

FINANCIAL ANALYSIS

1. The financial sustainability of the Sindh Secondary Education Improvement Project has been assessed on a fiscal and project-level basis in accordance with Asian Development Bank (ADB) guidelines.¹ The assessment includes an analysis of historical and projected expenditures to evaluate the impact of the project on the budget of the Government of Sindh (GOS). Since the project has no revenue-earning component, financial costs and benefits are not analyzed.
2. The project aims to increase the inclusiveness of the secondary education system in Sindh Province through investments, capacity building, and policy and program development. The project will (i) finance construction of secondary-level school blocks operated by education management organizations; (ii) improve teaching capacity through the development of an innovative teacher training and mentoring program in five key subjects: English, mathematics, biology, chemistry, and physics; and (iii) strengthen the secondary education examination system.
3. The School Education and Literacy Department (SELD) will be the executing agency and a dedicated independent project implementation unit will be established. Project costs are estimated at \$82.5 million, of which the ADB will finance \$75.0 million. The implementation period is 2020–2025.

A. Macroeconomy and Fiscal Position of the Government of Sindh

4. Since 2009, economic growth in Sindh has increased at an annual average rate of 3.7%.² That is lower than that of the national economy and of other provinces, and is partly the result of natural disasters, including the devastating floods during 2010–2012. Table 1 lists selected indicators for Sindh.

Table 1: Selected Indicators, FY2014–FY2019

Item	FY2014	FY2015	FY2016	FY2017	FY2018	FY2019
	Actual	Actual	Actual	Actual	Rev. Budget	Budget
Provincial GDP growth (%)	4.9	3.2	NA	NA	NA	NA
Total GOS revenues (PRs billion)	491.3	536.7	757.9	693.2	816.1	923.2
Federal transfers (PRs billion)	406.8	433.7	518.2	539.9	619.1	680.1
Provincial revenues (PRs billion)	84.6	103.0	239.7	153.2	197.0	243.1
Total GOS expenditures (PRs billion)	466.3	529.6	592.4	761.0	965.9	1,117.1
Current revenue expenditure (PRs billion)	337.7	393.2	455.0	550.9	683.5	773.2
Development expenditure (PRs billion)	128.6	136.4	137.3	210.1	282.4	343.9
Operating balance (PRs billion)	25.0	7.1	165.6	(67.8)	(149.8)	(194.0)
Education sector spending (PRs billion)	105.1	115.1	131.9	144.3	178.5	229.0
Share of total GOS expenditure (%)	22.5	21.7	22.3	19.0	18.5	20.5

() = negative, GDP = gross domestic product, GOS = Government of Sindh, NA = not available, PRs = Pakistan rupees. Sources: World Bank. 2017. *Sindh Public Expenditure Review*. Washington, DC.; Government of Sindh, Finance Department. 2016. *Budget Strategy Paper 2016/17–2018/19*. Karachi; and Government of Sindh, Finance Department. 2017. *Budget 2018/19—Annual Budget Statement, Volume I, Fiscal Framework*. Karachi.

¹ Asian Development Bank (ADB). 2005. *Financial Management and Analysis of Projects*. Manila; and ADB. 2009. *Financial Due Diligence: A Methodology Note*. Manila.

² World Bank. 2017. *Sindh Public Expenditure Review*. Washington, DC.

5. The GOS's fiscal management is generally prudent and the province maintains a positive operating (and fiscal) balance. The negative operating balance in FY2017 was financed by the large operating surplus in FY2016, which was due to unusually high non-tax receipts.³ Federal transfers, which are unpredictable, account for the biggest share of provincial revenues. In recent years, provincial revenues have grown more quickly than federal transfers.⁴ Revenue expenditures make up most of GOS spending, but their share has declined slightly because development expenditures have increased more rapidly.⁵ Education sector spending represents a significant share—about 20%—of total government spending.⁶

B. Financial Sustainability

6. The recurrent cost drivers of the project outputs have been identified as follows: output 1: number of students (to calculate the recurrent costs of newly constructed school blocks that will be operated by education management organizations), output 2: equipment depreciation costs, and output 3: number of optical mark recognition systems (to calculate maintenance costs).

7. Three types of expenditure analyses are relevant to assess the sustainability of the recurrent costs that will follow from the implementation of the project: (i) the spending of the GOS (in relation to loan repayments), (ii) SELD and the Universities and Boards Department (UBD) (in relation to project recurrent costs), and (iii) the “education affairs and services” component of the GOS's revenue expenditure (in relation to project recurrent costs).

8. **Government of Sindh expenditures.** The GOS pays interest on foreign debt and foreign debt management (loan repayments) from current revenue expenditures. Interest payments start in 2020 while principal repayments will start in 2026. In FY2024, the total payment will be highest—\$5.25 million, equivalent to 0.075% of the total current revenue expenditures of the GOS at the level forecast for the same year (Table 2).

