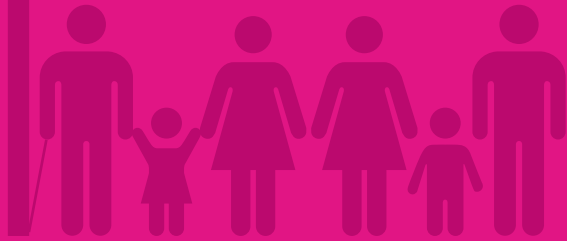


# Why does public social expenditure matter?



01





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Public social expenditure underpins the well-being and economic potential of individuals and entire societies. As repeatedly demonstrated during the COVID-19 pandemic, it protects poor and vulnerable populations, and stabilizes small businesses and economies. It fuels progress on education, poverty and inequality that is directly linked to realizing the global Sustainable Development Goals (SDGs).

Over the last 60 years, the Arab States have used social welfare provisions to make strides towards improving human well-being. Starting from relatively weak social indicators on the eve of their independence, most leapfrogged forward on access to education and health. In the last two decades, the region has closed some gaps between the rich and poor<sup>1</sup> and reduced gender disparities in health and education.

At the same time, shortfalls in public social expenditure remain, sustaining poverty<sup>2</sup> and constraining more dynamic, inclusive economic growth. The Arab States not only spend less on social expenditure than the global average but also spend less efficiently. This wastes billions of dollars in some cases, adding up to a significant share of gross domestic product (GDP). In the wake of the devastating COVID-19 pandemic, and against weakening social contracts, global food and energy crises, and unsure growth prospects, adequate, efficient and equitable public social spending is more important than ever before. Recovery and resilience to future shocks will largely depend on it.

ESCWA, in partnership with Jordan and Tunisia, developed the Social Expenditure Monitor (SEM) to inform current budget choices and “smart spending” for the SDGs. UNDP and UNICEF have joined the initiative given that social policy and related fiscal aspects are placed at the heart of their daily work in the region. This report on “Social Expenditure Monitor for Arab States”, produced in collaboration between ESCWA, UNDP and UNICEF, offers a pioneering assessment of public social policy spending in the region, asking where it is and where it needs to be. Going beyond the traditionally limited arena of social services and aligned with the broader vision of the SDGs, the report maps Government-wide expenditures, providing insights on budget choices that can galvanize progress on the goals. It looks at increasing public expenditure efficiency and rebalancing priorities to improve social protection and equitably deepen human capital, productivity and growth. Through detailed data and macroeconomic modelling, the report aims to help optimize links between public expenditure choices and macroeconomic objectives and provide a basis for better statistics. All such elements can strengthen capacities and advocacy for much-needed fiscal policy reforms.

## A. Lagging on development and now constrained on expenditure

Political economy factors have long explained strong social welfare provision in the Arab region. Generous social spending was part of State building and early nationalist discourse catering to a highly mobilized citizenry. Education and health services also became prime vehicles for job creation that reduced income inequality. But after the global economic downturn in 2008 and the slow recovery that followed, the cracks in the social contract accelerated amid rising demands for employment and better-quality public services.<sup>3</sup>

Today, the region faces significant development challenges exacerbated by the pandemic and the spillover effects of the war in Ukraine on food and energy prices. Poverty has increased; income and wealth inequality have risen. Economies remain poorly diversified, with large shares of informal activity. Fiscal space is inadequate to finance social and development expenditures and to meet the demands of the pandemic response. With uneven rates of SDG achievement,<sup>4</sup> the region will not reach many targets under the global goals by 2030. It lags many other regions on core issues such as income poverty, gender equality, health-care coverage, social protection, peace and security, the sustainable management of natural resources, and climate change. Underperformance is worse among groups of people struggling with multiple layers of social, economic and political marginalization, such as women, persons with disabilities, migrants, refugees, and displaced persons, among others.<sup>5</sup>

In reaching education targets, for example, many countries, including middle-income ones, confront persistent challenges from poor-quality, outdated teaching and learning methods, and inequitable access to quality public services and infrastructure. Almost all Arab countries with available international test scores fall on the lower end of global distribution. With States increasingly

unable to provide public-sector jobs,<sup>6</sup> students with educational credentials but without skills demanded by the market have little hope of finding employment in the formal private sector. Public expenditure therefore needs to be geared towards improving both educational access and quality, and to equitably reaching all social and economic groups. Evidence suggests that in most countries, including in Arab states, increased education spending, as a share of Government expenditure, raises the primary school enrolment rate (figure 1).

In health, shortfalls in service reach and quality are worse in rural areas, with noticeable disparities in rates of child stunting and infant mortality. The pandemic has further accentuated such gaps, coming at a time when many public health-care systems are fragmented and pay insufficient attention to primary care. One third of Arab countries have fewer than 10 health-care providers per 10,000 people, while the richest third have at least 50 providers per 10,000 people and in some cases more than 70. The regional physicians -to-population ratio, on average, stands at 2.9 per 1,000 people, below the world ratio of 3.4 per 1,000.<sup>7</sup> Inadequate public spending is reflected in the region's low number of hospital beds per capita as well as in high out-of-pocket expenditure on health care (figure 2). The latter averages 37 per cent of total health-care costs and can soar to 80 per cent or more in poorer Arab countries.<sup>8</sup>

