Bargaining for Fiscal Space: Mobilizing Domestic Resources for Social Development

Research

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The Challenge...

 ...to build social policies on financial arrangements that are sustainable in fiscal and political terms, equitable & progressive, and conducive to economic development







Resource mobilization

Efficiency gains Fund reallocation

Revenue sources

Financing techniques

Expenditure choices

Taxation/Contributions
Aid / Borrowing
Remittances/OOP
Mineral Rents

private/public funded/PAYG Direct/indirect tax Social services
Social protection
Labour market policies





The Context: Globalization

- Globalization has put pressure on states' capacity to raise revenues:
 - Liberalization of markets
 - Income and asset concentration
 - Labour market problems
 - External debt and global imbalances
 - Global economic and financial crisis
 - Aid flows / commitments?

- Demand for social policy has increased:
 - Volatility of market processes, economic and financial crises
 - Unemployment, informality, poverty (working poor)
 - Demographic change
 - HIV/AIDS pandemic and natural disasters
 - MDGs and national development strategies





The crisis and finance for social development

- Foreign capital/aid and domestic credit
 - Financing costs (internal/external) 个
- Trade and FDI
 - tax revenues ↓
- Commodity prices and Terms of Trade
 - tax revenues √
- Remittances
 ↓ Household income ↓
- Social expenditures 个, subsidies 个

Refocus on importance of domestic resource mobilization (Monterrey Consensus etc.)



Fiscal Space

 <u>Budgetary</u> room to finance public policies in a sustainable way (honour debt obligations, maintain solvency..)

Expanding fiscal space:

- Reallocation of existing revenues/efficiency gains
- Mobilization of additional revenues

Estimating fiscal space:

- Compare actual expenditure with benchmarks
- Compare actual expenditure with costs of basic package (SPF)
- Assess space to increase tax revenues or public borrowing (Oxfam Report, IMF)





Is Social Policy affordable?

- Social policy is an <u>investment</u> in people's well-being and in development (productivity, social cohesion)
- Type of interventions and programmes as well as costs depend on policy legacies and structural factors, political priorities, and contemporary needs
- Basic social protection packages are affordable, even in low-income countries (ILO/SPF costing studies, DESA simulation on MDG financing for LA, Unicef/Helpage costing tools etc.)
- The costs of inadequate financing of social policy are high...





Social Expenditure is a Policy Variable

Government expenditure on social protection (social insurance, social assistance) in three middle income countries in LA

(Barrientos, 2010)

Country	In % of GDP
Argentina (2004)	9.2
Brazil (2004)	13.2
Mexico (2002)	3.5





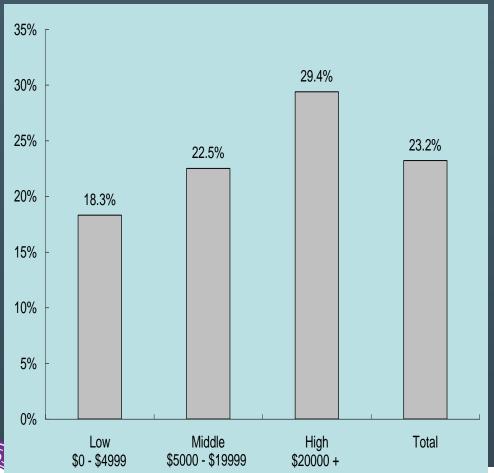
Mobilizing Revenues

- Tax reform
- Extension of contributory systems (social insurance)
- Capture of mineral rents
- Trade, tariffs
- Foreign aid
- Domestic and external borrowing, FDI
- Public-private partnerships
- Private funds (HH income/savings, remittances)





Tax Revenue as % of GDP by country group



The aggregate view: tax shares as % of GDP rise with income level

Source: Bird and Zolt (2005).



Tax Reform

- Tax reform remains a key challenge for developing countries.
- Taxation
 - Is superior to other revenues in terms of distributional justice and to reach universal coverage
 - <u>Direct taxes</u> have greater potential in terms of progressivity / redistribution / solidarity
 - indirect taxes (VAT): design matters for redistribution
 - trade tariffs ↓
 - Can enhance strong state-society relations and state accountability (all contribute, all benefit)
 - Is more sustainable than external revenues





Revenue type, distribution and social relations

- Time-burden tax (self-provision)
- User fees (most regressive, least solidaristic)
- Pre-paid schemes
- Generalized insurance
- Indirect taxes
- Earmarked taxes
- Direct taxes (most progressive, most solidaristic)

Source: Delamonica and Mehrotra 2009.

Regressivity



Solidarity







Political-economy of taxation

- More convincing to argue for progressive direct taxation if public/social expenditures benefit all (universalism)
- To overcome obstacles towards direct taxation, find <u>functional</u> <u>equivalents</u>:
 - Marketing boards
 - Land/export taxation etc.

Key questions

- What are the political conditions for progressive tax reforms?
- Who are the actors involved in bargaining and negotiation processes?
- What are the linkages with social development policies?





