FINANCIAL AND FISCAL COMMISSION

SUBMISSION TO THE SELECT AND STANDING COMMITTEES ON APPROPRIATIONS ON THE MEDIUM TERM BUDGET POLICY STATEMENT

11 NOVEMBER 2020

Introduction

- The MTBPS is tabled shortly after government was forced to adopt a supplementary budget due to the Covid-19 pandemic
- The pandemic has exacerbated existing structural and fiscal fragilities. On the social front, it has amplified the existing inequalities and pushed many people into poverty and unemployment.
- The economic and fiscal outlook is uncertain and likely to undermine the credibility of the overall fiscal framework, given the outstanding wage bargaining agreement and deteriorating SOE fiscal position.
- Core spending functions are facing stagnant and declining budgets in 2020/21 likely to affect service delivery and overall development targets. On an aggregate level, Government needs a plan to increasingly reprioritise expenditure in a growth friendly consolidation manner over the MTEF period; and on a institutional level expenditure efficiencies must be realised
- The uncertainty calls for much bolder relief or stimulus package and clear commitment to quality execution and reforms.
- In line with the request from the Standing Committee on Appropriations, the Commission makes this submission on the 2020 Division of Revenue Amendment Bill and Adjustments Appropriation Bill in terms of Section 214 (1) of the Constitution and Section 35 of the Intergovernmental Fiscal Relations Act (1998) as well as S4(4c) of MBARARMA (Act 9 of 2009), as amended.

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Presentation Outline

- Macroeconomic outlook and the budget
- Consolidated fiscal framework and outlook
- Provincial fiscal framework
- Local government fiscal framework
- Risk to provincial fiscal sustainability
- Covid-19 economic relief package review
- Alignment of the budget to economic policy interventions
- Zero based budgeting for improved spending efficiency

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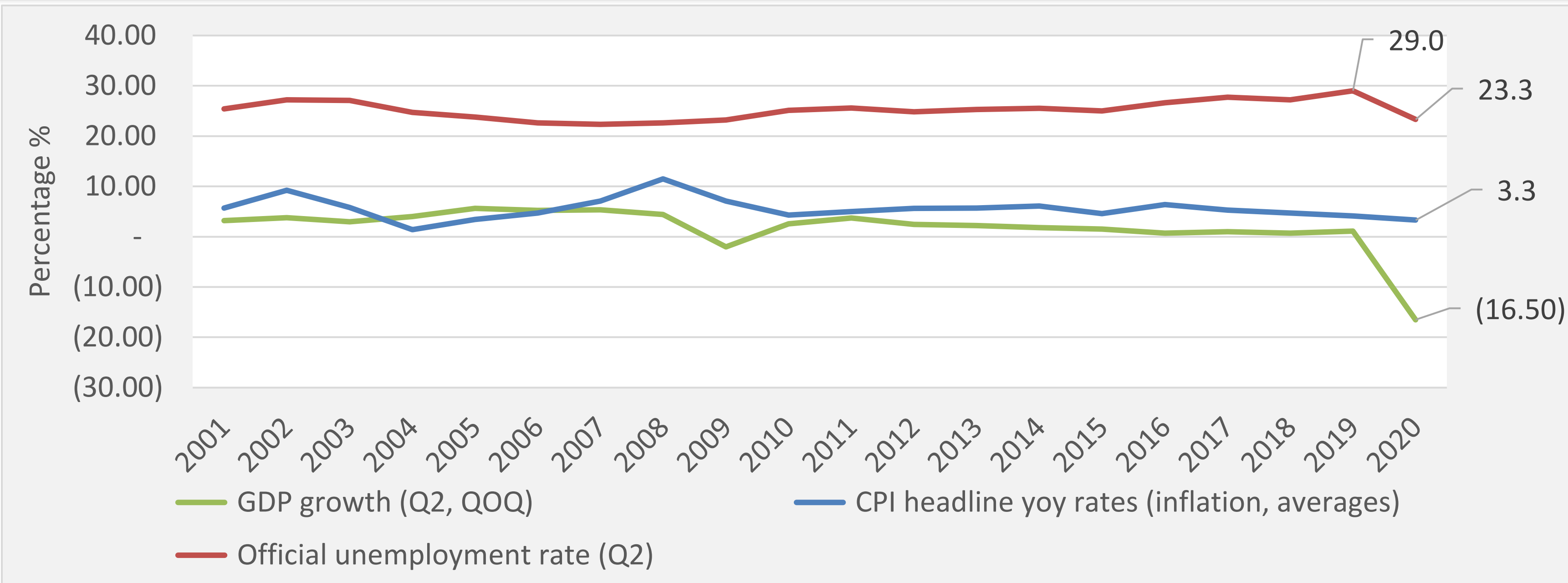
MACRO-ECONOMIC PERFORMANCE 2001-2020



- Due to the COVID-19 pandemic and lockdown, GDP contracted in Q2, QOQ (i.e. quarter-on-quarter) by 16.5 per cent. Inflation rate year-on-year average remained stable.
- Although the official unemployment rate dropped from 29.0 per cent to 23.3 per cent in the second quarter, this was due to the fact that people were unable to engage in job search during the lockdown, resulting in a mass increase of the **economically inactive** population by 5.2 million between the 1st and 2nd quarter of 2020. Currently, there are **more people of the working age between 16-64 years who are economically inactive than the labour force – inequality and poverty worsens**

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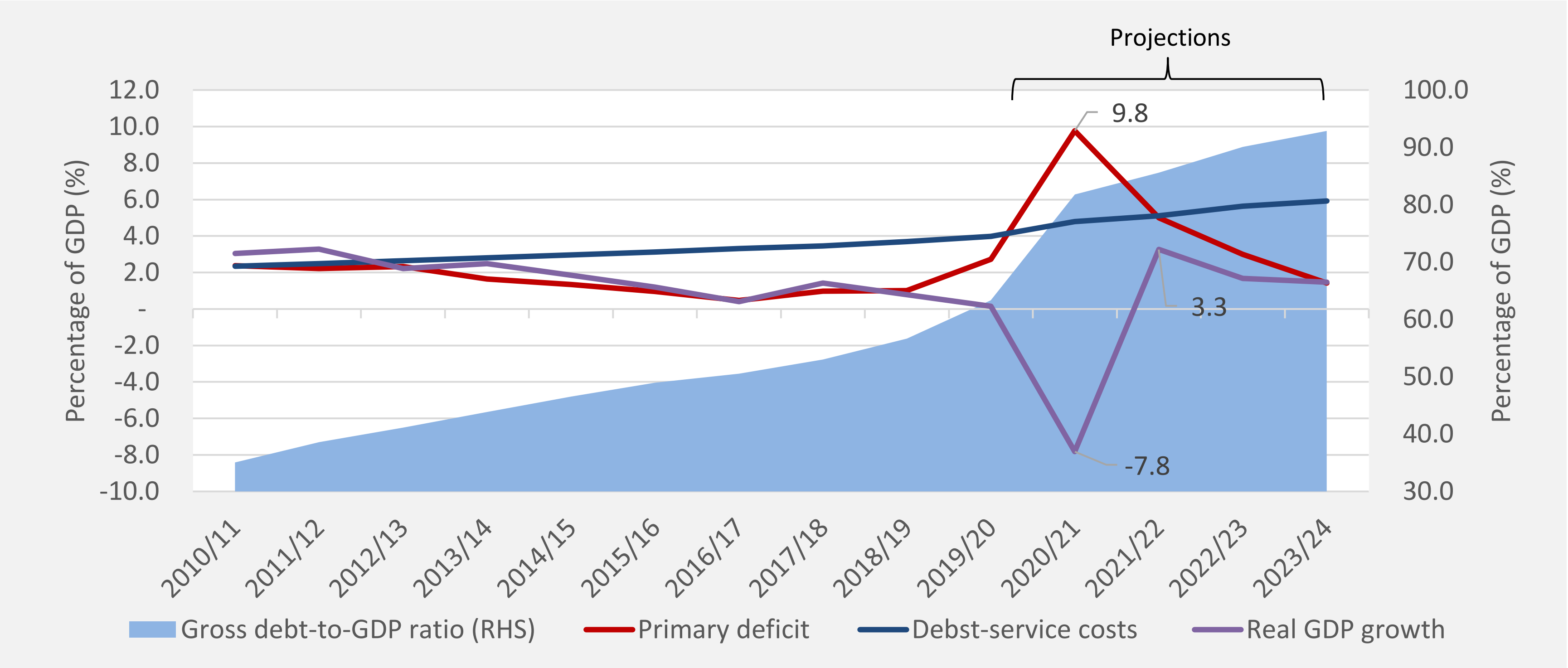
Source: StatsSA Gross Domestic Product (Q2 2020), Consumer Price Index (September 2020), Quarterly Labour Force Survey Q2 2020, and Commission Calculations

