

MEDIUM TERM BUDGET POLICY STATEMENT 97 - A POLICY FRAMEWORK

Introduction

Reconstruction and development

The Medium Term Expenditure Framework takes the nation's Reconstruction and Development Programme as its point of departure. A broad range of social development and economic transformation goals flow from this commitment. Their expenditure implications have to be accommodated within a sound macroeconomic and fiscal framework, consistent with the division of responsibilities between national, provincial and local government. These dimensions of the MTEF are set out in the preceding chapters of this Statement. An introduction is provided below to the expenditure trends and the policy choices that the MTEF represents.

Government cannot achieve all its goals immediately, because there are constraints on the capacity to deliver and on resources available. It is the responsibility of government to determine priorities from among the nation's goals. The RDP provides clear guidance on these choices. The needs of the poor, and the prospects for our children, come first.

The purpose of the MTEF is to articulate these choices systematically and comprehensively. This empowers the Government, Parliament, civil society and the nation as a whole to determine priorities collectively. This chapter summarises the links between policy choices and Government's expenditure plans. It draws on cooperative planning and policy analysis undertaken by national and provincial departments, and valuable perspectives on education and health submitted by the NEDLAC fiscal and monetary chamber.

Cooperative government

The development of medium term expenditure plans is a cooperative undertaking of the national and provincial governments, drawing on both ongoing departmental planning and focused analyses of selected functions and programmes. The provinces are responsible for nearly 60 per cent of expenditure on public services. They work within a framework of nationally determined norms and standards and of cooperative governance, and act in the interests of shared national objectives. But they exercise considerable discretion over the management of resources, how they go about meeting those objectives, and the relative priority they give to competing spending pressures.

Publication of medium term plans

Three year expenditure plans will be published by the national government on 11th March 1998 and by the nine provinces shortly afterwards. The first drafts of these plans were prepared in mid-1997, and both the Cabinet and provincial Executive Councils have been integrally involved in the policy reviews and expenditure planning that have accompanied the

refinement of budget projections. A broad outline of the expenditure trends and policy issues that have emerged from the MTEF process is provided below.

This Medium Term Budget Policy Statement makes explicit the policy framework within which these expenditure plans will be finalised. It provides Parliament and civil society with an opportunity to discuss the nation's medium term fiscal commitments and to contribute to resolving outstanding issues.

Policies and programmes

Spending pressures

Government's RDP and public service transformation expenditure commitments can be organised into several clusters of policies and programmes. The following section lists some of the initiatives that will put upward pressure on national and provincial budgets during the MTEF period.

Public institutions

Reorganising the public service, strengthening democracy and building capacity – spending pressures include the establishment of commissions and regulatory agencies; organisation of the 1999 elections; public service transformation, affirmative action and reform of personnel policies; public sector training; creation of an autonomous revenue service; and consolidation of financial management systems.

These are straightforwardly government responsibilities, requiring well-managed and accountable departmental programmes and public institutions, supported where appropriate by a range of non-governmental and civil initiatives.

Building the economy

Investment in economic infrastructure, industrial promotion and small enterprise development – government commitments include spatial development initiatives; improvement in roads and other transport infrastructure; industrial cluster studies and supply-side support programmes; a consolidated municipal infrastructure programme; rural development and agricultural support; electrification and telecommunications promotion; water supply and sanitation; small enterprise finance and advisory services; and tourism promotion.

Government infrastructure investment is, where practical, subject to transparent cost-benefit analysis, and costs are often directly recovered from users. Investment in industrial development is largely undertaken in the private sector, supported by targeted incentives.

Education & training

Strengthening human resource development – spending pressures include expansion and restructuring of higher education; skills development, employment services and financing of training; education for learners with special needs; extension of further education and college

programmes; Curriculum 2005; redressing education infrastructure backlogs; and strengthening the financing of provincial schooling.

Education and training are high priority commitments, reflecting the promotion of equal access to learning opportunities, extension of further and higher education and promotion of skills development throughout the economy. Education and training yield benefits to individuals and employers and thus attract private spending, over and above government expenditure.

Criminal justice

Re-engineering the criminal justice system – this includes integration of information systems; expansion of prison capacity; reorganisation of crime prevention and detection services; improvement in court management and prosecuting capacity; extension of legal aid; and a renewed focus on priority crimes.

