PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA

RESEARCH UNIT

PO Box 15 Cape Town 8000 Republic of South Africa
Tel: 27 (21) 403 8273 Fax: 27 (21) 403 8118
www.parliament.gov.za

BUDGET 2022:

LAYING THE FOUNDATION FOR ECONOMIC RECOVERY

The Budget is an important policy, planning and monitoring instrument that can be used by Parliament to oversee the alignment of the proposed expenditure with Government policy priorities and more broadly alignment to the National Development Plan (NDP) goals as well as other short-term goals such as dealing with the pandemic. The Budget can also be used an oversight tool for monitoring the implementation and achievement of priority service delivery outputs towards the realisation of the NDP goals.

The 2022 Budget focuses on fiscal sustainability; economic recovery and reconstruction; social wage; job creation; and a rigorous response to the economic cost of the COVID-19 pandemic with spending on learning and culture (24.3%), social development (18.1%) and health (13.8%) continuing to dominate. Given the high level of unemployment, the special COVID-19 Social Relief of Distress Grant is extended for 12 months until March 2023. The 2022 Budget proposes supporting economic growth through a range of reforms, including infrastructure built programmes, financed through innovative funding mechanisms. With regard to ailing SOEs, the 2022 Budget resolves to implement various measures to improve financial and operational performance, as well as measures to minimise risks to the fiscus.

This brief provides a snapshot of the Government's spending priorities for 2022 as well as risk factors to both revenue and expenditure projections for the year ahead as well as implications for oversight.

1.The Economic Outlook

- **Global economic outlook weaker than initially anticipated**
  - Global growth is projected at 4.4 per cent in 2022 and is expected to decline further to 3.8 per cent in 2023.[1]
  - Emerging market and developing economies (EMDEs) are projected to grow at a slightly faster rate than advanced economies in both 2022 and 2023.
    - The growth rate of advanced economies is projected at 3.9 per cent in 2022 and is expected to contract to 2.6 per cent in 2023, while the growth rate of EMDEs is projected at 4.8 per cent and 4.7 per cent in 2022 and 2023, respectively.[2]

- **The main risks to the global economic outlook**

[1] IMF (2022).

[2] Ibid.

- Vaccination rollouts in emerging market and developing economies have been slow:
  - This poses a risk to global economic recovery if new variants of COVID-19 emerge and circulate widely, especially if it also results in economic activity being disrupted for longer periods.[3]
- The United States' withdrawal of the fiscal support package together with supply chain disruptions and a less accommodative monetary policy[4] may place undue pressure on emerging market currencies. [5]
- China's deepening property crisis also likely to impact negatively on growth projections.[6]

- **South Africa's growth rates remain low over the medium-term**

  - In contrast to the 2021 Medium Term Budget Policy Statement (MTBPS) growth forecast of 1.8 per cent for 2022, South Africa's real gross domestic product (GDP) growth is now projected at 2.1 percent in 2022 before slowing to 1.6 per cent in 2023, and 1.7 per cent in 2024.[7]

- **The main risks to the domestic outlook**

  - In the context of slow vaccination rollouts, new COVID-19 variants leading to a new wave of outbreaks may mean that the country has to re-impose stricter mitigation measures, which could result in a prolonged decline in economic activity.
    - As it stands, only 42.58 per cent of the adult population has been fully vaccinated, with KwaZulu-Natal and Mpumalanga experiencing the lowest vaccination rates of 36.20 per cent and 38.12 per cent, respectively.[8]
  - The impact of load-shedding on economic activity, increasing inflation and borrowing costs remain a threat.

- **The effects of COVID-19 on job creation, unemployment, depress tax revenues and increase demands on the fiscus**

  - COVID-19 has resulted in millions of people losing their jobs with women experiencing much larger job losses and reduction in hours worked than men.[9] According to the National Income Dynamics Study-Coronavirus Rapid Mobile Survey, whilst there has been evidence of some employment recovery for both men and women, it tends to be slower for women.

[3] Ibid.

[4] Generally speaking, accommodative monetary policies "aim to make interest rates sufficiently low to spur strong enough economic growth to reduce unemployment or to prevent unemployment from rising" (Federal Reserve, 2015).

