
ESS Extension of Social Security

Fiscal space and the extension of social protection: Lessons learnt from developing countries

**Bolivia, Botswana, Brazil, Costa Rica, Lesotho, Namibia,
Thailand and South Africa**

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José Francisco Pacheco

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Global Campaign on Social Security and Coverage for All

International Labour Office

**Social Security Department
Geneva**

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Contents

	<i>Page</i>
List of acronyms.....	ix
Foreword	xiii
Acknowledgements	xv
1. Introduction.....	1
2. Fiscal space and social protection: Summary of lessons learnt.....	5
2.1. Information sources	5
2.2. Brief overview of the countries.....	6
2.3. General economic and fiscal conditions and their relation to fiscal space for social protection	10
2.4. Trends and lessons learnt	13
2.4.1. Main characteristics of social protection programmes.....	13
2.4.2. Mechanisms for creating fiscal space: Practical evidence	14
2.4.3. Fourteen lessons learnt.....	17
3. Bolivia: Financing the extension of social protection through taxes on hydrocarbons.....	23
3.1. Country profile.....	23
3.2. Bolivia's social protection system.....	24
3.2.1. Contributory benefits	24
3.2.2. Non-contributory benefits	24
3.3. <i>Renta dignidad</i> : Universalizing old-age pensions	25
3.4. Coverage indicators	26
3.5. How fiscal space was created to finance the extension of non-contributory coverage?	28
3.6. Fiscal space and the sustainability of investment for development	31
3.7. Impact of new social investment in Bolivia.....	32
3.8. Lessons learnt	33
4. Botswana: Creating the basis for improved social protection.....	35
4.1. Country profile.....	35
4.2. Social protection policy	43
4.2.1. Organization and coverage	43
4.2.2. Social protection financing and expenditure.....	47
4.2.3. Pensions	50
4.3. Considerations regarding the creation of fiscal space.....	51
4.4. Policy considerations and lessons learnt.....	53
4.4.1. Policy considerations	53
4.4.2. Lessons learnt.....	54

5.	Brazil: Increasing fiscal space through social contributions	57
5.1.	Country profile.....	57
5.2.	Social investment.....	58
5.3.	Overview of the Brazilian social protection system	59
5.3.1.	Social insurance programmes	59
5.3.2.	Universal health system	60
5.3.3.	Social assistance.....	61
5.4.	Fiscal space for social protection.....	64
5.4.1.	The 1988 Constitution and fiscal space	64
5.4.2.	Gross tax burden: The role of social contributions	65
5.4.3.	Rural pensions.....	66
5.5.	Temporary tax on financial transactions.....	67
5.6.	Fiscal space, economic growth and development.....	68
5.7.	What about creating fiscal space for development?.....	70
5.8.	Lessons learnt	72
6.	Costa Rica: Prioritizing fiscal space for social protection	75
6.1.	Country profile.....	75
6.2.	Social protection programmes and social spending.....	80
6.3.	Contributory social security programmes: The Costa Rican Social Insurance Fund (CCSS)	83
6.4.	Non-contributory pensions	85
6.5.	Poverty reduction initiatives	86
6.5.1.	Initial efforts to reduce poverty in Costa Rica: FODESAF	86
6.5.2.	The Bono de vivienda housing programme	87
6.5.3.	The Comedores escolares school meals programme	87
6.5.4.	The Avancemos conditional cash transfer programme	87
6.5.5.	The CEN-CINAI programme.....	88
6.5.6.	Coverage rates of the main poverty reduction initiatives.....	88
6.6.	Fiscal space for social protection in Costa Rica	89
6.7.	Challenges and lessons learnt	89
6.7.1.	Challenges.....	89
6.7.2.	Lessons learnt.....	91
7.	Lesotho: Taking advantage of good economic conditions and strong political will to increase social protection.....	95
7.1.	Country profile.....	95
7.2.	Social protection programmes: Initiatives and financing	100
7.2.1.	Social protection programmes	100
7.2.2.	Social programme financing	101
7.2.3.	Old-age pension scheme	103
7.2.4.	Other pension schemes	104

7.3.	Fiscal space for social protection.....	104
7.4.	Challenges and lessons learnt.....	106
7.4.1.	Challenges.....	106
7.4.2.	Lessons learnt.....	106
8.	Namibia: When politics overcomes limited resources.....	109
8.1.	Country profile.....	109
8.2.	Social protection: Programmes and public spending.....	114
8.2.1.	Social spending and expenditure on social protection.....	114
8.2.2.	Old-age pensions.....	118
8.2.3.	Contributory social security system.....	118
8.2.4.	Other social assistance initiatives.....	119
8.2.5.	The basic income grant.....	120
8.3.	The creation of fiscal space in Namibia.....	121
8.4.	Challenges and lessons learnt.....	122
8.4.1.	Challenges.....	122
8.4.2.	Lessons learnt.....	123
9.	South Africa: Social protection for integration.....	125
9.1.	Country profile.....	125
9.2.	Social protection: Programmes and investment.....	130
9.2.1.	Social assistance programmes.....	133
9.2.2.	Social insurance programmes.....	135
9.3.	The creation of fiscal space for social protection.....	137
9.4.	Challenges and lessons learnt.....	138
9.4.1.	Challenges.....	138
9.4.2.	Lessons learnt.....	139
10.	Thailand: A hybrid strategy for achieving universal coverage in health care.....	141
10.1.	Country profile.....	141
10.2.	Social protection programmes and social spending.....	145
10.2.1.	Contributory social security schemes.....	145
10.2.2.	Non-contributory social programmes.....	148
10.2.3.	Expenditure on social protection.....	149
10.2.4.	Filling the gap in the healthcare sector: The Universal Coverage Scheme.....	151
10.3.	The construction of fiscal space for social protection.....	152
10.4.	Challenges and lessons learnt.....	155
10.4.1.	Challenges.....	155
10.4.2.	Lessons learnt.....	155
	References.....	157
	Other documents consulted.....	163

List of tables

Table 1.	Decline in debt servicing and ODA flows by country, 2005-2008.....	12
Table 2.	Increments in social spending and social protection spending (as a multiple of the initial year).....	12
Table 3.	Matrix of programmes (by country)	13
Table 4.	Matrix of fiscal space strategies (by country).....	15
Table 5.	Bolivia: Social protection coverage indicators, 2000-2009	27
Table 6.	Botswana: Social protection programmes	44
Table 7.	Brazil: Evolution of the coverage of the pension system.....	60
Table 8.	Costa Rica: Key socioeconomic indicators, latest available year	80
Table 9.	Costa Rica: Contributory and non-contributory programmes.....	81
Table 10.	Lesotho: Main social indicators	99
Table 11.	Lesotho: Social protection programmes	100
Table 12.	Namibia: Socioeconomic conditions	113
Table 13.	Namibia: Social protection programmes	114
Table 14.	South Africa: Socioeconomic indicators, various years	130
Table 15.	Thailand: Main social indicators.....	144
Table 16.	Thailand: Social protection programmes	145
Table 17.	Thailand: Contributory rates under the Social Security Fund as a percentage of insurable earnings	147
Table 18.	Thailand: Social protection benefits and sources of financing	153

List of figures

Figure 1.	Human Development Index, countries analyzed in the study.....	7
Figure 2.	GDP per capita 2009 and GDP growth by country (1995-2009, PPP terms)	7
Figure 3.	Social spending and social protection as a percentage of GDP (2005-2008)	8
Figure 4.	Social spending and social protection expenditures as a percentage of total government expenditure (2005-2008).....	9
Figure 5.	Public spending and fiscal revenue, 2005-2008 (percentage of GDP)	10
Figure 6.	Net changes in fiscal revenue and public expenditure in percentage points of GDP ...	11
Figure 7.	Relationship between social security expenditure and HDI (latest available year).....	14
Figure 8.	Bolivia: Total tax revenue and hydrocarbons tax revenue, as a percentage of GDP (1990-2008)	29
Figure 9.	Bolivia: Social expenditure as a percentage of GDP and revenue from taxes on hydrocarbons (1995 – 2007)	30
Figure 10.	Bolivia: Trend of spending on social assistance programmes as a percentage of GDP	31
Figure 11.	Botswana: Historical population growth rates, 1960-2008.....	35
Figure 12.	Botswana: Population pyramid, 2010.....	36
Figure 13.	Botswana: Long-term GDP and GDP per capita growth rates, 1960-2010	37
Figure 14.	Botswana: Structure of the economy by sector.....	37
Figure 15.	Botswana: Diamond exports as a percentage of total exports, 2001-2008	38
Figure 16.	Botswana: Fiscal revenue and public expenditure as a percentage of GDP, 1991-2008	39
Figure 17.	Botswana: ODA as a percentage of gross national income, 1960-2008.....	40
Figure 18.	Botswana: External debt and debt service, 1975-2007	41
Figure 19.	Botswana: Poverty rates in Botswana, several years	42
Figure 20.	Botswana: Human development index, 1980-2007	42
Figure 21.	Botswana: Infant mortality, 1980-2008	43
Figure 22.	Botswana: Public social expenditure as a percentage of GDP and of total public expenditure, 2000-2008	48
Figure 23.	Botswana: Structure of social spending by sector, 1991, 1995, 2000, 2005 and 2008.	48
Figure 24.	Botswana: Expenditure on social protection as a percentage of GDP and of total public expenditure, 1991-2008	49

Figure 25.	Botswana: Structure of expenditure on social protection, 1991-2008	50
Figure 26.	Brazil: Evolution of social expenditure as a percentage of GDP.....	58
Figure 27.	Brazil: Insured contributors to the pension system as a percentage of EAP.....	59
Figure 28.	Brazil: Real per capita public expenditure on health (R\$, 1998=100).....	61
Figure 29.	Brazil: Coverage of social assistance programmes (thousands)	63
Figure 30.	Brazil: Fiscal revenue (including social contributions) and social contributions, as a percentage of GDP.....	65
Figure 31.	Brazil: CPMF as a percentage of social protection expenditure and GDP	67
Figure 32.	Costa Rica: Population growth rate, 1960-2010.....	75
Figure 33.	Costa Rica: Population pyramids, 1995, 2010 and 2025 (projected).....	76
Figure 34.	Costa Rica: GDP per capita, 1960-2008	77
Figure 35.	Costa Rica: Government expenditure and revenue, several years.....	78
Figure 36.	Costa Rica: Debt service as a percentage of total exports, 1977-2008	79
Figure 37.	Costa Rica: ODA flows as a percentage of GNI, 1960-2008	79
Figure 38.	Costa Rica: Social spending as a percentage of GDP, 1990-2009.....	82
Figure 39.	Costa Rica: Composition of social spending, 1990-2009	82
Figure 40.	Costa Rica: Average participation of social protection categories, 2000-2009	83
Figure 41.	Costa Rica: Social contributions as a percentage of GDP and of expenditure on social protection, 1990-2009.....	84
Figure 42.	Costa Rica: Contributory health insurance and pension coverage, as a percentage of the economically active population (EAP), 1990-2009.....	85
Figure 43.	Costa Rica: old-age coverage by contributory and non-contributory old-age pensioners (people over 65 years of age), 1990-2009	86
Figure 44.	Costa Rica: Poor beneficiaries as a percentage of the target population, by programme, 2007	88
Figure 45.	Costa Rica: Percentage of beneficiaries who are not part of the target group, by programme, 2007	90
Figure 46.	Lesotho: Population growth rate, 1960-2008.....	95
Figure 47.	Lesotho: Public revenue and expenditure as a percentage of GDP (5-year periods, 1990-2008).....	96
Figure 48.	Lesotho: Structure of tax revenues, 2008	97
Figure 49.	Lesotho: Structure of public expenditure, 2004 and 2008	97
Figure 50.	Lesotho. External debt and total debt service in Lesotho, 1975-2008	98
Figure 51.	Lesotho: ODA as a percentage of GNI, 1966-2008.....	99
Figure 52.	Lesotho: Composition of social spending as a percentage of GDP, 2005-2008	102
Figure 53.	Lesotho: Expenditure on social protection as a percentage of GDP, 2005-2008.....	103
Figure 54.	Lesotho: Composition of social protection expenditure, 2009	104
Figure 55.	Namibia: Population growth rate, 1960-2010.....	109
Figure 56.	Namibia: Population pyramids for 2010 and 2030	110
Figure 57.	Namibia: GDP per capita, 1980-2008 (US\$ current).....	111
Figure 58.	Namibia: Tax revenues and public spending as a percentage of GDP (several years) .	111
Figure 59.	Namibia: External debt as a percentage of GDP, 2003-2008	112
Figure 60.	Namibia: Official development assistance as a percentage of GNI, 1985-2008.....	113
Figure 61.	Namibia: Public social expenditure, 2005-2008.....	115
Figure 62.	Namibia: Composition of social expenditure as a percentage of GDP, 2005-2008.....	116
Figure 63.	Namibia: Expenditure on social protection as a percentage of total public spending, 2005-2008	117
Figure 64.	Namibia: Health, contributory social security and social assistance as a percentage of GDP, 2005-2008.....	117
Figure 65.	South Africa: Total population 1960-2010	125
Figure 66.	South Africa: Population pyramids, 2000, 2010 and 2025	126
Figure 67.	South Africa: GDP per capita in US\$, 1960-2010.....	127
Figure 68.	South Africa: Fiscal revenue and expenditure, 2000-2008.....	128
Figure 69.	South Africa: Total debt service as a percentage of total exports, 1994-2008	128
Figure 70.	South Africa: ODA flows as a percentage of GNI and in per capita terms, 1993-2008	129

Figure 71.	South Africa: Social spending, 2000-2008	131
Figure 72.	South Africa: Composition of social spending as a percentage of GDP, 2000-2008 ...	132
Figure 73.	South Africa: Real per capita spending on social protection programmes in Rands, 2000-2008	132
Figure 74.	South Africa: Coverage rates of the state old-age pension programme, selected years	134
Figure 75.	Thailand: Population growth rate, 1960-2009	141
Figure 76.	Thailand: GDP per capita in current US\$, 1960-2009.....	142
Figure 77.	Thailand: Total revenue, total expenditure and the fiscal balance as a percentage of GDP, 1995-2008	143
Figure 78.	Thailand: Total debt service as a percentage of total exports, 1975-2008.....	143
Figure 79.	Thailand: ODA flows as a percentage of GNI, 1960-2008.....	144
Figure 80.	Thailand: Cost per beneficiary in selected social protection programmes, 2006-2008	149
Figure 81.	Thailand: Social spending as a percentage of GDP and of public spending, 2005-2009	150
Figure 82.	Thailand: Social spending by category, 2005-2009.....	150
Figure 83.	Thailand: Health, social insurance and social assistance expenditure as a percentage of GDP, 2005-2009.....	151
Figure 84.	Thailand: UC budget as a percentage of GDP and of the government budget, 2003-2009	152

List of acronyms

AfDB	African Development Bank
AFP	Pension Fund Administrators
AIDS	Acquired immune deficiency syndrome
APC	African Pioneer Corps (Lesotho)
APS	Autoridad de Fiscalización y Control de Pensiones y Seguros (Bolivia–Audit authority and control of pensions and insurance)
ART	Antiretroviral treatment
BAIS	Botswana AIDS impact survey
BCCR	Banco Central de Costa Rica (Costa Rica Central Bank)
BFTU	Botswana Federation of Trade Unions
BIG	Basic income grant (Namibia)
BONOSOL	Bono Solidario (Bolivia)
BPOPF	Botswana Public Officers Pension Fund
CBO	Community-based organizations
CBS	Central Bureau of Statistics (Namibia)
CCSS	Caja Costarricense del Seguro Social (Costa Rican Social Insurance Fund)
CCT	Conditional cash transfer
CEF	Caixa Econômica Federal (Brazil - Federal Economic Bank)
CELADE	Latin American and Caribbean Demographic Centre
CEN-CINAI	Early childhood programme (Costa Rica)
COIDF	Compensation for Occupational Injuries and Diseases Fund (South Africa)
CONAI	Comisión Nacional de Asuntos Indígenas (Costa Rica–National Commission of Indian Affairs)
CPMF	Contribuição "Provisória" por Movimentação Financeira (Brazil–Financial transactions provisional contribution)
CSG	Child Support Grant (South Africa)
CSLL	Contribuição Social sobre o Lucro Líquido (Brazil–Social Contribution on Net Income)
CSMBS	Civil Servant Medical Benefit Scheme (Thailand)

DG	Disability Grant (South Africa)
DTH	Direct tax on hydrocarbons (Bolivia)
EAP	Economically Active Population
ECF	Employee's Compensation Fund (Namibia)
ECLAC	Economic Commission for Latin America and the Caribbean
FAO	Food and Agriculture Organization
FCC	Fondo de Capitalización Colectiva (Bolivia - Collective Capitalization Fund)
FODESAF	Fondo de Desarrollo Social y Asignaciones Familiares (Costa Rica - Fund for Social Development and Family Allowances)
FONABE	Fondo Nacional de Becas (Costa Rica - National Scholarship Fund)
GDP	Gross Domestic Product
GEP	Government Employees Pension (South Africa)
GEPF	Government Employees Pension Fund (South Africa)
GNI	Gross national income
GPF	Government Pension Fund (Thailand)
HDI	Human development index
HIV	Human immunodeficiency virus
IBGE	Instituto Brasileiro de Geografia e Estatística (Brazilian Institute of Geography and Statistics)
ILO	International Labour Organization
IMAS	Instituto Mixto de Ayuda Social (Costa Rica - Joint Social Welfare Institute)
IMF	International Monetary Fund
IMR	Infant mortality rates
INAMU	Instituto Nacional de las Mujeres (Costa Rica - National Institute of Women)
INSS	National Social Insurance Institute (Brazil)
IPEA	Instituto de Pesquisa Econômica Aplicada (Brazil - Institute of Applied Economic Research)
IRIF	Inter-Regional Inequality Facility (South Africa)
ISSA	International Social Security Association

IU	Unemployment insurance (South Africa)
LDC	Least developed countries
LEI	Life expectancy index
LHDA	Lesotho Highlands Development Authority
MDG	Millennium Development Goals
MDS	Ministério do Desenvolvimento Social e Combate à Fome (Brazil - Ministry of Social Development and Fight against Hunger)
MFDP	Ministry of Finance and Development Planning (Botswana)
MFDP	Ministry of Finance and Development Planning (Lesotho)
MGECW	Ministry of Gender Equality and Child Welfare (Namibia)
MHI	Mandatory health insurance
MHSS	Ministry of Health and Social Services (Namibia)
MIDEPLAN	Ministerio de Planificación Nacional y Política Económica (Costa Rica - Ministry of National Planning and Economic Policy)
NGO	Non-governmental organization
NHSO	National Health Security Office (Thailand)
NSSF	National Social Security Fund (South Africa)
OAP	Old-age pension programme
OECD	Organisation for Economic Co-operation and Development
ODA	Official development assistance
PANI	Patronato Nacional de la Infancia (Costa Rica - National Foundation for Children)
PLHIV	People living with HIV/AIDS
PPP	Purchasing power parity
PSTWF	Private-School Teachers' Welfare Fund (Thailand)
RHVP	Regional Hunger and Vulnerability Programme
SASSA	South African Social Security Agency
SENARC	Secretaria Nacional de Renda de Cidadania (Brazil - National Secretariat on Citizenship Income)
SIDES	Sistema de Información Sociodemográfica, Económica y Ambiental (Costa Rica - System of Indicators of Sustainable Development)

SMG	Special maintenance grant (Namibia)
SSC	Social Security Commission (Namibia)
SSF	Social Security Fund (Thailand)
SSPAM	Adult Health Insurance (Bolivia)
SSW	Social security and welfare (South Africa)
STPA	Short-term plan of action for orphans (Botswana)
SUMI	Universal Mother and Child Health Insurance (Bolivia)
SUS	Sistema Único de Saúde (Brazil - Unified Health System)
TPS	Total public spending
UBIG	Universal Basic Income Grant (South Africa)
UC	Universal Coverage Scheme (Thailand)
UDAPE	Social and Economic Policy Analysis Unit (Bolivia)
UN	United Nations
UNDP	United Nations Development Programme
UNFPA	United Nations Population Fund
UNGASS	United Nations General Assembly Special Session
UNICEF	United Nations Children's Fund
UNPD	United Nations Procurement Division
VAT	Value added tax
WB	World Bank
WCF	Workmen's Compensation Fund (Thailand)
WDI	World Development Indicators
WFP	World Food Programme
WHO	World Health Organization

Foreword

This paper focuses on the analysis of experience in creating fiscal space for the extension of social protection. This study was undertaken within the framework of the STEP/Portugal Project, whose purpose is to promote the extension of social protection.

The paper presents the results of studies conducted in eight developing countries that successfully extended social protection including floors for national social protection systems in recent years. The studies seek to identify the strategies that were adopted to finance the extension of social protection and how the necessary fiscal space was created.

The creation of fiscal space is a highly complex issue, which transcends purely economic issues. Decisions on the extension of social protection are made in specific national contexts set by idiosyncratic cultural, demographic, economic, social and political circumstances. The findings and lessons learned from this study must be considered within these specific frameworks.

Based on the country analyses, this paper shows that the selected countries were able to extend one or more components of their social protection systems by typically using a combination of diverse strategies to create fiscal space. Some strategies are common to several countries, while other strategies can only be applied in particular national contexts.

The paper demonstrates that developing countries are able to create fiscal space to extend social protection and that investment in human development generates high returns in terms of social and economic development.

We hope that the evidence presented in this paper can be useful for countries aiming to implement social protection floors and build-up comprehensive social security systems.

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1. Introduction

Financing is a centrepiece for the design of strategies for the implementation of universal social protection systems. Without adequate and sustainable financing, government interventions in this field will have difficulty in achieving their ultimate goals. For this reason, the pursuit of fiscal space to finance the extension of social security is an issue that lies at the heart of the concerns of policy makers in social protection.

The ultimate goal of the ILO's Global Campaign on Social Security and Coverage for All is the development of comprehensive, consistent and properly coordinated social security systems that can provide universal protection against social risks throughout an individual's life cycle. This was one of the key findings of the International Labour Conference in 2011, in the framework of the extension of social protection and national efforts to create social protections floors.

Because of their nature, decisions to ensure the sustainability of financially comprehensive social protection systems transcend the field of social protection. They call for nationwide strategies that include taxation within the framework of the economic system as a whole.

Throughout the years, the issue of fiscal space has been the subject of intense analysis and debate in various areas of public policy. In recent times, the agenda for the financing of human development, in particular the establishment of the Millennium Development Goals (MDGs), has sparked renewed interest in the problem of generating fiscal space to finance policies linked to the MDGs. The issue also extends to other fields of analysis related to the concept of "development" and the role of social protection, both as an instrument for fighting poverty and as an objective of the welfare society.

This report seeks to make a specific contribution in the field of creation of fiscal space for the extension of social protection, in order to provide an analytical view of the experience of countries in different parts of the world, so that other countries can understand better the processes involved.

There is a close link between the feasibility of extending social protection and the economic and political capacity of a country to generate sustainable resources that render the public funding of such initiatives viable in the long term.

Fiscal resources are limited and the process by which they are generated and distributed among the various public policy objectives, including social protection, is both technically and politically complicated. In the developing world, the challenge of financing social security is increasingly difficult, given the "natural" constraints imposed both by the limited capacity of the economy and by specific local factors related to social, historical and cultural characteristics.

From a fiscal standpoint, the challenge of creating fiscal space has two facets. On the one hand, a government's ability to generate new internal or external resources on a sustainable basis, by modifying either the source or level of funding, is necessarily limited. On the other hand, the State must use these resources in the most efficient way possible to achieve its welfare goals.

Beyond such fiscal issues, there is the fact that decisions on financing and spending usually respond to the specific interests of stakeholders that have sufficient power to influence them. No intervention on financing or public spending is neutral in terms of which groups in society are winners or losers. Thus, the creation of fiscal space, whatever its purpose, unfolds in a context dominated by the relationships between the power groups in society. This is relevant when considering measures relating to social investment, particularly those

directed towards social protection. The financing of social protection therefore entails a complex decision making process in which the political dimension carries a very significant weight.

Taking into account all these complex factors, the precarious situation of social security coverage, particularly in the developing world comes as no surprise. It is estimated that more than 80 per cent of the world's population does not have any social security protection at all. In sub-Saharan Africa and South Asia, it is estimated that only between 5 and 10 per cent of the workforce is protected by social security. Even in industrialized countries, the coverage of contributory social security schemes does not extend to the entire economically active population. This situation is also reflected in the existence of major national and regional disparities in the level of public investment in social protection. According to the *World Social Security Report 2010-11*, while European countries spend between 20 and 30 per cent of GDP on social security, investment in Africa ranges from 4 to 6 per cent (ILO, 2010a).

For the ILO, an institution inspired by the principles of social justice and by strategic objectives that explicitly address the development and extension of social protection, the issue of fiscal space is paramount; virtually all decisions relating to the extension of social protection also involve corresponding decisions relating to the generation of fiscal space.

This report addresses some of the practical experiences of developing countries that have engaged in a major process of extending social security. Inter alia, the report highlights the efforts of Brazil and Costa Rica to extend social insurance coverage in urban and rural areas. In the Brazilian case, the process was accompanied by measures to rebuild and increase efficiency in the allocation of expenditure among social programmes.

When the debate on the implementation of a social protection floor focuses on extending the coverage of non-contributory schemes financed by non-labour-based revenue, the main decisions focus on the availability and sustainability of existing resources (general taxation and earmarked taxes), the level of priority of social protection spending and the reorganization of existing programmes in order to optimize efficiency. This report therefore also addresses the interesting developments in this area of Bolivia, Botswana, Lesotho, Namibia, South Africa and Thailand.

This report does not attempt to quantify the fiscal space requirements of financing social protection. Instead, it analyses the practical experience of some developing countries that have had a degree of success in extending social protection. From an analysis of national experiences, it seeks to develop a set of lessons, conclusions and recommendations related to the creation of fiscal space, taking into account the major advances achieved and practical challenges encountered by these countries in creating fiscal space for extending social protection.

The experiences discussed here show that it is conceivable to build social protection floors in developing countries. In addition, such experiences have shown that there is no single recipe for creating fiscal space to finance social protection, and that each national context has singularities determined by its historical, political, economic and cultural characteristics. That said, the lessons learnt are very useful for identifying some common perspectives and strategies that could be adapted to other developing countries.

Following these introductory paragraphs, Section 2 summarizes the lessons learnt in preparing this report and presents a comparative overview of developments in the countries analysed, including their fiscal and economic circumstances, the main trends in social spending and social protection spending, and, finally, the lessons learnt from the strategies adopted by the different countries to finance the extension of social protection. The body of the report, from Section 3 to Section 10, is devoted to a presentation of the eight case

studies (Bolivia, Botswana, Brazil, Costa Rica, Lesotho, Namibia, South Africa and Thailand). Broadly speaking, the case studies observe the following structure: profile and background, description of the main elements of the social protection system, size and main characteristics of coverage, level of financing and expenditure, national strategies to achieve fiscal space for investment in social protection, the sustainability of these strategies and their likely impact on poverty and welfare.

2. Fiscal space and social protection: Summary of lessons learnt

This section summarizes the main facts and lessons derived from the analysis of eight countries (Bolivia, Botswana, Brazil, Costa Rica, Lesotho, Namibia, South Africa and Thailand). The summary contains some good news for policymakers in other countries who are interested in implementing something similar in their countries.

At this point, attention can be drawn to two conclusions. The first is that the creation of sustained fiscal space for social protection is feasible and there are multiple options for expanding this fiscal space. This is not a merely Utopian idea. As will be observed in the rest of this report, policymakers are not restricted to one or two options only; on the contrary, there is a considerable range of options to explore. The necessary tools are at hand, and even the poorest countries considered in this study achieved extraordinary results. On the other hand, their various experiences also show that there is no single recipe for raising the level of social protection financing. Although these countries have several points in common, the decisions adopted by governments depend on the social, political, economic and cultural environment of each nation. In other words, the best strategy has a strongly idiosyncratic component.

2.1. Information sources

Developing countries face difficulties in collecting uniform and statistically comparable information on social protection expenditure, largely because of the different definitions and criteria used for measuring the expenditure components. Given these difficulties, this study endeavours to collect, systematize and analyse the data on social protection in order to reduce the methodological problems associated with its definition and measurement. The information provided here is the exclusive responsibility of the authors.

In this report, the terminology “social security” and “social protection” are interchangeable. Accordingly, reference is made to “social protection” as having the following aspects: (1) interchangeable with “social security” or (2) as “protection” provided by social security in case of social risks and needs.

Following a broad definition of social protection, the statistical definition used throughout this report to measure social protection expenditure is based on the functional definition of the ILO (Scholz, Cichon and Hagemeyer, 2000), considering three categories: expenditure from contributory programmes (social insurance), spending on non-contributory programmes (for social assistance or universal programmes), and public spending on health. By function, social protection expenditure (cash benefits or benefits in-kind) includes health care, sickness, disability, survivors, employment injury, old-age, family and children, labour market programmes, housing, basic education (primary school, cash benefits, and benefits in-kind), and food and nutrition (food aid, food stamps, food subsidies). In developing countries, it is customary to classify benefits according to local needs and customs.

For example, the components of social protection expenditure in Brazil include spending on health and sanitation, which comprises primary care, hospital and out-patient care, prophylactic and therapeutic support, health surveillance, epidemiological surveillance, food and nutrition and other public health functions. Spending on social security covers the basic scheme (*Previdência Básica*), the mandatory pension scheme (*Previdência do Regime Estatutário*), the supplementary scheme (*Previdência Complementar*) and the special scheme (*Previdência Especial*). Spending on social assistance is in the form of cash benefits for the elderly, the disabled, children and adolescents (including the popular *Bolsa*

Família) and for the community. In the case of South Africa, social protection expenditure comprises health expenditure, which covers outpatient services, hospital services, research and development of health, public health services, outpatient care and other unspecified health expenditure, expenditure on contributory programmes, which includes social insurance and unemployment protection, and expenditure on social assistance to protect the elderly, veterans, the disabled, to promote care and attention for dependents and to provide child support, inter alia.

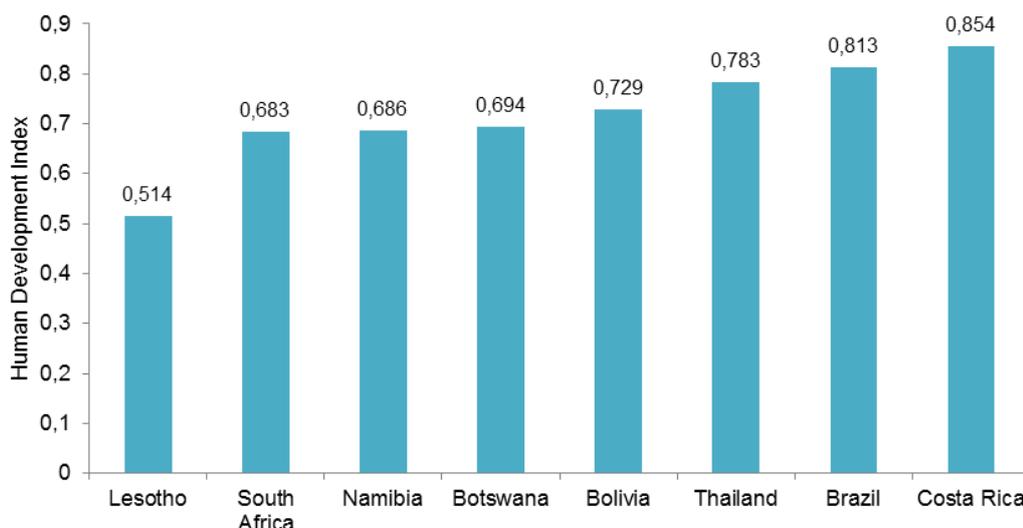
The information sources used in this report include both primary and secondary sources. In the particular case of information on social protection expenditure, primary sources were used. For example, the data from Bolivia, Brazil, Costa Rica, Lesotho, Namibia and Thailand were extracted from the annual statistics published by the finance ministries of each country. The information for South Africa comes from Statistics South Africa (Stats SA), a government agency. For information on Botswana, the main source is the annual reports presented by the Central Bank. Other information that does not refer to social protection, such as macroeconomic, fiscal and demographic statistics, was collected from the databases and publications of institutions in each country (finance ministries, central banks, social security institutions, statistical agencies and other public agencies), as well as from the online databases of international organizations such as the World Health Organization (WHO), International Labour Organization (ILO), United Nations Development Programme (UNDP), Economic Commission for Latin America and the Caribbean (ECLAC), World Bank (WB), International Monetary Fund (IMF), Organization for Economic Cooperation and Development (OECD), African Development Bank (AFDB) and Asian Development Bank (ADB).

2.2. Brief overview of the countries

The eight case studies are a sample of highly heterogeneous countries. There are three Latin American countries, one Asian and four African countries, with populations ranging from 2-5 million inhabitants (Namibia, Lesotho, Botswana and Costa Rica), to around 10 million (Bolivia) to over 50 million (South Africa, Thailand and Brazil).

The group of countries is also diverse in terms of socioeconomic conditions. Human development, measured by the Human Development Index, ranges from a low-ranked country like Lesotho to the high-ranking Costa Rica (see figure 1). Similarly, poverty rates move between low incidence rates in Thailand to high rates in Lesotho, while inequality as measured by the Gini coefficient includes nations among the highest rating in the world (Brazil, Botswana, Lesotho, Namibia and South Africa).

Figure 1. Human Development Index, countries analyzed in the study

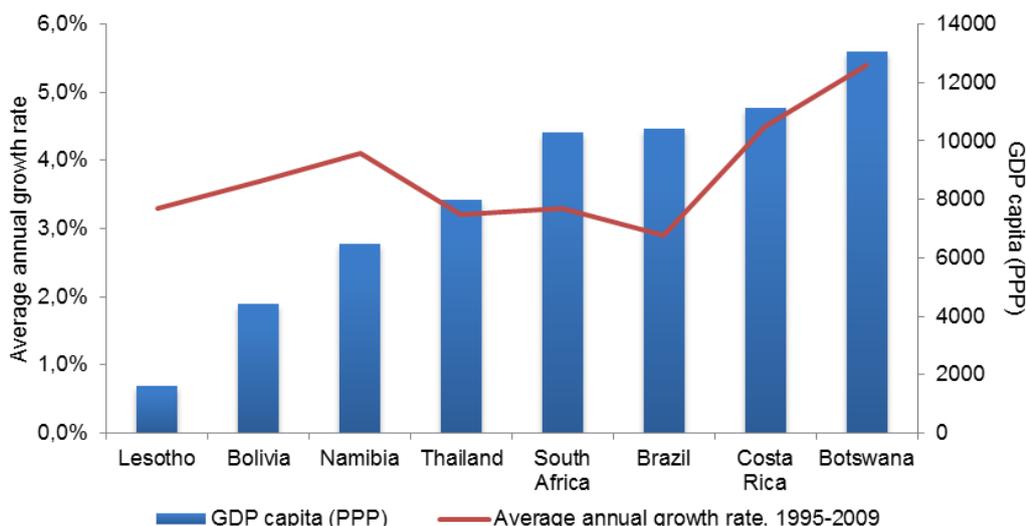


Source: UNDP 2009.

By size of the economy, Brazil ranks among the top 10 economies in the world and is the biggest economy in the group, followed by Thailand and South Africa (see figure 2). In terms of GDP per capita, the top four countries are Botswana, Brazil, Costa Rica and South Africa (all with a GDP per capita above US\$10,000 in PPP terms); at the bottom of the group we find poor economies like Lesotho (US\$1,613) and Bolivia (US\$4,426). Thus, the sample contains a group of economies at very different stages of economic development and institutional maturity and with very different political models.

With respect to GDP growth, one can identify three groups of countries. A first group, to which Botswana, Costa Rica and Namibia belong, presented an average annual growth rate above 4 per cent between 1995 and 2009. A second group comprises Bolivia, Lesotho, South Africa and Thailand, with average growth rates in the range of 3.0 to 3.9 per cent. Brazil lagged behind the other countries with an average GDP growth rate of 2.9 per cent, partially attributable to low rates during the 1990s crisis.

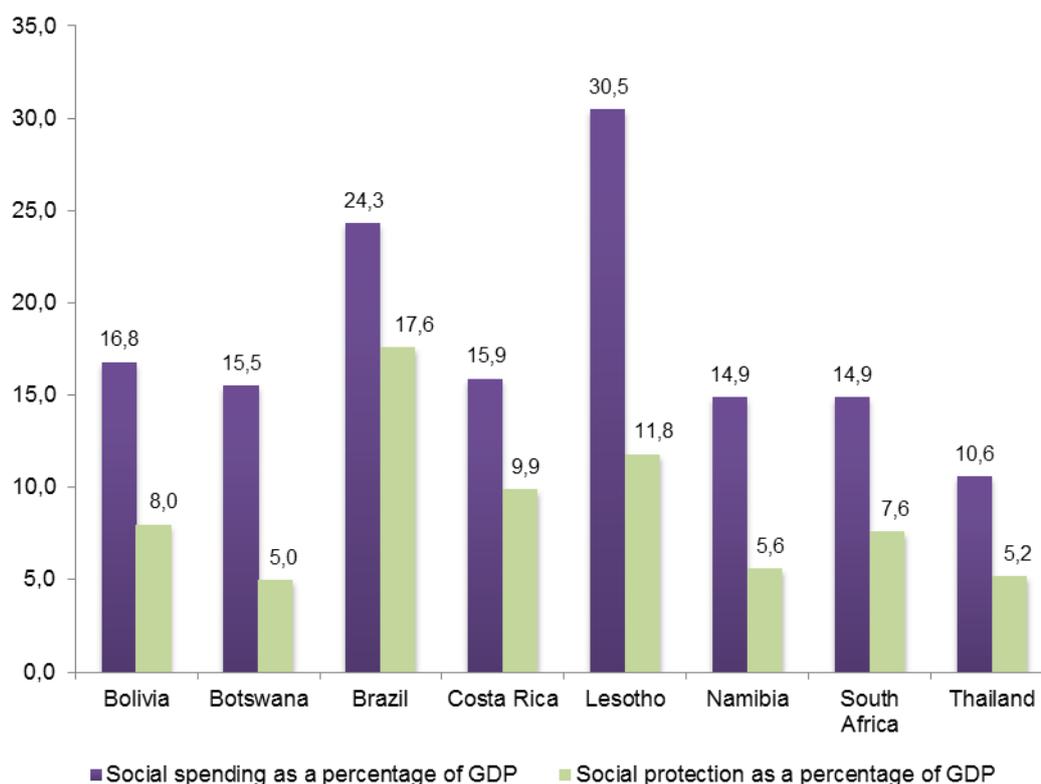
Figure 2. GDP per capita 2009 and GDP growth by country (1995-2009, PPP terms)



Source: World Bank 2010.

Between 2005 and 2008, social spending averaged 21.3 per cent of GDP¹ while social protection (including health expenditures) averaged 14.6 per cent. Overall, two in every three dollars spent in the social sector were allocated to social protection initiatives, a clear indication of the political will to support social protection initiatives. In comparison to regional levels, three countries (Brazil, Costa Rica and Lesotho) show coefficients above the regional figure (see figure 3). According to the ILO's *World Social Security Report 2010-2011*, social security expenditures (including health) accounted for 9.7 per cent of GDP in Latin America, 8.7 per cent in sub-Saharan Africa and 12 per cent in Asia and the Pacific (ILO, 2010a, Table 8.1).

Figure 3. Social spending and social protection as a percentage of GDP (2005-2008)

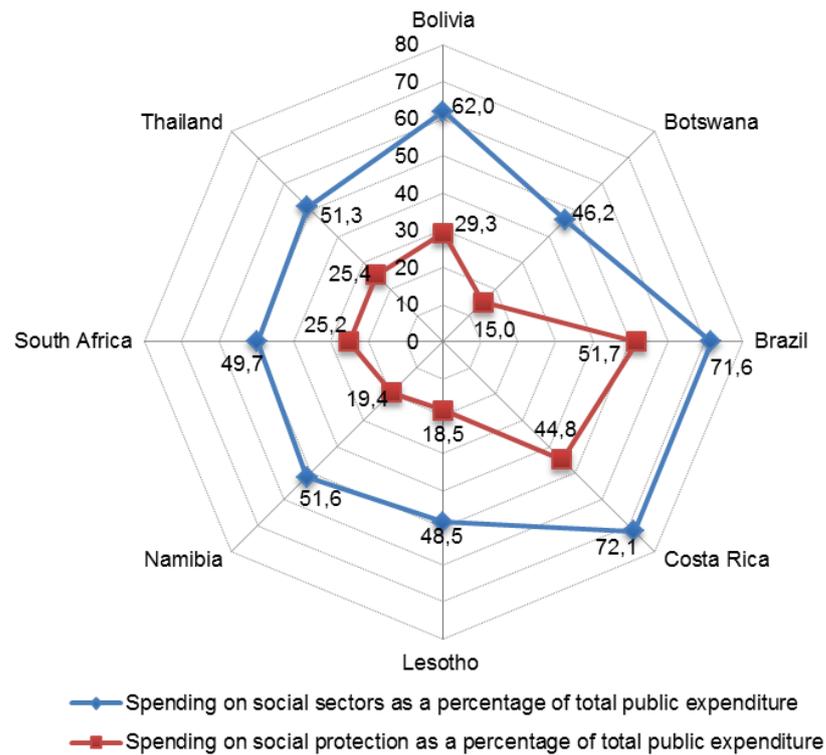


Source: Individual country data based on ministries of finance, housing, education of each country, central bank (Botswana), national statistical offices, ECLAC (2010a), IMF (2010b), World Bank (2010) and WHO 2010b.

As a share of total public expenditure, social spending accounted for an average of 56.6 per cent of GDP. Costa Rica ranks at the top of the list of countries with roughly 72.1 per cent of public spending going to social expenditure (see figure 4). Botswana's share of expenditure on the social sector (46.2 per cent) ranks at the bottom of the list. About half of social expenditure went to social protection initiatives, with great variations between Brazil (51,7 per cent) and Botswana (15 per cent).

¹ Weighted average by size of the economy. Simple average for this indicator was 17.9 per cent.

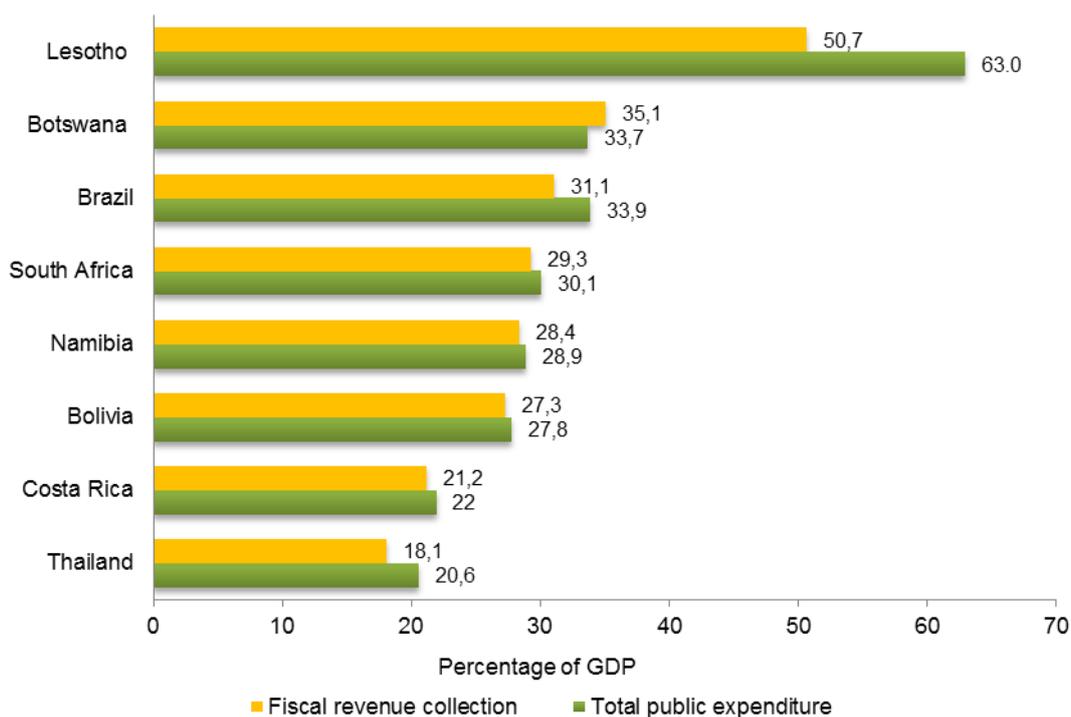
Figure 4. Social spending and social protection expenditures as a percentage of total government expenditure (2005-2008)



Source: Individual country data based on ministries of finance, housing, education of each country, central bank (Botswana), national statistical offices, ECLAC (2010a), IMF (2010b), World Bank (2010) and WHO 2010b.

Countries also differ in terms of the size of their governments. Smaller governments, in terms of their participation in the economy as expressed by fiscal revenue collection and total expenditures as percentage of GDP, correspond to Thailand and Costa Rica with public expenditures representing less than 25 per cent of GDP (social contributions included). Lesotho represents the biggest government of the group accounting for 50.7 per cent of GDP (revenues) and 63 per cent for expenditures. The rest of the countries present public spending levels ranging between 27 and 35 per cent of GDP (see figure 5).

Figure 5. Public spending and fiscal revenue, 2005-2008 (percentage of GDP)



Source: Individual country data based on ministries of finance, housing, education of each country, central bank (Botswana), national statistical offices, ECLAC 2010a, IMF 2010b, World Bank 2010.

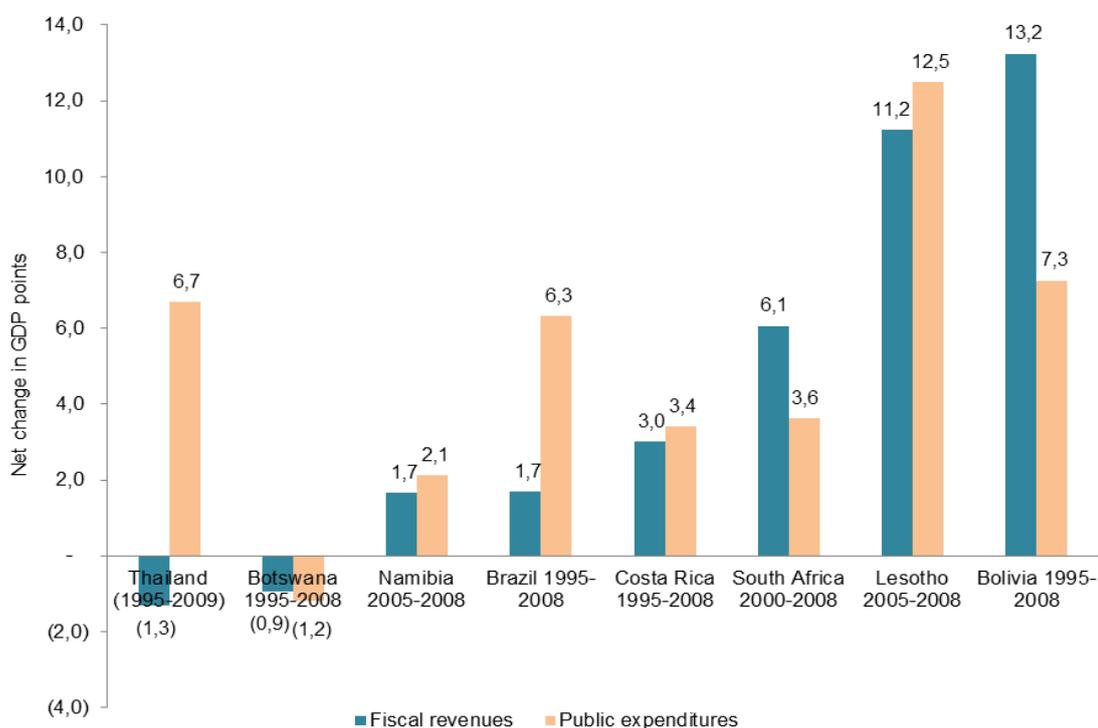
2.3. General economic and fiscal conditions and their relation to fiscal space for social protection

The sample of eight countries selected for this study shows that the creation of fiscal space for social protection purposes requires a combination of economic growth, macroeconomic priority, political support and other complementary strategies.

The relationship between social investment and economic growth is of paramount importance, as the literature on the subject has established that growth is critical for increasing social budgets. When assessing the annual growth rates of GDP and social spending in the countries studied, the evidence shows that the average GDP growth rate (3.0 per cent) closely paralleled the annual increments in social spending (2.9 per cent). Social protection tended to grow at the faster pace of 3.4 per cent per year, an indication that this category gained considerable support that increased its overall participation over time.

The financial position of the public sector is another critical factor in the degree of freedom to create fiscal space. The size of the governments of the sample (as expressed by fiscal revenue collection and total expenditure as a percentage of GDP) ranged from 25 per cent to 63 per cent of GDP, and during the period 2005-08 all the countries except Botswana experienced a fiscal deficit of between 1 per cent and 12.3 per cent of GDP. As presented in figure 6, during the period analyzed all the countries (except Botswana) increased the participation of the public sector in the economy, sometimes by more than 10 percentage points of GDP. This is good news for low- and middle-income countries because it shows that increasing taxation in order to expand government expenditure on the social sector is feasible even under the constraints that these economies usually face.

Figure 6. Net changes in fiscal revenue and public expenditure in percentage points of GDP.



Source: Individual country data based on ministries of finance, housing, education of each country, central bank (Botswana), national statistical offices, ECLAC 2010a, IMF 2010b, World Bank 2010.

The establishment of complementary strategies to create fiscal space for social protection is also one of the features that characterized this group of countries. The report explored two main strategies. Under the first strategy, the reduction of the total debt and then debt service (especially public debt ratios) were one of the main channels utilized to create fiscal space by allowing the Government to free resources for social protection purposes. All the countries in the study achieved substantial reductions in this way. Looking at the decline in the ratio of total debt service as a percentage of total exports, Botswana, Bolivia, Lesotho and South Africa experienced a reduction in their debt servicing coefficients of over 54 per cent from their 1995 levels. More modest but still significant cuts in debt servicing were observed in Brazil, Costa Rica and Thailand.

A complementary strategy commonly used by countries in the creation of fiscal space is the use of official development assistance (ODA) flows to strengthen social protection initiatives. In general, the use of ODA in the countries which form part of this report brought mixed results, but the dependence on external funding declined in all the countries (see table 1). Overall, Bolivia and Lesotho, and to a lesser degree Namibia, received the most development assistance, while in Brazil, Costa Rica, South Africa and Thailand ODA flows were very low and practically none was used to finance social spending. The scarce evidence on the use of the ODA funds reflects that, even where they constituted a large share of the GNI, the amount of money allocated to social protection was limited.

Table 1. Decline in debt servicing and ODA flows by country, 2005-2008

Country	Net decline in debt servicing (%)	ODA flows as a percentage of GNI
Costa Rica	24.4	0.1
Thailand	33.8	0.2
Brazil	37.8	0.0
South Africa	54.4	0.3
Lesotho	58.8	6.2
Bolivia	61.6	8.7
Botswana	82.2	1.4
Namibia	NA	3.6

Source: World Bank, 2010.

Macroeconomic priority and fiscal priority (i.e. political commitment) to increase social protection spending is better approached by considering the share of government expenditure assigned to the relevant programmes. In general, social spending accounted for an average of 40.9 per cent of total public spending compared to social protection's 26.4 per cent.² These figures alone reflect the strong commitment of the governments to finance social protection programmes. However, macroeconomic and fiscal priority has to be assessed over time in order to determine whether this high level of investment is the result of a cumulative process or, on the contrary, reflects a decreasing participation in public budgets.

Table 2 shows that all the countries analyzed increased their rate of social spending and of social protection spending as a percentage of GDP compared with the initial year of analysis. Only in the case of Lesotho did spending on the social sector remain the same. In general, social protection expenditure benefitted more from the increments in total social spending. For those countries with available data for 2005-08, total social spending grew on average by a multiple of 1.15 and social protection by a multiple of 1.5. Thailand led the increments in social protection spending thanks to its aggressive universal healthcare programme that provides health services to over 50 per cent of the population and has helped the country to cover more than 94 per cent of the population.

Table 2. Increments in social spending and social protection spending (as a multiple of the initial year)

Country	Social spending	Social protection spending
Lesotho 2005-2008	1.2	1.8
Namibia 2005-2008	1.1	1.2
Botswana 1995-2008	1.1	1.5
South Africa 2000-2008	1.2	1.3
Brazil 1995-2008	1.3	1.2
Thailand 2005-2008	1.4	1.6
Bolivia 1995-2007	1.4	1.7
Costa Rica 1995-2009	1.5	1.4

Source: Individual country data based on ministries of finance, housing, education of each country, central bank (Botswana), national statistical offices, ECLAC (2010a), IMF (2010b), World Bank (2010) and WHO (2010b).

² Weighted average by size of the economy. Simple average of spending on social sectors as a percentage of total public expenditure was 56.6 per cent, while simple average of spending on social protection as a percentage of total public expenditure was 28.7.

Finally, political commitment was approached in terms of how much any expansion in fiscal expenditures was used to cover social or social protection programmes. Excluding Botswana and Costa Rica, about 55 per cent of the total increments in public spending was spent on financing social spending and 85 per cent of that additional social spending was allocated to social protection initiatives. These results are a clear indication of the increasingly important participation of social spending and social protection spending in the agenda of the governments included in the study.

2.4. Trends and lessons learnt

2.4.1. Main characteristics of social protection programmes

Before addressing the strategies for creating fiscal space, a brief mention should be made of the type of programmes that have benefited most from the creation of fiscal space in the countries studied. The matrix in table 3 shows that education, health and social benefit programmes received priority in every single country. In this context, priority means either that the programmes account for a high proportion of GDP or that they have expanded considerably in the last decades. In most cases, education is the single most important social subsector, with budgets exceeding 5 per cent of GDP. Even in Lesotho, which reduced the share of education spending in GDP, the current level of expenditure is still over 10 per cent of GDP.

Table 3. Matrix of programmes (by country)

Type of programme	Bolivia	Botswana	Brazil	Costa Rica	Lesotho	Namibia	South Africa	Thailand
Health and nutrition	X	X	X	X	X	X	X	X
Education	X	X	X	X	X	X	X	X
Old age pension	X	X	X	X	X	X	X	X
Other social security benefits (maternity, disability, survivors, etc.)	X	X	X	X	X	X	X	X
Conditional cash transfers	X		X	X				
Unconditional cash transfers		X			X	X	X	X
Housing	X			X		X	X	

Social security benefits (including disability benefits, survivors and employment injury, sickness and maternity allowance and family allowances, but not health insurance and old-age pensions) also appear in all countries as part of the portfolio of social protection entitlements. However, one should be cautious about these components, because the scope of the benefits offered differ substantially from one country to another. For instance, South Africa and Bolivia offered a full range of benefits while Lesotho concentrates on disability benefits and other pensions.

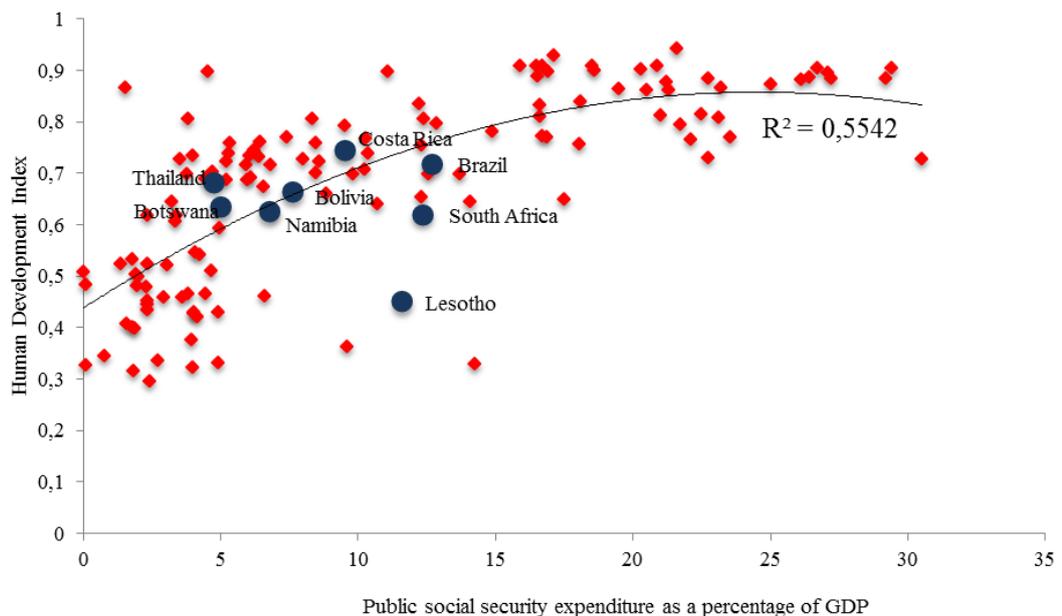
The four African countries in the study (Botswana, Lesotho, Namibia and South Africa) consolidated their old-age pension initiatives in the last two decades, and in Botswana, Lesotho and Namibia coverage exceeds 90 per cent of the population. The case of Lesotho is particularly attractive, given that it is the only least developed country (LDC) in Africa with a non-contributory pension scheme and. And with Nepal they are the only two LDCs in the world in that situation (Pelham, 2007). Lesotho is a clear example that poorer nations are perfectly able to protect their citizens if the political commitment exists. In general, old-age pensions usually do not account for more than 1 per cent of GDP, but they have a significant effect on a country's level of poverty.

Poverty reduction programmes also appear on the list of initiatives that experienced a considerable increment in their budget as a result of expanded fiscal space. There is, however, a marked trend in the approaches adopted in the different regions. In Latin America conditional cash transfers prevailed as the preferred option, while in Africa the popular alternative was unconditional transfers, particularly cash transfers to highly vulnerable groups such as children, the elderly, orphans and people living with HIV.

