an increase in priority expenditure.
- Alternative Scenario 4 considers how an increase in grants could finance priority expenditure.

Private financing will play an important role in creating fiscal space. As this fiscal space model only incorporates government budget data, and data on private sector investments are not available, it is difficult to predict how an increase in private funding will affect priority expenditure. Therefore, ‘indirect’ assumptions have been made to set up Scenario 5:

- Alternative Scenario 5 assumes private financing will increase and take up some important investments in, for example, infrastructure. This will allow the government to reallocate funding from non-priority sectors to priority sector.

GDP growth is at the heart of Rwanda’s macro-economic policy, and one option to increase priority expenditure and fiscal space is to achieve higher GDP growth:
Alternative Scenario 6 assumes private sector development and export substitution policies take off, and Rwanda is able to realize higher growth in GDP;

Alternative Scenario 7 mirrors Scenario 6, assuming investments will not be realized and GDP growth will be lower than assumed in the base scenario.

4.2.1 Increasing revenues to fund priority expenditure

**Alternative Scenario 1: Improved VAT collection efficiency**

Rwanda has already implemented numerous reforms to improve revenue administration and tax policy, which means many weaknesses have already been addressed. Compared to other countries, the possibility to increase fiscal space through improving revenue collection is not as strong – at least, not in the next couple of years. In addition, increases in revenue collection are partially offset by tax expenditures, which are the result of the government’s strategy to attract private sector funding and promote exports.

However, there is some scope to increase collection efficiency, especially through improved compliance. The recently introduced electronic billing (e-billing) machines aim to improve VAT compliance, but are not yet functioning optimally.

**Scenario 1** considers an improvement in the VAT collection efficiency. Table 4.4 shows that the key assumptions about GDP, consumer price index (CPI) and population growth remain the same. Two assumptions related to VAT collection efficiency have been altered as compared to the base scenario (‘alternative assumptions’). Thus, an assumption is made that domestic VAT collection efficiency increases gradually from 20 per cent in FY2017/18 to 25 per cent in FY2023/24, while import VAT collection efficiency increases gradually from 42 per cent in FY2017/18 to 54 per cent in FY2023/24.

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</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>6.3</td>
<td>6.5</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.3</td>
<td>7.5</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Population growth</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
<td>2.1</td>
</tr>
<tr>
<td>Domestic VAT collection efficiency (%)</td>
<td>20</td>
<td>21</td>
<td>22</td>
<td>23</td>
<td>24</td>
<td>24</td>
<td>25</td>
</tr>
<tr>
<td>Import VAT collection efficiency (%)</td>
<td>42</td>
<td>44</td>
<td>46</td>
<td>48</td>
<td>50</td>
<td>52</td>
<td>54</td>
</tr>
</tbody>
</table>

Table 4.5 shows the projections using the alternative assumptions on VAT collection efficiency. The projection results show that increased VAT efficiency would lead to a faster decline of the fiscal deficit over the projection period.
Table 4.5: Key projection results for Scenario 1

<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>Percentage of total expenditure</td>
<td>20.08</td>
<td>20.79</td>
<td>21.57</td>
<td>22.33</td>
<td>23.15</td>
<td>24.05</td>
<td>25.00</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>5.89</td>
<td>5.98</td>
<td>6.07</td>
<td>6.16</td>
<td>6.25</td>
<td>6.35</td>
<td>6.45</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>119.47</td>
<td>127.35</td>
<td>136.45</td>
<td>146.85</td>
<td>158.51</td>
<td>171.44</td>
<td>185.81</td>
</tr>
<tr>
<td>Net internal financing gap (fiscal gap)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>10.20</td>
<td>6.36</td>
<td>2.18</td>
<td>-1.73</td>
<td>-5.72</td>
<td>-9.73</td>
<td>-13.70</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>2.99</td>
<td>1.83</td>
<td>0.61</td>
<td>-0.48</td>
<td>-1.54</td>
<td>-2.57</td>
<td>-3.53</td>
</tr>
<tr>
<td>Fiscal deficit (surplus/deficit)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>-5.36</td>
<td>-4.21</td>
<td>-3.00</td>
<td>-1.92</td>
<td>-0.86</td>
<td>0.15</td>
<td>1.10</td>
</tr>
</tbody>
</table>

Table 4.6 compares the results from alternative Scenario 1 with the results from the base scenario. With the assumptions of Scenario 1, the average tax and non-tax revenue collection would increase with an average of 0.37 per cent of GDP over the projection period, compared to the base scenario. The net internal debt flow would be -0.38 per cent of GDP (compared with 0.02 per cent of GDP in the base scenario). The total (external and internal) government debt stock would conclude in FY2023/24 at 39.7 per cent of GDP (compared with 42.2 per cent in the base scenario).

Table 4.6: Results from Scenario 1 compared to the base scenario

<table>
<thead>
<tr>
<th>Results</th>
<th>Base scenario</th>
<th>Scenario 1</th>
<th>Variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average tax and non-tax revenue/GDP, 2017–2024</td>
<td>17.79</td>
<td>18.15</td>
<td>0.37</td>
</tr>
<tr>
<td>Average priority expenditure/GDP, 2017–2024</td>
<td>6.16</td>
<td>6.16</td>
<td>=</td>
</tr>
<tr>
<td>Average priority expenditure per child (US$ at 2015 prices and exchange rate), 2017–2024</td>
<td>149.41</td>
<td>149.41</td>
<td>=</td>
</tr>
<tr>
<td>Net internal debt flow/GDP, 2017–2024</td>
<td>0.02</td>
<td>-0.38</td>
<td>-0.40</td>
</tr>
<tr>
<td>Total government debt/GDP, 2024</td>
<td>42.19</td>
<td>39.71</td>
<td>-2.48</td>
</tr>
</tbody>
</table>

Alternative Scenario 2: Increased priority expenditure

To demonstrate how increased fiscal space (such as that projected in Scenario 1) could be used to finance an increase in priority expenditure, it is first necessary to construct an alternative scenario which projects an increase in priority expenditure that is higher than the increase projected in the base scenario.

Scenario 2 considers an increase (compared to the base scenario) in priority expenditure. Table 4.7 shows the alternative assumption, an increase of priority expenditure in per cent of GDP from 6 per cent of GDP in FY2017/18 to 6.6 per cent of GDP in FY2023/24. Compared to the base scenario, this scenario assumes the priority expenditure (as a percentage of GDP) would be on average 2 per cent higher.

It should be noted that projecting a significant increase in priority expenditure is difficult based on the assumptions used. The assumption underlying this scenario, which is setting the elasticity of staff in one of the priority sectors (education) to 3 and thus assuming an enormous increase in education staff, is not very realistic. For the purposes of this exercise it was decided to take this approach as otherwise the increase of priority expenditure would be nil, but it is important to underscore that significantly increasing priority expenditure is not an easy task.
Table 4.7: Key assumptions for Scenario 2

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</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>6.3</td>
<td>6.5</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.3</td>
<td>7.5</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Population growth</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
<td>2.1</td>
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<tr>
<td>Alternative assumption</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total priority non-interest expenditure (% of GDP)</td>
<td>6.0</td>
<td>6.1</td>
<td>6.2</td>
<td>6.3</td>
<td>6.4</td>
<td>6.5</td>
<td>6.6</td>
</tr>
</tbody>
</table>

Using the assumptions in Table 4.7, the projection results (see Table 4.8) obviously show an increase in priority expenditure over the projection period in terms of per cent of total expenditure and per-child expenditure, which is slightly higher than the projected increase in the base scenario.

Table 4.8: Key projection results for Scenario 2

<table>
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</tr>
</thead>
<tbody>
<tr>
<td>Percentage of total expenditure</td>
<td>20.27</td>
<td>21.10</td>
<td>21.96</td>
<td>22.75</td>
<td>23.57</td>
<td>24.44</td>
<td>25.34</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>5.96</td>
<td>6.10</td>
<td>6.22</td>
<td>6.32</td>
<td>6.42</td>
<td>6.52</td>
<td>6.61</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>120.86</td>
<td>129.84</td>
<td>139.74</td>
<td>150.71</td>
<td>162.80</td>
<td>176.02</td>
<td>190.55</td>
</tr>
<tr>
<td>Percentage change (compared to base scenario)</td>
<td>0.93</td>
<td>1.53</td>
<td>1.85</td>
<td>1.97</td>
<td>1.98</td>
<td>1.89</td>
<td>1.75</td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>1.16</td>
<td>1.95</td>
<td>2.41</td>
<td>2.63</td>
<td>2.71</td>
<td>2.67</td>
<td>2.55</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>1.16</td>
<td>1.95</td>
<td>2.41</td>
<td>2.63</td>
<td>2.71</td>
<td>2.67</td>
<td>2.55</td>
</tr>
<tr>
<td>Net internal financing gap (fiscal gap)</td>
<td>10.70</td>
<td>7.37</td>
<td>3.70</td>
<td>0.31</td>
<td>-3.12</td>
<td>-6.53</td>
<td>-9.85</td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>3.14</td>
<td>2.13</td>
<td>1.05</td>
<td>0.09</td>
<td>-0.85</td>
<td>-1.74</td>
<td>-2.57</td>
</tr>
<tr>
<td>Fiscal deficit (surplus/deficit)</td>
<td>-5.52</td>
<td>-4.51</td>
<td>-3.44</td>
<td>-2.48</td>
<td>-1.56</td>
<td>-0.68</td>
<td>0.14</td>
</tr>
</tbody>
</table>

Table 4.9 demonstrates that using this alternative assumption of higher than expected spending in the priority sectors, priority expenditure would increase by 0.14 of GDP as compared to the base scenario over the projection period (FY2017/18–2023/24). Average per-child priority expenditure would increase by US$3.52. Overall, compared to the base scenario, priority expenditure would increase by 2 per cent.