### Social expenditure is important for

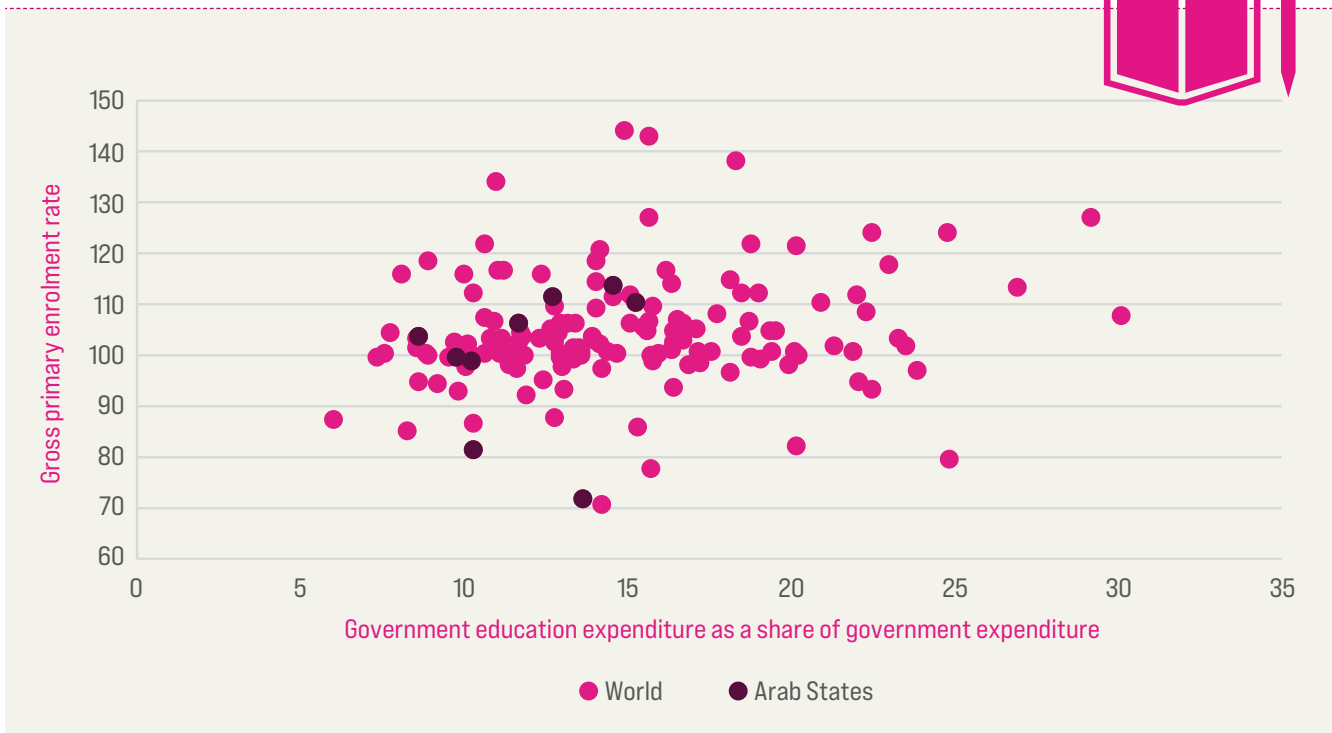


inclusive recovery from  
COVID-19



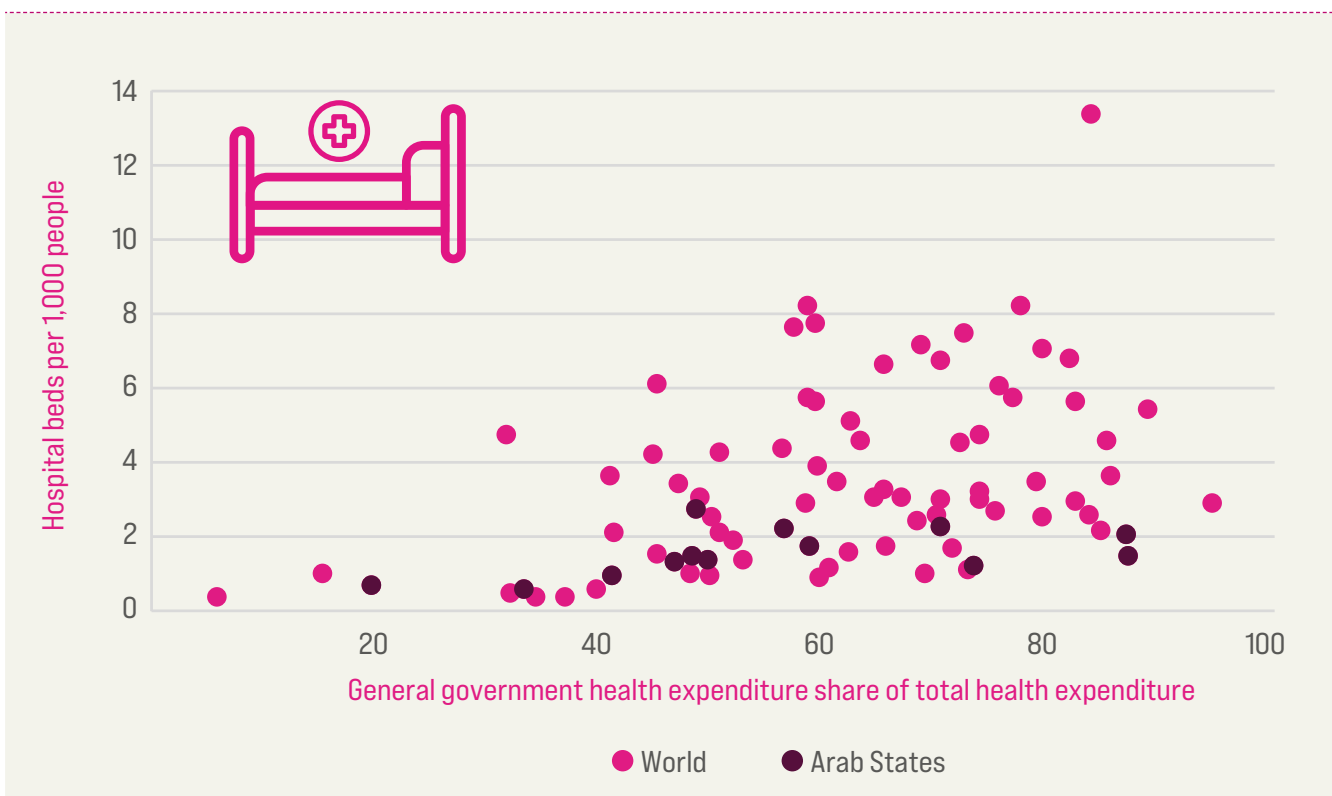
mitigating the effects of  
war in Ukraine

