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Financial and Fiscal Commission says private consumption spending and private investment would also fall

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CAPE TOWN — Growth in gross domestic product (GDP) would fall if the government decided to fund the proposed National Health Insurance (NHI) scheme through tax increases rather than by borrowing, research conducted by the Financial and Fiscal Commission has shown.

Private consumption spending and private investment would also fall if the government decided to pursue this option, the commission's acting chairman and CEO, Bongani Khumalo, said yesterday. He was addressing a joint sitting of Parliament's finance committees which are holding public hearings on the budget's fiscal framework and revenue proposals.

The commission is a constitutional body tasked with advising the government at various levels on intergovernmental finances.

Mr Khumalo said there were fiscal risks involved in the various options of funding the scheme. The Treasury is looking at four possible options to fund the National Health Insurance, including raising value-added tax , a surcharge on income tax, payroll taxes and user fees.

The African National Congress and the commission estimate the insurance would cost R128bn in the first year and, the commission's estimates say, rise to R325bn in 2025.

"In the long run, greater public spending financed through increased taxes would translate into a loss of GDP of close to 2%, although a small positive effect is observed in the shorter run. Our research indicates that GDP growth is lower when utilising taxation compared to borrowing." Mr Khumalo said.

The commission made long- term budget projections under three scenarios which reflected different assumptions about future policies for government revenue and spending that mimicked the introduction of the health insurance.

In the "business as usual" scenario in which all variables were constant per effective labour unit, an increase in public spending of 10% for the first two periods and of 2% for the next three years would be required. If no constraints were placed on state debt, GDP would grow faster than would otherwise be the case in the short run.

But this would result in less productive capacity and lower GDP in the long run. Borrowing more in the first few years would increase interest payments in future periods, intensifying the crowding-out effect. In this scenario, the debt-to-GDP ratio would be 5% greater than on the "business as usual" level.

If the debt-to-GDP ratio was fixed at its "business as usual" level and the insurance was funded from tax, the budget deficit would not grow as rapidly, but the positive effects on GDP would not be as great, Mr Khumalo said.

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