Cape Chamber
OF COMMERCE AND INDUSTRY

MEDIUM TERM BUDGET POLICY STATEMENT 2023:

CAPE CHAMBER OF COMMERCE AND INDUSTRY: IMPLIED COMMENTARY AND SUMMARY

To make for easier reading, the structure of the document is based on the up-front stated four key objectives of the Medium Budget Policy Statement (MTBPS).

This also allows for the stated MTBPS initiatives to be measured against the four key objectives, starting with the reconfiguration of the state, as this is the most difficult objective to achieve, with just about everything else dependent on the success of this objective.

Implicitly, that also traces the causes of and mooted possible solutions in the 2023 MTBPS to the current fiscal and socio-economic stresses more closely.

The MTBPS aims to address four key objectives, acknowledging the *hard work*[1] required to deal with what it terms as *pressing challenges*[2].

- Reconfiguring the state for greater efficiency with zero tolerance for waste and corruption.
- Protecting vulnerable households
- Stabilising debt and debt service costs via fiscal consolidation.
- Strengthening jobs-rich and tax revenue enhancing economic growth.

It further notes that government spending per person in real terms has grown from R27 629 in 2008/09 to R33 390 in 2022/23, and in overall annual nominal government spending terms rising over the same period from Rb713 to Rb2100, with little impact on economic growth.

Reconfiguring the state for greater efficiency with zero tolerance for waste and corruption.

Core to the credibility of the MTBPS is the ability of Government to improve future state performance, both from an efficiency and effective perspective, as this is essential for both socio-economic enhancement and curtailment of corruption.

The MTBPS effectively places a more *efficient*[3] state central to both the debt management and growth enhancing objectives, but the credibility of such an objective need to be measured against past similar statements and simply the extent of the challenge and the approach to this as outlined in the MTBPS:

- Firstly, the size and complexity of the state over the three tiers of government. On rough count there are 42 national departments, 209 National Public Entities (including all the major SOE's), 112 Provincial Departments, 76 Provincial Public Entities (including 19 SOE's) and 257 municipalities.
  Total public servant employment of apparently around 1, 2 million individuals across the national and provincial spheres, with another some 250000 municipal employees and a significant number across all the public entities.
- Secondly, the stated intent is to improve the provision of electricity, logistics, infrastructure delivery and making the state more efficient and fit-for-purpose, scaling down overlapping and unproductive programmes, all of the former based on expenditure reviews executed by the National Treasury over the last three years.
- Thirdly, the four sets of criteria to be applied:
    - The performance of the entity/department relative to its assigned mandate.
    - The ability of a larger department to absorb the function(s) of a smaller department.
    - Duplication and overlap of functions across departments and entities; and
    - Clarity and execution of the relevant legislative mandate.

[1] The understatement of the year as this represents the core of the dilemma.
[2] In part articulated in the MTBPS.
[3] As per later, also seems to imply "effectiveness".

- Fourthly, noting that high-level recommendations and entity closures are being formulated by the Presidency, the National Treasury, the Department of Public Service and Administration, the Department of Planning, Monitoring and Evaluation.
- Fifthly, noting that a technical team with the requisite expertise has been constituted to drive implementation.
- Sixthly, to reduce executive responsibilities, improve fiscal credibility and savings in non-interest expenditure.
- Further noting the President's stated intention in his 2022 SONA to professionalise the public service, which has not yet materialised.
- In addition, noting that a review of conditional grants is underway due for completion in 2024, intended to improve intersectoral and interdepartmental coordination and minimising duplications.
- Associated with this, further unspecified work is apparently underway covering a range of initiatives to improve the management of municipalities.
- Further, the development of a compulsory national norms and standards by the National Treasury to regulate municipal surcharges on electricity and the co-identification of alternative sources of revenue to replace these surcharges.
- A conundrum, which has existed for the last 20 odd years, where Heads of Departments as accounting officers do not have direct control over personnel composition and recruitment, the latter falling with the purview of political heads (executive authorities). The reason being that the Public Service Act was never brought in line with that of the Public Finance Management Act, the latter making the political head responsible for policy and the head of the department for execution and delivery[4].
- Interestingly, the MTBPS (Chapter 3: Fiscal Policy) makes the executive authority responsible for managing headcounts and thus operating within assigned budgets.

