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The Macroeconomic Environment for Jobs in South Sudan: Jobs, Recovery, and Peacebuilding in Urban South Sudan – Technical Report II

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Jobs

THE MACROECONOMIC ENVIRONMENT FOR JOBS IN SOUTH SUDAN:

JOBS, RECOVERY, AND PEACEBUILDING IN URBAN SOUTH SUDAN – TECHNICAL REPORT II

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KEY MESSAGES

This report is one of a set of studies on urban jobs outcomes. This study is one of a four reports covering different aspects of jobs in urban South Sudan. Readers may refer to the respective companion reports on the macroeconomic environment for jobs (World Bank, 2020b), markets and market-linked agriculture (World Bank, 2020c), and jobs in businesses and NGOs (World Bank, 2020d). A synthesis report summarizes and contrasts findings from all four studies (World Bank, 2020e).[1]

Summary

The macroeconomic environment could hardly be more difficult for South Sudanese looking to make a living. The environment of macroeconomic instability is not kind to the self-employed and those looking to make a living with a small business. Conflict has destroyed many activities and depressed demand in the markets. Inflation continues to pose significant difficulties; the impact of dual exchange rates is harder to measure, but is likely to undermine the competitiveness of local products. Oil revenue has declined, and continues to be mismanaged, with little investment in infrastructure, or human capital. Arrears and eroding purchasing power in public sector salaries are weakening the civil service and reducing its role in stimulating market demand.

Structure of the economy and patterns of contraction

For workers, the dramatic contraction of non-oil output since the beginning of the conflict reflects a loss of job activities and a breakdown in market demand. Since 2011, real GDP has contracted by more than 55% - but changes in overall GDP growth in South Sudan strongly reflect changes in oil revenue (which has contracted by 72%), and are hence of limited use in understanding shifts in jobs outcomes. However, since 2011, real non-oil GDP has also dropped by 37%, and household disposable income by 70% (IMF, 2019). South Sudan is a low-income economy, and jobs are largely in informal self-employment in agriculture and services. Hence, for workers, the GDP decline essentially reflects a loss of small market-linked activities that provided cash income. Millions have lost such activities to displacement, but even among urban households who have not had to flee, half say they have lost an activity since the beginning of conflict. Many others have seen their productivity decline, whether farmers unable to go to the fields, traders hesitant to risk trips between villages and towns, or artisans unable to find customers. On the expenditure side, the corollary of the decline in output is a collapse in market demand, with a significant share of food consumption shifted from market to aid.

Inflation and foreign exchange

Monetization of the budget deficit, import price inflation, and conflict induced disruption of food production, markets and supply chains contribute to chronically high inflation. With limited data available, it is not possible to identify what policy decisions and shocks contribute most to rising prices. However, three factors are clearly important. Firstly, the Government has periodically resorted to printing money to finance the budget deficit. Secondly, exchange-rate pass-through (that is, changes in domestic prices due to changes in the value of the currency) has further fueled price increases in the

[1] World Bank (2020a). *Jobs outcomes in the towns of South Sudan.* World Bank (2020b). *The macroeconomic environment for jobs in South Sudan.* World Bank (2020c). *Reviving markets and market-linked agriculture in South Sudan.* World Bank (2020e). *Synthesis report: jobs in recovery and peacebuilding in urban South Sudan.*

import-dependent economy. Thirdly, a breakdown in food production due to conflict and climate shocks has fueled price changes.

Amid conflict and economic decline, a 60-fold increase in prices since before the conflict poses a serious obstacle to job activities at all levels. Over the 2015-18 period, South Sudan experienced explosive price rises, with annualized rates of up to 550%. Since then, inflation has waxed and waned, but had again reached 170% as of October 2019. Most recently, inflation in April 2020 was reported to have been at an annualized rate of 40%, but steep food price increases suggest that this figure may not yet have captured the full inflationary pressure due to the Covid-19 pandemic. Inflation has taken a serious toll on livelihoods. Surveys conducted in 2019 show that households, market traders, and more established businesses alike view the rapid price changes as a serious problem, and that they reduce or stop their activities because of the difficulty of coping with inflation.

There is a wide spread between the official and parallel market exchange rates, with some clear negative impacts on competitiveness. Since independence, the SSP has depreciated nearly one hundred-fold, and a gap of 105% has opened between the parallel and official exchange rates (as of June 2020). While the impact of this differential on the real economy is difficult to analyze, because there is little information on USD flows at the official rate, the first effect of a dual exchange rate is to distort prices and to distance the demand and supply of goods from their relative scarcity. Secondly, the dual exchange rate regime has created opportunities for rent-seeking for those able to access USD. Thirdly, budgeting USD-denominated oil revenue at the official rate favors government spending on imports over domestic purchases. Lastly, customs duties on imports are assessed at the official rate, leading to lower than intended taxes on imports.

An overvalued exchange rate can do far deeper damage to competitiveness, but it is not clear to what degree such distortions currently materialize. There is no good information on what USD amounts from oil revenue and aid flow into South Sudan, who can access USD at the official rate, and how much. Anecdotally, it appears even formal businesses and commercial banks have little access. Overvaluation of the official rate in principle makes domestic production less competitive with imports, and sets incentives against foreign investment. But because businesses in practice may not buy USD at the official rate, it is not clear whether these impacts currently materialize.

Fiscal policy and oil revenue management

The oil sector is a big part of the economy, but governance and accountability are weak, with widespread reports of corruption and misuse. The oil industry is a big player in the economy, and prior to the oil price drop resulting from the Covid-19 crisis, accounted for 30% of GDP, 90% of government revenue, and nearly all exports. At the same time, it remains shrouded in secrecy. Credible data on production and export are not publicly available, and the use of oil advance contracts leads to opacity and complicate budget management. Public perceptions about the scale of foul play have had a corrosive effect on incentives and social trust.

The budget is dependent on oil revenue, pro-cyclical, and orientated toward security rather than productive investment. The national budget is almost entirely funded by oil sales, which in the FY20 budget accounted for 90% of revenues (valued at USD55 per barrel). There are no mechanisms to buffer fluctuations in production and price, so that fiscal policy is procyclical. In the tense political context, spending on security and police account for 69% of the executed budget in FY 2018/19 data. The Government's FY 2019/20 budget foresees a dramatic increase in infrastructure spending, but it is not

clear how well this ambition was met by execution – and even if implemented, public investment in a jobs-agenda would have remained far below the enormous needs.

Budget allocations are only loosely related to actual spending, and other spending is completely outside the budget. Recent budget execution reports indicate large discrepancies between budgeted and actual spending. In addition, budgets are opaque and a large proportion of oil revenues in particular does not go into the budget. Extra-budgetary expenditures and financing shortfalls due to unaccounted-for advance oil sales lead to a continuous accumulation of domestic arrears and complicate budget and debt management. Such difficulties have in the past foiled efforts to re-orient spending toward investment, and put the Government's current plans at risk.

Public employment

For a country with an estimated population of 11.8 million, the public sector is large, employing some 400,000 soldiers and police, and the 50,000 other civil servants are as many as there are workers in established businesses. The public sector at the national level accounts for the largest share of formal sector employment in South Sudan. In addition, there is significant employment at the sub-national level. About eight out of nine of those on the national public payroll are soldiers or police. Yet, the remaining 50,000 public employees are still about equal in number to all urban workers in established businesses (among whom many do not have a formal employment relationship) and make up about 4% of the estimated urban labor force. That said, employment statistics are unreliable, and likely to include a significant number of 'ghost-employees.'

Public employment is a form of patronage but has an important function as a source of demand for goods and services. There is a perception that the recruitment as well as allocation of positions in civil service is driven by political and kinship considerations. However, public employment plays a redistributive function, as many of those receiving a regular salary support a significant number of dependents. When salaries are paid, the public wage bill is also a way of ensuring that some government spending is directed toward creating demand for goods and services.

Erosion of real wages and payment arrears have taken a toll on motivation, and diminished the role of civil servants as customers to local businesses. Salaries have been undermined by inflation and real wages have been declining steadily. In addition, the government has delayed wage payments and accumulated arrears. By May 2019, civil service salaries were in arrears of four months, transfers to states were in arrears of 5 months, and foreign diplomatic missions were in arrears of up to 14 months. Low and late payments are taking a toll on civil service motivation, and weakening the contribution of the public payroll to market demand.

Policy implications

Even second-best reforms and gradual changes to bad policy can help ease the real difficulty South Sudanese daily face in making a living. Re-shaping macro-fiscal management will take much political will, time, and effort. However, it is worth noting that the current state of affairs is so adverse that there is no shortage of policy opportunities that – while far from perfect – could make a concrete difference in making it easier for workers to make a living.

1. **Addressing the underlying causes of the conflict and restoring peace and stability is an absolute prerequisite for recovery and jobs**. While a Revitalized Transitional Government of

National Unity (RTGoNU) was finally formed in February 2020 following signing of the latest truce in September 2018, the situation in South Sudan continues to be fluid and conflict persists across the country. Recently the United Nations Security Council voted to extend an arms embargo and other sanctions on South Sudan until May 31, 2021, reflecting the immense political, security, and governance challenges that still need to be overcome. Exiting fragility and rebuilding an inclusive economy that offers economic opportunity and jobs will be a slow and winding process. However, what is important is the complete cessation of hostilities and proper implementation of security and governance arrangements to break the cycle of conflict and to usher in a new era of sustained stability.

2. **To tame inflation, the Government must abstain from monetizing deficits.** Businesses and households are vocal about the difficulty of dealing with inflation, and sustained efforts to reduce price hikes are vital for economic recovery and better jobs. The key policy lever to control inflation is to abstain from monetizing budget deficits. In addition, making effort to diversify the economy, and unleash the vast untapped economic potential in non-oil sectors such as agriculture, fisheries, and livestock; natural resources extraction; and agro-processing. It would also allow for a gradual return of some confidence in South Sudan's future, and hence, less pressure on the exchange rate.

3. **Authorities in South Sudan should take steps to unify the current multiple exchange rate system by discontinuing the special accounts arrangements and allow the exchange rate to be market determined.** In the shorter run, such reforms will allow more revenue into the budget. In the medium-term, it will also provide more flexibility on the use of interest rates to influence monetary policy, improve resilience to external shocks, and encourage investment. Greater transparency on foreign currency flows is urgently needed to formulate an exchange rate policy that promotes jobs, and to understand whether reform needs to consider changes in implicit subsidies, for instance, to fuel. More clarity on USD flows is necessary to responsibly develop policy proposals.

4. **South Sudan must dedicate at least some more oil revenue to development priorities if its oil wealth is to support better jobs and economic opportunity.** There is a well-known set of best practices for transparency and effective use of resource revenue, and South Sudan should make progress toward them. However, because of the outsize role of oil in the economy, there is a chance to make a difference for jobs and recovery even with far more limited steps to invest more oil revenue in infrastructure and basic services. One option is to dedicate resources toward visible flagship public investment projects, and to invite greater scrutiny of their implementation.

5. **To make progress toward its development priorities, the Government must improve budget transparency and end the practice of extra-budgetary contracting.** Maintaining security will continue to absorb significant resources, but the Government hopes to gradually shift spending toward development priorities. At the same time, resource and budget management is extraordinarily opaque. While fiscal transparency is no cure-all, more information is needed to help the Government successfully prepare investment plans, track their execution, and improve scrutiny that can keep policies on track.

6. **In early recovery, the Government should look to public employment to channel resources to revive demand.** With greater stability, the Government must renew its post-independence

commitment to building a professional civil service that provides real services to the people. In the short term, however, it can use the existing payroll as a conduit to injecting much-needed demand in the market by paying arrears and considering a reasonable adjustment of salaries to account for inflation. A campaign to remove ghost employees from the payroll can help provide funds.

