National Budget
2020

Alternative Budget Proposals

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Introduction:

Minister Tito Mboweni's budget speech on Wednesday, 26 February 2020 must address South Africa's immediate fiscal crisis, described by four devastating simultaneous pressures:

- the unrestrained expansion of public debt means more is spent on interest charges, and there is less money for essential services;
- the sharp decline in tax revenues because of near-zero economic growth means there is less money for essential services;
- the ballooning of the public wage bill which means less money for essential services;
- continuous enormous bailouts for zombie state owned companies, which means less money for essential services.

If this does not change in a very significant way, then South Africa will lose its investment grade credit rating, and will not avoid bankruptcy.

If Minister Mboweni does not make watershed commitments that will arrest this situation, then his budget will simply not be credible.

There is a growing credibility gap between the strong language in budget speeches on cutting debt and the public wage bill, and achievements to date.

Despite the stern commitments in last year's budgets, national debt, measured as net loan debt, is set to increase to a staggering R4.2 trillion, or 67.5% of GDP by 2022/23. That is *if* there are no further revenue shortfalls, an increasingly unlikely outcome.

Therefore, the only really important test of this budget's credibility is the seriousness of the plans presented to rein in national debt, cut the public wage bill, and grow the economy. That is how we will judge his speech.

Our proposal to restore fiscal responsibility:

We also present proposals today to demonstrate that the Democratic Alliance can and would restore fiscal discipline in South Africa, on which all sound economic policy and growth is based.

Specifically, the Democratic Alliance is today re-introducing a legislative fiscal rule that will help stabilise national debt.

The DA has initiated a Parliamentary process to introduce a Private Members Bill, in terms of Section 73(2) of the Constitution, titled the *Fiscal Responsibility Bill [B_2020]*.

The Fiscal Responsibility Bill (FRB) will ensure that debt levels and debt service costs are kept under control by setting legislative limits on how much the government can borrow each year.

Legislative fiscal rules, sometimes referred to as 'fiscal anchors', are now frequently recommended in public finance literature, and are becoming an increasingly common feature of public finance legislation around the world.

Tito Mboweni has recommended these for South Africa, saying in his 2018 Medium Term Budget Speech: "New fiscal anchors may be required to ensure sustainability, in addition to the expenditure ceiling. We must choose public sector investment over consumption."

In its 2019 Article IV Consultation Report on the South African economy, the IMF recommended that '*authorities should establish a credible debt anchor to stabilize debt in the medium term.*'[i] Similarly, in November 2019, Moody's Investor Services indicated that '*it wants to see a credible fiscal strategy to contain the rise in debt in the budget*'[ii] in South Africa.

The Fiscal Responsibility Bill aims to introduce, inter-alia, a "fiscal rule" that would reduce national debt and debt service costs in South Africa.

First, the Fiscal Responsibility Bill provides for:

- a fiscal rule prescribing that, for each financial year from 2020/21 to 2023/24, net loan debt expressed as a percentage of GDP must not be more than it was the previous year.

Second, the Fiscal Responsibility Bill provides for:

- a review of the fiscal rule by the National Assembly every four years, beginning in 2023/24 by either amending, renewing or terminating the fiscal rule; and
- an annual Fiscal Responsibility Report to be tabled by the finance minister at the same time as the budget is tabled, setting out whether the fiscal rules were complied with or not, together with reasons for those outcomes, and recovery plans in the event of a failure to comply with the fiscal rule.

And, finally, because South Africa is a small open economy, vulnerable to shocks, the Fiscal Responsibility Bill provides for:

- an exemption from the fiscal rule to be granted in respect of a specific financial year, or years, by the National Assembly upon application by the finance minister, with good cause having been shown and on the recommendation of the Standing Committee on Finance.

<u>Our proposal to alleviate the electricity crisis:</u>

The admission by President Ramaphosa and Eskom CEO Andre de Ruyter that loadshedding will remain a possibility for the near to medium term is another blow to the economy. **South Africans need their "Freedom from Eskom"**. We propose income tax incentives to incentivise and assist individuals to generate electricity at their private residences for their own consumption. This will alleviate pressure from the grid, helping to lower the load-shedding burden for other families, and importantly for businesses.

