NATIONAL TREASURY BUDGET VOTE SPEECH

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Mister Speaker, I present the National Treasury's Budget Vote for the consideration of the House. In doing so let us take stock of an increasingly dangerous global environment and the economic challenges we face in our journey to a more inclusive growth path.

The global turmoil of the past four years has reminded us not just of the risks associated with credit-based booms and the importance of rigorous financial regulation, but also of the inter-connectedness of financial and fiscal systems. Breakdowns in banking lead to budgetary interventions; budget failures require banking intermediation.

But the issues confronting Europe and other parts of the world are not just about the economy but more broadly about the political economy of policy making in complex and challenging times.

Much of the work of the National Treasury, Mister Speaker, is focused on understanding these dynamics and ensuring that we don't step over critical solvency and sustainability frontiers. But financial and fiscal health is not enough. We also need a vigorous enterprise economy, we need prosperous mines and factories, we need our schools and hospitals to function well, we need to enhance competitiveness and improve productivity, both in government services and in the private sector. These are not just outcomes of sound budgets and sustainable financing arrangements, they also depend on effective implementation of policies and programmes.

Economic outlook and global developments

Global economic growth has remained weak this year, as we anticipated at the time of the Budget in February. Growth in output in our own economy is uneven and slow, though consumption spending is still buoyant. But the challenge we face is not just growth, it is a more broad-based transformation; not just development, but structural change that will extend opportunities to the unemployed, and unshackle the enterprise potential of our people.

What are the trends, Mister Speaker, in our economic performance? The domestic economy is showing some signs of moderate growth but the external environment remains weak and risks are high. The most recent data from the South African Reserve Bank, for the last quarter of 2011, showed that household consumption and investment were still growing robustly. Consumption grew by 4.6 per cent in the quarter, investment by 7.2 per cent and government consumption grew by 7.3 per cent. National Treasury forecasts that household consumption and investment will continue to grow robustly in 2012, and government spending will also support growth.

But output growth in the first quarter of this year was slower than we forecast at Budget time, mainly due to the effect of the Impala platinum strike on mining production. Retail sales have also slowed somewhat. Mining output recovered in March, growing by 5.3 per cent month-on-month, but manufacturing production was disappointing, falling by 4.3 per cent. Monthly figures are volatile, but it is clear that investment is still held back by both global and domestic uncertainties.

Leading indicators, such as the Kagiso Purchasing Managers Index and the Reserve Bank's Composite Leading Business Cycle Indicator, point to continued growth but at a moderate rate. Despite high oil prices and a weaker exchange rate, inflationary pressures have remained relatively subdued.

The main risks to the economy remain external. Political developments in the Eurozone have heightened the risk that Greece will exit the single currency within the next year, though there is little clarity on how this would be achieved and what its impacts would be. More serious for both the global economy and the potential impact on South Africa is the continuing vulnerability of several larger European economies, including Spain. A large budget deficit and a deflating housing bubble have reduced confidence in government finances and the solvency of Spanish banks. Our expectation is still that there will be a shallow recession in the Eurozone but the risk of a deeper contraction has grown since the Budget.

The United States should post subdued but positive growth in 2012, at a pace similar to the 2.2 per cent expansion in the first quarter of this year. The US recovery is not as robust as expected, and it appears likely that fiscal contraction will subtract from US growth in 2013.

There are also risks to Chinese growth, due to slowing exports to the Eurozone area and a deflating domestic housing bubble. Easier monetary policy should help sustain China's growth, but it is expected to slow.

Several economies in Africa and the developing world continue to grow more quickly than the main developed economies. Trade and investment patterns are shifting rapidly. Both our international relations and our trade and industry policies have to adapt to this rapidly changing global environment. We need to join our African partners in boosting industrialisation in Africa, developing regional value chains, and increasing intra-African trade.

We need to take stock of where we are in the light of the financial crisis.

Growth is an imperative if we are to reduce poverty and inequality in our society. Much of Europe is currently grappling with the tension between growth and structural reforms, on the one hand, and the need to reduce debt and financial imbalances on the other. Our choices may not seem so stark, and perhaps our challenges are more about institution-building and adjustment to new global trade opportunities. There is good evidence that countries with sustainable macroeconomic policies, sound institutions and good governance fare better than others in sustaining rapid growth for long periods. The evidence is also clear that human development and the quality of education are critical for growth and development.

