

ADDIS ABABA UNIVERSITY

SCHOOL OF GRADUATE STUDIES

LAND TENURE ISSUES AND DEVELOPMENT IN THE MIDDLE AWASH VALLEY:

CASE STUDY ON AMIBARA AND GEWANE WOREDAS

*Afar*

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The Fear of the Lord is  
the beginning of the knowledge

Proverb 1:7

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## Table of Contents

	<u>Page</u>
Chapter I Introduction .....	1
Chapter II Budget System of the Ethiopian Government .....	6
A. Budget Planning.....	9
B. Budget Preparation.....	10
C. Approval of the Budget.....	11
D. Budget Implementation .....	12
E. Auditing the Budget .....	14
Chapter III Structure of Budgetary Expenditure	17
A. Classification of Budgetary Expenditure.....	17
B. Budgetary Expenditure of Recurrent Account.....	22
i) General Services .....	22
ii) Economic Services .....	23
iii) Social Services .....	23
C. Sectoral Allocation of Recurrent Expenditure.....	24
D. Capital Expenditure .....	27
i) General Services .....	27
ii) Economic Services .....	27
iii) Social Services .....	28
E. Capital Expenditure Sectoral Allocation.....	28
Chapter IV. The Size of Budgetary Expenditure.	28
A. Size of Public Sector.....	31
B. Growth of Expenditure Budget...	34
C. Deficit Financing .....	36
D. Recent Development.....	37
Chapter V. Conclusion .....	40
Bibliography.....	

## BUDGETARY EXPENDITURE OF THE TRANSITIONAL GOVERNMENT

### I. INTRODUCTION

The competitive economy in the real world is in non-existence and the effect of this i.e. the failure of the price system to allocate resources efficiently and the failure of market forces to allocate resources in an efficient way rationalize government intervention.

Ordinary markets can not be used to allocate resources efficiently. By what method do government intervene in the economy?. The government can use fiscal and monetary policy.

Budget making necessitated due to the various need arises from scarcity of resources of the growing needs of the society. Budgeting is one of the universal human experience which helps in solving problems of what could be done with what we can afford.

Budget help us to know the resources that could be available and mobilized with possible ways in the country's territory and the best possible allocation of the available resources to various objectives. In general budgets is simply a plan of the government to carry out investment plans and development services such as education, health, communication and other governmental services such as administration,

defence, law & order.

In general budget has two aspects: Revenue budget & expenditure budget. On the revenue side:

- a. Inland revenue duties such as income tax,
- b. Customs and excises duties,
- c. Earning of governmental ministries & public sector,
- d. Special revenues such as loans.

On the expenditure side of the budget we also find the following items:

- a. Capital budget comprising of public investment project of developmental nature. It consists:
  - i) general service
  - ii) economic service
  - iii) social service
- b. Recurrent budget consists of cost of running ministries, agencies and other branches of the government. It consists:
  - i) general service
  - ii) economic service
  - iii) social service

How can this government allocate resources that are scarce and limited? In general expenditure must be made often searching the available resource. Budget will serve the purpose of expenditure decision on an efficient way. "The

central instrument of expenditure policy is the budget."

The way of making rational expenditure is giving national priority to different programmes & projects. Making rational expenditure means confronted with the scarcity of resources the national priorities and cost benefit analysis among other things.

Broadly, the purpose of associated features of the budget

may be considered in terms of three aspects: as a tool of accountability, as a tool of management and an instrument of economic policy.<sup>2</sup>

Budget regardless of the type of the government is a political exercise. From this point of view, budget is expected to state clearly the purpose of expenditure and provide them with the form that will be useful for government action. In addition budget is the instrument of accountability in that government agencies are responsible for the proper management of funds and programmes for which funds are appropriated.

It is also a tool for management because budget as operational document specifies either directly or indirectly the cost, time and nature of expected result.

Budget as an instrument of economic policy has more varied functions. First, it indicates the direction of the economy and expresses the allocation of the society's resources. It also leads to the determination of national growth and investment goals and more detail. With the allocation of resources among consumption, transfer and investment among sectors. Second, a major function of the budget is to promote macroeconomic balance in the economy such as employment, price stability and balance of payment. Budgeting requires that attention must be paid to revenue, expenditure and monetary policies.

Third, within recent emphasis on distribution of resources, the budget has become a means for reducing inequalities. The role of taxation and expenditure programmes and their distributional effect must be shown by the budget. In fact, distributional goals are sought to be achieved through a variety of instruments, and the budget is an important one.

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2. A Puri chand, Government budgeting and Expenditure controls theory and practice/ Washington DC: IMF) p.36-37.

Fourth, the budget should be organized so as to permit meaningful measurement of its impact on the national economy. It should permit the government share in national income and the extent to which growth and associated objectives of the government are fulfilled by the budget.

The origin of the budget can be traced back to the time of magna carta in 13th century. During this period the parliament in England was aware of the fact that the financial control should be under its own hand and not under the crown.<sup>3</sup>

The word budget is derived from the French word bougette.<sup>4</sup> This word referred to the white bag or pouch that held the seal of the medieval court of the Exchaguer. After 18th century the word budget was gradually used to mean any plan, or expectation for future periods. It has different names such as programmes, forecasts and estimates.

The development of budgeting both in depth and width is directly related to the development of the state apparatus. Thus, coming to the Ethiopian case, trying to find the exact beginning to budget practice in the country in almost for the origin of the state in Ethiopia. Systematic to modern budgeting has got a recent origin and it has emerged gradually with the development of state administration in Ethiopia. Almost starting from the reign of Menelik II, more organized and systematic budgeting practice could be observed to some extent. The inclination towards modern budgeting at that time was partially influenced by the relationships with foreign states which were presumed to have more experienced in government budgeting.

By the year 1907 when modern type of government administration started in Ethiopia, Ministry of Finance was

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3. Jesse Burkhead. Government budgeting (London. John Wiley and Sons Inc 1956) p.2

4. Royal<sup>4</sup>institute of public administration, budgeting in public authorities (London: Hertford & Harlow. 1959)p.13

established to fulfil the role of treasury both for the government and for the Emperor. But the concept of annual budget was not introduced until 1940's. Budget for the year 1944 was published on Negarit Gazeta of 1946. Budget was not published in any term after its appearance on the Negarit Gazeta of 1946 up to 1952/53.