This increase in priority expenditure should be funded somehow. Comparing the projection results of Scenario 2 with the projection results from the base scenario (see Table 4.9), it appears that the average net internal debt would increase to 0.18 per cent of GDP (compared with 0.02 per cent of GDP in the base scenario) over the projection period. The total (external and internal) government debt would increase with 0.95 per cent of GDP to 43.14 per cent of GDP in FY2023/24 (compared with 42.19 per cent in the base scenario).
Table 4.9: Results from Scenario 2 compared to the base scenario

<table>
<thead>
<tr>
<th>Results</th>
<th>Base scenario</th>
<th>Scenario 2</th>
<th>Variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average tax and non-tax revenue/GDP, 2017–2024</td>
<td>17.79</td>
<td>17.79</td>
<td>=</td>
</tr>
<tr>
<td>Average priority expenditure/GDP, 2017–2024</td>
<td>6.16</td>
<td>6.31</td>
<td>0.14</td>
</tr>
<tr>
<td>Average priority expenditure per child (US$ at 2015 prices and exchange rate), 2017–2024</td>
<td>149.41</td>
<td>152.93</td>
<td>3.52</td>
</tr>
<tr>
<td>Net internal debt flow/GDP, 2017–2024</td>
<td>0.02</td>
<td>0.18</td>
<td>0.16</td>
</tr>
<tr>
<td>Total government debt/GDP, 2024</td>
<td>42.19</td>
<td>43.14</td>
<td>0.95</td>
</tr>
</tbody>
</table>

Alternative Scenario 3: Increase in priority expenditure funded by enhanced VAT administration

Scenario 3 combines the assumptions of Scenario 1 and Scenario 2, so that the increase in priority expenditure would effectively be funded through higher tax revenue resulting from enhanced VAT administration. Table 4.10 specifies the three assumptions, which are changed in comparison to the base scenario assumptions (which are similar to the alternative assumptions used to construct Scenario 1 and 2).

Table 4.10: Key assumptions for Scenario 3

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>6.3</td>
<td>6.5</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.3</td>
<td>7.5</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Population growth</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
<td>2.1</td>
</tr>
</tbody>
</table>

Alternative assumptions

| Domestic VAT collection efficiency (%) | 20.1 | 20.9 | 21.8 | 22.7 | 23.6 | 24.5 | 25.4 |
| Import VAT collection efficiency (%) | 42.4 | 44.2 | 46.0 | 47.8 | 49.7 | 51.6 | 53.6 |
| Total priority non-interest expenditure (% of GDP) | 6.0 | 6.1 | 6.2 | 6.3 | 6.4 | 6.5 | 6.6 |

Table 4.11 shows the projection results when using the assumptions of Table 4.10. Priority expenditure will grow at the same pace as projected in Scenario 2, but the net internal financing gap and fiscal deficit will be different because of the increased revenue through more efficient VAT collection.
Table 4.11: Key projections results for Scenario 3

<table>
<thead>
<tr>
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</tr>
</thead>
<tbody>
<tr>
<td><strong>Priority expenditure</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>20.27</td>
<td>21.11</td>
<td>21.97</td>
<td>22.77</td>
<td>23.60</td>
<td>24.50</td>
<td>25.43</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>5.96</td>
<td>6.10</td>
<td>6.22</td>
<td>6.32</td>
<td>6.42</td>
<td>6.52</td>
<td>6.61</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>120.86</td>
<td>129.84</td>
<td>139.74</td>
<td>150.71</td>
<td>162.80</td>
<td>176.02</td>
<td>190.55</td>
</tr>
<tr>
<td><strong>Net internal financing gap (fiscal gap)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>10.40</td>
<td>6.75</td>
<td>2.72</td>
<td>−1.08</td>
<td>−4.97</td>
<td>−8.90</td>
<td>−12.81</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>3.06</td>
<td>1.95</td>
<td>0.77</td>
<td>−0.30</td>
<td>−1.35</td>
<td>−2.37</td>
<td>−3.33</td>
</tr>
<tr>
<td><strong>Fiscal deficit (surplus/deficit)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>−5.43</td>
<td>−4.33</td>
<td>−3.16</td>
<td>−2.10</td>
<td>−1.06</td>
<td>−0.05</td>
<td>0.90</td>
</tr>
</tbody>
</table>

Table 4.12 compares the outcome of this scenario with the base scenario. It appears, when combining the assumptions used in Scenario 1 and 2, that the average net internal debt flow would be −0.24 per cent of GDP over the projection period (FY2017/18–FY2023/24). This is lower than the 0.18 per cent internal debt projected in Scenario 2, which assumes only an increase in priority expenditure, without higher revenues (see Table 4.9), and the 0.02 per cent projected in the base scenario. Total government debt stock (external and internal) would amount to 40.66 per cent of GDP in FY2023/24, 1.53 per cent of GDP lower compared with the debt stock of 42.19 per cent projected in the base scenario.

In summary, the increase in average revenue to GDP could fund the increase in average priority expenditure and would also have positive effects on government debt. The projected increase in VAT efficiency would ‘overcompensate’ the increase of 2 per cent in priority expenditure.

Table 4.12 Results from Scenario 3

<table>
<thead>
<tr>
<th>Results</th>
<th>Base scenario</th>
<th>Scenario 3</th>
<th>Variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average tax and non-tax revenue/GDP, 2017–2024</td>
<td>17.79</td>
<td>18.15</td>
<td>0.37</td>
</tr>
<tr>
<td>Average priority expenditure/GDP, 2017–2024</td>
<td>6.16</td>
<td>6.31</td>
<td>0.14</td>
</tr>
<tr>
<td>Average priority expenditure per child (US$ at 2015 prices and exchange rate), 2017–2024</td>
<td>149.41</td>
<td>152.93</td>
<td>3.52</td>
</tr>
<tr>
<td>Net internal debt flow/GDP, 2017–2024</td>
<td>0.02</td>
<td>−0.22</td>
<td>−0.24</td>
</tr>
<tr>
<td>Total government debt/GDP, 2024</td>
<td>42.19</td>
<td>40.66</td>
<td>−1.53</td>
</tr>
</tbody>
</table>

**Alternative Scenario 4: Increased external financing to fund priority expenditure**

Although the relative share of external grants has declined, in absolute terms grant financing is still increasing. The health sector, especially, is actively pursuing more external financing by issuing grant proposals. A similar attempt could be made by the other social sectors, e.g. the education sector could also try to raise more funding from grants by more actively approaching donors for support. As such, there seems to be scope for increased external financing via grants, if those initiatives are successful.

**Scenario 4** considers an increase of external grants to fund priority expenditure. The increase in priority expenditure equals the assumptions of Scenario 2 (i.e. higher than in the base scenario), while external grants for current and capital expenditure will slowly increase to 3 per cent of GDP in FY2023/24, i.e. a total of 6 per cent of GDP. Table 4.13 lists the standard and alternative assumptions used to project this scenario.
Table 4.13: Key assumptions in Scenario 4

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>6.3</td>
<td>6.5</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.3</td>
<td>7.5</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Population growth</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
<td>2.1</td>
</tr>
</tbody>
</table>

Alternative assumptions

<table>
<thead>
<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total priority non-interest expenditure (% of GDP)</td>
<td>6.0</td>
<td>6.1</td>
<td>6.2</td>
<td>6.3</td>
<td>6.4</td>
<td>6.5</td>
<td>6.6</td>
</tr>
<tr>
<td>Central government external grants for current expenditure (% of GDP)</td>
<td>2.7</td>
<td>2.8</td>
<td>2.8</td>
<td>2.9</td>
<td>2.9</td>
<td>3.0</td>
<td>3.0</td>
</tr>
<tr>
<td>Central government external grants for capital expenditure (projects) (% of GDP)</td>
<td>2.2</td>
<td>2.4</td>
<td>2.5</td>
<td>2.6</td>
<td>2.7</td>
<td>2.9</td>
<td>3.0</td>
</tr>
</tbody>
</table>

Table 4.14 summarizes the projection results, using these assumptions. Priority expenditure will grow at the same pace as projected in Scenario 2, but the net internal financing gap and fiscal deficit will be different because of the increased revenue through more grant financing.

Table 4.14: Key projection results in Scenario 4

<table>
<thead>
<tr>
<th>Priority expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage of total expenditure</td>
</tr>
<tr>
<td>Percentage of GDP</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
</tr>
</tbody>
</table>

Net internal financing gap (fiscal gap)

| Percentage of total expenditure | 10.12 | 6.15 | 1.80 | –2.34 | –6.58 | –10.90 | –15.21 |
| Percentage of GDP              | 2.97  | 1.78 | 0.51 | –0.65 | –1.79 | –2.89  | –3.94  |

Fiscal deficit (surplus/deficit)

| Percentage of GDP | –5.35 | –4.16 | –2.90 | –1.75 | –0.62 | 0.47   | 1.51   |

Table 4.15 shows that, with these assumptions, the average net internal debt flow would be –0.57 per cent of GDP (compared with 0.02 per cent of GDP in Scenario 0) over the projection period (FY2017/18–FY2023/24). The total (external and internal) government debt stock would amount to 38.53 per cent of GDP in FY2023/24 (compared with 42.19 per cent in Scenario 0). Grants could thus fund an increase in priority expenditure and a decrease in government debt.
Table 4.15: Results from Scenario 4

<table>
<thead>
<tr>
<th>Results</th>
<th>Base scenario</th>
<th>Scenario 4</th>
<th>Variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average tax and non-tax revenue/GDP, 2017–2024</td>
<td>17.79</td>
<td>17.79</td>
<td>=</td>
</tr>
<tr>
<td>Average priority expenditure/GDP, 2017–2024</td>
<td>6.16</td>
<td>6.31</td>
<td>0.14</td>
</tr>
<tr>
<td>Average priority expenditure per child (US$ at 2015 prices and exchange rate), 2017–2024</td>
<td>149.41</td>
<td>152.93</td>
<td>3.52</td>
</tr>
<tr>
<td>Net internal debt flow/GDP, 2017–2024</td>
<td>0.02</td>
<td>–0.57</td>
<td>–0.59</td>
</tr>
<tr>
<td>Total government debt/GDP, 2024</td>
<td>42.19</td>
<td>38.53</td>
<td>–3.66</td>
</tr>
</tbody>
</table>

4.2.2 Private sector funding allows reallocation of public funds to the priority sectors

Should private sector financing take off, these investments will most likely take place in the non-priority sectors, such as infrastructure. As the model does not capture private financing flows, it is not able to model increased private financing, but it can model a decrease in non-priority expenditure by the government. It is supposed that as a result of increased private investments in infrastructure, the government can afford to reallocate some funds from the non-priority sectors to the priority sectors.

