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BUDGET BRIEF 4

Budget 2009: Still Getting the Balance Right?

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Budget 2009:
Still Getting the Balance Right?

Len Verwey, Kate Lefko-Everett and Ahmed Mohamed

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Over the past eighteen months, and in the run-up to the 2009 general elections, South Africa has undergone a period of political transition and intense self-scrutiny.

The re-emergence of the "left" in ANC leadership has heightened public discourse over economic policy and service delivery since the 1994 transition to democracy. Many in the Tripartite Alliance have not concealed their distaste for South Africa's relatively conservative fiscal stance under the Mbeki administration, and under Trevor Manuel's leadership in the Finance Ministry.

There has been widespread speculation over the extent to which the new ANC leadership may adopt a more "leftist" economic policy, allowing for increased social spending and greater government intervention in the economy. This possible shift also intersects with the prospect of new budgetary amendment powers in Parliament, as the Money Bills Amendment Procedure and Related Matters Bill [B75-2008], which is currently awaiting the President's signature.

However, this shift also coincides with the global economic downturn. In the 2009 Budget, the budget deficit has been revised from the 1.6% in the 2008 MTBPS to 3.9%.As such, it is by far the largest deficit proposed in recent years, and goes some way to ensuring that medium-term government spending priorities remain on track. The increased deficit remains continuous with preceding budget policy, which explicitly link budget deficits and surpluses to trends in the business cycle and the commitment to a mildly counter-cyclical fiscal policy stance. At the same time, it should go some way to unifying the ANC around economic policy in the run-up to the elections.

Fiscal and Economic Context

The South African economy remains relatively small and open, and inextricably linked to developments in the international sphere. The 2009 Budget is distinguished by its response to the global financial crisis, which has already had a discernible impact on the domestic economy, particularly in terms of reduced demand for South African exports. Reduced export demand may also lead to job loss and rising poverty levels, and as a consequence, higher demand for social grants and services, as well as lower tax revenue in coming years.

The global financial crisis also has implications for South Africa's growth projections. The 2008 Medium-Term Budget Policy Statement (MTBPS), released in October, estimated a rate of 3.5% growth for the current fiscal year. However, Reserve Bank figures show an annualised growth rate of only 0.2% for the third quarter of 2008, compared to 5.1% in the second quarter. Therefore, the 2009 Budget estimates real GDP growth for 2008/09 at only 2.6%. Tax revenue is also likely to be less than anticipated, and therefore a deficit of 1% rather than a surplus will result.

Analysis suggests that the 2008 MTBPS, though correct in asserting the robustness of the financial sector, underestimated declining demand for South African exports as a result of the contraction of the global economy. Reserve Bank figures suggested a significant decline in nominal export value at the end of 2008. Trends in business indicators used by the Reserve Bank also suggest that the economy is still far from recovery. Given this gloomy outlook, the growth forecast for this fiscal year has been adjusted down to 1.4%.

On this basis, it is unsurprising that the 2009 Budget does not propose significant changes to tax policy, aside from some adjustment to personal income tax brackets. Increasing tax rates would be ill-advised in light of declining consumption demand, and would counteract the stimulatory effects of recent downward adjustments in the repo rate. Accordingly, tax revenue estimates for 2009/10 have also been adjusted downward, from R683 billion in the 2008 MTBPS to R 643 billion.

Faced with reduced growth and revenue in 2009/10, and the need to finance investment, policy-makers had little choice but to run a sizeable deficit. The main budget deficit increases to 3.9% of GDP from the 1.6% already projected in the 2008 MTBPS. Budget 2009, in other words, aims to maintain an average real increase in government expenditure over the next three years of between 5 and 6% through increased borrowing. South Africa's use of a deficit to fund investment, particularly in infrastructure and other physical assets, is generally consistent with the approach taken by other countries. Given a rate of expenditure increase higher than the anticipated growth rate, Budget 2009 entails a significant increase in the share of government spending in total GDP, which rises to 29.9% before declining again slightly over the medium-term as, it is hoped, growth and tax revenue performance pick up.

Expenditure on Social Services

At the crux of the current debate over economic policy are the critical questions of whether government has effectively used public funds to achieve poverty alleviation, increase income and deliver basic services.