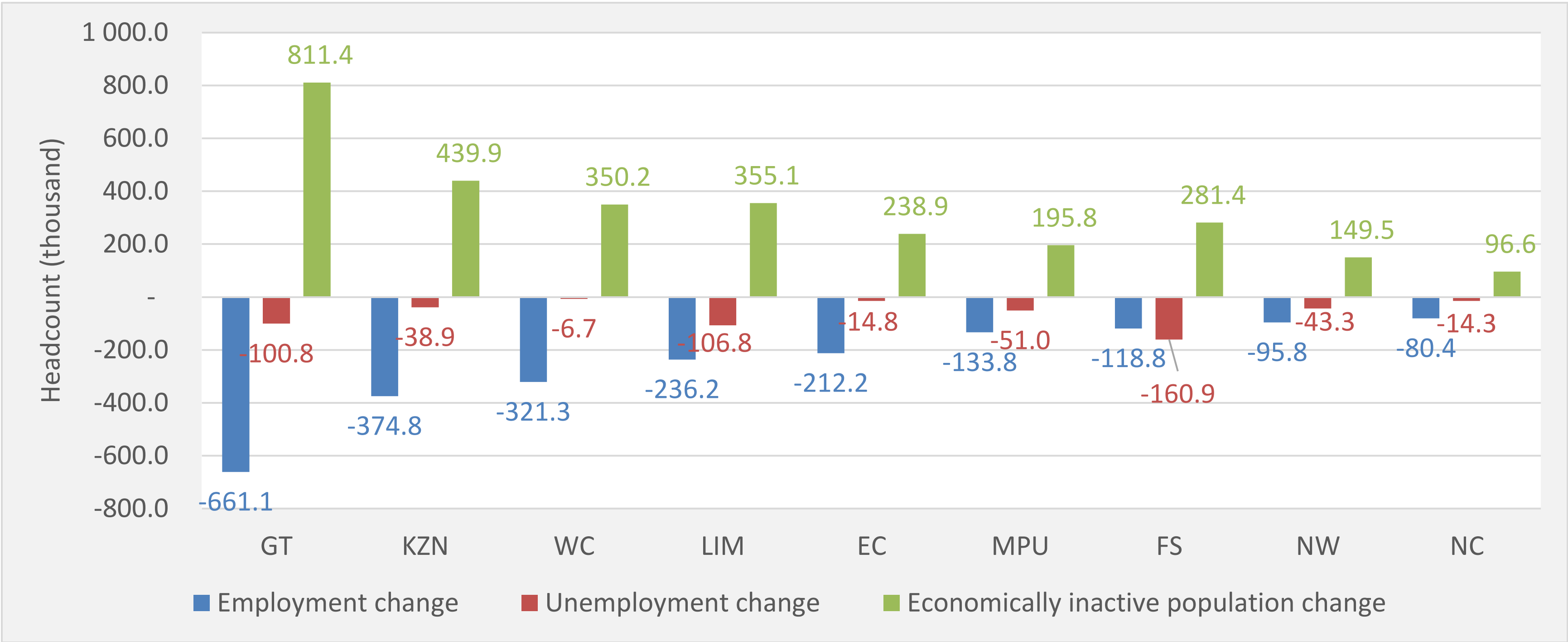
Fiscal performance analysis 2010 – 2020 MTBPS



- Gross debt-to-GDP ratio is set to increase substantially, caused by the sharp rise in primary deficit (at 9.8 per cent of GDP) that needed financing - which incurs more debt and debt-service costs (at 4.8 per cent of GDP).
- The hope is that despite the 7.8 per cent contraction in real GDP, the economy will quickly recover to 3.3 per cent growth next year and taper the primary deficit and debt.

Source: National Treasury, 2020 MTBPS.

PROVINCIAL (UN)EMPLOYMENT AND ECONOMICALLY INACTIVE POPULATION CHANGE, Q1-Q2 2020



- The patterns of (un)employment and economical inactive population change suggest that there is a rural-urban divide in terms of economic performance as it impacts the labour market due to the COVID-19 pandemic and the lockdown. More specifically, areas where there are high population densities and economic centres suffered the job losses than rural areas.
- In Gauteng and KwaZulu-Natal alone, more than one million jobs were lost. And with the economic lockdown, more than 1.2 million individuals became economically inactive in a single quarter.

Source: StatsSA Quarterly Labour Force Survey Q2 2020, and Commission Calculations

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Reigniting the economy – Economic Reconstruction and Recovery Plan

- The government's economic plan for recovery is to forge a social partnership to boost confidence, restart the economy and conduct urgent reforms as per the 2019 Strategy document: Economic Transformation, Inclusive Growth and Competitiveness. Focus areas of growth are **infrastructure**, **expanding energy generation capacity**, **creating mass public employment** and **supporting rapid industrialization**.
- Although the FFC appreciates the government's recovery plan to be **strengthening the continuity and consistency of the position taken**, and in line with FFC's **2021/22 Annual Submission for the Division of Revenue, Chapter 3: Recommendation 1**.
- However, consistency should not be confused with repetitions **without proof of real reforms, impacts and outcomes**, for it may lose even more credibility of policy and that of implementation of government programmes.
  - For instance, the assumption of a recovery shock in growth rates over the 2021 medium term expenditure framework (MTEF) at 3.3, 1.7 and 1.5 per cent, from the negative real GDP growth rate of 7.8 per cent for the 2020 financial year seems extremely optimistic, given historical trends.
  - Notwithstanding this, **gross fixed-capital formation (i.e. investment)**, which is one of the fundamental factors for both the current and medium-term growth rates **had decelerated even before the onset of COVID-19 pandemic and lockdown.**
  - The electricity availability factor remained **unstable** despite that demand decreased during the lockdown, which is a cause for concern in terms of credibility of the assumptions for infrastructure-led growth and growth prospects, and the feasibility and viability of the economic recovery plan itself.

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REIGNITING THE ECONOMY – ECONOMIC RECONSTRUCTION AND RECOVERY PLAN (CONT.)

