SUSTAINABLE SOCIAL PROTECTION FINANCING: QUESTIONS AND (SOME) ANSWERS

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KEY QUESTIONS
Key question 1: What’s different about social protection?

• Social protection systems have numerous and diverse funding sources
• Social protection is intended to alleviate poverty and inequality
• Social assistance can absorb a high proportion of revenues (>1% of GDP)
• Social assistance is recurrent spending – programmes tend to last a long time
• Benefits need to retain their purchasing power, so must keep pace with inflation
• Highly counter-cyclical: demand spikes during economic shocks
• Demand changes over time as economies develop, demographics evolve etc
• Complex political economy – who gets what, when?
• Social insurance programmes can represent a large long-term liability on public finances
• Social protection benefits affect individual incentives
• Social protection systems often possess accurate and up-to-date information about beneficiaries
Key question 2: What does this mean for financing?

- Financing needs to be regular, significant and sustainable
- Sources of financing should not worsen poverty or inequality
- Domestic revenue mobilisation is critical to expanding social protection but external support might have key role to play, especially in low-income settings
- Social protection programmes face tough competition from other areas of spending
- Can be difficult to locate and quantify all social protection spending
- Financing should reflect the capacity to contribute of different individuals and other economic actors
- Social insurance benefits should correspond to contributions both at an individual level and in aggregate (in broad terms)
- Shock-responsiveness should be hard-wired into social protection systems
- Potential for tax systems to “talk to” the social protection systems
Key question 3: How much revenues do developing countries raise?

Tax-to-GDP ratios: 2018 averages

Africa (30): 16.5%
Latin America and the Caribbean: 23.1%
OECD: 33.9%
Key question 4: How do developing countries raise their revenues?
ILO data show that low-income countries would need to invest an additional USD 77.9 billion or 15.9% of GDP per annum to guarantee at least a basic level of social security for all through a nationally-defined social protection floor.

Notes: The graph shows the financing gap for achieving a universal package comprising social protection benefits for children, maternity, disability, and old-age and access to essential health care in 2020 as a percentage of GDP (low- and middle-income countries only).

SOME ALIGNMENTS
Aligning objectives in revenues and spending
Part 1: Progressiveness

We know that (usually)
- Social protection is likely to reduce poverty and inequality
- Ditto in-kind benefits: health, education, basic services
- Subsidies can have mixed impact

But when we consider how these benefits are financed...
- Taxes can be regressive or progressive (different people pay different taxes in different amounts)
- Any tax payment reduces consumption
- Direct taxes are a much lower proportion of revenues in developing countries

Fiscal incidence analysis shows both sides of the coin and to assess which groups are getting more or less out of the system.
Fiscal incidence analysis – a key innovation

• Fiscal incidence analysis (FIA) calculates how much individuals / households receive from the government and how much they pay to the government

• Distributional effects show overall impact of taxes and transfers on poverty and inequality

• This is an accounting exercise rather than dynamic model: it cannot be used to predict the impact of a change in tax and transfer policy

• However, it can highlight major distributional issues in taxes and transfers alike that require a policy response
Limitations of FIA

- Some taxes are difficult to attribute to individuals, in particular corporate income tax (which is an important source of revenues in developing countries).

- Social protection transfers are often poorly captured in household surveys, especially smaller programmes.

- Contributory pensions (contributions and payments) are hard to capture in this exercise

- FIA only as good as the survey and administrative data on which it is based

- Results tend only to capture distribution between income groups rather than inter-generational or inter-regional transfers – or to vulnerable individuals
Commitment to Equity and net social protection – givers & takers

- Commitment to Equity has developed a methodology for FIA that is has implemented in almost 60 countries, with another 18 ongoing.

- Here we see net payers and beneficiaries in cash terms.

In low-income countries, lowest decile is a net payer.

Source: Fiscal policy, income redistribution and poverty reduction in low and middle-income countries (Lustig, 2017)
Aligning objectives in revenues and spending
Part 2: Reliability

Source: Revenue Statistics in Africa 2020
Aligning objectives in revenues and spending
Part 3: Stability

Coefficient of variation

Source: Revenue Statistics in Africa 2018
Aligning objectives in revenues and spending
Part 4: Shock responsiveness

• Countries worldwide scaled up social protection provision in response to the COVID-19 pandemic

• For developing countries, social assistance accounted for the majority of the response

• The scale of the revenue impact severely constrained what governments could do

LAC CUMULATIVE COLLECTION VARIATIONS BY TAX

Source: CIAT 2021

- ISC = EXCISES
- ISR = INCOME TAXES
- IVA = VAT
- OTROS = OTHER
THE SEARCH FOR FISCAL SPACE
Fiscal space – Look within

• Best source of fiscal space is domestic resource mobilisation but revenues will take time to recover in developing countries

• Higher debt levels post-pandemic will further constrain fiscal space

• Political economy of social protection post-pandemic a great unknown – social protection has proven its worth but demand will evolve post-pandemic

• Increasing financing for social protection best achieved within existing envelopes while competing for other budgetary funds two-stage task: find what you spend, spend it optimally

• Explore innovative social insurance solutions
Concluding thoughts

• Social protection planners need to know where every cent is being spent – invest it where it gets best results
• Make a long-term plan for the programme(s) you want to scale up, including a financing strategy
• Align and strengthen registries and delivery mechanisms for tax and spending
• Enlist civil society voices for tax reform and higher social protection spending...
• ...but remember nothing will be affordable and everything will be a priority post-COVID-19 (for Ministers of Finance)
• Make sure social protection experts are in the room when taxes are discussed...
• ...and make sure tax experts are in the room when social protection financing is discussed
• International cooperation on a number of areas – esp debt & taxation – needed to ensure sufficient financing for social protection