Table 2: Government of Sindh Expenditures on Loan Repayments, FY2015–FY2020
(PRs billion)

Item	FY2015 Actual	FY2016 Actual	FY2017 Actual	FY2018 Revised	FY2019 Budget	FY2020 Forecast	FY2021 Forecast
Current revenue expenditure	393.2	455.0	550.9	651.6	773.2	793.9	847.0
Estimated interest and principal repayment					0.003	0.032	0.082
Relative share (%)					0.000	0.004	0.010

FY = fiscal year, PRs = Pakistan rupees.

Source: Government of Sindh, Finance Department. 2018. *Budget 2018/19—Annual Budget Statement, Volume I, Department-Wise Expenditure Statement*. Karachi; Government of Sindh, Finance Department. 2018. *Budget Strategy Paper 2018/19–2020/21*. Karachi.

³ The operating balance during FY2016–FY2019 would be substantially negative. However, the FY2018 (revised estimates) and FY2019 (original estimates) figures are budgets, which are unlikely to be fully spent as actual expenditure is always 10%–25% less than total expenditure.

⁴ Federal transfers accounted for 83% of total revenues in FY2014, but 74% in the budget for FY2019.

⁵ Revenue expenditures accounted for 72% of total spending in FY2014, but 69% in the budget for FY2019.

⁶ This compares with 18.1% in Bangladesh (2016), 17.0% in Nepal (2015), and 14.1% in India (2013). Source: World Bank. DataBank. World Development Indicators. <http://databank.worldbank.org/data/reports.aspx?source=world-development-indicators>. Last accessed 5 June 2019.

9. The maximum project-related loan repayment as a share of total GOS current revenue expenditures would be low (0.075% for FY2025, based on the GOS's current revenue expenditure forecast for FY2021).⁷

10. **Departmental expenditures.** Based on the present distribution of portfolios among GOS departments, the recurrent costs related to outputs 1 and 2 would be covered by SELD, while those related to output 3 would be covered by the UBD. The actual expenditures of these entities for FY2015–FY2017⁸ and the planned spending for FY2018–FY2020 are in Table 3.⁹

Table 3: School Education and Literacy Department and Universities and Boards Department Expenditures, FY2015–FY2020
(PRs billion)

Item	FY2015 Actual	FY2016 Actual	FY2017 Actual	FY2018 Estimate	FY2019 Budget	FY2020 Forecast
SELD current revenue expenditure	101.7	115.3		151.9	170.8	171.5
SELD development expenditure	6.5	7.3		12.3	16.1	17.3
SELD total expenditure	108.2	122.6	132.5	164.2	186.9	188.8
UBD current revenue expenditure	-	-		5.1	5.0	5.4
UBD development expenditure	-	-		3.6	3.4	3.9
UBD total expenditure	-	-	4.6	8.7	8.4	9.4
Total current revenue expenditure	101.7	115.3		157.0	175.8	176.9
Total development expenditure	6.5	7.3		15.9	19.4	21.2
Total expenditure	108.2	122.6	137.1	172.9	195.3	198.1

FY = fiscal year, PRs = Pakistan rupees, SELD = School Education and Literacy Department, UBD = Universities and Boards Department.

Sources: Government of Sindh, Finance Department. 2017. *Budget 2017/18—Annual Budget Statement, Volume I, Department-Wise Expenditure Statement*. Karachi; Government of Sindh, Finance Department. 2018. *Budget 2018/19—Annual Budget Statement, Volume I, Department-Wise Expenditure Statement*. Karachi; and Government of Sindh, Finance Department. 2017. *Budget Strategy Paper 2017/18–2019/20*. Karachi.

11. SELD's current revenue and development expenditures are significantly larger than those of the UBD, with SELD current revenue expenditures accounting for more than 90% of total expenditure, while the equivalent figure for the UBD is about 60%. The estimated recurrent costs associated with the project's outputs will increase from PRs193 million in FY2022 to PRs2.2 billion in FY2028 (Table 4). While the recurrent costs for outputs 2 and 3 (i.e., nonsalary expenditures) are expected to stay the same in nominal terms, those for output 1 (about two-thirds salary expenditures and one-third nonsalary expenditures) will increase and reach their maximum in FY2028, after which they will remain constant in nominal terms. This is because (i) project schools will open gradually from FY2022, which will increase annual student numbers; (ii) there will be annual increases in cohort numbers, which—given the five grades at secondary level (grade 6–10)—will continue for 4 years after the last batch of schools has started operating in FY2025 (i.e., cohort numbers will increase until FY2028, then remain stable).

12. The estimated project recurrent costs for FY2023 amount to 0.11% of the forecast current revenue expenditures of SELD and the UBD for FY2020 (Table 3). Using the same basis for FY2028, the estimated project recurrent costs that year would amount to 1.25% of the FY2020 forecast current revenue expenditures of SELD and the UBD. However, such a comparison

⁷ The latest forecast available for the Government of Sindh's current revenue expenditure is for FY2021. Last accessed 30 June 2018.

⁸ The Universities and Boards Department (UBD) was established in FY2017, hence data for earlier years are not available.