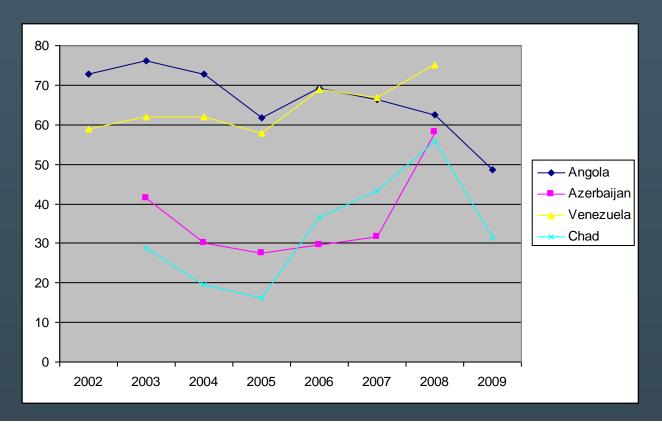
Mineral rents and financing social policy

- Can mineral rents ease the financing constraint?
- Challenges:
 - Dutch disease effects and volatility
 - State capacity and democratic governance
 - Build a social consensus on the use of funds:
 - Norway: Government Pension Fund Global
 - Bolivia: Renta Dignidad financed through Direct Hydrocarbons Tax (32% production tax 2005)
 - Chile: Extension of Social Pension Coverage (2008)





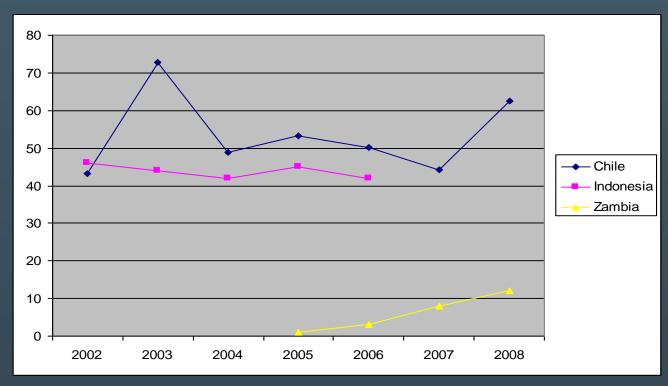
Share of government revenues in oil rent (in % of total, UNCTAD TDR 2010)







Share of government revenues in copper rent (in % of total, UNCTAD TDR 2010)







Mineral wealth: Blessing or Curse?

- Resource curse thesis ⇒ empirical works by Richard Auty and by Sachs and Warner (1995) followed by many others – dominates global debates on natural resource-led development
 - Negative relationship between natural resource abundance and growth performance
 - causal relationship exists that explains this negative link
- Main criticism
 - methodological issues
 - deterministic conclusions
 - pessimistic prospects
- ⇒Interesting question is to identify specific challenges of mineral-led development and how to overcome these





The challenges of mineral-led development I

- Economic challenges: Dutch disease, price and revenue volatility, terms of trade, enclave nature of mineral production, limited employment creation, limited incentives for skills investment and education
- Political challenges: who captures rents (foreign investors, private investors, state, elites)? How are mineral rents invested, revenues spent? Rent-seeking and corruption? Distributional conflicts? Access to rents finances violent conflict or undemocratic regimes?





The challenges of mineral-led development II

- Social challenges: inequalities (income, regional, gender, ethnic/indigenous peoples' rights), potential fragmentation of social systems
- Environmental challenges: ecological costs associated with EI: depletion; pollution and destruction of environment; climate change





Natural resource based sectors drive growth

- Global demand/prices ↑ (India, China)
- Incentives for investments
 (portfolio and FDI)
- New technologies (exploration, extraction)
- Path dependency of growth models based on natural resources
- Impact of neoliberal policies and globalization on domestic production (manufacturing): reorientation towards comparative advantages: « reprimarización »





Successful mineral-led development also requires

- Policies that foster diversification while safeguarding stability
- State capacity and institutions that are adapted to national contexts
- Consensus building on redistribution of rents and compensation of producing regions
- Sector strategies that minimize environmental and social costs
- Regulation and monitoring of foreign investors and global commodity (and related financial) markets; reduced trade barriers for more processed goods; policy space (capital controls, industrial policies etc.)
- Mobilization of domestic resources such as taxation and social insurance contributions





Interesting lessons from case studies

- Country context more important than resource abundance
- Mineral-led development has specific challenges that need to be addressed
- Balancing of economic and social goals and democratic politics lead to more sustainable and equitable outcomes





New Project:The Politics of Domestic Resource Mobilization for Social Development

- The project seeks to inform global debates on the political and institutional contexts that enable poor countries to mobilize domestic resources for social development
 - How to bridge funding gaps (MDGs, social protection floors)
 - How to enhance national ownership and policy space
 - Understand politics of revenue and social expenditure bargains
 - Connect literatures on politics of resource mobilization with politics of social provision





'Resource Bargains'

- Close relation between revenues and expenditures; limits to debtinancing
- LICs: dependence on IFIs and donors:
 - resource mobilization as technical issue (ideal tax system, neutrality, reduced redistribution through tax system)
 - Less responsibility for recipient countries to strike bargains with their citizens, bargains between governments and donors
- Social protection (poliy) literature focuses on expenditure/demand side (issues of retrenchment, privatization, coverage extension)
- Resource bargains: more negotiation, less coercion; can be informal, implicit, indirect, or direct; between state and citizens, state and enterprises/investors etc.