The global financial crisis has exposed the limitations of unfettered liberalisation as a growth strategy, and has also highlighted the inadequacy of international cooperation in addressing collective interests and shared risks. In ensuring that our own interests are addressed in this global landscape, we seek with other developing countries a better balance in global governance and better institutions for collaboration and partnership.

In this respect the work of the National Treasury and its associated institutions – the Development Bank of Southern Africa, the Public Investment Corporation, the Financial Services Board, the South African Revenue Service, the Financial Intelligence Centre, amongst others – is highly dependent on the policies and programmes of my fellow Ministers, other departments and our provinces and municipalities. Our successes, and our shortcomings, are shared. And we have to share in the challenge of finding a growth path that creates jobs, reduces poverty and broadens participation in a more rapidly expanding economy.

The Treasury has several specific responsibilities in this challenge. These are elaborated in the Strategic Plan for the period ahead, and the more detailed performance plan for 2012/13. Allow me to highlight a few key themes.

- Our countercyclical fiscal stance, reflected in the budget framework tabled in February this year remains correect. It requires continuous monitoring of economic and public finance trends and analysis of long term prospects. Work is in progress on a long term fiscal report and fiscal guidelines, as requested by Parliament. We expect to be able to table a first report later this year, and look forward to discussion in the House.

- The Presidential Infrastructure Coordinating Commission has made excellent progress in the planning and assessment of strategic infrastructure programmes required as the foundations of faster long term growth and more inclusive development. The financing and financial management of these projects are critical for their successful implementation. The Treasury has stepped up its capacity to assess and support major infrastructure programmes, and will continue to strengthen work in this area.
- We recognise that accelerating infrastructure investment and maintenance will require further shifts in the composition of expenditure in future years. Alongside the emphasis on transparency and performance measures in our budget process, we continue to work intensively on better value for money in government expenditure, combating corruption and improved procurement and supply chain management processes. The second phase in our review of procurement legislation will go ahead this year.
- Faster economic growth depends in part on improving our national savings effort. An initial discussion document on savings and retirement reform has recently been published, and social security proposals will shortly be released. We look forward to public consultation and engagement within this House on these reforms over the months ahead.
- In support of faster employment creation, the Government has established a Jobs Fund which is administered by the Development Bank of Southern Africa. It has allocated R1.8 billion to 34 projects to date, which will be matched by project sponsor contributions of about R1.7 billion. These projects are expected to generate about 102 000 new jobs, and over 50 000 placement and training opportunities. A second call for proposals has been issued, and in due course we hope to be able to report on lessons learnt from Jobs Fund initiatives, which are structured to encourage innovation and new approaches to addressing the urgent imperative of creating jobs for young people.
- Our cities and towns play an important role in economic development. In addition our townships are and must increasingly be turned into centres of economic vibrancy. Two programs will promote this ambition.
    - o We will soon be in a position to report on lessons from the Neighbourhood Development Programme Grant, which will see about 85 projects under construction by the end of this year. Work is already in progress on a broader framework for township regeneration and improved integration of urban landscapes, drawing on the experience of this programme.
    - o A new Cities Support Initiative will get underway this year, beginning with needs assessments and identification of pilot interventions to

support improved infrastructure planning, management of the built environment and economic development of major urban areas.

- The Treasury has also assisted in the renewable energy procurement process overseen by the Minister of Energy, which is currently assessing the second round of proposals by independent power producers and will in due course lead to multi-billion rand investments in harnessing wind and solar power as part of our national electricity network.
- Better financial management requires investment in financial skills and capacity. The Treasury continues to expand its training and support activities in public finance management, internal audit, municipal finance, supply chain management and government accounting.