Budget during these times were far from being proper as they were published after the fiscal year they were supposed to serve has passed, or a few weeks before the fiscal year.

The year 1958 is considered as a turning point in the development of budget in Ethiopia in that, since then budget has been continually published on Negarit Gazeta. Perhaps because the indispensable role of budget was properly understood by the government authorities.

The transitional government of Ethiopia took measures to reform the structure of budgetary expenditure aimed at improving the efficiency of public investment programmes and services. The government withdraw from productive sectors and give greater emphasis on social and economic infrastructure.

## CHAPTER II

## BUDGET SYSTEM OF THE ETHIOPIAN GOVERNMENT

Government budgeting is a process by which the financial policy of government including its monetary requirements is formulated, adopted & carried into effect. It involves all department of gov't through which money are raised and spent. It touches all the economic resources of the country which are taxed for the support of the government. 1

The success of any budgetary system is dependent up on the condition under which it is operated. The budget is not just forecast of revenue and expenditure. But it is a means for a good economic policy.

A whole range of factors enter when the budgetary system of a country is required to meet the challenges of developmental objectives. Many governmental and non governmental factors affect the budgetary system of a country are as follows: the level of economic development, the nature of government, the level of social development and technical knowhow. 2

The political philosophy of the government and its role in the management of the economy determines how the increase in saving is to be brought about, how it is changed into productive investment, what the relative role of the public sector and how the fruits of economic growth & development is to be distributed among the population.

The level of a country's economic development determines the size, scope & complexity of the budget system. The level of consciousness of the people, the attitudes, values &

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1. A prēmchaud. Government budgeting and expenditure control theory & practice /Washington D.C the free press. 1983) p. 185

2. Aronsōn, J. Richard: Public Fiance/ MC. Graw Mill book company. 1985) p. 120

cultures of the society also affect the budgetary system of the country.

The techniques of budgeting the facilities that are placed at the disposal of the government machinery and the system of management & control that is employed by the government is also of no less important in determining the budget system.

The condition required for rational budgetary system was not met in the present day less developed countries. The level of economic development, the nature of government, and the conditions surrounding these, prevent the budgetary system from being an instrument of economic development.

Budgeters in low income countries often do not where they stand with respect to the basic features of national financial life; their estimates of income may be way off their estimates of expenditure may be even inaccurate. It may take two years or more before they know (within reasonable margin of error) how much their government has spent, for them not prediction but "retrodiction" is the problem. 3

In general there is no such a thing as a formula which all governments should follow in preparing their own budget. Different countries have different methods of preparing their budgets.

A budget procedure must determine simultaneously the answer to two questions at the limited resources which a country has to be allocated efficiently.

These are:

1. Where and how can we most efficiently spend our money?
2. How much money we spend.

A good budget must fulfil two conditions: First the programmes should be clearly checked out programme, ready

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3. N. Carden and Wildausky. A Planning & Budgeting in Poor countries (New York: A Wiley series, 1974) p.66

for execution on approval. Secondly, there should be a clear indication as to how the required money will be available. 4

Before proceeding to the description of budgetary system of Ethiopia, let us consider the essential features which account for the existence of budgetary system in a country. 5

1. No tax, duties, imports or levies should be imposed except as provided by the law.
2. all such taxes, imports, duties or levies together with other governmental revenues should accrue to the government and constitute the budgetary system.
3. No expenditure may be effected from the government funds unless authorized by law and within the authority given by law.
4. The budget is approved by legislative body, usually on the recommendation of the executive and such an approved budget has a power of law.
5. The executive carries out the budget within and in accordance with the legislative intent and
6. The executive account the implementation of the budget and that such accounts are audited by independent body on behalf of the legislature.

Actually, budgetary activity has a continuous character meaning, after one budget year is over, immediately the next one enters. The activities in each budget period are interdependent & interrelated to the extent budget period start with in the preceding period. In many cases, there are definite process repeated every budget period often referred to as the budget cycle.

Generally the budget cycle refers to the whole process of any annual budget which can be divided into four main phases:

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4. B.N.<sup>4</sup> Gupta, government budgeting with special reference to India, (Bombay: Allana bad low Journal press, 1967) p.30

5. Ministry of finance (unpublished material)

these are:

- a) Preparation of the budget,
- b) Legislative approval of the budget,
- c) The execution of the budget,
- d) Auditing the budget.

Hence, the cycle covers all the functions from the budget preparation to the evaluation of its implementation. The Ethiopian budget cycle reflect the four basic phases.

#### A. BUDGETARY PLANNING

Planning is more general than budgeting; planning established programmes, sets, goals and objectives and basic policy decisions for the economy as a whole. Budgeting analyses in detail the many functions of activities that the economy must perform to implement each programme, analyses the alternatives within each activity to achieve the end product desired, and identifies the trade off between partial or complete achievements of the established goals and the associated cost. 6

If the plan is to be meaningful, it must be reflected in the budget. If the plan and the budget do not coincide, the plan simply is ignored.

If the budget controls but a small part of the public expenditure if the pattern of expenditure at the end of the year bears little relation to initial budget figures, and it budgetary classification hides more that it reveals, the budget help planners how much influence they have over it.

Budget without planning cease to be a plan of action plans that do not have a realistic recognition of the budgetary constraints, have little functional value. Each disciplines the other and the end product should ideally bears

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6. J. Birkhead, Government Budgeting /New York, John Willyand Sons inc, 1956/ p.271

the imprint of both. 7

The main concern of all plans and budgets in the allocation of resources and policy analysis is an emphasized one. But in planning the economic aspect dominates. While in budgeting more attention is paid to financial aspects.

The Ethiopian economy can be described at present as a free market economy. It is a transition from centrally planned to a free competitive market economy. Ethiopia now is in accordance with current political situation of the world.

## B. BUDGET PREPARATION

Budget preparation varies from country to country, and even among the various units within countries. But the cycle, or sequence of events of operation of the budget system has certain common steps. The first is that of preparation and submission of the budget.