A sound criminal justice system is an essential foundation of a stable and secure society, underpinned by the rule of law and protection of human rights.

Welfare services

Developmental welfare, social security reform and poverty relief – commitments include development programmes focused on women and children; support for income-generating and employment-enhancing social welfare services; transformation of the child and youth care system; special protection measures for children; transformation of the welfare financing system; introduction of the child-support benefit and phasing out of the maintenance grant system; integration and better management of grants programmes; investment in job creation and poverty relief.

Government welfare and social security are the means through which society collectively provides a safety net to protect the poor and vulnerable. Improvements in the quality of life of the poor are also promoted through water supply, transport, energy, housing and other development programmes. In addition, the tax system encourages individuals who can afford to do so to invest contractually in advance of retirement.

Health care

Equitable and affordable access to health services – priorities include clinic building and district health services; free primary care; hospital rehabilitation; and rationalisation of central hospital services.

Government is responsible for ensuring equitable access of the poor to a full schedule of primary health care and hospital services. Beyond this public provision, individuals have access to private sector services, and medical schemes provide a degree of risk-pooling to income-earners who seek this protection.

Reprioritisation

Each of these programmes makes a contribution to reconstruction and development objectives. Each represents a pressing claim which Government should try to accommodate. However, neither the economy nor the public sector has the capacity or financial resources to meet all these claims immediately. Government must find ways to reprioritise in favour of these RDP commitments, and to deliver them as cost-effectively as possible.

Better targeting

Government therefore has to ensure that resources are well targeted towards the poor and the interests of future generations. Delivering greater equity and accelerated social development will require a continuing redirection of resources. Government has to find ways to ensure that people who can afford to pay for services do so, thereby releasing resources which can be redirected towards the poor.

Public-private partnerships

Government is responsible for ensuring that high quality public services are delivered equitably. In many cases, it will discharge that responsibility by working in partnership with the private sector and civil society, rather than producing the services directly itself. This enables Government to harness the skills and capacity of the business sector and non-governmental organisations and to promote small and medium sized enterprises. It also permits the Government to focus on its core role of specifying, regulating and subsidising the services, and not secondary roles such as engineering and construction.

Public utilities

There are functions that remain public sector responsibilities but should be performed by corporatised institutions, with appropriate oversight over pricing and financial accountability. Improved governance of public corporations and utilities has a key role to play in achieving efficient and equitable delivery of services.

Macroeconomic priorities

In deciding its public spending priorities, Government must also take account of the particular economic challenges facing South Africa, looking towards faster growth and development in the next century. Government's macroeconomic strategy implies several priorities for government:

- accelerated investment in infrastructure – both social and residential infrastructure, which are strongly redistributive, and investment in transport, communications and other economic services, which are necessary complements to more rapid industrial growth and urbanisation;
- training – a significant expansion in the contribution of public spending to training and vocational education, of both the employed and the unemployed;

- poverty relief and jobs – a labour-intensive shift in government spending on poverty relief and basic infrastructure development; and
- redistribution of social services – redistribution within the education, health and welfare service budgets in favour of historically under-served communities.

Reallocation and reprioritisation

Confronted by many pressing needs, Government cannot allocate substantially increased resources to all priority services. Medium term expenditure plans must strike a careful balance between reallocation of resources between functions and reprioritisation within the budgetary constraints of the main spending programmes.

The criminal justice system and education, health and welfare spending already consume over 60 per cent of total expenditure. These services may increase somewhat further as shares of total spending, but they cannot do so indefinitely if, for example, infrastructural investment is to be accelerated.

This means that equity and enhancement of services in the criminal justice system, education, health, welfare and social security will mainly have to be funded by improving efficiency and cutting back on lower priority spending within these sectors, rather than increased spending shares. Increased delivery of services to the poor will require a re-examination of the degree to which services people could pay for themselves are subsidised.

Principles

Government has agreed on several principles governing the reprioritisation of expenditure on high priority functions:

- The criminal justice system must be strengthened, but with appropriate encouragement of greater integration of programmes and activities across component parts of the system;
- Welfare and social security spending should continue to be firmly targeted towards meeting development and income support needs of the poor, and allocations for employment-based relief projects should be extended;
- Growth of education spending on personnel needs to be curtailed, with additional resources assigned to key quality-enhancing initiatives and improved management in the education system; and
- Promotion of a district-based primary health system should continue to be the first priority in health services, but together with a coordinated programme of hospital rehabilitation and strengthened hospital administration and service delivery.