Noting that the Portfolio Committees of the Chamber have expressed frustration in their dealings with the State over several years, this space will be watched with interest and undoubtedly with a healthy degree of scepticism.

Protecting vulnerable households.

Over the 2024 medium term 61% of the consolidated non-interest expenditure is reserved for the *social wage*, implying planned spending on health, education, housing, social protection, transport, employment and local amenities.

Of this Rb949.9 is meant for social protection transfers (i.e., old age grant, child support grant, disability grant, Covid-19 social relief of distress grant, the latter now extended to March 2025) reportedly collectively representing just over 3% of GDP, representing some of the highest proportions amongst developing economies.

The MTBPS envisages a complete review *before March 2025* of the entire social grant system, jointly by the Department of Social Development and the National Treasury.

Government's public employment programme, i.e., the Expanded Public Works Programme, inclusive of the Community Works Programme, are due to be *repurposed* into the Presidential Employment initiative.

Stabilising debt and debt service costs via fiscal consolidation

[4] Just imagine a CEO being held accountable for the performance of a company, but not having due authority over personnel.

The current debt dilemma is ascribed to poor economic growth, which remains precarious, worsened by load shedding, rail performance, high inflation (nationally and internationally), rising borrowing costs, collapse of commodity prices, VAT refunds and challenges to international economic growth.

Collectively the impact has been a fall in revenue of some Rb56.8 relative to previous estimates, the rise of gross loan debt by 47.2% between 2008/09 and 2022/23, crowding out spending on government's objectives and consuming a greater share of the budget than social development, health, community development, economic development and peace and security, crowding out expenditure on job-creating growth initiatives. Key stated objectives for the MTBPS are:

- Realising a primary budget surplus in 2023/24, implying that for the first time since 2008/09 revenue will exceed non-interest spending and continue to do so over the new MTEF, with debt-service costs peaking in 2026/27.
- Protecting frontline services, i.e., education, health and police services budgets growing in nominal annual terms, but below CPI rates.
- Economic and community development functions are due to grow by 4.5% and 6.2%.
- Only marginal growth is foreseen for general public services.
- Reconfiguration of government functions as previously stated to achieve savings.
- Managing the public sector bill.
- Keeping the composition of spending largely in line with current policy.
- Moderate revenue increases, limiting negative effects on the economy.
- Setting new fiscal spending anchors.
- Stabilising the debt-to-GDP ratio in 2025/26.
- Tax to GDP ratio declining to 24.7% 2023/24.
- With the gross borrowing requirement for 2023/24 increasing from Rb515,6 to Rb563.6, associated with the weighted funding cost[5] increasing from 8.3% in February 2023 to 9.5% in October 2023, it has become necessary to reduce the South African sovereign risk premium, reflecting investor concerns with the weaker economic and associated fiscal outlook.

In-year (2023/24) revenue and revenue outlook

- Gross tax revenue has been revised downwards by Rb56,8., mainly company and VAT tax contributions dropping by Rb35.8 and Rb25.6 respectively, but with PIT[6] rising by Rb6.4.
- Reduced mining profitability, with corporate tax falling by Rb24.6.
- Rb 21.5 higher VAT export related refund payments.
- The National Revenue Fund increases by Rb11.3 due to higher expected evaluation profits from foreign currency transactions.
- Consequently:
  - Main 2023/24 budget revenue has been lowered by Rb44.4, non-interest expenditure lowered by Rb3.7 and debt service costs are revised upwards by Rb14.1.
  - The main budget deficit increases by Rb54.
  - The 2023/24 to 2025/26 Rb254 Eskom debt relief has been incorporated on the balance sheets of both Government and Eskom, with Rb16 of the Rb78 for 2023/24 disbursed by 30 September 2023. Officials from National Treasury and Public Enterprises are assessing compliance with the conditions set for conversion of the loan (moving to interest bearing via amendments to the Eskom Debt Relief Act) to equity.