The process of decision making that results in a budget, what even its complexities, contain three necessary ingredients: 8

1. Determination of the variety of policy objectives the government intends to pursue: such as defence, education, or law enforcement.
2. Estimation of the cost of pursuing each of these objectives in varying.
3. An assessment of the willingness of the public and its ability to pay for the government's programme as a whole.

The preparation of the budget is probably the most important action of the government affecting the financial and general economic conditions of the country.

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7. A prečhand. Government budgeting and expenditure control theory & practice /Washington D.C. the Free press 1983/ p.188

8. Arthur Smithes. "Government Budgeting", international encyclopedia of social science, vol. 2/ New York, the free press 1968/ p. 185

According to the organization structure of the region the lowest level is the Woreda and the budget preparation starts from here.

Woreda bureaus are the lower budget requesting bodies pursuant to the organizational structure of the national regional administration. They will receive the budget call from their respective departments and services in accordance with this, the Woreda executives committee will set up a budget committee to study and examine the budget proposal which will be defended and explained by the budget requesting body. This will be approved by the finance bureau. The proposal which has passed through all this process will, upon acceptance by the chairman of the budget committee, be submitted to the Woreda council along with supportive document.

The Woreda council will approve the budget after considering all issues and negotiating with all concerned authorities. All approved proposal will be compiled together and then they will be sent to the zone administration with every necessary explanation. The zone administration will send this to the zone financial bureaus within the times provided for this by the executive organ of the zone. The proposal will pass through the same process to reach the national regional administration.

### C. APPROVAL OF THE BUDGET

For economy to develop, society's productive capacity must grow faster than its population. But development is not a process where by increase material flow-in their own accord. Sacrifice and efforts are demanded. Economic grow implies using society's resources more efficiently.

The budget information set by the budgetary units includes financial requirements and the plan of the need for

which money has to be required. But this does not mean that budgetary unit got the amount of money they required to have.

Ministry of Finance prepare and submit to the council of ministers, together with its recommendation, a consolidated annual budget of the central government upon analyzing recurrent budget proposal received from central government organs, capital budget proposals prepared and forwarded to it by the Ministry of Planning and economic development and request from regional self governments for budget subsidies.

The council of ministers after analyzing submit to the council of representatives for final approval. After this the authorized budget is published as a budget proclamation on *Negarit Gazeta*.

#### D. BUDGET IMPLEMENTATION

The preparation and approval of the budget is as good as nothing if it is not implemented and serve the purpose of development. The budget proclamation is merely declaration of the financial plan of the country. And the plan has to be put into practice.

The implementation stage of the budget process involves the management of the approved financial plans or activities for designated period of time at a cost that is within estimated available resources.

These are two distinct aspects of budget implementation. One deals with the provision and use of methods and devices to assure compliance with the approved financial plan. The other is concerned with flexibility, with obtaining the proper use of funds under constantly changing circumstances and adjusting and adopting the financial plans to new needs. 9

The first aspect requires the introduction of discipline

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9. J. Burkhead, *Government budgeting* /New York, John Willey and Sons Inc., 1956/ p.341

and the establishment of rigidity in the budget implementation process. The manner in which expenditure authorization are made establishes limitations and requirements with respect to purposes, amounts & time of departmental expenditure.

The budget system must recognize the need for flexibility by providing the legal basis for making transfers, permitting, contingency expenditure or establishment of mechanism for emergency authorization.

Successful budget implementation highly depend on achieving the proper balance between the two aspects: elements that generally operated in conflict.

After the approval of the budget draft by the council of representatives, budgets are issued by the Ministry of Finance to budgetary unit. Advice issued by the Ministry of Finance how to allocate each object of expenditure into its detailed components. The various governmental units are supposed to strictly comply with the official budget allocations is using the fund. Budget transfers are allowed only if the fund to be transferred could be placed in more efficient way.

The Council of Ministers, the Ministry of Planning & Economic Dev't and Ministry of Finance have the power to authorize budget transfers which depend upon the type of the budget transfer.

The request for additional budget is acceptable under 3 conditions. 10

1. If the work has to be done within the budget period
2. If payment through transfer is not possible
3. If the originally allocated budget improved to be insufficient.

The budgetary unit present their request for additional budget on the form prescribed for this purpose. If the demand is supported by the Ministry of Finance, it will be communicated to the Council of Ministers. After analyzing the

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10. Ministry of Finance / unpublished material/

Council of Ministers submit to the Council of Representatives for approval after approval it is published on Negarit Gazeta as additional budget.

The budget allocation disbursed to different units in terms of cash or cash items. The unit which receive the budget allocations are required to present monthly reports covering the implementation of the revenue and expenditure budget of the period.

Budgetary units are allowed to spend up to the previous years approved budget levels for undecided expenditure by the Ministry of Finance, with the exception of equipment which can only be incurred by receipt of budget appropriation.

Budgetary appropriations of the current part of the budget are distributed by monthly disbursements of one twelfth of the total budget appropriation and subsequently monitoring is undertaken by the Ministry of Finance. During implementation stage expenditures are made on project appropriation basis for capital expenditure.

The department classified as budgetary programme will at the same time account for the expenditure from the previous allotment by submitting the central budget office a monthly receipt and payment in duplicate. Money that is not used during the month has to be returned to the Ministry of Finance at the end of the month and at the end of fiscal year accounts for all departments are closed.

Budget implementation requires a government wide responsibility. Successful budget implementation requires that each administrative head actively support the budget and its objectives. Budget implementation depends also on the internal organization of the budget.

#### E. AUDITING THE BUDGET

A budget may be well planned and formulated but unless

adequate provision is made for effective financial control there is small linkage with the budget plan. The accounting & auditing systems are the principal means of exercising such control.

The objectives of budgetary control may be to make available funds for various purposes by time periods. The control aspect of the annual budget execution takes place not only at specific point in time, but also at part of the day to day activity of the budget execution.

Auditing the budget helps to control the amount of expenditure in relation to the entire fiscal period and to permit commitments in the event that revenues fall short of expenditure.