Reprioritisation and public service transformation consistent with these principles will be reflected in the medium term budgets to be published in March 1998. The MTEF process has identified a range of policy issues to be confronted in taking this transformation programme further.

MTEF sectoral reviews

Introduction

The 1997 MTEF programme included sectoral reviews conducted by six work teams, comprising officials of national and provincial line departments and treasuries. The sectoral teams examined medium term spending plans in health, education, welfare, the criminal justice cluster and defence, and investigated public sector personnel management issues. Their task was to analyse the policy implications of projected expenditure, and to identify policy options for political office-bearers to consider.

Some of the main conclusions of the sectoral reviews are summarised here.

Education

The sectoral review of education found that current personnel spending trends will lead to higher expenditure than envisaged in the preliminary medium term provincial education estimates. Personnel costs absorb too high a share of available funds, leaving insufficient resources for renewed infrastructure, curriculum reform and learning materials. Improved financial management and greater flexibility in personnel management are required if inequality in education spending is to be redressed and quality-enhancing initiatives supported.

In order to achieve equitable financing of public schools, consideration may need to be given to subsidising schools that serve higher-income communities on a standard per learner basis, making these institutions responsible for meeting costs above their equitable entitlement through fees and other own revenue.

It is recognised that the financing of further and higher education should continue to draw strongly on private sources. This means that bursary and loan schemes should be strengthened to ensure that students are not denied access as a consequence of inability to pay, but there is also scope for rationalising existing institutions and strengthening cost-recovery from learners and employers, coordinated in part through the evolution of Government's skills development strategy.

Health services

Reprioritisation in favour of district-managed primary health services is in progress in all provinces. Further efficiency gains will need to be achieved if the targets for primary health care are to be reached, but there is considerable evidence of improved utilisation of clinics and district hospitals. Expenditure management has proved difficult in hospitals with medical training and tertiary care facilities, as they face both rising referral rates and pressure to rationalise and reduce costs.

The health sectoral team has proposed a system of conditional grants to supplement the budgets of provinces with medical schools and central hospitals, and to facilitate the redistribution of tertiary health services.

There is considerable scope for further decentralisation of hospital management and greater competition of public hospitals for fee-paying patients, including preferred provider and other contractual arrangements with medical schemes and employers.

Welfare

The MTEF review of welfare and social security identified strong upward pressures on spending associated with increased registration of social grants beneficiaries in most provinces. The introduction of the new child support programme will add to this trend over the next few years, offset somewhat by the phasing out of the former maintenance grant. Several provincial welfare budgets will need to be reviewed, taking account of both the phasing in of the child support grant and the need to budget fully for beneficiary numbers.

The welfare team recommended that efforts to improve social security management and to root out fraud and abuse should be strengthened, building on the progress that has been made in integrating provincial information systems. It was noted that managerial control and financial responsibility for social security should be located together, either at a national or a provincial level.

There is scope for favouring more discretionary programmes focused on the needs of the poor and limiting expenditure growth on broader entitlement programmes. In the longer term, private contractual savings needs to be extended to a larger share of the work force, thereby limiting the burden of retirement provision met by the public sector.

Defence

An MTEF team examined defence spending needs, in the light of the Defence Review and the security threats South Africa faces. Spending on defence has fallen considerably in real terms since the 1980s. The review recommended that defence spending should be stabilised at around 1½ per cent of GDP during the MTEF period. In the short term this will require a substantial reduction in the numbers of service personnel. The report also recommends efforts to improve defence budgeting and inventory management.

Criminal Justice

The MTEF process has included a joint review of the criminal justice system, focused mainly on police, correctional services and the law courts. Work is continuing on coordination between the government agencies involved and improved case management through the system. It has been recommended that the budget should make provision for integrated projects involving the whole criminal justice cluster.

Personnel management

The MTEF review of personnel issues concluded that improving the management of personnel is the single most important priority for Government. It is the key to improving service delivery, making the provision of services more equitable, and enabling Government

to meet its reconstruction and development priorities within a level of spending that can be afforded. This requires dismantling over-centralised and bureaucratic controls, empowering managers to manage staff, and providing incentives to keep personnel costs under control. The team recommended the introduction of an affordable right-sizing instrument, amendments to the Public Service Act to improve disciplinary procedures, restructuring the salary and grading system to give managers greater flexibility, decentralisation of collective bargaining, tight control of personnel budgets and improvements in information systems.

