



Independent Review of Afghanistan 1397 Draft National Budget

A Snapshot of Resources, Allocations, and Public
Finance Management Performance

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Acronyms

ACTA	Afghan Coalition for Transparency and Accountability
AFN	Afghani (currency)
ARTF	Afghanistan Reconstruction Trust Fund
BC	Budget Circular
BRT	Business Receipts Tax
BU	Budgetary Unit
EPD	Equality for Peace and Democracy
FY	Fiscal Year
GDP	Gross Domestic Product
GRB	Gender Responsive Budgeting
IDLG	Independent Directorate for Local Governance
IMF	International Monetary Fund
M&E	Monitoring and Evaluation
MAIL	Ministry of Agriculture, Irrigation and Livestock
MoD	Ministry of Defense
MoEd	Ministry of Education
MoEW	Ministry of Energy and Water
MoF	Ministry of Finance
MoFA	Ministry of Foreign Affairs
MoHE	Ministry of Higher Education
Moi	Ministry of Interior Affairs
MoLSAMD	Ministry of Labor, Social Affairs, Martyrs and the Disabled
MoPH	Ministry of Public Health
MoPW	Ministry of Public Works
MoUD	Ministry of Urban Development and Housing
MRRD	Ministry of Rural Rehabilitation and Development
MTBF	Medium-Term Budget Framework
NAP 1325	National Action Plan for 1325
NDS	National Directorate of Security
NGO	Non-Government Organization
O&M	Operations and Maintenance
PFEM	Public Finance and Expenditure Management
PFM	Public Financial Management
PFMR	Public Financial Management Roadmap
SAO	Supreme Audit Office
USD	United States Dollars (currency)

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1. Introduction

Through its Afghan Coalition for Transparency and Accountability (ACTA) platform, EQUALITY for Peace and Democracy (EPD) has pioneered the utilization of the national budget as a monitoring tool for monitoring government resource distribution and service delivery. EPD conducts an annual review of the National Budget, which started in 1391, to provide further details to Parliament to review the national budget. The process gives insight to the national budget from a civil society perspective on national budget planning, approval, execution, monitoring and reporting with special emphasis on the role of civil society and citizens in the entire process.

1.1 Methods

The 1397 National Budget Review began with a desk review of the implementation process of key budget and Public Financial Management (PFM) reforms as outlined in policy documents and discussed in the literature. Accordingly, questionnaires were developed and divided thematically for each separate cluster of interviews for

With this annual project, EPD aims to present a simple and coherent review of the budget so that people can understand the budget and what it means for their daily lives and review the quality of services via allocated

resources. This independent budget review also provides details to Afghan parliament to review and approve the national budget. The process furthermore provides a platform for input on national budget planning from a civil society perspective. This snapshot budget review is a summary review released along with the sending of the budget to Parliament to provide a timely review of the budget and this year's developments in public financial management, reforms, and benchmarks.

Ministry of Finance's (MoF) Budget Policy and Reform Directorate, Aid Management Directorate, Revenue, and the Budget Execution Directorate. All figures for Fiscal Year (FY) 1397 are taken from the National Budget Draft sent to Parliament in 11 November 2017. The percentages mentioned in the report are rounded to the nearest whole number.

2. 1397 National Budget at a Glance

The 1397 National Budget represents a significant shift in the Government's approach to fiscal planning. For the first time, the Government presents a consolidated national budget over the medium-term with both the operating and development budgets in line with good international practices.

According to the budget draft, the aim of the 1397 budget is regulating public financial management. The draft has been prepared based on international standards of Government Financial Statistic (GFS) and Classification of the Functions of Government (COFOG).

GFS system provides a picture of the fund trend and expenditure. The expenditures for FY 1397 have been categorized into 100 sections including salary and fuel. On the other hand, COFOG System classifies the government functions in public welfare areas such as health, education and social protection. This initiative has considered the expenditure allocation based on the government function which facilitated governmental service delivery in the most essential areas in the society.

The Government of Afghanistan is committed to open, accountable and credible management of the national budget. These budget reforms will reduce corruption and strengthen public

financial management. More realistic base estimates for existing policy will increase the Government's ability to assess the fiscal space available for new investment and accelerate the process of shifting resources from poor performing low priority activities to high priority high performing ones. This is reflected most strikingly in the elimination of the poor practice of carrying forward previous year commitments, particularly in the development budget. In addition, the Government is replacing the systematic overestimation of program and project expenditures with more accurate and credible rolling forward estimates. As a result, the Government expects to achieve higher rates of budget execution not only in 1397 but also over the next few years, with the quality of expenditure improving over time.

The budget also presents historical data on original budgets versus actual outcomes to allow for transparent analyses of the trends in public investment, which is crucial to improving the allocation of national resources.

Total expenditure on the consolidated budget for 1397 is estimated to be AFN 354 billion, representing 24 percent of GDP (Table 1).¹ Out of the total national budget, 74 percent makes up the

¹ "Other expenditures not reported in Table one comprise an amount of AFN6 billion.

operational budget which includes financing the civil service and national plans. The estimated actual expenditure for 1396 on the operating budget is expected to be AFN 244 billion. In 1397, the Government is budgeting for over a 9 percent increase in the level of ordinary budget expenditure at AFN 267 billion. The estimated actual expenditure on the Discretionary Development budget for 1396 is expected to be AFN 30 billion; a little higher than in 1395. In 1397, the government has forecasted AFN 38 billion for discretionary developmental budget. For the non-discretionary budget, the

estimated actual expenditure is AFN 55 billion. The Government is budgeting for a lower amount reflecting conservative estimates of expenditure with a view of improving the performance of existing projects and providing additional funding to programs and projects based on outcomes achieved. This means that the Government is budgeting for less overall expenditure in 1397 than it did for 1396, reflecting lower grants and a more realistic estimate.

