2019

MTBPS

MEDIUM TERM BUDGET POLICY STATEMENT

RESPONSE TO PUBLIC HEARINGS ON THE 2019 MTBPS

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

2030 NDP

List of organisations that made submissions for public hearings on the 2019 MTBPS

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- African Women Chartered Accountants (AWCA)
- Black Tobacco Farmers Association (BTFA)
- British American Tobacco (BAT)
- Budget Justice Coalition
- Congress of South African Trade Unions (COSATU)
- Financial and Fiscal Commission (FFC)
- Fiscal Cliff Study Group
- Helen Suzman Foundation
- Limpopo Tobacco Processors (LTP)
- Parliamentary Budget Office
- Pietermaritzburg Pensioners Forum
- PricewaterhouseCoopers (PwC) Tax Services (Pty) Ltd
- Rural Health Advocacy Project (RHAP)
- ShotSpotter
- The South African Institute of Chartered Accountants (SAICA)
- Tobacco Institute of Southern Africa (TISA)
- WoMin African Alliance and International Rivers
- Organisation Undoing Tax Abuse (OUTA)

Main comments from public hearings

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1. **Economic growth and revenue forecasts**
    - Causes of the large revisions
    - Medium-term growth and revenue forecasts
2. **Fiscal sustainability**
    - Fiscal targets and rules
    - Austerity/stimulus debates
3. **General budget matters**
    - Infrastructure expenditure
    - Financial support for Eskom and state-owned companies
    - Improving efficiency and reducing wasteful expenditure
    - Tobacco taxes

Introduction

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- Since Budget 2019, the public finances have experienced a series of shocks:
  - Nominal GDP has been revised down due to weaker real GDP growth (including a contraction in the first quarter), lower GDP inflation, and statistical revisions to the size of the economy
  - Tax revenue projections have been revised down over the medium term, reflecting weak in-year collections, and the lower tax base outlook
  - Spending pressures have increased, including additional support to Eskom and other state-owned companies, together with a reversal of estimated savings from compensation measures (including early retirement)
- Government has taken the first steps towards debt stabilisation through reductions amounting to R49.5 billion over the next two years, and non-interest expenditure growth limited to CPI inflation in the outer year.
- On their own, these interventions are not sufficient. The MTBPS 2019 proposes a series of growth reforms and fiscal measures that, if effectively implemented, should restore the momentum of growth and stabilise the public finances

Latest debt projections

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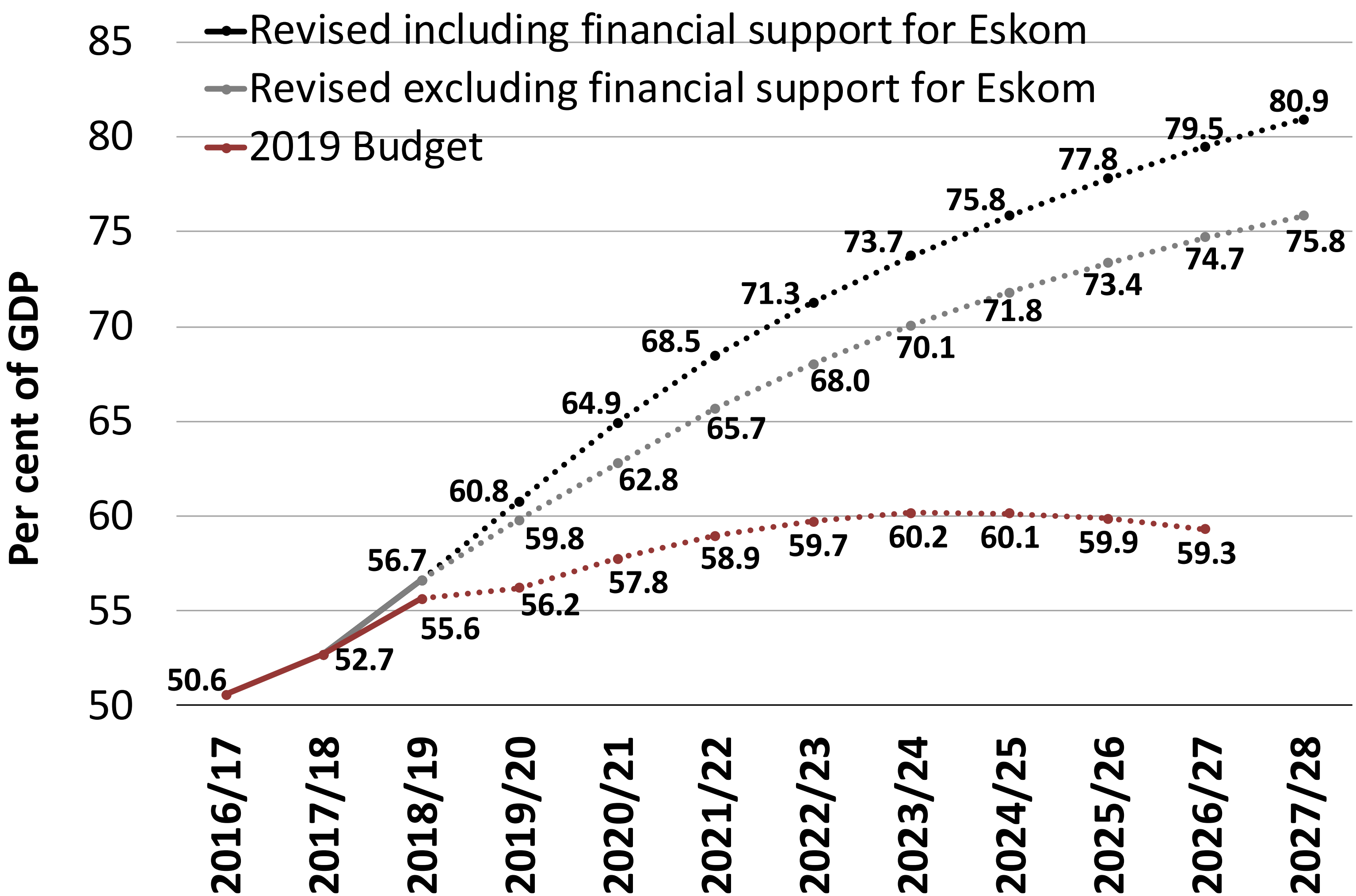