Hence, the Commission reiterates as stated in the *2021/22 Annual Submission for the Division of Revenue* - with respect to economic and social development in the context of Covid-19 (Chapter 3, Recommendation 2):

- *After reviewing the economic situation leading up to the Covid-19 crisis, the Commission is convinced that a fundamental structural transformation of the economy is inevitable.*
- *Therefore, the ministers of finance, of economic development and trade and industry, and of labour should jointly address the economic barriers, social inequality, and societal polarisation by adopting a localised product value chain approach.*
- *The expression of this approach should be found in the incentive grants frameworks of both provincial and local conditional grants, as hard conditions to permit procurement of goods only if they are made or assembled locally within the South African borders, to stimulate the domestic economy and encourage job growth while taking international trade agreements into account.*

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CONSOLIDATED FISCAL FRAMEWORK AND OUTLOOK

Fiscal Framework: Special Adjustments Budget Relative to MTBPS 2020

R billion/% of GDP	Budget 2020	SAB			MTBPS 2020		
	2020/21	2020/21	2021/22	2022/23	2021/22	2022/23	2023/24
Main budget revenue	**1,398.0**	**1,099.5**	**1,268.2**	**1,378.8**	**1,263.6**	**1,388.3**	**1,487.1**
	25.8%	22.6%	23.8%	24.5%	23.8%	24.7%	24.9%
Main budget expenditure	**1,766.0**	**1,809.2**	**1,763.8**	**1,809.3**	**1,801.1**	**1,874.8**	**1,924.6**
	32.5%	37.2%	33.1%	32.2%	33.9%	33.3%	32.3%
Non-interest expenditure	1,536.7	1,572.7	1,500.6	1,508.2	1,529.3	1,557.2	1,571.5
	28.3%	32.4%	28.2%	26.8%	28.8%	27.7%	26.4%
Debt-service costs	229.3	236.4	263.1	301.1	271.8	317.6	353.1
	4.2%	4.9%	4.9%	5.4%	5.1%	5.6%	5.9%
Main budget balance	**-368.0**	**-709.7**	**-495.6**	**-430.5**	**-537.4**	**-486.6**	**-437.5**
	-6.8%	-14.6%	-9.3%	-7.7%	-10.1%	-8.6%	-7.3%
Primary balance	**-138.7**	**-473.2**	**-232.4**	**-129.5**	**-265.7**	**-169.0**	**-84.4**
	-2.6%	-9.7%	-4.4%	-2.3%	-5.0%	-3.0%	-1.4%

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- Assessing allocations between Special Adjustment Budget (SAB) relative to MTBPS, FFC notes:
  - MTBPS revenue projections for 2021/22 are lower by R4.6 billion
  - Slight easing of consolidation path set out in June – evident in additions to main budget expenditure with R37 billion added in 2021/22 and R66 billion in 2022/23
  - Bulk of the additions go to non-interest expenditure (R29 billion in 2021/22 and R49 billion in 2022/23)
  - **But** debt service costs also higher and continues to also crowd out other forms of spending, and the burden of this is being pushed to provinces and municipalities

Analysis of Growth Rates

	2019/20	2020/21	2021/22	2022/23	2023/24
	Outcome	Revised	Medium-term estimates		
Non-interest expenditure	12,2%	5,8%	-2,8%	1,8%	0,9%
Consolidated expenditure including June 2020 budget adjustments	11,9%	10,2%	-2,2%	4,3%	2,9%
Payments for capital assets	-3,6%	13,1%	13,4%	8,3%	2,1%
Consolidated expenditure	11,9%	5,9%	1,8%	4,3%	2,9%

- Assessment of growth rates show that despite the additions to non interest expenditure, in terms of year-on-year growth, cuts are envisaged for 2021/22
- There is however a clear prioritisation of capital spending with payments for capital assets projected to grow by 13.4% in 2021/22
    - The budget protects capital spending from reductions, thus reflecting the decision to adopt an infrastructure-led approach to growth – this trend continues over entire MTEF period, but with a declining trajectory.

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SUMMARY- FISCAL FRAMEWORK

- The Commission welcomes and supports the slight easing of the consolidation path as evidenced in additions to non-interest expenditure in 2021/22 and 2022/23
- Despite these additions, broad and significant cuts are expected in 2021/22
  - The Commission expresses concern around reductions to equitable share allocations as consumption spending (spending on health, education, water, sanitation) is the core of government's mandate
- Provinces and municipalities should devise plans and report on how the reductions to the PES and LES will be managed with specific emphasis on the effects on service delivery
- The Commission is concerned about lack of adjustment/decreases to Basic Education, Agriculture, Defence and Social Security Funds envisaged for 2021/22 - the Commission is particularly concerned about the implications of no increases in basic education
  - The Commission recommends that the implications of budget cuts for the affected departments be detailed as it is important to understand the implications of cuts in order to mitigate any negative effects
- The attempt at large fiscal adjustment may impose unsustainable social pressures, impact on the recovery and deal a second blow to livelihoods on top of the Covid-19 catastrophe

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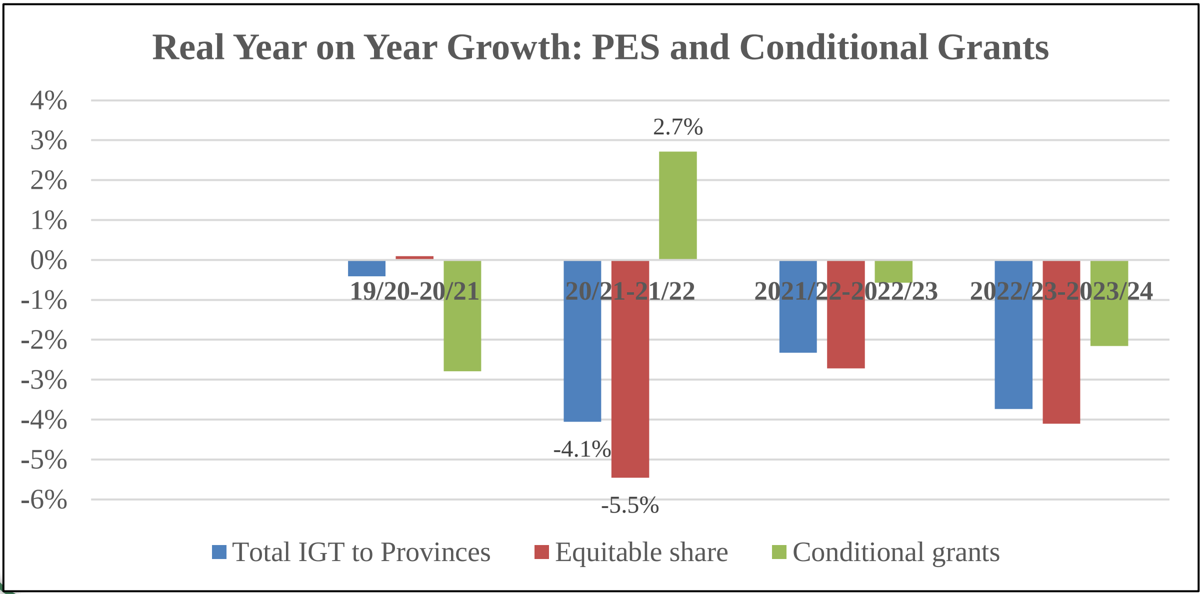
PROVINCIAL FISCAL FRAMEWORK

PROVINCIAL FISCAL FRAMEWORK OVERVIEW

Intergovernmental Fiscal Transfers to Provinces (PES and CGs)

R billion	Budget 2020 2020/21	SAB 2020/21	MTBPS 2020 2020/21	2021/22	2022/23	2023/24	Real Annual Average Growth 2020/21-2023/24
Provinces	**649.3**	**645.3**	**628.3**	**629.4**	**641.8**	**645.6**	**-3.4%**
Equitable share	538.5	538.5	520.7	514.0	522.0	523.1	-4.1%
Conditional grants	110.8	106.8	107.6	115.4	119.8	122.5	0.0%



- Provinces are projected to experience real annual average decline in resources over the next three years – decline driven by reductions to the PES allocation
- For 2021/22, reductions projected to be significant
  - Overall, intergovernmental transfers to provinces will decline by 4.1% in real terms
  - PES projected to decline by 5.5% in real terms
  - Conditional grants to provinces set to grow by 2.7% in real terms
- Trends indicate attempt to shift spending towards capital through relative protection of allocations to conditional grants
- Trends to reduce PES a concern given role of provinces in delivery of basic services (education, health, welfare)