The DA is therefore proposing an Emergency Solar Rebate (ESR) that would offer tax rebates for solar systems installed at residential properties.

The Emergency Solar Rebate would be available for three years only, designed to alleviate our current energy crisis, and would work as follows:

- **100% tax deduction for the cost of installed solar equipment, up to a maximum of R75 000;**
- **The purchaser would fund the cost of installation upfront, and would claim the cost against their taxable income at time of submitting their ordinary annual returns.**

This emergency initiative would cost R4 billion over 3 years, and remove 480 MW from the grid, with even a moderate take-up rate.

Under the ESR, households would be very significantly incentivised to install this equipment immediately. Private home owners will be incentivised to install solar infrastructure on their properties using the same tax provisions, set out in s12B(h) of the Income Tax Act, which give small businesses tax rebates to install renewable energy on their properties. This would take pressure off the grid and act as a stimulus as savings are mobilised now and offset against tax later.

Cost of this initiative:

Assuming the take up is 20 000 homes in the first year, 30 000 in the second year, and 50 000 in the third (final year), then the cost of the initiative over the MTEF would be:

	Year 1	Year 2	Year 3	Electricity Saved
20 000 rebates	R800 million			96 MW
30 000 rebates		R1,2 billion		144 MW
50 000 rebates			R2 billion	240 MW
Total Cost/Saving			R4 billion	480 MW

<u>Our proposal to cut the primary deficit</u>

Economic growth is expected to average below 1% this year, with a likelihood of a further revision downwards[iii]. This low growth trap means that South Africa will continue to miss revenue targets due to declining VAT and corporate receipts, and as unemployment continues to tick upwards.

This paucity of growth also means there is no question of raising new revenue through new taxes. New taxes would only act as another brake on growth.

In last year's budget, the failure to adjust income tax brackets for inflation led to a stealth tax increase of R12 billion from working families' pockets. This should not be repeated.

Next year, at current expenditure levels, the budget deficit is expected to reach R374 billion, 6.8% of GDP, and 35.3% of total government expenditure.

In order to stabilise the budget deficit, bring down debt and restore fiscal discipline, there is an urgent need to reduce spending by R250 billion over the next three years, averaging R83 billion per fiscal year.

The DA's plan to stabilise the budget deficit and the national debt will be achieved through the significant cuts to the public wage bill that the Minister has called for, but has not shown in progress in delivering; as well as by stopping all bailouts to failing zombie state owned entities.

These changes will achieve an adjustment of R349.95 billion over the MTEF period.

It has become morally indefensible for government to continue bailing out SOEs despite clear evidence that they are beyond saving due to years of state capture and poor management. A choice has to be made on whether to keep throwing money at these zombie SOEs or to protect essential public services: policing, education and healthcare.

Expenditure cuts

The DA proposal to stop all bailouts to SOEs will help realise R35.1 billion in the 2020/21 financial year:

- R33 billion will be from the Special Appropriations Bill passed in 2019 to bailout Eskom in 2020/21;
- R1 billion reserved for Denel in 2020/21;
- The outstanding R1.1 billion from the approved R3.2 billion bailout for the SABC.

Evergreen multi-billion bailouts to Eskom will not only continue to pose a serious threat to fiscal stability but will serve no purpose as long as entrenched interests continue to resist an overdue restructuring.

Moody's has cautioned that any additional support without an accompanying plan to make the company more sustainable is "credit negative". Eskom's immediate objective should be to decommission or sell off some of its assets, especially its aging and inefficient coal power plants that require investment to keep operational, and are partly responsible for the load shedding crisis we currently face.

In addition to the R35.1 billion realised from SOE bailouts, the DA is still the only party that has presented credible plans for how to achieve the public wage bill savings that the Minister has targeted.

In October 2019 we presented a credible, costed plan to achieve a R168 billion cut to the public wage bill over the next three years through:

- Freezing the wages of the 33.7% of public servants not covered by the Occupation Specific Dispensation (OSD) (including the likes of highly paid head office managers and supervisors) at 2019/20 levels over the three-year MTEF period. This would protect the real front-line delivery staff, and would also yield R138,6 billion;
- Saving another R29.4 billion over the MTEF period through reductions and a hiring freeze on all managerial positions (non-OSD levels 11 to 16) until the number of managers is reduced by a third – approximately 9 200 posts.