Although housing expenditure also appears in practically all the cases, the overall trend is to reduce the share of housing programmes in social spending. In some cases, including Botswana and Lesotho, housing programmes accounted for over 3 per cent of GDP but they have now declined, in some cases by 50 per cent of their initial share. In short, housing initiatives exist but they play a less important part in social strategies as a whole.

A straightforward conclusion can be drawn from the above which is important to highlight, namely that investing efficiently in social programmes definitely pays off. Figure 7 presents the relationship between social security expenditure (as a percentage of GDP) and the HDI. The evidence shows that there is a positive correlation between the two variables, and that increasing expenditure on social security yields important gains in the overall circumstances of the population as measured by the HDI.

Figure 7. Relationship between social security expenditure and HDI (latest available year)



Source: UNDP 2011; ILO 2010a.

2.4.2. Mechanisms for creating fiscal space: Practical evidence

The group of countries analysed is rich in the evidence it provides regarding the creation of fiscal space for social protection and regarding the implementation of successful social programmes that have had a marked impact on the living standards of the population. The analysis that follows provides a wide range of illustrations of how countries dealt in practice with fiscal space for extending their social programmes. Attention should be drawn to South Africa's and Lesotho's significant success with their old-age pensions, to Costa Rica's strong contributory social security programme and to Brazil's successful conditional cash transfer initiative, *Bolsa Família*. All four countries basically decided to do something different and to prioritize the social sector over other areas. As a result, all the countries in the study have pursued ingenious policy alternatives to expand fiscal space for social purposes – from specific taxes on financial transactions in Brazil, to strategic

negotiations with multinational companies in Botswana and from risky political moves such as the abolishment of the army in Costa Rica to the reduction of other social spending programmes to increase social protection outlays.

Several features are apparent in table 4. First, not one of the single strategies adopted sought to increase fiscal space for social protection alone. The mix of strategies is clear, as is the fact that countries do not base their social protection financing on just one source of funds. Diversification is the key for sustainability, and such is the strategy that was followed by most of the countries covered in this report.

Table 4. Matrix of fiscal space strategies (by country)

Strategy	Bolivia	Botswana	Brazil	Costa Rica	Lesotho	Namibia	South Africa	Thailand
Mineral-based taxation or similar taxes for specific purposes (earmarked taxation)	X	X	X					
Increasing general taxation			X		X			X
Increasing Social contributions			X	X	X	X	X	X
Budget surpluses		X	X			X		
Budget redefinition. Reduction of non-priority spending or decline of military expenditure				X	X		X	X
Reduction in national debt and in debt servicing	X	X	X	X	X		X	X
Official Development Assistance						X		
Sale of state assets	X							
Gains of efficiency			X					
Amendment of the Constitution			X	X			X	X

Earmarked taxation based on natural resources. In countries that have the advantage of possessing natural resources, as do Bolivia and Botswana, taxes on their exploitation is a viable alternative, especially when countries renegotiate the terms on which operations have been performed in the past. The developing world is full of countries with immense natural resources but carry a heavy burden of poverty from generation to generation.

Increasing general taxation. Three of the countries studied, Brazil, Lesotho and Thailand, achieved impressive increases in general taxation, which shows that this is also a feasible path. It is noteworthy that such policies are implemented over a relatively long term and must be accompanied by other relevant policies within a framework of macroeconomic and fiscal discipline.

Social contributions. As a way of creating fiscal space, generating funding through social contributions is by its nature associated with the extension of contributory social security. Most of the countries studied – Brazil, Costa Rica, Lesotho, Namibia, South Africa and Thailand – increased financing significantly via social contributions. Brazil, for example, which greatly expanded its social security coverage in both urban and rural areas, established a special tax on financial transactions to finance the universal health care system. As in Brazil, Costa Rica's social contributions account for the highest share of the funds used to finance its social protection programmes. In both countries, social contributions are closely associated with the introduction of innovations to encourage the formalization of the labour market and to expand the coverage of contributory social security. This kind of innovation explains in large part the progress made in generating fiscal space.

Budgetary reallocation. When a significant expansion of current revenue was not possible, some countries opted for a reorientation of their public budget structure. In several cases,

such as Costa Rica, Lesotho, South Africa and Thailand, the governments reduced spending in certain areas that they did not consider a priority or where funding could be reduced. Lesotho, for instance, opted to reduce the participation of expenditure on education in total government spending. In Costa Rica and Thailand, military spending fell or (in Costa Rica) was completely eliminated many years ago.

Africa accounted for 1.1 per cent of the world's military spending, but in sub-Saharan Africa, according to data published by the Stockholm International Peace Research Institute (2010), this amounted to 1.9 per cent of GDP (US\$17.4 billion). Just in the group of countries analyzed, military expenditure ranged from 1.3 to 3.5 per cent of GDP.

Reduction of debt service. Another interesting feature is the active role that the reduction in total debt and debt service played in expanding the fiscal space for extending social protection. All the countries experienced a major reduction in their debt burdens, especially public debt, and in the corresponding debt service payments. As a result, more resources were allocated to the social sector, as in Thailand where almost a third of the resources thus freed went to social programmes.

Official development assistance (ODA). ODA was not a significant source of funds for social initiatives in the countries analyzed. In every case, whether the level of ODA declined or increased, it still accounted for only a small proportion of GNI. Moreover, of the total external assistance received only a fraction was allocated to social protection. As a result, ODA did not play a critical role, which shows that an endogenous strategy of social protection financing is possible even in developing countries.

Constitutional channel. This refers to the practice observed in many cases of defining social spending either fully or partially in the Constitution, thereby obliging governments to consider certain programmes as priority initiatives for the nation and therefore to expand their budgets. Explicit reference is made to education, health and social security financing in the Constitutions of Brazil, Costa Rica, South Africa and Thailand. In the case of Costa Rica, expenditure on education cannot be lower than 6 per cent of GDP, and in Brazil, South Africa and Thailand the Constitution includes health and social security in the rights of the citizen. It is thus possible to ensure a minimum level of social spending by tying future political decisions to a predetermined framework.

Gains in efficiency. One way of releasing resources, which can then be channelled to social security, is to reduce costs by improving the effectiveness of the money spent. The experience of Brazil, where both the structure of cash transfer programmes and the criteria and mechanisms of resource allocation were revised in order to improve targeting, shows that it is feasible to save costs by restructuring social transfers.

Finally, there are a number of other strategies that illustrate the wide range of possible ways of expanding fiscal space. They include prudent macroeconomic management, which yields fiscal surpluses that permit the subsequent expansion of social financing (Botswana, Brazil and Namibia) and the sale of state assets (Bolivia). Corruption, too, is a common cause of leakage of social protection resources. According to the Transparency International's Corruption Perceptions Index (Transparency International, 2010), about 75 per cent of the countries considered in this report have an index below 5, where 10 corresponds to low corruption, with African and South Asian countries at the bottom of the list. In sub-Saharan Africa, the African Union estimated aggregate losses due to corrupt practices at US\$148 billion in 2002, equal to 50 per cent of total fiscal revenue. At the household level, this figure constitutes an average of 3.2 per cent of the family income.

2.4.3. Fourteen lessons learnt

Lesson 1

Macroeconomic stability and fiscal discipline are essential to expand the fiscal space. The experiences of Botswana, Brazil, Lesotho and Thailand show that all that can be done to maintain macroeconomic stability by applying principles of fiscal prudence, will eventually bring benefits in terms of creating fiscal space and its sustainability. In Botswana, the new resources generated by the diamond mining agreements were used prudently by the Government, so as not to jeopardize the fiscal situation. Brazil was able to combine macroeconomic stability with social inclusion policies based on high levels of social investment, which helped boost demand for domestic consumption; an important part of its success rested on monetary policy and fiscal responsibility. In Botswana and Lesotho, despite the rapid growth in tax collection, governments didn't embark on a similar expansion of public spending, so the resulting cumulative surplus made it possible not to sacrifice the budget for social protection to any great extent during the recent economic crisis. Thanks to prudent fiscal policy and notable social spending priorities, Thailand, despite a modest performance in terms of tax collection, was able to reallocate resources to strengthen its universal health strategy. This experience also shows that creating fiscal space for a particular purpose can be achieved by reallocating resources from less efficient to more efficient sectors or categories of expenditure.

Lesson 2

Economic growth is important, but it is not always the main determinant in creating fiscal space for the extension of social protection. The analysis of fiscal space creation does not bear out the belief that it is dependent on exceptional economic growth. Brazil and Costa Rica, which are very different in both size and economic characteristics, are proof that the right combination of economic growth (even if moderate) and inclusive policies aimed at generating funds give good results. Costa Rica took advantage of a sustained policy to strengthen the social sector institutions in the 1960s and 1970s; especially social insurance and non-contributory cash transfers programmes. South Africa shows that social protection spending can be substantially increased even if the country's economic performance is moderate. Likewise, Thailand's poverty reduction policies allowed the Government to lower the level of financing of its social assistance programmes.

Namibia is an excellent illustration of the mechanisms available to countries with moderate macroeconomic and fiscal performance. None of the macroeconomic factors usually associated with the creation of fiscal space were in any way outstanding. Production grew at a moderate rate and was not transformed into a higher level of fiscal revenue, as had been expected. From a macroeconomic standpoint, average economic growth was far below the dynamic rates of countries such as Botswana and Mozambique, where average GDP growth exceeded 8 per cent per year. In addition, the Government decreased its participation in the economy and by 2008 the level of taxation and expenditure was considerably lower than in 1991, just after Independence. Nonetheless, the Government was able to generate a fiscal surplus in the second half of the 2000s, an indication of the highly prudent fiscal policy.

Lesson 3

Political will is crucial. From the evidence culled from the countries analysed in this report, it is clear that political commitment is the key to extending social protection. A country may experience high economic growth and generate a fiscal surplus, but if social protection is not a fiscal priority, that extension will not happen automatically. The existence of active policies for extending social protection is crucial. This is particularly

true in contexts such as that of South Africa where the Government operates under very restrictive fiscal conditions, usually accompanied by a fiscal deficit. If public funds grow just at a moderate rate and external aid is limited, then the critical decision involves modifying the composition of public spending by increasing the budget of priority sectors as against that of other sectors. In Lesotho, the Prime Minister and the key political parties demonstrated a strong political commitment to approve and proceed with the allocation of more funds to existing programmes, to open up additional fiscal space by implementing new social programmes and to reform existing mechanisms that were not financially sustainable in the long term.

However, there is always some degree of competition for any new fiscal space when it comes to investing in development. In a world characterized by scarcity of resources and by opportunity costs, social protection is just one among many possible uses of fiscal resources. This is particularly true when the new fiscal space is created by increasing taxation. Then, once fiscal space has been generated, the process of "allocating" the new fiscal space among alternative uses responds to complex social criteria in which many forces play a part. Factors that play an important role in such decisions include a country's idiosyncrasy, its culture, its political situation, its history, the interests of power groups and the distribution of political and economic power among them, to name just a few.

Lesson 4

Fiscal space for extending social protection is a highly political matter. Decisions such as reducing (in Thailand) or eliminating (in Costa Rica) the army, or renegotiating the revenue from the exploitation of hydrocarbons (in Bolivia) explain certain major changes in the financing of social protection. In Bolivia, the decision involved a series of highly complex, and sometimes antagonistic, political processes involving the various stakeholders. The outcome, however, was the creation of a truly universal social pension system in a country with one of the highest levels of poverty in South America. In Brazil, heated political battles were fought for years over the advantages or disadvantages of creating a tax on financial transactions, which eventually played a key role in financing and consolidating the universal health system until social contributions based on financial transactions were finally abolished and replaced by other sources of income.

Lesson 5

Social contributions are an effective tool for generating fiscal space. This conclusion is crucial in terms of the economics of social protection financing. Fiscal space for social security is quite specific because, unlike other areas of investment for development, social insurance (usually based on payroll contributions) has been a source of financing from the very inception of social security systems. Depending on the particular social security model adopted, social contributions can play an important role in explaining the size of fiscal space generated by the country as a whole. In many countries, especially in the industrialized world, it is difficult to imagine a social security scheme without its specific sources of financing based on social contributions. Several of the developing countries studied also provide positive evidence of the feasibility of generating a significant proportion of fiscal space through social contributions. Apart from Brazil and Costa Rica there are nations in Latin America (Argentina, Chile, Colombia, Panama, Uruguay) where it would be unthinkable today to envisage a sustainable system of social protection without the resources generated from social contributions.

Lesson 6

Labour formalization policies are a means of creating fiscal space through the extension of coverage. In the absence of a change in real wages or personal income, an increase of social contributions can, by definition, only come from reductions of

informality. The interventions to extend social security to independent workers and to extend effective coverage to micro and small enterprises would generate fiscal space regardless of general taxation policies.

Innovations in the creation of fiscal space by increasing coverage or the collection of social contributions can bring very significant returns. In Brazil there have been innovations both in fiscal instruments and in social policy. From the standpoint of the country's social protection system, some of the most important innovations include the introduction of the rural “semi-contributory” pension scheme, the use of taxes on financial transactions to generate resources from the formal economy, improvements in the administrative and institutional framework of the social contribution collection system, and measures to facilitate and increase the tax coverage and social security of micro and small enterprises.

Case studies of Brazil and Costa Rica provide evidence contrary to the neoclassical argument that increased levels of social contributions may cause greater informality. Costa Rica has one of the highest rates of nominal and effective social contributions in all Latin America, yet, along with Chile and Uruguay, it has one of the lowest rates of informality. The country also appears among the top countries in terms of competitiveness, well above regional averages. As in the case of Brazil, social contributions do not therefore seem to be associated with labour market informality. If social inclusion policies are able to improve the quality and employability of the labour force, and if such interventions provide more opportunities for the development of an extended business base, the expected outcome should be a reduction in the level of informality.

Lesson 7

Renegotiating the terms of distribution of wealth generated by the exploitation of natural resources is a feasible option. In the developing world there are many experiences of countries whose natural resources have been exploited for a long time, with few benefits in terms of the distribution of gains among the population. Yet the example of Bolivia and Botswana addressed in this report are proof that this can change and that the results in terms of creation of fiscal space can be impressive.

Bolivia is an example of the political and economic feasibility of negotiating more equitable terms for the distribution of profits from the exploitation of natural resources. In Bolivia the renegotiation was radical, and because of its positive impacts on the creation of fiscal space it constitutes a strategic step in the direction of sustainable development and economic growth. In Botswana, the diamond agreement with De Beers was essential for the expansion and consolidation of fiscal revenues. It proves that win-win strategies can be implemented in that kind of context and that agreements can be renegotiated under advantageous terms. This is also a good example for mineral-driven economies that opt for joint ventures between the Government and the private sector to exploit this type of resource.

Lesson 8

The efficiency of social expenditure management *does* matter. It is possible to create fiscal space by reviewing programmes and institutional and administrative mechanisms. Reforms in the organization of social transfer programmes, in terms both of its structure and the tools and criteria used for allocating resources, so as to introduce a degree of selectivity and progressive incentives – such as the renovation of educational programmes and the *Bolsa Família* – can be effective as a mechanism for creating fiscal space. As in Thailand, governments should adopt a pragmatic and strategic approach to policymaking. Thailand's experience is thus proof that improvements in the allocation of resources and in the appropriateness of expenditure can make a valuable contribution to efficiency.

Money is important but, again, money alone is not enough. For more than a decade, from 1994 to 2006, poverty rates in Costa Rica remained stable at around 20 per cent of the population, despite the fact that an extensive institutional framework was already in place. That said there remain problems with targeting and with programme design, which reduce efficiency.

Lesson 9

The design of the social protection system does matter. In connection with the concept of the social protection floor promoted by the ILO, a central idea is the need to design comprehensive social protection systems that combine different types of instruments in a coordinated manner. Countries should be very careful about the initiatives they create. A long list of social programmes may generate problems of coordination between these. Moreover, the contribution of some programmes to the fight against poverty may be quite small. Costa Rica's experience raises two potential problems. Firstly, it is usually very difficult to cancel or reverse programmes that are under way, and so policymakers may tend to keep them even though they do not bring the desired results. Secondly, if there are too many programmes, the demand for additional financing may set them in competition with other priorities.

Lesson 10

Social investment pays and contributes to economic development. Studies on the impact of increased social investments in Bolivia confirm the advantages of such a strategy on economic growth. Bolivia provides evidence against the argument that investment in social protection competes against private investment. Expenditure on social protection is injected into the economy and becomes part of a circular flow of income. These injections are useful to support growth in spending in the short term and contribute to macroeconomic stabilization in times of crisis.

Viewed in the long term, the social security system has acted as a direct contributor to the country's competitiveness by enhancing the health status of the population, and as an indirect contributor by reducing inequality and promoting social peace – two elements that investors are inclined to give weight to when deciding where to locate their companies. In addition to the experience of Bolivia, there is evidence from Brazil, Costa Rica and Thailand which supports the idea that investment in social protection has a positive effect on the generation of income, growth and fiscal revenue in the long term.

Lesson 11

There are advantages in combining contributory programmes with non-contributory programmes. The evidence from Thailand suggests two things about universal health coverage. First, it reaffirms the idea that general taxation plays a critical role in the achievement of this objective in countries where informal labour markets prevail. Second, universal coverage in Thailand was not the product of just one source of financing (general taxation), but was made possible by using a hybrid model that combined the mechanisms of both contributory and non-contributory schemes.

Lesson 12

Non-contributory social protection benefits are a viable option in the pursuit of universal coverage in countries with a large informal economy. The example of social pensions in Bolivia and South Africa show that, while the possibility of extending traditional social insurance may be limited (mainly because of the predominance of the informal economy over the formal economy), a non-contributory benefit scheme is a viable option for guaranteeing universal rights in accordance with the approach to the social protection floor promoted by the ILO. Once we have created the universal programmes

that constitute the social protection floor, contributory programmes can be developed gradually (i.e. the "vertical" development of the system) as conditions in the labour market improve.

Lesson 13

Tripartite social dialogue and good governance are important to protect social contributions. Tripartite representation and the participation of other stakeholders in the governance of social protection systems have functioned as a powerful political shield to protect social contributions. The experiences of Brazil and Costa Rica are very rich in this regard. In Costa Rica, during the 1980s and 1990s, when the neoliberal structural adjustment and stabilization packages reduced central Government spending on health to a historical low, the revenue of the social security system actually increased and helped to keep expenditure on health at the same level. Civil society should be seen as a partner in the creation of fiscal space. Its involvement does not imply that it should present a finished product to its audience, but that it should co-design the main features of the project jointly with its social partners. In Thailand, a combination of three key elements encouraged the process: bringing together of all the necessary know-how by means of research; social participation; and political commitment.

Lesson 14

A sustained effort and patience are indispensable. Developing a comprehensive social protection system with all its contributory and non-contributory components, calls for a persistent effort in terms of investment and of political commitment to the extension of social security. No country can expect extraordinary results from social investment in the short term. To achieve those results, what is required is the establishment of permanent institutions and great patience.

3. Bolivia: Financing the extension of social protection through taxes on hydrocarbons

3.1. Country profile

Bolivia is a country of 10 million inhabitants located in the Andean region of South America. It has a territory of 1.1 million square kilometres, administratively organized in nine departments and 334 municipalities.

The country is one of the world's low-income economies, with a per capita gross national product (PPP 2008) of US\$4,278, which in global terms puts it in 104th position. In 2008 its global position was 113th in the Human Development Index (HDI) of the United Nations, with 65 per cent of the population living below the poverty line, an infant mortality rate of 43 per thousand and a life expectancy of 66 years.

The main economic activity of the Bolivian people is agriculture, although the most important source of revenue for the country is the exploitation of natural resources, mainly hydrocarbons in the form of natural gas.

This set of features makes Bolivia one of the Latin American countries with the lowest level of economic and social progress. The country's history has been marked by a considerable degree of political and economic instability, with very frequent alternations of power.

According to a recent IMF analysis, Bolivia's economy has in recent years done very well. The country has benefited from a substantial improvement in its terms of trade (particularly in the mining and gas sectors), and this has consolidated its stock of international reserves and its large fiscal surplus. Even during the recent economic crisis, the country's position among the developing nations improved in terms of its macroeconomic performance. In 2009 the economy grew at 3.25 per cent, inflation fell and the fiscal surplus was around 4 per cent of GDP. According to the IMF, the Government's fiscal policy for 2010 seems consistent with a set of reforms that in the medium term could help to reduce the high dependence on revenues from hydrocarbon production. The IMF also indicates that there is no significant evidence of any exchange rate misalignment and that, in the financial sector, recent regulations aimed at strengthening liquidity and managing the country's credit risk seem properly focused. Improving the investment climate is a high priority and includes the recent approval of constitutional mandates, which according to the IMF seem consistent with the pursuit of a clear and stable framework for private investment (IMF, 2010a).

According to official data, Bolivia's per capita GDP, measured in real terms, has undergone a significant expansion in recent years, from an average of about US\$2,500 in the early 1990s to US\$3,059 in 2009, an increase of approximately 20 per cent in 10 years. These figures are consistent with official data regarding recent performance of other indicators such as average household consumption, rate of consumption of electricity, water and gas, and public deposits in the banking system.

In recent years, the major developments in respect of social protection in Bolivia have been the expansion of certain welfare programmes, including the consolidation of a universal non-contributory pension for all people at least 60 years of age known as *Renta dignidad* (dignity pension), and the creation of two conditional transfer programmes, *Bono Juancito Pinto* and *Bono Juana Azurduy*, both of them directed at vulnerable groups.

This chapter on the Bolivian case analyzes the scope of the universal pension system and its implications in terms of social investment, the sources of financial support and the strategy for creating the necessary fiscal space, the context in which the new fiscal space was generated, and the extent to which these changes are sustainable.

3.2. Bolivia's social protection system

The social protection system in Bolivia, as in other Latin American countries, has evolved into a model that combines contributory and non-contributory components in a number of benefits. Because of the wide range of programmes, each with its palette of benefits for different categories, and of the inadequate coordination between them, the system is highly fragmented and the contributory programmes have a very low coverage. Non-contributory pensions for the elderly are the exception in terms of social protection coverage.

3.2.1. Contributory benefits

Except for unemployment insurance, the contributory component of Bolivia's social security system covers the contingencies listed in the ILO's Social Security (Minimum Standards) Convention, 1952 (No. 102): disability, old age, survivors, employment injuries, health insurance, sickness and maternity allowances, family benefits and allowances (including marriage, childbirth, nursing and funeral expenses).

Until 2010 the contributory pension scheme was administered by private pension funds (AFPs), which managed individual accounts. After a complicated political process, a new legislation to nationalize the system and transfer its administration to a state entity was approved. In 2011 a process of transition was initiated in order to gradually transfer the management of the new system to the state entity. The contributory health benefits and some other subsidies are administered by the health insurance funds (*Cajas de salud*).

Historically, the contributory component is notable for its low coverage, one of the three lowest in Latin America. An ILO study (Durán-Valverde and Picado, 2009) estimated that no more than 13.5 per cent of the economically active population contributed to the health insurance scheme, which protects approximately 30 per cent of the total population and less than 15 per cent of the rural population. The situation of the contributory pension scheme is even more critical, as coverage has not managed to rise above the historic peak of 12 per cent of the economically active population.

3.2.2. Non-contributory benefits

Non-contributory benefits are a major feature of Bolivia's social protection system and cover a wide range of benefits in such critical areas as old-age pensions, health care services and conditional cash transfers to specific groups. The following are the main non-contributory programmes:

- Universal old-age pension known as *Renta dignidad* which provides a pension to all citizens from the age of 60;
- Universal mother and child insurance (*Seguro Universal Materno Infantil* (SUMI)), whose potential beneficiaries are all children under five years of age and all pregnant women from the start of pregnancy till six months after delivery (it does not cover the treatment of diseases that are included in the basic health package – the *Seguro Básico de Salud* (SBS) – for the general population);

- Health insurance for adults (*Seguro de Salud Para el Adulto Mayor* (SSPAM)), a free comprehensive insurance designed to provide health care benefits at all levels under the national health scheme to citizens over 60 years of age who are not covered by social health insurance, whether Bolivians or foreigners residing in the country;
- *Bono Juancito Pinto*, a cash transfer which is conditional on school attendance and which targets some of the most vulnerable segments of the population, such as children receiving formal public education, alternative youth education and special education;
- *Bono Juana Azurduy*, a cash transfer that is conditional on health care in support of women during the period of pregnancy and childbirth and of their children under two years of age; it includes four payments prior to the time of birth, a payment at birth and 12 subsequent payments until the child reaches 2 years of age;
- A social housing solidarity programme (*Programa de vivienda social y solidaria*), which consists of a 70 per cent subsidy on the cost of housing for people with low financial capability, with individual and joint guarantees.

Towards the end of 2009 official estimates indicated that benefits under the three conditional transfer programmes reached approximately 31 per cent of the total population of Bolivia.

3.3. *Renta dignidad*: Universalizing old-age pensions

One of President Juan Evo Morales' most demanding campaigns has revolved around the strengthening of the non-contributory pension scheme. This culminated in the creation of the *Renta universal de vejez* (universal old-age pension), better known in Bolivia as the *Renta dignidad*. The programme was founded in 2007 by Act No. 3791 and replaced the previous non-contributory pension scheme known as BONOSOL.³

The *Renta dignidad* is administered by the Ministry of Economy and Public Finances, with the participation of the military and the national banking system in the delivery of benefits.

The *Renta dignidad* is a non-contributory annuity benefit that the Bolivian State awards to all Bolivians over 60 years old who live in the country and do not receive a contributory social security pension or any other payment under the national Budget. It is also paid to beneficiaries of the contributory pension scheme, up to 75 per cent of the full amount of the *Renta dignidad*, and also covers funeral expenses.

The amount of the *Renta dignidad* is 200 bolivares (approximately US\$28.5) per month for people who do not receive a pension from the contributory pension scheme, and 150 bolivares a month (about US\$21) for those who receive a pension under the compulsory social insurance scheme. Calculations based on the *Boletín estadístico* of the Office of the Vice-Minister for Pensions (SPSV, 2009) show that towards the end of 2009 the average monthly pension was US\$27.

³ Created in 1995, the BONOSOL programme distributed US\$220 to Bolivians over 65 years old for over ten years. The programme was financed by a fund created from the privatization of state enterprises in 1997 under President Juan Evo Morales.

The main innovation of this scheme is its source of financing. Universal benefits are paid out of the *Fondo de renta universal de vejez*, which is financed as follows:

- (a) 30 per cent of all resources received by the State in respect of the direct tax on hydrocarbons from prefectures, municipalities, the Latin American Indigenous Fund and the National Treasury.
- (b) Dividends of public companies that were “capitalized”⁴ (partially sold by the state to transnational corporations), according to the proportion of shares owned by all citizens of Bolivia.

The *Renta dignidad* is paid on a monthly basis, according to the beneficiary's date of birth. To be registered as pension beneficiary, the person must present an identification document.

To be eligible for the *Renta dignidad* a beneficiary must be at least 60 years of age, be a Bolivian or naturalized citizen, be domiciled in the country and have a national identity document. The benefit may be paid in any licensed financial institution, which in practice means the entire national banking system as well as approved military bases.

Compared to the previous non-contributory scheme, the *Renta dignidad* has meant a substantial improvement in pensions. In 2008 the former annual payment was converted into a monthly payment and the age limit for entitlement was lowered from 65 to 60 years of age. Since then the number of beneficiaries has grown remarkably, from nearly 450,000 pensioners in 2006 to 750,000 in 2009, an increase of 65 per cent in less than four years.

3.4. Coverage indicators

Over the last decade there has been a sharp increase in the coverage of Bolivia's social protection programmes, except for the health insurance and contributory pension programmes. The relevant information is summarized in table 5.

The low coverage of the contributory schemes is mainly attributable to the existence of a very high proportion of independent workers, most of whom work in the informal economy or in the traditional agriculture sector. This is coupled with a high rate of evasion of social security contributions, even in the formal economy.

⁴ In the context of Bolivia, capitalization is defined as a type of privatization where investors acquire a fifty per cent share, and also the control of management for some public enterprises.

Table 5. Bolivia: Social protection coverage indicators, 2000-2009

Indicator	2000	2005	2006	2007	2008	2009
Contributory pensions, contributors as % of EAP	11,1	10,8	10,9	12,1		
Health insurances, contributors as % of EAP	12,4	14,4	14,5	15,7		
Population 60 years and older, receiving contributory pension (%)	17,6	15,6	15,5	15,3	15,7	
Population 60 years and older, receiving non-contributory pension (%)	62,1	75,8	71,7	75,2	110,7	
Population 60 years and older, receiving pension (%)	79,7	91,4	87,2	90,5	126,4	
Coverage of social assistance programmes (% total population)	4,0	5,0	16,8	23,1	33,6	36,8
" <i>Renta Dignidad</i> "	4,0	5,0	4,7	5,0	7,5	7,3
Bond " <i>Juancito Pinto</i> "	-	-	11,3	13,5	18,0	18,0
Bond " <i>Juana Azurduy</i> " ¹	-	-	-	-		3,6
Literacy programmes	-	-	0,8	4,6	8,2	8,0

¹ The bond of motherhood Juana Azurduy begins from the month of May 2009.

Source: APS, 2010; ILO, 2010b; International Monetary Fund, 2010b; World Bank, 2010; UDAPE, 2010; Ministry of Economy and Public Finances, 2010.

Unlike the contributory programmes, all the non-contributory programmes expanded rapidly in the space of a few years, including the *Renta dignidad*, the *Bono Juancito Pinto*, the *Bono Juana Azurduy* and the newly created literacy programme (*Programa libre de alfabetización*), with the total number of beneficiaries over the decade rising from 4 per cent to almost 37 per cent of the total population.

The coverage of the *Renta dignidad* was particularly significant. In 2000 some 60 per cent of the population 60 years old and over were receiving non-contributory pensions.⁵ Official data of registered beneficiaries from 2008 onwards combined with United Nations population projections (ECLAC, 2010a) indicate a coverage rate of 100 per cent.⁶

These statistics illustrate the minor importance of the contributory component of the social security system, at least in terms of the number of people covered, and the relative ineffectiveness of social insurance in terms of its coverage over the years. The coverage indicators also allow us to assert that the creation of BONOSOL and its subsequent consolidation in the form of a universal old-age pension, the *Renta dignidad*, is perhaps the most important development in social protection policy in Bolivia during the last years. In fact, the most important feature of the structural reform of Bolivia's pension system is the universal non-contributory pension scheme, much more significant perhaps than the transition from a defined benefit regime to an individual accounts scheme.

The coverage statistics of Bolivia's non-contributory programmes unquestionably make the country a success story in terms of policies dealing with universal social protection rights. It remains in the following sections to analyze the strategies for financing these measures in terms of sustainable fiscal space.

⁵ It should be noted that before 2006 the *Renta Dignidad* programme was universally granted to persons 65 years and older.

⁶ The coverage above 100 per cent can be justified by: some data flaws; cases in which one person receives more than one non-contributory pension (fraud); and/or the simultaneous reception of both types of pensions (legally possible).

3.5. How fiscal space was created to finance the extension of non-contributory coverage?

Because of the importance of social protection within national economies, creating fiscal space to finance the extension of coverage is one of the biggest challenges of social policy, as a universal policy usually requires the mobilization of a significant volume of resources.

In Bolivia the expanded coverage of social protection programmes described above, largely in the form of non-contributory benefits, was made possible by the combination of two developments, each of which occurred in quite different political circumstances – and, one might say, almost in opposition to each other:

- (a) First, there was the massive sale of state assets to the private sector which occurred in the 1990s, known in Bolivia as the capitalization of state assets.⁷ This process played a major role in the creation of the Collective Capitalization Fund (FCC). The FCC's sole function was to support the BONOSOL, an annuity benefit payable to all Bolivians from the age of 65 years who were 21 years old or over in December 1995. It is important to bear in mind that this process of sale of state assets took place at the same time as the reform of the Bolivian pension system, which introduced individual accounts under the private administration of the Pension Fund Administrators (AFP). BONOSOL was thus a crucial element in the economic policy aimed at the privatization of state assets.
- (b) Secondly, the re-nationalization of the hydrocarbon sector was decreed in 2006. Under the new law the State recovered full ownership, possession or control of the country's natural hydrocarbon resources. Moreover, the nationalization law established a new scheme that changed radically the redeployment of revenue from the production of hydrocarbon: 82 per cent of revenue for the State and 18 per cent for private companies. As a result, the Bolivian State's revenue from the exploitation and sale of hydrocarbons was multiplied, and this in turn brought a significant increase in fiscal revenue (and hence fiscal space).

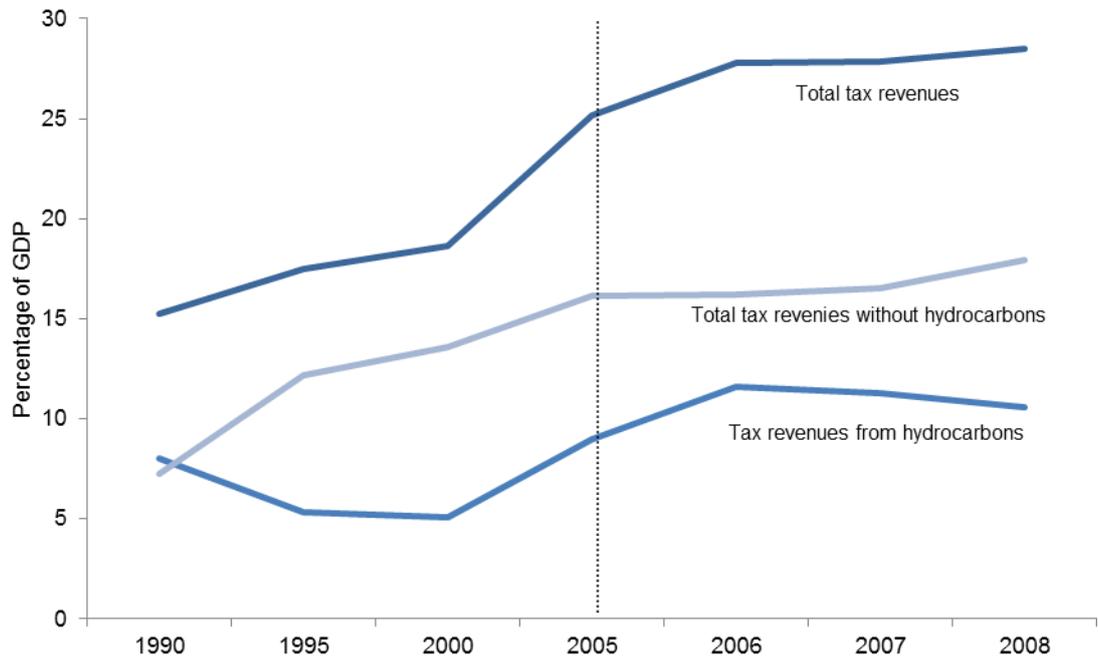
The consolidation of *Renta Dignidad*, then, is the historical product of two politically and ideologically antagonistic processes. Its predecessor, BONOSOL was devised as an instrument of "political compensation" for the privatization of state assets during the rise of neoliberalism in Bolivia. At that early stage, it was a means of delivering a non-contributory pension scheme to a specific generation of Bolivians. The second phase, which consolidated the instrument's financing and universality as a citizen's right, occurred as a result of the transfer of political power into the hands of socialist leaders.

As a way of creating fiscal space, the Bolivian method seems innovative, since it derives from a renegotiation of the terms for exploiting the country's natural resources. In fact, since the 1990s Bolivia's fiscal revenue has been growing almost continuously (figure 8),

⁷ The capitalization involved increasing the capital of some state enterprises, through new contributions from private foreign investors, in an amount equal to their book value. Thus, 50 per cent of the shares passed into the hands of private investors, while the other 50 per cent were offered to Bolivian citizens (those domiciled in the country and who reached the age of 21 years before 31 December 1995). These shares constituted the Collective Capitalization Fund (FCC), whose administration was entrusted to the Pension Fund Administrators (AFP) of the mandatory social insurance scheme. The profits from the sale of these shares were BONOSOL's sole source of financing. The whole process was reversed in 2006 under the administration of President Juan Evo Morales, who was brought back into power by a referendum that took place in 2004.

with total tax revenue growing from about 15.3 per cent of GDP in 1990 to 28.5 per cent in 2008.⁸

Figure 8. Bolivia: Total tax revenue and hydrocarbons tax revenue, as a percentage of GDP (1990-2008)



Source: Banco Central de Bolivia, 2009; World Bank, 2010.

To a large extent Bolivia's new fiscal space is attributable to government revenue from the production and sale of hydrocarbons. State taxes on revenue from hydrocarbons accounted for 5.3 per cent of GDP in 1995, rising to 9 per cent in 2005 and reaching 11.3 per cent of GDP by 2007.

Including the revenue from taxes on hydrocarbons, Bolivia's overall tax revenue in terms of GDP is now above the average for Latin America.

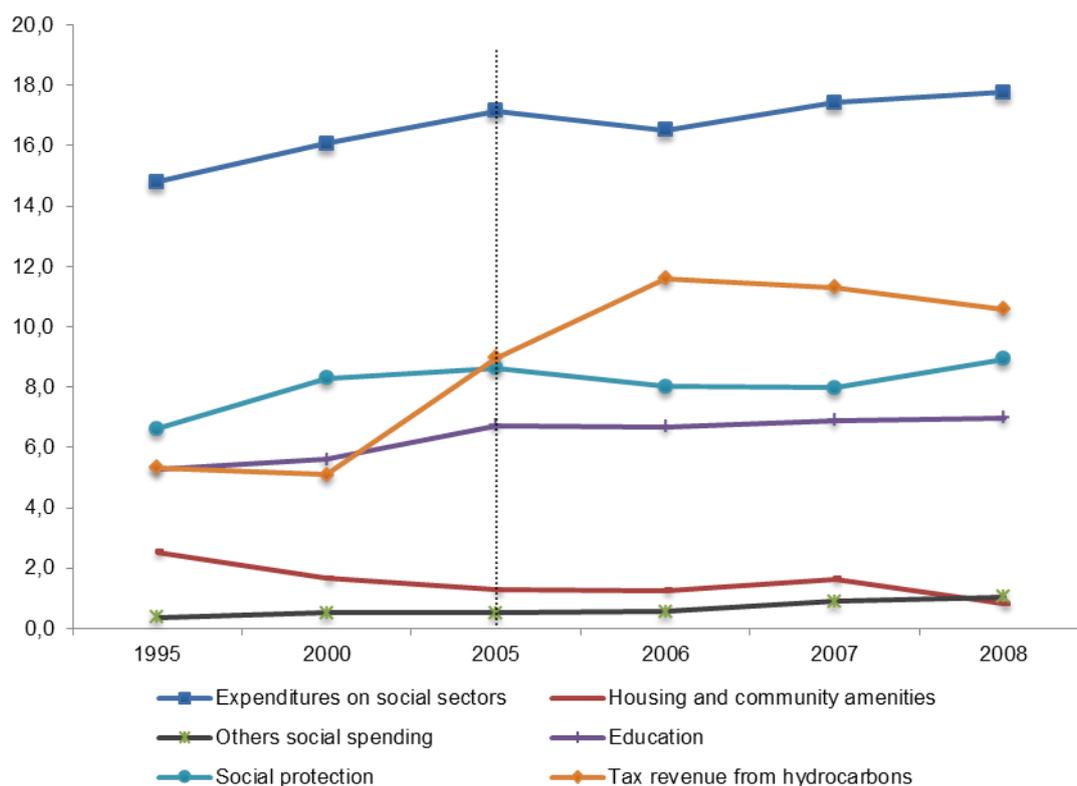
One important factor that should be mentioned is the effort of the Bolivian State to increase the tax burden in other areas than the hydrocarbon sector, and in fact the tax burden, not counting hydrocarbons, has grown steadily for the past 15 years. Between 1995 and 2008 tax revenue not related to hydrocarbons, including social security contributions, increased from 12.2 per cent to 17.9 per cent of GDP (figure 9).

The behaviour of Bolivia's fiscal pressure indicator speaks well of the policies for creating fiscal space undertaken in the country over the past 15 years.

Given this process of creating fiscal space, the degree to which the new fiscal space has been allocated to development financing, particularly the promotion of social investment, is critical.

⁸ This includes social security contributions.

Figure 9. Bolivia: Social expenditure as a percentage of GDP and revenue from taxes on hydrocarbons (1995 – 2007)



Source: Ministerio de Economía y Finanzas Públicas, 2008; International Monetary Fund, 2010b.

The main indicator of the macroeconomic priority attached to social spending, i.e., the ratio to GDP of expenditure on the social sectors, shows that public policy has been clearly focused on social investment. Between 1995 and 2007, the ratio of social expenditure to GDP increased by 4.7 percentage points; this increase was lower than the overall increase of 11 percentage points experienced in total tax revenues. New investment, though significant in relative terms, was still lower than the increase in state revenues generated exclusively by the sales of hydrocarbons – 6 percentage points of GDP over the same period. These indicators reflect a cautious but not restrictive policy vis-à-vis the allocation of fiscal resources compared to the new size of the Bolivian tax burden.

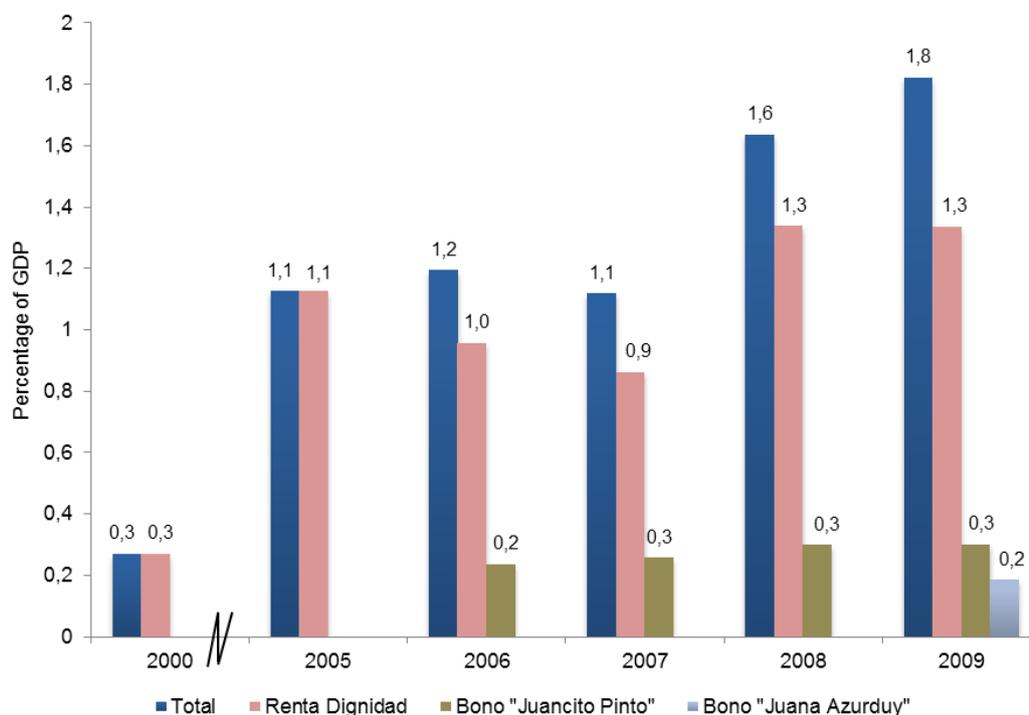
It is important to emphasize the major contribution of revenue from hydrocarbons in relation to the volume of social spending; that revenue is currently equivalent to two-thirds of Bolivia's total expenditure on the social sector (figure 9).

The extent to which priority is given to investment in social protection is likewise significant. While the contributory social insurance programmes have not managed to increase their revenue much beyond the historical levels of the last two decades, non-contributory social protection has received a considerable boost, clearly facilitated by the new fiscal space. It should be noted that this situation differs greatly from that of other countries of the region, such as Argentina, Brazil, Chile and Colombia. Unlike Bolivia, these countries have succeeded in mobilizing substantial amounts of revenue through social contributions.

Total expenditure on social protection, contributory and non-contributory, rose from 4.6 per cent to 7.6 per cent of GDP over the period 1995-2007. During the same period, expenditure on social protection measured in real terms were multiplied by a factor of 2.5.

The bulk of this increase was due to the expansion of expenditure on non-contributory programmes.

Figure 10. Bolivia: Trend of spending on social assistance programmes as a percentage of GDP



Source: Ministry of Economy and Public Finances, 2010; UDAPE, 2010.

Investment in the three main non-contributory social protection programmes – the *Renta universal de vejez* for old-age pensions, the *Bono Juancito Pinto* for education benefits and the *Bono Juana Azurduy* for maternity and child benefits – grew at a rapid pace during the last decade, mainly as a result of an extension of the coverage of non-contributory pensions (*Renta dignidad*). In 2009 the official figure for expenditure on these three programmes was equivalent to 1.8 per cent of GDP, of which nearly three-quarters went to the *Renta dignidad* (figure 10).

3.6. Fiscal space and the sustainability of investment for development

Certainly, then, the creation of *Renta dignidad* and other conditional cash transfer programmes recently established in Bolivia is a success story, given the limited choice of public policies on social protection in the country. This is true of many other low- and middle-income countries.

Given Bolivia's current position in its process of economic and social development, especially considering the great importance of the informal economy in total employment generation, it is impossible to identify options allowing for universal coverage – or even a significant expansion of existing coverage – based entirely on contributory financing. In any case, the results that could be obtained by extending contributory insurance to the entire formal economy, while necessary and indispensable in a long-term strategy, would not be significant in the short and medium term.

Because of their source of financing, the sustainability of *Renta dignidad* – the most expensive of the non-contributory programmes – and other social assistance programmes created in recent years would seem to be directly linked to Bolivia's ability to generate

revenue from the exploitation of its hydrocarbon resources. Because Bolivia is immensely rich in terms of its endowment in hydrocarbons, especially natural gas, the sustainability of any scheme will depend also on the future evolution of the social and political pact that is behind the increase in expenditure on social protection. That evolution is very complex and difficult to predict, especially in a country that throughout its history has shown a high degree of political instability.

In contrast to other countries that have been similarly favoured with an optimal endowment in natural resource for extraction and commercial exploitation, Bolivia seems to be making a sustained effort to expand its fiscal space by other means, such as regular tax revenue, without having regard exclusively to its hydrocarbon wealth. This is a promising sign in terms of ensuring the sustainability of fiscal space already capitalized.

3.7. Impact of new social investment in Bolivia

In the case of Bolivia, in addition to the sustainability of fiscal space created through taxes on the exploitation of natural resources, it is possible to evaluate the creation of fiscal space from the standpoint of the quality of new social spending, especially in terms of its impact on development goals.

Several studies have documented the country's recent achievements in terms of investment growth and poverty reduction and, in general, in attaining the MDGs. A prospective quantitative study carried out by Valdivia and Montenegro (2009) argues that since 2006 the growth rate of public investment has increased, including a 3 per cent rise in social investment and another 3 per cent in investment in the productive sector. The same author states that the transfers made through the *Renta dignidad* and the allowances paid through the *Bono Juancito Pinto* and *Bono Juana Azurduy* have had an intergenerational effect on the level of welfare of Bolivian society: "...the main effect of this fiscal shock is increasing the level of welfare of people with fewer resources, as well as an increase in GDP of 1.1 per cent over its natural trend" (Valdivia and Montenegro, 2009).

In Bolivia improvements have been documented in access to education and maternal and child health, thanks to monetary incentive programmes. Regarding school attendance benefits, Pardo (2010) mentions that the rate of school attendance in Bolivia for the 6-11 year age group increased by 2.6 percentage points between 2006 and 2007. It is further estimated that, on average, families in urban areas which have children in primary school spent around Bs. 375 (approximately US\$55) on education each year and that the education benefit can cover 53 per cent of family spending on education in urban areas and more than 100 per cent in rural areas. Increases in school enrolment have been also documented.

Regarding the impact of the *Renta dignidad*, it is estimated that in 2008 almost 7 per cent of the population and 20 per cent of all households benefited from the programme, which contributed about 9.4 per cent of the monthly household income and thus had a significant impact on domestic consumer demand (Pardo, 2010).

As to the impact on poverty, Pardo (2010) estimated that, as a result of conditional cash transfer programmes, extreme poverty would be reduced by 14.6 percentage points between 2007 and 2015 and that on the contrary, if benefits from these programmes were not granted, then the percentage of people living in extreme poverty in 2008 would be 39.8 per cent higher.

3.8. Lessons learnt

Lesson 1

It is feasible to renegotiate the terms of the distribution of wealth generated by the exploitation of natural resources. Developing countries favoured by natural resource endowments have an obvious advantage in terms of their ability to finance public spending and social investment, especially for development purposes. However, judging from the historical experience of Bolivia, a country which over the past 500 years has gone through several cycles of massive exploitation of its non-renewable natural resource base (silver, guano, rubber, tin and hydrocarbons), it does not seem an easy goal to achieve, especially in terms of political economy. The case of Bolivia shows that it is feasible, politically and economically, to renegotiate the conditions of the distribution of profits from the exploitation of natural resources in order to obtain more balanced and fair terms for the country. In Bolivia this renegotiation was radical, and by its positive impact on the creation of fiscal space it represents a strategic step towards sustainable development and economic growth.

Lesson 2

State revenue from the exploitation of natural resources can account for a significant proportion of investment for development. Bolivia's revenue from the exportation of hydrocarbon products accounts for about 40 per cent of total tax revenues and for 10 per cent of GDP. This is highly significant, because these “fresh” sources are equivalent to more than two-thirds of Bolivia's total expenditure on the social sector. Over the last two decades the cost of social protection increased considerably, but it was greatly exceeded by the increase in taxes on revenue from hydrocarbons.

Lesson 3

Non-contributory social protection benefits are a viable option for achieving universal coverage in countries with a large informal economy. The example of Bolivia shows that, while the possibility of extending traditional social insurance may be limited (mainly because of the predominance of the informal economy over the formal economy), a non-contributory benefit scheme is a viable option for guaranteeing universal rights in accordance with the approach of the Social Protection Floor promoted by the ILO. However, financing policies and other efforts to increase tax coverage in sectors of the economy where this is practicable, as well as strategies for creating fiscal space by increasing social contributions and for strengthening social protection in the long term, should on no account be overlooked.

Lesson 4

Investment in social protection pays. Recent studies on the impact of increased social investment in Bolivia confirm the advantages of such a strategy for economic growth. Bolivia offers clear evidence that the argument that investing in social protection competes with private investment is erroneous. Such an idea is a fallacy, because it is evident that expenditure on social protection, regardless of its origin, is injected into the economy and becomes part of a circular flow of income. These injections of resources are useful to support growth in spending in the short term and, by increasing human capital, contribute to macroeconomic stabilization in times of crisis. This, in turn, is a genuine source of expansion of fiscal space.

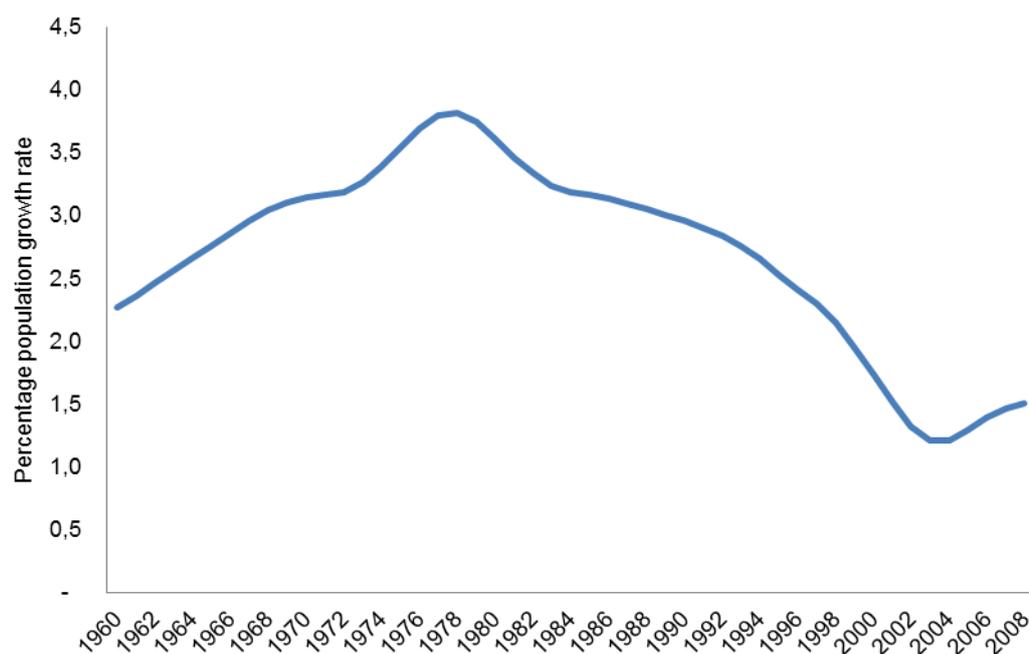
4. Botswana: Creating the basis for improved social protection

4.1. Country profile

Located in the southern part of Africa, Botswana is a parliamentary republic that became independent in 1966. The country is a landlocked nation that borders Namibia to the north and west, South Africa to the south and south-east and Zimbabwe to the north-east. Botswana covers a total territory of 581,730 square kilometers and is the 47th largest country in the world. Since Independence, the country has had free and democratic elections.

The total population was estimated at 1,978,000 million inhabitants in 2010, according to the United Nations population database (United Nations-Population Division of the Department of Economic and Social Affairs, 2010). The population growth rate peaked in 1978 when it reached 3.8 per cent, after which the annual rate started to decline, reaching a low of 1.2 per cent in 2003 and 2004 (figure 11). At the current rate, the population is projected to reach 2.7 million by 2050.

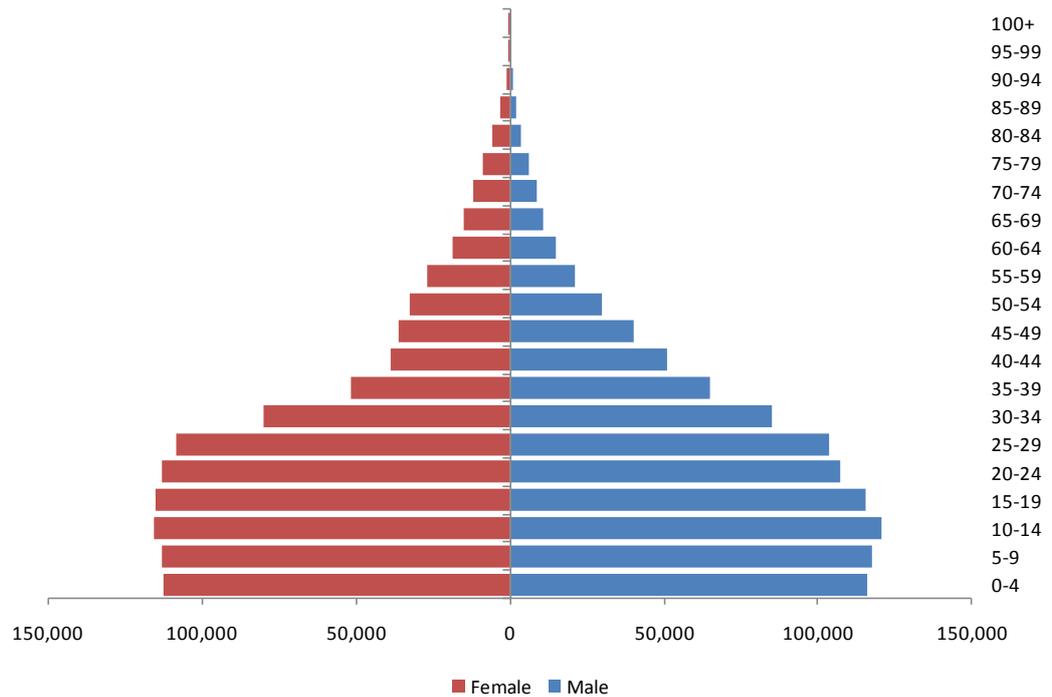
Figure 11. Botswana: Historical population growth rates, 1960-2008



Source: United Nations Population Division database, 2009.

Overall, the population of Botswana is young, with a median age of 21.7 years. The population pyramid (figure 12) shows a strong predominance of the lower age groups. By 2010 one-third of the population was less than 14 years old and 75 per cent of the population was under 30 years of age. At the other end of the age scale, a mere 5.5 per cent of the current population is 60 years old or older.

Figure 12. Botswana: Population pyramid, 2010



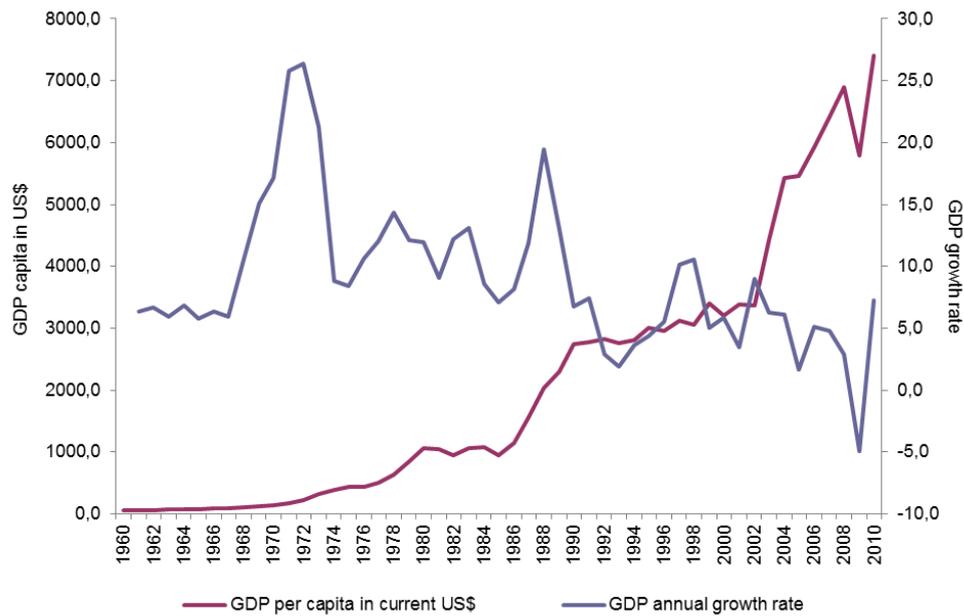
Source: US Census Bureau, 2010.