[5] IMF (2022).

[6] Ibid.

[7] Ibid.

[8] RSA (2022).

[9] Casale and Shepherd (2021).

- The country's official unemployment rate, which is calculated using the number of persons who are employed and unemployed but excludes economically inactive[10] persons, has increased from 34.4 per cent in the quarter two of 2021 to 34.9 per cent in quarter three of 2021.[11]
    - In quarter three of 2021, the rate of unemployment among women stood at 37.3 per cent and 32.9 per cent for men.
- With the already high levels of unemployment and poverty, the pandemic has compounded these challenges, which puts more pressure on the State to provide social grants and other relief measures.

- **The inflation outlook and the repurchase rate**

    - Inflation remains well within the South African Reserve Bank (SARB) target range of 3-6 per cent.
        - The consumer price index (CPI) inflation forecast for 2021 is 4.5 per cent.[12]
    - According to the South African Reserve Bank (SARB), the risks to the inflation outlook have been assessed to the upside. Electricity and other administered prices present short and medium-term risks, while higher domestic import tariffs and higher wage demands present long term upside risks.[13]
    - The repurchase (repo) rate[14] has increased by 25 basis points from 3.75 per cent to 4 per cent per annum as of January 2022.

- **Business confidence declines in most sectors, while consumer confidence improves but remains depressed**

    - Owing to the NUMSA strike and load-shedding, supply chain disruptions and the intensification of stock shortages, most sectors experienced a decline in confidence levels:
        - Apart from building confidence levels, confidence levels in the retail, manufacturing and new vehicle trade sectors declined in the fourth quarter of 2021.
    - Between quarter three and quarter four of 2021, consumer confidence improved but remains depressed:
        - Consumer confidence levels for high-income households remain unchanged between quarter three and quarter four of 2021, but increased slightly for middle and low-income households.[15]

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[10] A person is considered economically inactive if they were able and available to work in the week prior to the Quarterly Labour Force Survey being administered, but did not work or look for work or start their own business.

[11] Stats SA (2022).

[12] National Treasury (2022a).

[13] SARB (2022).

[14] The repo rate determines the interest rate at which the central bank lends money to commercial banks — which then affects the amount they lend to their consumers.

[15] Ibid.

2. The Fiscal Outlook

Table: Consolidated fiscal framework

R billion/percentage of GDP	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
		Outcome		Revised estimate		Medium-term estimates	
Revenue	**1 447,7**	**1 519,3**	**1 406,0**	**1 721,3**	**1 770,6**	**1 853,2**	**1 977,6**
	26,7%	*26,7%*	*25,3%*	*27,5%*	*27,5%*	*27,2%*	*27,3%*
Expenditure	**1 642,5**	**1 807,1**	**1 964,1**	**2 077,0**	**2 157,3**	**2 176,8**	**2 281,8**
	30,3%	*31,8%*	*35,3%*	*33,2%*	*33,5%*	*32,0%*	*31,5%*
Non-interest expenditure	*1 450,5*	*1 593,1*	*1 722,3*	*1 800,2*	*1 846,4*	*1 833,1*	*1 909,8*
	26,8%	*28,0%*	*30,9%*	*28,8%*	*28,7%*	*26,9%*	*26,4%*
Budget balance	**-194,9**	**-287,8**	**-558,1**	**-355,7**	**-386,6**	**-323,6**	**-304,2**
	-3,6%	*-5,1%*	*-10,0%*	*-5,7%*	*-6,0%*	*-4,8%*	*-4,2%*

Source: National Treasury

- **Revenue outlook has improved with higher than expected corporate income tax collections and stronger personal income tax.**
    - The economic and revenue outlook improved since the 2021 MTBPS. In the tabled 2022 budget, tax collection for 2021/22 are expected to exceed the 2021 budget estimate by R181.9 billion and the 2021 MTBPs estimate by R61.7 billion.
    - The improved performance of the economy has been largely attributed to elevated commodity process and consumption (VAT) performing above expectations.
    - Funding pressures from State-owned companies such as South African Special Risk Insurance Association (SASRIA) have forced National Treasury to allocate a total of R22 billion through the Special Appropriation during 2021/22.