⁹ The Finance Department's Budget Strategy Paper 2018/19–2020/21 (March 2018), unlike earlier publications, does not include sector- and entity-level medium-term expenditure forecasts. Hence, FY2020 is the latest year for which the planned spending of SELD and the UBD are known and can be shown.

ignores the fact that the GOS's departmental current revenue expenditure budgets increase annually. In other words, the actual project recurrent costs in FY2028 as a share of the two departments' current revenue expenditures would be much lower than 1.25%. The project's impact on the current revenue expenditures of SELD and the UBD is expected to be limited.

Table 4: Estimated Project Recurrent Costs, FY2021–FY2028
(PRs billion)

Item	FY2021	FY2022	FY2023	FY2024	FY2025	FY2026	FY2027	FY2028
Output 1 (students)	0	0.13	0.46	0.86	1.31	1.76	2.02	2.12
Output 2 (equipment)	0	0.04	0.05	0.05	0.05	0.05	0.06	0.06
Output 3 (maintenance)	0	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Total	0	0.19	0.52	0.93	1.38	1.83	2.10	2.21

FY = fiscal year.

Source: Asian Development Bank estimates.

13. **Education affairs and services expenditures.** The bulk of project-related recurrent costs will be covered from the Education Affairs and Services component of the GOS's revenue expenditure. The FY2014–FY2018 actual revenue expenditures for each education subsector are shown as absolute figures in Table 5 and as relative figures in Table 6. The annual total expenditures for education (Table 5) are slightly lower than those of SELD and the UBD combined (Table 3). This is because the SELD figures include technical and vocational education and training, but the UBD figures do not. As can be seen in Table 5, total revenue expenditures are growing at a relatively high annualized rate of about 10%.

Table 5: Education Affairs and Services Actual Current Revenue Expenditure, by Subsector, FY2014–FY2018
(PRs billion)

Item	FY2014	FY2015	FY2016	FY2017	FY2018
	Actual	Actual	Actual	Actual	Actual as of April 2018
091 Pre-Primary and Primary Education Affairs and Services	48.39	54.78	63.08	55.30	49.73
092 Secondary Education Affairs and Services	27.10	29.69	33.29	40.45	39.01
093 Tertiary Education Affairs and Services	15.45	15.32	16.93	21.53	20.15
094 Education services nondefinable by level	1.15	0.91	1.15	0.54	0.52
095 Subsidiary Services to Education	0.52	0.56	0.62	0.46	0.40
096 Administration	7.85	9.03	11.34	16.52	13.13
Total	100.57	110.28	126.41	134.81	122.94

FY = fiscal year.

Sources: Education sector budget execution reports provided by the Government of Sindh, School Education and Literacy Department, Reform Support Unit.

14. The relative shares of education expenditure the subsectors have remained broadly similar over time (Table 6). However, the share of secondary education affairs and services has grown slightly because annual increases have been somewhat higher in this subsector.

Table 6: Education Sector Current Revenue Expenditure Shares, by Subsector, FY2014–FY2018
(%)

Item	FY2014	FY2015	FY2016	FY2017	FY2018
	Actual	Actual	Actual	Actual	Actual as of April 2018
091 Pre-primary and primary education affairs and services	48	50	50	41	40
092 Secondary education affairs and services	27	27	26	30	32
093 Tertiary education affairs and services	15	14	13	16	16
094 Education services nondefinable by level	1	1	1	0	0
095 Subsidiary services to education	1	1	0	0	0
096 Administration	8	8	9	12	11
Total	100	100	100	100	100

FY = fiscal year.

Note: Percentages may not total 100% because of rounding.

Sources: Education sector budget execution reports provided by the Government of Sindh, School Education and Literacy Department, Reform Support Unit.

15. The budget execution rates for salary expenditures in the secondary education subsector are generally high (Table 7). However, they are much lower for nonsalary recurrent expenditure and development expenditures because of funds flow issues, capacity constraints, coordination problems, and procurement bottlenecks.¹⁰ Given that the salary component accounts for about 66% of the original budget (compared with 20%–25% for the nonsalary recurrent component and about 10% for the development component), the high salary budget execution ratio to a large extent explains the high budget execution ratio for the secondary education subsector.

Table 7: Secondary Education Affairs and Services Budget Execution, FY2014–FY2018
(%)

Item	FY2014	FY2015	FY2016	FY2017	FY2018
	Actual	Actual	Actual	Actual	Actual as of April 2018
Salary					
Actual expenditure to original budget	89	87	91	88	59
Actual expenditure to budget released	86	96	103	75	96
Nonsalary					
Actual expenditure to original budget	13	37	52	35	23
Actual expenditure to budget released	89	42	51	48	45
Development expenditure					
Actual expenditure to original budget	58	30	47	-	-
Actual expenditure to budget released	58	80	89	-	-
Total expenditure/average					
Actual expenditure to original budget	87	83	87	84	57
Actual expenditure to budget released	86	92	97	74	94

FY = fiscal year.

Sources: Calculated from budget execution reports provided by the Government of Sindh, School Education and Literacy Department, Reform Support Unit.

16. The expected impact of the project on recurrent costs will be small relative to the GOS's current revenue expenditures.

¹⁰ ADB. 2019. *School Education in Pakistan: A Sector Assessment*. Manila.