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Real GDP growth and tax revenue forecasts

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Institution	Last Update	2019	2020	2021
National Treasury	**September 2019**	**0.5**	**1.2**	**1.6**
IMF	October 2019	0.7	1.1	n.a
World Bank	October 2019	0.8	1.0	1.3
SARB	September 2019	0.6	1.5	1.8
BER	October 2019	0.4	1.0	1.6
Reuters - median	September 2019	0.6	1.3	1.6
Reuters - average	September 2019	0.6	1.3	1.6
Bloomberg	October 2019	0.6	1.4	1.6

*Bloomberg weighted average assigns a higher weight to more recent forecasts

Sources: NT; IMF; WB, SARB; BER; Reuters; Bloomberg

- National Treasury published all the tax bases and buoyancies used to calculate the revenue forecasts (page 68 of 2019 MTBPS)
- No change in methodology: all buoyancies, except personal income tax, at 1

Economic reforms to raise GDP growth

- Short-term reforms can be implemented immediately, without significant state resources:
  - Support tourism by reducing cost of traveling to South Africa, cutting red tape for small business in the tourism sector
  - Diversify power generation by granting licences for small-scale power generation projects approved by the Minister of Energy
  - Expand telecommunications services by allowing the rapid expansion of fibre infrastructure
  - Lower the cost of doing business by automating registration and filing processes.

- Medium-term reforms should begin immediately in transport, water, telecommunications, and industrial and trade policy

Increase in debt-to-GDP amongst highest of peer economies

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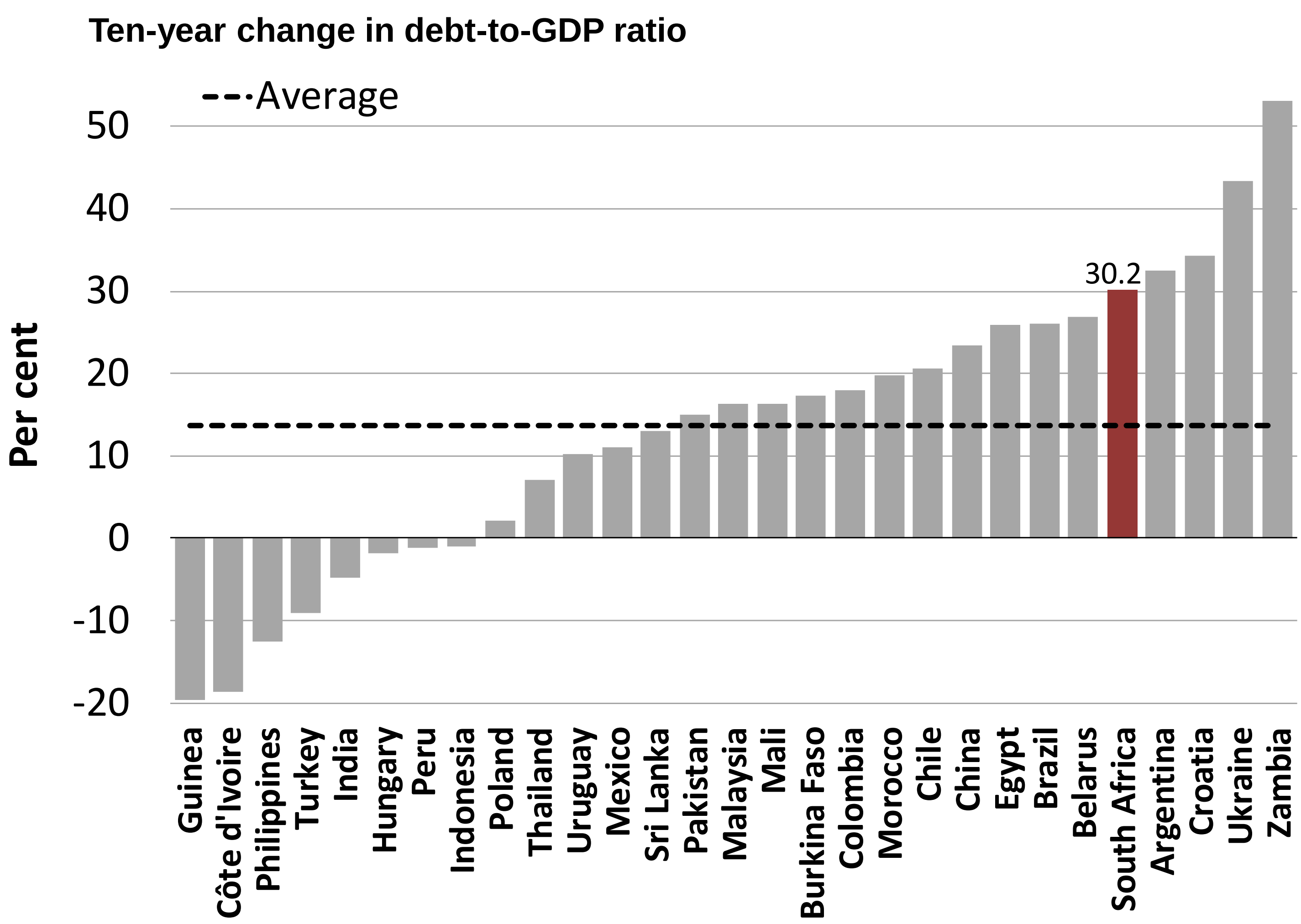

