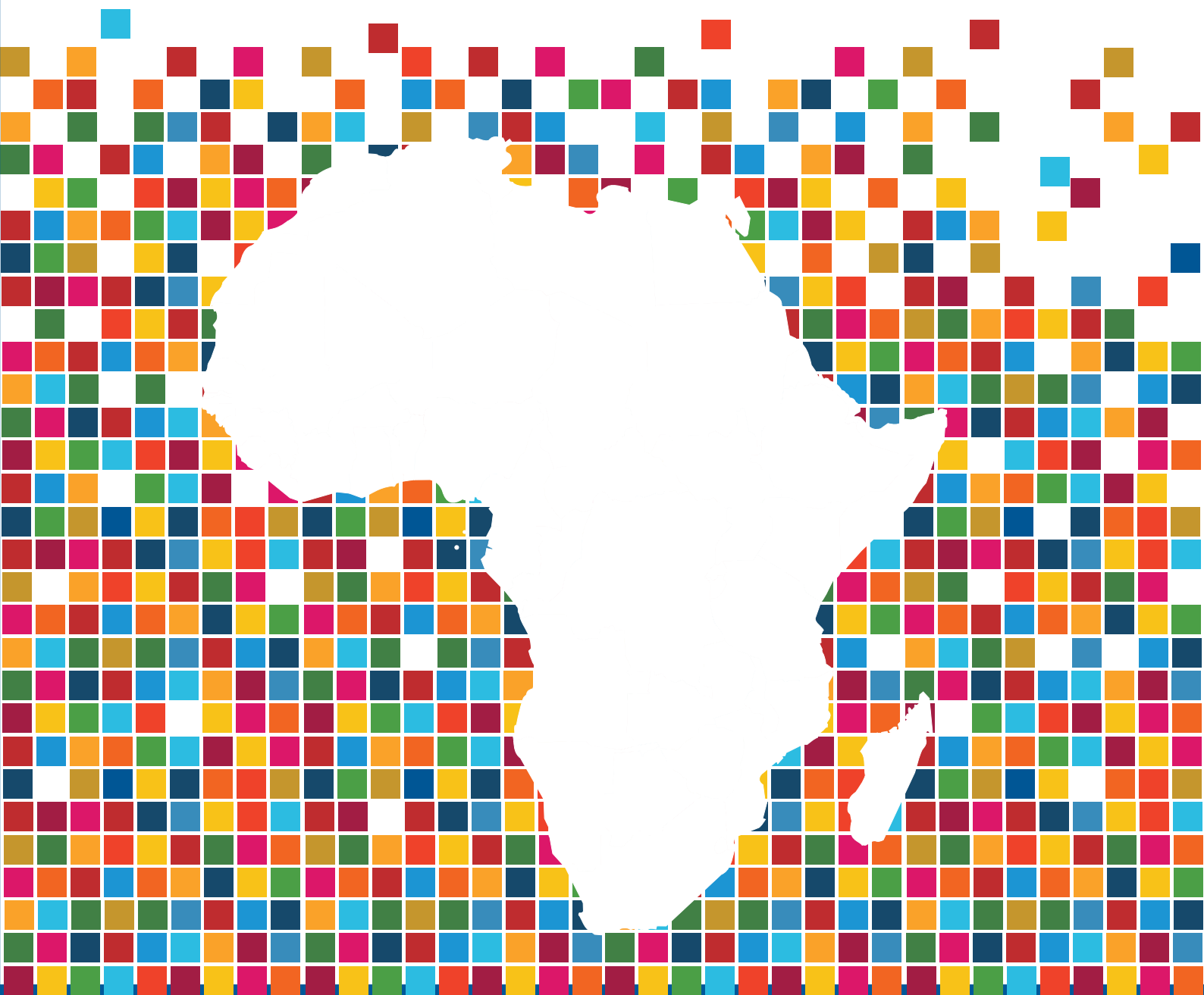


FISCAL POLICY FOR FINANCING SUSTAINABLE DEVELOPMENT IN AFRICA



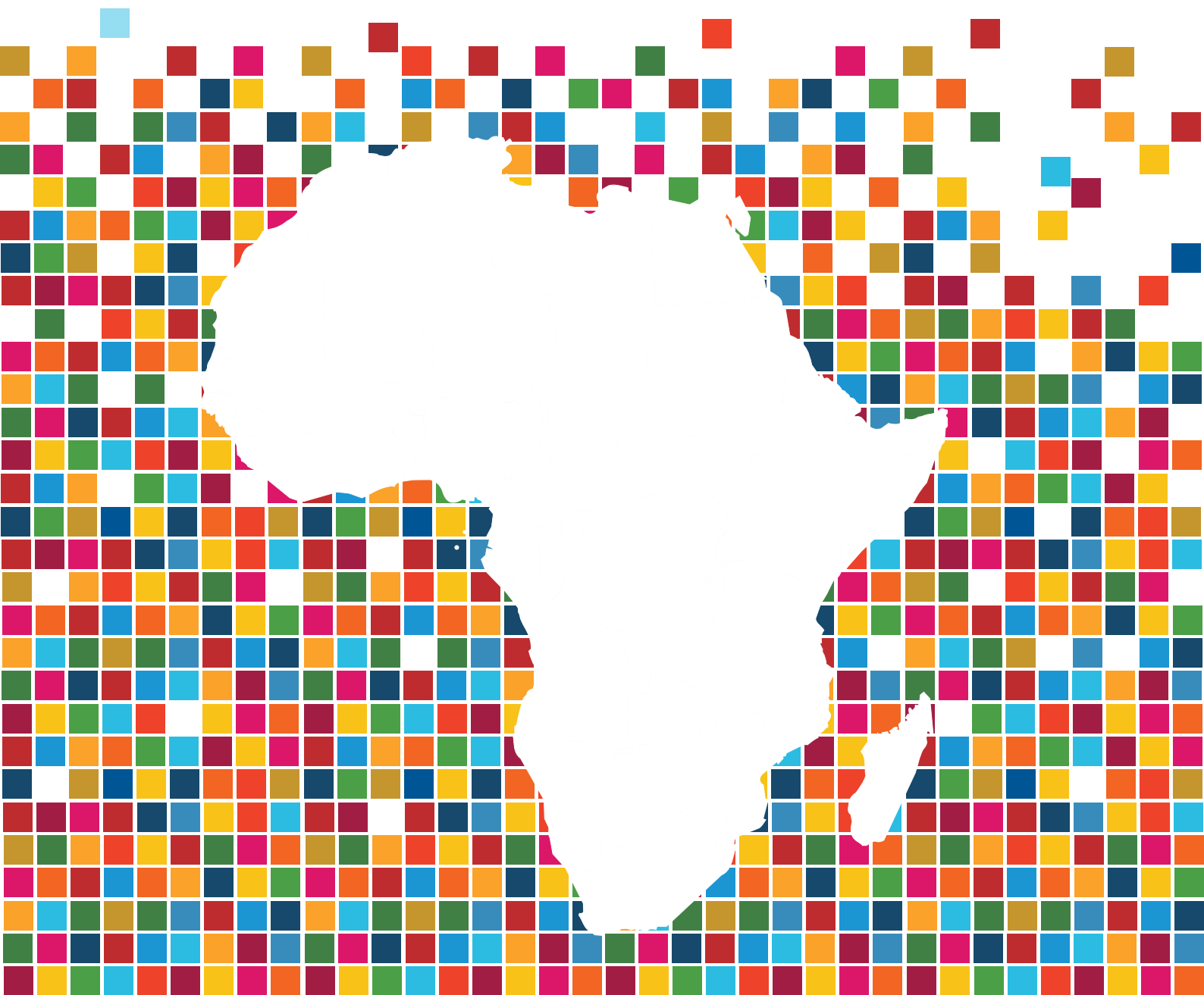
ECONOMIC REPORT ON AFRICA



United Nations
Economic Commission for Africa

2019

FISCAL POLICY FOR FINANCING SUSTAINABLE DEVELOPMENT IN AFRICA



ECONOMIC REPORT ON AFRICA



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LIST OF ABBREVIATIONS

AAAA	Addis Ababa Action Agenda
AfCFTA	African Continental Free Trade Area
ARDL	Autoregressive distributed lag
AU	African Union
BEPS	Base Erosion and Profit Shifting report of the Organisation for Economic Co-operation and Development
CFAF	Coopération financière en Afrique centrale francs
ECA	United Nations Economic Commission for Africa
EITI	Extractive Industry Transparency Initiative
EIU	Economist Intelligence Unit
FDI	Foreign direct investment
GDP	Gross domestic product
GNI	Gross national income
HIPC	Heavily Indebted Poor Countries
IGT	Identifiable group tax
IMF	International Monetary Fund
KSh	Kenya shilling
MDGs	Millennium Development Goals
MDRI	Multilateral Debt Relief Initiative
MRA	Mauritius Revenue Authority
MTRS	Medium-Term Revenue Strategy
OECD	Organisation for Economic Co-operation and Development
PwC	Pricewaterhouse Coopers
SDGs	Sustainable Development Goals
SIM	Subscriber identity module
SITC	Standard International Trade Classification
TADAT	Tax Administration Diagnostic Assessment Tool
TV	Television
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNIDO	United Nations Industrial Development Organization
US	United States of America
VAT	Value-added tax
ZIMRA	Zimbabwe Revenue Authority

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FOREWORD

Africa is at a critical juncture in its development trajectory. Policies adopted now will determine how quickly the continent accelerates growth and creates prosperity for all. In 2015, African countries signed up to two important development agendas: the global 2030 Sustainable Development Goals (SDG), which aims to leave no one behind as countries develop, and the African Union's Agenda 2063, which sets out a blueprint for the "Africa we want". A decade away from the SDG endpoint, African countries continue to search for policy mixes to help accelerate the achievement of these targets. However, for many countries, financing remains the biggest bottleneck with implementing capacity a close second.

To meet the SDGs Africa will need to raise an estimated 11 per cent of GDP per year for the next 10 years to close the financing gap. Today, Africa's average tax revenue to GDP is below 16 per cent. Efficient and effective domestic resource mobilization can address a substantial portion of this financing shortfall. The Economic Commission for Africa has consistently highlighted this position culminating in the position paper for the 2015 Addis Ababa Action Agenda on Financing for Development. The Economic Report on Africa: Fiscal Policy for Financing Sustainable

Development in Africa, 2019, examines the institutional and policy reforms required to enable African countries to maximize domestic resource mobilization. The report focuses on the instrumental role of fiscal policy in crowding in investment and creating adequate fiscal space for social policy, including supporting women and youth-led small and medium enterprises.

African governments could increase fiscal space, particularly through increased government revenues by 12-20 per cent of GDP annually by implementing fiscal reforms in six key areas. These areas include: adopting the right fiscal policy stance, reviewing and updating tax policy, expanding and deepening the tax base, improving tax administration, tackling tax avoidance, enhancing non-tax revenue collection and improving natural resources governance to combat tax evasion. The Report identifies several quick wins in Africa's pursuit of additional fiscal space to finance its accelerated development and meet the SDGs and Agenda 2063. Among other tools, rapid digitalization offers especially promising opportunities for African countries to increase revenue generation, reduce collection costs and extend taxation to some hard to tax sectors, such as the agribusiness sectors, real estate and services sectors, while improving the

enabling environment for the private sector and in particular small and medium enterprises.

The first priority for increased revenue is the fiscal policy stance. Countercyclical fiscal policies in Africa are shown to have growth enhancing effects. Second, with the changing composition of many economies, policy makers must review effectiveness of tax types and ratios. Exemptions and amnesty constitute important leakages and only serve to bolster company's profits without being a critical determinant of the decision to invest in a particular country. The African Continental Free Trade Area, is expected to boost investment and growth with no significant long term negative impact on government revenues. Third, improving revenue administration by broadening the base and simplifying collection are important areas which could raise over \$99 billion each year for the next five years. A number of countries such as Uganda have recently witnessed substantial improvements in tax collection by implementing electronic tax filing systems for example. Fourth, non-tax revenue is a significant source of revenue, such as the property taxes and in the case of commodity producing countries royalties. Five, base erosion and profit shifting, part of illicit financial flows are major sources of leakages, which if addressed could boost tax

revenue by an estimated additional 2.7 per cent of GDP. Finally, prudent debt management is required to ensure benefits of increased fiscal space do indeed go to find much needed social and physical infrastructure.

Africa can meet the SDG challenge and agenda 2063 through adequate and sustained efficient fiscal policy. While governments have chosen several country specific policy options, there are a number of lessons from successful implementation of reforms such as the introduction of electronic tax filing and payment automation in Rwanda, South Africa, Mauritania, Uganda, Kenya, Burkina Faso and others that all African countries can learn from to boost revenue collection. However, key to achieving this objective will be effective leadership, prudent public sector management and good governance.



Vera Songwe

Under-Secretary General of the United Nations

Executive Secretary of the
Economic Commission for Africa

EXECUTIVE SUMMARY

BACKGROUND

Transitioning to the Africa we want is within our reach. Africa is making steady progress in building the critical ingredients for sustainable and resilient societies, but progress towards achieving the Sustainable Development Goals (SDGs) is slow and uneven across the continent. Access to basic infrastructure such as energy, water and sanitation services is improving but falls well below the global average.

Effective implementation of Agenda 2063 and the 2030 Agenda for Sustainable Development requires African countries to scale up investments in science, technology and innovation to promote rapid and inclusive growth. The costs of these investments are enormous and require increased resource mobilization.

The Addis Ababa Action Agenda of 2015 provides a new global framework for financing sustainable development by aligning all financing flows and policies with economic, social and environmental priorities. It recognizes the importance of domestic public resources, supplemented by international assistance, in attaining sustainable development and achieving the SDGs. However, despite the numerous fiscal reforms undertaken by many African countries since 2000, government revenue as a share of GDP (21.4 per cent in 2018) remains low relative to the continent's potential and the financial resources needed to achieve national development aspirations. African countries can boost the government revenue by 12–20 per cent of GDP by implementing countercyclical fiscal policy, taxing hard to reach sectors, tapping non-tax revenue, introducing e-taxation and fighting tax evasion and avoidance, particularly in the natural resources sector.

The financing needs across the continent to meet the SDGs are huge, and the financing gap is wide. Estimates of the financing needs range from \$614 billion to \$638 billion a year (UNCTAD, 2014). Africa's annual financing needs for infrastructure, food security, health, education and climate change mitigation alone are estimated at \$210 billion (UNCTAD, 2014). To narrow the financing gap, African countries need to enhance domestic resource mobilization, and that requires sustained improvement in the efficiency and efficacy of fiscal policy.

This Report provides an evidence-based assessment of the nature and performance of fiscal policy in Africa. It analyses both challenges and opportunities and identifies best practices in order to draw policy recommendations and facilitate exchange of experiences. This can help member states to undertake necessary fiscal policy reforms and improve macroeconomic management.

The Report addresses critical questions of fiscal policy and financing of the SDGs in Africa. These include the nature and role of fiscal policy; the potential of fiscal policy, including tax and non-tax revenue, to enhance domestic resource mobilization; and the role of fiscal policy in macroeconomic management and achievement of the SDGs. The Report examines the key opportunities as well as the challenges in making fiscal policy more effective and efficient and offers policy lessons and recommendations to inform fiscal policy reforms in Africa.

Data for the Report's analysis include secondary sources and primary data and information collected from 12 African countries (Angola, Benin, Chad, Ethiopia, Ghana, Kenya, Mauritius, Mauritania, Mozambique, South Africa, Sudan and Zimbabwe).



Africa is making steady progress in building the critical ingredients for sustainable and resilient societies.



The Report addresses critical questions of fiscal policy and financing of the SDGs in Africa.



The number of countries included in the analysis of each issue depends on data availability. While the intention was to cover as many countries as possible, for some topics coverage is limited to a handful of countries with adequate data.

account deficits, stable exchange rates and lower inflation, revenue streams have narrowed since the commodity price shocks of 2014, leading to higher debt levels as countries increased borrowing to ease fiscal pressures.

KEY FINDINGS

GLOBAL ECONOMIC GROWTH AND FAVOURABLE DOMESTIC CONDITIONS UNDERPINNED AFRICA'S ECONOMIC PERFORMANCE, BUT PROGRESS ON SOCIAL DEVELOPMENT HAS BEEN SLOW

Economic growth in Africa, which moderated from 3.4 per cent in 2017 to 3.2 per cent in 2018, was supported largely by solid global growth, a moderate increase in commodity prices and favourable domestic conditions. In some of Africa's largest economies—South Africa, Angola and Nigeria—growth trended upwards but remains vulnerable to shifts in commodity prices. At the subregional level East Africa remains the fastest growing, at 6.1 per cent in 2017 and 6.2 per cent in 2018. West Africa's economy expanded by 3.2 per cent in 2018, up from 2.4 per cent in 2017, while Central, North and Southern Africa's economies grew at a slower pace in 2018 compared to 2017.

Although domestic demand, public investments and stronger trade between Africa and global markets supported growth, commodities remain a key driver of growth in Africa, exposing economies to commodity price volatility. Consequently, although the macroeconomic stance for African countries improved in 2018, with narrower fiscal and current

Africa has made notable progress in education, health and other social outcomes. Progress in poverty reduction has been steady. The poverty rate dropped from 54.3 per cent in 1990 to 36 per cent in 2016. However, the pace of poverty reduction is also slow, and inclusive growth—leaving no one behind—remains elusive. The poverty gap, which measures the depth of poverty, remains high, at 15.2 per cent against a global average of 8.8 per cent, partly because of high income-related inequities in access to public services. Income inequality is also high, at 0.44, measured by the Gini coefficient, despite being on the decline. Unemployment stood at just above 7 per cent in 2017 and is projected to remain there in 2019 as countries intensify efforts to diversify their economies.

FISCAL POLICY CAN BE AN ANCHOR FOR MACROECONOMIC STABILITY AND A KEY TOOL FOR ACHIEVING THE SUSTAINABLE DEVELOPMENT GOALS

While growth is projected to pick up in the medium term, current growth rates are not adequate to eradicate poverty or achieve the other SDGs in Africa. Accelerating growth is necessary to achieve the SDGs, but it is not enough.

African governments need to harness the fiscal policy instruments at their disposal to accelerate

efforts to achieve the SDGs. That means rethinking fiscal frameworks and directing them towards the achievement of the SDGs, as well as towards rebuilding fiscal space. Recalibrating fiscal policy could increase revenue collection. That includes taking business cycles into account in implementing fiscal policy to avoid the adverse impacts for macroeconomic stability that come with ignoring the business cycle. The Report finds that countries that adopt a countercyclical fiscal policy could increase government revenue by 5 per cent of GDP.

CORPORATE TAX REDUCTIONS OFFER LITTLE INCENTIVE FOR INVESTMENTS

For African countries, lowering taxes does not significantly influence investment. The Report finds that to achieve a 1 per cent increase in total investment, governments could lose up to 20 per cent in tax revenue. African countries should thus avoid joining the race to the bottom and lowering taxes to attract foreign investment, since the gains will be much smaller than the revenue loss.

In contrast, fiscal policy is vital for “crowding in” private investment in Africa, which has a significant effect on real GDP per capita. In the long run a 1 per cent increase in private investment could boost GDP per capita by up to 1.6 per cent.

Fiscal policy can speed up economic diversification and accelerate structural transformation in Africa, since government consumption has the second largest impact on manufacturing value added. In light of that knowledge, governments need to revisit their spending plans so that they boost domestic demand for manufactured products. Full implementation of the African Continental Free Trade Agreement will also increase investment in Africa.

INDIRECT TAXES HAVE BEEN THE MAIN SOURCE OF TAX REVENUE

African economies have large informal sectors, which for the most part function outside the

tax net. It is difficult to identify economic agents in the informal sector and ensure that they are appropriately taxed. Consequently, to reach them, governments rely mainly on indirect taxes such as consumption taxes, which generate more than 60 per cent of tax revenue. Realigning fiscal instruments to capture the large informal economy could increase revenue collection.

Taxing hard to reach sectors, improving governance in revenue collection and bolstering accountability would greatly reduce inefficiencies and mobilize up to \$99 billion a year over the next five years.

IMPROVING THE EFFICIENCY OF REVENUE COLLECTION COULD GREATLY INCREASE NON-TAX REVENUE

Non-tax revenue is another untapped source of revenue that could expand fiscal space in a majority of African countries. Sources of non-tax revenue include grants, property rents, fees and other miscellaneous sources. However, political capture is often an impediment to non-tax revenue collection, especially for property rents. Improving governance frameworks and actively monitoring non-tax revenue could increase revenue by as much as 2 per cent of GDP.

LEVERAGING THE USE OF INFORMATION TECHNOLOGY COULD TIGHTEN COMPLIANCE AND LOWER ADMINISTRATIVE COSTS

Tax administration reforms have been among the most successful fiscal reforms in Africa over the last two decades. Setting up semi-autonomous tax authorities, mainly in Anglophone countries, and leveraging the use of information technology have improved compliance, lowered the costs of compliance and tax collection and widened the tax base. The potential gains are substantial. Rwanda increased revenue by 6 per cent of GDP by introducing e-taxation, while in South Africa e-taxation reduced compliance costs by 22.4 per cent and lowered the time to comply with the value-added tax by 21.8 per cent.

BASE EROSION AND PROFIT SHIFTING ARE MAJOR SOURCES OF REVENUE LEAKS

Eliminating base erosion and profit shifting could boost tax revenue in Africa by an estimated 2.7 per cent of GDP. The main avenues of tax evasion and avoidance in the natural resources sector in Africa highlighted in the Report are the use of non-strategic tax incentives, loopholes in double-taxation agreements, difficulties in applying the arm's length principle effectively in regulating intra-company transactions, inclusion of fiscal stability clauses in contracts and a lack of coordination and information sharing among government agencies.

The Report also examines the relationship between fiscal policy and debt sustainability in Africa. It disaggregates external and domestic debt by instrument, creditors and debtors and assesses governments' cash-flow constraints, unsustainable debt levels and factors influencing fiscal sustainability and debt management.

The rise in government debt and in the vulnerability of fiscal policy in Africa has exposed governments on the margins of solvency to debt difficulties, including debt servicing challenges. Rebalancing fiscal and policy frameworks will be important for maintaining stable revenue and spending flows in the economy and sustaining policies for achieving the SDGs.

Finally, the Report highlights major gaps in fiscal data that limit analysis of country experiences and comparisons across countries and regions. It calls on African countries to address these gaps and improve access to data.

KEY POLICY RECOMMENDATIONS

The Report argues that **African countries can increase government revenue by 12–20 per cent of GDP** by adopting a policy framework to strengthen revenue mobilization in six key areas:


- **Fiscal policy options.** Anchoring fiscal policy to national medium-term financing strategies could allow African countries to leverage the full potential of all government revenue—tax and non-tax—for accelerated and sustained growth underpinned by macroeconomic stability.
- To safeguard macroeconomic stability, countries must align fiscal policy with the business cycle, improving revenue mobilization and reducing spending to curb supply-side pressures, while lowering taxes and increasing spending when economic activity slows.
- **Tax policy options.** African governments must widen the tax base by bringing hard to tax sectors into the tax net, including agriculture, the informal economy, the digital economy and the natural resources sector. Countries must reassess tax incentives and drop those that do not serve the intended purpose. Limiting the use of tax incentives in the agricultural and natural resources sectors could stem tax leakages and enhance revenue collection.
 - **Non-tax revenue options.** Investing in better data collection methods and implementation could strengthen monitoring of non-tax revenue collection and non-reporting. Non-tax revenue collection can be enhanced by establishing strong institutions with high levels of expertise, building new infrastructure and establishing effective coordination between central and local governments.
 - **Tax administration options.** Reforming tax administration systems through digitization and

other information technologies could increase revenue mobilization. Countries that have digitized their tax administration have increased compliance rates and saved on compliance costs. The rollout of digital technologies needs to be accompanied by capacity building for policy makers and tax collectors on how to take advantage of data generated through digitization for more efficient assessments.

- **Policy options for the natural resources sector.** African countries should strengthen their oversight of the natural resources sector. They could consider a more equitable and less administratively challenging approach to assessing what share of multinational corporations' profits to tax (for example, based

on the share of sales or other variables), or they could base taxes on variables that are harder to manipulate than corporate income. At the same time, governments need to close loopholes to thwart base erosion and profit shifting.

- **Debt policy options.** The new dynamics of public debt in Africa call for adapting debt sustainability strategies and frameworks to current debt portfolios. That includes improving revenue mobilization to enhance debt servicing and reduce long-term borrowing. The Report calls for better debt management strategies underpinned by increased deepening of domestic capital markets and reliance on local currency-denominated debt instruments.

A decorative graphic consisting of a grid of small, colorful squares in various colors including blue, green, orange, red, yellow, and pink. The squares are arranged in a pattern that is denser at the bottom and fades towards the top, creating a pixelated or mosaic-like effect.

African countries can increase government revenue by 12–20 per cent of GDP by adopting a policy framework to strengthen revenue mobilization in six key areas.

CHAPTER 1

RECENT ECONOMIC AND SOCIAL DEVELOPMENTS



Africa grew by 3.2 per cent in 2018, down slightly from 3.4 per cent in 2017, buoyed by improved global growth that is increasing demand for Africa's exports and by rising commodity prices, higher investment in infrastructure, strong private consumption and favourable weather. Growth is forecast to pick up to 3.4 per cent in 2019. However, Africa needs to triple this growth if countries are to achieve the Sustainable Development Goals (SDGs). Countries need to use new technology to improve productivity and to increase investment to 30–35 per cent of GDP by becoming more business friendly and using fiscal policy to encourage private investment. Africa's growth prospects remain positive in the medium term, despite risks and uncertainties.

In terms of social development, Africa has made notable progress in education, health and other social outcomes, but inclusive growth remains elusive. Africa's social gains could be greater if countries mobilized fiscal revenue in innovative ways and deployed it effectively to finance sustainable development.

GLOBAL ECONOMIC PERFORMANCE AND ITS IMPLICATIONS FOR AFRICA

Global GDP growth rose slightly, from 3.1 per cent in 2017 to 3.2 per cent in 2018, and is projected to remain stable in 2019 (figure 1.1). Strong global growth, driven by investment and trade in developed and emerging market economies and higher commodity prices, is expected to boost demand for African exports, especially from commodity-exporting countries. Clouding the growth picture are US protectionist policies towards China, which could mute medium-term growth, and a modest rise in global commodity prices, which could benefit commodity-exporting countries but exert inflationary pressures on oil-importing countries in Africa.

Rising commodity prices, higher yields on US bonds, escalating trade tensions, and domestic political and policy uncertainty have reduced capital inflows and driven up financing costs, exchange rates and inflationary pressures in some African countries, especially those with weak economic fundamentals. All this has adversely affected African economies.

Growth in emerging and developing economies stabilized during 2015–2017, at around 4.4 per cent. Emerging Asia continued to register robust growth, supported by strong demand in India, while China's growth eased downward, from



Africa's social gains could be greater if countries mobilized fiscal revenues in innovative ways and deployed them effectively to finance sustainable development.

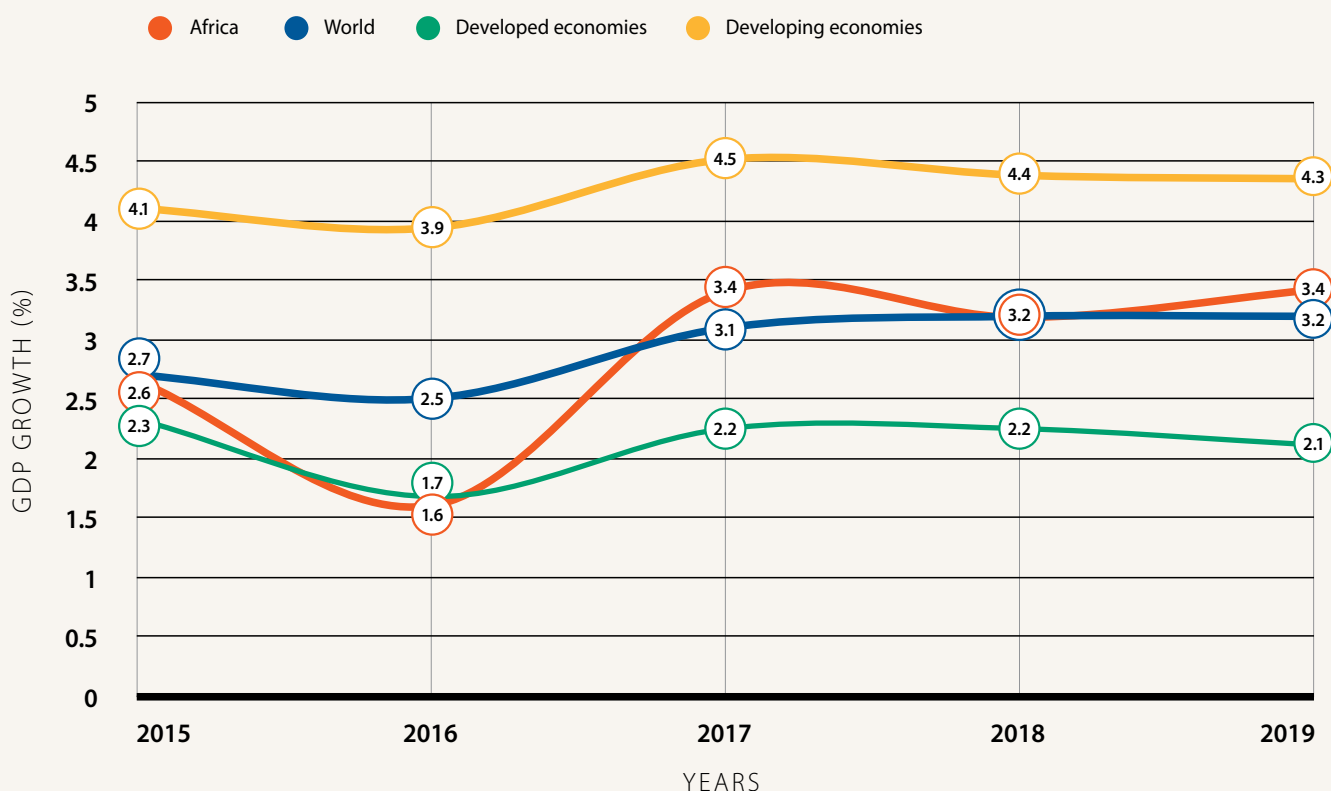
6.9 per cent in 2017 to 6.6 per cent in 2018, as export growth moderated. Growth in global trade declined to 4.3 per cent in 2018, from a six-year high of 4.8 per cent in 2017, due to decelerating global investment as financing conditions tightened. Consequently, capital flows to African and other developing economies are expected to slow. More generally, a projected deceleration in capital spending in China and most advanced economies will see growth in global trade moderate between 2018 and 2019 (EIU, 2018b; IMF, 2018b). On the positive side China's trade is forecast to remain strong, underpinned by an uptick in growth in emerging economies (including Argentina, Brazil and the Russian Federation), though at a subdued pace.

Higher energy prices fuelled rising inflation in advanced, emerging and some developing

economies over 2018, despite declining domestic demand in China (IMF, 2018b). With increasing inflation and strong job creation, the US Federal Reserve raised the policy interest rate by 25 basis points in June 2018, while the European Central Bank maintained its policy rate. Most emerging market economies have raised their policy rates to curb inflationary and exchange rate pressures, which were coupled with capital flow reversals in some countries (IMF, 2018b).

At the global level, countries tightened their monetary policy stance in response to a stronger US dollar after February 2018, while the euro, Japanese yen and British pound remained unchanged. Currencies depreciated sharply in some emerging market economies (such as Argentina, Brazil, South Africa and Turkey), reflecting signs of financial stress in some countries and growing trade tensions

FIGURE 1.1. GLOBAL ECONOMIC GROWTH, 2015–2019



Note: Data are estimated for 2018 and projected for 2019.

Source: Based on data from UNDESA (2019).

and capital flight. Argentina, India, Indonesia, the Russian Federation and Turkey intervened in foreign exchange markets or raised interest rates to contain exchange rate and inflation rate pressures.

As the dollar's supremacy as a means of exchange and a store of value remains unchallenged, the rising dollar would lead to an equal rise in the local currency cost of servicing dollar-denominated debt by African countries. Hence, as the dollar rises, so does the cost of servicing those debts. Currency depreciation due to the strengthening of the dollar, especially in emerging market economies, would lead to a decline in Africa's exports as imports become more expensive in Africa's trading

partners, especially those in the euro zone. The rising interest rates would also lead to a reversal of capital flows, as many developing countries rely heavily on capital inflows to fund their fiscal or current account deficits.

An expected decline in capital flows presents challenges for African economies, as the cost of debt and debt service are expected to rise. African countries need to enhance their resilience through an appropriate mix of fiscal, monetary and structural policies that reduce vulnerability to tightening global financial conditions, currency fluctuations and capital outflows. And they need to closely monitor the negative effects of external conditions on public and private sector balance sheets and domestic inflation.

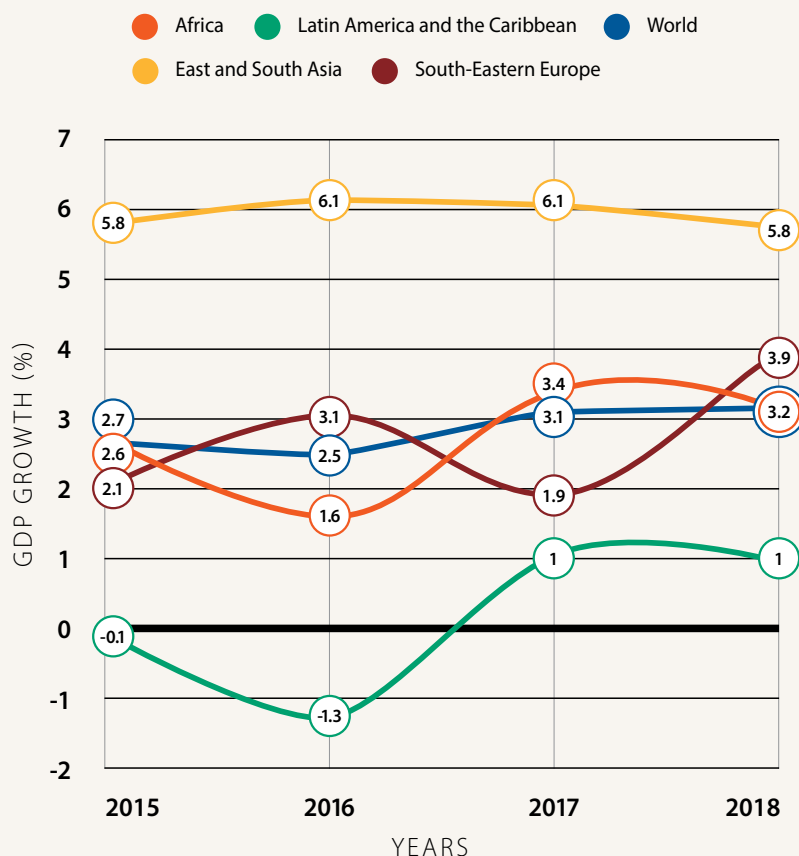
RECENT ECONOMIC DEVELOPMENTS IN AFRICA

ECONOMIC GROWTH

Africa's economic growth slowed slightly, from 3.4 per cent in 2017 to 3.2 per cent in 2018 (figure 1.2). Growth was driven by external factors, including strengthening global demand and a moderate increase in commodity prices. The domestic drivers include sustained investment in infrastructure and strong private consumption (figure 1.3), along with higher oil production (from new fields) and favourable weather.

Some of Africa's largest economies—Angola, Nigeria and South Africa—are rebounding, due to a rise in private consumption, but growth remains low. Growth in non-resource-rich countries such as Côte d'Ivoire, Ethiopia, Kenya and Senegal remains strong, driven by heavy public investments in infrastructure.

FIGURE 1.2. ECONOMIC GROWTH IN AFRICA AND DEVELOPING ECONOMIES, 2015–2018



Note: Data are estimated for 2018 and projected for 2019.

Source: Based on data from UNDESA (2019).

Africa's growth rate of 3.2 per cent in 2018 is not sufficient to eradicate poverty.

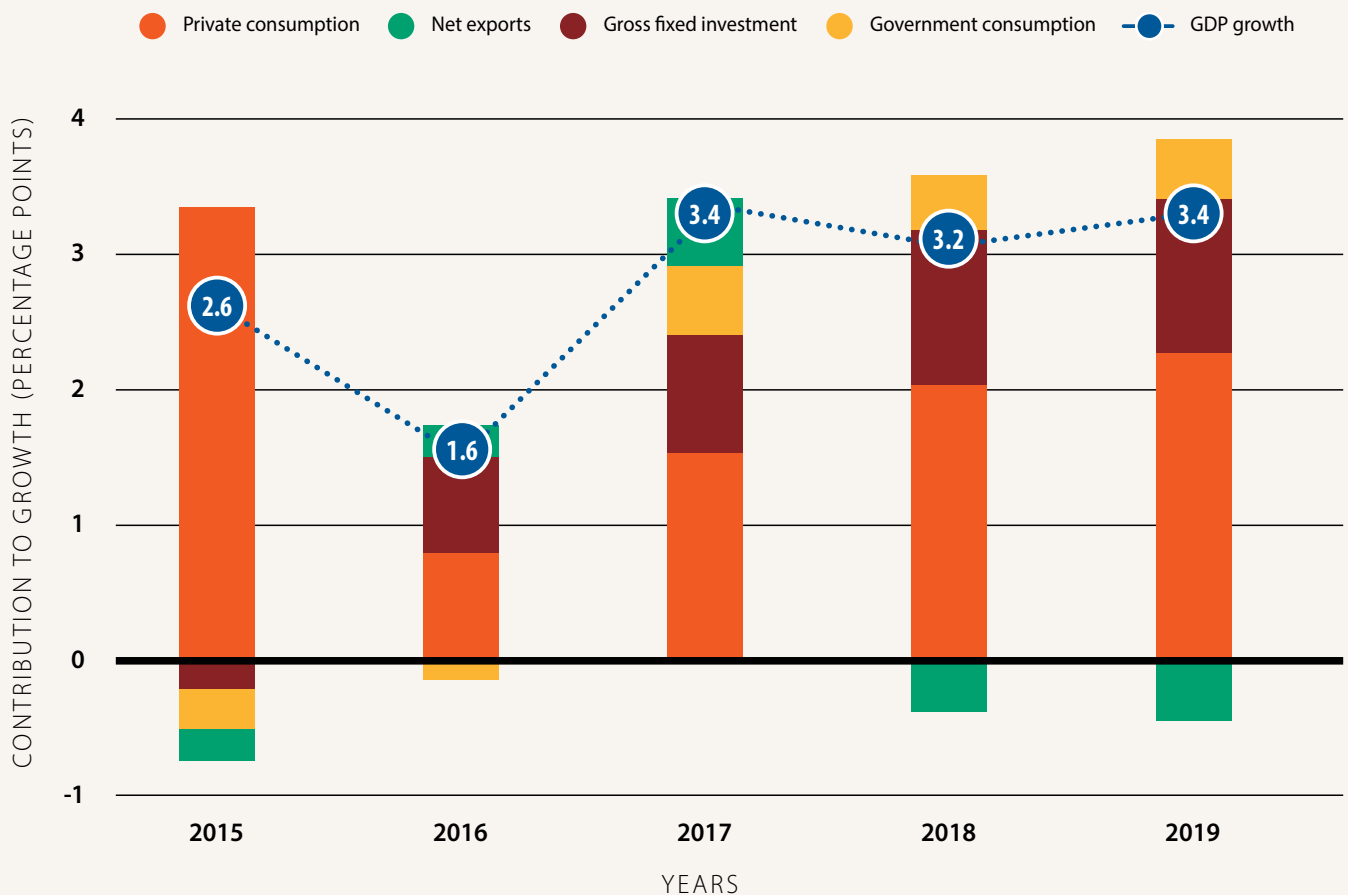
However, Africa's growth rate of 3.2 per cent is not sufficient to eradicate poverty or achieve the other SDGs by 2030. To accelerate growth to double digits by 2030, Africa needs to boost investment from its current 25 per cent of GDP—much lower than the 32 per cent in East Asia and the Pacific—to 30–35 per cent and substantially improve productivity (World Bank, 2018b). Productivity growth in Africa slipped from an average of 2.4 per cent over 2000–2008 to 0.3 per cent over 2009–2018,

well below the global average of 1.9 per cent over 2011–2017. African countries need to implement reforms that build resilience and raise potential growth and inclusiveness.

STEADY GROWTH ACROSS SUBREGIONS

All subregions recorded growth in 2018. East Africa remains the fastest growing subregion in Africa, with growth rising from 6.1 per cent in

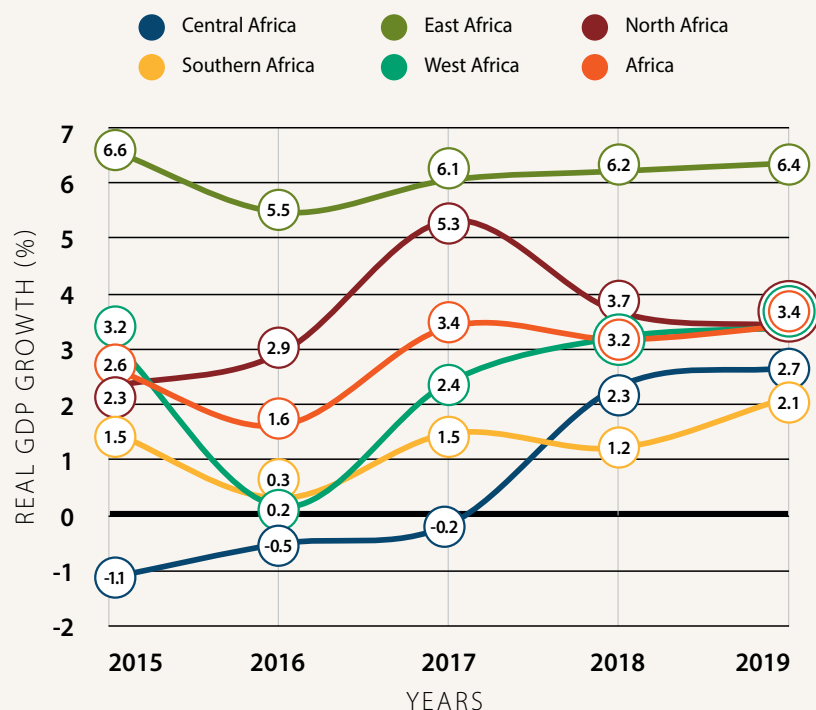
FIGURE 1.3. COMPONENTS OF ECONOMIC GROWTH IN AFRICA, 2015–2019



Note: Data are estimated for 2018 and projected for 2019.

Source: Based on data from EIU (2018a) and UNDESA (2019).

FIGURE 1.4. ECONOMIC GROWTH IN AFRICA,
BY REGIONAL GROUPING, 2015-2019



Note: Data are estimated for 2018 and projected for 2019.

Source: Based on data from UNDESA (2019).

2017 to 6.2 per cent in 2018, driven by strong public spending on infrastructure and rising domestic demand (figure 1.4). Growth in the subregion reflected strong growth in Djibouti, Ethiopia, Kenya, Rwanda, Tanzania and Uganda, with only Burundi growing at below 3.0 per cent. While agriculture remains the dominant economic activity in East Africa and the key driver of growth, industry and services have been expanding in Ethiopia, Kenya, Rwanda and Tanzania, and the mining sector has been strong in Democratic Republic of the Congo, Madagascar, Rwanda and Uganda. Rising government spending on infrastructure and the fast-growing construction, real estate and retail sectors in Ethiopia and Kenya will continue to boost growth in the subregion. At the same time oil and gas explorations, favourable weather and enhanced regional integration through the regional economic communities and the African Continental Free Trade Area (AfCFTA)

offer huge potential for growth across East Africa.

Growth in West Africa climbed from 2.4 per cent in 2017 to 3.2 per cent in 2018, reflecting higher growth in all countries in the subregion except Burkina Faso, Guinea and Guinea-Bissau. Ghana and Nigeria benefited from recovering oil prices and higher oil production, while services sector activities grew in all countries except Liberia and Sierra Leone. Benin, Côte d'Ivoire, Ghana, Niger and Senegal benefited from buoyant markets for mineral and agricultural commodities and higher private consumption and public investment.

Central Africa recovered from an economic slump of -0.2 per cent in 2017 to grow by 2.3 per cent in 2018. Growth is projected to reach 2.7 per cent in 2019. While the key drivers of this positive trend vary across countries, they include recovering oil prices;

new oil and gas production (Cameroon, Congo and Equatorial Guinea); strong performance in agribusiness, manufacturing and services (Cameroon, Congo and Gabon); tourism and construction (São Tomé and Príncipe); resumption of diamond exports (Central African Republic); and spillovers of Nigeria's recovery into Cameroon and Chad. However, inadequate economic diversification (Congo, Gabon and Equatorial Guinea) and adverse weather remain key risks that could derail economic growth in the subregion.

Growth in North Africa fell from 5.3 per cent in 2017 to 3.7 per cent in 2018, underpinned mainly by growth in Libya (11.0 per cent), Egypt (5.8 per cent) and Morocco (3.5 per cent). The decline was due to lower private consumption as a result of rising inflation in some countries, including Algeria, Egypt and Sudan, and political instability in Libya.

Growth improved in Tunisia, from 1.9 per cent in 2017 to 2.4 per cent in 2018, due to a resurgence in tourism, manufacturing and industry.

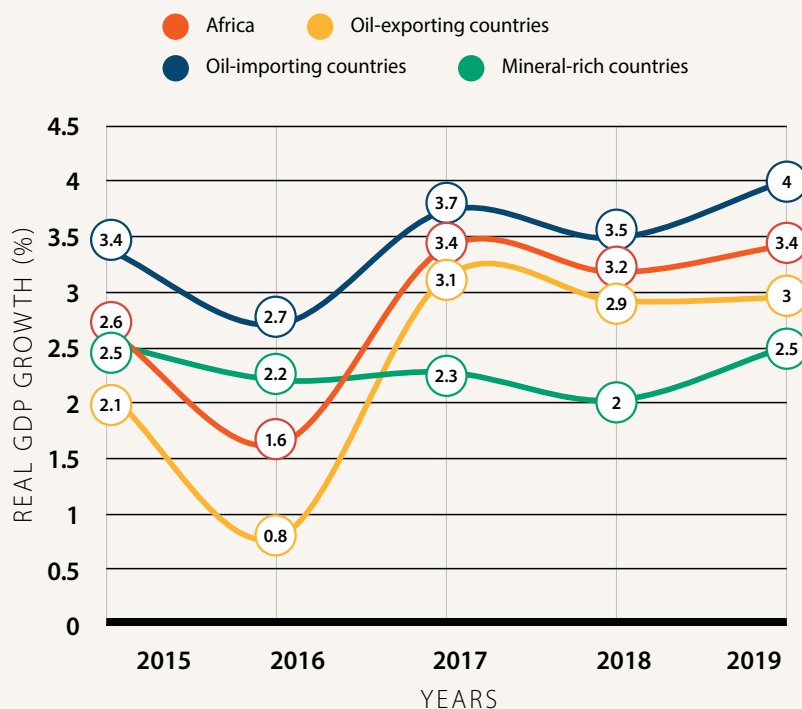
Growth also slowed in Southern Africa, dipping from an already low 1.5 per cent in 2017 to 1.2 per cent in 2018. The economy was supported by a moderate increase in commodity prices (copper and diamonds) and positive spillovers of an improved energy supply. In 2018 Southern Africa's performance was driven by growth in Botswana (4.4 per cent), Malawi (4.4 per cent), Zambia (4.1 per cent) and Mauritius (3.7 per cent). In South Africa growth was driven by an uptick in retail trade, manufacturing and mining. Angola, the only oil producer, saw the growth rate increase to 1.0 per cent in 2018 from 0.7 per cent in 2017. After the economy suffered a prolonged recession in 2016–2017 due to the slump in world oil prices, which led to a slowdown in the extractive and manufacturing industries. The economy picked up marginally in 2018 as global commodity prices began to recover. The Angolan government introduced a macroeconomic stabilization programme to improve the business environment through deficit reduction, debt consolidation and greater exchange rate flexibility. Growth in the subregion is projected to reach 2.1 per cent in 2019, underpinned by an expected rise in global prices and increased agricultural output due to improving weather conditions (UNDESA, 2018b).

Per capita growth rates in all subregions continued to trail population growth rates since the commodity price slump in mid-2014. Although in 2017 the population growth rate in North Africa (1.8 per cent) was lower than the per capita economic growth rate (4.8 per cent), once Libya, with its 70 per cent growth rate in 2017, is excluded, per capita GDP growth in North Africa falls below the population growth rate. Growth in oil-importing countries

All subregions recorded growth in 2018. East Africa remains the fastest growing subregion in Africa.

declined from 3.7 per cent in 2017 to 3.5 per cent in 2018 (figure 1.5), supported by agricultural production and services sector activities, as well as by strong private consumption and public investment. Most oil-exporting countries saw an uptick in growth, helped by higher prices and expanded production.

FIGURE 1.5. ECONOMIC GROWTH IN AFRICA, BY ECONOMIC GROUPING, 2015–2019



Note: Data are estimated for 2018 and projected for 2019.

Source: Based on data from UNDESA (2019) and EIU (2018a).

TIGHT GLOBAL MONETARY POLICY KEPT INFLATION IN CHECK

Inflation remained on a downward trend, declining from a weighted average of 14.4 per cent in 2017 to 11.1 per cent in 2018, reflecting mainly stable exchange rates and falling food prices, which countered the inflationary pressures of rising global oil prices.

Inflation dropped in oil-exporting countries, from an average of 20.7 per cent in 2017 to 15.4 per cent in 2018, and declined moderately in oil-importing countries, from 5.7 per cent to 5.2 per cent. However, inflation rose in some countries for reasons ranging from higher oil prices in Egypt to currency devaluation in Ethiopia and subsidy elimination in Sudan. However, West Africa is the only subregion where inflation rose substantially in 2018, due mainly to inflationary pressures in Nigeria (16.2 per cent), Sierra Leone (11.7 per cent), Liberia (11.2 per cent), Guinea

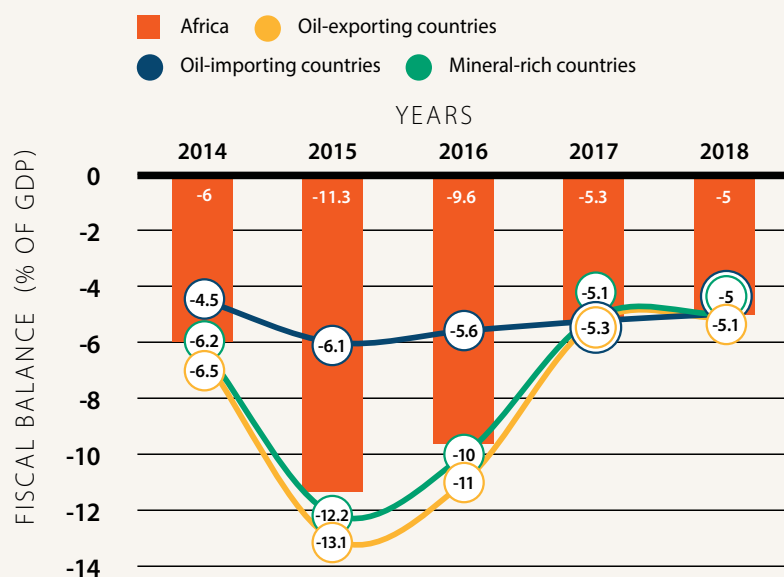
(9.2 per cent) and Ghana (8.3 per cent). Inflation was driven by rising global demand, poor harvests in the Sahel region leading to higher food prices, and higher import prices leading to increased production costs.

A NARROWING FISCAL DEFICIT WITH RISING EXTERNAL DEBT

Africa's fiscal deficit narrowed from 5.3 per cent of GDP in 2017 to 5.0 per cent in 2018 (figure 1.6). This improvement was supported by fiscal consolidation efforts (such as reductions in subsidies) in many countries, recovering oil prices and increased oil production (Angola, Chad, Ghana and Nigeria), widening tax bases and automation of tax administration (Congo, Lesotho, Malawi and Nigeria). Fiscal deficits narrowed in all country groups—oil importing, oil exporting and mineral rich. Africa's fiscal deficit is projected to remain stable at 5.0 per cent of GDP in 2019, supported by improving global economic conditions, particularly among commodity exporters. However, widespread commitments to investment in infrastructure will make it difficult to narrow fiscal deficits.

Even as Africa's fiscal deficit narrowed, debt as a share of GDP (weighted) increased marginally from 2017 to 2018, from 48.4 per cent to 50.5 per cent for domestic debt and from 35.5 per cent to 37.6 per cent for external debt¹. Both types of debt stabilized significantly in oil-importing countries but remain high in oil-importing and mineral-rich countries. In 2018, external debt (weighted) stood at 44.8 per cent of GDP in oil-importing countries and 44.3 per cent in mineral-rich countries, while public debt was 63.0 per cent of GDP in oil-importing countries and 47.5 per cent in mineral-rich countries.

FIGURE 1.6. AFRICA'S FISCAL BALANCE,
BY ECONOMIC GROUPING, 2014-2018

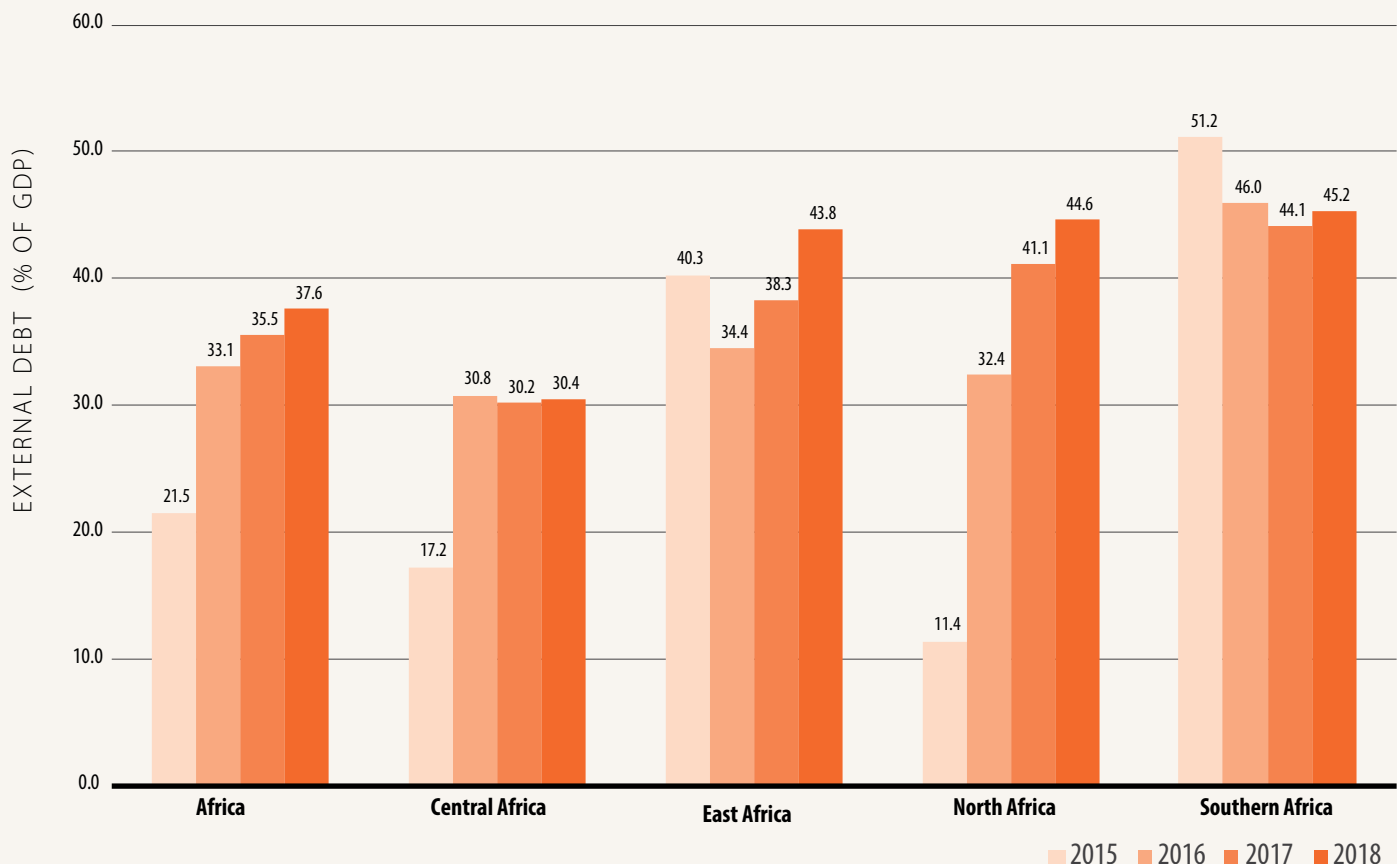


Note: Data are estimated for 2018
Source: Based on data from EIU (2018a).

¹ ECA calculations based on data from EIU (2018a) and UNDESA (2019).

Africa's fiscal deficit is projected to remain stable at 5.0 per cent of GDP in 2019, supported by improving global economic conditions, particularly among commodity exporters.

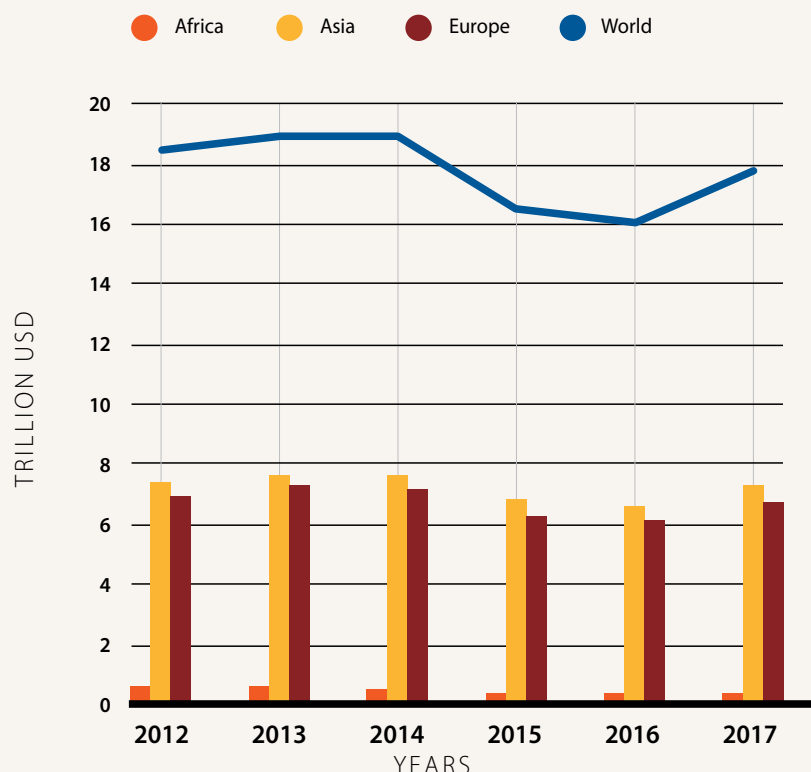
FIGURE 1.7. AFRICA'S EXTERNAL DEBT POSITION, BY SUBREGION AND ECONOMIC GROUPING, 2015-2018



Note: Data are estimated for 2018 and projected for 2019

Source: Based on data from EIU (2018a).

FIGURE 1.8. AFRICA'S MERCHANDISE EXPORTS, 2012-2017



Source: Based on data from UNCTAD (2018b).

Most African governments have taken steps to strengthen their debt management procedures. However, this has not been very effective, as debt remains high in Angola, Mozambique and Zambia. High debt levels, coupled with monetary tightening in most developed economies and the associated rise in interest rates (making external debt more expensive), raise doubts about the sustainability of debt dynamics in some countries (UNDESA, 2018a). More than a quarter of African countries had a debt-to-GDP ratio of more than 50 per cent in 2018, and some (Mauritania, Mauritius, Seychelles and Sudan) had a ratio of more than 100 per cent. Debt management needs attention, particularly with respect to conditions and sources of financing.

CURRENT ACCOUNT DEFICITS NARROWED AS EXPORTS PICKED UP

Current account deficits narrowed from 3.9 per cent of GDP in 2017 to 3.1 per cent in 2018, underpinned by rising commodity prices. However, current account deficits widened in some countries, including Seychelles (to 25.5 per cent of GDP), Mauritania (24.3 per cent), Mozambique (21.7 per cent) and Niger (15.3 per cent), due to increased demand for capital imports, high fuel prices in oil-importing countries, high food imports and higher interest payments on government debt.

Merchandise exports picked up in 2017 after four years of slowdown (figure 1.8). World exports increased by 10.6 per cent, the largest export growth spurt since 2012. All regions expanded their exports in 2017, with Africa registering the largest increase (18.3 per cent), followed distantly by Asia (11.3 per

cent) and Europe (10.3 per cent). Africa's share in world exports rose from 2.2 per cent in 2016 to 2.4 per cent in 2017.

Africa's merchandise imports also increased in 2017, following two years of lower performance, rising from \$495 billion in 2016 to \$534 billion in 2017, a nearly 8 per cent increase. As exports increased more than imports, the trade deficit was reduced from \$142.7 billion in 2016 to \$116.9 billion in 2017.