Research Themes

- Contestation, bargaining and outcomes
 - Conflicts over resources to be mobilized, who pays, design of policies etc.
 - Nature of revenue bargains, link to social provision
- Changes in key relationships
 - State-citizens
 - Donor-recipient
- Institutional development
 - E.g. institutions in financial sector, tax offices, central banks, independent revenue authorities, social service delivery
 - What reforms? Are there spill-over effects of institutional development? New modes of engagement with citizens?



A strategic approach towards the financing of social policy requires

- Reliable calculations on estimated costs of planned programmes over longer periods and taking into account different scenarios (ILO, Helpage)
- Evaluation of different funding sources and financing techniques and their pros and cons from a political, economic and social point of view
- Analysis of relevant experiences in other countries
- Early dialogue with relevant stakeholders, including Social <u>and</u>
 Finance Ministries, external donors, international organizations,
 social partners, civil society organizations etc.
- Contingency plan for crisis situation





Conclusions

- Financing mix is country specific, what is a (national, global) political priority is affordable
- Anchor a country's social policy system with domestic sources of finance (synergies between economic and social development)
- External resources (mineral rents, aid, remittances) have the potential to complement these, especially in LICs
- Successful transformation of resources into outcomes depends on design of social programmes (e.g. universalisms vs. targeting), broader strategy, politics and governance
- Avoid reforms that trigger long term costs for social development
- Fiscal constraints are no excuse to violate social rights!



Mineral rents and the financing of social policy:



POLICY BRIEF 16

Mineral Rents and the Financing of Social Policy: Options and Constraints

Mineral wealth is not a curse but an economic opportunity. UNRISD research suggests that when countries carefully balance productive and redistributive goals, mineral wealth can be harnessed for equitable and sustainable development. To manage the challenges of a mineral led growth path successfully, countries need to design and implement comprehensive, inclusive and rights-based social policies; build strong democratic institutions; and be given the policy space to foster productive diversification while safeguarding macroeconomic stability

Viscal reasonal reseases from commodity secons lines beind grown and realized the example of policy secons lines beind grown and realized the Ramy of today's rich countries have example of policy secons and ember of countries. Yet cheer is disregreening about whether an invested of development with the help of imboral reads. a diessing or a curse, especially in resource-dependent developing countries.

Fiscal Space

Resource-rich developing countries do not suffer the same constraints as resource-poor countries in providing

Policy decisions about the prospects for implementing and excanding social policies in develthat poor countries cannot afford universal public services such as health and education, or cash transfer schemes, due to a lack of fiscal resources and contributory capacity of the poor.

This constraint has become even more binding. This constraint has become even more in dring in the context of global value and the meaning often economic orise. A. The same is the , there is governed to growing more price to a governed to govern and the context of protection is urganity needed to be a context of protection is urganity needed to be a context of protection in the context of the contex

Transformative social policy

Transformacie social policy has muhiple functions and affects social softents are not less institutions and assist relations. It is conserved with production, reproduction, protection, and redistribution and postification in a normalize goals and as democracy, eguts, social inclusion and rights.

Renta from mineral extraction can play a role in foscoring social development and funding social policies in poor countries characterized by limited flacal resources, widescread coverty, inequality, and lack of decent employment on portunities. Mineral rerus have been utilized by many countries to initiate, develop and sustain their economic and sec all development. Rich their connersis and second decongreent. For countries such as Australia, Canada, the Yorkic countries and the United States scarted as producers of comic yeards from agriculture, fishing, forests or minerals. Revenues from commodity production holded to growth processes and advent for except on our foreign countries.

A Blessing or a Curse?

Despite resource abundance, and favourable commodities prices, mineral wealth is regarded by many as a curse

Many of today's developing countries are pro-ducers and exporters of crimary commodilles, and some nave recently uncovered vast in nera-deposits. This opens a window of page tunity for these countries to take advantage of naing international demand, sustained in part by the resource hungry Asian giants China and India.

If the international context is favourable for commodify exporters, we can resource our develop-ing hallons greep the opportunity and channel-revenues from their nature, resources towards improving their people's well boing and living standards? Deep as weeppead recognition of the revenue potentia of natura resources, thorre is disagreement about wice set a mineral led









Recent research on tax in Africa

- Taxation has been found to reflect colonial structures (Mkandawire 2010).
- Taxation has positive effect on democratization only where states, not proxies, have a role in collection of revenues (Herb 2003)
- Despite this, research suggests that country's in Africa that do tax develop in a slow but sustainable manner, and are less likely to suffer from civil wars (Ross 2001).
- This suggests that taxation helps empower the development of REAL representative institutions.





Taxation and democratization

- Interested in mineral poor regimes
- Taxation can support empowerment through contestation and bargaining
- Empowerment occurs as a process rather than an outcome
- Collective action and bargaining help develop representative structures and a more responsive state – civil society realtionship, democratization.