Practically all the key demographic indicators have shown a downward trend over the last three decades. The total fertility rate declined from 3.8 births per woman in 1995 to an expected 2.5 births per woman in 2010, while the crude birth rate fell from 30 to 23 births per 1,000 habitants during the same period.

In economic terms Botswana produces 22 per cent of the world's diamonds and is the most important producer of this mineral. Since the country's independence the economy has been driven by diamond exports, and this is perhaps the key element in understanding Botswana's economic performance since then.

Between 1966 and 2005 Botswana was the fastest growing economy in the world, with an average annual economic growth rate of 9 per cent. Between 1966 and 1990 the mean growth rate was even higher (13 per cent), though the 10-year average growth decelerated after 1980, from 11.5 per cent in the 1980s to 5.1 per cent in the 1990s and to 4.7 per cent in the 2000s (figure 13). The impressive performance of its economy allowed the country to multiply its per capita GDP by a factor of 50 between 1970 and 2008; despite the reduced growth rate in the 2000s, the per capita GDP doubled.

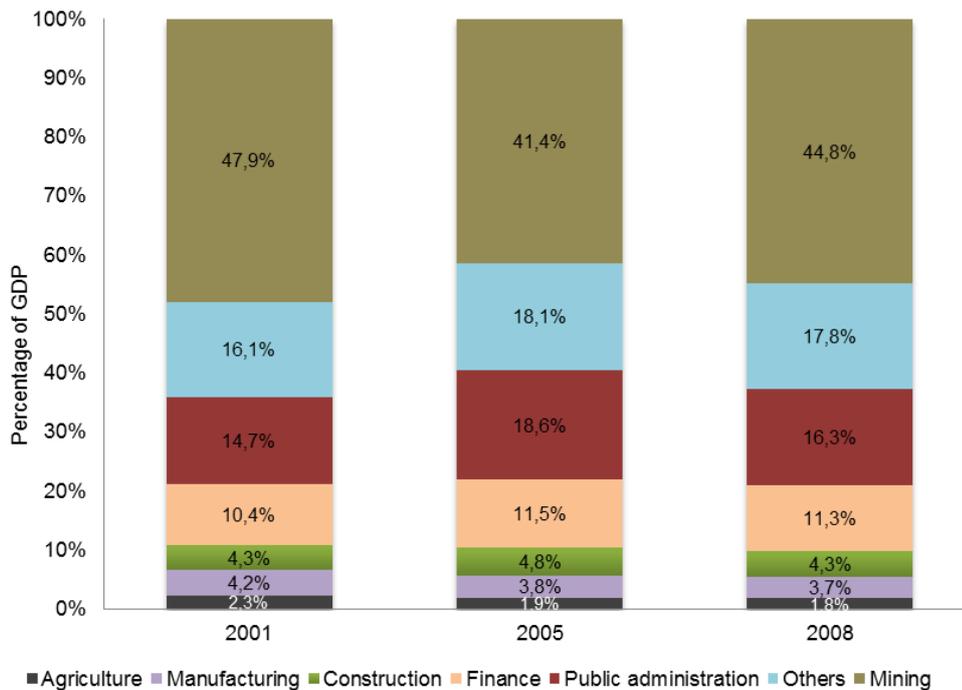
Figure 13. Botswana: Long-term GDP and GDP per capita growth rates, 1960-2010



Source: World Bank, 2010.

The economy of Botswana is a resource-driven economy, one whose most distinctive features is its strong reliance on diamond exports, its main product since Independence. Not surprisingly, therefore, mining is the country's main economic activity, accounting for 45 per cent of GDP in 2008. The participation of the public administration sector, the second largest in Botswana, represents roughly one-third of the contribution of the mining sector (figure 14).

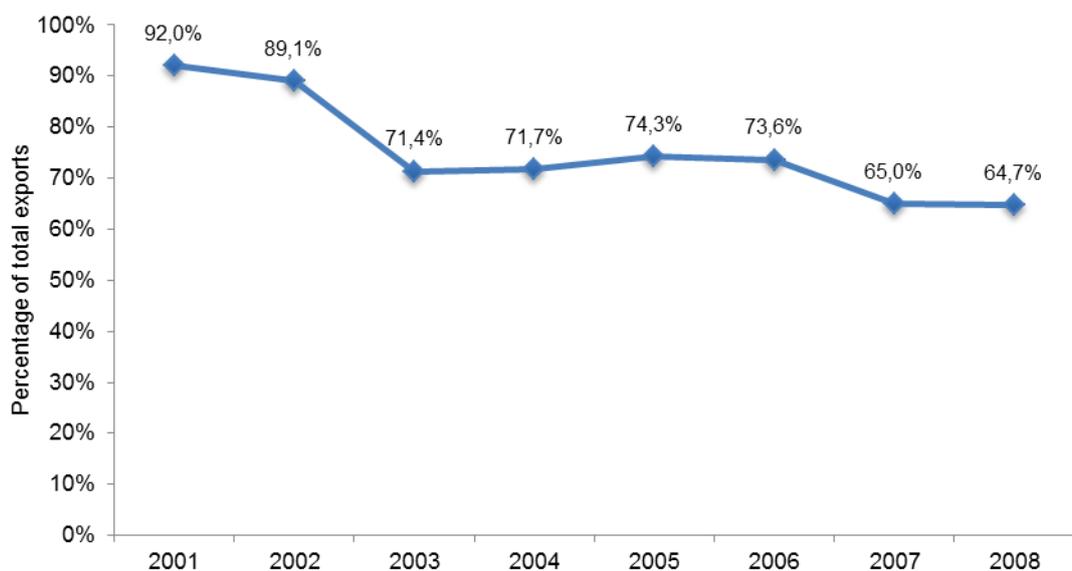
Figure 14. Botswana: Structure of the economy by sector



Source: AfDB et al., 2010.

Historically, diamonds have accounted for more than 90 per cent of total exports, though after 2003 their participation decreased to 65 per cent in 2008 (figure 15). This declining participation of diamonds in total exports was the result of two factors. First, the demand for diamonds on the international market fell sharply during the financial crisis of 2008.⁹ Second, other exports from Botswana grew at very dynamic rates that were well above the performance of diamonds. While diamond exports increased by an average of 5.5 per cent annually between 2001 and 2008, exports of copper-nickel matte and textiles grew by 43 per cent and 49 per cent respectively.

Figure 15. Botswana: Diamond exports as a percentage of total exports, 2001-2008



Source: AfDB et al, 2010.

Two additional features characterize the economy of Botswana. The first is that the unemployment rate was estimated at 7.5 per cent in 2007, with some sources citing even a two-digit rate. For the years for which data are available, the average unemployment rate between 1990 and 2006 was 21.4 per cent.

The second characteristic is the low inflation rates that have prevailed since 1997. With the exception of 2006 (11.6 per cent) and 2008 (12.7 per cent), the consumer price index increased at an average of 8.4 per cent between 1997 and 2009.

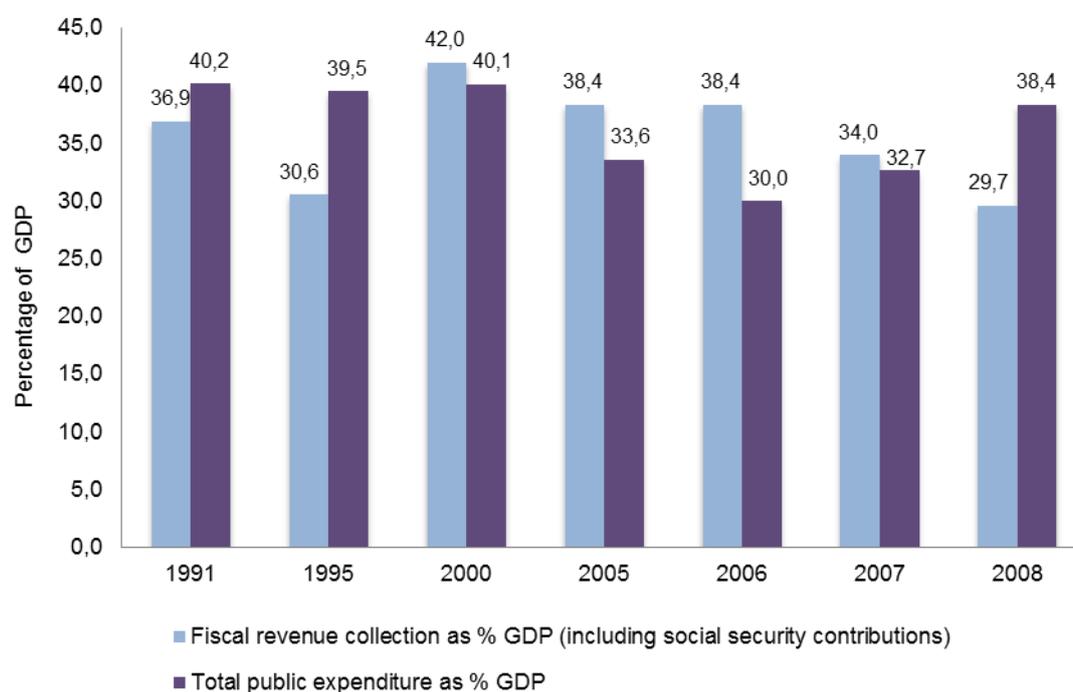
With regard to fiscal matters, from Independence to 1995 the economy experienced a great accumulation of international reserves and a sustained fiscal surplus. Despite fast-growing fiscal revenue (mostly derived from diamond export taxes and accelerated economic growth), the Government maintained a cautious policy and no fiscal deficits were ever observed. By 2008 fiscal revenue accounted for 29.7 per cent of GDP, with an average of 35.7 per cent of GDP between 1995 and 2008 (figure 16).

The participation of the Government in the economy is also high for a developing country. In 2008 public spending accounted for 38 per cent of GDP, while between 1995 and 2008 the average participation of the public sector was 36.4 per cent. The 2008 figure suggests

⁹ See, for instance, <http://www.nytimes.com/2009/02/20/business/worldbusiness/20iht-diamond.4.20339704.html>.

that public spending is recovering after three years in which it averaged 32 per cent of GDP. During the 1990s public expenditure stayed around 40 per cent of GDP.

Figure 16. Botswana: Fiscal revenue and public expenditure as a percentage of GDP, 1991-2008



Source: Central Bank of Botswana, 2010; International Monetary Fund, 2010b.

The Government of Botswana received most of its revenue from diamond exports. This strong source of income generation from the country's most important product is the result of an agreed 50/50 joint venture between the Government and the De Beers Botswana Mining Company (Debswana). The initial arrangement, which set up a 20/80 agreement, was later the subject of new negotiations and amendments, as a result of which Botswana increased its equity to 50 per cent by buying another 30 per cent of the company's shares (Gaolathe, 1997).

Regarding the successful negotiations between the two parties, Maipose (2008, pps. 10-11) explains the situation in the following way:

“One of the most important policy choices was the decision to negotiate for joint partnership with the mining companies. These agreements entailed leaving the management of the enterprises to private partners. Retrospectively, they can be viewed as the start of a “smart partnership” between the private and public sectors. ... Some observers wonder how the Government managed to negotiate such a good deal with a multinational company. The explanation lies in the nature of Botswana’s political economy, the nature of the interests at work, and demonstration effects outside Botswana. Asset owning by the state is traditionally legitimate; negotiations leading to partial state ownership of mines reflected the state’s traditional role as a conduit for redistributive policies...The wind of nationalization sweeping across the developing world in general and Africa in particular provided both leverage for Botswana negotiators and a good reason for the foreign investor to want to circumvent nationalization. As a very poor country, Botswana risked scaring off foreign investors, who were perceived as crucial to development... Afraid of the consequences of nationalization elsewhere and in order to fortify what turned out to be a profitable business interest, the mining companies were willing to give more

shares to the Government... Thus the outcome of the negotiations reconciled the two sides' interests."

ODA was a significant contributor to the creation of fiscal space in Botswana during the early years of independence; today, however, the inflow of grants and external resources is minimal when compared to those historical figures. As a proportion of the gross national income (GNI), ODA averaged 10.9 per cent between 1970 and 1989, after which it started to decline sharply to an average of 1.8 per cent of GNI between 1990 and 2008. In 2008 ODA flows recovered and accounted for 5.4 per cent of GNI, due in large measure to external assistance in the fight against HIV and AIDS (figure 17). The generally declining trend in ODA was, however, offset by rapid increments in exports, so in terms of fiscal space it is possible to talk of a "substitution effect" between the two flows of funds, given the strong link between exports and government revenues.

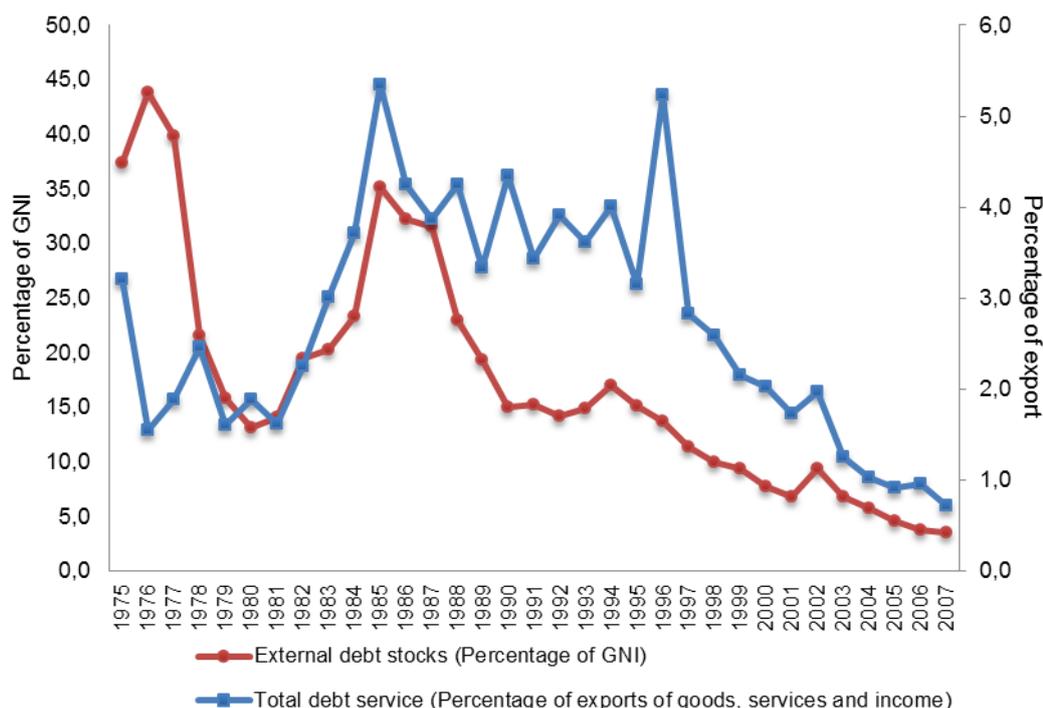
Figure 17. Botswana: ODA as a percentage of gross national income, 1960-2008



Source: World Bank, 2010.

Another relevant issue in terms of the generation of fiscal space was debt management, mainly characterized by prudence even during boom periods. External debt, for instance, fell from a maximum of 47 per cent of GNI in 1973 to 3.6 per cent between 2006 and 2008. As a result, the economy experienced high levels of gross savings, which jumped from 31.6 per cent of GDP in 1975 to 45.4 per cent of GDP in 2008. In addition, debt service payments fell considerably, to just 0.7 per cent of total exports in 2007 (figure 18).

Figure 18. Botswana: External debt and debt service, 1975-2007



Source: World Bank, 2010.

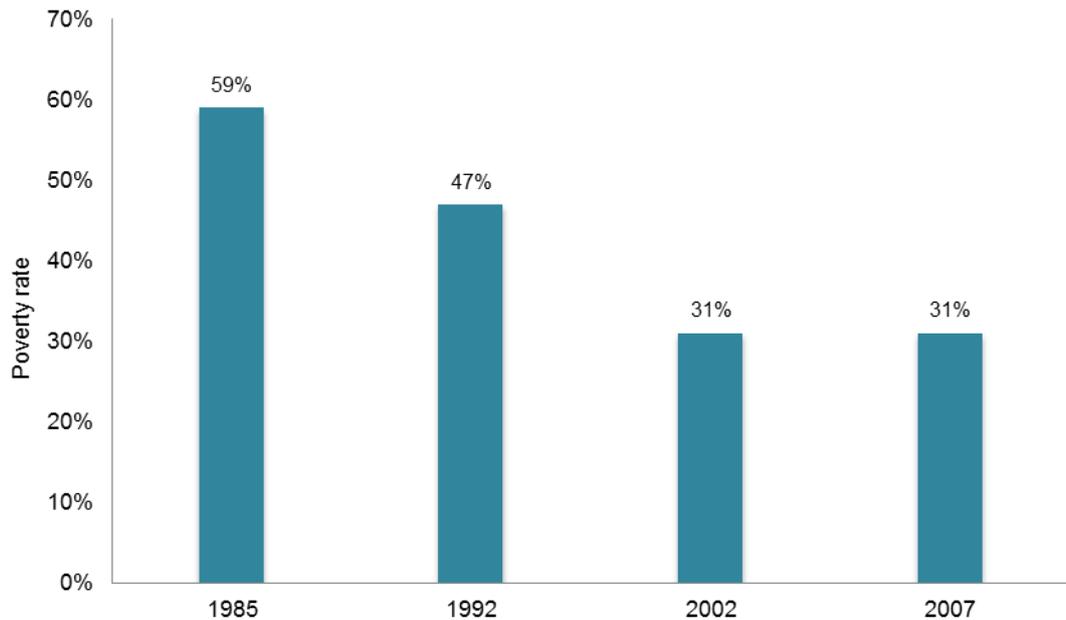
Budget surpluses and reserve accumulation allowed the country to increase savings in the form of off-shore capital investment and savings abroad (Jefferis, 1998). According to the Ministry of Finance and Development Planning (2006), cited by Maipose (2008), Botswana is an atypical case in the context of African and developing countries for three reasons:

- (a) Since 1986 domestic savings have exceeded domestic investment, so the economy has experienced excess liquidity.
- (b) The main sources of government revenue (minerals, customs, overseas aid and investment of reserves) deal in foreign currency and so the tax burden does not fall on the population.
- (c) By 2005 Botswana's international reserves were the equivalent of 40 months of imports.

In social terms, the incidence of poverty in Botswana averaged 31.2 per cent between 2000 and 2007, according to the UNDP database (UNDP, 2009).¹⁰ Several other estimates indicate that the poverty rate in the country was more than 30 per cent over even longer periods. According to Obuseng (2007), the head-count ratio since 1985, when the Government started systematic poverty calculations, has evolved in the way presented in figure 19 below. During the 2000s the country was unable to reduce the poverty level below 30 per cent. Inequality is thus a major concern for Botswana since by 2007 the Gini coefficient was 0.63, the third highest in the world.

¹⁰ Using a poverty line of US\$1.25 per person per day (UNDP, 2009).

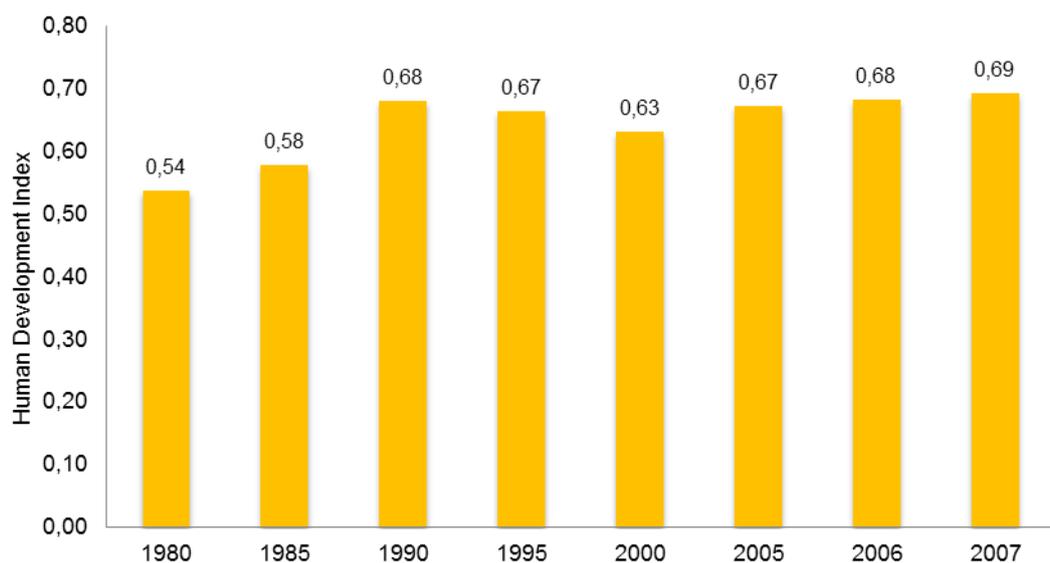
Figure 19. Botswana: Poverty rates in Botswana, several years



Source: Obuseng, 2007; UNDP, 2010.

Despite the country's extraordinary output growth, Botswana's Human Development Index (HDI) is considered in the “medium” category according to the UNDP classification (figure 20). The main limitation on further progress is the life expectancy index (LEI), the only component of the formula that declined between 1980 and 2007.

Figure 20. Botswana: Human development index, 1980-2007



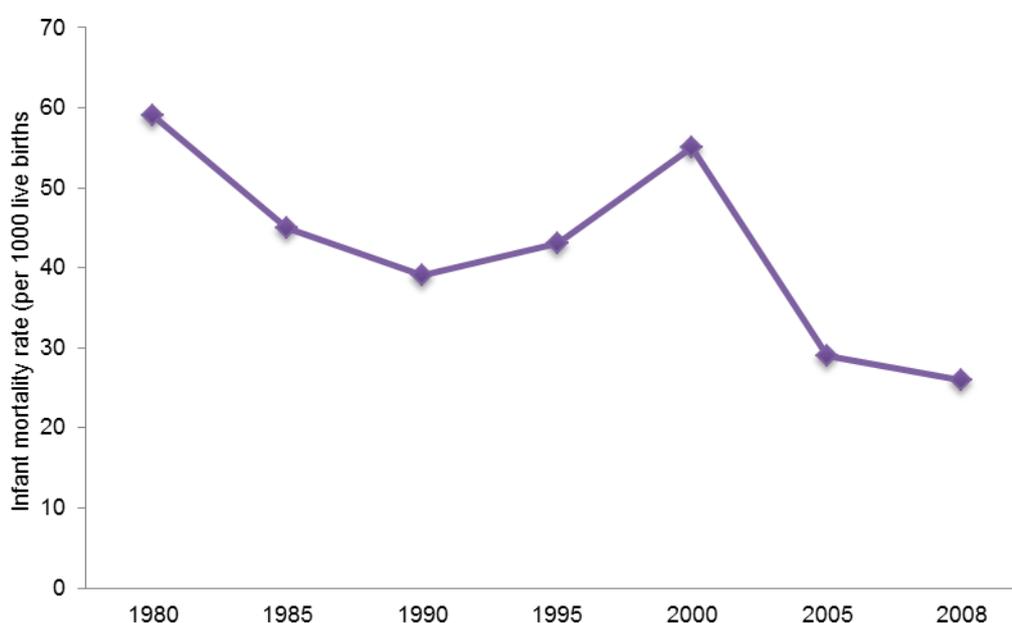
Source: UNDP, 2010.

Life expectancy in Botswana is estimated to be 53 years. Due to the high prevalence of HIV and AIDS among the adult population, the indicator declined from 64.2 years in 1990 to 50.9 years in 2005, since when it has started recovering. Even so, current life expectancy is still 12 per cent, lower than in 1980.

As already mentioned, the main factor behind the decline in life expectancy is the prevalence of HIV and AIDS. According to the UNAIDS and NACA (2010), the Botswana AIDS impact survey (BAIS) estimated in 2008 that 17.6 per cent of persons over 18 months old were HIV positive. On the other hand, the 2009 HIV and AIDS sentinel surveillance calculated that the prevalence among pregnant women was 33 per cent. In general, overall prevalence is thought to be around 17 per cent of the population, with roughly 340,000 adults and 20,000 children now living with the disease. Although prevalence rates have been declining since 2005, Botswana is still a high-prevalence country.

Substantial progress has been observed in the infant mortality rate (IMR). Between 1980 and 2008 the IMR fell by 56 per cent to the current level of 25.9 deaths per 1,000 live births (figure 21). Underweight problems affect 13 per cent of children under 5 years old. Maternal mortality is estimated at 380 deaths per 100,000 live births, a high rate for a middle-income country.

Figure 21. Botswana: Infant mortality, 1980-2008



Source: World Bank, 2010.

On the education side, the adult illiteracy rate among people over 15 years of age is 17.1 per cent. Compared to neighbouring countries, the rate in Botswana compares poorly with Namibia (12 per cent) and South Africa (12 per cent).

4.2. Social protection policy

4.2.1. Organization and coverage

Botswana has a wide array of public initiatives aimed at reducing poverty and lowering the level of vulnerability of people. There are programmes for a broad range of groups, from poor families to children, the elderly and World War II veterans. In general, most of the social protection programmes fall within the social assistance category (table 6). Their characteristics include the following:

- Both groups (social assistance and other social protection programmes) are financed by government budgetary allocations, except for employment injury entitlements which are covered by the employer.
- There is no contributory scheme.
- Practically all the initiatives are non-conditional.
- Most of the programmes are universal within specific target group. However, as will be observed in the next section, a large proportion of the population is still covered by universal programmes (old-age pensions and home-based care, for instance).

The list of key social protection initiatives is presented in table 6, and additional details of each programme are presented in matrix 1.

Table 6. Botswana: Social protection programmes

Social assistance programmes (Non classical cash transfer programmes)	Other social protection programmes
Programme for destitute persons	Universal old age pension
Vulnerable group feeding programme	Orphan care program
School- based food programme	Disability protection
World War II veterans allowance	Sickness and maternity
Labour based drought relief programme	Work injury
Programme for remote area dwellers	Family allowances
Community Home Based Care programme (HIV-AIDS related programme)	

Source: BFTU, 2007a; BFTU, 2007b; OPM, 2010; ISSA; SSA, 2010.

In terms of coverage, the most important initiatives are the programme for destitute persons, the old-age pension programme, the orphan care program and the Community Home Based Care programme (HIV-AIDS related programme). The WWII veterans programme is shrinking because of the nature of its beneficiaries, while the coverage of the drought relief programme varies according to the number of emergencies. Coverage across all the programmes rose during the 2000s, but some still protect only a small portion of the target population. Coverage evolved in the following way between 2000 and 2009:

- ***Destitute persons.*** Coverage almost doubled, from 23,873 persons in 2002 to 42,381 in 2009. Although the term “destitute” does not refer exclusively to poor people (see matrix 1), there is a close connection between the two. Taking poor people as the target population, coverage is a mere 6.8 per cent of the target.
- ***Orphan care programme.*** The number of registered orphans receiving benefits from the orphan care programme increased from 39,571 in 2002 to 47,964 in 2004 and to 51,578 children in 2006. The number of registered orphans dropped to 46,833 in 2009 (BFTU, 2007a; Matambo, 2010; OPM, 2010). The coverage rate in 2006 was 92 per cent of registered orphans, but there has been some dispute as to the real number of orphans in the country, especially as the Botswana Government uses a different definition of orphan from the United Nation.
- ***World War veterans.*** This budgetary provision aims at protecting people who participated in either World War I or World War II. The current cash transfer is 359.00 pula (about US\$47) per month. Coverage has of course been declining over

time, and the number of beneficiaries dropped from 6,953 in 2003 to 3,005 at the end of 2009.

- **Programmes for people living with HIV and AIDS.** There were 3,557 patients enrolled in the Community Home Based Care programme (OPM, 2010). Effective coverage, assuming a total of 340,000 people living with HIV and AIDS (PLHIV), would be 1 per cent of the number of patients.

Matrix 1. Social protection programmes in Botswana

Program	Rationale or objective	Eligibility and coverage	Benefits
<p>Program for Destitute Persons</p> <p>National Policy on Destitute Persons of 1980 and subsequent amendments</p>	<p>The objective of this policy was to ensure that government provides minimum assistance to needy persons to improve their health and welfare conditions and to alleviate poverty.</p>	<p>Elderly people and children that are destitute, according to the definition established by the National Policy on Destitute Persons. A destitute is:</p> <p>An individual who, due to disabilities or chronic health condition is unable to engage in sustainable economic activities and has insufficient assets and income sources.</p> <p>b) An individual who is incapable of engaging in sustainable economic activity and has unreliable and limited sources of income due to old age, mental or physical disability, emotional or psychological disability or is a terminally ill patient with no means of support</p> <p>c) A child under the age of 18 who is in need of care and may not be catered for under the orphan care program or has parent (s) who are terminally ill and are incapable of caring for the child or has been abandoned and is in need of care.</p>	<p>Food rations, cash entitlement, access to social services including rehabilitation, provision for funeral expenses and shelter.</p> <p>Temporary destitute persons residing in rural areas are entitled to P181.90 worth of food rations per month whereas those in urban areas receive P181.40. Included in this amount is P61.00 cash for personal needs.</p> <p>Permanent destitute persons on the other hand are entitled to P256.90 per month in rural areas and P256.40 worth of food items for urban areas. They also receive P61.00 cash for personal items. These amounts may go up to P400.00 depending on the rising costs of commodities particularly in the rural areas. Further, adjustments for inflation are made on a yearly base.</p> <p>Children under the age of 18 also benefit from the destitute program. According to the provisions of this policy; these are children who are in need of care and may not be catered under the orphan care program. In addition to food rations these children get assistance in the form of school uniforms, toiletries, transport, protective clothing, boarding requisites, tuition in private and vocational schools, street clothes, payment of additional fees required by the schools such as touring fees, sports fees, development fees and other incidental expenses.</p> <p>All categories of destitute persons are exempted from payment of publicly provided services such as medical fees, school fees, water charges, service levy and electricity charges.</p> <p>Burial expenses are fully covered by the Local Authorities.</p>
<p>Orphan Care Program</p> <p>Short Term Plan of Action on Care Orphans (STPA) as of 1999</p>	<p>Increasing number of orphans due to HIV and AIDS epidemics in the country.</p>	<p>Orphans understood as any child below 18years who has lost one (single parent) or two (married couples) biological or adoptive parents.</p>	<p>A food basket of P216.00 per month</p> <p>Clothing, toiletry, assistance with educational needs, and counselling and even protection from abuse</p> <p>Free medical fees in government health facilities, transport allowance</p>

Program	Rationale or objective	Eligibility and coverage	Benefits
		Children who are abandoned or dumped by their parents who can no longer be traced	and assistance with bills for utilities such water and electricity
Vulnerable Group Feeding Programme, 1966	The programme's aims at distributing meals and nutritional supplements to people who are vulnerable to malnutrition and women of child bearing age from poor or low income households	Pregnant and lactating mothers, nutritionally at risk under-fives and Tuberculosis patients	Supplementary feeding for under five Food rations for lactating mothers Coverage varies depending on whether or not there is a drought
School- Based Food Program	To provide prepared food to children to alleviate short term hunger thereby enhancing classroom learning	Urban and rural schools throughout the country	
Universal Old Age Pension, 1996	The major objective of the scheme is to provide financial security to the elderly citizens who otherwise are without means of support due to the disintegration of the extended family support system	Botswana citizens 65 years old and over. Mentally ill or Botswana citizens that receive another pension or live outside the country are also entitled Elderly in prison are not entitled	P166 monthly, adjusted for inflation each year.
World War II Veterans Allowance, 1998		World War II veteran or surviving spouse/s or child or children under 21 years of age	Monthly allowance
Labour Based Drought Relief Program, 1960	-Provision of temporary supplement to rural incomes through wage employment for the most affected by drought -Maximizing employment opportunities under the scheme -Creating a socially useful or productive infrastructure -Maximizing participation of rural communities in the identification of meaningful projects.	Any person or household that has lost its livelihood because of drought	A daily rate of P10.00 is given to each participant. Supervisors on the other hand receive P16.00
Program for Remote Area Dwellers, 1970s.several reviews of the program	To improve living conditions of remote area dwellers (Basarwa/Bushmen) who live in far and arid parts of western Botswana where there is very little economic activity	Same conditions of other social programmes apply	Social security benefits as described above (old age pension, orphans, etc) and the Economic Promotion Fund (EPF), a programme to create employment for remote area dwellers
HIV-AIDS related programs, 2004	HIV and AIDS incidence and prevalence is high and severely affect the country. In 2009, roughly 300,000 persons were living with HIV and AIDS or 25% of the population over the	People Living with HIV or relatives	Community Home-Based Care programme (CHBC) Orphan care programme National destitute programme

Program	Rationale or objective	Eligibility and coverage	Benefits
	<p>age of 18 live with that condition (AVERT¹¹ web page), the second highest prevalence rate in the world.</p> <p>The country spent \$340 million in 2008 just for HIV-AIDS response activities</p> <p>Programmes aimed at improving living standards and life expectancy of PLHIV</p>		<p>National Antiretroviral Therapy (ARV) Programme</p> <p>Private Social Assistance Schemes</p>
Source: BFTU, 2007a.			

Box 1. HIV and social protection in Botswana: The community home-based care programme

The Government of Botswana introduced the Community Home Based Care (CHBC) strategy in 1995 to provide comprehensive care services at home and at the community level in order to meet the physical, psychological, social and spiritual needs of the terminally ill, including PLHIV and their families. The Government of Botswana implements the programme jointly with non-governmental organizations and community-based organizations, and the Ministry of Health is in charge of formulating policies and protocols for professional guidance. The Ministry of Local Government, through the Department of Social Services, is responsible for the development of policies and standards for the provision of technical guidance on the social welfare component. The CHBC provides medical care, nursing care, psycho-social support, information, education and communication services for behavioural change, counselling and spiritual support. The most important means of support are:

(a) A food basket

Patients receive a monthly food basket that varies according to the condition of the patient – for example, whether or not the patient requires oral tube feeding. The cost of the prescribed food basket for patients on oral tube feeding is up to P1200.00 (about US\$157) per month.

(b) Transportation

Transportation of CHBC patients requiring medical check-ups is coordinated and managed under the programme. Vehicles purchased under the programme must be used solely for all transportation of patients.

Source: BFTU, 2007b.

4.2.2. Social protection financing and expenditure

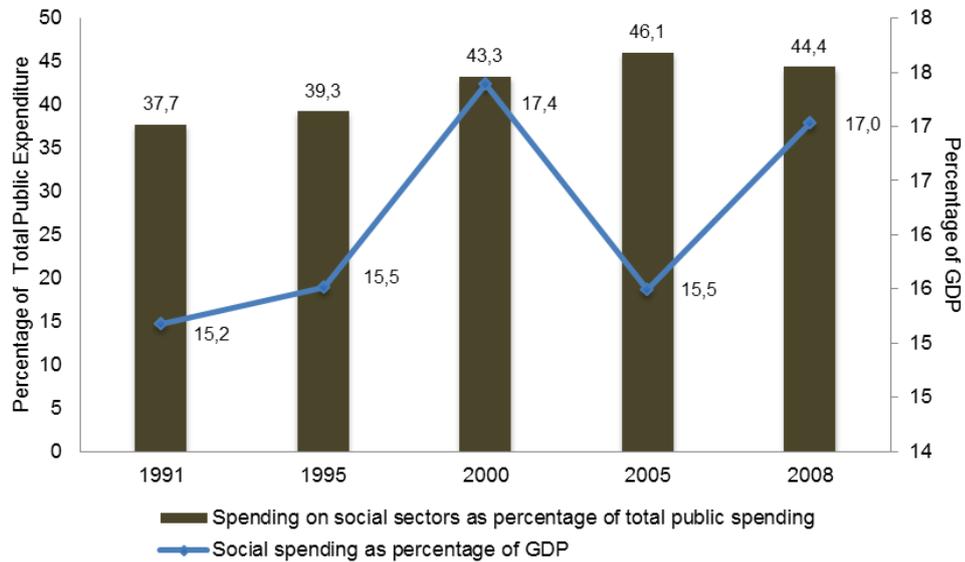
Except for the Botswana Public Officers Pension Fund (BPOPF) which is a bipartite contributory programme, social protection in Botswana is financed through budgetary allocations. The continuous surpluses and accumulation of financial reserves have allowed the country to self-finance its social policy; this is particularly important at a time of reduced ODA.

Public expenditure on the social sector in Botswana (including education, health, food and social welfare) accounted for 17 per cent of GDP in 2008, a 2 percentage point increment over the levels observed in 1991. During the same period, social spending gained considerable space in the public budget, moving from 38 per cent to 44 per cent of total

¹¹ “AVERT is an international HIV and AIDS charity, based in the UK, working to avert HIV and AIDS worldwide, through education, treatment and care”, <http://www.avert.org>.

government expenditure (figure 22). As a result, Botswana's real per capita social investment was multiplied by four between 1991 and 2008 (from US\$283.1 to US\$1,138.6).

Figure 22. Botswana: Public social expenditure as a percentage of GDP and of total public expenditure, 2000-2008

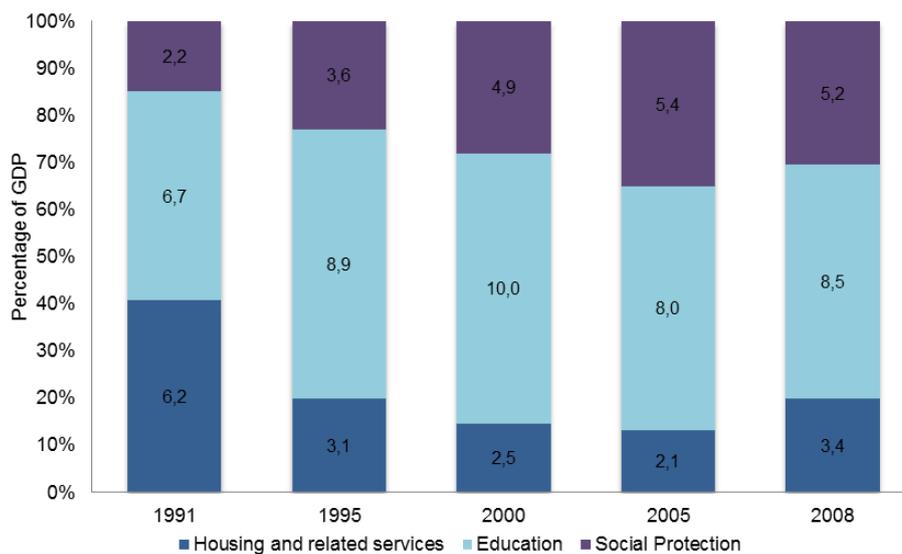


Source: Central Bank of Botswana, 2010; International Monetary Fund, 2010b.

Regarding the composition of social spending programmes, the last two decades reveal three noticeable trends (figure 23):

- a continuous decline in housing spending as a proportion of GDP;
- an up and down pattern in spending on education, which first grew rapidly between 1991 and 2000 and then decelerated until 2008. However, education accounts for the largest share of social expenditure allocations;
- a dynamic increment in the share of social protection in GDP.

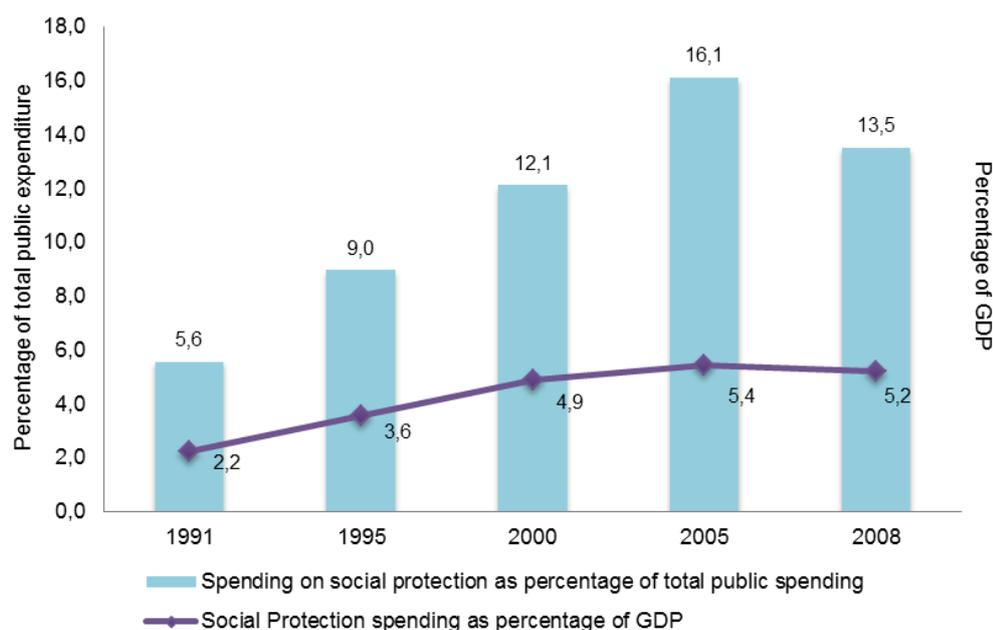
Figure 23. Botswana: Structure of social spending by sector, 1991, 1995, 2000, 2005 and 2008



Source: Central Bank of Botswana, 2010; International Monetary Fund, 2010b.

Proportionally, increments in social protection spending were much higher than increases in overall social spending. Social protection gained 3 percentage points of GDP between 1991 and 2008 and its share in total public spending increased by a factor of 2.4, from 5.6 per cent to 13.5 per cent (figure 24). In addition, real per capita spending on social protection programmes was multiplied by 5.6 between 1991 and 2008. As a consequence, expenditure on social protection accounted for an increasing share of social spending, from 14.8 per cent in 1991 to 28 per cent in 2000 and to 35 per cent in 2005 – the highest in the period. Some deceleration was observed during the following three years, and in 2008 expenditure on social protection made up 30.5 per cent of public social spending.

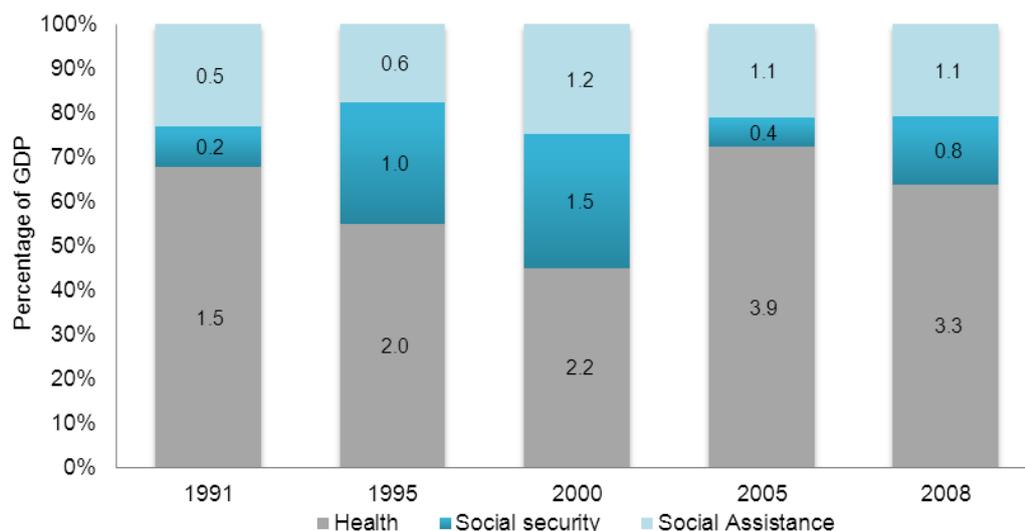
Figure 24. Botswana: Expenditure on social protection as a percentage of GDP and of total public expenditure, 1991-2008



Source: Central Bank of Botswana, 2010; International Monetary Fund, 2010b.

Regarding the composition of expenditure on social protection (figure 25), spending on health underwent a substantial increase, especially after 2005. Between 1991 and 2008 the share of health expenditure in GDP doubled and remained the biggest social protection programme. Social assistance programmes also doubled their share in GDP between the 1990s and the 2000s, but in terms of total spending they accounted for one-third of expenditure on public health activities. Finally, non-contributory social security spending, which includes old-age pensions, quadrupled its share in GDP. Estimates indicate that, with 90,639 beneficiaries receiving 220 pula (about US\$29) per month, the old-age pension programme accounts for 0.58 per cent of GDP, or 73 per cent of total expenditure on social security.

Figure 25. Botswana: Structure of expenditure on social protection, 1991-2008



Source: Central Bank of Botswana, 2010; International Monetary Fund, 2010b.

To sum up, during the last decade Botswana increased its budgetary allocations to social protection programmes. However, most of the new spending was biased towards a single sector, i.e. health, leaving the other two components (social insurance and social assistance) with reduced or zero increments during the same period.

4.2.3. Pensions

Botswana's pension system offers three different options: universal old-age pensions, pension plans for government and private employees, and voluntary occupational retirement schemes.

The universal old-age pension scheme is a non-contributory, non-means-test initiative aimed at providing financial security for senior citizens 65 years old and over. The programme was introduced in 1996 and is currently administered by the Commissioner for Social Benefits of the Ministry of Local Government. To become a beneficiary of the scheme, a person must be a citizen of Botswana, have attained the age of 65 and have a valid Omang card.¹²

Currently, the old-age pension amounts to 220 pula per month (around US\$29) and the financing of the programme is entirely covered by the Government out of its tax revenue. In the space of seven years, the number of registered pensioners increased from 84,577 in 2003 to 86,859 in 2006 and to 90,639 in 2009. According to government reports, the coverage rate is close to 95 per cent of people 65 years old and more.

There are two pension options for government employees. The most important is the Botswana Public Officers Pension Fund (BPOPF), revised in 2001 when the former scheme changed from a defined benefit scheme to a defined contribution scheme. More than 75 per cent of all pension fund members in Botswana belong to the BPOPF. The Government contribution to the Fund corresponds to 15 per cent of the payroll while

¹² "Omang" is a Tswana word for "Who are you?"

public sector staff contribute 5 per cent. Members of the BPOPF are entitled to retire at the age of 60. For government employees who did not opt to join the BPOPF, there is pay-as-you-go pension plan financed by the general government with recurrent revenues.

The third group of pensions consists of voluntary occupational retirement schemes and complementary occupational pension plans, usually established by medium-sized and large employers such as Debswana (9,000 members), the Bank of Botswana and some parastatal institutions. Under this option, employees make a monthly contribution from their salary, and this contribution is supplemented by the employer. Contributions depend on the specific rules and guidelines of each pension plan. On average, the rate of contribution ranges from 10 to 15 per cent of the salary (5 per cent from the employee and 5 to 10 per cent from the employer), but the existing regulatory framework allows contribution of up to 35 per cent.

Although in the last decade occupational pensions followed a very dynamic path, there are still large gaps in coverage. Around 40 per cent of the workers in the formal sector are members of pension funds, though membership is much higher in the public sector than in the private sector (Jefferis and Kenewendo, 2010). According to the International Organisation of Pension Supervisors, in 2009 only 16 per cent of the 300,000 private employees had an occupational pension. The coverage rate among public employees is 67 per cent. Over 190,000 workers have no pension coverage at all.

Finally, a gratuity scheme exists under which employers make cash payments on the fifth anniversary of an employee's term of employment, and similar payments at double the rate at the end of every five years thereafter. However, employers are not required to pre-fund these obligations and they often do not comply, so that the payments are not generally used to fund retirement income (Stewart and Yermo, 2009).

4.3. Considerations regarding the creation of fiscal space

By and large, Botswana has created the conditions for expanding its fiscal space in a sustainable manner. The impressive economic growth achieved since Independence has been the cornerstone for generating a material base from which to construct a better society. But growth by itself is not sufficient. The country has been able to combine rapid growth with additional elements in order for the process to be sustainable. These elements are:

- (a) *A strategic fiscal policy, particularly tax policy, to take advantage of Botswana's high monopolistic position in the international diamond market.* The Government of Botswana decided to make diamonds a profitable business for the whole nation and not just for a few. To do this it decided to formalize a win-win agreement with De Beers, allowing the company to exploit the country's diamond mines and to obtain a "normal" profit margin (non-monopolistic profit). Any revenue beyond that profit margin was collected by the Government in the form of taxes and royalties. By 2008 mineral-based taxes constituted 62 per cent of total government revenues, while mineral-related revenue (royalties, interest) accounted for 85 per cent of non-tax income.
- (b) *Prudent macroeconomic management during boom periods that allowed Botswana to generate fiscal surpluses and accumulate reserves in the long term (especially prior to 1990).* Even during long periods of strong GDP growth, the Government decided to increase expenditure within certain limits and to invest any savings in interest-generating activities. The accumulation of financial assets was used as a last resort to during the recent crisis, especially since international demand for diamonds has declined significantly in recent years.

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- (c) *Reduced debt and debt service payments.* The Government was able to reduce its external debt and debt payments in such a way that the latter constitute less than 1 per cent of current exports.¹³ This situation strengthens the fiscal position of the Government and opens up the possibility of allocating more funds to development-oriented activities.
- (d) *Declining dependence on ODA.* The country also made strategic use of international grants. During the first years after Independence, massive amounts of ODA were critical to finance public projects. As Botswana progressed and its exports grew, the country started a substitution process between financial grants and export earnings.

The result of this long-term process was an enhanced capacity of the Government to collect revenues and to expand its public spending. When compared to other African nations, revenue collection in Botswana is very much more efficient.

With regard to public spending, expenditure remained very similar in GDP terms between 1995 and 2008. By 2008 government spending was 38.4 per cent of GDP, 1.2 percentage points below the 1995 level. Fiscal policy was characterized by strict discipline and prudence, despite the rapid growth of tax revenue collection during the last three decades.

The enhanced financial capacity of the Government of Botswana was, in fact, accompanied by an increase in social spending allocations within the public budget. Although in net terms government spending remained practically the same from 1995 to 2008, social spending gained 1.9 percentage points of GDP and social protection 2.9 percentage points.¹⁴

Despite the net increments in those areas, the level of social protection can be considered low, given the relatively higher GDP per capita that Botswana enjoys compared to its closest neighbours. In comparison with other nations with a much lower level of development, such as Cape Verde and Lesotho, social protection in Botswana is substantially lower. Cape Verde, with a per capita GDP 3.8 times lower than Botswana, allocated 7.3 per cent of GDP to social protection programmes, while Lesotho, with a per capita GDP 11 times lower, assigned 9.3 per cent of its GDP to social protection during the second half of the 2000s. Despite significant gains in investment in health between 1991 and 2008, for instance, current levels of expenditure on public health in Botswana (3.3 per cent of GDP) lagged behind international recommendations (around 5 per cent of GDP). There is still considerable room for increasing social insurance and social assistance, given that public spending on both is in the range of 0.8 to 1.1 per cent of GDP. This is clearly not enough for a country where 31 per cent of the population lives below the poverty line.

In sum, the positive conditions experienced by Botswana after its Independence in 1966 created an appropriate environment for stepping up government spending. The Government took advantage of these favourable conditions and expanded revenue collection and public spending, with important allocations of resources to the social sectors. Expenditure on the social sector actually increased as a share of GDP and as a share of total spending, a reflection of strong political will. However, two important factors characterized investment in social protection:

¹³ International rating agencies usually evaluate Botswana's sovereign credit with an A.

¹⁴ Housing, on the other hand, decreased by 2.8 percentage points.

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- (a) With the exception of education (8.5 per cent of GDP in 2008), the level of investment in other social areas has lagged behind optimal levels. In the specific case of social insurance and social assistance programmes, current allocations of resources are low considering the existing poverty conditions and high GDP per capita in the country.
 - (b) The 2000s yielded a moderate performance in the creation of fiscal space for social protection.

4.4. Policy considerations and lessons learnt

4.4.1. Policy considerations

Recent economic conditions, characterized by an international crisis that led to a significant decline in demand for diamonds, have created a climate that is conducive to a review of Botswana's overall social policy. The comparison of the country's high GDP per capita with its moderate to high poverty rates provides the rationale for stepping up social protection allocations, particularly in the form of social assistance and social insurance. The experience of Botswana shows that rapid growth is not sufficient to reduce poverty, and it is therefore important to strengthen the Government's capacity to inject funds into social protection programmes. Given their current level, some of the typical fiscal space generators such as debt relief and ODA are likely to play a very limited role in the foreseeable future.

Alternative policy measures to create additional fiscal space for social protection programmes might include:

- (a) *a production diversification strategy*. The decline in fiscal taxes following the decline in diamond exports is a signal that strong dependency on a single product is undesirable in terms of economic sustainability. Certainly the country is opening up other sectors, such as tourism and textiles, but mining still accounts for 44.7 per cent of GDP (against 47.9 per cent in 2001). A review of the diamond agreement might also be considered.
- (b) *the recent increase in the value added tax* (from 10 per cent to 12 per cent¹⁵), which is seen as an excellent opportunity for raising allocations for social protection.
- (c) *the re-evaluation of existing social assistance programmes*. The current system is highly fragmented, with multiple initiatives of a non-conditional nature and very different target groups. In some cases coverage is quite low. Some programmes may remain, but the country should start thinking in terms of a different generation of public programmes, including the conditional cash transfer type. This could be an interesting option for a country that ranks 125th in the Human Development Index and where poverty affects over 30 per cent of the population. The improvement of education and health conditions demands the implementation of more cost-effective programmes to improve the living standards of the population. A more integrated strategy would also yield benefits in terms of reduced administrative costs, better coordination and improved targeting.

¹⁵ http://www.finance.gov.bw/index.php?option=com_content1&parent_id=334&id=358

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- (d) the *creation of a general social security pension scheme*. This is a solution that the Government of Botswana might wish to take into consideration as a means of expanding its fiscal space.

4.4.2. Lessons learnt

Botswana is an example of economic growth and strategic fiscal policy combining to improve the allocation of resources for social protection. Between 1990 and 2008 expenditure on social protection grew faster than any other social category in terms of both GDP and GDP per capita. Total expenditure on the social sector, however, has remained stable over time, so that the increments in spending on social protection seem to be more the outcome of reduced spending on housing and education (in GDP terms) than of an expansion in every component. Compared with neighbouring countries that have shown slower economic growth, Botswana's allocations of resources to social protection are lagging behind – although it is important to recognize the significant efforts that have been made in the last two decades.

Lesson 1

The case of Botswana shows that strategic fiscal management is essential for expanding fiscal space. This can be observed in two areas. First, the diamond agreement with De Beers was essential for the expansion and consolidation of fiscal revenue. Botswana proved that win-win strategies can be implemented in the kind of context that it enjoyed at the time and, even more important, that agreements can be re-negotiated in order to obtain more advantageous conditions. This is a good example for mineral-driven economies that decide to opt for joint ventures between the Government and the private sector to exploit their resources.

Lesson 2

The second issue is macroeconomic boom management. Instead of expanding public spending in the same proportion as revenue collection, the Government of Botswana has opted for a prudent policy of expanded spending to generate fiscal surpluses.

Lesson 3

Botswana has achieved important goals in the expansion of social protection, but more effort and political will are still required. The country has a wide and varied list of social programmes that target practically all the main vulnerable groups of its society. This is a good first step. However, the scope and coverage of some of these programmes (such as home-based care) are limited, while others (such as the orphan care programme and old-age pensions) performed according to their planned objectives (although universal coverage has still not been achieved in the case of old-age pensions). Given the serious socioeconomic problems facing Botswana and the outstanding production dynamics it has enjoyed for almost four decades, the first impression is that in the country's favourable output and fiscal circumstances additional funds should be allocated to social protection and social assistance.

Lesson 4

One may hypothesize that macroeconomic management has perhaps been too prudent. With the exception of education, Botswana's social policy lacks the ambition to expand budgets in key areas such as health and social security, both of them critical for the development of the country's human capital. This has occurred despite the fact that the share of social expenditure in total spending has risen, reflecting the existence of a strong political will but with tight limits. The most evident example of this situation is the absence of a contributory social security scheme, which could be oriented towards providing protection for the middle class, as well as to complement the current components of the social protection floor.

5. Brazil: Increasing fiscal space through social contributions

5.1. Country profile

With a population of 190 million inhabitants and a territory of more than 8.5 million square kilometres, the Federative Republic of Brazil is the largest country in Latin America; in fact, Brazil is the fifth most populous country in the world. Administratively, it is organized into a Federal District, 26 federal states and more than 5,500 municipalities. A large proportion of its territory (40 per cent) consists of Amazonian rain forest, and for this reason the country boasts the greatest animal bio-diversity on the planet. The Brazilian population is concentrated in large cities along the coast, contrasting with large uninhabited territories in the interior. Brazil is the only Portuguese-speaking nation in the Americas.

In the UNDP's Human Development Index (HDI), Brazil is in the high human development category of countries. According to UNDP data for 2000-2006 Brazil ranks 75th in the global HDI with 0.813 points, its population's life expectancy is around 73 years, the infant mortality rate is 22 per thousand and an estimated 21.5 per cent of its population lives below the national poverty line. The estimated GDP per capita in 2008 was US\$ 10,296 (PPP), one of the highest in Latin America and in 70th position worldwide.

According to the World Bank (2010), Brazil's economy is the second largest in the Americas, after the United States. Its exports are very significant globally. The country's main economic activities are agriculture, livestock, industry, mining, oil exploitation and tourism.

During the last decade Brazil was able to achieve a solid macroeconomic position, which helped to improve its resistance to the global economic crisis. These results were largely attributable to the fiscal discipline applied by the country, and generally correspond to the orientation of its economic policy. This does not mean that the situation is optimal or that reforms are not required, but at the regional level Brazil's macroeconomic performance is enviable.

According to data from the IMF and the WB, Brazil has witnessed a decline in its public debt-to-GDP ratio and a growth in its foreign currency reserves. This has increased its resilience to economic shocks and allowed for an improvement in the country's economic conditions, particularly when compared with the previous decade.

After the 2002 crisis economic reforms were aimed at improving incomes, employment, public debt, foreign currency reserves and the de-dollarization of domestic debt. Another of the highlights of Brazil's economic policy is the significant expansion of domestic demand; according to Brazilian authorities, this achievement is explained largely by the favourable development of social investment.