**Alternative Scenario 5: Reprioritization from non-priority to priority expenditure**

Assuming the government will attract more private funding for its non-priority expenditure (e.g. for infrastructure), it could reprioritize some of its own government funding towards the priority sectors. In addition, the new government plans may entail a renewed focus on social sectors, which would justify such a reprioritization. This scenario thus investigates what would happen if the government reallocates some of its funding from non-priority to priority expenditure.

**Scenario 5** considers a decrease of non-priority recurrent and non-recurrent expenditure (decreasing respectively to 11.8 and 5.6 per cent of GDP in FY2023/24), while priority expenditure increases (compared to baseline scenario) as considered in Scenario 2. Table 4.16 summarizes the alternative assumptions which construct this scenario.

Table 4.16: Key assumptions in Scenario 5

<table>
<thead>
<tr>
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</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>6.3</td>
<td>6.5</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.3</td>
<td>7.5</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Population growth</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
<td>2.1</td>
</tr>
</tbody>
</table>

**Alternative assumptions**

<table>
<thead>
<tr>
<th>Central government non-priority non-recurrent expenditure (% of GDP)</th>
<th>8.0</th>
<th>7.5</th>
<th>7.1</th>
<th>6.7</th>
<th>6.3</th>
<th>5.9</th>
<th>5.6</th>
</tr>
</thead>
<tbody>
<tr>
<td>Central government non-priority recurrent expenditure (% of GDP)</td>
<td>14.5</td>
<td>14.0</td>
<td>13.5</td>
<td>13.1</td>
<td>12.6</td>
<td>12.2</td>
<td>11.8</td>
</tr>
<tr>
<td>Total priority non-interest expenditure (% of GDP)</td>
<td>6.0</td>
<td>6.1</td>
<td>6.2</td>
<td>6.3</td>
<td>6.4</td>
<td>6.5</td>
<td>6.6</td>
</tr>
</tbody>
</table>

Table 4.17 presents the projections scenarios, using the assumptions of Table 4.16. Priority expenditure would take up 27.12 per cent of total expenditure in FY2023/24. The share is thus higher than in the base scenario, where 25 per cent of total expenditure would be used for priority expenditure by FY2023/24.
Table 4.17: Key projection results in Scenario 5

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage of total expenditure</td>
<td>20.30</td>
<td>21.38</td>
<td>22.50</td>
<td>23.56</td>
<td>24.68</td>
<td>25.88</td>
<td>27.12</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>5.96</td>
<td>6.10</td>
<td>6.22</td>
<td>6.32</td>
<td>6.42</td>
<td>6.52</td>
<td>6.61</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>120.86</td>
<td>129.84</td>
<td>139.74</td>
<td>150.71</td>
<td>162.80</td>
<td>176.02</td>
<td>190.55</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Net internal financing gap (fiscal gap)</th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage of total expenditure</td>
<td>10.54</td>
<td>6.40</td>
<td>1.83</td>
<td>–2.53</td>
<td>–7.02</td>
<td>–11.58</td>
<td>–16.13</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>3.09</td>
<td>1.82</td>
<td>0.51</td>
<td>–0.68</td>
<td>–1.83</td>
<td>–2.92</td>
<td>–3.93</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Fiscal deficit (surplus/deficit)</th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage of GDP</td>
<td>–5.47</td>
<td>–4.14</td>
<td>–2.76</td>
<td>–1.52</td>
<td>–0.33</td>
<td>0.79</td>
<td>1.84</td>
</tr>
</tbody>
</table>

Table 4.18 further summarizes changes between this scenario and the base scenario. With these assumptions (see Table 4.16), the average net internal debt flow would be –0.56 per cent of GDP compared with 0.02 per cent of GDP in the base scenario between FY2017/18–FY2023/24. The total (external and internal) government debt stock would amount to 37.38 per cent of GDP in FY2023/24 (compared with 42.19 per cent in the base scenario).

A reprioritization would thus not only lead to increased priority expenditure, but could also decrease the debt-to-GDP ratio and result in a positive internal borrowing flow. This result can be explained by the assumption that non-priority non-recurrent expenditure will decrease. Non-recurrent expenditure usually requires more borrowing. Hence, because non-recurrent expenditure decreases, it is expected less borrowing is needed.

Table 4.18: Results from Scenario 5

<table>
<thead>
<tr>
<th>Results</th>
<th>Base scenario</th>
<th>Scenario 5</th>
<th>Variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average tax and non-tax revenue/GDP, 2017–2024</td>
<td>17.79</td>
<td>17.79</td>
<td>=</td>
</tr>
<tr>
<td>Average priority expenditure/GDP, 2017–2024</td>
<td>6.16</td>
<td>6.31</td>
<td>0.14</td>
</tr>
<tr>
<td>Average priority expenditure per child (US$ at 2015 prices and exchange rate), 2017–2024</td>
<td>149.41</td>
<td>152.93</td>
<td>3.52</td>
</tr>
<tr>
<td>Net internal debt flow/GDP, 2017–2024</td>
<td>0.02</td>
<td>–0.56</td>
<td>–0.58</td>
</tr>
<tr>
<td>Total government debt/GDP, 2024</td>
<td>42.19</td>
<td>37.38</td>
<td>–4.81</td>
</tr>
</tbody>
</table>

4.2.3 GDP growth

The following two illustrative scenarios show how fiscal space and priority expenditure would be affected by exogenous factors, by projecting the effects of a higher or lower GDP growth.

Alternative Scenario 6: Higher GDP growth

Rwanda is focused on sustaining high GDP growth. If its policies of import substitution and export promotion as well as other measures to attract private funding take off, a higher GDP growth than assumed in the base scenario would be possible.

Scenario 6 uses the same assumptions as the baseline scenario with the only difference being that the real growth rate is now higher (gradually increasing from 6.3 per cent in FY2017/18 to 8 per cent in FY2023/24) than the growth assumed in the base scenario. This alternative assumption is highlighted in Table 4.19.
Table 4.19: Key assumptions in Scenario 6

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>6.3</td>
<td>6.6</td>
<td>6.8</td>
<td>7.1</td>
<td>7.4</td>
<td>7.7</td>
<td>8.0</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Population growth</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
<td>2.1</td>
</tr>
</tbody>
</table>

Table 4.20 shows the projection results using the assumption of a higher GDP growth than in the base scenario. The share of priority expenditure would somewhat reduce as percentage of GDP, because the GDP has increased. However, per-child expenditure would be positively affected and increase exponentially over the projection period.

Table 4.20: Key projection results in Scenario 6

<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>Priority expenditure</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>5.89</td>
<td>5.98</td>
<td>6.07</td>
<td>6.15</td>
<td>6.24</td>
<td>6.33</td>
<td>6.42</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>119.50</td>
<td>127.46</td>
<td>136.69</td>
<td>147.33</td>
<td>159.37</td>
<td>172.86</td>
<td>188.04</td>
</tr>
<tr>
<td>Percentage change (compared to base scenario)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>0.00</td>
<td>0.02</td>
<td>0.04</td>
<td>0.08</td>
<td>0.13</td>
<td>0.21</td>
<td>0.32</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>−0.01</td>
<td>−0.04</td>
<td>−0.09</td>
<td>−0.15</td>
<td>−0.22</td>
<td>−0.30</td>
<td>−0.39</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>0.02</td>
<td>0.08</td>
<td>0.16</td>
<td>0.33</td>
<td>0.54</td>
<td>0.83</td>
<td>1.20</td>
</tr>
</tbody>
</table>

Table 4.21 compares the projection results of this scenario with those of the base scenario. The assumption of higher GDP growth would lead to a minimal increase of average revenue. The average priority spending per child would be increased by US$0.77 to US$150.18. The average net internal debt flow would be −0.06 per cent of GDP (compared with 0.02 per cent of GDP in the base scenario). The total (external and internal) government debt stock would conclude in FY2023/24 at 41.05 per cent of GDP (compared with 42.19 per cent in the base scenario).

Table 4.21: Results from Scenario 6

<table>
<thead>
<tr>
<th>Results</th>
<th>Base scenario</th>
<th>Scenario 6</th>
<th>Variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average tax and non-tax revenue/GDP, 2017–2024</td>
<td>17.79</td>
<td>17.79</td>
<td>0.00</td>
</tr>
<tr>
<td>Average priority expenditure/GDP, 2017–2024</td>
<td>6.16</td>
<td>6.15</td>
<td>−0.01</td>
</tr>
<tr>
<td>Average priority expenditure per child (US$ at 2015 prices and exchange rate), 2017–2024</td>
<td>149.41</td>
<td>150.18</td>
<td>0.77</td>
</tr>
<tr>
<td>Net internal debt flow/GDP, 2017–2024</td>
<td>0.02</td>
<td>−0.06</td>
<td>−0.08</td>
</tr>
<tr>
<td>Total government debt/GDP, 2024</td>
<td>42.19</td>
<td>41.05</td>
<td>−1.14</td>
</tr>
</tbody>
</table>

77 The increase is very small: 0.038 per cent of GDP. Therefore, Table 4.21 includes a variation of 0.00 per cent.
Alternative Scenario 7: Lower GDP growth

However, Rwanda could also be facing external shocks, such as commodity price volatility or rising regional tensions, which would negatively affect its economic growth. This scenario therefore considers a GDP growth lower than that of the base scenario.

Scenario 7 uses the same assumptions as the baseline scenario with the only difference that the real growth rate gradually declines from 5.7 per cent in FY2017/18 to 4 per cent in FY2023/24. This alternative assumption is highlighted in Table 4.22.

Table 4.22: Key assumptions for Scenario 7

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>5.7</td>
<td>5.4</td>
<td>5.1</td>
<td>4.8</td>
<td>4.5</td>
<td>4.2</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Population growth</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
</tr>
</tbody>
</table>

Table 4.23 shows the projection results for this scenario. Lower GDP growth would reduce the percentage of total expenditure spent on priority sectors from 24.97 per cent in the base scenario to 24.19 per cent in FY2023/24. Per-child expenditure would decrease to US$167.99 in FY2023/24 (instead of US$185.81 in the base scenario).

