

# 5

## Public spending priorities and budget policy

- Accelerating economic growth, broadening access to services and improving community infrastructure are the core priorities of the medium-term expenditure framework (MTEF).
- Public spending will continue to expand strongly over the next three years. About R81 billion is proposed to be added to government expenditure over the period, bringing spending growth to 6.4 per cent a year in real terms. While providing for steady improvements in public services, the budget framework recognises that the present macroeconomic context calls for some moderation in government expenditure. The emphasis is therefore on investment that supports growth and employment creation, and strengthening critical social and human development programmes.
- Budget priorities include further investments in infrastructure, with emphasis on broadening access to basic household services, public transport, education, health, labour-intensive employment initiatives, industrial policy initiatives that raise productivity and employment, fighting crime and improving service delivery.
- In keeping with the government-wide challenge of improving service delivery within affordable spending limits, national and provincial departments and public entities will be expected to include specific efficiency improvements and cost-saving initiatives in their strategic plans for the 2008 Budget and beyond.

### ■ Improved service delivery and the MTEF

The 2008 budget framework aims to give greater impetus to the Accelerated and Shared Growth Initiative (AsgiSA) and the priorities set in government's Programme of Action. Transforming public

*Giving greater impetus to  
AsgiSA*

service delivery in keeping with the country's reconstruction and development challenges remains the central organising principle of public expenditure planning.

*Public spending needs to support long-term economic performance*

Over the next three years, government's spending plans will focus on investment in human resources and physical infrastructure, geared towards sustainable long-term social and economic development.

There has been marked progress in meeting service delivery targets and broadening social development since the advent of democracy 13 years ago.

*Across a wide range of social measures, government is making demonstrable progress*

The Community Survey released by Statistics South Africa in October 2007 records the advances made in several areas, while signalling also the scope of the challenges ahead. The proportion of South Africans living in informal settlements has declined from 16 per cent to 14.5 per cent since 1996. The number of households with access to electricity, sanitation and water has increased significantly. The proportion of South Africans who indicate that they have not been to school continues to decline. The proportion of people who have completed tertiary education rose from 7.1 per cent in 1996 to 9.1 per cent in 2006.

*Employment trends continue to improve, but youth unemployment remains too high*

The latest Labour Force Survey shows a continuing improvement in the employment trend, although youth unemployment in particular remains too high. Strong economic growth has enabled the fiscus to expand social security transfers to vulnerable households and to accelerate investment in services and infrastructure.

A central aim of government's policy framework is to broaden participation in a more rapidly growing economy, while progressively extending and improving public service delivery. The 2008 Budget will accelerate investment in both people and infrastructure, and strengthen capacity across national, provincial and local government.

Accountability in service delivery, however, continues to be a weakness in certain areas of the public sector. A government-wide monitoring and evaluation framework has been introduced under the auspices of the Presidency, strengthening oversight of the delivery of key policy outcomes. The National Treasury's guidelines for performance information aim to develop better measures of value for money in government expenditure, in alignment with the monitoring and evaluation framework.

*A focus on controlling costs and better value for money in government departments*

Recognising that sustained improvements in service delivery depend on efficient use of resources, the 2008 Budget will also put the spotlight on controlling costs. Government departments and public entities will be expected to include explicit efficiency savings and cost-containment initiatives in their strategic plans. Targeted expenditure includes unnecessary travel and subsistence costs, entertainment, poorly managed consultancy services, outdated administrative systems, misplaced marketing and communication initiatives, and weaknesses in supply-chain management. Through efficiency savings measures, R2.3 billion will be redirected to new and expanded frontline services over the next three years.

This chapter sets out broad proposals for the 2008 MTEF, within which departmental and programme allocations have to be determined during the remaining months of the budget process. It outlines some of the policy considerations and implementation challenges ahead and also discusses specific changes to the 2007/08 budget estimates. As always, the budget process confronts a wide range of pressing claims on public resources, not all of which can be accommodated given the resources available. Further details on the division of revenue and major changes to provincial and local government allocations are discussed in Chapter 6.