Table : Aggregate Budget

Source: FY 1397 draft national budget

Year	1395	1396	1397	1398	1399	1400
Source						
A. Cash receipts from Operating activities	351,845,964,870	416,708,930,916	357,261,140,510	355,008,270,882	350,002,552,613	285,342,595,777
B. Cash payments for operating activities	286,851,919,364	422,044,379,984	291,092,562,453	294,200,839,111	295,689,839,744	294,525,139,568
Net cash inflow from operating activities (A-B)	60,731,638,026	10,957,595,139	66,168,578,057	60,807,431,772	54,312,712,869	-9,182,543,791
C. Cash flows from investments In nonfinancial assets:						
Cash surplus/deficit (a-b-c)	53,395,186,848	7,348,304,831	53,694,949,084	51,887,693,854	45,918,142,519	37,415,358,203
D. Net acquisition of financial assets Other than cash	11,598,858,659	-12,683,753,900	12,473,628,973	8,919,737,917	8,394,570,350	-46,597,901,995
E. Net incurrence of liabilities	22,061,137,937	21,030,000	23,956,281,988	23,158,175,368	20,818,802,605	17,544,286,495
Net cash inflow from financing activities (E-D)	-1,034,525,936	2,654,787,275	1,547,700,000	1,465,816,698	1,229,667,064	614,833,532
Net change in the stock of cash (a-b-c-d+e)	-23,095,663,873	2,633,757,275	-22,408,581,988	-21,692,358,671	-19,589,135,540	-16,929,452,963
1 Revenue	-11,496,805,214	-10,049,996,625	-9,934,953,015	-12,772,620,753	-11,194,565,190	-63,527,354,985
2 Expenditure	364,098,241,435	416,708,930,916	349,410,669,761	347,159,349,391	342,155,043,290	277,496,379,075
Budget Aggregates as a % of GDP						
Revenue	354,186,777,254	372,732,564,045	354,575,443,066	357,419,201,548	351,241,314,548	339,195,047,951
Revenue	26.51%	29.63%	24.10%	23..18%	21.99%	17.08%
Expenditure	25.79%	26.51%	24.46%	23.87%	22.57%	20.88%

2.1 Ordinary and Developmental Budget

Afghan national budget mainly consists of two parallel budgets; Core Budget and External Budget. The External Budget is the fund spent through the international donor in Afghanistan. On the other hand, the core budget is the money comprised of domestic revenue and the donor assistance. It is further divided into two main parts of Ordinary Budget and Developmental Budget. The ordinary budget covers expenditures such as wages, salaries, goods, long-term assets and payment of interest while the developmental budget is mainly used for developmental and reconstruction purposes.

For the FY 1397, the government has allocated AFN 267.152 billion (USD 3.909 billion) for the ordinary budget which constitutes 74% of the core budget. 55.5% of the ordinary budget for the mentioned fiscal year will be financed through the domestic revenue and the rest will be covered through donor assistance. The ordinary budget shows a 0.5% decrease in comparison to the previous year.

Developmental budget has a very small share of the FY 1397 budget. This amount is AFN 93.739 billion (USD 1.371 billion) constituting 26% of the core budget. It shows a sharp decline in comparison to the previous year by a difference of 41.8%. The developmental budget is financed by both of the domestic revenue and donor assistance respectively, 35% and 65%.