I. Introduction

South Sudan is a low-income, resource-dependent country that gained independence in 2011 after decades of conflict. Several years after independence, it remains one of the world's most conflict affected and fragile countries, struggling to emerge from cycles of violence. In such a setting, the macro-fiscal environment is bound to be far from perfect. However, even by such standards, South Sudan exhibits a plethora of macro-fiscal issues, many of them linked to the effects of conflict, a lack of institutional capacity, and economic mismanagement. This chapter attempts to understand which challenges in the macroeconomic environment put the most severe constraints on jobs, and what policies may be both feasible and potentially have a high impact on improving jobs outcomes.

Conflict and bottlenecks in oil production have marred economic development in the short period since South Sudan's hard-won independence. South Sudan enjoyed a short period of relative stability after signing the comprehensive peace agreement in 2005 that laid the groundwork for independence in 2011. At the time, South Sudan enjoyed an oil windfall, with production peaking at about 330,000 barrels per day in 2011. However, disagreements with the Khartoum government, including unresolved issues over oil transit fees, led to a shutdown of oil production, precipitating an economic crisis. The economy contracted by 4.6 percent in 2011 and a further 46 percent contraction followed in 2012. While a new agreement with Sudan led to a resumption of oil production and growth in 2013, oil production levels are just about half of what used to be produced before the shutdown and onset of conflict. At the same time, recurring cycles of internal conflict and violence have eroded the economic base. With these developments, output has been contracting for consecutive years during 2015 - 2018. Consequently, real household disposable income is estimated to have declined by about 70 percent since independence in 2011 (IMF, 2019), contributing to an increase in poverty headcount ratio from 50 percent in 2012 to about 82 percent in 2016.

Starting in 2014, falling oil prices compounded an already precarious economic situation resulted in reduced government spending and a buildup of arrears to civil servants as the country's fiscal position deteriorated. As a consequence, the government defaulted on payments to Sudan as part of the Transitional Financial Arrangement (TFA), and started accepting advance payments for oil which further complicated budget management as they were usually patterned with rent seeking. Fiscal deficits were financed partly by printing money, fueling inflation which rose from 1.7% in 2014 to 480% in 2016. In a

bid to reduce the country's huge macroeconomic imbalances and to create conditions to build a stable macroeconomic environment, the Government adopted a floating exchange rate regime in December 2015. However, monetization of the fiscal deficit led to sharp depreciation of the local currency, which coupled with loss of confidence in the economy resulted in development of the parallel foreign exchange market.

Fiscal policy has been affected by budget indiscipline and inefficient allocation priorities. Recent budget execution reports indicate large discrepancies between budgets and outturns. Although this has often led to the accumulation of arrears, expenditures continue to be concentrated in three sectors, namely, security, accountability, and public administration, with limited spending on service delivery and capital goods. Consequently, South Sudan continues to underinvest in the sectors that would have the largest knock-on effect on reducing poverty, building resilience, and building a stock of physical and human capital that are supportive of a jobs-focused recovery and growth path.

Even with improved oil production over the past year, government's fiscal position has not improved as the share of oil revenues that reaches the budget is small. After deducting payments to Sudan, Nilepet's share, and payments towards oil advances, the share of oil revenue that enters the budget has been in the range of 5% and 45% between FY2018 and FY2020. These are from official data and it is not clear if this reflects the entire oil production or how the funds are distributed. The Government has been using oil resources to accumulate arrears by issuing oil advance contracts, which are non-transparent and complicate budget management, and transfers to the oil revenue stabilization account have not been effected, which is against the country's own policy and legal requirements. The prolonged conflict, Dutch disease effects, and donor aid dependency have led to an undiversified and import dependent economy, limiting opportunities for private sector development and job creation. Weak fiscal buffers and external position are further compounded by a precarious debt situation with depleted reserves estimated at less than one week of import cover (IMF, 2019).

Dominance of the oil sector presents unique risks for a jobs-focused economic recovery. While the major risk to economic recovery is peace and security in the country, developments in the oil sector have non trivial effects on economic performance, with little revenue going into the investment and payroll budgets. A key challenge to economic management regards governance and accountability in the oil sector, with widespread reports of corruption and misuse. Credible data on production and export volumes are not publicly available, shrouding the sector in secrecy. Reports recently released by The Sentry (2019) implicate the leadership and detail how oil revenues are being diverted with little oversight and accountability to support the country's security services and ethnic militias.

Through the mediation of the IGAD, the warring parties signed a revitalized agreement on the resolution of the conflict (R-ARCSS) in September 2018 which laid the ground for formation of a government of national unity in February 2020. The Revitalized Agreement on the Resolution of Conflict in South Sudan (R-ARCSS) signed in September 2018 provided a broad framework for a power sharing arrangement under a new transitional government of national unity. The formation of a unity government on 22 February 2020, delayed twice amidst political deadlock, gives the country's leaders a chance to build upon a ceasefire between the warring factions that has largely held since September 2018. While these developments are encouraging, significant challenges remain and the new government will have to work in concert to unify the national army, resolve disputes over control of key cities and make peace with holdout rebel groups.

The Covid-19 pandemic, falling oil prices, and locust infestation have dramatically changed the macroeconomic outlook over a relatively short period of time. With the ceasefire largely holding, South Sudan benefited from increased oil-related investment and a higher oil price, helping the economy to grow by an estimated 3.2 percent during FY2019 – the first positive GDP growth in five years. The economy was expected to build on this positive turn and continue on a gradual growth trajectory. However, coupled with falling oil prices, covid19 containment measures scaled down economic activity significantly, resulting in a dire economic situation. In addition, parts of the country have been affected by an infestation of locusts, with preliminary FAO estimates indicating up to 20% crop losses in affected areas. With these shocks, the economy is projected to contract in FY20, once again highlighting the unique vulnerabilities of South Sudan. Even if oil prices will recover in the future, past performances have indicated a disconnect between oil revenues, service delivery and jobs. To drive sustainable growth and a jobs agenda, therefore, authorities should consider taking steps to diversify the economy and re-orient expenditures to sectors that have the highest potential to create jobs and foster sustained non-resource dependent growth.

This chapter is organized in three sections. Section one provides the introduction. Section two discusses the macroeconomic environment for jobs, recovery, and peace building, providing insight into the following key aspects: structure of the economy and sources of growth; oil revenue management; fiscal policy; public employment; inflation developments; exchange rate policy; and financial sector and access to credit. Section three concludes with policy implications.

Box 1: The impact of the Covid-19 pandemic on livelihoods

The Covid-19 pandemic has had an impact on livelihoods through the increased burden of disease, lockdown measures and trade disruptions, as well as macro-fiscal challenges. As of June 28, 2020, the WHO reported nearly 2,000 confirmed cases of Covid-19 in South Sudan; with very low testing capacity, however, the actual burden of disease is almost certainly higher. Between late March and early May 2020, South Sudan imposed lock-down policies similar to those used in many countries to control the spread of Covid-19. Juba was under curfew, and non-essential businesses were closed (while these measures were intended to be nation-wide, anecdotally, other towns experienced less change). Borders have remained open for goods; however, rules on quarantine and turnaround times have slowed imports and raised prices. The prices of staple grains rose precipitously during the early pandemic response, between 20 percent and 40 percent, though inflation may have slowed recently.[2]

The fall in oil prices has put severe pressure on the government's budget. The fall in global oil prices from nearly USD70 a barrel in early January 2020 to about USD40 at time of writing is putting pressure on the Government's budget, with worrisome implications for market demand for goods and services. The fiscal deficit is projected to more than triple, to USD510m, complicating an already difficult budget execution. There is a risk that deficits may be monetized, reigniting inflation. Unrealized spending on capital investment, further arrears in paying civil servants, and slower service delivery are constraining demand, growth, and jobs. Before the crisis, development assistance and remittances were the first and second-largest foreign currency flows, both exceeding oil revenue. Remittances are likely to have fallen, and it is not known whether NGOs and intergovernmental agencies have fully maintained their activities.

[2] For instance, Mayai et al. (2020) report that the price of wheat flour rose by 27 percent and the price of rice by 25 percent over the month of March, while the University of Juba measured increases in the price of rice, sorghum, and wheat flour by 40 percent, 27 percent, and 19 percent between February and March.

Job activities have been lost due to Covid, especially in non-farm self-employed activities, but as of June 2020, the scale was limited. The World Bank conducted phone surveys in June 2020 to monitor the impact on livelihoods of Covid-19 and measures to contain the pandemic (World Bank 2020f and 2020g).[3] Unless indicated, results in this text box reflect findings from these surveys. One in eight households (13%) reported having lost all income from their main job activity at some point since the onset of the pandemic in early April. Losses were largest among the households that depend primarily on non-farm self-employed business activities. Among these households, one in five have lost all income from their primary activity (20%). Household businesses mostly attributed their losses to a lack of demand (52%) and to usual places of business being closed (49%). Among market traders, one in seven (15%) reported having lost their business, due to travel restrictions due to Covid (33% of those no longer active), but also a broad range of other issues both related and unrelated to the pandemic. Hardly any businesses reported having closed permanently (0.3%), and very few remained temporarily closed as of end-June (5%). However, measuring permanent business closure is difficult, and businesses do report that they know a direct competitor who has gone out of business (47%), and that they considered closing at some point (35%). Activities in Juba seem to have been particularly affected, with higher loss of activity among market traders (31%), and more businesses considering closing (52%) and having competitors who closed (58%).

With widespread poverty and a history of shocks, households are looking to replace lost income opportunities. The real but limited extent to which activities have been lost may be expected, given that households and businesses have lived through many shocks, and that generating income is an immediate question of survival for many households. It is worth recalling that, since 2013, conflict led to the loss of primary activities for 47% of households, that 50% of businesses lost assets and 43% had to temporarily close (World Bank 2020e). While the disruption due to Covid-19 is harmful, it is thus not unheard of. By June 2020, respondents also reported some potential signs of recovery. About one in five households that lost their main activity (22%) reported that they had started a new activity by the time they were surveyed. Similarly, while some traders had stopped their activities, respondents were about twice as likely to say that on balance, the number of traders in the market had increased since April than to say that it had decreased. Both market traders and businesses also reported a modest increase in the number of workers they employed since April, although the rate of hiring has slowed substantially among businesses.

Market activity has reduced, and loss of revenue and income is pervasive. While few job activities have stopped outright, many respondents report losing income from their main activities. This is true of every other main household activity (52%), and of three in five market traders (59%). Traders who offer consumer commodities reported larger declines in revenue (a 35% drop at the median) than food traders (a 25% drop), consistent with temporary closures of non-food markets and a loss of consumer disposable income. Among businesses, four in five (81%) reported a decrease, including 59% who say income has declined by half or more.

[3] Surveys were implemented between June 9 and July 3, 2020. Respondents included 1,213 mostly urban households, 118 market traders, and 612 businesses. Of the respondent households, 75% live in urban areas. Inherently, the phone survey reflects only households that own a cellphone and live where there is coverage. In the 2019 Youth Jobs Survey, 83 percent of urban households owned a cellphone. Of those that did, 12 percent were in the lowest asset wealth quintile, compared to 45 percent of those that did not. Demographics and labor market outcomes in the tracking survey are similar to those observed in earlier in-person surveys. Thus, household-level results are best interpreted as reflecting outcomes for a large stratum of urban households, with some under-representation of the most marginal.

The main obstacles to business activities reported today remain the same as reported in 2019, but they have tightened. When surveyed in mid-2019, households, market traders, and businesses consistently identified insecurity, bad roads, access to funding, and low demand as their main obstacles. They flagged the same constraints when re-surveyed now, but were likely to say that the constraints had become more difficult to navigate – perhaps with the exception of insecurity, where businesses were more likely to report an improvement (44%) than a deterioration (28%). Surveys in 2019 did not directly ask about inflation as an obstacle, while in 2020, inflation was the third-most frequently cited obstacle among market traders, and the second-most frequently cited among businesses.