Adjustments to Provincial Conditional Grants

R million	Budget 2020	SAB	MTBPS 2021/22	Growth Rate
Agriculture, land reform and rural development	**2153,4**	**2158,7**	**2153,4**	**-0,2%**
Comprehensive agricultural support programme	1522,2	1538,3	1522,2	-1,0%
Ilima/Letsema projects	548,8	538,1	548,8	2,0%
Land care programme: poverty relief and infrastructure development	82,4	82,2	82,4	0,2%
Basic Education	**19564,3**	**18569,2**	**19564,3**	**5,4%**
Education infrastructure	11008,0	10514,5	11008,0	4,7%
HIV and AIDS (life skills education)	246,7	257,0	246,7	-4,0%
Learners with profound intellectual disabilities	242,9	220,8	242,9	10,0%
Maths, science and technology	400,9	391,3	400,9	2,4%
National school nutrition programme	7665,9	7185,7	7665,9	6,7%
Cooperative Governance	**138,5**	**130,9**	**138,5**	**5,8%**
Provincial disaster relief	138,5	130,9	138,5	5,8%
Health	**49267,2**	**45524,1**	**49267,2**	**8,2%**
HIV, TB, malaria and community outreach	24387,2	22039,0	24387,2	10,7%
Health facility revitalisation	6367,7	6007,0	6367,7	6,0%
National tertiary services	14068,9	13185,5	14068,9	6,7%
National health insurance grant: health professionals	288,8	289,3	288,8	-0,2%
Statutory human resource, training and development	4154,6	3846,1	4154,6	8,0%
Human Settlements	**17493,5**	**19604,4**	**17493,5**	**-10,8%**
Human settlements development	16620,7	18779,8	16620,7	-11,5%
Title deeds restoration	577,8	547,7	577,8	5,5%
Provincial emergency housing	294,9	276,9	294,9	6,5%
Public Works and Infrastructure	**834,3**	**868,2**	**834,3**	**-3,9%**
Expanded public works programme (EPWP) integrated grant for provinces	420,8	437,4	420,8	-3,8%
Social sector expanded public works programme (EPWP)incentive for provinces	413,6	430,8	413,6	-4,0%
Social Development	**915,1**	**518,2**	**915,1**	**76,6%**
Sports arts and culture	**2075,7**	**2121,2**	**2075,7**	**-2,1%**
Community library services	1479,1	1501,2	1479,1	-1,5%
Mass participation and sport development	596,6	620,0	596,6	-3,8%
Transport	**18342,8**	**17768,2**	**18342,8**	**3,2%**
Provincial roads maintenance	11593,2	11442,4	11593,2	1,3%
Public transport operations	6749,6	6325,8	6749,6	6,7%
Total direct conditional allocations	**4060,1**	**107263,1**	**110784,8**	**3,3%**

- The agriculture, land reform and rural development conditional grants will decrease by 0.2% - driven by cuts to comprehensive agricultural support programme (CASP)
- Conditional grant to the human settlements sector will decrease by 10.8% - driven by a decrease in human settlement development grant which decreases by 11.5% in 2021/22
  - The Commission is concerned about this decrease since it may impact housing delivery
- The public works and infrastructure conditional grants (decreases by 3.9% in 2021/22) with broad cuts envisaged for both the Social Sector EPWP Incentive for Provinces (-4%) and the EPWP Integrated Grant for Provinces (decreases by 3.8%)
  - The Commission is concerned by the decreases in these two grants as it appears to contradict the infrastructure led approach to growth as per the economic recovery plan as well as attempts at job creation

Changes in Key Provincial Conditional Grants

R'million	Budget 2020	SAB 2020/21	MTBPS 2021/22	Net Adjustment
Comprehensive agricultural support programme	1522,2	1 538,3	1 522,2	-16,1
Ilima/Letsema projects	548,8	538,1	548,8	10,7
Community library services	1479,1	1 501,2	1 479,1	-22,1
Education infrastructure	11008,0	10 514,5	11 008,0	493,5
National school nutrition programme	7665,9	7 185,7	7 665,9	480,2
HIV, TB, malaria and community outreach	24387,2	22 039,0	24 387,2	2 348,2
Health facility revitalisation	6367,7	6 007,0	6 367,7	360,7
Statutory human resources, training and development	4154,6	3 846,1	4 154,6	308,5
National tertiary services	14068,9	13 185,5	14 068,9	883,3
Human settlements development	16620,7	18 779,8	16 620,7	-2 159,1
Provincial roads maintenance	11593,2	11 442,4	11 593,2	150,8
Public transport operations	6749,6	6 325,8	6 749,6	423,8

- The CASP will experience cuts of R16.1 million for the 2021/22 financial year
- Alongside this, the community library services will decrease by R22.1 million for the 2021/22 financial year.
- The human settlements development conditional grant will also see decreases of R2.2 billion for the 2021/22 financial year
  - The Commission is concerned about the implications of decreases in human settlements development grant as this may have implications for delivery of houses

Implications for Service Delivery

- The Commission expresses concern about cuts to the PES allocation it funds consumption spending (that is - spending on health, education, welfare) – this is the core of province’s mandate
  - Provinces should devise plans and report on how the reductions to the PES will be managed with specific emphasis on the effects on service delivery
- The Commission is also concerned about how the cuts to the EPWP Integrated Grant for Provinces will impact job creation efforts
  - This is because this grant aims to incentivise provincial departments to expand work creation efforts through the use of labour intensive delivery methods
- The cuts in the human settlement development grant will have a negative impact on housing provision

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LOCAL GOVERNMENT FISCAL FRAMEWORK

Local Government Issues

- A significant proportion of municipalities are distressed and dysfunctional- the fiscal health of many municipalities has deteriorated over the past few years.
- The Commission implores government to prioritise local government and by implication, the poor households.
- The Commission cannot overemphasise the point that allocations to municipalities should be deployed and used efficiently and effectively.
- Local government is set to receive a total allocation of R434.3 billion over the 2021 MTEF. The projected allocation is less by R17.7 billion from what was announced in the 2020 budget

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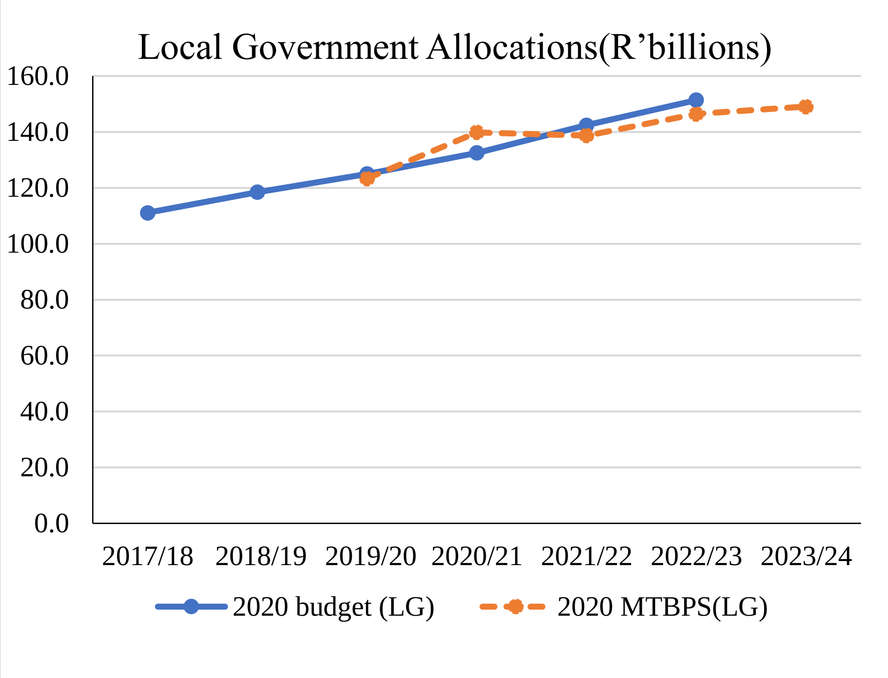
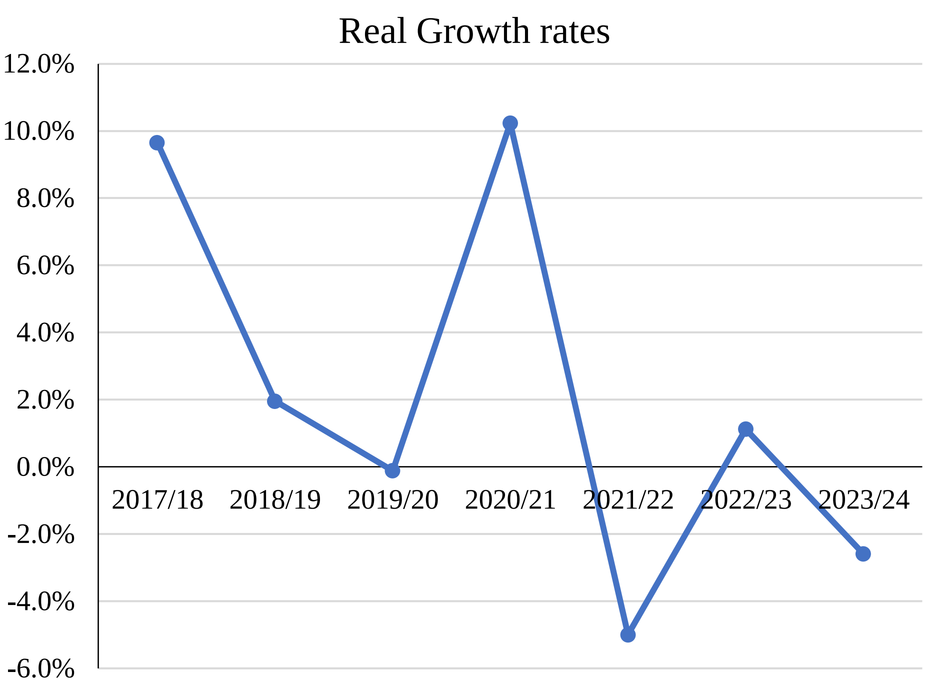
Local government Allocations and growth rates