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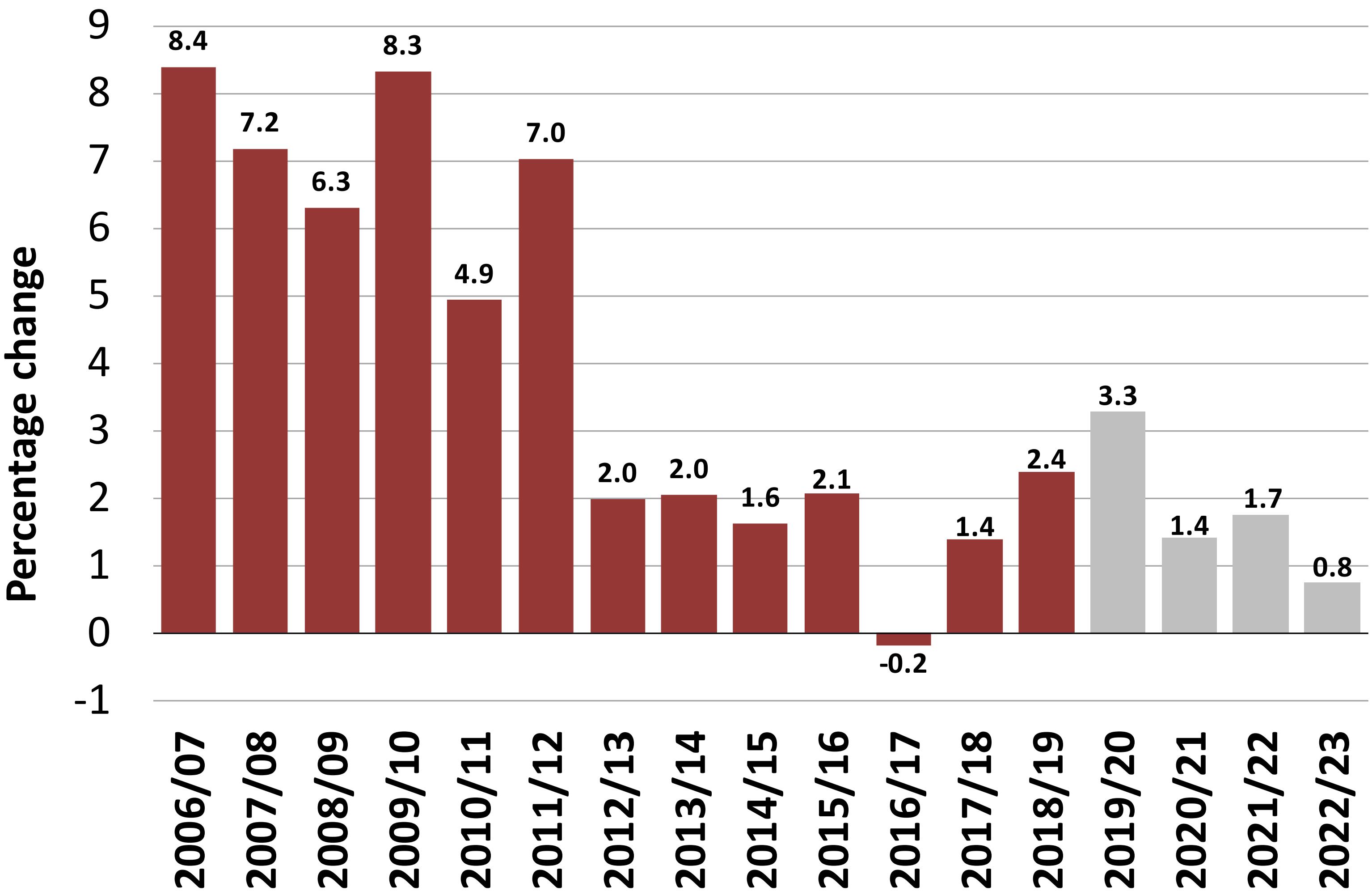
Real main budget non-interest spending grows in real terms



