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Our goals for the South African economy are clear.

We seek a faster rate of growth of incomes and employment. We intend the benefits of growth to be strongly reflected in rising living standards of the poor.

From these objectives flow many policy imperatives. We are restoring fiscal discipline, we are liberalising the foreign exchange regime, tariffs are coming down. Our industrial and export incentive schemes are now leaner and better targeted.

A major electrification drive is well underway, a telecommunications campaign has begun. Schools and clinics are being upgraded. We have put training and skills development firmly on the Nedlac agenda. We are investing in water – from a major venture in the Lesotho Highlands, to the provision of borehole water to Manganeng village in the Northern Province.

These are all undertakings in which government is forging constructive alliances with the private sector. Telkom is now partially privately owned. Private finance has been brought into our new roads projects. We are exploring ways of combining government finance with private spending on training. And the project that will bring water standpipes to the streets of Manganeng is a public-private partnership in which both private shareholding and commercial bank investment will be involved.

These are just some of the many elements of the programme of reconstruction and development of the South African economy that we tabled before the electorate in 1994. We are implementing these development initiatives within the context of a responsible macroeconomic and fiscal framework – recognising that these are commitments we will take with us into the next decade and beyond. Building a dynamic economy, securing jobs and basic services for all, strengthening the capacity and efficiency of government, balancing competing claims on the available resources, are challenges that require courage and patience.

We would like, of course, to achieve greater things, more quickly. But it is our vision for the next ten and twenty years that underpins our policy goals and commitments. As the President has made clear so many times, our children and our children's children have the first call on our resources.

What does this mean, for fiscal and financial policy?

Budgetary reforms

Let me speak first about the fiscal challenge and the budget process.

We collect taxes equivalent to about a quarter of GDP. In the early 1990s, in the last years of the previous administration, government spending reached over a third of GDP, (including off-budget expenditure such as losses to the government pension funds associated with expensive early retirement schemes and the costs to the Reserve Bank of running an asymmetric forward exchange book). It was not admitted at the time, but we now know that the national budget deficit reached over 10 per cent of GDP in 1993/94.

Last year the deficit was 5½ per cent of GDP. This is still too high. And so we have budgeted this year for total national expenditure growth of just 6,1 per cent, well below the expected rate of inflation. The deficit is 4 per cent of GDP. We intend to bring it down to 3 per cent by 1999/2000.

Government departments have had to trim their spending programmes and re-think their longer term commitments. We have a decentralised system of financial management and accountability, in which spending agencies have full responsibility for keeping within their budgets. Contrary to widespread belief, departments are accustomed to keeping within their budgets. Where additional allocations have to be made, this is done transparently in an Adjustments budget towards the end of the fiscal year. The rule is that only unforeseen and unavoidable additional spending is allowed. We keep a reserve on the budget to provide for this.

Last year, the Adjustments budget provided for shortfalls on the prisons and police budgets, mainly owing to the increasing numbers of prisoners in custody and rising case loads in the criminal justice system. We also provided for losses of the post office, and several minor items. After taking into account declared savings of R484 million, the net addition to national government expenditure was just under R1 billion. This year, we have kept aside a reserve to provide for these kinds of contingencies. We do not expect the national budget target to be exceeded.

Last year, provinces also received additional allocations in the Adjustments budget, amounting to R1,4 billion. By agreement with provincial MECs for Finance, there will be no such assistance this year. Provinces have independent fiscal standing, and have no recourse to the national fiscus. This is not just a question of maintaining fiscal discipline. It is also a Constitutional imperative. We have an agreed, equitable framework for sharing revenue between the national, provincial and local spheres of government. This is not a contract that can be overthrown to deal with *ad hoc* circumstances in one province or municipality.

As it turns out, several provinces and some local governments have indeed got into difficulties this year. The magnitudes involved are not yet entirely clear, nor are all the reasons for the problem.

Over the past few weeks, the departments of Finance and State Expenditure have been working intensively with provincial treasury officials and the main provincial spending departments to develop a strategy for budget management over the rest of the year. Similar exercises have been undertaken where local authorities need to put their finances on a sound footing.

Improved financial management is of course central to resolving the problems. I have reached agreement with my provincial colleagues that we will bring in the necessary skills, and the national departments of education, health and welfare will similarly help in putting provincial management on a sound footing. Where the private sector has the kinds of expertise we need, we will open up contractual partnerships both as short-term measures and with a view to building long-term capacity.

It appears that poor personnel management has been one of the major causes of provincial spending increases. Provinces account for two-thirds of the government wage bill, but are not sufficiently involved in pay negotiations, determining staffing norms or ensuring efficient utilisation of personnel. The present voluntary severance arrangement has probably reached the limits of its usefulness. Cabinet has agreed to take proposals for an affordable retrenchment package to the bargaining chamber, to facilitate ongoing public service personnel restructuring. Provinces are in the meantime implementing much stricter control of personnel recruitment, pay determination and temporary employment arrangements.

Welfare and social security programmes have also been an area of weak expenditure control. A consolidated pension database has now been established, and problems of fraud and mismanagement are being attacked more vigorously.

But I should add that we are well aware that spending trends are driven by policy commitments, in addition to management considerations. We are embarking on significant enhancements of the health services, schooling and welfare services available to the poor. Some 250 clinics have been built in areas previously unserved by the health system. Teacher qualifications are improving and we are putting books and equipment into schools that previously had only broken blackboards and crumbling sticks of chalk.