As a result of a decade of immoral patronage driven wage increases by the ANC government, expenditure on the public wage bill for 2020/2021 is projected to reach R713 billion.

This is the reason why infrastructure spending will be lower in 2021/22 than it was in 2016/17. In real terms, infrastructure investment has declined by 1.8% per year from 2017/18 to 2019/20, and is set to fall by an average of 6.3% from 2019/20 to 2021/22.

Instead of protecting infrastructure spending over the past decade, the government chose to sacrifice productive investment in favour of increasing public sector wages by 10.3% annually since 2009 – well above the rate of inflation.

To plug the revenue gap and raise the requisite funds to facilitate productive investments in the economy, government has to consider potential revenue that could be raised from its asset inventory. The DA proposes once-off revenue raising mechanisms and cuts over the MTEF period that can raise R67.85 billion:

Once-off mechanisms:

- Auctioning digital spectrum would raise R32.5 billion
- Selling Telkom shares would raise R14.5 billion
- Selling Sentech would raise R1.8 billion

Cuts over MTEF period:

- Eliminating New Development Bank funding would save R13.25 billion
- Eliminating National Health Insurance funding would save R5.8 billion

Expenditure cuts over MTEF period				
R billion	2020/2021	2021/2022	2022/2023	Total MTEF
Freeze non-OSD wages	21.9	45.7	71	138.6
Freeze bailouts to SOEs				
Eskom	33			33
Denel	1			1
Cuts over MTEF period				
Cut New Development Bank	4.25	4.5	4.5	13.25
Cut National Health Insurance	2.8	3	-	5.8
Total over MTEF period				**192.75**
Once-off mechanisms				
Auction digital spectrum				32.5
Reduce managers by a third				29.4
Sell Telkom shares				14.5
Sell Sentech				1.8
Total once-off				78.2
Total over MTEF plus once-off				**349.15**

Additional Information and Notes:

1. Fiscal Framework and Macroeconomic Outlook – October 2019

Table 1.2 Consolidated government fiscal framework

R billion/percentage of GDP	2018/19 Outcome	2019/20 Revised	2020/21	2021/22	2022/23
			Medium-term estimates		
Revenue	**1 445.4**	**1 537.8**	**1 618.5**	**1 729.6**	**1 841.2**
	29.4%	*29.5%*	*29.3%*	*29.4%*	*29.3%*
Expenditure	**1 652.8**	**1 844.1**	**1 978.7**	**2 097.5**	**2 214.9**
	33.6%	*35.4%*	*35.8%*	*35.6%*	*35.3%*
Budget balance	**-207.5**	**-306.2**	**-360.2**	**-367.9**	**-373.7**
	-4.2%	*-5.9%*	*-6.5%*	*-6.2%*	*-5.9%*
Total gross loan debt	**2 788.4**	**3 167.6**	**3 590.8**	**4 035.7**	**4 477.7**
	56.7%	*60.8%*	*64.9%*	*68.5%*	*71.3%*

Table 3.6 Main Budget Framework / Table 3.9 Total national government debt

R billion/percentage of GDP	2018/19	2019/20	2020/21	2021/22	2022/23
Gross national debt	**2 788.4**	**3 167.6**	**3 590.8**	**4 035.7**	**4 477.7**
	56.7%	*60.8%*	*64.9%*	*68.5%*	*71.3%*
Debt service costs	**181.8**	**203.7**	**232.8**	**264.6**	**299.1**
	3.7%	*3.9%*	*4.2%*	*4.5%*	*4.8%*
Net loan debt	**2 545.3**	**2 924.0**	**3 358.1**	**3 800.3**	**4 243.0**
	51.7%	*56.1%*	*60.7%*	*64.5%*	*67.5%*