AFRICA EXPORTS MAINLY PRIMARY COMMODITIES AND IMPORTS MANUFACTURES

Primary commodities and raw materials (fuels, ores and metals, and agricultural raw materials) constituted the largest share of Africa's merchandise exports in 2017. Fuels alone

accounted for 39.4 per cent of the value of Africa's exports, a 4.6 percentage point increase over 2016. Manufactures grew little as a share of Africa's exports, from 24.3 per cent in 1996 to 26.2 per cent in 2016, with a slight decrease to 23.9 per cent in 2017 (see figure 1.9a for the breakdowns for intra-African trade and for trade with the rest of the world in 2015-2017).

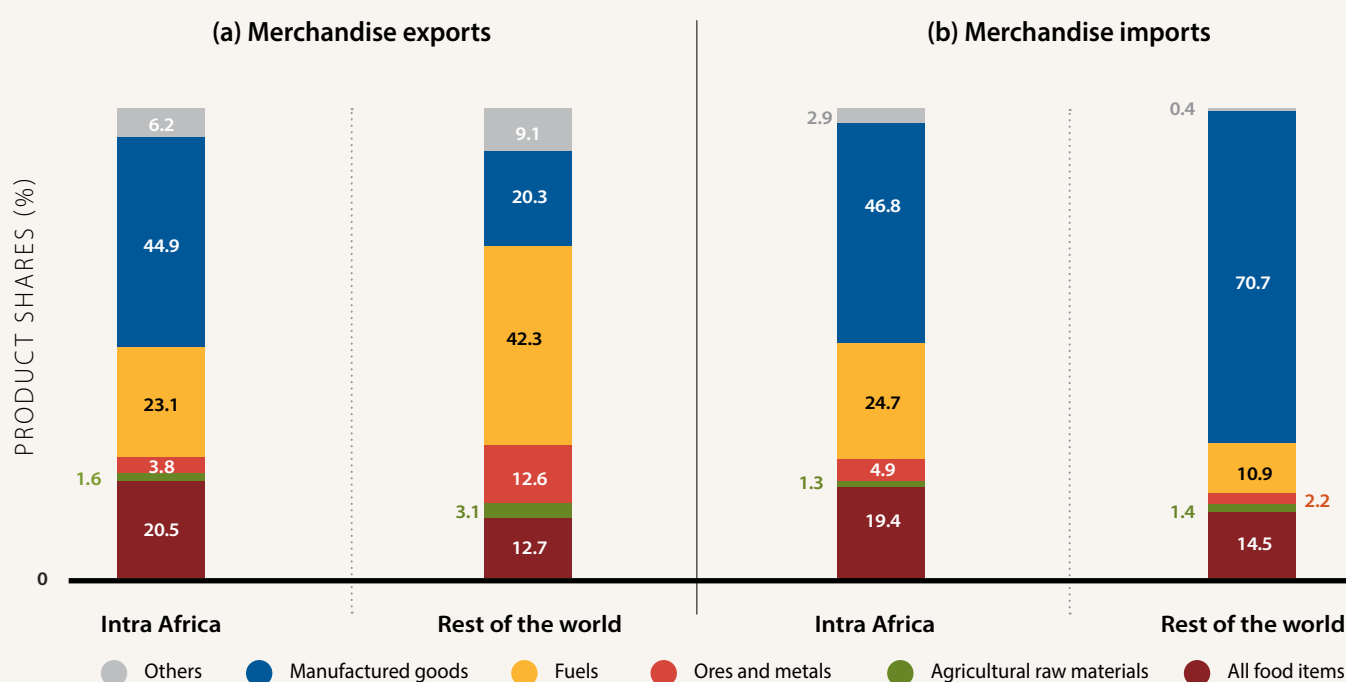
South Africa was Africa's top exporter to the rest of the world over 2015–2017 (18.2 per cent share), followed by Nigeria (12.0 per cent) and Algeria (10.0 per cent). Côte d'Ivoire was the top exporter of food items, accounting for 14.3 per cent of African food exports to the rest of the world, followed by South Africa (12.5 per cent) and Morocco (11.0 per cent). South Africa ranked first in Africa's agricultural exports to the rest of the world (18.1 per cent share), followed by Côte d'Ivoire (10.1 per cent) and Cameroon (7.7 per cent). South Africa (45.7 per cent), Zambia

(12.1 per cent) and Democratic Republic of the Congo (10.7 per cent) dominated exports of ores and metals to the rest of the world, while Nigeria (26.1 per cent), Algeria (22.9 per cent) and Angola (22.3 per cent) were the main exporters of fuels. South Africa also dominated machinery and transport equipment² exports (42.7 per cent share), followed by Morocco (24.6 per cent) and Tunisia (18.3 per cent).

But Africa's merchandise imports reveal a different picture. Manufactured goods constituted 70.7 per cent of merchandise imports from the rest of the world in 2017 (figure 1.9b, reflecting

² Machinery and transport equipment includes power-generating machinery and equipment, specialized machinery, metal working machinery, other industrial machinery and parts, road vehicles, and other transport equipment; electronic machinery excluding their parts and components (SITC 751 and 752), television receivers, radio-broadcast receivers and sound recorders or reproducers (SITC 761, 762 and 763); and household equipment (SITC 775).

FIGURE 1.9. AFRICA'S MERCHANDISE EXPORTS AND IMPORTS, 2015–2017 AVERAGE



Source: Based on data from UNCTAD (2018b).

Three-quarters of intra-African exports were concentrated in just 13 countries, with South Africa alone capturing about 45 per cent of that share.

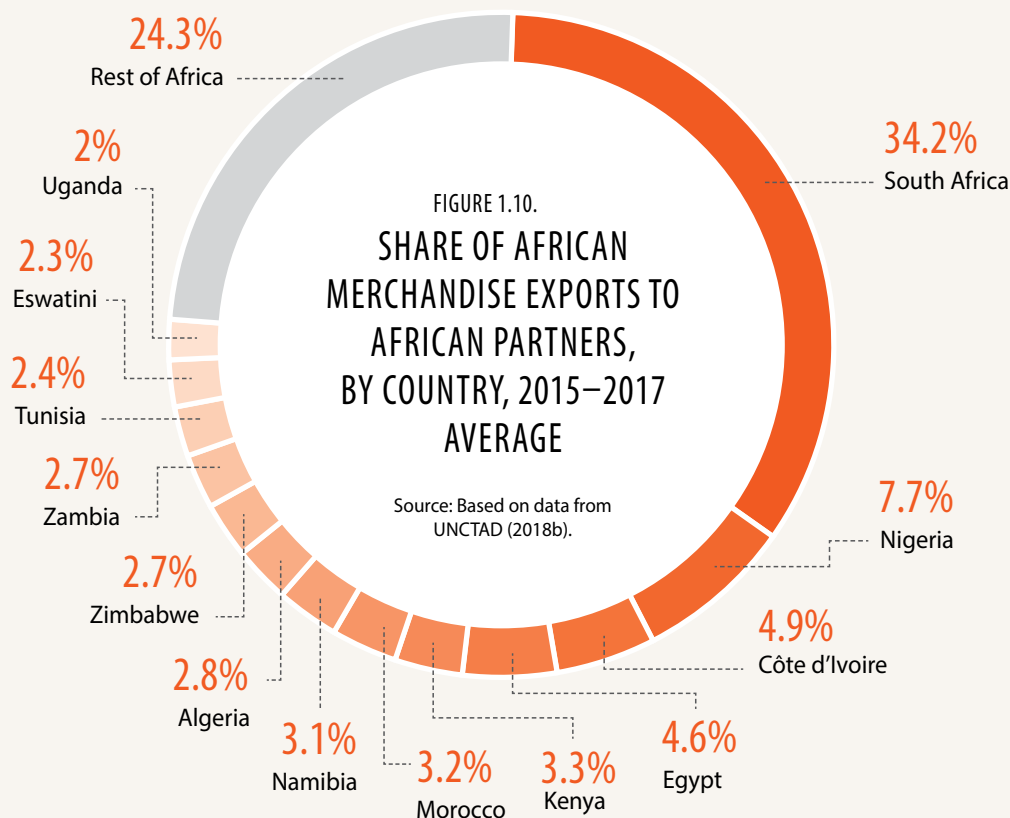
Africa's comparatively low technology base and productivity and its continuing dependence on external partners to satisfy its industrial needs.

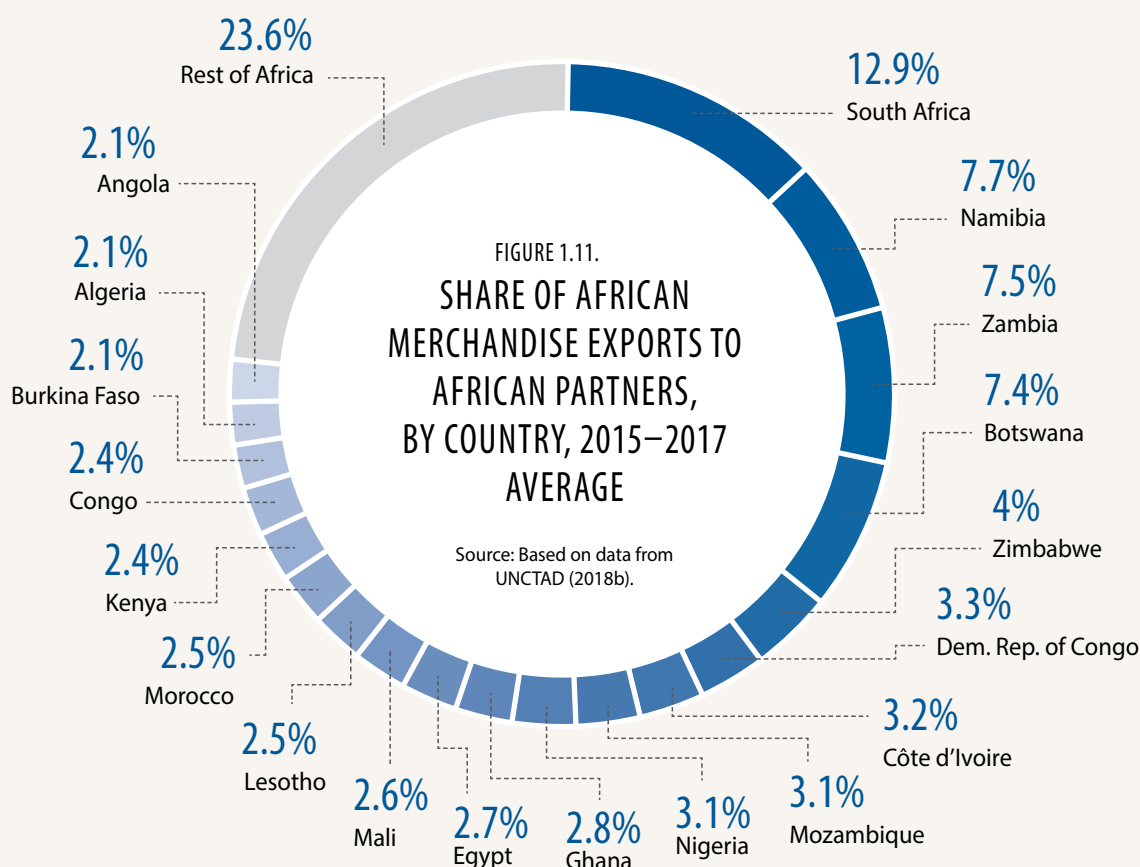
Egypt accounted for the largest share of African food imports from outside the continent over 2015–2017 (17.6 per cent), followed by Algeria (14.4 per cent) and South Africa (8.3 per cent). Egypt also accounted for the largest share of African imports of ores and metals (19.8 per cent), followed by South Africa (18.0 per cent) and Morocco (16.6 per cent), while Egypt (16.5 per cent), South

Africa (15.4 per cent) and Nigeria (14.7 per cent) were the top African importers of fuels. South Africa was the biggest importer of machinery and transport equipment (18.6 per cent share), followed by Algeria (11.9 per cent) and Egypt (10.3 per cent).

INTRA-AFRICAN TRADE IS MORE DIVERSIFIED AND INDUSTRIALIZED

Three-quarters of intra-African exports were concentrated in just 13 countries, with South Africa alone capturing about 45 per cent of that share (figure 1.10). South Africa topped intra-African exports in three of the five main sectors over 2015–2017: machinery and transport equipment (60.2 per cent), food items (28.9 per cent), and ores and metals (25.4 per cent). Eswatini leads in raw agricultural materials with an average of 20.1 per cent of that sector's exports, and Nigeria leads in fuels with 30.7 per cent.





However, 19 African countries accounted for three-quarters of African imports from African partners (figure 1.11). South Africa again had the largest share, though smaller than for exports. Intra-African trade is composed mainly of machinery and transport equipment.

AFRICA'S TRADE IN SERVICES PICKS UP

Africa's exports of services increased from \$95.7 billion in 2016 to \$109.1 billion in 2017, driven by travel (44.4 per cent of Africa's services exports), transport (28.3 per cent) and other business services (14.4 per cent). Leveraging expertise on the continent by creating more value chains in modern services sector could maximize benefits to businesses. Modern services, unlike traditional services, have been proven to have a significant impact on developed and developing countries' productivity.

ESTABLISHMENT OF THE AFRICAN CONTINENTAL FREE TRADE AREA AND ITS IMPACT ON TARIFF REVENUE

The characteristics of Africa's trade and the current uncertain global context make deepening regional integration an imperative for Africa. The AfCFTA has the potential to contribute to growth and structural transformation in Africa.³ In particular, all countries would benefit from trade expansion following removal of tariff and non-tariff barriers within Africa, and the least developed countries would gain more through expansion of industrial exports (ECA, 2018).

³ Nearly three years after the start of negotiations, 44 African countries signed the AfCFTA on 21 March 2018 and 8 more signed it by March 2019, bringing the total to 52 AU member States. Twenty-two countries must ratify the agreement for it to enter into force and by 5 March 2019, 19 countries did so and 15 of them have already deposited their ratification instruments with the AU.

The AfCFTA is expected to have a moderate and gradual effect on revenue from tariffs on intra-African trade for several reasons (ECA, 2018).⁴ As of March 2019, the particular products to be excluded from liberalization under the AfCFTA have yet to be determined by each country.⁵ Nevertheless, ECA calculations, using a number of informed scenarios to approximate the implications of the AfCFTA for tariff revenue, forecast that reducing and removing tariffs on African trade flows would result in a 6.5–9.9 per cent decrease in tariff revenue for Africa in the long run.

While tax collected on African trade flows will fall, the overall effect of the AfCFTA on total government revenue may be more balanced, especially over the medium term, because import duties are only a small component of government revenue, accounting on average for only 15 per cent of total tax revenue in Africa (ATAF, 2017). This means that reductions to tariff revenue, which are expected to be limited, will affect only a small share of tax generation for most countries. While the AfCFTA will reduce tariff revenue, it is expected to stimulate GDP growth by as much as 1–6 per cent, which would increase the broader tax base and boost revenue collection from other sources (UNCTAD, 2017). Moreover, the

sectors that are expected to gain from the AfCFTA, such as manufacturing and processed agriculture (and to some extent services), are those that tend to have a larger multiplier effect, contributing to sustainable growth and fiscal sustainability.

The overall effect of the AfCFTA is estimated by ECA to be a slight increase in the economic welfare of Africa due largely to the expansion of intra-African exports.

FOREIGN INVESTMENT FLOWS INTO AFRICA CONTINUE TO DECLINE

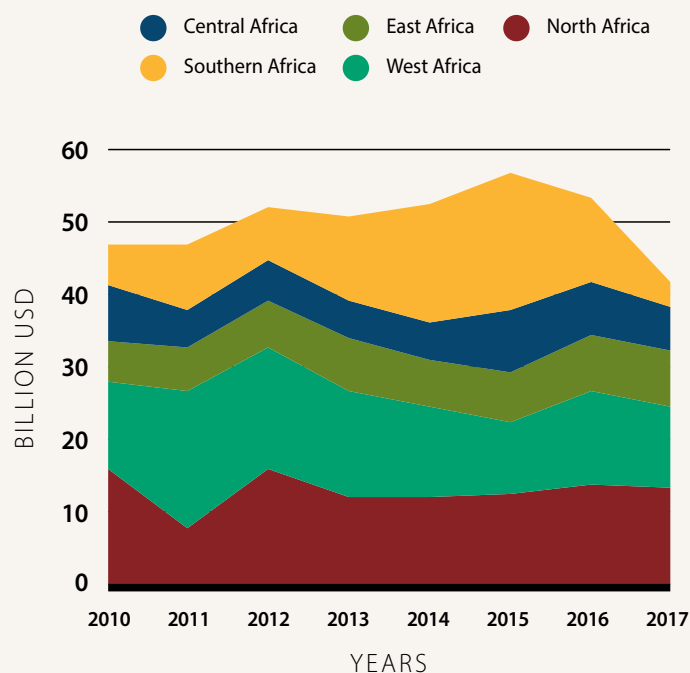
Mirroring global trends, foreign direct investment (FDI) inflows to Africa fell by 21.5 per cent in 2017, to \$41.8 billion (figure 1.12), as global flows declined by 23.4 per cent to \$1.43 trillion.⁶ FDI flows into

⁶ FDI data collected by the United Nations Conference on Trade and Development are periodically updated and revised and therefore may not be consistent over time.

⁴ In the short term these effects are estimated to be minimal for several reasons. First, intra-African imports currently account for only 14 per cent of total imports in Africa, and existing tariffs will be retained on the remaining 86 per cent of imports from non-African countries. Second, 56 per cent of these intra-African imports occur through pre-existing regional economic community free trade areas, in which most trade is already fully liberalized. Third, countries will be allowed to exclude a certain amount of sensitive tariff lines from liberalization. Finally, tariff reductions under the AfCFTA are to be phased in over 5 years for developing countries and 10 years for least developed countries. There is an even longer phase-in period for “sensitive” products of 10 years for developing countries and 13 years for least developed countries.

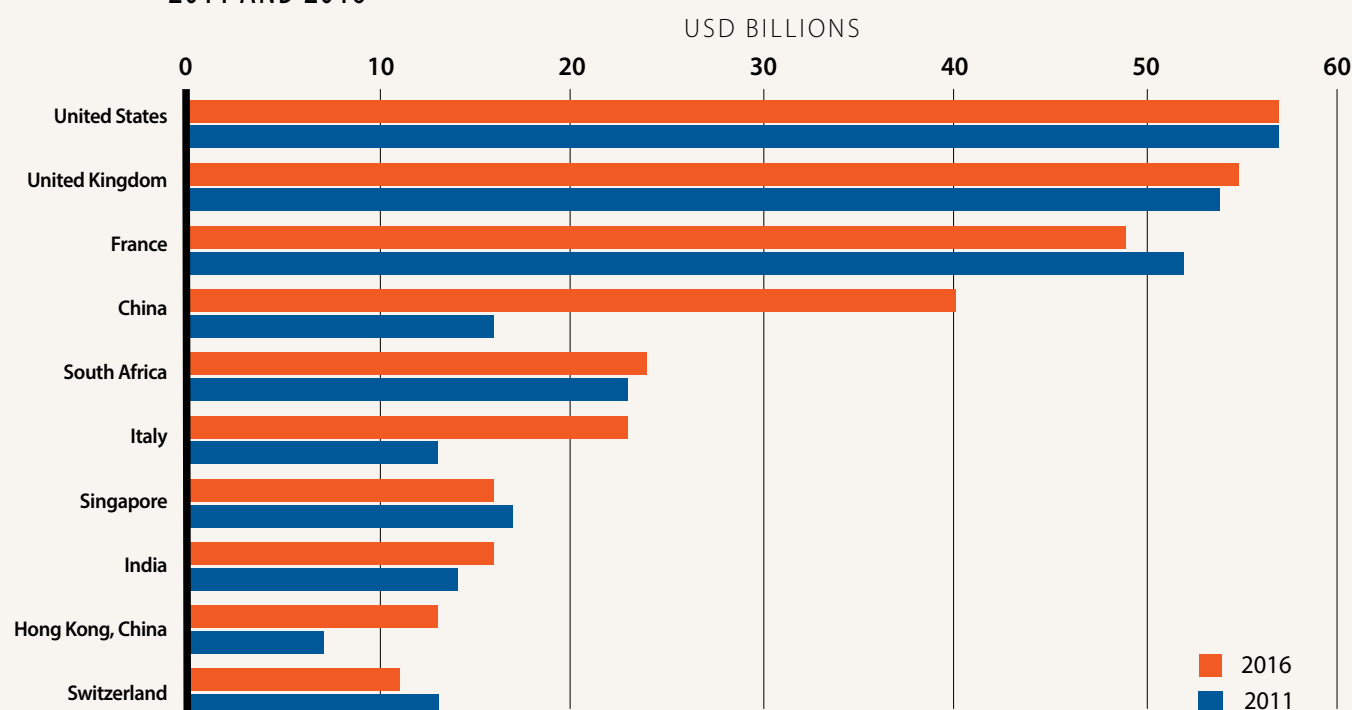
⁵ These products will be identified under Annex 1 Schedules of Concessions of the AfCFTA Agreement, which, at the time of writing, are expected to be concluded by July 2019.

FIGURE 1.12. INFLOWS OF FOREIGN DIRECT INVESTMENT INTO AFRICA, 2010-2017



Source: Based on data from UNCTAD (2018c).

FIGURE 1.13. TOP 10 ECONOMIES INVESTING IN AFRICA, BY STOCKS OF FOREIGN DIRECT INVESTMENT, 2011 AND 2016



Source: Based on data from UNCTAD (2018c).

**Mirroring global trends,
foreign direct investment (FDI) inflows to Africa
fell by 21.5 per cent in 2017, to \$41.8 billion.**

developing countries stagnated in 2017, but flows into Africa are projected to strengthen by 20 per cent in 2018, to \$50 billion, due mostly to a recovery in commodity prices, investments in infrastructure projects and accelerating regional integration efforts (UNCTAD, 2018a). North Africa and West Africa were the most sought after in 2017, registering \$13.3 billion and \$11.3 billion in FDI inflows, respectively, mainly targeting the technology, automotive, textiles and mining sectors.

FDI outflows from Africa to the rest of the world rose by 8 per cent, to \$12.1 billion in 2016, with

South Africa (\$7.4 billion) leading the investment outflows, followed by Nigeria (\$1.3 billion) and Morocco (\$0.96 billion). The United States remains the top country in terms of investing in Africa, although Chinese companies more than doubled their investments on the continent over 2011–2016, increasing by \$24 billion (figure 1.13).

GREENFIELD INVESTMENTS IN AFRICA DECLINED

The value of newly announced greenfield projects in Africa shrank 10 per cent in 2017, falling to

Africa's real GDP growth is projected to increase marginally, from 3.2 per cent in 2018 to 3.4 per cent in 2019.

\$85 billion. The value of projects in the primary and manufacturing sectors declined, while that in the services sector increased by \$5 billion, to \$64 billion, giving services a three-quarters share in greenfield projects. Greenfield projects tend to have a larger impact on economic development than do mergers and acquisitions (Neto, Brandão and Cerqueira, 2010).

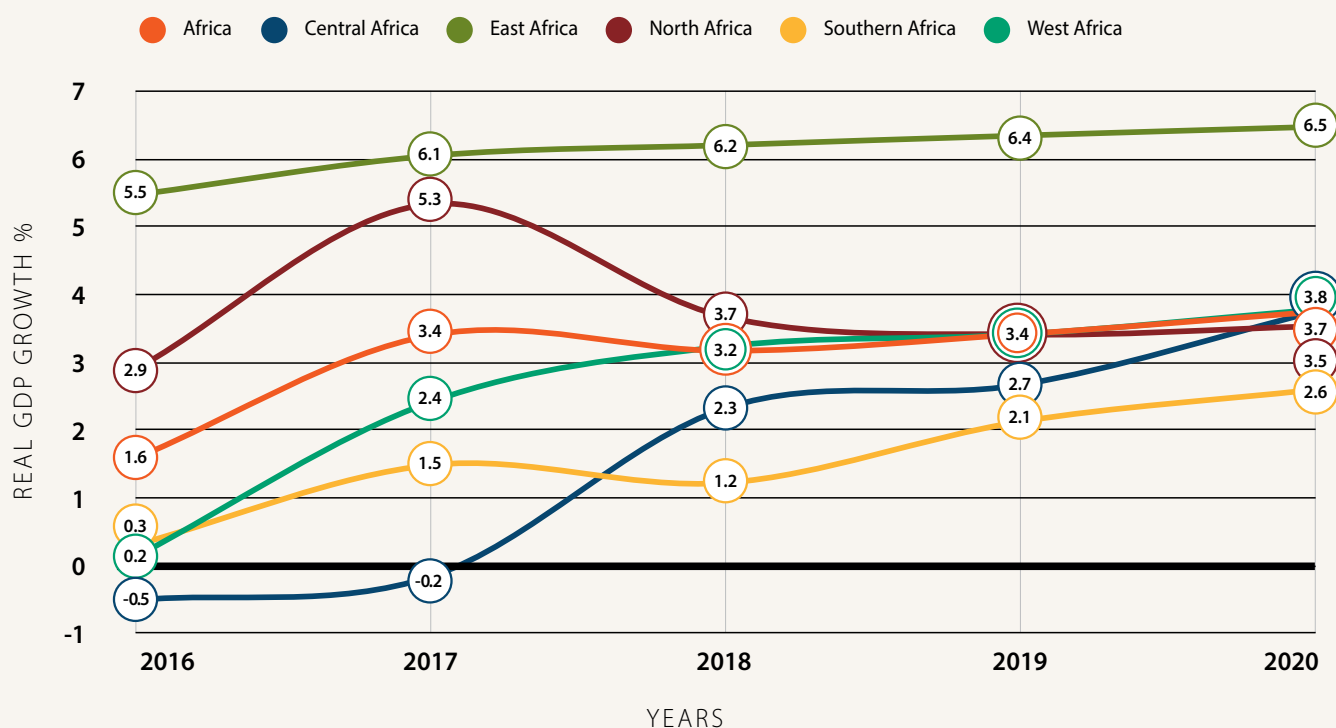
Net sales in cross-border mergers and acquisitions in Africa shrank by 64 per cent,

to \$3.5 billion. Driven by US purchases, the largest share of the value of transactions was in the services sector. Net purchases by African companies declined by 73 per cent, to \$2 billion, \$0.8 billion of which was in the services sector.

MEDIUM-TERM GROWTH FORECASTS AND PROSPECTS

Africa's real GDP growth is projected to increase marginally, from 3.2 per cent in 2018 to 3.4 per cent in 2019, before rising to 3.7 per cent in 2020. These forecasts are revised upwards from last year's to reflect rising private consumption, rising and sustained public investment, higher commodity prices, ongoing oil exploration and production and expected favourable weather. All subregions are projected to post real GDP growth in both 2019 and 2020 (figure 1.14).

FIGURE 1.14. AFRICA'S GROWTH AND GROWTH PROSPECTS, BY SUBREGION, 2016-2020



Note: Data are estimated for 2018 and projected for 2019 and 2020.
Source: Based on data from UNDESA (2019).

GDP growth is projected to be highest in East Africa, rising from 6.2 per cent in 2018 to 6.4 per cent in 2019 before reaching 6.5 per cent in 2020. Growth is likely to be boosted by increased private investment; growth in industry and services (especially in Ethiopia, Kenya, Rwanda and Tanzania); higher public investments in infrastructure; stronger private consumption; oil and gas explorations; more inflows of foreign direct investment; and larger diaspora remittances.

West Africa's growth is projected to be moderate in 2019, at 3.4 per cent, before rising to 3.8 per cent in 2020, lifted by good economic performance in Ghana and Nigeria. In general, growth in the subregion is expected to continue to benefit from fairly high oil prices and increases in oil production, expanding services sectors across the subregion, rising private consumption and public investment in infrastructure.

Growth in Central Africa is projected to pick up, from 2.3 per cent in 2018 to 2.7 per cent in 2019 and accelerating to 3.8 per cent in 2020, driven by a recovery in commodity prices, both new and increased production of oil and gas and strong performance in agribusiness, mining (in Central African Republic), manufacturing and services.

Growth in North Africa is projected to decline, from 3.7 per cent in 2018 to 3.4 per cent in 2019 before moderating to 3.5 per cent in 2020, driven by higher oil prices, gas production and continued investments in non-oil sectors (manufacturing and services).

Southern Africa is projected to remain the slowest growing subregion, with a growth rate of 2.1 per cent in 2019, up from 1.2 per cent in 2018. Growth will be driven by increasing agricultural production and rising global commodity prices.

However, most African economies face downside risks to growth from the tightening of monetary policy and new protectionist policies in advanced economies; weather-related shocks, especially in agriculture-dependent economies; threats of

terrorism and conflict; political instability; and high chance of debt distress in some countries.

RECENT SOCIAL DEVELOPMENTS IN AFRICA

Africa has recorded notable gains in social development since 2000, although inclusive growth has remained elusive. Public expenditures on education and health have generally been on the rise.

Gains in social outcomes could be expanded and sustained if African countries mobilize fiscal revenue in innovative ways and deploy them more effectively. Countries need to explore how social development can contribute to fiscal policy effectiveness in financing sustainable development. And in formulating and implementing fiscal policies, countries should be mindful of the potential differential impacts of fiscal policies on men, women and children arising from their different roles in society.

...most African economies face downside risks to growth from the tightening of monetary policy and new protectionist policies in advanced economies; weather-related shocks, especially in agriculture-dependent economies; threats of terrorism and conflict; political instability; and high chance of debt distress . ■

SOCIOECONOMIC OUTCOMES ARE IMPROVING

Poverty and inequality

Africa's progress in poverty reduction remains steady, albeit slow. The poverty rate dropped from 54.3 per cent in 1990 to 36 per cent in 2016 (AUC and OECD, 2018; ECA, 2017a). However, poverty reduction has not kept up with population growth, so even as the poverty rate falls, the number of people in absolute poverty has remained around 390 million (ECA, 2017a). Especially concerning is the large size of the poverty gap (the depth of poverty),⁷ which at 15.2 per cent is considerably higher than the global average of 8.8 per cent. The large gap partially explains the slow reduction in poverty and contributes to income-related inequities in access to public services, particularly health, where out-of-pocket costs are high.

Income inequality is high, with a Gini coefficient of 0.44, though it is declining. Inequality has been declining in 7 of 12 countries in West Africa (most of them agrarian) and in some countries in East Africa, though more slowly. However, inequality has been rising in nine African countries in the Southern Africa subregion (Cornia, 2016). Within-country inequality explains more than half of total

--The poverty gap provides a measure of how far below the poverty line the poor in a given country or region fall. This gap is expressed as a share of the poverty line and represents the average distance to the poverty line among all the poor.

Poverty reduction has not kept up with population growth, so even as the poverty rate falls, the number of people in absolute poverty has remained around 390 million.

inequality in Africa, which is in sharp contrast to the pattern of global inequality where across country differences contribute more to overall inequality (Lakner and Milanovic, 2015).

Unemployment and informal employment

Unemployment, at just above 7 per cent in 2017, is expected to remain at that rate until 2019, as countries intensify efforts to diversify their economies. Meanwhile, the share of workers who are extremely poor (earning less than \$1.90 a day) has been falling in Central, East, Southern and West Africa, from 52.8 per cent in 2000 to 33.5 per cent in 2015 (ECA, 2017a) and is projected to continue falling from 31.9 per cent in 2017 to 30.4 per cent in 2019 (ILO, 2018). By gender, women represented 54.8 per cent of working poor compared with 51.3 per cent of men in 2000, representing a gender gap of 3.5 percent; the gap dropped slightly to 3 per cent in 2014 (ECA, 2017a).

Most of Africa's working poor are employed in the informal sector, where productivity and pay are low and workers have no access to social protection services. Informal activity may be, on average, as high as 42 per cent of non-agricultural employment in Africa, while constituting approximately 80 per cent of employment in Ghana, Kenya, Madagascar and Mali (Zulu, Assefa and Sinha, 2016). Nearly three-quarters of informal workers are women.

Health

Africa has lowered under-five mortality faster than other global regions, cutting it by 42 per cent from 1990 to 2017—from 165 deaths per 1,000 live births to 70—compared with a global average reduction of 44 per cent (UNIGME, 2018). Three of the six African countries that have achieved the SDG target of 25 deaths per 1,000 live births are in North Africa (Egypt, Libya and Tunisia), driving the reduction in under-five mortality in the subregion from 44.3 per 1,000 live births in 2000, to 24.1 in 2016, a 46 per cent reduction; the others are Cabo Verde, Mauritius and Seychelles (ECA, 2017b). Notwithstanding this



notable progress, however, Africa has the highest proportion of deaths among children under age of five globally.

The maternal mortality ratio for Africa dropped by 36.5 per cent between 2000 and 2015. The maternal mortality ratio for Central, East, Southern and West Africa combined dropped by 35 percent, from 846 deaths per 100,000 live births to 546, while in North Africa maternal mortality dropped by 38 percent, from 113 deaths per 100,000 live births to 70 (ECA 2017a).

Primary school enrolment

Africa has achieved an impressive increase in primary school enrolment, with most countries more than doubling the number of primary school students since 1990. Since 2009, 15 countries have abolished school fees, enabling more children to attend primary school, though obstacles such as transport and learning material costs remain (UNESCO, 2015). Burundi, Ethiopia, Morocco, Mozambique and Tanzania have achieved good, albeit uneven, progress on several indicators of primary schooling, such as net enrolment ratios and primary school attainment rates, and reduced gender and income disparities in access to education (UNESCO, 2015). Indeed, Africa has nearly closed the gender gap in primary education, with the ratio of female to male primary enrolment rates reaching 92 per cent (ECA, 2017a). However, progress has been uneven. Eritrea enrolled fewer than 47.1 girls per 100 boys in primary school over 2010–2015, while Angola and South Sudan enrolled fewer than 70 girls per 100 boys, in large part because of political instability.

PUBLIC EXPENDITURE AND SOCIAL DEVELOPMENT

There is substantial variation across subregions and countries in terms of public expenditure on social development across Africa (IFPRI, 2015). For example, Nigeria spent an average of about

Increased spending on education since 2000 has contributed to improved education outcomes such as higher primary school enrolment and higher youth literacy rates.

20 per cent of its consolidated government budget on health, education, skills training and social protection over 2006–2016 (Obona, 2018), while Kenya spent 25.2 per cent of its budget in 2016/17 on social development (Nafula, 2018).

Education spending

Increased spending on education since 2000 has contributed to improved education outcomes such as higher primary school enrolment and higher youth literacy rates. The allocation to primary schooling rose from 14.8 per cent of government spending in 1999 to 18.4 per cent in 2012 and from 3.9 per cent of GDP to 4.9 per cent (UNESCO, 2015). However, in 2012 per capita spending on primary education in North Africa (\$136) was just half that in South East Asia and one-ninth of that in Latin America.⁸ The steep increase in primary school enrolment between 1999 and 2012, combined with the abolition of primary school fees, kept per capita spending on education unchanged or even lowered it. For example, despite increased total public spending on education as a share of GDP, between 1990 and 2012, spending per primary school student fell from \$207 to \$130 in Nigeria and from \$74 to \$54 in Malawi as enrolment rose (UNESCO, 2015).

8 These figures are expressed in purchasing power parity terms using 2011 constant prices.

Public spending on health needs to become more inclusive to achieve the goals of the 2030 Agenda for Sustainable Development and the AU Agenda 2063.

Under the Fast Track Initiative, a global partnership between developing and donor countries that emerged from the Education for All Conference in 2000, 43 countries signed up to meet public spending targets in education (FTI, 2009). Donors agreed to increase their aid commitments for education, and governments agreed to boost education spending to 20 per cent of government spending (FTI, 2009). On average, country spending on education has been close to the target over 1995–2016 (figure 1.15). Completion rates have remained low at 70 per cent of those enrolled, reflecting some loss in quality driven by large

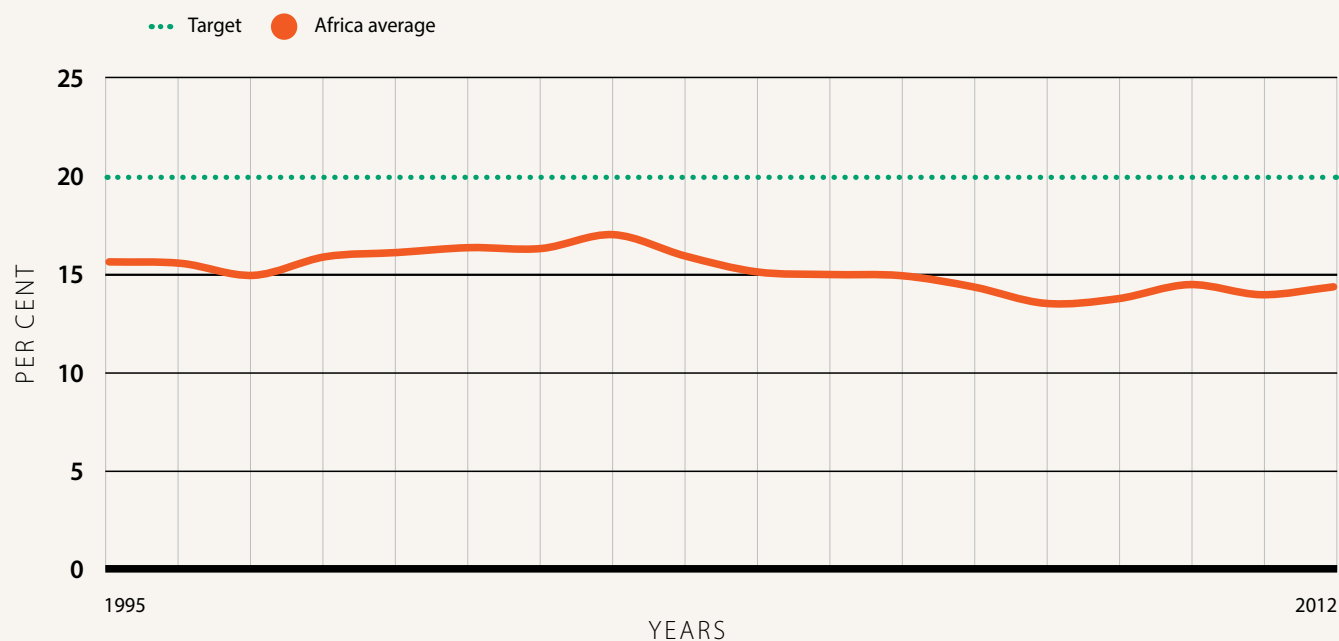
student inflows and diminishing per capita spending, demonstrating that demographic dynamics need to be factored into public finance.

Health spending

Health spending followed a similar pattern to that of education spending. On average, African governments spent 7.2 per cent of their budgets on health over 2000–2015, with wide variation across subregions (figure 1.16). Health spending shares have consistently been lower in Central Africa than in other subregions. All subregions increased their allocations to health over 2010–2015, with the increase particularly notable in North Africa.

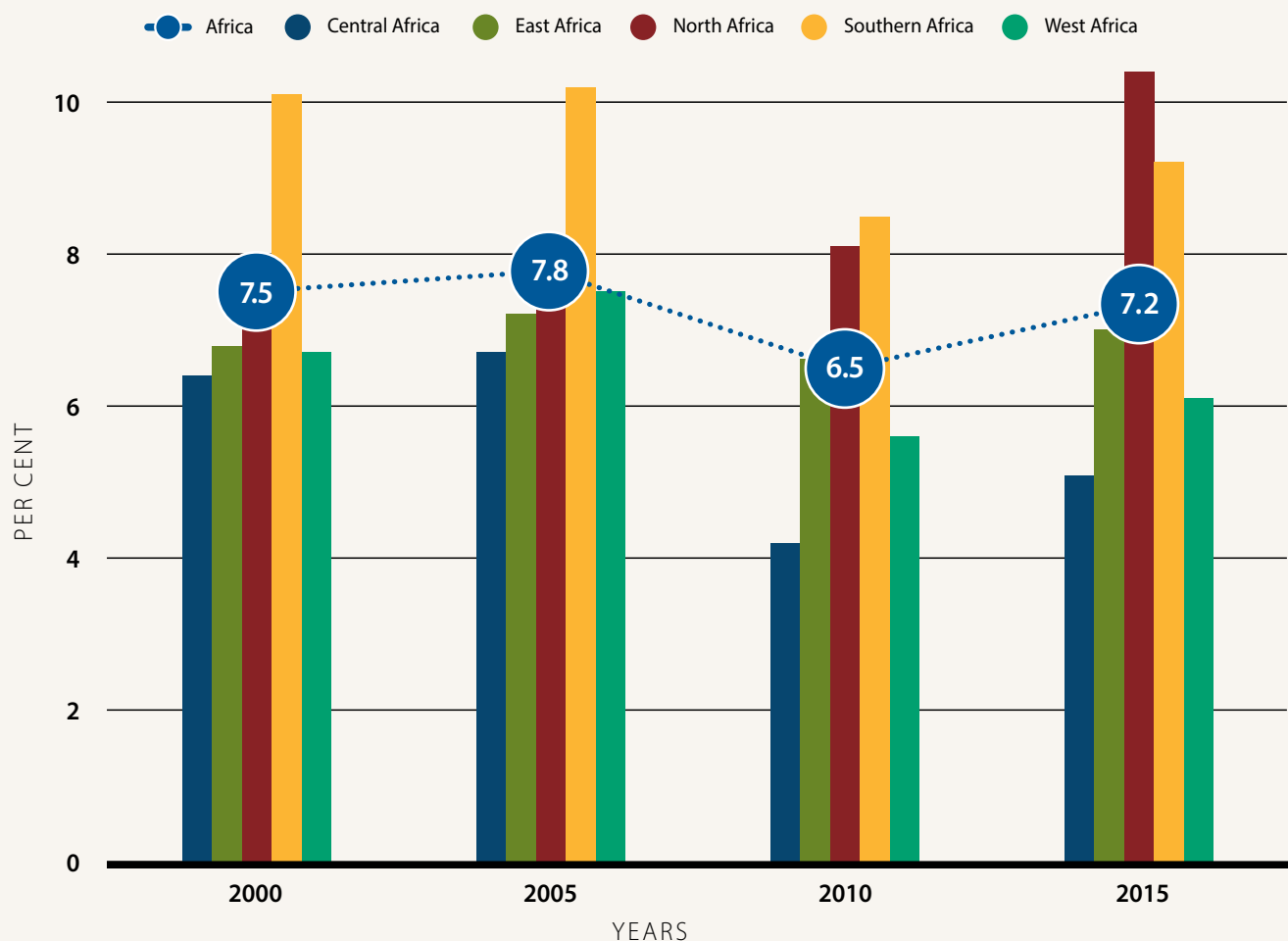
While overall per capita spending on health has increased, most of the increased burden fell on households rather than governments. That aggravated inequality by blocking access for people who cannot afford to pay for it. For example, average out-of-pocket spending on health increased in nearly all African countries,

FIGURE 1.15. PUBLIC EDUCATION SPENDING IN AFRICA AS A SHARE OF GOVERNMENT SPENDING, 1995–2012



Source: Based on data from World Bank (2018b).

FIGURE 1.16. PUBLIC HEALTH SPENDING IN AFRICA AS A SHARE OF GOVERNMENT SPENDING, 2000-2015



Source: Based on data from ECA (2018).

rising from \$15 per capita in 1995 to \$38 per capita in 2014. In Lesotho 1–3 per cent of households spent 40 per cent or more of their monthly income on health services in 2012, a catastrophic share for those households (Akinkugbe, Chama-Chiliba and Tlotlego, 2012). Public spending on health needs to become more inclusive to achieve the goals of the 2030 Agenda for Sustainable Development and the AU Agenda 2063.

Africa needs to accelerate economic growth from 3.2 per cent to double digits to achieve the SDGs.

CONCLUSIONS AND POLICY IMPLICATIONS

Africa needs to accelerate economic growth from 3.2 per cent to double digits to achieve the SDGs (see chapter 2). Doing that requires boosting investment to 30–35 per cent of GDP and greatly increasing productivity, growth of which fell to 0.3 per cent over 2009–2018, well below the global average of 1.9 per cent over 2011–2017. To achieve the SDGs, African countries should implement comprehensive macroeconomic reforms to build resilience, raise potential growth and improve inclusiveness.

With estimated annual population growth of 2.6 per cent over 2010–2015 and 2.5 per cent over 2015–2018, and GDP per capita growth averaging 1.9 per cent over 2010–2018, Africa needs targeted policies to enhance structural transformation and achieve the SDGs. These policies should be coupled with improved public financial management to enhance the efficiency of government spending. In addition, countries must build the fiscal space needed to finance development through effective tax policy and administration and a wider tax base.

To reduce vulnerabilities to global economic conditions, such as tighter global financial markets, currency fluctuations, capital outflows and volatile commodity prices, African countries need to enhance resilience through fiscal, monetary, exchange rate and prudential policies to maintain their growth momentum. Close monitoring of the negative effects of these policies on public and private sector balance sheets and domestic inflation would be key to achieving the intended objectives.

Most African countries rely heavily on imports of manufactured and agricultural products, while intra-African trade is concentrated in machinery and transport equipment. Countries need to diversify their production and accelerate their structural transformation to support their industrialization through trade. This would offer opportunities for industrial upgrading, increased exports and foreign reserves and lower debt-service obligations. Africa's high debt levels, which threaten long-term development, call for improved debt management to avoid the detrimental growth effects that arise from domestic currency and interest rate risks and uncertainties.



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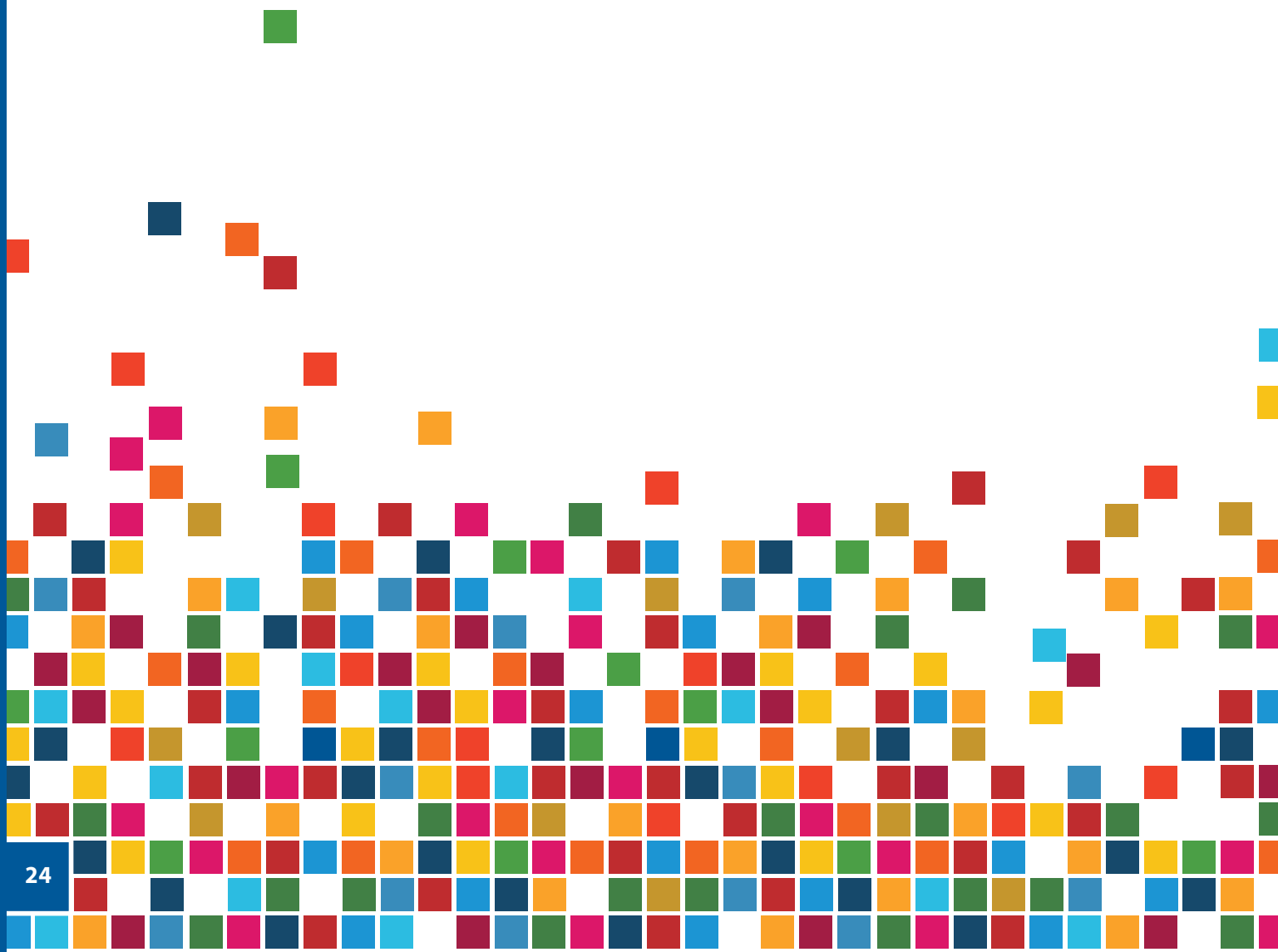
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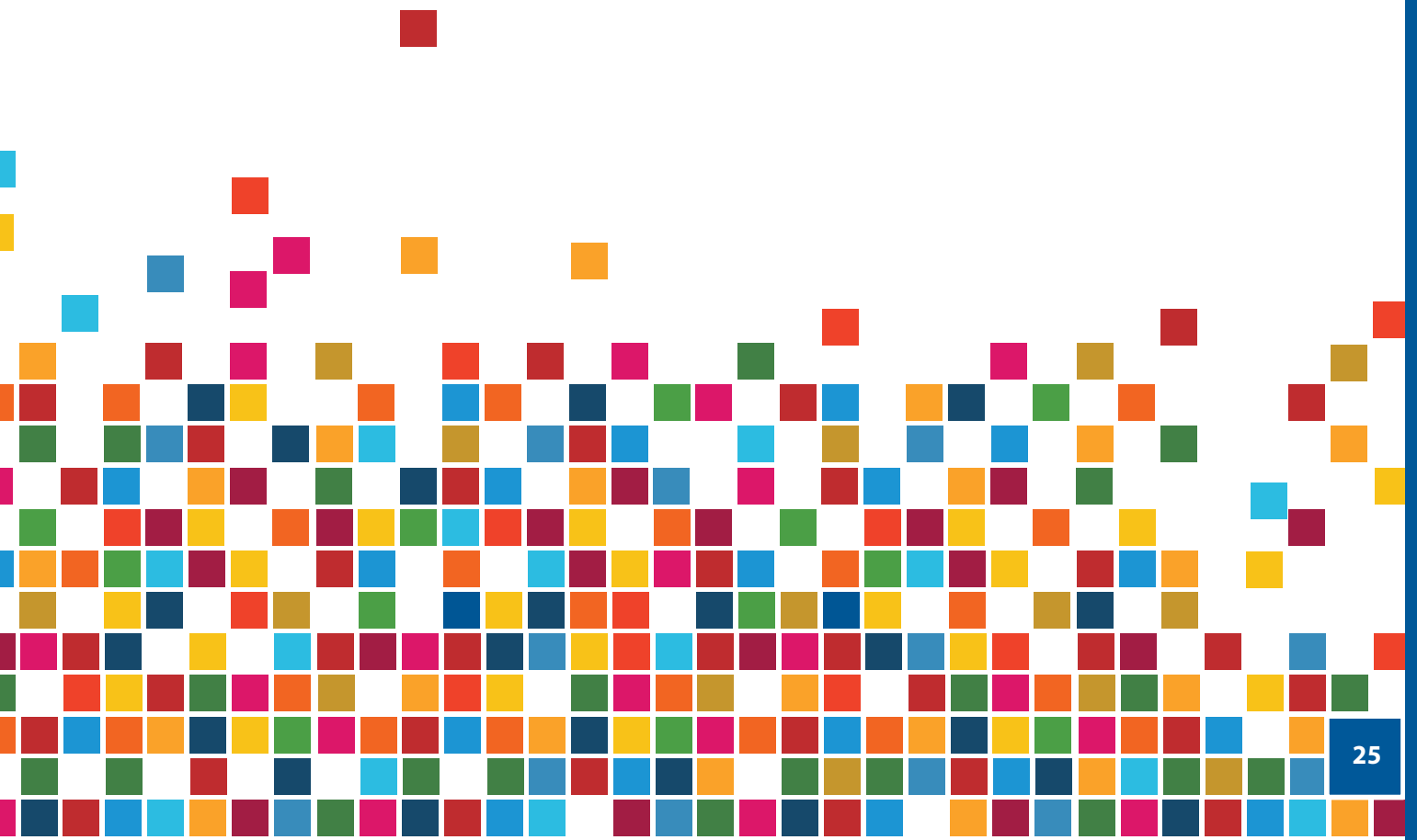
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CHAPTER 2

FISCAL POLICY AND DEVELOPMENT FINANCE



Despite substantial fiscal reform, revenue ratios, fiscal balance and debt levels have deteriorated in Africa, reflecting a continuing reliance on commodity revenue and the recent steep decline in commodity prices. Although growth and employment remain primary objectives of fiscal policy, many African economies need to adopt a countercyclical fiscal policy that also focuses on macroeconomic stability. Overall, African countries could increase their government revenue by up to 5 per cent of GDP by shifting from acyclical or procyclical fiscal policy to countercyclical fiscal policy.

African tax authorities should steer clear of the global “race to the bottom” in cutting corporate tax rates to attract foreign companies. The Report’s analysis shows that cutting taxes will lead to large losses in revenue in return for small and often uncertain gains in investment: to achieve a 1 per cent increase in total investment, governments could lose up to 20 per cent in tax revenue.

Fiscal policy can boost investment in Africa by promoting the African Continental Free Trade Area (AfCFTA). Trade openness has the largest impact on investment in Africa. A 1 per cent rise in Africa’s trade can boost private investment by an average of about 0.5 per cent.

INTRODUCTION

Endogenous growth theory provides the analytical framework to explain the impact of fiscal policy on long-run growth (see, for example, Barro and Sala-i-Martin, 1992). Endogenous growth models show that government policy can affect long-term growth, in contrast to neoclassical growth theory, which sees long-term growth as driven by exogenous factors, with government policy having only short-term effects on growth (Solow, 1956; Swan, 1956).

Fiscal policy is a powerful instrument for influencing the economy. By adjusting spending levels and taxes, governments can achieve such desired policy objectives as increased growth and employment, macroeconomic stability, income distribution, allocative efficiency and operational efficiency.

During the 2008 financial crisis, many governments across the globe responded by lowering interest rates and bailing out banks. Disappointed in most cases with the impact of these monetary policies, governments turned to fiscal stimulus policies. The recent indications of global economic recovery owe much to the active use of fiscal stimulus measures to weather the impact of the global crisis (Izvorski, 2018).

Although growth and employment remain primary objectives of fiscal policy, many African economies need to adopt a countercyclical fiscal policy that also focusses on macroeconomic stability.

The role of fiscal policy in mobilizing financial resources to achieve the Sustainable Development Goals (SDGs) is articulated well in the Addis Ababa Action Agenda (AAAA), the outcome document of the 2015 Third International Conference on Financing for Development (UN, 2015). The AAAA recognized the need to mobilize sizeable domestic public resources, supplemented by international assistance, under six action areas aimed at realizing the SDGs. Countries committed to strengthening revenue collection and administration through modernized, progressive tax systems and improved tax policy. Countries also pledged to improve the fairness, transparency, efficiency and effectiveness of tax systems and to scale up international tax cooperation.

This chapter highlights the financing requirements in Africa to achieve the SDGs and discusses fiscal developments since 2000. It assesses the availability of fiscal space and empirically examines the role of fiscal policy in Africa. It also analyses the role of fiscal policy in promoting macroeconomic stability, investments, growth, structural transformation and income inequality.

THE ROLE OF FISCAL POLICY IN THE ECONOMY

The rationale for fiscal policy is threefold: to promote macroeconomic stability, improve resource allocation and address distribution disparities (Musgrave, 1959). Fiscal policy can therefore support growth acceleration and structural transformation in Africa.

MACROECONOMIC STABILITY

Fiscal policy takes three main forms: countercyclical, procyclical and acyclical. Countercyclical fiscal policy means reducing government spending and raising taxes during boom periods and increasing spending and cutting taxes during recessions. Procyclical fiscal policy means the reverse: increasing government spending and reducing taxes during booms and reducing spending and

 **Acyclical fiscal policy does not take the business cycle into account.**

increasing taxes during recessions. Acyclical fiscal policy does not take the business cycle into account.

In the short term applying timely countercyclical fiscal policy in response to macroeconomic shocks reduces the gap between potential output and aggregate demand, thus slowing unemployment and easing inflationary pressures.¹ In the long run prudent fiscal management would ensure the sustainability of the fiscal balance and public debt so that public finance contributes to macroeconomic stability rather than becoming a source of macroeconomic instability. It does this through two main channels. First, it cushions national expenditure shocks through automatic reductions in government savings during downturns and increases during upturns (Blinder and Solow, 1973). Second, it can offset business cycle fluctuations by deliberately changing public spending and tax instruments (Debrun and Kapoor, 2012).

Fiscal policies in Africa and many other developing countries are mostly procyclical (Carmignani, 2010). Fiscal policy was procyclical in almost two-thirds of a sample of 45 African countries during 1980–2000 (Leibfritz and Rottmann, 2013). After 2000, however, this share declined to less than 40 per cent, as spending became countercyclical or acyclical in a majority of countries.

¹ It is debatable theoretically whether fiscal policy is the best policy to reduce the negative consequences of a business cycle.

LONG-TERM GROWTH

Along with the right spending composition, stronger budgetary positions are generally associated with higher economic growth (Gupta et al., 2005). Specific types of public spending can contribute significantly to the level and quality of GDP growth. For example, while public spending may crowd out private investment, efficient public investments can enhance private investment productivity and enhance long-run growth. The government may supply key public goods and services, such as law and order, justice and infrastructure, that the private sector is unable to provide in optimal quantity or quality due to market failures. The production of such key goods and services by the government would boost private sector productivity.

Little is known about the size of the growth effects of different types of public spending in developing countries or the circumstances under which these effects may be influenced.

Another link between fiscal policy and growth is the impact of taxes on factor accumulation. For example, a tax on income from capital would lower the after-tax return on savings and investment, affecting private investment decisions.²

EQUITABLE GROWTH

Redistributive fiscal policies can affect such private decisions as whether to seek employment, change labour effort, or save and invest, in turn influencing the level and growth of economic output. For example, the income tax on wages influences private economic agents' allocative decisions on whether to participate in the labour market and how much to work.³

Over the short and medium terms, tax and spending policies can affect the distribution of income. For example, education spending can reduce inequality through its impact on future earnings. Other fiscal instruments, such as income taxes and cash transfers, can reduce inequality in disposable incomes, including indirectly through the impact on market incomes due to employment and savings responses (IMF, 2014). Endogenous growth models show that income tax reductions can encourage human capital accumulation and thus growth by increasing the returns to education (Pecorino, 1993). Conditional cash transfers have been used successfully to reduce inequality in Latin America.

Some empirical analyses suggest that greater reliance on income taxes and higher spending on social and social protection reduce inequality and that direct (and progressive) taxes are more redistributive than indirect taxes (Woo et al., 2013).

ECONOMIC DIVERSIFICATION AND STRUCTURAL TRANSFORMATION

Fiscal policy can accelerate structural transformation in Africa by supporting technology, rapid accumulation of human and physical capital, trade openness, financial development, markets, institutions and governments (Mensah et al., 2016). In a study of 21 African countries, governance and fiscal reforms were found to be important determinants of transformation (Mensah et al., 2016). Additionally, empirical evidence shows that macroeconomic policy (including fiscal policy) is critical for the structural transformation of African economies (ECA, 2016).

² The ultimate impact of capital taxes on growth is ambiguous. It depends on how other factors, such as human capital, that cooperate with physical capital in the production process are affected by the tax (Tanzi and Zee, 1997).

³ All taxes are non-neutral and distort economic behaviour, resulting in net efficiency loss in the whole economy, even if the government engages in exactly the same activities as the private sector with the tax revenue raised (Tanzi and Zee, 1997).

THE SCOPE OF FINANCING REQUIREMENTS

ESTIMATING THE DEVELOPMENT FINANCING GAP

Since the launch of Agenda 2030, there have been several estimates of the cost of financing sustainable socioeconomic development in Africa and of the size of the financing gap. Despite notable variations, all estimates indicate huge financing needs and financing gaps in order to achieve the SDGs in Africa (table 2.1).

Schmidt-Traub (2015) estimated Africa's incremental financing needs to achieve the SDGs at \$614–\$638 billion a year over 2015–2030 and at as much as \$1.2 trillion a year in low-income and lower-middle-income African countries, or about 11 per cent of GDP. The United Nations Conference on Trade and Development (UNCTAD, 2014) forecasts an annual financing need for Africa of \$210 billion for basic infrastructure, food security, health, education and climate change mitigation and global investment needs of \$5–\$7 trillion a year

■ Fiscal policy can accelerate structural transformation in Africa by supporting technology, rapid accumulation of human and physical capital, trade openness, financial development, markets, institutions and governments. ■

to achieve the SDGs. The International Monetary Fund (IMF, 2018a) estimates that the 49 low-income developing countries need, on average, additional annual outlays of \$520 billion, or 14 per cent of their GDP, with some countries needing even more, such as Benin (21.3 per cent) and Rwanda (18.7 per cent). However, these estimates vary depending on the growth scenario, from about \$300 billion for a high-growth scenario to about \$900 billion for a low-growth scenario.

