Preview Statement
Medium-Term Budget Policy Statement 2018
22 October 2018

“We need to hold the fiscal line in SA”

1. Introduction

We are in deep economic trouble, with ordinary people, who are battling to make ends meet, experiencing an income squeeze, following tax increases and petrol price hikes, and with 9.6 million people who do not have jobs, or who have given up looking for jobs, in South Africa.

2. MTBPS 2018

What this means is that the Minister of Finance, Tito Mboweni's, "mini-moon" is over and he faces a "*six pack*" of challenges that will have to be dealt with in his "maiden" Medium-Term Budget Policy Statement, which will be delivered on 24 October 2018 in Parliament.

2.1 Economic Outlook

The minister has a reputation of having fairly orthodox views on the economy, but during his political exile he often took to social media posting controversial content, which included a flirtation with Radical Economic Transformation.

Here is an example:

We do need to know whether these posts were a flirtation with Radical Economic Transformation, or a conversation to Radical Economic Transformation.

***We believe the minister should define himself by explaining his flirtation with Radical Economic Transformation and clarifying his views on extending state ownership in the mining sector, establishing a state bank and creating a sovereign wealth fund in South Africa*.**

2.2 Economic Growth

President Cyril Ramaphosa's "*new path*" of economic growth, employment and transformation lost momentum when the economy slipped into recession in South Africa.

We expect the economic growth rate to be revised down to about 0.7% (2018), 1.9% (2019) and 2.0% (2020).

Which is insufficient to sustain our public finances or provide employment to the 9.6 million people who do not have jobs, or who have given up looking for jobs, in South Africa.

***We believe the minister should present a credible plan to boost economic growth to at least 3% by announcing a package of structural reforms designed to increase private sector investment in South Africa*.**

What this requires is a fundamental change in economic policy aimed at, for example, increasing private sector investment by:

- exempting small businesses employing fewer than 250 employees from having to comply with restrictive labour laws, other than the basic conditions of employment;

- removing the extension of bargaining council agreements to non-parties, who often cannot carry the cost of wage agreements imposed on them; and

- most importantly, scrapping reckless economic policy proposals such as the formation of state banks, land expropriation without compensation and the nationalization of the reserve bank in South Africa.

2.3 *Fiscal Consolidation*

We have a staggering national debt which is expected to stabilise at about R3.8 trillion, or 53.2% of GDP, in 2023/24.

However, there is likely to be significant "fiscal slippage" given:

- lower-than-expected economic growth with the economy expected to grow at an average of about 1.5% over the medium term;

- lower-than-expected revenue given, *inter alia,* the recommendations of the independent panel on value added tax, which may decrease revenue by about R18 billion over the medium term;

- higher-than-expected expenditure given, *inter alia,* the public sector wage agreement, which may increase expenditure by about R30 billion over the medium term;

- higher-than-expected debt service costs of about R34 billion as a result of increasing national debt over the medium term; and

- financial assistance required by zombie state-owned enterprises over the medium term, such as the R22 billion in "bailouts" required by South African Airways.

The R50 billion that will be spent on the "economic stimulus and recovery plan" is expected to be funded by reprioritisation and is assumed to be "budget neutral" between 2018/19 and 2020/21.

We expect fiscal deficits to increase and national debt to stabilise at a level above R3.8 trillion, or 53.2% of GDP, some time after 2023/24.

What this means is that debt service costs will skyrocket to about R280 billion in 2023/24, which is a staggering R87 billion more than we will spend on social grants this year, in 2018/19, in South Africa.

We believe the minister should hold the fiscal line by announcing a comprehensive spending review and presenting a credible plan to stabilise national debt at, or below, 50% of GDP in South Africa.

The Comprehensive Spending Review would be aimed at reviewing the efficiency of spending, composition of spending, future spending priorities and asset sales, with a view to:

- selling off assets including public entities, underutilised buildings, underutilised land parcels and liquid assets;

- improving the composition of spending by funding investment in infrastructure to support economic growth; and

- cutting the fiscal deficit to reduce national debt, and debt service costs, over the medium term between 2019/20 and 2021/22.

However, if we are serious about the expenditure problem then we have to get serious about cutting the cost of "compensation of employees" in the Comprehensive Spending Review.

The fact is that the cost of "compensation of employees" in general government will consume an average of about 40% of tax revenue over the medium term between 2019/20 and 2021/22.

We could cut costs on "compensation of employees" through a combination of measures including retrenchments, early retirements, severance packages, headcount freezes and wage freezes.

To illustrate the savings envelope available, a "wage freeze" in general government could save a total of about R238 billion over the medium term between 2019/20 and 2021/22.

2.4 Institutional Strength

The fact is that, as a result of state capture, public trust has been shattered in many institutions in the "finance family", not least the South African Revenue Service.

The interim report of the Commission of Inquiry into Tax Administration and Governance by the South African Revenue Service paints a terrifying picture of intrigue, fear, distrust and suspicion at the South African Revenue Service.

> ***We believe the minister should restore public trust by announcing that the Commissioner of the South African Revenue Service, Tom Moyane, will be removed and a new appointment will be made without delay, in line with the recommendations of the Commission of Inquiry into Tax Administration and Governance by the South African Revenue Service***.

2.5 State-Owned Enterprises

The "boards and bailouts" strategy of Minister of Public Enterprises, Pravin Gordhan, means that there are several zombie state-owned enterprises that require financial assistance of some form over the medium term including: Denel (+/- R1 billion); South African Broadcasting Corporation (+/- R1.2 billion); South African Post Office (+/- R2.7 billion) and South African Airways (+/- R21.7 billion).

> ***We believe the minister should present a credible plan to reform failing state-owned enterprises by:***
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> - ***placing a moratorium on any further government guarantees to state-owned enterprises; and***
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> - ***placing the national airline in business rescue and then privatising, or part privatising, South African Airways***.

2.6 Major Fiscal Risks

The fact is that Eskom, with its R387 billion debt mountain, much of which is backed by government guarantees, could blow up the balance sheet in South Africa.

With declining demand, revenue shortfalls, cost overruns and a debt mountain, the question remains, what to do with Eskom?

What makes matters worse is that Eskom recently received a “confidential” R34.4 billion loan from the Chinese Development Bank.

We believe the minister should present a credible plan to:

- ***turnaround the utility by privatising, or part privatising, the power generation assets;***
- ***end the monopoly by allowing cities to purchase electricity directly from independent power producers;***
- ***make it clear that the R350 billion government guarantee currently in place is a hard ceiling for Eskom*; and**
- ***make a full disclosure of the terms and conditions of the confidential R33.4 billion loan from the Chinese Development Bank to Eskom***.

3. Conclusion

We believe that if the Minister of Finance, Tito Mboweni, deals decisively with the “*six pack*” of challenges during the Medium-Term Budget Policy Statement, he will give hope to ordinary people who are battling to make ends meet, and who are experiencing an income squeeze, and to the 9.6 million people who do not have jobs, or who have given up looking for jobs, in South Africa.