**Excluding Eskom financial support and transactions in financial assets and liabilities*

Main budget deficit

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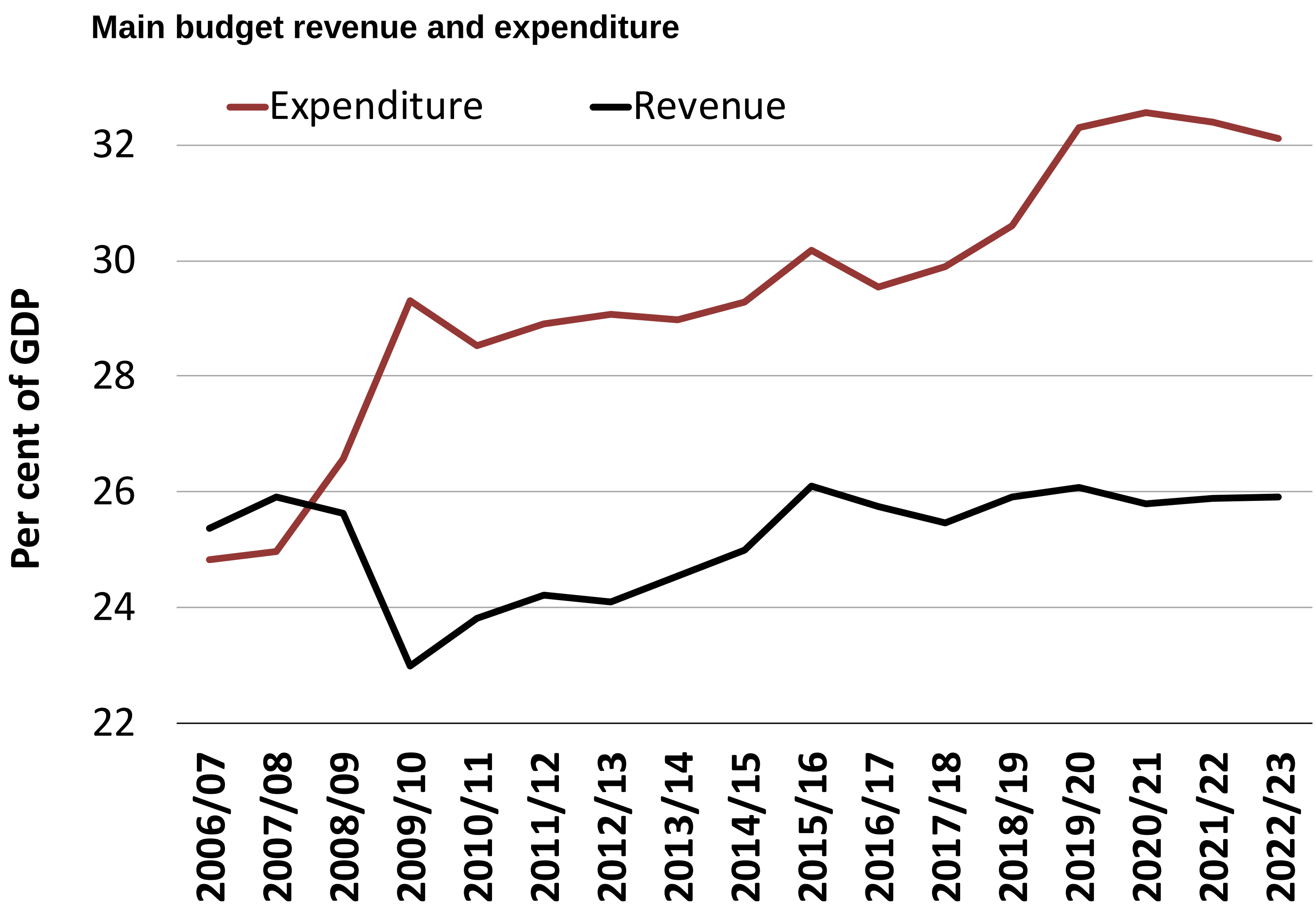

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Spending growth by function group

