4

Expenditure priorities

In brief

- Medium-term spending plans have been developed in the context of weak economic growth trends, limited budgetary resources and rising pressures on the fiscus.
- Over the three-year spending period ahead, consolidated expenditure will grow by an annual average of 7.3 per cent, from R1.6 trillion in 2017/18 to R1.9 trillion in 2020/21. The fastest-growing functions are Community Development, Learning and Culture, and Health. The fastest-growing category of expenditure is debt-service costs, which grows by 11 per cent.
- Government will protect spending on core social programmes that benefit poor South Africans. Funding for any new policy priorities will come mainly from reprioritisation.
- The division of non-interest expenditure between national, provincial and local government remains stable at 47.6 per cent, 43.2 per cent and 9.2 per cent respectively.

Introduction

In August 2017, Cabinet approved a Mandate Paper to guide the spending choices of national government. As in recent years, additional allocations over the medium-term expenditure framework (MTEF) period will be funded mainly through reprioritisation of existing budget baselines. Additional resources to support spending priorities will be severely limited by the economic outlook presented in Chapter 2 and the fiscal policy challenges set out in Chapter 3. Structural increases in expenditure to accommodate new policy initiatives, and resulting adjustments to the spending ceiling, will need to be matched by parallel tax increases.

Spending on new policy initiatives will require reprioritisation or matching tax increases

Over the three-year spending period ahead, consolidated expenditure will grow by an annual average of 7.3 per cent, from R1.6 trillion in 2017/18 to R1.9 trillion in 2020/21. The fastest-growing functions are Community Development, Learning and Culture (which includes post-school education and training) and Health, with growth rates of 7.9 per cent, 7.6 per cent and 7.5 per cent respectively. Debt-service costs as an expenditure category grows the fastest at 11 per cent.

Reductions in expenditure ceiling may be required to stabilise public finances

Further reductions in the expenditure ceiling may be required over the next three years to stabilise the public finances. A presidential task team will identify savings and programme closures to improve the efficiency and impact of expenditure. Details will be announced in the 2018 Budget.

Expenditure priorities and pressures

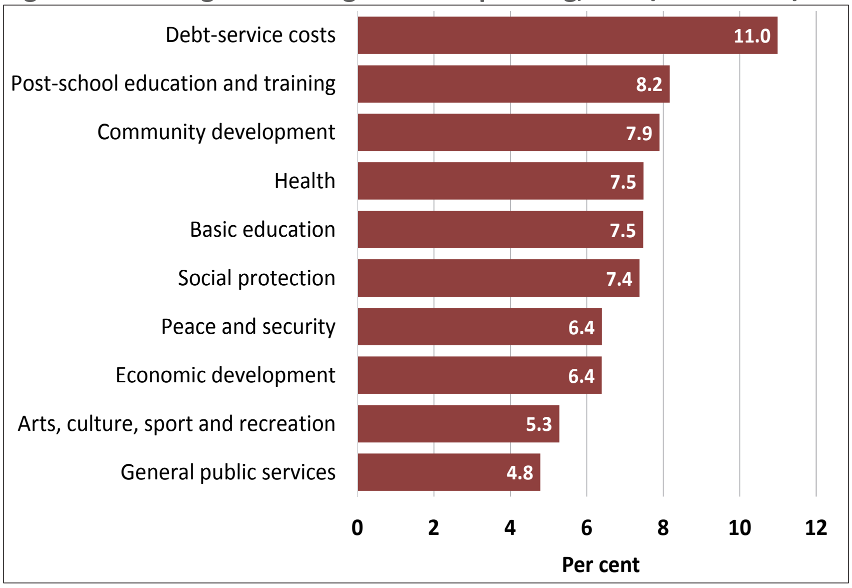
The Mandate Paper prepared by the Department of Planning, Monitoring and Evaluation serves as a Cabinet-endorsed mandate against which departments and public agencies should refine their plans and budget proposals. The purpose is to strengthen alignment of the national budget, the medium-term strategic framework and the National Development Plan (NDP), during the final 24 months of the current administration.

Mandate Paper notes that on current trends, South Africa is unlikely to meet its NDP goals

The paper observes that on current trends, South Africa is unlikely to achieve its NDP goals. It also notes that there will be no additional funds available to increase baseline expenditure over the 2018 Budget, and some programmes might have to be cut to meet unanticipated spending pressures. It establishes seven expenditure priorities and identifies focus areas that should be addressed in the 2018 Budget.

To support spending in these areas the Mandate Paper proposes to cut programmes that are not aligned to the NDP ("non-core"), or which are not realising their intended outcomes. It suggests that departments can realise savings by reducing spending on consultants; establishing strict limits on contingent liabilities and litigation costs; ensuring that the initiatives of the Office of the Chief Procurement Officer take effect; and improving returns and value for money on state infrastructure projects.