**Figure 1.** Higher spending on education tends to boost school enrolment rates, average 2017-2019



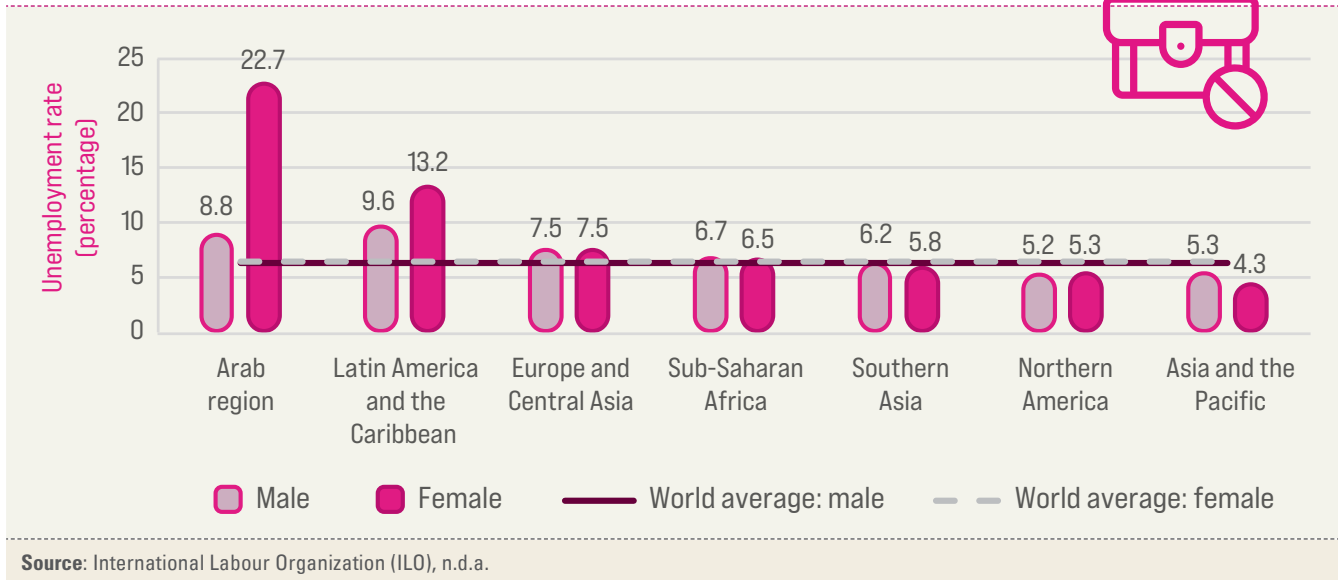
Source: Authors' calculations based on data from World Bank, n.d.c.

**Figure 2.** Fewer hospital beds per capita reflects inadequate public health expenditure, average 2017-2019



Source: Authors' calculations based on data from World Bank, n.d.c.

**Figure 3.** The region's high female and male unemployment rates reflect factors including underinvestment in active labour market policies, 2021



The region's unemployment rate continued to be the highest in the world at 11.8 per cent in 2021,<sup>9</sup> putting the Arab States far off course on SDG targets. Unemployment is particularly acute in the many countries affected by conflict and/or fragility<sup>10</sup> or that are least developed States. Across countries, women not only have lower labour force participation rates than men but are more at risk of being unemployed. The female unemployment rate reached 22.7 per cent in 2021, the highest rate in the world and far above the global average of 6.4 per cent (figure 3). A large share of employment in Arab economies is informal. The lack of structural transformation and relatively low productivity in most countries is also a major challenge. Most Governments have prioritized improving productivity and generating new jobs, yet this requires deliberate policy shifts in public social spending, such as to accelerate active labour market policies that provide incentives to start-ups and small businesses, upgrading skills and expertise, and creating provisions to increase female employment.

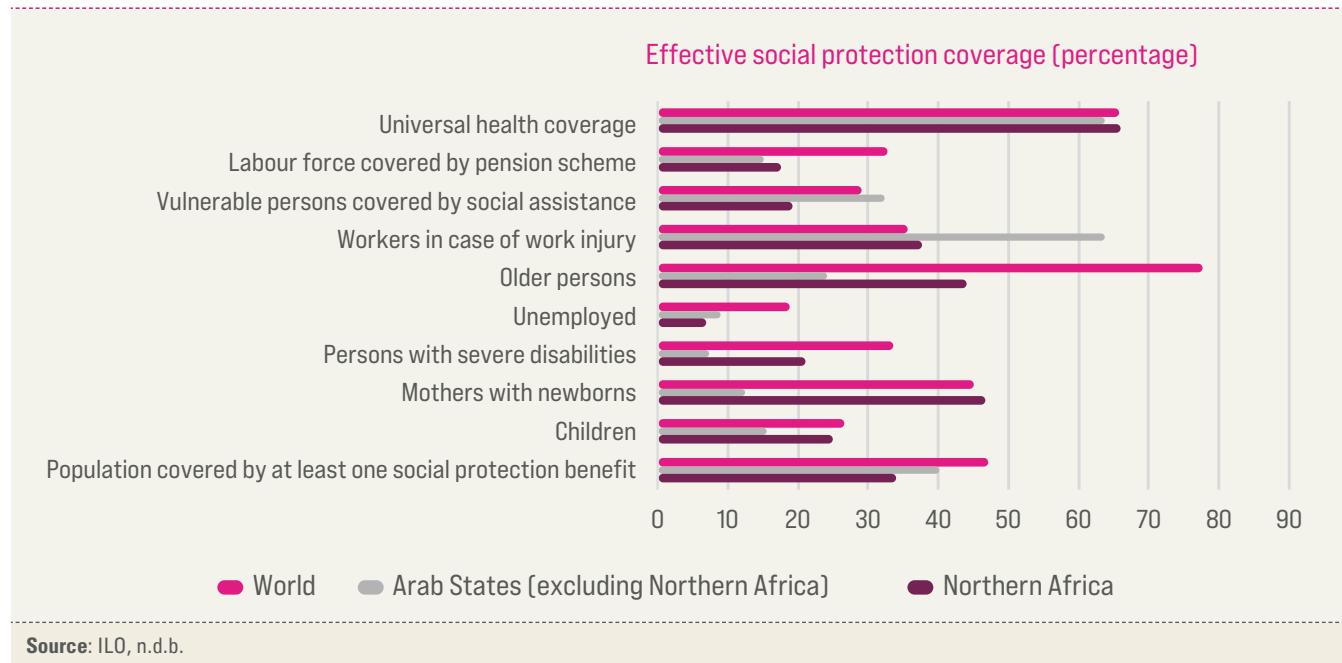
Social protection is critical to achieving the SDGs but significant coverage gaps result from segmented and exclusionary social insurance schemes and underinvestment in

non-contributory social protection. The latter remains fragmented and narrowly targeted. Just 40 per cent of people in the region is covered by at least one social protection cash benefit (figure 4). Coverage gaps are particularly large for women, youth and non-national workers, including refugees, given low labour force participation and high levels of unemployment and informal employment. Extending social protection to vulnerable populations is essential given substantial social needs and informal employment. It should be among the first steps towards the longer-term goal of universal access.