An equally important factor in Brazil's policy of seeking macroeconomic stability and maintaining the country's international competitiveness has been the modification in its exchange rate policy toward a floating rate, as the dollar indexation policy pursued in the 1980s and 1990s had generated great instability and exchange vulnerability.

More recently, as a result of the international economic crisis, the Brazilian economy contracted temporarily in 2009, but it subsequently recovered its growth towards 2010.

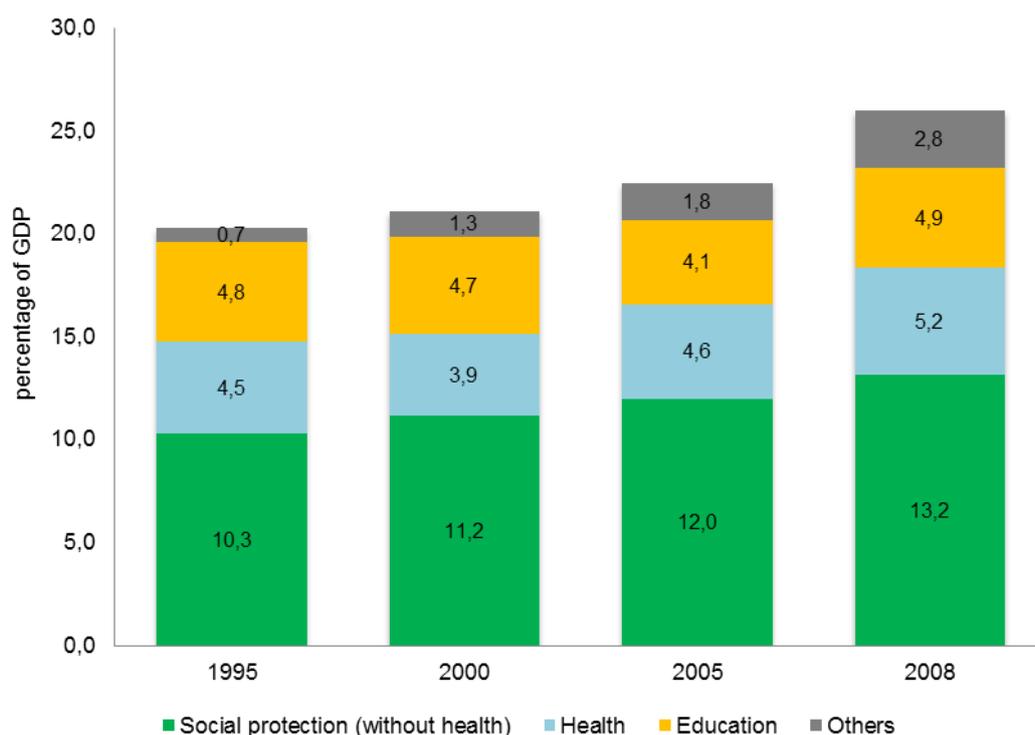
During the current economic crisis household consumption was supported by social programmes, which have been vigorously promoted in recent years. This growth in consumer spending reflects an increase in consumer confidence in relation to their current and future income. Another element that seems to be contributing to sustainable economic growth is the favourable performance of investment, thanks to a positive investment climate and good business expectations.

5.2. Social investment

Social investment plays an important role in public finances in Brazil. The social protection programmes (health, social insurance and social assistance programmes) form the largest component of social spending in Brazil, of which they account for 70 per cent. The importance of social protection in terms of its financing, coverage and protective action reflects the State's clear focus on social policy as a means of guaranteeing the people's social security rights, firmly established in the new Constitution of 1988.

Over the past 15 years Brazil's social spending¹⁶ has grown steadily, rising from 20.3 to 26.1 per cent of GDP between 1995 and 2008, an impressive gain of 5.7 percentage points (figure 26).

Figure 26. Brazil: Evolution of social expenditure as a percentage of GDP



Source: Ministry of Finance and National Treasury, 2010; International Monetary Fund, 2010b.

¹⁶ For the purposes of this analysis the definition of social spending follows that of the Economic Commission for Latin America and the Caribbean (ECLAC); its more significant components are education, health, social insurance, social assistance and housing.

As discussed in the next section, contributory social security accounts for a large part of the expansion of social spending in Brazil in terms of creating fiscal space and expenditures.

5.3. Overview of the Brazilian social protection system

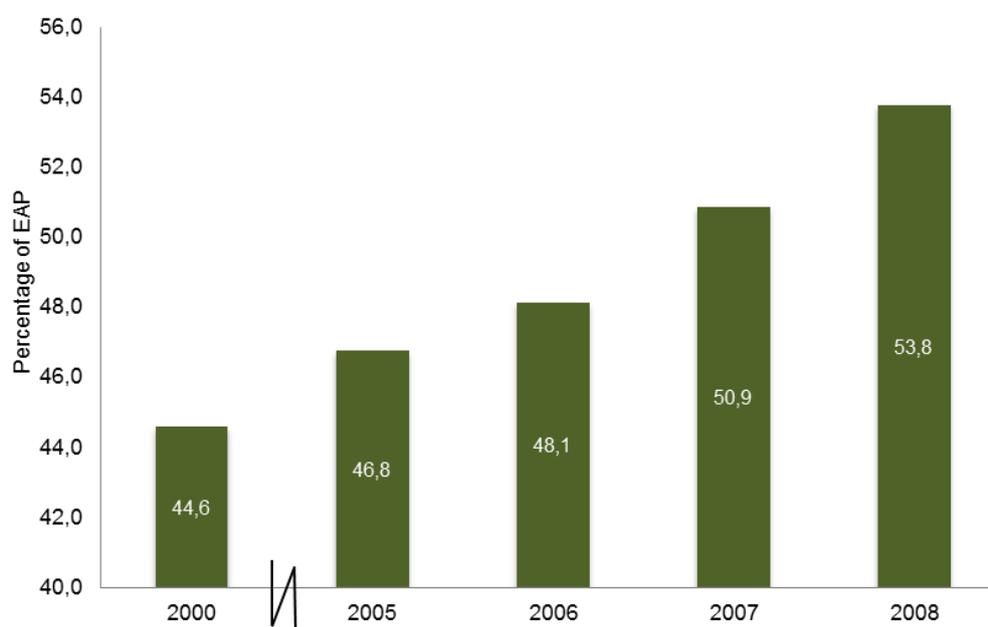
The Brazilian social protection system is one of the most highly developed in Latin America. It is organized on the basis of four main pillars: social insurance (*Previdência social*), which manages the cash benefits; the unified health system (*Sistema universal de saúde, SUS*); the social assistance programmes; and the complementary programmes. The social insurance programmes and the SUS are the most important components of the system in terms of the resources mobilized and the size of the population covered.

5.3.1. Social insurance programmes

Social insurance in Brazil combines programmes under the general scheme (*Regime Geral*) and programmes for public servants. Administration of the general scheme is the responsibility of the Ministry of Social Security and the National Social Insurance Institute (INSS), while the programmes for public servants are administered directly by social insurance bodies at the federal and local level. The protective action of social insurance programmes includes all the typical benefits of social insurance referred to in the ILO Social Security (Minimum Standards) Convention, 1952 (No. 102), except for health which is covered by the SUS.

Social insurance covers all categories of workers: salaried employees and independent workers. There is also extensive coverage of groups not traditionally protected in other countries, such as domestic servants and rural workers.

Figure 27. Brazil: Insured contributors to the pension system as a percentage of EAP



Source: Ministry of Finance and National Treasury, 2010; International Monetary Fund, 2010b.

The statistical coverage of registered contributors in relation to the labour force reached 53.8 per cent in 2008 (figure 27),¹⁷ showing a robust growth of 9 percentage points since 2000. This is one of the fastest increases in coverage recorded in Latin America over the last two decades, and it reflects the political will of the Brazilian State to implement the social security system provided for in the Constitution of 1988.

Contributory financing of social insurance, based on payroll contributions, is undoubtedly the most important factor in creating fiscal space for social protection in Brazil.

Table 7. Brazil: Evolution of the coverage of the pension system

Indicator	1995	2000	2005	2006	2007	2008
Contributory pensions, active contributors as % of EAP	47,7	44,6	46,8	48,1	50,9	53,8
Population 60 years and older receiving contributory pension (%) ^(a)	59	62,7	71,6	72,4	73	74
Population 60 years and older receiving non-contributory pension (%)	4,3	5	7,6	8	8,3	8,6
Population 60 years and older receiving pension. (%)	63,3	67,7	79,2	80,4	81,2	82,6

^a The data for 2000 corresponds to 2003.
Source: Ministry of Social Security, 2008 and 2010; United Nations Statistics Division, 2010.

Another way of measuring the coverage of the pension system is to look at the proportion of people over the age of 60 who are in receipt of pensions. This indicator, too, increased sharply during the last three decades (notably from 63.3 to 82.6 per cent between 1995 and 2008, a gain in coverage of 19 percentage points in just 13 years). Most of this increase in the number of beneficiaries is attributable to the expansion of contributory pensions by 15 percentage points (table 7).

5.3.2. Universal health system

The SUS administered by Brazil's Ministry of Health is the only national health system in Latin America with universal coverage and with comprehensive tax-funded health benefits. Its strength derives from the Brazilian Constitution of 1988, whereby health was established as a citizen's right and an obligation on the State. Today it is estimated that over 80 per cent of Brazilians are covered by the SUS, though not all of them with the same access to services in practice. Prior to this constitutional reform, only people with the ability to pay social insurance contributions had access to health care protection.

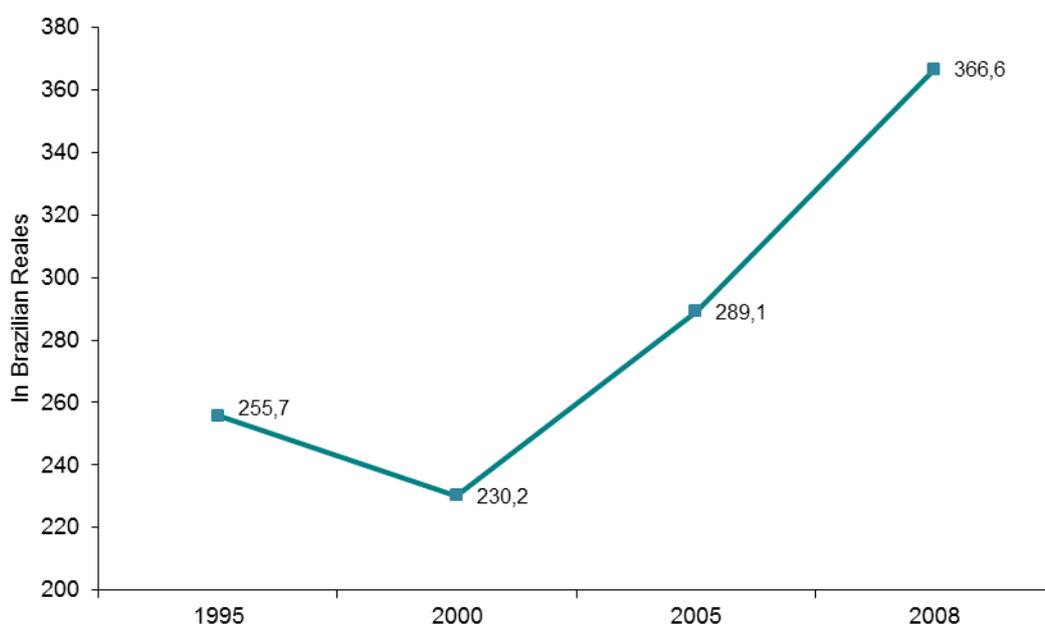
Since 1996 the administration of the SUS is under the responsibility of the municipal governments, which receive funding and technical assistance from the federal and state governments. However, the level of participation of the municipal governments, both in funding the SUS and in the provision and management of health care, are determined by the level of compliance with accreditation requirements.

SUS benefits include the three levels of health care: basic ambulatory services, hospital treatment and highly complex health care. Though theoretically coverage is universal, private spending on health care is still high, accounting in 2006 for 52 per cent of total expenditure on health (WHO, 2010a). The current legislation offers Brazilians the

¹⁷ This figure probably underestimates the total coverage of the economically active population, because it does not take into account the coverage generated through "indirect" contributions based on the value of sales by rural farmers.

opportunity to opt for private health care and complementary protection schemes. There are four means of access to private supplementary protection: private health insurance, medical cooperative plans, plans managed by hospitals, and self-managed health care plans. In practice, some of these forms of private insurance are within the financial means of the middle class only. Moreover, insurance costs rise sharply with the age of the person covered, and consequently a large part of private health expenditure takes place in the form of “out-of-pocket expenditures”. It is, however, important to appreciate the major effort made by the Brazilian government to increase social investment in health (figure 28).

Figure 28. Brazil: Real per capita public expenditure on health (R\$, 1998=100)



Source: Ministry of Finance and National Treasury, 2010; World Bank, 2010.

Thanks very largely to the creation of the SUS, Brazil's health system has been marked by a vigorous expansion in coverage and spending. Measured in per capita terms real public expenditure on health grew by 43 per cent between 1995 and 2008; however, if total expenditure is measured in real terms the increase over the period was 70 per cent.

5.3.3. Social assistance

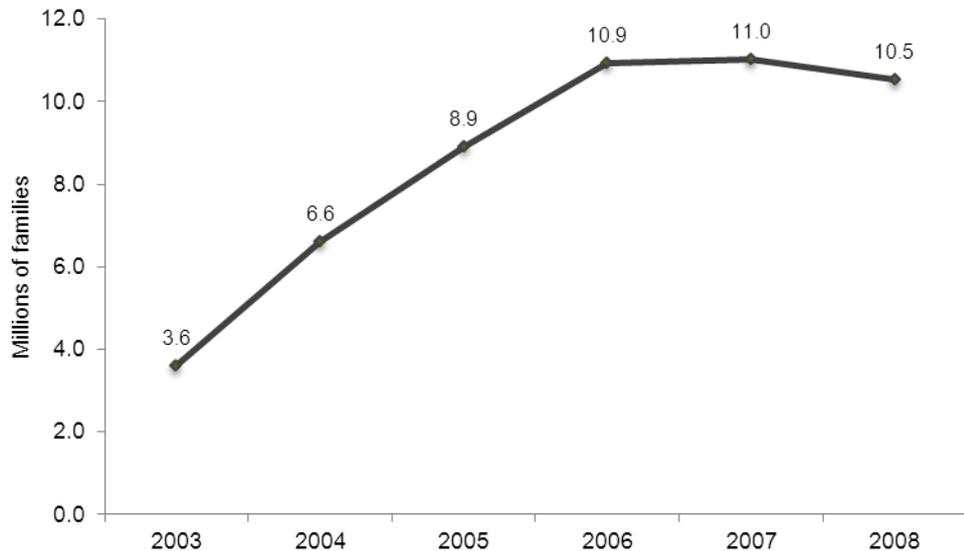
In recent years Brazil has made a great effort to develop a set of social assistance programmes aimed at protecting the family, motherhood, childhood, adolescence, the elderly and people with disabilities. Broadly speaking, the programmes focus on the most vulnerable segments of the population and are financed by the Ministry of Social Development and Hunger Alleviation (MDS).

The most prominent issue with respect to the social assistance programmes in Brazil is the horizontal level of coverage. In 2008 these programmes reached about 47 million beneficiaries, about 25 per cent of the total population, but in recent years, following the introduction of a new programme known as *Bolsa Família*, the number of beneficiaries has grown substantially (box 2).

Box 2. The *Bolsa Família* programme

Bolsa Família was launched in 2003 as a conditional cash transfer programme to support poor families. It brought together the federal Government's various cash transfer programmes aimed at meeting certain basic family needs (*Bolsa Escola*, *Bolsa Alimentação*, *Cartão Alimentação* and *Auxílio Gas*). The coverage of the programme spread quickly, from 3.6 million families in 2003 to 10.5 million in 2008.

Families benefiting from the *Bolsa Família* programme (millions)



Source: IPEADATA, 2010.

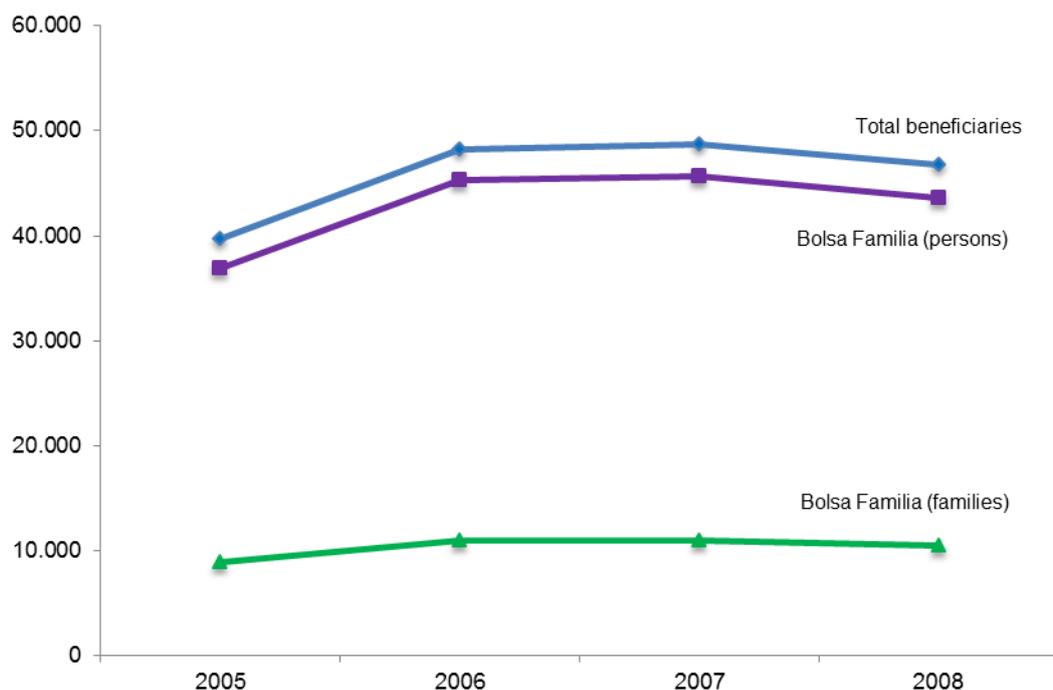
Eligibility: extremely poor families (determined on the basis of per capita household income), pregnant women or nursing mothers with children up to 12 years old, and adolescents up to 15 years of age. **Targeting:** this is done through a system of registration of poor families nationwide. Data collection and registration are the responsibility of municipalities, while the Ministry of Social Development and Hunger Alleviation centralizes the databases. The *Caixa Econômica Federal (CEF)* handles the administration and operation of the programme. **Conditionality:** coverage is subject to compliance with certain human development requirements, such as school attendance (for children between 6 and 17 years of age), vaccination (for children up to the age of 6), nutritional management, and prenatal and postnatal consultations. **Institutional organization:** the programme is administered by the National Secretariat of Income for Citizenship (SENARC) under the Ministry of Social Development and Hunger Alleviation. Decisions are taken by the President on the recommendation of a programme management committee. **Monitoring and evaluation:** municipalities are responsible for verifying compliance with the conditions for coverage, while quality control is the responsibility of the SENARC.

After a slight contraction of the programme in 2008, preliminary figures point to an increase in expenditure and in the number of beneficiaries for 2009. This was due to a government decision to increase investment in the programme in order to offset the impact of the global economic crisis. It is estimated that by 2009 the programme was benefiting 12.4 million families.

Source: Ministry of Social Development and Hunger Alleviation, 2010.

Of an estimated 47 million beneficiaries of cash transfer programmes in 2008, approximately 43 million were covered by *Bolsa Família* (figure 29). In just three years, between 2005 and 2008, expenditure on conditional cash transfer programmes, measured in real terms, grew by almost 50 per cent.

Figure 29. Brazil: Coverage of social assistance programmes (thousands)



Source: IPEADATA, 2010.

Expenditure on cash transfer programmes in 2008 was approximately 1.3 per cent of GDP, 0.4 per cent of this being implemented through *Bolsa Família*.

Recent developments

In the context of recent efforts made by Brazil to increase social protection coverage the government launched in June 2011 the “Brazil without Misery” Plan (*Plano Brasil sem Miséria*). The Plan aims to promote social inclusion and "productive inclusiveness" of 16.2 million people living in extreme poverty. Much of this population does not participate in any social protection programme. This operation is managed by the Ministry of Social Development and Hunger Alleviation which coordinates with other federal agencies and performs partnerships with the private sector. The programme operates at federal, state and municipal levels. The Plan seeks to increase per capita household income, improve access to public services and increase "productive inclusiveness", improving the economic means of Brazilians through job creation.

The increase in household income is ensured by the *Bolsa Família* Programme and BPC pension (*Benefício de Prestação Continuada*). The Plan expands the scope of the *Bolsa Família* Programme by increasing the number of eligible children per family from three to five. The government seeks to extend benefits to an additional 1.3 million children. Payments will range from USD 22 to USD 200 a month. The government hopes to reach an additional 800,000 families who qualify for but currently don't receive the benefit due to a lack of information, isolation or administrative problems. The BPC pension is a constitutional right which provides income security (one minimum wage) to poor elderly and disabled people.

Access to public services is ensured by integrating programmes on education, social assistance, food and nutrition security, healthcare, running water and electricity. In the field of education, the Plan integrates programmes which offer literacy courses for young people and adults as well as activities in different areas in public schools. In the field of healthcare are included the Unified Health System and programmes focusing on family

health, school health, promotion and prevention of oral health and medicine delivery. Social assistance and food and nutrition security include the Social Assistance Reference Center, Specialized Social Assistance Reference Center and programmes such as food bank and food at school.

The "productive inclusiveness" is ensured in rural areas through technical assistance, support access to public and private markets, building cisterns and the Green Grant Programme (*Bolsa Verde*) which transfers USD152 per three months (by *Bolsa Família* card) to families registered in the Support for Environmental Conservation Programme. In urban areas, the government seeks "productive inclusiveness" through vocational training and job creation. Its goal is the inclusion of *Bolsa Família* beneficiaries in the labour market.

The target population is identified by an "Active search" based on poverty maps. Families' registration is done at local level using the Unified Registry for Social Programmes of the Federal Government (*Cadastro Único para Programas Sociais*). This mechanism collects socio-economic information about families in poverty (household characteristics, education level, employment status and income level). The families which qualify for but currently don't receive benefits from any social protection programme are identified and included in various programmes according to their needs. Families already registered are automatically included in the Plan, and must also meet the criteria for participation. The government has budgeted about Reales 20 billion annually to finance the Plan. This budget includes *Bolsa Família* funds. This annual budget is covered through 2014.

Although the number of families and individuals receiving conditional cash transfers is considerable, the same cannot be said of the volume of expenditure of these programmes especially when compared with the level of total investment in social protection, which reached 18 per cent of GDP in 2008.

This suggests that, even though expenditure on social assistance programmes in Brazil experienced a significant increase in recent years, it is still far below the level of spending on other social protection programmes, such as health and social insurance.

Social insurance programmes are currently the main beneficiaries of spending on social protection and, in terms of the revenue they generate, they have in recent years been the main creators of fiscal space in the country.

5.4. Fiscal space for social protection

As we have seen, Brazil's social spending, especially its social security expenditure, has increased considerably over recent years, with a strong acceleration during the 2000s.

This scenario raises two questions. What were the sources of financing that were used to cover the growth in expenditure on social protection? How was this related to the mechanisms for creating fiscal space?

5.4.1. The 1988 Constitution and fiscal space

The new Constitution introduced explicit guarantees with regard to the Brazilian people's right to social security. This is very positive in terms of the government social protection policy's compliance with the provisions of the main international instruments protecting human rights: the Declaration of Philadelphia, the Universal Declaration of Human Rights and the International Covenant on Economic, Social and Cultural Rights.

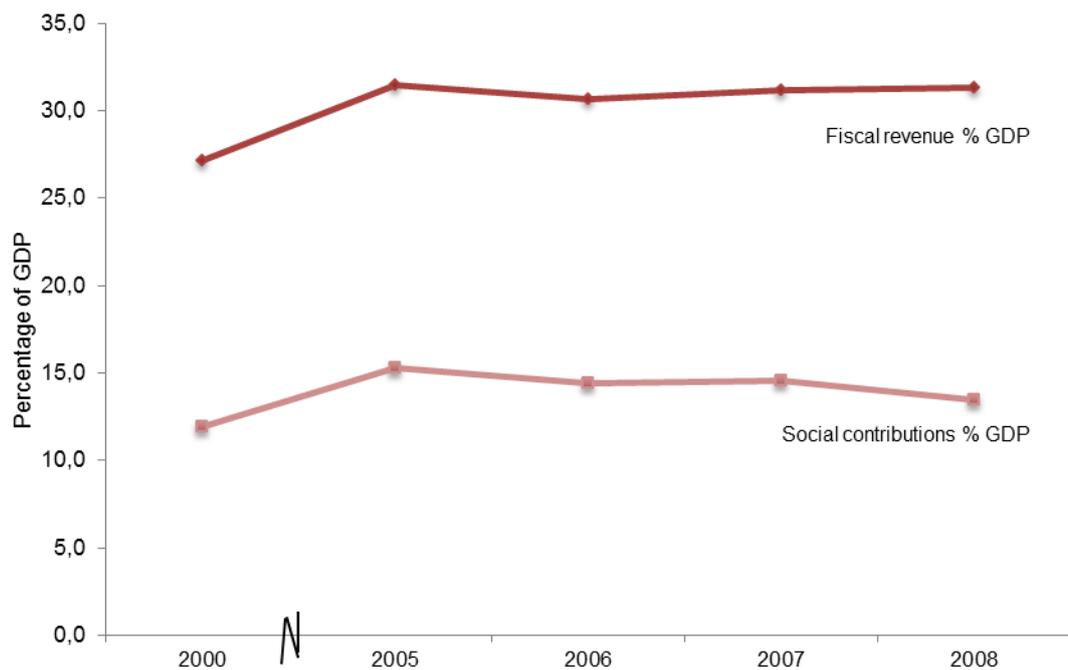
A direct consequence of the progressive consolidation of this framework of rights was the very substantial expansion of the State's obligations compared to the country's minimum level of spending on social protection in the past. This in turn posed a challenge in terms of fiscal sustainability because of the rigidity in fiscal management that normally is associated with the commitments to pay contributory benefits. This issue will be addressed later in this chapter.

5.4.2. Gross tax burden: The role of social contributions

In accordance with the definition proposed by the United Nations, the Brazilian Institute of Geography and Statistics (IBGE) divides taxes into five categories: taxes on products, other taxes linked to production, taxes on income and property, social contributions, and taxes on capital. These are the components that constitute Brazil's gross tax burden, usually expressed in terms of GDP.

Santos and Costa (2007) have documented the increase in Brazil's gross tax burden from 27 per cent in 1996 to almost 31 per cent in 2006. This is without doubt one of the biggest increases to have occurred in Latin America, and it places the country in a privileged position compared with the rest of the developing world. The remarkable expansion of the tax burden is largely attributable to changes in social contributions, which as defined in Brazil go beyond social security contributions to include other components as well.

Figure 30. Brazil: Fiscal revenue (including social contributions) and social contributions, as a percentage of GDP



Source: Ministry of Finance and National Treasury, 2010; International Monetary Fund, 2010b.

Total tax revenues, including social security contributions and other social contributions such as the *Contribuição "Provisória" por Movimentação Financeira* (CPMF), a temporary or interim tax on financial transactions, expanded greatly between 2000 and 2005.

Brazil's tax structure is marked by a strong presence of social contributions, in which social insurance payments are the main component. As can be seen from figure 30, almost half of the State's fiscal revenue comes from social contributions.

The introduction in 1997 of a temporary tax based on financial transactions as a form of social contribution (the CPMF) was an interesting attempt to draw resources from the formal economy in order to finance social spending targeted at the poorest segments of the population. Most of the revenue from the CPMF was used to finance non-contributory programmes.

The relative weight of social contributions in public finances is also apparent in other developing countries. In Latin America, Chile, Colombia, Costa Rica, Mexico and Uruguay head the list of countries where social security contributions make up a substantial proportion of public finance and social investment for development. In Africa, Tunisia is another example, where social security contributions stand at around 5.6 per cent of GDP and contribute about 30 per cent of total tax revenues.

This is very important for understanding the role of social security institutions in the creation of fiscal space, even in developing countries.

In countries with a lower level of development, as is the case of most African economies, social insurance is still at an embryonic stage and, if this situation does not change, their social protection systems will continue to rely heavily on non-contributory financing – and, in some African countries, perhaps also on direct foreign aid. However, this is no reason to renounce efforts to establish social protection systems financed by social contributions. On the contrary, it should serve as an encouragement to continue developing social protection in the long term, with the idea of combining a capacity to create fiscal space based on social insurance systems with general taxation to finance non-contributory programmes. Given the experience of Brazil and other middle-income economies, one focus of the discussion on creating fiscal space in low-income economies should be on innovative ways of collecting public resources so as to generate some degree of income redistribution.

5.4.3. Rural pensions

Rural pensions are just such an innovative tool for extending coverage to rural populations in Brazil. The country's social assistance scheme was set up in 1971, when it was known as FUNRURAL. The 1988 Constitution subsequently changed the method of financing and administering the programme. By means of this innovation, Brazil had by 2007 managed to incorporate it into the special insurance scheme (*Segurado especial*) aimed at small rural producers and over 80 per cent of rural employees,¹⁸ a remarkable social security indicator for Latin America.

Since 1991 producers, partners, sharecroppers, tenants and fishermen working for family businesses with no permanent employees contribute to social security at a rate of 2.1 per cent on the gross income earned from marketing their products. Under this scheme retirement pensions equal to the minimum wage are paid from the age of 60 for men and 55 for women. The benefit is conditional on having engaged in a rural activity for at least 15 years. In 2008 the scheme was the subject of special legislation.

Between 1992 and 1994, Brazil's rural social insurance legislation had a great impact on the expansion of the country's fiscal space and social insurance coverage (IPEA, 2007).

The special insurance scheme established under the legislation receives a very substantial volume of state subsidies, estimated at about 85 per cent of total expenditure; the benefits

¹⁸ Cited in Cabanas, 2008.

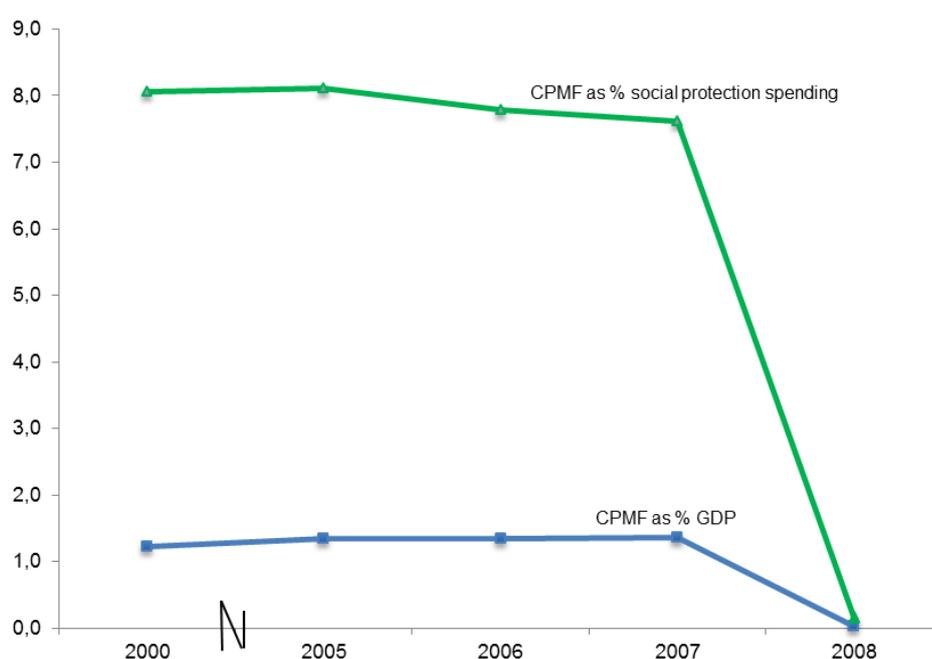
paid under it can therefore be said to be semi-contributory in nature. Such an innovation in the method of financing must be looked at carefully from the standpoint of its capacity to create fiscal space, contrasting as it does with the situation in most developing countries where benefits aimed at the rural population, if they exist, are funded under a non-contributory system. In Brazil, the collection of contributions based on the sales value of production allows the State to finance a portion of the cost of the social protection. This mechanism is also very attractive to economists who are opposed to social contributions based on earnings, since the tax base here is the value of sales of agricultural products. However, the scheme can also be criticized, on the grounds that this kind of direct taxation implies a significant degree of regression.

5.5. Temporary tax on financial transactions

The CPMF tax was levied in Brazil from 1997 to 2007, when it was repealed in a heated political controversy. The contribution took the form of deductions from accounts held by financial institutions.

The maximum value of the CPMF quota reached 0.38 per cent of the value of financial transactions. For accounting purposes and because the CPMF was designed mainly to finance social protection expenditure, the mechanism was classified as a "social contribution".

Figure 31. Brazil: CPMF as a percentage of social protection expenditure and GDP



Source: Ministry of Finance and National Treasury, 2010; International Monetary Fund, 2010b.

Although many were opposed to the scheme, the CPMF managed to survive for ten years¹⁹ and played an important role in financing several major components of social protection

¹⁹ The CPMF in fact existed previously under a different name.

expenditure. During the period in which the tax was applied, 42 per cent of the revenue collected was used for the public unified health system (SUS), 21 per cent for social insurance, 21 per cent for the *Bolsa Família* and 16 per cent for other social purposes.

By 2007 the total revenue of the CPMF was the equivalent of 1.4 per cent of GDP (figure 31), enough to cover the total cost of *Bolsa Família* and other non-contributory social protection programmes. In terms of social protection expenditure, between 2000 and 2005 the CPMF came to account for more than 8 per cent of total expenditure on social protection, which shows just how important it was in financing social protection.

Where it is not possible to increase direct or indirect tax revenue sufficiently to generate necessary fiscal space, a tax on financial transactions has several advantages. In the first place, it is relatively easy to implement and monitor because it works within regulated and supervised institutions, which is the case of most developing countries. Secondly, it covers everyone, even agents who are able to pay and who thus evade payroll contributions. Thirdly, it is a fiscal control instrument that allows cross-checks to be made with information on financial transactions throughout the economy. Fourthly, it allows resources to be channelled directly from the formal economy, with a high progressive component. This is especially important considering that most developing countries have a highly regressive tax structure which relies primarily on indirect taxes. Under these circumstances, the introduction of a tax on financial transactions to finance pro-poor social spending is an interesting innovation.

The main argument raised against the CPMF by its opponents is that it introduces a distortion into the financial market and discourages the development of banking, and that it can thus have a negative impact on the efficiency and growth of the economy. There is, however, no empirical evidence to support this claim.

In January 2008 two measures were announced to neutralize in part the loss of tax revenue caused by the disappearance of the CPMF. First, the rate of the social contribution on net income (CSLL) paid by financial institutions was increased from 9 per cent to 15 per cent. Secondly, a tax increase was decreed on credit operations and on currency transactions and insurance. The increase in revenue from these measures was estimated at US\$10 billion (Banco Central do Brasil, 2008).

5.6. Fiscal space, economic growth and development

With the Brazilian currency crisis of the late 1990s, domestic shocks coming from the power rationing crisis of 2001 and uncertainty as to the future economic policy of the newly elected President Lula in 2002, the Brazilian risk premium rose above the average on the Emerging Markets Bond Index.²⁰

That scenario was offset by the fiscal adjustment policies initiated during the period, which resulted in a reduction in the country's risk indicators and in an improvement in its public debt situation and fiscal position.

The main instrument employed in Brazil to generate primary surpluses was the increment of the tax burden. During the 1970s and 1990s the tax burden remained around 25 per cent

²⁰ The Emerging Markets Bond Index (EMBI) is a country risk indicator based on the behaviour of the foreign debt incurred by each country. As the certainty of compliance with sovereign debt obligations increases, so does the EMBI rate.

of GDP, but after 1994, with the implementation of the *Plano Real*,²¹ the tax burden on goods and services increased.

Brazil's favourable macroeconomic and fiscal situation, supported by the good performance of exports, allowed it to accumulate a significant amount of international monetary reserves and ultimately, in terms of its fiscal burden, to reduce the external public debt. As a percentage of GDP, Brazil's foreign debt turned negative from 2006 onwards, making the country a net external creditor for the first time in many years.

In terms of the country's fiscal position, the current surplus on general government account (general revenue less expenses) reached 2.9 per cent of GDP in 2008, its highest value in Brazil's recent economic history.

Government policy with regard to the increased funding capacity of public expenditure can be assessed in the light of the concept of fiscal space. Under the traditional definition of fiscal space, the significant increase in tax revenue experienced by Brazil, including social security contributions is regarded as a genuine creation of fiscal space only if it does not jeopardize fiscal sustainability and macroeconomic stability.

A fundamental question here is the time horizon within which the impact of fiscal expansion at the macroeconomic level is evaluated, particularly with respect to the potential for sustained economic growth.

In the case of Brazil, government reports and the IMF have highlighted the country's prosperous fiscal and macroeconomic situation, even in the context of a global financial crisis. In 2008, at the most critical point of the international economic crisis, the Brazilian economy grew by over 5 per cent in real terms, positioning itself as one of the few economies in the world with a high growth rate. More recently, after a decline in growth in 2009, the projections of the Government and of some international organizations (ECLAC and the IMF, for instance) point to a significant recovery of economic growth from 2010 onwards.

During the recent international financial crisis, the Brazilian monetary authority documented the fact that private consumption and investment had contributed substantially to GDP growth in 2009 – 2.4 and 1.9 percentage points, respectively. They argued from this conclusion that the favourable trend in private household consumption was supported by the expenditure of social assistance programmes, as well as by the relative stability of the labour market. For its part, investment became a key factor in sustaining the process of economic growth.

No doubt the economy of Brazil has revealed strengths in important areas to economic growth, and these were put very much to the test during the global economic turmoil of recent years.

One might question, however, whether one of the Brazil's greatest strengths – namely, its tax collection capacity, which allows the country to impose a tax burden comparable to the average in OECD countries – might not in the medium and long term prove to be too heavy a burden on economic agents and an obstacle to growth. This issue is part of an ongoing debate, often marked by ideological convictions, that has so far led to no clear conclusions. That said, the Brazilian authorities and specialists in the field of taxation have

²¹ The Plano Real was a package of economic measures aimed at stabilizing the Brazilian economy in early 1994.

referred to the need for a significant structural reform of the current tax model, regarding whose complexity and fragmentation there appears to be broad agreement.

Aboal et al. (2009) refer to the importance of the composition and efficiency of public expenditure in creating fiscal space in Brazil, noting that the rules governing the operation of the pension scheme and the entitlement to benefits have given rise to a certain lack of flexibility in the structure of government spending, since total expenditure on pensions averaged about 11 per cent of GDP between 2000 and 2008 and 68 per cent of primary expenditure by the central Government; specifically, spending on INSS benefits grew to 7.26 per cent of GDP in 2007. For the authors of the research, the rigidity of these components of expenditure means that in the current institutional climate the ability to generate fiscal space for growth is quite small, and that the potential for improving Brazil's fiscal situation lies in the modification of capital items, especially education and public investment.

Aboal et al. (2009), in a comprehensive study of fiscal space in the Southern Cone (Argentina, Brazil, Chile and Uruguay), concluded that in recent years there had been an expansion of fiscal space for policy-making and that the region was now in a relatively favourable situation. This in turn extends the planning horizon for policy design, by reducing the threat of unsustainable debt. The authors added, however, that the improvements observed did not result in an "immediate extension" of fiscal space for growth.

It should be noted that, although Aboal et al. provide extensive evidence of fiscal developments in Brazil, their findings with respect to the creation of fiscal space are based on immediate results, rather than on the overall implications in the medium and long term. Thus, they argue that, so long as the tax pressure grew, it was possible for growth-related expenditure to increase only partially, owing to the rigidity of other components of expenditure that influenced the surplus and prevented it from rising automatically along with increased taxation.

5.7. What about creating fiscal space for development?

Whether or not the increase in the tax burden and fiscal intervention in Brazil corresponds to a genuine expansion of fiscal space can be evaluated by the approach employed by the UNDP. According to the UNDP approach, the evaluation should consist more of an analysis of the impact of such measures in the medium and long term. Therefore, the main criteria to be applied would revolve around the appropriate balance between fiscal discipline and the effectiveness of expenditure in the accumulation of productive capacity, in terms of the stock both of physical and of human capital.

By their very nature, the attainment of the MDGs and the establishment of a welfare society in general must be intrinsic goals of a sustainable development policy. That being so, we shall now analyse some of the variables related to development objectives.

Investment in education has expanded significantly in Brazil over the past years, in both real and per capita terms. Between 2000 and 2008 real expenditure on education rose by 36 per cent, while in per capita terms the increase was 24 per cent. The expansion of investment in health was significantly greater, since during the same period real spending on health grew by 75 per cent, while per capita expenditure was up by 60 per cent.

This investment has had a direct impact on the quantity and quality of available human resources. At the same time it has meant an increase in the country's productive capacity, for three reasons: (i) the reduction in mortality and the growth of the economically active population; (ii) the increased productivity of labour thanks to improvements in health; and

(iii) the increased productivity of labour resulting from improved training of the workforce, generated in turn by an increase in school attendance. The sum of these effects should be reflected in the medium and long term, perhaps over a time horizon of 15 years or so, by an increase in the aggregate income of households and, therefore, by an expansion of domestic demand for consumption and investment.

While the repercussions of better health and education on families' income levels have been extensively studied, their ultimate impact on economic growth has not. This is of course a highly complex quantitative issue, mainly because of the interrelationships between the variables concerned, which quantitative models are not able to capture with any degree of accuracy.

Studies by Pochmann (2007), Lavinás (2007) and Soares et al (2006), together with data from household surveys conducted in 2004 and 2006, show that Brazil's socioeconomic indicators improved and that progress was made in reducing absolute poverty and inequalities in income distribution. According to ECLAC the poverty rate in Brazil fell from 38 per cent of the population in 2002 to 28 per cent in 2007 (UNDP, 2008).

According to Paes de Sousa (2010), 19.4 million Brazilians have overcome extreme poverty in the last decade and in 2008 the extreme poverty rate was one-third that of 2001. The same report shows that Brazil was able to reach one of the MDGs a decade before the scheduled date and has established stricter targets for poverty reduction. In terms of reducing inequality between 2001 and 2008, 10 per cent of the low-income population increased their income by six times more than did the 10 per cent of those earning the highest incomes (IPC-IG, 2008).

The quality of social spending, in terms of its efficiency and effectiveness, is critical for creating fiscal space, and it serves as a useful criterion for analysing fiscal policy in Brazil over the two decades since the 1988 Constitution. The impact of social spending has been very noticeable in areas that are critical for the sustainability of economic growth. Besides the improvements in the country's poverty indicators already referred to, there has been an increase in the coverage and performance of the educational system. The illiteracy rate among Brazilians aged between 15 to 17 years decreased from 8.2 per cent in 1992 to 1.7 per cent in 2007, and the average years of schooling for people aged 15 years and over increased from 5.2 to 7.3 years (from 2.6 to 4.5 years in rural areas) during the same period. Between 2000 and 2008 the size of the population benefiting from social insurance grew by 9 percentage points, a clear indication that workers are moving from the informal to the formal sector of the economy. Benefits paid under the social assistance system were extended to almost 50 million people, from an initial base of 2 million in 2000. However, despite the strong health system restructuring process experienced by the sector (including the strengthening of health promotion and prevention programmes, as in the “*Saúde da Família*” Programme and the universalization of health access through the SUS), private expenditure on health is still considerably high in Brazil. Some of the more recent measures adopted by the Government in response to the economic crisis which are expected to have a medium- to long-term social impact include substantial increases in the Continuous Cash Benefit Programme (*Benefício de Prestação Continuada*), the maintenance of the investment schedule under the Growth Acceleration Programme (Programa de Aceleração do Crescimento), which is seen as playing a key role in the creation of jobs in the formal sector, and the pursuit of social infrastructure projects in rural areas (power supply, housing and sanitation) that are recognized sources of growth for the economy.

In conclusion, fiscal intervention supported by a significant increase in state funding seems so far to have been altogether compatible with Brazil's goals of economic growth and development. Brazil is certainly one of the few countries in Latin America, and perhaps in the developing world, whose experience in increasing the tax burden has been successful,

and this has undoubtedly played a key role in supporting the country's economic growth policies and in financing social security and social spending. However, while Brazil's macroeconomic indicators over the last decade speak well of the responsible management of the tax issue, this is no reason to disregard opportunities to revise the tax system, as has been suggested by various experts and institutions.

5.8. Lessons learnt

Lesson 1

Innovation aimed at expanding fiscal space through increases in contributions can generate very significant returns. Brazil's innovations comprise both fiscal instruments and social policy. From the standpoint of the social protection system, the most important innovations include: the introduction of the rural pension scheme; the use of taxes on financial transactions to generate funding from the formal economy, mainly to support the extension of social protection; improvements in the administrative and institutional framework of the collection system; measures to facilitate and increase tax coverage and social protection coverage in micro and small enterprises.

Lesson 2

Efficiency of social expenditure management does matter. It is possible to create fiscal space through the review of programmes and of institutional and administrative mechanisms. Reforms in the organization of social transfer programmes, in terms both of their structure and of the tools and criteria for the allocation of resources to generate some selectivity and progressive incentives (such as the renovation of educational programmes and the *Bolsa Família*), can be an effective means of creating fiscal space. In Brazil these reforms were very important for extending the coverage of the universal health scheme and, at the same time, ensuring more effective social investment. The Brazilian experiences in integrated universal health care, in its education system indicators and in its social assistance coverage, are significant in terms of their impact on poverty reduction and capital accumulation.

Lesson 3

Fiscal and macroeconomic discipline does matter. Brazil has been able to achieve a great degree of macroeconomic stability, which relies heavily on the effect of social programmes on the demand for domestic consumption. However, these achievements are to a very large extent attributable to the Government's responsible management of its monetary and fiscal affairs. The management of the country's external debt and of the external sector of the economy has been a key element in the creation of fiscal space – so much so that the Brazilian economy has become a foreign creditor.

Lesson 4

Social protection can leverage the formalization of the economy while at the same time generating fiscal space for growth. The classic idea that social security contributions generate distortions in the labour market and increase informality is not borne out by the experience of Brazil. In Brazil much of the increase in state revenues is attributable to increases in social security contributions, which explains the remarkable expansion observed in contributory social insurance coverage in recent years. More specifically, the strong positive development of social security registration rates is a clear reflection of a process of labour formalization. Of course, this mechanism does not operate alone; it requires instrumental and administrative reforms as well, to encourage and even oblige enterprises to adhere to the social insurance scheme while at the same time making it easier for them to do so. In terms of growth and macroeconomic stabilization, the overall

gains from direct investment in social protection appear to be very considerable in Brazil's experience – much greater than simple quantitative models seem able to explain. The gains are notable in terms of human capital, productivity, a stronger sense of citizenship, social cohesion, political stability and a good investment environment, inter alia.

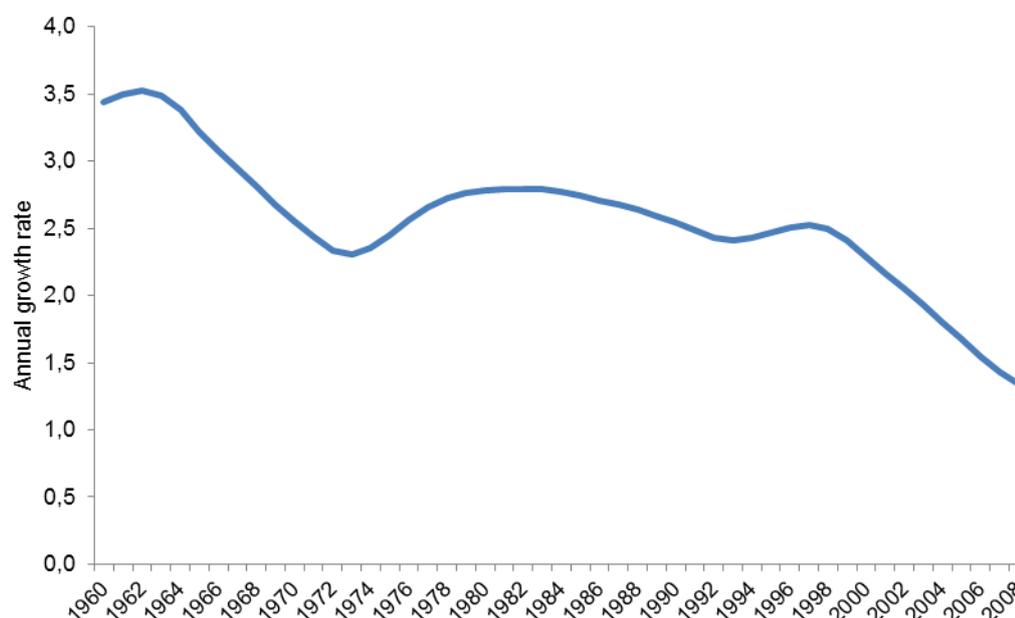
6. Costa Rica: Prioritizing fiscal space for social protection

6.1. Country profile

Costa Rica is a small country of Central America with a total surface area of 51,100 square kilometres. It borders Nicaragua to the north, the Pacific Ocean to the south and west, Panama to the south-east and the Caribbean to the east. It is usually considered the most solid democracy of Latin America. Its army was abolished in 1948. Costa Rica is a Republic with a four-year presidential mandate.

The total population of Costa Rica was estimated at 4.5 million inhabitants in 2010. During the last decade, the annual population growth rate averaged 1.7 per cent, with a clear declining trend since 1982 when population increased by 2.8 per cent (figure 32). In other words, the current population growth rate is almost half the 1982 rate and almost 60 per cent lower than in 1962.

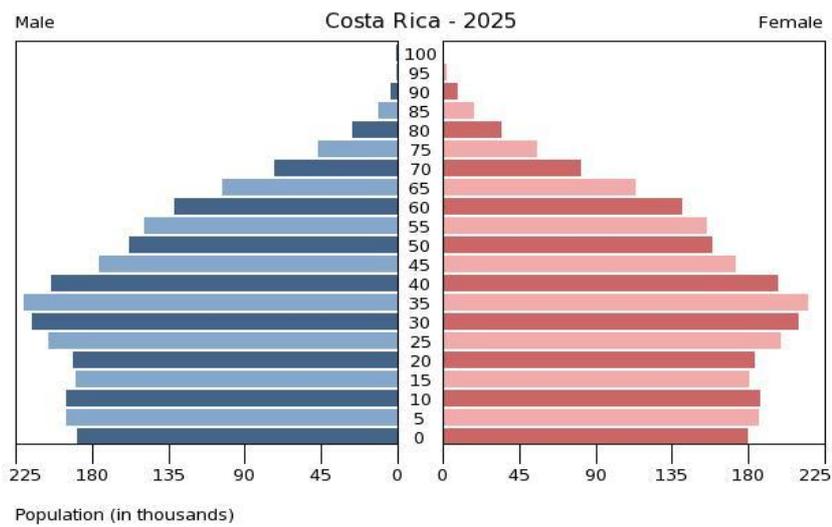
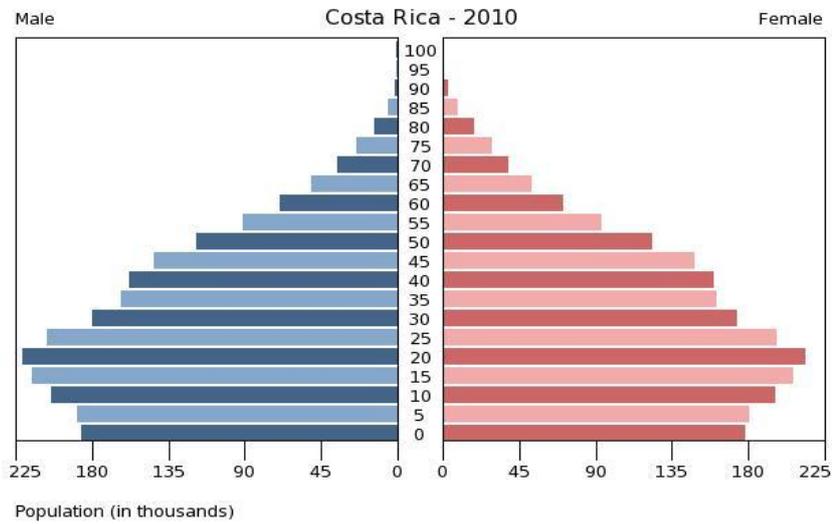
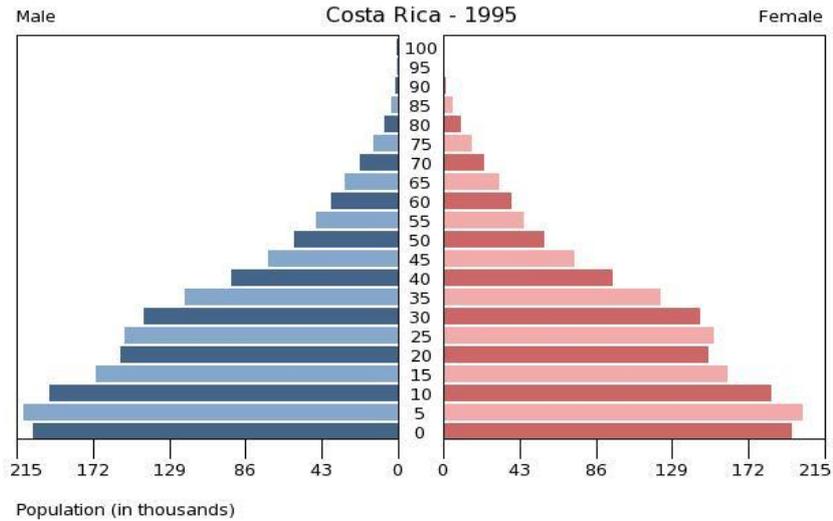
Figure 32. Costa Rica: Population growth rate, 1960-2010



Source: United Nations Population Division, 2010.

The combination of a low birth rate and increasing life expectancy has accelerated the ageing of the population. Between 1995 and 2010 the share of people over 65 years old jumped from 4.7 per cent of the total population to 6.2 per cent, a trend that is expected to speed up over the coming years so that by 2025 one out of ten Costa Ricans will be over 65 years of age. On the other hand, children below the age of 14, who used to make up 34.7 per cent of the total population in 1995, account for 25 per cent in 2010, with a projected share of 21 per cent in 2025 (figure 33).

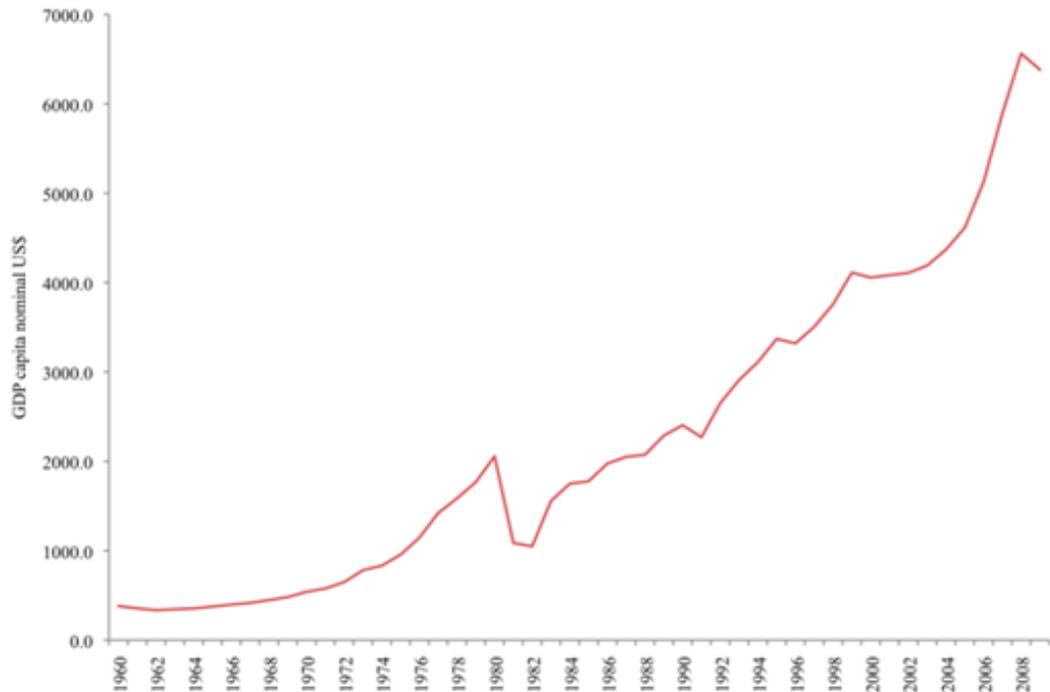
Figure 33. Costa Rica: Population pyramids, 1995, 2010 and 2025 (projected)



Source: US Census Bureau, 2010.

Costa Rica's GDP per capita (figure 34) was estimated at US\$6,382 in 2009 (US\$11,122 in terms of purchasing power parity), the second highest in the Central American region after Panama and 4.2 times the GDP per capita of Nicaragua (the Central American country with the lowest income in PPP terms).