[5] The average funding cost weighted proportionally by each funding instrument.
[6] Personal income tax.

- Non-interest expenditure of Rb1 694 120 with Rb29 422 for the 2023/24 wage increase for personnel intensive departments.
- Downward adjustments totalling Rb33 130.
- Debt service costs are up by Rb14.1.

Medium Term Revenue and Expenditure Outlook

- Further gains in tax administration are required to improve tax revenues over the medium to long term[7]:
- Overall gross tax revenue increases to R2.1 trillion (25.1% of GDP) by 2026/27 with shortfalls of Rb121 between 2024/25 relative to Budget 2023 estimates.
- Expecting medium employment growth to remain muted.
- Relative to the 2023 Budget, main budget revenues for 2024/25 and 2025/26 have been lowered by Rb152.
- Similarly non-tax revenues decrease by Rb24.4 due to lower petroleum royalties and departmental receipts, with average borrowing of Rb553.7 per annum.
- Main budget non-interest expenditure due to increase by Rb85 relative to Budget 2023 Budget estimates. These include:
    - Reductions of Rb213.3 by reducing baselines, provincial allocations not yet assigned to votes and a net drawdown of 2023 unallocated reserves.
    - Spending additions of Rb128.4 for the carry-through costs of personnel intensive departments, the Covid-19 Social Relief of Distress grant and preservation of the 2025/26 fiscal framework.
    - Reduction of the expenditure ceiling by Rb36.9 and Rb47.3 in 2024/25 and 2025/26 respectively.
- Debt service costs have been increased by Rb51.5, with the main budget deficit to reduce from 4.7% of GDP in 2023/24 to 3.7% by 2026/27.
- Main budget expenditure reaches 29.2% of GDP by 2023/24, reducing to 28.2% by 2026/27, but dependent on realising fiscal consolidation measures, i.e., to lower main budget expenditure below 29% of GDP.
- Maintenance of a prudent fiscal stance, which should aid economic growth and vulnerable individuals in our society, while stabilising public finances and economic risks.

Risks to the medium-term outlook

- Weaker than expected economic growth, both domestically and globally.
- Continued losses by municipalities and SOE's.
- Higher borrowing costs due to the elevated risk premium.

Expenditure priorities: see Table 4.4 Division of Revenue Framework overleaf for the main divisions.

- Bulk of spending focused on social wage, i.e., primarily health, education (basic and fee-free higher) and social protection, but also transport, housing, employment programmes and social security funds, totalling Rb1 211.3, Rb1244.1 and Rb1294.6 over the new MTEF.
- Transport apparently does not include taxis.
- Efficiency improvements and value for money spending and reducing wasteful expenditure and reducing debt costs, which are currently crowding out spending on basic services and other priorities.

[7] It would seem, according to NEWS 24 that government is considering removing tax credits linked to medical aid contributions as one of such steps.