TABLE 2.1. ESTIMATES OF ANNUAL DEVELOPMENT FINANCING NEEDS IN AFRICA

STUDY	ESTIMATED DEVELOPMENT FINANCING NEEDS/FINANCING GAP	SCOPE OF THE ESTIMATE
Schmidt-Traub (2015)	\$614–\$638 billion	Annual incremental financing needed to achieve the Sustainable Development Goals (SDGs)
UNCTAD (2014)	\$210 billion	Annual cost of basic infrastructure, food security, health, education and climate change mitigation
IMF (2018a)	14 per cent of GDP (about \$520 billion)	Additional annual outlay in all low-income countries (not just in Africa) for meeting the SDGs
AfDB (2018)	\$130–170 billion	Annual infrastructure financing gap in Africa
Chinzana, Kedir and Sandjong (2015)	\$1.2 trillion	Additional investment needed to meet goal 1
World Bank (2012)	\$18 billion	Annual cost of climate change adaptation
World Bank (2015)	\$93 billion	Annual financing needed for infrastructure

NARROWING THE DEVELOPMENT FINANCING GAP

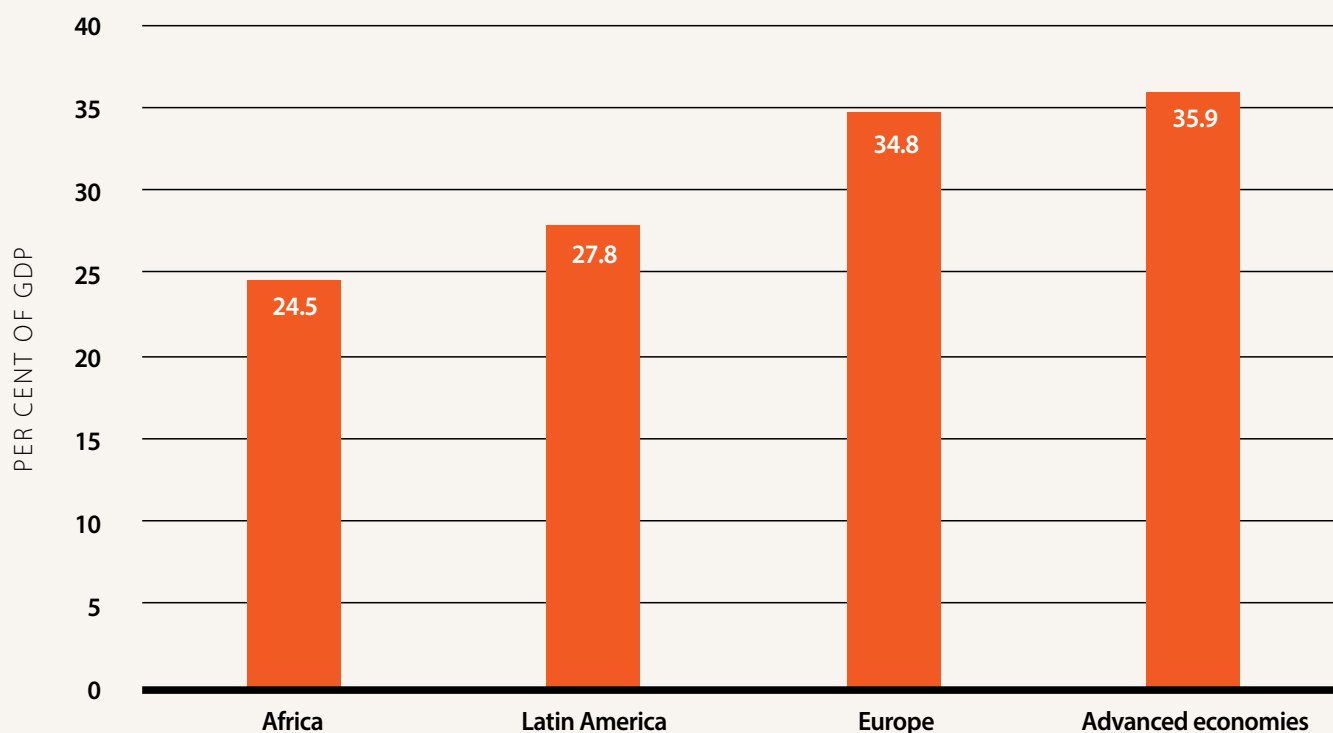
Given the huge financing needs and the savings–investment gap in Africa, the key question for policymakers is where to source the financing. Over 2000–2015, when the Millennium Development Goals defined the primary development challenges, official development assistance was a major source of financing. Today, achieving the SDGs (2015–2030) will require many different sources of financing. With dwindling global donor funding and unpredictable economic conditions, domestic resource mobilization—and in particular fiscal policy—has to make a larger contribution to financing development and narrowing the financing gap in Africa. Public finance also has a role to play in catalysing private resources, particularly for long-term investments in infrastructure and public goods.

FISCAL DEVELOPMENTS SINCE 2000

RESOURCE MOBILIZATION

Total government revenue in Africa, including revenue from natural resources, increased from 25.2 per cent of GDP in 2000 to 31.4 per cent in 2008 and then declined in the aftermath of the global financial crisis to 18.6 per cent in 2016 before rising to 21.4 per cent in 2018, the lowest total government revenue to GDP ratio of any region in the world. Its average ratio over 2000–2018 was 24.5 per cent, below that of emerging market and middle-income economies in Latin America (27.8 per cent) and in Europe (34.8 per cent) and that of advanced economies (35.9 per cent). (Figure 2.1)

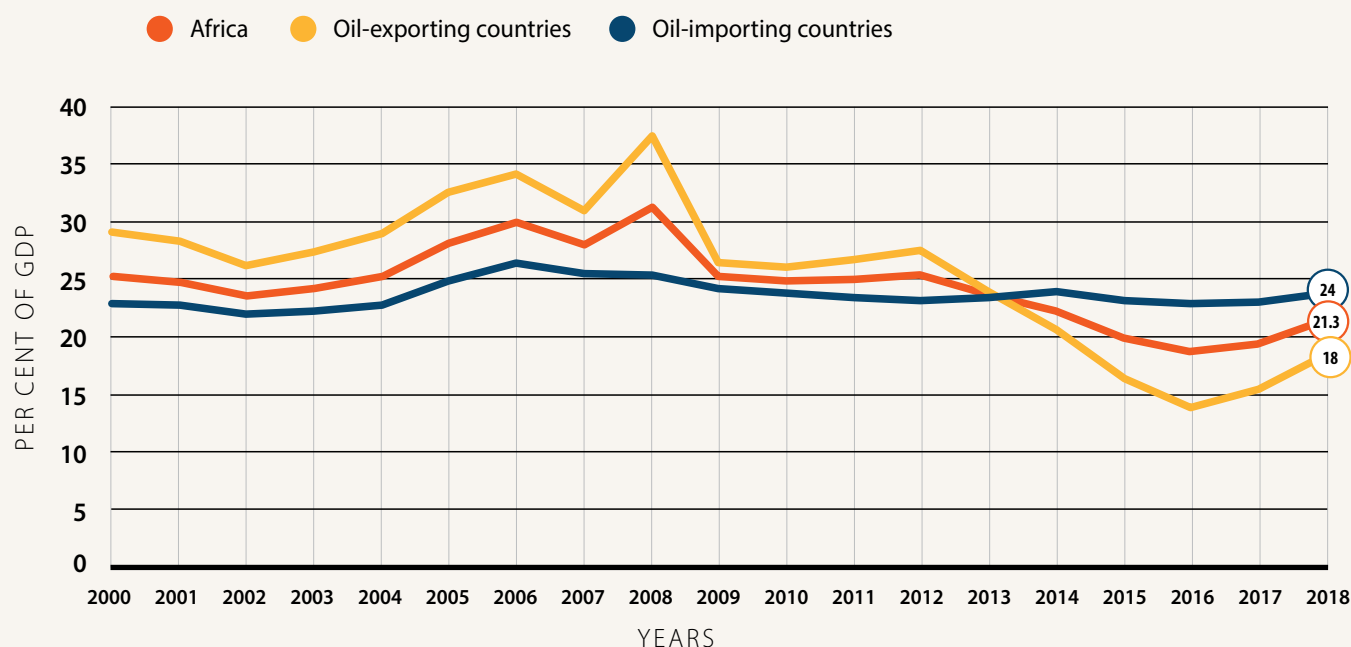
FIGURE 2.1. GOVERNMENT REVENUE IN AFRICA COMPARED TO OTHER REGIONS (2000–2018)



Note: Only emerging market and middle income countries in Latin America, Europe and Advanced economies are used in the grouping. Data for 2018 are projections by ECA.

Source: Based on data from IMF World Revenue Longitudinal Data (2018).

FIGURE 2.2. TOTAL GOVERNMENT REVENUE IN AFRICA, 2000-2018



Note: Data for 2018 are projections by ECA.

Source: Based on data from IMF World Revenue Longitudinal Data (2018).

Commodity price shocks had a notably unfavourable effect on total government revenue. Before 2014, the total government revenue to GDP ratio in Africa was higher in oil-exporting countries than in oil-importing countries (figure 2.2). Over 2014–2016 revenue declined in both groups, but they declined more in oil-exporting countries, falling by about 5 per cent of GDP.

Fiscal performance has varied across African countries. Some countries successfully implemented fiscal reforms, resulting in higher fiscal revenue over 2000–2018. Fiscal reforms in Rwanda over 2000–2013 increased revenue by some 18.8 per cent.⁴ Similarly, Burkina Faso's fiscal reforms in 2006 resulted in a revenue increase of 3 per cent of GDP in 2007, from 17 per cent of GDP

4 Reforms included introducing an e-tax information system, reforming customs administration, lowering dependence on import duties, extending working hours at borders and customs offices, reforming tax administration, introducing a new income tax policy and eliminating many exemptions.

Fiscal performance has varied across African countries. Some countries successfully implemented fiscal reforms resulting in higher fiscal revenues over 2000-2018.

to 20 per cent. While revenue declined to 16.8 per cent of GDP in 2008, additional reforms in 2008 and 2010 led revenue to rise to 19.7 per cent of GDP in 2010 and to 29.2 per cent in 2017.⁵

5 Reforms included reducing the percentage of late taxpayers and tax evaders from 12 per cent at the beginning of 2007 to less than 7 per cent at the end of the third quarter of 2008, introducing a corporate income tax instead of the existing schedule of taxes on business and industrial income, ending the exemptions for capital gains that are reinvested and for start-up businesses, and creating a manual of tax procedures.

Figure 2.3 shows African countries with highest and lowest government revenue during 2000–2018. Libya and Angola had the highest average government revenue of 58 and 38 per cent of GDP, respectively, whereas Congo Democratic Republic and Guinea had the lowest average of 11 and 13 per cent, respectively. At the upper end, countries such as Congo, Algeria, Angola and Libya registered an average of more than 35 per cent of GDP. By contrast, countries such as Congo Democratic republic, Guinea, Sudan and Madagascar registered an average of less than 15 per cent of GDP.

Over 2000–2018 Congo had the highest average government revenue to GDP ratio (35.6 per cent) in Central Africa, followed by Cameroon (17.5 per cent) and Chad (16.4 per cent). In North Africa, two oil-producing countries, Algeria and Libya, recorded remarkably high ratios of 36.7 per cent and 57.7 per cent, respectively, compared with 13.1 per cent in Sudan, 26.2 per cent in Morocco and 24.0 per cent in Egypt. In West Africa, Senegal, Burkina Faso and Niger had government revenue ratios above 20 per cent, while Benin, Mali, Côte d'Ivoire, Guinea and Nigeria recorded ratios of less

than 20 per cent. In Southern Africa government revenue exceeded 30 per cent of GDP in Angola, Botswana and Namibia and was as low as 13.1 per cent in Zimbabwe.

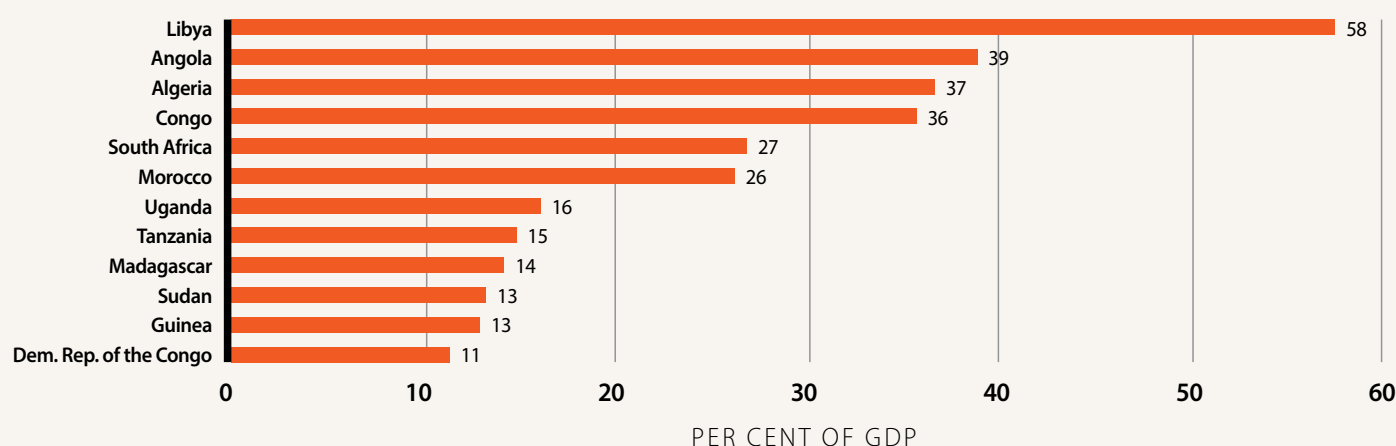
Despite widespread tax reforms, tax revenue mobilization in Africa has been mixed, limited by structural factors such as low per capita income, large informal sectors, large peasant agriculture and very small manufacturing and modern services, implying very low effective tax bases.

On average, non-tax revenue increased to 10.6 per cent of GDP in 2008 but has been decreasing since 2009, due to the 2008 financial crisis. Indeed, non-tax revenue, especially resource wealth, has been less resilient than tax revenue to the impact of the 2008 financial crisis. The commodities price shock of 2014 accentuated the decline in non-tax revenue in oil- and other commodity-exporting countries.

GOVERNMENT SPENDING

Government spending increased between 2000 and 2009, peaking at 29.9 per cent of GDP in 2009, and declined to 25.5 per cent in 2017; it is projected to rise to 28.3 per cent in 2018

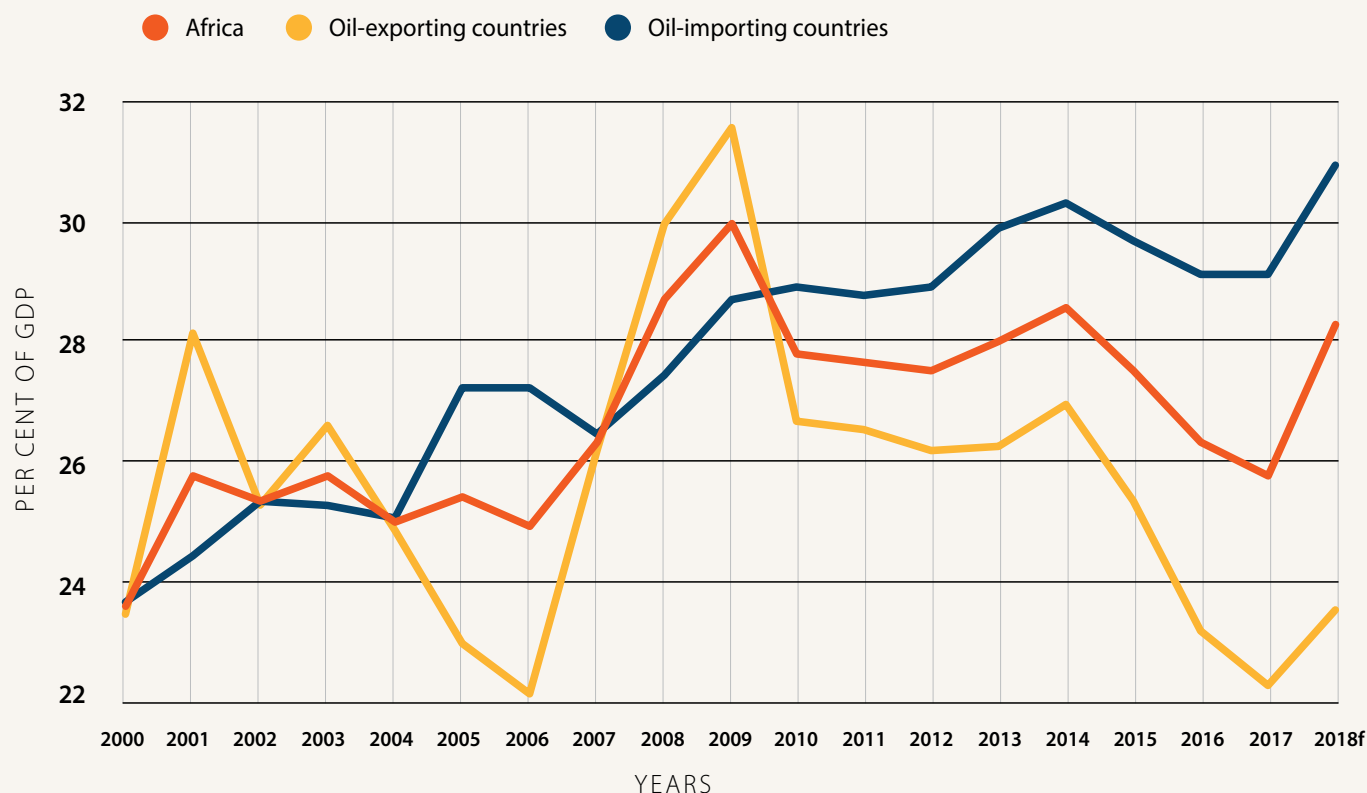
FIGURE 2.3. COUNTRIES WITH HIGHEST AND LOWEST GOVERNMENT REVENUE, 2000–2018.



Note: Data for 2018 are projections by ECA.

Source: Based on data from IMF World Revenue Longitudinal Data (2018).

FIGURE 2.4. GOVERNMENT SPENDING IN AFRICA, BY COUNTRY GROUP, 2000-2018



Note: Data for 2018 are projections by ECA.

Source: Based on data from IMF World Revenue Longitudinal Data (2018).

(figure 2.4). Trends differed in oil-importing countries and oil-exporting countries. On average, public spending was higher in oil-importing countries over 2000–2017, at 27.5 per cent of GDP, though it declined slightly after 2015. In oil-exporting countries public spending rose over 2006–2009 and then stagnated after 2010 before falling again over 2014–2017 and is projected to recover slightly in 2018 to about 23.5 per cent. A breakdown of government spending during 2000–2018 shows a low and generally stable average share for health and education (see chapter 1).

FISCAL BALANCE

Most African countries recorded fiscal surpluses over 2000–2008. Since then, deficits have prevailed and have mounted. The expanding fiscal deficits have been driven by commodity price shocks, weak

domestic resource mobilization and increased government spending. The overall primary deficit in Africa averaged 1.9 per cent of GDP in 2000–2017, with considerable variation across countries. Oil-exporting countries had primary fiscal balance surpluses until 2013 and deficits thereafter. Oil-importing countries had fiscal deficits over the entire period.

Fiscal consolidation has been a key feature in the region in recent years, leading to narrowing deficits over 2015–2017. Nevertheless, the fiscal deficit is projected to widen through 2023, since heavy investments will continue in Africa to build infrastructure and advance social development to achieve the SDGs by 2030.

FISCAL SPACE

A 2016 pilot assessment of fiscal space based on an International Monetary Fund (IMF) framework reveals that very few countries globally have substantial fiscal space. Of the five African countries included in the assessment, none had adequate fiscal space: Algeria and Morocco had the most, while Egypt, Nigeria and South Africa had very limited fiscal space.

An assessment by the United Nations Economic Commission for Africa measures fiscal space as the difference between a country's debt limit⁶ and current debt level at two total public debt limit thresholds: 50 per cent of GDP, as recommended by the IMF for developing countries, and 40 per cent, the African average (OECD, 2016; Pienkowski, 2017). Fiscal space in Africa over 2016–2018 was moderately constrained in both scenarios, at –9.6 per cent of GDP for the 50 per cent debt limit and –19.6 per cent for the 40 per cent limit.

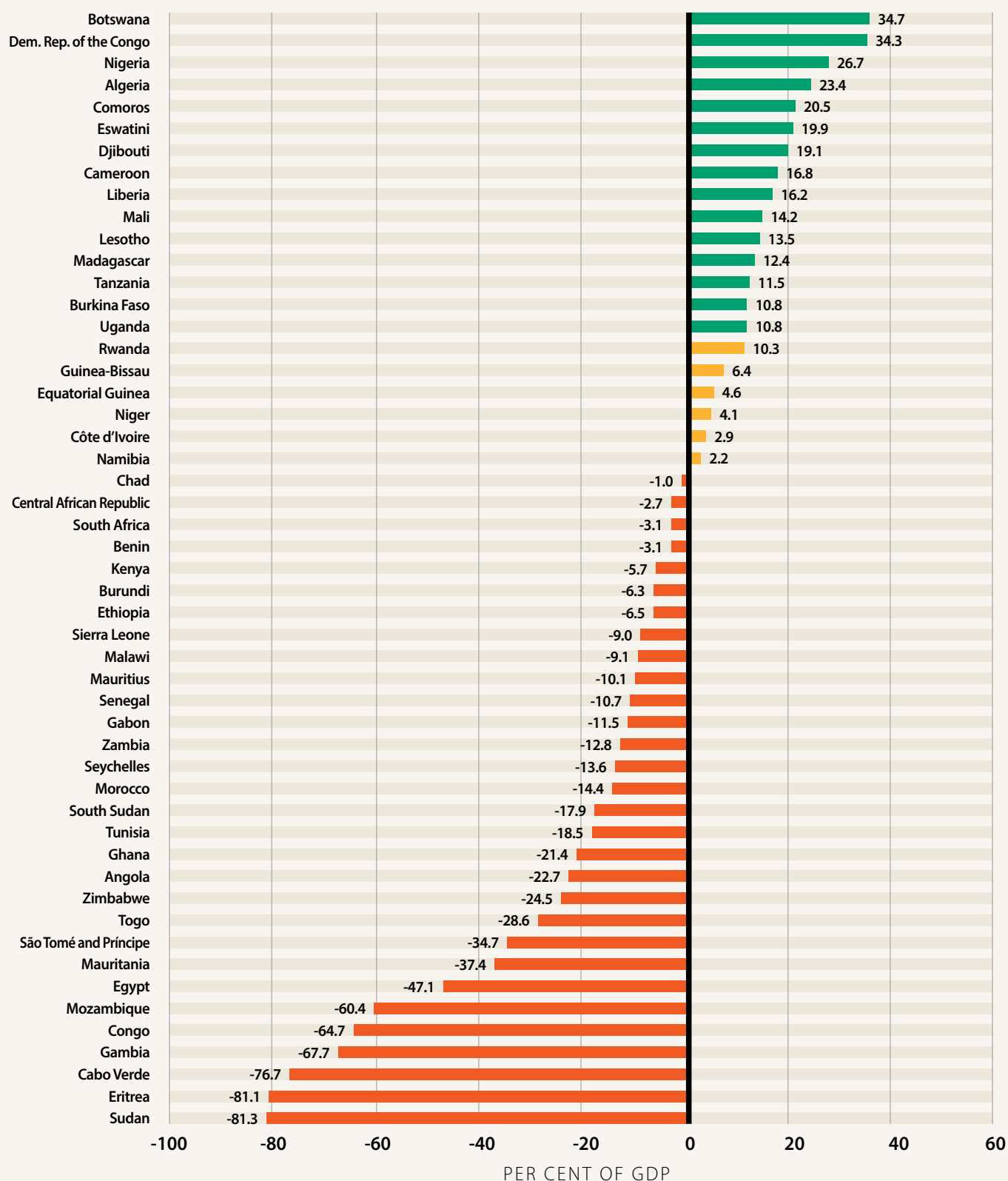
In the 50 per cent debt limit scenario, 40 per cent of African countries have positive fiscal space that

can be tapped to finance sustainable development (figure 2.5). That share goes down to 30 per cent in the 40 per cent debt limit scenario. (figure 2.6). Botswana has the highest positive fiscal space, at 34.7 per cent of GDP in the 50 per cent scenario and 24.7 per cent in the 40 per cent scenario, while Sudan is the most constrained African country, at –81.3 per cent of GDP in the 50 per cent scenario and –91.3 per cent in the 40 per cent scenario. The number of countries with fiscal space of 10 per cent of GDP or less is 6 in the 50 per cent scenario and 11 in the 40 per cent scenario. In absolute terms, at the 40 per cent debt threshold, the total fiscal space available among the 16 African countries with limited or substantial fiscal space is about \$155 billion, which is tiny compared with the huge financing gap on the continent (see the section above on “The Scope of Financing Requirements”).

Governments need to build fiscal space for priority social and economic development by strengthening spending controls and boosting the efficiency of spending. Creating fiscal space also requires assessing all public spending to ensure not only that it is directed towards improving productivity but also that it is aligned to achievement of the SDGs. Additionally, governments will need to leverage public–private partnerships to enhance resource mobilization and investment in priority areas.

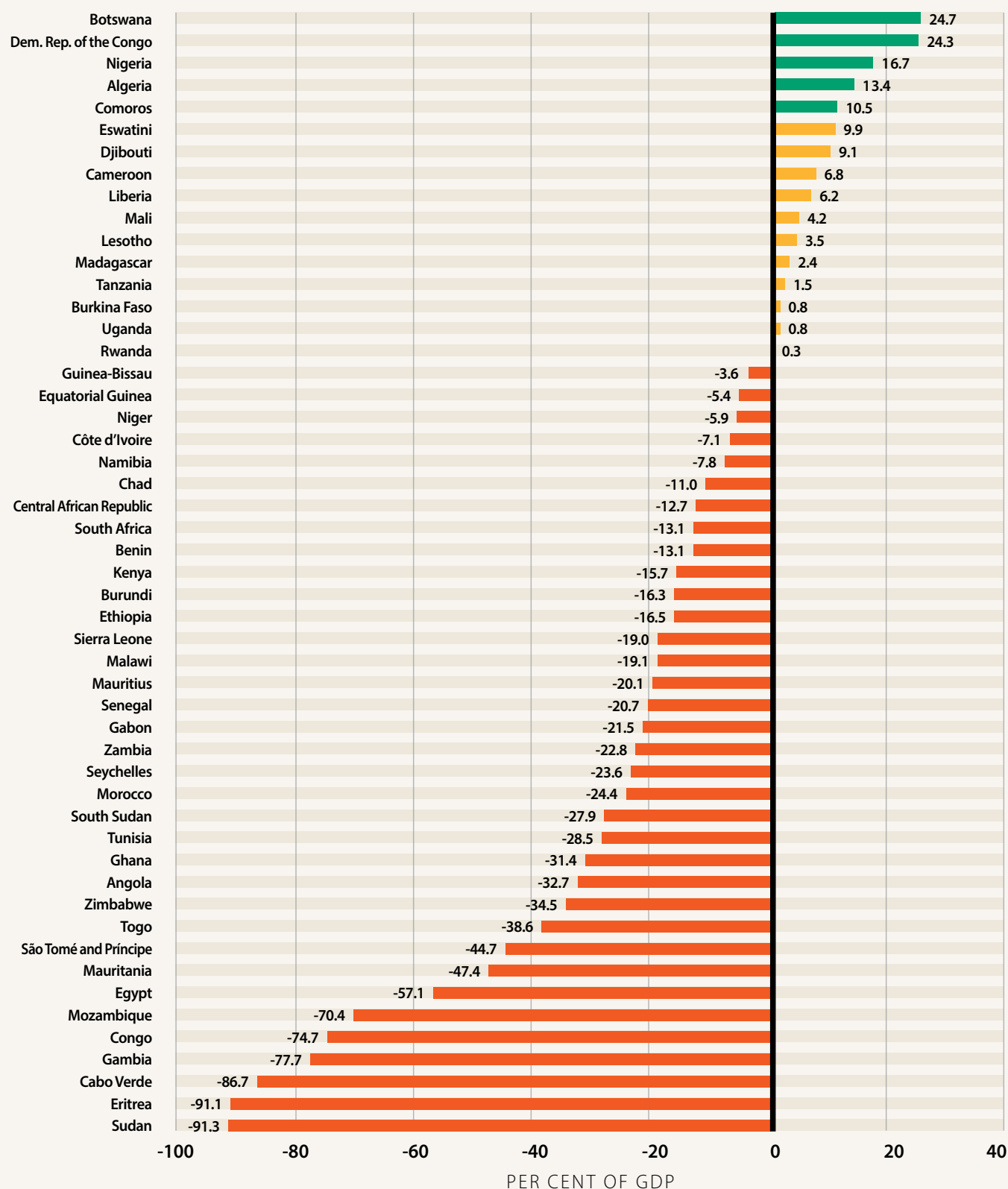
⁶ The debt limit approach to estimating fiscal space is based on the assumption that governments borrow only as a last resort, after exhausting all other financing options.

FIGURE 2.5. FISCAL SPACE IN AFRICA, AS MEASURED BY A DEBT THRESHOLD OF 50 PER CENT OF GDP, 2016-2018



Source: Based on data from IMF World Economic Outlook database (2018).

FIGURE 2.6. FISCAL SPACE IN AFRICA, AS MEASURED BY A DEBT THRESHOLD OF 40 PER CENT OF GDP
2016–2018



Source: Based on data from IMF World Economic Outlook database (2018).

THE IMPACT OF FISCAL POLICY

ON MACROECONOMIC STABILITY

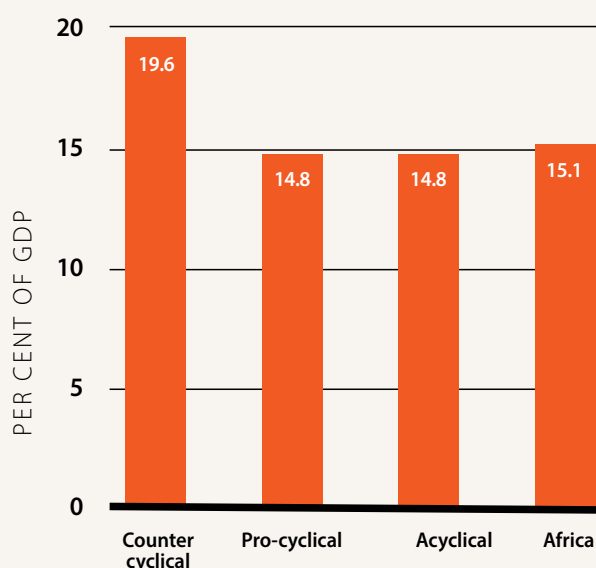
Over 1980–2015 only 4 of 45 African countries with available data had countercyclical fiscal policies (Ethiopia, Morocco, Nigeria, and Zimbabwe), 7 had procyclical policies (Central African Republic, Eswatini, Egypt, Ghana, Madagascar, Rwanda, and Seychelles) and 34 had acyclical policies, which are associated with macroeconomic instability.⁷ More countries had acyclical policies after 2000 than before then.

⁷ The analysis established a correlation between the change in government spending and real GDP growth. Countries are found to follow a countercyclical policy when the coefficient is negative and significant at the 10 per cent level, a procyclical policy when the coefficient is positive and significant at the 10 per cent level and an acyclical policy when the coefficient is insignificant. The correlation coefficient results are presented in table A2.1 in the annex.

African countries could improve their fiscal performance by shifting to a countercyclical fiscal policy. That shift brings about changes in tax rates and revenue over the business cycle and has the potential of boosting taxes as a share of GDP by 5 percentage points. Over 2010–2015 taxes averaged 14.8 per cent of GDP for countries that followed an acyclical fiscal policy and 15.1 per cent for Africa overall, well below the 19.6 per cent average for countries that followed countercyclical policies (figure 2.7).

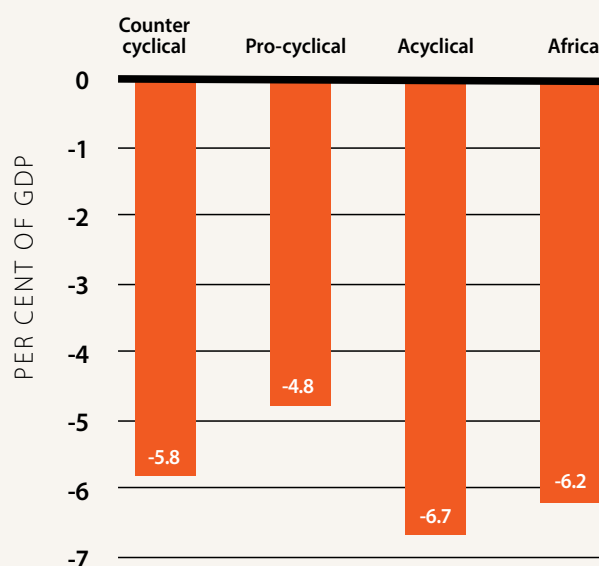
Shifting from an acyclical fiscal policy to a countercyclical fiscal policy could also lower the fiscal deficit by about 1 percentage point, reducing the average fiscal balance over 2015–2018 from –6.7 per cent to –5.8 per cent (figure 2.8). Additionally, the greater macroeconomic stability that comes with countercyclical fiscal policy is associated with higher investment and economic growth, which also enhance revenue collection and reduce the fiscal deficit.

FIGURE 2.7. AVERAGE RATIO OF TAXES TO GDP IN AFRICA BY FISCAL POLICY STANCE, 2010–2015



Source: Based on data from UNU-WIDER (2018).

FIGURE 2.8. AVERAGE FISCAL BALANCE IN AFRICA BY FISCAL POLICY STANCE, 2015–2018



Source: Based on data from AfDB (2018).

ON LONG-TERM GROWTH

The impact of fiscal policy on growth in Africa was assessed by examining the effects of fiscal components on investment and on real GDP per capita in 45 African countries over 1980–2015.⁸ Investment responds significantly and negatively to total tax revenue, direct tax revenue, income taxes, profit and capital gains taxes, and taxes on goods and services and positively to taxes on international trade.⁹ However, the tax impact on investment is small. For example, tax revenue has to decline by 20 per cent to raise investment by 1 per cent.

This means that taxes are not an obstacle to investment in Africa, because they have only a marginal impact on investor decisions. These results are in line with a UNIDO (2011) survey of 7,000 firms in 19 African countries that found that tax incentives ranked 11 out of 12 factors that influence investment decisions. It also means that African governments should stay out of the global race to attract foreign investment by offering lower taxes.

In contrast, investment responds positively and strongly to government consumption in Africa: a 1 per cent increase in government consumption is associated with a 0.3 per cent increase in total investment.¹⁰ Thus, government consumption policies can redirect investment to particular sectors and products. Investment also responds positively and significantly to government spending on health and education but not to military spending. At a constant level of government spending, increasing spending on either education or health at the expense of consumption can boost investment in Africa.

⁸ The assessment used the autoregressive distributed lag procedure, which has several advantages over the traditional co-integration models: the estimates are consistent even if the variables do not have same level of integration, the estimates are unbiased even in the long run and the estimates are more efficient in cases of small and finite samples (Harris and Sollis, 2003). The regression results are presented in table A2.2 in the annex.

⁹ All variables are taken as a percentage of GDP.

¹⁰ See regression results in table A2.3 in the annex.

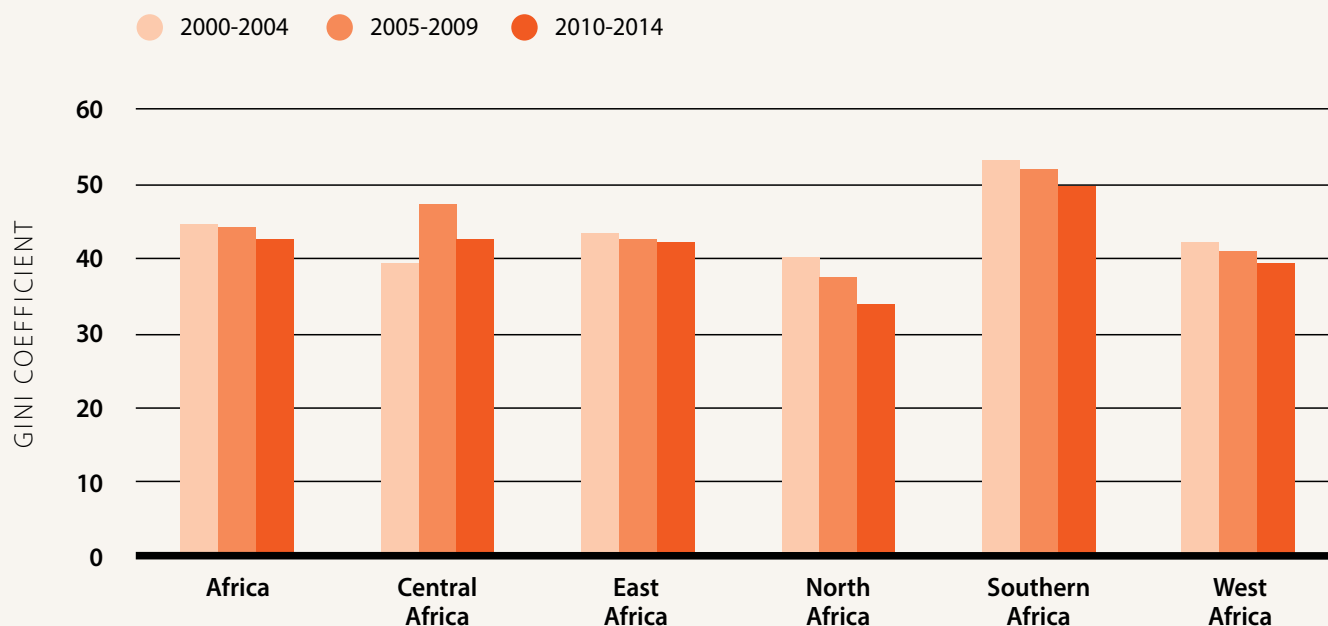
 Taxes are not an obstacle to investment in Africa, because they have only a marginal impact on investor decisions.

Investment in Africa is most strongly and positively correlated with trade openness: a 1 per cent increase in total trade raises total investment by 0.4–0.7 per cent. This implies that full implementation of the AfCFTA would drive investment in the continent. Investment is negatively and significantly associated with increasing debt and lending rates and positively correlated with GDP growth. Thus, the recent increase in domestic and foreign debt in Africa not only increases the risk of default in many African countries but also harms investment. Thirty-eight African countries have exceeded the 40 per cent of GDP public debt threshold, meaning that any additional borrowing in these countries will reduce debt sustainability and discourage investment.

Real GDP per capita is also positively correlated with non-tax revenue and with all types of tax revenue (direct, indirect, goods and services, income, profits and capital gains) except revenue from international trade taxes. A 1 per cent increase in tax revenue is associated with a 0.6 per cent increase in real GDP per capita in the long run, and a 1 per cent increase in non-tax revenue is associated with a 0.7 per cent increase, reflecting the importance of fiscal policy for economic growth. However, a 1 per cent increase in trade taxes is associated with a 0.5 per cent decline in real GDP per capita because of trade's role as an engine of growth.

Finally, private investment has the largest effect on GDP per capita: a 1 per cent increase in private investment is associated with a 1.4 per cent rise in GDP per capita in the long run. Fiscal policy has a

FIGURE 2.9. INCOME INEQUALITY IN AFRICA, BY SUBREGION, 2000-2014



Note: The Gini coefficients in the figure are unweighted averages.

Source: Based on data from World Bank (2017).

crucial role in boosting private investment in Africa by increasing spending on health and education and by developing a fair tax system. Fiscal policy can also boost private investment through public-private partnerships and by spending more on infrastructure and encouraging the adoption of new technology.

ON INCLUSIVE GROWTH

Africa has the second highest income inequality in the world, after Latin America. Despite remarkable economic growth, income inequality (as measured by the Gini coefficient) in Africa fell only slightly, from 44.7 in 2000 to 42.5 in 2014.¹¹ On average inequality increased in 20 countries and fell in 17. Guinea-Bissau, Central African Republic, Zambia, Malawi and South Africa recorded the largest rise in inequality, while Angola, Niger, Burkina Faso, Mauritania and



Despite remarkable economic growth, income inequality in Africa fell only slightly.

Sierra Leone recorded the largest decline. Changes in income inequality also varied by subregion (figure 2.9). Expansion in social protection programmes in Africa has been limited (UNCTAD, 2012).

Estimates of the impact of fiscal policy on inclusive growth (a measure combining growth and equity) in Africa reveal a positive and significant effect of

¹¹ The Gini coefficient is used to measure income inequality based on a sample of African countries for which data on inequality were available in the 2017 World Development Indicators database (World Bank, 2017).

government spending on inclusive growth.¹² A 1 per cent increase in government spending leads to a 0.3 percentage point increase in inclusive growth, other things remaining equal. In contrast, tax incidence has a negative impact on inclusive growth. These findings suggest that government spending that effectively targets the poor could reduce inequality as long as government transfers and subsidies do not distort prices in the economy and as long as governments pay attention to the source of finance (taxes and deficit financing) and to the efficiency and effectiveness of spending.

AS A KEY DRIVER OF STRUCTURAL TRANSFORMATION

An assessment of the effects of fiscal policy on Africa's structural transformation over 1960–2014 reveals that household consumption and government consumption have a larger impact than other variables (including investment, trade openness, urbanization, capital–labour ratio and human capital) on manufacturing value added.¹³ A 1 per cent increase in government consumption leads to an increase of 0.7 per cent in manufacturing value added, 0.3 per cent in services value added but just 0.003 per cent in agricultural value added.

12 The analysis used data from the World Development Indicators database for 42 countries for which at least two observations were available for inclusive growth (World Bank, 2017). Previous studies on the effect of fiscal policy on inclusive growth are mixed. On the one hand, studies such as Okun and Summers (2015; originally, Okun, 1975) argue that there is a trade-off between growth and equality. Thus, an increase in fiscal redistribution could hinder growth since redistribution through taxes and subsidies could dampen the incentive to work and invest. On the other hand, studies such as Benabou (2000) and Saint-Paul and Verdier (1993) point out that fiscal policies that increase health and education spending benefit the poor while enhancing growth through improved human capital. Ostry, Berg and Tsangarides (2014) conclude that the combined direct and indirect effects of income redistribution are on average pro-growth.

Using cross-section analysis, a set of regressors that affect growth and inequality is included as independent variables since both macroeconomic policies and non-policy factors could affect the inclusivity of growth. These sets of regressors include initial GDP per capita in purchasing power parity terms, investment, trade openness, inflation, GDP volatility, official development assistance, information and communication technology, financial deepening, indicators of the quality of institutions and governance, natural resources rent and abundance, and dummy variables for economic groupings.

13 A generalized method of moments instrument variable regression model was applied using unbalanced panel data for 54 African countries. Measured structural transformation, by sectoral output, is regressed on variables including lagged real GDP per capita, household consumption, government consumption, investment, trade openness, urbanization, capital–labour ratio and human capital.

A 1 per cent increase in government spending leads to a 0.3 percentage point increase in inclusive growth.

CONCLUSIONS AND POLICY IMPLICATIONS

Fiscal policy has the potential to be a key driver of Africa's growth and development. However, the fiscal reforms and adjustments introduced since 2000 have had a mixed impact on fiscal performance across countries. In many countries increased government revenue supported investment in infrastructure and services, fostering economic growth. However, several African countries are experiencing persistent fiscal deficits and a narrowing fiscal space with high and rising debt, threatening macroeconomic stability. Most countries continue to practice acyclical fiscal policy. To reduce fiscal vulnerability, countries need to change their fiscal practice. Countries could increase their tax revenue by up to 5 per cent of GDP by shifting from acyclical to countercyclical fiscal policy. African governments should therefore put more effort into strengthening macroeconomic management and improving spending efficiencies.

African countries are advised to re-allocate more funds to health and education to achieve higher investment and growth. Fiscal policy can also crowd in private investment in infrastructure and health, encouraging research and development and enhancing the business environment.


African governments should not take part in the ongoing global race to the bottom, as countries rush to cut corporate taxes to enhance competitiveness and attract investment. Empirical analysis shows that such cuts will cause large losses

of tax revenue in African countries in return for small gains in investment. Taxes on income, profits and capital gains would have to be cut by half to increase total investment by just 1 per cent.


This chapter has also shown how fiscal policy can speed structural transformation in Africa, since government consumption has the second largest impact on manufacturing valued added.

The factors affecting fiscal performance are interconnected and thus require a holistic policy

framework to address them. The rest of the report examines in detail the performance, challenges and opportunities related to tax revenue mobilization (chapter 3), non-tax sources of revenue (chapter 4), tax policy and tax administration (chapter 5), efforts to tax multinational enterprises (chapter 6) and the role of fiscal policy in macroeconomic management and debt sustainability (chapter 7). Chapter 8 summarizes the key issues and findings of the report and proposes a policy framework for African countries that can enhance the efficiency and effectiveness of fiscal policy in financing development.



African governments should not take part in the ongoing global race to the bottom, as countries rush to cut corporate taxes to enhance competitiveness and attract investment.



ANNEX

TABLE A2.1. CORRELATION COEFFICIENTS OF GROWTH IN GOVERNMENT EXPENDITURE AND REAL GDP GROWTH IN AFRICA, 1980-2015

COUNTRY	COEFFICIENT
Algeria	-0.44
Angola	-0.10
Benin	0.31
Botswana	-0.03
Burkina Faso	-0.18
Burundi	-0.08
Cabo Verde	0.35
Cameroon	-0.41
Central African Rep.	0.47**
Chad	-0.23
Comoros	-0.19
Côte d'Ivoire	-0.17
Dem. Rep. of the Congo	0.08
Egypt	0.46*
Equatorial Guinea	-0.16
Eswatini	0.29*
Ethiopia	-0.34*
Gabon	0.13
Gambia	0.01
Ghana	0.50***
Guinea	0.21
Guinea Bissau	0.24
Kenya	-0.16

COUNTRY	COEFFICIENT
Lesotho	-0.19
Madagascar	0.46***
Malawi	0.37
Mali	-0.22
Mauritania	0.22
Mauritius	-0.28
Morocco	-0.46**
Mozambique	-0.17
Namibia	0.24
Niger	-0.15
Nigeria	-0.72***
Rwanda	0.47**
Senegal	0.12
Seychelles	0.32*
South Africa	0.25
Sudan	-0.02
Tanzania	-0.01
Togo	-0.26
Tunisia	-0.22
Uganda	-0.31
Zambia	-0.38
Zimbabwe	-0.64**

Note: * $p < 0.1$; ** $p < 0.05$; *** $p < 0.01$.

TABLE A2.2. REVENUE SIDE OF THE INVESTMENT MODEL:
DEPENDENT VARIABLE — GROSS CAPITAL FORMATION (% OF GDP)

VARIABLE	EQUATION 1	EQUATION 2	EQUATION 3	EQUATION 4	EQUATION 5	EQUATION 6	EQUATION 7
Total government revenue (% of GDP)	−0.0317	—	—	—	—	—	—
Total tax revenue (% of GDP)	—	−0.0478**	—	—	—	—	0.0037
Total non-tax revenue (% of GDP)	—	0.0233	—	—	—	—	—
Direct tax revenue (% of GDP)	—	—	−0.0150***	—	—	—	—
Indirect tax revenue (% of GDP)	—	—	—	0.0137	—	—	—
Tax on international trade (% of GDP)	—	—	—	—	0.0856***	—	—
Tax on goods and services (% of GDP)	—	—	—	—	−0.0782***	—	—
Tax on income, profits, capital gains (% of GDP)	—	—	—	—	—	−0.0230***	—
Indirect tax revenue (% of total tax revenue)	—	—	—	—	—	—	0.0359*
Lending interest rate (%)	−0.0090***	0.0002	−0.0076***	−0.0057***	−0.0086***	−0.0069**	−0.0061***
Trade openness (% of GDP)	0.3767***	0.4334***	0.4343***	0.3832***	0.4005***	0.4288***	0.3595***
GDP growth (%)	0.1169***	0.0705***	0.0541***	0.0917***	0.0761***	0.0706***	0.0791***
Constant	0.4145***	0.3878***	0.3570***	0.4076***	0.4219***	0.3553***	0.4900***
Error correction term (speed of adjustment)	−0.2869***	−0.3248***	−0.3181***	−0.2744***	−0.2861***	−0.3070***	−0.2896***
Number of observations	1,083	1,081	1,083	1,083	1,078	1,082	1,082
Log likelihood	726.59	752.00	687.18	699.28	741.16	692.62	736.16

Note: The regression results are based on panel autoregressive distributed lag autoregressive distributed lag model estimation for 45 African countries using pooled mean group technique.

* $p < 0.1$; ** $p < 0.5$; *** $p < 0.01$.

TABLE A2.3. EXPENDITURE SIDE OF THE INVESTMENT MODEL:
DEPENDENT VARIABLE—GROSS CAPITAL FORMATION (% OF GDP)

VARIABLE	LONG-RUN COEFFICIENTS						
	EQUATION 1	EQUATION 2	EQUATION 3	EQUATION 4	EQUATION 5	EQUATION 6	EQUATION 7
Total government expenditure (% of GDP)	0.0357***	—	—	—	—	0.1323***	0.0307***
Government consumption expenditure (% of GDP)	—	0.2913***	—	—	—	—	—
Government health expenditure (% of GDP)	—	—	0.0642***	—	—	—	—
Government education expenditure (% of GDP)	—	—	—	0.162**	—	—	—
Government military expenditure (% of GDP)	—	—	—	—	0.0024	—	—
Government health expenditure (% of government expenditure)	—	—	—	—	—	0.1352***	—
Government education expenditure (% of government expenditure)	—	—	—	—	—	—	0.0159***
Total debt (% of GDP)	-0.0284***	-0.0189***	-0.0548***	-0.0128**	-0.0178***	-0.0951***	-0.0171***
Trade openness (% of GDP)	0.6803***	0.6676***	0.6549***	0.6668***	0.7156***	0.4041***	0.6380***
GDP growth (%)	0.0520***	0.0694**	0.0627***	0.0639***	0.0588***	0.0693***	0.0653***
Constant	0.0200	-0.1189***	0.1474***	0.028***	0.0168	0.4719***	0.1148***
Error correction term (speed of adjustment)	-0.2998***	-0.2501***	-0.3346***	-0.3046***	-0.2812***	-0.2796***	-0.3123***
Number of observations	1,064	1,064	1,064	1,064	1,064	1,079	1,079
Log likelihood	579.27	685.24	579.24	568.73	560.18	696.66	683.75

Note: The regression results are based on panel autoregressive distributed lag model estimation for 45 African countries using pooled mean group technique.

* $p < 0.1$; ** $p < 0.5$; *** $p < 0.01$.

TABLE A2.4. REVENUE SIDE OF THE GROWTH MODEL: DEPENDENT VARIABLE—REAL GDP PER CAPITA

VARIABLE	LONG-RUN COEFFICIENTS						
	EQUATION 1	EQUATION 2	EQUATION 3	EQUATION 4	EQUATION 5	EQUATION 6	EQUATION 7
Total government revenue (% of GDP)	0.9941***	—	—	—	—	—	—
Total tax revenue (% of GDP)	—	0.6377***	—	—	—	—	0.1576
Total non-tax revenue (% of GDP)	—	0.7113***	—	—	—	—	—
Direct tax revenue (% of GDP)	—	—	0.4750**	—	—	—	—
Indirect tax revenue (% of GDP)	—	—	—	0.3159***	—	—	—
Tax on international trade (% of GDP)	—	—	—	—	-0.4657***	—	—
Tax on goods and services (% of GDP)	—	—	—	—	0.3831***	—	—
Tax on income, profits and capital gains (% of GDP)	—	—	—	—	—	0.4059***	—
Indirect tax revenue (% of total tax revenue)	—	—	—	—	—	—	-0.5931***
Private investment (% of GDP)	1.3428***	1.6169***	1.7642***	1.6537***	1.7099***	1.5391***	1.6471***
Population growth (%)	-0.4405**	-0.3447	0.5043	-0.4097*	-0.4312***	-0.4484***	-0.3733**
Constant	0.0727***	0.0884**	0.0481***	0.0678***	0.1355**	0.1066***	0.0423*
Error correction term (speed of adjustment)	-0.0094***	-0.0079**	-0.0072***	-0.0102***	-0.0218**	-0.0136***	-0.0077**
Number of observations	1,485	1,478	1,486	1,485	1,481	1,485	1,481
Log likelihood	2,953.01	3,002.42	2,929.39	2,920.30	2,950.87	2,917.31	2,996.03

Note: The regression results are based on panel autoregressive distributed lag model estimation for 45 African countries using pooled mean group technique.

* $p < 0.1$; ** $p < 0.5$; *** $p < 0.01$.

TABLE A2.5. EXPENDITURE SIDE OF THE GROWTH MODEL: DEPENDENT VARIABLE—REAL GDP PER CAPITA

VARIABLE	EQUATION 1	EQUATION 2	EQUATION 3	EQUATION 4	EQUATION 5
Total government expenditure (% of GDP)	0.3399***	—	—	—	—
Government consumption expenditure (% of GDP)	—	0.0899	—	—	—
Government health expenditure (% of GDP)	—	—	0.1931***	—	—
Government education expenditure (% of GDP)	—	—	—	0.1355***	—
Government military expenditure (% of GDP)	—	—	—	—	-0.1387*
Private investment (% of GDP)	1.713***	1.7322***	1.0576***	1.4788***	1.4081***
Population growth (%)	-0.5307*	-0.6542***	-0.2044	-0.6551***	-0.5765***
Constant	0.05351***	0.0722***	0.1188***	0.0708***	0.0821***
Error correction term (speed of adjustment)	-0.0094***	-0.0255***	-0.0181***	-0.0116***	-0.0136***
Number of observations	1,485	1,485	1,485	1,485	1,485
Log likelihood	2,916.67	2,931.02	2,919.56	2,893.43	2,908.81

Note: The regression results are based on panel autoregressive distributed lag model estimation for 45 African countries using pooled mean group technique.

* $p < 0.1$; ** $p < 0.5$; *** $p < 0.01$.

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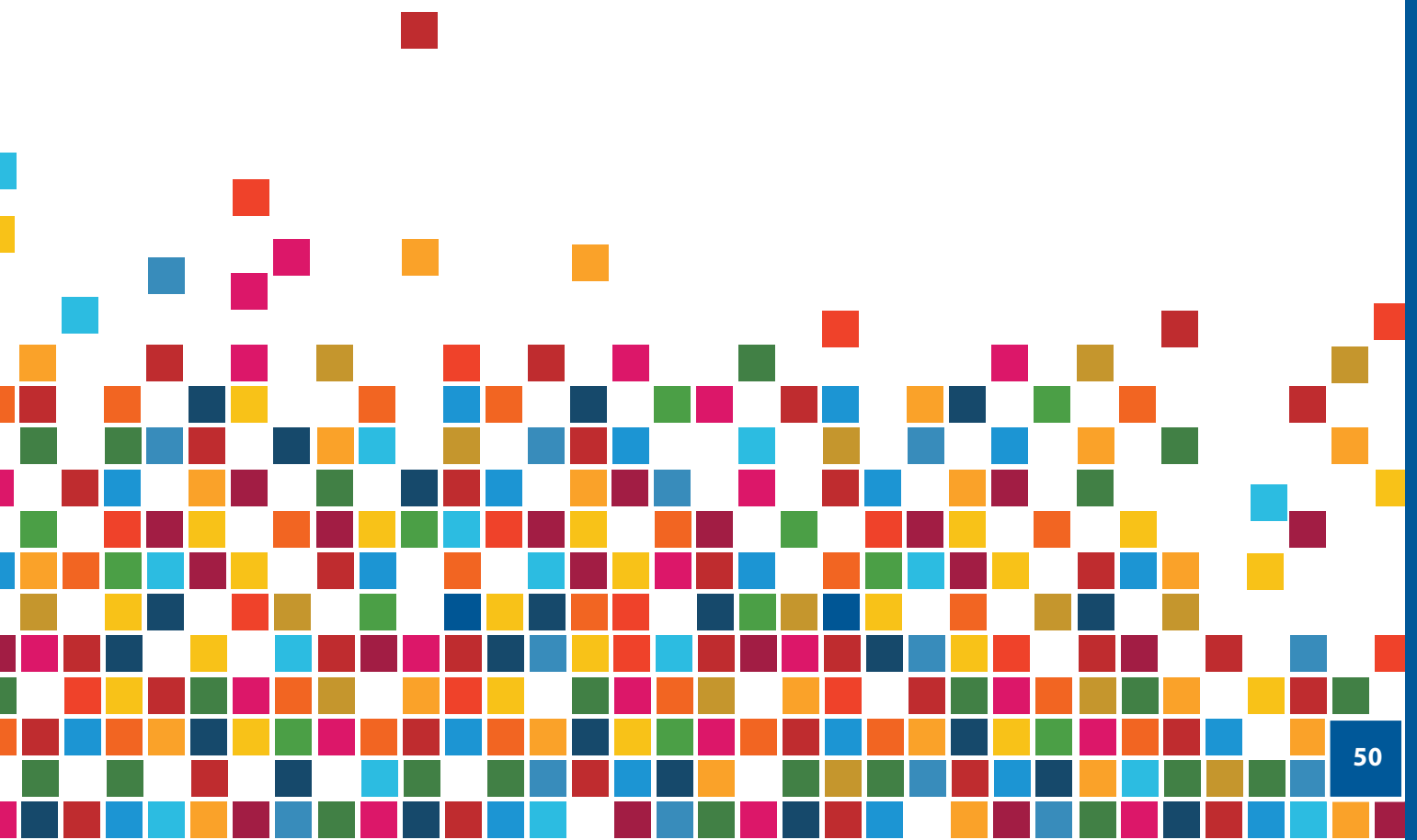
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CHAPTER 3


TAX POLICY AND PERFORMANCE IN AFRICA



Africa has a low tax capacity (ability to collect taxes) of about 20 per cent of GDP and a lower tax revenue to GDP ratio (17 per cent) than other regions, largely because of inefficiencies in tax policy and revenue collection. Thus, addressing tax capacity constraints and collection inefficiencies could boost tax revenue in Africa by 3 per cent of GDP (the difference between the current tax ratio and tax capacity).

Collection efficiency for the value-added tax (VAT) in many African countries is less than 50 per cent, and property and wealth taxation are still un-tapped sources of revenue.

Improving tax governance by combating corruption and bolstering accountability could reduce inefficiencies and, on average, mobilize up to \$72 billion a year—about a third of the estimated average investment financing gap of \$230 billion for achieving the Sustainable Development Goals (SDGs) and Agenda 2063 in Africa.



Africa's weighted average ratio of taxes to GDP was 17 per cent over 2000–2018.

INTRODUCTION

Tax policy—the instruments governments use to raise revenue by taxing economic activities—is an important revenue component of fiscal policy. It is also sensitive to microeconomic aspects of fairness (who to tax and how much) and allocative efficiency (which taxes will minimize the distortions in economic activity) to support higher economic growth. Tax policy in Africa focuses on scaling up domestic revenue mobilization to enable countries to implement development strategies to achieve the SDGs and the aspirations of Agenda 2063.

This chapter explores how to leverage tax policy to raise more revenue for financing sustainable development in Africa. It takes stock of tax policy since 2000, draws lessons from tax policy reforms in Africa and best practices around the world and examines the tax system and the performance of different taxes. It also identifies what needs to be done to increase tax revenue to finance sustainable development.