Figure 34. Costa Rica: GDP per capita, 1960-2008

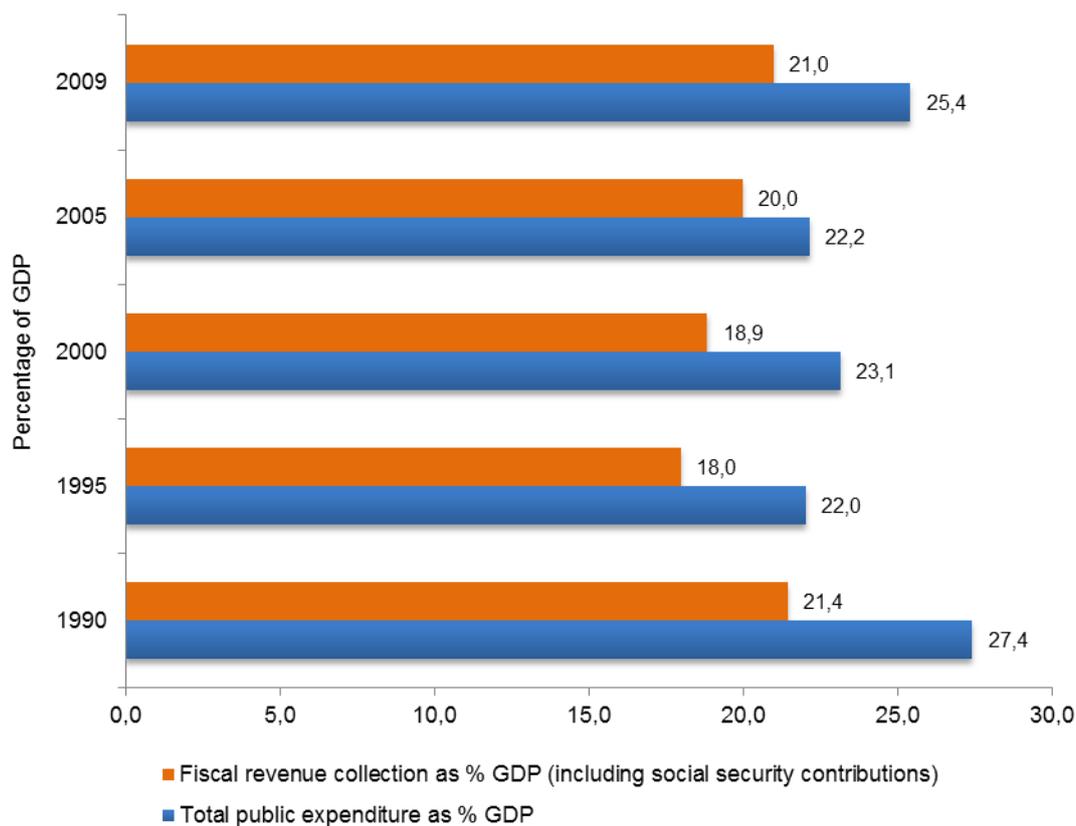


Source: World Bank, 2010.

The long-term economic growth rate between 1961 and 2010 averaged 4.8 per cent per annum. Prior to the 2008-09 crisis the country grew at 4.6 per cent during the 2000s. This, however, was still lower than the 6.3 per cent rate experienced during the 1970s and the 5.5 per cent of the 1990s. Since the 1981-1982 economic crisis, the worst in the country's history, Costa Rica experienced only one episode of negative economic growth, in 2009 (2.8 per cent). In per capita terms, negative growth rates were observed on five occasions, in 1985, 1991, 1996, 2001 and 2009.

From a fiscal perspective, chronic fiscal deficits are the rule in Costa Rica. With the exception of 2007 and 2008, the fiscal balance has been negative since 1970. Public sector fiscal deficits, on average, constituted 2.5 per cent of GDP during the 2000s (figure 35).

Figure 35. Costa Rica: Government expenditure and revenue, several years



Source: Ministerio de Hacienda, 2010; International Monetary Fund, 2010b.

Overall, Costa Rica's public debt has been declining over the years. External debt, which stood at 28 per cent of GDP in 1995, fell to 19.8 per cent in 2000, then to 18.3 per cent in 2005 and to 12.2 per cent in 2009. This steady reduction is the result of a Government strategy aimed at replacing external debt by internal debt, given the more advantageous interest rates on the domestic market. This is reflected in a continued decline in debt service, measured as a percentage of exports (figure 36). Between 1995 and 2009 internal debt fell from 24.5 per cent of GDP to 22.4 per cent in 2009.

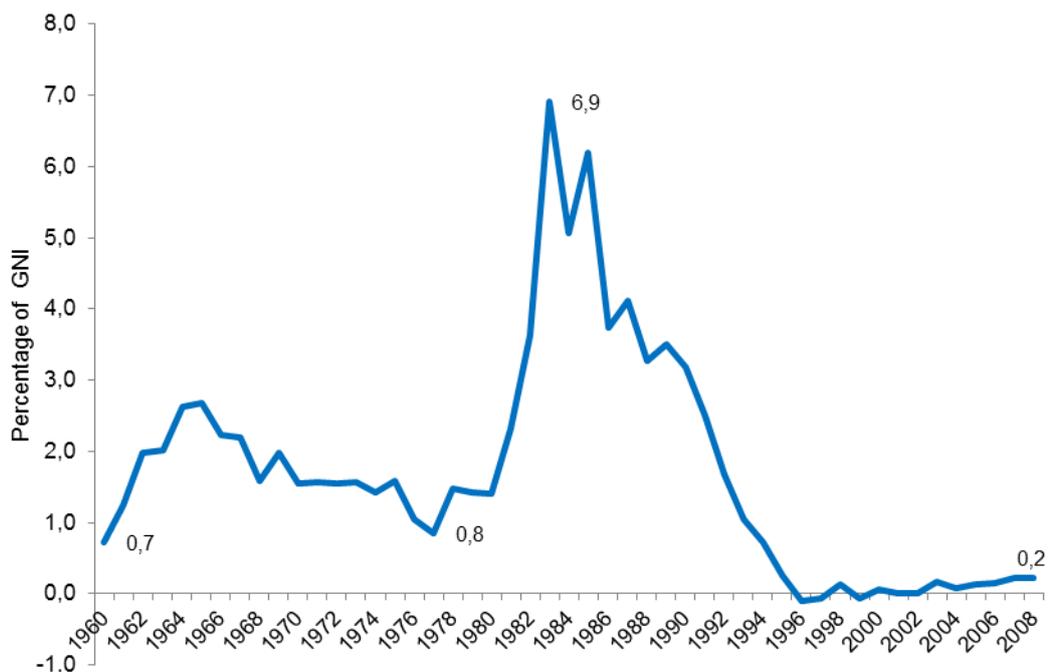
Figure 36. Costa Rica: Debt service as a percentage of total exports, 1977-2008



Source: World Bank, 2010.

External aid has been declining rapidly since the mid-1980s and Costa Rica today is almost entirely independent of official development assistance (ODA). Between 1983 and 1985, net ODA constituted 6 per cent of GNI, a figure that contrasted with the corresponding figure of 3.7 per cent for the rest of the 1980s, 0.9 per cent during the 1990s and 0.1 per cent during the 2000s (figure 37). ODA per capita, which peaked at US\$103.5 in 1985, reached US\$14.6 per person in 2008.

Figure 37. Costa Rica: ODA flows as a percentage of GNI, 1960-2008



Source: World Bank, 2010.

Socioeconomic conditions in Costa Rica are in general much better than in most developing countries. The country's long tradition of investing in health, education, nutrition and housing ever since the army was abolished seems to have paid off. Poverty affects less than 20 per cent of the population and the country ranks among the top five Latin American countries in terms of human development. Health conditions compare to those of developed countries, average life expectancy is close to 80 years and infant mortality is less than 10 deaths per 1,000 live births. HIV prevalence is among the lowest in the continent (table 8).

Table 8. Costa Rica: Key socioeconomic indicators, latest available year

Indicator	Value	Year
Poverty headcount at national poverty line (percentage)	18.5	2009
Gini coefficient	0.44	2009
Human development index	0.85	2009
Life expectancy at birth (years)	79	2008
Infant mortality rate per 1000 live births	8.8	2009
Maternal mortality rate per 10,000 live births	3.3	2005
HIV-AIDS adult prevalence rate (15 to 49 years old)	0.4	2007
Adult literacy rate (percentage)	96	2007
Children underweight for age (percentage)	6.6	2008

Source: Ministerio de Planificación Nacional y Política Económica, 2010.

6.2. Social protection programmes and social spending

Costa Rica has a long tradition of implementing social policies. Primary education was declared universal in the 19th century and social security was introduced in the 1940s. To date, an extensive network of contributory and non-contributory programmes constitutes Costa Rica's social protection floor. There are at least 34 programmes aimed at reducing poverty, excluding the contributory social protection initiatives (pensions and health insurance). Table 9 below summarizes the list of programmes currently operating in the country, according to the nature of the programme.

The table is divided into two blocks of programmes, contributory social protection initiatives and non-contributory initiatives. Other social categories such as education and culture are also included.

The contributory social security programmes are grouped around the management and coordination of the Costa Rican Social Insurance Fund (CCSS) created in 1943. The CCSS administers the national health insurance fund and the contributory pension scheme. Although the Fund also delivers health services to indigent persons and pays pensions to non-contributory groups, these segments are not classified as contributory in nature.

Non-contributory poverty-reduction programmes can be classified in two broad categories, each subdivided into five subcategories (Trejos, 2009). The two categories are:

1. **Selective promotional programmes.** This group comprises all programmes aimed at enhancing the capabilities of the target population or which complement existing universal programmes. The group includes key initiatives such as the CEN-CINAI (an early childhood development programme), the *Comedores escolares* (a school meals programme) and *Avancemos*, a conditional cash transfer programme to combat high-school dropout.

2. **Social assistance programmes.** These were created with the primary purpose of compensating household income and reducing exclusion or vulnerability. Overall, they are not a significant factor in total expenditure on the social sector. With the single exception of the National Care Network (*Red nacional de cuidado*), the programmes do not account more than 15 per cent of public spending on poverty or vulnerability reduction strategies.

Table 9. Costa Rica: Contributory and non-contributory programmes

Contributory programmes	Non-contributory poverty reduction programmes				
	Promotional selective programmes		Social Protection Network		
	Complementary to universal programmes	Support to capability enhancement	Compensation	Social assistance	Fight against vulnerability or exclusion
National health insurance (CCSS)	<i>Centro de Atención Infantil (CEN-CINAI): early childhood care</i>		Employment-generation programmes of the Ministry of Labour	Subsidies, IMAS	PANI
Contributory Pensions schemes (CCSS and others)	<i>Comedores Escolares: school meals programme</i>		Emergencies, IMAS	National Network of Care	INAMU
	<i>Avancemos: conditional cash transfers to reduce high school dropout</i>		National Emergency Commission		National Political Council for Young People
	Indigent population coverage with health-care services				CONAI
					Handicapped people
					Elderly people

Source: Céspedes; Jiménez, 2010.

Note: The most important programmes in terms of coverage and expenditure are indicated in italics.

IMAS: Instituto Mixto de Ayuda Social (Joint Social Welfare Institute)

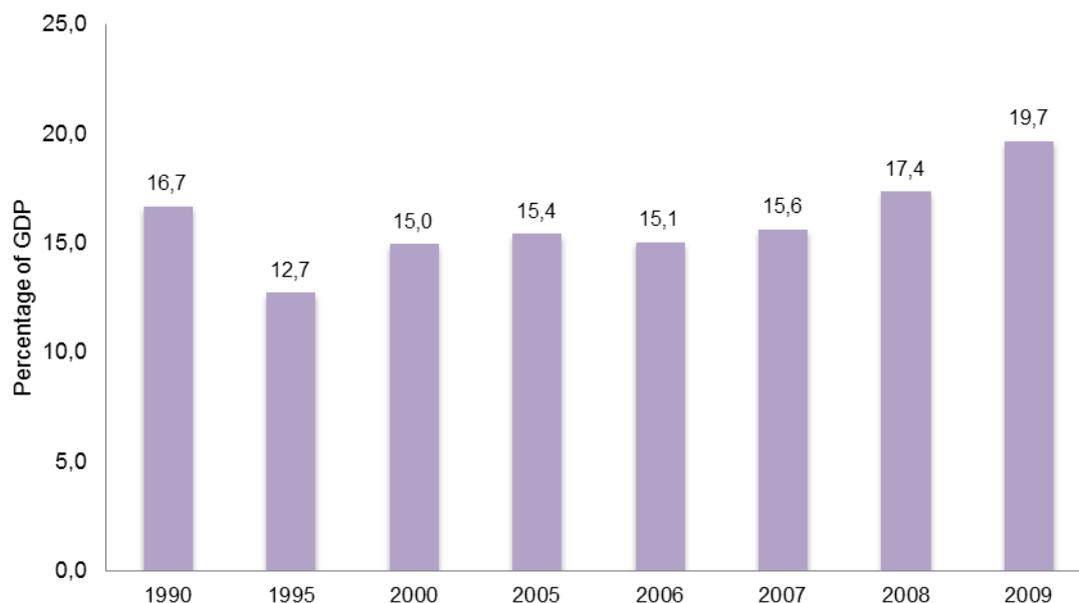
PANI: Patronato Nacional de la Infancia (National foundation for children)

INAMU: Instituto Nacional de las Mujeres (National Institute of Women)

CONAI: Comisión Nacional de Asuntos Indígenas (National Commission of Indian Affairs)

By 2009 about one-fifth of Costa Rica's GDP was allocated to social spending. After a sharp decline in the level of social investment during the mid-1990s, public social expenditure recovered during the 2000s and stayed at around 15 per cent of GDP (figure 38). A second wave of increments was experienced after 2006 with the introduction of the *Avancemos* conditional cash transfer programme. What is also remarkable is the strong share of social expenditure in total public expenditure. In 1990 some 60 per cent of government spending was assigned to social investment, rising to 70 per cent in 2006 and to 77.4 per cent in 2009.

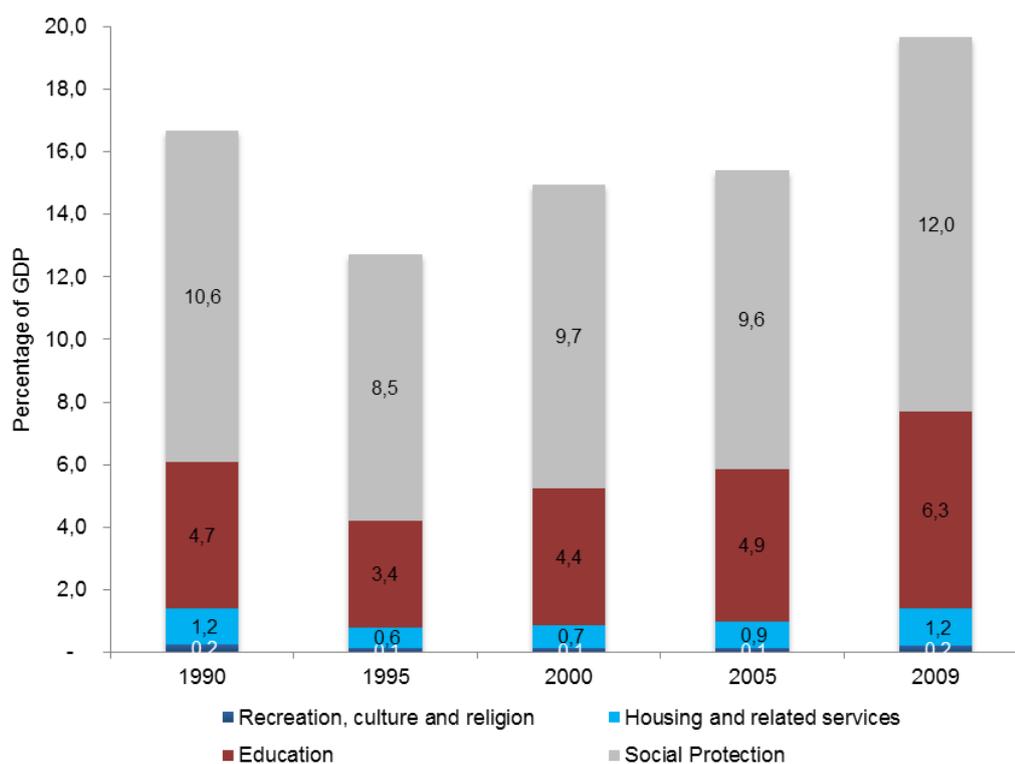
Figure 38. Costa Rica: Social spending as a percentage of GDP, 1990-2009



Source: Ministerio de Hacienda, 2010; International Monetary Fund, 2010b.

By category of spending, the share of education and social protection in total expenditure on the social sector was somewhere between 92 and 94 per cent (figure 39). Their share remained much the same throughout the last two decades, rising slightly in the second half of the 2000s. Between 1990 and 2009 culture and housing lost some ground and the growth of social protection dropped behind that of education, at least during the last five years.

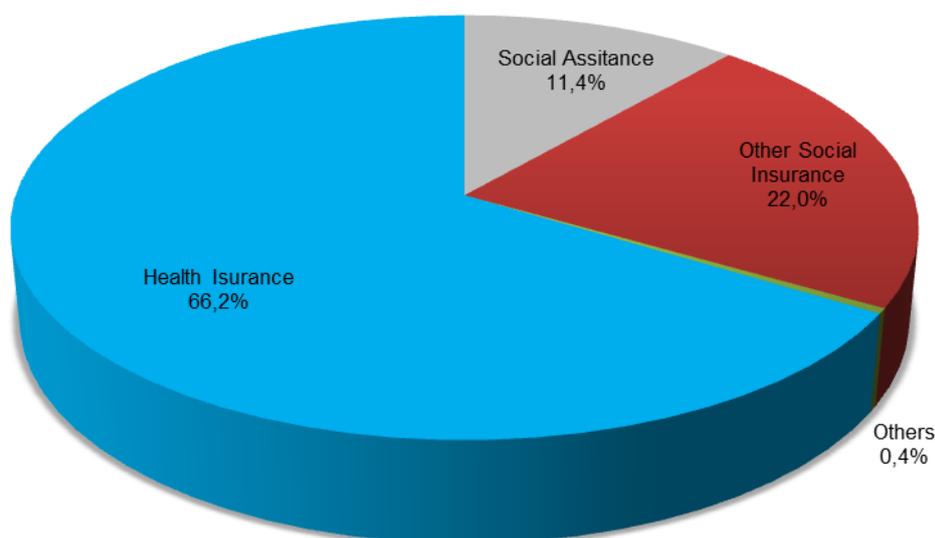
Figure 39. Costa Rica: Composition of social spending, 1990-2009



Source: Ministerio de Hacienda, 2010; International Monetary Fund, 2010b.

As mentioned earlier, expenditure on social protection in the last two decades accounted for 10 per cent of GDP. At the top of the list, two-thirds of this expenditure went on healthcare, and social insurance accounted for a further 22 per cent (figure 40). The share of social protection was roughly half of total government expenditure in 2009.

Figure 40. Costa Rica: Average participation of social protection categories, 2000-2009



Source: Ministerio de Hacienda, 2010; International Monetary Fund, 2010b.

6.3. Contributory social security programmes: The Costa Rican Social Insurance Fund (CCSS)

Even though various governments made a serious effort to organize Costa Rica's health sector during the 19th century, it was not until 1941 that a mandatory health insurance (MHI) scheme was implemented, later to take the form of the Costa Rican Social Insurance Fund (CCSS) and the social security system as a whole. In addition to the creation of the CCSS, the Government of the time approved key legislation regarding the Labour Code (1943), the Social Guarantees Constitutional Chapter and the creation of the University of Costa Rica.

The establishment of the MHI was the outcome of a social consensus that involved the Government itself, the Communist Party and the Roman Catholic Church, an unusual triumvirate that agreed on the importance of the project.

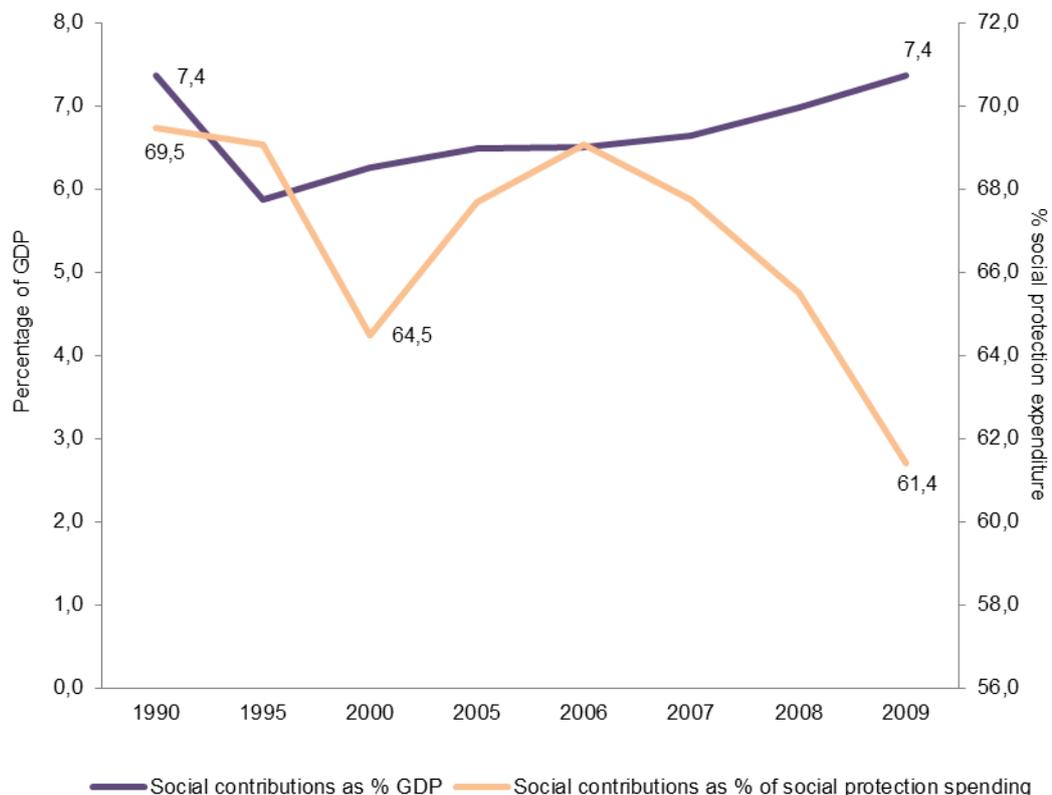
The MHI was originally set up to protect workers against the risk of illness, maternity and employment injuries, and to grant an old-age pension to older people when they retired. As it evolved from basic coverage of industrial and government employees, the MHI expanded to include benefits for workers' families, to provide voluntary health insurance and, by means of budget transfers to the CCSS, to cover those who had previously been excluded.

To finance the contributory health insurance scheme, the regulations introduced a 15 per cent payroll contribution in the formal sector, a 10.25 per cent rate on reported income for independent workers and a 14 per cent rate for pensioners. The State finances health

services for poorer households and indigents and finances this expenditure with a specific tax on luxury goods, alcohol, beer, colas and other imported goods.

Contributory pensions are funded by an 8 per cent payroll contribution, but further 0.5-point increments are expected every five years until 2035. During the last decade contributory health and pension contributions together constituted, on average, 6.7 per cent of GDP and 66 per cent of expenditure on social protection (figure 41). The share of expenditure on social protection, however, has experienced a progressive decline since 1990, for two main reasons. The first is that, of all the social protection components, social contributions grew more slowly than expenditure on health, non-contributory pensions and poverty reduction programmes. This is explained by the second factor, which is related to a decrease in the coverage rate of the economically active population (EAP) by social insurance. After peaking at 71.7 per cent of the EAP in 1994-1995, coverage declined to 66.4 per cent in 2000, the same level as in 1991. During the 2000s the rate of coverage continued to decline until 2003 (52.2 per cent), when it started a period of recovery to reach 64.8 per cent in 2009 (CCSS annual reports for 1995 to 2009).

Figure 41. Costa Rica: Social contributions as a percentage of GDP and of expenditure on social protection, 1990-2009



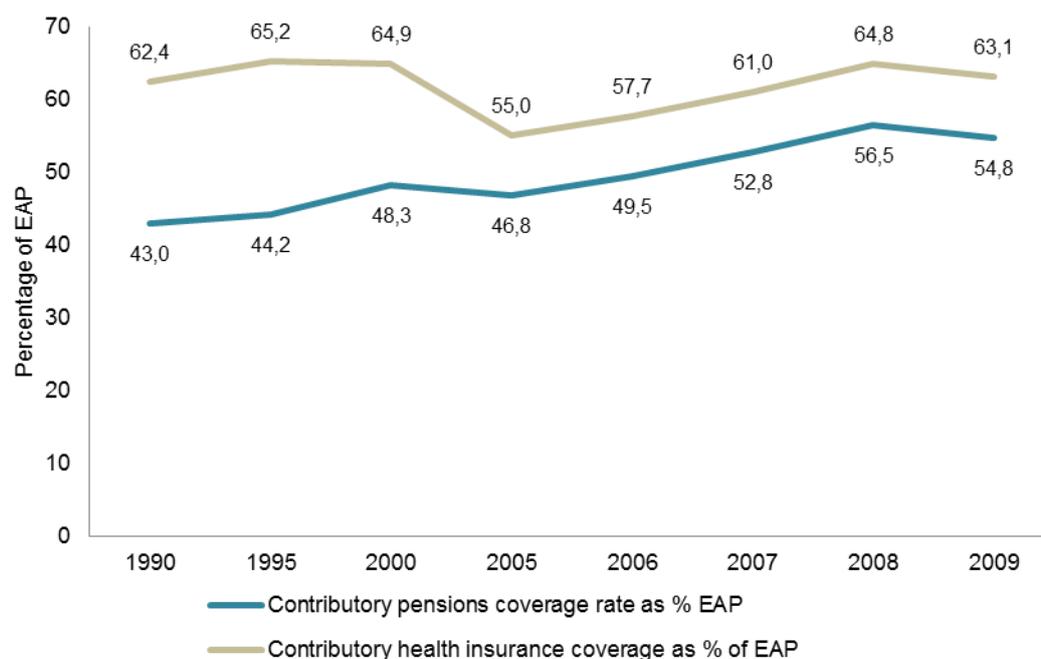
Source: Ministerio de Hacienda, 2010; International Monetary Fund, 2010b.

Besides the CCSS contributory pension scheme there are other special contributory schemes administered by specific government bodies. In total there are currently eight additional pension schemes covering public employees, but most of them are in the process of extinction. The programmes for teachers and judicial employees remain as the most important in terms of coverage and expenditure.

In terms of coverage (figure 42), almost 63 per cent of the economically active population was affiliated to the health insurance scheme in 2009. Between 1990 and 2009, affiliation

averaged 61.8 per cent of the EAP and 88 per cent of the total population. In the case of contributory pensions, they covered a total of 54.8 per cent of the EAP in 2009, up from 43 per cent in 1990. CCSS contributory pensions account for 53.4 per cent of that coverage, while the remaining 46.5 per cent are affiliated to the special schemes. More people belong to the health insurance scheme than to the pension scheme, possibly due to the existence of a voluntary health programme within the CCSS that increases the share of the population with access to health coverage.

Figure 42. Costa Rica: Contributory health insurance and pension coverage, as a percentage of the economically active population (EAP), 1990-2009



Source: Ministerio de Planificación Nacional y Política Económica, 2010.

6.4. Non-contributory pensions

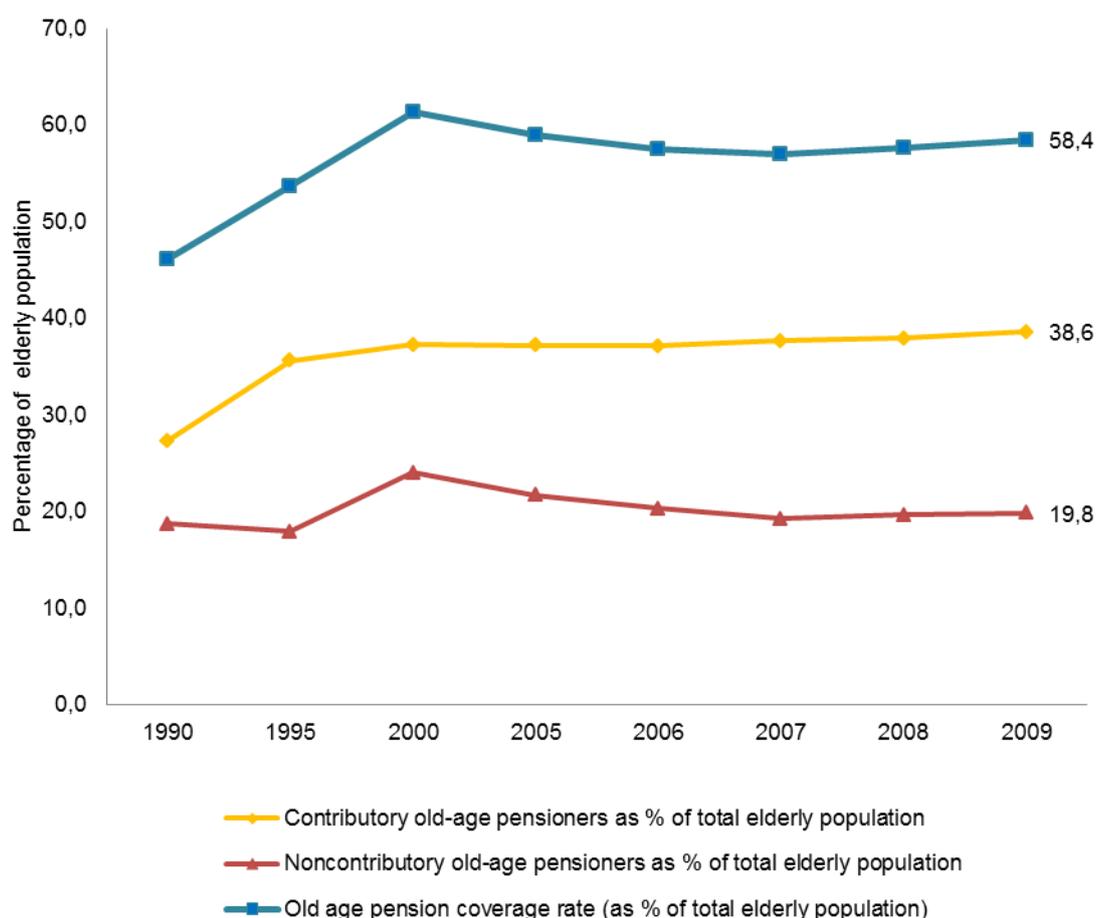
Non-contributory pensions covered by budgetary transfers from the Ministry of Finance are also available to particular groups. To become a beneficiary of non-contributory pension, a person must fall in one of the following categories:

- over 65 years of age;
- between 18 and 64 years of age with a handicap and unable to work;
- widow aged 55-65 years with no other income;
- orphan child;
- student aged 18-21 years not formally working;
- indigent.

Special non-contributory schemes also exist to cover special groups such as former Presidents and war victims. All in all there are 57,437 beneficiaries of non-contributory schemes in Costa Rica, or 1.3 per cent of the population. In total 89 per cent of this group is covered by the CCSS. According to the Ministry of Planning, the average non-contributory pension was US\$118 per month in 2009.

By 2009 almost 60 per cent of people aged 65 or more received a pension, a proportion that has increased by 27 per cent in the last 20 years. The ratio of contributory to non-contributory pensioners has also undergone major changes since 1990. In 1990 this ratio was 1.45:1, rising in 2009 to almost 2:1. In other words, non-contributory pensioners, which accounted for 40.7 per cent of all Costa Rican pensioners in 1990, now make up 34 per cent of the total.

Figure 43. Costa Rica: old-age coverage by contributory and non-contributory old-age pensioners (people over 65 years of age), 1990-2009



Source: Ministerio de Planificación Nacional y Política Económica, 2010.

6.5. Poverty reduction initiatives

As seen in table 9, Costa Rica has a wide range of policy initiatives aimed at reducing poverty, social exclusion and social vulnerability. However, only five are critical in terms of spending, accounting as they do for more than 80 per cent of poverty-based social spending: the housing programme (*Bono de vivienda*), non-contributory pensions (described above), the school meals programme (*Comedores Escolares*), the early childhood programme (CEN-CINAI) and the *Avancemos* conditional cash transfer programme.

6.5.1. Initial efforts to reduce poverty in Costa Rica: FODESAF

In 1971 President Figueres created the Joint Social Welfare Institute (IMAS) as the state agency in charge of reducing extreme poverty levels. Then, in 1974, policy efforts to fight

poverty were complemented with the establishment of the Family Allowances Fund (FODESAF), a special fund created to finance poverty alleviation and poverty reduction programmes. FODESAF is financed by a 5 per cent payroll tax and a 20 per cent sales tax, although this 20 per cent is not always paid up in full. The Fund has four specific features:

- It is a permanent fund.
- It aims at financing programmes geared towards human capital formation.
- It has relatively stable financial resources that do not compete with universal programme funds.
- It is controlled and supervised like any other public institution.

6.5.2. The Bono de vivienda housing programme

In 1986 the Government of Dr. Oscar Arias created a housing finance scheme and, as part of it, a housing subsidy known as the *Bono de vivienda*. The primary objective of the *Bono de vivienda* fund was to provide financial support to poor families in order to facilitate access to housing. This Fund, administered by the Housing Mortgage Bank, is financed by resources coming from FODESAF. Under the scheme, the Bank awards housing bonds that currently amount to US\$10,290 and are granted once only to families, not individuals. To become a potential beneficiary, a family's total income must be no more than US\$1,456 per month. Current investment in the housing programme corresponds to 0.3 per cent of GDP.

6.5.3. The Comedores escolares school meals programme

Costa Rica's school meals programme is the *Comedores escolares* initiative, created in 1975 with the following objectives:

- To provide students with complementary meals to improve their nutrition.
- To encourage hygiene and good behavioural habits.
- To promote a healthy nutrition.

By 2008 some 598,552 school and high school students (approximately 55 per cent of the student population) were beneficiaries of the programme and ate at their assigned cafeteria in the academic centre at least once a week. The programme covered 4,750 academic centres and had a budget equivalent to 0.2 per cent of GDP.

6.5.4. The Avancemos conditional cash transfer programme

In 2006 the Government launched the *Avancemos* programme, a conditional cash transfer programme aimed at reducing the high-school dropout rate. The initiative was fully rolled out in 2007. *Avancemos* is the only conditional cash transfer programme in Costa Rica but not the only scholarship-based initiative. In 1997 the national scholarship fund (FONABE) was created to reduce the secondary school dropout rate. In principle, FONABE was the sole body in charge of administering scholarships for the whole education system, but after 2009 the Government decided to move *Avancemos* to the IMAS. As a result, the dual nature of the programme – to control dropout and to reduce poverty – was made clear. Primary school scholarships are now managed by FONABE and secondary school scholarships by IMAS.

Coverage under *Avancemos* has increased dramatically in recent years, from 94,621 beneficiaries in 2007 to 130,469 in 2008 and to 165,749 in 2009. In 2009 *Avancemos*

covered 51.5 per cent of state high-school students. The cash transfer varies depending on the school level in which the student is enrolled, but it goes from US\$30 to US\$97 per month. In total, the *Avancemos* programmes cost US\$161.9 million in 2009, corresponding to 0.5 per cent of GDP.

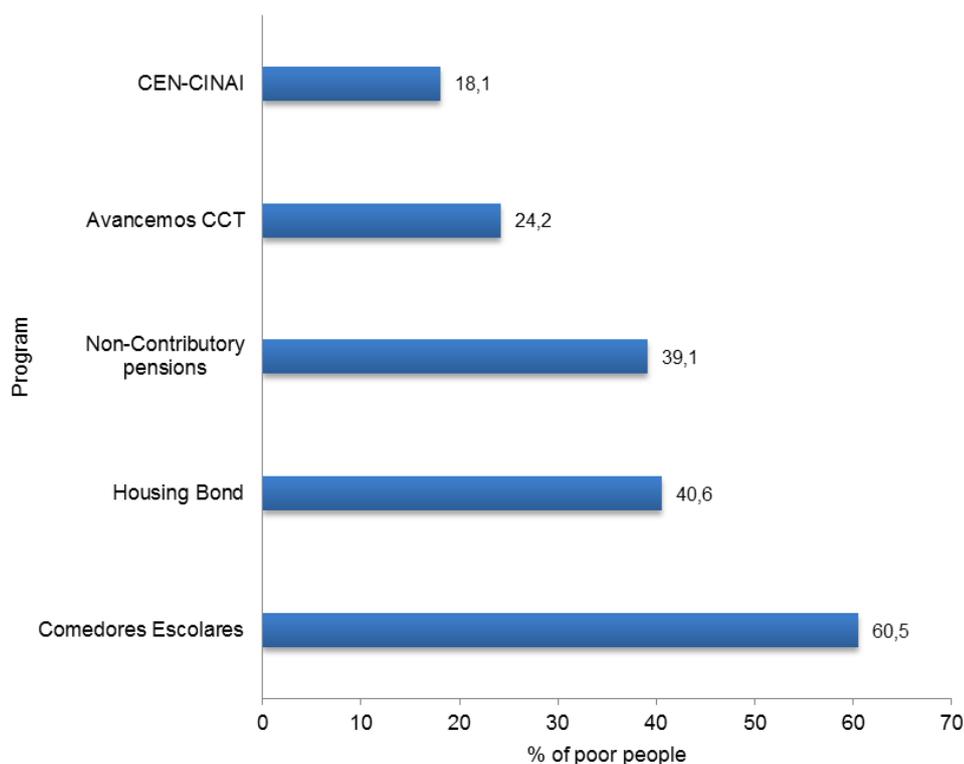
6.5.5. The CEN-CINAI programme

The CEN-CINAI programme is a network of 619 centres that distribute (either at each centre or directly to beneficiary families) food, milk and integrated health care to roughly 72,000 children under the age of 7 and, since 2008, to mothers. Annual expenditure in 2008 was equivalent to 0.05 per cent of GDP.

6.5.6. Coverage rates of the main poverty reduction initiatives

Figure 44 shows the coverage of people living in poverty as a share of the total target population – in this case, poor people for the year 2007. Most of the programmes face some difficulty in reaching the entire target population, and in no case does their coverage exceeded 60 per cent, with a low of 18 per cent by the CEN-CINAI programme. This targeting problem may be due to a variety of causes. First, there is a shortage of supervisors to verify the information provided by the applicant. Secondly, the target population may not necessarily only be people living in poverty; for instance, the *Comedores escolares* programme has an open-door policy so that any student may go to one of its cafeterias and eat free of charge. Thirdly, the rules laid down by a programme may affect poor households more than other groups; thus, in the case of *Avancemos* the beneficiary must be a student and must comply with the programme's conditions, and this may have a negative impact on groups such as people living in extreme poverty where dropout rates are higher than in any other socioeconomic group.

Figure 44. Costa Rica: Poor beneficiaries as a percentage of the target population, by programme, 2007



Source: Trejos, 2009.

6.6. Fiscal space for social protection in Costa Rica

The previous section shows that Costa Rica has an extensive network of social protection programmes. In addition to government spending on poverty reduction initiatives and social protection allocations, education plays a critical role in overall social investment. Several mechanisms have been introduced since 1940 to expand fiscal space; some of them are standard mechanisms, others are specific to Costa Rica.

1. Over the last seven decades, the various governments and political and social forces have committed themselves to allocating an increasing and *permanent* share of resources to social investment. The creation of the CCSS and the mandatory social insurance system was the result of a consensus among three groups with quite distinct ideologies (Government, communists and the Catholic Church).
2. Economic growth was strong between 1960 and 1978, exceeding 6 per cent per year, and this allowed the governments of the time to increase significantly revenue collection. The boom in coffee prices in the mid-1970s was essential for the establishment of the FODESAF fund, the cornerstone of the poverty reduction initiatives. However, economic growth and increasing fiscal revenue do not explain Costa Rica's high social protection floor. In subsequent decades economic growth decelerated but social spending continued to increase and social programmes to diversify.
3. The abolishment of the army in 1948 freed a large volume of resources for social purposes permanently. This was a critical decision in the life of the country, not only for civil reasons, but also for the funds it made available for human capital accumulation. In the course of the 30 years that followed the abolishment of the army, life expectancy in Costa Rica rose from 40 years to over 70 years.
4. A large number of social spending initiatives have constitutional force in Costa Rica. Whether the Constitution is the correct place to define social policy or not is subject to debate, but the fact remains that it has served as a means of obliging policymakers to tie government revenue to social investment. A recent reform of the Constitution provided that public investment in education must be at least 6 per cent of GDP.

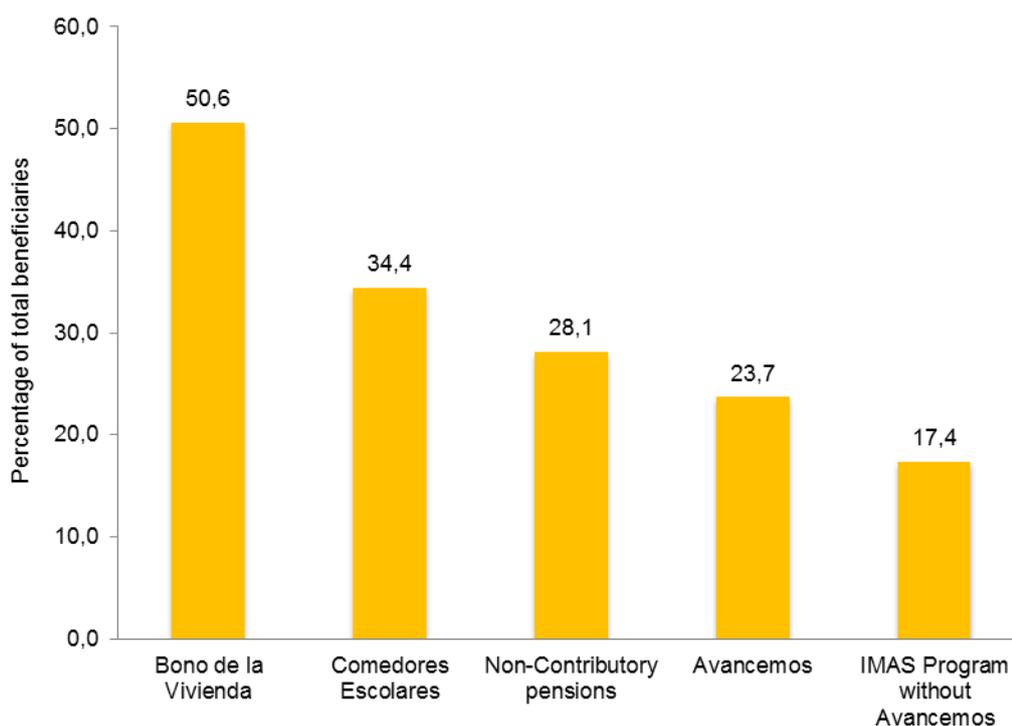
6.7. Challenges and lessons learnt

6.7.1. Challenges

Costa Rica is an interesting case of long-term efforts to consolidate a network of institutions and programmes designed to enhance human development and improve living standards. There is, however, room for increasing the return on each *colon* spent on the social sectors. The main challenges of the social protection system are described below.

1. At this point in time there is a general perception that additional funds are not a priority for social investment. On the contrary, government expenditure on social investment is one of the highest in Latin America. It cannot be claimed, however, that all this spending is being put to the most effective use. Figure 45 shows the "leakages" of a sample of the country's social programmes. A bit more than half of the beneficiaries of the housing bonds, for instance, were not part of the target population, and almost 30 per cent of non-contributory pensioners did not come from the poorer households. Improving the targeting of these programmes is therefore critical to maximizing the impact of available resources.

Figure 45. Costa Rica: Percentage of beneficiaries who are not part of the target group, by programme, 2007



Source: Trejos, 2009.

2. Social contributions play a critical strategic role in the sustainability of Costa Rica's entire social protection system. The earmarked contributions are adjusted according to the aggregate wage and to the administrative capability of the CCSS to collect that revenue. The contribution collection mechanism is isolated from short-term fiscal decisions and social expenditure is reduced accordingly. Even if future governments increase spending on social protection (as is currently happening with the National Care Network), the possibility of raising the level of social investment is certainly constrained by the country's relatively low tax burden of 16 per cent of GDP (excluding social contributions). Such a possibility depends on the implementation of far-reaching fiscal changes. The tax burden would need to be increased by 2-3 percentage points of GDP and tax evasion would need to be cut at least by half. The National Comptroller's Office (Ministerio de Hacienda, 2010) has estimated that income tax evasion is about 79 per cent of potential income tax collection, an unacceptable figure that corresponds to 3.6 per cent of GDP.
3. The reallocation of resources is a very complex task. First, as previously established, the level of social spending as a percentage of government expenditure is already high, so reducing the budget in certain areas to increase social budgets will affect the performance of other sectors. In addition, more than 80 per cent of Government expenditure is fixed and thus it is difficult to move resources to other priorities. Finally, competition for funds has recently been increasing on account of the country's severe infrastructural problems.
4. The network of institutions should be reduced in order to lower administrative costs and improve coordination among plans and programmes. The integration of all the existing databases of beneficiaries into a single system would seem to be an urgent matter. Existing targeting problems, duplication of efforts and the apparent inability

to disenfranchise families that receive more than one benefit point to a need to integrate many of the schemes that exist.

5. The relatively small number of people with a very low income in Costa Rica (in comparison to Latin America as a whole) calls for the concept of poverty to be redefined and for an expanded multidimensional approach to be adopted. Institutions such as FONABE are now looking for alternative targeting methods that measure *vulnerability* instead of poverty alone, so that the identification of beneficiaries can be more efficient than before. A change of this nature implies the incorporation of social groups that are not typically considered as poor.

6.7.2 Lessons learnt

Some of the main lessons learnt from the case of Costa Rica are set out below.

Lesson 1

Costa Rica is an excellent illustration of the fact that economic growth is important but not the key determinant in the provision of extensive social protection. The country took advantage of the highly positive growth rates experienced in the 1960s and 1970s to establish core bodies that became permanent institutions.

Lesson 2

Social contributions in Costa Rica play a critical role in the creation of fiscal space. Although, theoretically, higher social contributions are associated with higher labour costs and, therefore, with increasing labour market informality, the evidence in this case is not conclusive. On the contrary, Costa Rica has one of the highest rates of nominal and effective social contributions in all Latin America yet, along with Chile and Uruguay, it has one of the lowest rates of informality. The country also appears among the top countries in terms of competitiveness, well above regional averages. As in the case of Brazil, social contributions do not therefore seem to be associated with labour market informality.

Lesson 3

Viewed in the long term, the social security system has acted as a direct contributor to the country's competitiveness by enhancing the health status of the population, and as an indirect contributor by reducing inequality and promoting social peace – two elements that investors are inclined to give weight to when deciding where to locate their companies. The national health insurance scheme is a solidarity-oriented system in which the lowest income groups receive at least four times their contribution to the system. This cross-subsidization has allowed low-income classes to have access to the same services as high-income classes. All this has a positive effect on the generation of future income, growth and fiscal revenue.

Lesson 4

Costa Rica is also a case in which social development has come from within. ODA resources played no significant role in the construction of the country's social protection system. Yet, at the time the mandatory social insurance programme was launched, fewer than 40 per cent of the population wore shoes.

Lesson 5

The extension of social protection is a highly political issue. The abolishment of the army and the approval of the Social Security Act were two atypical decisions for a highly underdeveloped country, as well as in terms of their timing. The first decision made Costa Rica the first country in the world without a military budget. The second involved agents that, in principle, had nothing in common. Both measures signified an enhancement of the availability of resources and helped to consolidate a model in which human capital formation was the centrepiece. All this required a clear long-term vision on the part of society as a whole.

Lesson 6

In terms of governance, the tripartite body that manages Costa Rica's social insurance fund (workers, employers and Government, all represented on the Board of the CCSS) and the mechanisms that promote social dialogue among the different parties have worked as a powerful political shield to protect the collection of social contributions. For instance, during the 1980s and 1990, when the neoliberal structural adjustment and stabilization packages reduced central Government spending on health to a historical low, the revenue of the social security system actually increased and helped to keep expenditure on health at the same level.

Lesson 7

Money is important but, again, money alone is not enough. For more than a decade, from 1994 to 2006, poverty rates in Costa Rica remained stable at around 20 per cent of the population, despite the fact that an extensive institutional framework was already in place. That said, there remain problems with targeting and with programme design.

Lesson 8

Achieving results demands patience. The social insurance programme did not cover the entire population from the very start but was a process that took more than 30 years to complete. A strategy such as this calls for permanent institutions, and that is what Costa Rica established. More than 80 per cent of the country's core social programmes were created 25 years ago and the two building blocks of the social strategy, the CCSS and the FODESAF, have been in existence for more than 35 years.

Lesson 9

To meet the necessary conditions, the country had to identify appropriate financing sources. In the case of Costa Rica, there is a mix of financial sources that includes payroll contributions, earmarked taxes and other lesser sources such as profits from the national lottery. The problem with this type of design, however, is that in times of crisis the revenue tends to decrease just when poverty is on the increase. It is therefore important that part at least of the financing be fixed or stable, even though this may have negative fiscal implications.

Lesson 10

Countries should be very careful about the initiatives they create. A long list of social programmes may generate problems of governance throughout the system. Moreover, the contribution of some programmes to the fight against poverty may be quite small. Costa Rica's experience raises two potential problems. First, it is usually very difficult to cancel or reverse programmes that are under way, and so policymakers may tend to keep them even though they do not bring the desired results. Secondly, if there are too many programmes, the demand for additional funds may set them in competition with other priorities such as infrastructure and the environment.

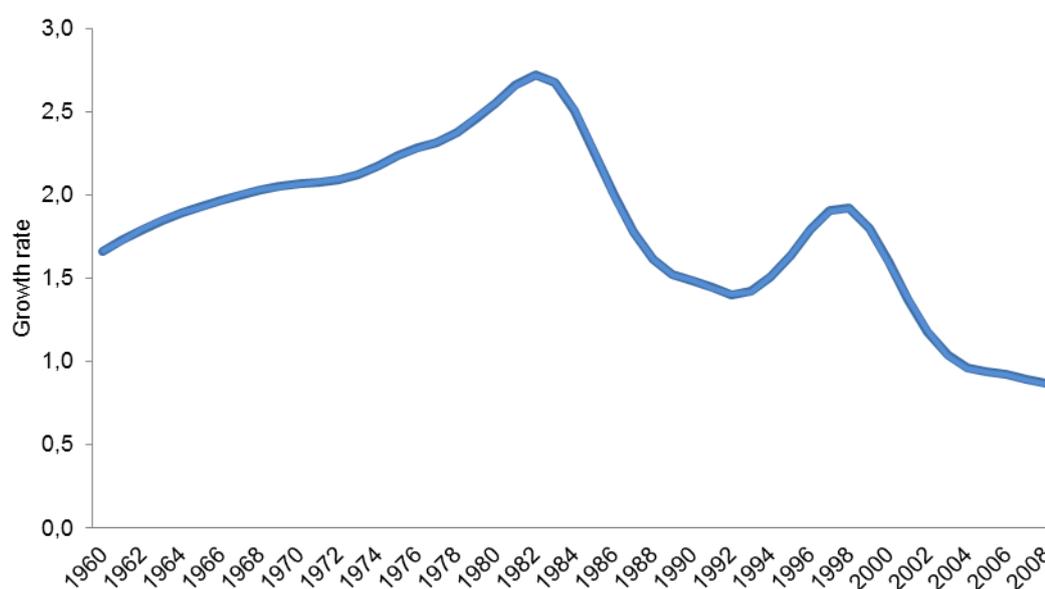
7. Lesotho: Taking advantage of good economic conditions and strong political will to increase social protection

7.1. Country profile

The Kingdom of Lesotho is a small landlocked country of southern Africa with a total surface area of 30,355 square kilometres. It has a single neighbour, South Africa, which surrounds the kingdom on all sides. Lesotho became independent from the United Kingdom in 1966. Politically speaking, Lesotho is a parliamentary system with a Constitutional monarchy.

The total population in Lesotho was estimated at 2,067,000 inhabitants in 2009 (United Nations-Population Division of the Department of Economic and Social Affairs). Population growth has averaged 1.8 per cent per year since 1960 but the annual rate has oscillated since 1982, declining for a while, recovering and then dropping off again. Since 1998 population growth has been lower each successive year; between 2004 and 2008 the average growth rate was 0.92 per cent (figure 46).

Figure 46. Lesotho: Population growth rate, 1960-2008



Source: United Nations-Population Division of the Department of Economic and Social Affairs, 2010.

The median age of the population in Lesotho is 22.6 years, with a projected 25.2 years by 2025. Fifty-five per cent of the population is under 25 years of age, but this group is expected to decline to 49 per cent by 2025. Over the next 15 years the country will experience a transition to a more mature society in which the 35 to 49 year-old age bracket will increase its share from 12.6 per cent to 20.3 per cent of the total population. People over 65 years of age will not increase their share significantly and are expected to account for 5.9 per cent of the total in 2025.

From an economic standpoint, contrary to what occurred in many countries in the southern part of Africa (Mozambique and Botswana, for instance) where the economy grew at impressive rates, Lesotho did not exhibit an outstanding macroeconomic performance or

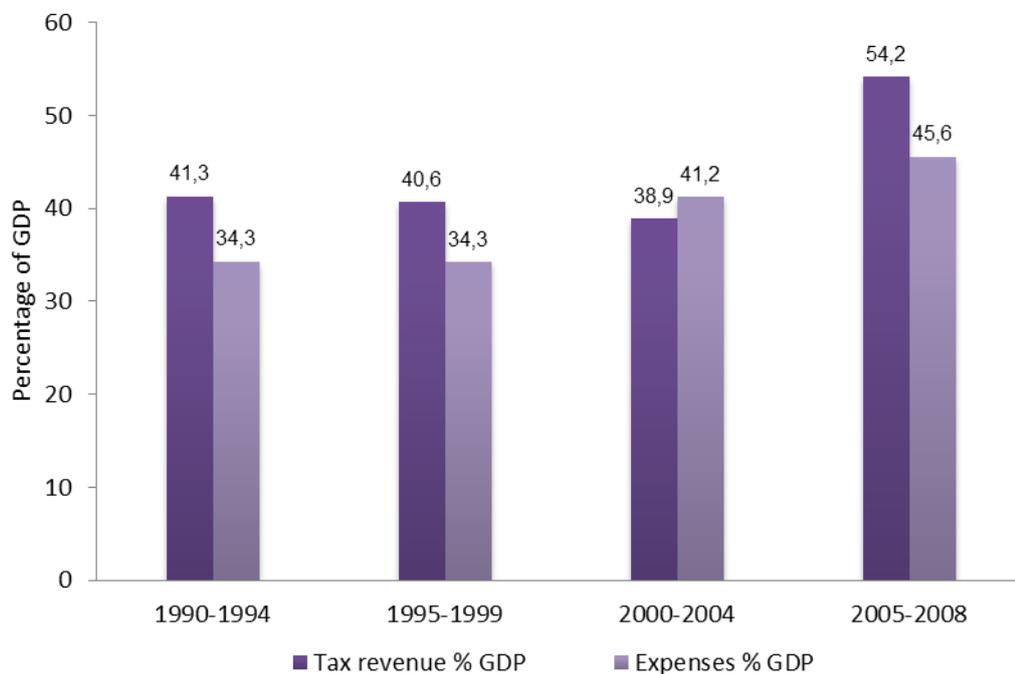
benefit from any special feature that might distinguish its economy from that of the rest of the region.

Lesotho's economy is small, with a GDP per capita of US\$775 in 2009 (US\$1,700 PPP) that was ranked 156th in the Human Development Index (HDI). GDP per capita has multiplied by a factor of 13 since Independence, at an average rate of 4.6 per cent per year (2.8 per cent in per capita terms). Lesotho ranks below the sub-Saharan Africa region in terms of gross national income (GNI) and its per capita income is half the average among lower-middle income nations.

The country relies heavily on the United States for exports and on South Africa for employment and remittances. Some 59 per cent of total exports go the United States, while most of the remittances received by Lesotho come from miners working in South Africa. Services account for the biggest share of the economy (58 per cent) and agriculture for 7 per cent of GDP. By contrast, 86 per cent of the occupied labour force works in the agriculture sector, but 45 per cent of the total labour force is unemployed. Finally, exports achieved their highest ever level of 58.2 per cent of GDP in 2002, since when they have decelerated year after year to 47.3 per cent of GDP in 2008.

The Government plays a critical role in Lesotho's economy. During the second half of the 2000s public spending accounted for 45.6 per cent of the economy, having increased steadily since 1990 (figure 47). Tax revenue followed a similar pattern to expenditure and, with the exception of the period 2000-04, the Government has enjoyed fiscal surpluses. These surpluses were 8.3 per cent in 2007 and 4.1 per cent in 2008 (Ministry of Finance and Development Planning, 2009b).

Figure 47. Lesotho: Public revenue and expenditure as a percentage of GDP (5-year periods, 1990-2008)

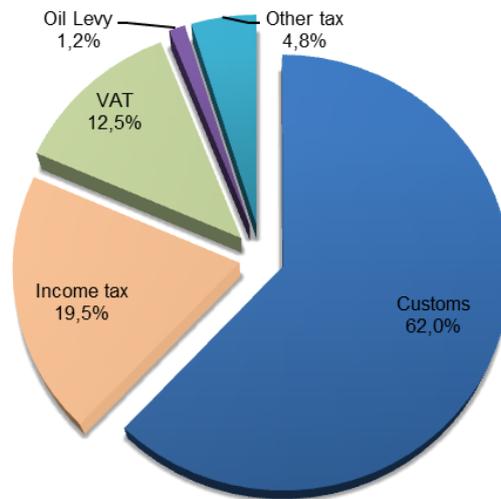


Source: World Bank, 2010.

The major source of revenue is taxes (89 per cent) and, within this group, custom revenue constitutes more than 60 per cent of the total (36.3 per cent of GDP). This strong dependence on one category of funds, far from declining over the years, has become even more marked, rising from 54.4 per cent in 2004 to 62.0 per cent in 2008 (figure 48). The

participation of VAT, on the other hand, fell between 2004 and 2008 from 17.7 per cent to 12.5 per cent of total taxation (figure 48).