## ■ Revised expenditure estimates for 2007/08

This year government tabled a special adjustments appropriation in September. The normal adjustments bill is published alongside this statement. The Adjusted Estimates of National Expenditure sets out detailed changes to the 2007/08 allocations proposed in both adjustments appropriation bills.

*A special adjustments budget tabled in September 2007*

The special adjustments appropriation of R5.2 billion provides for:

- R1.9 billion brought forward from the 2008/09 estimate to accommodate accelerated spending on stadium construction
- A R222 million transfer to Denel to meet a guarantee claim relating to its Airbus supply commitments
- Recapitalisation of R700 million to the Land Bank
- R1.8 billion for the Pebble Bed Modular Reactor project
- R500 million to contribute to Sentech's wholesale wireless broadband network
- R44.7 million to support the Alexkor diamond mining company.

The main adjustments appropriation bill for 2007/08 proposes the following changes:

*Changes proposed to normal adjustments appropriation bill*

- R654 million for unforeseen and unavoidable expenditure associated with fire, floods, drought and other adverse weather conditions
- R400 million for treatment and prevention of multidrug-resistant tuberculosis
- R300 million for bus subsidies
- Approved rollovers of R4.0 billion arising from unspent balances in 2006/07
- R181 million of self-financed expenditure
- R1.9 billion to accommodate the higher-than-budgeted cost of the 2007 salary agreement
- Supplementary allocations of R707 million.

Taking into account projected underspending, declared savings and the adjusted state debt cost estimate, the revised estimate of total expenditure from the National Revenue Fund in 2007/08 is R542.4 billion, or 15.4 per cent more than 2006/07 expenditure. A summary of mid-year spending estimates for 2007/08 for both national departments and provinces is included in Annexure A.

*Revised estimate for National Revenue Fund expenditure is R542.4 billion*

## ■ Medium-term budget policy

*Budget priorities for the next three years*

Spending priorities are informed by government's Programme of Action, which in turn reflects the annually updated medium-term strategic framework overseen by the Policy Coordination and Advisory Service in the Presidency. In reviewing plans for the next three years, attention has focused on identified priority programmes associated with AsgiSA, the Joint Initiative for Priority Skills Acquisition (Jipsa) and requirements for a successful 2010 FIFA World Cup. Continuing cross-cutting priorities include:

- Investing in both economic and social infrastructure so that the economy can grow faster, and access to basic social and household services can be assured.
- Improving the quality of education, health and other social services, and stepping up targeted anti-poverty initiatives.
- Enhancing job creation associated with growth by supporting labour-absorbing industries and active labour market initiatives, and expanding employment-intensive government programmes.
- Improving the efficacy of police services and the justice system to make further progress in reducing crime.
- Enhancing the effectiveness of economic and sectoral interventions through appropriate regulation of and support for business to expand the productive side of the economy, and through regional and international partnerships.

*An additional R81.4 billion to be added to the R1.7 trillion baseline*

The proposed framework for the 2008 Budget makes available an additional R81.4 billion over the next three years, in addition to more than R1.7 trillion already included in departmental and provincial baseline allocations. About R50 billion of the available additional funds will go to municipalities and provincial governments.

The 2007 public service salary settlement results in additional personnel costs over the next three years, for which R15 billion is included in the additions to baseline allocations of national departments and provinces.

*Inflation-related increases protect value of social grants*

Inflation-related adjustments to the value of social grants are also provided for, and are expected to take up R4.3 billion of the available additional funding over the MTEF.

Medium-term budget priorities and key policy considerations relating to public spending are summarised below.

### Investing in infrastructure

*Public infrastructure investment has risen strongly for three years*

Since 2004, public infrastructure investment has risen strongly. Some of these investments are financed from resources allocated through the budget process; others are financed directly by state-owned enterprises through their own revenue or financing sources. These include the sale of non-core assets, retained earnings, borrowing from capital markets and public-private partnerships.

Table 5.1 shows projected consolidated national and provincial government expenditure by type of service.

