HIV/AIDS – a fiscal policy perspective

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Over the last decades, HIV/AIDS – through its numerous health, social, and economic consequences – has emerged as a major development threat. That means inevitably that it has fiscal policy implications. HIV/AIDS not only impairs government capacities, it makes additional demands on governments to address pressing health and other social issues. Ministries of Finance can also play a role in formulating national responses to HIV/AIDS, helping to identify longer-term financing needs, and collaborating with donors and other ministries to ensure that these needs are met.

HIV/AIDS stands as one of the largest obstacles to development in many countries, particularly in sub-Saharan Africa. Recent experience has shown that HIV/AIDS can spread rapidly, so that it constitutes a significant risk to development, even in those countries in which it is now confined to a small proportion or sub-groups of the population. Most evidently, the disease jeopardises significant health-related improvements attained in recent decades. The social and economic consequences of HIV/AIDS, as well as the substantial challenges associated with formulating and financing the response to it, also make the epidemic a significant economic and fiscal issue.

For instance, taking the United Nations Millennium Development Goals (MDGs) as a point of reference, one MDG explicitly refers to HIV/AIDS ("halt and begin to reverse the spread of HIV/AIDS"), but the disease also has a bearing on most of the others, most obviously on MDGs 4 (to "reduce child mortality") and 5 (to "improve maternal health"). Moreover, to the extent that being orphaned impedes access to education, it affects MDG 2 ("to achieve universal primary education"), and the higher prevalence of HIV/AIDS among women (as well as their traditional role in care) means that HIV/AIDS also has a bearing on gender equality (MDG 3).

Policy impacts

Through its numerous social and economic consequences, the scale of the epidemic in some countries, and the challenges associated with formulating, financing, and implementing a national response to HIV/AIDS, the epidemic is also relevant to fiscal policy. Here we highlight some of the social and economic impacts, analyse their implications for governments facing an epidemic, and discuss some economic (particularly fiscal) policy aspects of national responses to HIV/AIDS.

The most direct effects of HIV/AIDS are the illness and death of its sufferers and their dependents. In this regard, the impact of HIV/AIDS can be compared to a major war: for example, the United Nations estimates that life expectancy in Liberia declined by about five years during the civil war. In 14 countries with high HIV prevalence rates, life expectancy has declined by at least five years – and in some the losses in life expectancy exceed 20 years.

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The impact of HIV/AIDS on life expectancy reflects not only the high mortality rates associated with the disease in Africa and elsewhere, but also the fact that it primarily affects young adults. One consequence of increasing mortality among young adults is that the number of orphans rises as parents die. Even relatively moderate HIV prevalence rates of less than five per cent can double mortality for young adults, and thus double orphan rates. For some of the worst affected countries, orphan rates have been creeping up to around 20 per cent of the young population (an average – this means that over a third of the young population could lose one or both parents before they reach adulthood).

HIV/AIDS has also been identified as contributing to food insecurity or shortages in many countries, as people falling ill cannot tend to their crops. More generally, HIV/AIDS contributes to poverty, as households lose income, have to devote time and resources to care, or must support other households that are affected. A recent IMF study on how HIV/AIDS affects poverty finds that increased income insecurity results in higher poverty rates even when changes in average income are small.

From a bird's eye view, the recent experience of some countries with high HIV prevalence (such as Lesotho, Malawi, South Africa, Swaziland, and Zambia) would suggest that the immediate impact of HIV/AIDS on economic growth is moderate. While the per capita growth of GDP has declined somewhat (or accelerated less) in some of these countries over the last 10 years relative to other countries in the region, it is not clear whether the decline can be attributed to HIV/AIDS. But keep in mind that these relatively benign findings on the impact of HIV/AIDS on GDP may not hold in the longer run. One influential World Bank study stresses that through its impact on households, its effects on poverty, and its impairment of access to education, HIV/AIDS lowers the long-term growth rate.

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Comparing the need for HIV/AIDS-related government services from country to country is complicated, because the epidemiological situation and the role of public health services differ across countries, and differential levels of economic or health sector development enable different strategies to respond to the epidemic. One useful indicator of the scale of the challenge is the cost of achieving a certain standard of HIV/AIDS-related health services. For a group of highly affected countries, a fairly rapid scaling up – say, trebling access to antiretroviral treatment by 2010 – would require expenditures that exceed total public health budgets. The highest fiscal effect does not occur in countries that have very high prevalence rates like Botswana, Namibia, South Africa, Swaziland (because they also have relatively high GDP per capita). The financial burden relative to GDP is heaviest in low-income countries like Ethiopia, Malawi, or Mozambique.