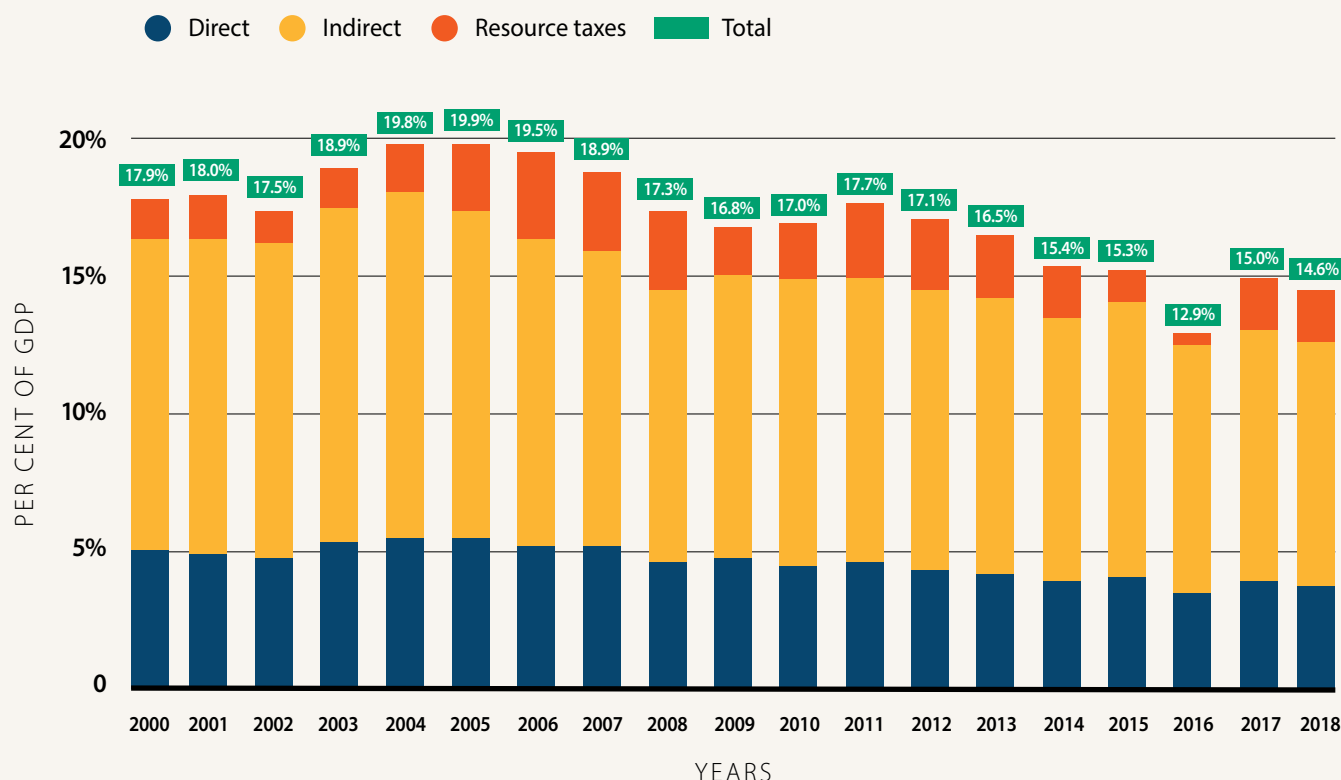
TRENDS IN TAX POLICY AND PERFORMANCE

Africa's weighted average tax to GDP ratio was 17 per cent over 2000–2018.¹ It improved from 17.9 per cent in 2000 to 19.9 per cent in 2005, the period high, but has since trended downwards, reaching its lowest level of 12.9 per cent in 2016 and was 14.6 per cent in 2018 (figure 3.1). This trend was reflected in both direct taxes and indirect taxes, which peaked at 5.5 per cent and 12.6 per cent, respectively, in 2004. Resource

1 The analysis in this chapter is based on data from the Government Revenue Dataset, compiled by the International Centre for Tax and Development and United Nations University World Institute for Development Economics Research from multiple sources and last accessed in November 2018 (ICTD and UNU-WIDER, 2018). As of November 2018, the data set covered up to 2016, so data for 2017 and 2018 are forecast. Not all countries had a full set of data, and therefore data on some variable are averages of the available data.



FIGURE 3.1. TRENDS IN TAX REVENUE AND IT COMPONENTS IN AFRICA, 2000-2018



Note: Data are estimated for 2017 and 2018.

Source: Based on data from ICTD and UNU-WIDER (2018), accessed in November 2018

taxes followed the same general trend, rising from 1.5 per cent in 2000 and peaking at 3.2 per cent in 2006, before gradually falling to 0.35 per cent in 2016, with a slight recovery to 1.9 per cent in 2017 and 2018.

Tax revenue declined over this period, with the continental weighted tax ratio averaging 17 per cent of GDP, well below the 20 per cent ratio needed to help countries fast track achievement of the SDGs.

The overall decline in the weighted average tax revenue to GDP ratio for Africa between 2000 and 2018 reflected drops in 29 of 51 countries with data, including major economies such as Angola, Ethiopia, Kenya, Morocco and Nigeria. However, in a subgroup of 19 countries, the number of countries with a tax revenue to GDP ratio of at

least 10 per cent increased from 9 in 2000 to 16 in 2018 (table 3.1). Between 2000 and 2018, four countries (Democratic Republic of the Congo, Eswatini, Malawi and Mozambique) increased their ratio by at least 10 percentage points, and seven countries (Congo, Gambia, Guinea, Namibia, Rwanda, Tanzania and Togo) increased it by 5–9 per cent. Twelve countries had an average tax revenue to GDP ratio of at least 10 per cent over 2000–2008, compared with 16 over 2009–2018, with Mozambique (9.6 per cent), Malawi (6 per cent) and Namibia (5.5 per cent) recording the largest increases between the two periods.

Furthermore, whereas only 3 of the 19 countries (Eswatini, 18 per cent; Namibia, 26 per cent; and Senegal, 16 per cent) had a tax to GDP ratio of at least 15 per cent in 2000, 12 of them did so by 2018 suggesting potential for many African countries

TABLE 3.1. IMPROVEMENTS IN AVERAGE WEIGHTED RATIOS OF TAX REVENUE TO GDP
IN 22 AFRICAN COUNTRIES BETWEEN 2000–2004 AND 2014–2018

COUNTRY	WEIGHTED TAX TO GDP RATIOS (%)		2000 - 2018 INCREASE (PERCENTAGE POINT)	AVERAGE WEIGHTED TAX TO GDP RATIOS (%)		INTER-PERIOD INCREASE (PERCENTAGE POINT)
	2000	2018		2000 - 2008 <i>Fast growth</i>	2009 - 2018 <i>Post crisis</i>	
Burkina Faso	11	15	4	12	14	2.0
Cameroon	11	13	2	11	12	0.9
Chad	6	6	0	5	6	0.8
Congo, Dem. Rep.	1	12	11	5	10	4.6
Congo	6	11	5	8	10	2.7
Côte d'Ivoire	14	15	1	14	15	0.7
Eswatini	18	31	13	22	26	4.2
Gambia	11	17	6	12	15	3.1
Guinea	8	16	8	9	14	4.7
Guinea-Bissau	7	9	3	5	8	2.9
Malawi	8	18	10	10	16	6.0
Mozambique	9	23	14	10	20	9.6
Namibia	26	34	8	25	31	5.5
Niger	8	13	4	10	12	1.5
Rwanda	10	15	5	11	14	2.5
Senegal	16	20	4	18	19	1.6
Sudan	5	7	2	6	7	0.2
Tanzania	7	13	6	8	11	3.1
Togo	11	20	9	14	18	3.8

Note: Data are estimated for 2017 and 2018.

Source: Based on data from ICTD and UNU-WIDER (2018), accessed in November 2018.

to make progress towards the goal of 20 per cent (Coulibaly and Gandhi, 2018).

While the number of countries with an average tax revenue to GDP ratio of more than 20 per cent remained stable at 9 between 2000–2008 and 2009–2018 (figure 3.2), some countries increased their tax revenue collection despite the declining growth trend from 2009 onwards. The number of countries with a tax revenue to GDP ratio of 0–10 per cent decreased from 15 over 2000–2008 to 9 over 2009–2018, while the number with a ratio of 10–20 per cent increased from 26 to 33 over the same periods.

STRUCTURE OF THE TAX SYSTEM AND PERFORMANCE OF TAX TYPES

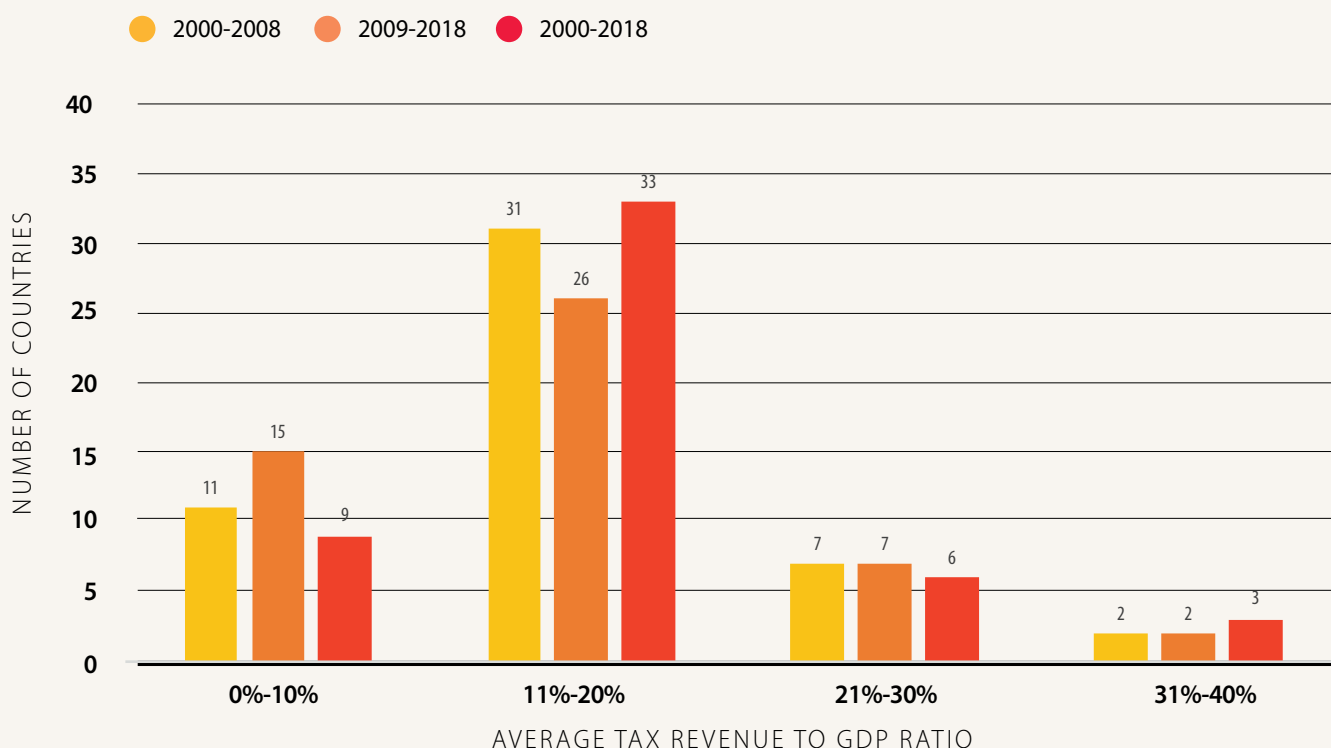
The primary function of the tax system is to generate revenue for the government while ensuring economic efficiency and easing the tax burden on the poorest segments of society through tax structures with some progressivity. Tax structures influence the incidence of each type of tax. Having an efficient tax system is a key consideration in achieving Agenda 2063 and the SDGs.

Taxes include direct taxes and indirect taxes. The main components of direct taxes are taxes on individual and corporate income, payroll and workforce taxes, and property taxes. The main components of indirect taxes are taxes on goods and services (sales taxes, VAT, turnover taxes and taxes on financial and capital transactions), excise duties and international trade taxes. How various tax components perform over time can inform the tax policy debate by revealing the evolution of tax structures and the contribution of each tax type to government revenue.

Emerging from a prolonged period of stagnant economic growth in the 1980s and early 1990s, and encouraged by signs of positive growth in the late 1990s, African countries entered the 21st century determined to improve their tax revenue collection by introducing tax reforms.

Tax revenue rose over 2000–2004 (table 3.2). Revenue from direct taxes as a share of GDP barely rose from 5.0 per cent in 2000 to peak at 5.5 per cent in 2004 before gradually declining to 3.5 per cent in 2016; it is estimated to have increased to 3.9 per cent in 2017 and 3.7 per cent in 2018. Revenue from indirect taxes as a share of GDP followed the same pattern, rising from 11.4 per cent in 2000 to peak at 12.6 per cent in 2004, then dropping gradually to 9.0 per cent in 2016, with modest improvement to 9.3 per cent in 2017. Revenue from resource taxes as a share of GDP began at 1.5 per cent in 2000, peaking later than other tax types at 3.2 per cent in 2006 and falling gradually at first, to 2.3 per cent in 2013, then rapidly to 0.3 per cent in 2016, before recovering to 1.9 per cent in 2017 and 2018, reflecting the impact of the slump in commodity prices that began in 2014. The performance of individual components of each tax type varied, however.

FIGURE 3.2. DISTRIBUTION OF AFRICAN COUNTRIES BY AVERAGE TAX REVENUE TO GDP RATIO, 2000–2008, 2009–2018 AND 2000–2018



Note: Data are estimated for 2017 and 2018.

Source: Based on data from ICTD and UNU-WIDER (2018), accessed in November 2018

TABLE 3.2. TRENDS IN TAX REVENUE BY TAX TYPE AND COMPONENT, 2000-2018 (PER CENT OF GDP)

	DIRECT TAXES				INDIRECT TAXES					RESOURCE TAXES
	Personal income	Corporate income	Payroll and workforce	Property taxes	Goods and services	VAT	Excise duties	International trade	Other taxes	
2000	3.01%	1.64%	0.05%	0.30%	5.13%	1.98%	1.23%	2.52%	0.50%	1.52%
2001	2.85%	1.81%	0.07%	0.22%	5.17%	2.07%	1.19%	2.52%	0.53%	1.55%
2002	2.67%	1.82%	0.07%	0.22%	5.26%	2.39%	1.28%	2.13%	0.38%	1.25%
2003	2.96%	2.03%	0.10%	0.31%	5.66%	2.76%	1.36%	2.03%	0.38%	1.36%
2004	3.05%	2.08%	0.10%	0.28%	5.79%	3.01%	1.35%	2.00%	0.40%	1.72%
2005	2.87%	2.24%	0.09%	0.27%	5.56%	2.93%	1.23%	1.83%	0.41%	2.43%
2006	2.61%	2.34%	0.08%	0.23%	5.18%	2.79%	1.12%	1.70%	0.33%	3.17%
2007	2.53%	2.32%	0.07%	0.23%	5.20%	2.72%	1.02%	1.59%	0.26%	2.93%
2008	2.15%	2.20%	0.06%	0.18%	4.86%	2.45%	0.90%	1.47%	0.25%	2.82%
2009	2.31%	2.10%	0.07%	0.27%	5.10%	2.44%	1.08%	1.44%	0.28%	1.74%
2010	2.31%	1.90%	0.07%	0.25%	5.29%	2.62%	0.98%	1.31%	0.22%	2.02%
2011	2.33%	1.98%	0.08%	0.28%	5.21%	2.58%	1.01%	1.31%	0.22%	2.66%
2012	2.21%	1.77%	0.08%	0.26%	5.00%	2.50%	0.98%	1.42%	0.25%	2.65%
2013	2.15%	1.74%	0.07%	0.24%	4.96%	2.46%	0.95%	1.36%	0.30%	2.28%
2014	2.14%	1.47%	0.07%	0.24%	4.75%	2.31%	0.87%	1.33%	0.29%	1.95%
2015	2.25%	1.47%	0.08%	0.25%	5.05%	2.31%	1.02%	1.33%	0.29%	1.22%
2016	1.98%	1.24%	0.06%	0.22%	4.74%	2.02%	0.98%	1.05%	0.24%	0.35%
2017f	1.93%	1.62%	0.07%	0.24%	4.85%	2.41%	0.87%	0.94%	0.19%	1.93%
2018f	1.87%	1.53%	0.07%	0.24%	4.77%	2.32%	0.84%	0.86%	0.18%	1.86%

Note: Data are estimated for 2017 and 2018.

Source: Based on data from ICTD and UNU-WIDER (2018), accessed in November 2018.

Among direct taxes, revenue from personal income taxes as a share of GDP declined almost continuously, from 3.0 per cent in 2000 to 1.9 per cent in 2018, indicating low personal income tax responsiveness to the robust economic growth on the continent. Revenue from corporate income taxes as a share of GDP rose initially, from 1.6 per cent in 2000 to 2.3 per cent in 2006, before gradually declining to 1.5 per cent in 2018. Revenue from payroll and workforce taxes (about 0.1 per cent of GDP over 2000–2018) and property taxes (about 0.2–0.3 per cent) has been largely inconsequential. If properly harnessed by expanding the tax base, these last two components could increase tax revenue.

Nearly all indirect taxes followed the same pattern: a brief rise until 2003 or 2004 and then a gradual decline. Revenue from taxes on goods and services

as a share of GDP rose slightly, from 5.1 per cent in 2000 to 5.8 per cent in 2004, and then gradually declined to its lowest level in 2016, at 4.7 per cent. Similarly, VAT revenue as a share of GDP rose from 2.0 per cent in 2000 to 3.0 per cent in 2004, before drifting down to 2.0 per cent in 2016. Revenue from excise duties as a share of GDP rose from 1.2 per cent in 2000 to a high of 1.4 in 2003 and declined thereafter, dwindling to 1 per cent in 2016. For revenue from international trade taxes and other taxes, the decline began earlier. Trade tax revenue as a share of GDP dropped from a high of 2.5 per cent in 2000 to 1 per cent in 2016, while other tax revenue as a share of GDP dropped from a high of 0.5 per cent in 2000 to 0.2 per cent in 2016.

Resource tax revenues marginally declined from 1.5 per cent of GDP in 2000 to 1.2 per cent in 2002, and gradually rose to 3.2 per cent by 2006, before falling

to 1.7 per cent in 2009. They improved to 2.7 per cent of GDP in 2011 and 2012 and fluctuated widely before stabilizing at 1.9 per cent of GDP in 2017 and 2018 thanks to improvement in commodity prices.

Tax structures varied across countries over 2000–2018. In a sample of 12 African countries, taxes on goods and services were the principal source of tax revenue in 9 countries (Benin, Egypt, Mauritius, Morocco, Rwanda, Senegal, Seychelles, Tunisia and Zimbabwe), while trade taxes dominated in two (Eswatini and Namibia) (figure 3.3). Revenue from taxes on goods and services as a share of GDP was at least 5.0 per cent in all countries except Eswatini (3.0 per cent) and Sierra Leone (3.0 per cent). Revenue from personal income taxes as a share of GDP was at least 4 per cent in five countries but was only 1 per cent in Egypt and Seychelles. Revenue from

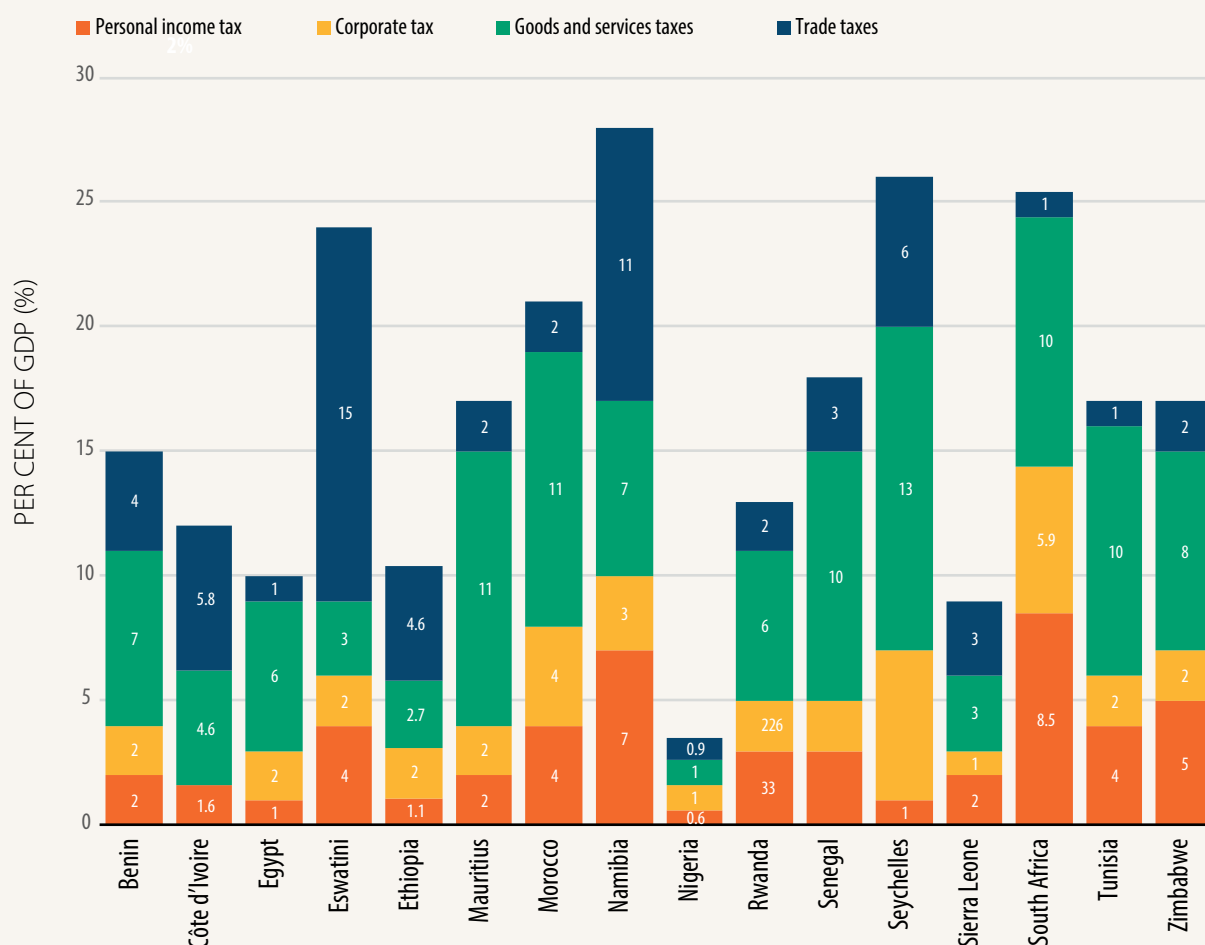
corporate taxes as a share of GDP was 2 per cent or less in most countries except Seychelles (6 per cent), Morocco (4 per cent) and Namibia (3 per cent).

These variations in tax structure underscore the importance of tailoring tax reforms and tax structures to country conditions when the aim is to improve tax mobilization.

TAX POLICY REFORMS AND IMPACTS

Since 2000 several African countries have reformed their tax policy and tax administration to mobilize additional revenue for development. Tax policy reforms included adjusting tax rates and broadening the tax base. Key reforms in the administration

FIGURE 3.3. AVERAGE TAX STRUCTURES IN SELECTED AFRICAN COUNTRIES, 2000–2018



Note: Data are estimated for 2017 and 2018.

Source: Based on data from ICTD and UNU-WIDER (2018), accessed in November 2018.

of taxes included integrating revenue collection responsibilities within a single agency, often a semi-autonomous revenue authority (Moore, 2013), and promoting compliance among taxpayers (discussed in chapter 5).

ADJUSTING TAX RATES

A number of African countries reduced tax rates, in line with the warnings in the Laffer curve literature about the detrimental revenue effect of excessively high tax rates (see, for instance, Laffer, 2004; Khaldun, 1967; Wanniski, 1978).² Countries made other adjustments as well.

To encourage investment, some African countries reduced or simplified the corporate income tax rate. In 2006 Lesotho reduced the standard corporate income tax rate from 35 per cent to 25 per cent and the rate for manufacturers from 15 per cent to 10 per cent to encourage private sector growth (ATAF, 2017). Revenue from corporate income taxes rose from 1.7 per cent of GDP in 2006 to 2.1 per cent in 2007 and to 4 per cent in 2009.

In 2015, Egypt replaced its two-tier corporate tax system with a single tax of 22 per cent (ATAF, 2017)³. Tanzania began modernizing its tax system and tax administration in 2004, which has improved tax revenue collection and increased e-filing (see box 3.1). And in 2017, Tanzania reduced the corporate income tax rate for assemblers of vehicles, tractors and fishing boats from 30 per cent to 10 per cent for the first five years of operations to encourage manufacturing growth. In 2018 Kenya reduced the corporate income tax rate for property developers who construct more than 400 housing units and for vehicle assemblers from 30 per cent to 15 per cent (ATAF, 2017). It is too early to determine the impact of these reforms.

Countries have also reformed personal income taxes. In 2017, South Africa increased the marginal income tax rate for individuals from 41 per cent to 45 per cent. To cushion taxes against the effects of inflation, South Africa regularly reviews personal income tax brackets and tax relief measures; recent reviews were conducted in 2013 and 2016 (National Treasury and SARS, 2016). A 2013 reform resulted in revenue from personal income taxes as a share of GDP increasing from 8.9 per cent in 2013 to 9.8 per cent in 2016. Other countries have lowered rates. To

2 The Laffer curve expresses the relationship between tax rates and tax revenue as a trade-off between higher tax rates and higher revenue, showing that there is a point on the curve at which raising the tax rate lowers rather than increases overall revenue; if the tax rate is higher than that rate, cutting it would increase revenue collection (Laffer, 2004).

3 In 2018, the average statutory corporate tax rates ranged from 18.4 per cent in Europe, 21.6 in EU countries, 23.7 in OECD countries, 23 per cent across all 208 jurisdictions, to 28.8 per cent in Africa (Tax Foundation, 2018) (see annex 3.2).

BOX 3.1. LESSONS FROM TANZANIA ON INTEGRATED TAX REFORM

Tanzania's debt was increasing while tax revenue collection remained low, at 10.8 per cent of GDP in 2005 (World Bank, 2017). With the support of the World Bank, Tanzania embarked on the Tax Modernization Project to improve the efficiency and effectiveness of tax administration by the Tanzania Revenue Authority by (IEG, 2012):

- Building the capacity of tax administrators.

- Educating taxpayers on how to file and pay taxes.
- Training staff to avoid corruption.
- Automating systems for registering, documenting and collecting taxes.
- Introducing an e-filing system.
- Creating stronger infrastructure for monitoring and evaluation (using two digital forensics laboratories to enhance the capacity of the tax investigation unit; World Bank, 2017).

As a result of these measures:

- Revenue collection improved on average by 21 per cent over 2007–2011.
- E-filing of value-added taxes increased from less than 500 in 2009 to over 4,000 in 2011.
- A new mobile tax payment system for property taxes registered 376,666 taxpayers in 2011.

Tanzania embarked on the Tax Modernization Project to improve the efficiency and effectiveness of tax administration.

make personal income tax rates more progressive, Kenya reviewed and increased the number of bands and increased the personal relief rates (thresholds for tax liability) by 10 per cent in 2016 and 2017 (Government of Kenya, 2016). In 2018 Mauritius reduced the personal income tax rate from 15 per cent to 10 per cent for income below \$18,840 a year (Government of Mauritius, 2018). It is too short to assess the impact of the reforms in Kenya and Mauritius.

BROADENING THE TAX BASE

To increase domestic revenue mobilization, several African countries have implemented measures to broaden the tax base by introducing or adjusting capital gains taxes or consumption taxes.

Many African countries have some form of capital gains tax. Some countries exempt capital gains from listed securities and apply a reduced rate to gains on unlisted shares. For example, South Africa introduced a capital gains tax in 2001, while Kenya, following many unsuccessful attempts, reintroduced the tax in 2015 after a 30-year suspension (Government of Kenya, 2014).

Goods and services (sales) taxes, the principal source of tax revenue in many countries, have undergone many reforms since 2000, ranging from introducing the VAT to replace those taxes to adjusting VAT rates. Botswana introduced a 10 per cent VAT in April 2002 and then raised it to 12 per cent in April 2010 following the financial crisis (Bakwena, 2012). Rwanda and Egypt replaced sales taxes with a VAT. Rwanda replaced the 15 per cent sales tax in 2001 with a 15 per cent VAT and then raised it to 18 per cent in 2002 (Government of Rwanda, 2001); VAT revenue rose from 3.2 per cent of GDP in 2001 to 4.7 per cent in 2016. Egypt replaced its 10 per cent goods and services tax with a 13 per cent VAT in 2016 and raised it to 14 per cent in 2017 (Rahman, 2017).

VAT revenue as a share of continental GDP barely increased between 2000 and 2018, from 2 per cent to 2.3 per cent, and increased by at least a percentage point in 11 of the 30 African countries with available data (table 3.3). It increased the most in Mauritania (7.3 percentage points), Benin (3.8 per cent), Guinea (3.3 per cent), Burkina Faso (3.4 per cent) and Ghana (2.6 per cent).

TABLE 3.3. REVENUE FROM VALUE ADDED TAXES AS A SHARE OF GDP, 2000–2018 (%)

COUNTRY	2000	2008	2018F
Benin	3.8	6.8	7.6
Burkina Faso	3.3	4.8	6.7
Cameroon	4.4	5.3	6.0
Cabo Verde		8.7	4.7
Central African Republic		2.4	
Côte d'Ivoire	3.8		0.6
Dem. Rep. of the Congo			4.2
Gabon	1.9	1.2	1.9
Ghana	2.9	4.3	5.5
Guinea	1.6		4.9
Kenya	3.8	4.6	3.2
Lesotho		6.2	7.3
Madagascar		2.2	6.3
Malawi	2.9		4.6
Mali	3.9	4.4	5.3
Mauritania	2.8		10.1
Morocco		8.5	9.3
Mozambique	4.0		5.2
Nigeria	0.8	1.0	0.9
Rwanda		4.4	5.0
Senegal	6.6	7.3	7.6
Seychelles		10.3	9.3
South Africa	5.8	6.5	7.0
Sudan	0.5		2.7
Tanzania	2.7	3.2	2.9
Togo		6.4	9.6
Tunisia	6.1	6.0	6.0
Uganda	3.2	3.5	3.6
Zambia		3.3	3.3
Zimbabwe		0.5	8.7
Africa	2.0	2.4	2.3

Note: Data are estimated for 2017 and 2018.

Source: Based on data from ICTD and UNU-WIDER (2018), accessed in November 2018.

Tax avoidance and evasion—by taking advantage of loopholes or exceptions, liberally interpreting tax codes or even falsifying invoices—results in large losses in tax revenue in Africa.

Lesotho replaced the sales tax with the VAT in 2003 to stop the abuse of tax exemption certificates and close loopholes used by suppliers to evade sales taxes (Koatsa and Nchake, 2017). VAT revenue rose from 5.9 per cent of GDP in 2003 to 7.5 per cent in 2014 before drifting down to 6.7 per cent in 2016. Other countries focused on adjusting VAT rates and the list of exemptions or zero-rated products. Kenya reduced VAT rates from 18 per cent to 16 per cent in 2003, and in 2013 it overhauled the VAT, greatly reducing the list of zero-rated goods and thus the amount of VAT refunds (Government of Kenya, 2013). VAT revenue edged up from 4.3 per cent of GDP in 2002 to 4.4 per cent in 2003 and stayed above the initial level before dropping to 4.3 per cent of GDP in 2012 and then to 3.9 per cent in 2013, prompting a second review of VAT policy that year.

In fiscal year 2018/19, South Africa increased its VAT rate from 14 per cent to 15 per cent, estimating that the resulting additional revenue would finance the newly introduced fee-free tertiary education and training for students from low-income households, among other development policy objectives (SARS, 2018).

TACKLING TAX AVOIDANCE

Tax avoidance and evasion—by taking advantage of loopholes or exceptions, liberally interpreting tax codes or even falsifying invoices—results in large losses in tax revenue in Africa. African countries have been reforming their tax policies to address these issues. For example, to counter tax evasion through invoice mispricing and tax avoidance through profit shifting, several African countries have introduced transfer pricing rules

to ensure the fairness and accuracy of transaction pricing within and between enterprises under common ownership or control.⁴

PERFORMANCE OF TAX REFORMS

While the weighted average tax revenue to GDP ratio for Africa did not change much following these reforms, the number of countries with a ratio below 15 per cent fell by more than half (from 31 countries to 14) between 2000 and 2016. In addition, the number of countries with a ratio above 20 per cent rose from 8 to 11.

Income tax, which increased between 2000 and 2015 by 6.6 percentage points in South Africa, 6.5 percentage points in Rwanda, 5.9 percentage points in Tunisia, 2.6 percentage points in Morocco and 0.6 percentage point in Mauritius, was a key driver of growth in tax revenue (OECD, 2016). This growth was attributed to higher taxes on income and profits, particularly corporate income tax rates.

Box 3.2 illustrates the extensive benefits of tax reforms, particularly simplification of the excise tax structure, in the Philippines. The reforms not only raised additional revenue, but they also contributed to the achievement of several SDGs. African countries could consider similar measures as a vehicle for increasing revenue generation.

⁴ Tax avoidance and tax evasion are discussed in detail in chapter 6.

BOX 3.2. TOBACCO TAXATION AS WIN-WIN: THE CASE OF THE PHILIPPINES

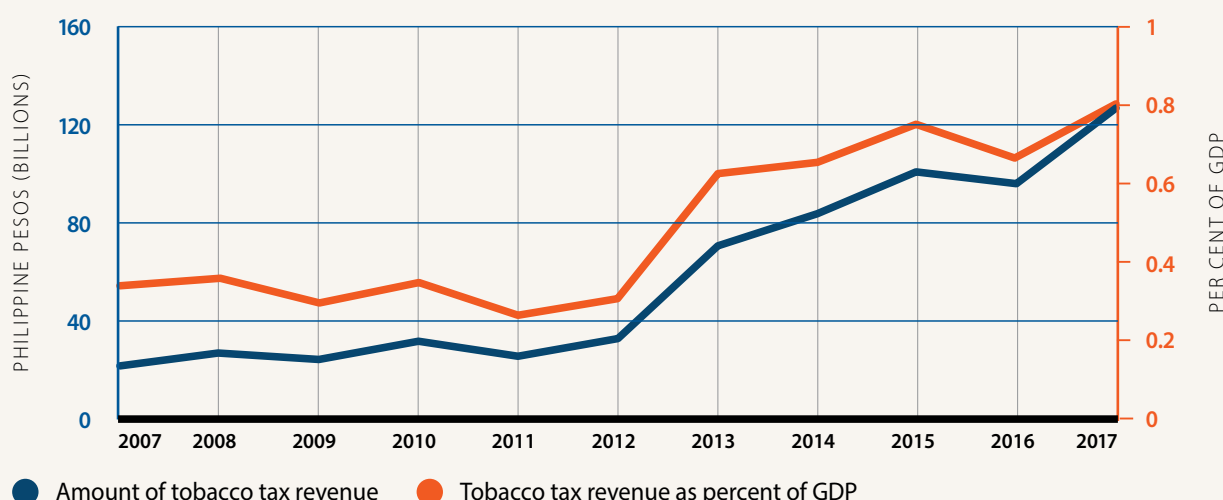
The 2012 Sin Tax Reform Law in the Philippines substantially increased excise taxes and simplified the tax structure for tobacco. The reform resulted in a huge increase in excise revenue, which enabled large increases in the health budget (see box figures 1 and 2). Tobacco excise revenues doubled as a share of GDP after 2012. The higher tax also reduced tobacco use by close to 20 per cent according to the 2015 Global Adult Tobacco Survey. The increased fiscal

space allowed the Philippines to provide fully subsidized health insurance to the poorest 40 per cent of the population, moving the country closer to its declared goal of universal health coverage.

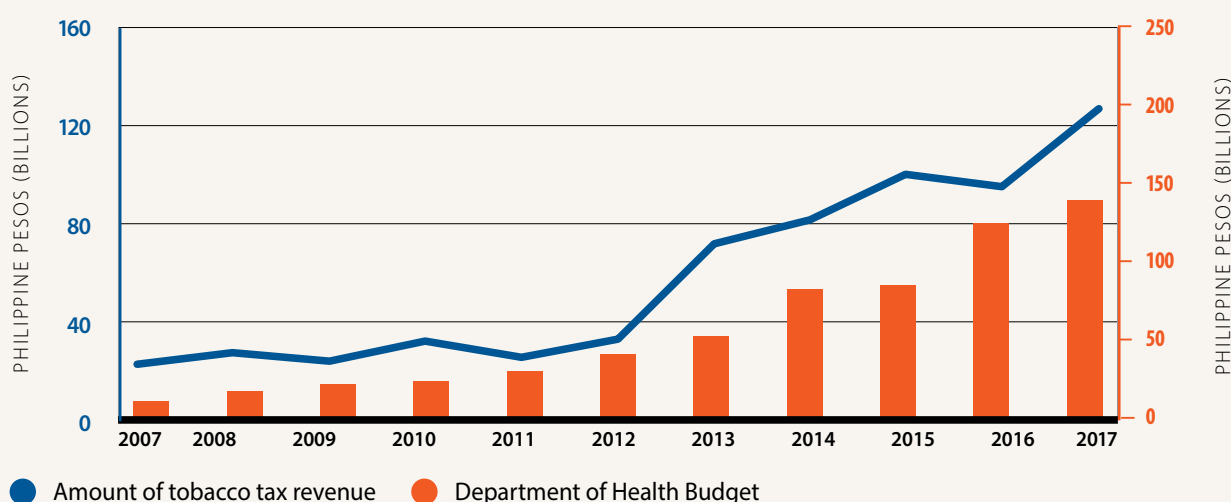
As recognized by the Addis Ababa Action Agenda on Financing for Development, this example shows how countries can use price and tax measures to reduce tobacco consumption and health care costs, while at

the same time generating more revenue to finance development. This win-win reform for public health and domestic resource mobilization did not require a massive amount of resources to achieve. Indeed, tobacco taxation has been highlighted as one of the “Best Buy” interventions by the World Health Organization, recognizing it as a highly cost-effective measure for tobacco control and a revenue source for governments to fund their country’s development priorities.

BOX FIGURE 1 Tobacco excise tax revenues in the Philippines before and after the tax reform of 2012, 2007–2017



BOX FIGURE 2 Philippine Department of Health budget before and after the tax reform of 2012, 2007–2017



Source: Adapted from Kaiser, Bredenkamp and Iglesias (2016), with updated data from the Philippines Department of Finance and Department of Health.

MEASURING AFRICA'S TAX GAP: SELECTED EXAMPLES

Measuring the tax gap—the difference between the amount of taxes paid and the amount that should have been paid during a given year—is challenging. Analysis must contend with the multitude of tax types and national tax systems and the dearth of relevant data (Raczkowski and Mróz, 2016).

THE EXAMPLE OF THE VALUE-ADDED TAX

The VAT, a consumption tax, is used here to illustrate these challenges. The estimates highlight the potential for further resource mobilization in Africa.

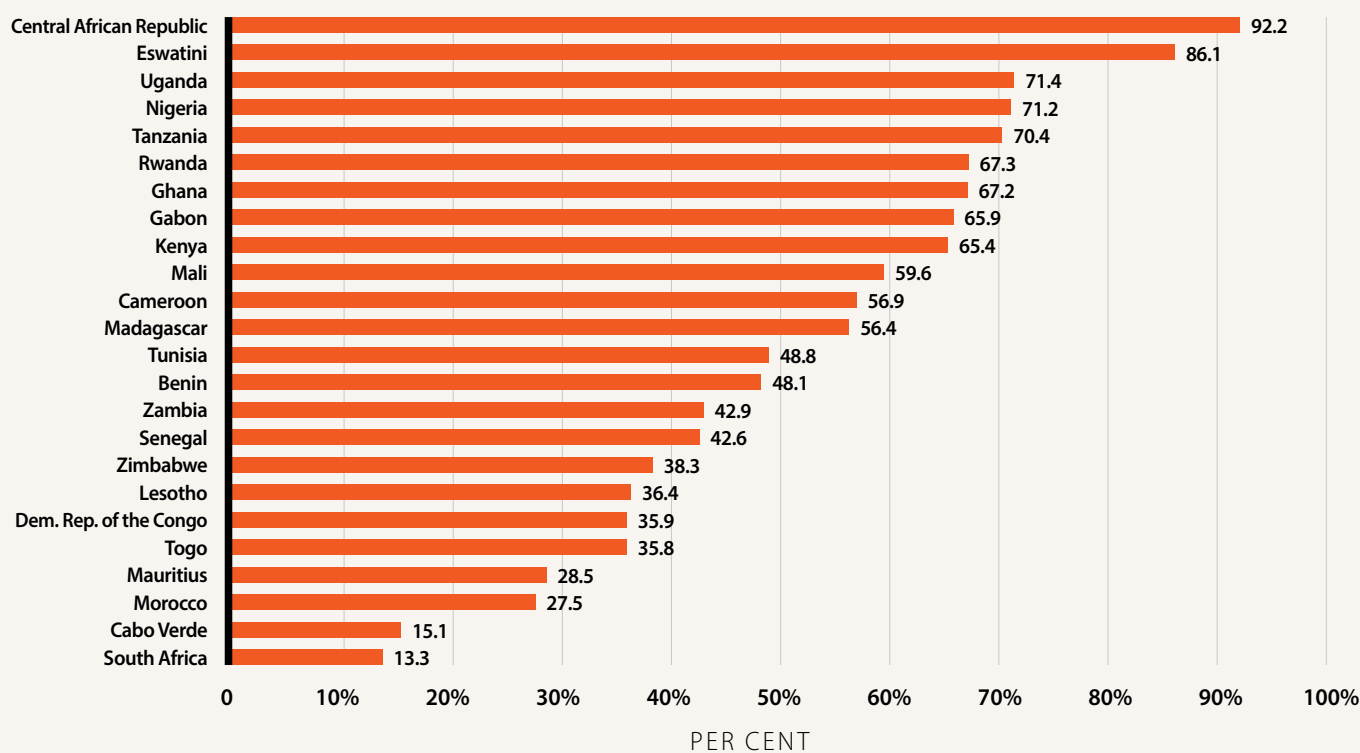
The tax gap for the VAT (the shortfall between potential and actual VAT collections) captures both policy and compliance shortcomings (Cnossen,

2015). Policy gaps arise from provisions in VAT policy or law relating to exemptions and zero and other reduced rates. Compliance gaps arise from inadequacies in administering the VAT, which result in lower than expected revenue, including operational inefficiency, limited capacity, fraud and unreliable consumption data. Despite these and other limitations, the compliance efficiency measure⁵ yields a useful estimate of a country's VAT performance (Keen, 2013).

Of 24 countries with adequate data, 12 had a VAT gap of 50 per cent or more in 2018, while 12 had a gap of less than 50 per cent, indicating considerable

⁵ Keen (2013) also identified technical shortcomings, such as lack of uniformity across countries in defining consumption, including public sector consumption, and in treatment of purchases by non-residents, all of which lead to potentially overestimating the VAT.

FIGURE 3.4. VALUE-ADDED TAX GAP FOR 24 AFRICAN COUNTRIES WITH DATA, 2018



Note: Data on VAT performance were available for 24 African countries. The analysis assumes that all final private consumption should have been subjected to the VAT (see the annex for the calculation of VAT collection efficiency, where the VAT gap is calculated as 1 minus this ratio). The results may overestimate the VAT gap because the private consumption data used in calculating the gap were obtained residually and because a share of final private consumption that might have been zero-rated could have been erroneously considered subject to the VAT. Thus, the results are indicative of the trend and potential.

Source: Forecast based on VAT data from ICTD and UNU-WIDER (2018), accessed November 2018, and private consumption data from World Bank (2018b).

BOX 3.3. INSIGHTS FROM CHAD ON TAX GAPS

Chad is a low-income, fragile country with development challenges that have intensified as a result of oil price declines and security shocks (IMF, 2018a, 2018c). Between 2014 and 2016 Chad responded to a contraction in oil revenue and a mounting burden of external commercial debt by cutting spending. An overreliance on oil revenues has depressed tax revenues, so the potential for improvement is high. Revenues from non-resource sectors in Chad are at 5 per cent of GDP, and Chad's tax gap of 9 per cent of GDP is much higher than the average of 4.6 per cent for Africa excluding North Africa (Coulibaly and Gandhi, 2018).

To respond to budgetary and debt obligations and increase revenue, Chad introduced several reforms to its non-oil tax system:

- Strengthened core tax administration functions such as tax registration and identification of new taxpayers. As part of this reform an automated tax administration system was rolled out in 2014
- Modernized and simplified tax filing payment procedures.
- Increased and improved collection of excise tax revenues

- Suspended tax exemptions, which is estimated to yield an additional \$174 million (ECA n.d.).

The average tax ratio in Chad improved from 6 per cent of GDP over 2000–2004 to 11 per cent over 2011–2015 (see table 3.1 in the text), suggesting a large impact from the reforms.

scope for increasing VAT collections (figure 3.4). The most efficient VAT collections were in South Africa (13.3 per cent gap) and Cabo Verde (15.1 per cent gap), and the least efficient were in Central African Republic (92.2 per cent gap) and Eswatini (86.1 per cent gap).

Nigeria had the fourth largest VAT gap (71.2 per cent) in 2018 and one of the lowest VAT rates in Africa, at 5 per cent. Doubling the VAT rate could double VAT collections from 0.8 per cent of GDP, and improving collection efficiency could boost VAT collection to more than 1.6 per cent of GDP. Further revenue could be obtained by addressing policy gaps.

While increasing the VAT rate could substantially improve resource mobilization in some countries, countries also need to address the gaps rooted in policy and compliance deficiencies. For example, despite having a high VAT rate of 20 per cent, Madagascar has a VAT gap of 56.4 per cent. Similarly, Cameroon's VAT tax rate is 19.25 per cent, yet its VAT gap is 56.9 per cent.

AFRICA'S TAX GAP

Each country has an optimum tax revenue as a share of GDP—referred to as its tax capacity—that it can raise according to its underlying macroeconomic, demographic and institutional characteristics (Coulibaly and Gandhi, 2018). Sub-Saharan Africa

Of 24 countries with adequate data, 12 had VAT gaps greater than 50 per cent in 2016, while nine had gaps under 50 per cent, indicating considerable scope for increasing VAT collections.

has the lowest tax capacity in the world, estimated at 20 per cent of GDP. The low tax capacity is attributable to low level of economic development and a large informal sector (Coulibaly and Gandhi, 2018).

Taking 20 per cent as the conservative tax capacity in Africa and Africa's average tax revenue to GDP ratio of 17 per cent for 2000–2018 yields an estimated tax gap of 3 per cent of GDP, or approximately \$72 billion in forgone revenue.

At the country level the tax gap ranges from 3 per cent of GDP to 9 per cent, with the largest gaps estimated for natural resource-rich countries (see box 3.3 on Chad's experience; Coulibaly and Gandhi, 2018). The large gaps are attributable to inadequate fiscal policy and low tax capacity, leakages in revenue collection and weak enforcement (Coulibaly and Gandhi, 2018).

Addressing these challenges could mobilize additional revenue to finance sustainable development and Agenda 2063 aspirations.

KEY CHALLENGES TO TAX POLICY: COUNTRY CASE STUDIES

Tax policy challenges in Africa include hard to reach sectors (informal economy and agriculture) and the digital economy, curbing corruption, managing growing debt levels and debt-service obligations and resisting pressures to use excessive tax incentives

to attract investment.⁶ Countries' experiences with these challenges also reveal some successes from which other countries could learn.

SECTORS THAT ARE HARD TO TAX

Across Africa there are economic agents whose activities are beyond the reach of the tax authorities, for reasons ranging from administrative weaknesses to policy shortcomings (see box 3.4). These economic agents range from small, informal enterprises to medium and large firms that avoid or evade taxes in multiple ways (Bird and Wallace, 2003). Firms may fail to register for taxes or may register but then fail to comply, sometimes by keeping incomplete or falsified records, which make it difficult for tax authorities to police their activities (Terkper, 2003). While these leakages from the tax system are a challenge to tax administration, they also represent an opportunity to mobilize additional resources to finance sustainable development (see chapter 5 for more details).

Informal sector

Informality in Africa spans a wide range, from 20–25 per cent of GDP in South Africa and Mauritius to 50–65 per cent in Benin, Tanzania and Nigeria (Medina, Jonelis and Cangul, 2017).

Monitoring informal activity is difficult because of the lack of data and the large number of informal firms. When monitoring is possible, the cost of bringing these activities within the tax net may outweigh any potential revenue gains in the short term (see box 3.4 for Kenya's experience; Joshi, Pritchard and Heady, 2014; Kundt, 2017).

Achieving formalization requires better record keeping at the national and subnational levels. Subnational governments can begin by requiring businesses to register for local permits or access to markets; that information can then be digitized

BOX 3.4. CHALLENGES IN TAXING THE INFORMAL ECONOMY IN KENYA

Between 2010 and 2017, the government of Kenya attempted to bring the small and micro enterprises and traders in the informal sector into the tax system by introducing the turnover tax. The 3 per cent turnover tax applied to any resident persons, excluding limited liability companies, rental income and professional or management fees, whose annual turnover from business does not exceed \$50,000. The Kenya Revenue Authority also made administrative changes to increase compliance by simplifying their systems and creating easy access to information for taxpayers through the iTax platform introduced in 2015. Despite these

changes, however, there was little success in taxing the sector.

In 2018 the National Treasury overhauled the turnover tax and replaced it with a presumptive tax. The presumptive tax is applicable to the same resident persons with the same annual turnover limit of \$50,000 as the predecessor turnover tax, but it is chargeable at the rate of 15 per cent of the single business permit fee issued by a county government. The revenue collected may not be very substantial, but the presumptive tax is an important step towards bringing the informal sector into the tax system.

⁶ Chapter 6 deals with the issues in the natural resources sector, but tax incentives are mentioned here to underscore the relevance to raising more tax revenue.

BOX 3.5. TAXING THE TRANSPORT SECTOR IN GHANA

Ghana has implemented a series of presumptive taxes in an effort to tax the informal economy. The first, introduced in 1963, required businesses to make lump-sum tax payments, in accordance with specific occupational groupings, and to display a certificate on their premises as evidence of complying (Adeyiga, 2013). Though registrations increased, many complained that the tax was too high and administratively burdensome. The tax also faced challenges of corruption, rampant evasion and limited administrative capacity on the part of the revenue authority (Adeyiga, 2013). These challenges prevented the tax from meeting its revenue goals.

The turnover tax was replaced in 1987 by the Identifiable Group Tax (IGT), a form of association tax. The tax made use of the business associations formed in various sectors to collect taxes from their members (Joshi and Ayee, 2002). The tax was collected daily at first, then weekly and eventually monthly. The associations received a small commission as compensation for their efforts. The IGT increased revenue collection from 0.97 per cent of total revenue in 1988 under the presumptive tax to 1.6 per cent in 1991 (Ayee, 2007; Dube and Casale, 2016). However, the new tax faced the same challenges as the presumptive tax, including lack of capacity and continuing corruption—some associations kept the money collected instead of remitting it to the tax authorities—and revenue declined (Dube and Casale, 2016).

The IGT was abolished in 2003 and replaced by the Vehicle Income Tax, which is payable quarterly; stickers placed on the windshield are evidence of having paid the tax (Adeyiga, 2013). Compliance rates in the transport sector were at 85.5 per cent in 2010 (ATAF, 2014).

Ghana's experience reveals the need for an integrated approach that not only creates a simple tax system for hard-to-tax sectors but also uses existing social structures, such as business associations, and focuses on increasing capacity in tax administration and tackling corruption at all levels (Dube and Casale, 2016).

and made available to revenue authorities. Governments can then consider implementing a simplified revenue accounting system for taxation (see box 3.5 on Ghana's experience). The system should be freely available and easy to access so that it supports the growth and administration of the businesses it is designed to include. Formalization can then be progressively strengthened through improved record keeping.

Governments can also provide incentives for firms to formalize, such as offering access to credit, training programmes and government tenders. Since taxation of the informal sector could be regressive for small firms and microenterprises, governments should establish a minimum tax threshold with a graduated scale to protect small businesses and entrepreneurship and promote compliance.

The agriculture sector

The agriculture sector accounted for about 16 per cent of GDP in Africa in 2017 and employs the largest number of active workers on the continent (World Bank, 2018a). But agriculture is hard to tax because

the large number of unregistered, widely dispersed small-scale farmers makes it difficult for revenue authorities to verify incomes and tax liability.

Land taxes, which are indirect taxes levied on the value of land, are viewed as simple to apply and progressive since they increase with the value of the land held (IBFD, 2018). However, performance of the tax has been poor because of inadequate data and valuation practices, incomplete property coverage and political interference (Franzsen and McCluskey, 2017). Property taxes have contributed

...agriculture is hard to tax because the large number of unregistered, widely dispersed small-scale farmers make it difficult for revenue authorities to verify incomes and tax liability.



between 0.2 to 0.3 per cent of GDP between 2000 and 2018 (see Table 3.2).

THE DIGITAL ECONOMY

Advances in information technology and the digital economy have revolutionized the business world, from the types of goods and services produced to how they are produced, delivered and paid for. That has created opportunities for better harnessing economic activities for development—including through taxation of profitable activities.

The digital economy—whose key factors of production are digitized information and knowledge (ADB, 2018)—also presents challenges to tax policy because of the difficulty of capturing where value is created and of measuring it (Jakurti, 2017). This is made more complicated with cross-border transactions. Current tax rules relating to cross-border income do not effectively address digital activities, which may not have a fixed physical location, making it easier for such income to remain untaxed (OECD, 2018). Historically, the factors of production were relatively immobile and required extensive use of labour and tangible resources, and cross-border income was allocated on the basis of the permanent establishment or physical presence of a business (CIAT, 2018).

The development of the digital economy has enabled businesses to use digital assets such as

intellectual property to shift profits from where they are generated to jurisdictions where taxes are lower, thus eroding the tax base in the originating jurisdiction. These changes necessitate a review of tax laws to ensure that they are appropriate to the current business environment.

The multijurisdictional nature of the digital economy demands a global solution. The Organisation for Economic Co-operation and Development (OECD) has been at the forefront on this issue through its Base Erosion and Profit Shifting project, which makes the following recommendations for taxing the digital economy:

- For the VAT, the suppliers of digital services should be responsible for remitting the tax to the jurisdiction in which the service is consumed.
- The reduced need for a physical presence for digital services means that taxing rights can be established by using rules to determine the characterization of income and a threshold for data exchange.

Though a global solution has yet to be found, some countries (such as South Africa and India) have introduced interim measures to reduce the tax losses resulting from shifting profits through the digital economy (see box 3.6 for South Africa's experience).

BOX 3.6. SOUTH AFRICAN E-COMMERCE TAX LAWS

A review of taxation of the digital economy in South Africa concluded that tax laws enabled foreign e-commerce suppliers to avoid taxation, not only denying the country tax revenue but also competing unfairly with resident suppliers who had to pay taxes (Davis Tax Committee, 2014).

Following the recommendations of the review, South Africa amended its value-added tax in 2014 to capture the digital

economy and to level the playing field for local suppliers and foreign suppliers in the digital economy. Foreign suppliers of e-commerce services (such as music, electronic books, internet games, electronic betting and software) are now required to register as VAT vendors; those whose turnover in South Africa meets the threshold of 50,000 rand (about US\$3,500) are required to pay an output tax. The services are considered to have been supplied in South Africa—and

therefore subject to the tax—if the payment was made from a South African bank or if the supply was sold to a resident of South Africa.

Between June 2014 and September 2017, more than 200 foreign entities producing digital services registered in South Africa and paid taxes of almost 2 billion rand (about US\$140 million) (National Treasury, 2018).

TABLE 3.4. CORRUPTION PERCEPTIONS INDEX IN SELECTED COUNTRIES, 2012–2017

COUNTRY	2017 RANK	2017 SCORE	2016 SCORE	2015 SCORE	2014 SCORE	2013 SCORE	2012 SCORE
Angola	167	19	18	15	19	23	22
Benin	85	39	36	37	39	36	36
Botswana	34	61	60	63	63	64	65
Burkina Faso	74	42	42	38	38	38	38
Burundi	157	22	20	21	20	21	19
Cameroon	153	25	26	27	27	25	26
Cabo Verde	48	55	59	55	57	58	60
Central African Republic	156	23	20	24	24	25	26
Chad	165	20	20	22	22	19	19
Comoros	148	27	24	26	26	28	28
Congo	161	21	20	23	23	22	26
Dem. Rep. of the Congo	161	21	21	22	22	22	21
Côte d'Ivoire	103	36	34	32	32	27	29
Djibouti	122	31	30	34	34	36	36
Equatorial Guinea	171	17	N/A	N/A	N/A	N/A	N/A
Eritrea	165	20	18	18	18	20	25
Eswatini	85	39	N/A	N/A	N/A	N/A	N/A
Ethiopia	107	35	34	33	33	33	33
Gabon	117	32	35	34	37	34	35
Gambia	130	30	26	28	29	28	34
Ghana	81	40	43	47	48	46	45
Guinea	148	27	27	25	25	24	24
Guinea-Bissau	171	17	16	17	19	19	25
Kenya	143	28	26	25	25	27	27
Lesotho	74	42	39	44	49	49	45
Liberia	122	31	37	37	37	38	41
Libya	171	17	14	16	18	15	21
Madagascar	155	24	26	28	28	28	32
Malawi	122	31	31	31	33	37	37
Mali	122	31	32	35	32	28	34
Mauritius	54	50	54	53	54	52	57
Mozambique	153	25	27	31	31	30	31
Namibia	53	51	52	53	49	48	48
Niger	112	33	35	34	35	34	33
Nigeria	148	27	28	26	27	25	27
Rwanda	48	55	54	54	49	53	53
Sao Tome and Principe	64	46	46	42	42	42	42
Senegal	66	45	45	44	43	41	36
Seychelles	36	60	N/A	N/A	N/A	N/A	N/A
Sierra Leone	130	30	30	29	31	30	31
Somalia	180	9	10	8	8	8	8
South Africa	71	43	45	44	44	42	43
South Sudan	179	12	11	15	15	14	N/A
Sudan	175	16	14	12	11	11	13
Tanzania	103	36	32	30	31	33	35
Togo	117	32	32	32	29	29	30
Uganda	151	26	25	25	26	26	29
Zambia	96	37	38	38	38	38	37
Zimbabwe	157	22	22	21	21	21	20

Note: (1) name change from Swaziland to Eswatini to reflect current political realities (2) the scale is 0 to 100, where 0 is perceived to be highly corrupt and 100 is not corrupt at all

Source: Transparency International available at https://www.transparency.org/news/feature/corruption_perceptions_index_2017#table

CORRUPTION

Corruption, a symptom of weak economic governance, is a challenge for most African countries and undermines tax collection (Imam and Jacobs, 2007). In a sample of 49 African countries, the Corruption Perceptions Index has broadly improved in 16 countries, hardly changed

in eight countries, and deteriorated in 22 countries (see table 3.4) (Transparency, 2017). Only five countries (Botswana, Cabo Verde, Mauritius, Namibia, Rwanda and Seychelles) have indices above 50 in 2017.

When perceptions of corruption are high, residents are less willing to pay taxes, fearing that their taxes

will be misused or misappropriated (Barone and Mocetti, 2011; Baum et al., 2017). Strengthening public financial management and enhancing the efficiency and equity of public spending will build trust in the system and improve compliance and revenue collection.

Africa, where the gap between average tax revenue and tax capacity is 3 per cent of GDP, has the lowest average scores globally on indicators of both corruption and democratic accountability. Improving the region's corruption and democratic accountability scores to the global median could reduce this gap considerably (see box 3.7; Coulibaly and Gandhi (2018).

PRESSURE TO ATTRACT INVESTMENT

Countries the world over offer tax incentives to attract foreign investors, thereby forgoing the tax revenue that would have accrued to the country. Yet evidence indicates that tax incentives and tax treaties are of questionable efficacy in attracting investments, especially when the primary motivation to invest is access to natural resources or to a specific market (Tanzi and Zee, 2001). Tax incentives are subject to abuse and rank low in determining the investment location (Tanzi and Zee, 2001), while tax treaties that cede taxing rights to other countries often result in loss of tax revenue that far exceeds the gains from foreign investment (Van de Poel, 2016; see also chapter 6).

Tax holidays and preferential tax rates are the most prevalent types of tax incentives in Africa. These incentives seem to be mostly ineffective (see chapter 2).

African countries, most of which are capital importers, have been slowly ceding taxing rights over income earned within their jurisdiction through residence-based treaties, which have few provisions allocating taxing rights to the country where the income is earned (Hearson, 2016).

While tax allowances are recommended as a more effective form of tax incentives—because the benefit depends on the cost of the investment and not on its profits—some African countries grant tax allowances that are greater than the investment cost incurred.

BALANCING REVENUE NEEDS AND TAX EQUITY


Along with revenue sufficiency, equity is an important goal of taxation – adjusting revenue collection to meet development needs (Musgrave and Musgrave 1976). Equity calls for people with the same income or wealth to pay the same amount of taxes (horizontal equity) and for people with greater income or wealth to pay more taxes (vertical equity; Black, Calitz and Steenkamp, 2015).

BOX 3.7. LEVERAGING GOVERNANCE FOR TAX REVENUE MOBILIZATION


Average tax capacity in Sub-Saharan Africa is the lowest in the world, at 20 per cent of GDP, according to an assessment of prospects for mobilizing additional tax revenue for financing sustainable development in Africa (Coulibaly and Gandhi, 2018). Using data up to 2015, the study found that non-resource tax revenue had increased as a share of GDP but not by enough. To bridge the gap, the study recommended that African countries improve both tax capacity and tax efficiency.

The study estimated that improving efficiency to 100 per cent could raise tax revenue by 3.9 per cent of GDP, bringing revenue collection close to the average tax capacity of 20 per cent. The study also estimated that reaching a higher tax to GDP ratio of 24 per cent of GDP to fast track achievement of the Sustainable Development Goals would require increasing tax capacity by a further 4 percentage points of GDP. Improving governance (measured by corruption and

accountability in the International Country Risk Guide) would reduce inefficiencies and help raise about additional \$110 billion a year, or almost half of the average \$230 billion investment financing gap over 2015–2020. The study illustrates the potential for African countries to raise additional tax revenue by strengthening economic governance, including by combating corruption and promoting accountability and transparency in public financial management.



...evidence indicates that tax incentives and tax treaties are of questionable efficacy in attracting investments, especially when the primary motivation to invest is access to natural resources or to a specific market



Given the levels of poverty and inequality and the large informal sector, an important concern for taxation in Africa is equity. Failure to address inequality undermines economic growth and development and in some cases is an underlying cause of social tensions and violent conflict (Langer and Stewart, 2015).

Equity in taxation is determined by who bears the final burden of a tax. The design of the tax system thus plays a key role since a poorly designed system may make the poor even poorer (Bird and Zolt, 2005). To promote equity, tax policies need to be informed by studies of tax incidence. Government policies need to respond to the challenges of equity without unduly compromising the tax revenue needed to finance policies to reduce poverty and inequality, which are at the core of the SDGs.