Figure 4.1 Average nominal growth in spending, 2017/18 — 2020/21



Source: National Treasury

Departmental submissions for the 2018 Budget complement the Mandate Paper priorities with several proposals that require large additional resource commitments. These include significant additional funding for the post-school education and training system, national health insurance (NHI), qualified teachers for Grade R, the implementation of the defence review, land restitution and large infrastructure projects.

Mandate Paper priorities for the 2018 Budget

Job creation and small business development	- Implement 30 per cent set-asides - Localisation - Integrated community development and community-based workers.
Youth development	- Business opportunities for youth including the internet - Capacitate youth enterprises, particularly in tourism and hospitality - Scale up labour-intensive programmes, learnerships and artisan training
Infrastructure spending	- Maintain real infrastructure spend - Revitalise township industrial parks and technology innovation hubs - Expand agri-parks programme - Rural roads, broadband and water infrastructure - Maintenance, especially at local level.
Land reform and agricultural development	- Fast-track restitution settlement and redistribution - Implement farmer support - Transform wildlife economy - Off-take agreements for small business and cooperatives
Comprehensive social protection, education and skills	- Implement national health insurance, and HIV/AIDS and tuberculosis plan - Expand early childhood development - Establish different pathways to work - Free education for the poor - Expand student accommodation
Integrated plan to fight crime	- Combat violence during protests - Integrated criminal justice system and national identification system - Fight corruption and economic crimes - Finalise border management
Regional integration and development	- Advance the national interest in the Southern African Development Community, throughout Africa, and through participation in BRICS (Brazil, Russia, India, China and South Africa) and the Indian Ocean Rim Association.

Pressure on the public finances

The public finances face growing strains and risks. Several years of fiscal restraint have left funding gaps in a number of programmes, reflected in the build-up of unpaid accounts and financial imbalances. Without resolute action and planning to cut wasteful and inefficient spending areas, there is a growing danger that the most vulnerable citizens will suffer the effects of fiscal consolidation.

Public-sector wage bill has increasingly crowded out other areas of spending

The public-sector wage bill has increasingly crowded out other areas of spending, including complementary inputs that public servants need to do their work. Infrastructure budgets that are poorly designed or not effectively delivered have resulted in high operating deficits, with insufficient allocations for maintenance. Many departments are delaying paying their bills – a trend that contributes to a rising hidden deficit. Provinces entered 2017/18 with R26.4 billion of unpaid bills from the prior year, and a number of municipalities are in financial distress.

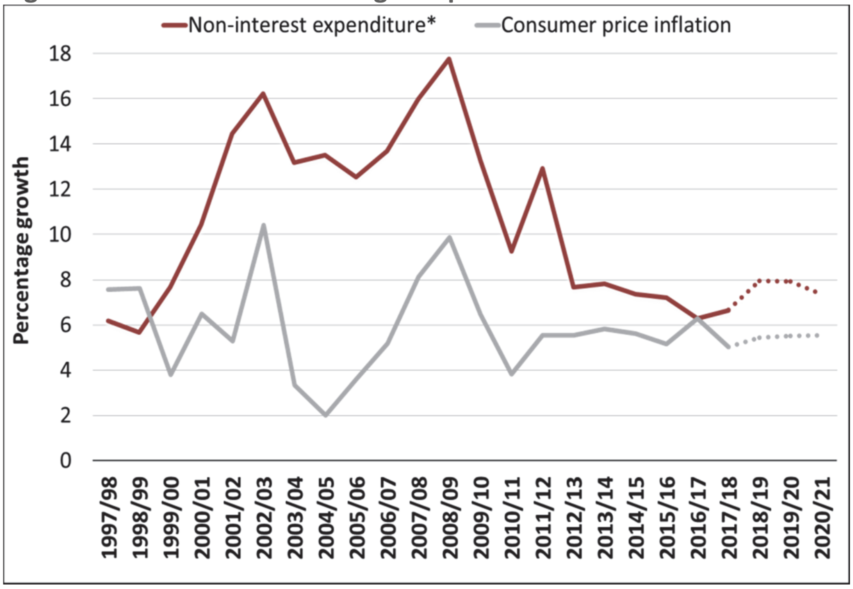
Determined action needs to balance competing demands and interests

This situation requires determined action that balances competing demands and interests. These trade-offs are particularly stark in the current round of public-service wage negotiations. Since 2011, government has been forced to restrict employee headcount growth to accommodate rising salaries. Yet spending on compensation has continued to grow more quickly than nominal GDP. A fair and reasonable compromise between government and state employees in the current round of wage talks is in the public interest.

The MTEF provides for an overall increase of 7.3 per cent a year to accommodate improvements in conditions of service. Many departments are already at risk of exceeding this limit, even assuming that personnel numbers do not increase. Moderation in public-service personnel costs is essential if improvements in service delivery are to be achieved.

