MINISTRY OF FINANCE
REPUBLIC OF SOUTH AFRICA

National Treasury-World Bank Workshop on Fiscal Policy and Inequality

5 November 2014, Manhattan Hotel Pretoria

Remarks by Mr Mcebisi Jonas, Deputy Minister of Finance

Good morning Ladies and Gentleman. Let me thank you all for your attendance here today.

Let me begin by acknowledging our partners in this undertaking, The World Bank. Mr. Alam and team, your work is playing an increasingly valuable role in helping us to fashion policy for a better, more equal society. I trust that the discussion today will produce new insights into our continuing efforts to resolve the triple challenges of unemployment, inequality and poverty.

Let me also welcome the representatives of civil society, organised labour, government, academia, NEDLAC, the IMF, the Fiscal and Financial Commission, the media and members of the general populace. Your presence today emphasises the wealth of knowledge that we as a country can draw upon to address these issues, as well as the depth of commitment we all have to engaging with the problem of high inequality.

We meet today against a backdrop of economic uncertainty, we face structural domestic constraints to growth and the outlook for global growth remains gloomy. Many of our trading partners in the emerging markets are turning inward as they address their own structural challenges, and also face the prospect of a period of weak growth. Lower-than-expected-GDP growth and consequent lower-than-expected-tax-revenues over the next few years have led us to shave our planned total government expenditure budgets.

It is an environment that makes it all the more difficult for us to address the triple challenges.

It was with this backdrop in mind that the Minister of Finance unveiled a Medium Term Budget Policy Statement (MTBPS) that had three strategic priorities namely stabilising public finances, growing our productive economy and increasing the real value of the social wage so that over the long-term we are solving the core problems we face as a society:

- Ensuring that we leave future generations a fair debt burden with a matching portfolio of social assets.

- Guaranteeing that our state owned corporations operate sustainably and advance our development goals.

- Making certain that our core policy commitments, especially to the most vulnerable members of society, are protected in the face of swings in the business cycle

This was an MTBPS grounded in our current realities, but with an eye on the future. Though special focus is given to the deficit and debt, low deficits and debts are of themselves not the end goal, we are clear, our aim is to achieve radical economic transformation. However, we recognise that a radical economic transformation must also be a sustainable economic transformation. We recognise that the current environment makes achieving our social objectives more difficult, and so we must make hard choices to achieve them. Put plainly the message of this MTBPS is that the total government spending ceilings are firm and cannot be breached. To do otherwise would be reckless and would compromise implementation of the National Development Plan.

The measures to reduce the budget deficit and stabilise public debt will allow us to ensure the sustainability of the most important public spending programmes. They are measures that complement reforms under way to encourage lower consumption, higher savings and productive investment. These measures will re-establish a sustainable foundation for public finances and open the way for investment-led growth.

The NDP calls for private and public sector investment reaching 30 per cent of GDP. Over the past 5 years, investment has risen to nearly 20 per cent of GDP, supported by a doubling of public sector spending on infrastructure. Yet two challenges remain:

- The first, is to increase saving by reducing consumption and boosting growth. The fiscal package proposed will, over the medium-term, work to reduce government consumption and increase saving. The package will further create fiscal space for countercyclical support to the economy over the long-term and work to decrease debt service costs so that those resources can instead be used to build economic infrastructure and expand the social security net.

- The second is to promote greater private-sector investment in the economy. In a mixed economy, vibrant markets and private investment complement public action to improve people’s lives and sustain progress. Removing obstacles to private investment must be a priority for government at all levels.

Our aim is to create fiscal space with the measures we have undertaken and transition our economy towards an investment led growth path. Public investment can complement private investment if it is well designed and targeted, it can ignite more private investment rather than crowding it out.

An example is good transport and broadband infrastructure which can benefit the business sector as well. The focus of government should not be on glamorous investments or “white elephants” which result in little or questionable value. Investments should be judged on the basis of their overall economic impact with proper procedures put in place to avoid public funds from being wasted.

In this context, we also need more entrepreneurs to take risks and be more innovative. Since there is a high degree of risk aversion in the private sector it is imperative that public investment should be stepped up to share the risks with private players. This is also important if we are to overcome any further stagnation of our economy.

A lower rate of government consumption implies that government will contribute to the effort of closing the deficit on the current account and reduce the external imbalance.