When assessing equity, it is important to consider the equity of the entire tax system, not just of individual tax components. “Making the system as a whole progressive does not require every individual tax to be progressive” (Mirrlees et al., 2011: 26). An individual tax cannot fulfil all the principles of a good tax—revenue sufficiency, equity, economic efficiency and administrative efficiency. Broad-based taxes such as the VAT may be economically and revenue efficient, but their

impact may be regressive. Progressive tax systems have the potential to reduce inequality, but to achieve sustainable development they must be accompanied by effective public spending and a responsive welfare system. Personal and corporate income taxes may be designed to be progressive, but their impact on economic activity may reduce tax revenue, especially in countries with a very large informal sector.

Assessing equity also requires examining public spending measures that reduce inequality through income redistribution. Evaluating whether a tax system is progressive or regressive thus needs to take into account the effect of all taxes in the system on different individuals or households, along with the effects of cash transfers and other public benefits (Varela, 2016).

Progressive taxation, if well designed, could reduce inequality by enabling low-income workers to allocate a greater portion of income to savings and investment, thus improving their economic situation. Furthermore, by boosting revenue, progressive taxation enables governments to fund key services, such as education and health, that favour low-income households and to invest in growth-enabling infrastructure that can increase social equity.

CONCLUSIONS AND POLICY RECOMMENDATIONS

The overall weighted tax revenue to GDP ratio for the continent has been declining since 2004, underscoring the slower pace of tax growth than income growth. The overall decline in the ratio between 2000 and 2018 reflects declines in the ratio in 29 African countries, including major economies such as Angola, Ethiopia, Kenya, Morocco and Nigeria. At the same time, however, 9 countries had a ratio of at least 10 per cent in 2000, while 16 did in 2018. Four countries increased their ratio by at least 10 percentage points between 2000 and 2018, and 7 increased it by 5–9 percentage points.

Indirect taxes dominate income taxes, raising the possibility that tax systems are regressive but also implying space for collecting additional revenue from income taxes. Low overall tax capacity and large tax gaps signal the potential for raising additional tax revenue by closing these gaps. With comprehensive tax reforms, Africa could raise additional tax revenue of 3 per cent of GDP (\$72 billion) a year.

To achieve the SDGs and the aspirations of Agenda 2063, African countries need to increase revenue generation in ways that are equitable and sustainable:

1. To ensure that the tax system is progressive, neutral, fair and efficient, African governments should address the system as a whole, rather than each tax separately. In this way, governments may find additional opportunities to expand the tax base, create more certainty for taxpayers and contextualize any global standards.

The overall weighted tax revenue to GDP ratio for the continent has been declining since 2004, underscoring the slower pace of tax growth than income growth.

2. To broaden the tax base, African countries need to include more and more diverse payers in the tax net.
 - The low contribution of payroll and workforce taxes and property taxes (taxing income from properties) signals areas that need particular attention to increase revenue by broadening the tax base.
 - Governments should formulate policies to bring the informal economy and agriculture into the tax system, taking care to avoid harming low-income workers.
3. To deepen the tax base, African countries need to review their VAT regulations to reduce the policy gaps (excess use of exemptions and zero or reduced rates). Many African countries' VAT collection efficiency is well below 50 per cent, indicating that improving VAT collection could increase overall tax revenue collection. (Compliance gaps are covered in chapter 5 on tax administration.)

4. African governments should leverage information and communication technology to improve revenue generation. African governments could promote the spread of information technology by using tax policy to support the dissemination of information technology. Information technology facilitates digitization of economic information and makes it easier to tax economic activity. Information technology could be used to bring more economic agents within the tax system (for example, by registering informal workers, using e-tax filing to make it easier to file taxes and simplifying payment processes) and make it easier for them to comply with fair taxation policies.
5. African governments should support development of the digital economy to expand the type of economic activities that

could generate additional revenue. In doing this, governments need to set up infrastructure and legal frameworks to prepare for the complex economic operations of the digital economy, which are susceptible to tax evasion and avoidance.

6. African governments should improve governance in revenue collection by combating corruption and bolstering accountability to reduce inefficiencies in tax collection, which could help realize an extra 3 per cent of GDP in tax revenues.

The most widely used measure of VAT performance in the tax literature is the VAT Collection Efficiency (C-efficiency) indicator proposed by Ebrill et al.

To achieve the SDGs and the aspirations of Agenda 2063, African countries need to increase revenue generation in ways that are equitable and sustainable.

ANNEX 3.1 MEASURING VALUE ADDED TAX PERFORMANCE IN AFRICA

(2001), which measures the actual VAT revenue as a proportion of potential VAT revenue (assuming perfect enforcement of a uniform VAT on all consumption, which would be a C-efficiency ratio of 1 or 100 per cent).

It is computed as:

$$\text{VAT C-efficiency} = \frac{\text{Actual VAT revenue}}{\text{Standard rate} * \text{Final consumption}}$$

Departures from a C-efficiency ratio of 1 or 100 per cent (the benchmark VAT) signal a VAT collection inefficiency, which can result from either policy gaps or compliance gaps (Cnossen, 2015). Policy gaps arise from provisions in VAT policy or laws relating to exemptions or zero and other reduced rates for some categories of consumption. Compliance gaps arise from shortcomings in VAT administration that result in lower revenue than would be expected from VAT policy or law, including operational inefficiency, limited capacity and fraud. While the C-efficiency measure has

limitations⁷ (see Keen, 2013), it is a useful indicator of a country's VAT performance.

The C-efficiency ratio by itself does not indicate the extent to which policy gaps or compliance gaps account for the departure of VAT collections from the benchmark VAT; examination of VAT laws and the efficiency of tax administration in various countries helps to contextualize the gaps that undermine VAT revenue collection. Chapter 5 examines issues in tax administration in Africa, shedding light on shortcomings in government policy and actions that cause compliance gaps in VAT collection.

⁷ Limitations include unreliability of consumption data, especially in Africa. Keen (2013) also raised technical shortcomings—including non-uniformity in defining consumption across countries, the treatment of purchases by non-residents and public sector consumption—which potentially lead to overestimating the VAT and could undermine cross-country comparisons.

ANNEX 3.2 AVERAGE CORPORATE TAX RATE BY REGION OR GROUP, 2018

REGION OR GROUP	AVERAGE RATE	WEIGHTED AVERAGE RATE	NUMBER OF COUNTRIES
Africa	28.81%	28.39%	50
Asia	20.65%	26.42%	46
Europe	18.38%	25.43%	49
North America	23.01%	26.22%	33
Oceania	22.00%	27.04%	17
South America	28.08%	32.20%	13
BRICS	28.40%	27.33%	5
EU	21.86%	26.03%	28
G20	27.37%	27.18%	19
G7	27.63%	27.21%	7
OECD	23.93%	26.58%	36
World	23.03%	26.47%	208

Source: Tax Foundation 2018, Corporate Tax Rates Around the World 2018

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CHAPTER 4

NON-TAX REVENUES FOR FINANCING SUSTAINABLE DEVELOPMENT

Non-tax revenue to African governments is equivalent to 4.5 per cent of GDP. There is considerable potential for boosting this contribution. Simply improving collection efficiency could raise non-tax revenue by 2 per cent of GDP. Thanks to improving efficiency and increasing diversity of sources, Botswana and Congo recorded non-tax revenue of up to 16 per cent of GDP during 2000 and 2018.

The composition of non-tax revenue varies across countries, depending mainly on each country's efforts to innovate and diversify non-tax sources of revenue. Countries have used a variety of non-tax revenue instruments, from levies on natural resource extraction to pollution fees. Each country should design non-tax revenue sources according to its own economic context, development objectives and target groups.

Because non-tax revenue is volatile, often reflecting fluctuations in natural resources prices, countries need to develop realistic collection targets based on prudent financial management. Challenges to mobilizing more revenue from non-tax sources include the lack of strong institutions, appropriate infrastructure and effective relations between the central government and subnational governments.

INTRODUCTION

Governments raise revenue using tax and non-tax instruments, where non-tax sources include any revenue that do not come from taxes. Non-tax revenue is an important but often under-tapped source of public revenue that is all the more vital in Africa today as countries face declining official development assistance, rising indebtedness, limited domestic resource mobilization capabilities, poor financial management and systemic corruption, among other challenges. Projections indicate that high levels of financing will be required to bring about Africa's structural transformation and to achieve the 2030 Agenda for Sustainable Development and Agenda 2063 (Kedir et al., 2017; UNDP, 2018).

Non-tax revenue instruments are much more varied than tax instruments. They include royalties, fees for mining rights, dividends on government investments in state-owned enterprises and in stock portfolios, sovereign wealth funds and government shares in joint ventures with private operators. Fees for trade licenses for commercial establishments, construction permits and for registering or issuing birth, marriage and death certificates are additional sources. User and service fees are important too and are levied on leases for government buildings or other venues, school and university attendance, hospital admission and tourists visiting museums and parks. Resource-rich countries depend heavily on mining royalties on the extraction and sale of oil and minerals while mineral-poor countries rely more on administrative fees, fines and other service-related revenue sources.

Non-tax revenue can address some of the structural challenges in revenue collection. For example, most of the practical problems involved in taxing the informal economy do not affect non-tax revenue collection. Non-tax revenue can be collected as readily from economic agents in the informal sector as from those in the formal sector. For instance, user charges (such as for health and

education services) and payments for services (such as water, electricity and telecom utilities) can be levied on the services used by all customers.

Country experiences reveal a variety of context-specific non-tax revenue instruments and performance. Africa's non-tax revenue was estimated to be \$133 billion in 2017. This is a considerable amount relative to the \$230 billion financing gap for development investments for the continent (Coulibaly and Gandhi, 2018) and is greater than the \$100 billion Africa loses every year in illicit financial flows (ECA, 2018b). However, countries accounted for widely differing shares of this total, ranging from less than 1 per cent to more than 10 per cent, and the share fluctuated within countries over time.

Non-tax revenue has the potential to become a much greater source of revenue. Their diversity opens opportunities to both increase revenue and achieve other policy objectives. For instance, countries can impose levies on environment-damaging production and consumption and use the revenue to reduce environmental degradation or mitigate its impact. Non-tax revenue can also advance inclusive decentralization by allowing subnational authorities to collect and use non-tax revenue for development. Furthermore, the flexibility of non-tax revenue instruments may circumvent some of the entrenched structural challenges of tax collection, such as taxing multinational firms, by applying more direct levies (ECA, 2018c).

This chapter provides an overview of trends and performance of non-tax revenue, examines the major components of non-tax revenue and discusses the institutional, administrative and regulatory challenges.

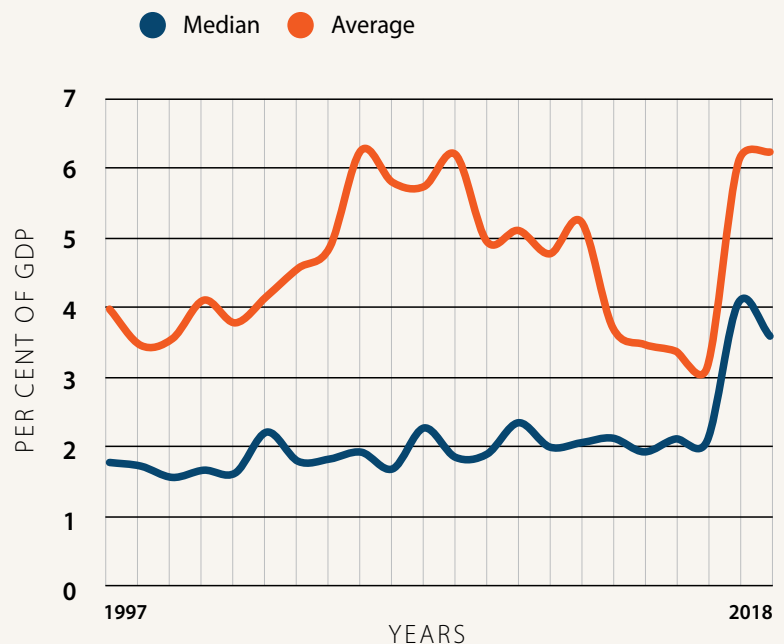
OVERALL ASSESSMENT OF NON-TAX REVENUE

TRENDS AND PERFORMANCE

Average non-tax revenue in Africa increased over 1997–2008, driven largely by commodity price booms, but declined sharply after that, particularly after 2012, as commodity prices plummeted (figure 4.1).¹ Despite this volatility and recent declines, African countries mobilized \$133 billion in non-tax revenue in 2017 (6.1 per cent of GDP), but with large variations across countries.

¹ The analysis in this section is based on data for the 48 African countries with data in the Government Revenue Dataset of the International Centre for Tax and Development and the United Nations University World Institute for Development Economics Research as of September 2018 (ICTD and UNU-WIDER, 2018). More details on non-tax revenue data are in table A4.1 in the annex.

FIGURE 4.1. NON-TAX REVENUE IN AFRICA, 1997-2018



Source: Based on data from ICTD and UNU-WIDER (2018) for 1997–2016, accessed in September 2018; IMF (2018a) for 2017; and ECA (2018k) forecasts for 2018.

Only 10 countries collected non-tax revenue of at least 6 per cent of GDP in 2018.

Only 10 countries collected non-tax revenue of at least 6 per cent of GDP in 2018 (figure 4.2). At the lower end, 8 countries collected less than 2 per cent. There were also some surprises. Chad, though not in the top 20, collected CFAF 76.92 billion, more than double its target of CFAF 35.29 billion, a 117.9 per cent increase over 2016 (ECA, 2018a).

In 2018, the top performers were oil-exporting and mineral-rich countries, although this has not

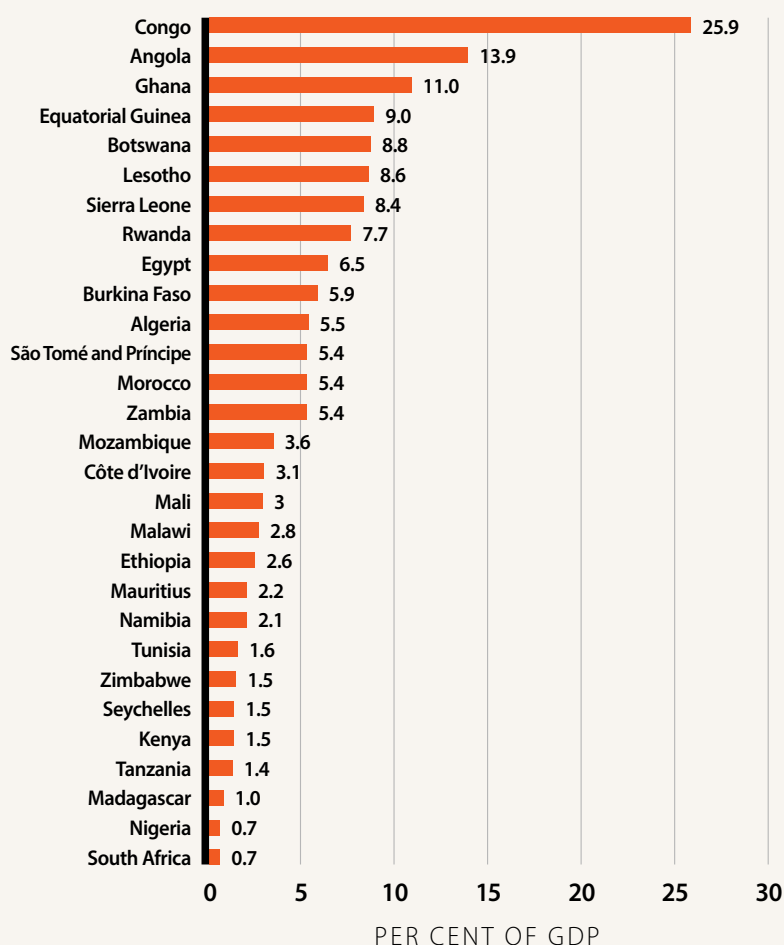
always been the case. Oil-exporting countries' non-tax revenue peaked at 15 per cent of GDP in 2008, followed by the mineral-poor group, at 8 per cent in 2008 (figure 4.3). Since 2008, non-tax revenue has declined sharply in both country groups, to lows of 2–4 per cent of GDP. In the past 18 years, non-tax revenue was 3–4 per cent of GDP in mineral-rich countries and below 3 per cent in oil-importing countries.

Central Africa has been the best performing subregion since 2000, with non-tax revenue peaking at 16 per cent of GDP in 2005, followed by North Africa (excluding Libya) and Southern Africa. Non-tax revenue in North Africa reached 7.3 per cent of GDP in 2008 but then fell to about 4.7 per cent in 2018. For East and West Africa this ratio averaged around 3 and 2 per cent, respectively, between 1997 and 2018, with a notable upward trend in recent years.

Africa's non-tax revenue mobilization over 1997–2016 was moderated compared with that of other developing regions. Africa performed better than Latin America and the Caribbean, about as well as South Asia, but worse than the Middle East, Europe and Central Asia, and East Asia and the Pacific. The Middle East collected about twice as much (as a share of GDP) as any of the other regions.

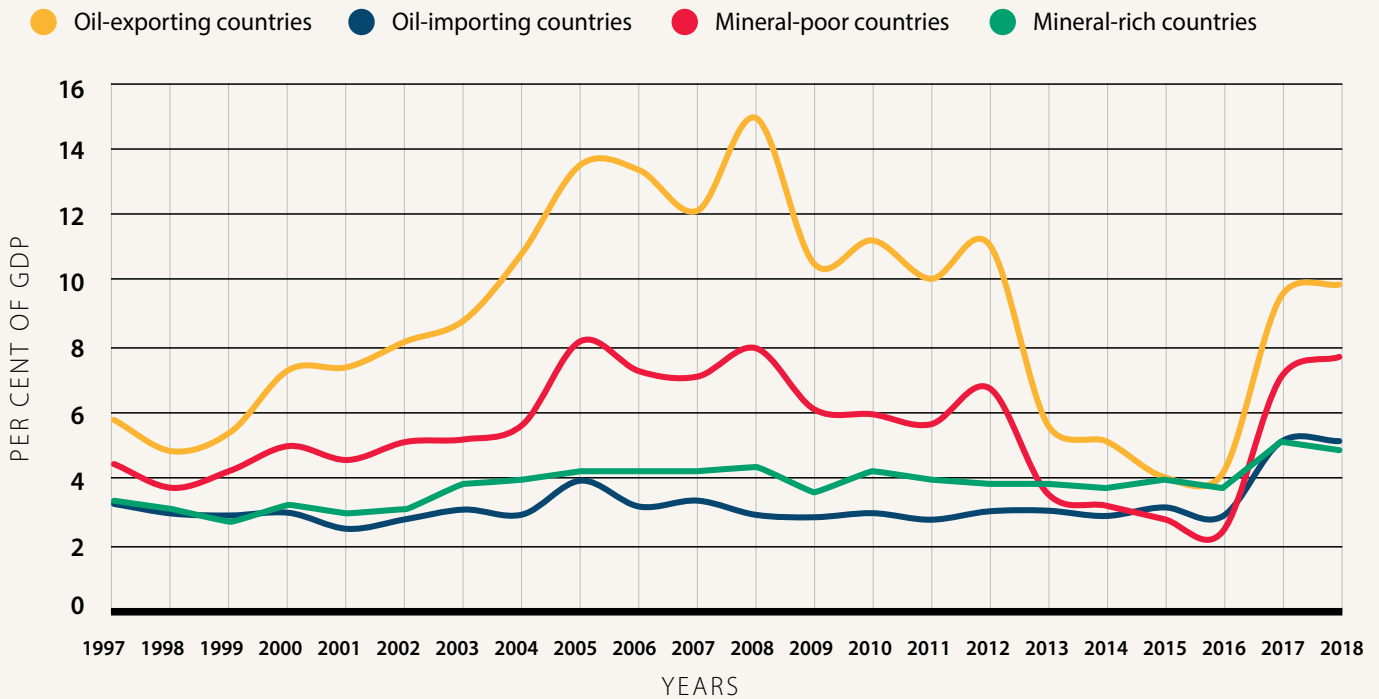
Africa's moderate performance in non-tax revenue mobilization suggests that there is room for further improvement. However, some strands of the public finance literature claim that the higher non-tax revenue is, the lower tax revenue is, suggesting a negative correlation

FIGURE 4.2. NON-TAX REVENUE COLLECTION, BY COUNTRY, 2018



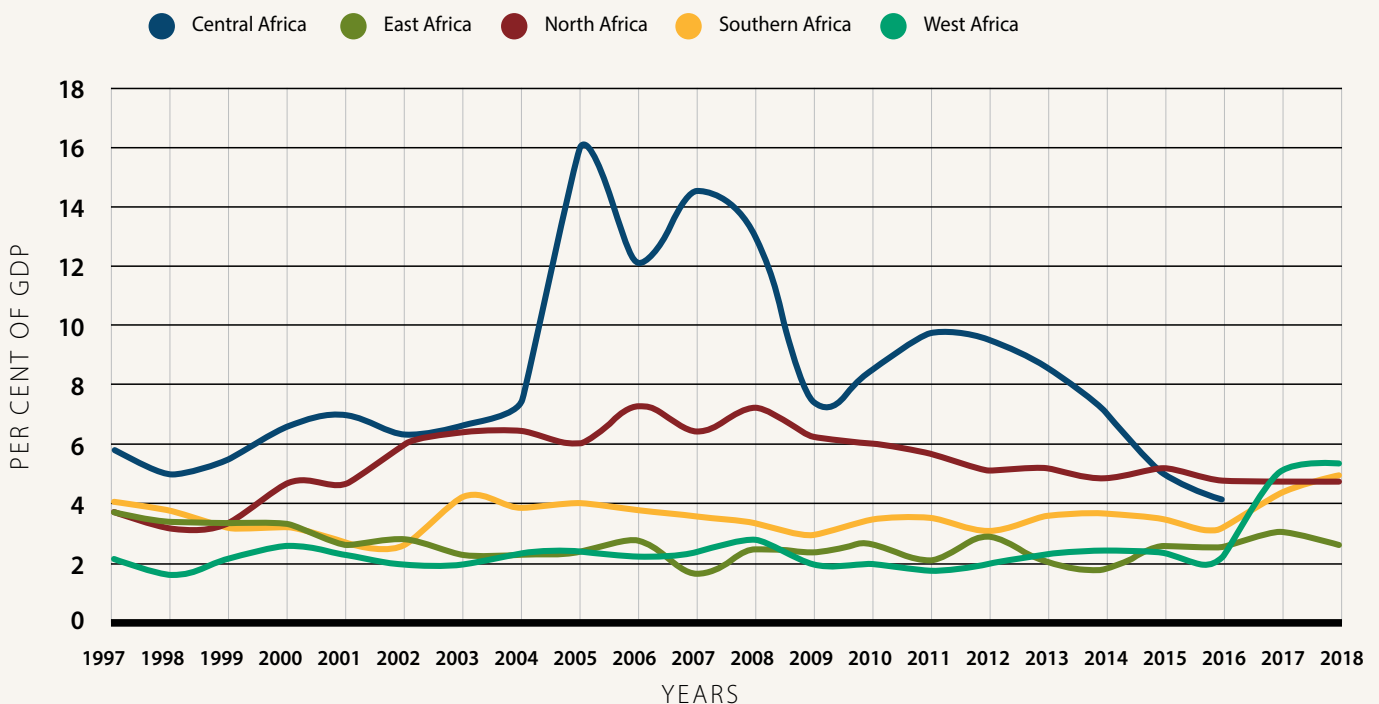
Source: ECA (2018k) forecast.

FIGURE 4.3. NON-TAX REVENUES IN AFRICA BY ECONOMIC GROUPING, 1997-2018



Source: Based on data from ICTD and UNU-WIDER (2018) for 1997–2016, accessed in September 2018; IMF (2018a) for 2017; and ECA (2018k) forecasts for 2018.

FIGURE 4.4. NON-TAX REVENUES IN AFRICA BY SUBREGIONAL GROUPING, 1997-2018



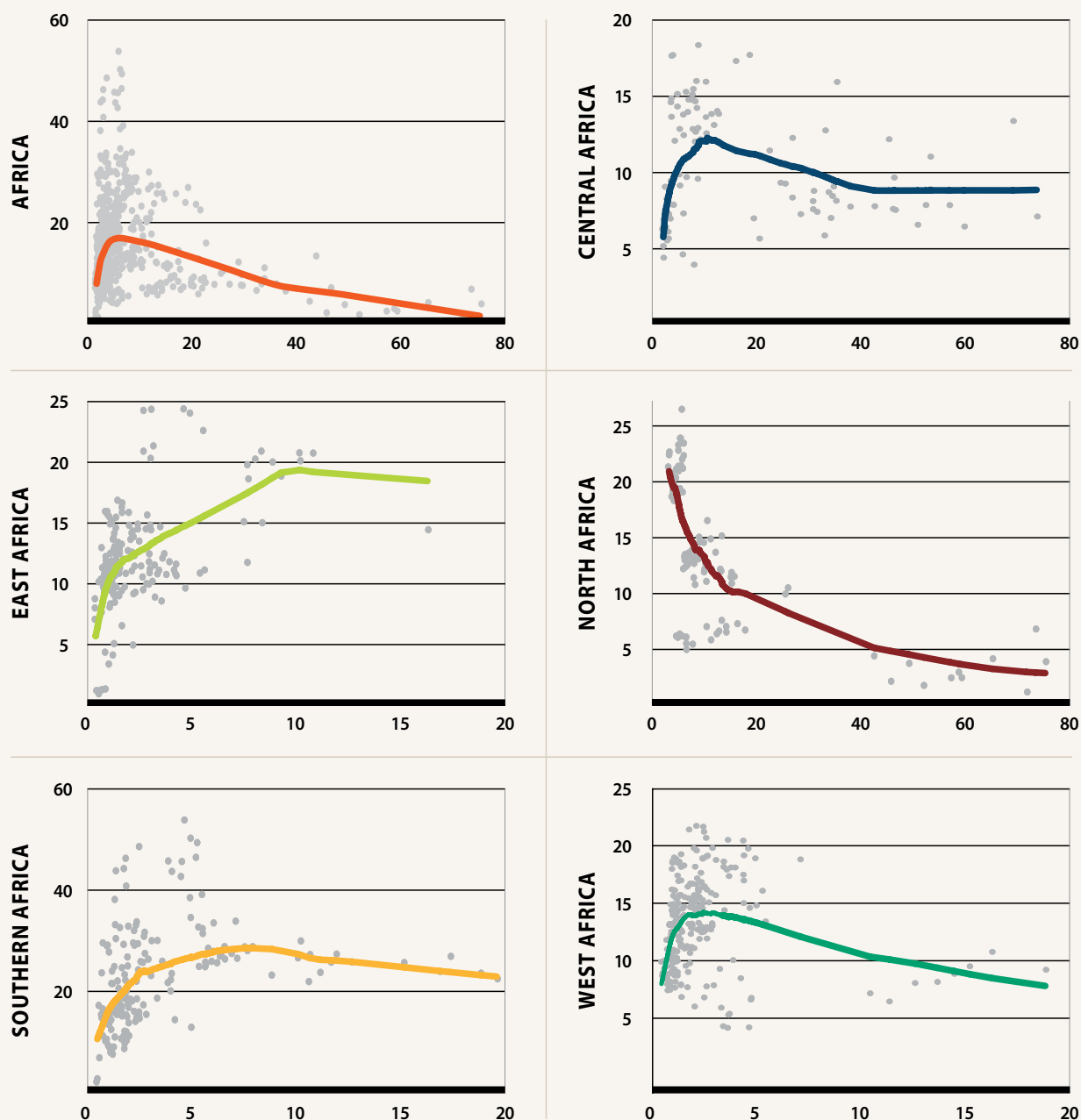
Source: Based on data from ICTD and UNU-WIDER (2018) for 1997–2016, accessed in September 2018; IMF (2018a) for 2017; and ECA (2018k) forecasts for 2018.

BOX 4.1. RELATIONSHIP BETWEEN NON-TAX AND TAX REVENUES

The box figures show differences in the correlation between non-tax and tax revenues by subregion. For Africa as a whole, there is a non-linear relationship between non-tax revenue and tax revenue: non-tax revenue rises with tax revenue until it reaches a certain threshold (non-tax revenues of about 10 per cent of GDP); after that, it declines with increases in tax revenue. For subregions, there is a positive correlation for East and Southern Africa, a negative correlation for North Africa and a non-linear relationship for Central and West Africa.

BOX FIGURE 1 Tax and non-tax revenue, 2000–2016

Left axis: Tax revenue (Per cent of GDP). *Bottom axis:* Non-tax revenue (Per cent of GDP)



Source: Based on data from ICTD and UNU-WIDER (2018), accessed in September 2018.

between the two, with further implications for the degree of democracy in the countries. The relationship was studied empirically for this report for African economies using non-parametric regression (locally weighted regression). The results show a more nuanced picture. The correlation between non-tax revenue and tax revenue for Africa as a whole shows that tax revenue rises with non-tax revenue until a certain threshold, after which it declines as non-tax revenue rises. The correlations differ by regional subgroups (see box 4.1).

VOLATILITY OF NON-TAX REVENUE

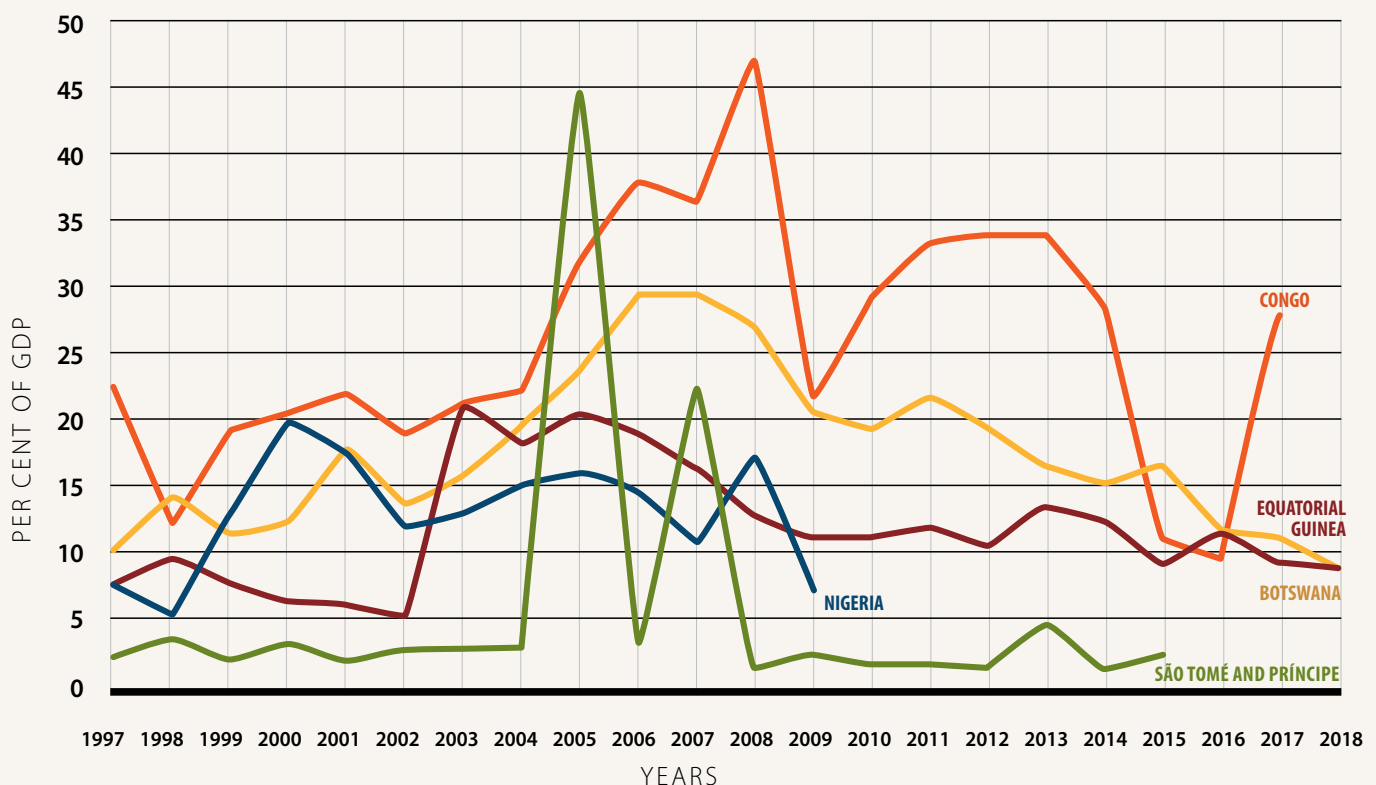
In contrast to the low to moderate volatility of tax revenue, non-tax revenue in African countries has been highly volatile (see table A4.1 in the annex). Volatility leads to uncertainty in annual projections of fiscal revenue and spending and is thus a source of risk for public finances, especially

in countries with high public indebtedness. Figure 4.5 shows countries with high non-tax revenue volatility over 1997–2018. For instance, Congo's non-tax revenue ranges from 9.5 per cent of GDP to 47 per cent of GDP.

Resource-rich countries were the worst performers in terms of volatility due to their almost exclusive reliance on resource rents: when commodity prices fall, so does non-tax revenue. Some oil-importing countries, including Ethiopia and Tanzania, also performed poorly in non-tax revenue collection.

At least some volatility may arise from poor design and management of non-tax revenue as a policy tool. Algeria, Comoros, Cabo Verde, Mozambique, Morocco, Rwanda, Senegal and Zambia took advantage of high growth in the past decade to increase non-tax revenue. By contrast, Cameroon,

FIGURE 4.5. NON-TAX REVENUE IN SELECTED COUNTRIES WITH HIGH VOLATILITY, 1997–2018



Source: Based on data from ICTD and UNU-WIDER (2018) for 1997–2016, accessed in September 2018; IMF (2018a) for 2017; and ECA (2018k) forecasts for 2018.

Gabon, Ghana, Guinea, Nigeria and Zimbabwe failed to mobilize expected non-tax revenue due to poor fiscal discipline.

NON-TAX REVENUE INSTRUMENTS AND PERFORMANCE

Individual countries use only a small subset of the wide array of non-tax instruments. For example, Kenya's non-tax revenue instruments include property income; business permits; social security contributions; fines, penalties and forfeitures; and interest and other income from lending (ECA, 2018d). Chad is overhauling its non-tax revenue instruments. It abolished its charges for motor vehicles and replaced them with a special tax on petroleum products. It replaced its flight boarding charge with a flat airport modernization fee in 2016 that varies by ticket class (ECA, 2018a). Chad also abolished a series of levies (including on mobile phones and audio-visual products, used to finance the National Sports Development Fund and anti-retroviral drugs, and various stamp duties on contracts and SIM cards) and replaced them with an 18 per cent excise duty on the turnover generated by mobile network operators and a per-minute fee on incoming international calls. Finally, it added a 0.2 per cent levy on imports to finance the African Union (ECA, 2018a).

Some non-tax revenue instruments, such as road tolls, can be used to finance infrastructure, while user charges for health and education can finance improvements in health care delivery and education (Bird, 2001). However, user charges need to be introduced cautiously because of their equity implications.

MAJOR SOURCES BY COUNTRY

An Organisation for Economic Co-operation and Development (OECD) data set of 21 African countries was used to assess the performance of

individual non-tax instruments (OECD, 2018).² Disaggregated data are unavailable for a majority of African economies, including large economies such as Ethiopia and Nigeria. Governments need to be more transparent in reporting their non-tax revenue to improve their fiscal management. Better reporting can also help them identify the revenue sources that are lumped in the residual category of miscellaneous and unidentified revenue, which can aid in fiscal planning.

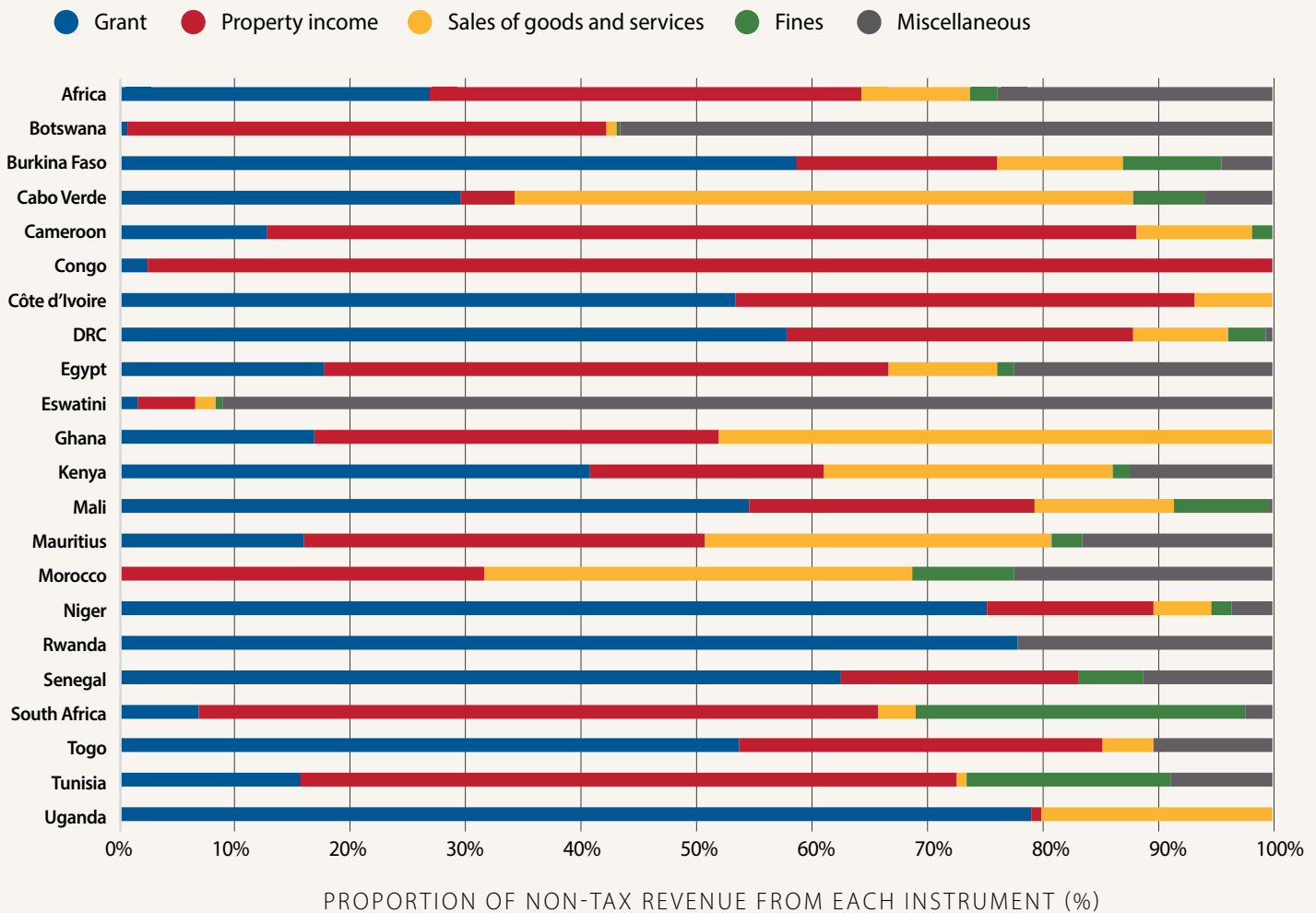
Non-tax revenue instruments were diversified across countries in 2018, but they were limited within countries, implying a need to broaden the non-tax revenue base (figure 4.6). Property income and grants were the largest contributors to non-tax revenue in 2018 across the 21 countries considered. For example, Côte d'Ivoire, Democratic Republic of the Congo, Niger, Rwanda, Togo and Uganda received a majority of their non-tax revenue from grants, whereas Cameroon, Congo, South Africa and Tunisia received a majority from property income. For Ghana the main source of non-tax revenue was sales of goods and services and for Eswatini its was miscellaneous and unidentified income.

In Egypt, Kenya, Mauritius, and Morocco no single instrument accounted for a majority of non-tax revenue. A majority of non-tax revenue came from grants and property income combined in Egypt; grants and sales of goods and services in Kenya; and property income and sales of goods and services in Mauritius and Morocco.

Over 2000–2018 property income (2.9 per cent of GDP) was the most important source of non-tax revenue, followed by grants (2.3 per cent of GDP), miscellaneous and unidentified income (1.5 per cent of GDP) and sale of goods and services (0.6 per cent of GDP). Fines, penalties and forfeits (0.1 per cent of GDP) contributed the least to non-tax revenue. The pattern for 2018 was the same.

² Because the ICTD and UNU-WIDER (2018) Government Revenue Dataset is not very well disaggregated, the analysis in this section draws on an OECD data set that breaks non-tax revenue down by instrument used for 21 African countries (OECD, 2018).

FIGURE 4.6. MAJOR NON-TAX REVENUE INSTRUMENTS USED IN 21 AFRICAN COUNTRIES, 2018



Note: Shares are based on the revenue from each instrument as a share of GDP. Figures for Uganda are for 2016.
Source: Based on data from OECD (2018).

Non-tax revenue has been volatile, due largely to fluctuations in commodity prices that have affected resource rents (figure 4.6). The short duration and low predictability of grant flows also create volatility, as do the largely unknown and often non-recurring nature of miscellaneous and unidentified non-tax revenue sources.

POTENTIAL TO INCREASE NON-TAX REVENUE

Both intra-Africa and international comparisons reveal considerable room to increase non-tax revenue in Africa. So does an analysis of non-tax revenue capacity, which measures how well a

Non-tax revenues have been volatile, due largely to fluctuations in commodity prices that have affected resource rents.

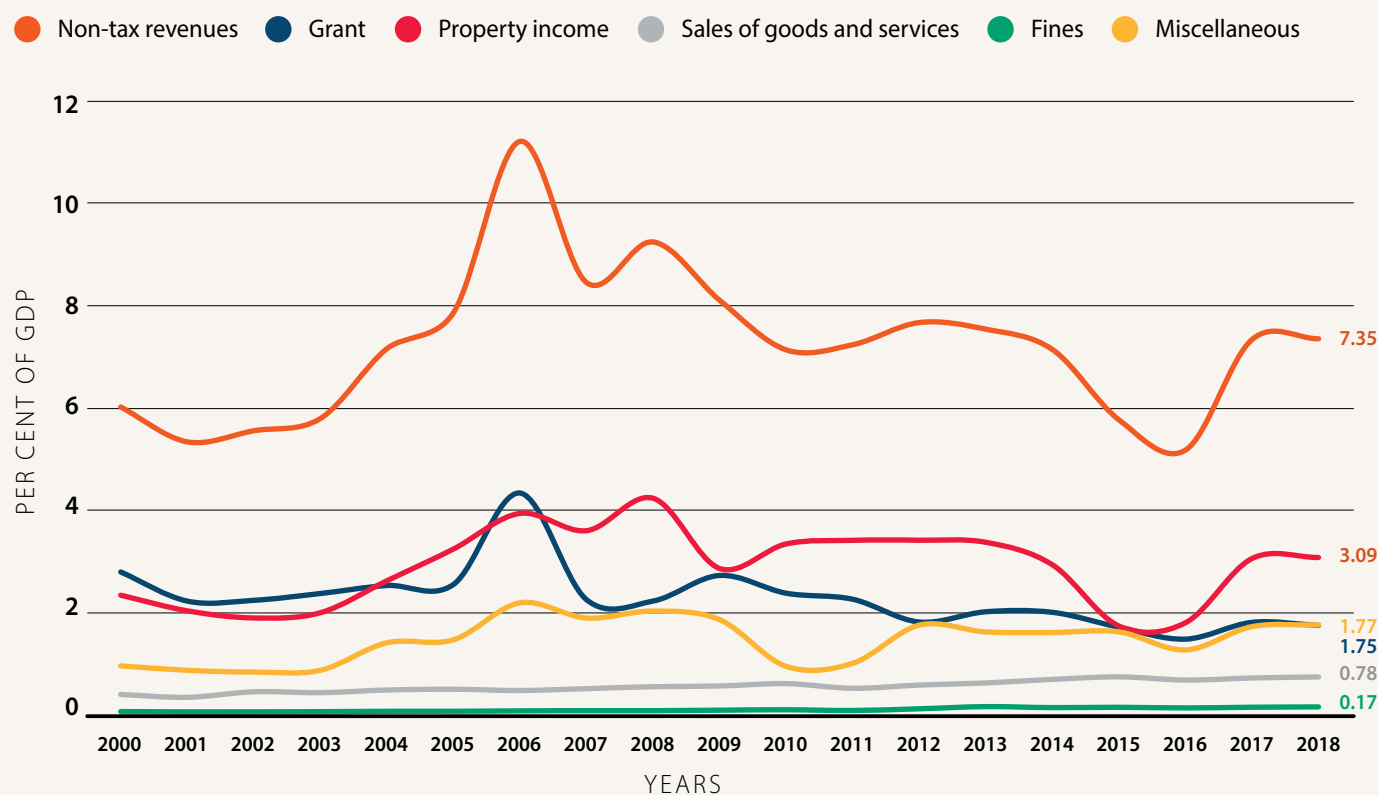
Improving collection efficiency could boost average non-tax revenues for low-collecting countries by up to 4.5 per cent of GDP, an increase of about 2 per cent of GDP from the current non-tax revenue collection.

country is doing in non-tax revenue collection relative to what it could be expected to do given its economic potential. That analysis—using the ratio of actual non-tax revenue collection to potential non-tax revenue collection assuming the average performance of non-tax revenue in Africa—shows a range of national non-tax revenue effort of 0.09 to 4.0. More than half the countries collected below their potential, with an average effort

index of 0.64 of potential collection, while others collected more than they would be expected to collect, given their economic potential.

Improving collection efficiency could boost average non-tax revenue for low-collecting countries to 4.5 per cent of GDP, an increase of about 2 per cent of GDP from the current non-tax revenue collection of 2.6 per cent. African countries

FIGURE 4.7. MAJOR NON-TAX REVENUE INSTRUMENTS USED IN 21 AFRICAN COUNTRIES OVER TIME, 2000-2018



Source: Based on data from OECD (2018).

with higher potential could improve their non-tax revenue collection to 15.7 per cent of GDP, about the average in Botswana and Congo.

INSTITUTIONAL, ADMINISTRATIVE AND REGULATORY CHALLENGES

Countries that are well governed anchor their revenue collection activities in transparency. They specify why each type of revenue is collected and how it will be allocated. Regulatory bodies monitor revenue reporting and allocation. Public finance management incorporates non-tax revenue planning into the budgetary process, ensuring that the revenue collected is efficiently allocated (IMF, 2018b). Strong political will is required to develop expertise in core departments and fiscal units. Consistent development of institutions over time lays the foundation for more efficient and effective collection and allocation of non-tax revenue.

Many of these conditions are absent in African countries, where increasing revenue collection from non-tax sources requires addressing a host of challenges (IMF, 2015). Revenue institutions are generally weaker in Africa than in emerging market and advanced economies, making for an unfavourable administrative and regulatory environment for non-tax revenue. Unlike the case for tax mobilization, there are often no systematic processes for non-tax revenue administration. In most countries, it is unclear where non-tax revenue originates, who pays them and when. In addition, friction between central and subnational government authorities is common, especially in the retention and transfer of non-tax revenue.

The combination of poor governance and inadequate infrastructure for collecting revenue at different government levels presents a major hurdle to effective resource mobilization, especially outside the main urban centres. For instance, Angola is a large country with extremely limited

infrastructure and under-supported education and health systems except in small pockets where the elite live. Infrastructure is a barrier to mobilization of both tax and non-tax revenue in Angola (ECA, 2018f) and inhibits outreach to taxpayers and compliance with revenue collection (ECA, 2018e). Other common challenges include lack of capacity and ethical standards in institutions. Structural challenges include corruption, political instability, lack of government effectiveness, widespread inequality and large informal sectors. Forgone non-tax revenue is enormous in countries with a large informal sector, such as Benin. Angola is working to formalize more of the informal sector and increasing decentralization of revenue collection (ECA, 2018f).

INSTITUTIONAL AND ADMINISTRATIVE ISSUES

Inefficient collection of non-tax revenue and its misallocation are common in some African countries, reflecting a lack of systematic, transparent, accountable, coordinated and regularly monitored data compilation (Hodler and Raschky, 2015). This results in a lack of clarity about the amount of revenue collected and its allocation and increases the potential for misuse and corruption, thus weakening incentives to better report non-tax revenue. Resource-rich economies, in particular, often suffer from bad governance and low tax revenue because they can rely on their natural resources for non-tax sources of revenue.

A severe weakness in many non-tax revenue systems is the failure of some agencies to report all the non-tax revenue they collect. In Sudan, where non-tax revenue accounted for just 3 per cent of government revenue in 2017, a government-commissioned report found that the major constraint affecting the proceeds of fees, royalties and other charges was revenue retention within collecting units (ECA, 2018g). The report recommended levying heavy penalties on government units and individuals that abuse their position and mishandle revenue. A lack of efficient and standardized oversight and an absence of well-coordinated public financial systems mean

that the revenue contributions of the more than 40 public corporations are negligible.

In South Africa, despite a multitude of non-tax revenue instruments (interest and dividends from state enterprises and other public entities, administrative charges, driver licences, fees on sales of goods and services, mineral and petroleum royalties, mining leases, departmental revenue and sales of capital assets), non-tax revenue constituted only about 2.6 per cent of consolidated budget revenue in 2017 (ECA, 2018i).

In Ghana, non-tax revenue collection has been rising in amount and as a proportion of public revenue, surpassing 14 per cent every year since 2000 (ECA, 2018j). According to public officials, non-tax revenue is the future of government revenue. A recent policy change allows public authorities to retain 66 per cent of non-tax revenue collected to finance agency operations and requires them to transfer the rest to a common account. Ghana managed to boost revenue collection without unduly burdening residents by introducing flexible payment arrangements for fees, fines and charges (ECA, 2018j). Setting predictable and realistic non-tax revenue targets and monitoring collections

can also improve revenue performance, and so can setting a regular schedule of rate reviews, as is done for taxes, to rationalize and streamline complex non-tax revenue systems (ECA, 2018a).

FISCAL DECENTRALIZATION

Fiscal decentralization, which devolves varying degrees of revenue mobilization and spending powers to lower levels of government, could contribute considerably to non-tax revenue mobilization (Bird and Vaillancourt, 1998). Greater revenue autonomy for subnational governments could enhance public service delivery by increasing the accountability and transparency of policy makers and service providers and making them more responsive to local preferences and needs (Elhiraika, 2007; see box 4.2 on fiscal decentralization in South Africa). In developed economies, revenue decentralization facilitated the move from an emphasis on taxes to more reliance on user charges, which function as a price signal that helps to improve the economic efficiency of public service delivery and government resource allocation (Feld, Kirchgasser and Schaltegger, 2003).

There is a lack of coherence, coordination and commitment to the smooth and efficient administration and management of non-tax revenue among levels of government, as the country case studies and the literature show (Burgess et al., 2015; Hodler and Raschky, 2015; Ilorah, 2009). The relationships among these centres of power are often warped by nepotism and favouritism along political party lines, ethnic affiliation, commercial ties and the like. There are also inefficiencies due to capacity constraints, lack of regulatory frameworks and failures in policy direction. For instance, there are often delays in sending funds to other levels of government, disturbing budgetary processes and service delivery at the subnational level, which relies heavily on transfers from the central government to finance infrastructure and services. There

BOX 4.2. FISCAL DECENTRALIZATION IN SOUTH AFRICA

The South African federal system has devolved considerable expenditure responsibilities and administration authority to provincial and municipal governments. However, owing to acute historical imbalances across provinces and municipalities, constitutional and institutional arrangements allow for extremely limited revenue autonomy. For instance, provincial governments are responsible for 43 per cent of public sector expenditure, while their own-source revenue represents only 4 per cent of their total revenue and 2 per cent of total public revenue.

In other developing countries globally, own-source revenue accounts for an average of 58 per cent of subnational government revenue.

Accordingly, own-source revenue does not play the expected positive role in stimulating efficiency in public service delivery. Increased fiscal decentralization and greater revenue autonomy could lead to improved service delivery by enhancing transparency and shifting accountability from the central government to the local level, which is closer to the people being served.

Source: Elhiraika (2007).

are also communication and coordination failures between government departments at the same level. The lack of clarity, consultation and cooperation erodes trust in public institutions and thus weakens their authority.

Lack of clarity about the degree of autonomy granted to local government authorities exacerbates the arbitrariness of non-tax revenue collection. Absent sound management structures, local governments have used multiple fees, fines and charges almost at will, opening up opportunities for mismanagement and arbitrary action by corrupt bureaucrats. Thus, in addition to building institutional, administrative and regulatory mechanisms for the efficient collection and allocation of non-tax revenue, governments need to establish a strong legal framework to work against corruption.

In Zimbabwe local authorities sometimes retain revenue that is intended to flow to the central government (ECA, 2018h). Among the reasons for this behaviour are the absence of appropriate legal arrangements and the failure of the central government to transfer resources intended for local authorities. In addition, Zimbabwe levies a range of fees and other charges on citizens for basic utilities and services that should be free—and that are often substandard in quantity and quality. Consumers who object to the poor delivery or refuse to make further payments until service improves are often assessed penalties.

The design of a well-functioning subnational revenue system is complex but could be rewarding for local development. An amicable and fair relationship between levels of government is essential for the smooth transfer of grants and other funds from the centre (Bird and Smart, 2002; Martínez-Vázquez and Smoke, 2010). Most efforts at fiscal decentralization have focused on devolution of taxing and spending power, so there is limited evidence on the impact of decentralization of non-tax revenue collection and spending.

Greater revenue autonomy for subnational governments could enhance public service delivery by increasing the accountability and transparency of policymakers and service providers.

GOVERNANCE OF REVENUE FROM NATURAL RESOURCES

An encouraging development in revenue management is the number of African countries that have signed on to the Extractive Industries Transparency Initiative (EITI), which seeks to increase the transparency of government revenue collection and spending and thus to increase public understanding of how revenue is collected and spent. The initiative, which relies on voluntary compliance, sets standards for revenue disclosure primarily for non-tax revenue sources such as royalties, dividends, license fees, rental fees, entry fees, and any other substantial payments and material benefits to government. The focus on extractive industries has been instrumental in increasing revenue disclosure by resource-rich countries.

To date, compliance has been uneven. For instance, Nigeria's EITI audits in 2016 revealed inconsistencies and delays in dividend payments on transfers from the state-owned Nigerian National Petroleum Corporation and the government (EITI, 2016). Several countries have been suspended from EITI in recent years for compliance failures, including Central African Republic from 2013 to 2015, Côte d'Ivoire from 2012 to 2014 and Madagascar from 2011 to 2014.

However, compliance by most African countries is improving, including in Côte d'Ivoire since 2014, where peace and economic development are restoring lost gains. Overall, the current situation and future outlook are positive for Burkina Faso, Chad, Ghana, Liberia, Malawi, Mauritania, Mozambique, Niger, Nigeria, Togo and Zambia.

While signing onto the EITI is a good start, for non-tax and other revenue streams to have a transformational impact requires integrity in reporting revenue streams on the part of political leadership, multinational firms and all stakeholders. The payments made to governments by resource-extracting companies should be fully reported and monitored by both parties. Civil society organizations can exert pressure to see that this happens, and their activities should be respected and protected. Governments need to cooperate with civil society organizations to make the initiative more effective.

By addressing institutional challenges (for example, solving the coordination problem among institutions in recording and reporting revenue), building a culture of transparency and accountability and improving reporting of non-tax revenue at a disaggregated level, countries could advance sustainable growth in Africa.

...the current voluntary compliance situation and future outlook are positive for countries such as Burkina Faso, Chad, Ghana, Liberia, Malawi, Mauritania, Mozambique, Niger, Nigeria, Togo and Zambia.

POLITICAL ECONOMY ISSUES

Several political economy issues affect the volume and volatility of non-tax revenue. For example, changing donor priorities can reduce funds for budget support and other development funds, while the suspension or removal of African countries from the Generalized System of Preferences can reduce revenue. Other political economy issues that affect non-tax revenue mobilization are the provisions in complex mineral agreements governing royalty payments and contract renegotiation, capital flight and money laundering.

CONCLUSIONS AND POLICY IMPLICATIONS

African governments are facing rising debt as well as an increased need for financing to achieve the SDGs and Agenda 2063. Efforts to improve revenue collection need to focus on non-tax revenue mobilization as well as taxes in a search for innovative ways to finance development. Many domestic resource mobilization efforts have concentrated on boosting tax revenue and improving the administrative efficiency of tax institutions; little systematic attention has gone to non-tax revenue collection.

Non-tax revenue contributes significantly to government revenue in Africa, averaging 4.5 per cent of GDP, yet a majority of countries collect below their potential, with an average non-tax revenue effort of 0.64. Improving countries' collection efficiency in low-collecting countries in particular could boost their average non-tax revenue to 4.5 per cent of GDP, from the average 2.6 per cent.

Though countries use a wide range of non-tax revenue instruments (from levies on natural resources extraction to pollution fees), innovation and diversification of instruments are inadequate in most countries. The heterogeneity of country contexts and the complexity of non-tax revenue

frameworks mean that solutions are best developed on an individual country basis. Countries should design non-tax revenue instruments that best match their economic structure, development objectives and target groups.

Diversification requires attention to consequences. For instance, user charges have wide-ranging welfare impacts. The OECD (1998) has identified best practice guidelines for implementing user charges that can be adapted to the context in which they are introduced: clear legal authority, iterative consultation with users, knowledge of full costs, effective and efficient collection system, monitoring of organizational performance, treatment of receipts, pricing strategies, equity considerations (are the planned instruments regressive or progressive?) and competitive neutrality.

Countries need to establish the right mix in public financing among taxes, grants, intergovernmental transfers and user charges that will result in sustainable and predictable revenue streams. Due diligence, clear guidelines and built-in regulatory systems are needed to design an effective structure of non-tax revenue. Chad and other countries that have recognized the fiscal importance of mobilizing non-tax revenue are putting such policies in place (ECA, 2018a).

Improving countries' collection efficiency could boost their average non-tax revenues to 4.5 per cent of GDP, from 2.6 per cent.

Countries must also prepare for the volatility of non-tax revenue. Commodity prices fluctuate, and grants and miscellaneous sources of non-tax revenue are hard to predict or plan for. Prudent financial management practices can help buffer the impact of volatile non-tax revenue.

Other reforms are also needed to strengthen non-tax revenue mobilization, including investment in infrastructure, better reporting of non-tax revenue collection and clearer relationships between the centre and subnational authorities. Countries need to adapt international standards for non-tax revenue mobilization to their individual context and apply good governance practices to improve institutions, policies, and regulatory and administrative processes.

Countries need to establish the right mix in public financing among taxes, grants, inter-governmental transfers and user charges that will result in sustainable and predictable revenue streams.