Sourcing goods has become more difficult, but is rarely considered a key business obstacle. Border closures and movement restrictions have raised transport cost and slowed down sourcing. Among market traders who source agricultural products from Juba or abroad, 85% say buying supplies has become more difficult since the onset of the pandemic. At the same time, while traders mention poor availability of inputs (8%) and transport cost (13%) as obstacles, they give less prominence to them than to other constraints. Similarly, nearly four in five businesses (79%) say that since April, it has become more difficult to buy goods to re-sell or use as inputs. Yet, transport cost is mentioned less frequently as an obstacle than a lack of funds, high inflation, and low demand, and very few point to poor availability of inputs.

Low market demand already posed an important obstacle before the pandemic, and it has further declined due to the crisis. Even before the pandemic, businesses of all sizes viewed constrained demand for goods and services as a key obstacle. Respondents across all three surveys agree that demand has further tightened. Among the households who were unable at some point during the pandemic to buy staple cereals (46% of all households), most say that this was due to a lack of funds (44%), rather than to traders being out of stock (7%) or price changes (11%). Majorities of market traders explain that they have fewer customers on a typical market day (63%), and that customers buy less (60%). Businesses agree: most (73%) say that demand for their products has declined, and half (52%) say that it has dropped by half or more.

II. The macroeconomic environment for jobs, recovery, and peacebuilding

1. The economy and sources of growth

For South Sudanese workers, a steep decline in aggregate output by 55% since independence in 2011 reflects a loss of job activities and breakdown in market demand. Since 2011, real non-oil GDP has dropped by 37%, and real oil GDP by 72%. In a higher-income economy, such a drop in GDP would typically be associated with wartime destruction of infrastructure and capital. However, in a low-income economy, jobs are largely in informal self-employment in agriculture and services. The decline in non-oil GDP chiefly reflects a loss of job activities, most dramatically, among the displaced, but also among farmers unable to access lands safely, or traders unable to travel between towns. It also results from a decline in productivity of those activities that remain, for instance, among market traders and artisans struggling to find customers. On the expenditure side, it further reflects the shift in a significant share of food consumption from the market to aid. While there is a history of mismanagement of resource revenue, the decline in oil GDP from a jobs perspective mainly speaks to the loss of potential productivity-enhancing public investments in infrastructure and human capital.

The structure of the economy changed with a fall in oil production, with the relative contribution of the non-oil sectors expanding. South Sudan is a low-income, resource-dependent economy. Oil exports and oil related investment provide major sources of growth, and hence, economic growth cycles closely follow developments in the oil sector. Consequently, economic performance has been characterized by extraordinary volatility. At independence, the oil and mining sector accounted for about 60 percent of the economy, making South Sudan one of the most oil-dependent economies in the world. However, the structure of the economy changed slightly with a fall in oil production after 2012. The relative contribution of the non-oil economy expanded as the economy shrank when the country descended into conflict and oil production was suspended.

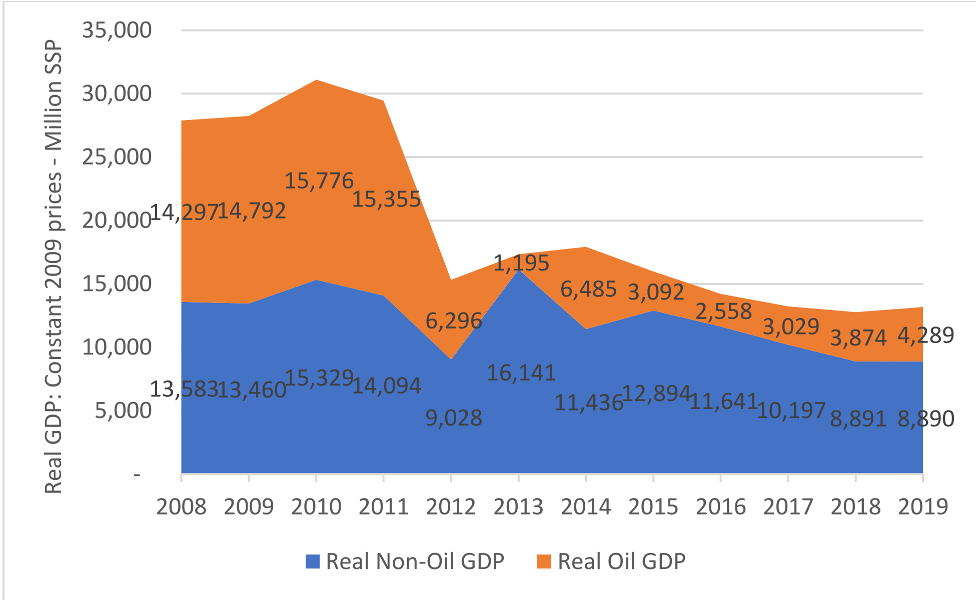
As South Sudan spiraled toward conflict in 2013, solid non-oil growth before independence was followed by a contraction in non-oil activity, and a plunge in oil-sector output. In the two years that preceded independence, economic growth averaged 5.3 percent, with growth in the non-oil economy reaching 14 percent driven by activities in retail, real estate and construction sub sectors. Activity in the oil sector was subdued. The shutdown of oil production in 2012 and onset of conflict in 2013 led to the first economic crisis, with output contracting by 46 percent in 2012 followed by a further contraction of 27 percent in 2013. During this time oil production shrunk by 94 percent in 2012 and 75 percent in 2013. The non-oil sector contracted sharply by 8 percent in 2011, and barely grew over the following two years.

Conflict and macroeconomic challenges have caused the non-oil sector to contract each year since 2011, with a cumulative drop in non-oil GPD of 37%. While the economy recovered briefly in 2014 with the oil and mining sector growing by 18 percent, the non-oil economy continued to struggle, and the cumulative effects of conflict and a difficult macroeconomic environment weighed heavily on private sector activity. The economy continued to struggle as the fall in global oil prices starting in 2014 exacerbated an already precarious fiscal situation. The resumption of conflict in 2016 further aggravated matters as the economy contracted for four consecutive years during 2015 – 2018.

The peace process holds the promise of reversing South Sudan's economic decline, but further concrete progress is needed. A revitalized peace agreement was signed in September 2018, preparing the ground

for formation of a government of national unity in February 2020, following a last minute compromise that restored the ten historical states. However, progress on key aspects of the peace process have been much slower than anticipated. In particular, implementation of the so-called security arrangements which include the demilitarization of all major towns and civilian centres, disarmament of civilians, as well as unification of armed forces has delayed. At the same time, the allocation of state Governors has delayed as parties have pushed back on the allocation of states to the parties to the peace accord. With these challenges, the security situation in the country has worsened. Intercommunal violence has intensified in the three historical regions of Bhar-el-Gazal, Equatoria and Upper Nile, as well as in the three new administrative areas of Abyei, Greater Pibor and Ruweng.

Figure 1: South Sudan real GDP estimates 2008 - 2019



Source: World Bank staff estimates

The share of oil revenue in GDP has halved, and some of the resulting structural changes may present an opportunity for the future. Conflict has led to a big shift in the composition of GDP: the share of the oil sector has declined from about 60 percent in 2011 to about 32 percent in FY2019. A change of this magnitude may also reduce incentives to extract oil rents to some degree. At the same time, the conflict has induced changes in local settlement patterns, demand and trade routes. Such changes may then offer new opportunities for a post-conflict reconstruction agenda that is jobs centered and less reliant on resource revenue. However, because there is no transparency on the use of oil revenue, it is hard to understand whether one should look at this shift as a structural change in the economy. Since much oil revenue is thought to be diverted (see below), not much economic activity may previously have catered to the oil sector. However, some opportunities to make use of the reduced role of oil may still exist. Firstly, in the past public employment played a leading role in absorbing labor in the formal sector, and expectations for public employment were very high. The decline in oil production and high security spending have also forced a hiring freeze in the public sector that may have gradually reduced high expectations for public employment, along with a recent decision to return to 10 states from 32[i]. In early recovery, the Government should help bolster aggregate demand by resuming regular salary payments to civil servants and clearing arrears (as we explain below). However, if oil revenue recovers, the Government

could seize this opportunity to orient incremental spending away from an expansion of the public payroll toward investment in human capital, infrastructure, and the agriculture and agribusiness sectors.

Since 2013, government's predatory behavior captured most of the wealth created, while household consumption has dropped every year, often steeply, and investment has been absent. Between 2013 and 2015, net exports were the major drivers of growth, driven by oil production. However, the contribution of exports waned as production and prices declined. Two trends have emerged since 2013: the contribution of private consumption to growth has been negative, and government predatory consumption absorbed whatever little wealth could have been created over the same time period, mostly through increased security and military spending[ii]. The decline in private consumption reflects the cost of conflict and humanitarian crisis. Conflict has not only affected food production, but also constrained trade, limited access to markets, and impeded the timely delivery of humanitarian and relief items in various remote locations across the country. In addition, the macroeconomic crisis that followed conflict and the shutdown of oil production further eroded consumer spending since 2013/14. At the same time, government consumption has grown as oil receipts have been used to expand expenditures on defense, security, and peacekeeping operations. Investment has played a negligible role, and this is mainly observed in private sector engagement in the real estate, construction, and oil sectors. Recovery will require a resurgence of private consumption, as well as, hopefully, greater investment.

Table 1: Contributions to growth, %

	2011	2012	2013	2014	2015	2016	2017	2018	2019
Real GDP growth (Supply Side)	**-4.6**	**-46.1**	**13.1**	**3.4**	**-10.8**	**-11.2**	**-6.9**	**-3.5**	**3.2**
Agriculture	-0.8	-1.4	4.7	-1.8	1.6	-1.8	-1.5	-1.0	-0.2
Industry	-2.7	-33.6	-26.0	26.1	-17.2	-3.9	-1.2	5.1	3.2
o/w oil	-1.4	-31.9	-33.3	30.5	-18.9	-3.3	3.3	6.4	3.2
Services	-1.1	-11.1	34.4	-20.9	4.7	-5.5	-4.2	-7.6	0.2
Real GDP growth (Demand Side)	**-4.6**	**-46.1**	**13.1**	**3.4**	**-10.8**	**-11.2**	**-6.9**	**-3.5**	**3.2**
Final consumption	-5.3	1.1	7.2	-2.1	-20.3	-9.5	-8.2	-2.5	1.9
o/w Government	-2.9	-1.1	3.1	3.7	0.4	1.0	1.2	1.8	2.4
o/w Household	-2.4	2.2	4.0	-5.8	-20.8	-10.6	-9.4	-4.3	-0.5
Investment	0.9	-7.3	2.1	-0.3	0.2	0.0	0.5	0.7	0.8
Net exports	-0.2	-39.9	3.9	5.9	9.3	-1.7	0.8	-1.7	0.5

Source: World Bank staff estimates

2. Oil revenue management

Oil production is recovering after a steep drop due to conflict and remains the dominant economic sector, but a deep drop in prices has altered the sector outlook. Oil extraction is the most important economic sector, contributing 33% of gross domestic product (GDP), 90 percent of revenues (SSP 269 Billion or USD 1.7 billion at the official exchange rate), and almost the totality of exports. However, oil production was badly affected by war with production falling to just a third of pre-war levels by 2018, precipitating severe macroeconomic imbalances. Estimates indicate that oil production declined from about 350,000 barrels per day in 2011 to about 110,000 barrels per day in 2017. The September 2018 peace agreement and cessation of hostilities have already enabled the reopening of some damaged oil wells. The Government is working to revamp oil production and attract new investments in the oil sector. Consequently, daily oil production has increased from about 130,000 barrels per day in FY2017/18 to about an estimated 175,000 barrels per day during FY2019/20. However, the recent drop in oil prices has

changed the sector outlook and it remains unclear how this may impact on future investments in the sector.