Table 4.23: Key projection results for Scenario 7

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage of total expenditure</td>
<td>20.07</td>
<td>20.75</td>
<td>21.47</td>
<td>22.13</td>
<td>22.80</td>
<td>23.51</td>
<td>24.19</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>5.90</td>
<td>6.01</td>
<td>6.13</td>
<td>6.26</td>
<td>6.39</td>
<td>6.54</td>
<td>6.68</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>119.08</td>
<td>126.09</td>
<td>133.69</td>
<td>141.85</td>
<td>150.37</td>
<td>159.09</td>
<td>167.99</td>
</tr>
<tr>
<td>Percentage change (compared to base scenario)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percentage of total expenditure</td>
<td>–0.05</td>
<td>–0.19</td>
<td>–0.44</td>
<td>–0.81</td>
<td>–1.34</td>
<td>–2.02</td>
<td>–2.87</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>0.20</td>
<td>0.55</td>
<td>1.03</td>
<td>1.60</td>
<td>2.25</td>
<td>2.94</td>
<td>3.67</td>
</tr>
<tr>
<td>Per child in US$ at 2016 exchange rate and prices</td>
<td>–0.33</td>
<td>–1.00</td>
<td>–2.02</td>
<td>–3.40</td>
<td>–5.13</td>
<td>–7.20</td>
<td>–9.59</td>
</tr>
</tbody>
</table>

Table 4.24 compares the projection results with those of the base scenario. The average internal debt flow would be 0.86 per cent of GDP (compared with 0.02 per cent of GDP in the base scenario). The total (external and internal) government debt stock would conclude in FY2023/24 at 53.36 per cent of GDP (compared with 42.19 per cent in base scenario).
Table 4.24: Results from Scenario 7

<table>
<thead>
<tr>
<th>Results</th>
<th>Base scenario</th>
<th>Scenario 7</th>
<th>Variation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average tax and non-tax revenue/GDP, 2017–2024</td>
<td>17.79</td>
<td>17.74</td>
<td>−0.04</td>
</tr>
<tr>
<td>Average priority expenditure/GDP, 2017–2024</td>
<td>6.16</td>
<td>6.27</td>
<td>0.11</td>
</tr>
<tr>
<td>Average priority expenditure per child (US$ at 2015 prices and exchange rate), 2017–2024</td>
<td>149.41</td>
<td>142.60</td>
<td>−6.82</td>
</tr>
<tr>
<td>Net internal debt flow/GDP, 2017–2024</td>
<td>0.02</td>
<td>0.86</td>
<td>0.84</td>
</tr>
<tr>
<td>Total government debt/GDP, 2024</td>
<td>42.19</td>
<td>53.36</td>
<td>11.17</td>
</tr>
</tbody>
</table>

4.2.4 Summary of scenario results

The impact on fiscal space of the scenarios considered is summarized in Table 4.25.

Table 4.25: Summary of scenario results

<table>
<thead>
<tr>
<th>Policymaking scenarios</th>
<th>Government debt FY2023/24</th>
<th>Priority spending per child (in US$, average FY2017/24)</th>
<th>Percentage change compared to the base scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base scenario</td>
<td>42.19</td>
<td>149.41</td>
<td>=</td>
</tr>
<tr>
<td>Enhanced VAT administration (10 per cent increase)</td>
<td>39.71</td>
<td>149.41</td>
<td>=</td>
</tr>
<tr>
<td>Increased priority expenditure</td>
<td>43.14</td>
<td>152.93</td>
<td>2</td>
</tr>
<tr>
<td>Increased priority expenditure and enhanced VAT administration (10 per cent increase)</td>
<td>40.66</td>
<td>152.93</td>
<td>2</td>
</tr>
<tr>
<td>Increased external grants for social sectors and increased priority expenditure</td>
<td>38.53</td>
<td>152.93</td>
<td>2</td>
</tr>
<tr>
<td>Reduction of non-priority expenditure and increased priority expenditure and increased priority expenditure</td>
<td>37.38</td>
<td>152.93</td>
<td>2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Change in economic growth scenarios</th>
<th>Government debt FY2023/24</th>
<th>Priority spending per child (in US$, average FY2017/24)</th>
<th>Percentage change compared to the base scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td>Higher real GDP growth</td>
<td>41.05</td>
<td>150.18</td>
<td>1</td>
</tr>
<tr>
<td>Lower real GDP growth</td>
<td>53.36</td>
<td>142.60</td>
<td>−5</td>
</tr>
</tbody>
</table>

The projection exercise has produced illustrative results that show alternative means of creating enhanced fiscal space that can be used to finance priority spending. These scenarios show that the projected increase in priority spending, which is a 2 per cent increase in real priority spending per child between FY2017/18 and FY2023/24 (Scenario 2), could be financed in a number of different fiscally neutral ways (i.e. that would not lead to any increase in the level of government debt at the end of the projection period):

- A gradual increase in the efficiency of tax administration of 10 per cent (increase in VAT collections without any increase in tax rates) (Scenario 3);
- An increase of external grants, to 6 per cent of GDP (Scenario 4); and
- A reprioritization of priority/non-priority spending, reallocating funding from non-priority sectors to priority sectors (Scenario 5).

All these scenarios would ‘overcompensate’ – meaning they also have a positive effect on government debt.
Scenarios 6 and 7 demonstrate the effect of different potential economic growth scenarios. Should economic growth be higher than anticipated, priority spending per child would increase by 1 per cent and at the same time decrease debt to 41.05 per cent. If growth is lower (and declines to 4 per cent by 2024), this would lead to a decrease of 5 per cent in priority spending per child as compared to the base scenario. Debt levels would rise to above 50 per cent.

Out of the scenarios above, while the reprioritization of expenditure could realize an increase in priority expenditure of 2 per cent as well as the largest decrease in debt, it should not be forgotten that reprioritization might have consequences on economic growth. A decrease in (capital) expenditure on non-priority sectors such as infrastructure could lead to a somewhat slowed down economic growth, which would in turn negatively affect fiscal space and priority spending.

Figures 4.2, 4.3 and 4.4 summarize the effects of the different scenarios on Rwanda’s fiscal surplus/deficit, total government debt as a percentage of GDP and child priority expenditure in constant US dollars.

Figure 4.2: Rwanda, fiscal surplus/deficit as percentage of GDP
Figure 4.3: Rwanda, total government debt stock as percentage of GDP

Figure 4.4: Rwanda, per-child priority expenditure, US$ 2015 price and exchange rate
4. Fiscal space scenarios

4.2.5 Summary of scenario results per sector

The table below summarizes the effect of each scenario per sector. It details that the modelled increase in priority expenditure consists of an increase of 1.3 per cent per-child education priority expenditure, 2.5 per cent per-child health priority expenditure, 4.8 per cent per-child social protection priority expenditure and 3.4 per cent per-child water supply priority expenditure. These increases can be financed by means of Scenarios 3, 4 and 5 – and at the same time decrease government debt. Economic growth would also affect the level of per-child expenditure. A higher than projected economic growth would increase per-child priority expenditure in each sector by about 0.5 per cent. Should GDP growth be lower than anticipated, this could result in 4.7 per cent decrease in per-child priority expenditure in most sectors, and 3.8 per cent decrease in per-child social protection priority expenditure.

<table>
<thead>
<tr>
<th>Scenario Description</th>
<th>Government debt FY2023/24*</th>
<th>Education**</th>
<th>Health**</th>
<th>Social protection</th>
<th>Water supply**</th>
<th>Total**</th>
</tr>
</thead>
<tbody>
<tr>
<td>0. Base scenario</td>
<td>42.19</td>
<td>66.01</td>
<td>55.2</td>
<td>21.6</td>
<td>6.6</td>
<td>149.4</td>
</tr>
<tr>
<td>Policymaking scenarios</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Enhanced VAT administration (10% increase)</td>
<td>39.71</td>
<td>66.0</td>
<td>55.2</td>
<td>21.6</td>
<td>6.6</td>
<td>149.4</td>
</tr>
<tr>
<td>2. Increased priority expenditure</td>
<td>43.14</td>
<td>66.9</td>
<td>56.6</td>
<td>22.59</td>
<td>6.8</td>
<td>152.9</td>
</tr>
<tr>
<td>3. Increase priority expenditure and enhanced VAT administration (20% increase)</td>
<td>40.66</td>
<td>66.9</td>
<td>56.6</td>
<td>22.6</td>
<td>6.8</td>
<td>152.9</td>
</tr>
<tr>
<td>4. Increased external grants for social sectors</td>
<td>38.53</td>
<td>66.9</td>
<td>56.6</td>
<td>22.6</td>
<td>6.8</td>
<td>152.9</td>
</tr>
<tr>
<td>5. Reduction of non-priority expenditure and increased priority expenditure</td>
<td>37.38</td>
<td>66.9</td>
<td>56.6</td>
<td>22.6</td>
<td>6.8</td>
<td>152.9</td>
</tr>
<tr>
<td>Change in economic growth scenarios</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Higher real GDP growth</td>
<td>41.05</td>
<td>66.4</td>
<td>55.5</td>
<td>21.7</td>
<td>6.6</td>
<td>150.2</td>
</tr>
<tr>
<td>7. Lower real GDP growth</td>
<td>53.36</td>
<td>62.9</td>
<td>52.7</td>
<td>20.7</td>
<td>6.3</td>
<td>142.6</td>
</tr>
</tbody>
</table>

* Percentage of GDP on average
** Per-child priority expenditure at 2015 exchange rate and prices (difference in % compared to the base scenario)

4.3 Other options to enhance fiscal space

This section mentions other options to increase fiscal space that have not been used for the above-mentioned scenarios. It briefly explains why these options have not been chosen to be worked out in a set of illustrative alternative scenarios.

4.3.1 Reducing external debt service through agreements with creditors

While external debt service reduction would, in principle, augment the fiscal space, this is not a realistic possibility. Since the mid 2000s, with the conclusion of the cycle of debt reduction that began with the Heavily Indebted Poor Countries Initiative in the late 1990s and continued through the Multilateral Debt Relief Initiative in the 2000s, the international financial community has generally been unwilling to consider debt reduction.
4.3.2 Increasing external debt disbursements

When increasing external debt to fund priority expenditure, caution is needed with regard to the maturity of such debt. In general, macroeconomic policy specialists concur that it is inadvisable to use commercial external debt to fund education, health or social protection expenditure. The reasoning is straightforward: eventual returns to education and health expenditure are realized over decades, but debt service on commercial external debt is generally due within a decade.