ANNEX 4.1 VOLATILITY IN NON-TAX REVENUES

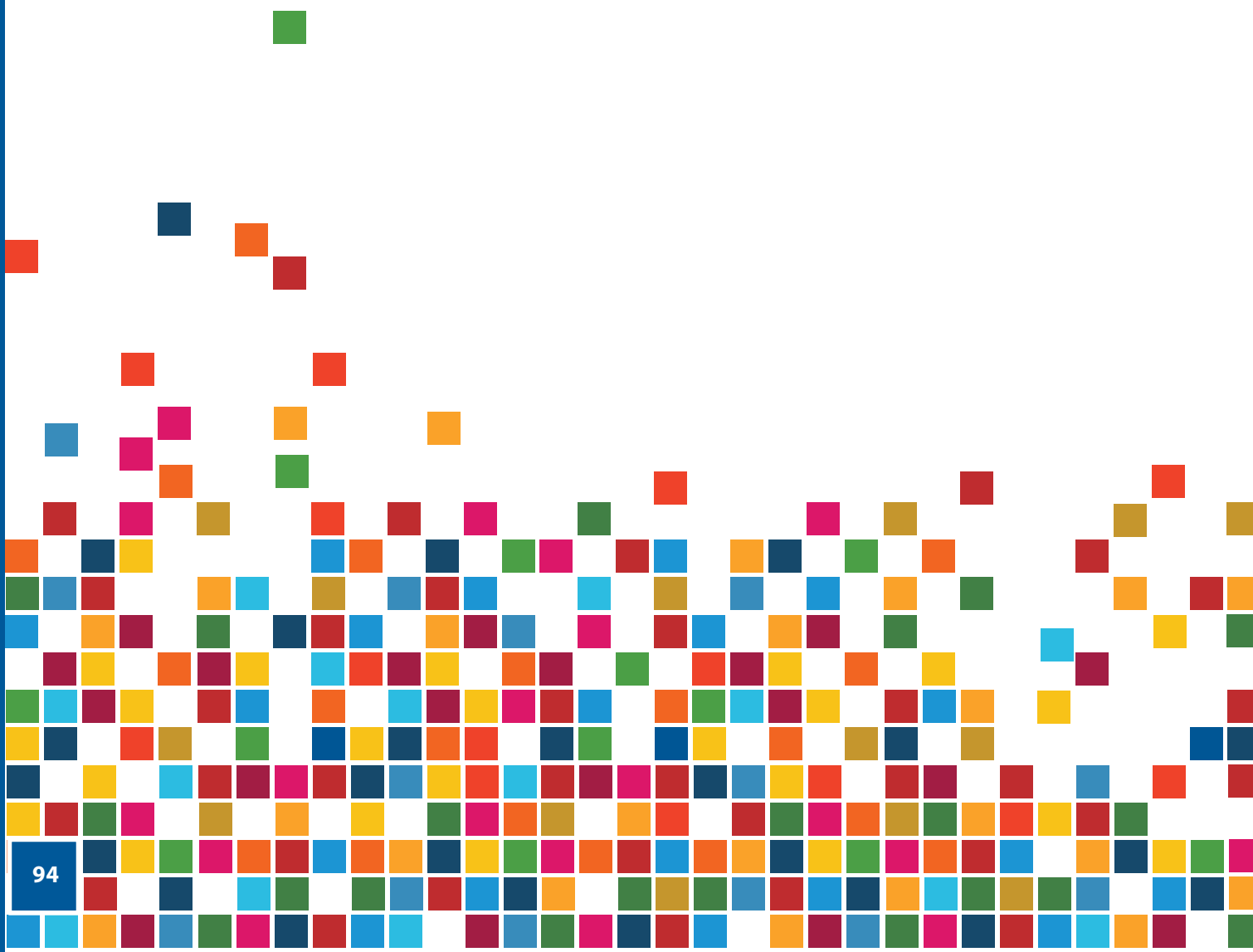
TABLE A4.1. SUMMARY OF TRENDS AND VOLATILITY IN NON-TAX REVENUES AS A SHARE OF GDP, 1997–2018

COUNTRY	TREND	DEGREE OF VOLATILITY
Algeria	Rising	Low
Angola	Constant and below 5 per cent (not improving)	Low
Cameroon	Declining	Low
Central African Republic	Declining	Low
Côte d'Ivoire	Rising but at low levels	Low
Mozambique	Rising steadily	Low
Rwanda	Steadily rising	Low
Botswana	Declining but still above 10 per cent	Moderate
Burkina Faso	Declining then rising slightly	Moderate
Cabo Verde	Rising	Moderate
Egypt	Declining	Moderate
Eswatini	Dramatic decline	Moderate
Gabon	Slightly rising but at very low level	Moderate
Gambia	Rising steadily	Moderate
Ghana	Rising slightly	Moderate
Equatorial Guinea	Declining steadily	Moderate
Kenya	Declining	Moderate
Lesotho	Erratic and declining recently	Moderate
Mauritius	Declining	Moderate
Morocco	Rising	Moderate
Niger	Rising	Moderate
Nigeria	Sharp decline but few data points	Moderate
Senegal	Rising steadily	Moderate
Sierra Leone	Erratic	Moderate
South Sudan	Rising but only five data points	Moderate
Sudan	Declining recently	Moderate
Tanzania	Declining	Moderate
Zambia	Rising	Moderate
Benin	Erratic but rising the last few years	High
Burundi	Declining	High
Chad	Rising	High
Congo	Declining	High
Comoros	Rising	High
Democratic Republic of the Congo	Rising	High
Djibouti	Rising	High
Eritrea	Declining but with few data points	High
Ethiopia	Declining	High
Guinea	Erratic at low levels	High
Guinea-Bissau	Erratic but mainly on declining trend	High
Liberia	Erratic and declining recently	High
Madagascar	Erratic but rising recently	High
Malawi	Erratic but rising recently	High
Mali	Rising erratically at low levels	High
Mauritania	Erratic but rising	High
Namibia	Erratic and declining recently	High
Seychelles	Declining	High
South Africa	Declining recently and at a low level	High
Togo	Erratic	High
Tunisia	Declining	High
Uganda	Erratic	High
Zimbabwe	Declining	High

Source: Based on data from ICTD and UNU-WIDER (2018), accessed in September 2018.

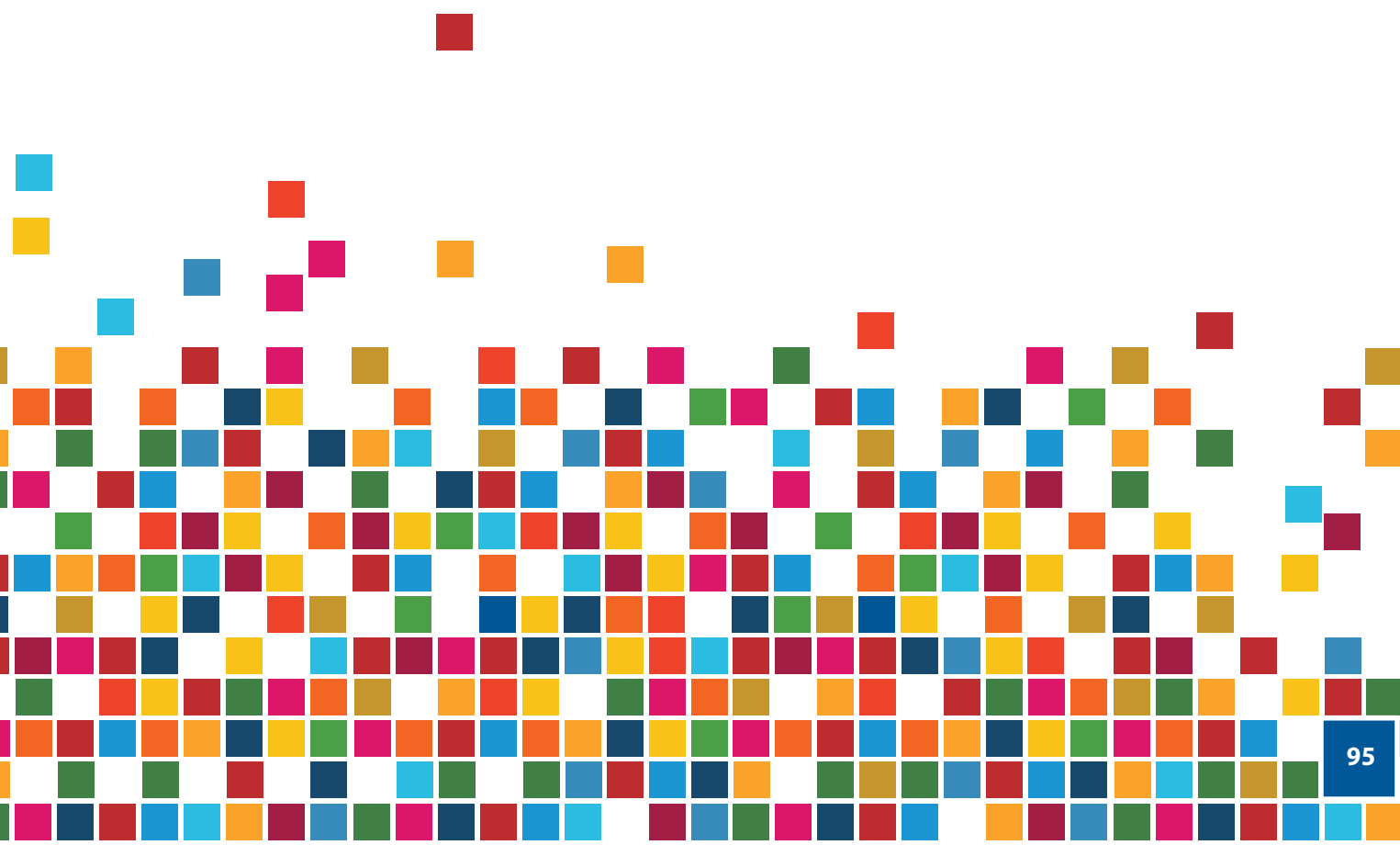
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CHAPTER 5

TAX ADMINISTRATION IN AFRICA



African countries have made extensive efforts to improve the effectiveness and efficiency of tax administration. These efforts need to be sustained and strengthened, especially in promoting tax compliance.

While each country also needs to address its unique challenges in tax administration, all of them need to strengthen the use of data to inform decision making and improve the efficiency and effectiveness of tax administration. One promising tool to guide these efforts is the Tax Administration Diagnostic Assessment Tool (TADT).

Countries should take full advantage of the opportunities for greater efficiency and effectiveness offered by digitalization. So far, 18 African countries have introduced electronic tax filing and payment systems. Rwanda was able to boost tax revenue by 6 per cent through such measures, suggesting the large scope for revenue gains in countries that have not yet done so. In South Africa, e-taxation lowered the time (by 21.8 per cent) and cost (by 22 per cent) of complying with the value-added tax (VAT). In Kenya, digitization of VAT operations helped identify data inconsistencies and raised VAT collections by more than \$1 billion between 2016 and 2017.

INTRODUCTION

Tax administration is the execution of the core activities for collecting taxes:

- Identifying “taxable subjects” (individuals or business enterprises).
- Assigning unique identifiers that make it possible to recognize them in future.
- Creating a system of records on taxable subjects.
- Establishing the procedures for taxable subjects to transfer to the tax agency the information needed to assess their tax liabilities (“filing”).
- Regularly assessing tax liabilities.
- Billing taxpayers accordingly.
- Collecting payments.
- Dealing with non-payments, arrears and refunds.
- Auditing the tax assessments of samples of taxpayers.
- Resolving disputes between taxpayers and tax collectors.

While there is limited quantitative information on the comparative performance of national tax administrations, data in the annual *Paying Taxes* report of the World Bank and PwC (2018) give a sense of the performance of African countries. The picture is mixed.

In 2016, Africa had the highest number of tax payments averaging 35.4 payments a year, compared with the global average of 20.6 (table 5.1). Africa also had the second longest compliance time for major taxes (profit taxes, labour taxes and mandatory contributions, and consumption taxes), at 285 hours compared with the global average of 240 hours. The high number of



In 2016, Africa had the highest number of tax payments, averaging 35.4 payments a year, compared with the global average of 20.6.

TABLE 5.1. REGIONAL DIFFERENCES IN TAX ADMINISTRATION PERFORMANCE, 2016

REGION	NUMBER OF TAX PAYMENTS	TIME TO COMPLY (hours)	POST-FILING INDEX ^a (distance to frontier; 0 = least efficient, 100 = most efficient)
Africa	35.4	285	55.6
Asia Pacific	22.1	204	56.7
Central America and the Caribbean	31.2	206	51.9
Central Asia and Eastern Europe	16.2	230	62.0
Europe	12.0	161	81.6
Middle East	17.2	154	46.5
North America	8.2	182	69.3
South America	22.8	547	41.7
World average	24.0	240	58.0

a. This index measures two processes that might take place after filing: claiming a value-added tax refund and correcting an error on a corporate income tax return, including going through an audit. Distance to frontier is a measure of the region's distance from the best observed performance.

Source: Based on data from World Bank and PwC (2018).

payments and long time to complete them increase the burden of tax collection for tax administrations.

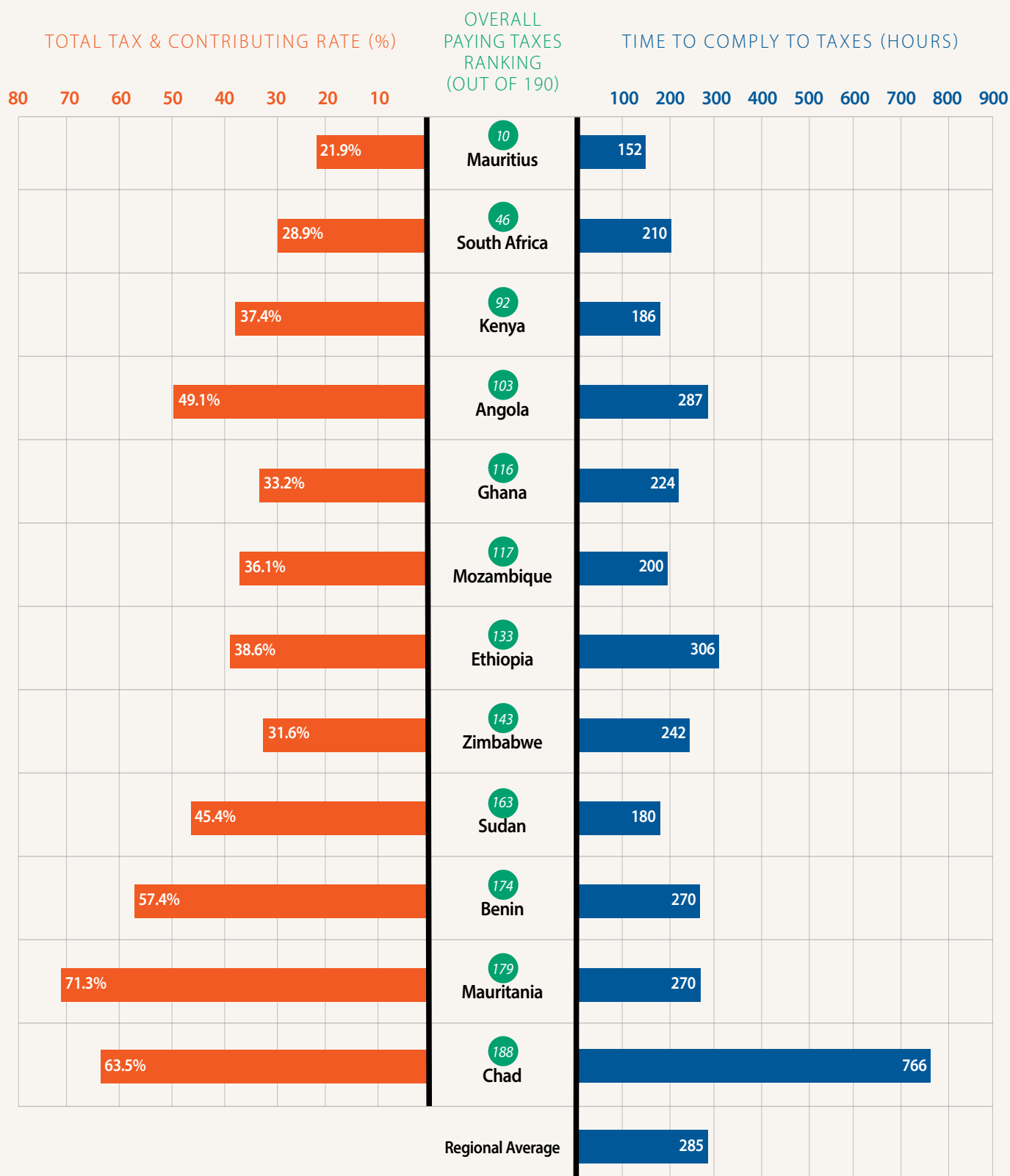
However, Africa performs well on another measure of tax administration, the post-filing index, which measures two processes that might take place after filing: claiming a VAT refund and correcting an error on a corporate income tax return, including going through an audit. For 2016 Africa scored the same as the Asia Pacific region and better than South America, the Middle East, and Central America and the Caribbean (World Bank and PwC, 2018). While Africa is starting from a moderately encouraging position, there is considerable room to improve tax administration in most countries (figure 5.1 and table A5.1 in the annex).

This chapter assesses tax administration in Africa, highlighting progress and challenges and identifying ways to enhance efficiency and effectiveness.

PURPOSE AND FUNCTIONS OF TAX ADMINISTRATION

Modern tax administrations attempt to collect adequate revenue while keeping tax administration and compliance costs low and treating taxpayers fairly. The most cost-effective systems are those that convince the vast majority of taxpayers to meet their tax obligations voluntarily, so that tax officials can concentrate on the small number who do not comply. Features of the tax administration that encourage compliance include a service-oriented attitude that educates and assists taxpayers in meeting their obligations, effective audit programmes and consistent use of penalties as strong deterrents to non-compliance, and transparent administration of the tax laws that is viewed as honest and fair (Okello, 2014).

FIGURE 5.1. STATUS OF TAX ADMINISTRATION INDICATORS FOR SELECT COUNTRIES, 2018



Source: Based on data from World Bank and PwC (2018).

Successful tax collection depends on the tax administration's effective performance of several supporting tasks, including human resource management (recruitment, training, posting and promotion); internal vigilance in identifying, controlling and punishing staff misbehaviour, especially corruption; treasury activities, including managing and accounting for revenue collected; and taxpayer education and outreach activities.

Tax administration and tax policy are closely related. Tax policy needs to take into consideration tax administration capabilities, while tax administration may result in actual tax policy differing from formal tax policy. For example, the declared policy may state that all doctors in private practice must declare their incomes and pay personal income tax. However, if the tax agency makes little effort to register doctors, fails to ensure that they routinely file tax returns or never audits suspicious tax returns, then the actual policy is that doctors' private practice earnings are not taxed as personal income.

There are also organizational dimensions that distinguish tax administration and tax policy. The global norm is that the two activities should be organizationally separate: one agency should set tax policy, and another should implement it. Globally and throughout most of Africa, tax policy is formally the responsibility of a tax policy unit in the ministry of finance, while revenue is collected by separate units under the direct control of the ministry or by a semi-autonomous agency.

It is difficult to define clear principles for dividing responsibilities between tax policy units and tax administrations. For example, is a decision to increase resources for auditing tax returns a policy issue or purely an administrative or managerial matter? It seems at first glance to be administrative. But if auditing is rarely or badly done, and a large increase in resources holds reasonable promise of improving compliance and revenue collection, then it is arguably more of a policy issue.

While Africa is starting from a moderately encouraging position, there is considerable room to improve tax administration in most countries.



Tax policy units and tax administrations should cooperate closely. This means that the specialists in tax policy units should respect the operational knowledge of the senior staff of tax administrations and that the senior administrative staff should provide the tax policy specialists with the detailed data needed for policy-relevant analysis. This cooperation is not always forthcoming in Africa. Interorganizational rivalries are sometimes intense,¹ and other factors also colour the relationship in diverse ways. Where there is an imbalance in power between the two organizations, it tends to favour tax administrations, particularly when they are organized as a semi-autonomous revenue authority and outside the direct control of the minister of finance. Twenty years ago many African ministries of finance lacked tax policy units. While that is no longer true, they tend to be underpowered relative to tax administrations.

STRUCTURE OF TAX ADMINISTRATION

There has been some convergence towards global best practice in tax administration in Africa, and today's collection processes are less diverse than they were 20 or 30 years ago. But convergence has been partially masked by the major organizational reform that has been implemented in almost half of

¹ This is especially likely if revenue collection is undertaken by a semi-autonomous revenue agency whose staff are paid much more than those in comparable jobs within the ministry of finance.

the countries over that period: the creation of unified semi-autonomous revenue authorities.² The other countries in Africa have retained their organizational structure, with two or three departments within the ministry of finance responsible for collecting different categories of taxes.

THE EMERGENCE OF SEMI-AUTONOMOUS REVENUE AUTHORITIES

Second only to the introduction of the VAT, the most visible tax reform in Africa since the early 1990s has been the creation of semi-autonomous revenue authorities. This has involved a substantial change in the organization of tax collection:

- Existing revenue collection organizations—typically two to four departments in the ministry of finance—were merged into a single agency.
- This agency is removed from the direct control of the ministry of finance and given semi-autonomous status under a separate management board.

The notion that central banks, revenue authorities and other important fiscal, financial and regulatory organizations should be apart from direct government control has its roots in the New Public Management reforms that were fashionable in the Anglophone world from the 1990s on. Such semi-autonomous revenue authorities are nearly universal in Anglophone Africa and have also spread to Burundi, Mozambique, Rwanda and Togo. Their establishment was stimulated by funding and technical assistance from the World Bank and the UK aid programme.

The creation of these semi-autonomous revenue authorities was often met with considerable resistance and tension. Their impact continues to be debated. A number of factors complicate the

debate. First, their creation did not occur in isolation. It was part of a package of reforms in tax policy and administration and was intended to facilitate those wider reforms. Second, the organization change was accompanied by large increases in salary for the staff of the new semi-autonomous revenue authorities,³ who today are often paid three to four times as much as counterparts in the ministry of finance with whom they interact. Their high salaries generate resentment. They also help explain why the costs of tax collection are so high in Africa. Third, there is no single semi-autonomous revenue authority model. They are diverse organizations, and their relationships to other parts of government, notably to the ministry of finance, vary across countries and over time (table 5.2). These variations mean that there is no reason to expect that semi-autonomous revenue authorities would have similar effects in all countries.

Semi-autonomous revenue authorities are in practice much less autonomous than their original proponents expected or intended them to be. To the extent that the people who manage them enjoy some autonomy, it relates mainly to (lower level) managerial issues—for example, who they recruit and how and how they deploy their staff. For major decisions, including pay structures, they are typically very much under the control of the ministry of finance or the president.⁴ And they do not seem generally to be immune from political interference.

At the same time, the high salaries and attractive working conditions have enabled some semi-autonomous revenue authorities to hire more skilled workers, who sometimes play an active role in issues that are formally the remit of the ministry

² The extent of divergence hints at some bad practices and positive scope for reform. For example, in a sample of 16 countries studied by the African Tax Administration Forum, the number of taxpayers per tax administrator averaged 202 in Africa, ranging from about 30 in Togo to 961 in Mozambique (ATAF, 2017, figure 8.7). The Mozambique Revenue Authority registers all potential taxpayers, even those who do not file tax returns or make payments.

³ In some cases, the establishment of semi-autonomous revenue authorities led to large-scale dismissals of existing tax collectors. In other cases, most existing staff were transferred to the new organization.

⁴ When applied to an organization such as a revenue authority that is ultimately answerable to government, the concept of “autonomy” eludes easy definition. One theoretical study suggests that autonomy can be measured along six dimensions: managerial, policy, structural, financial, legal and interventional (the extent of reporting requirements against pre-set goals; Verhoest et al., 2004).

TABLE 5.2. ORGANIZATIONAL LOCATION OF REVENUE AUTHORITIES IN THE CASE STUDY COUNTRIES

COUNTRY	TAX ADMINISTRATION AUTHORITY	SEMI-AUTONOMOUS STATUS (yes or no)	LOCATION AND MANDATE OF REVENUE AUTHORITY
Angola	Administração Geral Tributária (AGT)—The General Tax Administration	Yes, under the Ministry of finance	Its mission is to propose and execute government tax policy and ensure full compliance; administer taxes, customs duties and other taxes as assigned; and study, promote, coordinate, execute and evaluate tax policy programmes, measures and actions related to the organization, management and improvement of the tax system.
Benin	Direction Générale des Impôts (DGI)	No	In charge of determining the basis, liquidation, control and litigation of all taxes provided for in the Tax Code; the recovery and repayment to the public treasury of taxes and state fees and ancillary taxes; tax audits; land conservation, mortgages and other land rights; management of the state private domain; and evaluation of the administrative accounts and the management of its entire accounting network.
Chad	Direction Générale des Impôts (DGI)	No	A department in the Ministry of Finance.
Ethiopia	Ethiopian Ministry of Revenue (EMOR)	Fully autonomous	Responsible for collecting revenue from customs duties and domestic taxes.
Ghana	Ghana Revenue Authority (GRA)	Yes	A corporate body established to replace the Customs, Excise and Preventive Service; Internal Revenue Service; Value Added Tax Service; and the Revenue Agencies Governing Board Secretariat for the administration of taxes and custom duties. This represents a change in identity for the revenue agencies and unifies the administration of taxes and customs duties in Ghana. The merger of the three revenue agencies into an integrated and modernized revenue authority is part of a worldwide trend to achieve efficiency and effectiveness.
Kenya	Kenya Revenue Authority (KRA)	Yes	Responsible for collecting revenue on behalf of the government, focussing on assessment, collection, administration and enforcement of laws relating to revenue.
Mauritania	Direction Générale des Impôts (DGI)	No	A department in the Ministry of Finance. Responsible for mobilizing revenue for the government by participating in the definition of tax policy and the drafting of legislative and regulatory texts, including the finance laws; identifying, locating and registering taxpayers by assigning them a tax identification number; establishing the tax base, licences and their recovery; combatting fraud through tax audits; handling the tax claims of taxpayers; and representing Mauritania in international bodies in charge of tax issues.
Mauritius	Mauritius Revenue Authority (MRA)	Yes	MRA is an agent of state and as such the Ministry of Finance and Economic Development continues to have overall responsibility for MRA and monitors its performance. MRA is responsible for collecting approximately 90 per cent of tax revenue and for enforcing tax laws.
Mozambique	Autoridade Tributária de Moçambique (AT)—Mozambican Tax Authority	No	A department under the direct control of the Ministry of Finance.
South Africa	South African Revenue Service (SARS)	Yes	Established under the South African Revenue Service Act 34 of 1997 as an autonomous agency, responsible for administering the South African tax system and customs service and collecting taxes.
Sudan	Sudan Taxation Chamber (STC)	No	Established in 1954 as a section in the Ministry of Finance. It is now a department under the same ministry.
Uganda	Uganda Revenue Authority (Authority)	Yes	A government revenue collection agency established by the Parliament. Operating under the Ministry of Finance, Planning and Economic Development. Mandated to assess, collect and account for Central Government Tax Revenue (includes Non-Tax Revenues) and to provide advice to government on matters of policy relating to all revenue sources.
Zimbabwe	Zimbabwe Revenue Authority (ZIMRA)	Yes	Under the Revenue Authority Act and other subsidiary legislation is responsible for assessing, collecting and accounting for revenue on behalf of Zimbabwe through the Ministry of Finance. Collected taxes include customs duties, value-added taxes, excise duties, income taxes, pay-as-you-earn taxes; mining royalties; capital gains taxes; and others.

Source: Based on data from national revenue agencies, ATAF (2017) and the International Survey on Revenue Administration.

of finance, such as tax policy analysis, advocacy activities and public outreach activities to explain taxes to citizens (von Soest, 2007). The divergence in salaries and other forms of remuneration from those of colleagues in the ministry of finance can become an obstacle to cooperation and the effective governance of taxation more broadly.

ASSESSING THE PERFORMANCE OF TAX ADMINISTRATION

A basic measure of tax administration performance is total revenue collection (tax and non-tax) as a share of GDP (see chapters 3 and 4). A more sophisticated measure is tax effort, which is the ratio of actual revenue collected to the amount expected to be collected given the structure of the national economy.

During 1991–2006 average tax effort was 75 per cent for 14 Sub-Saharan Africa countries, higher than the average for 6 Latin American countries (59 per cent) and 4 South Asian countries (51 per cent; IMF, 2011: 59–60). A more recent analysis covering 120 developing countries over 1990–2012, which also takes into account the potential depressing effect of economic vulnerability on tax collection, assessed the average tax effort of the elected countries as “outstanding” (Yohou and Goujon, 2017: 1). These countries are converging towards global benchmarks in tax administration.

Globally, job turnover among heads of revenue administrations is very high, which is likely to adversely affect the performance of tax administration. Over 2009–2013 the turnover rate in Africa was about the same as in Europe and the Middle East and Central Asia and considerably lower

than in Latin America and the Caribbean and Asia Pacific (IMF, 2011). There is also evidence that tax reforms over the past decade have strengthened the belief among Africans that governments have a right to tax them (Moore, Prichard, and Fjeldstad, 2018).

But shortcomings remain pervasive. Indirect taxes such as the VAT, which have broad tax base advantages, are now common in Africa. However, poor design and implementation mean that collection costs are unusually high as a percentage of total collection, indicating poor linkages between policy and administration in Africa.

The International Monetary Fund (IMF)-sponsored Tax Administration Diagnostic Assessment Tool (TADAT) framework is focused on nine key performance outcome areas that cover most tax administration functions, processes and institutions (figure 5.2).⁵ Country TADAT Performance Assessment Reports are confidential, however, unless a government makes them public. Of the 29 African countries that have undergone TADAT assessments, only 3 (Burkina Faso, Liberia and Zambia) have made their assessment reports public.⁶ The observation that standards of tax administration vary widely within Africa is therefore based mainly on a diverse range of “soft” evidence.

Morocco and South Africa are the top performers in tax administration. While they collect fairly

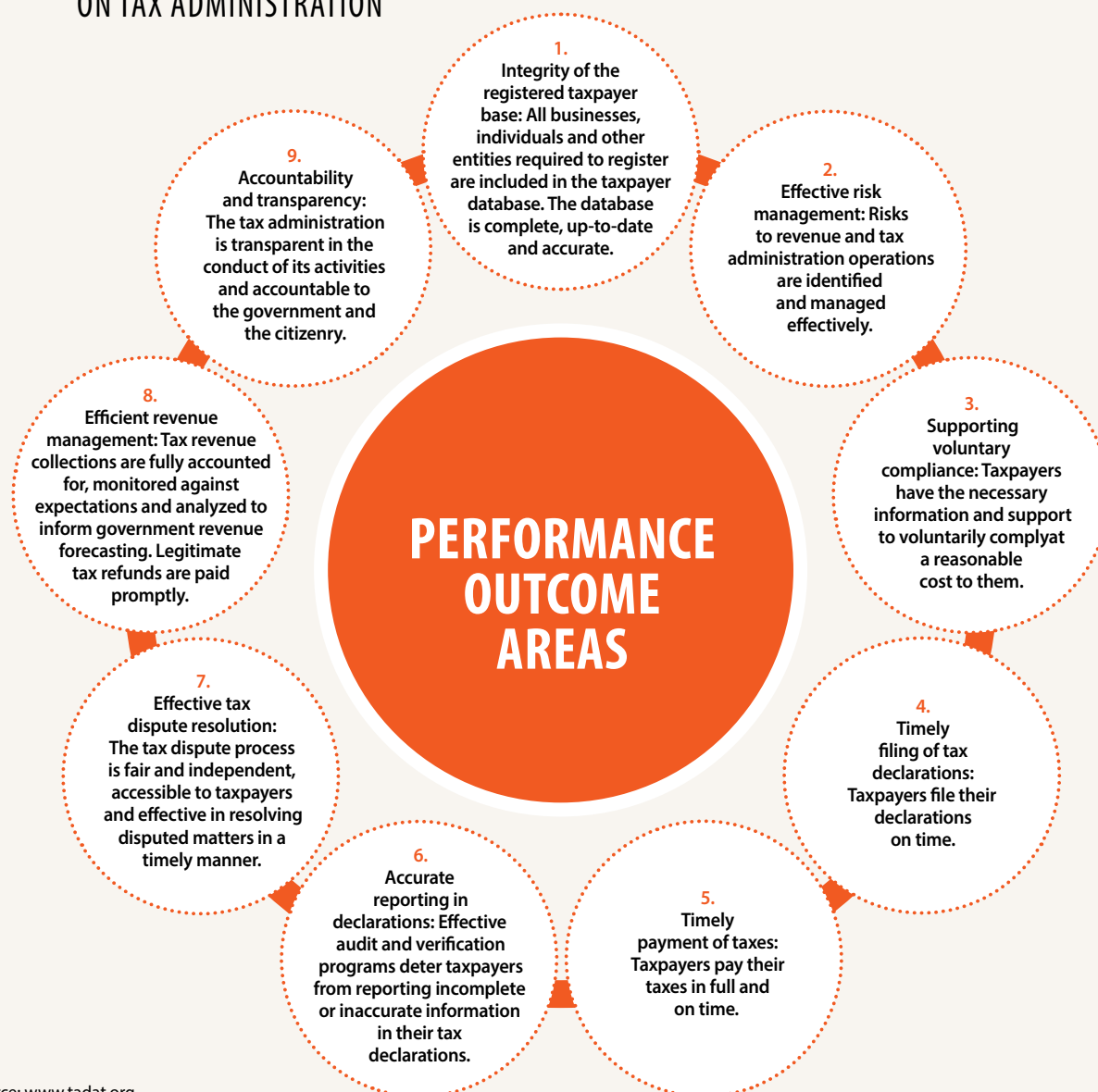
5 The IMF sponsored the development of the Tax Administration Diagnostic Assessment Tool (TADAT) and the training of specialists who assess and score national tax administration country by country.

6 Angola, Burkina Faso, Burundi, Cameroon, Comoros, Côte d'Ivoire, Democratic Republic of the Congo, Egypt, Ethiopia, Gambia, Ghana, Kenya, Liberia, Madagascar, Malawi, Mauritius, Morocco, Mozambique, Namibia, Niger, Nigeria, Rwanda, Sierra Leone, South Africa, Tanzania, Tunisia, Uganda, Zambia and Zimbabwe; see <http://www.tadat.org/files/TADAT-Assessments-NOV2018.pdf>



During 1991–2006 average tax effort was 75 per cent for 14 Sub-Saharan Africa countries, higher than the average for six Latin American countries and four South Asian countries.

FIGURE 5.2. THE TAX ADMINISTRATION DIAGNOSTIC ASSESSMENT TOOL IS A DATA COLLECTION TOOL ON TAX ADMINISTRATION



Source: www.tadat.org.

high revenue as a share of GDP, that alone does not define them as high performers—tax administrations in other African countries collect higher proportions of GDP in revenue despite indifferent standards of tax administration.⁷ Morocco also has the lowest number of tax payments, followed by South Africa (see table

A5.1 in the annex). Both tax administrations collect revenue fairly efficiently, seek to help and encourage taxpayers to be more compliant and, unlike most tax administrations in Africa, devote considerable resources to analysing data collected through routine operations, with a view to making operations more efficient. Kenya is another example of good practice for other African tax administrations.

At the other end of the performance scale are

⁷ This is especially likely in resource-exporting countries, such as Angola. Over the past decade, government revenue has been at typical OECD levels of 35–40 per cent of GDP.

■ Some African countries are well ahead of others and are increasingly able to provide technical assistance to other countries in the region. ■

Somalia and Nigeria. In Somalia security risks prevent the government from collecting much more than some limited customs revenue from Mogadishu port and airport. Nigeria is in a less parlous position, but its tax administration has deteriorated since the 1960s, as revenue from oil production began to eclipse all other sources of revenue, which were soon neglected. Estimates of how much revenue Nigeria collects vary—7 per cent of GDP is widely quoted—attesting to the poor average quality of tax administration.⁸ Good tax administrations report accurately how much money they collect and remit to the treasury.

Overall, the standards of national tax administrations in Africa range from similar to those in Organisation for Economic Co-operation and Development (OECD) countries to very poor. This diversity should be kept in mind in discussions of potential tax administration reforms. Some African countries are well ahead of others and are increasingly able to provide technical assistance to other countries in the region. This is especially so in the use of digitalization and electronic tax filing to improve efficiency and effectiveness.

⁸ Nigeria is one of the few countries in Africa where there has been considerable *de facto* privatization of revenue collection. This has occurred at the state rather than at the federal level, and accurate information is not available.

TAX ADMINISTRATION REFORMS

The global consensus on tax administration reform since the 1980s reflects mainly the experiences of tax professionals,⁹ but with little input from those in Africa and other low-income regions, which have been recipients rather than initiators of reforms (Fjeldstad and Moore, 2008). This global consensus has been neither consistently questioned nor explicitly rejected in Africa, though it has met greater resistance in Francophone countries, no doubt because of the reforms' Anglophone roots.¹⁰ Except in appeals to traditional practices, there is no consistent or coherent alternative vision of tax administration to that of the global Anglophone consensus.

This new global consensus has evolved less as doctrine than as a set of best practices that reflect interactions between tax administration and changes in forms of economic activity, digitalization and introduction of the VAT. Six important features of the way best practices are now understood in tax administrations in Africa are discussed below.

PRIORITY SHIFT: FROM POLICY TO ADMINISTRATION

The new consensus on tax reform that took shape in the 1970s and 1980s emphasized the importance of taking tax administration into account when designing tax policy. This was

⁹ There is not the same degree of consensus in relation to international tax issues. These remain very contested.

¹⁰ We do not have sufficient quantitative evidence to test the claim that change has been less extensive in the Francophone countries. There is some relevant information in Fossat and Bua (2013), who suggest that Francophone Africa has been particularly slow in digitizing tax administration functions. It also seems that the Francophone tradition of maintaining dense networks of local tax offices to maintain close direct and personal contact with taxpayers has not given way to the kinds of organizational reforms, discussed in the main text, that in Anglophone countries have led to a shift of personnel and functions to head offices. There is some indirect evidence for this in the figures that are available on the ratio of taxpayers to tax administration staff in a sample of African countries in 2015. That ratio was generally lower in the Francophone countries (ATAF, 2017).

a reaction against previous tax policies, which in many countries were intended to achieve ambitious social and economic goals (including income redistribution) in addition to raising revenue. Reformers believed that the attempts to use the tax system as an instrument of social and economic change were generally ineffective and had had adverse side effects, including the creation of complex tax codes that were difficult to implement and prone to corruption. In the new orthodoxy, tax policy and tax administration were expected to focus more on raising revenue. Reformers emphasized simplification.

FROM PHYSICAL VERIFICATION TO ANALYSIS OF RECORDS AND ACCOUNTS

Methods of tax collection have also changed. Thirty years ago, in most of Africa as in many other parts of the world, tax collection involved tax collectors visiting taxpayers in their homes and businesses to verify their economic activities, assess their tax obligations and often to collect payment. While this emphasis on physical verification and face-to-face assessment is still evident in many parts of Africa today, especially in customs administration, that is not the norm for progressive tax administrations in Africa, nor is it the vision for the future of tax collection.

There has been a shift from physical verification—and from the accompanying opportunities for collusion between tax collectors and taxpayers—towards office-centred assessment systems that require little direct interaction with taxpayers and are based on the analysis of written or digitalized records and business accounts. The process of assessing dues has also been separated from the process of paying taxes. Increasingly, payments are made to banks and other collection agents, to dedicated front-desk bill payment facilities within tax offices or on-line (Moore, 2014).

These changes in methods of tax collection reflect changes in the structure of national economies and in available technologies. Visits by tax collectors to inspect and verify production facilities and

production may make sense for agriculture and manufacturing, where there is something to see, but little sense in increasingly service-oriented economies, where there is much less to see. The information tax administrations need is found in written or digital records and accounts.

Related trends such as globalization, including the proliferation of global production chains, and wider use of banks and other financial services also contribute to changes in tax collection. They render production and value added less visible to the eye, while simultaneously increasing the volume of written or digital records on economic transactions.

Digitalization also increases access to business records and greatly reduces the cost of analysing them. For example, it is increasingly easy for tax administrations to access and use third party sources to cross-check taxpayers' submissions (such as bank and credit card accounts; telephone bills; electricity, water and other public utility bills; motor vehicle sales and registrations; real estate transactions; government procurement processes and company ownership and dividend payments).

INTRODUCTION OF THE VALUE-ADDED TAX

Convergence in tax administration reform in Africa has to a large extent been driven by the shift from a dependence on trade taxes to reliance on the VAT. Getting countries to introduce the VAT was the main focus of tax reforms efforts by international organizations and aid donors since the 1980s.

Until the 1970s and 1980s taxes on international trade (imports and exports) were the major source of revenue for most African governments, in large part because of the prominent economic role of commodity exports. The secular decline of global commodity prices raised alarms about this dependence. International organizations argued that trade taxes were a serious obstacle to more efficient economic specialization and long-term economic development in Africa and that they should largely be replaced by the VAT. That

The VAT will continue to be contentious in Africa. But whatever its general appropriateness to the continent, it seems likely that—along with the simultaneous paring down of trade taxes—its introduction has given a boost to the modernization of African tax administration.

narrative, backed by the power of aid, was generally persuasive. Most African countries slashed trade taxes and introduced the VAT.¹¹

The change was not without controversy, however, as doubts were raised about the VAT's appropriateness for Africa. The VAT is a complicated tax. It requires taxpayers, many of them small retailers and other small businesses, to keep extensive accounts and issue invoices. It involves detailed schedules about which goods and services are subject to which VAT rate, which are zero rated and which are exempt. It requires tax administrations to collect more data than before and, at least in principle, to put more resources into verifying data by checking samples of invoices against receipts. It also requires issuing VAT refunds to exporters, to avoid discriminating against exports.

The complexity of the VAT was seen as a positive feature, arguing that it imposed a useful discipline on both taxpayers and tax administrations. Taxpayers would need to keep more extensive and accurate accounts, which would be good for their businesses and for tax administration in the long run. And tax administrations would be compelled to use more modern (accounts-based) practices

and assessment methods, which would have positive spillover effects on their performance.

In many African countries the VAT did not generate the expected revenue (Baunsgaard and Keen, 2005) and has generally been poorly designed and implemented, with many legal and de facto exemptions. The efficiency of VAT collection, measured by C-efficiency (the ratio of actual to potential tax revenue), is significantly lower on average for Africa than for any other region (Keen, 2013).

Yet the VAT accounts for more revenue than any other single tax in Africa and has become a reliable generator of revenue—and one that automatically adjusts for inflation. However, around half of VAT collections are on imports. These are in effect little more than import duties under a new label, and they could easily be re-labelled again. The VAT is not costless. If the tax is not to penalize exporters, there needs to be a functioning system for refunding VAT payments to them. This does not exist in about half of the African countries that levy the VAT.¹² Where refunds are payable, they generate much friction and, second only to customs checks, are likely to be a major source of corruption in tax administration. These problems in turn motivate businesses to demand exemptions from the VAT to protect against unfairness or hassle.

The VAT will continue to be contentious in Africa. But whatever its general appropriateness to the continent, it seems likely that—along with the simultaneous paring down of trade taxes—its introduction has given a boost to the modernization of African tax administration.

THE GENDER OF TAX COLLECTORS

The shift from physical verification to the analysis of records and accounts has had broad implications for the work of tax collectors. Direct personal contact with taxpayers is becoming less frequent. The skills that are in demand are decreasingly those

11 The 2018 edition of the annual *Paying Taxes* report has information on 41 of the 45 African countries that have a VAT.

12 VAT refunds are not available in 19 of the 41 countries with information on the VAT in the 2018 edition of annual *Paying Taxes* (World Bank Group and PwC, 2018).

In OECD countries women typically account for about 60 per cent of the total workforce in national tax administrations. In Africa, however, men still outnumber women in most tax administrations, sometimes by a large margin.

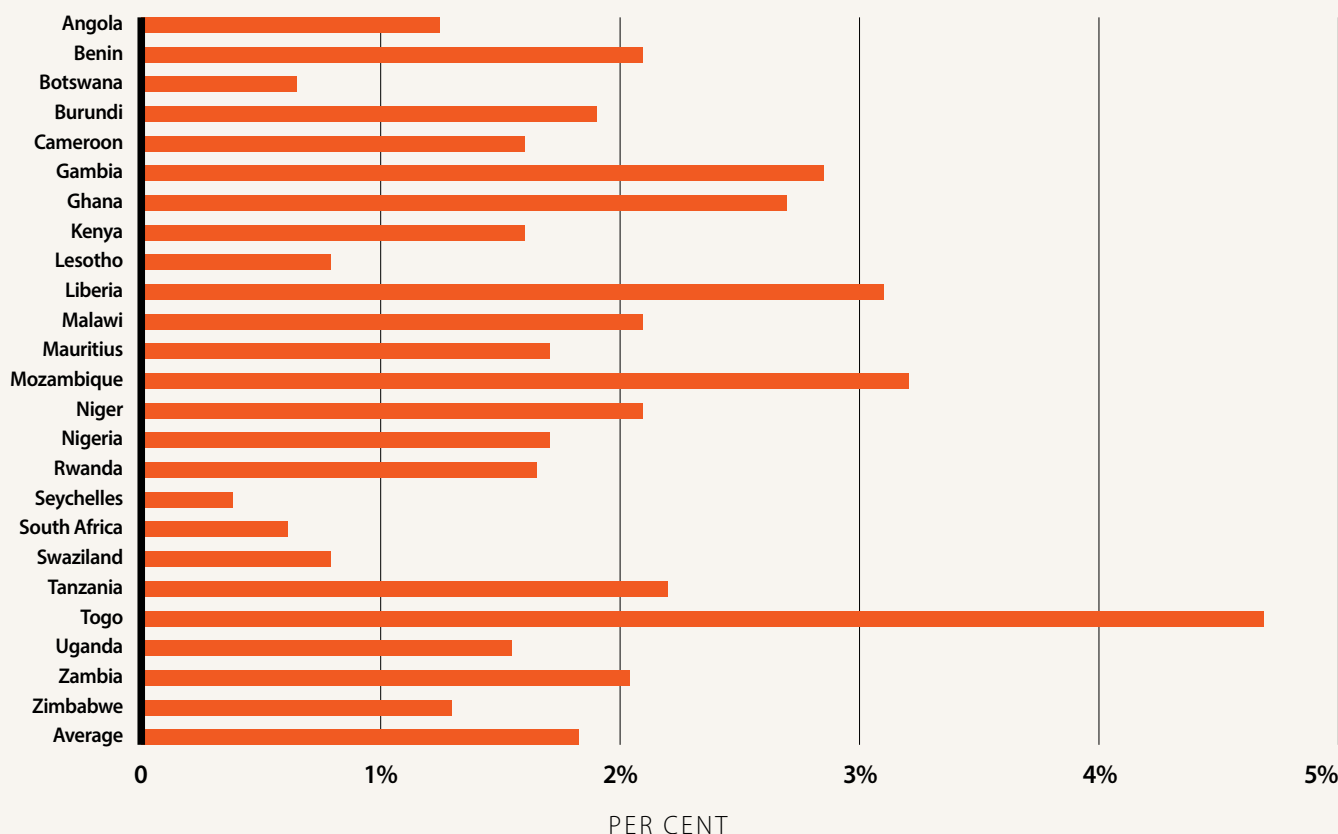
of enforcer and increasingly those of accountants, auditors, lawyers, researchers, information technology specialists, human resource managers, data analysts, outreach specialists and service desk staff. These changes in the character of jobs in tax administration, together with broader changes in labour markets and in gender relations, contribute to the increasing numbers of women working in tax administration. In OECD countries women typically account for about 60 per cent of the total workforce in national tax administrations (OECD,

2017).¹³ In Africa, however, men still outnumber women in most tax administrations, sometimes by a large margin (figure 5.3).

In 2016 there were on average three times more male than female senior managers in the 24 national tax administrations reporting for the *African Tax Outlook* (ATAF, 2017). The proportion

¹³ As in most large organizations globally, women tend to be concentrated in the lower ranks and to account for a small proportion of senior management.

FIGURE 5.3. RATIO OF MALE TO FEMALE STAFF IN TAX ADMINISTRATION IN 24 AFRICAN COUNTRIES, 2016



Note: The average is for the 24 countries included in the figure.

Source: Based on data from ATAF (2018).

of women in tax administration is rising, however. Only one study for Africa has ever examined the implications of the growing number of women for the performance of tax administrations (box 5.1). The study, for the Uganda Revenue Authority, suggests that women have a positive effect (Mwondha et al., 2018).

ORGANIZATIONAL AND OCCUPATIONAL SPECIALIZATION

Twenty or thirty years ago, most tax administration staff in Africa had relatively low education qualifications and few professional credentials. Their jobs were fairly homogeneous. Most staff worked in an organization devoted to collecting just one type of tax—for example, trade taxes (customs), direct domestic taxes like income taxes, indirect domestic taxes (sales taxes), excise taxes (notably on alcohol) or stamp duties (fees on official transactions)—and did much the same kind of work as all the other people in the office. They were based in a fairly small local office, close to the taxpayers for whom they were responsible. They tried to keep close tabs on those taxpayers and to get to know them personally. They assessed taxes, prepared tax bills, ensured that

those bills were paid and sometimes even collected the payments themselves. They had considerable personal control over the written records that they maintained.

Today, tax administration jobs are more diverse, reflecting the organizational changes discussed above. In some countries all tax collection has been assigned to semi-autonomous revenue authorities, responsible for both trade and domestic taxes.¹⁴ Even where customs and other tax collection units have not been placed under the same operational management, there has been an emphasis on improving coordination. Generally speaking, the more coordination, common management or direct merging that has taken place among units formerly focused on collecting specific types of tax, the easier it is to adopt internal structures that are similar to those of tax administrations in OECD countries. Three dimensions of this modern structure are especially relevant:¹⁵

- Internal units are defined by function rather than by the type of tax they collect. With the exception of customs, which continues to have a distinct character, units identified in terms of type of tax (such as Stamp Duty or Income Tax) have largely been replaced by units with names such as Taxpayer Registration, Tax Returns, Payments Processing, Debt Collection, Audit and Investigations, Finance, Information

BOX 5.1. A CASE FOR GENDER MAINSTREAMING IN TAX ADMINISTRATION: THE UGANDA REVENUE AUTHORITY

Men have dominated tax administrations in Africa. However, the situation is changing as more women enter tax-related professions. A recent study of the Uganda Revenue Authority finds not only increasing parity between men and women but also higher levels of performance by female employees (Mwondha et al., 2018). The study finds that women perform slightly better than men based on their regular six-month staff performance appraisals and that on average women serve the organization slightly longer (12.3 years) than

men (11.6 years), important for an organization with traditionally high staff turnover rates. The study also found that men had twice as many disciplinary actions against them as women did. Both women and men reported being generally relaxed about and satisfied with working in a mixed-gender environment. These findings make the economic case for gender mainstreaming, as women help to improve organizational performance. Gender mainstreaming is also a human rights issue (ECA, 2016).

¹⁴ Even within the framework of semi-autonomous revenue authorities, customs remain organizationally distinct. This is almost unavoidable, because of the large—and generally growing—focus of customs on non-revenue activities, notably trade facilitation and national security. Common management nevertheless facilitates cooperation between customs and domestic tax units, the sharing of common services and, perhaps most important, the interfacing of their software systems to facilitate sharing data on taxpayers.

¹⁵ In a number of Francophone countries, the business of assessing tax liabilities had historically been undertaken jointly by a tax administration unit and the treasury unit within the ministry of finance. This practice has been discontinued (Fossat and Bua, 2013).

TABLE 5.3. TAXPAYER SEGMENTATION AND ASSOCIATED RISKS IN SELECT COUNTRIES

SEGMENT	DEGREE OF RISK	ATO COUNTIES WITH THIS SEGMENTATION
Large taxpayers	<ul style="list-style-type: none"> • Low risk of under-declaration • High level of tax planning • Low risk of misclassification 	Benin, Botswana, Burundi, Cameroon, Eswatini, Gambia, Kenya, Liberia, Lesotho, Malawi, Mauritius, Mozambique, Nigeria, Rwanda, Senegal, Seychelles, Tanzania, Togo, Uganda, Zambia and Zimbabwe
Medium taxpayers	<ul style="list-style-type: none"> • Moderate risk of under-declaration and misclassification 	Benin, Burundi, Cameroon, Kenya, Malawi, Nigeria, Senegal, Seychelles, Tanzania, Togo, Uganda and Zambia
Small taxpayers	<ul style="list-style-type: none"> • High risk of under-declaration • Hard to track and trace • Inaccurate returns • Constantly change International Standard Industrial Classification (ISIC), which makes them hard to monitor 	Benin, Burundi, Cameroon, Kenya, Malawi, Senegal, Seychelles, Tanzania, Togo, Uganda and Zambia
Micro taxpayers	<ul style="list-style-type: none"> • Very high risk of non-declaration • Determination of income is difficult • High compliance enforcement costs • Highly difficult to trace 	Benin, Cameroon and Nigeria

Source: ATAF (2018).

Technology, Human Resources, Legal Affairs, Dispute Resolution, Taxpayer Services, Research and Planning, and Internal Compliance (anti-corruption).

- Because fewer staff need to be in local offices to facilitate face-to-face contact with taxpayers and because specialist support functions (such as human resource management and taxpayer services) have become relatively more important, there is typically a shift in staff numbers from local offices to headquarters.
- There is extensive use of segmentation, or allocating different categories of taxpayers (in practice, mainly different business sizes) to separate units within the tax administration. At a minimum, the tax returns, assessments and auditing of large businesses is undertaken in a special unit.

Organization around the principle of segmentation varies widely (table 5.3). Some tax administrations simply have two separate units: one for large taxpayers and one for the rest. The South African

Revenue Services has six units, including ones dealing with embassies, tax-exempt organizations and tax practitioners.¹⁶ In 2014 the Uganda Revenue Authority established a Public Sector Office, initially to deal with the tax affairs of ministries and other government agencies and expanded to cover politically influential individuals. Segmentation recognizes that different types of taxpayer require different treatment and tax collectors with different skills and abilities. Most important, the legal and accounting competencies needed to deal effectively with—and if necessary to challenge—tax returns from large (transnational) companies are very different from those needed to identify and collect taxes from small retailers or motorcycle taxis. Segmentation, by specializing and focusing on a set group of taxpayers is aimed at creating opportunities for improving the efficiency of tax administration.

¹⁶ For a summary of information on some African tax administrations, see ATAF (2017).

COOPERATIVE COMPLIANCE

For tax administration specialists, cooperative compliance is the defining feature of the new global consensus on tax administration. Several core ideas underlie cooperative compliance and are intended to increase the efficiency and the legitimacy of the tax system. Tax administrations should prioritize the education of taxpayers about the tax system and make it easy and low in cost for taxpayers to comply with reporting, filing and payment obligations. Relatedly, tax administrators should then assume that most taxpayers will be adequately honest in their declarations. Administrators should thus focus their enforcement and auditing¹⁷ activities on the taxpayers most likely to be non-compliant and on random audits of a small proportion of taxpayers.

Tax administrations, supported by legislation, should work harder at informing high-income and corporate taxpayers in advance about what kinds of complex schemes intended to reduce tax bills will be considered acceptable and legal (tax avoidance) and which will be considered illegal (tax evasion). Disputes between taxpayers and tax administrations should be settled as quickly, cheaply and independently as possible, particularly through independent tax tribunals.

There are few national tax administrations in Africa that do not formally accept the broad principles embodied in the notion of cooperative compliance. There is little overall information on the extent to which they adhere to them in practice. It is clear that they have some way to go.

CHALLENGES TO TAX ADMINISTRATION

Modern tax administrations seek to optimize tax collections while minimizing administration costs and taxpayer compliance costs. While the reforms discussed above have contributed to an increase in revenue, a number of weaknesses in national tax administration in Africa need attention. The challenges vary from country to country and over time. As discussed below, key challenges include the high cost of tax collection, lack of political will and coordination, and the slow adoption of new technologies. Other important challenges are discussed elsewhere in this Report—corruption and the complexities of informalities (chapter 3), inadequate tax administration especially at the subnational level (chapter 4) and inadequate tools to tax wealthy Africans (chapter 6).

HIGH COST OF TAX COLLECTION IN AFRICA

The average cost of tax collection is considerably higher in Africa than in OECD countries. On average in 2016 revenue administrations in Africa spent 1.6 per cent of the revenue collected on operational costs, a marginal increase over the average between 2011 and 2016 (ATAF, 2017). The costs vary across the continent (figure 5.4).

Country comparisons show that Eswatini has the highest cost collection ratio relative to its peers (5.2 per cent) followed by Zimbabwe (4.0 per cent). Senegal (0.1 per cent) had the lowest cost-to-revenue ratio followed by Cameroon (0.3 per cent), Seychelles (0.5 per cent) and South Africa

For tax administration specialists, cooperative compliance is the defining feature of the new global consensus on tax administration.

¹⁷ Audit units are often used to squeeze taxpayers suspected of having the capacity to pay more or as a last minute means of helping the tax agency meet its revenue collection targets.

The average cost of tax collection in Africa is considerably higher than in OECD countries.



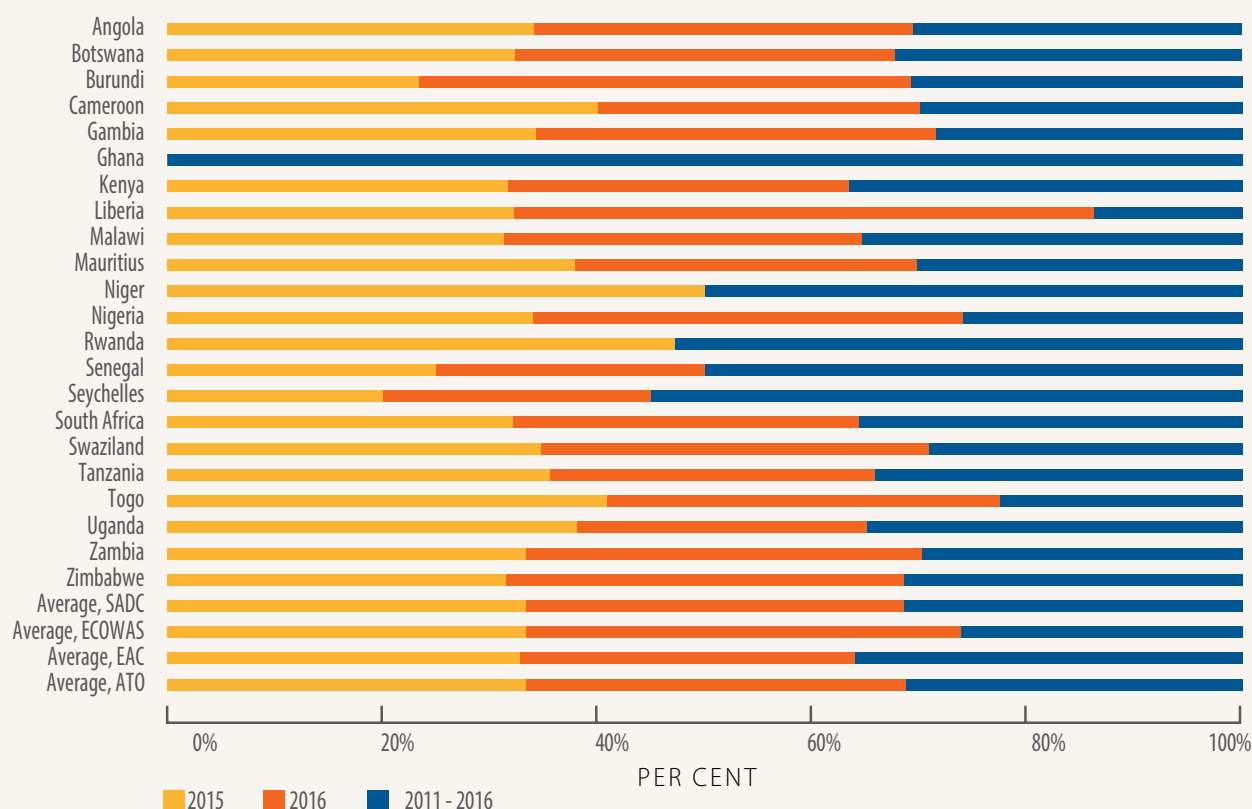
(0.9 per cent). Among regional economic groups, the Southern African Development Community and the East African Community had the highest cost-to-revenue ratio (1.9 per cent) followed by the Economic Community of West African States (1.4 per cent) (ATAF, 2018). The range of reported costs is high, suggesting considerable under-reporting in some cases. Estimates often seem to exclude aid. These challenges are compounded by the absence of comparably extensive and reliable data for Africa.

Some tax reforms, notably the creation of semi-autonomous revenue authorities, with their highly paid staff, have also pushed up collection costs.

More fundamentally, African tax administrations usually need to deal with a very wide variety of taxpayers. The routine operational costs of an organizational system equipped to engage with very large companies such as the multinationals Rio Tinto and Dangote Cement are high relative to the tax they can collect from the vast bulk of taxpayers, which are small and micro enterprises, many of which do not appear in databases.

The administrative costs of taxing small businesses can be high. African tax administrations are often under pressure to register and tax small and micro enterprises, especially from people who see the

FIGURE 5.4. COSTS OF TAX ADMINISTRATION RELATIVE TO REVENUE IN SELECT COUNTRIES, AVERAGE, 2011–2016



Source: ATAF, 2018.



While African tax authorities have modernized in ways that improve their capacity to tax the private sector, few have the authority or political backing needed to induce other parts of government to become good taxpayers and promoters of tax compliance.

under-taxation of informal sector activities as a big problem. But identifying, registering and managing these small taxpayers is expensive. They may generate little net revenue, while diverting attention from the small number of large business enterprises that generate a high proportion of the total revenue in most African countries (ATAF, 2017).

LACK OF POLITICAL WILL AND COORDINATION

While African tax authorities have modernized in ways that improve their capacity to tax the private sector, few have the authority or political backing needed to induce other parts of government to become good taxpayers and promoters of tax compliance more generally.¹⁸ Other government agencies are often bad tax citizens. First, they delay in remitting the taxes that they are liable for paying directly (such as import duties and the VAT on their purchases), are licensed to collect directly (such as motor vehicle licence fees and royalties on natural resource extraction) or collect as intermediaries (such as the personal income taxes of government employees that are deducted at source under pay-as-you-earn arrangements and withholding taxes on public sector contracts).¹⁹

Second, other government agencies decline to provide the tax authority with the information it needs—and that private companies are required to supply—to properly assess the tax obligations of

third parties. This includes information on the non-salary benefits of public sector employees that are formally taxable, detailed personal information on public sector employees to enable the tax authority to correlate earnings from their formal salaries with their earnings from other sources,²⁰ and automatic notice of the details of the identity of recipients of (large) public sector contracts.

Third, other government agencies sometimes refuse to participate in charging or paying the VAT, thus compromising the information chain on which effective VAT collection depends and worsening the problem of inefficient VAT collection, mentioned above.

The effectiveness of tax administration depends in part on the effectiveness of other public bodies, including tax courts and tribunals, police, and law and other providers of tax-relevant public information, including passport authorities, land registries, electricity utilities, banks and government procurement agencies (most government agencies do some procurement). These all need to work together coherently.

SLOW ADOPTION OF NEW TECHNOLOGY

One of the most important digital issues in Africa today is that tax administrations are not exploiting the full potential of digital management information systems, many of which they already have access to. These gaps in the use of digital technology make it

¹⁸ For rare information on this issue and how the Uganda Revenue Authority is approaching it, see Saka, Waiswa, and Kangave (2018).

¹⁹ The motivation for payment delays may be to increase organizational budgets or to permit staff to use the money to invest in financial markets for personal gain.

²⁰ It is not unusual for government organizations—and private employers—to remit taxes to the tax authority without even identifying the people from whose salaries the taxes are deducted.

more difficult for senior management to monitor and control work performance and revenue inflow. They also limit the ability to analyse the extensive data that are already being collected digitally, in order to better understand taxpaying clients and assess organizational performance (Moore, Prichard and Fjeldstad, 2018). Future improvements in the performance of tax administrations will be closely linked to how well they take advantage of digital information systems.