A key challenge in the oil sector regards governance and accountability, with widespread reports of corruption and misuse. The oil industry is shrouded in secrecy, and credible data on production and export volumes are not publicly available. The Government has been using oil resources to accumulate arrears by issuing oil advance contracts, which are non-transparent and complicate budget management. A policy requirement to transfer oil revenue to a stabilization account has not been fulfilled. Reports recently released by the Global Witness and The Sentry groups implicate the leadership in South Sudan and detail how oil revenues are being diverted to support the country's security services and ethnic militias, with little oversight and accountability. These reports list over USD 80 million in payments to authorities and private companies directly linked to the government's defense effort (The Sentry, 2018). The local politically connected elites usually act with the support of an international web of partners and financial institutions to bleed the country of critical resources, while little is left to cater for citizen needs, leaving behind a trail of hunger, deprivation, and desperation (The Sentry, 2019). The public perceptions about the scale of foul play in the use of oil resources at such massive scale has had a corrosive effect on trust and motivations, exacerbating feelings of marginalization, despondency, and malcontent among South Sudanese.

South Sudan's oil wealth will only lead to better jobs and economic opportunity if the Government makes headway in spending oil revenue on development priorities. For the oil sector to benefit development, there is an urgent need for reforms to ensure that revenues are used prudently to finance the government's strategic investment program, as stipulated in the national development strategy and operationalized through the annual budgets. However, current indications are that this is not happening as government continues to face financing challenges despite increased oil production. In the short run, oil revenues can lead to better jobs and economic opportunity if the Governments starts to re-orient expenditure priorities to remove some of the obstacles that most impede business activities and constrain jobs. Businesses, market traders, and households with market-linked activities alike consistently say that their worst challenges are insecurity, bad roads, lack of demand in the markets, and an inability to fund their activities (World Bank, forthcoming). These are good priorities to tackle in early recovery; other constraints will become more important as peace stabilizes.

South Sudan has a window of opportunity to reconsider its growth path by putting in place measures to transition to a more diversified economy. The authorities recognize the need to diversify the economy and are already trying to rebrand South Sudan as a viable investment destination[iii]. While attracting FDI is desirable, in early recovery, the greater impact is likely to come from using budget spending to domestic investments for a broad jobs focused recovery. Considering its geographical and geological advantages, South Sudan has economic potential in non-oil sectors such as agriculture, fisheries, mining, and construction. To fully mobilize these sectors, there is need to restore greater security and begin to close a huge infrastructure gap—a key constraint, which requires mobilizing revenues, improving expenditure composition and efficiency, and regaining confidence with donors and investors. It is also important to support a recovery of demand in the markets and help farmers and others make the small but crucial investments needed to resume production.

The Government can do much more for jobs by using oil revenues in non-oil sectors than in continually trying to develop the oil value chain. The oil sector is capital intensive and entails enclave activities with

minimal linkages to the rest of the economy, and limited direct impact on jobs. National content provisions based on an assessment of where in the oil value chain South Sudanese businesses may become competitive could create some future opportunities and some indirect jobs. However, job creation would likely be limited and take time. By way of contrast, the Government has the opportunity today to broadly support jobs in recovery by better investing oil revenue.

3. Fiscal Policy

Fiscal policy is dependent on oil revenue, spending is pro-cyclical, and lacks an orientation toward productive investment. South Sudan's national budget is almost entirely funded by oil revenue receipts. With the establishment of the National Revenue Authority (NRA), a reform process is underway with the goal of increasing the contributions from non-oil tax revenues, but the impact is not yet clear. With no mechanisms in place to buffer fluctuations, budget expansions and contractions closely follow oil revenue receipts, and fiscal policy is procyclical. Budgets are opaque and a large proportion of oil revenues does not go into the budget. In consequence, public investment in a jobs agenda is limited, despite the enormous investment needs. Extra-budgetary expenditures and financing shortfalls due to unaccounted-for advance oil sales lead to a continuous accumulation of domestic arrears and complicate budget and debt management. Budget indiscipline, allocation priorities, and corruption compromise economic recovery in the short term and are not aligned to delivering a jobs agenda in the medium term.

Budget allocations are only loosely related to actual spending. Recent budget execution reports indicate large discrepancies between budgeted and actual spending. As mentioned, in addition to this difference, there is much extra budgetary spending. Although this has often led to the accumulation of arrears, expenditures continue to be concentrated in three sectors largely related to public salary expenditure, namely, security, accountability[iv], and public administration. Capital spending remains limited. Consequently, South Sudan continues to under invest in sectors that would have the largest knock-on effect on poverty reduction and building resilience, building a stock of physical and human capital, and creating jobs.

Table 2: Mismatches between sector budgets and outturns

	FY2018/19 sector allocations		FY2018/19 outturns (based on 9 months)	
	SSP billions	% Budget	SSP billions	% Expenditure
Security	15.5	19.21	38.4	40.8
Accountability	28.5	35.45	26.6	28.3
Public Administration	15.4	19.14	13.8	14.7
Social & Humanitarian	0.2	0.29	5.9	6.3
Rule of Law	4.6	5.76	5.2	5.5
Education	7.6	9.48	2.1	2.2
Infrastructure	2.8	3.42	0.7	0.7
Economic functions	2.9	3.58	0.5	0.5
Nat Res & Rural Dev	1.2	1.43	0.5	0.5
Health	1.8	2.23	0.4	0.4

Source: Approved Budget Tables, FY2019/20, Ministry of Finance and Planning

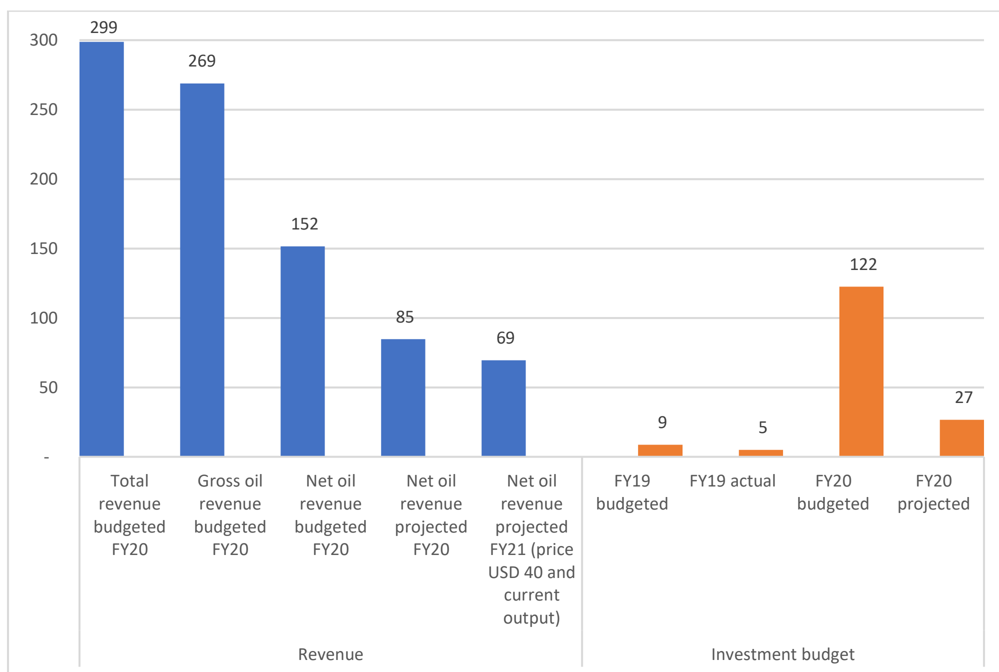
Despite arrears in public sector salaries, much spending goes toward security forces and public administration, with little spending on investment projects. While recent budget allocations indicate an

ambition to shift from security and defense spending to a more diversified expenditure plan, actual budget executions show that the security sectors still absorb a large share of the budget. For instance, the security sector had been allocated 19% in the FY2018/19 budget but received 41% of total resources in the first 9 months of the fiscal year. By way of contrast, spending on health and education was significantly less than budgeted (table 2). Spending on service delivery thus remains limited, and South Sudan continues to underinvest in sectors that would help prevent an erosion of education levels due to the conflict, and that have the largest knock-on effect on poverty reduction, building resilience, and human capital development. In addition, allocations to sectors that would unlock the productivity of the non-oil economy such as in agriculture and rural development is limited. In this regard, the revitalized agreement on the resolution of conflict (R-ARCSS) envisages the creation of enterprise development funds, which would work through private sector associations to improve productivity through capacity enhancement and easing access to financing. However, these are not yet operational. Thus, the fiscal outlays are not supportive of a job-focused development agenda.

Poor budget execution has been exacerbated by lower revenue going into the budget with FY20 government spending on infrastructure and service delivery estimated to be lower than budget. The FY20 budget envisaged increased spending on roads infrastructure that would be operationalized through an oil-for-roads deal with a daily allocation of 10k – 30k barrels approved for this purpose. With these arrangements, allocations to infrastructure accounted for more than 50% of FY20 budget. However, estimates from official data indicate that under execution challenges are more pronounced for capital and service delivery items. Capital spending is projected to be 22 % of budget, with significant under-execution in key sectors such as infrastructure (13%), health (27 %), social and humanitarian (9%), and education (73%). By contrast current spending is projected to be 186% of budget, with accountability (483%), rule of law (345%), public administration (193%), and security (113%) all spending significantly above budget.

Amid the Covid-19 pandemic, the FY2019/20 budget deficit has widened with large shortfalls for both oil and non-oil revenue. The FY20 budget envisaged gross oil revenue receipts of about SSP 269 billion (US$1.7 billion) and net oil revenues of about SSP 152 billion (US$ 942 million) with the difference being statutory deductions, including transfers to Sudan. However, with the recent plunge in oil prices, estimates show that gross oil revenues will likely turnout at SSP 209 billion (US$1.3 billion) with net flows into the budget amounting to SSP 85 billion (US$ 527 million), leading to a shortfall of about US$ 415 in FY20 budget on oil revenues alone (Figure 2). At the same time, non-oil tax revenues are expected to turn out 3 percent lower than budgeted, with a short fall of about US$ 4.7 million. With these developments, coupled with current budget overspending, the fiscal deficit is expected to reach US$ 510 million (8.5% of GDP) from US$ 166 million (3% of GDP) that was in the budget.

Figure 2: Government revenue and investment budget (bn SSP)



Budgeting oil revenue at the parallel market rate would provide more funds flowing into the budget in SSP terms, alleviating some of the pressure on the resource envelope. South Sudan expects to export about 175,000 barrels of oil per day in FY2021. While a significant amount of this will be used for in-kind settlement of the Transitional Financial Assistance owed to Sudan as well as well for pipeline transit fees, this reform would provide immediate relief on the budget leading to greater available resources for investment and payroll expenditure. The savings on this exchange rate reform would more than double the amount of resources available for both consumption and investment spending. To illustrate, assuming an oil price of US$ 40 per barrel in FY21 would translate into net oil revenues of about SSP 71 at an official exchange rate of 164 and the planned SSP 44 billion expenditure on the payroll would be 62% of expected net oil revenue. However, if oil revenue were budgeted at a parallel market rate of 335, net oil revenue would reach SSP 144 billion and the payroll expenditure would be 30% of net oil revenue. With South Sudan authorities struggling to meet budget obligations and salary arrears well in excess of six months by June 2020, there would be sufficient funds to pay salaries, settle outstanding arrears, and increase capital investment – contributing to aggregate demand and jobs.

In the short-run, security expenditures will dominate the budget, but the government hopes to shift spending toward development priorities over the coming three years. In the foreseeable future, however, the Government will continue allocating sizeable resources to the security, rule of law, and accountability sectors. This is consistent with the enormous fiscal burden of peace and security related expenditure, and the expenditure associated with the revitalized peace agreement. The expected higher oil revenue arising out of higher production will likely not be realized as prices have collapsed, and will be insufficient to cover initial peace-related costs as well as meet other expenditure needs. However, over the medium term, the Government aims to align expenditures to the National Development Strategy whose major focus is consolidating peace, delivering basic services, and economic stabilization. If

implemented the strategy will see an increased focus on (i) creating conditions for and facilitate the voluntary return and integration of displaced South Sudanese; (ii) developing appropriate laws and enforce the rule of law; (iii) ensuring secure access to adequate and nutritious food; (iv) silencing guns by facilitating a permanent cessation of hostilities; (v) restoring and expanding provision of basic services; (vi) restoring and maintaining basic transport infrastructure such as roads and bridges. Accordingly, the strategy is expected to guide the country's public investment plan over the next three years and will ensure that public investment responds to the most immediate and crucial needs of the economy. Of course, this is subject to a robust implementation and execution strategy.