These choices will be more beneficial to the South African economy than the business-as-usual path of high deficits by:

- Lowering the cost of capital across the entire economy
- Reducing production costs to depreciate the real exchange rate and make our exports competitive in the global market place
- Opening fiscal space to address the structural bottlenecks to production

As the Minister said in his speech “The MTSF will guide our budgeting decisions in making the NDP a reality.” This reality is not easily achieved; it requires that we make short-term sacrifices in order to place the economy on a sustainable high-growth trajectory. By making these choices now, we are giving the state sufficient dynamism to respond to risks and changes in the domestic and global macro environment while implementing its agenda without compromising the sustainability of public finances.

Consolidation is an essential first step if we are serious about building the South Africa envisioned in the NDP, a South Africa which is inclusive, guarantees the economic wellbeing of all South Africans and continues to lead on the continent and globally.

The current MTBPS does not mean abandoning counter-cyclicality; it remains one of the cornerstones of our fiscal policy, along with debt sustainability and intergenerational fairness. The MTBPS recognises the current economic picture, a picture that makes it clear that we cannot address structural constraints to growth with countercyclical measures. As the Minister put it in his speech, "The difficult decisions to narrow the deficit and restore fiscal sustainability can no longer be deferred. It is clear; the fiscus has reached a turning point."

As we continue our counter-cyclical fiscal stance to mitigate the impact of the weak global economy, we must simultaneously control the amount of government borrowing. Failing to do so is likely to result in South African sovereign debt being viewed as increasingly risky. This will, in turn, increase the cost of borrowing, and undermine the other cornerstones of our fiscal policy. Our investment-led growth strategy would be seriously compromised.

Having said this, we are pleased to note, Ladies and Gentleman that we have been able to craft the MTBPS in such a way that the fiscal deficit and national debt are stabilised, while at the same time the real value of allocations to health, education and social grants over the medium term are protected. The MTBPS further supports the continuing growth in real terms allocations for employment programmes, post-school training, housing and social infrastructure.

If we are to address poverty and inequality, it will also require that we accept some "hard-truths". The first being that, poverty and inequality cannot be solved merely through fiscal intervention. For example, while social spending has more than doubled in real terms over the past decade to around 60 per cent of non-interest expenditure, and social grants provide a safety net for more than 16 million most vulnerable people, the inequality has not shrunk to the extent we would have loved it to. Despite doing so much as a government, the number of poor South Africans remains heartbreakingly high.

We must therefore acknowledge a second truth; the constraints to growth and unemployment are in fact structural not cyclical. The issues that have constrained our growth thus far such as prolonged work stoppages and constrained electricity supply are not issues that can be addressed overnight or through running wide deficits.

Alleviating these constraints will require a two-pronged approach: On one hand we must focus on microeconomic reforms, and on the other, we need to pursue economy-wide massive job-creation. Simply put, the economy must grow at a significant pace and in a manner that creates jobs that absorb semi-skilled and unskilled people.

As government, we recognise that higher growth is fundamental to solving our problems as a society. We also recognise that that we cannot stand on the side-lines and wait for these changes to take place. We must support these changes by complementing them with the necessary structural reforms particularly enhancing dispute-resolution mechanisms in industrial relations, continuously improving the quality of our basic education system, and by increasing the supply of appropriately skilled workers. Alignment of these efforts to interventions that support the recovery of industrial sectors with high labour absorption capacity is vital.

The NDP, the MTSF and most recently the MTBPS do precisely that. The NDP outlines the vision of where we are headed as a society, the MTSF outlines the steps we must take as a society and the MTBPS identifies the tools and resources required to begin this journey.

This matters because if current trends continue then millions of young people will never experience the freedom and liberation that comes with having a stable job, thousands of households will not know what it is like to not worry where their next meal is coming from and far too many of our elderly will enter their twilight years not with a deserved sense of achievement, but instead feelings of anxiety.

Therefore, allow me to end by articulating my hopes for this conference:

- First, that we broaden the debate on inequality and influence the research agenda on this topic
- Second, that we develop cross-country benchmarks to track our performance relative to our peers
- Third, inform government's fiscal choices as it implements the National Development Plan
- Fourth, set a new tone for this debate, anchored in facts and data and not emotion. It is an opportunity to influence government's policy agenda as we work towards achieving our NDP outcomes.

I look forward to your report-back and I thank you for this opportunity.