**Most Governments have prioritized improving productivity and generating new jobs, yet this requires deliberate policy shifts in public social spending.**

**Figure 4.** Many groups in the Arab region lack effective social protection coverage compared to the rest of the world, 2020 or latest available year



## B. Moving beyond the trade-off mentality

One question for policymakers in recent years—and now highly relevant in mapping a post-pandemic future—has centred on the perception of a trade-off. Social expenditures have conventionally been seen as having value in reducing poverty and inequality but not necessarily in enhancing economic growth. This report argues that the notion of a trade-off between a fairer society and a more efficient economy should be put aside. Fiscal policy aimed at reducing poverty and inequality improves human well-being. It spurs economic growth. And it advances social justice. It is therefore a powerful tool to unleash progress on three fronts at once, ensuring they reinforce each other and accelerate the pace of inclusive and sustainable development.

Early studies of the impacts of aggregate public social expenditures on growth and human development yielded mixed results.<sup>11</sup> Other

research examined only specific sectors such as health and education.<sup>12</sup> More recent studies have convincingly affirmed, however, that targeted public social expenditure does make positive contributions to human development and human capital and therefore enhances economic growth, particularly in low- and middle-income countries.<sup>13</sup>

Increased social spending on education, health and social protection, for example, leads to a variety of better socioeconomic outcomes, such as lower poverty and inequality and longer life expectancy.<sup>14</sup> Public health spending has had a greater impact than private health spending on lowering poverty, improving life expectancy and reducing child mortality.<sup>15</sup> In broad terms, human capital investments in education, health and so on correlate with lower income inequality, strengthening the social contract and human empowerment.

Most of the top 10 countries globally in terms of human development have high human capital; in contrast, Arab countries typically have low human capital (table 1). The International Monetary Fund (IMF) suggests that to achieve five SDGs central to boosting human, social and physical

capital, the median Arab State must increase public expenditure by 5.3 per cent of GDP per year between 2020 and 2030.<sup>16</sup> Equally important will be to ensure that expenditures are allocated efficiently and equitably, and managed sustainably, points explored throughout this report.

**Table 1. Countries at high levels of human development have high scores on human capital**

Country	Human Development Index (2019)	Human Capital Index (2020)	Public social expenditure, percentage of GDP, latest available figures	Public social expenditure per capita (dollars), latest available figures
<b>Top 10 countries on the Human Development Index</b>				
Norway	0.957	0.771	25.3	15868.8
Ireland	0.955	0.792	13.4	11125
Switzerland	0.955	0.756	16.7	11550.5
Hong Kong, Special Administrative Region of China	0.949	0.812		
Iceland	0.949	0.745	17.4	8896.8
Germany	0.947	0.751	25.9	13488.8
Sweden	0.945	0.795	25.5	13736.8
Australia	0.944	0.770	16.7	8571.5
Netherlands	0.944	0.789	16.1	9192.7
Denmark	0.940	0.755	28.3	16053.5
<b>Arab countries</b>				
Tunisia	0.740	0.516	23.4	691.5
Jordan	0.729	0.553	14.9	620.7
Egypt	0.707	0.494	12.5	466.2
Iraq	0.674	0.407	22.2	1370.4
Lebanon	0.744	0.515	9.9	1103.5
Oman	0.813	0.608	17.2	2644.5
Morocco	0.686	0.504	13.2	433.5

**Source:** Authors' compilation.

**Note:** Public social expenditures are compiled from OECD and ESCWA databases for OECD and Arab States respectively.

In many Arab countries, efforts to invest in development and economic progress are complicated by a shortage of fiscal space, given high public debt and budget deficits. This is a concern even in higher-income Gulf Cooperation Council (GCC) countries such as Bahrain, Kuwait and Qatar. Financial challenges due to COVID-19 have further aggravated limited fiscal space in middle-income countries, such as Egypt, Jordan and Tunisia. Countries with fragile and conflict-affected situations and the least developed

countries face the worst situations. Lebanon's severe fiscal and trade deficits and skyrocketing debt levels have resulted in the Government reducing essential services and fiscal support even during the pandemic.<sup>17</sup>

Limited fiscal space meant that in responding to the pandemic, the Arab States extended stimulus packages totaling only about 4 per cent of GDP. This was far behind the global average of 22.6 per cent, as estimated by the COVID-19 Stimulus

Tracker,<sup>18</sup> and inadequate given the extent of socioeconomic damage. The tracker predicts that the region requires an additional \$462 billion to achieve a resilient and fast recovery on par with other regions and to surmount challenges on top of those already hindering progress on the SDGs.