These are just some of the Treasury's activities. Mister Speaker, in the flurry of debate on issues of the day, we are inclined to forget the ordinary business of planning and monitoring, consultation with departments and government agencies, negotiation around budgets, analysis of financial trends, impact and risks; revenue collection, loan management, financial supervision – our economic and development progress depends on steadily advancing our capacity in these ordinary activities, because they need to be done well, responsibly and honestly if our plans are to succeed.

Employment

Data from the Quarterly Labour Force Survey (QLFS) shows overall employment decreased by 75 000 in the first quarter of 2012. Employment fell across all age groups, with job shedding most severe among those aged 25 to 34 years old (31 000, q/q), 35 to 45 years (22 000 q/q), and 55 to 64 years (21 000 q/q).

Employment for all age groups (except those aged 35 to 44) remains below pre-crisis level, although young people aged 15 – 24 years continue to be worst affected (360 000 or 20% below 2008 levels).

A broad range of measures is needed if we are to make progress in expanding employment and alleviating the special problem of youth unemployment. These include measures aimed at stronger investment and growth through our infrastructure build programme and economic support package, and addressing skills constraints in the economy through measures to improve access to and the quality of basic, further and higher education. Tailored employment policies including the Community Work Programme, environmental sector public work programmes and the National Rural Youth Service Corps received additional allocations in February's budget and will help boost youth and overall employment in the short-term.

There have been a number of concerns raised with the proposed youth employment incentive. Discussions with social partners are aimed at mitigating these concerns. The rules, design and monitoring of a youth employment incentive need to ensure that it does not have negative unintended consequences, including potential displacement. We would like to see these issues addressed fully in discussion between social partners at NEDLAC, but with urgency as the challenge of creating jobs for young people cannot be indefinitely deferred.

Expenditure reviews

In supporting the work of the Ministers' Committee on the Budget, several programmes and reform initiatives of government will come under review to establish their value for money, effectiveness and impact. These include:

- Public service remuneration trends
- School education expenditure and the reasons for breakdowns in support activities such as text book delivery and school building maintenance
- Costing and financing of National Health Insurance
- Options for improvement in the Human Settlement Development Grant programme and introduction of the Mortgage Indemnity Scheme
- Water sector expenditure and pricing, and the Acid Mine Drainage problem
- Agriculture and rural development programmes and support for emerging farmers
- Implications of the Defence Review
- Budgeting and financing of major infrastructure capital projects.

Our support for provincial budgeting and expenditure control has already brought excellent results in both better budgeting and more effective financial management, and will continue this year. Part of the effort is targeted at rooting out corruption and fraud, but we have also found that lapses in financial management often result from weak systems and inadequate training of officials. The necessary reforms need to be undertaken more systematically, and will be the focus of the work of the Budget Council this year.

I am pleased to be able to report on the outcome of our interventions in Limpopo since December 2011, Mister Speaker. The provincial finances are under control and the cash position has improved with a positive year-end balance due to cash management controls that have been put in place since the start of the intervention. Whilst the cash position has improved and payment and procurement systems in departments have stabilised, further work still need to be done. The departments under administration are developing recovery programmes which will form an integral part of a comprehensive plan for implementation in the short, medium to long term period. A credible 2012 provincial budget has been tabled to deal with the accumulated debts and unauthorized expenditure. The law enforcement processes and other forensic investigations are under way in ensuring that any wrong doing is identified and necessary action taken against individuals involved. In sum, there has been good progress, but there is more to be done.

Allow me to comment also on the steps Cabinet has agreed to in respect of the financing of the Gauteng Freeway Improvement Project. Major improvements have been effected to Gauteng freeways under this programme, which have brought about substantial improvements in the flow of traffic and benefits to road-users. This investment has been made not out of general revenue, but through debt which has to be repaid. Cabinet has reiterated its commitment to the e-toll system as an efficient and appropriate mechanism of partial cost recovery from road-users. However, we are also mindful that more rapid progress needs to be made in improving complementary and alternative roads in the Gauteng region and elsewhere, and in extending and improving public transport services. It is clearly unhelpful, if we are to make progress in these challenges, that an important source of revenue for the road system has been delayed.