Annexure B provides data on public-service employment and compensation trends.

Figure 4.2 Growth in main budget expenditure and consumer inflation



**Non-interest expenditure excluding payments for financial assets, skills development levy and fuel levy sharing with metros*
Source: National Treasury and Statistics South Africa

Commission of Inquiry into Higher Education and Training delivered its final report in August 2017

A second major cost pressure over the period ahead is higher education. The Commission of Inquiry into Higher Education and Training delivered its final report to the President in August 2017.

Higher education funding shortfalls

In 2016, the National Student Financial Aid Scheme (NSFAS) provided financial assistance to 225 950 university students whose family income was below R122 000 per year. This amounts to about 30 per cent of university undergraduates. In general, NSFAS loans and bursaries are only able to cover a portion of the full cost given the many students requesting aid. Tuition fees account for about 35 per cent of the full cost of study, which includes lodging, food and textbooks.

If NSFAS were to cover the full cost of study for the 30 per cent of undergraduates who currently qualify, the scheme would require about R10.7 billion in the 2018 academic year in addition to the R11.4 billion currently available. Proposals have been made to extend the provision of financial aid to students from middle-income households. Estimates of the number of students falling within this threshold are unreliable. Government is working with universities to verify the data.

The table below shows the additional funding that would be required to cover the full cost of study for various proportions of the undergraduate population. For example, extending funding to 40 per cent of undergraduates would create a shortfall of R17.7 billion in 2018, or R61.7 billion over the next three years.

Funding shortfalls on full cost of study for university students

Share of undergraduate students	2018	2019	2020	2021
	Shortfall (R million)			
30%	10 724	12 661	14 875	17 343
40%	17 691	20 432	23 550	27 035
50%	24 980	28 553	32 606	37 143
75%	40 728	46 060	52 083	58 827
NSFAS budget	**11 428**	**12 045**	**12 702**	**13 464**

There is also a large gap in funding for technical and vocational education and training (TVET) colleges. In 2016, NSFAS provided financial assistance to 225 557 TVET college students whose family income is below R122 000 per year – about 70 per cent of full-time equivalent students. Covering the full cost of study for all TVET students, while ensuring that adequate programme funding is available, would require an additional R7.1 billion next year in addition to the R10 billion already allocated, or R23.5 billion over the next three years.

Cost containment and improved value from procurement

Spending on goods and services by national and provincial departments increased by only 5.6 per cent between 2013/14 and 2016/17. Spending on core service delivery items like medicines, schoolbooks and fuel has continued to grow faster than inflation.

Table 4.1 Summary of expenditure on cost-containment related items: national and provinces

Cost-containment related expenditure items R million	2013/14 Audited outcome	2016/17 Preliminary outcome	2013/14 to 2016/17 Change in value	2013/14 to 2016/17 Average annual growth
Consultants	6 980	6 148	-832	-4.1%
Travel and subsistence	9 828	9 305	-523	-1.8%
Catering and events	908	815	-93	-3.6%
Entertainment	44	25	-19	-17.5%
Advertising	1 246	1 094	-152	-4.2%
Newspapers and publications	270	202	-68	-9.2%
Conferences (venues and facilities)	1 241	999	-242	-7.0%
Other expenditure (communication)	3 227	3 243	16	0.2%
Total	**23 744**	**21 831**	**-1 913**	**-2.8%**

Source: National Treasury

Since expenditure ceilings and cost-containment measures were introduced in 2012/13, spending on consultants, travel, lodging, catering, advertising and conferences has fallen sharply. There is now little room for departments to further curb such spending without negatively affecting service delivery.

Transversal contracts negotiated by government have begun to yield positive results. Under these agreements, a supplier procures goods and services for more than one department, provided that the contracts are cost-effective. Centralised tendering has resulted in a sharp reduction in antiretroviral drug prices, for example.

In-year adjustments to spending

Adjustments Appropriation Bill includes allocations for SAA and the South African Post Office

The Adjustments Appropriation Bill allows for revisions to the budget tabled in February, as prescribed in the Public Finance Management Act (PFMA) (1999). Major additions to spending include:

- Allocations for items that were not included in the February budget, but were announced in the budget speech. This includes R4.8 billion allocated to South African Airways (SAA), R3.7 billion to the South African Post Office and a R117 million transfer to the Tirisano Construction Fund Trust, which promotes development projects and black participation in the construction sector.
- R5.2 billion to defray expenditure authorised by the Minister of Finance in terms of section 16 of the PFMA to forestall a call on government-guaranteed debt by an SAA creditor.
- R1.5 billion in self-financing expenditure, the bulk of which is for the Department of Home Affairs passport programme.
- R586 million of expenditure deemed unavoidable, but which was "unforeseeable" when the 2017 Budget was tabled. Of this amount R500 million was allocated to the Department of Water and Sanitation to implement the Butterworth emergency water supply scheme and to upgrade the capacity of the Thukela Goedertrouw transfer scheme.