While a great deal of progress has been made in respect of these issues, enormous challenges persist. The Statistics South Africa 2005/06 Income and Expenditure Survey (IES) found that about half (48%) of all South Africans live on a month income of below R462 (2007 Rands). Income inequality has in fact worsened, from a Gini coefficient of 0.57 in 2000 to 0.73 in 2005/06, when social grants are taken into account. (Presidency, 2008a; Statistics South Africa, 2008a, 2002)

In 2007, the narrow unemployment rate was 25.5%, and the broad rate which includes discouraged job-seekers was 37.1%. The global financial crisis has reportedly already caused the loss of 100,000 jobs in South Africa in the last quarter of 2008, and a further 165,000 jobs in the informal sector. (Cape Argus, 2009) Recent opinion polls also suggest that citizens judge government performance in job creation fairly harshly, with an average of only 31% approval between 2004 and 2008. (Presidency, 2008b)

Given these challenges, it is unsurprising that Budget 2009 continues a trajectory of substantive social spending, as anticipated last year. Consolidated expenditure on Social Services will reach about R359.4 billion in 2008/09, and increase to R394.8 billion in 2010/11 at a rate of about 10.3% annually. The highest estimates of consolidated expenditure for 2009/10 are for Education (R140.4 billion) and Social Protection (R118.1 billion).

As of April 2009, 13,4 million South Africans will receive social grants, compared to less than 3 million in 1997. The 2009 Budget allocates R86.4 billion to the Department of Social Development for 2009/10, of which the vast majority (R85.6 billion) goes to Comprehensive Social Security, including grant payments and the administration of the South African Social Security Agency (SASSA). (National Treasury, 2009c: 345) Spending on grants will grow from an estimated R80.4 billion in 2009/10 to R95.2 billion in 2011/12 at an average annual rate of 10.2%.

Provision of affordable housing has remained a high policy priority, and government recognises that in spite of delivery achievements, it is "barely keeping pace with the expanding number of households" in the country. (Presidency, 2008b) The ANC's Polokwane Resolutions and Election

Manifesto recommended increased funding for housing, as well as delivery alternatives including rental and social housing, hostel conversions and broadened access to private housing finance.

The 2009 Budget allocates R13.6 billion to the national Department of Housing for 2009/10, of which R12.6 billion consists of grants directly to provinces. Consistent with the prioritisation of Housing, average annual growth in allocations remains high over the medium-term, averaging 20.2% between 2008/09 and 2011/12. A key issue, however, will also be in the delivery of rural housing and development, as most delivery has been concentrated in urban areas, and in Gauteng in particular.

ANC and government discourse in recent years has prioritised education. The ANC's Election Manifesto commits the party to bringing about a minimum of 60% no-fees schools, a sustainable Early Childhood Education system, and the extension of the School Feeding Scheme. Manuel announced a relatively immediate commitment to increase the no-fees schools policy to 60%. Educational spending increased from R12.4 billion in 2005/06 to R19.7 billion in 2008/09 at an annual average rate of about 16.7%, but this rate will slow somewhat to 12.6% over the medium term.

Finally, funding for health is a major concern, and research suggests that life expectancy in South Africa has continued to decline. The ANC has proposed that a National Health Insurance system be introduced within the next five years. Other proposals include the upgrading of hospitals and clinics, investment in research, and treatment, care and support to "at least 80% of all HIV positive people and their families."

In the 2009 Budget, the Minister has announced that government is "profoundly conscious of the complexity of the challenges facing our health services, and the strain on resources associated with a rising disease burden." Budget priorities, in particular, emphasise improvements to the healthcare system, including expansion of the hospital revitalisation programme and improved remuneration for health officials. Distinct emphasis was also placed on disease prevention.

Expenditure on Health constitutes more than one-fifth of all consolidated government expenditure on social services in 2009/10. The 2009 Budget allocates R17.1 billion to the national Department of Health, of which R15.6 billion goes to grants for provinces. The national Health budget is set to increase by 10.3% on average annually over the medium term: at a rate comparable to spending on Comprehensive Social Security, but slower than the Housing budget. This growth rate is also lower than that projected between 2007/08 – 2010/11, which was 14.1% on average.

Governance and Departmental Expenditure

In these uncertain economic times, it is imperative that economic actors in both the public and private sector work towards growing the economy, through effective service delivery, attracting foreign investment and competing with other economies. This must be motivated by the objective of "a better life for all", through good governance that ensures sustainable development and poverty alleviation.