- Over this period, local government total allocation is set to increase by an annual average of 2.1% in real terms, with annual real growth rates of -5.0% in 2021/22, 1.1% in 2022/23, and -2.6% in 2023/24
- The Commission notes the proposed reductions in the total allocation to the local government but remains concerned about the implication of these reductions for service delivery

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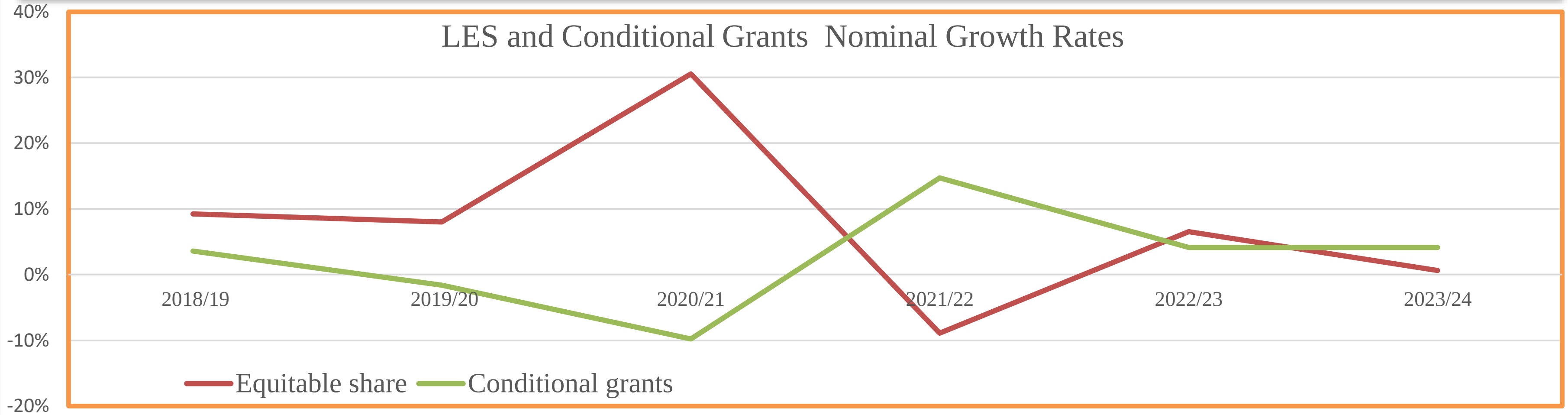
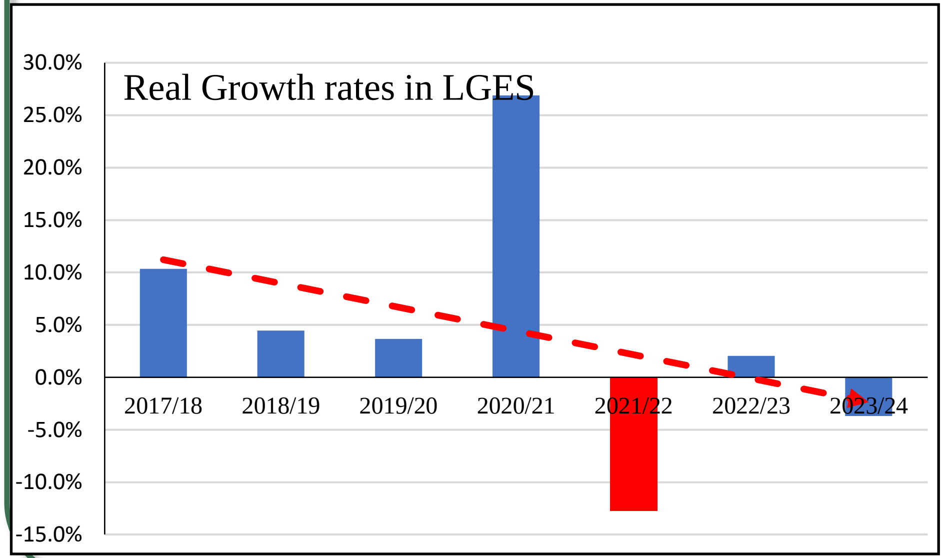
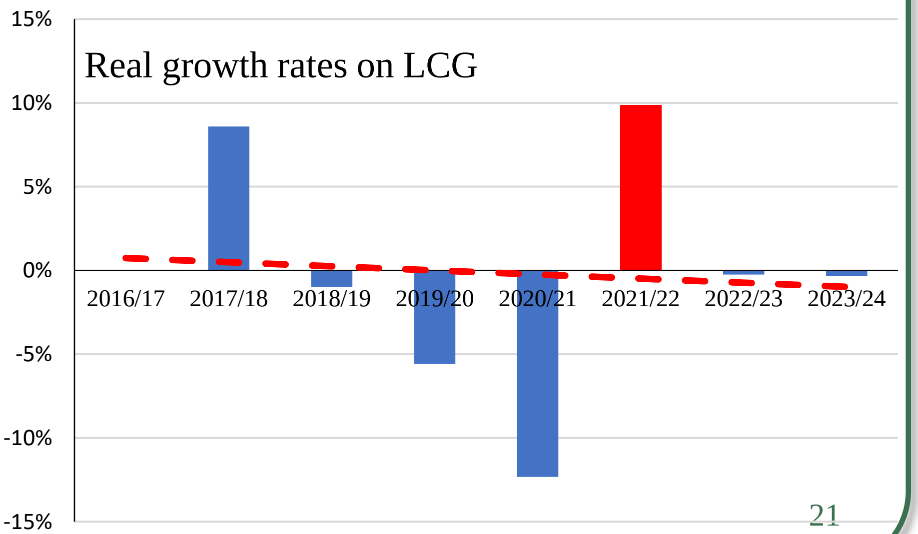
LG Equitable Share and Conditional Grant Allocations and Growth Rates