The budget control helps also to specify the system by which budgetary units are required to establish and allocate amounts of limits of expenditures for specified purposes within subordinate divisions of the budgetary units. In addition it makes possible formalized control over number of positions & salaries. Control over budgetary expenditure may take one or more of the following forms: 11

1. Technical control: ensuring the budgetary allocations are in fact spent on the purpose for which they were made available.
2. Efficiency control: checking that an allocation for approved purposes is used as efficiently as possible.
3. Economic control: to ensure that the total available resources are put to the best possible use.

For supervising and controlling the financial operations of budgeting, a special body for external control/Auditors General/ is appointed by the government. The Auditors General has responsibility to audit departments and organizations, to audit private contractors accounts, to issue the directives

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11.R.W. <sup>1</sup>Davies, The Department of Soviet budgetary system/Cambridge University Press, 1958/ p. 203

for the keeping of books of account for department and organizations.

The other supervising unit is the inspection department or Ministry of Finance. This department has a power to administer the governments's unit budget and ensure that financial policies are properly implemented, control governments institutions by ensuring proper accounting systems, to ensure the existence and proper implementation of laws governing taxes, duties, financial administration and fees which meet the economic and social development needs of the country. It also issue directives regarding the purchase and utilizations of various government supplies and supervise their implementation.

These controlling unit prepare a detailed annual work plan which provides full details of government budgetary units which will be subjected to detailed audit.

### CHAPTER III

#### STRUCTURE OF BUDGETARY EXPENDITURES

Budget information on expenditure must be organized in such a way that it can be understood. The pattern of government expenditure gives a clear picture of policy of the government and the effect of government spend on the future development of the country.

On the expenditure side, the inquiry was concerned what were the desirable forms of expenditure and how far expenditure should be pushed in each direction. <sup>1</sup>

The structure of government expenditure depends on a number of factors. First, it is determine by the level of economic development and influence the structure of the economy. The state of underdevelopment influence the structure and the extent of involvement of a government in its economy. And also the existing international situation is important in determining the structure and the extent of involvement of a government in its economy. And also the existing international situation is important in determining the structure of budgetary expenditure.

In view of the problem of underdeveloped countries, proper allocation of public fund is very important. Capital formation in underdeveloped countries is low. The budget policy should be made in such a way that this problem is removed.

#### A. CLASSIFICATION OF BUDGETARY EXPENDITURE

The establishment of budget classification is one of the most important steps in governments' budget system. The basic classification structure provides for decision making through

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<sup>1</sup> R.J. Chllfah, Fiscal policy in under developed countries /London: Allen and unwin, 1960/p. 45

out the budget process. The classification employed must facilitate formation of the budget in relation to policy objectives. It should also be advised in such a way that it effectively reflects in the budget what the government proposes to do with available resources and provide administrative control structure that will permit determining what has been done in relation to the approved budgets.

There is no single ideal type of expenditure budget classification that is superior to one another. The test is in the usefulness of the product of a particular process or approach.

The approach adopted by the Ethiopian government may be termed as a programme and performance budget approach. As budgetary units are expected to provide full details of programme objectives and activities to be undertaken with physical indicators of performance or alternatively work loads included, whenever possible. Each budgetary units is expected to justify each expenditure items for both existing and new programmes.

This programme budgeting is further development of the functional classification which separate budgetary transactions according to the general purpose or function. Accordingly the expenditure budget is divided into 3 categories: general services, economic services and social services. The functional classification groups a specific expenditure under one heading regardless of the budgetary units making the expenditure such as agriculture, health, education. Each sub-head intern split into component programmes, activities and tasks which contribute to the achievement of government policy objectives.

Thus according to Laiden and Wildausky, "the technique of separating ordinary and capital expenditure like planning, helps poor countries expend beyond the narrow *of the possible*."

The budget in Ethiopia is divided into two parts: one reflecting the recurrent nature of public expenditures in ultimately prepared by the Ministry of Finance; the other which contains capital investment project, is the responsibility of the Ministry of Planning and Economic Development. Inputs for the preparation of both parts of the budget are provided at the beginning of the budget cycle by line ministries, and by regional governments. The preparation of both parts of the budget proceeds on parallel ways until late in the process, when the two responsible ministries and other officials meet to finalize the budget.

Table 1  
Government Recurrent and Capital Expenditure  
(in million birr)

Year	Budgetary Expenditure On Recurrent Account		Budgetary Expenditure on Capital Account		Total
	Amount	Percent	Amount	Percent	
1977/78	2,387.9	61.9%	1,471.8	38.1%	3,859.7
1978/79	2,619.7	65.4%	1,383.1	34.6%	4,002.8
1979/80	3,132.0	68.2%	1,459.2	31.8%	4,591.2
1980/81	3,567.4	64.7%	1,939.7	35.3%	5,507.1
1981/82	3,722.2	72.1%	1,440.1	27.9%	5,162.3
1982/83	3,409.9	73.9%	1,204.0	26.1%	4,613.9
1983/84	3,093.0	67.5%	1,486.8	32.5%	4,579.8
1984/85	3,164.0	53.3%	2,767.8	46.7%	5,931.8
1985/86	4,600.0	54.4%	3,847.1	45.6%	8,447.1
1986/87	5,369.8	53.8%	4,595.8	46.2%	9,965.6

Source: Ministry of Finance

The data clearly shows that the share of recurrent expenditure in the total expenditure budget has been decreasing for the last four years. But the amount allotted has been increased. If we compare 1983/84 with that of 1986/87, it is more than 2,276.8 million birr.

The share of capital expenditure in the total expenditure has been increased. If we compare 1982/83 with 1986/87, it is more than tripled. To understand the pattern of government expenditure, a detailed study of various components of recurrent and capital budget is essential.