At the same time, in the region and globally, COVID-19 has shifted understanding of the value of social expenditure in protecting the poorest and most vulnerable populations while sustaining people and the economy more broadly. Much depends, however, on defining public social expenditures that both meet human needs, across all social groups, and are efficient in enhancing economic growth and social equity. In this, governance plays a role; so does targeting to specific populations and using measurement capturing multiple and intersecting points of vulnerability.<sup>19</sup> Financial inclusion, digitalization and institutional

quality in managing fiscal balances are other important factors.<sup>20</sup>

The right mix of schemes and the adequacy and equity of social expenditures are key in making links to greater economic growth and more equitable outcomes. On balance, this report maintains that social assistance through cash or in-kind transfers and public social investments such as in skills development are both important for reducing poverty in the near term. They also have strong longer-term impacts as they improve opportunities for the poor and enhance upward social mobility. In Egypt, for instance, social assistance programmes improving workers' health and skills have alleviated the most frequent forms of food insecurity, while financial assistance purely to reduce food insecurity has had less of an impact over the long term (box 1).<sup>21</sup> Cutting some energy subsidies could reduce poverty and market income inequality significantly in Tunisia.<sup>22</sup>

### Box 1. Human capital investments reduce vulnerabilities in Egypt

While social assistance programmes have been a central strategy in the Arab region to mitigate severe vulnerabilities, they often centre on regressive and inefficient subsidies that impose a heavy burden on the gross domestic product. By contrast, investments in human capital, such as vocational training and health insurance, tend to cost less, make more significant contributions to long-term welfare and lower vulnerabilities, as seen in Egypt.

A study assessing alternative public programmes for workers measured the effects of publicly funded vocational training, health insurance and financial assistance on employment status and deprivation. The study found that social assistance programmes targeting workers' health and skills have positive long-term effects, alleviating the most frequent forms of food insecurity. Work experience, marital status and urban residence had marginal effects on food insecurity in comparison. The impact of financial assistance in reducing food insecurity over the long term was low and unclear. While it contributes to decreasing food insecurity in some cases, it yields the opposite results in others, depending on the entity providing the assistance (figure A).

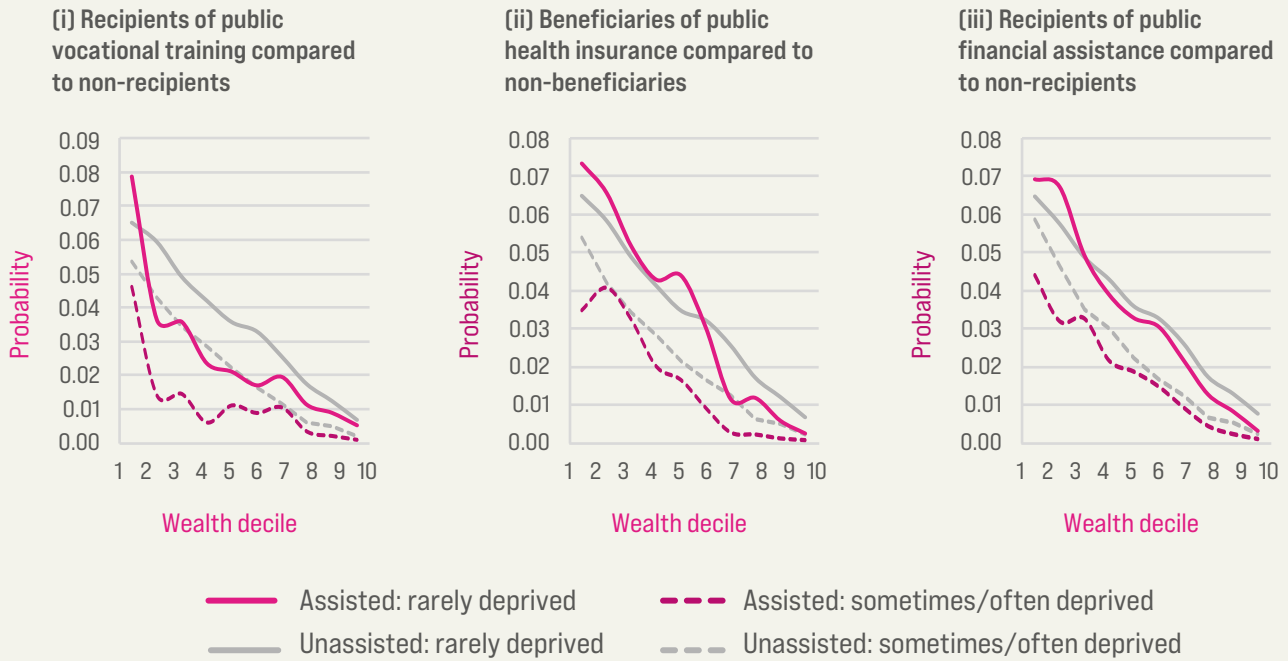
Previous or present recipients of financial assistance tend to report lower job satisfaction, although this may reflect a moral hazard, where beneficiaries may report lower levels of living conditions to meet eligibility criteria for cash handouts. In contrast, investments in human capital through higher education and vocational training as well as health tend to realize higher job satisfaction and greater prospects for career advances in the short and long run. Workers' human capital has a strong return in matching them to suitable jobs with decent working conditions (figure B).

While financial assistance is important to support the extremely poor and deprived, the findings suggest balancing it with programmes increasing human capital, skills and other capabilities with a greater long-term impact. The latter not only support the poorest but also middle-income groups and informal workers to reduce their vulnerability to poverty.