Local Government Allocations and Growth Rates

- The Commission is concerned about the effect of these reductions on service delivery, given the increasing bulk costs for water and electricity, and declining own revenue collection
  - And remains concerned about the expected progressive decline in the real growth rates of the LGES
- Local government conditional grants were reduced in the supplementary budget by R3,7 billion in 2020/21
  - LG grants allocations will be further reduced by R569 million to make funds available for the SAA business rescue plan among other things, over the 2021 MTEF
- The Commission is concerned that the reprioritisation of local government funds is meant to fund SOEs. The sphere is also currently under fiscal stress due to the Covid-19 induced decline in revenues on one hand and the increase in demand for infrastructure for basic services, on the other.
  - Cuts on CGs go against the infrastructure investment objective which underpins government's recovery plan
- And repeated baseline cuts will have a negative effect on service delivery, infrastructure investment, repairs and maintenance, and it goes against the government objective of infrastructure led growth and objectives indicated in the economic recovery plan
- The Commission is of the view that government should assess the effect of baseline reductions, before implementing the planned reductions over the MTEF period

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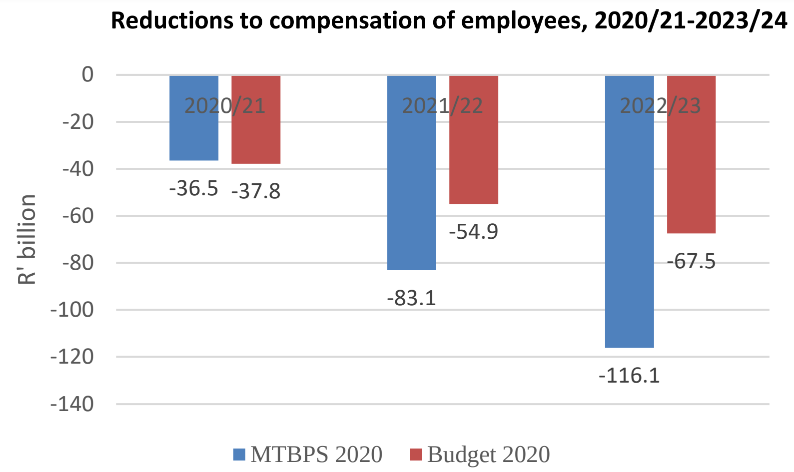
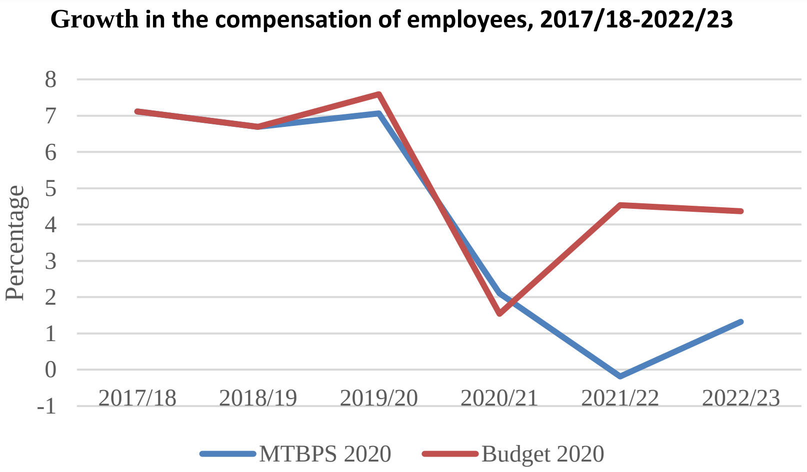
RISK TO PROVINCIAL FISCAL SUSTAINABILITY

National and provincial Wage bill reductions





- The 2020 Budget reduced the wage bill of national and provincial departments by R160.2 over the 2021 period thus reducing in the average annual growth of the wage bill from 6.8% over the 2020 MTEF period to 3.5% over the 2021 MTEF period.
- The 2020 MTBPS announced additional reductions in the wage bill of national and provincial departments in 2020/21 and over the 2021 MTEF period amounting to R311 billion. This decelerated the growth of the wage bill from 1.8% in the current year to an average annual growth is 0.8% over the 2021 MTEF period.
- The massive cuts and declining growth of the wage bill represents a huge risk in the services delivered by provinces because their compensation budgets account for a large share of their total expenditure.

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Provincial Wage Bill shares and reductions

Provincial compensation of employees, 2015/16-2021/22

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Gauteng							
Health COE as % of total spending	59,2	62,2	59,7	56,6	58,2	57,9	58,9
Education COE as % of total spending	71,6	72,7	75,9	74,7	75,0	76,1	76,5
Social Development COE as % of total spending	31,3	31,3	31,3	31,3	33,1	33,2	35,2
Eastern Cape							
Health COE as % of total spending	66,3	65,6	65,4	65,9	67,3	69,0	69,4
Education COE as % of total spending	79,6	77,1	78,7	77,6	79,8	80,8	81,4
Social Development COE as % of total spending	58,0	58,9	61,8	60,1	59,8	61,0	62,0

Source: National Treasury Estimates of the Provincial Revenue and Expenditure, 2019/20

- In Gauteng, the health wage bill accounts, on average, for 59 % of the total health budget, education (75%) and Social Development (32%). In Eastern Cape, the health wage bill accounts, on average, for 67% of the total health budget, education (79%) and Social Development (60%).
- The 2020 Budget and MTBPS announced reductions to the PES amounting to R209.7 billion over the 2021 MTEF period. Wage bill reductions amount to R178 billion or 85% of the total PES reductions.
- These massive provincial wage bill reductions in the context in which the wage bill of provincial strategic sectors account for a relatively large share of provincial budgets, raise risks of sustainability and maintenance of the same level of service delivery at provincial level.

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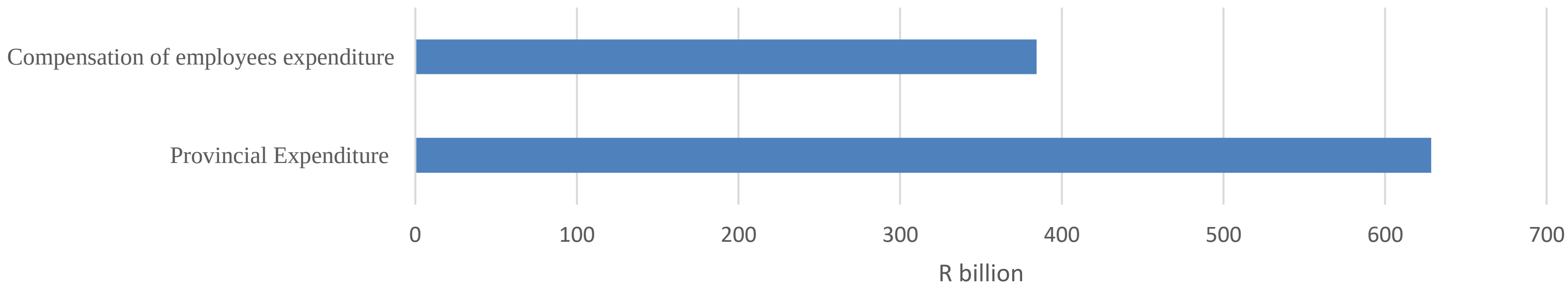
WAGE FREEZE IMPACT ON PROVINCES

Provincial compensation of employees expenditure, 2019/20



- In 2019/20, the spending on compensation of employees accounted for 61 percent of the total provincial spending.
- The 2020/21 last leg of the multi-year wage agreement has not been implemented and has been subjected to litigation at the Labour Court, presenting uncertainty for provincial budgets.
- The 2020 MTBPS announced a unilateral proposal to freeze wages for three years for civil servants. The lack of an agreement on the wage freeze means it could fail to materialise thus triggering potential increases in the provincial wage bill that would have a proportionally bigger impact on overall provincial expenditure given the larger share of compensation of employees budget to total provincial expenditure.
- Provinces could be forced to shift spending from productive sectors to cater for the potential increases in the wage bill, if the wage freeze is not implemented.
- There is no credible plan on how the risks from the potential wage freeze fallout will be mitigated, particularly at provincial level.