As such, concessional debt – with multi-decade terms and near-zero interest rates – would be more realistic for such purposes. Although Rwanda has a low debt status, taking up additional debt is not seen as a likely strategy. The country may reach middle-debt status if it does, and it would put further pressure on its current account balance. In addition, increasing debt is not advisable when considering unanticipated potential future liabilities, such as the risk the demand for electricity will not pick up and the government will need to pay for supply.

4.3.3 Increasing net internal borrowing flows

In the analytical structure of the projection exercise, net internal borrowing is calculated residually. In effect, it is the consequence of all the programming assumptions taken together. Evaluation of its feasibility therefore amounts to evaluation of the feasibility of all the programming assumptions taken together. In principle, if it is inadvisable to fund priority expenditure with external debt, it is even more inadvisable to use internal debt, which usually carries a higher interest rate and shorter maturities.

4.3.4 Increasing expenditure efficiency

For some countries where budget absorption rates were low, a scenario assumed increase in expenditure efficiency. Because of Rwanda’s solid fiscal performance, this scenario was not deemed adequate for this analysis.

4.3.5 Increasing local revenues or increased efficiency in local expenditures

While local governments have great potential to increase own revenues, this would be mainly achieved via general economic development and not necessarily via changes in taxation. Tax administration is done by the RRA and is relatively efficient; tax policy is set at central level, taxes collected at local level are a relatively small part of the total amount of taxation, and – except from the fixed asset tax – no space was identified for new local taxes. In terms of expenditure efficiency, districts have high rates of budget execution. This does not mean there are no opportunities in generating more revenue at local level, or that expenditures could be done more efficiently (i.e. improving the quality of spending), but that based on the nature of the projection exercise as well as the available data, no appropriate scenario could be run.

4.3.6 Reducing illicit financing flows

While not included in the model, another (unquantifiable) option to free up resources is to improve capturing illicit financial flows. Illicit financial flows (IFFs) are illegal movements of money or capital from one country to another. The latest report of Global Financial Integrity (GFI) has investigated these IFFs, using two sources: (1) deliberate mis-invoicing in merchandise trade (the source of GFI’s low and high estimates), and (2) leakages in the balance of payments (also known as ‘hot money flows’). The GFI report provides low estimates, which are based on trade between Rwanda and advanced economies only; and high estimates, which also consider trade between developing countries. Naturally, measurements of illicit financial flows are identified indirectly and hence data on IFFs is imprecise. Figure 4.5 illustrates that the estimates of IFFs in Rwanda significantly differ. When taking into

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account IFFs between Rwanda and all countries, the estimates suggest an increase up to 2011, after which the IFFs have been somewhat decreased.

Figure 4.5: Illicit financial flows in Rwanda, 2005–2014 (in US$ millions)

Figure 4.6 demonstrates illicit financial inflows and outflows as percentage of total trade. Illicit financial outflows are estimated at 5.5 to 16.4 per cent of Rwanda’s total merchandise trade, and inflows at 3.3 to 9.3 per cent of Rwanda’s total trade. Whereas illicit inflows in Rwanda are below the average in the region, its illicit outflows (the high estimates) to both developed and developing countries, are the sub-Saharan African average. If the government of Rwanda was able to more effectively address trade mispricing practices, significant resources could be potentially captured and directed towards priority sectors.

Figure 4.6: Illicit financial flows, 2005–2014 average (as percentage of total trade)
5. Conclusions

In coming years, UNICEF will participate in continuing dialogue with Rwanda’s government and other stakeholders regarding expenditure flows affecting children. This report recommends that UNICEF develops and maintains a multi-annual projection exercise to enable it to participate effectively in discussions regarding the fiscal-resource flow available to fund these expenditure flows. The report has described the recommended features of such an exercise, and has illustrated ways in which it could be applied to evaluate policy options.

As it engages in Rwanda’s dialogue, UNICEF must take careful account of Rwanda’s present macroeconomic predicament. Rwanda remains committed to a high real growth rate, but may need to rely less on public investment to stimulate this growth. Rwanda’s economy is in the process of a structural transformation. The government invested heavily in infrastructure to increase the shares of industry and services in the composition of GDP. While this public investment helped sustain high growth, it widened the current account deficit. The growing deficit had to be financed with increased external debt and international-reserve loss, forcing Rwanda to change its approach. Rwanda is now focusing on promotion of local production and exports to help limit the current account deficit. Even so, Rwanda is determined to sustain the high levels of GDP growth, to take advantage of its population dividend and to continue its promising path of poverty reduction.

The current fiscal policy recognizes that the scope for increased domestic and external revenue is limited and prescribes careful borrowing and expenditure control. Given the need to control the current account deficit, the government’s fiscal policy has moved from a more expansionary policy to fiscal consolidation and a more prudent borrowing policy. On the revenue side, the next two to three years offer little scope for additional inflows from own tax/non-tax revenue and external grants. As a result, Rwanda aims to control its current and capital expenditure, to limit the fiscal deficit and avoid having to engage in large-scale borrowing, which would endanger its present low likelihood of debt distress.

The macroeconomic and fiscal situation thus suggests that Rwanda will find it difficult to find much additional fiscal space, at least in the next two to three years. This is plainly relevant for those advocating increased spending on child-friendly sectors, especially since at the same time, Rwanda must dedicate the resources necessary to enhance economic growth – which is, after all, the key to enhancing the fiscal space in the medium and longer term.

Spending on ‘priority’ sectors has been uneven over the past years, but this may change in the future if the National Strategy for Transformation (NST1) places a renewed focus on these sectors. For the purposes of this study, ‘priority’ sectors have been defined as a set of sub-sectors of the education sector, the health sector, the social protection sector, and the sub-sector water supply. Spending in these budget categories is called ‘priority’ expenditure. The trend in spending on these sectors has been uneven over the years covered by the EDPRS II. Also, spending on education, health, social protection and water supply is below international benchmarks. This is not completely surprising, as the EDPRS II was focused on economic growth, and only to a lesser extent on education and health. The upcoming NST1 will include a separate pillar for the social sectors, and it is well possible that this will help ensure that future priority spending will be set on a stable growth trajectory.

Given the development challenges within the priority sectors, there is a clear case to increase spending in those sectors. While in all priority sectors much progress has been made, challenges persist. In the past few years, the priority sectors funding fell short of what they needed to fully execute their sector plans. While
in some countries, improvements in budget execution and increasing expenditure efficiency are options to deal with inadequate fiscal space, this is less likely for Rwanda, which appears to have highly efficient expenditure management.

The developments mentioned above are reflected in the base scenario of the projection exercise, which consists of a set of neutral, non-controversial assumptions. Under the base scenario, Rwanda could achieve a steady increase of priority expenditure without creating a ‘fiscal gap.’ The base scenario projects that Rwanda will decrease its fiscal deficit over the projection period (which runs from FY2017 to FY2024) and that priority expenditure will increase. This would be the result of a conservative fiscal policy, with some cuts to capital expenditure. The key assumption is that Rwanda will maintain high economic growth: the base scenario assumes that real GDP growth would reach 7.5 per cent by FY2024.

Alternative scenarios indicate that Rwanda could fund a small additional increase in priority expenditure through increased VAT efficiency. While the potential to increase tax revenues is limited in the near future, some improvement could be made in VAT collection efficiency. The additional revenue generated from this improvement could fund an increase in priority expenditure higher than that in the base scenario and also have a positive effect on government debt.

An alternative scenario in which social sectors attract additional external grant funding shows that this approach has the potential both to increase priority expenditure and to limit government indebtedness. An alternative scenario assuming an increase in external grants to 6 per cent of GDP, would enable the government to increase priority expenditure while reducing the government debt stock as a percentage of GDP.

Assuming a reallocation of funding from non-priority sectors to priority sectors, projection results show an increase in priority expenditure and a decrease in debt – but it is uncertain if such a scenario would be advisable. A reprioritization would not only lead to increased priority expenditure, but could also decrease the debt-to-GDP ratio and result in a positive internal borrowing flow. This result can be explained by the assumption that non-priority non-recurrent expenditure will decrease. Non-recurrent expenditure usually requires more borrowing. Hence, because non-recurrent expenditure decreases, it is expected less borrowing is needed. However, this scenario could also turn out very differently. It is important to remember, that non-priority expenditure includes infrastructure investment. If infrastructure investment is lower, real GDP growth is likely to be lower as well. Since the growth of tax revenue depends on real GDP growth, such reallocation could end up reducing fiscal space over the medium term.

In addition to these policy-related scenarios, priority expenditure is also dependent on exogenous factors, and is affected by higher or lower real GDP growth. The projection exercise assumes that allocations for capital expenditure in priority sectors are given percentages of GDP. To the extent this is in fact the case, priority expenditure can be expected to be higher with higher real GDP growth. Equally, priority expenditure is projected to increase less than in the base scenario when GDP growth slows down.

Financing an increase in priority expenditure through additional external debt is less likely in the short run. Generally, caution is needed when funding such investments with commercial debt, because the maturity of debt is usually not in line with the long-term yields likely from investment in health, education and social protection. Concessional debt would be more suitable for this purpose, although the availability of concessional debt is plainly diminishing and Rwanda may want to be careful accumulating much more debt, which could endanger its low level of debt distress.

For the near future, scenarios on expenditure efficiency and increasing local taxation would not have a significant effect on fiscal space in Rwanda. Increasing expenditure efficiency, i.e. improving budget execution,
while always desirable, is less important as a means of augmenting fiscal space compared with neighbouring economies. Rwanda has managed relatively high budget execution at both local and central level. Local government have great potential to increase their own revenues, but at the moment, the share of local government taxation as part of total tax collection is too small to have a significant effect on fiscal space. Surely, capturing illicit financing flows would increase fiscal space – but this cannot be captured in the model.

In summary, Rwanda appears now to be favourably placed to increase its priority expenditure over the medium term. The government’s upcoming strategy suggests a commitment to high prioritization of such expenditure. The present base scenario projects Rwanda could increase its per-child expenditure adequately without creating a significant fiscal gap. Alternative scenarios 6 and 7 do suggest, however, that GDP growth can be expected to affect priority expenditure through its effect on the fiscal space.