Proposals to reduce appropriations to national departments in anticipation of underspending

The adjustments budget also proposes to reduce appropriations to national departments by R1.67 billion in anticipation of underspending. In these cases, expenditure trends indicate that the resources will not be used by the end of the year.

Details of all the revised national spending allocations are set out in the 2017 *Adjusted Estimates of National Expenditure.* Changes to conditional grants are included in the 2017 Division of Revenue Amendment Bill. Revised provincial appropriations will be tabled in provincial legislatures before the end of the current financial year.

Medium-term spending priorities

Spending on services to low-income households remains a priority

Government spending priorities continue to align with the NDP, as elaborated in the medium-term strategic framework and the Mandate Paper. Despite limited fiscal resources, government is protecting expenditure that aims to deliver services to low-income households.

Table 4.2 Consolidated expenditure by function[1]

R billion	2016/17 Outcome	2017/18 Revised	2018/19 Medium-term estimates	2019/20	2020/21	Average annual growth 2017/18 – 2020/21
Learning and culture	**295.3**	**317.8**	**340.7**	**367.3**	**395.7**	**7.6%**
Basic education	216.9	230.8	249.8	267.2	286.5	7.5%
Post-school education and training	68.7	76.7	80.1	88.8	97.0	8.2%
Arts, sport, recreation and culture	9.7	10.4	10.8	11.3	12.1	5.3%
Health	**176.1**	**189.6**	**204.5**	**220.0**	**235.5**	**7.5%**
Peace and security	**184.8**	**195.5**	**206.2**	**220.7**	**235.5**	**6.4%**
Defence and state security	47.9	49.8	51.4	54.7	58.2	5.3%
Police services	86.9	93.7	100.0	106.8	114.2	6.8%
Law courts and prisons	41.3	43.6	46.5	49.7	53.1	6.7%
Home affairs	8.7	8.4	8.3	9.5	10.0	6.1%
Community development	**181.4**	**193.5**	**210.1**	**226.5**	**243.1**	**7.9%**
Economic development	**175.9**	**190.9**	**202.2**	**217.7**	**229.9**	**6.4%**
Industrialisation and exports	32.3	33.2	36.0	38.9	41.2	7.5%
Agriculture and rural development	25.9	26.5	28.1	30.1	31.8	6.3%
Job creation and labour affairs	17.9	20.0	21.3	22.5	23.9	6.1%
Economic infrastructure and network regulations	83.3	93.7	98.7	107.1	112.6	6.3%
Innovation, science and technology	16.6	17.5	18.1	19.2	20.4	5.2%
General public services	**60.4**	**62.3**	**64.7**	**67.5**	**71.6**	**4.8%**
Executive and legislative organs	13.1	14.8	16.2	16.9	17.7	6.1%
Public administration and fiscal affairs	39.5	40.1	40.7	43.0	45.9	4.6%
External affairs	7.8	7.4	7.8	7.6	8.1	3.1%
Social development	**218.2**	**234.2**	**251.2**	**269.0**	**286.9**	**7.0%**
Social protection	165.1	178.7	192.8	207.3	221.7	7.5%
Social security funds	53.1	55.5	58.4	61.7	65.2	5.5%
Payments for financial assets	**7.2**	**19.5**	**5.0**	**5.2**	**5.5**	**–**
Allocated by function	**1 299.2**	**1 403.3**	**1 484.5**	**1 594.0**	**1 703.8**	**6.7%**
Debt-service costs	146.5	163.3	183.1	203.3	223.4	11.0%
Contingency reserve	–	–	3.0	5.0	8.0	–
Consolidated expenditure	**1 445.7**	**1 566.6**	**1 670.6**	**1 802.3**	**1 935.1**	**7.3%**

1. Consisting of national and provincial departments, social security funds and public entities

Source: National Treasury

Health and social development

The NDP envisages a strong public health system that works for everyone, and a sharp reduction in the disease burden. Government also aims to provide a social safety net for all South Africans, particularly the young, elderly and disabled. Spending priorities include rolling out NHI, expanding provision of antiretroviral treatment, continuing early childhood development and building an integrated community health worker programme.

Government intends to expand NHI services in a progressive and affordable manner

The National Treasury and the Department of Health are working on proposals to expand NHI services in a progressive and affordable manner. Legislation is being drafted to establish the legal framework for an NHI Fund. Government is considering options to establish an interim fund structure to support a limited set of priority interventions, and operate in line with current legislation.

Provision for additional support to antiretroviral treatment programme and early childhood education

Government's antiretroviral treatment programme has been growing by about 400 000 patients each year. The MTEF makes provision for the growth in patient numbers expected with the implementation of the universal test-and-treat policy.