Financial regulation, savings and retirement reform

Mister Speaker, our financial sector proved exceptionally resilient during the global financial crisis. However, we should not be complacent, especially since the crisis continues, as we see in Europe, where Spanish and Greek banks face great challenges. In the 2011 Budget Speech, I announced a range of reforms to further strengthen our regulatory system, and to announce our intention to shift towards a twin-peaks approach to financial sector regulation.

The twin peaks approach emphasises two things: firstly, it establishes a prudential regulator in the Reserve Bank to supervise and monitor the health and soundness of financial institutions, and importantly also transforms the Financial Services Board into a dedicated market conduct regulator. In particular, this regulator will focus on improving transparency and disclosure, in the financial sector, particularly given opaque and high costs.

Overall, the new approach also gives the Reserve Bank the requisite powers to monitor and respond to systemic risks, wherever they arise.

National Treasury has been working with the Reserve Bank and Financial Services Board to give effect to these reform proposals. It is my hope that the policy proposals will be finalised this year for consultations with all the key stakeholders and that the legislation to establish the twin peak regulators will be tabled next year. I should point out that in the meanwhile, steps have already been taken, like introducing stricter capital requirements, and setting up the necessary forums like the Financial Stability Oversight Council, to monitor financial stability overall. Further, we will already be tabling four pieces of legislation this year, including the, the Financial

Markets Bill, Credit Rating Services Bill, Banks Act Amendment Bill and the Financial Services Laws General Amendment Bill. These bills give effect to our G-20 commitments on the regulation of derivative markets, and strengthens the fight again market abuse and manipulation.

In my 2012 Budget Speech, I reiterated the importance of household savings and ensuring that South Africans retire comfortably. I indicated that we need to urgently look into ways to improve preservation of existing retirement savings, and ensuring that fees do not deter people from saving. Fees across the financial industry and on certain financial products, like annuities, remain a source of major concern.

On Monday we published an overview paper on proposed urgent retirement reforms entitled, *"Strengthening Retirement Savings: An Overview of Proposals Announced in the 2012 Budget"*. This paper will be followed by a series of detailed discussion or policy proposal papers on the importance of preservation, reforming the annuities market and cost structures, introducing tax-preferred individual savings and investment accounts, and lastly, harmonising the tax treatment of retirement contributions. These detailed papers are expected to be released by October 2012.

Engagements with unions, industry and employers will continue and precede any final decisions on these key proposals. I should stress that the reforms proposed will not interfere with existing rights. All South Africans must become more conscious of the need to save for retirement nad ensure that unless absolutely necessary these savings must not be used for any other purpose. We must increasingly become a nation of savers not just consumers!

Supply chain management reforms

Mister Speaker, in the February budget speech I announced several steps to improve our oversight and regulation of procurement and supply chain processes.

We have commenced with the institutional reforms within the National Treasury to reduce fragmentation of these responsibilities. This will lay the foundation for the creation of a Chief Procurement Officer and supporting capacity, with overall responsibility for monitoring procurement across government.

A comprehensive review of the treasury regulations is nearing completion. This will mean a complete review of Chapter 6 of the PFMA regulations and the issuing of further instruction notes to close the loopholes in the supply chain processes as identified by the Multi-Agency Work Group.

The Treasury has provided support to the Minister of Public Works both for his review of the structure and functioning of his Department, and for the joint review of government property leases that is in progress. These reforms will not only lead to better management of government's accommodation and property responsibilities, but will in due course contribute to increased investment and better maintenance of physical assets under the stewardship of the state.

The Development Bank of Southern Africa

Mister Speaker, I am pleased to report that the Corporate Plan of the Development Bank of Southern Africa, recently tabled in the House, outlines an extended development drive with a sharp focus on supporting implementation of national and regional infrastructure investment plans. The Bank has established firm partnerships with several national departments and continues to strengthen its role in provincial and municipal infrastructure development. Its activities include financial and non-financial support. Priority areas include support for renewable energy projects; Industrial Development Zones (IDZs) and special economic zone infrastructure; partnership with state-owned enterprises and municipal infrastructure investment. The DBSA will continue playing a funding and supportive role in reducing backlogs in basic services delivery in respect of water, sanitation, electricity, training of municipal officials and operational maintenance.