Finding additional fiscal space to increase priority expenditure beyond the flow projected in the base scenario is likely to be challenging for Rwanda. Increased VAT collection efficiency, additional external financing, and some reprioritization of expenditure could increase priority expenditure without creating a fiscal gap. Other possibilities, such as increasing debt or higher expenditure efficiency, seem less advisable and less likely for Rwanda.

When discussing fiscal space to fund priority expenditure, UNICEF should take account of this context. This study has provided UNICEF with a methodology and a set of alternative assumptions to engage in a dialogue on how best to maximize the availability of fiscal resources that could be allocated to child-friendly policies, without endangering the sustainability of the country’s macroeconomic position. For the medium term, UNICEF would focus on ensuring as high a growth rate for priority expenditure as possible, subject essentially to two constraints: first, the need to ensure that the economy maintains sufficient infrastructure investment to ensure sustained real GDP growth; and second, the need to ensure fiscal sustainability.
6. References


IMF, Staff Report for the 2017 Article IV Consultation, Seventh Review under the Policy Support Instrument, and Second Review under the Standby Credit Facility, June 2017.


Rwanda Revenue Authority Annual Report FY2015/16.


United Nations Development Programme (UNDP) Human Development Index, Table 6A: Multidimensional Poverty Index: changes over time.


Appendix 1: Fiscal space projections

This appendix describes the details of the base scenario projection exercise discussed in Chapter 4, and then describes the results of a sensitivity analysis as done in Chapter 5.

**Programming assumptions base scenario**

The base scenario programming assumptions are intended to be simplified, to make the calculations relatively easy to carry out and to understand. The following general explanatory points are noted:

1. The assumptions are ‘programming’ assumptions. They are not intended, and should not be understood, as forecasts, but rather as plausible possibilities for planning purposes. In particular, the growth rates of government expenditure are intended as plausible policy settings.

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

3. The elasticities that help determine the government’s revenue performance are taken to be unitary for Scenario 0. This is also a ‘neutral’ assumption. (In general, it is inadvisable to apply econometric point estimates based on historical data for these values, for at least two reasons. The first is that future elasticities of tax revenue with respect to their underlying determinants are likely to differ from historical elasticities. The second is that, for example, if the elasticity of a given revenue line with respect to nominal GDP is assumed to exceed (be less than) 1, the projected revenue flow would rise (diminish) indefinitely as a percentage of GDP.

4. It is straightforward to set programming assumptions that adjust gradually over the projection period, using (‘geometric’) adjustment formulas. This is useful for several different assumption lines. For example, a large proportion of the assumptions are set as growth rates. These can be assumed to rise or diminish gradually from their initial projection values towards their final projection values. Another way to use a gradual adjustment would be for the elasticity of a given revenue line with respect to nominal GDP to take on an initial value somewhat different from 1, but then gradually adjust towards a long-term value of 1.
### Table A.1: Programming assumptions: Base scenario

<table>
<thead>
<tr>
<th><strong>A) World economic conditions (1–3):</strong></th>
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<tbody>
<tr>
<td>(1) The growth rate of the world trade volume decreases gradually from its estimated FY2016/17 value of 5.9 per cent to a FY2023/24 value of 5 per cent.</td>
</tr>
<tr>
<td>(2) The growth rate of the US$ world price level declines gradually from its estimated FY2016/17 value of 3.7 per cent to a FY2023/24 value of 2 per cent.</td>
</tr>
<tr>
<td>(3) The London Inter-bank Offered Rate rises gradually from its FY2016/17 value of 2.4 per cent to a FY2023/24 value of 1.5 per cent.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>B) Basic Rwanda macroeconomic variables (4–10):</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>(4) The growth rate of real GDP gradually increases from 6.1 per cent in FY2016/17 to 7.5 per cent in FY2023/24.</td>
</tr>
<tr>
<td>(5) The GDP deflator grows at the same rate as the year-average consumer price index.</td>
</tr>
<tr>
<td>(6) The December–December growth rate of the consumer price index (CPI) declines gradually from 4.7 per cent in FY2016/17 to 4 per cent in FY2023/24.</td>
</tr>
<tr>
<td>(7) The December–December growth rate of the US$ exchange rate grows at a rate (approximately) equal to the differential of the Rwandan and the world US$ inflation rates.</td>
</tr>
<tr>
<td>(8) The overall population growth rate slowly decreases from 2.5 in FY2016/17 to 2.1 per cent in FY2023/24.</td>
</tr>
<tr>
<td>(9) The under-15 population growth rate slowly decreases from 1.3 in FY2016/17 to 0.7 per cent in FY2023/24.</td>
</tr>
<tr>
<td>(10) The headcount poverty incidence declines gradually from 54.2 per cent in FY2016/17 to 50 per cent in FY2023/24.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Exports and imports of goods and non-factor services (11–17):</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>(11) The export volume grows at the same rate as the world trade volume.</td>
</tr>
<tr>
<td>(12) Export prices grow at the same rate as the world US$ price level.</td>
</tr>
<tr>
<td>(13) The import volume grows at the same rate as real GDP.</td>
</tr>
<tr>
<td>(14) Import prices grow at the same rate as the world US$ price level.</td>
</tr>
<tr>
<td>(15) Non-factor service exports grow at a rate equal to the combined growth rates of world trade volume and the world US$ price level.</td>
</tr>
<tr>
<td>(16) Non-factor service imports, excluding insurance and freight charges for merchandise imports, grow at a rate equal to the combined growth rates of world trade volume and the world US$ price level.</td>
</tr>
<tr>
<td>(17) Insurance and freight charges decline gradually from 12 per cent of the value of merchandise imports in FY2016/17 to 12 per cent in FY2023/24.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>National expenditure accounts (18–20):</strong></th>
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</thead>
<tbody>
<tr>
<td>(18) Consumption expenditure by government entities outside the central government remains at 7.6 per cent of GDP over the projection period.</td>
</tr>
<tr>
<td>(19) Gross fixed capital formation remains at 25.6 per cent of GDP.</td>
</tr>
<tr>
<td>(20) The net increase in inventory stocks remains at 0 per cent over the projection period.</td>
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</tbody>
</table>

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<thead>
<tr>
<th><strong>C) Tax and non-tax revenue (21–31):</strong></th>
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<tbody>
<tr>
<td>(21) The elasticity of personal income tax with respect to nominal GDP declines from 1.2 in FY2017/18 to 1 in FY2023/24.</td>
</tr>
<tr>
<td>(22) The elasticity of company tax revenue with respect to nominal GDP declines from 1.2 in FY2017/18 to 1 in FY2023/24.</td>
</tr>
<tr>
<td>(23) The elasticity of other income tax revenue with respect to nominal GDP declines from 0 in FY2017/18 to 0 in FY2023/24.</td>
</tr>
<tr>
<td>(24) The elasticity of customs revenue with respect to merchandise-import value declines from 1.9 in FY2017/18 to 1 in FY2023/24.</td>
</tr>
<tr>
<td>(25) The elasticity of excise revenue with respect to nominal GDP declines from 1.2 in FY2017/18 to 1 in FY2023/24.</td>
</tr>
<tr>
<td>(26) The elasticity of export duty revenue with respect to export value increases from 0.6 in FY2017/18 to 1 in FY2023/24.</td>
</tr>
<tr>
<td>(27) The internal VAT rate remains unchanged at 18 per cent.</td>
</tr>
<tr>
<td>(28) The internal VAT collection increases gradually from 19.8 per cent in FY2017/18 to 23.1 per cent in FY2023/24</td>
</tr>
</tbody>
</table>
(29) The import-based VAT rate remains at 18 per cent.

(30) The import-based VAT collection increases gradually from 41.7 per cent in FY2017/18 to 48.7 per cent in FY2023/24.

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

(D) External grants to the government (32–33)

(32) Central government external grants for current expenditure slowly decline from 2.7 per cent of GDP in FY2016/17 to 2.7 per cent of GDP in FY2023/24.

(33) Central government external grants for capital expenditure slowly decline from 2.1 per cent of GDP in FY2016/17 to 2.1 per cent of GDP in FY2023/24.

(E) Government expenditure in priority and non-priority categories (34–55)

(E.1) For non-interest recurrent expenditure

(E.1.a) In the education sector

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

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

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

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

(E.1.b) In the health sector

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

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

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

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

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

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

(E.1.d) In the water supply sector

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

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

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

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

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

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

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

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

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

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

(51) Education non-recurrent central government expenditure remain at the FY2016/17 value of 1.2 over the projection years.

(52) Health non-recurrent central government expenditure remain at the FY2016/17 value of 1 per cent of GDP over the projection years.
(53) Social protection non-recurrent central government expenditure remain at the FY2016/17 value of 0.4 per cent of GDP over the projection years.

(54) Non-recurrent water and environment expenditure remain at the FY2016/17 value of 0.1 per cent of GDP over the projection years.

(55) Non-priority non-recurrent central government expenditure decreases gradually from the FY2016/17 value of 8.2 per cent of GDP to a FY2023/24 value of 7 per cent of GDP.

(F) For external and internal debt (56–60)

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

(57) Average interest rates on the previous year’s year-end internal debt stock decreases gradually from 6.5 per cent in FY2016/17 to 5.3 per cent in FY2023/24.

(58) External debt repayments gradually decrease by 1 per cent of the preceding year.

(59) External debt repayments gradually decreases from 5 per cent of GDP in FY2016/17 to 2.8 per cent of GDP in FY2023/24.

(60) External debt disbursements in each projection year amount to 45.4 per cent of total non-recurrent expenditure.