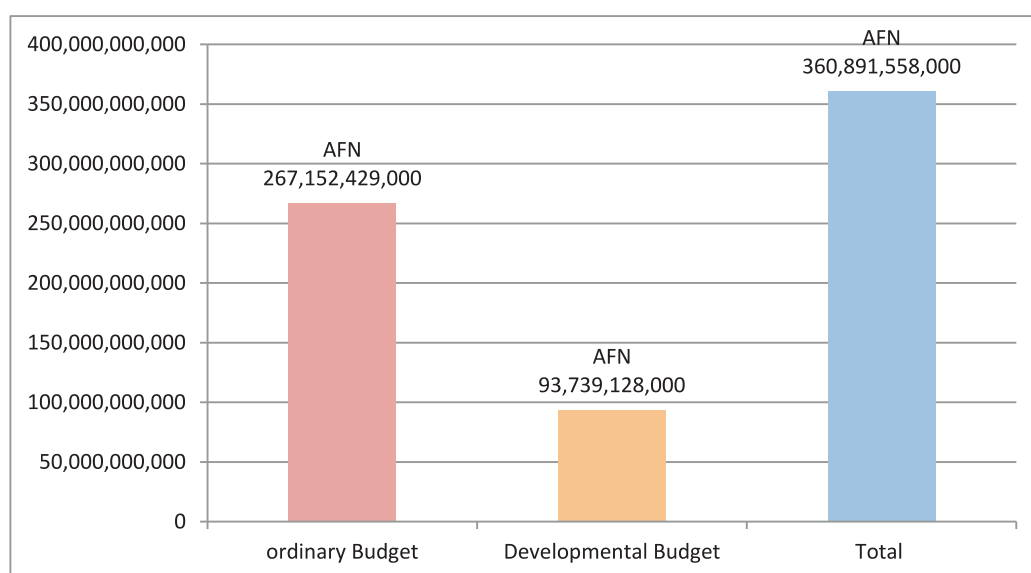


Figure 1: Ordinary and Developmental Budget for FY1397

Source: FY 1397 National Budget-Second Draft

Table 2: Comparing 1396 & 1397 National Budget

Source National budgets for FY 1396 & 1397/Figures are in AFN

	FY 1396 (000)	%	FY 1397 (000)	%	budget Difference (000)	% of difference
Ordinary Budget	268,412,219	63	267,152,429	74	-1,259,790	-0.5
Developmental Budget	161,001,496	37	93,739,128	26	-67,262,368	-41.8
Total	429,413,715	100	360,891,558	100	-68,522,158	-16

AFN 55.226 billion has been allocated for non-discretionary budget and 38.512 for discretionary budget, respectively, constituting 59% and 41% of the developmental budget. The percentage of the discretionary share in developmental budget shows an increase in comparison to the previous year (39%). As the government usually face critical challenges in terms of implementing the developmental budget. Therefore, it is very important for executives' administrations and National Assembly to closely monitor the related projects' financial expenditures and physical implementation.

Table 3: Comparing discretionary and non-discretionary budget for FY1396 and 1397

Source: National budget draft for 1397 and approved budget for 1396

Developmental Budget	1396 (000)	1397 (000)	1396 %	1397 %	Difference in the budget amount	% of difference
Discretionary Budget	63065933	38512862	39.17	41.09	-24553071	-38.93
Non-discretionary Budget	97935563	55226267	60.83	58.91	-42709296	-43.61
Total	161001496	93739129	100	100		

2.2 Estimated Allocations 1397

Budget allocation for FY 1397 is based on the government's priorities and capacity of the budgetary units in spending budget. As it is shown in the table below, Ministry of Rural Rehabilitation and

Development (MRRD) has received the highest amount of developmental budget allocation. Ministry of Public Health (MoPH) and Ministry of Irrigation and Livestock (MAIL) have also received higher amounts after MRRD. According to the QATYIA report for FY 1395 the mentioned ministries respectively, have spent 88%, 72% and 82% of their developmental budget.

Table 4: Comparing discretionary and non-discretionary budget for FY1396 and 1397

Source: National budget draft for 1397 and approved budget for 1396

No	Budget Unit	Allocated budget in AFN	%
1	MRRD	18,944,518,440	20.21
2	MoPH	9,979,005,480	10.65
3	MAIL	9,697,911,190	10.35
4	MoPW	9,370,496,000	10.00
5	Da Brishna Shirkat	7,255,000,000	7.74
6	MoUD	4,201,972,000	4.48
7	MoF	3,397,048,800	3.62
8	MoEW	3,071,682,000	3.28
9	Civil Aviation Authority	2,877,150,000	3.07
10	Kabul Municipality	1,989,900,000	2.12
Total budget for the 10 Budgetary units		70,784,683,910	75.51
Total developmental budget		93,739,128,474	

As it was mentioned, ordinary budget for FY 1397 is slightly less than the previous year. Ministry of Defense (MoD) and Ministry of Interior (Mol) have the

highest shares of the ordinary budget, respectively, 23.25% and 22.08%. Each of these ministries has a Tashkil over than 208,000 for 1397.

Table 5: Ten governmental entities with the highest amount of ordinary budget

Source: FY1397 national budget

No	Budget Unit	Allocated budget in AFN	%
1	MoD	62,122,387,000	23.25
2	Mol	58,977,268,000	22.08
3	MoEd	36,527,200,000	13.67
4	MoLSMD	23,339,796,000	8.74
5	NDS	16,037,000,000	6.00
6	MoHE	5,693,100,000	2.13
7	MoFA	5,290,000,000	1.98
8	IDLG	4,260,003,580	1.59
9	MoPH	3,720,000,000	1.39
10	Supreme Court	3,569,128,442	1.34
Total budget for the 10 Budgetary units		219,535,883,022	82
Total ordinary budget		267,152,429,000	

3. Fiscal Sustainability

As the following bar-chart presents, the government endeavors to raise amount of domestic revenue and decrease its dependence on aids. The increasing slope of domestic revenue indicates the government's progress in this regard.

It is worth mentioning that however 1397 budget shows a significant improvement in terms of domestic revenue but the financial gap will emerge after four years when the donor assistance will shrink drastically. Medium Term Fiscal Framework (MTFF) shows that 1397 budget is facing more financial limitations which should be addressed.

