SUMMER 2010

DOMESTIC RESOURCE MOBILIZATION IN AFRICA

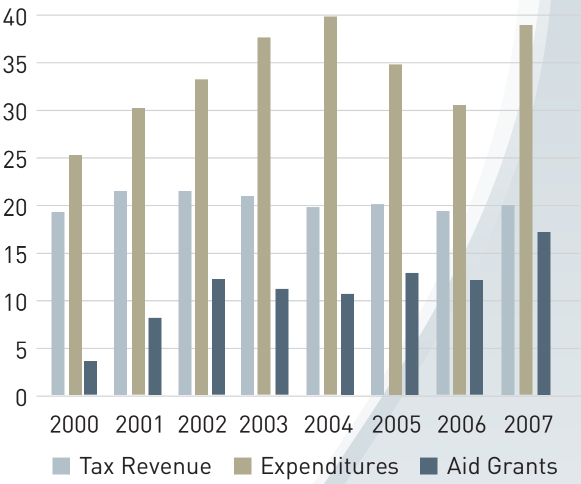
BURUNDI

The project: The North-South Institute has been working with African, UK and Canadian partners on case studies exploring the potential for domestic resource mobilization (DRM) in five Sub-Saharan countries: Burundi, Cameroon, Ethiopia, Tanzania and Uganda. DRM refers to savings and investments that are generated by both the public sector (primarily through taxation) and the private sector (as a channel for private savings by households and domestic firms). Interest in DRM as a means to support sustainable growth and reduce dependence on external aid has been growing: in 2002, the Monterrey Consensus made improved DRM the first of its leading recommended actions; and, the current global economic crisis has only drawn more attention to DRM's potential, due to declining flows in external assistance and global remittances. This summary sets out our key project findings for Burundi.

Context: One of the world's poorest countries, Burundi is struggling to rebuild after a decades-long civil war that has only recently ended. The economy contracted severely during the strife due, in part, to an embargo (1996-99) that cut off external aid, plunging per capita GDP in half. By 2008, it rose to US$338 (PPP), still far below the Sub-Saharan average of US$2,056 (PPP). A largely subsistence-based agricultural sector accounts for 45% of the country's GDP, but Burundi's slow growth and demographic pressures are increasing its dependence on food imports. Burundi is one of the most aid-dependent countries in the world. External funding provides over 50% of the budget.

Revenue, Expenditures and Aid Grants

(% GDP)



Source: Ministry of Finance, Burundi

Rank in Doing Business Database 2010:	176/183
Tax revenues (% GDP):	19.9*
Savings rate (% GDP):	-20.0*
Sub-Saharan average:	16.6 (2000-08)

*latest available figures

Sources: World Bank, Doing Business Database, 2010 and World Development Indicators Database; International Monetary Fund, International Financial Statistics

Key constraints to DRM: In the 1990–2007 period, the **savings rate** was negative, running at about -3.5% of GDP on average. Burundi lost an estimated US$2.6 billion due to capital flight between 1970 and 2004. With an end to conflict, the financial sector is improving, but remains poorly developed. There are only eight commercial banks; none are in rural areas. Only 2% of the population has a bank account. Assets of pension funds and insurance companies are growing, as is micro-finance, but so far these do not mobilize substantial resources.

Years of conflict, high tax rates, and a complex set of investment incentives and tax exemptions have contributed to widespread fraud, as well as corruption. In fact, the revenue authority has recently been cited by Transparency International as the most corrupt institution in East Africa. In 2006 tax exemptions totaled over 10% of GDP or around 65% of tax revenue. Incomes are too low to be taxed and subsistence agriculture dominates. Nonetheless, **tax revenues** are about 19% of GDP, not far off the African average (explained by the very small size of the economy). Most revenues come from indirect taxes on trade and retail sales. The tax base is very narrow, with 10% of taxpayers providing 70% of revenues. Although efforts to reform the tax system are under way, serious concerns remain about governance and political interference.

The way forward: To increase tax revenues, Burundi needs to take **aggressive action against corruption** in the tax authority. Measures are needed to remove discretionary powers and penalize proven cases of abuse. Donors can help support the independence of the new tax authority by working with local stakeholders to ensure reforms are implemented. Effort must be made to make certain the right people are hired and revenue targets are met (possibly by linking performance to future aid disbursements). Lessons can be learned from successful donor interventions in building tax capacity in neighbouring Rwanda, where revenues doubled over a decade, though from a lower base. Burundi would also benefit from **a single, simpler tax code and a taxpayers' charter** that would help build trust.

The greatest potential for increasing private savings mobilization lies in the **gradual expansion of the pension system** to cover more workers. Donors can play a role in supporting private DRM by helping set up a credit reference bureau and land and business registration systems.

Using new technologies such as the mobile phone to reduce savings collection costs, especially in rural areas, and expanding microfinance institutions could increase coverage and would build on the experiences of other countries like Kenya. Ultimately steps, including regulatory initiatives, are needed to promote linkages between the financial system and microfinance as well as informal networks.

This is a summary of ***Domestic Resource Mobilization in Sub-Saharan Africa: The Case of Burundi*** *by Astere Girukwigomba, an independent consultant based in Burundi. To read the full case study, go to www.nsi-ins.ca and follow the research project links.*

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