Funding patterns

Reflecting the global commitment to fight HIV/AIDS, global funding for HIV/AIDS spending in low- and middle-income countries increased in 2005 to about US$8.3 billion (from about US$6.1 billion in 2004), reflecting primarily a very substantial increase in bilateral and multilateral funding. For sub-Saharan Africa, where many of the worst affected countries are located, disbursements from major donors in 2005 amounted to 0.24 percent of recipient countries' GDP; for the World Bank they rose from US$153 million to US$256 million (on a fiscal year basis); for the US President's Emergency Plan for AIDS Relief, from US$517 million to US$916 million (fiscal year, numbers relate to country-managed projects only), and for the Global Fund from US$186 million to US$310 million (calendar year, specific HIV/AIDS-related grants only).

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Commonwealth project for setting up a day centre in Malawi for AIDS orphans and children.

External funding was complemented by domestically financed spending on HIV/AIDS. For 35 countries for which data are available, domestic spending in 2005 (or the latest year available) amounted to about US$900 million – 0.16 percent of GDP. Note, however, that South Africa and Botswana account for about two-thirds of domestic spending; external financing predominates in most other countries in the region.

While the fiscal costs of responding to the epidemic are substantial, the repercussions for public policy go much further. Increased deaths or retirements of public servants reduce government capacity. What little data there is on death-related attrition of public servants points at increasing mortality among young public servants. Using HIV prevalence and mortality rates for the general population as a proxy for public servants (which may be a misleading assumption, especially in the context of the scaling-up of antiretroviral treatment), it appears that the probability that a young person joining public service will reach retirement age drops by half in some of the worst cases, owing to increased mortality.

The indirect cost impact

Adding to the burden on governments, the fiscal costs of HIV/AIDS go far beyond the costs of a national response to HIV/AIDS. The epidemic incurs numerous indirect costs, expenses that are not covered by a specific HIV/AIDS line item in the government budget. The most important are such personnel expenditures as medical and death-related benefits and the costs associated with higher staff turnover, as well as various social expenditures. Increased mortality and a rising number of surviving dependants can also affect the balance of a public service pension fund – one study from Swaziland suggests that this cost alone accounts for about 0.5 percent of GDP.

While much smaller than the direct costs of a national response to HIV/AIDS, these indirect costs have a disproportionate impact on government finance. The reason for this is that in most countries, HIV/AIDS programmes are at least partly financed by external grants, while such financing is not normally available to cover indirect costs. Together with some domestically financed HIV/AIDS-related spending, the fiscal impact of HIV/AIDS can therefore be substantial even if the national response is largely financed by external grants.

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Absorptive capacity

One important concern that has been raised in light of the large resources that have become available to finance HIV/AIDS programmes is the issue of absorptive capacity. If the demand for local supplies or services financed by HIV/AIDS-related grants exceeds current capacity, the result would be inflation and a destabilised economy. That concern is, however, more pressing in situations with very high grant inflows, such as a post-conflict situation, where overall external aid may amount to well over 20 percent of GDP. As the scale of HIV/AIDS programmes is much smaller, amounting to several percentage points of GDP, this is probably less of an overall concern, unless it occurs in the context of already very high grant inflows.

To ensure that a national response to HIV/AIDS is consistent with national development objectives for the health sector and beyond, careful planning and coordination is necessary. For example, conflicts can arise if HIV/AIDS programmes compete for scarce personnel with general health services. The issue of coordination is particularly pressing. HIV/AIDS-related services are often outsourced to implementing agencies, which may be primarily accountable to the funding agency. The World Health Organization therefore emphasises the need for one national coordinating agency as part of its 'Three Ones' principle. Major donors underwriting national HIV/AIDS programmes, such as the Global Fund, can also facilitate the formulation and implementation of effective national responses.

Implications for Ministries of Finance

In addition to the responsible line ministries, the Ministry of Finance can play several important roles in formulating and implementing the national response to HIV/AIDS. First, formulating the national response is a complex exercise in sectoral and financial planning that is beyond the expertise of any single ministry. The Ministry of Finance can be useful in clarifying the budgetary implications of proposed responses and projecting costs and financing needs over the medium term. More generally, in countries where the national response to HIV/AIDS is substantial from a fiscal perspective, the Ministry of Finance must also integrate it into the overall medium-term expenditure framework.

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Second, financing the national response is a continuous effort that requires considerable planning – particularly where the response is to a large extent financed by grants, and a delay or decline in disbursements could disrupt essential services or place heavy demands on domestic resources. While the lack of predictability of external grants creates challenges for fiscal management in general, the problems are particularly pressing here because expenditures related to HIV/AIDS tend to be current rather than capital expenditures, and as disruptions to services may have serious consequences. That is why it is necessary to fully understand what national responses to HIV/AIDS imply for the fiscal outlook. It also underlines the need for donor agencies to make commitments that give the national authorities the required planning horizon.

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