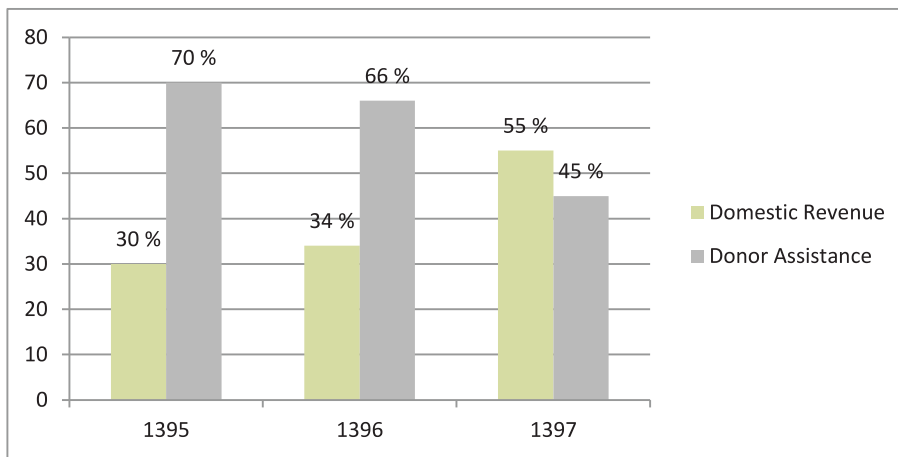


Figure 2: Fiscal sustainability and source of the budget finance

Source: National budgets for FY1395, 1396 and 1397

While there has been steady progress made to increase domestic revenue, projections remain well below the total amount of revenue required to meet future recurrent costs. The demands on national resources will continue to rise, and for the foreseeable future, the cost of maintaining security will be beyond the capacity of the tax system to meet. Estimated actual domestic revenue for 1396 is projected to be around AFN 153 billion or 10.8 percent of GDP. While Government outlays as a percentage of

GDP in 1396 are expected to be around 27.0 per cent.

This means there is a structural gap in Government revenue versus expenditure of 16.2 percent of GDP, which does not include security costs met with support from the Resolute Support Mission. Within this context, international assistance will remain a crucial factor in funding national development. The estimates in the budget assume an on-going commitment of 50 percent of

current levels from international donors beyond 1399 (2020).

Considering unforeseeable security situation in Afghanistan, the 1397 budget is very limited. Most of foreign countries are enforcing policies of refugee reversion and if the security situation

improves, Afghanistan will confront with reversion of returnees while still the government has not enough budget to host them. The following table demonstrated available funds and the budget gap in this regard.

Table 6: International Development Assistance for the Migration Program

Source: National budgets for FY1397

Lead Agency	Target Population	Budget Forecast (AFN)	Available Funds	Budget Gap (AFN)	Funding Source	Funding Type
MoRR	Returnees from Pakistan, Iran and Europe for 2017 and 2018	69,744,540	-	69,744,540	TBD	On-Budget
ACCRA (E-Tazkira Dept)	Returnees and IDPs	139,489,080	-	139,489,080	EU	Off-Budget
MoRR, ANDMA, Shelter Cluster	Vulnerable groups of returnees, IDPs and host communities in high altitude areas	1,088,014,824	585,854,136	502,160,688	UNHCR, other cluster members	Off-budget
Humanitarian Agencies	Returnees and IDPs for 2017 and 2018	5,579,563,200	-	5,579,563,200	WFP & BPRM/US	Off-Budget
MoE	Returnees, IDPs (2016-2017) and host communities	3,408,232,242	-	3,408,232,242		On-Budget
MoPH	Returnees, IDPs (2016-2017) and host communities	1,814,414,902	143,922,880	1,670,492,022	ARTF/WB	On-Budget
MRRD	Returnees and IDPs (2016-2018) and host communities	5,579,563,200	5,579,563,200	-	IDA, ARTF/WB Germany & Denmark	On-Budget

Lead Agency	Target Population	Budget Forecast (AFN)	Available Funds	Budget Gap (AFN)	Funding Source	Funding Type
IDLG	Returnees and IDPs (2016-2018) and host communities	3,487,227,000	3,487,227,000	-	IDA/WB	On-Budget
MUDH + UNHABITAT	Vulnerable groups of returnees, IDPs and families of martyred ANSF	4,184,672,400	1,743,613,500	2,441,058,900	India	Both
Consortium (UN-H and IOM)	Vulnerable groups of returnees, IDPs and families of martyred ANSF	627,700,860	-	627,700,860	EU	Off-Budget
ARAZI	Returnees, IDPs and host communities	209,233,620	139,489,080	69,744,540	GOIRA	On-Budget
MoF, MAIL, MoLSAMD	Returnees, IDPs (2016-2018) and host communities	139,489,080	-	139,489,080	WB	On-Budget
MoLSAMD, MoE	Returnees, IDPs (2016-2018) and host communities	697,445,400	-	697,445,400	WB	On-Budget
MoPW, MoEW, MAIL	Returnees, IDPs (2016-2018) and host communities	2,789,781,600	-	2,789,781,600	WB	On-Budget
UNESCO/National Sports Authority	Returnees, IDPs (2016-2018) and host communities	697,445,400	-	697,445,400		Off-Budget
CEO Office	N/A	34,872,270	-	34,872,270	TBD	Off-Budget
M&E Cell	N/A	104,616,810	104,616,810	-	UNDP	Off-Budget
Total		30,651,506,428	11,784,286,606	18,867,219,822		

3.1 Budget Execution

Regardless of the small fluctuations, overall the government has shown good progress in spending its ordinary budget. As it has been illustrated in the table below, its rate for 1396 has reach 87% (MoF execution report-10 Dec 2017).