There are those who have argued that our deficit reduction targets threaten these RDP commitments. Of course, it would be easier to redress historical imbalances without cutting back elsewhere. But we know that we have to reprioritise. In practice, our deficit reduction programme sharpens the reprioritisation process. It focuses the collective mind of government on its core business. And in some areas of government’s business – in education, health and welfare services, for example – government is phasing down its subsidisation of services to higher-income communities.

These are difficult things to do – parents feel the pressure of rising school fees; homes for the elderly are having to find other sources of funding; hospitals cannot offer unlimited access to expensive services. But we inherit a structure of public services that is manifestly unjust. The state cannot continue to spend more on meeting the social needs of the rich than of the poor. Reprioritisation is partly about choosing a mix of public spending that is in tune with our needs and aspirations – less on defence; more on rural water supplies. It is also about fair rules of access and funding, phased in over a realistic period of adjustment.

The most important budgetary reform currently in progress in South Africa is the adoption of a multi-year expenditure planning framework, to be introduced as a three-year expenditure framework tabled alongside the 1998/99 national and provincial budgets. It is a cooperative undertaking of the national and provincial treasuries, in which all spending agencies have prepared their budget submissions on a three-year basis, making explicit the links between policy commitments and their expenditure estimates. Needless to say, there is a substantial gap between the first estimates and the affordable expenditure.

Deliberate forward planning and publication of medium-term estimates put the emphasis firmly on policy prioritisation. In the context of South Africa's post-apartheid transition, it is clearly right that this should be the central theme in budget reform. Our performance has to be measured by our success in bringing services to those denied them in the past.

The first draft of a medium-term expenditure framework has been compiled. This has not just been a technical exercise in budgeting and programme accounting. We have taken a wide range of policy issues to Cabinet, relating the budget projections for the next three years to the choices to be made over priorities, service standards, phasing in of new commitments and closure of redundant programmes.

Before the MTEF is finalised, Cabinet will have taken some tough choices – we cannot fund all the schemes that national and provincial departments would like to undertake over the next three years.

Publishing three-year forward budgets will be a major step forward in itself. It will greatly add to the transparency and credibility of our policy commitments. It will also mean that policy discussion, and the continued reprioritisation of spending commitments, will take place within a clear and agreed budgetary framework. New commitments will have to be accommodated with the available resource envelope – making explicit the choices and trade-offs involved.

Financial developments
I come now to the broader financial context.

We have benefited since 1994 from a more open international financial environment, bringing foreign savings into the South African economy, together with corporate skills and industrial technology.

We have also suffered somewhat from the volatility of capital flows – investors are a cautious and sentimental lot, which no doubt helps keep finance ministers appropriately prudent.

In general, the mobility of capital and the intelligence that the financial markets bring to bear on investment decisions have played important roles in sustaining economic expansion in industrialised countries and strengthening the performance of many developing countries. I am not going to hazard any predictions against the background of recent market developments, but I think we can look back with some pride on the progress we have made in our financial reforms over the past few years. I am sure there is somebody out there who lost his shirt last week, but the rand and our capital markets have shown considerable resilience in rather stormy circumstances. We have a policy framework, and economic growth potential, that should continue to attract foreign investment. We have a central bank and a financial industry that are, I know you will agree, equal to the challenges before us.

There are several areas in which the fiscus plays its part in the evolution of a more competitive financial environment.

- A framework of principles has been adopted for debt management and there will soon be a shift from market-making in government bonds by the Reserve Bank to primary dealers operating for their own risk. It is intended that the role of the Reserve Bank will be reduced over time to that of supervisory agent over the primary dealers, on behalf of the Department of Finance.
- We have also adopted a formal cash management function in the Department of Finance, contributing both to cost-saving and improved and more timely information flows. These reforms are being extended to provincial treasuries.
- We have adopted a revised set of guidelines for granting borrowing powers to government agencies and for issuing government guarantees. Fees are now charged for this function.
- We have a new regulatory framework for borrowing by provinces and local government.
- We are developing improved financial reporting requirements for public sector entities, which will in due course include accounting standards consistent with best international practice.
- As I have noted, there are several areas in which we are bringing private finance into partnership with government in innovative ways.

These are not reforms for the sake of change. Our objective in reorienting the public finance environment is to ensure that capital is efficiently allocated. This means more intelligent management of risk, a more competitive approach to debt management, more transparent reporting of public sector assets and liabilities and an appropriately phased restructuring of the investment portfolio of the government pension funds.

Life being what it is, I have to tell you that there may be tax implications.

We would like to bring income tax rates down, but this cannot be done without reforms that extend the tax base and combat tax avoidance arrangements of various kinds. Efficient capital markets also require that the influence of the tax code on investment decisions should be kept to a minimum. Of course, confident investment decisions also require a sufficient degree of tax certainty. The Katz Commission’s work has been undertaken in stages, which has helped establish tax reform as an ongoing process rather than an event. This is as it should be.

Our intention is not to eliminate fiscal uncertainties. But we have gone a long way towards clarifying where we are going – the macroeconomic framework is in place, our deficit reduction targets have been agreed, we will maintain the overall tax burden at around its current level and a three year expenditure programme will be introduced next year.

Conclusion

You have a stimulating programme before you for the remainder of this *financial markets conference*. I hope it will be possible to take forward the discussion of practical ways in which private finance can be brought into partnership with the public sector, adding value to projects and not just substituting private capital for taxpayers' funds. I am sure you share with me a conviction that this is one of the foundations on which we must build a more prosperous and a more just South Africa.