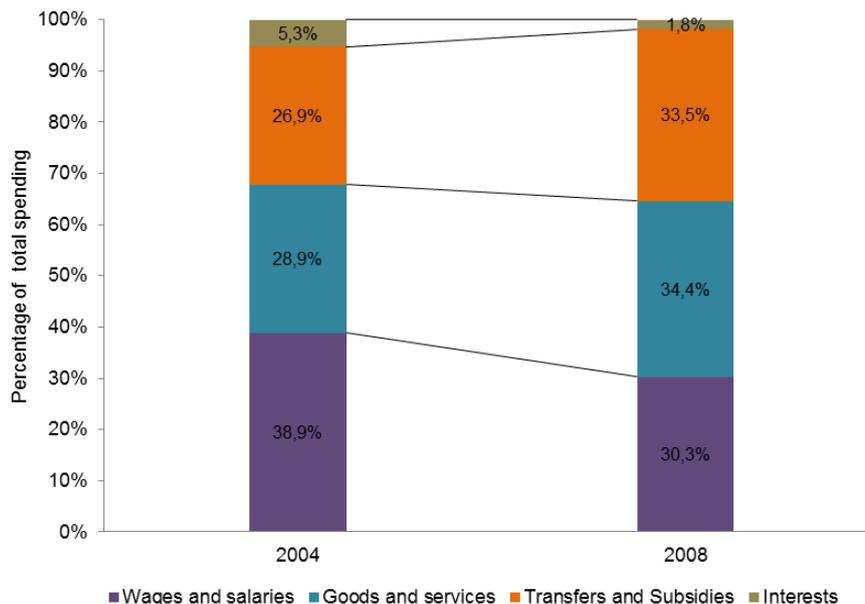
Figure 48. Lesotho: Structure of tax revenues, 2008



Source: Ministry of Finance and Development Planning, 2009b.

Important changes in the structure of government spending have emerged during the last five years. First, public expenditure as a percentage of GDP grew quickly, and by 2008 the Ministry of Finance and Development Planning was able to report a 61.7 per cent participation rate. Second, wages, formerly the most important component, now account for the third largest share of GDP (figure 49), lagging behind goods and services (34.4 per cent) and transfers and subsidies (33.5 per cent). As will be seen later, the introduction of a universal old-age pension programme in 2004 helps to explain the shift in the allocation of public funds.

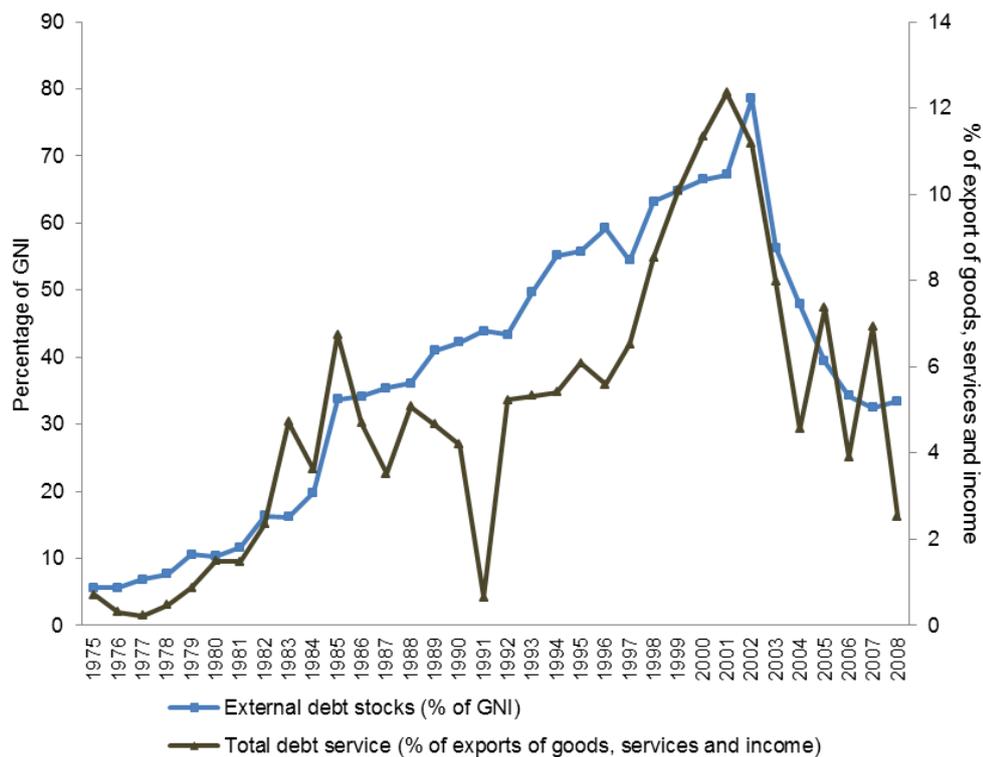
Figure 49. Lesotho: Structure of public expenditure, 2004 and 2008



Source: Ministry of Finance and Development Planning, 2009b.

Interest payments on both foreign and domestic debt have accounted for a smaller share of Government expenditure. This is the result of a falling external debt since 2002 when it peaked at 78.5 per cent of GNI. By 2008 external debt made up 33.4 per cent of GNI, almost half the level of a decade earlier but higher than that of most of the least developed countries in Africa. Similarly, total debt service corresponds to only 2.5 per cent of total exports after a high of 12.3 per cent in 2001 (figure 50); in other words, the country in general was able to free resources for other purposes thanks to its responsible debt management. However, the Ministry of Finance expects some growth in debt repayments and interests between 2010 and 2013. In short, Lesotho's reduced debt payments generate gains in overall fiscal space, regardless of whether they were fully or partially allocated to social protection expenditure.

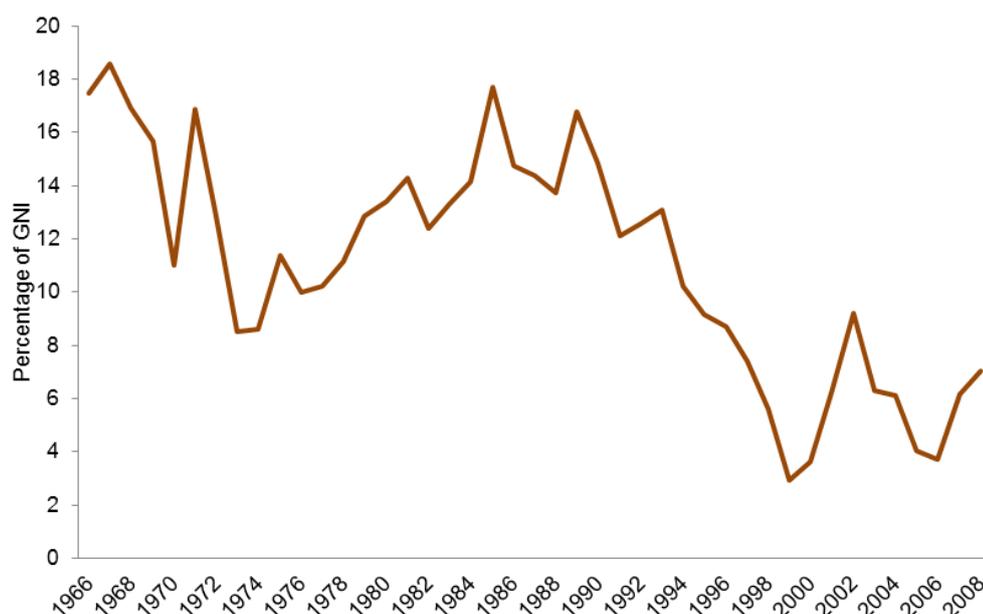
Figure 50. Lesotho. External debt and total debt service in Lesotho, 1975-2008



Source: World Bank, 2010.

Another feature that has characterized Lesotho in the last three decades has been the relatively small flows of ODA that the country has received to finance its development. Between 1980 and 2008 (figure 51) ODA averaged 10.1 per cent of GNI, having doubled between 2000 (3.6 per cent) and 2008 (7 per cent).

Figure 51. Lesotho: ODA as a percentage of GNI, 1966-2008



Source: World Bank, 2010.

As to the social sector, poverty and inequality remain at very high levels. The incidence of poverty, measured as the share of the population living on less than US\$1.25 a day, was 43 per cent among the Basotho people (table 10). Considerable progress has, however, been observed since 1999, when poverty was estimated at 68 per cent of the population according to a Poverty Mapping Exercise. Deprivation is mostly concentrated in remote rural areas, particularly the Mountain and the Sengu River zones (Save the Children UK, HelpAge International, Institute of Development Studies, 2005). Inequality persists as a major problem and Lesotho's Gini coefficient is among the highest in the world (0.62, in 2nd place). In addition, malnutrition among children under 5 years old is chronically high, particularly in the mountain region (42 per cent) and in the Senqu River Valley (54 per cent) (WFP, 2008).

Table 10. Lesotho: Main social indicators

Indicator	Date	Latest available information	Source
Population living on less than US\$1.25 a day	2003	43.4 per cent	World Bank, 2010.
Gini index	1995	62.5	UNDP, 2009.
Human Development Index ranking	2011	160	UNDP, 2009.
Life expectancy at birth (women)	2008	45.5 years	World Bank, 2010.
Life expectancy at birth (men)	2008	44.4 years	World Bank, 2010.
Infant mortality rate	2008	63.1 deaths per 1,000 live births	World Bank, 2010.
Infants with low birth-weight	2004	13 per cent	World Bank, 2010.
Estimated HIV prevalence among persons in the 15–49 year age group	2009	23.6 per cent	World Bank, 2010.
Literate women over 14 years old	1999-2007	90.3 per cent	UNDP, 2009.
Literate men over 14 years old	1999-2007	73.7 per cent	UNDP, 2009.

One of the main challenges faced by policymakers is to reduce the prevalence of HIV and AIDS, which currently affects about a quarter of the population between 15 and 49 years old. Lesotho has the third highest HIV prevalence rate in the world (Kaiser Family Foundation, 2005), with 270,000 PLHIV and 100,000 orphans of one or both parents due

to HIV and AIDS. The prevalence of high HIV and AIDS is responsible for the low life expectancy at birth (44 years) because of the high level of neonatal deaths (56 per cent) caused by the disease.

7.2. Social protection programmes: Initiatives and financing

Despite the substantial progress observed in the last 15 years, a large segment of the Basotho population continues to suffer from poor socioeconomic conditions. There is therefore every reason to establish an extensive network of social protection programmes that comprises social insurance, food protection and health initiatives, etc. The next three sections present a broader picture of existing programmes in Lesotho, particularly the main features of the universal old-age pension, as well as of the performance of the country in terms of providing the necessary financing to operate the programmes.

7.2.1. Social protection programmes

According to the Regional Hunger and Vulnerability Programme report of 2007, there are more than 20 different social programmes in Lesotho aimed at protecting a wide range of population groups from poverty, hunger, economic shocks and unemployment. The programmes are divided into four categories, and table 11 refers to all those that the Government finances or implements in full or in part.

Table 11. Lesotho: Social protection programmes

Social protection	Social insurance	Food transfers	Farming inputs	Health and other
Cash transfer	Old-age pension	Food transfers – WFP and C-SAFE	FAO emergency and rehabilitation	Lesotho AIDS programme
Lesotho Fund for Community Development	War veterans pension	School meals programme	Increase food production (KR2)	LHDA Compensation and Resettlement Programme
Disability allowance	Civil servant pension	Food for Work programme		Mother-Child Health Programme
Minimum threshold allowance		Targeted vulnerable group meals		Supplementary meals
		Food support for orphans and vulnerable children		Therapeutic meals Free health

Note: LHDA- Lesotho Highlands Development Agency
WFP – World Food Programme
FAO – Food and Agriculture Organization
Source: Regional Hunger and Vulnerability Programme, 2007.

Although there are many public and non-public initiatives in Lesotho, only five programmes are critical in terms of coverage and fiscal impact: the non-contributory old-age pension scheme, the civil servant pension schemes, the cash transfer programme, the school meals programme and some in-kind programmes.

The school feeding programme was introduced several decades ago with the objective of providing supplementary meals for needy children in all primary schools in Lesotho. It was also an essential part of the strategy for ending hunger and poverty in Lesotho (Lambers,

2009).²² Only students enrolled in the education system are entitled to benefits under the programme.

Before 2009 the programme received considerable support from the United Nations World Food Programme (WFP) which by 2004 was providing assistance to 176,393 children, of whom 51 per cent were girls. Thereafter this assistance started to decline and by 2007 the number of student beneficiaries was 113,695 (Lambers, 2009). The programme entered into a new phase after 2008 when the Government started to take full control of the initiative while the WFP reduced the number of assisted schools, lowering its coverage to 80,000 children in 2008, to 65,000 in 2009 and to 50,000 in 2010. This however did not mean that fewer children were receiving benefits, because the Government increased the number of beneficiaries at public schools. The Ministry of Education and Training is to have taken over the programme fully by the end of 2010 and to cover 100 per cent of school-children by 2011.

The primary objective of cash transfers and transfers in kind is to provide a safety net for all vulnerable groups in Lesotho, including the elderly, the chronically ill, orphans and vulnerable children and disabled people. Potential beneficiaries are targeted by a process of vulnerability assessment and the transfer takes place once the person concerned has been identified as belonging to a high-risk group. The cash transfer amounts to M100 per person per month (100 maloti equal roughly US\$12.85). According to the Ministry of Finance and Development Planning (2010b), during the fiscal year 2009/10 some 2,000 orphans received cash grants (roughly 10 per cent of orphans) and 27,000 orphans (13.5 per cent) were provided with packages which include food, shelter and educational support.

Overall, the number of beneficiaries (and hence the coverage rate of certain programmes) is certainly higher than reported by the Government, given the participation of NGOs and charity organizations that complement the public effort. For instance, according to the Regional Hunger and Vulnerability Programme (2007), the Food for Assets Programmes implemented and managed by CARE SA Lesotho, World Vision, Catholic Relief Services and TEBA Development covered almost 5,600 persons in 2007.

Since 1991 the Lesotho AIDS programme, managed by the AIDS Programme Coordinating Authority, provides testing, counselling, home care and medication for PLHIV. Social assistance in this regard has been increasing at a rapid rate during the last five years. While in 2005 a total 65,215 PLHIV required antiretroviral treatment (ART) only 8,684 persons received it (13 per cent coverage); by 2009 an estimated 122,818 persons were in need of ART and 62,190 were receiving treatment (51 per cent). In 2010 the Coordinating Authority expected 126,251 persons to be in need of ART and set a coverage goal of 80 per cent.

7.2.2. Social programme financing

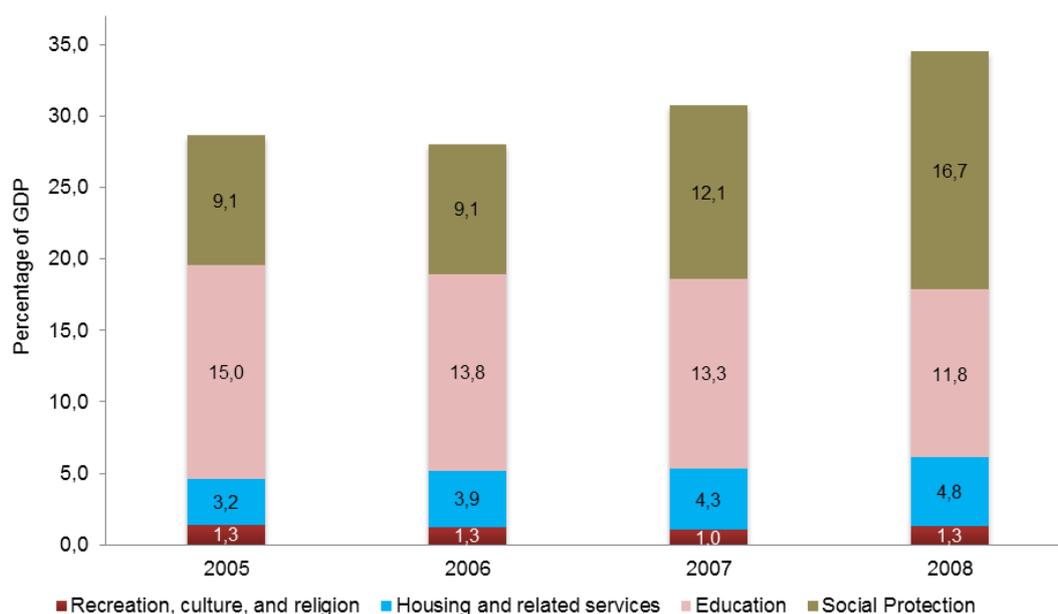
Social programmes were traditionally financed with budgetary allocations. This situation changed after 2008, however, when the Government introduced the new contributory system mentioned above. By 2009 roughly 90 per cent of expenditure on social protection came from taxation.

Lesotho reports one of the highest rates of social spending in Africa. This fact is quite remarkable as Lesotho is a least developed country. If housing, education and recreation

²² <http://voices.yahoo.com/ending-child-hunger-school-feeding-lesotho-2458263.html>

are included, total expenditure on social programmes accounted for 30.5 per cent of GDP between 2005 and 2008.

Figure 52. Lesotho: Composition of social spending as a percentage of GDP, 2005-2008



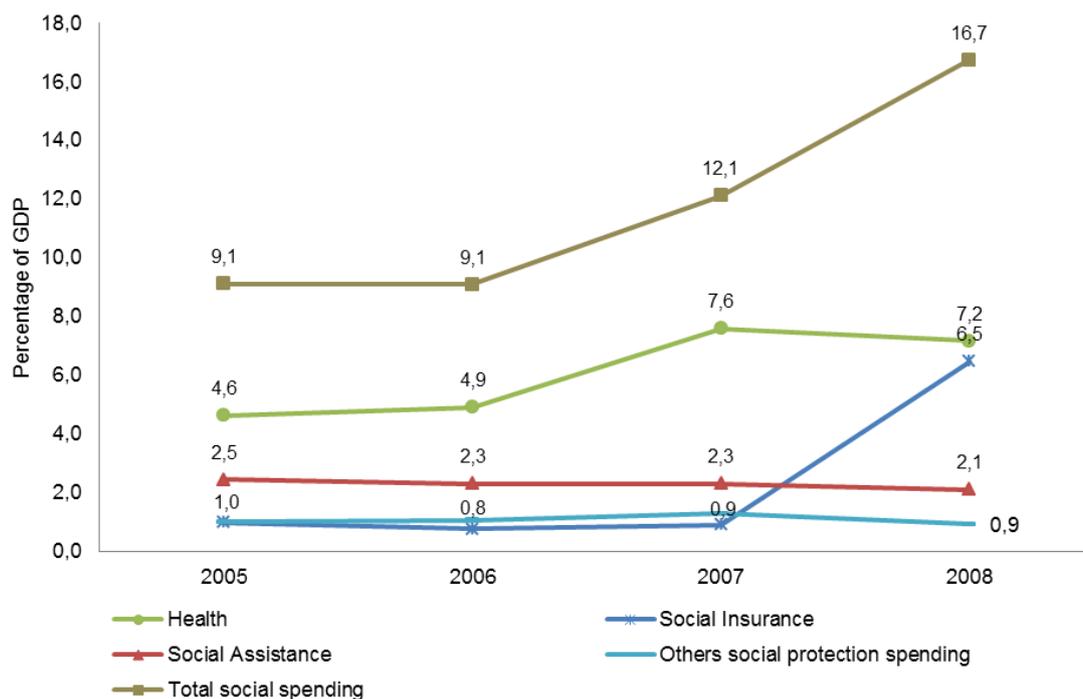
Source: Ministry of Finance and Development Planning, 2007, 2008 and 2009b; International Monetary Fund, 2010b.

The largest share of the expenditure went to education, which accounted for 13.5 per cent of GDP during the period (figure 52). Proportionately, Lesotho spends almost three times the worldwide average level of expenditure on education (about 4.4 per cent of GDP). Social expenditure corresponding to recreation and housing has not undergone significant changes in recent years.

Social protection (social insurance, social assistance, health and others) has continued to grow, from 9.1 per cent of GDP in 2005 to 16.7 per cent in 2008. In net terms, total expenditure on social protection between 2005 and 2008 gained 7.6 percentage points of GDP; measured over a longer period the figure is even higher (figure 53). The recent trend in total social protection spending can be divided into three phases. Prior to 2004 social protection expenditure was focused mainly on social insurance payments (Civil Servants Pension System). Social assistance did not account for more than 0.2 per cent of GDP while public transfers to pensions accounted for an average of 1.8 per cent. From 2004 to 2008 the establishment of the old-age pension scheme increased social assistance spending substantially, up to 2.1 per cent of GDP in 2008.

Expenditure on social insurance remained stable until 2007, between 0.8 per cent and 1.0 per cent of GDP. Expenditure on health had also experienced a significant increase. While in 2000 public health spending accounted for 4 per cent of GDP, by 2008 it had reached 6.5 per cent. In real terms, the per capita spending on health almost doubled in the eight years between 2000 and 2008, from 148.4 maloti (about US\$19) to 286.2 maloti (US\$37).

Figure 53. Lesotho: Expenditure on social protection as a percentage of GDP, 2005-2008



Source: Ministry of Finance and Development Planning, 2007, 2008, 2009a and 2009b; International Monetary Fund, 2010b.

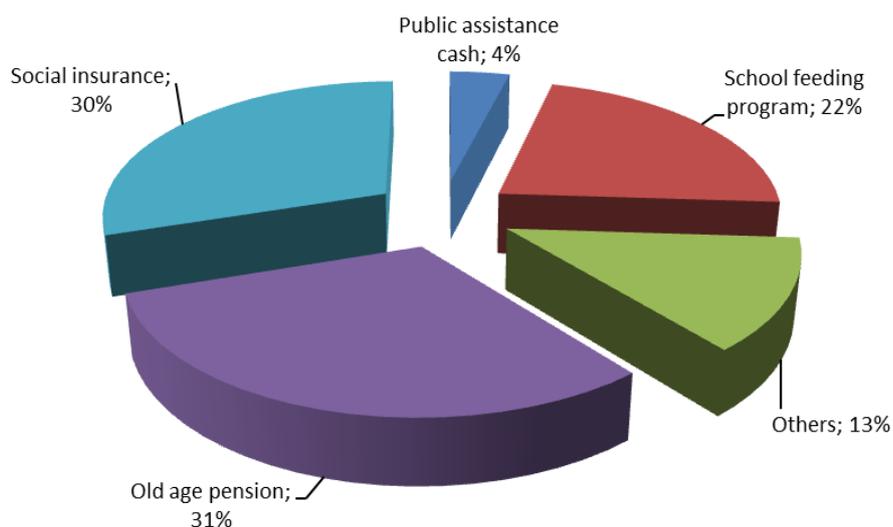
7.2.3. Old-age pension scheme

The old-age pension (OAP) programme was launched in November 2004 as a universal scheme aimed at increasing the living standards and reducing the incidence of poverty among older people. The programme was designed to cover all people aged 70 years or more, who were initially entitled to M150 per month (about US\$22 at the time). The Government has applied successive increments to the pension, the last one in the 2009/10 fiscal year when the transfer was doubled to M300 per month (US\$39.7). Lesotho is the only least developed country in Africa with a non-contributory pension scheme and, along with Nepal, one of the only two least developed countries in the world to have a non-contributory pension scheme (Pelham, 2007).

Coverage under the old-age pension scheme reflects a clear trend toward universalization. In May 2005 there were 69,046 beneficiaries, about 93.3 per cent of the target population. According to the Ministry of Finance and Development Planning (2010a) the 2010 budget earmarked sufficient funds (M295 million or roughly US\$38 million) to cover 81,245 beneficiaries – in other words, universal coverage.

As to the share of expenditure on pensions in overall social protection spending, the composition of the latter for 2009 is presented in figure 54. The OAP and the new defined contribution pension fund jointly represent 61 per cent of total social protection expenditure. The school meals programme in 2010 is now the third most important initiative, accounting for 22 per cent of the social protection budget. Given the target, set by the Government, of reaching all schools by 2011, the Ministry of Finance expects the programme to absorb 25 per cent of expenditure on social protection by 2012.

Figure 54. Lesotho: Composition of social protection expenditure, 2009



Source: Ministry of Finance and Development Planning, 2010a.

7.2.4. Other pension schemes

Three pension schemes exist in Lesotho: the African Pioneer Corps (APC) pension, the smallest in terms of the number of beneficiaries and of cost; the recently established contributory pension scheme for civil servants, to which both the Government and the public employees contribute, and a non-contributory old-age pension scheme established in 2004 (mentioned in the previous section).

The beneficiaries of the APC pension comprise World War I and World War II veterans and their widows who are citizens of Lesotho. The programme is to be merged with the old-age pension scheme.

In 2008 the Government reformed the civil servant pension system and transformed it from a defined benefit scheme to a fully funded defined contribution scheme. Previously, it had been a pay-as-you-go system that granted people pensions upon retirement. It was fully financed by the public budget, but the increasing financial burden resulted in the Government converting it into a contributory scheme based on defined contributions. Under this system both parties (Government and employees) contribute a share of the workers' annual salary to a pension fund – 5 per cent from the employees and 11.2 per cent from the Government. Only employees aged 45 years old or less are part of the new scheme. Under the new system, unlike the earlier system, the pension can be left to the spouse and children in case of death, so that the family remains protected even in the absence of the official beneficiary. An Independent Board of Trustees administers the pension fund.

7.3. Fiscal space for social protection

Lesotho is an outstanding example of the extension of fiscal space for social protection purposes. As was stated in the previous section, social assistance and social insurance expenditure grew by a multiple of 3.2 and 2.1 respectively between 2005 and 2010. In other words, they grew much faster than the economy as a whole. To achieve this, the country utilized several mechanisms:

-
1. The old-age pension scheme was included in the financial statement for 2004/05 by the Lesotho Congress for Democracy after several attempts to formalize the new programme. As a result, increasing protection was granted, first, to an ever increasing population and, second, by doubling the amount of the transfer between 2005 and 2009.
 2. The civil servant pension scheme was restructured, from a non-contributory defined benefit scheme to a contributory fully funded defined contribution scheme in 2008, allowing for an expansion of total financing for social insurance objectives. In other words, the Government made use of the establishment of a 5 per cent payroll tax to expand fiscal space (at least from the standpoint of public employees).
 3. The administration and funding of the school meals programme was taken over by the Ministry of Education and Training and the universal coverage of schools by 2011 that the Government decided upon speeded up the allocation of resources to the programme.
 4. Certain vulnerable groups like orphans, the elderly, the disabled and PLHIV were given priority and coverage of the latter group with ART treatment was accelerated.

Progressive increments in social protection financing were achieved under quite interesting conditions. Contrary to what has been observed in other nations such as Botswana and Mozambique, which enjoyed exceptionally high growth rates, reduced debt payments and/or substantial ODA flows, most of the fiscal space determinants in Lesotho performed just moderately. Long-term economic growth was 4.6 per cent per year, about 60 per cent of the rate in Mozambique and 40 per cent of the rate in Botswana. Moreover, ODA resources were well below those of Lesotho's close neighbours and, although external debt declined, it did not do so to the extent observed among the group of heavily indebted poor countries.

What makes Lesotho markedly different from other African countries is its ability to collect taxes, taking full advantage of its economic growth and dynamic external trade. The fiscal burden in Lesotho exceeds by far the average revenue collection capacity of sub-Saharan countries, with the result that between 2005 and 2008 tax revenue was 10 percentage points higher than in the previous decade and 15 percentage points higher than in the previous 15 years. Public spending, however, was much more prudent, increasing only by 4.4 percentage points of GDP between 2000/04 and 2005/08.

From a political standpoint, two issues need to be highlighted here. First, the introduction of new social benefits such as the school meals programme and the old-age pension comes with a clear political commitment to approve the required legal amendments, implement critical reforms and reallocate additional financing to social benefits. Nyanguru (2007) explains that the introduction of the old-age pension scheme, for instance, was the result of an initiative by the Prime Minister despite opposition from development partners within the United Nations that favoured increasing allocations of resources to education instead.

Furthermore, the increasing allocation of resources to social protection was accompanied by an increase for other social sectors too, thus reinforcing the idea that a political willingness to improve social financing was a constant throughout the last decade. As has been noted before, the introduction of the old-age pension scheme constituted a 3 percentage point increment in GDP terms by 2009 and the school meals programme contributed with an additional 2.2 percentage points. Similarly, public health spending grew by 2.5 percentage points and public education also gained 1 percentage point between 2000 and 2009, despite the fact that its share started to decline after 2006. Altogether, the four programmes (old-age pensions, school meals, public health and public education) accounted for a net increment of 8.7 points of GDP during the 2000s, much

more than the 4.4 percentage points by which overall public spending grew during the same period.

7.4. Challenges and lessons learnt

7.4.1. Challenges

The Government of Lesotho faces major challenges if it is to improve the impact of its programmes and the sustainability of its overall social policy.

1. Regarding the old-age pension scheme, the country faces the challenge of expanding coverage by reducing the age limit from 70 years to 65, which is the international standard for this type of programme. The Government has made significant progress in providing effective protection for the beneficiaries, first by achieving practically universal coverage and second by establishing a pension above the poverty line. The next step is to expand the target group to include the 65-69 year age group, which would extend the scheme to a further 32,300 beneficiaries and cost M116.3 million (some UD\$15 million) – 41 per cent of the expected budget for the old-age pension programme in 2011.
2. A second challenge facing Lesotho is to increase coverage among other vulnerable groups. Although the figures show that a large number of children (including orphans) and PLHIV are beneficiaries of one or other of the existing social protection programmes, coverage rates hardly exceed 50 per cent among the target groups. The expectation that fiscal revenue will decline in the next years will certainly limit the capacity of the Government to expand its social protection programmes, so the major challenge will be to assist more people with the same volume of resources.
3. A third challenge is to pursue the reform of the social insurance scheme. Moving to a contributory pension scheme was an important step in increasing fiscal space, and the Government can now start assessing the possibility of creating a comprehensive contributory social security system in order to cover maternity, sickness, employment injuries, family allowances, among others.
4. Lastly, there is a need to improve tax collection from other sources that at the moment play a relative minor role. VAT, for example, brought in less than 15 per cent of total taxation in 2009, and together with income tax accounted for only three of every 10 maloti coming from taxation. There is thus still room for increasing their participation in the tax structure.

7.4.2. Lessons learnt

Lesotho offers important lessons for countries operating under better macroeconomic conditions which still lag behind in terms of social spending. Without experiencing above-average growth and international aid conditions, Lesotho has been able to expand fiscal space for social protection purposes significantly. From this we can draw the following lessons.

Lesson 1

Raising the level of financing for social protection calls for a Government that is able to manage boom conditions responsibly and to think strategically about how to spend the additional resources. Favourable macroeconomic and fiscal conditions plus a continuous decline in debt payments increased fiscal space and were complemented by other structural

changes in the financing of contributory pension schemes. As a result, the country expects the protection of the elderly to be universal within the near future.

Lesson 2

Prudent fiscal management is critical for the sustainability of the Government's overall social strategy. Despite a rapid increase in revenue, the Government did not embark on a corresponding expansion of public spending, but opted instead for controlled increments under certain budgetary headings (such as salaries) while giving priority to allocations for social protection. Regular surpluses and the wide gap between revenue and expenditure (4 percentage points of GDP in 2009) have allowed the Government not to sacrifice its social protection budget to any great extent in times of crisis. Its savings may in fact permit increments in social coverage.

Lesson 3

The Prime Minister and the key political parties have demonstrated a strong political commitment to approve and proceed with the allocation of more resources to existing programmes, to open up additional fiscal space by implementing new social programmes and to reform existing mechanisms that were not financially sustainable in the long term.

8. Namibia: When politics overcomes limited resources

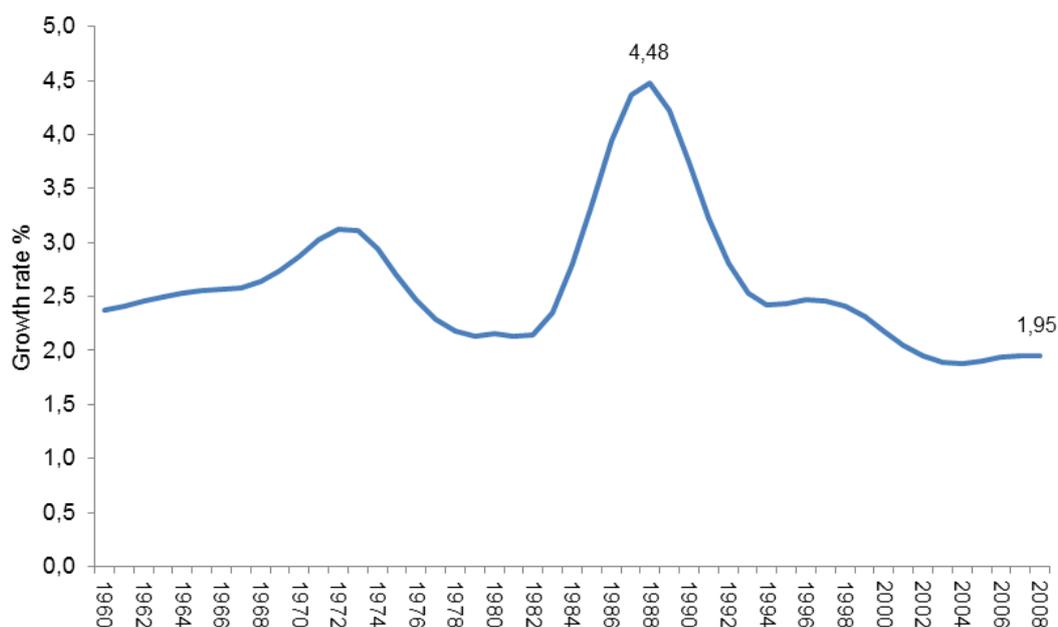
8.1. Country profile

The Republic of Namibia is located in the southern part of Africa, bordering Angola and Zambia to the north, South Africa to the south and east, Botswana and Zimbabwe to the east and the Atlantic Ocean to the west. The country became independent in 1990 and is one of the largest nations of the southern part of the African continent, with a total territory of 825,418 square kilometres.

Despite possessing such an extensive territory Namibia's population is small, with an estimated 2.2 million inhabitants in 2010, similar to that of neighbouring countries such as Botswana and Lesotho. Population density is 2.5 persons per square kilometre, one of the lowest in the world.

Since Independence Namibia's population has increased by a factor of 1.6, growing at an annual average of 2.3 per cent. Population growth has, however, been declining. It stabilized at roughly 1.95 per cent per year during the last 5 years (figure 55), but the downward trend is expected to continue in the long term and the annual rate to drop to a mere 0.1 per cent by 2025. The overall fertility rate is estimated to have declined from 4.6 births per woman in 1995 to 1.8 births in 2025.

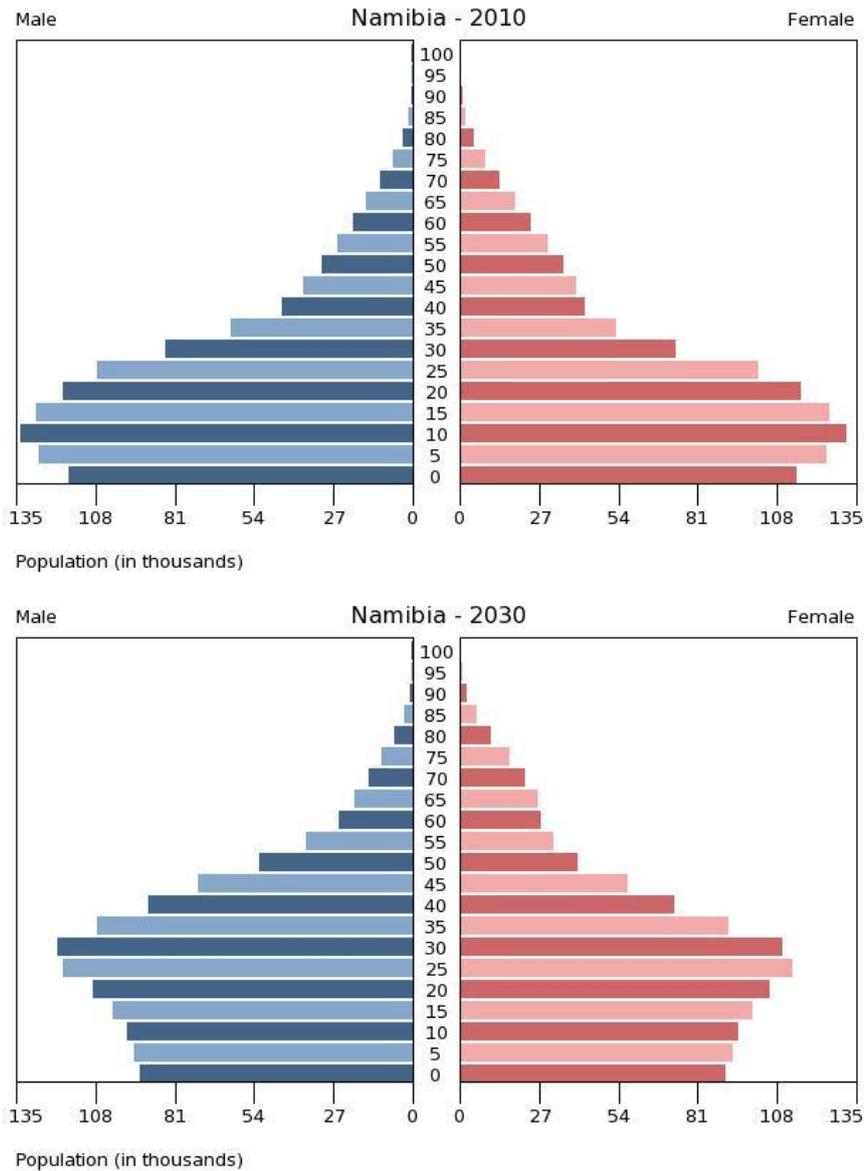
Figure 55. Namibia: Population growth rate, 1960-2010



Source: World Bank, 2010.

Namibia has a young population whose median age is around 20 years. No accelerated aging process is envisaged in the short or medium term. The mean age is expected to increase to 21.7 years in 2025 and to 29.9 years by 2050 (UNFPA, 2009). In terms of participation of the different age groups (figure 56), this implies that children below 15 years old will make up 24.6 per cent of the total population in 2030 (35.1 per cent in 2010) while people over 65 years of age will account for 6.1 per cent (currently 4 per cent).

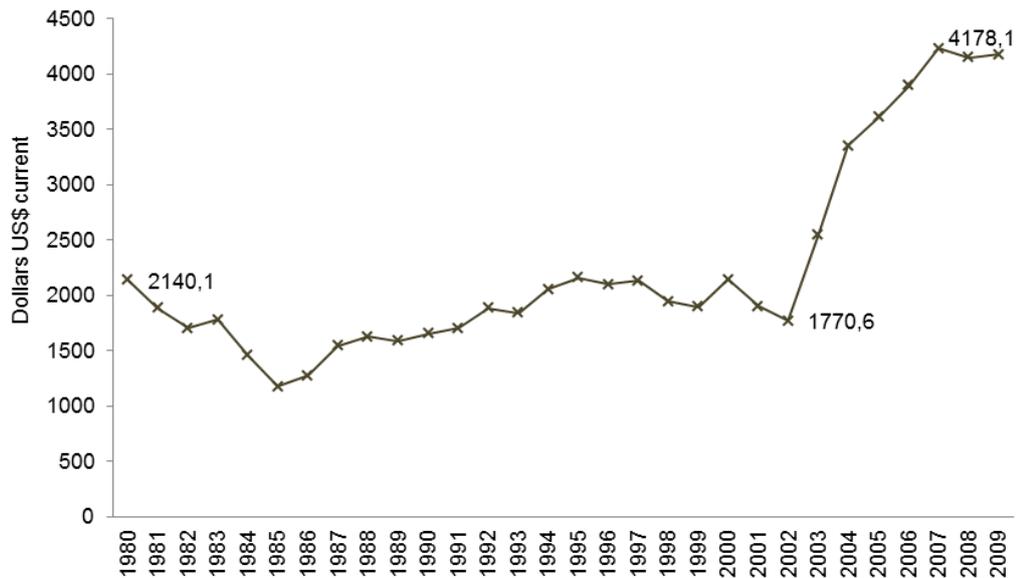
Figure 56. Namibia: Population pyramids for 2010 and 2030



Source: US Census Bureau, 2010.

From an economic standpoint, Namibia is a low-middle-income country with a GDP per capita in 2009 of US\$4,178 (US\$6,457 in PPP terms). Annual economic growth before independence was low, averaging 1.1 per cent between 1981 and 1989. The decade that followed Independence improved the country's overall economic circumstances and its average annual growth rate tripled from the previous decade (3.8 per cent per year). However, it was during the 2000s that Namibia enjoyed a substantial boost to its GDP, with rates moving from 2.5 per cent to 12.3 per cent for an average of 5.2 per cent per year. As a result, GDP per capita, measured in nominal terms, showed a remarkable increase during this period, from US\$ 1,770 in 2002 to US\$ 4,178 in 2008 (Figure 57).

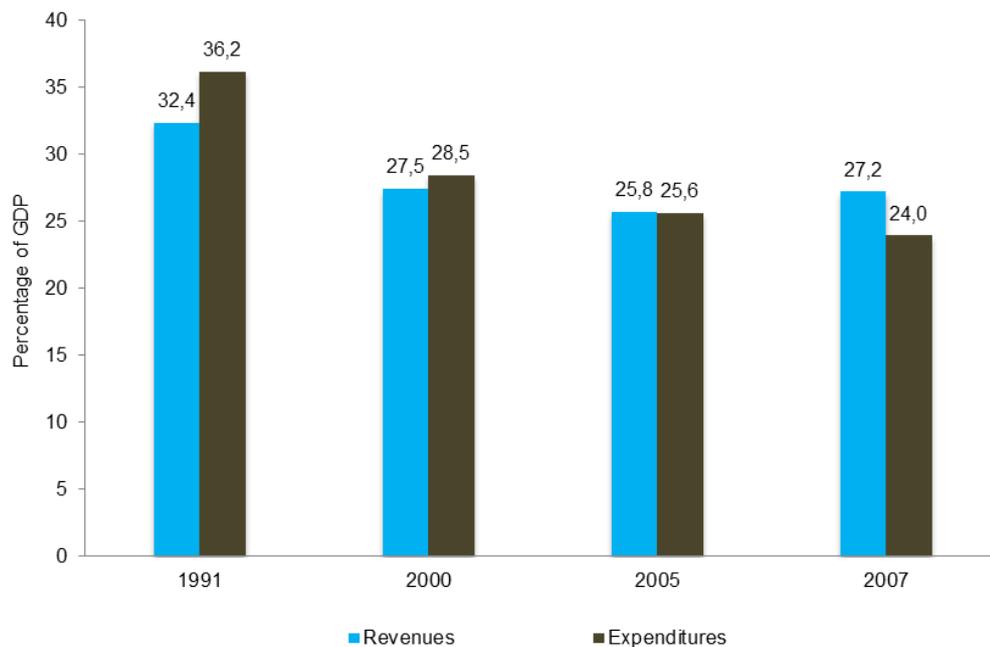
Figure 57. Namibia: GDP per capita, 1980-2008 (US\$ current)



Source: World Bank, 2010.

Contrary to neighbouring countries such as Botswana and Lesotho whose fiscal position changed significantly, Namibia's public finances have remained at a more or less constant level since Independence (figure 58). In 1991 tax revenues accounted for 32.4 per cent of GDP and public spending for 36.2 per cent. Perhaps the most important factor in this respect was the strong decline in the participation of public spending, which dropped to 24 per cent of GDP in 2007. As a result, the net balance of the Namibian Government moved from a deficit in the 1990s to a surplus by the end of the 2000s. This was achieved by reducing expenditure instead of increasing revenue collection. In fact, the share of tax revenue in GDP also fell between 1991 and 2007.

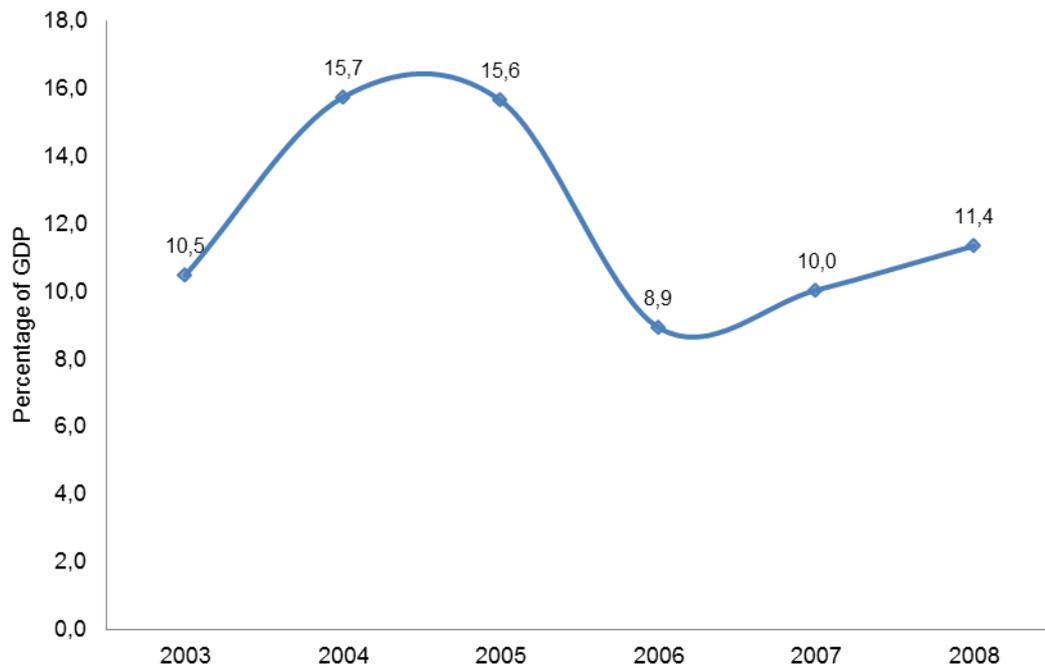
Figure 58. Namibia: Tax revenues and public spending as a percentage of GDP (several years)



Source: World Bank, 2010.

External debt remained at a manageable level during the 2000s (12 per cent of GDP), with a slight drop in average terms during the second half of the decade (figure 59). This reduction in the external debt seems to have contributed to the fiscal surplus experienced in the late 2000s, as is evidenced by the decline in public expenditure on debt service from 7.2 per cent of GDP in 1990 to 1.6 per cent in 2008.

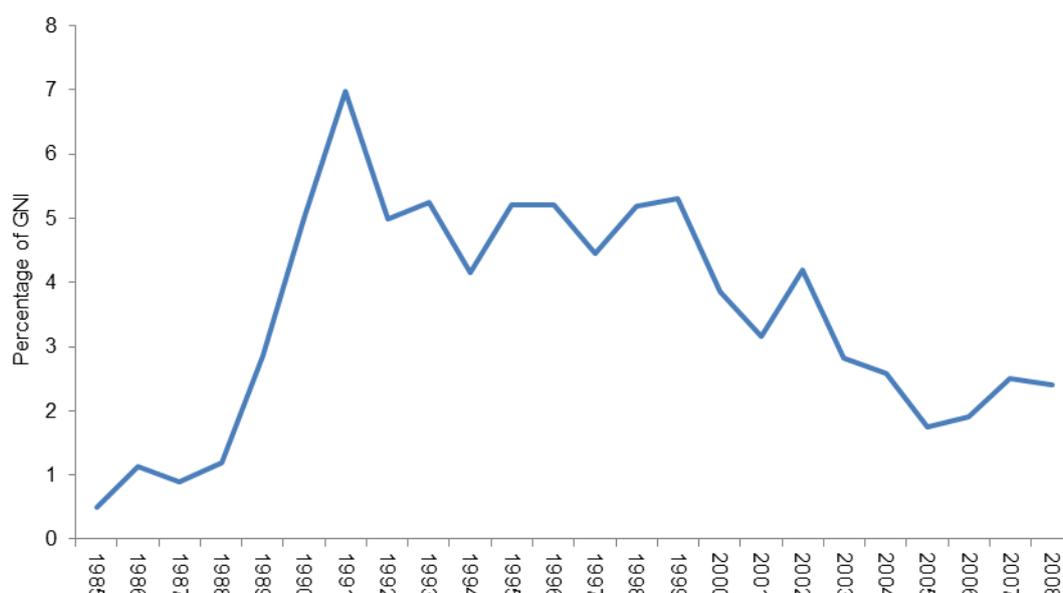
Figure 59. Namibia: External debt as a percentage of GDP, 2003-2008



Source: World Bank, 2010.

Another remarkable feature of Namibia's recent economic evolution is the low level of ODA received by the country since 1990. On average, ODA constituted 4.1 per cent of the gross national income (GNI) between 1990 and 2008, but it declined substantially to 2.8 per cent of GNI during the 2000s. This contrasts with the experience of countries such as Mozambique which on average received ODA flows that were above 15 per cent of GNI.

Figure 60. Namibia: Official development assistance as a percentage of GNI, 1985-2008



Source: World Bank, 2010.

Namibia is a country of interesting socioeconomic contrasts. Poverty incidence and infant mortality are below Africa's average, but the country presents the highest Gini coefficient in the world. Progress in the Human Development Index (HDI) has been slow since Independence (0.657 to 0.686 between 1990 and 2007). High HIV prevalence rates (roughly 390,000 PLHIV) affect over 15 per cent of the population and influence life expectancy, which is the same now as in 1985. Adult literacy and GDP per capita contribute positively to improving the country's position on the HDI, but enrolment in literacy programmes is now the sand in the wheels of the Government's attempts to improve overall socioeconomic conditions. For instance, where the adult literacy rate was 76 per cent in 1990, by 2007 it had jumped to 88 per cent of the target population. However, at the same time, enrolment of children in primary and secondary education was under 70 per cent during the 2000s after having reached a high of 83 per cent in 1995.

Table 12. Namibia: Socioeconomic conditions

Indicator	Outcome	Year	Source*
Poverty incidence (as percentage of total households)	27.6	2008	Central Bureau of Statistics, 2008.
Gini coefficient	74.3	1992-2007	UNDP, 2009.
Human Development Index	0.678	2007	UNDP, 2009
Life expectancy at birth (in years)	60.4	2007	UNDP, 2009.
Infant mortality rate (per 1,000 live births)	31.4	2007	World Bank, 2010.
Maternal mortality rate (per 100,000 live births)	210	2005	World Bank, 2010.
HIV and AIDS prevalence (as a percentage of population aged 15-49)	17.8	2008	Ministry of Health and Social Services, 2008.
Adult illiteracy rate 2007 (as percentage of population aged 15 or more)	12	2007	UNDP, 2009.

* Last column shows the sources for each individual indicator.

8.2. Social protection: Programmes and public spending

According to a government statement in 2008, Namibia's integral social protection strategy consists of more than 15 policy initiatives aimed at ensuring equitable access to basic social and welfare services as a means of achieving equality and enhancing welfare – in particular, access to these services for the underserved and un-served vulnerable and marginalized segments of society. They also seek to reduce inequalities in social welfare, instil culture and morality in the population (especially the youth) and promote gender equality, in order to contribute to a more equitable society.

The full list of existing programmes is presented in table 13. Five different institutions manage all the programmes, with the Ministry of Labour and Social Welfare, the Ministry of Gender Equality and Child Welfare and the Social Security Commission (SSC) as the key players in the social welfare strategy. Other programmes may not fall within the realm of social protection, but they do have a social purpose (for instance, the Ministry of Lands and Resettlement is in charge of securing land for the landless rural population through resettlement).

Table 13. Namibia: Social protection programmes

Programme	Managing institution
Old Age Grant	Ministry of Labour and Social Welfare
Disability Grant	Ministry of Labour and Social Welfare
Funeral Benefit	Ministry of Labour and Social Welfare
Places of Safety Allowance	Ministry of Health and Social Services
Special Maintenance	Ministry of Gender Equality and Children Welfare
Maintenance Grant	Ministry of Gender Equality and Children Welfare
Foster Parent Allowance	Ministry of Gender Equality and Children Welfare
Veterans Subvention	Ministry of Veteran Affairs
Maternity Leave & Sick Leave	Social Security Commission
Death Benefit	Social Security Commission
National Pension Fund and National Medical Benefit Fund	Social Security Commission
Development Fund	Social Security Commission
ECF (Employees' Compensation Fund)	Social Security Commission
Housing programmes	Ministry of Regional, Local Government and Housing
Motor Vehicle and Accident Fund	Motor Vehicle Fund

Source: Government of the Republic of Namibia, 2008.

From a budgetary perspective, the Ministry of Finance is responsible for the allocation of resources for social assistance programmes, while the Social Security Commission manages payroll contributions collected from employers and employees in order to finance the social insurance scheme.

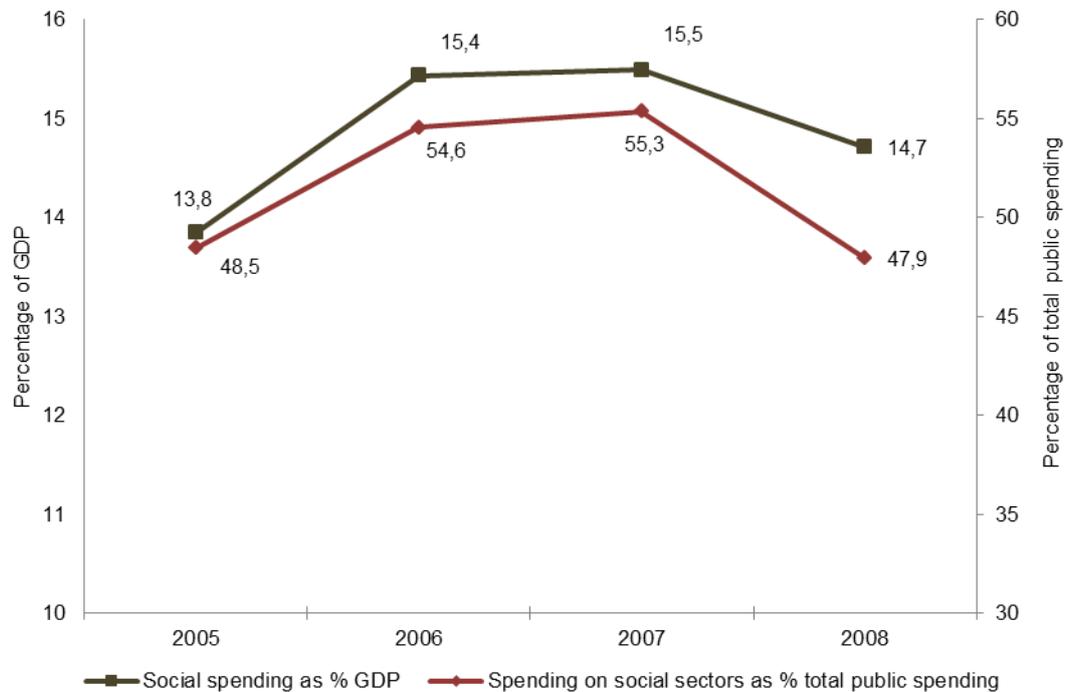
8.2.1. Social spending and expenditure on social protection

Two main features characterized social spending in Namibia during the second half of the 2000s. First, it accounted for a significant share of production and total government spending and, second, it followed an upward trend despite some cut-backs in 2008. Between 2005 and 2008, in fact, social spending constituted 14.9 per cent of GDP, a figure that compares with that of South Africa (14.9 per cent) and Botswana (15.5 per cent),

exceeds the level of social investment in Mozambique (10.2 per cent of GDP) but is still far below that of Lesotho (30.5 per cent).

During the same period almost 52 per cent of government spending was allocated to the social sector (figure 61). This high average may reflect strong political support in favour of stepping up investment in that area. In fact, with the exception of 2008, social spending kept growing from 48.5 per cent to 55.3 per cent of total government expenditure.

Figure 61. Namibia: Public social expenditure, 2005-2008

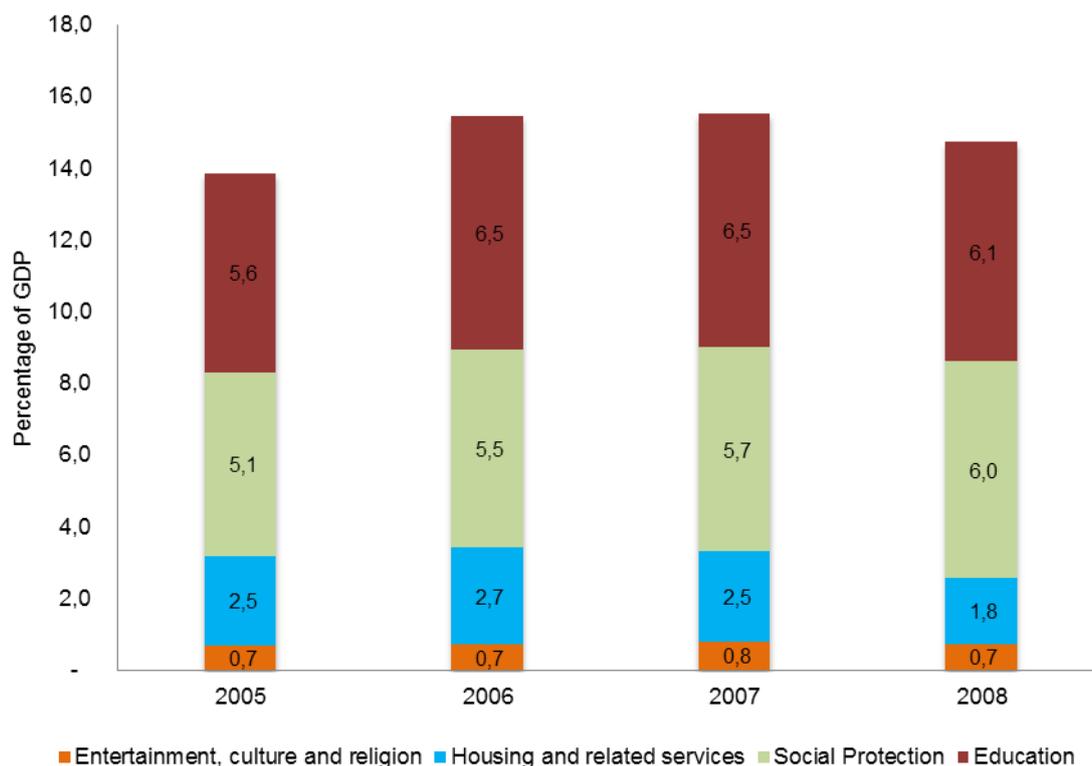


Source: Ministry of Finance, 2009; International Monetary Fund, 2010b.