According to QATIYA statement for 1395, the governmental entities could spend around 54.4% of its developmental budget. This amount becoming higher for 1396 reaching to 67% (MoF Final Execution Report-21 Dec 2017). FY1 395 QATYIA also has revealed that 23.4% (158 projects) of the developmental projects did not have any activities while a significant number of the projects had an expenditure of less than 50% during last seven years.

However, corruption and lack of capacity are among the main reasons for low budget expenditures, but it should be emphasized that a high percentage of the developmental budget has being financed through non-discretionary sources which limits the government's control over budget and project implementation. Furthermore, during last year, a high number of the ministers had been disqualified by the National Assembly which had negative impact on the ministries' functions.

The governmental offices' weak planning and their low capacity in estimation of their next year budget are the other challenge leading to low expenditure of the developmental budget.

Table 7: The figures have been prepared according to SAO's QATIYA reports (FY 1386-1895) and MoF's Execution rate report till 10 Dec 2017.

Fiscal Year	% of Ordinary Budget Expenditure	% of Developmental Budget Expenditure
1386	96.60%	55.00%
1387	92.35%	40.00%
1388	93.26%	37.00%
1389	95.61%	39.00%
1390	95.54%	49.50%
1391	86.55%	51.00%
1392	90.41%	57.00%
1393	80.99%	45.81%
1394	82.97%	54%
1395	90%	54%
1396 (till 21 Dec 2017)	94%	67%

3.2 Estimated Resources

3.2.1 Domestic Revenue

The government's revenue target for 1397 is AFN 349,410,669,761 (5.010 USD billion). Of that amount, 54 percent consists of grants, 34 percent of taxes, one percent social contributions and 12 percent other recipients. Domestic revenue is increasing, but grants, especially for the operating and discretionary development budgets are declining. The increase in domestic revenue falls short of the decrease in grants. This means that in 1397 there is around 10 billion AFN deficit that will be funded from 1396 treasury reserves of MoF.

The fiscal outlook for forward estimates to the year 1400 is equally constrained. Assuming modest increases in expenditure in 1398 and 1399 the medium-term expenditure framework shows small deficits in these years. These deficits would have to be met through higher tax receipts, cash balances or by reducing expenditure through savings. The Government intends to address these deficits through a policy of offsetting new expenditure from savings in current activities. This process will be targeted at removing poor performing or low priority programs from the budget over the next few years.

The final year of the forward estimates, 1400, shows the impact of the end of current commitments from international

partners. While no agreement for support beyond 1399 is in place, for the purposes of the forward estimates, the Government has assumed donor commitments of around 50 per cent of current levels. Expenditure is maintained for operating and discretionary development (reflecting no change in policy) with non-discretionary development expenditure lowered in line with the practice of matching grants to expected expenditure. This is not meant to pre-empt future discussions on assistance but to highlight Afghanistan's continuing reliance on international development assistance, with the forward estimate for 1400 showing a deficit of AFN 61 billion. During 1394 and 1395, revenue from domestic sources increased significantly. Revenue as a proportion of gross domestic product (GDP) rose from 8.6 per cent of GDP in 1393 to 10.1 per cent and from 10.1 to 10.6 per cent in 1394 and 1395.

Total revenue collection in 1395 was AFN 147 billion compared to AFN 122.4 billion in 1394 an increase of 20 per cent. For FY 1397, the total domestic revenue is expected an amount of AFN 169 billion which show a notable climb. This amount can finance 55% of the ordinary budget and a portion of the developmental budget. The increase in revenue collection was largely driven by new tax policy measures taken in 1394 (2015) including:

- Increasing the Business Receipt Taxes (BRT) from 2 per cent to 4

per cent yielding AFN 4.4 billion in additional revenue;

- Increasing fuel fees from AFN 1 per letter to AFN 2 per letter;
- Introducing a tax on mobile phone pre-paid top-ups of 10 per cent;
- Increasing the fees for overflight from USD 400 (AFN27,000) to USD 500 (AFN34,000) for additional revenue of AFN2 billion in 1394 (2015);
- Increases in tariff rates for selected imports such as beverages, gas, tea, soup, cigarettes, carpets, steel, IT equipment, furniture, vehicles;
- The government's capacity in terms of revenue collection has been increased;
- Amendments in Income tax law to increase investment in Afghanistan;
- Awareness raising to promulgate tax paying culture;

These measures were partially implemented from mid-1394 (2015) with full year impacts on revenue shown in 1395 (2016).

According to Supreme Audit Office's Qatiya statement for FY 1395, the government, in spite of notable achievements, is still facing challenges in terms of revenue collection and preparing proper plan for it. Tax payment is a new concept in Afghanistan and individuals usually do not consider it as a compulsory duty. Having support of the political influential figures, a significant

number of tax payer especially large Tax Payer (LTP) evade tax. Additionally, tax law still needs more amendments and enforcement so that everyone follows it without any exception.

The government's domestic revenue mainly consists of tax-based revenue while there are many other non-tax revenue sources which the government needs to extract and develop them. Due to insecurity and lack of infrastructure, mining resources is being controlled by the anti-governmental group and they are extracting them in an unprofessional way, damaging the resources and wasting the domestic revenue. On the other hand, while 10% phone top-up fee could be a good source of revenue, extensive corruption and lack of transparency in its process has resulted to wasting resources. Simultaneously, it has created a huge gap between people and the government.