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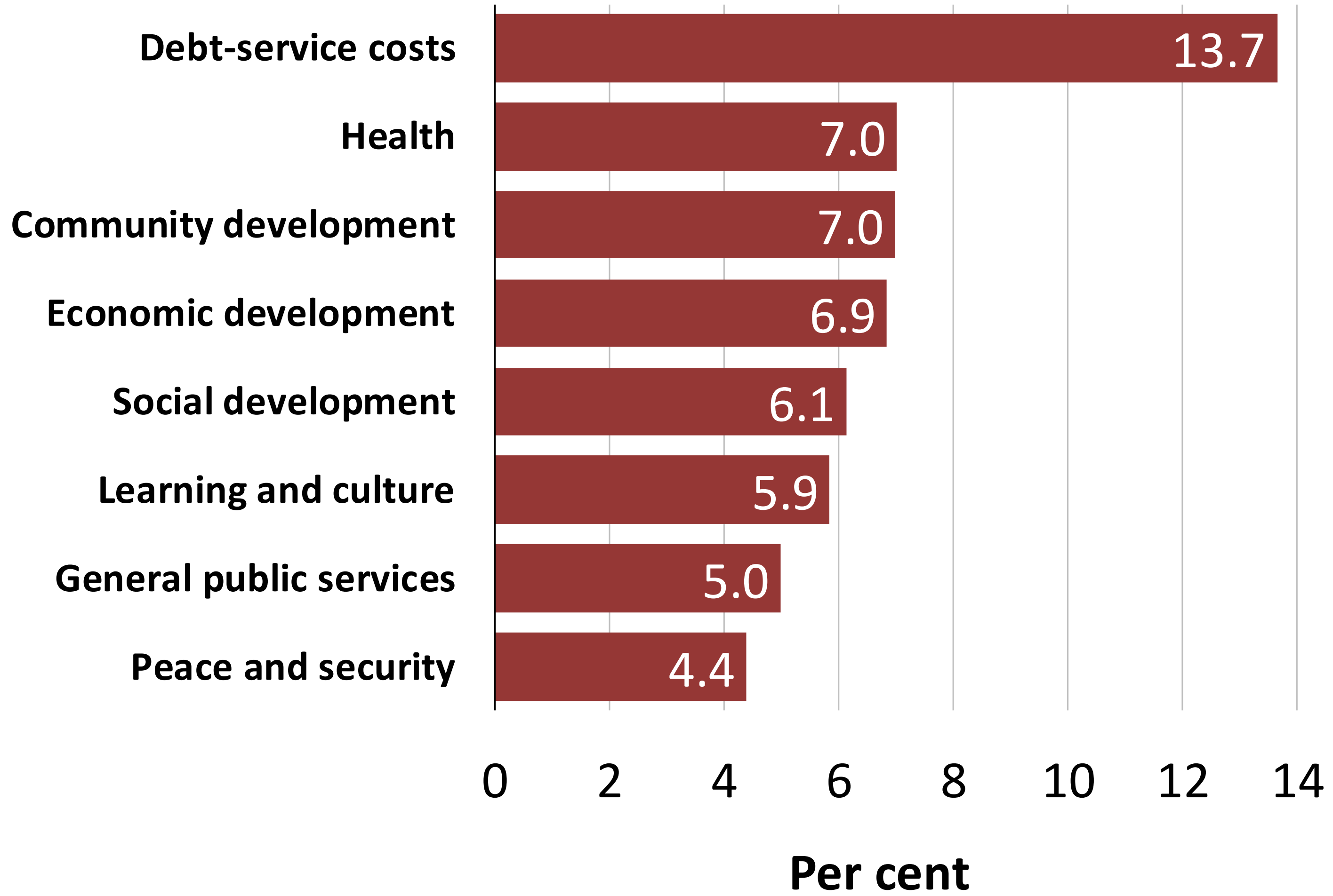
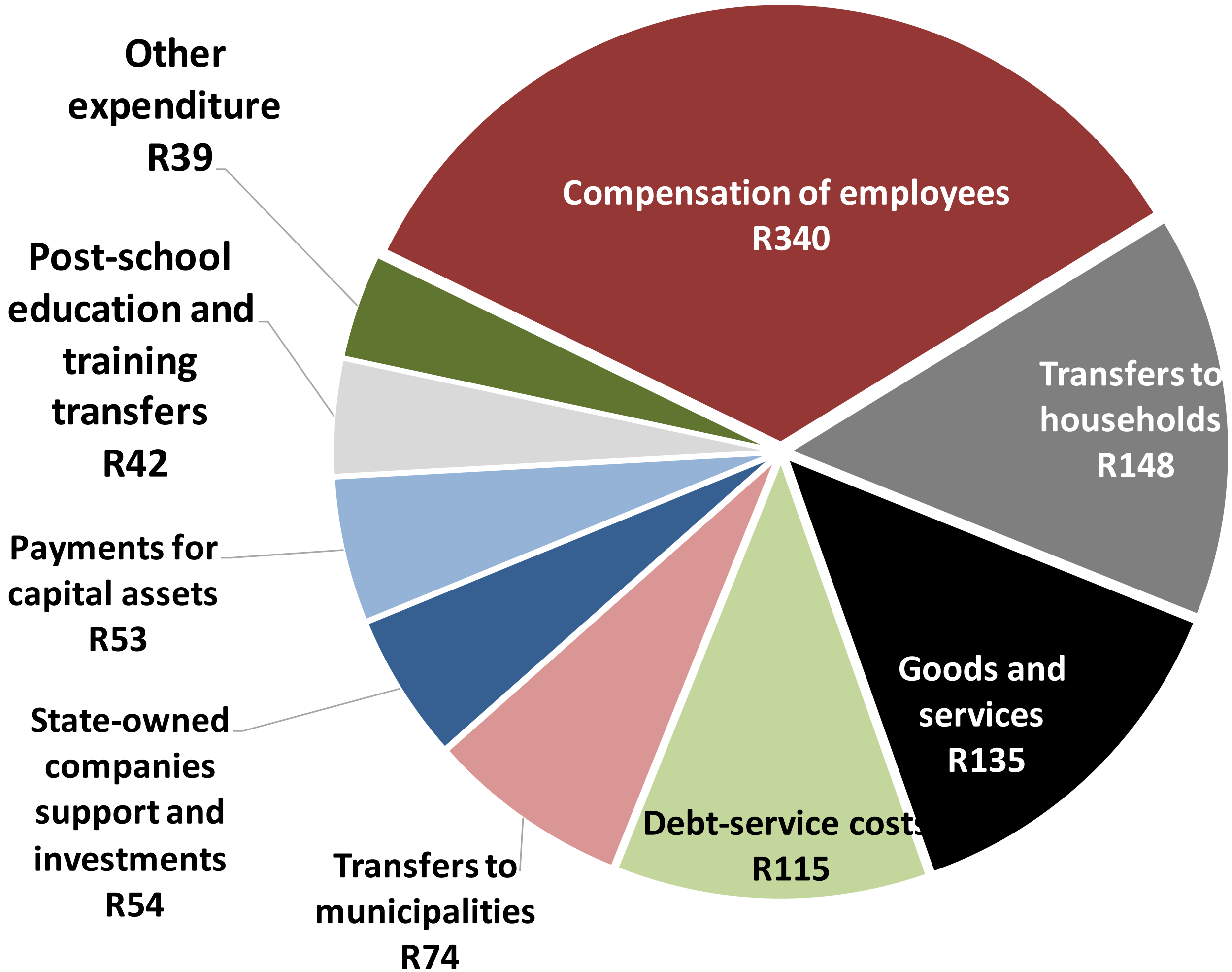
Average nominal growth in consolidated spending, 2020/21 – 2022/23