The *early childhood development conditional grant* will receive allocations of about R500 million per year over the medium term to improve health and learning outcomes. Government also proposes to shift the current home-based care programme in the *comprehensive HIV, AIDS and TB grant* to a more integrated community health worker programme. This will include health-related early childhood development services such as breastfeeding support for the first 1 000 days of a child's life.

Government's centralised approach to dispensing and distributing chronic medicines allows patients to collect their medication from alternative pick-up points such as private pharmacies. By June 2017, over 1.5 million patients were on the programme, which is more convenient for patients and reduces unnecessary consultations.

Learning and culture

Improving the quality of education and building skills are core objectives of the NDP. The Mandate Paper proposes strengthening support for skills development. Over the medium term, the budget supports increased university access by students from poor households, and the expansion of technical and vocational education and training.

Early childhood development to reach universal enrolment by 2019

About 95 per cent of six-year-olds are enrolled in Grade R, which forms part of early childhood development. Universal enrolment is expected by 2019. Over the three-year spending period ahead, the focus is to improve the quality of education by strengthening educator qualifications, and providing appropriate learner and teacher support materials.

The Department of Basic Education is working on a proposal to introduce a technical occupational stream in secondary schools. It would operate alongside the existing technical vocational and academic streams. The "three streams" model aims to provide additional pathways to work and complement existing training programmes. Findings from pilot sites will be used to refine the model.

The NSFAS was allocated over R40 billion from 2017/18 to 2019/20 to enable more than 450 000 students from poor households to access public universities and TVET colleges.

Government proposes to allocate R11.1 billion over the medium term for infrastructure projects at higher education institutions. Expanding student accommodation is a priority, and the Department of Higher Education and Training is refining a proposal to provide 300 000 new beds at public universities and TVET colleges by 2026.

Revenue from skills development levy to produce over 69 000 qualified artisans

Over the MTEF period, R51 billion in revenue from the skills development levy will support programmes expected to produce over 69 000 qualified artisans, and create 405 000 work-based learning opportunities through learnerships, internships and apprenticeships.

Table 4.3 Consolidated expenditure by economic classification[1]

R billion	2016/17 Outcome	2017/18 Revised	2018/19 Medium-term estimates	2019/20	2020/21	Average annual growth 2017/18 – 2020/21
Current payments	**872.0**	**939.6**	**1 014.4**	**1 097.9**	**1 180.8**	**7.9%**
Compensation of employees	510.3	549.3	587.9	629.9	677.8	7.3%
Goods and services	208.1	220.0	236.4	255.8	270.2	7.1%
Interest and rent on land	153.6	170.4	190.0	212.2	232.7	11.0%
of which: debt-service costs	*146.5*	*163.3*	*183.1*	*203.3*	*223.4*	*11.0%*
Transfers and subsidies	**472.9**	**505.1**	**543.1**	**584.8**	**627.1**	**7.5%**
Provinces and municipalities	112.5	120.7	131.9	143.3	155.9	8.9%
Departmental agencies and accounts	25.2	24.9	26.2	27.7	30.9	7.5%
Higher education institutions	30.9	38.1	38.9	41.0	43.2	4.3%
Foreign governments and international organisations	2.2	2.0	2.1	2.2	2.3	5.4%
Public corporations and private enterprises	32.8	31.4	33.7	36.2	38.1	6.8%
Non-profit institutions	29.6	31.9	34.0	36.2	38.4	6.4%
Households	239.8	256.2	276.3	298.2	318.2	7.5%
Payments for capital assets	**93.6**	**102.4**	**105.1**	**109.3**	**113.8**	**3.6%**
Buildings and other capital assets	72.8	79.5	83.1	86.7	90.0	4.2%
Machinery and equipment	20.8	22.9	22.1	22.6	23.8	1.3%
Payments for financial assets	**7.2**	**19.5**	**5.0**	**5.2**	**5.5**	**–**
Total	**1 445.7**	**1 566.6**	**1 667.6**	**1 797.3**	**1 927.1**	**7.1%**
Contingency reserve	–	–	3.0	5.0	8.0	–
Consolidated expenditure	**1 445.7**	**1 566.6**	**1 670.6**	**1 802.3**	**1 935.1**	**7.3%**

1. Consisting of national and provincial departments, social security funds and public entities
Source: National Treasury

Protection services

The NDP underlines the need for an effective criminal justice system and responsive police services. The budget will continue to fund the normal operations of the departments within the justice, crime prevention and security cluster, giving effect to a priority of the Mandate Paper – the integrated operational plan to fight crime. However, this cluster needs to manage pressures arising from employee compensation budgets. This will require reconsideration of recruitment strategies, as well as the composition and suitability of existing staff complements.

Pressures arising from employee compensation in justice, crime prevention and security need to be managed

Medium-term priorities include completing infrastructure projects under way, and maintaining and rehabilitating police stations, courts, correctional facilities, and military bases and health facilities. The new Mpumalanga High Court will open in 2018. Funding options for the Defence Review's recommendations are also under consideration (see Annexure A).