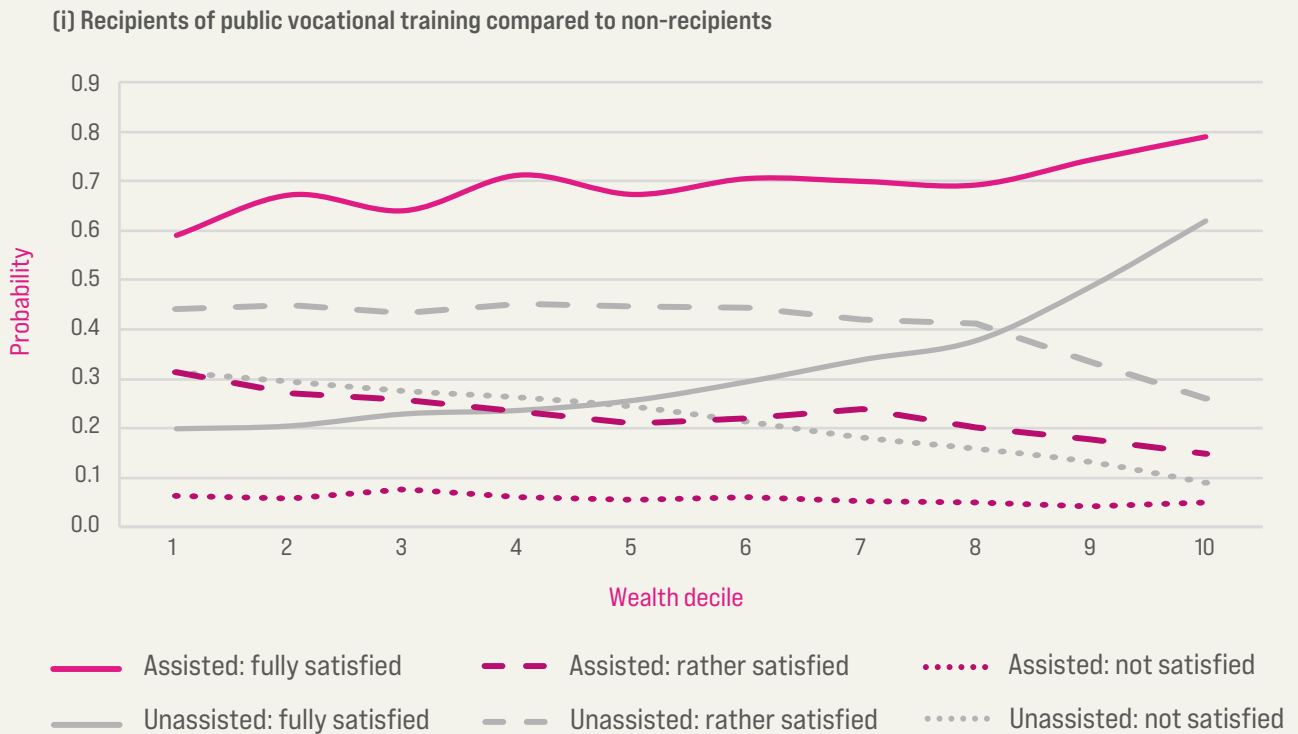




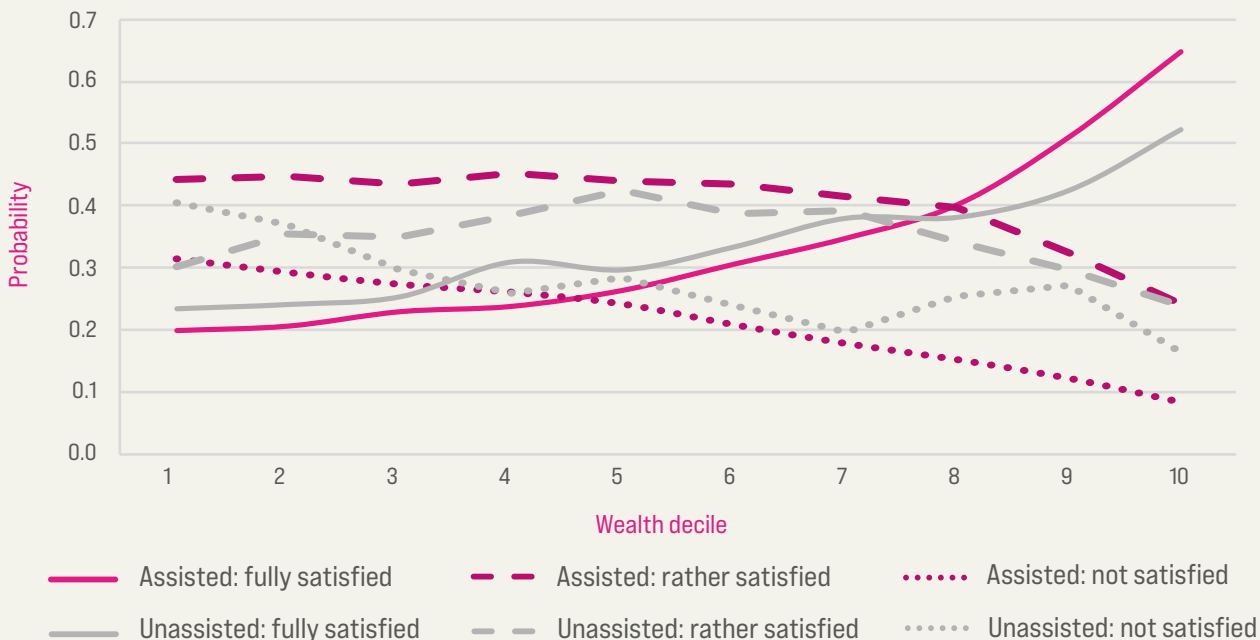
**Figure A.** Predicted probability of severe food deprivation, by wealth decile



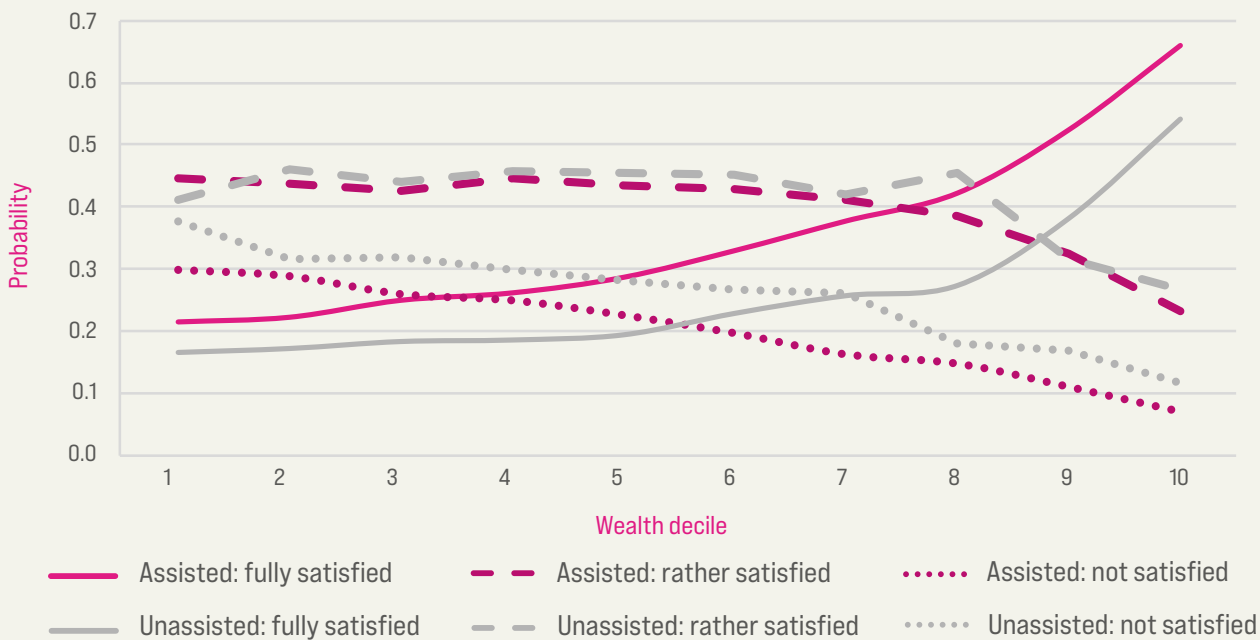
**Figure B.** Predicted probability of degree of satisfaction in current job, by wealth decile