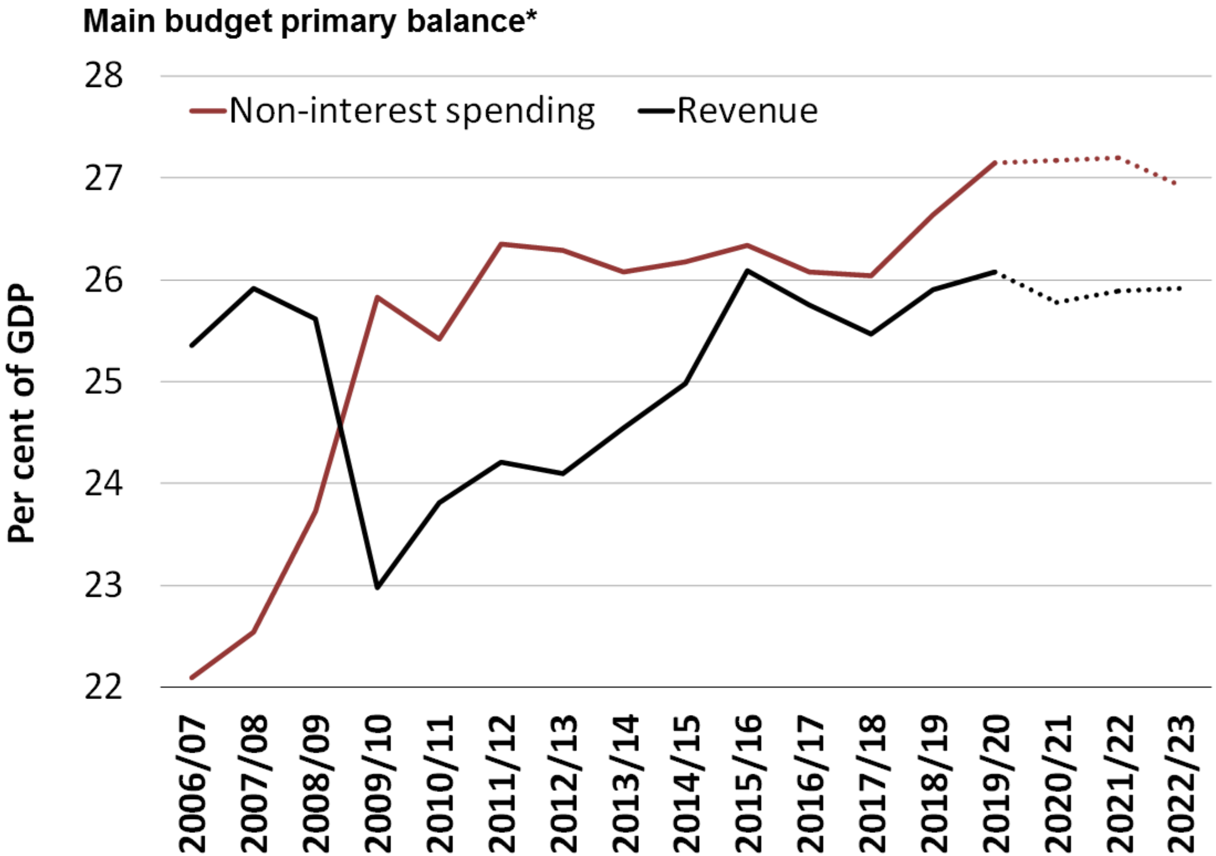


Breakdown of every R1 000 spent by economic classification, 2019/20



- Financial payments (mostly support for state-owned companies), debt-service costs and wages are the fastest-growing areas of expenditure

Fiscal target



**Excluding Eskom financial support and transactions in financial assets and liabilities*

- MTBPS 2019 proposes targeting a main budget primary balance by 2022/23, excluding Eskom financial support
- Fiscal rules are difficult to apply in highly uncertain economic environments