Regarding the composition of social expenditure, education accounts for the highest share, but expenditure on social protection has been the fastest growing component in recent years. Government spending on education averaged 6.2 per cent of GDP between 2005 and 2008, while social protection received the equivalent of 5.6 per cent of GDP and its share increased by 18.2 per cent during the same period (figure 62).

The pattern described here is a particular feature of Namibia that is not frequently observed in other nations. Typically, the tendency of neighbouring countries has been to allocate the highest share of social spending to education, sometimes tripling the ratio of expenditure on education to expenditure on social protection. In Namibia expenditure on these two components is more or less the same. The share of housing in GDP fell by 27 per cent and was the subsector most severely affected by cut-backs.

Figure 62. Namibia: Composition of social expenditure as a percentage of GDP, 2005-2008

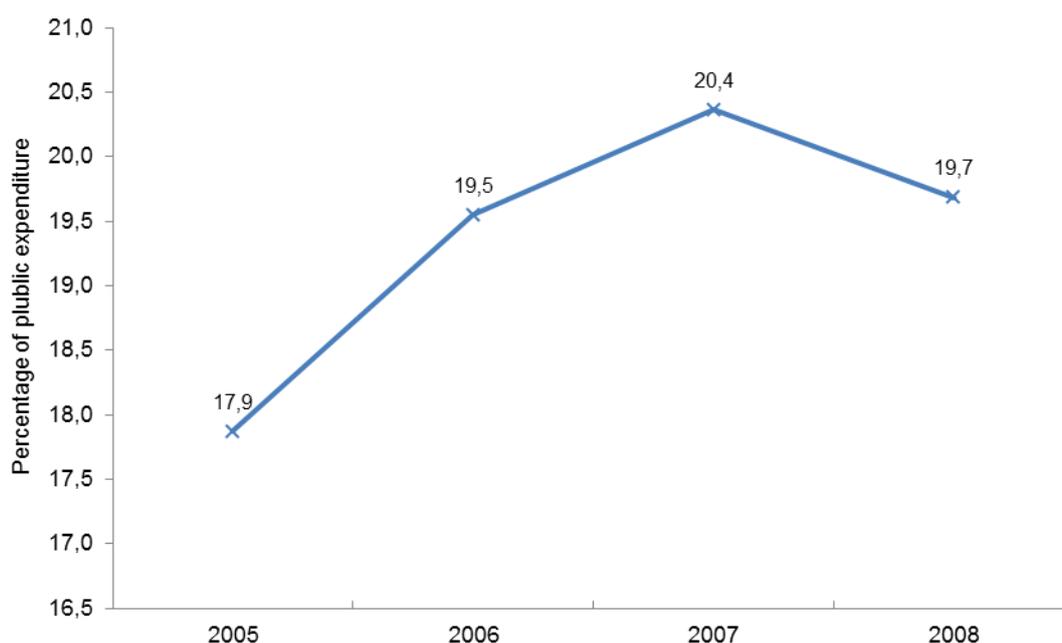


Source: Ministry of Finance, 2009; International Monetary Fund, 2010b.

Expenditure on social protection also increased its share of total public spending and went up from 17.9 per cent in 2005 to 19.7 per cent in 2008 of total government expenditure (figure 63). Namibia is one of the countries in the southern part of Africa that has the highest expenditure on social protection (19.4 per cent of GDP on average) – less than South Africa (25.2 per cent), but more than Lesotho (18.5 per cent), Botswana (15 per cent) and Mozambique (13.3 per cent).

In real per capita terms, social protection increased by 30 per cent between 2005 and 2008, from 876.7 to 1,141.8 Namibian dollars (at today's rate, 1 Namibian dollars equals roughly US\$0.13). These figures confirm the earlier conclusion that the Government of Namibia has been placing special emphasis on social protection programmes ever since Independence.

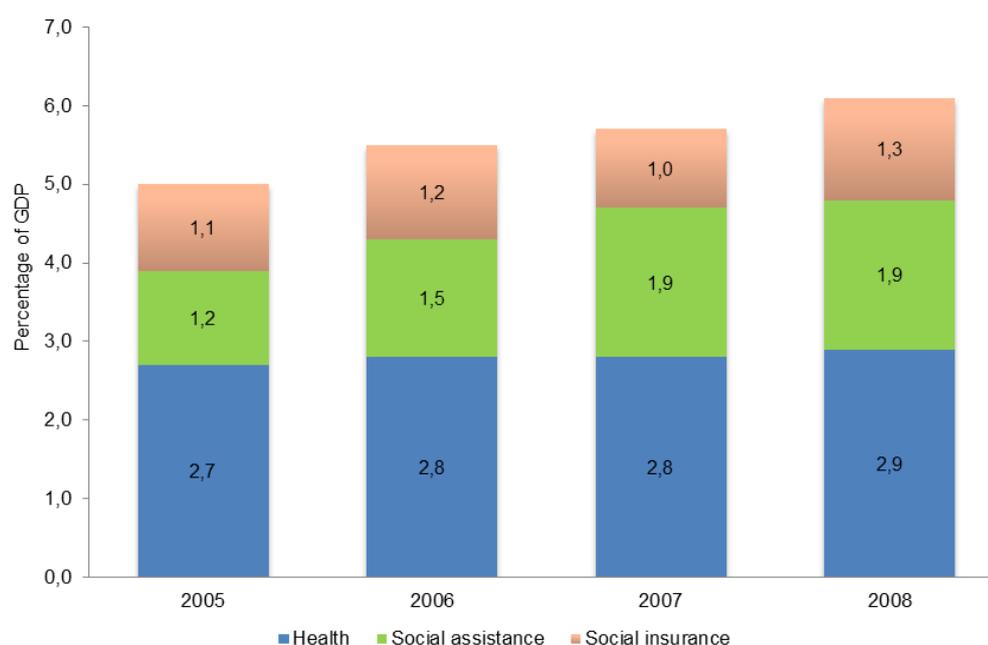
Figure 63. Namibia: Expenditure on social protection as a percentage of total public spending, 2005-2008



Source: Ministry of Finance, 2009; International Monetary Fund, 2010b.

Regarding expenditure on social protection, the most important point to note is that the three main categories (health, social insurance and social protection) increased their share of GDP between 2005 and 2008 (figure 64). Social assistance increased by 0.7 percentage points (a growth of 58 per cent) and became the most favoured component in terms of increases in expenditure. Health gained 0.2 percentage points, a growth of 7 per cent.

Figure 64. Namibia: Health, contributory social security and social assistance as a percentage of GDP, 2005-2008



Source: Ministry of Finance, 2009; International Monetary Fund, 2010b.

8.2.2. Old-age pensions

The roots of the old-age pension programme can be traced back to the Old-Age Pensions Act of 1928 in South Africa. At that time the people of South-West Africa, by which name Namibia was then known, were not entitled to receive an old-age benefit. In 1949 the law was reformed so that White South-West Africans could be considered beneficiaries. It was not until 1973 that all Namibians were incorporated into the programme. Just after Independence, the Government undertook to approve the National Pensions Act, 1992 (Act No. 10 of 1992), entitling all people over 60 years old to a basic state pension. As things stand today, beneficiaries must be over 60 years old, be Namibian citizens or permanent residents and reside in the country.

During the last 10 years the Government increased the state pension several times. In 1999 the average pension was 160 Namibian dollars, but by 2008 it had almost tripled to 450 Namibian dollars. The 2010 poverty line was estimated at 398.5 Namibian dollars, so the benefit was good enough to cover the basic needs of 1.13 adults.²³ However, this amount corresponded to roughly half the minimum salary of an agricultural worker (860 Namibian dollars a month).

The fiscal impact of the programme is fairly low. In 1996 the old-age programme made up 3.6 per cent of total government spending. Estimates calculated for this report yield a figure of 3.1 per cent of total government spending in 2008, or 0.95 per cent of GDP.

From the standpoint of coverage, the programme aims to be universal. In 2005 the coverage rate of people over 60 years old was 91.4 per cent, and in 2008 the number of beneficiaries was reported to be 129,228.

The coverage rate remained very similar during the rest of the 2000s, so that by 2008 Namibia was the African country with the third highest coverage rate for old-age pensions after Mauritius and South Africa. Namibia had thus made substantial progress from the estimated 58 per cent coverage rate of 1991 (Devereux, 2001).

8.2.3. Contributory social security system

Namibia's social security system was established by the Social Security Act, 1994 (Act No. 34 of 1994) and is administered by the Social Security Commission. The scheme was set up by the Government to address socio-economic conditions and poverty. It aims to provide an income in the event of sick leave or maternity leave and also pays out benefits in the event of retirement, permanent disability or death of a scheme member.

The Social Security Commission was established on 15 January 1995 and is in charge of collecting contributions, registering members (employers and employees), paying out benefits and investing its funds. The SSC administers three funds:

1. the maternity leave, sick leave and death benefit Fund (MSD), which grants benefits to registered beneficiaries in those three areas;

²³ The Central Bureau of Statistics (2008) established that the poverty line for 2003/2004 was 262.45 Namibian dollars. This value has been adjusted for inflation to estimate the 2010 value, using an expected annual inflation rate of 10.3 per cent.

-
2. the Employees' Compensation Fund (ECF), which compensates for disablement caused by occupational accidents or industrial diseases suffered by employees in the course of their employment, or for death resulting from such accidents and diseases;
 3. the Development Fund, which was created with the primary objective of financing training activities for selected socio-economically disadvantaged persons and students at institutions of higher learning; it is financed by transfers from other SSC funds, budget allocations or donations.

Act No. 34 also created two other funds, the National Pension Fund and the National Medical Benefit Fund, but neither of them is yet in operation.

Maternity leave benefits cover 12 weeks at 100 per cent of the beneficiary's remuneration, the minimum being 300 Namibian dollars a month and the maximum 6,000. Sick-leave benefits apply once the employee has worked for the required period of time specified in Labour Code or employment contract. The sick-leave benefit amounts to 75 per cent of the worker's salary during the first six months, the minimum being 250 Namibian dollars a month and a maximum of 4,750 ; for the following 18 months the benefit is 60 per cent of the beneficiary's remuneration. Finally, the death allowance consists of a single lump sum of 3,500 Namibian dollars paid upon the death of a SSC member, whether he was employed, retired or permanently disabled at the time.

Regarding the Employee Compensation Fund, the contingencies covered under this scheme in 2008 included:

- medical expenses for injured employees;
- cost of transportation of an injured employee;
- temporary total disablement benefit;
- compensation for permanent disablement;
- funeral and burial expenses;
- payment of a partial dependency lump sum;
- compensation for survivors (accident pensions).

Registration of employers and employees is compulsory by law. Both employers and employees contribute 0.9 per cent of the latter's remuneration up to a maximum of 54 Namibian dollars per month. Employers are required to register with the Employee Compensation Fund, and only registered employers and employees (not their family members) are entitled to receive benefits under the social insurance scheme.

The total number of employers and employees registered in the various funds rose from 2,730 employers and 2,598 employees in 1996 to 38,703 employers and 446,921 employees in 2006.

8.2.4. Other social assistance initiatives

Additional social assistance programmes exist to cover and protect vulnerable groups in a wide range of circumstances. As with the old-age pension, they are all non-contributory programmes. Seven such initiatives can be classified as the most important: the Disability Grant, the Funeral Benefit, the Special Maintenance Grant (grant for children), Maintenance Grant, the Foster Parent Grant, the Place of Safety Allowance and the Veterans Subvention.

The second most important social assistance programme is the Disability Grant which, like the old-age pension, consists of a monthly allowance of 450 Namibian dollars. To receive the benefit, a person must (i) be 16 years old or above, (ii) be diagnosed as temporarily or permanently disabled by a state doctor or as HIV and AIDS positive by a medical practitioner, and (iii) be a citizen or permanent resident of Namibia and reside in the country.

In 2008 there were 19,671 beneficiaries under the Disability Grant programme. Estimates show that the fiscal impact of the programme is 106.2 million Namibian dollars, which is equivalent to 0.47 per cent of total government spending or 0.15 per cent of GDP.

The Funeral Benefit programme consists of a grant of 2,200 Namibian dollars provided by the Government to beneficiaries of the old-age pension or Disability Grant programmes. Inter alia, the package covers the cost of the coffin, grave site, transportation if required and funeral services. The fiscal cost of the programme in 2008 was estimated at 71.6 million Namibian dollars paid out to 2,713 beneficiaries. This figure corresponds to 0.32 per cent of total public spending and 0.10 per cent of GDP.

The Maintenance Grant (MG) and Special Maintenance Grant (SMG) provide monthly benefits to parents and to children, respectively. In the case of the MG, the benefit is 200 Namibian dollars for the first child and 100 Namibian dollars for each additional child, up to 6 children.

The MG is given to biological parents (one of whom at least is a beneficiary of the old-age pension or Disability Grant, whose spouse has passed away or is serving a prison sentence) whose monthly income is less than 1,000 Namibian dollars, whose children are at least seven years old and go to school and who are Namibian citizens or permanent residents. The SMG is payable to Namibian children under the age of 16 who have been diagnosed as permanently or temporarily disabled or as suffering from HIV and AIDS.

The Foster Parent Grant subsidy consists of a 200 Namibian dollar monthly grant for the first foster child and 100 Namibian dollars for additional children. It is given to any person who is temporarily or permanently taking care of a child or has custody of a child. A similar programme, the Place of Safety Allowance, provides 10 Namibian dollars per day to any person or institution that takes care of children under 21 years old.

Finally, the Veterans Subvention is a special subsidy payable to any Namibian who lives in the country, is over 55 years old and participated in the Independence War in 1990. The monthly benefits amounts to 2,500 Namibian dollars.

8.2.5. The basic income grant

Between 2008 and December 2009 a number of church groups, NGOs focusing on AIDS and labour unions launched the Basic Income Grant Coalition and piloted a Basic Income Grant Project (BIG) in Otjivero-Omitara. The idea behind the project was that every resident should receive a monthly income no matter his or her socioeconomic circumstances. As a result, every person in the village received an 80 Namibian dollar allowance each month. The pilot project ended in 2009 and, according to Chung (2010), the results of the initiative were highly encouraging:

- the number of malnourished children declined from 42 per cent to 10 per cent of total children in the village;
- the crime rate in the village fell by 36.5 per cent from the time the pilot project was launched;

-
- the poverty rate in the village dropped from 86 per cent to 68 per cent;
 - unemployment fell from 60 per cent to 45 per cent while average earnings grew by 29 per cent irrespective of the grant.

8.3. The creation of fiscal space in Namibia

Namibia has a long tradition of social programmes. Even before Independence the country had accumulated considerable experience in implementing social initiatives that had allowed the country to pursue the objective of universal coverage of the various target groups. Currently, Namibia boasts one of the most firmly established models of social protection in Africa, which includes a universal old-age pension, a wide range of social assistance programmes and a social insurance scheme. Regarding its overall social protection strategy, the country presents some interesting features. First, the old-age pension is granted to people over 60 years old, which is a move from similar programmes on the continent which start at 65 or even 70 years of age. Second, expenditure on both social insurance and social assistance has grown in recent years and, in the latter case, shows the Government's strong positive bias towards allocating public funds to such programmes. It should be noted, too, that spending on social protection is on an equal footing with education. Third, the Social Security Act, 1994 comprises all the key elements that are required to provide adequate social protection to the population covered. However, the fact that the Pension Fund and the National Medical Benefit Fund have still not materialized 16 years after their approval in law are missing pieces of the puzzle.

The creation of fiscal space seems to be the result of four key factors:

1. *First, the approval of the Social Security Act, 1994 established that both employers and employees had to pay contributions.* With coverage rates above 60 per cent of the labour force, the fund creates a wide space for social protection activities.
2. *Second, the Government's political commitment to increase allocations to social assistance programmes in the absence of an upward shift in the level of tax collection.* As was noted earlier, both revenue collection and government spending underwent serious decline in GDP terms after 2000, since when they have remained stable at around 24-29 per cent of GDP. Broadly speaking, the Government has not changed its economic position to any great degree. But social spending and social protection have nevertheless tended to increase and to account for a growing share of total public expenditure, a sign of a firm budgetary policy. The social protection and education budgets were the net winners of the 2000s, while housing lost ground in GDP terms. The root of this political commitment can be traced back to the decision of post-Independence Governments to reduce or eliminate any inherited features that promoted discrimination. It was a position that implied, for instance, the levelling of all old-age pension transfers across the various population groups.
3. *Third, the fact that in recent years the observable increments in education, health, social insurance and social assistance budgets have been associated with the cumulative fiscal surpluses experienced by the Government during the second half of the 2000s, which in turn were linked to the country's accelerated economic growth rate.* This may explain some recent Government decisions, such as the 50 per cent increment in the old-age pension in 2008.
4. *Fourth, the declining level of debt repayment appears to have contributed to the expansion of fiscal space,* albeit more moderately than other factors, given the up-and-down pattern of debt service during the 2000s. On the other hand, ODA flows have done little to widen fiscal space.

8.4. Challenges and lessons learnt

8.4.1. Challenges

Namibia faces major challenges in pursuing its efforts to improve the population's living conditions. Inequality is at the heart of these difficulties, though absolute poverty itself has to be reduced too. Regarding the future of social protection initiatives and the corresponding financing strategy, the following are some of the key challenges to be taken up.

1. It is important that total revenue collection be stepped up. In the last decade tax revenue grew at the same rate as GDP or even more slowly, so that by the end of the 2000s it was proportionately lower than in 1991.
2. Future changes in the social protection system are needed in at least three areas:
 - (a) The National Pension Fund and National Medical Benefit Fund that were set up under the Social Security Act have to be made operational. Private health expenditure is still in the moderate-to-high range (it averaged 35 per cent of total health expenditure before 2007) and so the introduction of the National Medical Benefit Fund could provide substantial financial relief for the beneficiary families. The National Pension Fund is the strategic piece that is missing from the social protection puzzle, and its creation could in the medium term provide a means of liberating funds that are currently allocated to old-age pensions.
 - (b) The extension of coverage to family members and other vulnerable groups is essential to reduce problems of inequality. Benefits under the social insurance scheme are currently restricted to registered members, excluding the rest of the beneficiary's family, and programme coverage is usually concentrated in urban areas or is well under the population targeted. Coverage for antiretroviral treatment, for instance, was under 60 per cent in 2008 and disability grants to people living with HIV and AIDS were recently restricted to those with medical certification that they are at least 50 per cent disabled.
 - (c) Social contributions are low and do not exceed 1 per cent of the employee's salary. The expansion of the social insurance scheme could thus be accompanied by an increment in contribution rates.
3. There is a current debate about the best way for the development of a national social protection strategy. Although several issues may arise concerning design and implementation (financing sources, condition or unconditional nature of the programme, etc.), this seems to be an excellent opportunity for discussing the suitability of the current social protection initiatives for achieving significant reductions in the level of poverty. In other words, Namibia could be at the crossroads of defining a new social protection strategy that addresses the problem of fragmentation, attempts to reduce administrative costs and increase efficiency.
4. Fiscal surpluses in recent years could be one of the main sources of financing for a cash transfer programme for poor families. McCord (2009) estimated that, depending on population size and the current level of deprivation, a cash transfer programme might cost between 2 per cent and 9 per cent of GDP in West and Central African nations. If the programme targeted households in extreme poverty only, then the net cost would be under 1 per cent of GDP. Given the existing social protection programmes in Namibia, it would seem that expanding the scope of its social assistance programmes could be achieved at only a small additional cost for the Government.

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5. Raising tax levels to increase fiscal space is a difficult option for the Government. According to Doing Business data, the VAT in Namibia, now at 15 per cent, is higher than in Lesotho (14 per cent), South Africa (14 per cent) and Botswana (10 per cent), though lower than in Mozambique (17 per cent). Corporate income tax, too, is among the highest in the southern part of Africa.

8.4.2. Lessons learnt

Lesson 1

Namibia is a good illustration of the circumstances in which countries with moderate macroeconomic and fiscal performance often find themselves. None of the macroeconomic factors usually associated with the creation of fiscal space are in any way outstanding. Production grew at a moderate rate and was not transformed into a higher level of fiscal revenue, as was expected. From a macroeconomic standpoint, average economic growth was far below the dynamic rates of countries such as Botswana and Mozambique, where average GDP growth exceeded 8 per cent per year. In addition, the Government decreased its participation in the economy and by 2008 the level of taxation and expenditure was considerably lower than in 1991, just after Independence. Nonetheless, the Government was able to generate a fiscal surplus in the second half of the 2000s, an indication of the highly prudent fiscal policy pursued in recent years, which has expanded fiscal space.

Lesson 2

Namibia did not benefit from huge ODA flows to complement social investment (with the possible exception of HIV programmes) and its external debt did not experience a significant downward shift.

Lesson 3

The evidence indicates that the creation of fiscal space for social protection was the result of what one might call “implicit fiscal space creation”, meaning that the allocation of resources for social protection objectives grew, but fiscal revenue and government expenditure remained at much the same level or actually declined. The increased share of social security expenditure is thus the result of re-allocating funds from non-priority to priority sectors without altering the level of spending. This mechanism is complemented by other options such as the establishment of social insurance programmes.

Lesson 4

Despite the limited availability of resources, Namibia has performed well in terms of social protection budgets and initiatives. With the exception of housing allocations, all the major headings of social expenditure (health, social insurance, social assistance, education) enjoyed a bigger share of GDP and internal public expenditure. Key programmes such as the old-age pension and the social insurance schemes report high levels of coverage among the target population and this has clearly improved the living standards of the Namibian people, as reflected in the relatively low incidence of poverty compared with their neighbours.

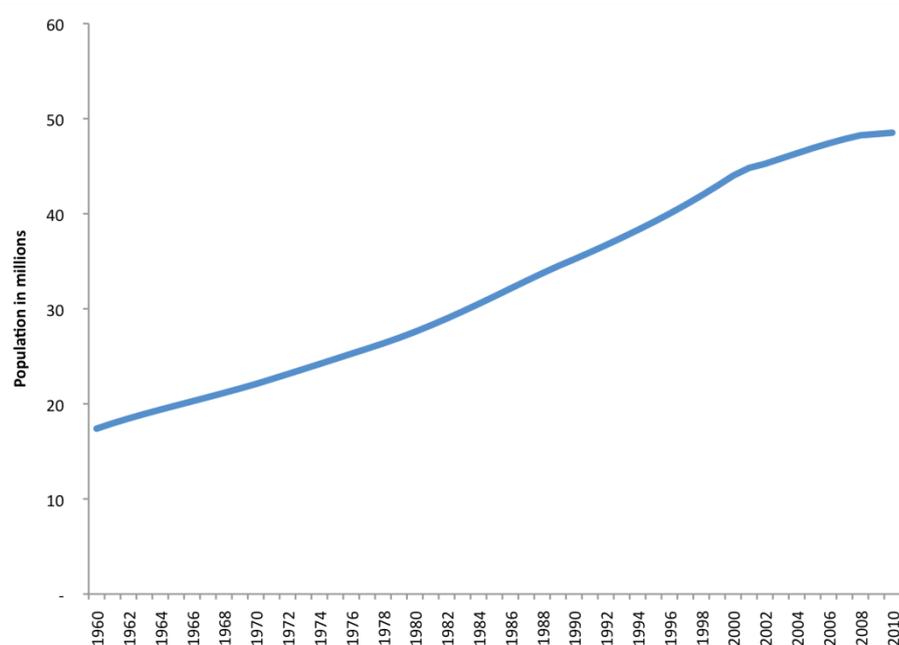
9. South Africa: Social protection for integration

9.1. Country profile

With a territory of 1,221,037 square kilometres, the Republic of South Africa is located in the southernmost part of the African continent. The country shares boundaries with Namibia, Botswana and Zimbabwe to the north, with the Atlantic and Indian oceans to the south and west and with Mozambique and Swaziland to the east. South Africa is a highly diverse nation with eleven official languages and a large number of ethnic groups. Politically speaking, the nation is a constitutional democracy in the form of a parliamentary republic.

The total population of South Africa was 48.5 million in 2010 (figure 65), of whom 50.7 per cent were female, 34.8 per cent were children under 15 years of age and 7.1 per cent were over 65 years old. Between 1960 and 2010 the population grew at an average annual rate of 2.1 per cent, but in the last decade this annual rate declined to 1.2 per cent and since 2007 has been less than 1 per cent.

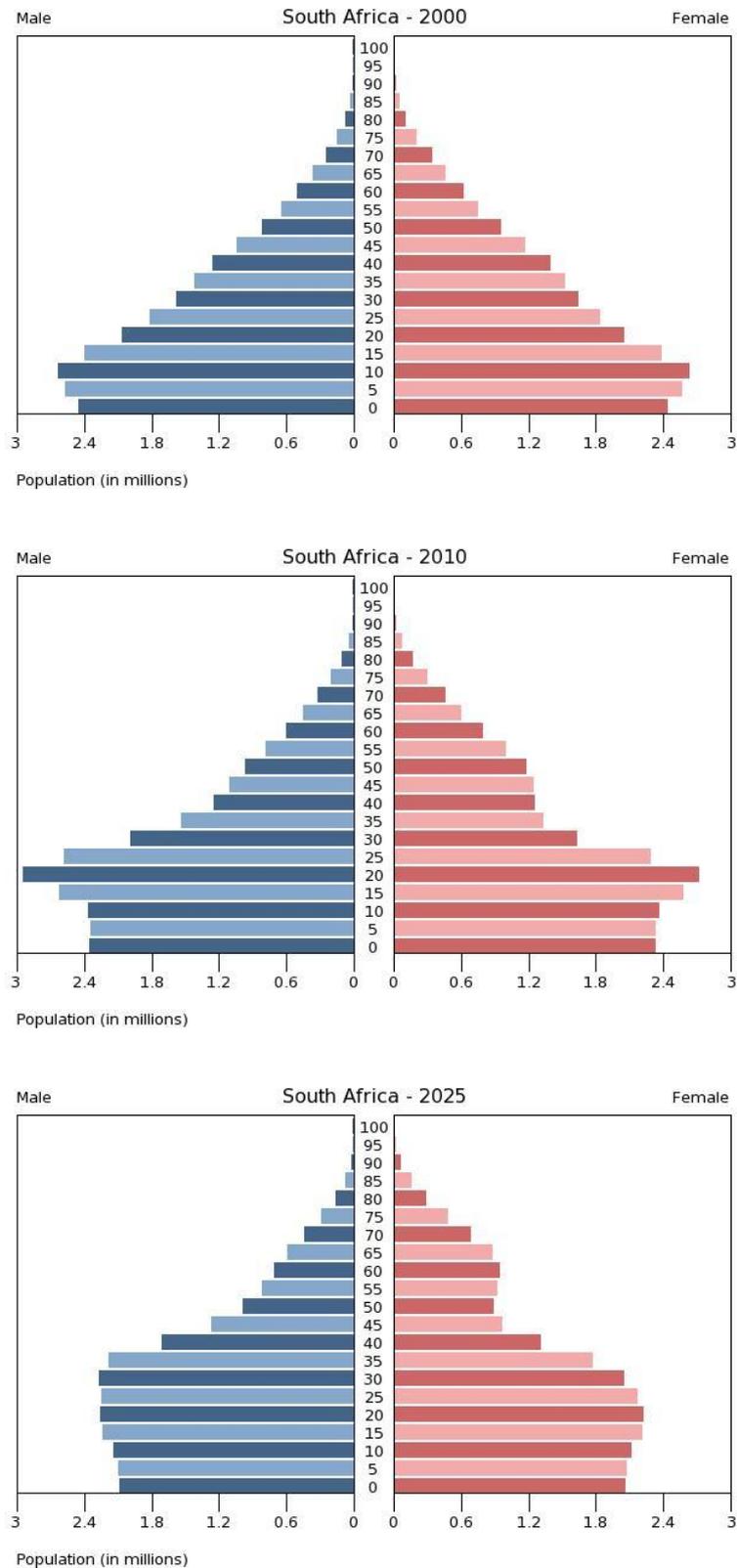
Figure 65. South Africa: Total population 1960-2010



Source: UNFPA, 2010.

Projections for the next 15 years point to a steady increase in the share of over 65 year olds in the total population; by 2025 one in every ten South Africans is expected to be in that age group (figure 66), a 55.8 per cent increase over the figure today.

Figure 66. South Africa: Population pyramids, 2000, 2010 and 2025

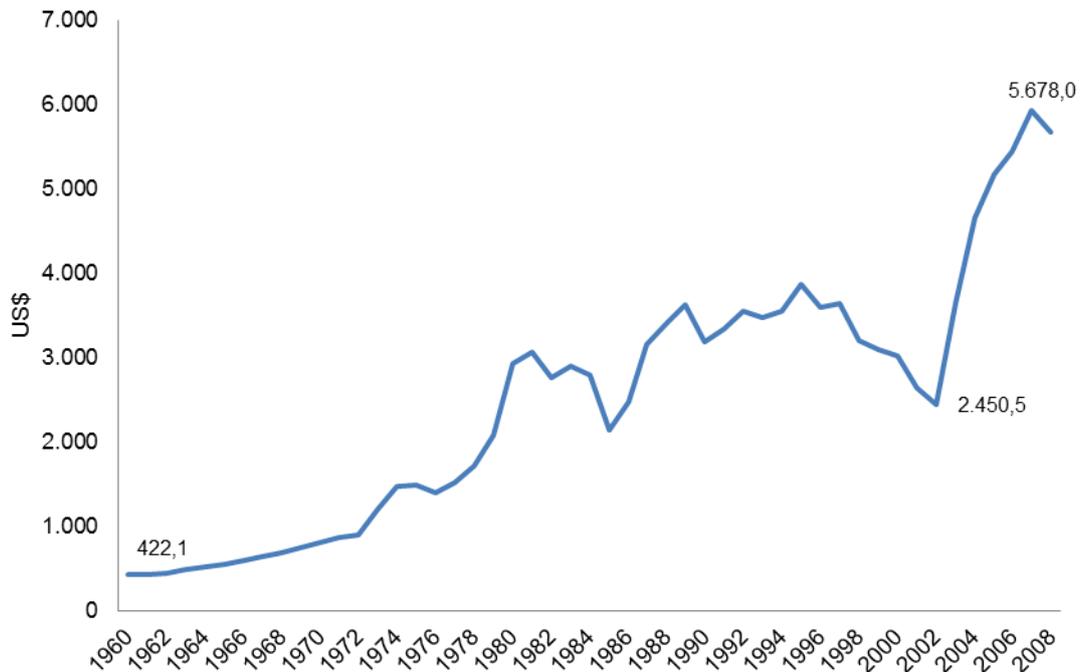


Source: US Census Bureau, 2010.

From an economic standpoint, the performance of the South African economy has not been outstanding. Between 1961 and 2010 the economy grew at an average rate of 3.2 per cent per year, or 1.2 per cent in per capita terms. The economy was the object of strong and

periodical cyclical downturns that greatly limited its expansion. By 2002 GDP per capita was 16.3 per cent lower than in 1980, and in six of the 22 years between 1981 and 2002 the GDP growth rate was negative. After 2002, however, the economy experienced a period of recovery (except during the financial crisis of 2008 and 2009) which allowed the country to double the GDP per capita (figure 67).

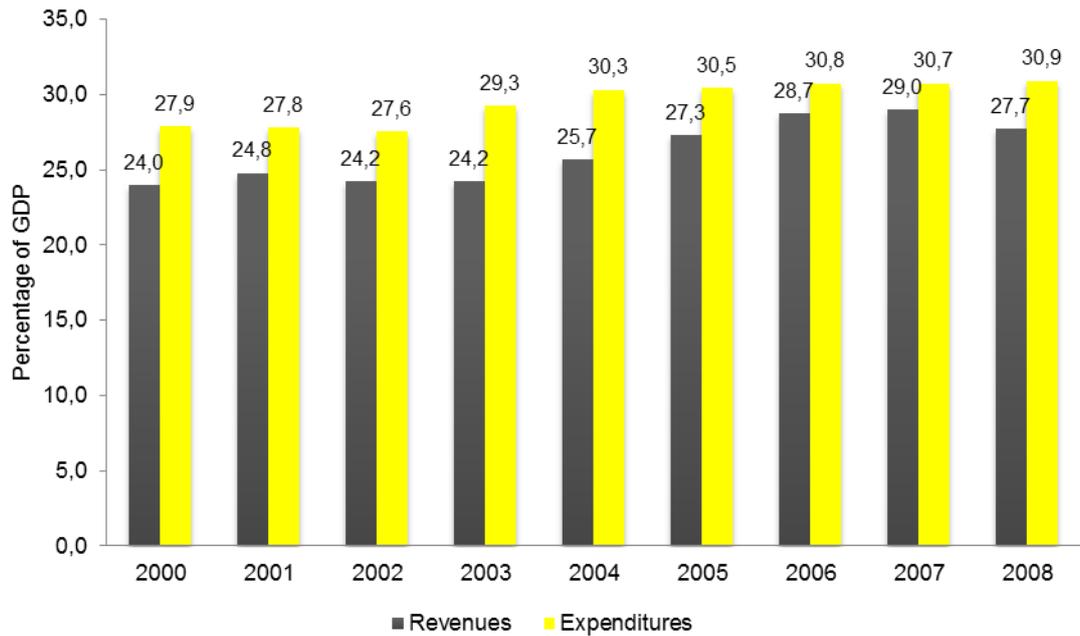
Figure 67. South Africa: GDP per capita in US\$, 1960-2010



Source: World Bank, 2010.

South Africa suffers from a chronic fiscal deficit. During the 2000s government revenue averaged 26.2 per cent of GDP while expenditure accounted for 29.5 per cent of total production; as a result, the deficit averaged 3.3 per cent of GDP (figure 68). Both aggregates, revenue and expenditure, experienced an upward trend during the decade, but revenue grew at a faster rate, especially after 2005, and thus helped to reduce the fiscal gap. Between 2000 and 2007 the share of revenue in GDP grew by 5.2 percentage points; expenditure, on the other hand, increased by only 2.8 percentage points. Most of the Government's revenue is derived from income tax, and roughly one-third of total revenue comes from indirect taxes, mainly VAT.

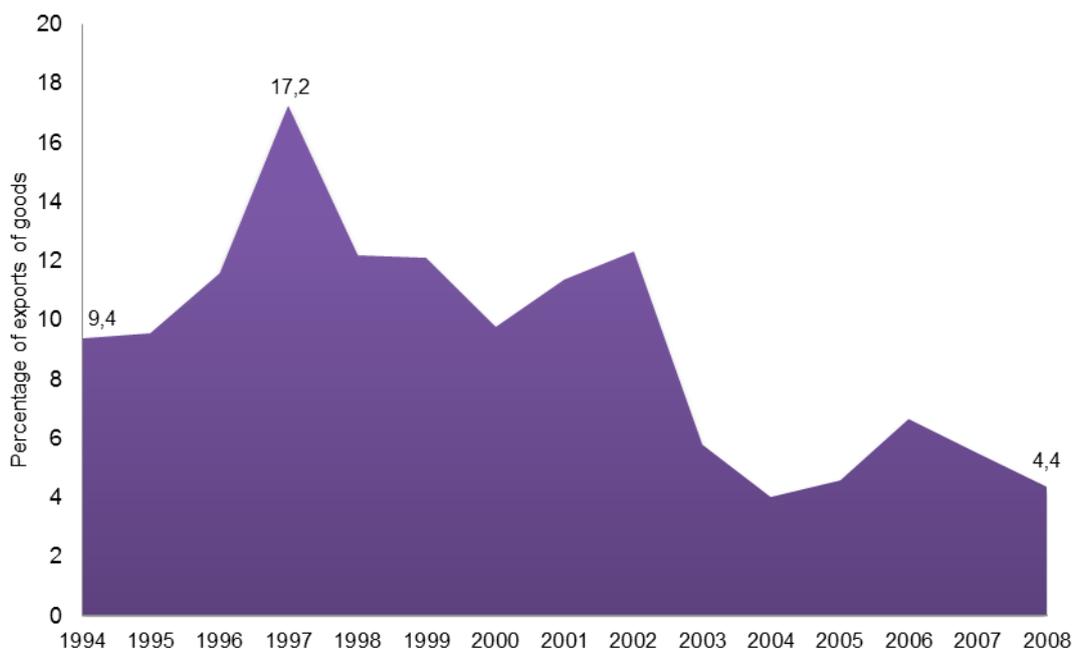
Figure 68. South Africa: Fiscal revenue and expenditure, 2000-2008



Source: World Bank, 2010.

One of the most important features in terms of the creation of fiscal space has been the significant reduction in debt service and overall public debt. Total public debt fell from 49.5 per cent of GDP in 1996 to 29.5 per cent in 2009, with a marked decline in domestic debt. As a result, total debt service is now only a quarter of the 1997 level in terms of exports (figure 69) and roughly two percentage points lower in GDP terms. This has allowed the government to increase spending without incurring additional deficits.

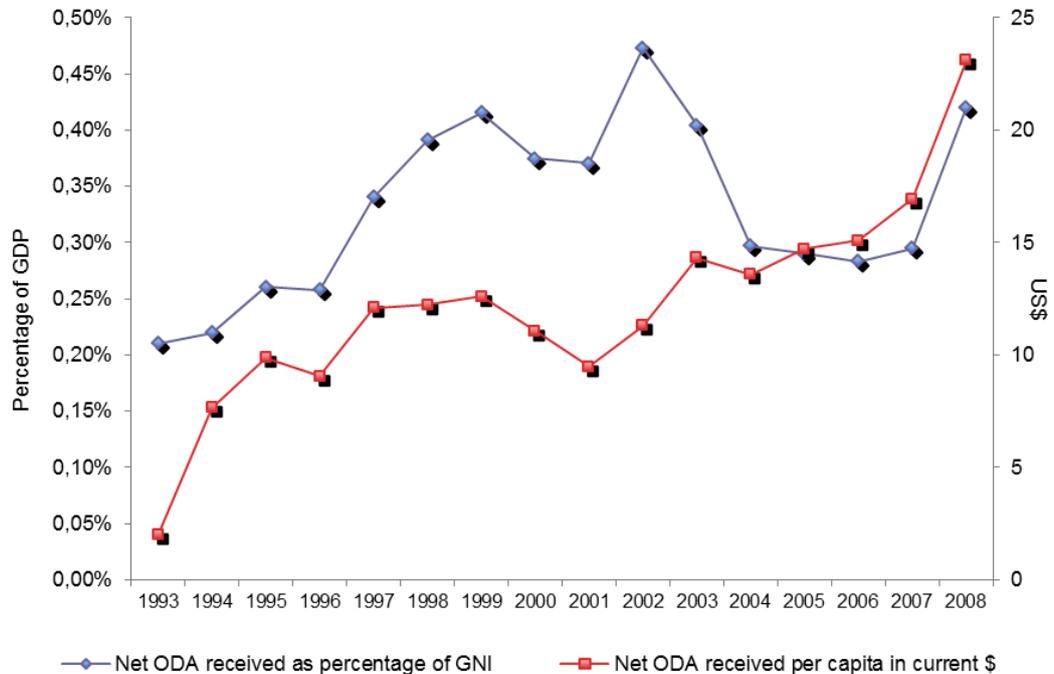
Figure 69. South Africa: Total debt service as a percentage of total exports, 1994-2008



Source: World Bank, 2010.

Although the flow of official development assistance started increasing just after Independence, it has in practice not served as a major source of financing. Between 1993 and 2008 per capita ODA grew from US\$2 to US\$23, an increase from 0.21 per cent to 0.42 per cent of gross national income (figure 70). Despite the steady rise in ODA funds, they clearly lagged behind the volume from which some neighbouring countries benefited during the same period.

Figure 70. South Africa: ODA flows as a percentage of GNI and in per capita terms, 1993-2008



Source: World Bank, 2010.

As to the social sector, South Africa still faces important challenges in terms of poverty and inequality. The country has one of the highest rates of inequality in the world, and more than four of every ten citizens still live under conditions of poverty. As to human development, South Africa ranked 129th in the *Human Development Report 2009*, far below its position in terms of GDP per capita, which is almost double that of Namibia. Yet Namibia ranks one position above South Africa in the Human Development Index. This is due largely to a low life expectancy index (0.442) for South Africa which is affected by the high prevalence of HIV (UNDP, 2009). Roughly 5 million South Africans are living with HIV. In addition, special challenges face the country with regard to infant and maternal mortality (table 14).

Table 14. South Africa: Socioeconomic indicators, various years

Indicator	Year	Result	Source
Poverty (percentage of the population living on less than US\$2 a day)	2000-2007	42.9	UNDP, 2009.
Gini coefficient	2007	57.8	UNDP, 2009.
Human Development Index	2007	0.683	UNDP, 2009.
Life expectancy at birth	2007	51.5	UNDP, 2009.
Infant mortality rate per 1,000 live births	2008	45	World Bank, 2010.
Maternal mortality rate per 100,000 live births	2010	300	World Bank, 2010.
HIV and AIDS prevalence (percentage of the population)	16.9	2007	Shisana et al., 2009.
Adult literacy rate (percentage)	1999-2007	88	UNDP, 2009.
Children under-weight for age (percentage)	1998	15	World Bank, 2010.

9.2. Social protection: Programmes and investment

South Africa's social protection system is what the Inter-Regional Inequality Facility (2006) calls “a system of targeted social grants” that provides cash transfers to specific groups such as the disabled, the elderly and children. Access to both social insurance and social assistance is considered a right under Section 27(1c) of South Africa's Constitution.

Eligibility to all grants is determined by income-based means-testing and all the programmes are financed out of general taxation. Of the three categories of social protection programmes in South Africa (social insurance, social assistance and universal benefits), social assistance is the most important in terms of coverage and financing.

Since 2006 the management and payment of social assistance grants is in the hands of the South African Social Security Agency (SASSA). Currently, SASSA administers the following social assistance grants:

- Grants for people 60 years of age or more, in the form of a state old-age pension.
- Disability grants, which provide support for adults with disabilities.
- Child support grants, which provide a subsidy for families with children under 14 years of age.
- Foster child grants, in the form of a cash transfer to families with under 18 year olds in foster care.
- Care dependency grants, which provide monetary support for families with children with disabilities.

The SASSA also administers the War Veterans Grant, the Grant-in-aid and the Social Relief of Distress programmes, but these are more limited in scope than the five grants mentioned above. All the programmes are financed through general taxation, and eligibility is dependent on an income-based means test.

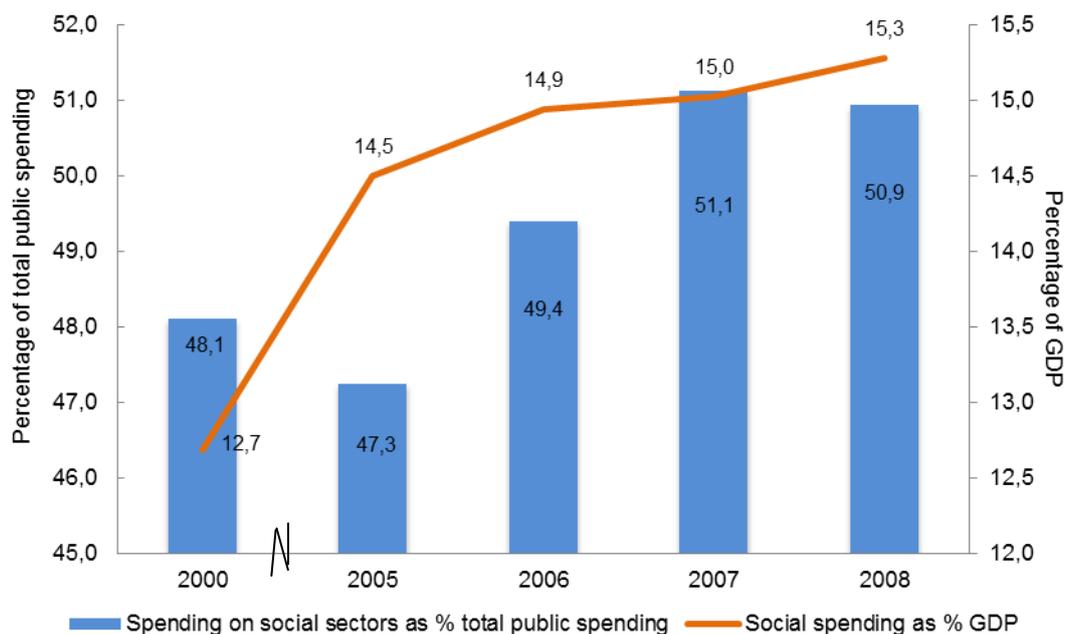
South Africa also has three social insurance programmes: Unemployment Insurance Fund, the Compensation for Occupational Injuries and Diseases Fund and the Road Accident Fund. Contributory pensions also exist for public servants under the Government Employees Pension Fund.

By 2008 a total of 13.1 million South Africans, or 27 per cent of the population, were receiving a grant of some kind. The total number of beneficiaries thus increased by a

multiple of 5.4 in relation to 1995 (from 2.4 million to 13.0 million) and by a multiple of 3.5 in relation to 2000 (from 3.8 to 13.0 million). As to coverage, whereas 6.2 per cent of the South Africans received at least one type of benefit in 1995, by 2008 roughly 27 per cent of the population was covered by one social programme or another.

Public expenditure on the social sector (including education, housing, health protection, etc.) in 2008 accounted for 15.3 per cent of GDP and 50.9 per cent of total public spending (figure 71). During the last decade social spending grew by 2.6 percentage points of GDP (a 20.5 per cent growth). Social spending has also gained ground in terms of government expenditure, though in 2008 the net increment was only 5.9 per cent higher than in 2000, when half the government budget was allocated to the social sector.

Figure 71. South Africa: Social spending, 2000-2008



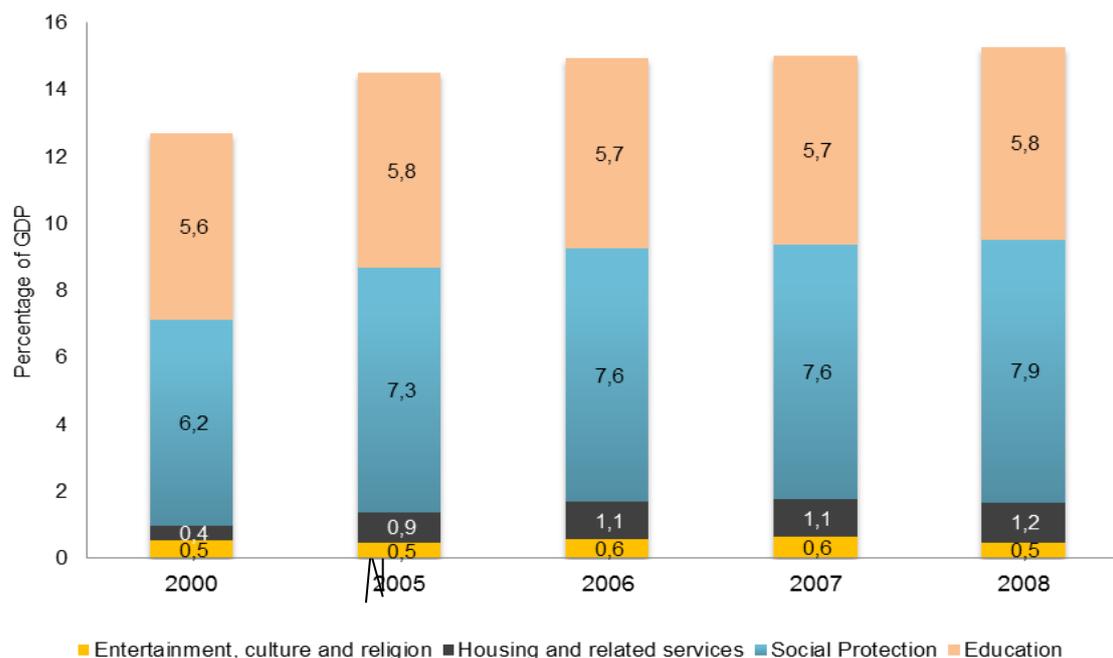
Source: National Treasury, 2009; International Monetary Fund, 2010b.

Regarding the composition of South Africa's social spending, social protection accounts for the highest share of expenditure and consumes roughly half of available social funds.

Certain general trends can be observed regarding the composition of social spending between 2000 and 2008 (figure 72):

- Social expenditure on housing tripled in GDP terms and was by far the fastest growing component. Almost 8 of every 100 rands are spent on covering housing needs.
- Social protection constitutes about 7.6 per cent of GDP and 50.8 per cent of social expenditure.
- Education gained a net 0.2 percentage points of GDP but its share of overall social spending dropped from 43.8 per cent to 37.7 per cent.
- The share of entertainment and culture in social expenditure was also smaller.

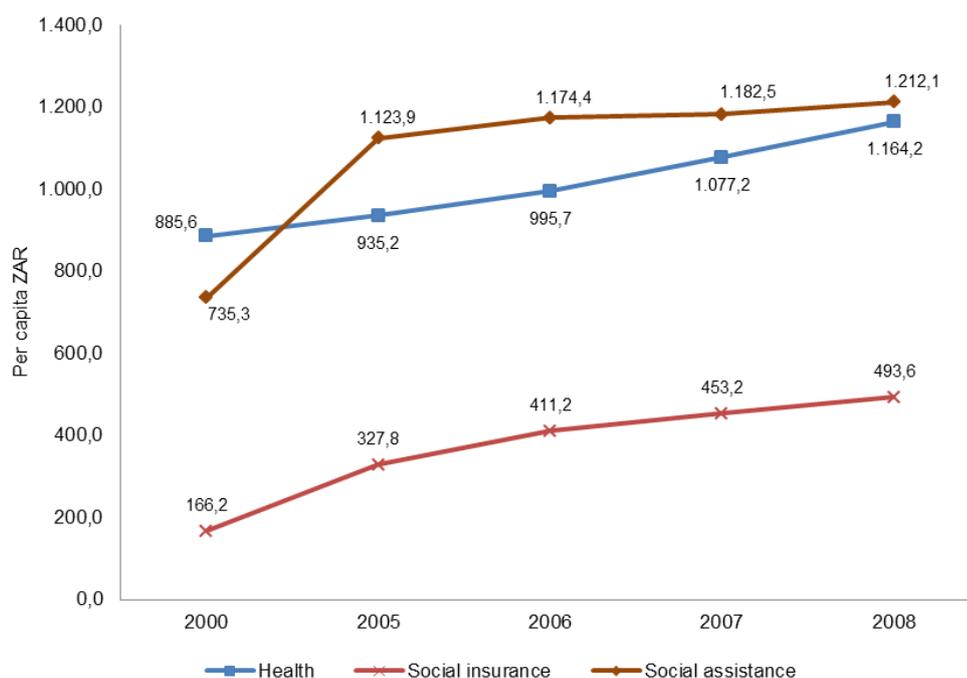
Figure 72. South Africa: Composition of social spending as a percentage of GDP, 2000-2008



Source: National Treasury, 2009; International Monetary Fund, 2010b.

Regarding expenditure on social protection, real per capita spending grew in each of the three categories considered here (health, social insurance and social assistance). Social insurance was the fastest growing component, with a per capita expenditure in 2008 that was almost three times the level observed in 2000. Social assistance also grew (1.6 times), while public health expenditure lagged behind, increasing by only 31.5 per cent during the period (figure 73).

Figure 73. South Africa: Real per capita spending on social protection programmes in Rands, 2000-2008



Source: National Treasury, 2009; ILO, 2010b; International Monetary Fund, 2010b.

There are three notable features in the composition of social protection expenditure:

- As a percentage of GDP, social insurance spending grew from 0.6 per cent to 1.4 per cent during the last decade. In 2000 social insurance constituted a net investment of 0.09 cents per rand allocated to social protection. By 2008 this figure had risen to 17 cents per rand.
- Expenditure on social assistance became the most important component of social protection, with 42 per cent of expenditure going directly to social assistance programmes (3.3 per cent of GDP).
- The share of public health spending in GDP remained more or less stable (3.1 to 3.2 per cent), but in the last decade, its participation in the total expenditure on social protection, declined; in 2000 some 50 per cent of expenditure on social protection was assigned to public health, but in 2008 this share fell to 40.5 per cent.

9.2.1. Social assistance programmes

Child support grant (CSG)

The CSG was launched in April 1998 to replace the discriminatory state maintenance grants that had existed previously (Kaseke, 2010) and to provide social assistance to children in need. To be eligible for the Child Support Grant a person must meet the following conditions:

- The primary care-giver must be a South African citizen or a permanent resident living in the country.
- The applicant must be the primary care-giver of the child or children concerned.
- The child or children must be under the age of 15 years (this condition changed after April 2009).
- The applicant and his or her spouse must meet the requirements of the means test.
- The application may not concern more than six non-biological children.
- The child or children may not be cared for in a state institution.

The CSG is the most important cash transfer in South Africa in terms of coverage but not in terms of expenditure. In 2008 the beneficiaries numbered 8.8 million children. Between 2000 and 2008 coverage grew by a multiple of 7.9, making it the most dynamic coverage rate among the various grant programmes. The estimated coverage of children under the age of 15 was 57.4 per cent of all children in that group. Over the coming years the Government aims to expand the age limit so that in the short term the grant should cover all children up to the age of 18 inclusive. The outstanding performance of the grant during the last decade was the result of regularly increasing the average grant and of raising the age limit of the beneficiaries. The CSG transfers a total of 240 rand per child per month (US\$34), at a total cost amounting to 0.9 per cent of GDP that has remained more or less stable during the last five years. Since 2000 the grant has thus increased 2.4 times from the original 100 rand per month.

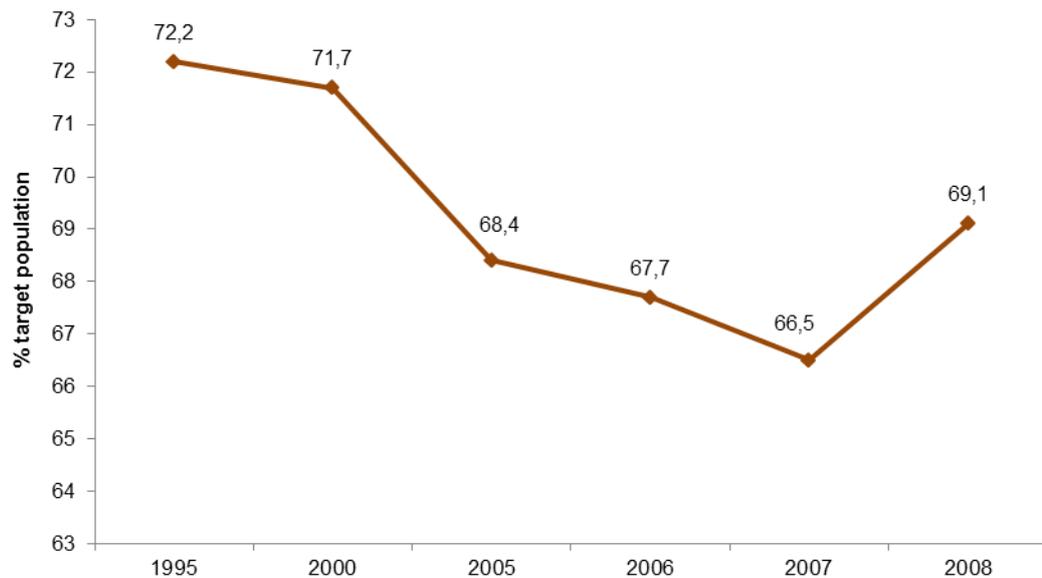
State old-age pension

To be eligible for an old-age pension, a potential beneficiary must be a South African citizen, be a permanent resident of South Africa, be at least 60 years old (prior to April

2010 the eligible age for male beneficiaries was 63 years), be subjected to a means test if he or she has a spouse, not be in the care of a state institution and not be in receipt of any other social grant.

The state old-age pension is the grant initiative with the second highest level of coverage in South Africa. By 1995 some 1.6 million citizens were receiving the benefit, but 13 years later the coverage jumped to 2.4 million. Despite this, coverage rates declined during the same period, so that by 2008 the share of beneficiaries was 3.1 percentage points lower than in 1995 (figure 74). For 2010 the monthly pension per person was set at 1,010 rand (US\$143), up from 780 rand (US\$130) in 2005. Overall, expenditure on the old-age grant declined from 1.3 per cent of GDP in 2005 to 1.1 per cent in 2008.

Figure 74. South Africa: Coverage rates of the state old-age pension programme, selected years



Source: SASSA, 2009.

The state old-age pension has been the subject of various assessments regarding its impact on the level of poverty of the beneficiaries. A study by Woolard et al (2006) concluded that the benefit has reduced the prevalence of poverty by 33 percentage points among older people, by lowering the incidence of poverty among beneficiaries from 55.9 per cent when they received no pension to 22.9 per cent after they began receiving the pension.

Disability Grant and Care Dependency Grant

The Disability Grant (DG) is awarded to people between 18 and 60 years of age who suffer from a medical condition recognized by a medical board. Similarly, the Care Dependency Grant (CDG) is targeted at children under the age of 18 who have a disability that requires special care at home. Both grants are awarded only to South African citizens or permanent residents who meet the requirements of the means tests and who are not beneficiaries under any other programme.

In total roughly 1.4 million people were receiving the benefit in 2008, of whom 1.3 million were recipients of the DG. Between 2000 and 2008 the number of DG beneficiaries doubled and CDG beneficiaries tripled. On the assumption that approximately 10 per cent of the population suffers from a disability, then about 27 per cent of the target population is receiving the grant. The monthly grant in 2010 was the same as the state old-age pension (1,010 rand), up from 780 rand (US\$130) in 2005. Total spending on sickness and

disability accounts for 0.7 per cent of GDP, having lost 0.2 percentage points during the last decade.

War Veterans Grant

The War Veterans Grant is the second type of pension that older people may be entitled to. The benefit is payable to veterans who fought in World War II or in the Korean War but is restricted to those living in conditions of poverty. The usual conditions of residence and receipt of other grants apply.

As would be expected, the number of beneficiaries has declined naturally over time, with the total number of recipients falling from 13,473 in 1995 to approximately 1,500 in 2008. Total spending on this programme corresponds to less than 0.1 per cent of GDP.