(ii) Beneficiaries of public health insurance compared to non-beneficiaries



(iii) Recipients of public financial assistance compared to non-recipients



Other issues relate to whether social expenditures are countercyclical, supporting people and reviving the economy during downturns. In most Arab countries, public expenditure follows economic output, largely due to dependence on commodity prices and the rentier nature of their economies.<sup>23</sup> Some variations in this pattern emerged after the 2008 economic downturn as several countries increased discretionary social expenditure to prevent discontent amid losses in economic growth. A similar response took place to support people and economies to withstand COVID-19.

With limited fiscal space now under intense pressure from the demands of the pandemic, and amid spiraling uncertainty in the global economy due to factors including the conflict in Ukraine, Arab countries face many questions around the fiscal sustainability of enhanced social expenditures. This report stresses, however, that “enhancing” means not just spending more but spending smartly.

When compared to countries with similar income levels, Arab States on average lag on growth and human development as well as on social expenditure.<sup>24</sup> Reasons for the discrepancy include inefficiency in targeting and allocations, budget rigidities related to salaries and wages, and the neglect of social investments in sectors that boost productivity.<sup>25</sup> Smart policy choices would consider how to use resources most efficiently and equitably. This could mean achieving the same

outcomes while saving resources or achieving greater outcomes with the same spending.<sup>26</sup>

Another consideration is that increasing social expenditure with quality public service provisions, beyond stimulating growth, can lead to more revenue generation.<sup>27</sup> Tax collection tends to be higher in countries with greater social investments, implying better public services for health, housing and education.<sup>28</sup> Raising revenues primarily through higher rates or a broader tax base may lead to resentment or tax evasion unless people trust that Governments will provide quality public services.

The COVID-19 pandemic has created a two-sided problem, increasing the need for expenditure while constraining abilities to mobilize resources. Meeting emergency health and social protection needs has consumed funds that could otherwise have been allocated to the other SDGs and imposed additional costs. Amid higher poverty rates, increased mortality and erased gains in education,<sup>29</sup> an IMF study of four countries estimated that SDG spending requirements shot up by 21 per cent due to the pandemic.<sup>30</sup> Another assessment defined \$2.5 trillion in unmet SDG financing globally prior to 2020, and projected that the gap rose by \$1.7 trillion during the pandemic.<sup>31</sup> Obstacles to raising more resources are particularly acute for least developed countries dependent on official development assistance that is now in short supply amid constraints in partner countries.

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## C. A better means of measurement

Given the critical role of public social expenditure and the pressures on fiscal space, this report presents the SEM as a tool to align spending with progress on multiple SDGs (figure 5). Many Arab countries currently lack holistic monitoring of social expenditure, which undercuts efficient and effective budget choices. Compounding these gaps are ineffective coordination among

ministries and insufficient tools for social expenditure and fiscal sustainability analysis.

These deficits help explain the lower performance of public social expenditure in Arab countries compared to peers in other developing regions. Without quality monitoring, public social expenditure often results in inefficiencies such

as allocations to multiple and overlapping social programmes, inequities in reaching vulnerable populations, and mismatches between expenditures and needs. While public budgets are now under pressure in most Arab countries in the wake of the COVID-19 pandemic, and several face heavy debt burdens, another grave concern is the unsustainable and inefficient management of public social expenditure. This puts the achievement of all the SDGs at risk.

The SEM goes beyond traditional ways of measuring expenditures on essential services. Such approaches focus primarily on health, education and social protection, while the SEM covers the breadth of SDG targets.<sup>32</sup> The SEM framework classifies social expenditure into seven dimensions, namely, education; health and nutrition; housing and community amenities; labour market interventions and employment generation; social protection, subsidies and support to farms; arts, culture and sports; and environmental protection.<sup>33</sup> These dimensions cover all public expenditure with a social purpose, and 70 out of 169 SDG targets.

The SEM helps demonstrate why fiscal policy should not be restricted to redistribution through social assistance, social insurance and transfers. It can assist in steering fiscal policy towards a much larger role in reducing poverty and vulnerabilities and ensuring inclusive development and social justice (figure 6). It supports rationalizing social expenditures and finding the right mix of social protection and social investment<sup>34</sup> to enhance human capital, kickstart opportunity and innovation, and realize the productivity and economic participation of all members of society. All these investments contribute in turn to greater macroeconomic and social stability.<sup>35</sup>

One innovation of the SEM is to generate data on social expenditures based on their purpose and beneficiary populations. The aim is to create better statistics for more robust and responsive policymaking that supports the equitable and efficient targeting of priority