Taking steps to improve public financial management and putting in place a credible reform strategy will be critical to improve the effectiveness of fiscal policy. In the short term, this may involve improving cash management and the introduction of short-term notes for cashflow management purposes. Efforts to improve government's audit and anti-corruption functions, as well as streamlining procurement and the payroll, including management of the wage bill and arrears would be necessary to safeguard public resources. Over the longer term, fiscal policy management could be strengthened by the adoption of an indicative reference multi-year expenditure framework, consistent with the national development plan/strategy. However, this would require authorities to first and foremost build capacity and put in place a credible macro-fiscal framework, as well as tools for forecasting a range of targets including revenue, expenditure, and output.

Improving the business environment for jobs creation would require unlocking the largest constraints on business survival, growth, and competitiveness. South Sudan's investment climate continues to be constrained by inadequate provision of public capital and subdued demand. In the context of limited service delivery, budgets have fed the state's predatory consumption with the effect that capital investment is not funded. Consequently, there is a disconnect between fiscal policy and growth. Increasing expenditures on for service delivery, paying salaries, and starting the transition to spending on capital goods will help to unlock some of the binding constraints in the business environment and help firms grow, expand, and create jobs.

4. Public employment

Public employment plays a large role, with some 400,000 soldiers and police, and about as many other civil servants as there are workers in established businesses. The public sector accounts for the largest share of formal sector employment in South Sudan. This is not surprising given the non-diversified structure of the economy with few formal private sector employment opportunities. In FY 2019/20, the national-level civil service consisted of 449,343 personnel[v]. The roughly 50,000 public employees outside of the armed forces and police are about as many as all urban workers in established businesses (formal or not), and equivalent to about 4% of the estimated urban labor force. Consequently, public employment plays a critical role in South Sudan's labor market, as well as in sustaining demand in the markets for goods and services. Public employment is dominated by the security and rule of law functions, which employ nine in ten public sector employees (91 percent). Of these, most (78 percent) are in the army, and 12 percent in police and prisons services – as compared to three percent in the education and health sectors combined (see table 4). The FY2018/19 expenditure outturns indicate that security sector salaries accounted for 61 percent of the total national wage bill excluding arrears payments, and 71 percent if combined with police and prison services.

Public employment is often a form of patronage, but has an important redistributive function. The general perception is that the recruitment as well as allocation of positions among existing staff is driven by political and kinship considerations, more than merit. Patronage and loyalty play a role in employment appointments at all levels, including in the non-technical and support functions. Furthermore, public employment plays an important redistributive function, as many of those receiving a regular salary support a significant number of dependents: at the median, households with a worker who is on the public payroll (in the armed forces or beyond) have seven members, and no other income-generating activity (World Bank, 2020a). The fastest and most significant expansion in public employment occurred in the organized and armed forces. The South Sudanese armed forces grew from an estimated 90,000 in 2005 to about 200,000 in 2015 and 330,000 in 2018. At the same time, the civil service has a considerable number of staff employed in un-approved positions, usually considered to be support staff.

The dearth of skilled personnel is a major hinderance to productivity in public sector employment and may become a constraint on formal employment in general if recovery succeeds. The pool of educated citizens from which public sector staff can be recruited continues to be quite limited but should be just large enough to allow the recruitment of qualified staff. South Sudan has one of the lowest literacy rates in Africa, explained by low availability, access, and quality of education. In 2016, only about 4 in 10 people reported being able to read and write. While this constitutes an improvement over the 2009 rate of about 3 in 10 (29 percent), it still performs among the lowest in Sub-Saharan Africa (World Bank, 2017a). The quality of education continues to be a challenge and school enrolment rates are very low.

Table 3: Distribution of public employment and wages

Spending agency	No. of Employees	% Employees	% Wages
Accountability	2,097	0.5	9.6
Economic functions	4,748	1.1	1.4
Rule of Law	60,956	13.6	12.7
o/w police and prisons	53,904	12.0	10.1
Public administration	6,213	1.4	7.1
Infrastructure	2,042	0.5	0.3
Social and Humanitarian Affairs	1,596	0.4	0.7
Health	5,034	1.1	1.2
Nat. Res. & Rural Devt	9,927	2.2	1.6
Education	8,363	1.9	4.2
Security	348,367	77.5	61.1
Total	449,343	100.0	100.0

Source of data: FY 2019/20 Budget, Ministry of Finance and Planning[vi]

The recent return to 10 states may have led to job losses at the sub national level, but the extent is not yet clear given that the reorganization of structures is not yet complete. While a hiring freeze had been formally in place since 2012, the increase in the number of states in 2015 first to 28 and later to 32 had come with more hiring at the sub-national level, significantly expanding public employment as more administrative staff were recruited for each newly created unit, usually at the expense of service delivery (World Bank, 2017b). However, the recent return to 10 states may have led to job losses, as positions across many former states become redundant. While it is not clear the extent to which employees will be absorbed in the new state level structures, the new arrangements nevertheless provide a great

opportunity to streamline state-level employment, kickstarting a long-delayed process of cleaning the subnational payroll of ghost employees.

With no functioning pension scheme, few civil servants retire, making it difficult to add fresh talent under the hiring freeze. Further renewal and skill upgrading have been hindered in recent years by the extended recruitment freeze on the one hand and the absence of a public sector pension system on the other hand. Due to the recruitment freeze and the fact that current staff cannot retire on a government pension, there have been very few opportunities to employ newly qualified staff. Constraints to expanding staff numbers have been a particularly difficult issue in the health sector—which has generally suffered from a lack of prioritization among expenditures.

A major distortion in public service employment data arises from the inclusion of ghost employees in payrolls on a large scale. Reports indicate that the problem extends to ghost institutions including schools, hospitals and public service institutes with many ghost staff on their payrolls. While these challenges exist across all sectors, they are likely to be more pronounced in the security services (The Enough Project, 2017). In the police force alone, an audit carried out jointly by the UNPOL and UNDP unearthed more than 16,000 ghost police officers (31% of the police force at the time), reducing the police force from an estimated 52,000 to about 36,000 leading to substantial budgetary savings (UNDP, 2013). At the same time an armed forces (SPLA) led audit in the same year is reported to have discovered 40,000 ghost soldiers (The Sentry, 2015). While the current state of ghost employees across government departments cannot be established, there is an ongoing civil service headcount verification exercise across 70 public institutions. All appointments and promotions were suspended until the exercise is completed[vii]. This is intended to result into a payroll cleansing exercise under the public service reform envisaged in Chapter IV of the peace agreement.

Erosion of real wages and payment arrears have taken a toll on motivation, and diminished the role of civil servants as customers to local businesses. Motivation and incentives for public employment have been affected by the volatile macroeconomic situation and dire government fiscal position. Due to initial oil revenue wealth as well as learning from neighboring countries, the initial intention was to establish a well-paid but relatively small civil service, and wage levels were set relatively high in 2007 (World Bank, 2015). However, salaries have been undermined by inflation and real wages have been declining steadily. The current wage structure is no longer sufficient to provide a decent standard of living. Pay gaps are significant for certain employment groups such as nurses relative to pay provided by international nongovernmental organizations. At the same time, motivation in public sector employment has been affected by government accumulation of civil service arrears. By May 2019, civil service salaries were in arrears of four months, transfers to states were in arrears of 5 months, and foreign diplomatic missions were in arrears of up to 14 months. In addition, unrealized budgetary allocations mean that many public sector departments can barely meet the minimum running costs, paralyzing government services.

Many highly qualified public servants cope by leaving service to work in the humanitarian sector, and many who remain in public employment work other jobs on the side. Many public servants, particularly the professionals, have left their roles to find employment elsewhere. Many of them have been absorbed into the humanitarian sector, while others have sought employment in private enterprise or emigrated to other countries, bleeding the public service of much needed technical capacity. Those who have stayed have significantly scaled back on effort, compounding an already alarming public service situation. Many public servants make up for the lost incomes by using government assets to make a living and by extracting

rents. Consequently, the public service is burdened by low capacity, inefficiency, and rent seeking with limited motivation to deliver services.

Low morale has come with a loss of public sector ethics, and has led to an increase in bribery and extortion, with a very large attendant burden on the public. Besides reducing motivation and public service delivery efficiency, unpaid civil service salaries are likely to lead to corruption in the form of informal taxes/payments for public services. In addition, where public services are not provided, the cost of making alternative private arrangements increases the cost of doing business with implications for private sector profitability and demand for jobs. There are numerous reports detailing illegal security checkpoints at which traders are harassed and extorted for informal payments along major trade routes. The cost of such payments is huge and was estimated to be as high as 8 percent of the value of goods (Pape et al. 2017).

5. Inflation developments

Since the beginning of conflict, the consumer price index has increased by 5,680% – a 58-fold increase in prices over 7 years. South Sudan experienced very high inflation, particularly during 2015 – 2018 as the country grappled with the consequences of conflict and macroeconomic collapse. During that time, inflation rose to 550 percent at its peak, fueled by monetization of the fiscal deficit, exchange rate depreciation, and conflict-induced domestic supply constraints. To date, inflation remains high. In late-2018 and early 2019, inflation declined to a range of 20-50 percent, on the back of a significant decline in money and exchange rate growth, highlighting the close link between money supply, exchange rate developments, and inflation. However, by October 2019, price levels were growing again at up to 170%, before declining to 40% by March 2020 as the exchange rate maintained some stability.

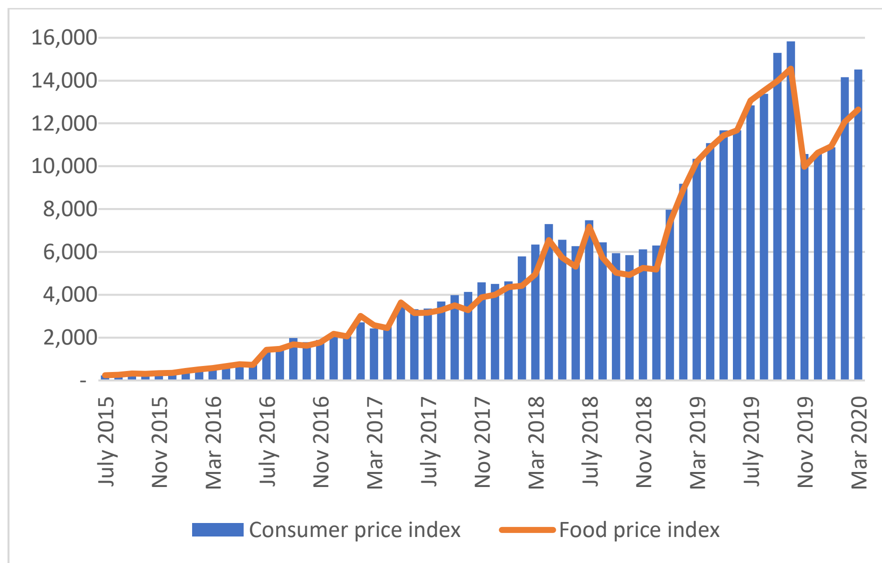
The rise and fall in inflation have tracked the degree to which the Government has monetized the budget deficit. During 2016 and 2017, monetization of the budget deficit led to strong money growth, with the result that inflation accelerated. Before it started to decline, the rate of money growth had risen considerably, reaching a peak in June 2016, at 223 percent. Since then, the Government has eased the monetization of the deficit, and by November 2018, growth in broad money had continued to decline, reaching a rate of 38 percent (year-over-year). Thus, the reduction in inflation in the first half of FY2018/19 (declining from 122% in July 2018 to 40 percent by December 2018) partly reflected reduced central bank financing of the budget deficit. However, the downward trend was not sustained in the second half of FY2018/19, with inflation estimated to have increased to 86 percent in June 2019. By October 2019, inflation is estimated to have risen further to 170 percent, its highest level for more than 18 months.