Foster Child Grant

The last social assistance programme of importance is the Foster Child Grant (FCG), a government subsidy to families in charge of children who require foster care. The benefit is granted once a court confirms the child's situation and places him or her in the custody of a family supervised by a social worker. The FCG is the only benefit that is not means-tested, as the child's circumstances are not considered a poverty issue.

By 2010 the foster care grant amounted to 690 rand per month (US\$98.5), up from 590 rand (US\$90) in 2005. The number of grants rose from 42,990 in 1995 to 66,697 in 2000 and to 474,759 in 2008. Total spending on the programme increased from 0.13 per cent of GDP in 2000 to 0.18 per cent in 2008.

9.2.2. Social insurance programmes

As indicated above, social insurance programmes have been the most dynamic social protection component in terms of increases on expenditure. Social insurance in South Africa consists of four programmes, three of which are employment-based while the other covers road traffic accidents. The country has no social health insurance programme as such, although the possibility has been discussed of introducing one in the near future. The four programmes are:

- Unemployment Insurance Fund;
- Compensation for Occupational Injuries and Diseases Fund;
- Government Employees Pension Fund;
- Road Accident Fund.

The Unemployment Insurance Fund (UIF) was established in 2001 under the Unemployment Insurance Act No. 63 of 2001. The UIF provides protection for workers, including domestic workers, against the risk of temporary unemployment. The programme excludes civil servants and non-South Africans in temporary employment but covers temporary unemployment arising from maternity, illness and termination of employment. The UIF is mainly financed by compulsory contributions from employers and employees (1 per cent of the monthly payroll from the employer and 1 per cent of earnings from the worker).

The Compensation for Occupational Injuries and Diseases Fund (COIDF) was launched in 1993 following the adoption of the Compensation for Occupational Injuries and Diseases Act No. 130. The scheme pays benefits to workers who are injured, fall ill or die during the normal execution of their activities. The following categories are, however, excluded from the programme:²⁴

- domestic worker employed at a private home;
- members of the South African National Defence Force, for whom there is a separate fund;
- members of the South African Police Services, for whom there is a separate fund;
- workers who do not work for an employer;
- workers who work outside South Africa for more than 12 months at a stretch.

The COIDF is financed by contributions from the employer only. There is no contribution from employees and employers may not deduct any amount of money from their earnings. The size of the contribution depends on the degree of risk in the industry concerned.

The Road Accident Fund is designed to protect South Africans who suffer traffic accidents. The Fund pays compensation to the injured persons or to their relatives. The scheme is financed by a compulsory fuel tax of 72 cents per litre.

Finally, the Government Employees Pension Fund (GEPF) is a defined benefit fund established by the Government Employees Pension Law, 1996 (Proclamation No. 21 of 1996). The following categories of benefits are provided by the Fund:

- normal retirement benefits,
- early retirement benefits,
- sickness benefits and other benefits in the event of termination,
- late retirement benefits,
- resignation benefits,
- death benefits,
- spouse and dependants benefits, and
- funeral benefits.

The GEPF has 1.2 million active members and 300,000 members receiving benefits. To finance its operations the Fund collects contributions from registered affiliates. Employees of participating employers contribute 7.5 per cent of their pensionable remuneration, while employers contribute 13 per cent in the case of civil servants and 16 per cent in the case of uniformed employees.

²⁴ <http://www.westerncape.gov.za/eng/directories/services/7296/21409> [last accessed on 21 august 2012]

9.3. The creation of fiscal space for social protection

The previous section shows clearly that, since the end of Apartheid in 1994, South Africa has advanced steadily towards consolidating the main components of a social protection floor. The establishment of a network of initiatives served several purposes. First, it sought to reduce the high level of poverty and inequality that had characterized South Africa in the past. Secondly, the social protection programmes were a means of strengthening government efforts to eliminate any remnants of the Apartheid era, during which most social protection benefits were designed exclusively for the White population and served to deepen social inequality and discrimination. The post-Apartheid era saw the emergence of a different, more inclusive social system with the clear objective of reducing poverty levels. As noted by Hickey (2007, p. 8), *“the social pension programmes in both South Africa and Namibia were transformed into a progressive form of social protection aimed at reversing previous discrimination as the terms of the broader social contract altered.”*

The results of the last 15 years show that the country has been able:

- to increase expenditure on social protection steadily as a percentage of GDP;
- to allocate half of government spending to the social sector;
- to multiply the total number of beneficiaries by 350 per cent between 2000 and 2008;
- to increase the value of grants in real terms;
- to diversify the number and scope of the social assistance programmes.

In order to attain these significant results, South Africa used two fiscal space mechanisms: the reduction of the public debt, and the re-allocation of public spending so as to assign more funds to social programmes at a time when expenditure on other components was dwindling or growing more slowly. Moreover, these results were all achieved in the face of circumstances that are usually blamed for restraining the expansion of social protection, notably:

- a moderate and highly unstable economic growth rate during the last three decades;
- moderate to low gains in fiscal revenue during the last decade;
- lack of significant ODA flows to finance social programmes;
- a difficult socioeconomic context characterized by the transition from Apartheid and by high levels of poverty and inequality, all exerting severe pressure on government expenditure.

In this context, the creation of fiscal space for social purposes is more the product of policy decisions than of a buoyant fiscal position or any other favourable circumstances (such as increasing ODA flows or borrowing). The financing of the various social protection initiatives is a domestic achievement that was backed by a strong political commitment. This commitment can be seen from the fact that:

- budgetary allocations to social assistance programmes are now 65 per cent higher in real per capita terms than in 2000;
- South Africa's Bill of Rights and Constitution stipulate that social protection is a basic right and that the State is required to provide citizens with services such as proper nutrition, education, health and social assistance.

In addition to the increase in the resources collected by the Government in the form of taxation, the reallocation of resources within the government budget has served as a second mechanism for financing social protection plans. Nyamongo and Schoeman (2007), reviewing the composition of government expenditure between 1983 and 2006, showed that social protection was one of the budget categories that benefited from a steady increase in financing. By contrast, expenditure on defence and on housing declined significantly. Defence spending, notably, which accounted for roughly 15 per cent of total government expenditure in 1983, now accounts for about 5 per cent, thereby freeing funds for other purposes such as social protection.

The recent increases in social investment have been successful in minimizing the negative aspects of Apartheid, particularly in the most underserved areas of the country. Notwithstanding the great progress made in this field, South Africa is still in need of temporary and massive investments in social protection.

9.4. Challenges and lessons learnt

9.4.1. Challenges

The following are some of the key challenges facing South Africa that have been identified in preparing this report.

1. Although people living with HIV and AIDS or their relatives may be entitled to certain grants, their poor coverage in terms of ART treatment may be eroding benefits for this particular group. According to the WHO (2010a), in 2010 only 56 per cent of the target population in need of ART was covered, which means that the grant is not enough to cover both treatment and regular domestic expenses. A more active ART policy is required to enhance the effectiveness of the social grants.
2. The grant-based system currently in place has been a cornerstone in the fight against deprivation and has saved a large proportion of people, particularly children and the elderly, from falling below the poverty line. However, from an administrative standpoint the fragmented systems are costly and difficult to manage. In addition, group-specific grants tend to exclude certain social segments of the population from the system. For instance, none of the grants are available to people aged between 18 and 50 unless they suffer from a disability. In this regard several authors (IRIF, 2006) have proposed the introduction of measures to facilitate access to benefits and to improve the system's administration.

One such proposal is that the means test used to assign benefits be changed. The means test, it is argued, places institutional barriers in the way of the poorest people because of their limited access to government offices and, consequently, to the documentation they need in order to apply.

Another proposal is to launch a universal basic income grant addressed at both poor and non-poor people. In this way, every person would have access to a minimum income and poor households would be more able to satisfy their needs. However, due to a lack of favorable political conditions for the approval of such a proposal, the debate has faded into the background.

3. There is widespread debate about the desirability of establishing a comprehensive social security system, including a health insurance scheme. A government proposal prepared by the Inter-departmental Task Team on social security reform is expected to be presented for consultation in 2012. Smith et al. (2008) presented the findings of a survey among more than 1,000 South African workers regarding their need for

health insurance coverage and social protection. The survey showed that 57 per cent of private workers had no health insurance and 65 per cent had no insurance at all or only partial coverage. The debate about South Africa's needs in terms of social security is therefore still relevant. Since 1997 the Department of Health has been promoting the launch of just such an initiative and the Taylor Committee Report of 2002 pursues the same line of thought.

4. It would seem that the social assistance system needs to be rationalised. The existing grant-based system has been effective in reducing poverty among certain groups but it lacks the scope to avoid problems of equity and efficiency. It is time for the Government and South African society as a whole to go a step further and transform the grant system into a social protection strategy that includes social insurance and employment benefits, the delivery of social services, etc. Whatever the final decision is in this regard, the social assistance programmes may well be in need of a major renovation to make them more inclusive and more cost-effective.

9.4.2. Lessons learnt

Some of the key lessons that the foregoing analysis of the South African experience has to offer with respect to the creation of fiscal space are outlined below.

Lesson 1

Political commitment is the key factor in raising the level of investment in social protection. This is particularly true in contexts such as that of South Africa where the Government operates under very restrictive fiscal conditions, usually accompanied by a fiscal deficit. If public funds grow just at a moderate rate and external aid is limited, then the critical decision involves modifying the composition of public spending by increasing the budget of priority sectors as against that of other sectors.

Lesson 2

In the same line of thinking, significant gains can be achieved even if economic circumstances are not particularly favourable. Substantial increments in social assistance coverage have been achieved in a country where average economic growth was low and unstable and where the country's external financing position was not very good.

Lesson 3

It is important to have an overall view of the country in order to consolidate the establishment of a social protection floor. The break with Apartheid has unified the country, and the social protection system has been shown to be a powerful tool in the fight against inequality, poverty and discrimination.

Lesson 4

The launch of the National Social Security Fund (NSSF) is an excellent opportunity to increase fiscal space and reduce inequality. The most recent trend of expenditure on social insurance and health shows that both have been losing steam in recent years. Moreover, almost 60 per cent of total health spending comes from private expenditure, and this has severely affected the finances of South African households. The formal establishment of the NSSF may address many of the problems of expanded financing and equal access to healthcare services by forcing all workers to enrol in the programme.

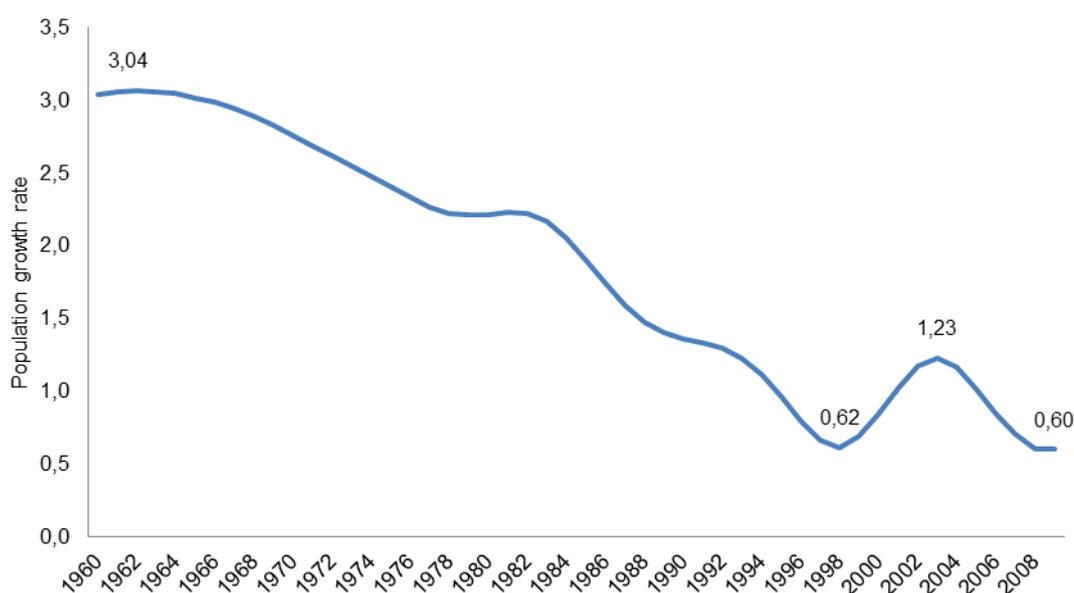
10. Thailand: A hybrid strategy for achieving universal coverage in health care

10.1. Country profile

Located in Southeast Asia, the Kingdom of Thailand covers a total territory of 513,120 square kilometres. The country has borders with Burma and Laos to the north, the Gulf of Thailand and Malaysia to the south, Laos and Cambodia to the east and the Andaman Sea to the west. Thailand is a constitutional monarchy governed by King Bhumibol Adulyadej, who has reigned since 1946.

The total population of Thailand was estimated at 67.8 million inhabitants in 2009. Since 1960 the population growth rate has been declining; the growth rate in 2009 was only a fifth of that observed in 1960 (figure 75). During the 2000s the average population growth rate was 0.92 per cent per year.

Figure 75. Thailand: Population growth rate, 1960-2009



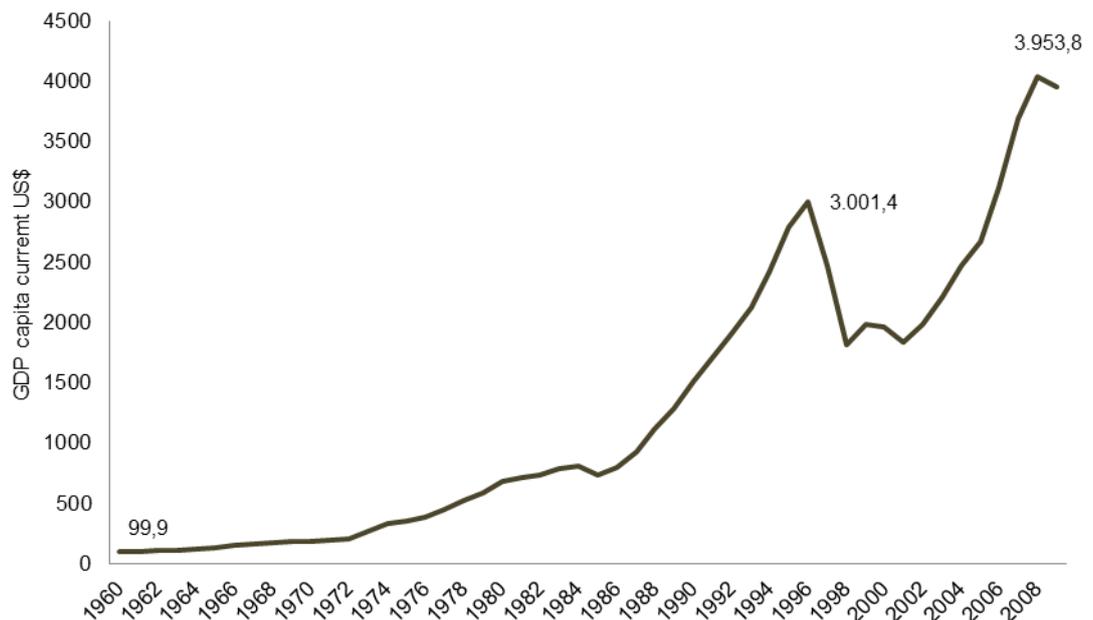
Source: UNFPA, 2009.

During the last two decades and as a result of a sustained decline in fertility and mortality rates, Thailand has experienced an accelerated ageing process. The 0-14 year age group that accounted for 30 per cent of the population in 1990 now stands at 21.9 per cent of the total. By contrast, the share of over 65 year olds increased from 4.6 per cent in 1990 to 7.4 per cent in 2009. One out of every ten Thais is over 60 years old, making Thailand the country with the second highest age pattern in the region (UNFPA, 2009). The ageing

index is currently 45 per cent but it is expected to exceed 100 per cent in 2020 and 140 per cent by 2050.²⁵

As a result of Thailand's outstanding economic performance since the 1960s the GDP per capita was multiplied by 30 between 1960 and 1996. However, the 1997 Asian financial crisis hit the economy severely and by 2001, GDP per capita was some 40 per cent lower than in 1996. Since then the economy has largely recovered and in 2009 GDP per capita was estimated at US\$3,953 (figure 76). The gross national income per capita, in PPP terms, was US\$7,770 in 2008. The long-term GDP growth rate has averaged 6.4 per cent per year, but the recent dynamics of the economy point to a major deceleration. While in the 1980s GDP grew at an annual rate of 7.3 per cent, during the 1990s it fell to 5.3 per cent and then to 4.1 per cent in the 2000s.

Figure 76. Thailand: GDP per capita in current US\$, 1960-2009

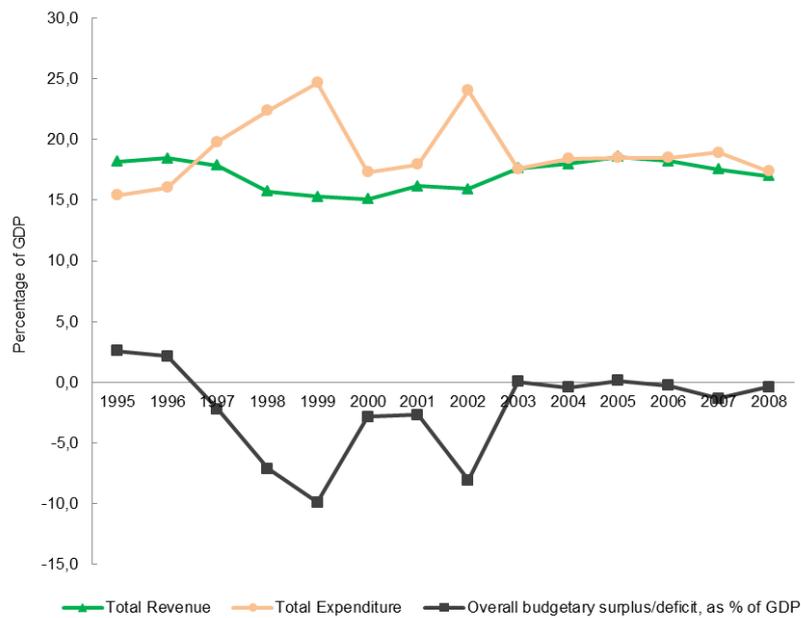


Source: World Bank, 2010.

Regarding its fiscal position Thailand has gone through three different stages (figure 77). Prior to 1997 the country enjoyed sustained fiscal surpluses of about 2.5 per cent of GDP. With the 1997 crisis the fiscal situation deteriorated considerably and the average deficit between 1997 and 2002 was 5.5 per cent of GDP. As of 2003 the Government corrected its fiscal imbalance and reduced its average deficit to 0.4 per cent of GDP.

²⁵ The ageing index measures the proportion of older people (>60 years) relative to the younger population (<15 years).

Figure 77. Thailand: Total revenue, total expenditure and the fiscal balance as a percentage of GDP, 1995-2008

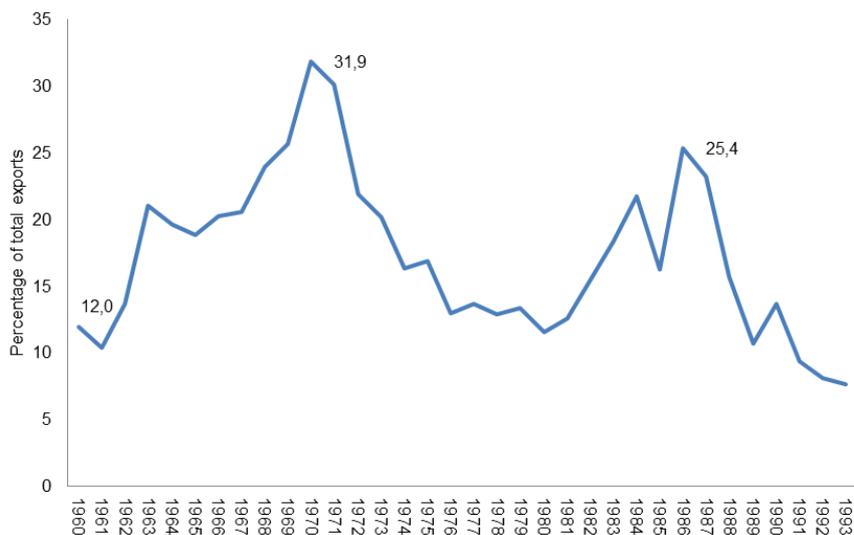


Source: ADB database, 2010.

Estimations by Jansen and Khannabha (2009) show that, in terms of revenue collection, Thailand's level of revenues is lower than one would expect given its economic development. Moreover, the share of fiscal revenue in GDP has remained very stable over time, which suggests that there is substantial room for increasing fiscal space by improving revenue collection without altering taxes.

Total debt service has been steadily declining since 2001 and now stands at 7.7 per cent of total exports, or 30 per cent of the debt burden at the beginning of the decade (figure 78). However, payments linked to debt service usually follow a cyclical pattern rather than a steady downward path.

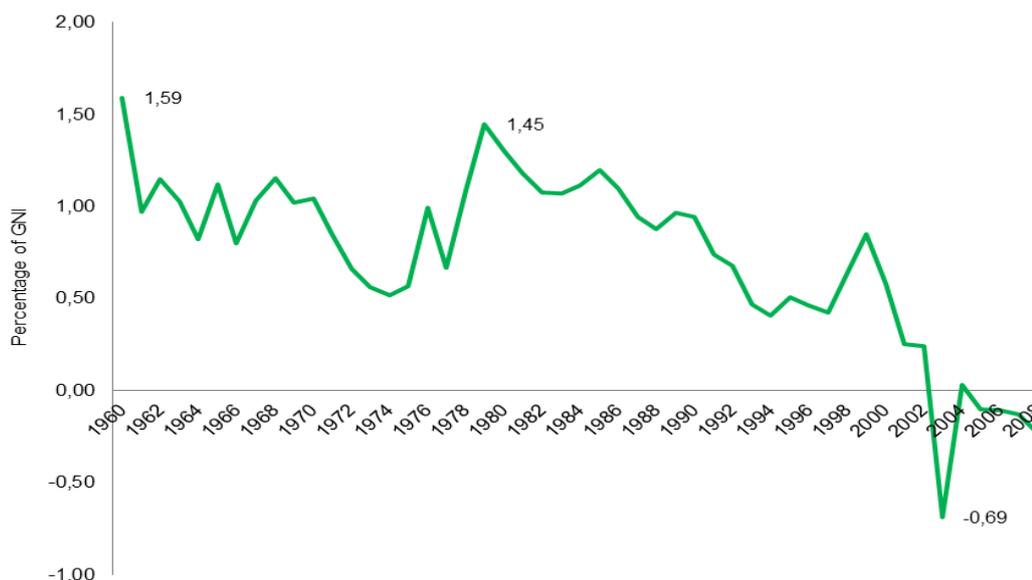
Figure 78. Thailand: Total debt service as a percentage of total exports, 1975-2008



Source: World Bank, 2010.

Historically, Thailand has not been a major recipient of ODA. The highest ratios of external aid were experienced during the 1960s and 1980s when ODA accounted for 1.1 per cent of GNI (figure 79). The most remarkable feature of Thailand, besides its minimal dependence on external funds, is that the country has since 2003 been a net donor of ODA rather than a net recipient.

Figure 79. Thailand: ODA flows as a percentage of GNI, 1960-2008



Source: World Bank, 2010.

Overall, Thailand has made substantial progress in most social sectors (table 15). Poverty declined sharply during the economic boom of the 1990s, falling from 45 per cent in 1988 to roughly 10 per cent in the second half of the 2000s. Inequality is high, however, though authors disagree somewhat in their calculation of the Gini coefficient. The *UNDP's Human Development Report 2009*, for example, estimated that income inequality was 0.42 in the mid-2000s, while Jansen and Khannaba (2009) indicated that the Gini coefficient was 0.50 in 2004.

Table 15. Thailand: Main social indicators

Indicator	Value	Year	Source
Poverty (percentage of the population living below the national poverty line)	13.6	2000-2006	UNDP, 2009.
Gini coefficient	0.42	mid-2000s	UNDP, 2009.
Human Development Index	0.78	2007	UNDP, 2009.
Life expectancy at birth (years)	68.9	2008	United Nations Population Division, 2010.
Infant mortality rate per 1,000 live births	12.5	2008	Inter-agency Group for Child Mortality Estimation, 2010.
Maternal mortality rate per 100,000 live births	54	2005	World Bank, 2010.
HIV/AIDS prevalence (percentage of the population)	1.4	2007	World Bank, 2010.
Adult literacy rate (percentage)	94.1	2007	UNDP, 2009.
Children under-weight for age (percentage)	7	2009	UNDP, 2009.

From a human development perspective, the country ranks in the medium human development group (87th in the world), with an impressive achievement in the education sector (94.1 per cent adult literacy rate and 78 per cent gross enrolment rate), but life expectancy (69 years) lags behind the progress observed in other areas. Health indicators show mixed results, with a low infant mortality rate but a maternal mortality rate that leaves considerable room for improvement.

10.2. Social protection programmes and social spending

Thailand's social protection system comprises both contributory and non-contributory programmes covering a wide range of groups, including public servants, private employees, non-agricultural workers and teachers. The Government's policy is thus, in this sense, fragmented. Social protection was first declared to be a strategic component of Thailand's development policy in the ninth plan (2002-06), with its five pillars (ILO, 2008a): human development; employment promotion; social protection; drug control and safety of people and their assets; and promotion of institutional participation in development. The list of social protection initiatives is presented in table 16 below.

Table 16. Thailand: Social protection programmes

Social insurance programmes	Non-contributory social protection programmes	Other social assistance programmes
Workmen's Compensation Fund (WCF)	Civil Servant Medical Benefit Scheme (CSMBS)	Children
Social Security Fund (SSF)	Universal Coverage Scheme (UCS)	Disadvantaged women
Provident funds	Pensions	Elderly
Government Pension Fund (GPF)		Disabled
Private-School Teachers' Welfare Fund (PSTWF)		Homeless and beggars
		Low income families and families in need
		Ethnic minorities
		Victims of disasters

Source: ILO, 2008a and 2008b.

10.2.1. Contributory social security schemes

Thailand has established five different contributory schemes, as shown in table 16. The main features of each programme are presented below.

Social Security Fund (SSF)

In 1954, the National Assembly approved the Social Security Act. After several decades and repeated attempts to put it into force, the Act was finally implemented in 1990. It benefited Thai workers by providing special coverage and protection in respect of illness or accident, physical disability, death not related to work, child delivery, old age, child assistance and unemployment.

The Social Security Office of the Ministry of Interior administers the SSF, which covers all employees of firms with one or more workers. Initially, the programme covered enterprises with 20 or more workers, but two amendments to the Social Security Act in 1993 and in 2002 extended coverage, first, to companies with 10-19 workers and then to any company with one or more workers. The Fund is restricted to non-agricultural companies and is available to the self-employed but excludes the following groups:

-
- government officials and regular employees of various government levels;
 - employees of foreign governments or international organizations;
 - employees of a company located in Thailand but whose headquarters are abroad;
 - teachers or headmasters of private schools;
 - students, student nurses, undergraduates, and medical interns who are employees of schools, universities or hospitals.

The SSF provides the following benefits:

- Sickness benefit. Inpatient and outpatient benefits, sickness compensation equivalent to 50 per cent of the monthly wage, reimbursement for dental care (twice a year) and prostheses.
- Maternity benefit. In-kind and cash benefits. The maternity benefit is a lump-sum payment of 12,000 baht per delivery up to two deliveries. Cash benefits are in the form of 50 per cent compensation based on the average salary of the last three months (up to 90 days).
- Invalidity benefit. Lifetime invalidity compensation of 50 per cent of the average wage, lifetime medical reimbursement up to 2,000 baht per month, reimbursement for prostheses, funeral grant and, in the event of death, compensation to relatives ranging from 1.5 to 5 times the average wage of the beneficiary, depending on the number of contributing months.
- Death and survivors' benefit. Compensation for funeral expenses, compensation for relatives in the event of death, under the same conditions as indicated under the previous point.
- Child allowance. A monthly grant of 350 baht per child for up to 2 children.
- Old-age benefit. A pension equal to 20 per cent of the last 60-month average wage, plus various compensatory and lump-sum amounts payable to secondary beneficiaries if the primary beneficiary dies within 60 months of retirement or has contributed for less than 6 months.
- Unemployment benefit. A subsidy of 50 per cent of the highest three-month average wage for a maximum 180 days in case of involuntary unemployment and 30 per cent and 90 days in case of voluntary unemployment.

The SSF is financed by a tripartite mechanism under which the employee, the employer and the Government contribute to the scheme. Contributory rates vary according to the benefit concerned, as shown in table 17. All in all, the SSF covers 8.8 million workers and 400,000 self-employed persons, i.e. 26 per cent of the total labour force.

Table 17. Thailand: Contributory rates under the Social Security Fund as a percentage of insurable earnings

	Contributory rate (%)			Total
	Sickness, maternity, invalidity and death benefits	Child allowance and old-age benefits	Unemployment insurance	
Government	1.5	1	0.25	2.75
Employer	1.5	3	0.5	5.00
Employee	1.5	3	0.5	5.00

Source: Social Security Office of Thailand, 2010.

Workmen's Compensation Fund (WCF)

The WCF is designed to cover the negative consequences of work-related injuries, diseases, disabilities and death. The Fund is financed exclusively by the employers, who contribute a percentage that ranges from 0.2 per cent to 1 per cent of the worker's insurable earnings, depending on the level of risk in the industry. It provides the following benefits:

- Sickness benefits in the form of cash compensation (60 per cent of the monthly wage within an upper and lower limit of 2,000 and 9,000 baht) and medical services.
- Disability benefits that comprise a cash compensation of 60 per cent of the monthly wage for up to 10 years for partial disability and 15 years for permanent disability, plus surgical and rehabilitation expenses.
- Death and survivors' benefit equal to 100 times the highest minimum daily wage to cover funeral expenses and compensation of 60 per cent of the monthly wage for eight years, up to a maximum of 9,000 baht per month.

In 2008 about 8 million workers in Thailand were affiliated to the WCF, from approximately half a million in 1991. The average number of workers receiving a benefit or compensation was 200,000 between 2000 and 2007. The Fund covered 22.6 per cent of the labour force.

Government Pension Fund (GPF)

The GPF was launched in 1987 under the Government Pension Fund Act B.E. 2539 to insure its members upon retirement and to encourage them to save and to improve their living conditions. The GPF, which is the only programme of its kind in Thailand, was originally voluntary, but in 1996 it became compulsory for all government staff. Since 2008 the contributory rate has been up to 12 per cent of the employee's salary plus 3 per cent from the Government. In 2008 the GPF had 1,168,085 members, which corresponds to 3.2 per cent of the labour force and 96 per cent of Government staff.

Provident funds

Provident funds are voluntary contribution schemes where the pay-out takes the form of a lump sum constituted from the employer's contributions, the employee's contributions and investment dividends that the employee receives upon retirement or when his or her employment terminates. The employee contributes between 2 and 15 per cent of the salary which the employer must match. By 2009 there were a total of 503 provident funds which were worth 66.9 million baht and involved 9,370 employers and 2 million employees (5.3 per cent of the 2009 labour force). After almost doubling between 2005 and 2008, revenue from total contributions fell by 27.2 per cent.

Private-School Teachers' Welfare Fund (PSTWF)

This fund was established in 1975 as a welfare measure for teachers in the private sector who were generally less well paid and had worse conditions of service than their counterparts in the public school system. Teachers contribute a maximum of 3 per cent of their salary and employers must contribute the same. The Government doubles the contribution of the teacher. Beneficiaries of the PSTWF are entitled to free health care, child allowances, the payment of school fees, invalidity and death benefits and old-age benefits.

Under the new Private School Act, PSTWF members can also borrow money from the Fund. The Fund had 150,000 members in 2006.

10.2.2. Non-contributory social programmes

Pensions

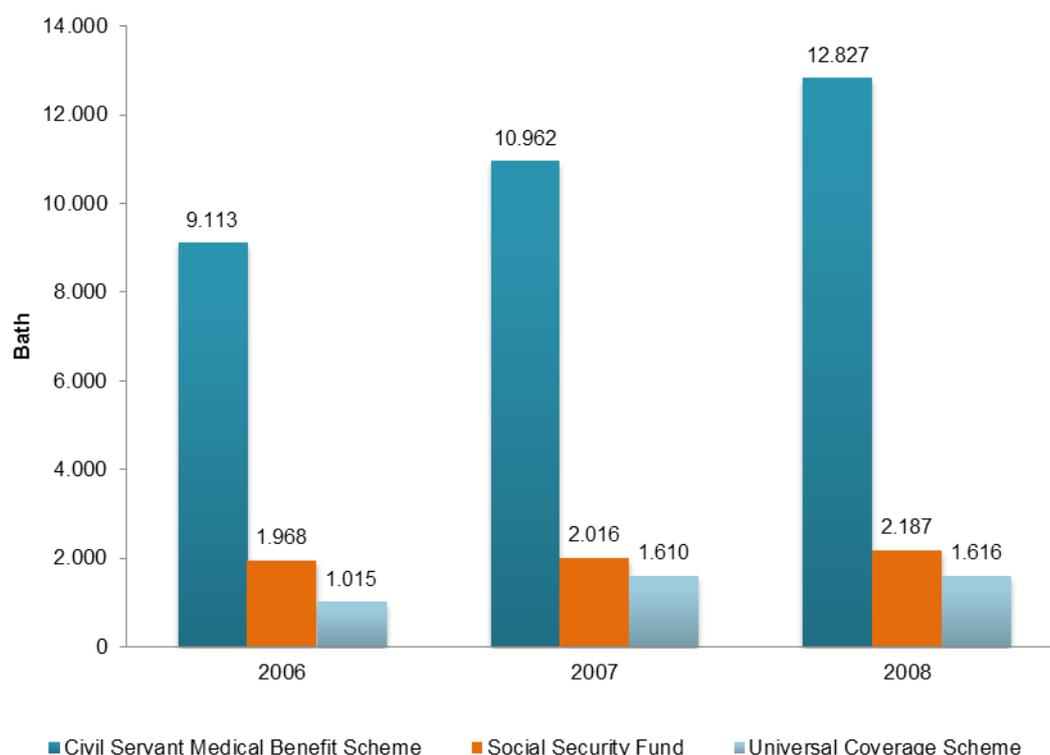
There is no universal pension scheme in Thailand. Only government officials and state-enterprise employees are entitled to non-contributory social pensions financed by budgetary allocations. These employees can choose between receiving a lump sum payment or a pension on condition that: (a) they have reached the retirement age of 60; (b) they have been working for the public sector for at least 25 years; and (c) they wish to terminate their employment. In 1996 the pension scheme reform introduced several changes. First, any public employee recruited after March 1996 must be affiliated to the GPF. Employees working with the Government before that date had the option to switch to the GPF or to continue under the previous system. If the latter, then the formula for calculating the pension is changed to include the average of the last 60 months salary instead of the last salary received. The pension is capped at 70 per cent of the average of the last 60 months salary.

In 2007 a total of 333,143 persons received a non-contributory pension from the Government; 9,277 received a lump-sum payment. The cost of these payments amounted to 20 per cent of the total government payroll for that year. Government expenditure on pensions increased by over 20 per cent per year during the first years following the 1996 reform, but by 2007 the annual increment had declined to 5 per cent.

Non-contributory health care – the Civil Servant Medical Benefit Scheme (CSMBS)

The CSMBS provides medical benefits to government officials and their dependents. It is usually described as the most generous scheme in Thailand (ILO, 2008a). Persons affiliated to the scheme are entitled to outpatient and inpatient medical services without limit, if received in public hospitals. Between 2006 and 2008 the total number of registered beneficiaries grew from 4.1 to 4.3 million persons, covering 6.4 per cent of the Thai population. However, the fiscal cost has been high in the last two decades, during which expenditure under the programme increased from 37 to 54.9 million baht, i.e. by 40.7 per cent in nominal terms. On average, the cost per beneficiary under the CSMBS was 5.3 times higher than in the Social Security Fund and 7.9 times higher than under the Universal Coverage Scheme (figure 80).

Figure 80. Thailand: Cost per beneficiary in selected social protection programmes, 2006-2008



Source: Author's estimates based on Chandoevrit, 2010.

Social assistance programmes

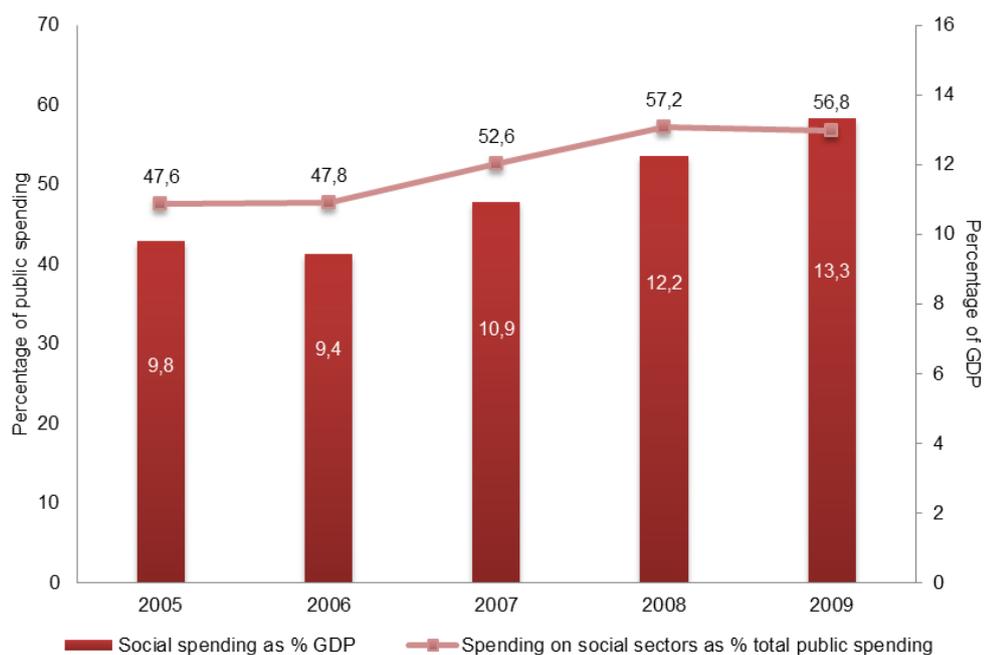
Thailand has a long tradition of implementing social assistance programmes, one of which dates back to 1941. Social assistance policies target highly vulnerable groups such as the elderly, people living with HIV and AIDS, children and poor families. Among others, the services provided to those groups include accommodation, basic needs, counselling, free education and training, and healthcare.

Social assistance programmes comprise both cash and in-kind benefits financed by general taxation. Cash benefits are granted to elderly people, PLHIV and disabled persons. Within the whole social protection policy, social assistance is the category with the lowest priority if judged by the small budget allocated to the Ministry of Social Development and Human Security. This limited budget restricts the expansion of the programmes and coverage is consequently low across the board. In 2006, for instance, the beneficiaries of social assistance were 6,247 children, 1,964 disadvantaged women, 1,390 elderly people, 4,804 disabled people and 8,490 beggars. Coverage was relatively high only among people with low incomes and very needy families (approximately 293,000 beneficiaries).

10.2.3. Expenditure on social protection

Social spending in Thailand accounts for 13 per cent of GDP, up from 9.8 per cent in 2005 (figure 81). This upward trend is not just a product of the last decade but has been a consistent pattern for the last two decades, running parallel with the accelerated economic growth experienced since 1987. Another remarkable aspect of social expenditure in Thailand is its increasing share in public expenditure. Between 2005 and 2009 a little more than 50 per cent of the public budget was allocated to social services, including health, social promotion, housing and entertainment, culture and religion.

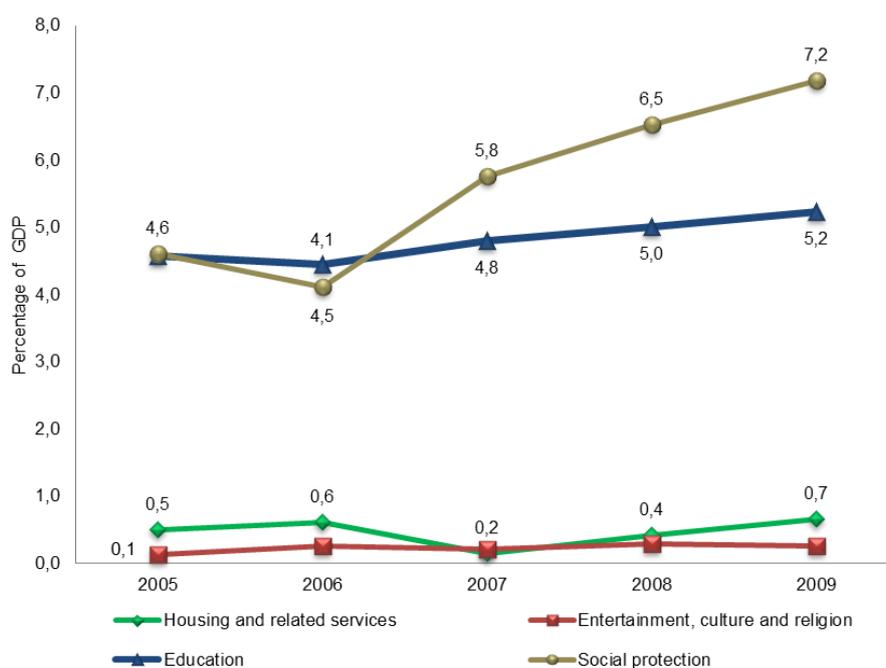
Figure 81. Thailand: Social spending as a percentage of GDP and of public spending, 2005-2009



Source: Ministry of Finance, 2010a and 2010b; International Monetary Fund, 2010b.

Not only is expenditure on social protection the component of social spending with the largest share in total public expenditure but it is the component that grew fastest between 2005 and 2009 (figure 82). Education too followed an upward trend, but the gap with social protection tended to widen over time. In 2005 the ratio of social protection to education was 1:1, but by 2009 it had risen to 1.37:1. This suggests that there is a strong commitment on the part of the Government to allocate more funds to social protection.

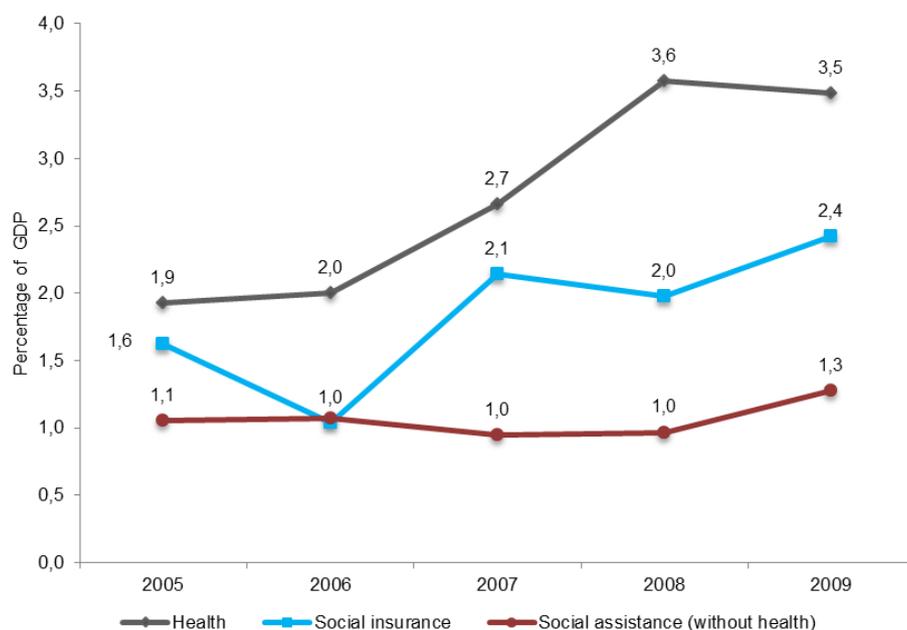
Figure 82. Thailand: Social spending by category, 2005-2009



Source: Ministry of Finance, 2010a and 2010b; International Monetary Fund, 2010b.

Regarding the composition of expenditure on social protection (health, social insurance and social assistance), the highest allocation of resources goes to healthcare services, although during the period assessed every single component increased its participation in GDP (figure 83). In fact, between 1995 and 2009 health expenditure doubled its participation in GDP as a result of increased spending under the CSMBS and the introduction of the Universal Coverage Scheme.

Figure 83. Thailand: Health, social insurance and social assistance expenditure as a percentage of GDP, 2005-2009



Source: Ministry of Finance, 2010a and 2010b; International Monetary Fund, 2010b.

10.2.4. Filling the gap in the healthcare sector: The Universal Coverage Scheme

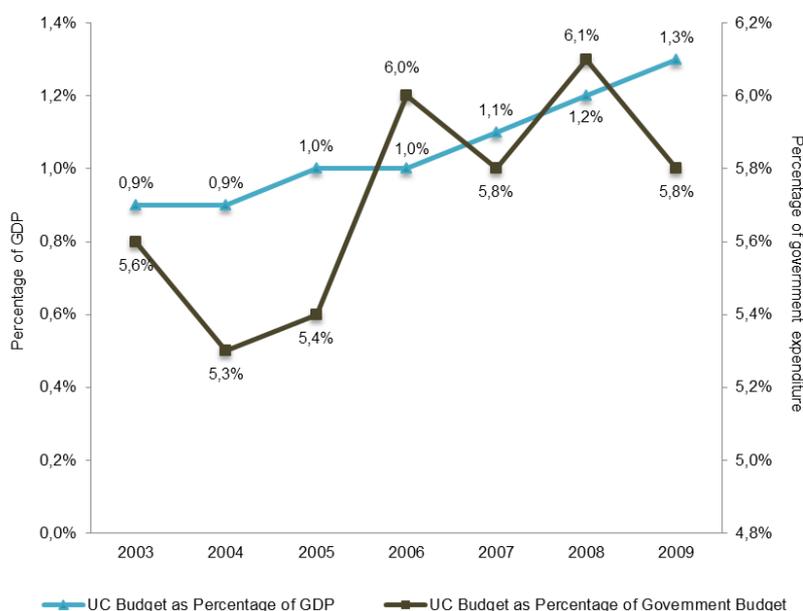
In terms of the number of people covered, the Universal Coverage Scheme is by far the most important social initiative in Thailand. The Government introduced the scheme in October 2001 in order to provide healthcare coverage for all Thai people excluded from the other programmes (CSMBS, SSF). Before 2001 approximately 30 per cent of the population was thus excluded. With the UCS the Government improved access to health services for low-income households and other excluded groups such as agricultural workers. In this way the Government defined a health scheme for each group: private employees, public staff and the rest of the population (Sakunphanit, 2006).

The legal framework of the UCS programme is the National Health Security Act B.E. 2545 of 2002, which stipulated that the National Health Security Office (NHSO) would administer the programme at the same time as it set up the National Health Security Fund. The UCS is financed by budgetary allocations from general tax revenue, although a 30 baht co-payment per visit was initially foreseen. After 2006 the co-payment was cancelled and access is now free of charge. The package of services includes annual physical check-ups, maternity benefits, prevention and health promotion services, ambulatory services and in-patient services.

Total coverage averaged 47 million people in the period 2006-08, or 70.3 per cent of the Thai population. This included most of the 30 per cent formerly without any coverage at all and the beneficiaries of other programmes such as the low-income scheme.

The fiscal cost of the programme grew considerably in that same period, from 48.3 to 76.6 billion baht (a 58.7 per cent increase). As has been seen, the cost per beneficiary under the UC programme increased but the allocation of government funds was still well below average expenditure in the CSMBS. Nevertheless, in its share both of GDP and of government expenditure, the UC has been on an upward path. Since 2003 the programme has gained 0.4 percentage points in terms of GDP, to average 1 per cent of GDP between 2003 and 2009. As a proportion of government spending, too, the UC accounted for an average of 5.7 per cent over the same period (figure 84).

Figure 84. Thailand: UC budget as a percentage of GDP and of the government budget, 2003-2009



Source: Ministry of Finance, 2010a and 2010b; International Monetary Fund, 2010b.

10.3. The construction of fiscal space for social protection

Thailand has an interesting tradition in the design and implementation of social protection policies of the most diverse nature, from contributory social security initiatives to small and fragmented social assistance programmes. Health-related programmes are of particular interest and are among the most important political issues in the country. Section 52 of the Constitution establishes that all Thai people have the right to health services, thereby recognizing the central role of health in the promotion of a more productive and equal society.

Mechanisms utilized by the Government to increase fiscal space for social protection include general taxation, special contributions from the Government, social insurance revenue and, in certain cases, voluntary health insurance.

To achieve universal healthcare coverage, Thailand has followed what Sakunphanit (2006) calls “a pluralistic approach”. Government strategy has relied on the establishment of three different programmes with different target populations:

- a Social Security Fund for private employees;
- a Civil Servant Medical Benefit Scheme for public employees;
- the Universal Coverage Scheme for the rest of the population.

Table 18. Thailand: Social protection benefits and sources of financing

Work status Contingency	Government employee	State-enterprise employee	Private employee in non-agr	Private school teacher	Other workers (self-employed, agric. employee)
Sickness and maternity	General tax revenue	State-enterprise revenue	WCF and SSF + contribution from government	PSTWF + contribution from government	UCS
Death and survivor					No
Disability					No
Child allowance					
Unemployment	not relevant	not relevant	SSF	No	No
Pension: Defined benefit	General tax revenue	No	SSF	No	No
Pension: Defined contribution	GPF + contribution from government	Provident fund	Provident fund	PSTWF	No

Source: Chandoevmit, 2010.

While the SSF is contributory in nature and is expected to be self-sustained, the other two schemes are non-contributory programmes that depend on budgetary allocations from the Government for their financing. This is certainly not a problem when the Government has an expansionary and sustained expenditure strategy, but one of the main characteristics of the Thai Government has always been its prudence in the management of both revenue and expenditure. In fact, with the single exception of the 1997 Asian financial crisis (period between 1997-2002), the country has maintained fiscal surpluses or very small deficits by pursuing a revenue-driven spending policy.

The key question, therefore, is how the Government has managed to increase its health-related expenditure at a time when public sector participation in the Thai economy has been relatively low and stable. As was noted earlier, fiscal revenue has typically remained under 20 per cent of GDP and so the room for expansionary programmes is certainly limited.

Regarding the evolution of the main components of public expenditure in the long term, three main conclusions may be drawn:

1. To finance improvements in public health, the Government decelerated the growth of expenditure on defence and education. In periods of prolonged peace, military spending need not be high, and so the security budget has followed a downward path from the 1970s, when it accounted for between 20 and 26 per cent of total public expenditure, to the 2000s, when it constituted roughly 15 per cent of the government budget.
2. Reduced debt service payments also helped to free resources for health programmes, particularly the Universal Coverage Scheme. Although the financial crisis pushed up debt-related payments, they still did not reach the level of 25 per cent of GDP observed in the mid-1980s.
3. Clearly, budgetary allocations for public health spending grew during this period and their share in the total government budget more than doubled between 1984 and 2007; today, one in every ten baht is spent on public health. The introduction of the UCS constituted another break in the trend, and since its launch in 2001 the health budget has increased by a further 3 percentage points in the Government's spending structure. Of the resources freed as a result of reduced security and public debt payments, 29 per cent were spent on health, education, social services and infrastructure (Wibulprasert, 2005).

Two missing points deserve some attention here. Besides the Government's strong political commitment to increase overall expenditure on social protection, by changing the composition of the public budget, economic growth also played an important role in generating new resources for the Government. The impact on unemployment, though significant in terms of the low levels experienced in the last two decades, has been limited because the SSF mainly covers the formal economy, but not the agricultural sector, which employs most workers. As to revenue collection, it is true that the share of total public revenue in the economy remained practically unaltered, but the level of resources grew considerably from 1987 onwards. The Government's prudent management of fiscal resources also resulted in budget surpluses that allowed the country to increase its expenditure on social protection even during times of crisis.

Furthermore, the high rate of economic growth was responsible for the remarkable decline in the incidence of poverty between 1990 and 2009, when that growth resulted in substantial savings for the Government in terms of reduced social assistance budgets.

Another issue frequently described as very largely explaining the successful implementation of the UC is the political process through which the programme was designed (Pitayarangsarit, 2004; Tangcharoensathien et al, 2007). With the backing of the 1997 Constitution, several civil society organizations gained power and pushed for the introduction of a universal health-care coverage scheme. This political cause was paralleled by the 2001 campaign led by the Thai-Rak-Thai party, which adopted it as one of its electoral promises. Once in office, the new Government endorsed the Universal Coverage Scheme and the initiative was quickly adopted thanks to several favourable circumstances surrounding its design and implementation, including:

- Strong evidence from academic sectors pointing to the tremendous social and economic benefits that would derive from universal coverage;
- the very active role played by the Prime Minister and the endorsement of the strategic overview of the crisis by the Government, which saw it as an opportunity to protect people by expanding health services;
- the initiative's fiscal feasibility and sustainability;
- the support the initiative received from non-governmental organizations and other civil society groups;
- the institutional capability of the Ministry of Public Health to launch a phased introduction of the programme.

The decision to finance the programme through general taxation was, in the opinion of Tangcharoensathien et al (2007), a pragmatic one, because universal coverage cannot be achieved by means of contributions. Moreover, the full coverage target called for immediate results. Finally, because most of the population not previously covered belonged to the informal agricultural sector, a group without regular income, the collection of contributory fees would have been very problematic.

Jansen and Khannabha (2009) have an interesting position regarding the establishment of the UC and the creation of fiscal space. According to these authors, the UC was part of a more general fiscal stimulus plan that followed after the 1997 financial crisis, which thus contributed to the approval of the UC scheme. The general plan, which also comprised such measures as the creation of a People's Bank, a debt moratorium for farmers and a village fund, aimed at increasing the amount of money in the hands of people with a high propensity to spend.

10.4. Challenges and lessons learnt

10.4.1. Challenges

In terms of challenges, the key issue is the sustainability of the UC scheme. It is widely accepted that general taxation as a source of financing could become a political issue, fluctuating according to the Government's agenda. Although in the past the Government of Thailand has shown a strong commitment to the concept of social protection, there is still some concern as to the fiscal possibility of expanding the programme in coming years, given the rate of population growth and existence of new demands deriving from the heightened prevalence of chronic diseases and the growing package of services sought under the UC programme. The establishment of "sin" taxes on luxury goods, for example, could increase fiscal space for universal coverage while at the same time avoiding the instability associated with general taxation.

Another possibility mentioned in Sakunphanit (2006) would be to reform the SSF so as to extend its benefits to the non-working spouses and children of current beneficiaries. This could contribute to reducing the pressure on the UC programme.

Another challenge relates to the fragmentation of the health sector. The current organization of the sector should be visualized as an intermediate stage towards an integrated network unifying the various existing schemes. This is clearly a major challenge given the political and economic implications of social protection and the existence of different packages of benefits which reflect the interests of groups that will oppose any deterioration in the benefits they currently enjoy. The integration of the system may, however, yield some positive results in terms of reduced administrative costs and enhanced efficiency and thus free more resources for healthcare purposes.

10.4.2. Lessons learnt

Thailand, a country with low revenue and expenditure ratios but high social spending, is an interesting case. There is a clear intention on the part of the Government to support human capital formation by shifting resources previously spent on debt service and security budgets to health and education. Whether or not this strategy is tantamount to creating fiscal space is subjective. That said, reallocating resources from one sector to another in the interests of social protection (or any other goal) does indeed expand fiscal space, in the sense that fiscal space can also be generated by shifting resources from less efficient to more efficient sectors, as Thailand has done.

Economic growth has also played a critical role by increasing the level of per capita fiscal revenue and by reducing poverty. Regarding the latter, the effect was indirect because lower poverty rates meant that fewer funds needed to be allocated to social assistance.

The launching of the Universal Coverage Scheme stands as a turning point in the history of social protection policies in Thailand. Despite the country's outstanding macroeconomic performance prior to the Asian financial crisis, one in every three Thais lacked adequate health coverage in 2000. With the introduction of the UC programme, the Government fulfilled its objective of providing full social security coverage for private employees (through the SSF), for government staff (through the CSMBS) and for the rest of the population (through the UC programme).

In this respect, the country offers several lessons in increasing fiscal space for social protection objectives.

Lesson 1

When fiscal revenue is limited, the key to increasing social protection is the political will to do so, as mentioned before. The Government of Thailand has approached social protection as an investment offering economic and social gains, and this focus has a positive effect on the allocation of resources.

Lesson 2

Governments should promote their policies with the kind of pragmatism and strategic approach adopted by the Government of Thailand. If no threats exist to the nation's security, then defence spending should be reduced so as to free resources for other purposes. In general, the internal reallocation of resources can be looked upon as expanding fiscal space in the way that any shift of funds increases the value for money of public expenditure.

Lesson 3

A pluralistic approach can be an alternative means of providing health protection by segmenting the market according to the key characteristics of each target group. Even with such mechanisms as the voluntary health card – not very popular elsewhere – Thailand achieved 20 per cent coverage. The danger of this approach, however, is the fragmentation of the health sector and the consequent inefficiencies and other problems in terms of quality of the services provided. Therefore, a pluralistic approach can be envisaged as an intermediate phase towards full coverage, but a more integrated or articulated system is needed to ensure the provision of services and the sustainability of financing.

Lesson 4

The evidence suggests two things about universal coverage. First, it reaffirms the idea that general taxation plays a critical role in the achievement of this objective in countries where informal labour markets prevail. Second, universal coverage in Thailand was not the product of just one source of financing (general taxation) but was made possible by using a hybrid model that combined the mechanisms of both contributory and non-contributory schemes.

Lesson 5

Politics and science can work in partnership without any problem. One of the key factors that explains the successful approval and implementation of the UC programme was the decision of the Government to base its support for the initiative on scientific evidence. In this way the Government created a solid foundation for the project and gained the support of academic circles and NGOs.

Lesson 6

Civil society should be seen as a partner in the creation of fiscal space. Its involvement does not imply that it should present a finished product to its audience but that it should co-design the main features of the project jointly with its social partners. The concept of “the triangle that moves the mountain” helps to understand the process, the idea being to bring together all the necessary know-how by means of research, social movement and political commitment.

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