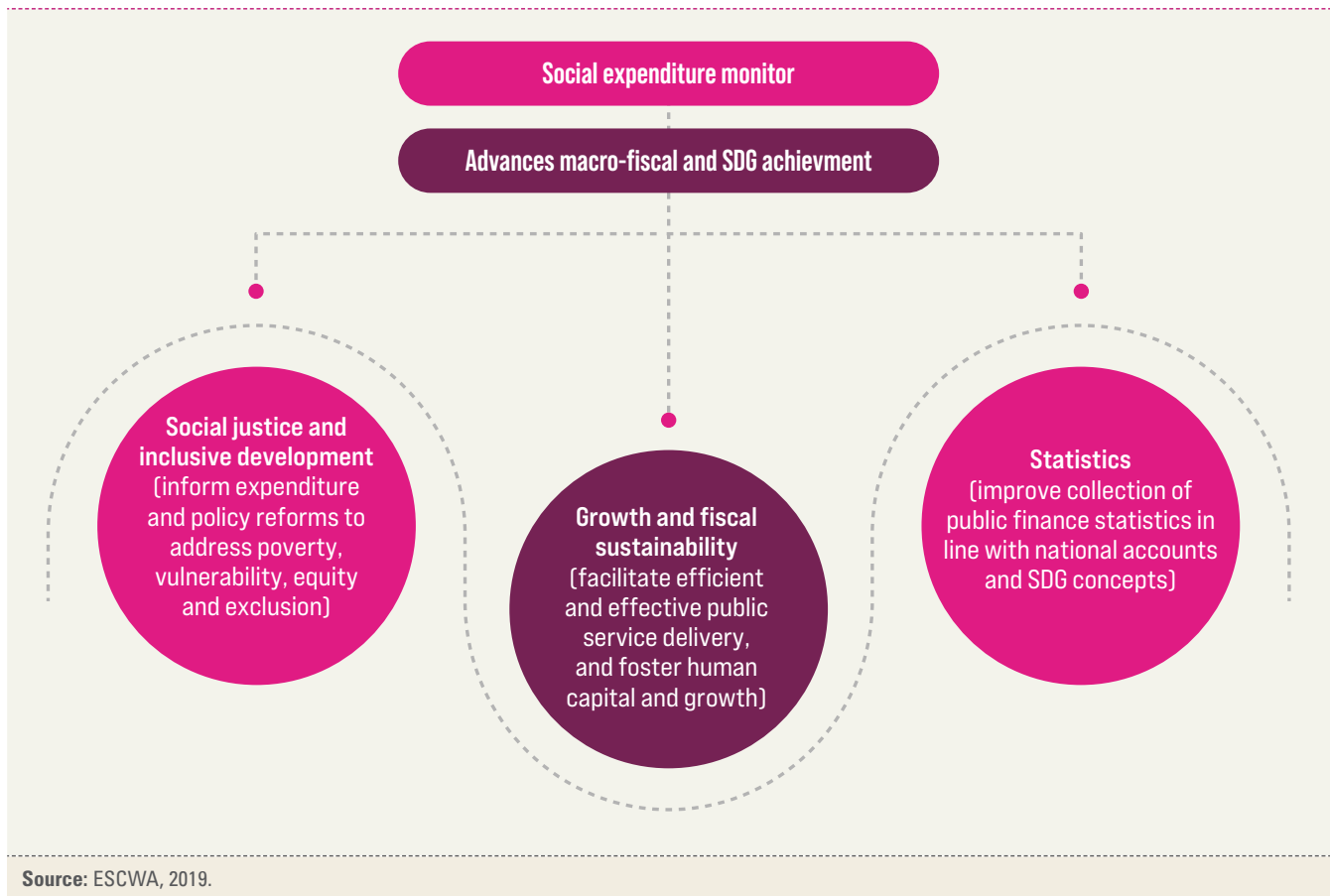
investments and beneficiaries, especially to reach the poorest populations and those struggling with multiple points of vulnerability.<sup>36</sup> The SEM attempts to disaggregate beneficiaries by sex to assess how public social programmes have allocated expenditures to men and women, although most public expenditure data are not currently disaggregated by sex. The SEM highlights this shortfall and suggests ways to improve social expenditure data as integral to guiding measures to achieve gender equality.

Figure 5. The SEM cuts across the SDGs and their targets



Source: ESCWA, 2019.

**Figure 6.** The SEM helps advance the SDGs by monitoring budgets and fiscal policy reforms



## D. What is ahead in this report

Chapter 2 explores social expenditure and international measures of social spending. It highlights the importance of comprehensive measures by introducing the broader SEM framework. It analyses public social expenditure on essential services (health, education and social protection) in the Arab region, compares the findings to global averages, and discusses total public social expenditure under the broader SEM measure for eight Arab countries with available data. The chapter concludes by highlighting major trends in public social services and allocations across beneficiaries, highlighting major gaps.

Chapter 3 examines the equity and adequacy of allocations to social spending, considering

vulnerabilities faced by different population groups in the Arab region. The chapter stresses the importance of putting equity at the heart of social spending to foster empowerment, promote sustainable progress and enhance social justice.

Chapter 4 examines the need to increase the efficiency of social expenditure in the Arab region to maximize its impact, enhance social outcomes and build an inclusive society. It assesses how countries compare with peers in other regions in terms of efficiency by employing a data envelop analysis methodology. It decomposes the overall efficiency of education, health, social protection, and environmental protection expenditures into components and attempts to assess their impacts

on particular social outcomes, including through exploring underlying contexts and policies.

Chapter 5 considers the region's fiscal space challenges in enhancing social expenditure and proposes concrete solutions through a macroeconomic modelling exercise. The chapter investigates fiscal policy choices related to domestic revenue reforms, enhancing fiscal space through innovative financing instruments such as debt swaps, new debt financing in a well-strategized debt-to-GDP stabilization framework, and efficiency improvements to enlarge fiscal space.

Chapter 6 delves into improved public financial management and budgeting as a foundation

for a more just and inclusive society. It stresses effective management, which includes developing medium-term expenditure and revenue frameworks to increase expenditure effectiveness and efficiency and macroeconomic stability. It also explores key fiscal policy and budgeting reforms required to better target budgets to achieving the SDGs, promoting an inclusive society and achieving gender equality.

Chapter 7 presents key findings and recommendations for improving the equity and efficiency of public expenditure as well as public financial management. It outlines fiscal policy and budgeting reforms essential for a well-strategized social expenditure policy that fosters inclusive development.



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- 31 Organisation for Economic Co-operation and Development (OECD), 2021a.
- 32 Chapter 2 of this report provides a detailed mapping of the SEM methodology and definition of social expenditure.
- 33 ESCWA, 2019c.
- 34 ESCWA, 2017a.
- 35 ESCWA, 2019c.
- 36 ESCWA, 2017a.