While tax administrations have been slow to use digital information to monitor performance, they have made considerable progress in electronic filing and payments. Eighteen countries have introduced electronic filing and payment systems (see box 5.2 for the experience of Kenya and Namibia).²¹ Three countries have made electronic filing compulsory for all taxpayers (Kenya, Uganda and Zimbabwe), and other countries require it for large taxpayers and for payment of core taxes (income tax, VAT and employment taxes; ATAF, 2017). In 2015 the Zimbabwe Revenue Authority (ZIMRA) launched e-filing, which led to an increase in tax submissions and improved the ease of doing business with ZIMRA. However, several factors make e-filing difficult, including the challenge of internet access and unreliable electricity service in some areas (Obert et al., 2018).

South Africa introduced e-filing in 2003 for the VAT and pay-as-you-earn taxes, expanding it in 2006 to cover corporate and personal income taxes. Tax compliance costs dropped 22.4 per cent and time to comply for the VAT dropped 21.8 per cent (Yilmaz and Coolidge, 2013). In Rwanda, as a part of the e-initiative of 2012, the introduction of electronic

BOX 5.2. DIGITALIZATION AND TAX ADMINISTRATION IN KENYA AND NAMIBIA

The digitization and automation reforms undertaken by the Kenya Revenue Authority and the private sector have had positive outcomes. The money-transfer system M-Pesa has transformed tax policy and administration. The system includes an online application for tax administration (the iTax System) and allows taxpayers to file and pay taxes electronically.

Kenya Revenue Authority has also automated and digitized several of its functions to improve the efficiency of service delivery, promote paperless operations, enforce compliance, reconcile tax collections, promote transparency

and enhance accountability. Digitization of VAT operations has helped identify data inconsistencies and raised VAT collections by more than \$1 billion between 2016 and 2017.

In Namibia the time to comply and the number of VAT payments have remained flat in recent years, though both are above the global average. At the end of 2016, the Namibia Inland Revenue Department migrated to an integrated tax administration system, which offers new functions and reporting capabilities that will reduce delays in processing tax returns and the number of misplaced returns.

Source: Kenya Country Case Study; World Bank and PwC (2018).

billing machines contributed to a 6 per cent year-on-year increase in tax revenue and reduced the time to file VAT returns from 45 hours to 5 (Bizimungu, 2018). Nigeria introduced e-taxation in 2015 to automate all core processes from tax registration, payment, assessment, monitoring, tax audit and investigation, taxpayer file management and returns filing.

Countries need to prepare for tax digitalization by developing strategies and infrastructure for managing big data. One option is to assign this role to the national bureau of statistics.

²¹ These were Angola, Botswana, Cameroon, Eswatini, Ghana, Kenya, Mauritius, Namibia, Nigeria, Rwanda, Senegal, Seychelles, South Africa, Togo, Tanzania, Uganda, Zambia and Zimbabwe.


CONCLUSIONS AND POLICY IMPLICATIONS

Most African countries are improving the efficiency and effectiveness of tax administration. The increasing use of information technology, including digitalization, is enhancing the efficiency and effectiveness of tax administrations in the African countries that have introduced electronic tax filing and payment systems. Recent progress in improving the effectiveness and efficiency of tax administration needs to be sustained, including through efforts to educate taxpayers on the importance of tax compliance.

Pervasive weaknesses remain, however, especially the lack of reliable, consistent data on the quality of tax administration in Africa and the cost of tax collection, informality and corruption. All countries need to address the data challenge in order to provide input to decision making and improve the efficiency and effectiveness of tax administration. Strengthening the capacity of tax administrations, including their ability to collect taxes from broad and diverse groups, remains an imperative.

Governments try to overcome antipathy to raising taxes by doing so in ways that taxpayers consider fair and tolerable and by spending tax revenue in ways that taxpayers welcome. More generally, effective taxing and spending are premised on trust in government. Trust is hard to sustain if tax collectors are widely believed to be corrupt; if their actions appear arbitrary or unfair; if their administrative processes are complex, obscure and time consuming for taxpayers; or if they appear to be targeting and imposing unfair tax burdens on those least able to pay.

Not all elements of the global tax consensus will be the best way of achieving effective and efficient tax systems in all African countries. There is undoubtedly scope for creative local adaptations.



At its core, the global tax consensus is about shifting from tax administration procedures designed by and suited to governments and their tax collectors to practices that are also acceptable and convenient to taxpayers. It is about creating at least grudging if not enthusiastic consent to taxation—rather than open hostility and active resistance—and about increasing the legitimacy of governments. Not all elements of the global tax consensus will be the best way of achieving effective and efficient tax systems in all African countries. There is undoubtedly scope for creative local adaptations, leveraging increasing citizen compliance²² and advancements in tools to modernize tax administrations towards efficiency and effectiveness.

²² Afrobarometer survey data for seven countries indicate that over 2005–2015 there was a steady increase in the proportion of people who expressed agreement with the statement “The tax authority always has the right to make people pay taxes” (Moore, Prichard and Fjeldstad, 2018: 34).

ANNEX

TABLE A5.1. PERFORMANCE OF 54 AFRICAN COUNTRIES ON TAX ADMINISTRATION VARIABLES,
MOST RECENT DATA AVAILABLE

COUNTRY	POST-FILING INDEX ^a (distance to frontier; 0 = least efficient, 100 = most efficient)	NUMBER OF TAX PAYMENTS	TIME TO COMPLY (hours)	USE OF ONLINE PUBLIC SERVICES (trend 2008–2017)
Algeria	49.8	27	265	–21.5
Angola	95.0	31	287	–12.2
Benin	49.3	57	270	+2.9
Botswana	82.7	34	120	+8.8
Burkina Faso	49.3	45	270	–0.7
Burundi	28.2	25	232	+18.8
Eritrea	99.5	30	216	–5.7
Ethiopia	50.9	30	306	+48.1
Equatorial Guinea	93.1	46	492	+2.2
Cabo Verde	80.7	30	180	+9.3
Cameroon	49.3	44	624	+10.8
Central Africa Republic	5.1	56	483	
Chad	11.0	54	766	+16.8
Comoros	57.3	33	100	+3.3
Congo	12.3	52	602	–3.6
Côte d'Ivoire	44.5	63	270	+16.9
Congo, Dem. Rep. of the Congo	27.1	52	346	0.0
Djibouti	49.6	35	76	–12.5
Egypt	26.6	29	392	–18.2
Equatorial Guinea	93.1	46	492	+2.2
Eritrea	99.5	30	216	–5.7
Eswatini	83.1	33	122	+3.4
Ethiopia	50.9	30	306	+48.1
Gabon	42.5	26	488	+10.2
Gambia	53.5	49	326	+3.0
Ghana	49.5	31	224	+21.0
Guinea	12.8	33	400	+2.3
Guinea-Bissau	45.3	46	218	+11.5
Kenya	62.0	26	186	+34.3
Lesotho	66.9	32	333	–28.0
Liberia	98.6	33	140	+17.5
Libya	90.2	19	889	+3.8
Madagascar	21.8	23	183	–2.2
Malawi	33.4	35	178	–0.5
Mali	25.7	35	270	–11.3
Mauritania	17.2	33	270	+0.7
Mauritius	87.6	8	152	+31.3
Morocco	98.6	6	155	+71.9
Mozambique	58.6	37		–14.6
Namibia	77.2	27		+14.7
Niger	38.0	41		–0.2
Nigeria	47.5	59		+25.6
Rwanda	63.7	8	95	+24.7
São Tomé and Príncipe	92.2	46		–9.5
Senegal	42.7	58		+9.4
Seychelles	93.4	29	85	+14.2
Sierra Leone	95.4	34		+8.0
Somalia				+2.0
South Africa	55.4	7	210	+0.8
South Sudan	95.9	37	210	–2.8
Sudan	20.2	42	180	+20.8
Tanzania	67.2	60		+47.0
Togo	14.9	49	216	+31.3
Tunisia	22.9	9	145	+79.5
Uganda	72.3	31	195	+31.4
Zambia	85.9	11	164	+50.0
Zimbabwe	52.8	51		+23.5

Note: Values highlighted in green show the best performance and values highlighted in red show the worst performance.

a. This index measures two processes that might take place after filing: claiming a VAT refund and correcting an error on a corporate income tax return, including going through an audit. Distance to frontier is a measure of the distance from the best observed performance.

Source: Based on data from World Bank and PwC (2018) and Mo Ibrahim Foundation (2018).

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CHAPTER 6

MULTINATIONAL CORPORATIONS, TAX AVOIDANCE AND EVASION AND NATURAL RESOURCES MANAGEMENT

Non-renewable natural resources are an important source of revenue for many African countries. Challenges in government oversight, loopholes in national tax policies and the challenges of applying the arm's length principle have led to widespread tax avoidance and engagement in illicit financial flows by multinational corporations, which dominate the sector. Generous tax incentives and fiscal stability clauses further undermine government revenue from natural resources.

African countries need to strengthen their oversight of the natural resources sector, consider shifting from corporate income taxation towards formulary apportionment (allocation of multinational corporation profits across countries based on sales, payroll and capital base in each country) and close loopholes to prevent base erosion and profit shifting. Elimination of base erosion and profit shifting alone could boost tax revenue by an estimated 2.7 per cent of GDP.

INTRODUCTION

Natural resources production in Africa has expanded in the past decade. Africa's production of 15 important metals was forecast to rise by 78 per cent over 2010–2017, more than double the 30 per cent forecast for the Americas and Asia (US Geological Survey, cited in AfDB, 2013). As

Africa's subsoil remains relatively underexplored, increased investment can only enhance discovery rates (Knebelmann, 2017).

The natural resources sector is dominated by multinational corporations and state-owned enterprises, which are the only firms that have the ability to raise the necessary capital and manage the associated high risks (IMF, 2014a; Mullins, 2010). However, multinational corporations also have the ability to undertake complex international tax avoidance strategies that shift profits from where the underlying economic activities take place to low- or no-tax jurisdictions, a behaviour referred to as base erosion and profit shifting. This can significantly reduce fiscal revenue in countries that rely heavily on natural resources revenue (UNDP, 2017; OECD, 2015).

Multinational corporations have engaged in tax avoidance running into the tens of millions of dollars for individual companies and billions of dollars a year for individual countries (ActionAid, 2015; Africa Progress Panel, 2013; Bloomberg, 2012; Oxfam, 2015). In 2015 base erosion and profit shifting led to an estimated \$240 billion annual revenue loss for countries around the world in all sectors (Solheim, 2016).

The impact of base erosion and profit shifting as a percentage of tax revenues is higher in developing countries than in developed countries (OECD, 2015, 2014). In 2013 base erosion and profit shifting cost Africa an estimated 2.7 per cent of GDP in lost revenues (Cobham and Janský, 2018).¹ Other estimates of losses through base erosion and profit shifting ranged from 1 to 6 per cent of GDP (Moore, Prichard and Fjeldstad, 2018). Natural resources taxation will continue to present critical fiscal concerns for developing countries, particularly in resource-rich countries (OECD, 2014).

¹ This estimate treats Africa as a single unit and is based on estimates for 42 African countries for which data were available. The median loss among countries for which data were available was 2.3 per cent, and the mean loss was 0.5 per cent (based on data from Cobham and Janský, 2018).

This chapter explores the challenges of natural resources taxation in Africa and how to respond to them, including the complex problem of illicit financial flows. It focuses on non-renewable natural resources. Most of the country examples draw on the mineral, oil and gas sectors, but much of the analysis is relevant to all extractives. The key questions addressed in this chapter are:

- How important is revenue from non-renewable natural resources for government budgets in Africa?
- Why do non-renewable natural resources need to be taxed differently?
- What are the key policy challenges?
- How do illicit financial flows by multinational corporations, including tax evasion and aggressive tax avoidance, affect non-renewable resources?
- How can African countries counter tax evasion and avoidance in the non-renewable resources sector?

This chapter builds on work on illicit financial flows in the natural resources sector by the Economic Commission for Africa (ECA) to provide original insights into tax avoidance, tax evasion and other illicit financial flows.

THE CONTRIBUTION OF NATURAL RESOURCES TO GOVERNMENT REVENUE

The International Monetary Fund (IMF) classifies natural resources revenue as:

[R]eceipts collected by governments from the natural resources sector through diverse tax and non-tax fiscal instruments. For example, natural resources revenues include “common” taxes, such as the corporate income tax and value added tax; special taxes on the sector, such as the resource rent tax; and other quasi-tax or non-tax instruments, such as royalties, profits, and bonuses. (IMF, 2014a: 1)

Rising exports signal the sector’s potential to contribute to government revenue to finance investments in physical and social infrastructure for development (Chuhan-Pole, Dabalen and Land, 2017; IMF, 2013).

In 2016 natural resources rents contributed some 13.4 per cent to GDP in Africa, with forests contributing the highest rents, at 8.2 per cent of GDP (table 6.1). The mineral sector was also an important contributor to GDP, with rents of 3.2 per cent. Other natural resources contributions

TABLE 6.1. CONTRIBUTION OF NATURAL RESOURCES TO GROSS DOMESTIC PRODUCT IN AFRICAN COUNTRIES, 2016 (PER CENT OF GDP)

COVERAGE	TOTAL NATURAL RESOURCES RENTS	OIL RENTS	NATURAL GAS RENTS	COAL RENTS	MINERAL RENTS ^a	FOREST RENTS
Africa ^b	13.4	1.8	0.2	0	3.2	8.2
Median for individual African countries ^b	11.8	0	0	0	0.3	4.2

a. Covers rents from tin, gold, lead, zinc, copper, nickel, silver, bauxite and phosphate, not from the entire mining industry.

b. Eritrea and Libya are excluded from the analysis because of missing data.

Source: Based on data from World Bank (2017a, 2017b) and ECA (2018a).

included oil rents, at 1.8 per cent of GDP, and natural gas, at 0.2 per cent (World Bank, 2017a, 2017b). The contributions vary by country, with oil-rich countries having a higher contribution of oil rent to GDP.

POLICY CHALLENGES IN NATURAL RESOURCES TAXATION

MULTIPLICITY OF FISCAL INSTRUMENTS AND FRAGMENTED INSTITUTIONAL AND REGULATORY OVERSIGHT

Because of the distinct stages that are part of the process of natural resources extraction and commercialization, a country usually has several ways of extracting revenues. In practice, countries adopt a combination of fiscal instruments to cover all potential tax bases, thus creating complex, overlapping fiscal regimes that can be a challenge for revenue collection and administration (table 6.2).²

² For a more elaborate description of the fiscal regimes, see IMF (2012) and IMF and World Bank (2014).

Although most countries adopt a mix of fiscal instruments, some countries are shifting from easier-to-administer royalties (based on the gross value of natural resources extracted or sold) towards levies based on net income (Durst, 2016). These include application of the standard corporate income tax regime to extractive companies, taxes that apply after an extractives company achieves a threshold level of profitability or recovers its costs (resource rent taxes) and income or production sharing from a project (production sharing contracts).

Income-based taxes may dis-incentivize excessive risk-taking for limited liability companies (companies might otherwise prefer risky investments as they stand to reap the full benefit of any financial upside while having limited liability for the downside). However, income-based taxes are more difficult for countries to administer because, unlike royalties which are based on gross values, income-based taxes take into account incurred costs (deductions). That raises the possibility of income understatements, so income-based taxes are more susceptible to base erosion and profit shifting (Durst, 2016; Brooks, 2013; ECA, AMDC and AUC, 2016).

Historically, regulation of the natural resources sector has been fragmented, with responsibilities

TABLE 6.2. TAX BASES AND FISCAL INSTRUMENTS IN THE NATURAL RESOURCES SECTORS

TAX BASE	FISCAL INSTRUMENT
Transactions	Licence fees and signature, discovery and production bonuses
Volume or value of production	Royalties or production sharing
Profits or gains	Corporate income taxes and capital gains
Excess profits	Resource rent taxes and variable income taxes intended to capture rents.
Others	Area rentals, minor "nuisance taxes", surface and rental payments

Source: IMF (2014a) and ECA, AMDC and AUC (2016).

TABLE 6.3. RECOMMENDED NATURAL RESOURCES ORGANIZATIONAL FRAMEWORK

POLICY AREA	INSTITUTION RESPONSIBLE	
	Policy formulation	Policy implementation
Fiscal	Finance ministry	Tax and customs administration
Natural resources management and operations	Natural resources ministry	Natural resources inspectorate
Commercial	Natural resources or finance ministry	Natural resources company

Source: Adapted from IMF (2014a).

distributed across different ministries and government agencies. The IMF recommends a division of responsibilities along the lines shown in table 6.3.

A fragmented institutional and regulatory framework can impede taxation of multinational corporations in the natural resources sector. The ministry of petroleum or mining usually leads in negotiating exploration, development and extraction agreements, which can mean that agreements are negotiated and concluded without sufficient participation by the ministry of finance or the tax administration. Government departments need to work together in policy design and implementation to effectively manage revenue from extractive industries (IMF, 2018).

A natural consequence of fragmented regulatory oversight is that government agencies may operate in silos and fail to share data and information, which undermines fiscal management of the sector (IMF, 2018). Some agencies may cite confidentiality as the reason for withholding information, even though all the agencies are part of the government that signed the contract. As a consequence the tax administration may not have access to information that would enable it to ensure compliance with tax laws by fully assessing and dealing with the risks posed by multinational corporations.

These challenges are apparent in Africa. For example, opaque management of the natural resources sector has been a long-standing challenge in Sudan. Problems include the non-disclosure of agreements entered into between the central government and extractive companies; ambiguous policies on managing oil, land and water resources; outdated and poorly enforced laws governing the oil industry and land administration; and inadequate environmental impact assessments, particularly in the oil industry, which has contributed to environmental damage and led to confrontations between local communities and the oil industry.

■ In practice, countries adopt a combination of fiscal instruments to cover all potential tax bases, thus creating complex, overlapping fiscal regimes that can be a challenge for revenue collection and administration.

An additional problem in Sudan is the multiplicity of fees, charges and royalties, some not supported by law, that are imposed, collected and even retained by various government agencies. This situation persists because multiple agencies have oversight roles without an effective coordination framework. With no law governing the collection and management of this revenue, institutional challenges arise, preventing the Ministry of Finance from effectively overseeing and coordinating natural resources revenue.

In some countries, production and export data are controlled by different government agencies, or extractive companies provide different reports to different agencies. Thus, the tax administration may have to reconcile multiple data points to effectively assess taxes. In Zambia, for example, there were large discrepancies in the statistics on copper production reported by different government agencies. The differences were ultimately explained as double counting of intermediate production as both intermediate and finished product, but the fragmented regulatory oversight and coordination challenges made it difficult for the revenue authority to reconcile these figures to properly assess tax and non-tax revenue (Readhead, 2016).

The multiplicity of tax bases and fiscal instruments means that different agencies administer different aspects of the fiscal regime. Licence fees, royalties, production bonuses and income from the government's share of production may be collected under the sector ministries; corporate income taxes, resource rent taxes and capital

gains taxes are collected by the tax administration; and customs duty and value-added taxes on imports are collected by customs authorities. The variety of fiscal instruments, compounded by the administrative fragmentation of oversight and revenue collection roles, can make it difficult for countries with low capacity to efficiently administer their fiscal regime,³ deal adequately with the risks of tax evasion and avoidance, and track all revenue collected from the natural resources sector.

TAX INCENTIVES

Tax incentives are favourable departures from general tax treatment granted through agreements or legislation to all investors in specified categories of corporations (IGF and OECD, 2018).

Incentives play a limited role in attracting investments to the resource sector.⁴ Rather, the investment decisions of mining companies are influenced by resource quality; economic factors such as location (cost of transport and routes to export), ease of extraction and price outlook; and the host country's policy climate (contract protections, tax regime, infrastructure, political stability, labour and security; IGF and OECD, 2018).⁵ Multinational firms in the natural resources sector often negotiate contract-based tax benefits. Often, weak governance systems and inadequate consultation among agencies result in overly generous tax incentives that reduce revenue (African Union and ECA, 2014).

 Incentives play a limited role in attracting investments to the resource sector.

³ See IMF (2014a), which also suggests that a concentration of revenue in a single sector or in a few companies may give rise to integrity and transparency issues.

⁴ See chapter 2 for results of investor survey.

⁵ See also ECA, AUC and AMDC (2017), which ranks geology as the decisive criterion for investors, with a key focus on mine grade quality.

TAX CERTAINTY AND FISCAL STABILITY CLAUSES

Tax certainty encourages private investment by enabling potential investors to accurately assess the tax and compliance costs associated with an investment over its lifetime. Tax certainty can help reconcile the expectations of taxpayers and governments while providing a tax environment that is conducive to foreign direct investment (FDI) and growth. Congo, Equatorial Guinea and São Tomé and Príncipe have received more FDI in natural resources sectors in part because of the greater tax certainty in their extractives sector than in other countries in the region (OECD, 2018a).

Tax certainty is strengthened by fiscal stability clauses in contracts, which are designed to prevent excessive changes to the tax code. However, fiscal stability clauses may undermine revenue collection, since they prevent host governments from renegotiating contracts to reflect improving fiscal regimes or to benefit from rising commodity prices. Multinational corporations often have the advantage of information asymmetry, technical expertise and negotiating power, which can result in contracts that unduly benefit firms while reducing government revenue (AU and ECA, 2014; ECA, 2018a).

For example, in Democratic Republic of the Congo, Article 276 of Mining Code of 2002 contained a fiscal stabilization clause that prevented transfer pricing rules enacted after negotiated contracts from being applied to potentially mispriced transactions. As a result, the transfer pricing rules could apply to existing mining contracts only 10 years after implementation (ECA, AUC and AMDC, 2017).

Tanzania has also experienced adverse impacts from stability clauses. Article 10(4a) of the 2010 Tanzania Mining Act allows mineral agreements to contain binding provisions that “guarantee the fiscal stability of a long term mining project, by reference to the law in force at the effective date of the agreement, with respect to the range and

The variety of fiscal instruments, compounded by the administrative fragmentation of oversight and revenue collection roles, can make it difficult for countries with low capacity to efficiently administer their fiscal regime.

applicable rates of royalties, taxes, duties and levies and the manner in which liability in respect thereof is calculated and, for that purpose and not otherwise, may contain special provisions relating to the payment of any such fiscal impost which shall take effect in the event of change in the applicable law.” Following a tax dispute between Acacia Mining and the Tanzanian government, the Tax Appeal Tribunal ruled that the company, a subsidiary of Barrick Gold, had employed a “sophisticated tax evasion scheme” that included transfer mispricing and generated losses. The Tribunal ordered the company to pay the government \$41.25 million in unpaid taxes over four years. As part of its defence, Acacia had argued (unsuccessfully) that its contract with the government provided for deductions of its \$3 billion capital investment in the three mines operated in the country, leading it to consistently declare no profits (ECA, AUC and AMDC, 2017: 67).

Stability clauses should benefit both parties, in addition to maintaining economic equilibrium when economic circumstances change. Additionally, they should protect government interests when the changes in fiscal position are the result of non-compliance with regulatory requirements—for example, economic sanctions for environmental damage as a result of a company’s operations (Oshionebo, 2010).

MULTINATIONAL CORPORATIONS AND ILLICIT FINANCIAL FLOWS

TAX AVOIDANCE AND EVASION

Tax avoidance is an elusive term. The Organisation for Economic Co-operation and Development notes that it is “generally used to describe the arrangement of a taxpayer’s affairs that is intended to reduce his tax liability and that although the arrangement could be strictly legal it is usually in contradiction with the intent of the law it purports to follow.” Defining tax evasion is more straightforward; it is “generally used to mean illegal arrangements where liability to tax is hidden or ignored, i.e. the taxpayer pays less tax than he is legally obligated to pay by hiding income or information from the tax authorities” (OECD, n.d.a).⁶

⁶ For more on using empirical evidence on the main channels of international tax avoidance, see Beer, de Mooij and Liu (2018), including transfer mispricing, strategic location of intellectual property, international debt shifting and intercompany loans, and tax treaty shopping.

ILLICIT FINANCIAL FLOWS

The High Level Panel on Illicit Financial Flows from Africa defines illicit financial flows as international financial transfers that are illegally acquired, transferred or used, as well as aggressive tax avoidance. Illicit does not necessarily mean illegal, but the harm that base erosion, profit shifting, aggressive tax avoidance and aggressive tax planning do to development justifies considering them illicit flows because they are morally wrong (ECA, 2018b, 2018c). Anyone who facilitates such flows (including the jurisdictions that attract them) has an obligation to act to prevent them.

CHANNELS FOR ILLICIT FINANCIAL FLOWS

Multinational corporations and other economic actors in the natural resources sector may generate illicit flows in a number of ways, as discussed below. Additional methods are described briefly in box 6.1.

Aggressive tax planning

Tax treaties may enable multinational corporations in the natural resources sector to structure their operations to minimize tax liabilities. One way is to set up a complex network of offshore companies

BOX 6.1. INTERNATIONAL CORPORATE TAX PLANNING: FURTHER TOOLS OF THE TRADE

In addition to the methods described in the main text, multinational firms also use the following techniques:

- **Taking deductions in high-tax countries.** For example, firms may borrow in high-tax countries (with interest payments being tax-deductible) and lend to affiliates in lower-tax jurisdictions, where the interest payment received will be taxed at a lower rate
- **And doing so repeatedly.** Passing funds raised by loans through conduit companies (that serve solely as intermediaries within a corporate group) may enable double dipping—taking interest deductions twice (or more) without an offsetting tax on receipts—that may lead to thin capitalization (high debt ratios)
- **Risk transfer.** Firms may operate in high-tax jurisdictions on a contractual basis, limiting the profits that arise there
- **Exploiting mismatches.** Tax arbitrage opportunities can arise if different countries classify the same entity, transaction or financial instrument differently.
- **Deferral.** Companies operating worldwide systems can defer home taxation of business income earned abroad by delaying paying it to the parent.
- **Inversion.** Companies may be able to escape repatriation charges or controlled foreign corporation rules by changing their residence.

Source: IMF (2014b).

to facilitate intra-company trade (Mullins, 2010). This network of offshore companies can be used to circumvent public disclosure requirements and create an avenue for tax avoidance by enabling multinational corporations to report more of their profits in low-tax jurisdictions.

Abusing transfer pricing

Multinational corporations can also manipulate the prices of goods and services traded between different parts of the multinational group in order to shift profits to jurisdictions where corporate income taxes are low. Such abuses of transfer pricing by multinational corporations can result in major losses of public revenue (Readhead, 2016).

Undertaking exploration, extraction, refining, marketing and distribution of resources in different jurisdictions offers multinational corporations many opportunities for abusive transfer pricing. Unprocessed resources can be transferred to affiliated companies at prices that are not at arm's length. Intellectual property can be licensed to affiliates in low-tax jurisdictions, enabling multinational firms to shift intellectual property-related income to these affiliates. Inputs and services such as managerial and technical services are often sourced from affiliates in low-tax jurisdictions, which can lead to excessive deductions for fees related to such services (Mullins, 2010). The capital-intensive nature of natural resources-based economic activities may also lead to excessive debt financing, which can erode the tax base of resource-rich countries (Mullins, 2010).⁷

In addition to avoiding taxes, abusive transfer pricing can also be used to enable multinational corporations to transfer funds to jurisdictions with a high degree of financial secrecy. This can allow them to use these funds to engage in corrupt transactions (such as paying bribes to government

agents in exchange for favourable treatment) while avoiding detection because of the financial secrecy surrounding the part of the company dealing with the relevant financial resources (Africa Progress Panel, 2013; OECD, n.d.a).

Misclassifying the quantity or quality of extracted resources

Taxes are levied on the value of extracted natural resource, so countries have an interest in ensuring that reported quantities and qualities are accurate. Royalty rates for mineral products generally depend on their composition or quality, which may vary. Companies may take advantage of this process of royalty calculation by declaring that extracted minerals are of lower quality than they truly are. Where companies export unprocessed minerals such as ores, it may be difficult for government authorities to assess the mineral content of the exports.

Firms may also underreport the quantity produced. The lack of data on the pricing of certain commodities in many resource-rich African countries makes it easier for multinational corporations to underreport the volumes produced (Platform for Collaboration on Tax, 2015). The High-Level Panel on Illicit Financial Flows from Africa found evidence of "extensive underreporting of the quantity and sometimes quality of natural resources extracted for export..., yet none of the countries we studied ... had its own independent means of verifying the precise amount of natural resources extracted and exported" (African Union and ECA, 2014: 67).

Misinvoicing trade transactions

Natural resources and commodities are susceptible to the intentional manipulation of invoices of goods or services exports or imports to disguise their true value and evade taxes and customs duties. Misinvoicing and mispricing

⁷ For more on these issues, see United Nations (2017: 145–190).

are also done to facilitate the shifting of profits to low-tax jurisdictions (African Union and ECA, 2014; Baker et al., 2014; Save the Children UK, 2015; UNCTAD, 2016).

Overvaluing deductible expenses

Another channel for illicit flows is inflating deductible expenses, again through relationships of multinational corporations with affiliates. For example, firms may inflate costs on loans and technical services acquired from related parties and overstate deductible expenses for equipment and other supplies. While under-declaration of the quantity and quality of resources affects royalty

payments to the government, cost inflation usually affects income-based taxes, which are becoming more common in many countries.

Treaty shopping and locating asset sales in low-tax jurisdictions

Treaty shopping has reduced corporate income tax revenue by above 15 per cent in African countries that have signed a treaty with an investment hub (Beer and Loperick, 2018), a particular blow to countries with a high dependence on corporate income taxes. Mauritius, which has received attention recently for facilitating treaty shopping, took steps to address this by revising its double taxation agreements with India and South Africa in 2015. Multinational corporations in the natural resources sector can also avoid taxation in resource-rich countries by routing asset sales through low-tax jurisdictions.⁸

Treaty shopping has reduced corporate income tax revenues in Sub-Saharan Africa by around 15 per cent in countries that have signed a treaty with an investment hub.

⁸ In response to the concerns of developing countries, the Platform for Collaboration on Tax, a joint undertaking of the IMF, OECD, United Nations and World Bank, has drafted a report and toolkit providing analysis and options for the tax treatment of offshore indirect transfers (Platform for Collaboration on Tax, 2018); see also International Consortium of Investigative Journalists (n.d.). See ACDE (n.d.) for an example of a case in Uganda.

TABLE 6.4. MAIN TYPES OF ILLICIT FINANCIAL FLOWS AND BENEFICIARIES

FLows AND BENEFICIARIES	CORRUPTION	ILLEGAL EXPLOITATION	TAX AVOIDANCE AND EVASION
Main financial flows	Facilitation payments (bribes) paid by companies, money embezzled from tax collection and budgetary allocation	Undeclared corporate revenues from illegal resource exploitation	Inflated costs deducted from taxable revenues, smuggling of resources
Main beneficiaries	Companies gaining undue advantage, and corrupt government officials	Domestic companies, local subsidiaries of foreign companies	Parent or holding companies, exporting companies

Source: Based on le Billon (2011).

Administrative corruption and illicit financial flows

Administrative corruption also contributes to the prevalence of illicit financial flows in the natural resources sector in Africa (table 6.4). Weak governance systems and lack of transparency give government officials too much discretionary power, making them susceptible to bribes or theft of natural resources or associated revenue (African Union and ECA, 2014). Officials' discretionary power can also be used to award contracts to multinational corporations that cede or limit some taxation rights in return for bribes, thus undermining competition. Multinational corporations often encourage the corruption that facilitates illicit financial flows (ECA, 2016).

Because illicit financial flows benefit both multinational corporations and corrupt officials, it can be difficult to introduce more transparency to stop illicit financial flows in Africa. This may explain why organizations dealing with illicit financial flows are often underfunded and lack the power to prosecute cases related to illicit financial flows (African Union and ECA, 2014; and ECA, 2018c).

Actions that disrupt any part of this vicious cycle of illicit financial flows and poor governance can help to tackle illicit financial flows. African countries may wish to strategically plan for which parts of the chain to address first, focusing on those that are easier to achieve and that will make it easier to target others later. For example, if the customs authority is a pocket of efficiency in a national administration, strengthening its capacities to prevent illicit financial flows through trade may cut off the resources used by corrupt officials to prevent improvements in public transparency. This, in turn, can make it easier politically to pursue anti-corruption measures.

Because illicit financial flows benefit both multinational corporations and corrupt officials, it can be difficult to introduce more transparency to stop illicit financial flows in Africa.

CONTENDING WITH ILLICIT FINANCIAL FLOWS

CHALLENGES IN ENDING ILLICIT FINANCIAL FLOWS

African countries face several challenges in fighting illicit financial flows from the natural resources sector. First, many countries lack the skills and resources (including laboratories for testing the composition and quality of extracted resources) needed to verify the submissions of multinational corporations. Countries need to build capacities in this area, in some cases with international assistance. Efforts to build national administrators' capacities in tax audit, such as the Tax Inspectors without Borders initiative, have experienced challenges. In some countries, national administrations have been sidelined, while the external auditors assigned to the project have had conflicts of interest (ECA, 2018b).

Second, in light of the complex network of offshore companies used by multinational corporations, weak public disclosure requirements and enforcement may jeopardize efforts to curb the abuse of tax provisions and illicit financial flows.

Third, the form that illicit financial flows take depends on individual country characteristics. Many government officials in Africa are unfamiliar with how such flows operate in their national context, and estimates of the extent of such flows and their sources are scarce. Learning more about them should be a priority (ECA, 2018c).

Fourth, as with natural resources taxation, there is little information sharing and coordination on illicit financial flows among relevant government agencies within or between countries. Coordination is a relatively inexpensive yet effective way to counter illicit financial flows (ECA, 2018b, 2018c; Institute for Austrian and International Tax Law, n.d.).

INITIATIVES TO COMBAT TAX AVOIDANCE AND EVASION

OECD Base Erosion and Profit Shifting package


The OECD's Base Erosion and Profit Shifting (BEPS) report set out a 15-point action plan to equip governments with the domestic and international tools they need to combat base erosion and profit shifting (OECD, 2014). The report recognised that greater transparency and improved data are needed to uncover and stop the divergence between where profits are made and where they are reported for tax purposes. With multinational corporations dominating the natural resources sector, cross-border transactions between related parties abound and create multiple opportunities for abusing transfer pricing. The OECD's BEPS (in particular Actions related to transfer pricing outcomes and value creation, and Country-by-Country Reporting) can provide a starting point for countries in Africa to deal with transfer mispricing.

Country-by-Country Reporting is a risk profiling tool that can be used to flag discrepancies between where economic activity by multinational corporations takes place and where the corporations pay taxes (OECD, 2014). Other priorities for tackling base erosion and profit shifting, such as non-strategic tax incentives, governance of tax administration and tax competition, are not included in the OECD package. African countries will therefore need to consider additional policies that are outside of the OECD BEPS package. For example, the "sixth method", pioneered and used successfully in Argentina, calls for commodities traded within a multinational group to be priced according to publicly quoted prices to simplify transfer pricing administration and settle disputes (Grondona, 2018).

Another method for preventing abusive transfer pricing that is not included in the ^{OECD} package is administrative pricing, in which the tax administration rather than the taxpayer sets the value of the commodity. This method shifts the burden of proof to the taxpayer and frees the tax administration from having to determine whether sales between related parties are at arm's length (Durst, 2016; Readhead, 2018).

Formulary apportionment and moves away from income-based taxation

While the OECD BEPS actions can be a useful starting point for African countries to reduce base erosion and profit shifting, some of the proposed solutions may be difficult to apply. Taxing multinationals on the income of their local branches or subsidiaries is inherently vulnerable to the manipulation of profits, even with the OECD BEPS package. And manipulation of reporting of



While the OECD BEPS actions can be a useful starting point for African countries to reduce base erosion and profit shifting, some of the proposed solutions may be difficult to apply.

firm revenues or costs has a larger relative impact on corporate income and profit-based taxes than on royalties (Durst, 2016).

In particular, for corporate income taxes, multinational corporations can use transfer pricing of imported inputs, intra-company loans and other techniques to manipulate profits and reduce tax liability. It can be difficult to apply the arm's length principle in determining the prices of goods and services traded within a multinational group. Tax administrations are at a disadvantage in gathering information about comparable transactions between unrelated parties and market conditions at the time of the transaction.⁹ In Africa, in particular, information on comparable transactions is hard to come by. And in the case of services or intangibles, which are beginning to dominate economic transactions and which may be specific to the company in question, comparable transactions simply may not exist (Chen et al., 2017; Pagano, 2014, cited in Durand and Milberg, 2018). Moreover, even when comparable transactions are found, to be truly comparable they need to be adjusted for differences in the circumstances of the transactions, such as differences in products, quality, economic conditions and geography.

The paucity of reliable information therefore makes it onerous for tax administrations, especially those in developing countries, to apply the arm's length principle. This is further complicated by timing, since tax administrations usually review taxpayer information long after the transaction occurred. Thus, tax administrations are disadvantaged when challenging transfer pricing, enabling multinational firms to manipulate intra-company transactions to shift profits (see OECD, 2010; Faccio and Fitzgerald, 2018).

⁹ Article 9(1) of the OECD Model Double Tax Convention is the starting point for the arm's length principle, which has formed the basis of all bilateral tax treaties involving both OECD member countries and an increasing number of non-member countries. See also Avi-Yonah and Tinhaga (2017).

Given the arguments about the role of income-based taxation in balancing risk, a good approach might be to use a variable that closely tracks corporate income but is less easy to manipulate.

The OECD BEPS project foresees a number of methods to tackle the manipulation of corporate income reporting. These approaches broadly aim to ensure that intra-company transactions (and financing arrangements) respect the arm's length principle.¹⁰ Yet these solutions (as well as the sixth method and administrative pricing, mentioned earlier) face challenges in addressing trade in unique services and intangibles, where comparable prices are not available and the proposed methods to estimate the arm's length price may require access to information on the entire corporate group (such as the transaction profit split method) or place excessive burdens on tax administrations (ECA, 2018b).

This suggests that there may be advantages to a shift away from income-based taxation, which may be easier to manipulate, towards taxation based on variables that are more difficult to manipulate. Given the arguments about the role of income-based taxation in balancing risk, a good approach might be to use a variable that closely tracks corporate income but is less easy to manipulate. This would seem to rule out any variable that is based on intra-company transfers (including sales and

¹⁰ Some of these methods (transaction profit split method, cost plus method and transactional net margin method) imply inferring the profit that should be attributed to the local branch or subsidiary of a multinational group on particular transactions, based on other variables (OECD, 2017a). Instead of applying this method transaction by transaction, it could be applied in bulk to all transactions between a multinational branch or subsidiary and the rest of the group to reduce the administrative burden of producing multiple estimates, or it could be applied to all of the branch or subsidiary's activities.

Implementation of international standards for the exchange of information for tax purpose can help African countries fight tax avoidance and evasion and illicit financial flows.



imports), particularly those for which comparable prices are not available, as these may be more susceptible to manipulation. Other variables may be less susceptible to manipulation, such as gross sales of minerals, payments to factors of production (capital, labour and land) that are located in country or domestic utility payments. Though gross sales of minerals, for example, can be manipulated by multinationals, in many cases this may be more difficult than manipulating corporate income, since the prices at which minerals are traded can be compared with global market prices.¹¹

One of the arguments against such an approach is the risk of double taxation. If different countries apply such criteria in different ways for inferring corporate income, the portions of a multinational group's corporate income that countries consider taxable in their jurisdiction would overlap. There are many countries in the world that are not linked by double taxation agreements, and most African countries have few such agreements, yet multinational corporations still operate in those countries. Indeed, so long as countries do not place excessive tax burdens on multinational corporations, and other factors to attract investment are strongly positive, the risk of double taxation should not prevent countries from pursuing this kind of approach to the taxation of multinationals.

While it can be argued that such an approach should be implemented at the global level, to ensure a fair distribution of global profits, OECD countries are opposed to pursuing alternatives to the arm's length principle (OECD, 2017a). Therefore, African countries may wish to pursue such an approach at a bilateral or regional level or with other groups of interested countries.

Transparency initiatives

Transparency is often lacking in the natural resources sector, which enables rent-seeking behaviour by government officials and tax avoidance and evasion by firms. Fiscal transparency is a pillar of good natural resources management. The IMF emphasizes that "being transparent about mining and petroleum fiscal terms and contracts, revenue collections, and the ultimate use of revenues through the budget builds public trust. Internal transparency by sharing information between government agencies also is critical for effective fiscal management" (IMF, 2018). The High Level Panel on Illicit Financial Flows from Africa quoted US Supreme Court Justice Louis Brandeis in asserting that "The best disinfectant is sunlight" (African Union and ECA, 2014: 45).

The High Level Panel on Illicit Financial Flows from Africa and others recommend increasing tax transparency, expanding networks for the exchange of information and participating in the automatic exchange of information between countries, and ensuring the availability of ownership information to reduce illicit financial flows (ECA, 2018b; Mullins, 2010).¹² There is now a burgeoning movement towards greater transparency in tax matters which may change the way that multinational corporations operate.

To facilitate the detection of aggressive tax planning, a new global standard for the Automatic Exchange of Information for Tax Purposes,

¹¹ As noted earlier in the chapter, there is an important exception for minerals exported in unprocessed form, as ores.

¹² Nigeria has also begun participating in the automatic exchange of country-by-country reports (OECD, 2019).

endorsed by the OECD in July 2014, calls on jurisdictions to obtain information from their financial institutions and automatically exchange that information with other jurisdictions. The standard is intended to “strengthen international efforts to increase transparency, cooperation and accountability among financial institutions and tax administrations and enable governments to recover tax revenue lost to non-compliant taxpayers. The new standard will generate secondary benefits by increasing voluntary disclosures of concealed assets and by encouraging taxpayers to report all relevant information” (OECD, n.d.b).

This common reporting standard can help tax administrations clamp down on companies that hide or withhold information relating to undeclared offshore funds. Implementation of international standards for the exchange of information for tax purpose can help African countries fight tax avoidance and evasion and illicit financial flows (Owens and McDonnell, 2018).

However, African countries face challenges in implementing tax transparency standards (OECD, 2017b). Participation in the system is based on full reciprocity. Most African countries lack the capacity, infrastructure and resources to meet the administrative requirements (data protection legislation) and bear the costs (secure information infrastructure, data collection from all affected financial institutions) of participation in the system (Monkam et al., 2018). To date only three African countries (Mauritius, South Africa and Seychelles) are participating in the system, and only one other country (Ghana) has passed the legislation needed as a first step towards participation (ECA, 2018b; OECD, 2018b, 2018c).

Noting the challenges that African countries face in the exchange of information for tax purposes, the Global Forum and its partners launched the Africa Initiative in 2014. The initiative is intended to use technical assistance and political engagement to enable African countries to take advantage of improvements in international tax transparency that can increase domestic resource mobilization and fight illicit financial flows (OECD, n.d.c). The original three-year mandate was renewed for three more years (2018–2020) at the Global Forum plenary meeting in November 2017 (OECD, n.d.d).

There is also a move towards public and centralized registers of the ultimate owners of trusts, foundations and other opaque vehicles used by multinational corporations. Advances in this effort will improve transparency in the natural resources sector and illuminate instances where “apparently unrelated parties” are engaged in base erosion.

In addition, due diligence from purchasers of natural resources may be required to ensure that the resources were not acquired illegally and to prevent the sale of conflict minerals (minerals whose sale proceeds are helping finance conflict). In particular, it may be helpful for foreign buyers of natural resources to apply “know your customer” rules when purchasing natural resources from Africa. This may help to ensure that the natural resources considered for purchase have not been stolen or smuggled out of their countries of origin. The Kimberly process for diamond origin verification is an example.

The High Level Panel on Illicit Financial Flows from Africa and others recommend increasing tax transparency, expanding networks for the exchange of information and participating in the automatic exchange of information between countries.

POLICY RECOMMENDATIONS

Overly generous incentives and fiscal stability clauses, fragmented government oversight and illicit financial flows by multinational companies have reduced government revenue from the non-renewable natural resources sector. African countries lose about 2.7 per cent of GDP through base erosion and profit shifting by multinational corporations. Some estimates put losses at between 1 per cent and 6 per cent of GDP (Moore, Prichard and Fjeldstad, 2018).

Heavy reliance on corporate income tax and the dominance of multinational firms in the natural resources sector have exposed African countries to the harmful effects of base erosion and profit shifting and illicit financial flows. To address these issues, African countries may consider the following actions.

DEVELOP EVIDENCE-BASED NATIONAL ACTION PLANS AND COORDINATING FRAMEWORKS TO TACKLE ILLICIT FINANCIAL FLOWS

- Deepen understanding of how illicit financial flows operate at the national level.
- Develop a national action plan that addresses key vulnerabilities.
- Develop a coordinating framework for tackling illicit financial flows that specifies the responsibilities of each government agency for each aspect of the plan to combat illicit financial flows.

ENHANCE CAPACITY FOR ASSESSING TAXES

- Build capacity in relevant agencies to verify the quality and quantity of extracted natural resources—for example, by investing in laboratory and testing facilities.
- Consider using benchmark prices for valuation, as in the “sixth method” use of publicly quoted prices.
- Consider alternative means for assessing the

value of natural resources, such as administrative pricing, to prevent transfer mispricing between related parties.

- Consider engaging external experts to verify the quality and quantity of extracted natural resources and the cost of equipment imported from related parties.
- Enhance the skills and capacity of tax administrations to understand tax issues in the natural resources sector, using toolkits for transfer pricing risk assessment.

INTRODUCE POLICIES TO COUNTER BASE EROSION AND PROFIT SHIFTING

- Focus on transfer pricing, which is one of the biggest challenges affecting the natural resources sector.
- Use the OECD’s BEPS package to review and update tax treaties to close loopholes that enable abuse. Consider the opportunities offered by the Multilateral Instrument for the natural resources sector.
- Consider going beyond the OECD’s BEPS package and applying the “sixth method” for trade in commodities for which price information is publicly available.
- Consider placing less emphasis on taxing corporate income, or use formulary approaches to tax a share of a multinational group’s profits.
- Discuss alternatives to the arm’s length principle with interested countries through bilateral, plurilateral or regional agreements—such as allocating taxes based on variables that are less easy to manipulate than reported local profits, and seeking legally enforceable agreements to limit tax competition, such as those in the European Union on state aid.
- Consider introducing tax coordination into negotiations on the African Continental Free Trade Area. Reaching agreement on tax issues could offer guarantees against base erosion and profit shifting that countries need in order to pursue deeper integration.

ENHANCE TRANSPARENCY AND ACCOUNTABILITY TO COUNTER TAX AVOIDANCE AND ILLICIT FINANCIAL FLOWS

- Require legislative approval of the award of rights to explore and extract natural resources.
- Require more transparency by extractive companies and accountability by governments, for example, by joining the Extractive Industries Transparency Initiative and implementing its recommendations and joining other transparency initiatives.
- Consider national legislation requiring disclosure of contracts by extractive companies and monitoring and enforcement mechanisms.
- Require politicians and others involved in managing natural resources to disclose their wealth and their interests in companies engaged in extractive activities or in companies that deal with them.

MAKE GREATER USE OF INFORMATION EXCHANGE

- Sign on to international efforts to improve tax transparency.
- To the extent that the OECD approach to information exchange is not appropriate to African countries' needs, pursue alternatives at the pan-African and South-South levels, where partners are more likely to share their perspectives, such as the pilot on information exchange being undertaken by the African Tax Administration Forum.
- Update the article on exchange of information in tax treaties, or negotiate tax information exchange agreements with key trading partners.
- To the extent possible, prepare to use new information sources, such as automatic exchange of information for tax purposes and the Country-by-Country Reporting risk profiling tool.
- Adapt the Country-by-Country Reporting tool to the needs of African countries by lowering the \$750 million threshold to one that is better adapted to African economies, and broaden its scope.

ENHANCE COLLABORATION AMONG GOVERNMENT AGENCIES IN NATURAL RESOURCES POLICY MAKING AND IMPLEMENTATION

- Encourage closer coordination of government agencies for a consistent approach in negotiating bilateral investment treaties, stability clauses and agreements to explore, develop and produce natural resources to ensure that they do not impede taxation. (Ideally, these non-tax agreements should not include tax provisions.)
- Encourage closer cooperation among government agencies engaged in natural resources management, tax administration and customs authorities to enhance data and information sharing.

REVIEW POLICIES RELATING TO TAX CERTAINTY AND TAX INCENTIVES

- Engage stakeholders in tax policy formulation and implementation and ensure that legislation is clearly drafted to avoid ambiguity.
- Issue public guidance and rulings to clarify ambiguous provisions.
- Avoid becoming locked in to agreements with stability clauses that are unduly generous to multinational corporations
- Consider revising existing agreements that are not in a country's best interest over the long term, balancing the potential gains against any temporary reduction in investment that might be associated with reduced tax certainty.

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CHAPTER 7

FISCAL AND PUBLIC DEBT SUSTAINABILITY



Public debt rose in Africa in 2017, reaching 59.1 per cent of GDP. The high and rising debt created debt vulnerabilities for many African countries. About 40 per cent of low-income countries now face debt servicing challenges, and an increasing number of countries are at high risk of debt distress or in debt distress. Five countries are in debt distress today (Chad, Mozambique, South Sudan, Sudan and Zimbabwe) compared with none in 2014.

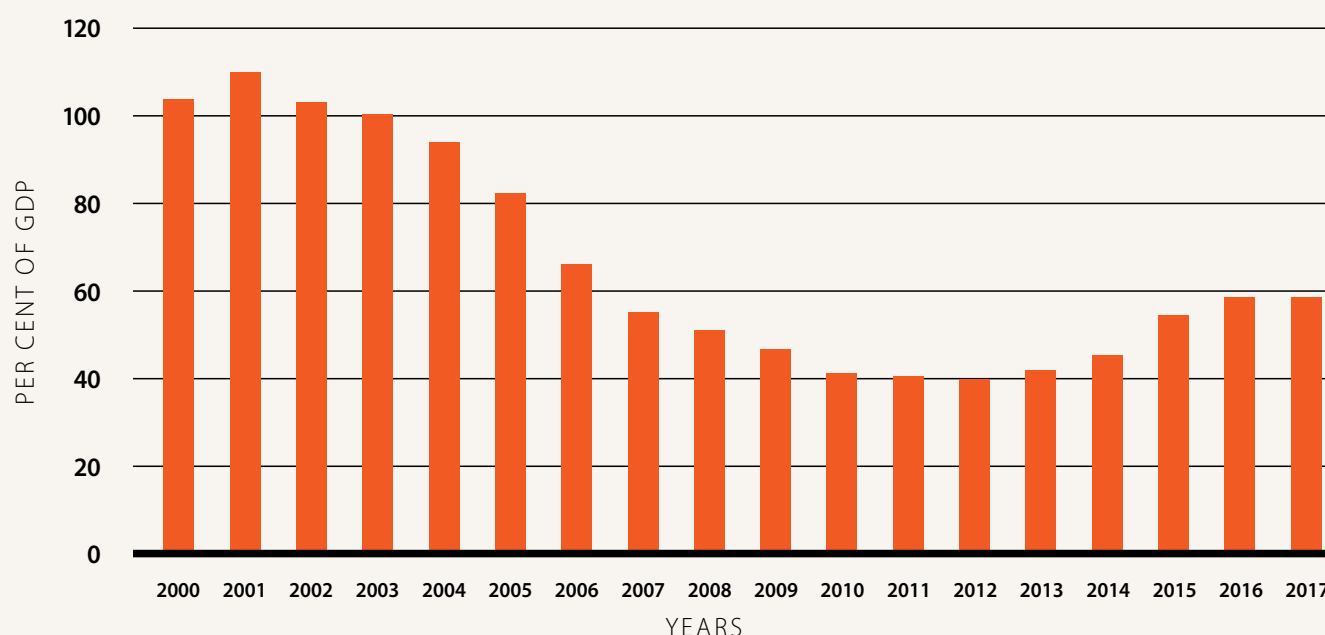
With 16 African countries in debt distress or high risk of debt distress, low government revenue is the most common factor. To ensure debt sustainability, countries need to increase the mobilization of tax and non-tax revenue and deepen the domestic capital market with increased reliance on local currency—denominated loans.

INTRODUCTION

With the slowdown in economic growth and low commodity prices, Africa's fiscal deficit peaked at 11.3 per cent of GDP in 2015 before declining to 5.0 per cent in 2018 (see figure 1.6 in chapter 1). As one of the instruments used by many African countries to partly finance their fiscal deficit, total public debt (general government gross debt) also increased, from 40 per cent of GDP in 2012 to 59 per cent in 2017 (figure 7.1).

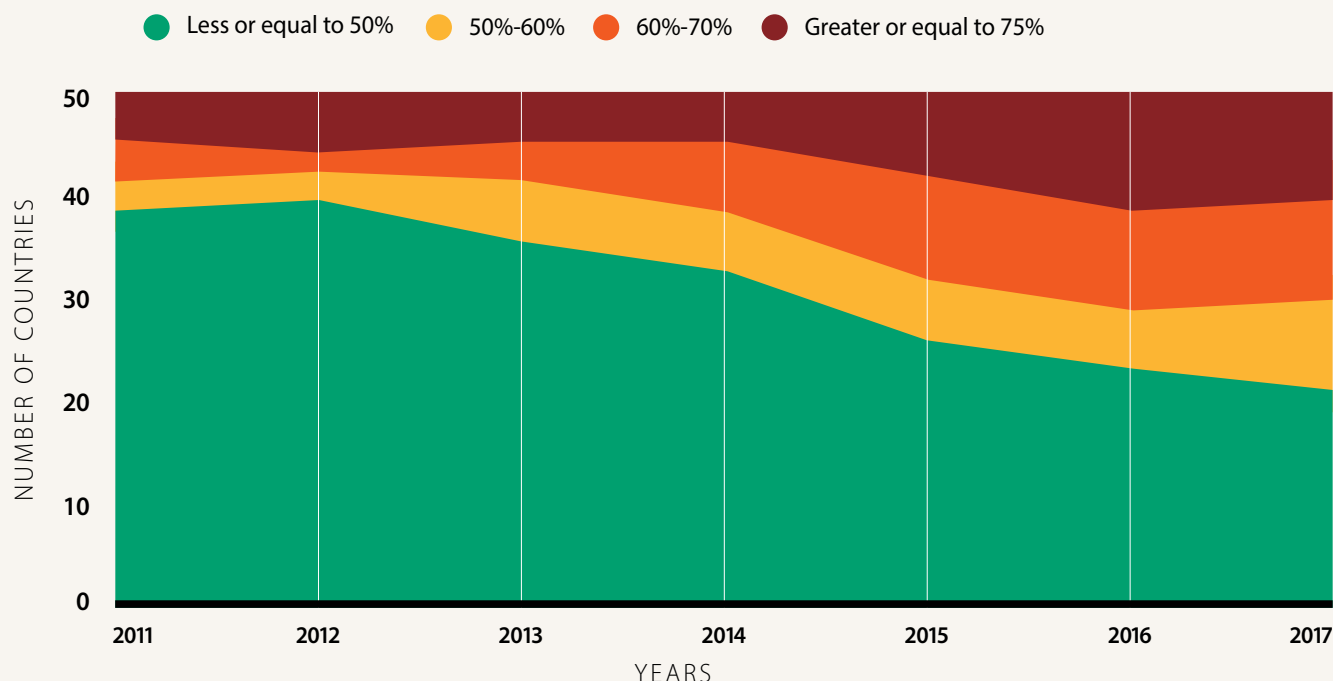
However, Africa's average debt to GDP ratio conceals widely different experiences, in part reflecting different resource endowments. The median public debt increased most noticeably among oil-exporting countries. Public and publicly guaranteed debt soared from an average of just over 20 per cent of GDP in 2011–2013 to 57 per cent in 2017. A similar level of public indebtedness was recorded in non-resource-rich economies with a history of government borrowing.

FIGURE 7.1. GROSS PUBLIC DEBT IN AFRICA, 2000–2017



Source: Based on data from IMF (2018e).

FIGURE 7.2. DEBT TO GDP RATIOS IN AFRICA, 2011–2017



Source: Based on data from IMF (2018e).

Although domestic revenue mobilization has improved in many countries in Africa, government revenue as a share of GDP remains fairly low by international comparisons (see chapter 2). In the run-up to the 2008–2009 global financial and economic crisis, African countries recorded fiscal surpluses, with a peak of 4.2 per cent of GDP in 2006, due partly to the commodity price boom. But as the global financial crisis hit, governments responded with countercyclical fiscal policy measures. As a consequence, Africa's median fiscal balance shifted from a surplus of 0.6 per cent of GDP in 2008 to a deficit of 3.8 per cent in 2009.

The post-crisis countercyclical expansion was financed through a combination of increased revenue collection (especially in resource-rich countries), domestic debt (bond issuances) and external borrowing, which led to a rising public debt burden (discussed in detail below). The fiscal balance deteriorated further after 2013 (reaching its worst level of –8.4 per cent of GDP in 2015), as government spending rose unsupported by similar increases in revenue.

This chapter examines public debt dynamics in African countries and disaggregates external and domestic debt by instrument, creditor and debtor. It discusses the relationship between fiscal policy and debt sustainability, emphasizing the need for increased revenue mobilization and prudent debt policies for African countries to address vulnerability, particularly to debt denominated in foreign currencies.

PUBLIC SECTOR DEBT

The number of countries with a debt ratio of more than 75 per cent of GDP has doubled since 2011, although there are signs that the number is stabilizing (figure 7.2). A much more dramatic increase has occurred in the number of countries with a debt ratio of 60–75 per cent of GDP (from 2 in 2012 to 10 in 2017), while the number of countries whose public debt is less than half of GDP has declined, from just below 40 to 23. The International Monetary Fund (IMF, 2018e) projects public debt across the continent to level out in the coming



Africa's stock of public external debt averaged about \$309 billion over 2000–2006 and then rose further to \$707 billion in 2017, with a 15.5 per cent increase from 2016 alone.

years and even decrease. Nevertheless, as Songwe (2018) argues, there are many reasons to be worried about African debt. These include potential adverse impacts on growth and job creation.

In 2017 debt rose to the highest levels in Eritrea (131 per cent of GDP), Cabo Verde (126 per cent), Sudan (126 per cent), Gambia (123 per cent), Congo (119 per cent), Egypt (103 per cent) and Mozambique (102 per cent). At the same time, ratios of public debt to GDP have been rising steadily, giving rise to worries about sovereign defaults and fiscal vulnerabilities.

Cabo Verde's high public debt reflects the government's fiscal policy focus since 2005 on expanding the tax base and increasing public investment. These policies reduced the fiscal deficit (from 5.6 per cent in 2015 to 4 per cent in 2017), but domestic resource mobilization fell short of spending targets. Government borrowing increased, aimed at addressing the public expenditure challenges, declining productivity and restructuring of public enterprises, as well as the negative effects of external shocks (including weak economic growth in Europe, which reduced tourism).

In Gambia the main driver of public debt was the adverse effect of bad weather on subsistence rain-fed agriculture, which resulted in higher government spending and a widening budget deficit (reaching a peak of 9.5 per cent in 2016 before settling at 2.5 per cent in 2017). To finance the budget deficit, the government borrowed extensively from the domestic debt market. The high public debt in the other countries (Congo, Egypt, Eritrea, Mozambique and Sudan) resulted

largely from fiscal imbalances due to external shocks (declining commodity prices and poor weather conditions).

Public debt has varied by subregion and country. In Central Africa Chad's debt rose from 25.8 per cent of GDP in 2004–2008 to 52.5 per cent in 2017. In East Africa Ethiopia reduced its borrowing from nearly 68 per cent of GDP in 2004–2008 to 37.8 per cent in 2009 before steadily increasing it to 56.2 per cent in 2017 while pioneering financing innovations such as diaspora bonds and bond issues in the Eurobond market (foreign currency bonds registered outside their country of issue; ECA, 2018f). In Kenya public borrowing held steady at just over 40 per cent of GDP through the first decade of the century but then began to rise, reaching 55.6 per cent in 2017.

In North Africa, where social spending is still increasing, government debt is expected to continue to rise, at least in the short term. Striking examples include Sudan, where government borrowing exceeded 120 per cent of GDP in 2017, a sharp rise from 77 per cent in 2011–2013, and Egypt, where government borrowing rose from similar levels in 2011–2013 to more than 100 per cent in 2017. In Southern Africa Angola's borrowing rose sharply after 2013, reaching 79.8 per cent of GDP in 2016. Public borrowing in Mauritius rose from 47.3 per cent of GDP in 2004–2008 to more than 60 per cent in 2017. In South Africa public borrowing has been much lower, but also rising, going from 30.5 per cent of GDP in 2004–2008 to 52.7 per cent in 2017. Zimbabwe's borrowing was much higher in 2004–2008, at 51.5 per cent of GDP, and more

volatile, with a sharp increase since 2015, rising to 78.4 per cent of GDP in 2017. In West Africa, Benin's public debt exceeded 50 per cent of GDP, while Ghana's borrowing rose even higher, from 39.2 per cent of GDP in 2004–2008 to 71.8 per cent in 2017.

