

Aid for AIDS: The IMF Role*

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Macro Consequences of HIV / AIDS

- *The Macroeconomic Impact of HIV / AIDS*, Markus Haacker (ed.) brings together research done by IMF, World Bank, UNAIDS, ILO, CGD, LSE etc.
 - Devastating social and microeconomic consequences. But equally devastating macroeconomic consequences.
 - Through mortality and morbidity in most productive segment of population, economic growth likely to be reduced.
 - Production costs may increase, eroding competitiveness and deterring investment.
 - Possible adverse consequences on human capital formation (orphaned children or sick parents), and hence future growth.
 - Civil service (hence implementation capacity and public services) can be devastated.
 - Tax revenues may fall as economic growth slows, while public health expenditures rise, creating fiscal burden.

Does the IMF stop low-income countries from spending money on HIV / AIDS?

- The answer is No. On the contrary, part of our job is to help spend aid money effectively.
- IMF fully engaged in implementing MDGS (one of which is to halt / reverse HIV / AIDS)
- HIV prevention / treatment programs are important parts of PRSPs – the basis for concessional multilateral lending and debt relief.
- Many IMF country reports have addressed macroeconomic implications of AIDS (e.g. recent Namibia Staff Report).
- Grants for HIV programs are treated as revenues, and hence have no impact on fiscal deficit targets in Fund programs.
- IMF programs aim to foster long-run growth, which is associated with positive health outcomes.

Resource scarcity complicates the fight against HIV / AIDS

- Aid should promote AIDS-eradication but also other MDGs, growth, poverty-reduction and development. Sometimes there are trade-offs between these multiple goals:
 - Competing needs in low-income country budgets (Fiscal Space).
 - Export sector vs. government investment (Dutch Disease).
 - Today vs. tomorrow (Debt, Aid Dependence, Aid Volatility).
- The IMF is well-positioned to advise on some of these trade-offs.

Fiscal Space

- A sustainable fiscal program must balance medium-term expenditure path with revenue sources including: (i) domestic taxes, (ii) external grants, (iii) external loans, (iv) domestic borrowing and (v) seignorage (inflation tax).
- Expenditure from domestic taxes and external grants, including on HIV / AIDS is generally best. The IMF encourages strong and pro-growth revenue effort and accommodates all grant-financed spending.
- Concessional external borrowing is generally a good source of revenue, provided it does not imply a debt crisis down the road.
- Domestic borrowing is problematic in excess. Can use up scarce private savings with adverse consequences for investment and growth.
- Inflation is generally not good source of government financing. Lots of inflation needed for significant finance, and high inflation bad for growth and regressive.

Critical concerns in fiscal space debate-1a

- There is likely to be competition from other parts of government for any available fiscal space
 - Infrastructure vital for growth
 - Other social sector needs
 - “exceptionality” of health argument not universally accepted

Critical concerns in fiscal space debate-1b

- AND recognize that Ministers of Finance want as much fungibility as possible. Not surprising that a MOF may, in formulating a budget, seek to substitute reliance on external resources for domestic budgetary support—implicitly shifting some domestic resources to nonaided sectors
- Even in health sector, aid flows often derive from vertical initiatives: unmet needs in other parts of the health sector—MOH may seek to take advantage of external resources and shift domestic budgetary support to other parts of health sector.

Critical concerns in fiscal space debate-2

- Decisions today MATTER: One must consider the *future* spending implications of current spending programs
 - Some expenditure programs, once started, effectively *preempt* future fiscal space
- May be ripple effects of policies to enhance absorptive capacity in health sector (e.g., financial incentives for medical care workers). Supplementing wages to health workers distorts the wage scale in relation to other public sector employees. This could effectively absorb some fiscal space.

Dutch Disease

- Apart from immediate welfare improvements, many positive externalities of development expenditures, including on health / HIV programs.
- But aid-financed expenditures on domestic goods and services can appreciate the real exchange rate, with an adverse effect on export sector.
- Exports have often allowed countries to “take off” into sustainable growth, hence squeezing exports may hurt MDGs.
- Difficult trade-off can be minimized by:
 1. High import content of expenditures (e.g. drugs, medical personnel).
 2. Expenditures directed at improving productivity (and hence competitiveness).

Today vs. tomorrow: debt, aid dependence

- If aid comes as loans rather than grants, debt accumulates. Debt crises / defaults can squeeze budgets, reduce investment and cause macro instability.
 - Concessionalities of debt, total amount borrowed, and rate of return on investments are crucial elements in ensuring a sustainable debt burden.
- Aid may engender declining revenue mobilization; adverse consequences if aid were ever scaled down.
 - Above is only one possible symptom of aid dependence, which may weaken political autonomy, accountability, and implementation capacity.

Today vs. tomorrow: aid volatility

- Aid volatility is ubiquitous, increasing and much larger than tax revenue volatility. Commitments are poor predictor of disbursements. Difficult to distinguish temporary from permanent shocks to aid.
- If expenditures rise one-to-one with aid, what happens when negative aid shock occurs?
- Capital expenditures may be easier to cut back than recurrent, but capital expenditures also need O&M.
- Aid shocks can occur not just at aggregate, but also at *sectoral* level. Some expenditures – such as HIV treatments – should not be stopped once started.

IMF Role

- IMF can help considerably in dealing with some of the issues / trade-offs outlined in previous slides.
- IMF can advise on appropriate medium-term fiscal path, which incorporates increases in spending on HIV / AIDS.
- Essential to ensure sustainable path of aggregate expenditures, for reasons discussed earlier (effectiveness of expenditures, macro stability and growth, etc).
- Also must ensure sustainable path of sectoral expenditures, and ability to “smooth” expenditures in critical sectors such as HIV / AIDS treatment in case of negative shock.
- Foreign exchange reserves can play important insurance role.

Senegal: Real GDP Per Capita, 1970-2005

Index 1970=100



HIV/AIDS Aid Disbursements, 2004

	Aid for HIV as a percentage of GDP	Total Official Aid and ODA as a percentage of GDP
Botswana	0.37	0.43
Côte d'Ivoire	0.20	0.99
Ethiopia	0.78	22.78
Guyana	1.53	18.40
Haiti	0.79	6.88
Kenya	0.80	3.95
Mozambique	0.94	20.18
Namibia	0.45	3.14
Nigeria	0.12	0.80
Rwanda	3.55	25.34
South Africa	0.05	0.29
Tanzania	0.79	16.09
Uganda	2.11	16.99
Vietnam	0.04	4.05
Zambia	2.40	20.01

Aid for HIV/AIDS consists of IDA disbursements in FY2004, PEPFAR disbursements in FY 2004, and Global Fund disbursements in calendar year 2004. Official aid, ODA, and GDP data are from the World Development Indicators.