Fiscal dilemma in a low growth, high debt environment

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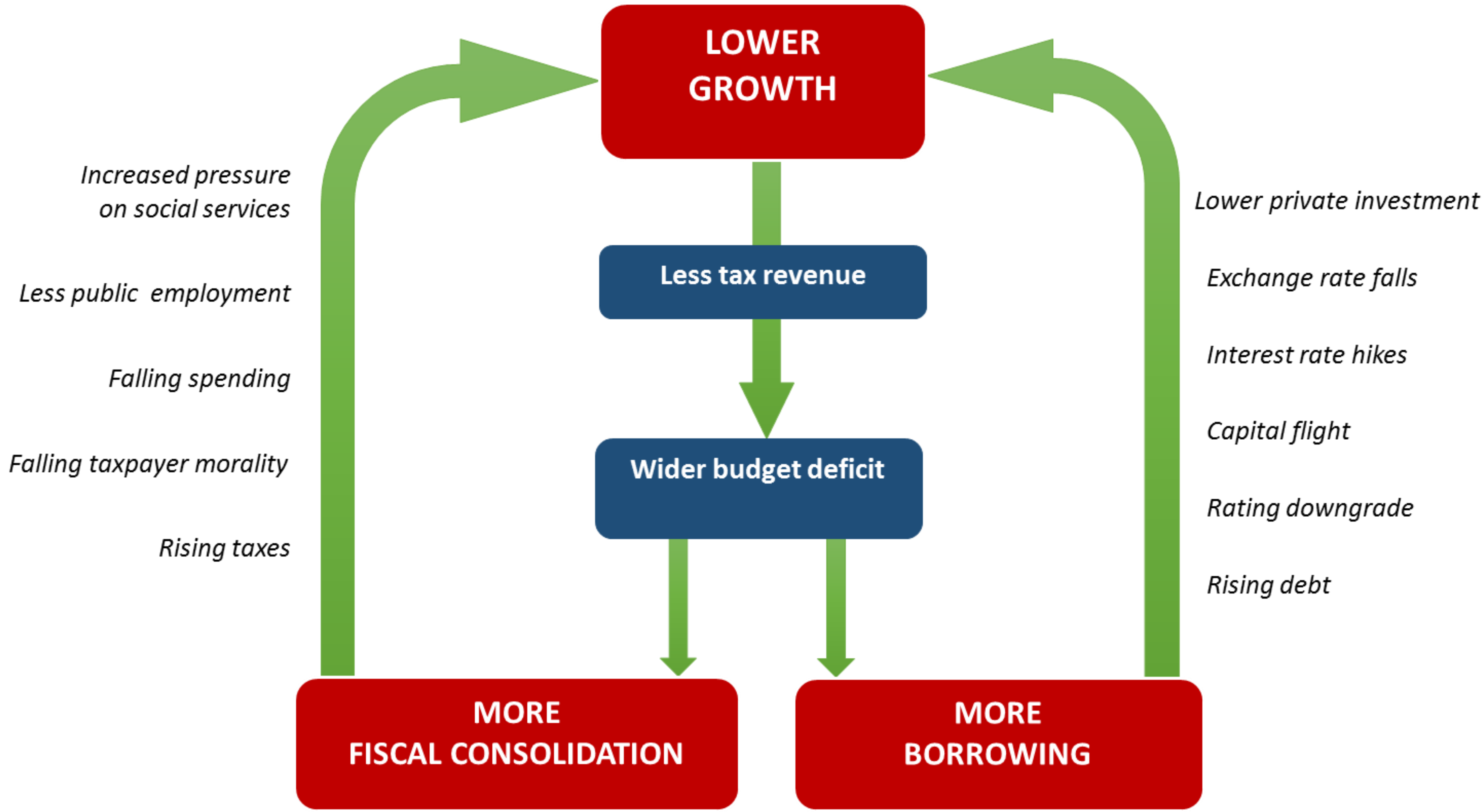