Transforming service delivery

In addition to strengthening RDP programmes, scaling down lower priority spending and concentrating on core Government business, resources can be released for improved and more equitable services by improving the delivery of services.

Human resources

At the heart of improved service delivery is better use of human resources. Government has prioritised improved training and organisational transformation in the public services. An employer-initiated right-sizing instrument together with social plan measures in support of affected groups, more streamlined public service disciplinary proceedings and greater devolution of discretion over pay and personnel management, within a broad framework and clear budgetary constraints, are amongst the reforms necessary to achieve more effective and more productive use of personnel in public sector service delivery.

Extra-budgetary agencies

The growth in the number of *extra-budgetary government agencies* that are not subject to the constraints of the public service staff code and pay agreements has led to concern that salary structures are sometimes neither disciplined by market pressures nor subject to appropriate regulatory oversight. Without bringing off-budget agencies under the ambit of the full public service code, it is important that their salary structures should be standardised, regulated and transparently reported.

Other measures

Other possible measures to improve service delivery include:

- greater cost-recovery from users that can afford to pay, which would release fiscal resources for redistribution and more equitable service delivery;
- changing regulations that have the effect of raising costs, such as levels of support service and hardware prescriptions in defence or protection services, building and other infrastructure standards and excessive tender specifications;
- improved coordination and rationalisation of government structures, including rationalisation and better cost control of commissions and regulatory agencies;
- strengthened coordination between national and provincial departments and local government and between spending departments and treasuries; and

- improved financial management, including information systems development, particularly in provincial treasuries and line departments.

Cutting back low priorities

Defence

Against the background of considerable reductions in defence spending in recent years and the policy commitments envisaged in the Defence Review, there may not be much scope for further cutbacks. The capacity of the defence force to respond to emergencies of various kinds contributes to several public policy objectives, in addition to providing protection against external threats. Nonetheless, Government will continue to seek ways to achieve these goals more cost-effectively, with the aim of releasing resources where possible.

Subsidies

There are a number of economic and social subsidies which could be reviewed and better targeted towards the poor or to achieve their purposes more efficiently. Examples include the interest subsidy payable in export credit schemes, subsidies implicit in below-cost pricing of government water schemes or transport projects, and subsidies to research organisations, cultural foundations and education or health facilities that mainly serve higher income communities.

Private sector involvement

In addition, consideration should be given to rationalisation or greater private sector involvement in some services or institutions. There are opportunities for greater private sector involvement in the funding of colleges, universities, technikons and hospitals. Opportunities for transfer to the private sector of government services include the government printing works, government garages and central computer services.

Projected expenditure trends

Based on preliminary national and provincial budgets for the next three years, it is possible to project likely consolidated spending trends. These estimates include provincial expenditure from their own revenue, and thus exceed somewhat the aggregate expenditure levels set out in Chapters Four and Five.

Table 6.1: Expenditure growth

| R billion | 1997/98 | 1998/99 | 1999/00 | 2000/01 | Average annual growth |
|---|----------------|----------------|----------------|----------------|------------------------------|
| National government | | | | | |
| Debt service costs | 39,9 | 42,6 | 45,4 | 48,8 | 6,9% |
| Spending on national functions | 60,8 | 64,9 | 69,8 | 76,8 | 8,1% |
| Conditional grants to provinces | 4,5 | 4,9 | 5,0 | 5,2 | 5,4% |
| Provincial government | | | | | |
| Spending excluding conditional grants | 81,8 | 85,1 | 92,6 | 100,5 | 7,1% |
| Policy reserve | 2,1 | 5,0 | 7,0 | 10,0 | |
| Total national and provincial spending | 189,2 | 202,5 | 219,8 | 241,3 | 8,5% |
| Total non-interest expenditure | 149,2 | 159,9 | 174,4 | 192,5 | 8,9% |

This table differs from Table 4.5 because provincial own revenues are included, and because the table does not include the local government equitable share or grants to local government for operating costs.

Projected growth

Table 6.1 shows that non-interest expenditure by national and provincial governments is expected to grow by some 8,9 per cent a year on average over the next three years.

Provincial spending is expected to grow less rapidly than national spending because of a projected decline in own revenues. The equitable shares of national and provincial government grow at the same rate over the MTEF period.