The Bank aims to disburse R9 billion in 2012/13, rising to R15.8 billion in 2014/15. We recognize the need to extend the capital base of the DBSA over the next five years, in support of its enhanced infrastructure financing programme. The DBSA's callable capital has been increased from R4.5 billion to R20 billion.

The DBSA's activities will also include an expanded international role. The International Division of the Bank already provides a range of financial and non-financial services to public and private sector clients in the region. It also plays a leadership role in regional development strategies and initiatives. The funding of the International Division for its regional operations is limited to 33% of the DBSA's risk capital and investments are targeted at Southern Africa Development Community (SADC) countries.

The DBSA plans to expand its role to the rest of Africa and deepen its partnership with other institutions involved in its mission to enhance and deepen development of the African continent. The DBSA will place strong emphasis on reconstruction and low-income countries with viable projects where the development impact can be particularly high, given the context and opportunities.

The Land and Agricultural Bank of South Africa (Land Bank)

Following a successful turnaround, the Land Bank has turned into entity of distinction that is properly aligned to deliver on its legislated mandate. The collaboration between the National Treasury, the Department of Agriculture, Forestry and Fisheries and the Department of Rural Development and Land Reform has led to a constructive alignment of roles and responsibilities, which has enabled the Land Bank to expand its development lending activities. Corporate governance has become more robust with the necessary controls in place. The business is demonstrating healthy growth signs and the Bank is reclaiming its space in the South African agricultural landscape. To give effect to the future sustainability of the business, the Land Bank has implemented a program called Fit for Future (FFF). The roll out of FFF has resulted in a number of initiatives that are intended to ensure that the Land Bank improves the levels of service to its clients.

We are happy to see the Land Bank helping to grow the economy while creating work opportunities in agriculture and contributing to food security. The Land Bank has increased its market share from 25 per cent in 2010 to 32 per cent this year. This year, the Land Bank was able to grow its performing loan book by 50 per cent - an increase of R7.5 billion. During the same period, non-performing loans were reduced from 11 per cent to 6.5 per cent. In partnership with the DBSA, a monitoring system for assessing the economic impact of Land Bank lending activities has been developed.

The banking division servicing emerging small-scale farmer, called Retail Emerging Markets (REM), is already operational. Through this programme, the Land Bank contributes to growth and viability of emerging farmers and their graduation to the commercial farming level. Notwithstanding its fairly recent establishment, the division has surpassed its target of R100 million and disbursed R109 million in the last financial year. Expansion of the emerging farmer portfolio will remain a central priority of the Land Bank. Ambitious goals have been set including increasing the development portion of the total loan book by R5bn in 2016. This is informed by the current growth rate of the development book which has achieved disbursements of R850 million against a target of R450 million.

In addition, the Bank introduced an Emerging Farmer Support Facility and a Wholesale Finance Facility (WFF) which have seen development farmers benefiting from more affordable rates and broader assistance. Under the WFF, the Land Bank and DAFF have agreed on an interest subsidy scheme, thereby capping the interest rate that emerging farmers are charged by the intermediaries. The intermediaries (commercial farmers and agribusinesses) provide the farmers with support in the form of skills, production support and arranging off-take agreements.

As the bank reaches another big milestone in 2012 – turning 100 years old – it has outlined its 5-year plan, captured in its 2016 Corporate Landscape. The high level targets the Land Bank has set itself are a reflection of forward looking institution with a clear vision. The Land Bank aims to disburse R5 billion in expanding its development loan book by 2016, and to raise its market share to 35 per cent, thus contributing to job creation of over 300 000 mainly in disadvantaged rural areas.

Mr Speaker, I repeat these are dangerous times. We have formidable challenges ahead arising from both the dismal situation in Europe and our own structure of economy and society. This is not the time for expedient politics and shortsighted actions. It is not the time for opportunism and emotive and ill-considered utterances. Let us become problem solvers not problem creators!

If we really want to serve our people, if we are really serious about employment creation and poverty eradication, then we must all demostrate a new kind of leadership that creates hope and confidence in and about our country. Even with our differences we must display the generosity and magnanimity that will genuinely promote consensus building and the national interest.