- **Higher-than-anticipated tax revenue allows the Government to narrow the deficit large debt burden while increasing non-interest expenditure to support economic growth, job creation and social protection.**
    - The 2022 Budget introduces various budget proposals on the back of high unemployment levels. As people recover from job losses, the additional revenue will address immediate spending pressures, including extending the special COVID-19 *Social Relief of Distress Grant* for 12 months until March 2023.
    - Furthermore, over the medium term, the 2022 Budget proposes supporting economic growth through a range of reforms, including infrastructure built programmes, financed through innovative funding mechanisms.
    - As the country is facing high debt service costs, it may be argued that difficult decisions must be taken for the economy and fiscus. This would then require State entities and the

Criminal Justice Cluster to clamp down on corruption, looting of State resources and wasteful expenditure.

- **Without higher economic growth to support long term revenue collections, options to stabilise the fiscus are becoming increasingly limited**

    - Tax proposals announced in the 2022 Budget include providing relief of R5.2 billion to support households and includes not adjusting the General Fuel Levy and the Road Accident Fund.
    - The Employment Tax Incentive (ATI) is expanded to a maximum of R1 500 in the first 12 months. This is to encourage businesses to employ more young people.
    - National Treasury has drafted legislation to address tax avoidance opportunities on interest limitation rules to enable better alignment with OECD/G20 recommendations on base erosion and profit shifting.
    - The Government proposed to make changes to tax incentives, namely, the Research and Development incentive will be extended while Section 12(DA), 1 2F, 12O and Section 13*sept* of the Income Tax Act will reach their sunset date.
    - In the 2020 Budget, the Government already started discussions on vaping proposals. Further consultation will continue to take place before being introduced in 2023.
    - There is an increase in the health promotion levy, which will increase to 2.31c/g from 1 April 2022.

- **Debt is increasing and to stabilise at 75.1%**

    - Government debt is projected to rise to R4.35 trillion in 2021/22. A portion of revenue improvements will be used to reduce the deficit over the Medium-Term Expenditure Framework (MTEF) period. As a result, the debt trajectory improves compared to the 2021 MTBPS.
    - Gross loan debt will stabilise at 75.1 per cent of GDP in 2024/25, a year earlier and at a lower level than projected in the 2021 MTBPS.
    - The Government expects to realise a primary surplus – where revenue exceeds non-interest expenditure by 2023/24, a year earlier than projected in the 2021 MTBPS. Achieving this objective will enable the Government to bring fiscal consolidation to a close.
    - The debt trajectory is threatened by high fiscal risks such as credit ratings and slow economic recovery and uneven implementation of reforms. National Treasury states in their presentation that the largest risk to recovery of public finances is:
        - “Deterioration in GDP growth.
        - Higher-than-expected global inflation could lead to higher global interest rates, affecting debt-service costs and the exchange rate.
        - The weak financial position of several State-owned companies that rely on Government support to operate.
        - A public service wage agreement exceeding the rate of growth of the compensation budget. An adverse decision by the Constitutional Court in the case relating to the 2018 wage agreement could significantly increase compensation costs.

- Additional spending pressures from new spending programmes or the realisation
  of contingent liabilities would affect the sustainability of the public finances, and could require spending cuts elsewhere.
- The Government's debt redemptions over the next five years will average about R150
  billion per year. Additional debt financing could increase refinancing risk and result in higher associated costs."

3. Medium Term Expenditure Priorities and Key Expenditure Measures

- **In terms of key highlights and themes, the 2022 medium term expenditure priorities remain unchanged from previous budgets with key focus being on: fiscal sustainability; economic recovery and reconstruction; social wage; job creation; and a rigorous response to the economic cost of the COVID-19 pandemic.**

  - The decision to retain the above-mentioned focus areas is logical given the prolonged levels of low economic growth and high unemployment[16], as well as social vulnerability caused by high poverty levels and the effects of COVID-19 pandemic.

  - As part of fiscal sustainability, reprioritization remains the main instrument for new expenditure commitments. Unfortunately, this will add more strain on various departments, municipalities and public entities that have been affected by fiscal consolidation for over a decade.