Table 4.4 Division of revenue framework

R billion	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
	Outcome			Revised	Medium-term estimates		
Division of available funds							
National departments	**790,5**	**822,8**	**855,9**	**826,3**	**840,9**	**846,4**	**884,2**
of which:							
Provincial indirect grants	*2,9*	*3,8*	*3,9*	*4,0*	*4,0*	*4,3*	*4,4*
Local indirect grants	*4,1*	*5,7*	*7,2*	*8,3*	*8,0*	*8,3*	*8,7*
Provinces	**628,8**	**660,8**	**694,1**	**706,4**	**720,5**	**752,4**	**784,6**
Equitable share	520,7	544,8	570,9	585,1	589,5	616,4	644,3
Conditional grants	108,1	116,0	123,3	121,3	131,0	136,1	140,3
Local government	**137,1**	**135,6**	**150,7**	**160,6**	**169,2**	**177,3**	**182,9**
Equitable share	83,1	76,2	83,9	95,2	101,2	106,1	110,7
General fuel levy sharing with metropolitan municipalities	14,0	14,6	15,3	15,4	14,5	15,2	15,9
Conditional grants	40,0	44,8	51,4	50,0	53,5	56,0	56,4
Provisional allocations not assigned to votes[1]	–	–	–	–	2,3	38,0	47,1
Projected underspending	–	–	–	-3,3	–	–	–
Non-interest allocations	**1 556,4**	**1 619,2**	**1 700,7**	**1 690,1**	**1 732,8**	**1 814,1**	**1 898,8**
Debt-service costs	232,6	268,1	308,5	354,5	385,9	425,5	455,9
Contingency reserve	–	–	–	0,4	5,0	7,6	14,5
Main budget expenditure	**1 789,0**	**1 887,3**	**2 009,2**	**2 044,9**	**2 123,7**	**2 247,2**	**2 369,2**
Percentage shares							
National departments	50,8%	50,8%	50,3%	48,8%	48,6%	47,7%	47,8%
Provinces	40,4%	40,8%	40,8%	41,7%	41,6%	42,4%	42,4%
Local government	8,8%	8,4%	8,9%	9,5%	9,8%	10,0%	9,9%

1. Includes amounts for projects approved through Budget Facility for Infrastructure and other provisional allocation.

Source: National Treasury

Strengthening jobs-rich and tax revenue enhancing economic growth

Government accepts that the central problem is low economic growth, with amongst others, frequent power cuts, deteriorating rail freight and desultory port operations impacting negatively on business sustainability and exports.

Associated with these are low capital investment, too many inefficient and overlapping government services/activities.

On top of domestic troubles, the international economic outlook has also dimmed, e.g., in China, higher persistent inflation levels in most countries, geopolitical tensions and conflict.

All the above make South Africa vulnerable to external shocks, making major reforms essential as the economy in its current state does not generate sufficient revenue to service government expenditures and its rising debt levels.

The stated intention is to deal effectively with these conundrums over the next three years via amongst others:

- The reconfiguration of the state.
- Establishment of new fiscal anchors to ensure fiscal sustainability and fiscal credibility.

- Rising primary budget surplus.
- Containment of the public sector wage bill.
- A new mechanism to crowd in financing from the private sector and international finance institutions for large infrastructure projects.
- Stabilise energy supply, building on measures/reforms for private energy generation, improving Eskom plant maintenance and management, unbundling of Eskom, revised regulations to de-monopolise the power grid and Eskom debt relief, the latter subject to strict conditions.
- Seeing that previous higher public spending did not bolster economic growth due to the weak multiplier effect, it in turn affected by debt finance increases, SOE bailouts, ineffective programmes and increasing vulnerability to global conditions, a new approach is required.
- The new approach includes fiscal discipline, reorienting government spending to enhance growth and developmental goals, and amongst others, to improve infrastructure delivery.
- Reducing the premium investors are demanding to invest in South Africa with debt servicing costs deemed a major investment risk: currently for every R5 collected as revenue, R1 goes to lenders.
- Calculated debt service costs will reach Rb385,9 in 2024/25 and Rb455,9 in 2026/27, with the generated revenue not able to service the additional interest costs and thus crowding out service delivery expenditure.
- To be able to service the debt, a primary budget surplus of 1.3% of GDP is required.
- Infrastructure delivery investment, quantitatively and qualitatively, is seen as central to achieving higher growth rates, but only achievable if the private sector is brought in to both co-finance and provide the expertise to deliver fit for purpose infrastructure. Part of this equation is for government to create alternative financing instruments and widen the scope for concessional borrowing. Further detail to be provided in the 2024 Budget.