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Table 2

Summary of Budgetary Expenditure of  
the Government  
(in million Birr)

Item	77/78	78/79	79/80	80/81	81/82	82/83	83/84	84/85	85/86	86/87
Recurrent Expenditure	2387.9	2619.7	3132.0	3567.4	3722.9	3409.9	3093.0	3164.0	4600.0	5369.8
General Serv.	1225.5	1358.0	1714.9	2031.1	2266.4	2001.9	1026.1	1146.8	1345.3	1478.4
Economic Ser.	141.4	155.3	190.8	206.9	222.3	241.1	274.4	294.2	462.6	573.6
Social Serv.	550.6	585.2	601.7	644.2	665.6	653.2	708.9	885.6	1219.9	1394.6
Others	440.6	521.2	624.4	685.2	567.9	540.7	1003.6	873.4	1572.2	1992.2
Capital Expend.	1447.7	1383.0	1459.1	1939.6	1440.1	1204.0	1486.6	2763.8	3847.1	4595.8
General Serv.	38.1	45.4	24.2	49.3	34.9	81.4	48.8	91.3	105.2	317.1
Economic Serv.	1327.8	1225.0	1327.3	1758.7	1267.9	1024.4	1286.9	2410.2	3214.3	3438.4
Social Serv.	105.8	122.6	107.6	131.6	138.0	108.2	151.1	266.3	527.6	840.3
Total	3859.7	4002.8	4591.6	5507.1	5162.3	4613.9	4579.8	5931.8	3447.1	9965.6

Source: Ministry of Finance

## B. BUDGETARY EXPENDITURE ON RECURRENT ACCOUNT

Recurrent expenditure consists of the costs of running ministries, agencies, and other branches of the government. They are those expenditures which must be made every year for the continuing activities of the government. To understand the size and pattern of public expenditure on recurrent account, it is useful to examine what has been happening to its major components. The present classification divides the recurrent expenditure budget into three categories: General services, Economic services and Social services.

### i) General Services

This heading includes these activities required for the gov't of the country that can not be associated with services to persons or business. It includes over all fiscal services, general personal policies, the conduct of external affairs, defence activities and public security. These services can not be allocated to particular groups or persons.

General service take up the largest share of the total recurrent budgetary expenditure. The budget under this head was 2001.9 million birr in 1982/83. It was 58.7 percent of the total recurrent budgetary expenditure. For the year 1986/87, the expenditure under this head was 1,478.4 million birr which was 27.3 percent of the recurrent budgetary expenditure.

Under this head 'general service' defence expenditure accounts for the major part of the recurrent budgetary expenditure. Defence expenditure for the year 1981/82 was 1,634 million birr about 42.3 percent of the recurrent budgetary expenditure. It has decreased to birr 681 million in 1986/87 budget. This was mainly because the long devastating war is over.

Second importance under the head 'general service' is the expenditure on welfare security. The expenditure on welfare

security has been birr 123.9 million in 1983/84, while it was 295.4 million birr in 1986/87.

#### ii) Economic Services

This heading covers government expenditure associated with the regulation and more efficient operation of business. It includes such objectives as economic development, and the creation of employment opportunities. Economic services include activities such as agriculture, mining, trade, industry, tourism, transportation and communication.

As compared to the expenditure on the other two components, it accounts for the smallest share of the recurrent budgetary expenditure. The expenditure under this head was birr 241.1 million in 1982/83, about 7% of the recurrent budgetary expenditure. It has gone up to birr 573.6 million in 1986/87, showing an increase of birr 332.5 million. Under this heading the largest share is accounted for agriculture and natural resource. In the budget for the year 1986/87 the expenditure under this sub heading was birr 351.1 million, about 6.5% of the recurrent budgetary expenditure.

Second importance under the heading 'economic service' is road construction. The expenditure on road construction in the year 1986/87 was 147.1 million birr. It was 2.7% of the recurrent expenditure.

#### iii) Social Services

This heading includes the services supplied to the community and to the persons directly. It includes education services, health services, social security & welfare services. Expenditure on social services is important factor in the continuous improvement in the national welfare of the people.

The expenditure under this head was birr 708.9 million in 1983/84, about 22.9% of the total recurrent expenditure. In the year 1986/87 the expenditure under this heading was birr

1395.6 million which comes to be 25.9 percent of the recurrent budgetary expenditure.

General education, culture and sport, and health represent the most important component of social services. Under this heading the largest share accounted for education. In the budget year 1983/84 the expenditure was birr 531.7 million and it was 17.1% of the total recurrent expenditure. In the budget year 1986/87 the expenditure under this is birr 885.3 million and it is 16.4% of the total recurrent expenditure.

Health is the next important category under the heading 'social services'. In the year 1983/84 the expenditure under this subheading was birr 170.3 million. On the same year it accounted for about 5.5 percent of the recurrent budgetary expenditure. In the year 1986/87 the expenditure on health was birr 345.7 million, accounts for 6.0% of the recurrent budgetary expenditure.

### C. SECTORAL ALLOCATION OF RECURRENT EXPENDITURE

Since the end of the war, sectoral allocation of the recurrent budget emphasize economic and social service. This is reflected by the increased allocations for education, from about 12% of recurrent expenditure during 1979/80 to about 17.1% for 1985/86 and 18.7% for 1986/87 budget. There is also a similar shift for the allocation of health. Recurrent expenditure on health decline from about 4.5% of total recurrent expenditure of 1979/80 to 3.6% in 1981/82, then increased to 6.2% of the total recurrent budget for 1985/86 and 8% of 1986/87. Recurrent budget allocations for infrastructure did not increase significantly reflecting the continued low funding for operation and maintenance of physical infrastructure. There has been an increase in 1985/86 and 1986/87 in allocation for other economic services compared

with 1970's. There is also drastical reduction in the allocation of recurrent expenditure for defence. Recurrent expenditure on defence decline about 42.3% of total recurrent expenditure of 1980 to 16% in 1986/87. This is due to the end of the civil war.