Non-interest expenditure on national and provincial functions is expected to grow by 8,1 per cent and 7,1 per cent a year, respectively. Non-interest expenditure growth accelerates over the MTEF period, as the share of debt service costs falls and expected economic growth increases.

Expenditure by type of service

Table 6.2 presents a projected breakdown of expenditure in 2000/01 classified by type of service, together with a comparable classification of the consolidated 1997/98 budgets. These are estimates based on preliminary departmental allocations and are subject to appreciable changes as budgets are further refined. The classification below does not fully correspond with the standard functional breakdown of expenditure that is published at budget time and used in Table 4.1.

Table 6.2: Projected breakdown of spending by type of service

| | 1997/98 | | 2000/01 | | Average annual growth |
|---|-----------|----------------------------|-----------|----------------------------|-----------------------|
| | R billion | % of non-interest spending | R billion | % of non-interest spending | |
| Education | 38,6 | 26,2% | 49,5 | 27,1% | 8,7% |
| Health | 20,1 | 13,6% | 24,9 | 13,6% | 7,4% |
| Welfare | 16,0 | 10,9% | 20,7 | 11,4% | 9,0% |
| Other social and provincial services | 22,1 | 15,0% | 25,8 | 14,1% | 5,3% |
| Defence | 10,8 | 7,4% | 12,4 | 6,8% | 4,6% |
| Justice, police & prisons | 18,3 | 12,5% | 24,1 | 13,2% | 9,5% |
| Economic services | 14,5 | 9,8% | 17,1 | 9,4% | 5,7% |
| General administration | 6,7 | 4,5% | 8,0 | 4,4% | 6,2% |
| Total | 147,1 | 100,0% | 182,5 | 100,0% | 7,5% |
| Reserve | 2,1 | | 10,0 | | |
| Total non-interest expenditure | 149,2 | | 192,5 | | 8,9% |

Social services

Education, health and welfare services are expected to receive stable or increased shares of total non-interest spending. Other social and community services, including housing and various provincial functions, will grow somewhat more slowly.

Protection services

Within total expenditure, defence spending grows relatively slowly, while the criminal justice cluster takes up a significantly increased share of the total. The strongest growth is projected for the correctional services function, which is expanding to cater for increasing numbers of prisoners and improved quality of rehabilitation and care.

Economic services

Economic services are projected to grow more slowly than total non-interest spending. These are functions of government that are complemented by infrastructure projects and other activities of various public sector corporations and extra-budgetary government agencies.

Capital and current spending

Investment

Government aims to increase the amount of public spending going towards investment. This is required if the nation is to address the substantial inherited infrastructure backlogs, and to provide higher quality and more equitable public services.

Public sector spending on infrastructure development is mainly the responsibility of public utilities and corporations and municipalities. There is nonetheless an important role for government spending, including support for housing development, roads construction and water schemes.

Based on preliminary budget estimates and before taking into account the unallocated reserve available, government capital spending is projected to remain about 8 per cent of non-interest expenditure over the MTEF period. Government aims to strengthen the capital spending trend implied by these projections.

Consumption spending

An increase in capital spending as a share of the total requires tight control over consumption expenditure and transfers. Since most consumption spending is wages and salaries of public servants, this means that pay increases must be held at fiscally responsible levels.

Almost 50 per cent of non-interest expenditure is budgeted for personnel costs. The total wage bill is projected to increase by an average of 8,4 per cent a year over the period of the MTEF, marginally more slowly than total expenditure.

Conclusion

This Medium Term Budget Policy Statement sets out Government's objectives, together with an assessment of the resources that are available over the next three years. The task of Government is to design policies to deliver those objectives within the resources available.

This chapter sets out Government's preliminary ideas on how that can be achieved. It is unlikely that there will be very substantial transfers of resources into the social services and protection services, although these sectors are anticipated to increase their share of spending. This means that the Government must deliver its objectives by targeting resources on services for the poor, reprioritising spending from lower priorities, focusing on the proper role of government, improving personnel management and securing greater efficiency from the money that is available.

Government is committed to delivering a Budget which expresses the priorities of the whole nation. All stakeholder groups, and all citizens of the new South Africa, are invited to reflect on the policies and priorities set out in this Medium Term Budget Policy Statement, and to express their opinions to enable the Government to take them into account as the Budget is finalised.