**Table 5.1 Consolidated government expenditure by type of service, 2006/07 – 2010/11**

	2006/07	2007/08	2008/09	2009/10	2010/11	Average annual growth 2007/08 – 2010/11
R billion	Outcome	Revised	Medium-term estimates			
<b>Social services</b>	<b>270.7</b>	<b>305.4</b>	<b>347.7</b>	<b>388.8</b>	<b>424.1</b>	<b>11.6%</b>
Education	92.3	106.4	120.8	135.6	148.6	11.8%
Health	57.3	63.1	71.0	79.5	87.3	11.4%
Welfare and social security	84.1	89.0	100.5	110.7	117.5	9.7%
Housing and community development	37.1	47.0	55.4	63.0	70.7	14.6%
<b>Protection services</b>	<b>78.9</b>	<b>89.2</b>	<b>96.8</b>	<b>105.0</b>	<b>114.2</b>	<b>8.6%</b>
Defence and intelligence	27.8	30.6	32.5	33.6	36.1	5.6%
Justice, police and prisons	51.1	58.6	64.3	71.4	78.1	10.1%
<b>Economic services and infrastructure</b>	<b>89.6</b>	<b>114.4</b>	<b>127.6</b>	<b>142.0</b>	<b>159.6</b>	<b>11.7%</b>
Water and related services	15.0	17.4	18.3	20.6	22.2	8.5%
Agriculture, forestry and fishing	10.7	13.2	14.1	14.6	15.4	5.3%
Transport and communication	34.7	46.1	57.4	64.9	76.3	18.3%
Other economic services	29.2	37.7	37.8	41.9	45.7	6.6%
<b>Administration</b>	<b>33.6</b>	<b>39.6</b>	<b>41.2</b>	<b>47.3</b>	<b>50.6</b>	<b>8.5%</b>
<b>Total</b>	<b>472.8</b>	<b>548.7</b>	<b>613.3</b>	<b>683.0</b>	<b>748.5</b>	<b>10.9%</b>
Interest	55.3	56.1	55.4	56.0	55.6	-0.3%
Contingency reserve	–	–	4.0	8.0	16.0	
<b>Consolidated expenditure</b>	<b>528.1</b>	<b>604.8</b>	<b>672.7</b>	<b>747.0</b>	<b>820.1</b>	<b>10.7%</b>

General government investment is mainly focused on the built environment, which covers housing, water, sanitation, electrification, schools, health facilities, police stations, roads and public transport investment – investments designed to create sustainable and viable communities. This category of public spending has been the single fastest-growing area of government expenditure, rising by 19.2 per cent a year in real terms since 2004.

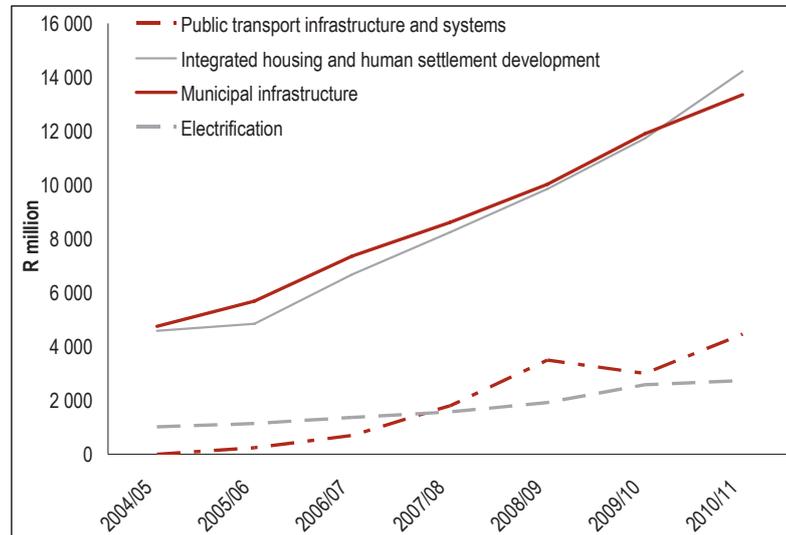
Government investment in the built environment is aimed at achieving universal household access to water, sanitation and electricity, and the elimination of informal settlements. These are ambitious targets, and substantial additional allocations are proposed for local and provincial government to expand the pace of delivery, and to contribute to the costs of providing free basic services at local level.