Once established, the Border Management Agency will take over management of South Africa's 72 air, land and sea ports of entry. The agency will be funded mainly through reallocations from those departments and agencies currently involved in border control and management.

Community development

Social and economic transformation requires South Africa to overcome the spatial legacy of apartheid. Integrated community development requires strengthened cooperation between national government, provinces and municipalities in housing, water, sanitation, electrification and public transport. Over the medium term, the focus remains on balancing resources to respond to water, sanitation and electrification infrastructure needs in rural areas, and improving public transport services and access to shelter in urban areas.

Public transport in smaller cities will have greater differentiation to ensure sustainability

Creating integrated public transport networks that expand access to economic activity and social services is a central objective of urban reform initiatives. To ensure that municipal public transport systems are sustainable, government aims to provide greater differentiation in the norms and standards of services and infrastructure. This includes moderating public transport service levels in smaller cities to ensure quality services that are affordable.

New conditional grants proposed for human settlements are discussed under the division of revenue. In addition, a new policy framework is being developed by the Department of Human Settlements.

Economic development

Spending focused on jobs, small businesses, small-scale agricultural production and industrial incentives

Growing and transforming the economy to create jobs and generate the resources needed to fund social services is at the heart of the NDP. Spending in this function will focus on expanding access to jobs, supporting small businesses and small-scale agricultural production, along with incentives for industrialisation, economic transformation and sustainable resource management.

The Community Work Programme maintains and improves local infrastructure using labour-intensive methods, providing income support to unemployed persons. It provides a bridging opportunity for youth and others who are actively looking for work. The work done by programme participants benefits their communities. Similarly, the social sector component of the Expanded Public Works Programme subsidises the pay of extra workers at non-profit organisations that are performing social functions.

Initial allocation of R1 billion for new fund to support small business and innovation

The National Treasury is working with the departments of Science and Technology and Small Business Development to establish a new fund for small business and innovation. The fund, which will be allocated R1 billion in 2019/20, will provide wholesale funding to private- and public-sector incubators, which will on-lend to entrepreneurs at the concept stage.

The Department of Science and Technology, with an allocation of R24.8 billion over the medium term, will invest in producing new knowledge, developing human capital, and for research and innovation.

Successful land reform programmes link new farmers into agricultural value chains. Agri-parks are central locations where smallholder farmers can process their produce and access market networks. Funding for agri-parks is provided through the Department of Rural Development and Land Reform. Three agri-parks are nearing completion, and government intends to build one such facility in each of the 44 district municipalities.

South Africa is a water-scarce country. Managing limited water resources is critical, as shown by the recent drought and the current water crisis in Cape Town. The Department of Water and Sanitation is expected to complete the water-pricing strategy in 2018/19. It will establish a new framework for how water is charged and subsidised for industrial, commercial, agricultural and domestic use. The institutional review for water resources, which includes establishing a national water infrastructure agency and catchment management agencies, is expected to be completed over the medium term.

New pricing strategy to be completed in line with urgent need to improve water resource management

Administrative services

The administrative services function comprises central planning and financial services, international relations and other general services. Government aims to build a people-centred, professional and ethical public service. Given fiscal pressures and needs in other areas, general public services will see a real decline in budgets over the medium term.

Given pressing needs in other areas, administrative services budgets will decline over medium term

Regional integration and development are important for economic and social progress in southern Africa. South Africa is currently chairing the Southern African Development Community, and is set to chair the Indian Ocean Rim Association for the next two years. The Mandate Paper identifies these responsibilities as priorities. The Department of International Relations and Cooperation will fund the associated costs from its current baseline through reprioritisation.

Division of revenue

The proposed division of revenue continues to prioritise funding of services for poor communities. Allocations to provinces focus on education, health and other social services. Allocations to local government subsidise the delivery of free basic services to low-income households, and the infrastructure needed to deliver those services.

Table 4.4 Division of revenue framework

R billion	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
		Outcome		Revised		Medium-term estimates	
Division of available funds							
National departments	**490.0**	**546.1**	**555.7**	**603.5**	**633.1**	**683.5**	**729.2**
Provinces	**439.5**	**471.4**	**500.4**	**538.2**	**575.8**	**617.8**	**663.9**
Equitable share	359.9	386.5	410.7	441.3	471.7	506.6	543.7
Conditional grants	79.6	84.9	89.7	96.9	104.1	111.2	120.1
Local government	**87.6**	**98.3**	**102.9**	**112.6**	**121.6**	**132.4**	**143.0**
Equitable share	41.6	49.4	50.7	57.0	62.7	69.0	75.7
General fuel levy sharing with metropolitan municipalities	10.2	10.7	11.2	11.8	12.5	13.2	14.0
Conditional grants	35.8	38.3	40.9	43.8	46.4	50.3	53.3
Total	**1 017.1**	**1 115.8**	**1 159.0**	**1 254.3**	**1 330.5**	**1 433.7**	**1 536.1**
Percentage shares							
National departments	48.2%	48.9%	48.0%	48.1%	47.6%	47.7%	47.5%
Provinces	43.2%	42.2%	43.2%	42.9%	43.3%	43.1%	43.2%
Local government	8.6%	8.8%	8.9%	9.0%	9.1%	9.2%	9.3%