  - The primary surplus[17] projected by 2023/24 offers an opportunity for an end to fiscal consolidation. Such opportunity is, however, contingent on notable economic growth and decisive action against current fiscal risks (i.e. unsound financial position of State Owned Entities (SOEs), a sizeable wage bill, electricity supply constraints etc.).

- **In terms of allocations:**

  - The 2022 Budget proposes a consolidated government spending of R6.62 trillion over the medium term. At 59.4 percent of non-interest spending, the social wage still accounts for the majority of the proposed consolidated spending over the medium term.

  - The main budget non-interest spending increases by a net amount of R282.3 billion over the 2022 MTEF period compared to the 2021 Budget. Additional allocations (i.e. R110.8

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[16] Stats SA reports that as per Q3 of 2021, youth aged 15-24 years and 25-34 years recorded the highest unemployment rates of 66.5% and 43.8% respectively.

[17] A primary surplus occurs when revenue exceeds non-interest expenditure.

billion in 2022/23, R60 billion in 2023/24 and R56.6 billion in 2024/25) are provided for several priorities that could not be funded through reprioritisation. These include:

- R44 billion allocation for the extension of the *special COVID-19 Social Relief of Distress Grant* for 12 months in 2022/23.
- R18.4 billion to support youth employment and the creation of short-term jobs in 2022/23 and 2023/24 under the Presidential Employment Initiative.[18]
- R32.6 billion for financial support to current bursary holders and first-year Students under the National Student Financial Aid Scheme.

- Over the medium term, the composition of spending by functions is still dominated by learning and culture, which receives the largest allocation (24.3%). The other two dominant function groups are social development (18.1%) and health (13.8%).

- **On SOEs, the Budget announces various measures to improve financial and operational performance, as well as measures to minimise risks to the fiscus.**

  - Among the measures is the work of the Presidential State-Owned Enterprises Council towards rationalising SOEs to minimise inefficiencies and duplication of roles.
  - In the 2022/23 financial year, National Treasury is expected to publish a framework outlining the criteria for Government funding of State-owned companies.
  - Some of the financial measures include:
    - During 2022/23, Eskom receives equity support of R21.9 billion for the settlement of its debt and interest; and a further provisional allocation of R21 billion and R22 billion is accommodated in 2023/24 and 2024/25 respectively for the entity's restructuring.
    - South African Airways is allocated R1.8 billion to cover capital and interest payments on guaranteed debt.
    - During the 2021 MTEF, Government made provision for a R7 billion allocation to the Land Bank, predicated upon the finalisation of a Liability Solution with its lenders. Due to significant delays in negotiations, this funding was not transferred thus the 2022/23 fiscal framework makes provision in the contingency reserve for a R5 billion conditional allocation to the Land Bank.

- **Government's multifaceted strategy to achieve sustained economic growth comprises the accelerated implementation of structural reforms, support for small business and new infrastructure investment.**

  - Over the MTEF, public sector infrastructure spending is estimated at R812.5 billion.
  - Through the Budget Facility for Infrastructure (BFI), R6.7 billion is allocated for several water resources and bulk infrastructure projects.

[18] The Presidential Employment Initiative was launched in October 2020 in response to the impact of the COVID-19 pandemic, with a focus on unemployed youth.

- Furthermore, over the MTEF Government provides an additional allocation of R9.9 billion to the South African National Roads Agency (SANRAL) for the rehabilitation of the non-toll road network.

4. The Division of Revenue

- **The total national revenue available for the equitable distribution between the three Government spheres amount to R1.975 trillion for 2022, as follows:[19]**
  - National Government's equitable share is R824.7 billion, which excludes conditional grants to provincial and local spheres, general fuel levy, debt service costs and the contingency reserve;
  - Provincial Government's equitable allocation is R560.8 billion; and the
  - Local Government equitable allocation is R87.3 billion.
    - The allocations to the three spheres have been made in line with national fiscal priorities (i.e. reducing the budget deficit and stabilising the debt-to-GDP ratio), the constitutional service delivery mandates and the fiscal capacity (i.e. the ability to raise own revenue) of the respective spheres.