*Government targets  
universal access to water,  
sanitation and electricity*

Economic growth, improved revenue performance and the fiscal space created by sound policies make possible continued strong growth in physical capital formation. Progress in industrial and trade policies and performance are necessary complements to these investments. South Africa's plans for power plants, rail lines, bus lanes and routes, dams, water purification plants, roads, ports and office accommodation are likely to see public sector gross fixed capital formation grow rapidly for well over a decade.

Figure 5.1 below shows the strong investment growth trends in the principal built environment spending streams.

**Figure 5.1 Built environment grants and subsidies, 2004/05 – 2010/11**



Two critical social sector infrastructure programmes – the hospital revitalisation grant and the school building programme – will be significantly boosted over the period ahead to contribute to improving health services and eliminating unsatisfactory school environments.

*A temporary operating grant to help host cities prepare for 2010*

Considerable infrastructure spending related to the 2010 FIFA World Cup is in progress. Stadium construction projects are on track or ahead of schedule. A World Cup host city operating grant is proposed for the 2008 Budget to help municipalities commission new stadiums, prepare training facilities, improve signage and develop fan parks.

Public transport infrastructure and systems related to the World Cup have been prioritised for the 2007-2010 period. Planning is under way for several public transport projects beyond 2010, mainly to link residential areas with places of economic activity.

Proposed public transport allocations over the MTEF will help to develop core economic infrastructure for the long term, and build up an integrated bus, rail and taxi system.

*Capital markets fund the bulk of state-owned enterprises' infrastructure projects*

In recent years financial assistance has been provided to state-owned enterprises – including South African Airways, Denel, Sentech, the Pebble Bed Modular Reactor and Infracore – to support their role in underpinning economic growth. Although the bulk of capital required by state-owned enterprises is sourced from debt markets and from own revenue sources, restructuring initiatives and further investment in transport and communications infrastructure will continue to be supported by the fiscus.

## Improving the quality of public services

In many areas, progress in improving public services has failed to keep pace with increased financial resources. The 2008 Budget will prioritise public services in under-served areas that improve the likelihood of success of other programmes. For example:

- In education, improved early learning opportunities increase success rates in later years, and collective purchasing of textbooks can reduce costs and allow for greater access to appropriate learning materials.
- Improved traffic enforcement and removing unroadworthy vehicles leads to fewer road accidents, alleviating pressure on the health and emergency services.
- Better agricultural extension services and post-settlement support to new farmers increases the likelihood that the land reform programme will meet its objectives. Further support for land restitution is envisaged, along with a step-up in spending on provincial agricultural support programmes.

*Targeted interventions to improve the quality of services and reinforce other programmes*

Targeted allocations will support service delivery improvements in the Department of Home Affairs, and communication and IT network infrastructure in the criminal justice sector. Improved capacity in departments that fulfil an economic regulatory role is also prioritised.

*Support for departments with an economic regulatory role*

The 2007 Public Sector Coordinating Bargaining Council resolution announced occupation-specific salary dispensations for teachers, nurses and legally qualified personnel. A new dispensation for social workers is also envisaged. These grading systems provide differentiated pay based on performance, seniority and qualifications, and are aimed at raising productivity, and recruiting and retraining skilled personnel.

Through Jipsa, government intends to work with the private sector to identify skills gaps, refocus training initiatives and attract skills from abroad. The intention is also to place 2 000 young South Africans abroad to gain international work experience.

*Jipsa partners with private sector to strengthen skills training*

As part of strengthening the professionalism and technical competence of the civil service, the South African Management Development Institute will receive further support over the MTEF period.

### Turning around Home Affairs

The Department of Home Affairs turnaround programme includes various short-term interventions focused on improved service delivery. These include:

- A tracking system enabling South Africans to chart the progress of their ID document applications without having to queue at an office
- A streamlined ID production process that is fast, efficient, customer friendly and reliable
- Clearing backlogs and upgrading facilities, and improving the application process for refugee and immigrant permits
- A new call centre service and IT systems upgrades
- Financial improvements and addressing audit concerns, including the identification of risk areas.

## Supporting employment growth and poverty reduction

*Through expanded public works the budget supports direct job creation*

Raising the level of employment is a critical economic policy objective. Initiatives grouped under the expanded public works programme receive further support over the medium term. Over the past three years, more than 300 000 short-term work opportunities have been created through these programmes. While some initiatives have shown good results, such as those in the environmental sector, there has not been sufficient progress in increasing the labour intensity in other critical sectors.