Table A.2: Programming assumptions for the fiscal space projection exercise (base scenario)

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<tbody>
<tr>
<td><strong>(A) External ‘state-of-the-world’ variables:</strong></td>
<td></td>
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<tr>
<td>Growth rates:</td>
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</tr>
<tr>
<td>World trade volume</td>
<td>5.8</td>
<td>5.7</td>
<td>5.5</td>
<td>5.4</td>
<td>5.3</td>
<td>5.1</td>
<td>5.0</td>
</tr>
<tr>
<td>World US$ price level</td>
<td>3.4</td>
<td>3.2</td>
<td>2.9</td>
<td>2.7</td>
<td>2.5</td>
<td>2.2</td>
<td>2.0</td>
</tr>
<tr>
<td>Average world US$ oil price (US$/ billion)</td>
<td>3.4</td>
<td>3.2</td>
<td>2.9</td>
<td>2.7</td>
<td>2.5</td>
<td>2.2</td>
<td>2.0</td>
</tr>
<tr>
<td>Average world US$ copper price (US$/MT)</td>
<td>3.4</td>
<td>3.2</td>
<td>2.9</td>
<td>2.7</td>
<td>2.5</td>
<td>2.2</td>
<td>2.0</td>
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<tr>
<td><strong>Interest rates:</strong></td>
<td></td>
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<tr>
<td>London Inter-bank Offer Rate (LIBOR)</td>
<td>2.1</td>
<td>1.8</td>
<td>1.5</td>
<td>1.5</td>
<td>1.5</td>
<td>1.5</td>
<td>1.5</td>
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<tr>
<td><strong>(B) Basic macroeconomic variables:</strong></td>
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<tr>
<td>Growth rates:</td>
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</tr>
<tr>
<td>GDP (national currency – millions)</td>
<td>11.5</td>
<td>8.6</td>
<td>7.9</td>
<td>8.5</td>
<td>7.1</td>
<td>7.3</td>
<td>7.5</td>
</tr>
<tr>
<td>GDP at 2016 prices and exchange rate (US$ million)</td>
<td>6.3</td>
<td>6.5</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.3</td>
<td>7.5</td>
</tr>
<tr>
<td>GDP deflator</td>
<td>4.9</td>
<td>2.0</td>
<td>1.2</td>
<td>1.5</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Consumer prices (year average)</td>
<td>4.9</td>
<td>2.0</td>
<td>1.2</td>
<td>1.5</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Consumer prices (December)</td>
<td>4.5</td>
<td>4.3</td>
<td>4.2</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Exchange rate (year average)</td>
<td>2.7</td>
<td>0.9</td>
<td>1.2</td>
<td>1.5</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
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<tr>
<td>Exchange rate (December)</td>
<td>1.1</td>
<td>1.1</td>
<td>1.4</td>
<td>2.0</td>
<td>0.3</td>
<td>0.3</td>
<td>1.3</td>
</tr>
<tr>
<td>Population (millions)</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.3</td>
<td>2.2</td>
<td>2.2</td>
<td>2.1</td>
</tr>
<tr>
<td>Population under 15 (millions)</td>
<td>1.5</td>
<td>1.4</td>
<td>1.1</td>
<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
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<tr>
<td>Population in poverty</td>
<td>–1.6</td>
<td>–1.6</td>
<td>–1.3</td>
<td>2.0</td>
<td>0.3</td>
<td>0.3</td>
<td>1.3</td>
</tr>
<tr>
<td>Headcount poverty incidence</td>
<td>52.8</td>
<td>51.4</td>
<td>50.0</td>
<td>50.0</td>
<td>50.0</td>
<td>50.0</td>
<td>50.0</td>
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<tr>
<td>Growth rates (US$ million):</td>
<td></td>
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<td></td>
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</tr>
<tr>
<td>Merchandise exports:</td>
<td>9.4</td>
<td>9.0</td>
<td>8.5</td>
<td>7.8</td>
<td>8.3</td>
<td>8.3</td>
<td>7.5</td>
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### Fiscal Space for Children: An analysis of options in Rwanda

#### Merchandise imports:

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<tbody>
<tr>
<td><strong>Unit value</strong></td>
<td>3.4</td>
<td>3.2</td>
<td>2.9</td>
<td>2.7</td>
<td>2.5</td>
<td>2.2</td>
<td>2.0</td>
</tr>
<tr>
<td><strong>Volume</strong></td>
<td>5.8</td>
<td>5.7</td>
<td>5.4</td>
<td>5.0</td>
<td>5.7</td>
<td>5.9</td>
<td>5.4</td>
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<tr>
<td><strong>Non-oil imports</strong></td>
<td>9.9</td>
<td>9.9</td>
<td>9.6</td>
<td>9.0</td>
<td>11.0</td>
<td>11.2</td>
<td>10.4</td>
</tr>
<tr>
<td><strong>Unit value</strong></td>
<td>3.4</td>
<td>3.2</td>
<td>2.7</td>
<td>2.0</td>
<td>3.6</td>
<td>3.7</td>
<td>2.7</td>
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<tr>
<td><strong>Volume</strong></td>
<td>6.3</td>
<td>6.5</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.3</td>
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#### Growth rates:

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<tbody>
<tr>
<td>Non-factor services receipts</td>
<td>9.4</td>
<td>9.0</td>
<td>8.2</td>
<td>7.9</td>
<td>7.5</td>
<td>7.1</td>
<td>7.1</td>
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<tr>
<td>Non-factor services payments excluding merchandise-imports insurance and freight</td>
<td>9.9</td>
<td>9.9</td>
<td>9.6</td>
<td>9.5</td>
<td>9.5</td>
<td>9.4</td>
<td>9.7</td>
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#### Ratios:

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<tr>
<td>Ratio insurance and freight costs/merchandise imports value</td>
<td>12.0</td>
<td>12.0</td>
<td>12.0</td>
<td>12.0</td>
<td>12.0</td>
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<tr>
<td>Incremental capital-output ratio</td>
<td>4.0</td>
<td>3.8</td>
<td>3.7</td>
<td>3.6</td>
<td>3.5</td>
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#### Percentage of GDP:

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<tbody>
<tr>
<td>Consumption expenditure by governments excl. central government</td>
<td>7.6</td>
<td>7.6</td>
<td>7.6</td>
<td>7.6</td>
<td>7.6</td>
<td>7.6</td>
<td>7.6</td>
</tr>
<tr>
<td>Gross fixed capital formation</td>
<td>25.6</td>
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# Appendix 1: Fiscal space projections

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### Table: Fiscal Space for Children: An analysis of options in Rwanda

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**Projection results base scenario**

Table A.3 shows the base scenario projection results. The top line of the projection (A) shows the evolution of priority expenditure, and the lines below show the evolution of the components of its fiscal space: tax and non-tax revenue (B), external grants (C), non-priority expenditure (−) (D), external debt disbursements (E), external debt service (−) (F), and the ‘fiscal gap’ (G).

The net internal debt flow as a percentage of GDP is the ‘bottom line’ result, determined residually for each year from the assumed priority-expenditure and fiscal space flows. For each projection year, it indicates the ‘fiscal gap’ implied by the programming assumptions, including those that determine priority expenditure and those that determine the other fiscal accounts. For Scenario 0 the average net internal debt flow would be 0 per cent of GDP. The total (external and internal) government debt stock would conclude in FY2023/24 at 42.2 per cent of GDP. Policymakers would presumably consider the fiscal balance projections satisfactory per se, although one of the main reasons for this outcome is that expenditure in education, health and other sectors relevant for children’s needs would remain low, and perhaps inadequate. These results would seem to imply there is scope for increasing expenditure beneficial to children.
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## Fiscal Space for Children: An analysis of options in Rwanda

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**Projection results alternative scenarios**

In **Scenario 0** the average FY2017/18–FY2023/24 net internal debt flow would be 0 per cent of GDP and the total (external and internal) government debt stock would conclude in FY2023/24 at 42 per cent of GDP.

**Scenario 1** considers an improvement in the VAT collection efficiency. Thus, an assumption is made that domestic VAT collection efficiency increases gradually from 20 per cent in FY2017/18 to 25 per cent in FY2023/24, while import VAT collection efficiency increases gradually from 42 per cent in FY2017/18 to 54 per cent in FY2023/24. With these assumptions, the average FY2017/18–FY2023/24 net internal debt flow would be –0.4 per cent of GDP (compared with 0 per cent of GDP in Scenario 0). The total (external and internal) government debt stock would conclude in FY2023/24 at 39.7 per cent of GDP (compared with 42.2 per cent in Scenario 0).

**Scenario 2** considers an increase (compared to the baseline scenario) of priority expenditure, which means the increase of priority expenditure as a percentage of GDP will be higher – from 6 per cent of GDP in FY2017/18 to 6.6 per cent of GDP in FY2023/24. Compared to the base scenario, the priority expenditure (as a percentage of GDP) would be on average 2 per cent higher. With these assumptions, the average FY2017/18–FY2023/24 net internal debt flow would be 0.2 per cent of GDP (compared with 0 per cent of GDP in Scenario 0). The total (external and internal) government debt stock would conclude in FY2023/24 at 43.1 per cent of GDP (compared with 42.2 per cent in Scenario 0).

**Scenario 3** combines the assumption of Scenario 2 and Scenario 1, so that the increase in priority expenditure would effectively be funded through higher tax revenue resulting from enhanced VAT administration. When combining these assumptions, the average FY2017/18–FY2023/24 net internal debt flow would be –0.2 per cent of GDP (compared with 0 per cent of GDP in Scenario 0). The total (external and internal) government debt stock would conclude in FY2023/24 at 40.7 per cent of GDP (compared with 42.2 per cent in Scenario 0).

**Scenario 4** considers an increase of external grants to fund priority expenditure. The increase in priority expenditure equals the assumptions of Scenario 2, while external grants for current and capital expenditure will slowly increase to 3 per cent of GDP in FY2023/24, i.e., a total of 6 per cent of GDP. With these assumptions, the average FY2017/18–FY2023/24 net internal debt flow would be –0.6 per cent of GDP (compared with 0 per cent of GDP in Scenario 0). The total (external and internal) government debt stock would conclude in FY2023/24 at 38.5 per cent of GDP (compared with 42.2 per cent in Scenario 0).

**Scenario 5** considers a decrease of non-priority recurrent and non-recurrent expenditure (decreasing respectively to 11.8 and 5.6 per cent of GDP in FY2023/24), while priority expenditure increases (compared to baseline scenario) as considered in Scenario 2. With these assumptions, the average FY2017/18–FY2023/24 net internal debt flow would be –0.6 per cent of GDP (compared with 0 per cent of GDP in Scenario 0). The total (external and internal) government debt stock would conclude in FY2023/24 at 37.4 per cent of GDP (compared with 42.2 per cent in Scenario 0).