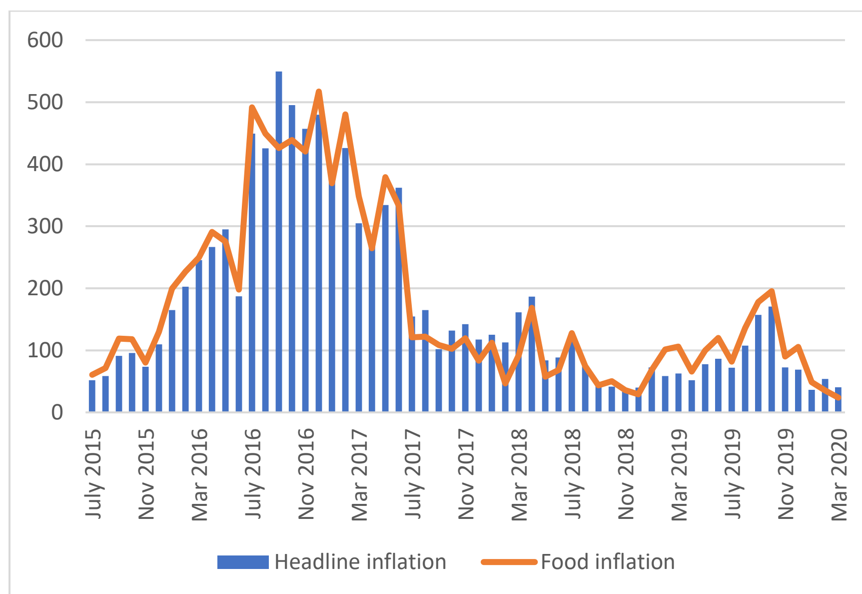
Because of foreign exchange pass-through, inflation also reflects changes in confidence in the South Sudanese economy. Given that South Sudan is an import dependent economy with limited domestic production capacities, exchange rate passthrough to domestic prices is high: changes in the inflation rate move together with changes in the rate of depreciation. For instance, when inflation slowed in the second half of 2018, the SSP, which had lost so much value to on the parallel market started to strengthen, driven by growing confidence in the economy and the positive impact of peace on trade and the functioning of markets.

Conflict, drought, and floods have taken a profound toll on food production, contributing in turn to inflation. Disrupted agricultural production, trade, and climate change induced losses have affected food

supply, destroyed livelihoods and agricultural jobs, and led to high food prices. However, food price pressures started to dissipate following the singing of the peace agreement in September 2018. The pressure on prices of basic food crops, including maize, sorghum, wheat, cassava, and groundnuts started to dissipate during the second half of FY2018/19, after having reversed the sustained upward trend experienced in much of FY2017/18. The prices of a kilogram of beans and a litre of vegetable oil reduced by 25 percent in June 2019 compared to June 2018, continuing a downward trend that started in March and April 2019 respectively. Likewise, the year-on-year increases for the prices of beef, fish, and rice have been declining in the second half of FY2019.

Figure 3: Consumer Price Index, June 2011=100

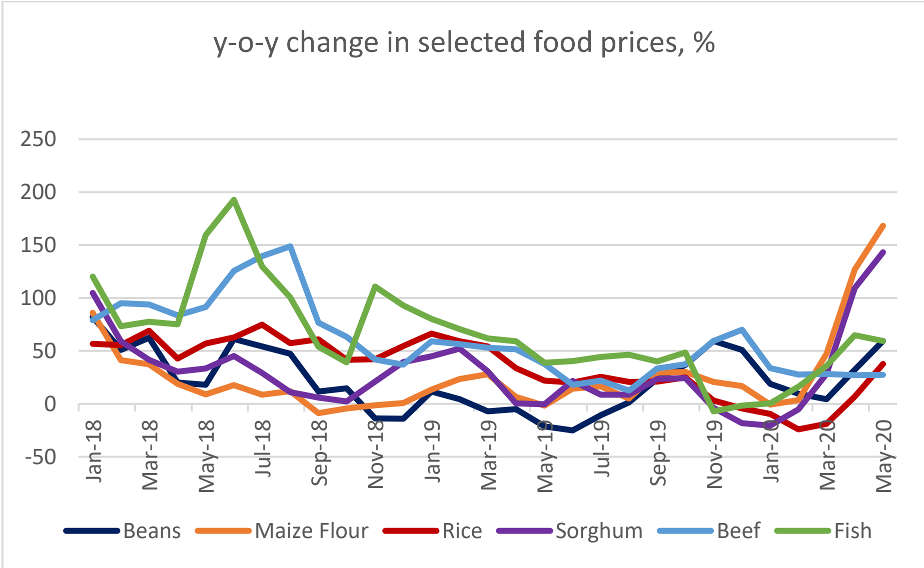




Source: National Bureau of Statistics, Bank of South Sudan

The pressure on food prices dissipated somewhat following the signing of the peace agreement in September 2018, but the trend reversed starting in early 2020 with covid19 containment measures disrupting supply chains and trade flows. The declining food inflation following signifying of the latest truce reflected the effects of increased trade flows, better access to markets, and recovering domestic production. However, covid19 related disruptions to trade, supply chains, and longer travel time have contributed to higher prices for essential commodities since the first quarter of 2020. By May 2020 Juba market prices for basic food stuff had risen by about 40-150% (annualized monthly change) possibly highlighting the effects of the containment measures introduced in late March. Although borders remained open to commercial traffic, the covid19 related screening processes put in place resulted in slower cargo movement, with volumes passing through Nimule reportedly falling by between 50-70% by April 2020[4]. At the same time widespread insecurity, disrupted production, disrupted markets, and weak local currency continue to have an adverse effect on prices, negating the would be supply response. To illustrate how vulnerable prices are to structural and macroeconomic shocks, the year-on-year change for the prices of beans rose from 5% in August to 65% in November 2019 due to the combined effects of floods that affected parts of the country and strong depreciation of the SSP against the USD during that period.

Figure 4: Covid19 related measures have led to a sharp rise in food prices



Source: Climis Database - http://www.climis-southsudan.org.

Inflation is a symptom of conflict and economic decline, but it also poses a very important obstacle to business activities at all levels. Inflation has taken a serious toll on livelihoods (Pape et al. 2018). Surveys conducted in 2019 show that households, market traders, and more established businesses alike view the rapid price changes as a serious problem, and that they reduce or stop their activities because of the difficulty of coping with inflation (World Bank, 2020a, 2020c, 2020d). The literature provides evidence that macroeconomic instability negatively affects firm level outcomes, with implications for labor demand. Inflationary pressures that result in input price hikes, for example, have been shown to affect business sentiment (Mawejje and Sebudde, 2019), investment and productivity growth (Fischer, 2016), thus affecting private sector demand for jobs. Therefore, sustained efforts aimed at reducing inflation and

[4] Correspondence with WFP staff.

ameliorating the overall macroeconomic environment are vital for supporting a jobs-centered recovery and growth agenda in South Sudan.

The key steps to stabilizing prices are stopping monetizing deficits, exchange rate stabilization, greater peace, and a recovery of food production playing a critical role on the supply side. The Government's key policy lever to control inflation is to abstain from monetizing budget deficits and restore independence of the central bank. This would go hand-in-hand exchange rate stabilization as the central bank resumes auctioning forex with the full participation of commercial banks, in addition to forex bureaus. In the medium term, these short-term policy needs to be then complemented by the adoption of a target for monetary policy and an intermediate target, adequate for countries with an underdeveloped financial sector. In the longer term, however, the control of inflation is complicated by inadequacy of central bank capacity to influence the transmission mechanism. This would be strengthened as the financial sector develops and the treasury bills market becomes fully operational. On the supply side, greater peace and stability would help a resurgence food production and allow for a gradual return of confidence economic prospects, and hence, less pressure on the exchange rate. These crucial developments would undoubtedly remove some of the worst pressure on prices.

6. Exchange rate policy

Access to foreign exchange is hard to understand fully, but the wide spread between the official and parallel market exchange rate causes some distortions that matter for jobs. Since independence, the SSP has depreciated by more than fifty-fold on the official rate, reflecting the destruction of much economic activity as well as money growth. The exchange rate has fallen from 2.95 SSP/USD at independence to nearly 164 SSP/USD in June 2020. At the same time, the gap between the parallel and official exchange rates was 105% as the conversion rate for 1 USD reached 335 SSP. With low foreign exchange reserves, there is little access to USD at the official rate even for formal businesses and commercial banks. Because there is no good information on who can access USD at the official rate, and how much, it is hard to assess the impact of exchange rate policy on economic activity and jobs. Those impacts that are certain are (i) the opportunity for rent-seeking due to the dual exchange rate, (ii) the fiscal consequences of budgeting USD-denominated oil revenue at the official rate, and (iii) low effective customs rates due to valuation of imported goods at the official rate. Overvaluation of the official rate in principle makes domestic production less competitive with imports, and sets incentives against foreign investment. But because businesses in practice may not buy USD at the official rate, it is not clear whether these impacts currently materialize.

At independence, South Sudan adopted a fixed exchange rate policy but conflict and collapse of oil revenue made it difficult to maintain. The exchange rate was arbitrarily fixed at 2.95 SSP/USD - the rate that prevailed at the time of secession from Sudan - and not necessarily determined by the economic circumstances of the newly-independent Republic. At the time, a fixed exchange rate regime was possible because the oil sector was booming, and South Sudan enjoyed a healthy balance of payments position that allowed accumulation of reserves. The economic situation changed significantly in the years that followed independence. The country had to deal with both internal and external shocks that affected both the balance of payments and fiscal balances. The resumption of civil conflict in December 2013 caused higher spending on defense and security operations, leading to a widening of the fiscal deficit. Oil production was disrupted, significantly affecting the flow of revenue. In addition, the collapse of oil prices

from over $100 per barrel in 2013 to nearly $30 in 2015 exerted more pressure on an already fragile government fiscal position.

By 2015, loss of confidence in the economy led to development of a parallel exchange market as government's external position deteriorated. At the start of FY 2015, Government deposits and foreign reserves had deteriorated significantly, with net foreign assets of the central bank amounting to US$379 million, the equivalent of about three weeks of imports. In addition, the availability of external financing had been limited owing to high levels of country risk. With heightened investor risk perceptions, and a loss of confidence in the economy, the spread between the official and parallel exchange rate widened considerably and reached 530 percent in October 2015.

A managed float adopted in 2015 initially helped reconcile the official and black market rates, but was soon overtaken by further rapid devaluation. With these challenges the Bank of South Sudan adopted a controlled floating exchange rate policy on 15 December 2015. Consequently, the currency was devalued with the new official exchange rate set at 18.5 SSP/USD, equal to the parallel market rate. A more flexible, market-determined exchange rate was needed to help absorb external shocks and maintain the Bank of South Sudan's ability to use monetary policy to influence domestic economic conditions. Despite the change in exchange rate policy, the South Sudanese Pound (SSP) continued to depreciate on both the official and the parallel market. On the parallel market, the Pound depreciated from SSP 18.5 per dollar in December 2015 to SSP 70 per dollar by August 2016 and SSP 172 per dollar by August 2017.