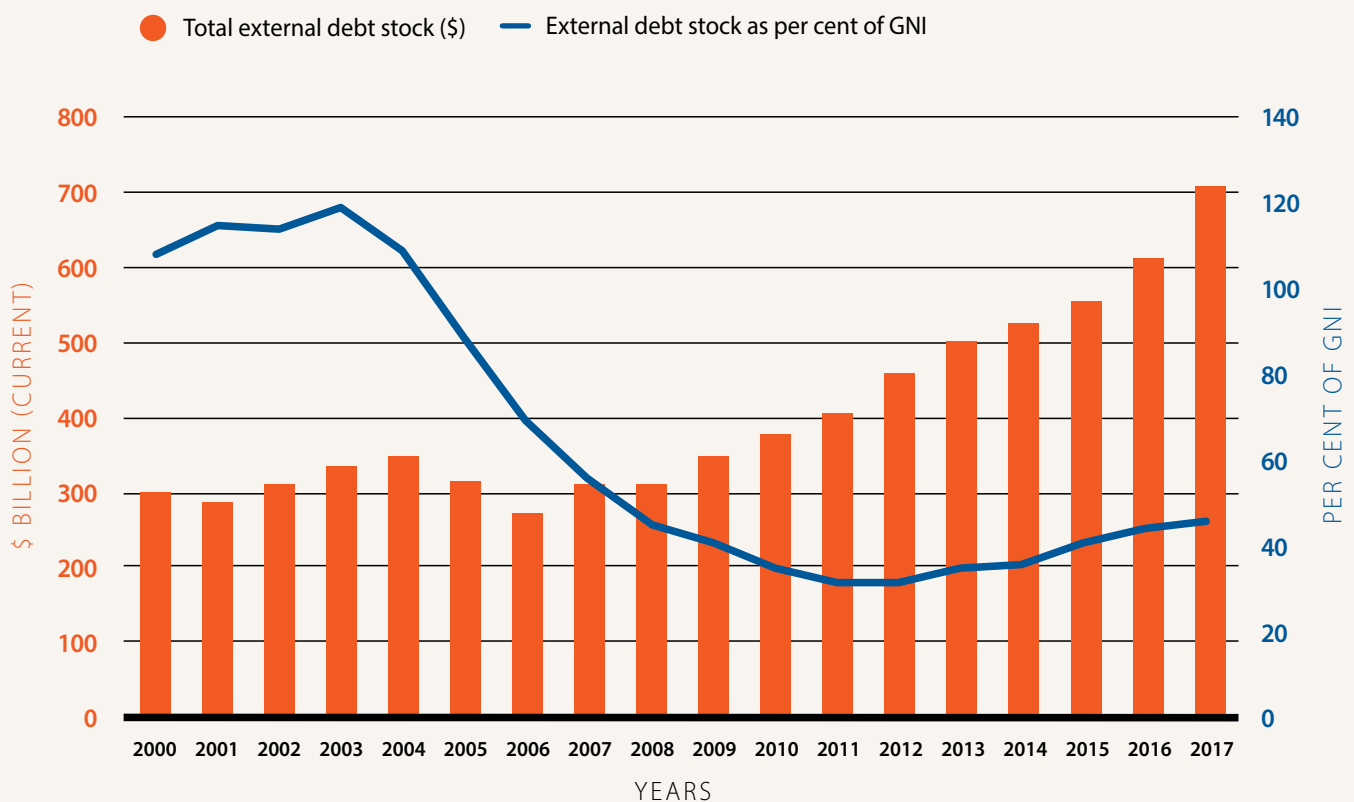
PUBLIC EXTERNAL DEBT

Africa's stock of public external debt averaged about \$309 billion over 2000–2006 and then rose further to \$707 billion in 2017 (figure 7.3), with a 15.5 per cent increase from 2016 alone. Most of the rise reflects increased external borrowing by middle-income countries, with five of the six largest economies on the continent accounting for more than half of public external borrowing in 2017. South Africa borrowed \$176 billion externally, followed by Egypt at \$82 billion, Morocco

at \$49 billion, Nigeria at \$40 billion and Angola at \$37 billion. The total debt stock was lower in some of the frontier markets than in middle-income countries, but the increase over the past few years was nonetheless considerable. For instance, Ethiopia's external debt stock rose more than 250 per cent, from \$7.3 billion in 2010 to \$26.5 billion in 2017. Kenya's pace of external debt accumulation was similar, with external debt stocks rising from \$8.8 billion in 2010 to \$26.4 billion in 2017 (nearly a 200 per cent rise). Ghana's public debt rise was close to 145 per cent between 2010 and 2017 (from \$9 billion to \$22 billion).

The increase in external debt accumulation raises concerns about debt sustainability in many African countries, especially as external debt stocks have risen much faster than economic growth owing

FIGURE 7.3. TOTAL EXTERNAL DEBT STOCKS IN AFRICA, 2000–2017



Source: Based on data from World Bank (2019).

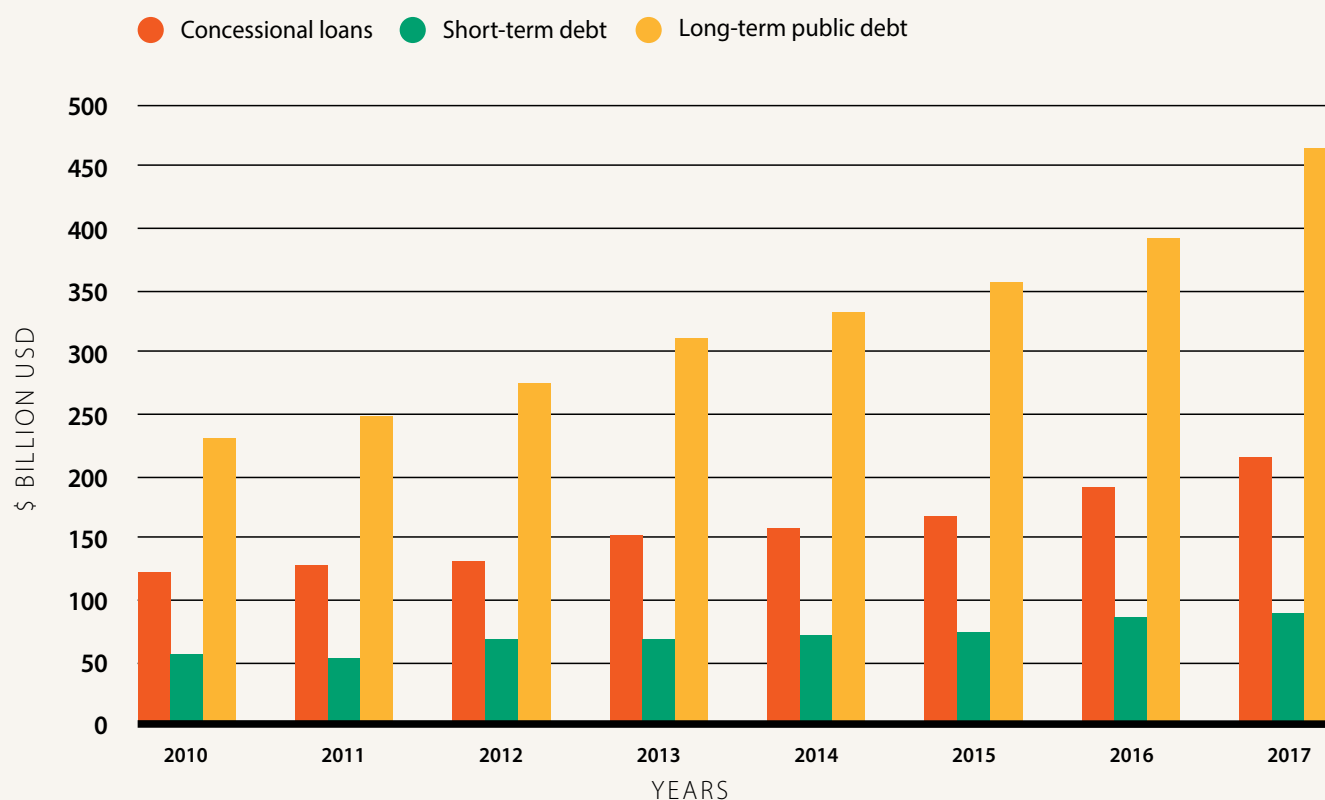
to rising interest rates in international capital markets. While the average ratio of external debt to GNI¹ in Africa declined from 119 per cent of GNI in 2003 to 32 per cent in 2012 before rising in 2013 and stabilizing at 46 per cent in 2017, debt ratios are still very high in some countries, mostly low-income economies. Debt ratios in 2017 were high in Djibouti (112 per cent), Mauritius (156 per cent), Mozambique (101 per cent), Mauritania (89 per cent), São Tomé and Príncipe (67 per cent) and Zambia (65 per cent). With the high share of external debt to GNI, debt servicing costs have increased. About a third of African countries had

debt servicing costs of more than 10–15 per cent of exports in 2017 (World Bank, 2018), including Côte d'Ivoire, with \$2.2 billion in external debt; Ghana, with \$2.1 billion; and Kenya and Zambia, both with \$1.6 billion; and Ethiopia, with \$1.4 billion.

The changing patterns of external borrowing help to explain Africa's rising external debt. In recent years African countries began to diversify the source and composition of their external debt (figure 7.4). They have increased their share of external borrowing from non-traditional creditors (non-Paris Club official bilateral creditors, foreign and domestic commercial creditors and other financial institutions) and reduced the share of concessional borrowing. Countries have been relying more on non-concessional sources (both bilateral and commercial creditors) and are

¹ Data on the ratio of external debt to GNI were available for all African countries up to 2017 while data on the ratio of external debt to GDP were available for only 14 countries. Thus, the discussion here uses the debt to GNI ratio instead of the debt to GDP ratio.

FIGURE 7.4. COMPOSITION AND TREND IN AFRICA'S EXTERNAL PUBLIC DEBT, 2010–2017



Note: Concessional debt is debt with an original grant element of 25 per cent or more. Short-term debt is debt with an original maturity of one year or less. Long-term debt is debt with an original or extended maturity of more than one year.

Source: Based on data from World Bank (2019).

increasingly tapping international bond markets. The expansion of non-concessional debt with longer maturity was due partly to enhanced IMF guidelines providing more flexibility in external debt sustainability limits and partly to progress by some countries in developing and deepening their financial sector, enabling them to issue dollar-denominated sovereign bonds in international capital markets.

While most African countries still rely heavily on financing from official bilateral and multilateral creditors (which together account for about 60 per cent of Africa's long-term external debt stock), non-traditional partners are emerging. These include the BRICS² countries as well as private creditors, commercial banks and other private entities. The increasing role of China among non-traditional bilateral lenders is especially noteworthy, particularly in external financing for large-scale infrastructure projects.

PUBLIC DOMESTIC DEBT

The recent expansion in domestic borrowing in Africa reflects efforts in middle-income countries such as Egypt, Ghana, Kenya, Morocco, Nigeria and South Africa to develop domestic debt markets to mobilize resources through bond issuance, improve financial sector development and deepen financial markets. Governments introduced securitized instruments (treasury bonds and bills) in the late 1990s and early 2000s to mobilize domestic resources and finance their fiscal deficit in the face of declining external assistance (concessional loans and grants).

In 2017 the stock of international sovereign bonds issued by African governments rose to more than \$30 billion, driven mainly by bond issues in South Africa (estimated at \$19 billion). Other countries that issued international bonds in 2017 include Nigeria (\$4.8 billion), Côte d'Ivoire

(\$2 billion) and Senegal (\$1.1 billion). The rise in bond issuance reflects improved borrowing conditions, increased investor confidence and a search for higher yields in the face of falling yield spreads in advanced economies.

There has also been a rise in local currency-denominated bond issuance, in part driven by the desire of some African governments and public sector entities to develop their domestic bond markets and meet demand from investors for low-volatility government, municipal, corporate and diaspora bonds. The rise has also been due partly to the need to address some of the financial vulnerability linked to foreign currency borrowing. For instance, in 2016 the stock of treasury bonds and treasury bills issued in local currency in Africa totalled close to \$220 billion, or about 9 per cent of GDP. Some countries that find it difficult to borrow at long maturities have been issuing medium-to long-term bonds in local currency, with 5–10 year maturities (for example, Mozambique, Niger and Uganda) or tenor of more than 10 years (for example, Benin, Burkina Faso, Kenya, Mali, Tanzania and Zambia).

Domestic bonds are usually oversubscribed. In Nigeria's government bond auction for June 2018, investors' bids reached 66.7 billion naira (\$183.4 million), well above the initial offer of 60 billion (\$165 million). In Kenya bond trading was 21 per cent higher over the same period in 2018 than in 2017, with a turnover of 232 billion Kenyan shillings (\$2.3 billion) in the five months to May 2018.

African governments view local currency bond markets as an effective means to mobilize alternative sources of finance for development, reduce dependence on foreign currency debt and mitigate the risks of external shocks and currency mismatches. However, to ensure sustainable development and the deepening of local currency bond markets, countries must address a range of challenges, such as weak legal, regulatory and institutional frameworks; underdeveloped

² Brazil, Russian Federation, India, China and South Africa.

secondary markets; illiquid debt instruments; short maturities and a restricted and undifferentiated investor base (DIE, 2015). Thus, countries need to create a sound macroeconomic environment, develop appropriate financial infrastructure, deepen the banking sector and promote trade openness. Moreover, harmonizing the legal and regulatory framework, improving the rule of law and facilitating the cross-listing of bonds on several exchanges will help create scale economies and deepen local currency bond markets.

Many analysts argue that domestic borrowing has advantages over external borrowing as a source of credit for governments. For instance, local currency—denominated loans can be serviced by tax revenue in the same currency, and governments have greater control over the conditions on which they can borrow, including the rate of interest and loan maturity. Moreover, advances to governments in the form of loans or bonds held by commercial banks in their asset portfolios serve as a form of liquid reserve, allowing banks to expand their lending to the private sector.

COSTS OF RISING PUBLIC DEBT

Rising public debt in Africa has led to increased government spending on interest payments. Strikingly, the largest increases have been among non-resource-rich countries, whose governments devoted nearly 10 per cent of total spending to interest payments in 2016, more than double the 4 per cent in 2011. Oil-exporting countries devoted close to 13 per cent of fiscal spending on interest payments in 2008, less than 4 per cent in 2012 as interest rates fell and then nearly 7 per cent in 2015.

A key part of public debt financing is the cost of servicing debt. Servicing domestic debt issued in

the local currency is easier than servicing external debt, particularly if debt service payments lead to a rise in private sector incomes and expenditures that may be taxed or are subject to central bank management of interest rates. Servicing external debt, by contrast, imposes pressures on government cash flow. External debt service rose overall, with some disparities among subregions. For instance, in oil-producing countries south of the Sahara, external debt service jumped from 1.2 per cent of GDP in 2011–2013 to 2.2 per cent in 2016 (a 1 percentage point increase) while in North Africa, external debt service was highest but rose 0.3 percentage point, from 2.4 per cent of GDP in 2011–2013 to 2.7 per cent in 2016, reflecting the subregion's greater integration in international financial markets.

The rise in total external debt service reflects increasing external borrowing by the private sector in African countries. As private economic activity stabilized in recent decades, and as African economies became more integrated into international financial markets, use of short-term trade credits expanded (Bonizzi and Toporowski, 2018). A typical example is Mauritania, which stands out for its very high levels of external debt. External trade plays a disproportionately large part in economic activity in Mauritania, a country with rich mineral resources and off-shore gas reserves. Mauritania's external borrowing has exceeded 100 per cent of GDP since 2014. Its public external debt is owed mainly to bilateral and multilateral official lenders, including Kuwaiti development lenders. But the scale of the government's external borrowing has placed Mauritania among countries with a high risk of debt distress (ECA, 2018a). The IMF expects the Mauritanian government to restructure its debt and, with appropriate fiscal management, to reduce the level of its borrowing to 73.2 per cent of GDP by 2019 and to fall below the 56 per cent benchmark from 2020 onward (IMF, 2017b).

Rising public debt in Africa has led to increased government spending on interest payments.



The experience of Ghana, in West Africa, has been different. Its total external debt rose from 19.3 per cent of GDP in 2009 to 42.8 per cent in 2016. Since 2007 the government has tapped the Eurobond market, with an initial issuance of a \$750 million Eurobond that matured in 2017. A further \$750 million bond was issued in 2013, partly to repay an earlier bond at a lower rate of interest. When the earlier bond matured, Ghana issued new bonds, with assistance from the World Bank, to refinance the outstanding amounts, culminating in a planned \$2.5 billion bond, \$1.75 billion of which is to be used to refinance earlier borrowing at a lower coupon rate (IMF, 2018d). This refinancing aims to facilitate the management of public external debt in Ghana in the short term (ECA, 2018d).

Within East Africa Ethiopia benefited from write-downs of its government's external borrowing at the turn of the century, lowering total external borrowing to 14.7 per cent of GDP by 2009. Since then the government has borrowed heavily to finance a large infrastructure investment programme, boosting total external borrowing to 37.9 per cent of GDP (\$18 billion) in 2015, most of it official debt owed to multilateral agencies. However, at the end of 2014 the government issued a \$1 billion Eurobond maturing in 2024 (IMF, 2017b). In Kenya the government managed to bring total external borrowing down to 19.3 per cent of GDP by 2012, assisted by the positive effects of high commodity prices on agricultural commodity exports. Since then, total private and public sector foreign debt crept up to 28.3 per cent in 2017, and it is expected to exceed 30 per cent in 2018. The Kenyan government tapped the Eurobond market, borrowing some \$2 billion. However, Kenya has kept external borrowing low by leveraging internal borrowing (ECA, 2018e).

The high and increasing debt levels have resulted in debt vulnerabilities for many countries, with an increasing number of countries falling into high risk of debt distress or into debt distress.

In the Southern African subregion a large financial sector coupled with controls on private sector external borrowing kept total external debt low for South Africa. Nonetheless, as commodity prices fell and economic activity slowed, external borrowing crept up, reaching 18.9 per cent of GDP in 2016. A much larger debtor in Southern Africa is Mozambique. The country benefited from a reduction in its public debt in the early 2000s, and in 2013 the government issued an \$850 million Eurobond to support the development of fisheries and liquefied natural gas. Total external borrowing rapidly mounted to 89 per cent of GDP in 2017. The Eurobond issue was refinanced in April 2016, but the government defaulted on a \$60 million coupon payment in January 2017. The IMF's latest Debt Sustainability Analysis (as part of its Article IV Consultation) put the Mozambique government's public debt at 112 per cent of GDP in 2017, down from 128 per cent in 2016 (IMF, 2018c).

RISING DEBT DISTRESS

Several factors have made debt servicing by African governments more difficult, including slowing economic growth, deteriorating terms of trade (as commodity prices fell), loosening fiscal policies and re-evaluation of cross-border risks in international financial markets³. The high and increasing debt levels have resulted in debt vulnerabilities for

³ Central banks in Europe and North America move away from the loose monetary policies implemented after the 2008 financial crisis

many countries, with an increasing number of countries falling into high risk of debt distress or into debt distress. By 2016, 14 African countries were in arrears. In many cases, the problems were political. Governance is the main problem in Sudan and Zimbabwe. Mozambique and Zambia are experiencing more purely financial difficulties for governments that only recently were able to access the Eurobond market.

About 40 per cent of low-income countries in Africa that are eligible to borrow at zero rates of interest from the Poverty Reduction and Growth Trust are now in debt distress or high risk of debt distress (IMF, 2018b). “While the causes of sliding into debt distress are country-specific, most of the countries in debt distress are those in fragile situations or those facing a large shock to the price of their major export commodity” (IMF 2018a: 12).

DEBT DISTRESS AND DOMESTIC RESOURCE MOBILISATION

With 16 African countries in debt distress or high risk of debt distress, low government revenue is the most common factor among them. Mozambique has the highest average government revenue to GDP ratio (23.5 per cent) among this group of countries, which is low compared with developing and emerging economies. Government revenue is below 20 per cent in most countries including Sudan, Chad, Zimbabwe, Ghana, and Ethiopia. Those countries will remain in the debt trap unless something is done to raise revenue through tax reforms, non-tax revenue, enhanced tax administration and reduced tax evasion and avoidance particularly in the natural resources sector. As the earlier chapters indicated, the potential to boost

BOX 7.1. RISK OF DEBT DISTRESS AMONG GOVERNMENTS IN AFRICA, 2014–2018

RISK OF DEFAULT ON DEBT	2014	2017	2018 ^a
In debt distress	0	2: Chad, Gambia	5: Chad, Mozambique, South Sudan, Sudan, Zimbabwe
High risk of debt distress	5: Burundi, Chad, Comoros, Democratic Republic of Congo, São Tomé and Príncipe	6: Burundi, Cameroon, Central African Republic, Ghana, Mauritania, São Tomé and Príncipe	11: Burundi, Cameroon, Cabo Verde, Central African Republic, Djibouti, Ethiopia, Gambia, Ghana, Mauritania, São Tomé and Príncipe, Zambia
Moderate risk	14: Burkina Faso, Central African Republic, Côte d'Ivoire, Gambia, Ghana, Guinea, Guinea-Bissau, Malawi, Mali, Mauritania, Mozambique, Niger, Sierra Leone, Togo	18: Benin, Burkina Faso, Comoros, Congo, Democratic Republic of Congo, Côte d'Ivoire, Ethiopia, Guinea, Guinea-Bissau, Liberia, Madagascar, Malawi, Mali, Mozambique, Niger, Sierra Leone, Togo, Zambia	14: Benin, Burkina Faso, Congo, Democratic Republic of Congo, Côte d'Ivoire, Guinea, Guinea-Bissau, Liberia, Madagascar, Malawi, Mali, Niger, Sierra Leone, Togo
Low risk	11: Benin, Cameroon, Congo, Ethiopia, Liberia, Madagascar, Rwanda, Senegal, Tanzania, Uganda, Zambia	4: Rwanda, Senegal, Tanzania, Uganda	6: Kenya, Lesotho, Rwanda, Senegal, Tanzania, Uganda

a. Data for 2018 are as of June.

Source: Based on data from IMF (2018b).

government revenue is huge, ranging from 12 to 20 per cent. Such an increase is sufficient to pull the 16 countries out of the debt trap.

To finance infrastructure and promote sustainable development, African countries should continue to borrow from the market to finance their growth (Songwe, 2018). However, noting that about 70 per cent of Africa's external debt is denominated in foreign currencies and that interest rates and debt servicing burden are rising⁴ due to tightening financial conditions in global markets, Songwe (2018) argues that African countries should increase borrowing in local currency in both domestic and international markets. This is important for countries to lower exposure and exchange risks. In this regard, prudent macroeconomic policies supported by development and better regulation of local capital markets are essential for countries to attract capital and manage their debt. At the same time, international financial institutions are urged to find means to hedge against exchange risks related to lending in local currency.

CONCLUSIONS AND POLICY RECOMMENDATIONS

The rise in government debt and the vulnerability of fiscal policy in Africa have exposed governments on the margins of solvency to debt difficulties, such as arrears to the IMF and other difficulties servicing debt. African countries are increasingly diversifying their sources of finance to mobilize both domestic and external resources. Today, around a third of African governments have taken advantage of financial markets and low interest rates in Europe

and the United States to issue Eurobonds. But these bonds have caused difficulties for some governments as interest rates in developed countries rose. With slower economic growth, little immediate prospect of rising commodity prices and intensifying pressure on government finances, debt difficulties are likely to spread in the near future.

To prevent fiscal and debt positions from deteriorating, African governments need to rebalance their policy framework to maintain stable income and expenditure flows for achieving the Sustainable Development Goals. Countries need to strengthen their capacity (especially human and institutional skills in national public budget agencies) to conduct more effective assessments of risks to public debt sustainability and to public borrowing for long-term development infrastructure projects (the capacity to design bankable projects and ensure cost-effective means of repaying debt).

African governments should finance their deficits in local currency markets by issuing financial obligations with the longest possible maturity. Local currency—denominated debt—has the advantage that it is “hedged” by the government's assets and income in that same currency, in contrast to government assets in foreign currencies, which consist overwhelmingly of their foreign currency reserves.

The deterioration in the finances of African governments and the squeeze on international financial liquidity threaten the fiscal balance and debt sustainability of those governments. To avoid this, governments need to rebalance fiscal policy to maintain government spending while increasing revenue to reduce fiscal deficits without austerity.

⁴ For example, the nominal value of Ghana's Eurobonds of \$750 million in 2007 was \$3.4 billion in 2017 (Songwe, 2018).

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CHAPTER 8

CONCLUSIONS AND POLICY RECOMMENDATIONS



Over the past two decades, African countries made notable progress in mobilizing domestic resources to finance their development goals. However, despite the fiscal reforms undertaken by many African countries since 2000, government revenue, at 21.4 per cent of GDP in 2018, remains low relative to the continent's potential and the financial resources needed to achieve national development aspirations. The incremental financing needs for Africa to achieve the Sustainable Development Goals (SDGs) are huge, with estimates ranging from \$614 billion to \$638 billion a year between 2015 and 2030. The incremental financing needs are particularly high in low-income countries and lower-middle-income countries, at as much as \$1.2 trillion a year. This translates into an estimated financing gap of 11 per cent of GDP between 2015 and 2030.

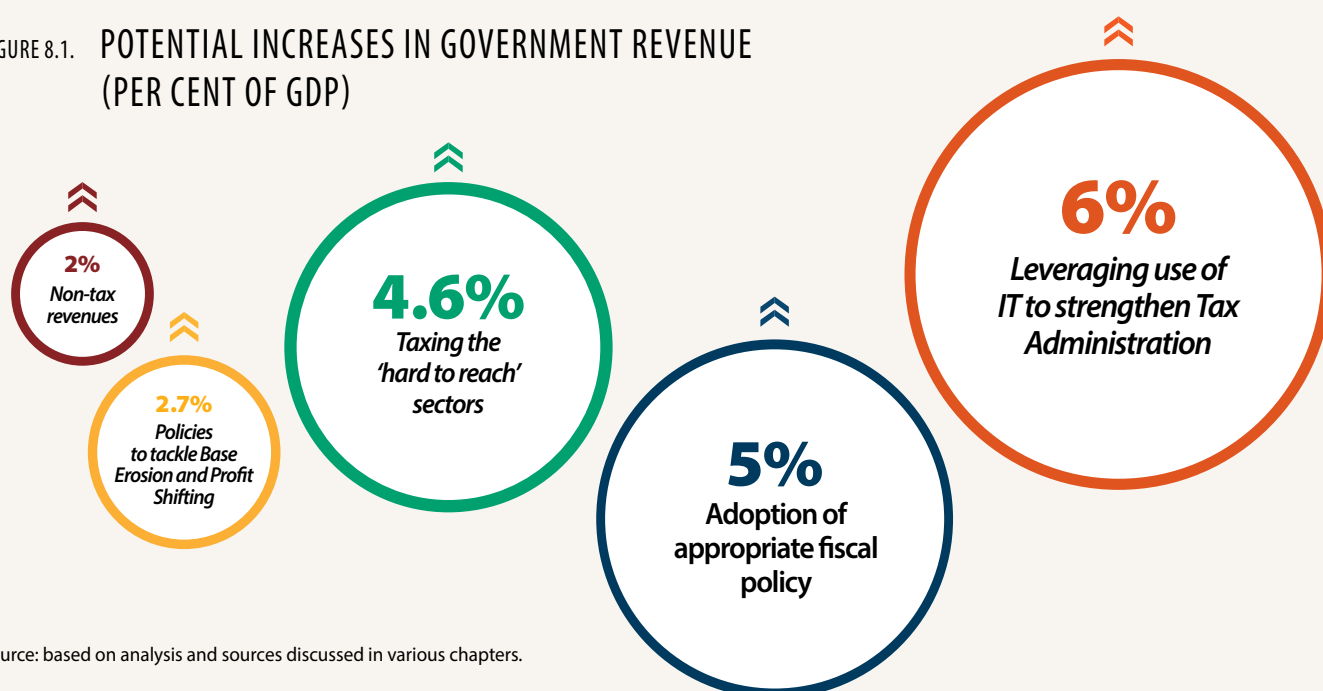
Against this backdrop, this Report analyses the state of fiscal policy and finds that African countries

can broadly increase government revenue by 12–20 per cent of GDP (figure 8.1). It identifies potential means of increasing revenue, including adopting appropriate fiscal policy; taxing hard to reach sectors such as agriculture, the informal sector and the digital economy; improving mobilization of non-tax revenue; leveraging information technology and digitalization to broaden the tax base, reduce revenue collection costs and improve tax administration; and strengthening policies that tackle base erosion and profit shifting, tax avoidance and tax evasion.

The report uses secondary data as well as primary data collected from 10 case study countries to examine the institutional and policy factors that influence the effectiveness and efficiency of fiscal policy. Fiscal performance and public revenue collection during 2000–2018 receive special attention.

This chapter summarizes the key fiscal policy issues in Africa and presents the salient findings. It proposes a policy framework for adoption by African countries that offers a menu of policy options for raising additional revenue to meet the SDGs.

FIGURE 8.1. POTENTIAL INCREASES IN GOVERNMENT REVENUE
(PER CENT OF GDP)



Source: based on analysis and sources discussed in various chapters.

ECONOMIC GROWTH, MODERATE IN 2018, IS EXPECTED TO PICK UP IN THE MEDIUM TERM

African economies grew by 3.2 per cent in 2018, down slightly from 3.4 per cent in 2017. Growth was underpinned by recovering commodity prices, consumption growth and the momentum of sustained government investment in infrastructure. Countering that, however, was the difficult external environment, with a strengthening US dollar, a slowdown in global trade and a decline in capital inflows in response to domestic political and policy uncertainty. Growth is projected to pick up again, to 3.4 per cent in 2019, supported by global growth, improved trade conditions and sustained increases in commodity prices.

However, the current pace and quality of growth are not sufficient for African countries to achieve the SDGs and meet the aspirations of Agenda 2063. Indeed, with slow value addition and structural transformation, Africa's growth has not been conducive to adequate job creation, equity and broader social development. To accelerate sustainable and inclusive growth, Africa needs to enhance productivity by boosting investment to 30–35 per cent of GDP and increase revenue in order to finance spending to support achievement of the SDGs. Fiscal policy is an important tool for development and an anchor for macroeconomic stability.

To advance more rapidly towards the priorities of greater prosperity, poverty reduction and sustainable development, African countries need to enhance the efficiency of government spending by improving public financial management. And countries need to reduce maternal mortality and gender disparities in education and employment to reduce inequality.

FISCAL POLICY COULD FOSTER INCLUSIVE GROWTH IN AFRICA

Africa has the second highest income inequality in the world, after Latin America. Inequality

Analysis of data for 42 countries shows a positive and significant effect of government spending on the inclusivity of growth.

increased in 20 countries between 2000 and 2015 and fell in 17 countries. Analysis of data for 42 countries shows a positive and significant effect of government spending on the inclusivity of growth. A 1 percentage point increase in government spending leads to about a 0.27 percentage point increase in growth inclusivity, other things remaining unchanged. Government spending that is more effectively targeted to the poor could reduce inequality if accompanied by measures to ensure that government transfers and subsidies do not distort prices in the economy.

ACYCLICAL FISCAL POLICY CAUSED MACROECONOMIC INSTABILITY

Of 45 African countries examined, 34 practiced acyclical fiscal policy, seven practiced procyclical policy and only four countries practiced countercyclical fiscal policy. Acyclical fiscal policies, which do not take the business cycle into account, had adverse effects on macroeconomic stability, leading to a deterioration in macroeconomic indicators such as public debt. On average, total public debt increased, with more than half of the 45 countries exceeding the debt threshold of 50 per cent of GDP between 2015 and 2017. In addition, fiscal balances, which were positive in 2000, deteriorated, exacerbated by the double shocks of the 2008 global financial crisis and the 2014 commodity price drop. Oil-exporting countries were the hardest hit.

GOVERNMENT REVENUE HAS RISEN SINCE 2000 BUT HAS TRENDED DOWN IN RECENT YEARS

With the large number of fiscal reforms implemented over the last two decades, (weighted)

African countries should not rush to adapt low-tax policies; doing so would reduce revenues that are critical for development without increasing investment.

fiscal performance varied across African countries, however. Some countries implemented fiscal reforms, boosting revenue over 2000–2018. The number of countries collecting revenue equivalent to 11–20 per cent of GDP rose from 25 to 35, while the number collecting revenue equivalent to 21–30 per cent rose from 5 to 8. Angola, Eswatini, Lesotho, Namibia, Seychelles and South Africa consistently collected revenue equivalent to more than 25 per cent of GDP between 2012 and 2015, indicating that economies of all sizes could achieve high rates of revenue collection. Average government revenue as a share of GDP in Africa increased from 22.8 per cent in 2000 to 31.4 per cent in 2008 and was 21.4 per cent in 2018. Of 51 countries, the tax revenue to GDP ratio dropped in 29, including in major economies such as Angola, Ethiopia, Kenya, Morocco and Nigeria.

COUNTERCYCLICAL FISCAL POLICY COULD BOOST REVENUE BY UP TO 5 PER CENT OF GDP

Countercyclical fiscal policy could enable African countries to increase revenue, improve fiscal balances, reduce debt to more sustainable levels and expand fiscal space. Countercyclical fiscal policy emphasizes macroeconomic stability by taking into account the business cycle. It focuses on ensuring that the economy does not overheat when demand pressures are high, while stimulating the economy during periods of low demand. The four African countries that practiced countercyclical fiscal policy (Ethiopia, Morocco, Nigeria and Zimbabwe)

collected more revenue on average—by as much as 5 per cent of GDP—than countries that practiced acyclical or procyclical fiscal policy.

African countries should, therefore, adopt countercyclical fiscal policy to improve revenue mobilization to finance investment and growth and at the same time promote macroeconomic stability. To safeguard macroeconomic stability, countries must align their fiscal policy with the business cycle, raising taxes and reducing spending to curb supply-side pressures during booms, while lowering taxes and increasing spending to boost the economy when economic activity slows down.

Synchronizing fiscal policy with the business cycle will require countries to adopt medium term planning frameworks (see box 8.1) and strengthen forecasting tools to inform medium-term planning.

In the long run fiscal policy affects development by encouraging investment. A recent wind of change has swept through tax policy, with developed economies lowering taxes as an incentive for investment, employment creation and retention, and income growth. However, in African countries taxes have very little influence on foreign investment decisions. An analysis of 45 African countries over 1980–2015 finds only a very small impact of tax policy on investment. A 1 per cent increase in investment comes at a cost of a 20 per cent decline in total tax revenue. An investor survey of 7,000 firms operating in Africa found that tax incentives rank 11 out of 12 factors that influence investment decisions. African countries should not rush to adapt low-tax policies; doing so would reduce revenue that is critical for development without increasing investment.

INDIRECT TAXES WERE THE MAIN SOURCE OF TAX REVENUE

Africa's tax revenue to GDP ratio increased from 17.9 per cent in 2000 to 19.9 per cent in 2005 but has since trended downward and was estimated at 12.7 per cent in 2018. Tax revenue was driven

BOX 8.1. MEDIUM-TERM REVENUE STRATEGY

In response to the concerns of developing countries, the Platform for Collaboration on Tax, a joint undertaking of the International Monetary Fund, Organisation for Economic Co-operation and Development, United Nations and World Bank, drafted a report and toolkit providing analysis and options for the tax treatment of offshore indirect transfers (Platform for Collaboration on Tax, 2018 [2015]). The Platform for Collaboration on Tax also submitted a paper on a Medium-Term Revenue Strategy (MTRS) in July 2016 to the G20 Finance Ministers meeting in Chengdu, China. The development and adoption of MTRS are a fundamentally new approach to strengthening developing countries' revenue mobilization.

Implementation of an MTRS requires the comprehensive and

consistent development of its four core elements:

1. Building broad-based consensus in the country for medium-term revenue goals to finance needed public expenditure.
2. Designing a comprehensive tax system reform covering policy, administration and legal framework to achieve these goals.
3. Committing to steady and sustained political support to implement the strategy over several years.
4. Securing adequate resources (from domestic sources as well as donors and development partners) to support implementation of the MTRS.

BROADENING THE TAX BASE BY TAXING HARD TO TAX SECTORS COULD BOOST REVENUE BY 4.6 PER CENT

Some economic agents, especially in the hard to tax sectors of the informal economy, agriculture and the digital economy, operate beyond the reach of tax authorities. Governments face difficulties bringing these economic agents into the tax net. They range from small enterprises operating in the informal sector to medium and large economic agents that simply evade taxes or report only portions of their income as subject to tax. These agents represent an opportunity for governments to increase revenue by bringing them into the tax net.

Broadening the tax base requires a major change in the mindset of policy makers, who need to pursue innovative means of reaching hard

largely by indirect taxes, such as value-added taxes (VAT), import duties and excise taxes. Revenue from indirect taxes as a share of GDP rose from 11.4 per cent in 2000 to 12.6 per cent in 2004 and then dipped to 9.0 per cent in 2018. Performance of corporate income tax revenue as a share of GDP was mixed, rising from 1.6 per cent in 2000 to 2.3 per cent in 2006 and declining thereafter to 1.2 per cent in 2018. Corporate taxes contributed a large share to tax revenue in some countries (as much as 6.0 per cent of GDP in Seychelles), while lagging behind in others.

to tax economic agents. Policy makers need to shift their focus from the easy target of compliant taxpayers, often burdened by unproductive bureaucratic procedures, to tax avoiders and tax evaders.

The inability to tax certain sectors and activities and the administrative challenges of tax collection result in lost revenue of up to 4.5 per cent of GDP in African countries. In 2001 Rwanda replaced its 15 per cent goods and services tax with a 15 per cent VAT, later raised to 18 per cent, which boosted tax collection by 1.5 per cent of GDP. Kenya lowered its VAT from 18 per cent to 16 per cent in 2003 and

Broadening the tax base requires a major change in the mindset of policy makers, who need to pursue innovative means of reaching hard to tax economic agents.

■ Non-tax revenue is an under-tapped source of government revenue in a majority of African countries, equivalent to just 2.6 per cent of GDP.

reduced the list of exempt and zero-rated items in 2013. As a result, VAT receipts rose by about 1 per cent of GDP in 2003 and another 0.5 per cent in 2013.

NON-TAX REVENUE COULD INCREASE GOVERNMENT REVENUES BY 2 PER CENT OF GDP

Non-tax revenue is an under-tapped source of government revenue in a majority of African countries, equivalent to just 2.6 per cent of GDP. Oil-exporting countries have been the best mobilizers of non-tax revenue through natural resources rents. One disadvantage, however, is the vulnerability of natural resources rents to commodity price changes. This non-tax revenue peaks during commodity price booms and declines during commodity price lows.

External grants are the main source of non-tax revenue in Africa, at 33.3 per cent of total non-tax revenue in 2016. African countries need to move away from this reliance on grants and build internal sources of non-tax revenue that are more robust to uncertainties in trade-related events. Several countries that have reformed their system

of non-tax revenue and shifted some of the burden to taxes on property income have reaped large revenue benefits (Botswana, Cameroon, Congo, Egypt, Mauritius, Morocco and Tunisia). Various levies on sales of goods and services are another important source of non-tax revenue in Africa, contributing 16.7 per cent of total non-tax revenue in 2016.

Over half of African countries (55 per cent) collect less non-tax revenue than they could. Improving efficiency could boost non-tax revenue collection by up to 2 per cent of GDP. Some African countries collect much more non-tax revenue as a share of GDP; Botswana and Congo collect as much as 16 per cent. Non-tax revenue falls short of potential in most countries because of lack of overall policy coherence, poor coordination between central and subnational authorities, lack of transparency, weak political will and inadequate infrastructure. Improving skills at the subnational level and strengthening revenue collection infrastructure would create more transparent institutions while bumping up revenue collection.

REFORMS HAVE BOOSTED THE EFFICIENCY AND EFFECTIVENESS OF TAX ADMINISTRATION IN THE REGION

Several countries have adopted tax administrative reforms, with the most popular reforms in Anglophone Africa being the establishment of semi-autonomous revenue authorities. The intention was to increase tax compliance and reduce collection costs by creating greater trust among taxpayers.

Another major reform has been the digitization of tax collection, which ensured the separation of tax

Over half of African countries (55 per cent) collect less non-tax revenue than they could. Improving efficiency could boost non-tax revenue collection by up to 2 per cent of GDP.



BOX 8.2. OPPORTUNITIES FOR FISCAL POLICY THROUGH DIGITALIZATION

African governments are using digital solutions for tax and expenditure policy, public financial management and public service delivery. Fiscal policy can benefit from digitalization in at least three ways.

DIGITAL IDENTIFICATION

Digital identification can broaden the tax base by making it easier to identify and track taxpayers and helping taxpayers meet their tax obligations. By improving tax assessments and administration, it enhances the government's capacity to mobilize additional resources. Digital ID systems yield gains in efficiency and convenience that could result in savings to taxpayers and government of up to \$50 billion a year by 2020 (Boston Consulting Group, 2012). At least 23 national identification programmes were introduced in Africa over 2000–2016, compared with 15 in the prior four decades.

AUTOMATION AND FILING

Automating tax administration systems provides multiple advantages for governments and taxpayers, including greater compliance and lower compliance cost, savings in tax collection time and costs, and more efficient assessments because of increased data. Seventeen African countries have introduced electronic filing and payment systems (Angola, Botswana, Cameroon, Eswatini, Ghana, Kenya, Mauritius, Nigeria, Rwanda, Senegal, Seychelles, South Africa, Togo, Tanzania, Uganda, Zambia and Zimbabwe), and three of them have made it compulsory for all taxpayers to pay their taxes electronically (Kenya, Uganda and Zimbabwe).

PUBLIC FINANCE MANAGEMENT

Digitization can enhance fiscal discipline through use of information technology systems that record, monitor and track

budget numbers based on a country's medium-term expenditure framework, underpinned by its national development plan. Such systems enable tracking changes in a country's development financing gap, information that can be used to strengthen the planning process and ensure that priority areas receive the required attention.

Information technology systems can enhance reporting and therefore the transparency and accountability of public finance. Transparency reduces opportunities for corruption and political influence, and by building taxpayer trust in the system boosts compliance. Addressing these challenges could raise tax revenue to GDP ratios, now at 13–18 per cent, by 3.5 per cent of GDP (IMF, 2018).

assessments and tax payments and has been more efficient than the previous physical verification system. By enhancing data collection, digitization has increased the availability of data for assessments. In addition, by enabling taxpayers to use technology such as payment through the banking system, digitization has saved time and strengthened data and records management. Digitization has also enhanced fiscal policy (box 8.2).

Rwanda adopted e-filing, which boosted revenue by 6 per cent of GDP. In Benin the tax division in charge of large corporate taxpayers saw its portfolio grow from 303 companies to 490 in 2017, thanks to a data exchange platform with customs and a revised system of public procurement. The country's Integrated Tax and Related Management System, launched in March 2018, enables filing tax returns online and is ultimately expected to

Use of information technology and digitization could enhance revenue mobilization by up to 6 per cent.

automatically manage more than 90 per cent of taxpayers in a large database. Tanzania undertook reforms in 2004 and 2012 that included automation of documentation, registration, tax collection and e-filing systems. Filings of VAT returns increased from less than 500 in 2009 to more than 4,000 in 2014, and revenue increased by 21 per cent between 2007 and 2011. In South Africa the introduction of e-taxation reduced both compliance time and cost by more than 22 per cent.

Digitalization of tax system can significantly boost fiscal revenue generation and management. Indeed, the use of information technology and digitization could enhance revenue mobilization by up to 6 per cent. African countries that digitized their tax administration strengthened data collection for tax assessment and saved on compliance costs. Even more can be saved on compliance costs by interfacing systems, which would reduce time for assessments and revenue monitoring.

Educating taxpayers on use of systems, tax obligations and the benefits of paying taxes should be a priority. In addition, countries will need to train tax collectors in how to use the data generated through digitization to make assessments more efficient.

TACKLING ILLICIT FINANCIAL FLOWS COULD BOOST TAX REVENUE BY AT LEAST 2.7 PER CENT OF GDP

Africa continues to suffer from revenue losses as a result of illicit financial outflows. These take place through aggressive tax planning, trade misinvoicing, misclassification of the quantity or quality of natural resources extractions, tax treaty shopping and cost inflation or overvaluation of expenses. The natural resources sector is particularly affected, because it is dominated by multinational corporations, with complex networks of affiliated businesses, and because of the large rents available in the sector. Fragmentation of oversight has also contributed to poor governance.

To reduce and halt illicit financial flows, countries have to gain a better understanding of the natural resources sector and of how illicit financial flows operate at the national level, which will allow them to negotiate better contracts with multinational firms and resist pressure for tax giveaways. Countries also need to develop a coordinated response to tax assessment and to information sharing across government agencies responsible for natural resources-related policy making and implementation.

The African Tax Administration Forum (2018) estimates that tax collections increased by about \$170 million after African countries adopted customized tools to tackle tax avoidance and illicit financial flows between 2017 and 2018. Fully addressing base erosion and profit shifting by multinational corporations would boost tax revenue by 2.7 per cent of GDP (Cobham and Janský, 2018); other estimates put the gains at 1–6 per cent of GDP (Moore, Prichard and Fjeldstad, 2018).

To maximize natural resources revenues, countries need to deepen their understanding of the vulnerabilities that make illicit financial flows possible. They can use this information in developing national action plans to coordinate the responsibilities of government agencies in dealing with illicit financial flows. National action plans should include an approach to taxing multinational corporations that is equitable, administratively straightforward and difficult to manipulate.

One method is to apply formulary apportionment (allocation of multinational corporation profits

 **Debt levels rose over 2011–2016 as revenue collections declined and spending increased, especially on infrastructure. General government debt for Africa increased from 40.1 per cent of GDP in 2011 to 59.1 per cent in 2017.**



across countries based on sales, payroll and capital base in each country) to determine the share of income to be taxed. Another is to reduce reliance on corporate income tax and taxing other variables that are harder to manipulate, such as gross sales of minerals, payments to factors of production (capital, labour and land) that are located in country or domestic utility payments. Exchanging information internationally, increasing transparency and avoiding overly -generous tax incentives and fiscal stabilization clauses will also be important. African countries should strengthen their oversight of the natural resources sector, in particular, including through better coordination among government agencies with responsibilities in this area.

LOWER THAN EXPECTED REVENUE COLLECTION INCREASED DEBT LEVELS AND REDUCED DEBT SUSTAINABILITY IN AFRICA

Debt levels rose over 2011–2016 as revenue collections declined and spending increased, especially on infrastructure. General government debt for Africa increased from 40.1 per cent of GDP in 2011 to 59.1 per cent in 2017. After the 2008 financial crisis, African countries faced severe constraints as financing from traditional donors on concessional terms declined. To meet their commitment to the SDGs and Agenda 2063, countries turned to borrowing in both domestic and international markets.

Concessional debt as a share of total debt peaked in 2004 at 55.4 per cent then sank to 35.8 per cent in 2016. The increase in commercial debt and the decrease in concessional debt meant that debt became more expensive. As the financial markets tightened in response to monetary policy in the West, the cost of borrowing in international financial markets rose. Tougher borrowing conditions included shorter debt maturities as investors anticipated changing financial conditions in the West. As a result, the stock of debt maturing

■ **To prevent further deterioration of fiscal and debt positions, African governments need to rebalance their policy frameworks to maintain stable income and expenditure flows to sustain policies to achieve the SDGs.**

in one year rose from 4.9 per cent of GDP in 2012 to 7.6 per cent of GDP in 2017.

As both debt stock and debt servicing costs rose, so did vulnerabilities, with some countries facing high risk of debt distress, including Chad, Congo, Eritrea, Mozambique, South Sudan and Zimbabwe, which were vulnerable to commodity price shocks or fragility. The joint International Monetary Fund and World Bank debt sustainability analysis finds that only six African countries are at low risk of debt distress (Kenya, Lesotho, Rwanda, Senegal, Tanzania and Uganda).

African countries need debt strategies that will improve debt management, including strengthening the fiscal framework by increasing revenue collection, taking a longer term approach to borrowing and restructuring the composition of debt, including increasing domestic local currency-denominated debt.

To prevent further deterioration of fiscal and debt positions, African governments need to rebalance their policy frameworks to maintain stable income and expenditure flows to sustain policies to achieve the SDGs. Countries also need to strengthen their capacity to conduct complex assessments of risks to public debt sustainability as well as risks to public borrowing for long-term development infrastructure projects.

* * *

■ Countries will need to achieve a fine balance between raising revenue and incentivizing investments.

The financing needed to enable African countries to achieve the SDGs and Agenda 2063 is substantial. The changes in global financial markets and the global economy mean that African countries need to look inward for financing, particularly through prudent fiscal policy. Coordinating fiscal and monetary policy is vital, since both tools must work together as stabilizers if they are to be effective in achieving the triple goals of growth, employment and stability. Taxation and spending must take the business cycle into account. It will be imperative

to understand the sources of revenue and how countries can ramp up their revenue collection to support development.

Countries will need to achieve a fine balance between raising revenue and incentivizing investments. Fiscal policy has the potential to reduce social inequities by reducing poverty and inequality. By advancing long-term growth and development, fiscal policy can help countries achieve the SDGs.

Finally, it is worth noting that analysis in this Report was limited by unavailability of detailed and comparable fiscal data for many African countries. We call upon these countries to address data gaps and make data accessible to enable analysis of country performance as well as useful comparisons across countries and subregions for experience sharing.

■ Fiscal policy has the potential to reduce social inequities by reducing poverty and inequality. By advancing long-term growth and development, fiscal policy can help countries achieve the SDGs.



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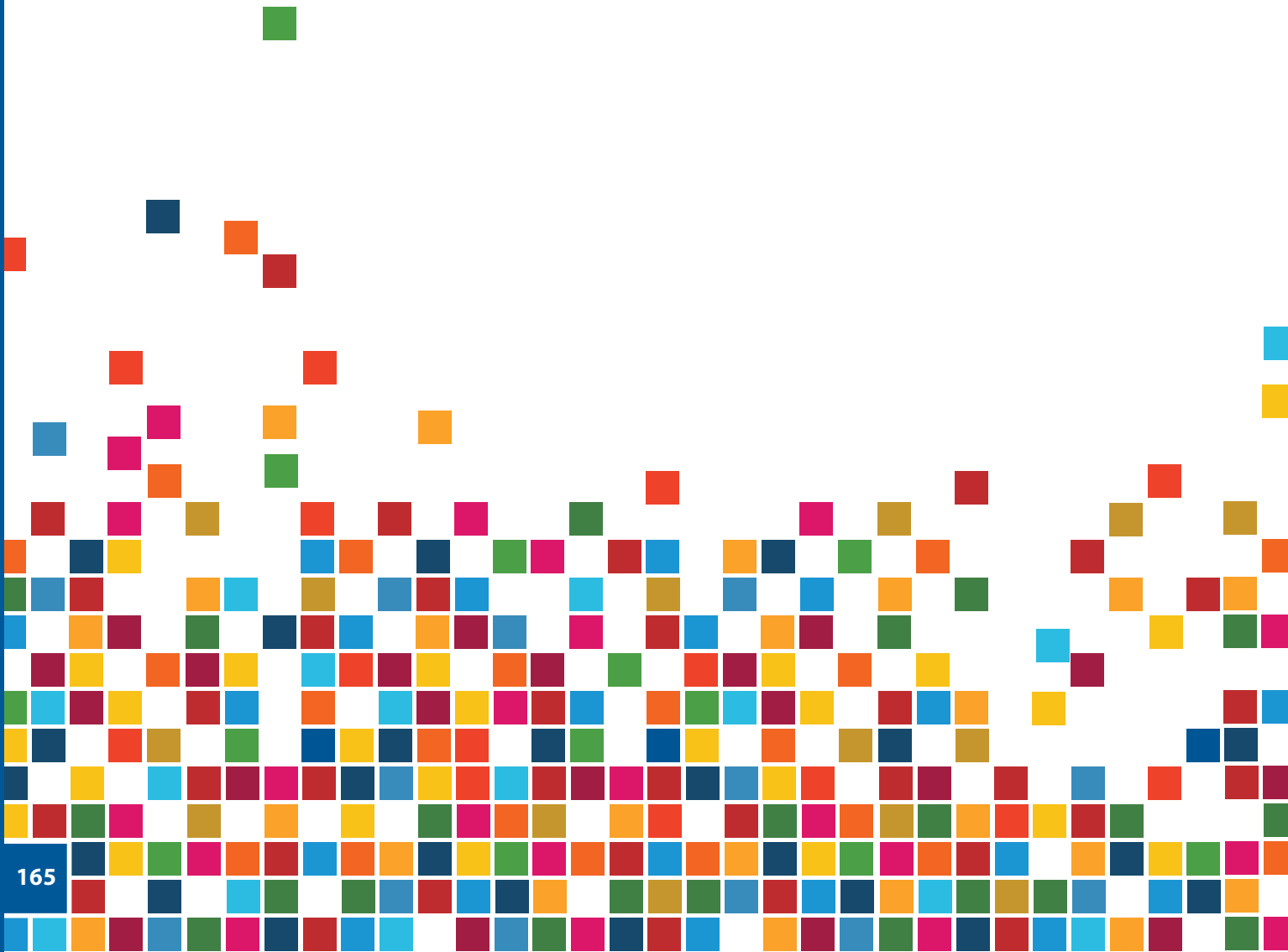
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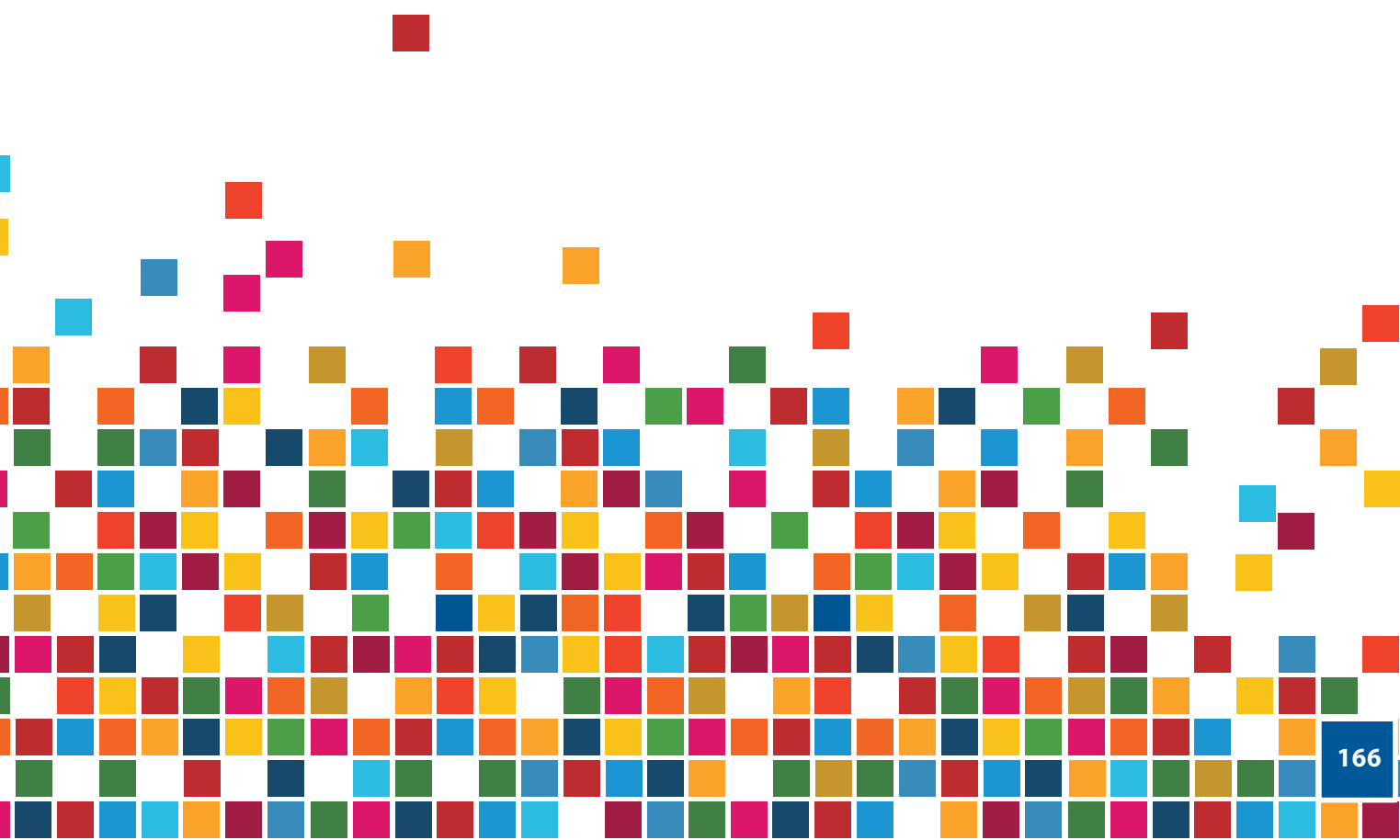
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STATISTICAL NOTE



The analyses in the 2019 *Economic Report on Africa* are based on the latest updated and harmonized data from leading sources, including questionnaires developed by ECA. The main economic and social data variables are from the United Nations Department of Economic and Social Affairs (UN-DESA) database. Data on some indicators are from the statistical databases of the International Monetary Fund (IMF), Economist Intelligence Unit (EIU), the International Centre for Tax and Development/United Nations University World Institute for Development Economics Research (ICTD/UNU-WIDER), United Nations Conference on Trade and Development (UNCTAD), United Nations Economic Commission for Africa (ECA) and the World Bank, as well as some government departments in African countries. Data published in the Report may differ from those of previous editions of the *Economic Report on Africa* due to recent assumptions and data revisions.

The UN-DESA Global Economic Outlook database provides comparable data on GDP growth for all African countries except Eswatini and Seychelles, for which data are obtained from the EIU database. Real GDP growth rates are generated using country data, with 2010 as the base year. Subregional inflation rates for country groupings are weighted averages, where weights are based on GDP in 2010 prices. Baseline scenario forecasts are based partly on UN-DESA Project LINK and World Economic Forecasting Model.

Social data are derived from the latest available data from ECA's African Centre for Statistics; African Development Bank; United Nations Children's Fund; UN-DESA; United Nations Development Programme; United Nations Educational, Scientific

and Cultural Organization; United Nations Statistics Division and the World Bank's World Development Indicators and PovcalNet databases. Employment and productivity figures are from Classification International Labour Organization's Key Indicators of the Labour Market and the World Employment and Social Outlook databases, while data on trade (exports and imports) are from UNCTAD and the World Trade Organization.

Government revenue data are obtained largely from the ICTD/UNU-WIDER Government Revenue Database, supplemented for some variables by macro-level data from the IMF's World Revenue Longitudinal Dataset, the World Bank's World Development Indicators database and ECA forecasts for 2017 and 2018.

Unless otherwise indicated, the data cover 53 African countries (excluding South Sudan due to the unavailability of historical data).

For some analyses, countries are classified into geographic subregions and country economic groupings, as shown in table SN1.

The thematic part of the Report employs primary data and information collected, harmonized and analysed by ECA staff from survey questionnaires. In addition, interviews were conducted with government officials and semi-autonomous revenue authorities in 12 case study countries: Angola, Benin, Chad, Ethiopia, Ghana, Kenya, Mauritania, Mauritius, Mozambique, South Africa, Sudan and Zimbabwe.

TABLE SN.1. CLASSIFICATION OF AFRICAN COUNTRIES IN THIS REPORT BY SUBREGION AND ECONOMIC GROUP

Economic group	African subregion				
	Central	East	North	Southern	West
Agricultural commodity exporters ^a	Cameroon Central African Republic São Tomé and Príncipe	Burundi Ethiopia Kenya Madagascar Rwanda Seychelles Tanzania Uganda	Egypt Mauritania Morocco Sudan	Malawi Mauritius Namibia Zimbabwe	Benin Burkina Faso Cabo Verde Côte d'Ivoire Ghana Mali
Mineral-poor countries ^b	Cameroon Chad Congo Gabon São Tomé and Príncipe	Burundi Comoros Ethiopia Kenya Seychelles Somalia Uganda	Egypt Libya Morocco Tunisia	Angola Eswatini Malawi Mauritius	Cabo Verde Côte d'Ivoire Gambia Ghana Guinea-Bissau Nigeria Senegal
Mineral-rich countries ^c	Central African Republic Equatorial Guinea	Congo, Dem Rep Djibouti Madagascar Rwanda Tanzania	Algeria Mauritania Sudan	Botswana Lesotho Mozambique Namibia South Africa Zambia Zimbabwe	Benin Burkina Faso Guinea Liberia Mali Niger Sierra Leone Togo
Oil exporters ^d	Cameroon Chad Congo Equatorial Guinea Gabon	Congo, Dem Rep South Sudan	Algeria Libya Sudan	Angola	Côte d'Ivoire Ghana Niger Nigeria
Oil importers ^e	Central African Republic São Tomé and Príncipe	Burundi Comoros Djibouti Eritrea Ethiopia Kenya Madagascar Rwanda Seychelles Somalia Tanzania Uganda	Egypt Mauritania Morocco Tunisia	Botswana Eswatini Lesotho Malawi Mauritius Mozambique Namibia South Africa Zambia Zimbabwe	Benin Burkina Faso Cabo Verde Gambia Guinea Guinea-Bissau Liberia Mali Senegal Sierra Leone Togo

Note: Groupings are based on UNCTAD trade data for 2012 and 2013 (SITC 33 for oil and SITC 27+28+32+34+35+68+667+971 for minerals).

a. Countries whose agricultural commodity exports account for more than 20 percent of exports.

b. Countries whose mineral exports account for less than 20 per cent of exports.

c. Countries whose mineral exports account for more than 20 per cent of exports.

d. Countries whose oil exports are at least 20 per cent higher than their oil imports.

e. Countries whose oil exports are less than 20 per cent higher than their oil imports.