- **Subsequent to the 2021 MTBPS, additional funds were added to the Provincial Government and Local Government equitable share allocation for 2022/23, as follows:[20]**
  - R9 billion to support Provincial Education Departments in addressing educator numbers and other shortfalls within the sector;
  - A further R6.2 billion is added for Provincial Education Departments to continue hiring assistants in schools as part of the Presidential Employment Initiative;
  - R7.4 billion is added for Provincial Departments of Health to continue to respond to the COVID-19 pandemic and to reduce the impact of budget reductions on essential medical goods and services; and
  - R204 million is added to fund non-profit organisations that are already contracted by the Provincial Departments of Social Development.
  - The Local Government equitable share receives an additional R4.2 billion in 2022/23 to expand the provision of basic services to poor households.[21]
    - These additional allocations to the Provincial and Local Government equitable shares are meant to alleviate various spending pressures faced by these two spheres. However, it also requires provinces and municipalities to improve spending efficiencies and effectiveness by implementing the findings of spending reviews, namely, good governance and better financial controls.

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[19] National Treasury (2022b), p.6.

[20] National Treasury (2022b), p.11.

[21] National Treasury (2022c), p.75.

- **Provincial and Local Government's also receive a second form of nationally raised revenue in the form of conditional grant transfers, which is aimed at supporting provincial and local government spheres to fulfil their service delivery mandates and contribute to national priorities.**

  - Provincial Government receives R121.8 billion in conditional grants for 2022/23, of which R471 million is unallocated to fund the *Provincial Disaster Response Grant* and *Provincial Emergency Housing Grant* should a disaster/emergency arise; and
  - Local Government receives R47.98 billion in conditional grants.[22]

- **Changes to Provincial and Local Government Conditional Grants, are as follows:[23]**

  - The *HIV, TB, Malaria and Community Outreach Grant* has been reconfigured from eight to two components, and has a name change, now referred to as the *District Health Programme Grant.*
    - The *Mental health services* and *Oncology services* components previously included in this *Grant* have been moved to the direct *National Health Insurance Grant.*

  - The *Early Childhood Development Grant* has been moved from the Department of Social Development to the Department of Basic Education.

  - The *Public Transport Network Grant* allocations are reduced by R754 million in 2022/23 and R105 million in 2023/24, and increased by R621 million in 2024/25.
    - These changes are made to align with the revised implementation plan of phase 2 of the MyCiTi project for the City of Cape Town.

  - To fund a sport project in Polokwane Local Municipality, R10 million in 2022/23 is shifted from the sport component of the *Municipal Infrastructure Grant* to the *Integrated Urban Development Grant.*

5. Concluding Remarks

- The rise of contingent liabilities and fiscal risks have increased, namely, SOE government-backed guarantees and the failure of SOEs to fulfil their mandate affects economic growth.
- Gross loan debt will stabilise at 75.1 per cent of GDP in 2024/25, a year earlier and at a lower level than projected in the 2021 MTBPS and it is projected that a primary surplus will be realised by 2023/24, which will enable the Government to bring fiscal consolidation to a close.
- Tax proposals announced in the 2022 Budget include providing relief of R5.2 billion to support households and includes not adjusting the General Fuel Levy and the Road Accident Fund.

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[22] National Treasury (2022b), p.6.

[23] National Treasury (2022c), pp. 73-75.

- South Africa remains the most unequal country globally and the World Economic Forum (WEF) warns that "social cohesion erosion" remains a top short-term threat as more people are projected to live in extreme poverty compared to pre-pandemic levels.
- Fiscal risks from SOE government-backed guarantees remain elevated and as these contingencies are realised, they crowd out essential social spending and much needed investment that supports economic growth.
- Hence, fiscal sustainability; economic recovery and reconstruction; social wage; job creation; and a rigorous response to the economic cost of the COVID-19 pandemic remain the key spending priorities over the 2022 medium term with spending on learning and culture (24.3%), social development (18.1%) and health (13.8%) continuing to dominate.
- The equitable division of revenue among the three spheres of government have been made in line with national fiscal priorities, the constitutional service delivery mandates and the fiscal capacity of the respective spheres.
- Provincial and Local Government have received additional allocations towards their equitable shares and conditional grant allocations for 2022/23 to alleviate spending pressures.

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