Source: National Treasury

Provincial allocations grow by 7.2 per cent and local government allocations by 8.3 per cent

Over the medium term, government proposes to allocate national departments 47.6 per cent of available non-interest expenditure, provinces 43.2 per cent and local governments 9.2 per cent. Over this period, national government resources grow by 6.5 per cent, provincial resources by 7.2 per cent and local government resources by 8.3 per cent.

Table 4.5 Changes to division of revenue[1]

R billion	2017/18 Revised	2018/19	2019/20
		Medium-term estimates	
Changes to baseline			
National allocations	**13.3**	**2.9**	**15.2**
of which:			
Indirect grants to provinces [2]	*-0.4*	*2.8*	*3.0*
Indirect grants to local government	*0.5*	*–*	*–*
Provincial allocations	**0.0**	**-2.8**	**-2.6**
Equitable share	–	0.2	0.5
Conditional grants	0.0	-3.0	-3.1
Local government allocations	**0.1**	**0.1**	**1.9**
Total	**13.4**	**0.2**	**14.6**

1. Additions include the confirmation of provisional allocations in the 2017 Budget, announced but not previously included in baselines
2. Amounts may be shifted between direct and indirect grants to provinces and local government before the 2018 Budget is tabled
Source: National Treasury

Provincial allocations

Nearly 80 per cent of provincial budgets are spent on health, basic education and social welfare.

The provincial equitable share formula has been under review since 2016 to ensure that it remains impartial, fair and responsive to the needs of the provinces. As part of the review, data used for learner enrolment, previously based on annual surveys of schools, will now be collected through a tracking system established by the Department of Basic Education. The new system allows data to be verified and learners' progress to be tracked throughout their school careers. The more advanced system results in small changes to allocations as previous over-reporting by schools is corrected. The new data will be phased in over three years. Changes to other components of the formula flowing from the review will be introduced in consultation with provincial treasuries.

Programmes to prevent violence against women and children get R788.2 million

The equitable share has been increased by about R1.2 billion over the MTEF period to take account of provincial responsibilities aimed at preventing violence against women and children, and to support organisations that provide statutory social welfare services on behalf of provincial departments. The latter flows from the judgement of the Free State High Court in the National Association of Welfare Organisations and Non-Governmental Organisations case. The court found that government must determine a fair and transparent method of funding non-profit organisations that provide statutory social welfare services on behalf of the state. Research is being done to quantify the gap between current funding and the actual cost of service provision.

Table 4.6 Provincial equitable share

R million	2017/18	2018/19	2019/20	2020/21
Eastern Cape	61 848	65 700	70 026	74 590
Free State	24 522	26 258	28 159	30 180
Gauteng	86 643	93 670	101 240	109 354
KwaZulu-Natal	93 757	99 567	106 697	114 271
Limpopo	51 960	55 347	59 373	63 656
Mpumalanga	36 082	38 585	41 524	44 662
Northern Cape	11 720	12 513	13 446	14 439
North West	30 330	32 491	34 898	37 462
Western Cape	44 470	47 592	51 240	55 135
Total	**441 331**	**471 724**	**506 604**	**543 749**

Source: National Treasury

Changes to provincial conditional grants

Changes to grants support community health workers and healthcare facility maintenance

Government proposes several changes to health conditional grants over the MTEF period.

- A component will be introduced in the *comprehensive HIV, AIDS and TB grant* to standardise the Community Health Worker Programme.
- A portion of the direct *health facility revitalisation grant* and the infrastructure component of the *indirect national health insurance grant* will be ring-fenced for maintenance.
- Proposed additions of R22.4 million to the *national tertiary services grant* will extend the diagnosis-related groups project across the Western Cape and build capacity for other provinces to implement this initiative. The diagnosis-related group approach is a patient classification system used globally for payment of hospital services.

Shifts to ensure completion of school infrastructure projects and adequate maintenance

Spending on the indirect *school infrastructure backlogs grant* has been poor for a number of years and was scheduled to come to an end in 2017/18. However, the Department of Basic Education needs to complete projects that are under way. Government now proposes that R7.3 billion that had been shifted to the provincially-administered *education infrastructure grant*, but had not been allocated to specific projects, be returned to the department's *school infrastructure backlogs grant* over the 2018 MTEF period. Within the direct *education infrastructure grant*, the remaining R1.5 billion shifted from the *school infrastructure backlogs grant* in the 2017 MTEF will be ring-fenced to maintain existing school infrastructure.