Table D.2 Macroeconomic performance and projections

Percentage change	2018/19	2019/20	2020/21	2021/22	2022/23
				Forecast	
Real GDP growth	0.6%	0.9%	1.2%	1.6%	1.8%
Nominal GDP growth	4.7%	5.9%	6.1%	6.6%	6.6%
CPI inflation	4.6%	4.5%	4.8%	4.8%	4.7%
GDP at current prices (R billion)	**4 921.5**	**5 210.8**	**5 530.3**	**5 893.1**	**6283.0**

Table 1.1 Macroeconomic outlook - summary

Real percentage growth	2018	2019	2020	2021	2022
				Forecast	
Real GDP growth	**0.8%**	**0.5%**	**1,2%**	**1,6%**	**1.7%**
Consumer price index (CPI) inflation	**4,7%**	**4,3%**	**4,9%**	**4,8%**	**4,8%**

Source: National Treasury

2. Updated Fiscal Framework

What has changed since October:

- Continued pressure to spend more, especially given the poor state of SOEs;
- GDP will be lower than what was forecast;
- The GDP to debt ratio is expected to breach the 65% mark for the first time;
- Another revenue shortfall is expected.

Increased appropriations:

- The Special Appropriation Bill allocated an additional bailout to Eskom amounting to R33 billion in 2020/21. This breaches the fiscal framework that was adopted by Parliament by R10 billion.

Additional bailouts to Eskom, SABC, SAA and Denel:

- While the DA is advocating for a stop to bailouts for SOEs, government seems intent on raiding the contingency reserve to fund their operations. MTBPS review 2019 states that 'Other state-owned companies are also adding to spending pressures on government. Funding for South African Airways (SAA), the South African Broadcasting Corporation, Denel and South African Express amounts to R10.8 billion in the current year, almost the entire contingency reserve for 2019/20'[iv] This means that, in the case of a national emergency, the government is not in a position to help vulnerable citizens affected by a disaster.

- Bailouts (apart from the Eskom bailout):

- **Denel: Assume R1 billion 2020/21** – the R1 billion bailout for Denel, in the 2020/21 financial year, could be potentially factored in during the current fiscal year.
- **SAA: Assume R5.5 billion 2020/21**: at the end of January 2020, SAA received a bailout of R3.5 billion from the Development Bank of Southern Africa. It is still not clear whether government will avail the additional R2 billion to fund the airline in the current financial year.

With the depletion of the contingency reserve, government will almost certainly have no fiscal space to continue bailing out SOEs. It has become urgent for government to lessen cumbersome red tape that has been used over the years to protect monolithic SOEs, and open up space for private investment to encourage competition and improve efficiencies.

Revenue collection:

MTBPS review 2019 expects the revenue collection shortfall to widen from R57.4 billion in 2019/20 to R84 billion in 2020/21. This will have a corresponding impact on the budget deficit, debt and debt-to-GDP ratio. Of particular concern is that the debt servicing costs will increase over the short term.

Growth and inflation expectation:

MTBPS 2019 (National Treasury)			
	2020	**2021**	**2022**
	Forecast		
Real GPD growth	1,2%	1,6%	1,7%
Consumer Price Index (CPI) inflation	4,9%	4,8%	4,8%
	2020	**2021**	**2022**
Real GDP growth (Financial year)	1,2%	1,6%	1,8%
SARB (September 2019)			
	2020	**2021**	**2022**
	Forecast		
Real GDP growth	1,2%	1,6%	1,9%
Consumer Price Index (CPI) inflation	4,7%	4,6%	4,5%

- Projected GDP growth is expected to be lower and inflation higher than what was expected in the October 2019 MTBPS. This means that, over the medium term expected revenue will be lower than initially forecast creating an upward pressure on deficit to GDP ratio and debt-to-GDP ratio.

References

[i] IMF Executive Board Concludes 2019 Article IV Consultation with South Africa - https://bit.ly/37EPjK2
[ii] Moody's changes South Africa's outlook to negative from stable, affirms Baa3 ratings - https://bit.ly/39G9M2y
[iii] South Africa : 2019 Article IV Consultation-Press Release; and Staff Report; and Statement by the Executive Director for South Africa - https://bit.ly/38wPGaT
[iv] Medium Term Budget Policy Statement October 2019 - http://www.treasury.gov.za/documents/mtbps/2019/mtbps/FullMTBPS.pdf