Government seeks to raise the labour-intensity of municipal infrastructure projects. The 2008 Division of Revenue Bill will emphasise the degree to which government expects municipal and provincial government to use labour, where feasible, to deliver community infrastructure and services.

Employment creation is also an objective of industrial and trade reform, through initiatives supporting labour-intensive sectors such as business process outsourcing (including call centres), small-scale agriculture and small business support. A new incentive programme for small business, to be introduced by the Department of Trade and Industry, will also be supported over the period ahead.

*School nutrition programme to be expanded*

Social assistance grant programmes play an important role in reducing poverty and vulnerability. Social grants are increased annually to maintain their purchasing power, and provision must also be made for rising beneficiary numbers. Expanding the school nutrition programme to cover more children for the full school year will also be provided for in the 2008 Budget.

*Work in progress on social security proposals*

Following the announcement of proposed reforms to the architecture of social security and retirement funding, government is assessing the viability of a wage subsidy to underpin job creation and income security of the poor. Work is still in progress on this and related regulatory, tax and social security reform options, and as a result their fiscal and financial implications are not taken into account in the present framework.

## A more efficient criminal justice sector

*Support for improved police IT and communications infrastructure*

Crime levels remain unacceptably high, though progress has been made in stabilising and in some instances reducing incidence rates. This remains an area where public expectations are a long way from being met. Over the past five years, police personnel numbers and remuneration have grown. However, there has been underinvestment in improving IT systems and bringing forensic capability up to a level commensurate with the high level of contact crime. We also need more detective training. Over the MTEF period the budget for the police will prioritise improved IT and communications infrastructure, and forensic laboratories. Budgetary provision will also be made to secure both citizens and visitors during the 2010 FIFA World Cup.

Improving court efficiency and sharply reducing longstanding case backlogs are key priorities for the criminal justice system. The

assignment of more public defenders and two prosecutors to each court is continuing, and provision is made for the appointment of more judges and magistrates. Further allocations are required for the implementation of an electronic case flow management system in the National Prosecuting Authority.

Correctional Services is taking steps to emphasise rehabilitation, which should reduce repeat offences. This strategy requires more social workers, psychologists, training capacity and critically, less overcrowding. Five new prisons, to house 15 000 offenders, are to be procured through partnerships with private contractors.

*Support for reorientation of Correctional Services towards offender rehabilitation*

## Raising the productive capacity of the economy

This year government announced a National Industrial Policy Framework and the Industrial Policy Action Plan. The policy framework entails a closer partnership between government and the private sector to facilitate business expansion, diversify the economy and increase its ability to absorb labour. To sustain the current growth trajectory it is critical to raise the level of exports. The 2008 Budget will support targeted industrial policy, trade and sectoral strategy initiatives. Consultations between government and business on several sector support programmes are under way.

Research and development (R&D) encourages innovation, helping the economy to introduce and adapt to technological change, and raising productivity in the process. The next budget will continue to provide support to R&D through the statutory science councils, universities and partnerships with the private sector. Infrastructure investment, education, skills development and reduction of the bureaucratic burdens facing business are all essential to strengthening the economy. These measures provide generalised support to all businesses, levelling the playing field for higher productivity.

*Support for increased research and development*

## Higher education funding

Government funding for universities falls into three main categories. The main institutional subsidy is a formula-based block grant that takes into account student enrolment, graduate rates and research outputs. It is complemented by earmarked grants, such as allocations to expand engineering studies and foundation programmes for disadvantaged learners. A separate allocation is also made for each institution's share of the National Student Financial Aid Scheme, which provides loans and bursary funding to cover fees of students who would otherwise not be able to afford higher education.

Additional amounts proposed increase allocations to higher education from R13.3 billion in 2007/08 to R19.1 billion in 2010/11, an average annual growth of 11.5 per cent over the MTEF.