3.2.2 Donor Assistance

International Development Assistance accounts for around 54 per cent of the National Budget in 1397. Off-budget support is also significant especially for security, making Afghanistan one of the most aid dependent countries in the world. Much progress has been made in building the domestic revenue base, with revenue increases of around 10 per cent a year over the forward estimates. This will only reduce, not eliminate, Afghanistan's short to medium-term reliance on foreign assistance. Donor commitments from the Warsaw and

Brussels conferences end in 1398-99 (2019-20). Significant reductions in international assistance pose a substantial fiscal risk to the budget.

The composition of grant financing to the national budget has also changed from fixed contributions to more variable. Over the last decade, the Afghanistan Reconstruction Trust Fund (ARTF) has given significant stability to the national budget, in particular to the recurrent or operating budget. This has been partly achieved by maintaining a recurrent cost window within the trust fund. In recent years, that arrangement has been gradually replaced by the introduction of an Incentive Program (IP) based on achievement of outputs. While output-based arrangements have many advantages, they are by their very nature variable. If the Government does not meet certain benchmarks, disbursement from the IP program will be lower.

The risks to the budget from the Incentive Program were highlighted in 1393-94 (2014-15) when uncertainty around the Presidential election led to a fiscal crisis brought about by lower domestic revenue forcing the Government to cut planned operations and maintenance spending. As a result, the Government missed a benchmark under the program and grant revenue from the IP program declined at the precise moment domestic revenue was also falling.

Since 1394 (2015) additional variable grant funding has been introduced in the form of the United States funded National Development Program and the European Union State Building Contract. Both programs provide direct budget support and help to strengthen national systems for public financial management, making them in the view of the Government, welcome additions to international development assistance. However, both are based on agreed performance benchmarks and have variable components that present unquantifiable risks to the budget as they are unpredictable. Additionally, restrictions on the use of this grant funding for the operating budget mean less flexibility for the Government than was the case under the recurrent cost window of the ARTF, while facing operational pressures as the Government assumes more responsibility for areas such as security, and growing demands for investment through the discretionary development budget.

3.3 The Balance of Payments

In 1396 (2017), the volume of exports has slightly increased compared to previous years. The expansion is partly due to the recent opening-up of the air corridor with the India, which has increased the export prospects of Afghanistan. The Government expects this improvement to continue for the next few years. Exports are also likely to increase as output from extractive

industries increases, although this will take some time.

The trade balance for goods shows a deficit due to the prevailing high import to export ratio. However, the balance of services shows a surplus, partly because of remittances from family members outside of Afghanistan. Overall, the outlook for the current account balance is not optimistic due to the anticipated reduction in international assistance over the long-term. This is a key macroeconomic risk as it will further depreciate the Afghani against the US dollar increasing domestic prices and reducing the demand for imports, which in turn will put more pressure on the currency. The only other source of financing for the current account once aid falls is foreign direct investment. This might happen in the extractives sector, but it will require a much-improved security situation, a stable macroeconomic outlook and a regulatory environment that provides stability for investors.

3.4 Fiscal Strategy

A credible and coherent fiscal strategy is a pre-condition for the success of the Government's self-reliance vision. The Government is adopting a more structured approach to fiscal planning with the long-term goal of ensuring sustainable finances to support economic growth and development. The Government's fiscal strategy set out in the Afghanistan National Peace and

Development Framework (ANPDF) includes three policy assumptions:

1. The Government will use fiscal policy as the primary tool for economic management;
2. The Government will, over time, collect enough revenue to meet operational and more of Afghanistan's development needs, gradually reducing international development assistance over the next fifteen years; and
3. The Government will balance the budget over the medium to long-term, without borrowing unsustainably. Any borrowing will be concessional and in accordance with agreements with the International Monetary Fund (IMF).

The foundation of the Government's fiscal strategy is the pursuit of self-reliance. This means in fiscal terms achieving economic and social objectives through sustainable means: not spending too much, not accepting too much aid, and making the best use of available resources. To do this, the Government will continue its ongoing fiscal reform agenda that will enable a much greater focus on increasing fiscal space in all five dimensions:

1. Being more efficient with way government does business – including by preventing, detecting and combating corruption;
2. Raising more domestic revenue to higher levels;
3. Seeking concessional debt and innovative financing for high impact lower risk investments;
4. Using aid more responsibly and effectively; and
5. Looking into the future to prioritize policies and improve fiscal performance over time.

3.4.1 Economic and Fiscal Goals

The Government has set goals in the short to medium-term, to guide the budget in identifying necessary investments.

The following three aspirational goals guide the preparation of the budget:

1. Achieve average growth of 5 per cent per year until 2020;
2. Increase development budget expenditures by 10-15 per cent each year as we expand delivery of education and health services in the medium-term; and

Grow domestic revenue by up to 12 per cent annually, with the overarching goal

of having domestic revenues account for 14 per cent of the GDP by 2020.

3.5 Fiscal Operations in the Provinces

The equitable and effective distribution of resources across the country based on the needs of the people and the greatest benefit to the country is a central tenant of the Government's self-reliance agenda. The road to peace and stability needs to be paved by a clear commitment to providing all Afghans with basic services and national infrastructure.

To increase accountability and transparency the Government is publishing detailed formation about budget allocations to provinces. This statement is presented in two parts:

1. Expenditure by Province – this section presents Government expenditure by province for the budget year, 1397 and three forward estimate years.
2. Citizen's Charter – this section presents progress on Citizen's Charter including allocations by village, for the budget and three forward estimate years.