New grants to clear backlog of title deeds for homes built with state subsidies

A full review of the *human settlements development grant* will be conducted based on the outcomes of the human settlements policy review. For the 2018 Budget, two new human settlements grants are proposed, both to be funded through reprioritisations from the *human settlements development grant:*

- Funds previously ring-fenced to clear the backlog of title deeds that have not yet been issued for homes built with state subsidies will now be allocated in a dedicated grant for a three-year period. The grant will have both direct and indirect components, with a small portion reprioritised for capacity in the national department.

- A grant will be established to fund responses to emergencies in line with housing policy. The funds will be held by the Department of Human Settlements and transferred to provinces or municipalities following an emergency.

Funds to maintain coal haulage roads in Mpumalanga will be ring-fenced in the *provincial roads maintenance grant* for another two years.

Encouraging transformation through procurement in provinces

Provinces will procure more than R600 billion in goods and services over the next three years. In line with the Preferential Procurement Policy Framework Act (2000), these purchases can promote transformation while ensuring value for money.

Several provinces are targeting increased procurement from disadvantaged areas. Gauteng has increased the number of registered township suppliers from 1 072 in 2014 to 8 268 in 2017. North West is focusing on procuring from townships, small towns and villages. By the end of 2016/17, the province had sourced goods and services from 6 659 suppliers, of which 3 263 (49 per cent) came from these targeted areas.

Mpumalanga has procured agricultural products, including for the School Nutrition Programme, to support black-owned businesses and small farmers. Several provinces have an integrated contractor development programme to promote construction-sector transformation. In the Western Cape, 51 per cent of the 5 500 suppliers the provincial government has done business with are small businesses, and about 2 221 are entirely black owned.

Local government allocations

The local government equitable share is the largest transfer to municipalities. Although funding is unconditional, it is calculated to subsidise the cost of delivering free basic services to poor households and to cover basic administrative costs in poorer municipalities. The confirmation of an additional R1.5 billion in 2019/20 that was part of a provisional allocation in the 2017 Budget means that the formula is fully funded to take account of rising bulk costs of electricity and water, as well as household growth.

New funding mechanisms for intermediate cities will be piloted in 2018/19

In line with government's integrated urban development framework, a new approach to funding intermediate cities will be piloted as part of the *municipal infrastructure grant* in 2018/19. It will emphasise a programme of capital investment that combines grant and non-grant funding. This approach may take the form of a separate grant for qualifying cities over the medium term, with strong performance incentives.

The allocation mechanism of the *public transport network grant*, which funds the improvement of urban public transport systems, will be amended. The changes will provide more stability in allocations for smaller cities. Performance incentives will be introduced and stricter conditions applied. Where cities fail to demonstrate that they have financially sustainable plans for public transport networks, allocations will be cut. Performance incentives will also be considered for other conditional grants, including for improved spending on infrastructure maintenance.

Spending on informal settlement upgrading in cities to be reviewed

The National Treasury and the Department of Human Settlements will review spending on urban informal settlement upgrading, with a view to changing the grant system to enable increased investment in on-site upgrading. This work will be aligned to the review of the provincial *human settlements development grant*.

Reforms over the medium term will enhance the ability of municipalities to raise revenue to invest in their own development. Government will:

- Table amendments to the Municipal Fiscal Powers and Functions Act (2007) to better regulate municipal development charges, through which landowners pay for the cost of connecting new developments to public infrastructure and services.
- Update the policy framework for municipal borrowing and financial emergencies. This will clarify the role of development finance institutions in enabling municipalities to obtain private-sector financing for infrastructure investment.

Reforms aim to enhance municipalities' ability to raise more revenue for development

Municipal revenue-raising capacities vary widely. The National Treasury will consider applications to waive co-funding requirements for infrastructure projects in municipalities with little or no ability to raise finance for such projects. Reprioritisations within the *regional bulk infrastructure grant*, *water services infrastructure grant* and *municipal infrastructure grant* will be made to fund the Bucket Eradication Programme.

Financial management challenges in municipalities

Like the rest of government, municipalities face a difficult fiscal environment. Even as demand for services rises, weak economic growth has put stress on consumers' ability to pay for services, while transfers from national government are growing more slowly than in the past.

Some municipalities have managed these challenges well, but others have fallen into financial distress and face liquidity problems. These include municipalities that are unable to meet their payment obligations to Eskom, water boards and other creditors. These municipalities need to rectify governance and management problems, focus on collecting revenues owed to them, and eliminate wasteful and non-core spending.

The National Treasury is working with other departments to develop a funding mechanism to support recovery plans for municipalities that face a financial crisis, as provided for in section 139(5) of the Constitution.

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