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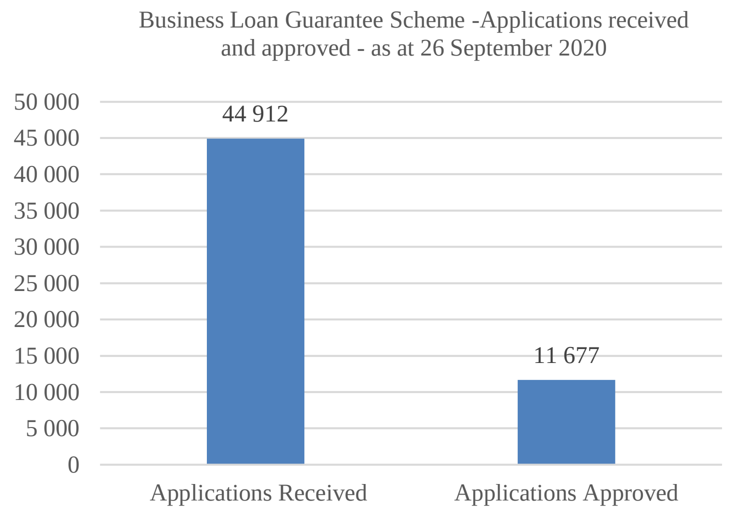
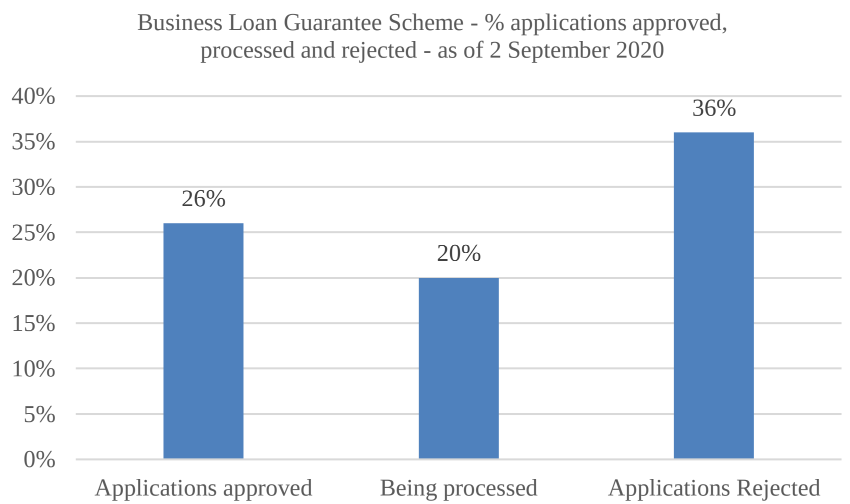
COVID-19 ECONOMIC RELIEF PACKAGE REVIEW

Economic Relief Package - Preliminary Review

- The Commission notes a slow uptake, delays in the disbursement of funds, overpayment/non-payment of beneficiaries, payment of incorrect beneficiaries, corruption and noncompliance with supply chain management policies/legislation arising from implementation of the relief package.



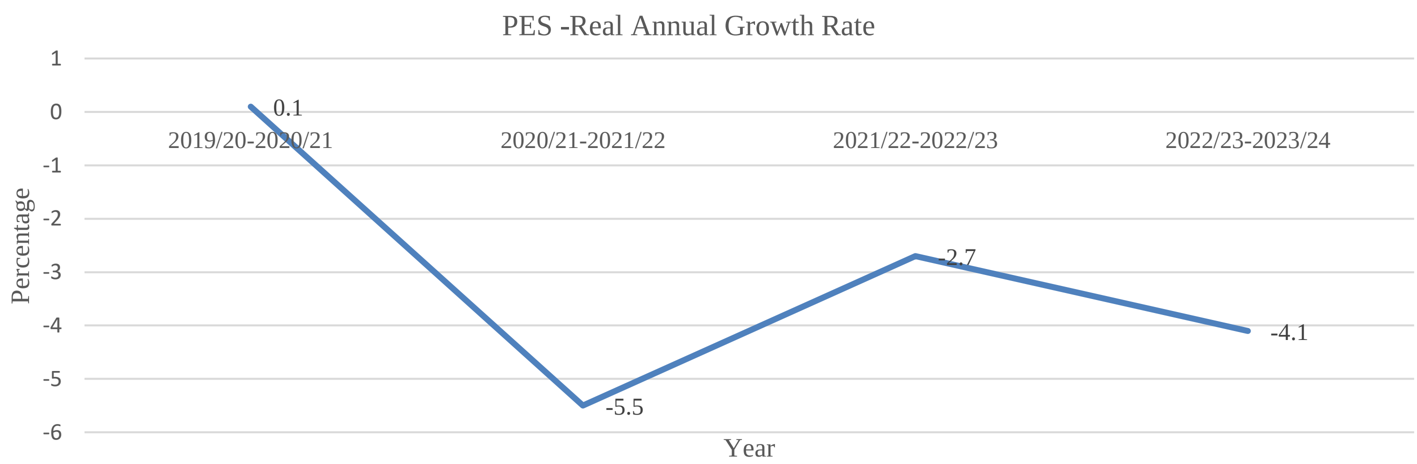


Data Source: The Banking Association of South Africa

- Effectiveness and efficiency of economic and social relief package has been undermined by poor planning, lack of accurate data of beneficiaries, poor reporting (financial and non-financial).

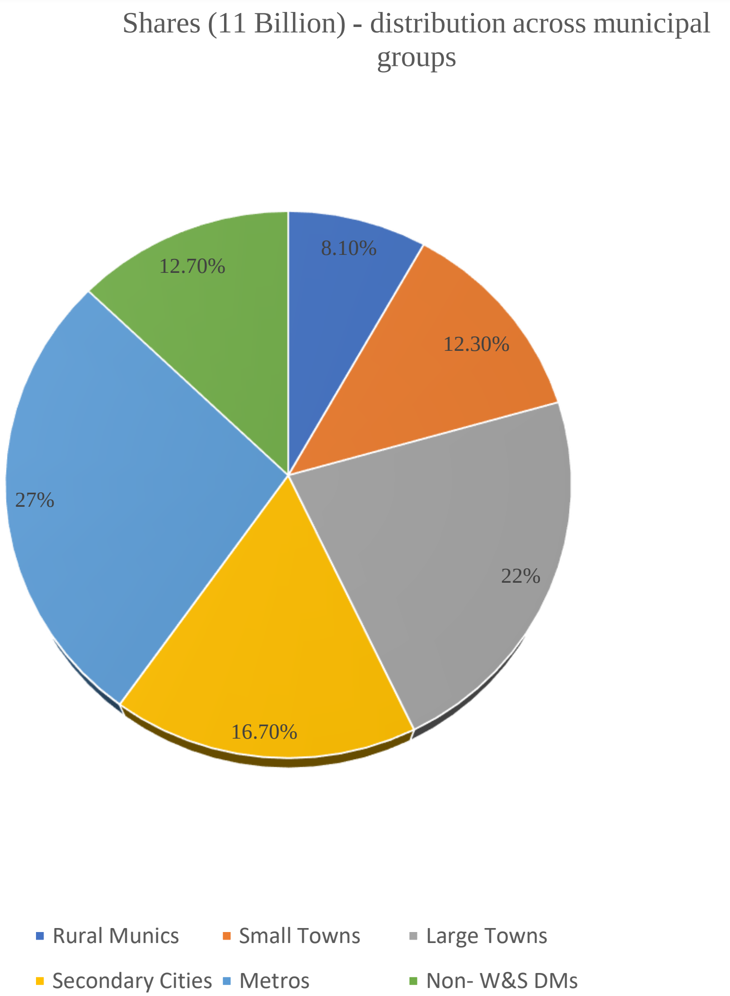
HEALTH BUDGET – COVID– 19 RELIEF

- Comparing February and adjusted budget 2020 - Allocations through the Provincial Equitable Share did not change
  - However, provinces committed to reprioritise R20 billion from the PES to the Covid-19 response from their own budgets given their respective disease profile risks - repurposing
- Out of R20 billion-R15 billion (75%) will be reprioritised to health and R5 billion (25%) to other sectors
- PES will have a negative growth over the 2021 MTEF – the largest negative real growth rate is between 2020/21 -2020/22 (-5.5%)
- The Commission is concern with this significant reduction which is likely has serious negative effect on service delivery