As with other parts of the 1397 budget, these are reforms that offer a greater level of transparency on how national resources are allocated and will help drive government policy over time to achieve improved outcomes for all communities.

Another way to look at spending is to examine provincial spending in the top five 'richest' provinces and the top five 'poorest' provinces. For this analysis, the top five 'richest' provinces are defined as the five provinces with the highest per capita monthly consumption. They are Kabul, Balkh, Parwan, Farah and Logar. They are a mix of provinces with large and small populations and account for 24 per cent of Government expenditure in the provinces and 14 per cent of the national budget.

The five 'poorest' provinces are defined as the provinces with the highest poverty rates. These are Takhar, Laghman, Zabul,

Badakhshan and Sar-e Pol. They are mix of small and medium-sized provinces by population and account for ten per cent of provincial expenditure and six per cent of the national budget. This analysis would indicate there is a need to shift some spending to increase the resources of those provinces with more poverty relative to other provinces.

In per capita terms, the top five provinces for Government spending are Nimruz, Kandahar, Helmand and Nuristan. Paktia has had the highest level of per capita Government spending of any province for most of the last eight years with the Government spending AFN 20,973 (\$313) for every person in this province in 1396.

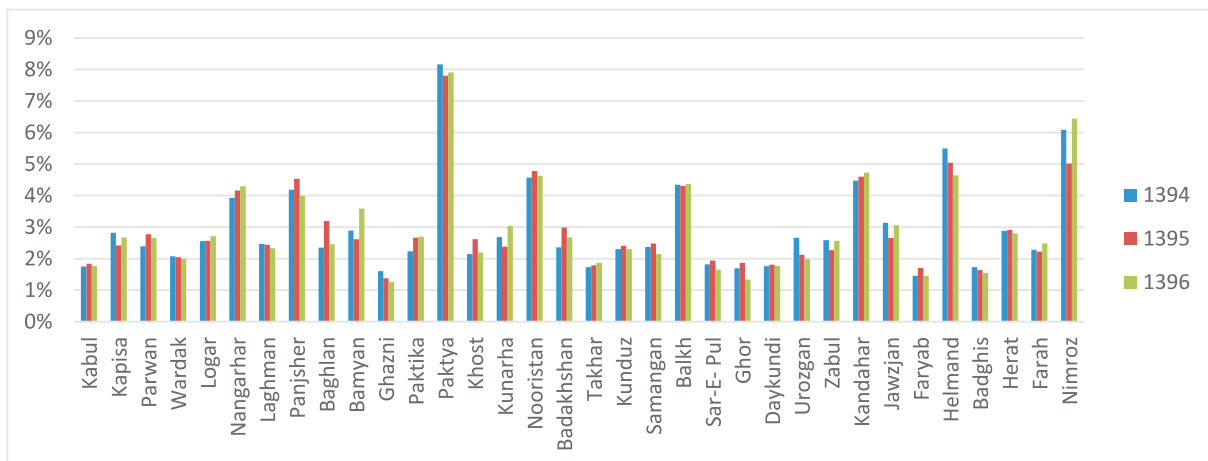


Figure 3: The government's per capita expenditure by provincial breakdown

Source: FY1397ational budget draft

The bottom five provinces in terms of per capita Government spending are Ghazni, Ghor, Faryab, Badghis and Sar-e Pol. The lowest level of per capita spending is in

Ghazni where the Government spent AFN3,336 (\$50) for every person in 1396.

The top level of per capita Government spending for any province (in Paktia) is a

little over six times the level of per capita Government spending in Ghazni, the province with the lowest level. This demonstrates a level of inequality that the Government will need to address in future budgets.

The top five and bottom five provinces in per capita Government spending by province have been quite stable in terms of their relative level compared to all other provinces over the last eight years. The rest, a majority, have seen a relatively high level of volatility in Government spending in their provinces. Some have seen one-off increases in a year associated with major projects, while the on-going security situation has meant that some provinces have moved back and forth between secure and insecure.

This volatility reflects the relatively centralized nature of Government in Afghanistan over the period. There are no independent sub-national administrations and there has been no development of inter-governmental transfers to provinces aimed at fiscal equalization that are common in most countries.

The current budget process does not systematically analyze allocations of expenditure by region. Operating budgets are largely driven by the structure, location and size of administrative units within Government Ministries and agencies. Development budgets are formulated by program and

project, and while the geographical location of investment is part of the assessment process, the Government is moving from 1397 to formulate a much more systematic approach. New policy proposals coming forward to the budget process for consideration will need to provide detailed analysis and costings for each proposal by province.

The Government's policy will aim to ensure that national resources are being applied fairly across the country and to the benefit of all Afghans. In addition, in line with the analysis of past spending by province in the previous section, there is a need to shift some spending from relatively better off areas of the country to those in most need. While the on-going security environment tends to skew resources to areas of high conflict, the Government will not let that be at the cost of lower or no services and investment in other regions.

These estimates are based on projections that assume current allocations by province will continue over the next four years. Given the volatility in actual expenditure by province over the last eight years, these projections will need to be revised to reflect actual program/project level data and will be updated for the mid-year Supplementary Budget and for the 1398 National Budget.