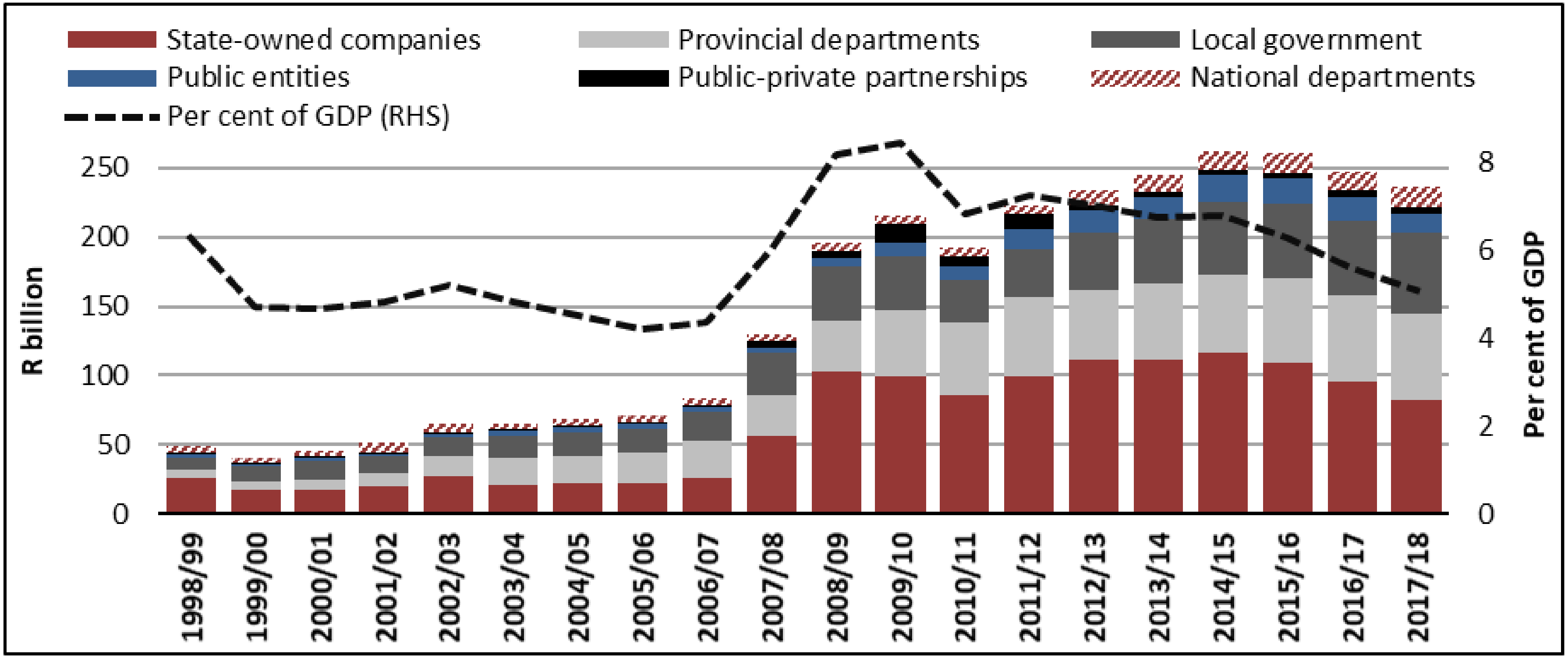
Austerity/stimulus debate

- Growth and distributional consequences of fiscal choices
  - More borrowing does not necessarily translate into higher growth
  - Fiscal stimulus cannot address underlying structural issues
  - Rising debt-service costs crowd out other areas of spending over time
  - Increasing reliance on foreign savings raises vulnerability to external shocks
- Quality of borrowing is crucial
  - Consumption vs investment
  - Ability to spend efficiently
- Spending reductions may have short-term harmful effects on growth. But the implications of a fiscal crisis would be profoundly negative

Fiscal proposals

- Government is proposing that debt stabilisation be achieved through a measured reduction in spending growth, applied primarily to compensation
    - Previous reductions to spending growth have mostly been applied to goods and services and capital budgets
- In designing this intervention, fairness and impact on service delivery must be considered including, where possible:
    - Relatively higher burden on higher-income earners
    - Application to the wider public sector (i.e. public entities and state-owned companies)
- Revenue options are limited, but will be considered. Efforts are also required to boost non-tax revenue
- Growth reforms are crucial, but are unlikely to raise potential GDP immediately

Public infrastructure spending



- Provisional numbers show that the public sector spent 80 per cent of its infrastructure budget in 2018/19, with the largest underspending in the local government and state-owned company sectors

Interventions to support public infrastructure spending

- Budget Facility for Infrastructure (BFI) is an institutional process to appraise and evaluate large infrastructure projects
- Funding for the PICC, GTAC and the DBSA to assist government institutions with project preparation and planning
- Infrastructure delivery improvement programme provides technical assistance and training for the provincial and national departments of health, education and public works
- Framework for Infrastructure Delivery and Procurement Management System (FIDPMS) aims to bring about efficiencies through coordinated management of the procurement processes
- Local government grants review is focussing on eliminating inefficiency and underspending by reviewing the overall grant structure and improving asset management
- Infrastructure Fund’s implementation unit has been established in the DBSA, and has identified potential projects in excess of R500 billion. A review of public-private partnership regulation is under way

Interventions to stabilise Eskom and other state-owned companies

- Eskom: provisional support of R49 billion available in 2019/20, R56 billion in 2020/21 and R33 billion in 2021/22, to secure energy supply and to honour the state's contractual obligations
  - Independent experts have been appointed to analyse the utility's daily cash-flow management and assess the implementation of operational efficiencies
  - National Treasury and Department of Public Enterprises are working with Eskom to separate the entity into three functions (generation, transmission, distribution)
  - Additional reforms to reduce Eskom's debt burden will only be considered once the utility reduces costs and makes progress in the unbundling process.
- Funding for South African Airways (SAA), the South African Broadcasting Corporation, Denel and South African Express amounts to R10.8 billion in the current year.
- Most SOCs are unlikely to generate sufficient cash flow to sustain operations in their current configuration. Operational changes are required urgently

Improving efficiency and reducing waste

- Reprioritisation: NPA receives an additional R1.3 billion, and SARS receives an additional R1 billion for the period 2019/20 to 2022/23, to combat corruption and improve revenue collection

Over the coming year, government will:

- Merge and consolidate entities and regulatory agencies, as well as consider salary controls at a wider range of public entities
- Dispose of unused land and other assets
- Initiate work to limit claims against the state, including through a review of medico-legal claims and accelerated implementation of the Road Accident Benefit Scheme
- Implement recommendations from expenditure reviews to identify cost savings and improve efficiency
- Manage the benefits received by political office bearers, through reforms to the Ministerial Handbook
- Review the existing procurement regulatory framework, through the Public Procurement Bill, to simplify procurement processes and governance. The bill will be gazetted for public comment once Cabinet grants approval to do so

Excise duties on tobacco

- Greater enforcement is required to reduce illicit tobacco and improve tax collections on excise duties of tobacco
- Weaknesses in enforcement over the past few years were described in the Final Report of the Nugent Commission of Inquiry
- New SARS Commissioner is implementing recommendations of Nugent Commission
- The Illicit Economy Unit has been re-organised and is strengthening its efforts to deal with illicit tobacco, as well as compliance concerns in the trade of clothing and textiles, poultry, gold and fuel.
- SARS are progressing towards a track-and-trace system to combat illicit tobacco and have placed officials in manufacturers to more actively audit production
- SARS will provide greater detail to the Committees in a dedicated session on this issue that is scheduled for 20 November 2019