Local Government – Covid-19 Relief

- While announced additional allocation to the local government aimed to assist municipalities to address Covid-19 associated costs amounted to of R20 billion
  - The adjusted budget provides for only R11billion additional funds, while the remaining amount was secured through repurposing funds within various LG grants
- The Commission supported the distribution as metros were the epicentres of COVID-19
- Parliament must receive detailed reports from government on how the remaining Covid-19 relief will appropriated
- The Commission recommends that government invest in reporting systems to ensure accurate and timely monitoring of relief package



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Economic Relief Package – Preliminary Review

- The economic relief package is unlikely to achieve expected results with the limited budget cycle.
- The negative and marginal expenditure growth rates in a number of crucial votes for 2021/22, as evidenced in the GDP growth forecasts, implies dire economic and social conditions ahead.
- The Commission is of the view that some elements of the economic stimulus need to be extended to the 2021/22 financial year to mitigate the effect of the Covid-19 pandemic.
  - For example, there were higher expectations with respect to the uptake of the BLGS as it was announced that the scheme could be extended to R200 billion.
  - However according to the Banking Association of South Africa, given the current trends extension could only be up to R24 billion, due to a number of factors including weakness in business and economic conditions.
- BLGS is one of the interventions that can make a measurable impact at lower levels or complete the lifting of lockdown; however business owners are reluctant to incur more debt under uncertain business conditions and weak economic outlook.

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ALIGNING THE BUDGET TO ECONOMIC POLICY INTERVENTIONS

ALIGNMENT OF BUDGET TO ECONOMIC POLICY INTERVENTIONS (1)

- President Ramaphosa announced an Economic Reconstruction and Recovery Programme to turn around the economy that has been battered by the Covid-19 pandemic: Main elements of the Economic Reconstruction and Recovery Programme are:
  - Creating jobs, through infrastructure investment and mass employment programmes;
  - Reindustrialise our economy, focusing on growing small businesses;
  - Accelerate economic reforms to unlock investment and growth;
  - Fighting crime and corruption; and,
  - Improving the capability of the state.
- The FFC is in agreement with the thrust of the ERRP and the key elements identified by the President.
- The expectation is that the 2020 MTBPS will respond to these pillars of recovery and allocate resources appropriately.
- The Commission looked at the alignment of budgets with the key elements of the ERRP. The FFC conducted an analysis on spending by national departments and provincial government in the sectors that drive the economic recovery plan
- ***First*** FFC looked at the **quality** of spending for key departments that would drive the ERRP. One lens for looking at this is expenditure smoothing- which implies government spending that is evenly distributed through the four quarters of the financial year.
- If such smoothing were to occur, it would be expected that total expenditure up to September would be at 50 per cent of the main budget. Expenditure smoothing would most likely lead to improved quality of spending and reduced level of unauthorised spending. This would of course differ depending on whether a government program that the department is dealing with is recurrent or capital-expenditure driven. This year Covid-19 had some bearing to this.

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Alignment of Budget to Economic Policy Interventions (2)

- Total government spending stood at 48%, slightly below the norm of 50%.
  - This is not that surprising given the shock of the Covid-19 pandemic.
- As at end of September, average spending by national government departments, was 54% of their budgets.
- However, departments such as the national department of Higher Education, Social Development, Small Business and Basic Education, far exceeded the spending norm – which can be due to Covid-19 related spending pressures.
- Departments such as Agriculture (43%), Human Settlements (33%), Energy (41%), Science and Innovation (42%), Tourism (22%), Trade and Industry (36%), Public Works (45%), Women (43%), Employment (41%), Communication (39%), Health (49%) registered spending below the norm of 50%.
- In spite of Covid-19, FFC remains concerned about excessive deviations below or above the norm from an expenditure smoothing perspective. Unless a department's in-year cash management plan explicitly identifies such deviations as a chosen spending profile, departments should be confined to spending performance guidelines

Budget Votes	% Spending (April-Sept)
Total Budget	48%
Total appropriation by vote	50%
Total direct charges against the National Revenue Fund	53%
Debt service costs	51%
Provincial equitable share (National Treasury)	50%
Selected key budget votes	54%
Public Works and Infrastructure	45%
Basic Education	51%
Higher Education and Training	76%
Health	49%
Social Development	57%
Women, Youth and Persons with Disabilities	43%
Agriculture, Land Reform and Rural Development	35%
Employment and Labour	41%
Human Settlement	33%
Mineral Resources and Energy	41%
Science and Innovation	42%
Small Business Development	73%
Tourism	22%
Trade, Industry and Competition	36%
Transport	44%
Water and Sanitation	36%
Provincial Level	40%
Education	41%
Health	42%
Social Development	39%

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ALIGNMENT OF BUDGET TO ECONOMIC POLICY INTERVENTIONS (5)

- What is clear is that 2020/21 will experience unprecedented cuts, and in areas that are envisaged to drive the Economic Reconstruction and Recovery Programme .
  - Economic development- continuous decline in growth of allocations over the MTEF
  - Peace and security, Learning and culture and social development face a disproportionate cut in 2021/22.
- Departments like agriculture and rural development, defence and state security, home affairs, education or police will experience no growth or negative growth. Either these departments will cut on service delivery or discontinue some services they are mandated to provide. The question is: How will departments manage such cuts and which aspects of service delivery will be affected?
- Reduced expenditure on education and social development are also likely to have some lagged impact on growth in the future
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ZERO BASED BUDGETING TO IMPROVED SPENDING EFFICIENCY

Feasibility of Implementing Zero Based Budgeting

- The Commission notes government's proposal to adopt a Zero Based Budget (ZBB) technique in an effort to improve allocative and spending efficiency
  - ZBB allocates funding on the basis of program efficiency and necessity rather than historical trend.
- Well implemented, ZBB is able to yield significant savings and reduce program inefficiency (wastage and duplications)
- However, government needs to exercise caution before implementing ZBB
- ZBB is fraught with multiple implementation risks and challenges
  - The process is costly, complex and time consuming
  - It may be difficult to scrutinise all spending programs within the limited time constraints of the budget cycle
- Government should rather institutionalise some aspects of ZBB – such as mandatory periodic program reviews and strengthen the process already initiated by the DPME

Conclusion

- The Commission welcomes the slight easing of the fiscal consolidation stance to cushion the impact of the economic downturn.
- The Commission further notes projected stagnant and expenditure reductions on core spending functions for the 2020/21
- The budget is susceptible to uncertainty due to the unresolved wage agreement budget proposal
- .Solutions to the wage bill conundrum should be shared by all spheres and all entities.
- Spending departments need to indicate to Parliament how they intend to absorb the budget cuts and minimise impact on service delivery i.t.o quantity and quality.
- There is need for improved alignment between the budget and economic policy interventions.
- Projected baseline reductions for 2021/22 suggest that the economy will need a bigger and bolder stimulus.
- The infrastructure led approach to growth hinges on better infrastructure delivery management across all government spheres and building capacity for infrastructure development.
- There is need to put in place sufficient data and systems to track spending and impacts of different interventions and initiatives
- Finally, there a need for stakeholders to revisit the local government fiscal framework and even the assumptions underpinning the current division of revenue to ensure that it effectively responds to developmental challenges such as rural-urban disparities; revenue bases that are increasingly shrinking in the context of equally diminishing pool of resources available for sharing; migration issues; and unrealistic costs of basic services

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