Table 3a

The Adjusted Recurrent Expenditure: Sectoral Allocation

(in million birr)

Sectoral Classification	1986/87 Actual Exp.	1987/88 Actual Exp.	1988/89 Actual Exp.	1992/93 Actual Exp.	1993/94 Actual Exp.
General Administration	335	351	347	444	677
Economic Infrastructure	63	68	64	79	127
Other Economic Services	412	429	496	829	828
Education	389	414	443	587	795
Health	121	128	137	215	341
Other Social Services	85	72	88	128	132
Defense	995	1,317	1,634	675	681
Others	319	670	665	481	680
Total	2,726	3,452	3,868	3,441	4,265

Table 3b

The Adjusted Recurrent Expenditure: Sectoral Allocation  
(% share)

Sectoral Classification	1986/87 Actual Expenditure	1987/88 Actual Expend.	1988/89 Actual Expend.	1992/93 Actual Expend.	1993/94 Actual Expend.
General Administration	12.3	10.2	9.0	12.9	15.9
Economic Infrastructure	2.3	2.0	1.7	2.3	3.0
Other Economic Service	15.1	12.4	12.8	24.1	19.4
Education	14.3	12.0	11.5	17.1	18.7
Health	4.5	3.7	3.6	6.3	8.0
Other Social Services	3.3	2.1	2.3	3.7	3.1
Defense	36.5	38.2	42.3	19.6	16.0
Others	11.7	19.4	16.9	14.0	16.0
Total	100.0	100.0	100.0	100.0	100

#### D. CAPITAL EXPENDITURE

Capital expenditure budget is mainly used for the implementation of long term planning. Capital budget and its procedures, together with long-range planning can serve as an instrument for orderly resource development and maintenance.

Capital budget needs attention and should be in the interest of securing economic development. That is why the capital budget preparation is assigned to the Ministry of Planning and Economic Development. Like that of recurrent expenditure, budget capital expenditure is also divided into three parts: general services, economic services & social services development.

##### i) General Service

The capital expenditure on general services related to that part of the total expenditure budget used for the construction of permanent facilities to assure effective administration system. This heading includes particular expenditure on administrative service and public building.

For the year 1984, the expenditure under this heading was 48.8 million birr, or about 3.2% of the total capital expenditure. In 1987, the expenditure under this head rises to 317.1 million birr, or 6.8% of the total capital expenditure. Under this heading, budgetary expenditure on public building accounts the larger part of the capital expenditure budget.

##### ii) Economic Services

As we can clearly observe from the data capital budgetary expenditure, 'economic services' take up the largest share. Total expenditure under this heading was 1286.9 million birr or about 86.56 percent of the total capital expenditure in 1984. It was gone up to birr 3434.4 million in 1987 registering an increase of birr 2151.5 million and it was 74.8

percent of total capital expenditure.

Under this head, agriculture accounts for 43.6 percent of the total capital expenditure in 1984. This figure has declined to 22.29 percent in the year 1987. The other component of economic service and development was road construction. The expenditure under this heading was birr 1273.3 million. It accounts 27.7% of total capital expenditure in 1987.

### iii) Social Services

Expenditure on social services is second in importance as far as the capital expenditure budget is concerned. In 1984, the expenditure on social services was birr 151 million, which was 10.1 percent of total capital expenditure. For the year 1987 the expenditure under this was 840.2 million birr, which was 18.28% of the total capital expenditure. Its share was increased from 10.1 percent to 18.2 percent.

Under the head social services, education expenditure accounts for the major part of the capital budgetary expenditure. In the year 1987, it accounted for 8.9% of the total capital expenditure, or birr 411.5 million.

Second importance under this heading was health. the expenditure on health, in the year 1984 was 68.1 million birr, while it was birr 234.0 million for the year 1987.

## E. CAPITAL EXPENDITURE SECTORAL ALLOCATION

Expenditure on capital account continues to be heavily biased towards economic development, which received about 91% of the total in each year up to 1984. But there was a decline in the last two capital expenditure for economic development.

This drop in the last two budgets, down to 85.6 percent in 1985 and further to 79.3 percent in 1986. Agriculture has experienced a significant decline as industry. Much of this

expenditure on industry and agriculture has been on productive activities which could be developed by private sector. Sectoral allocation in the capital budget & how that agriculture's share decline from over 17% in 1979 and 1980 to about 7% in 1986.

Similarly for industry whose share in capital expenditure has been increasingly steadily up until 1992, when it reaches over 28% of capital expenditure, there was a drastic decline in allocation down to 8%.

In this sectors, general government policy is to complete existing projects, but not start new ones, and to support extension and research rather than be involved in production.<sup>3</sup>

Road construction has experienced a dramatic increase in its share, quadrupling its share in 1986 capital budget from the 1981 level. As a percent of total budget, the road portion has increased from 4.8% in 1981 to 22.9% in 1986. This represent the largest single sectoral allocation.

<sup>3</sup> Ministry of Finance (unpublished material)

Table 4  
Adjusted Capital Expenditure:  
Sectoral Allocation  
(in million Birr)

Item	1978/79 Expend.	1979/80 Expend.	1980/81 Expend.	1981/82 Expend.	1982/83 Expend.	1983/84 Expend.	1984/85 Expend.	85/86 Expend.
Agriculture	181.8	196.6	181.3	129.9	86.4	20.6	314.5	224.4
Mining	57.9	101.3	138.2	109.4	110.2	17.4	151.6	100.7
Energy	204.4	157.0	172.5	83.5	55.6	14.7	186.3	267.7
Natural Resource	126.8	160.4	178.7	146.1	142.8	42.8	440.9	551.0
Industry	96.7	179.8	305.2	192.3	170.5	72.0	220.3	262.5
Trade & Tourism	20.6	21.7	3.5	00	00	00	4.0	5.2
Trans. Const.	111.1	108.2	91.9	55.3	50.8	30.0	257.4	882.4
Building Cons.	11.6	6.4	23.5	5.4	5.1	1.2	4.3	00
Transp. Comm.	99.6	68.0	264.3	82.1	68.0	17.6	187.9	149.9
Education	33.2	35.1	43.9	28.7	17.5	3.5	140.1	299.9
Health	21.8	23.3	28.7	26.1	8.6	2.7	56.4	147.6
Urban Dev.	10.3	11.1	20.2	21.7	20.0	0.9	26.6	117.3
Information	1.7	2.8	6.8	00	00	00	00	00
Social Wel.	1.8	1.5	1.0	1.2	0.7	1.2	1.7	2.2
Science & Tec.	0.8	3.5	3.8	3.7	0.2	0.8	7.2	4.9
Public . Buil.	32.0	7.1	31.2	12.6	10.9	5.2	28.2	85.7
Compens. & Paym.	11.5	14.2	9.8	00	00	1.5	4.0	00
Pub. Works. & Programmes	00	00	00	00	00	00	10.0	0.1
Social Rehab.	00	00	00	00	00	00	6.0	00
Total	1039.3	1132.9	1552.3	964.4	789.4	252.1	2096.9	3221.1

Source: Ministry of Finance

## CHAPTER IV

### THE SIZE OF BUDGETARY EXPENDITURE

Certain aspects of economic development are closely associated with the budget systems of the country. The effective use of budget policy is a key for speedy economic development can be accelerated through additional expenditure in desired sectors. Government expenditure affects the allocation of resources and the distribution of income. It also promotes capital formation and lowers inflation .