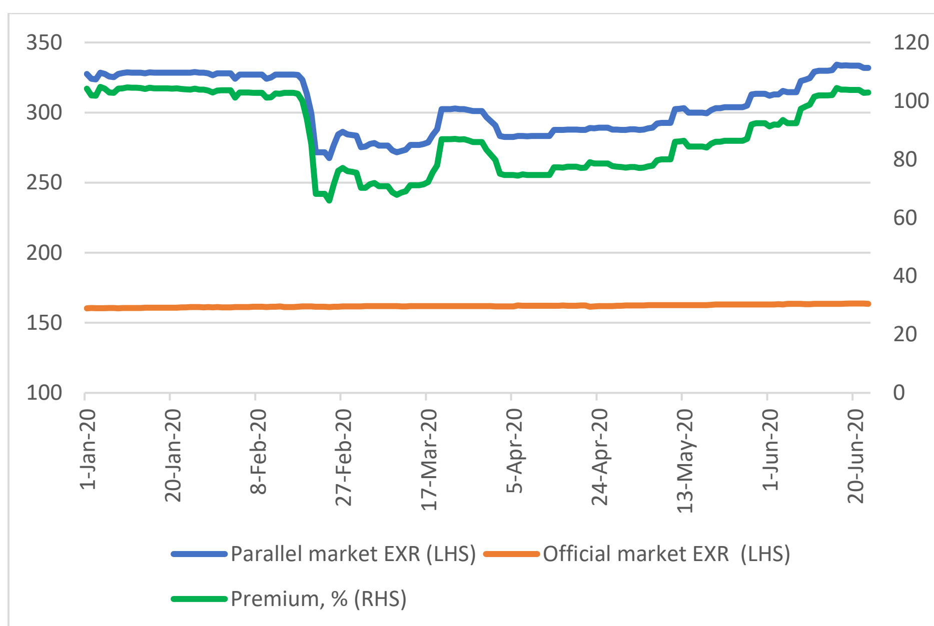
The current exchange rate policy that introduced provisions for special accounts lacks transparency and fairness in allocation of FX to the market. Since mid-2017, when the Bank of South Sudan introduced the "Special Accounts" scheme [viii], commercial banks have been required to immediately sell all the foreign exchange (FX) purchased from the special account holders to the BSS (both transactions should be at the official (indicative) rate), while banks have been allowed to subsequently repurchase 25 percent from the BSS. This exchange rate system and banks' surrender requirement to the BSS have contributed to a decline in FX inflows. Consequently, the exchange rate market is still beset with soaring premium, indicating that the official rate is overvalued and does not reflect the underlying economic fundamentals.

As of 2020, depreciation continued, but at a slower pace following formation of revitalized government of national unity, with covid19 related shocks leading to a reduction in import demand. Despite a brief appreciation in the three months leading to the signing of the latest peace deal in September 2018, the exchange rate has continued to depreciate and the spread between the official and parallel exchange rate widened further. However, the exchange rate appreciated on the parallel market following political events that led to the formation of the RTGoNU in February 2020 and maintained this position following the introduction of covid19 containment measures through March and April 2020, with the parallel rate averaging SSP 286 for each USD during this period. The demand for US$ probably dropped as traders of non-essential items were no longer able to open their stores, while the demand for SSP increased as citizens stocked up on food and essential items in anticipation of the wider lockdown and increased their precautionary holdings of SSP. However, recent trends indicate what may well be a market correction, with parallel market rate recorded at SSP 335 by the third week of June 2020 – its lowest value against the dollar since the start of 2020 (Figure 5). Over the medium term, a decline in inward remittances is expected to be a more significant driver of a deprecated market exchange rate, as the economic contraction in high-income countries home to South Sudan's diaspora affects incomes. However, the anticipated sharp fall in Government's foreign exchange receipts from oil may not have a big an impact

on the market exchange rate as government is understood to spend most of the forex it receives on its own operations and so sells relatively little into the market through auctioning to forex bureaus.

There are some standard implications of a distorted exchange rate, but it is hard to determine whether they materialize in South Sudan, since it is hard to know whether FX is traded at the official rate. Overvalued exchange rates are associated with shortages of foreign currency, rent-seeking and corruption, unsustainably large current account deficits, balance-of-payments crises, and stop and-go macroeconomic cycles – all of which constrain economic growth and jobs. In addition, exchange rate policies have large fiscal implications, particularly in countries where the government derives a substantial portion of income from windfall revenues, such as from exploitation of natural resource sectors or from aid. South Sudan is this type of country, where the indicative exchange rate is set below the market value and this is in principle a hindrance to investment. Money coming into the country has a lower local currency value and yet the factor inputs are priced at the higher exchange rate, leading to distortions that disincentivize investment and therefore job creation. At the same time, the current system has encouraged rent seeking because it entails a hidden transfer of resources from the government to individuals with privileged access to foreign exchange at the official rate.

Figure 5: Exchange rate developments



Source: Bank of South Sudan

In commodity exporting countries, such as South Sudan, competitive exchange rate policies play a crucial role in promoting diversification. From the point of view of both formal and informal investors, the exchange rate is a key determinant of the incentives facing domestic economic agents, because it influences the relative prices of both tradable and non-tradable goods. Indeed, economic theory shows that an overvalued currency makes imports too cheap, renders exporting unattractive, provides poor incentives for investors, and ultimately undermines confidence in the economic policy environment. In this respect, therefore, the exchange rate determines the flow and allocation of resources and how these

resources are invested. A competitive exchange rate policy enables the reallocation of domestic demand towards locally produced products and increase in foreign demand for locally produced goods. Therefore, exchange rate policies provide incentives for the nature of economic activities that evolve in the economy. Designing a jobs focused recovery agenda would require getting the exchange rate right as this will ensure the competitiveness of the domestic tradable sectors.

In addition, the type of exchange rate regime adopted has monetary policy implications, and therefore has a large influence on how the central bank operates, as well as the nature of its balance sheet and its financial strength. Maintaining a sound financial sector and price stability is a core objective of the central bank. The challenge facing the Bank of South Sudan in the conduct of monetary policy is the inadequate tools at its disposal. The interbank market and market for treasury bills is not developed and the central bank worries about the cost of monetary policy. Therefore, the means available to sterilize money growth are limited. With these challenges, the efficacy of the Bank of South Sudan in ensuring price stability is limited. The central bank would wish to diversify its monetary policy instruments by introducing treasury bills, the interbank market, and the time deposit facility. While the FX auction mechanism has been re-instated, the central bank does not get enough forex to auction limiting its effectiveness. From a jobs perspective, it is important that the central bank developed a FX policy that can ensure price stability and provide the right incentives for enterprise competitiveness.

However, devising the right policy prescriptions will depend on the ability to determine how much access to FX there is in the market. The issue of completely liberalizing the exchange rate is contentious and still requires an in-depth diagnostic of the exchange rate dynamic. Discussions with key policy makers indicate a deep reservations about changing the status quo, and this seems to derive from past experience when earlier such efforts led to dire consequences with a spiraling premium and loss of confidence in the SSP. Good policy advice will require understanding the degree to which there is access to FX at the official rate: if FX is traded at the official rate, devaluation might have much broader consequences in the real economy.

Dutch Disease effects are apparent, but the exact magnitude is not entirely clear as little revenue from the oil sector is spent through the budget. Recent estimates show that the share of oil revenues that reaches the budget has ranged between 5% and 45%. The rest is payment to Sudan, Nilepet's share, and for oil advances. These are from official data and it is not clear if this reflects the entire oil production or how the funds are distributed. However, given the size of the oil sector – as well as ODA inflows - we cannot completely discount the likely Dutch disease effects on exchange dynamics. Empirical evidence on this issue generally suggest that substantial exchange rate overvaluation has a strong negative impact on growth of the tradable sectors (Brahmbhatt, 2010), affecting firm survival, productivity, and demand for jobs which move to lower cost countries (Baggs, Beaulieu, and Fung, 2009). These effects are apparent where the majority of tradable items in the markets, including agricultural products, are imported from neighboring countries. While recent survey carried out across major towns indicate that wages for manual labor are no longer elevated, there may still be high wage expectations in some high-skilled niches.

Overall, exchange rate distortions are symptoms of wider economic mismanagement, but poses very pertinent challenges for business survival and competitiveness – affecting the demand for jobs. To address these challenges, a proper understanding of foreign exchange dynamics and more clarity on USD flows is necessary to responsibly develop policy proposals. However, as a first step, authorities in South Sudan should take steps to unify the current multiple exchange rate system and allow the exchange rate

to be market determined. This will help address external imbalances, improve resilience to shocks, encourage investment, and will allow more revenue into the budget. In addition, the resumption of exchange rate auctions for commercial banks and taking measures to replenish central bank reserves (for example using some of the oil revenue receipts) would support exchange rate stabilization. These measures would then have to be accompanied by appropriate policy actions and public investments that would unlock the structural constraints to business survival and competitiveness, including improving: access to credit, availability of reasonably priced and reliable electricity, efficient transport, communication technologies, and human capital development. These would enhance the response of the economy to competitive and stable exchange rates.

However, there are short run tradeoffs associated with pursuing a competitive real exchange rate policy, including lower wages and higher import prices. A more competitive (undervalued) real exchange rate would lead to higher import prices in local currency units. This would therefore lead lower real wages and incomes in the present, but with the objective of achieving higher real wages and incomes in the future (Guzman, Ocampo, and Stiglitz, 2018). However, in as far as the domestic production of tradable goods also has domestic contents, the profitability of the business sector will increase. But the development of sectors that eventually become internationally tradable may take time.

7. Financial sector development and access to formal forms of finance

South Sudan's financial sector is small and undeveloped. While the banking sector experienced dynamism and growth during the period after independence, progress stalled and even reversed because of cycles of conflict and economic tensions since 2013. There are 30 commercial banks operating, five of them foreign-owned. However, access to financial services is limited, and only 13% of the population own a bank account. In addition, many small banks remain undercapitalized. Capital markets do not exist. The interbank market is far from vibrant, with a few isolated transactions.

Table 4: Selected financial sector indicators

	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
Credit, % GDP	1.1	1.2	1.7	1.7	3.7	1.4	1.2	1.0
Deposits, % GDP	9.1	6.7	10.2	14.3	33.9	20.7	13.1	10.2
Credit, % deposits	12.5	17.8	16.7	11.7	10.8	6.9	9.3	10.3

Source: World Bank staff estimates

Levels of intermediation and private sector credit are negligible. The recurrence of conflict and subsequent collapse of the economy resulted in many banks scaling back operations and closing branches outside of Juba. Consequently, the financial sector has limited reach outside the capital. At the macro level, both credit and deposits as a percentage share of GDP have been declining over the past four years reflecting the turbulent economic situation. Credit as share of GDP declined from 3.7% to 1.0% and deposits declined from 33.9% to 10.2% over the period 2016 – 2019 respectively. In addition, credit as a percentage share of deposits, which is estimated at about 10.3%, is very low. These data reflect a minimal level of financial intermediation.

On the demand side, access to finance continues to be a major constraint to entrepreneurship, business growth, and firm competitiveness with likely negative implications for labour demand. The National Bureau of Statistics, Integrated Business and Enterprise Survey (2019) indicate that 44% of sampled firms reported having an SSP checking account and 10% have a foreign currency account. However, firms essentially do not use the formal financial system to access finance and hardly any businesses take formal loans - even among large firms. Only about 3% of firms have taken a bank loan over the past three years, and even among large firms, this share is only 6 percent. Similarly, businesses say they cover losses from shocks through loans or gifts from family and friends (67%) or using earnings or cutting salaries (30%). A mere seven percent said they had borrowed from a bank, again with no higher use of credit among large firms. While almost all loan applications require collateral, whose value is usually more than double the loan value, the land market is undeveloped, further constraining access to finance. In addition, property rights are not established and legislation allowing the use of chattels does not exist.