### Higher education funding, 2004/5 – 2010/11

	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Average annual growth
<b>R million</b>								
Institutional subsidy grants	8 798.5	9 190.3	10 260.6	11 344.2	13 309.7	14 667.0	16 133.7	10.6%
Restructuring Grants <sup>1</sup>	502.0	550.0	568.0	600.0	–	–	–	
NSFAS <sup>2</sup>	578.2	864.1	926.4	1 112.7	1 175.3	1 258.7	1 334.2	15.0%
<b>Sub-Total</b>	<b>9 878.7</b>	<b>10 604.4</b>	<b>11 755.0</b>	<b>13 056.8</b>	<b>14 485.0</b>	<b>15 925.7</b>	<b>17 467.9</b>	<b>10.0%</b>
Higher Education Programme <sup>3</sup>	9 911.4	10 646.8	11 967.6	13 330.9	15 068.2	16 830.9	19 066.4	11.5%

1. Included in Institutional subsidy grant from 2008/09.

2. Excludes teacher and FET College bursaries.

3. Includes departmental management costs and proposed additional allocations.

*Utility regulators and competition authorities likely to receive further support*

Competition policy can also serve as an instrument to raise productivity, since economic theory suggests that monopolies, either state or private, are likely to under-produce and overprice. Utility regulators and the competition authorities will be strengthened during the period ahead.

*Government moves to strengthen its diplomatic ties with Asia*

South Africa's foreign relations agenda, particularly initiatives aimed at regional peace and stability, have facilitated greater trade and investment opportunities with developing nations. Government will continue to support development initiatives in Africa, expand diplomatic capacity on the continent and simultaneously strengthen diplomatic ties with Asia, given improved trade and economic links with the East.

## ■ Consolidated government expenditure

An economic classification of projected government expenditure is set out in Table 5.2. These estimates indicate that the fastest-growing categories of spending are transfers to municipalities and investments in physical infrastructure.

**Table 5.2 Consolidated government expenditure by economic classification, 2006/07 – 2010/11**

	2006/07	2007/08	2008/09	2009/10	2010/11	Average annual growth 2007/08–2010/11
	Outcome	Revised	Medium-term estimates			
<b>R billion</b>						
<b>Current payments</b>	<b>316.3</b>	<b>351.5</b>	<b>386.0</b>	<b>426.6</b>	<b>460.8</b>	<b>9.5%</b>
Compensation of employees	169.7	191.9	215.7	237.1	257.8	10.3%
Goods and services	91.4	103.4	114.9	133.6	147.4	12.6%
Interest and rent on land	55.3	56.1	55.4	56.0	55.6	-0.3%
<i>of which: State debt cost</i>	52.2	52.9	51.2	51.0	50.4	-1.6%
<b>Transfers and subsidies</b>	<b>180.5</b>	<b>212.2</b>	<b>235.1</b>	<b>256.8</b>	<b>277.8</b>	<b>9.4%</b>
Municipalities	30.6	39.5	47.4	52.0	60.3	15.2%
Departmental agencies and accounts	22.0	24.5	24.8	25.2	27.3	3.7%
Universities and technikons	12.6	13.7	15.2	16.6	18.0	9.7%
Public corporations and private enterprises	19.6	26.1	23.6	27.4	27.9	2.3%
Foreign governments and international organisations	0.9	1.0	0.8	1.0	1.1	0.6%
Non-profit institutions	10.6	12.8	16.3	17.9	20.3	16.7%
Households	84.3	94.7	107.1	116.8	123.0	9.1%
<b>Payments for capital assets</b>	<b>31.2</b>	<b>41.2</b>	<b>47.6</b>	<b>55.6</b>	<b>65.5</b>	<b>16.7%</b>
Buildings and other capital assets	22.5	31.5	36.6	43.6	51.9	18.1%
Machinery and equipment	8.7	9.7	11.0	11.9	13.6	11.9%
<b>Total</b>	<b>528.1</b>	<b>604.8</b>	<b>668.7</b>	<b>739.0</b>	<b>804.1</b>	<b>10.0%</b>
Contingency reserve	–	–	4.0	8.0	16.0	
<b>Consolidated expenditure</b>	<b>528.1</b>	<b>604.8</b>	<b>672.7</b>	<b>747.0</b>	<b>820.1</b>	<b>10.7%</b>