Public expenditure is an important instrument to achieve the objective of public policy in such a manner that is ensures a maximum increase in national income and employment. It should also provide increased social and economic over head. There by it helps to raise the standard of living of the common man and provide a stimulus to private investment. 1

The development process of an economy implies that the role of the government in the allocation of natural resources tends to increase. This associated with large increase in the size of government expenditure.

#### A. SIZE OF THE PUBLIC SECTOR

The role of the government of developing countries have nowadays extended beyond the traditional function of maintaining law order. Because improvement of transport and communication, presume grows during the process of economic development for improved standards of public services, which can be met by greater centralization of control over the size and character of government expenditure. Due to the increasing

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1. R.N. Bhargava, Indian Public Finance (London: George Allen Willy Ltd. 1962) p.2

importance of externalities, especially associated with increasing urbanization, demands greater degree of control of government expenditure.

The role of government activities has been a source of debate over the years. Advocates of different economic systems have different approaches to this questions. On one hand, there are conservatives or classical liberals who say that government should be held to a minimum. According to them, government in any country should restrict its activities to defence, the administration of justice, & certain public works. Modern liberals support the use of government as instrument of bringing about the kind of society it requires. At the extreme, there are socialists who favoured public ownership and operation of public enterprise over the private. But the debate is almost solved after the collapse of Soviet Empire.

The quality of government goes a long way to determine the performance of the entire economy. If government is inefficient, resources are wasted and taxes are unnecessarily high. If government assumes too many functions private performance deteriorate. House hold and business are no longer able to reach national decentralized decisions that are essential for a properly functioning market economy. If government assumes too little responsibility, private economy power may be exercised in ways detrimental to the economy as a whole; disparity in income and wealth may become too great. 2

The economic role of government can be measured in different ways. It can be measured by the portion of total employment in the public sector, by national income ratio, or by the comparison of the total expenditure of the government

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2. Eckstein Otto, public finance/ London: Prentice Hall 1973/ p. 1

within national income account. 3 Various ratios may be used relatively budgetary activities to different components of the national income, and personal income.

The measure I used is the ratio of total governmental expenditure to gross domestic product. Government expenditure which go into the numerator include transfer payments, while gross domestic product in the denominator include expenditure for the purchases of goods & services only.

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3. R.N. Lindhold, Introduction to fiscal policy /New York, Pitman Publishing Co. 1955/ p.2-3

Table 6

The Ratio of Total Government Expenditure to  
Gross Domestic Product  
(in million birr)

Year	Government Expenditure Net of <u>Transfer</u>	Gross Domestic Product	Ratio of Government Expenditure to GDP
1980	4591.2	15996.1	0.28
1981	5507.1	16873.4	0.32
1982	5162.3	17871.7	0.28
1983	4613.9	19815.1	0.23
1984	4579.8	20393.8	0.22
1985	5931.8	26056.7	0.22
1986	8447.1	27386.7	0.30

Source: MOPED

The data clearly shows that the ratio of government expenditure to gross domestic product is decreasing with the exception of 1986. This is because the government expenditure increased due to mostly by external assistance and loan.

This size of the public sector of Ethiopia is decreasing now. This is due to the transition from centrally planned socialist economy to a free market economy. The government plan to withdraw from most of the productive sector. By introducing privatization policy, the government will withdraw from its hotel business to retail business and small scale industries for the coming years. Due to the above mentioned factors the size of public sector will decrease in the future.

#### B. GROWTH OF THE EXPENDITURE BUDGET

With an increasing responsibilities assumed by the government for securing balanced growth of the economy and for

social welfare of people, government budget particularly the expenditure budget plays an important role as an instrument of economic and social policy.

An underdeveloped countries, like Ethiopia, while initiating the process of economic development has to face growth in government expenditure in order to accommodate the rapid growth of population. Populations in most cases, increase at faster rate than the increase in national income. Increase in population implies more roads, housing facilities, water supply etc, for which the government has to spend money. Thus, there is a tendency that the rate of growth of expenditure as a whole is faster than that of population.

Table 7

<u>Year</u>	<u>Amount</u>	<u>Percent of Growth</u>
1980	4591.2	-
1981	5507.1	19.9
1982	5162.3	-6.2
1983	4613.9	-10.6
1984	4579.8	-0.7
1985	5931.8	29.5
1986	8447.1	42.4
1987	9965.6	17.9

Source: Ministry of Finance

The data clearly shows that except for the year 1984, for which negative growth rate is observed in government expenditure budget, budgetary expenditure of the transitional government has an increasing trend. This is mainly due to an increase in domestic revenue, external assistance and loan. If we compare 1984 domestic revenue with 1987, it is more than double. Due to current political situation of the country, external assistance and loans are highly increased. External assistance of 1987 is 6 times more than that of 1984.

### C. DEFICIT FINANCING

Expenditure making can not be separated from expenditure financing. Basically, government expenditure and revenue are but different side of the same coin.