**Scenario 6** makes the same assumption as the baseline scenario with the only difference being that the real growth rate is higher (gradually increasing from 6.3 per cent in FY2017/18 to 8 per cent in FY2023/24). The share of priority expenditure would somewhat reduce as per GDP, because GDP is growing. With these assumptions, the average FY2017/18–FY2023/24 net internal debt flow would be –0.1 per cent of GDP (compared with 0 per cent of GDP in Scenario 0). The total (external and internal) government debt stock would conclude in FY2023/24 at 41.1 per cent of GDP (compared with 42.2 per cent in Scenario 0).

**Scenario 7** reverses what is considered in Scenario 6. We thus consider a decline in real GDP growth rate (a gradual decline from 5.7 per cent in FY2017/18 to 4 per cent in FY2023/24). Lower GDP growth would reduce the percentage of total expenditure spent on priority sectors from 24.9 per cent in the base scenario to 24.19 per cent.
in FY2023/24. Per-child expenditure would decrease from US$185 to US$167.99. With these assumptions, the average FY2017/18–FY2023/24 net internal debt flow would be 0.9 per cent of GDP (compared with 0 per cent of GDP in Scenario 0). The total (external and internal) government debt stock would conclude in FY2023/24 at 53.4 per cent of GDP (compared with 42.2 per cent in Scenario 0).

**Table A.4: Summary scenario results for the projection exercise**

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<tr>
<th>Scenario</th>
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<td>Other revenue</td>
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<td>0.9</td>
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<td>2.4</td>
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<td>–0.1</td>
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<td>Final-year general-government debt stock</td>
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<td>43.1</td>
<td>40.7</td>
<td>38.5</td>
<td>37.4</td>
<td>41.1</td>
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<td>40.0</td>
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### Table A.5: Scenario descriptions

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<tr>
<th>Scenario descriptions</th>
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<th>Enhanced VAT administration</th>
<th>Increased priority expenditure</th>
<th>Increase priority expenditure and enhanced VAT administration</th>
<th>Increased external grants for social sectors</th>
<th>Reduction of non-priority expenditure and increased priority expenditure</th>
<th>Higher real GDP growth</th>
<th>Lower real GDP growth</th>
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<tr>
<td>Real GDP growth rate</td>
<td>The growth rate of real GDP increases gradually from 6.3 per cent in FY2017/18 to 7.5 per cent in FY2023/24</td>
<td>The growth rate of real GDP increases gradually from 6.3 per cent in FY2017/18 to 7.5 per cent in FY2023/24</td>
<td>The growth rate of real GDP increases gradually from 6.3 per cent in FY2017/18 to 7.5 per cent in FY2023/24</td>
<td>The growth rate of real GDP increases gradually from 6.3 per cent in FY2017/18 to 7.5 per cent in FY2023/24</td>
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<td>The growth rate of real GDP increases gradually from 6.3 per cent in FY2017/18 to 7.5 per cent in FY2023/24</td>
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<td>Domestic VAT collection efficiency</td>
<td>Domestic VAT collection efficiency increases gradually from 19.8 per cent in FY2017/18 to 23.1 in FY2023/24</td>
<td>Domestic VAT collection efficiency increases gradually from 20.1 per cent in FY2017/18 to 25.4 in FY2023/24</td>
<td>Domestic VAT collection efficiency increases gradually from 20.1 per cent in FY2017/18 to 25.4 in FY2023/24</td>
<td>Domestic VAT collection efficiency increases gradually from 20.1 per cent in FY2017/18 to 25.4 in FY2023/24</td>
<td>Domestic VAT collection efficiency increases gradually from 20.1 per cent in FY2017/18 to 25.4 in FY2023/24</td>
<td>Domestic VAT collection efficiency increases gradually from 20.1 per cent in FY2017/18 to 25.4 in FY2023/24</td>
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<td>Import VAT collection efficiency</td>
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<td>Import VAT collection efficiency increases gradually from 42.4 per cent in FY2017/18 to 53.6 per cent in FY2023/24</td>
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<td>Import VAT collection efficiency increases gradually from 42.4 per cent in FY2017/18 to 53.6 per cent in FY2023/24</td>
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<td>Central government external grants for current expenditure</td>
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<td>Central government external grants for current expenditure increase gradually from 2.66 per cent of GDP in FY2017/18 to the value of 2.7 in FY2023/24</td>
<td>Central government external grants for current expenditure increase gradually from 2.66 per cent of GDP in FY2017/18 to the value of 2.7 in FY2023/24</td>
<td>Central government external grants for current expenditure increase gradually from 2.66 per cent of GDP in FY2017/18 to the value of 2.7 in FY2023/24</td>
<td>Central government external grants for current expenditure increase gradually from 2.66 per cent of GDP in FY2017/18 to the value of 2.7 in FY2023/24</td>
<td>Central government external grants for current expenditure increase gradually from 2.66 per cent of GDP in FY2017/18 to the value of 2.7 in FY2023/24</td>
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<td>Enhanced VAT administration</td>
<td>Increased priority expenditure</td>
<td>Increase priority expenditure and enhanced VAT administration</td>
<td>Increased external grants for social sectors</td>
<td>Reduction of non-priority expenditure and increased priority expenditure</td>
<td>Higher real GDP growth</td>
<td>Lower real GDP growth</td>
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<td>Central government external grants for capital expenditure (projects) increase gradually from 2.11 per cent of GDP in FY2017/18 to the value of 2.1 in FY2023/24</td>
<td>Central government external grants for capital expenditure (projects) increase gradually from 2.11 per cent of GDP in FY2017/18 to the value of 2.1 in FY2023/24</td>
<td>Central government external grants for capital expenditure (projects) increase gradually from 2.11 per cent of GDP in FY2017/18 to the value of 2.1 in FY2023/24</td>
<td>Central government external grants for capital expenditure (projects) increase gradually from 2.11 per cent of GDP in FY2017/18 to the value of 2.1 in FY2023/24</td>
<td>Central government external grants for capital expenditure (projects) increase gradually from 2.11 per cent of GDP in FY2017/18 to the value of 2.1 in FY2023/24</td>
<td>Central government external grants for capital expenditure (projects) increase gradually from 2.11 per cent of GDP in FY2017/18 to the value of 2.1 in FY2023/24</td>
<td>Central government external grants for capital expenditure (projects) increase gradually from 2.11 per cent of GDP in FY2017/18 to the value of 2.1 in FY2023/24</td>
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<td>Elasticity of education staff size with respect to child population stays at the value of 1 over the projection years</td>
<td>Elasticity of education staff size with respect to child population stays at the value of 1 over the projection years</td>
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<td>Elasticity of health staff size with respect to total population stays at the value of 1 over the projection years</td>
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## Appendix 1: Fiscal space projections

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<th>Increased priority expenditure and enhanced VAT administration</th>
<th>Increased external grants for social sectors</th>
<th>Reduction of non-priority expenditure and increased priority expenditure</th>
<th>Higher real GDP growth</th>
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<td>Elasticity of water and environment staff size with respect to child population stays at the value of 1 over the projection years</td>
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<td>Growth rate of water and environment remuneration rates increases gradually from 9.71 in FY2017/18 to the value of 5.81 in FY2023/24</td>
<td>Growth rate of water and environment remuneration rates increases gradually from 9.71 in FY2017/18 to the value of 5.81 in FY2023/24</td>
<td>Growth rate of water and environment remuneration rates increases gradually from 9.71 in FY2017/18 to the value of 5.81 in FY2023/24</td>
<td>Growth rate of water and environment remuneration rates decreases gradually from 8.82 in FY2017/18 to the value of 5.28 in FY2023/24</td>
<td>Growth rate of water and environment remuneration rates increases gradually from 9.71 in FY2017/18 to the value of 5.81 in FY2023/24</td>
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<tr>
<td>Scenario descriptions</td>
<td>Base</td>
<td>Enhanced VAT administration</td>
<td>Increased priority expenditure and enhanced VAT administration</td>
<td>Increase external grants for social sectors</td>
<td>Reduction of non-priority expenditure and increased priority expenditure</td>
<td>Higher real GDP growth</td>
<td>Lower real GDP growth</td>
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<tr>
<td>Scenario number</td>
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<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>6</td>
</tr>
<tr>
<td>Real growth rate of recurrent water supply expenditure on goods and services</td>
<td>Real growth rate of recurrent water and environment expenditure on goods and services decreases gradually from 7.44 in FY2017/18 to the value of 2.11 in FY2023/24</td>
<td>Real growth rate of recurrent water and environment expenditure on goods and services decreases gradually from 7.44 in FY2017/18 to the value of 2.11 in FY2023/24</td>
<td>Real growth rate of recurrent water and environment expenditure on goods and services increases gradually from 8.18 in FY2017/18 to the value of 2.32 in FY2023/24</td>
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<tr>
<td>Real growth rate of other non-staff recurrent water supply expenditure</td>
<td>Real growth rate of other non-staff recurrent water and environment expenditure decreases gradually from 6.44 in FY2017/18 to the value of 0.73 in FY2023/24</td>
<td>Real growth rate of other non-staff recurrent water and environment expenditure decreases gradually from 6.44 in FY2017/18 to the value of 0.73 in FY2023/24</td>
<td>Real growth rate of other non-staff recurrent water and environment expenditure increases gradually from 7.09 in FY2017/18 to the value of 0.8 in FY2023/24</td>
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</tr>
<tr>
<td>Elasticity of central government non-priority expenditure on goods and services with respect to non-priority staff size decreases gradually from 1.2 in FY2017/18 to 1 in FY2023/24</td>
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</tbody>
</table>
### Appendix 1: Fiscal space projections

<table>
<thead>
<tr>
<th>Scenario descriptions</th>
<th>Base</th>
<th>Enhanced VAT administration</th>
<th>Increased priority expenditure</th>
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<td>4</td>
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<td>6</td>
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<tr>
<td>Central government non-priority non-recurrent expenditure as a share of GDP</td>
<td>Central government non-priority non-recurrent expenditure as a share of GDP decreases gradually from 8.01 in FY2017/18 to 7 in FY2023/24</td>
<td>Central government non-priority non-recurrent expenditure as a share of GDP decreases gradually from 8.01 in FY2017/18 to 7 in FY2023/24</td>
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<tr>
<td>External debt disbursements (+):</td>
<td>Increase gradually from 2.74 per cent of GDP in FY2017/18 to 2.79 per cent of GDP in FY2023/24</td>
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