4. Public Finance Management and Reform

4.1 Gender Responsive Budgeting (GRB)

Gender budgeting is mainstreaming gender perspectives in all budget process to ensure an equal distribution of revenue and expenditure. Men and women have different needs and requirement and it should be considered in the policies and make sure both genders benefit equally. Women are very vulnerable. During war and conflict, it is girls who first will stop going to school.

GRB doesn't mean to spend more or special money for women, but it rather means to distribute the available resources fairly and equally in terms of gender. It is also not about whether an equal amount is spent on women and men, but whether the spending is adequate to women's and men's needs. Gender responsive budgeting eventually results in gender responsive budgets, but does not in a separate budget for women.

Gender Budget Unit in MoF was established in 2005 by support of GIZ. In the same year, MoF elaborated and endorsed a Strategic Plan on GRB for the period 1394 to 1397. In 1389, for the first time GRB was mentioned in the national budget and for the FY 1396, MoF added a

gender analysis of the budget in the national budget draft.

GRB has been included as a main reform in the Public Financial Management Roadmap II (PFMR II). Furthermore, the ministries are responsible for considering GRB in Call circular 1 & 2 (BC1 & BC2). In this regard, besides including sex disaggregated data for beneficiaries of each project in BCs, the ministries are responsible to fill a GRB guideline as an annex to BCs and ensure the budget is gender responsive.² It includes the following sections:

- Gender-sensitive situation analysis
- The definition of gender-sensitive objectives
- The definition of gender-sensitive outcomes and outputs
- The definition of activities
- Gender-sensitive performance indicators
- Calculating the costs for gender-equality results

² Schneider, K, Gender assessment of the Public Finance and Expenditure Management Law, Berlin, 2017

A GRB reform and pilot has been implemented by MoWA and MoF, jointly, with particular focus on GRB capacity building. Currently, it targeted Ministry of Education; Public Health; Higher Education; Agriculture, Irrigation, and Livestock; Rural Rehabilitation and Development, Labor, Social affairs, Martyrs, and the Disabled.

In order to initiate mechanisms for enhancing political will and commitments toward GRB, Steering Committee (SC) and Technical Working Group (TWG) were established. The Technical Working Group (TWC) aims to ensure the implementation of GRB at the level of planning and budget departments. While, the goal of the Steering Committee (SC) is oversight of the implementation and institutionalization of GRB in the six pilot ministries and the rolling-out to other ministries at a later stage in other ministries. Moreover, Directorate General of Budget with support of UN Women designed a database of gender information collection and it will be used to provide sex-disaggregated data and conduct the gender marking of past, present and future on budget programs of line ministries.

However, some accomplishments in terms of GRB have been achieved but still there is long way to go in terms of a meaningful and effective GRB in Afghanistan. The efforts are being conducted particularly in the central level with focus on the mentioned six

pilot ministries while there is need to expand the reforms in the other budget units as well. Challenges such as lack of accurate sex-disaggregated data, political will, commitments and capacity especially, in the subnational levels are still the main barriers in GRB institutionalizing.

4.2 Budget Execution Guideline

MoF has brought changes in the budget execution guideline which some of the amendments can enhance accountability and facilitate a good coordination between the budget units and MoF. Overall, 27 articles have been omitted from the guideline and some others have been amended.

In article 16 of FY 1397 budget execution guideline, it has been stated that the projects with no activity within two years, will be removed from the national budget.

High number of the stagnant projects carried forward to the next fiscal year, increases bulk of the national budget documents and demonstrates an unrealistic amount of budget. This amendment can solve this problem and at the same time, put pressure on the implementers to spend their budget.

Article 26 in both FY 1396 and 1397 is the law on the National Technical Assistance (NTA) salaries. In 1396, according to the guideline, the NTA salary cannot exceed

than AFN 250,000 while for the 1397, no limitation has been mentioned in this regard. Instead, it is instructed that the NTA salaries should be determined according to the negotiations with the World Bank.

Lastly, Article 23 for FY1397, has been change to elaborate the terms and condition for the operation and maintenance projects.

5. Recommendations

In consideration of the findings of this annual budget review, EPD issues the following recommendations:

- In spite of monumental efforts, the Afghan government is still lagging behind in terms of GRB. The capacity in this regard should be built and commitments should be followed seriously;
- The goals and objectives mentioned in the National Budget should be redefined as they are unrealistic and too broad hence, hard to achieve.
- Afghanistan is a country with a high potential of resources. As the government is facing a big fiscal deficit gap and decline in donor assistance, measures should be taken to extract the resources.
- Transparency and accountability in revenue collection should be enhanced
- The government should mitigate the risk regarding the loans with interests. Accumulated interests due to lack of on time implementation of the projects will increase financial pressure on future generation;
- Ghost Tashkil still is a big concern in most of the ministries wasting national resources and creating unrealistic data which should be addressed;
- CSOs could be fully involved in all National Budget process that includes: Budget planning or formulation, approval, execution and monitoring or reporting. However, the CSOs participation would be useful for replicating of public real needs in National Budget process and will have positive impact for better implementation of development projects CSOs should be supported to monitor and evaluate the projects' implementation;
- CSOs recommendations should be considered in national budget draft;
- It should be noted that the donor assistance during past few years, had a declining slope. As there is no commitment for aid provision after 2020, the government should find other sources as alternative;
- Policies and mechanisms should be considered for more investment in Afghanistan;



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