Deficit financing is government practice of making more expenditure during the fiscal year that is taken from taxes. It is often adopted to prevent important governmental projects from being delayed because of lack of immediate funds.<sup>4</sup>

Table 8  
Budgetary Deficits of the Ethiopian Government  
(in million birr)

<u>Year</u>	<u>Domestic Revenue</u>	<u>Budgetary Expenditure</u>	<u>Shortfall (Deficit)</u>
1984	2292.0	4579.8	-2287.8
1985	3114.0	5931.8	-2817.8
1986	3936.19	8447.1	-4511.0
1987	3569.88	9965.6	-4595.6

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Source: Ministry of Finance

The data clearly show that the level of budgetary deficit has been increasing for the past years. This is mainly attributed to the fast increase in the level of government expenditure budget. In fact revenue has been increasing. But it could not keep pace with the increasing of total expenditure. The source of deficit financing used by the government are 1. External assistance, 2. Domestic bank

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4. R. Mathews, Budget structure and organization in developed & developing countries /London: Max Millan, 1973/ p.67

borrowing, 3. Borrowing from abroad.

The recurrent budget balance i.e. the difference between domestic revenue and recurrent expenditure, has been negative for most of the period except for 1987. Although government current revenue budget has been increasing in the period under review, but it could not keep pace with the fast increase in recurrent expenditure.

External loans and credits have shown an increasing trend. To finance the budget deficit external loans and credits have increased from Birr 656.4 million in 1984 to birr 1292.6 million in 1987.

Table 9  
Summary of Government Operation  
(In million Birr)

Item	1984	1985	1986	1987
Recurrent expenditure	3165.0	3164.0	4600.0	5231.8
Current revenue	2242.0	3069.0	3880.29	5231.8
Recurrent deficit	-923.0	-950.0	-717.71	0
Capital expenditure	1486.75	2767.85	3847.11	2940.1
Overall deficit	-2409.75	-2842.85	-4566.82	-2940.1
External loan & credit	656.42	1196.19	1003.82	1292.6
External assistance	336.13	506.88	2012.10	1793.6
Internal borrowing	1367.19	1114.78	240.0	0

Source: Ministry of Finance



#### D. RECENT DEVELOPMENT

The transitional government of Ethiopia took measures to

reform the budget based on past budget performance and the recent expenditure patterns. The first is civil service reform for effective delivery of government services. The second issue is strength budgetary planning and implementation, so as to increase the efficiency and sustainability of public investment programmes. The final issue regards the efficiency and equity aspects of the existing transfer system. 5

The decline in the quality of government services in the past has been aggravated by the declining productivity of civil services. The policy of immediate hiring of school graduates into the ranks of public employees, which was in effect until about 3 years ago, together with efforts to limit expansion in the wage bill has resulted in large and un paid civil services. The weak link between salary compensation and productivity also weakened work incentives. The potential & economic transition and the opening up of private employment opportunities has also led to loss of capable experienced civil service employees. To reverse this decline in quality, the government has already made civil services reform. It has two components: refreshment of redundant employees and reforms of wage structure.

The inefficient and unsustainable public investment programmes in Ethiopia have best manifested themselves through low capital implementation rates and deterioration of existing physical asset and services due to under funding of non-wage operating and maintenance. To ensure efficient and sustainable public investment and services, the government took measure to improve budgetary planning and implementation capacity.

The significant decline in the share of military expenditure in the recurrent budget has resulted in the increase in the budgetary allocation to transfer and safety nets. The composition of transfer has changed markedly over time with a substantial decline in price subsidies and more

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5. Ministry of Finance (unpublished material)

emphasis to social safety nets.

Given the priority level in Ethiopia & financial resource constraints, government transfers in the usual form of the poor. Therefore, the government liberalized agricultural policies, given emphasis to small and medium size private enterprises, encourage labour intensive technologies and gave conducive environment to private sector development.

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the budget into its administrative and policy aspects. The former is related to the management of budgetary operation of the Ethiopian government, where as the latter is related to the role of the budget as an instrument of achieving economic development.

The effectiveness of expenditure in serving the purpose of development is mainly determined by the type of administration provided.

It can be stated on the basis of economic principles that revenue raised in a particular manner, and expenditure made for a particular purpose, will bring about certain result; but the realization of the expected reaction will be obtained only if the programmes recommended are properly administered. 2

Many of the administrative qualities are lacking in the budget system of Ethiopia. These include the shortage of skilled and responsible workers, Law implementation rate and well developed techniques of budgeting.

The lack of confidence that exists between budgetary unit and the Ministry of Finance personnel in terms of budgetary unit preparing adjustable budget proposals is factor that affect budget procedures. There is a need to improve the working relationship & the level of confidence between the government budgetary unit and the Ministry of Finance and the introduction of detailed approach supported by the pre-budget discussions would prove beneficial.

Lack of skilled manpower in the field of budgeting and auditing equally contributes for the inefficient budget administration so as to upgrade the skill of the staff of the Ministry of Finance and the budgetary units, the skill of the staff of the Ministry of Finance and the budgetary units, training of manpower both local and abroad, short-term and

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2. L. Jøhansen Public Economics (Amsterdam, North - Holland, 1975,) p.21

constituted only about 10% of the total recurrent expenditure during the year 1987. There is a greater need to examine the recurrent budget allocation to economic services and allocation within its various sub-sectors. In view of its dominant role in the Ethiopian economy, special attention should be paid to the recurrent expenditure on agriculture.

In the context of scarce resources the question as to whether or not agriculture takes large volume over industry may be problematic. But economic development must be accompanied by a balanced progress between agriculture and industry. The allocation for industrial activities has remained about 0.25 percent of the recurrent budget for the past years. Due to its significance to the overall economic development, its labour intensity and thus little capital requirement and due to the need for food both in rural and urban sectors, relatively the government has paid attention to the agricultural sector.

The capital expenditure on economic development is dominated by non-directly productive sectors such as infrastructure. By the year 1987, the expenditure on road construction was birr 1273.3 million, 27.7% of the capital expenditure.

There has been a greater reliance on the foreign resources of financing than the domestic. Between 1985 and 1987, almost 30% of total expenditure was financed by foreign resources. Government borrowing, nowadays, is becoming a major source of deficit financing. The adverse effect of government borrowing is unquestionable. In a country like Ethiopia, a larger share of the government expenditure is tax-financed, i.e. public expenditures came from funds diverted from private sectors. These diverted funds should be allocated to high priority projects, keeping investment in line with the capacity to finance recurrent budget.

The main policy issue regarding budgetary expenditure is

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