Many governments face the key strategic challenges of optimal allocation of funds for public service delivery and efficient use of these resources. In South Africa, while government is committed to pro-poor allocative efficiency, problems persist with inefficient resource utilisation, particularly at the provincial and local government levels. In the 2009 Budget Speech, the Minister also remarked that "budgeting is not only about expanding expenditure on constructive and necessary activities, it is also about rooting out waste, promoting cost-efficiency and phasing out ineffective programmes". These challenges also relate to the broader issue of capacity development.

Some legislative and policy measures have been introduced that have improved operational efficiency, including the Batho Pele Principles of service delivery and the Promotion of Access to Information Act. The Accelerated Shared Growth Initiative for South Africa aimed to identify constraints in the economy and increase growth capacity; one such constraint the mismatch between available skills and those required in the economy. The enactment of the Public Finance Management Act (PFMA) and the Municipal Finance Management Act (MFMA) are part of the broader programme of capacity development for good governance.

In addition, the Money Amendment and Related Matters Bill 2008 – currently awaiting the President's signature – will entrench the role of Parliament in the budget process through the adoption or amendment of the fiscal framework, passing of the Division of Revenue and Appropriation Bills and the establishment of a parliamentary Budget Office, which will enhance oversight.

However, challenges persist and the Presidency has reported that "unauthorised expenditure increased from R30 million in 2004 to R103 million in 2006 and a third of the departments received qualified audits in 2006." (Presidency, 2008b: 10) Further, in 2005/06, only 55% of provincial departments received unqualified reports.

The challenges of capacity development, and the efficient use of public resources, are evident in departmental expenditure patterns for 2008/09. The departments of Education, Health, Social Development and Housing are critical in addressing key social challenges facing South Africa, including inequality, unemployment, poverty and related problems such as HIV/AIDS and crime. Collectively, these four departments account for 33.2% of the total revised expenditure estimate as at November for the 2008/09 financial year. Combined total expenditure is estimated at R120 billion by end of March, 2009, of which the Department of Social Development[1] accounts for more than half.

By the end of the second quarter of 2008, the Departments of Housing, Social Development and Health maintained relatively steady expenditure. However, patterns in the Education Department were more volatile, and by the end of the second quarter the department had already exhausted almost 80% of its overall budget. A closer look shows a sudden upswing in spending between August and September, in which the relative expenditure shift was over 100%.

A comparative overview of the total capital expenditure estimate, undertaken by November 2008, reveals a mixed picture. As a benchmark, departments should have spent nearly 75% of their capital budget allocation by this time, but the Education department had already overspent its revised annual capital budget expenditure estimate by nearly 1%. The departments of Housing and Health, however, had not yet spent 54% and 42% of their budgets respectively. In comparison, Social Development utilised nearly 75% of its capital budget, performing well in this respect.

When the total vote for current payments for each department is compared with current expenditure at end of November, expenditure results are relatively impressive. The departments of Health, Education and Social Development spent 64% of their vote on current payments, while the Department of Housing spent 84%.

The departments of Housing and Health in particular appear to be struggling to spend their capital budgets. By the end of November, the Department of Housing had spent only 46.5% of its capital budget and 84% of its budget for current payments, while the Department of Health did not spend 42% of its capital vote but managed to spend 63% of its current budget. This trend is suggestive of "fiscal dumping", in which the bulk of expenditure takes place in the fourth quarter of the financial year, sometimes on wasteful and/or non-productive expenditure. This also calls into question the rationale behind increased allocations to some departments in the adjustments appropriation vote.

Conclusion

It is clear that the South African economy has started to feel the inevitable pinch of the global financial crisis. The Budget does not shy away from this reality and acknowledges both the need to continue infrastructural expansion and to provide shorter-term measures for the amelioration of poverty.

More than ever before perhaps, the current challenge calls for a recommitment from both the private and public sectors. In the case of the public sector the challenge lies primarily in ensuring that allocations achieve the social and economic impact for which they were approved. Budget allocations matter but the quality of their spending is decisive and depends on the daily commitment of public servants to work for the common good. In the case of the private sector, the challenge will be to maintain production and avoid job losses in an unfavourable environment. It is crucial, therefore, in giving effect to Budget 2009, that cooperation and partnership between public and private sectors ensures the minimisation of poverty and suffering for ordinary South Africans.

Note

1 The National departments of Health, Education and Housing are mainly tasked with policy development and monitoring and evaluation, while implementation takes place at provincial level. For these departments, the largest expenditure items are in transfer payments and subsidies.