Table 5: Access to finance

	All businesses	**Micro businesses (up to 3 workers)**	**Small businesses (4-5 workers)**	**Medium businesses (6-9 workers)**	**Large businesses (at least 10 workers)**
% with an SSP checking account	44%	37%	57%	67%	84%
% with a foreign currency account	10%	6%	15%	26%	42%
% have taken a formal sector loan in the past three years	3%	2%	5%	7%	6%
% of businesses that took a formal sector loan to cope with a shock (among all businesses that experienced a shock)	7%	5%	8%	11%	15%
% of businesses that borrowed from family or friends to cope with a shock (among all businesses that experienced a shock)	67%	70%	64%	54%	44%
Number of businesses	*13,184*	*9,199*	*2,548*	*538*	*854*

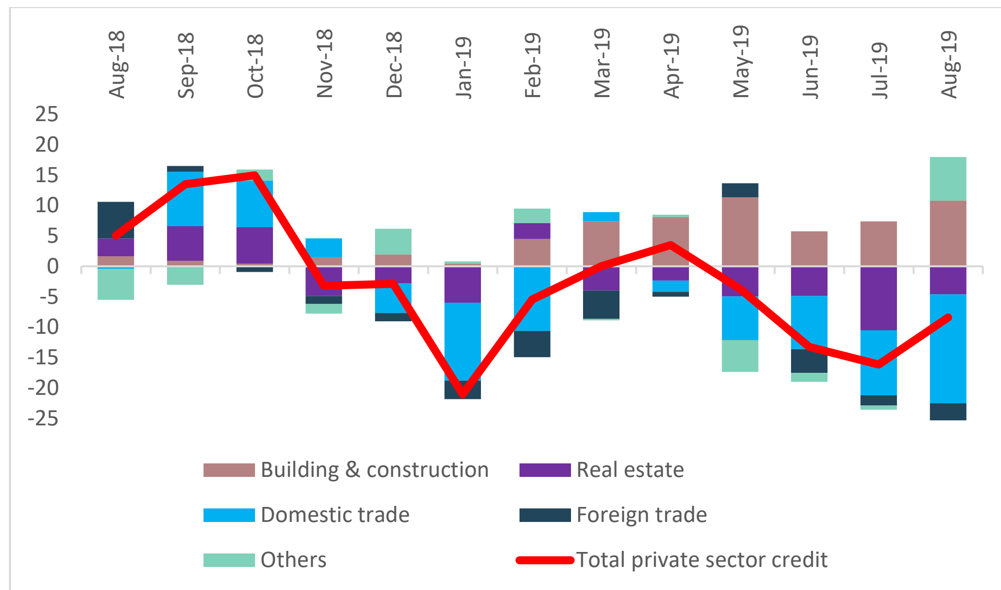
Source: National Bureau of Statistics, Integrated Business and Enterprise Survey 2019

Even beyond the formidable obstacles of conflict and economic risk, lending is further complicated by difficulties in the use of collateral. Banks are reluctant to lend against leased land, as there is no clarity about asset ownership and assets cannot be attached for foreclosure because the land owner (who is not typically the borrower) is the ultimate owner of the asset. This stifles economic activity and banking intermediation, as entrepreneurs and businesses end up either postponing capital purchases or using own savings to meet financing requirements.

Credit conditions are dire and real private sector credit growth is weak, with growth only in the buildings and construction sector. Real private sector credit expansion had slowed considerably since FY2014, with its rate of growth effectively negative for all but two months during July 2013 – July 2018 and contracting

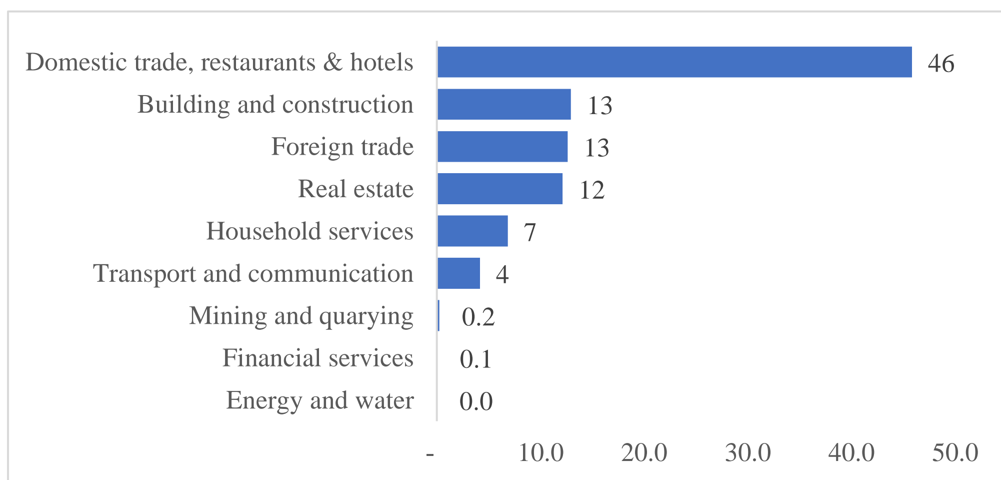
on average by 25% per month. This trend was reversed briefly starting in August 2018, with private sector credit growth averaging 11% in the first quarter of FY 2019 and reaching a growth rate of 15 percent in October 2018 from a contraction of 26 percent in July 2018. However, this growth was not sustained, and real private sector credit contracted in four successive months during November 2018 – March 2019 and during May – August 2019 (Figure 6). Solely the contribution of the building and construction sector to real credit growth has been positive and averaged seven percent during the period January – August 2019 despite its small share in total bank lending, signifying strong growth in this sector. Overall, the weak growth in real private sector credit growth is consistent with the lack of growth in the non-oil sectors over the past period.

Figure 6: Real private sector credit growth is weak



Source: Bank of South Sudan

Figure 7: Distribution of private sector credit (percent of total, FY 2018-19)



Source: Bank of South Sudan

There is virtually no lending for agribusiness and manufacturing. In South Sudan, there is very little employment in the kinds of formal businesses that could take bank loans. In addition, in an environment with as much risk, it is usually activities with the very highest short-run yields that attract any investment, and these do not tend to be labor intensive. It is noteworthy that trade, hospitality, real estate, and building & construction sectors accounted for more than 80 percent of all bank lending in FY2018/19. By contrast, the manufacturing and agricultural sectors accounted for negligible shares of private sector credit. There is therefore little indication of formal sector investment that could begin to reverse the current weakness of these two sectors. This is particularly disconcerting as agriculture accounts for two thirds of all jobs, and is the primary source of livelihood for more than 8 out of 10 households (World Bank, forthcoming). If greater stability returns, it will become essential to address the supply and demand-side factors that constrain agriculture credit. Supply factors include weak institutional framework and an undeveloped financial sector. Demand side factors include lack of collateral, a dearth of bankable projects, high risk associated with agricultural credit, missing agricultural insurance markets, and limited financial literacy.

III. Policy implications

Addressing the underlying causes of the conflict and restoring peace and stability in line with the provisions in the peace agreement is an absolute prerequisite for recovery and jobs. The protracted conflict has had a devastating effect on the economy and undermined the capacity of institutions to deliver basic services. Results from a survey of businesses and enterprises in major town across the country indicate that insecurity is the leading issue cited as a 'serious' or 'very serious' problem (40%), in line with the nearly universal experience of conflict impacts on businesses (World Bank, forthcoming). Conflict has affected virtually all surviving businesses, through loss of customers and assets, closures, and barriers to investment. At the same time, informal taxation at checkpoints is thriving in a conflict economy, which stifles economic activities. Rebuilding the economy in a way that provides inclusive access to economic opportunity and jobs will be a slow and onerous process. However, what is important at this stage to is to make every effort to break the cycle of conflict and to usher in a new era of sustained stability.

Improving transparency in oil revenue management would ensure that oil revenue flows into the budget, providing the wherewithal for higher productive spending. The share of oil revenue that enters the budget has been in the range of 5% and 45% between FY2018 and FY2020, the rest is payments to Sudan, Nilepet's share, payments towards oil advances. In particular, oil advance payments should be stopped as they are non-transparent, complicate budget management, and are likely to be abused. In addition, improving transparency around Nilepet operations, including completion of annual audits of its financial statements and transfer of profits to the Government of South Sudan fiscal accounts should be a priority.

Pursuing a public investment program that prioritizes, first stabilization, and bridging the large human capital and infrastructural deficits is key. Building on the National Development Strategy which focuses on security, stabilization, and provision of basic services, the government should prioritize investments to improve the productivity in key growth sectors and reduce the cost of doing business in the private sector. Accordingly, as a first step, government should develop a Public Investment Plan and gradually build capacity in project preparation, implementation, monitoring and evaluation. This way, the authorities can

strengthen value for money and ensure that investment projects yield the expected growth and jobs dividend

Macroeconomic stabilization with the aim of restoring price stability and reducing monetary, fiscal, and balance-of-payment imbalances is urgently needed. The revitalized peace agreement provides a broad set of reforms outlined in its chapter 4. These reforms are important but would require a carefully thought out sequencing. Addressing exchange rate distortions would improve the business environment and contribute to a competitive non-oil economy that would support a jobs focused recovery. In addition, it would ensure that more funds flow into the national budget from oil exports, which would then be strategically invested to address key constraints in the business environment. At the same time a commitment to ensuring fiscal discipline and stopping monetizing the deficit would lower the pressure on prices, while improving the balance of payments position.

Fiscal discipline is key to ensure that meager government resources are utilized in a manner that is supportive of growth. Budget execution is undermined by limited discipline and accumulation of arrears. At the same time capital spending is limited by any measure. Salaries are not paid on time even as some spending agencies consistently overspend their budgets. Decisively dealing with the civil service arrears problem will not only create demand for local businesses as many businesses rely on customers in salaried employment, but will also improve motivations in the public service, and is important step towards reestablishing discipline in the security sector, which could reduce the number of illegal checkpoints.

Addressing challenges in the financial sector is key to alleviating access to credit constraints. South Sudan's financial sector is small and undeveloped with negligible levels of intermediation and private sector credit. While there are 30 banks operating in South Sudan, access to financial services is limited, and only 13% of the population owns a bank account, and only 3% of businesses have taken a formal sector loan in the past three years. In addition, many small banks remain undercapitalized and capital markets do not exist in South Sudan. The interbank market is not vibrant with a few isolated transactions. Financial sector reforms should ultimately support financial deepening and the expansion of credit to the private sector in a number of sectors, beyond construction. However, in the short-term reforms should focus on ensuring banks' solvency and reducing financial sector risk by addressing the large non-performing loans.

Focus on improving the productivity of public employment by addressing motivations, paying salary arrears, and cleaning the payroll to remove ghost employees. Motivation and incentives for public employment have been affected by the volatile macroeconomic situation, and unpaid salaries going back many months. Real wages have been eroded by years of high inflation and many public servants make up for the lost incomes by using government assets to make a living and by extracting rents. This usually results in checkpoints at major trade routes and solicitations for bribes at service delivery points which increases the cost of doing business. At the same time, the public service is burdened by ghost employees to a large degree, with the state losing large sums of revenue on non-existent employees, further curtailing service delivery and productive investments. Improving the productivity of the public sector would benefit from a credible arrears clearance strategy and reforming the public service with a view of removing ghost employees from the payroll, and instituting a merit based employment and promotion framework.

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[i] On Saturday 15 February 2020 the president announced that the country would return to 10 states and three administration areas as a key compromise to facilitate formation of unity government by end of February 2020.

[ii] A recent report by The Sentry (2020) implicate the South Sudan military leadership and detail how army chiefs have engaged in business activities indicative of money laundering and corruption

[iii] In April 2019, South Sudan hosted a number of roadshows in major world cities, in an attempt to drum up foreign investment and private interest in investment in various sectors of the economy.

[iv] The accountabilibity cluster includes the following institutions: National Bureau of Statistics, Anti-Corruption Commission; South Sudan Reconstruction and Development Fund; Audit Chamber; Ministry of Finance and Planning; and National Revenue Authority

[v] Limited state level employment data are available and as such not included in this figure

[vi] Public sector employee data are based on the FY2019/20 budget tables; wages data are based on actual FY2018/19 outturns, excluding arrears payments

[vii] Interview with Mary Hilary Wani Pitia, Undersecretary for Labour and Industrial Relations, Ministry of Labour, Public Service, and Human Resource Development, 5 August 2019

[viii] Special accounts are the accounts of "all the foreign diplomatic missions, United Nations agencies, and offices of other organizations established by international and regional treaties, International Non-Governmental Organizations (INGOs), Oil & Mining companies, and the accounts of projects funded by international and regional partner bodies,"

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