2020 MTBPS

Medium Term
Budget Policy Statement

SECURING ECONOMIC RECOVERY BEYOND COVID-19

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

STAY SAFE
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Overview

- Government's medium-term policy priorities are economic recovery and fiscal consolidation.
- The social compact agreed to between government, business, labour and civil society prioritises short-term measures to support the economy, alongside crucial structural economic reforms.
- The economy is expected to contract by 7.8 per cent in 2020, recovering to real GDP growth of 3.3 per cent in 2021. Economic growth is expected to average 2.1 per cent over the three-year forecast period.
- Fiscal measures – primarily reductions to the wage bill – will narrow the budget deficit and stabilise debt over the next five years to return the public finances to a sustainable position.
- The consolidated deficit narrows from 15.7 per cent of GDP in 2020/21 to 7.3 per cent by 2023/24. Gross national debt is projected to stabilise at 95.3 per cent of GDP by 2025/26.

Global economic recovery is expected to be long and uneven

Table 2.1 Economic growth in selected countries

Region/country	2018	2019	2020	2021	2020	2021
Percentage	Actual		Projections		Difference from June 2020 Projections	
World	**3.5**	**2.8**	**-4.4**	**5.2**	**0.8**	**-0.2**
Advanced economies	**2.2**	**1.7**	**-5.8**	**3.9**	**2.3**	**-0.9**
United States	3.0	2.2	-4.3	3.1	3.7	-1.4
Euro area	1.8	1.3	-8.3	5.2	1.9	-0.8
United Kingdom	1.3	1.5	-9.8	5.9	0.4	-0.4
Japan	0.3	0.7	-5.3	2.3	0.5	-0.1
Emerging and developing countries	**4.5**	**3.7**	**-3.3**	**6.0**	**-0.2**	**0.2**
China	6.7	6.1	1.9	8.2	0.9	–
India	6.1	4.2	-10.3	8.8	-5.8	2.8
Brazil	1.3	1.1	-5.8	2.8	3.3	-0.8
Russia	2.5	1.3	-4.1	2.8	2.5	-1.3
Sub-Saharan Africa	**3.3**	**3.2**	**-3.0**	**3.1**	**0.2**	**-0.3**
Nigeria	1.9	2.2	-4.3	1.7	1.1	-0.9
South Africa[1]	0.8	0.2	-7.8	3.3	-0.6	0.4
World trade volumes	**3.9**	**1.0**	**-10.4**	**8.3**	**1.5**	**0.3**

[1] *National Treasury forecasts*
Source: IMF World Economic Outlook, October 2020

- Containment of COVID-19 is expected to support an improving growth outlook in advanced economies in 2021.
- Developing countries are set to grow faster than their developed counterparts next year.

Domestic economic outlook

Table 1.1 Macroeconomic projections

Calendar year	2019 Actual	2020 Estimate	2021	2022 Forecast	2023
Percentage change unless otherwise indicated					
Household consumption	1.0	-7.9	4.7	2.2	1.9
Gross fixed-capital formation	-0.9	-19.6	-1.4	3.9	3.9
Real GDP growth	**0.2**	**-7.8**	**3.3**	**1.7**	**1.5**
GDP at current prices (R billion)	**5 078**	**4 885**	**5 240**	**5 553**	**5 877**
CPI inflation	4.1	3.2	4.1	4.4	4.5
Current account balance (% of GDP)	-3.0	-0.8	-1.6	-2.0	-2.7

Source: Reserve Bank and National Treasury

- Following a sharp, synchronised 2020 COVID-19 recession, SA real GDP growth will average 2.1 per cent over the medium term, with output only returning to pre-pandemic levels in 2024.
- The main risks to the economic outlook are weaker-than-expected growth, continued deterioration in the public finances and a failure to implement structural reforms.
- A second wave of COVID-19 infections, accompanied by new restrictions on economic activity, would have significant implications for the outlook.

The COVID-19 fiscal relief package

- Main budget non-interest spending increased by R36 billion in the current year compared with 2020 Budget estimates, including COVID-19 fiscal relief package allocations to critical frontline services.
- The state's contingent liabilities increased through a R200 billion credit guarantee scheme for firms. In addition, the June 2020 special adjustments budget made provision for additional tax relief of R70 billion and temporary unemployment relief of R40 billion.
- By the end of September, R47.4 billion had been paid to 10.6 million beneficiaries from over 931 000 employers through the temporary employer/employee relief scheme.
- The Reserve Bank has also provided support to households and firms by lowering the main interest rate (the repurchase rate) by 2.75 percentage points since March 2020.
- Details on the take-up and effects of tax relief measures will be provided in the 2021 Budget Review.

The economic recovery plan

- Working with its social partners in business, labour and civil society, government has begun implementing an economic recovery plan, with immediate measures to boost confidence and investment, and longer-term reforms to promote sustained higher economic growth.
- In the short term, the economic recovery plan will focus on building infrastructure, expanding electricity generation, allocating digital spectrum, and supporting rapid industrialisation and employment.
- At the same time, government will roll out structural reforms such as modernising network industries, reducing barriers to entry, and increasing regional integration and trade. The National Treasury estimates that, in combination, these reforms can raise growth to over 3 per cent over the next 10 years and create more than 1 million jobs.
- The Infrastructure Fund will complement the plan's focus on capital investments.
- Operation Vulindlela implementation unit will be staffed by a full-time technical team that draws on additional expertise and capacity in the public and private sectors.

Revenue outlook

Table 3.4 Revised revenue projections

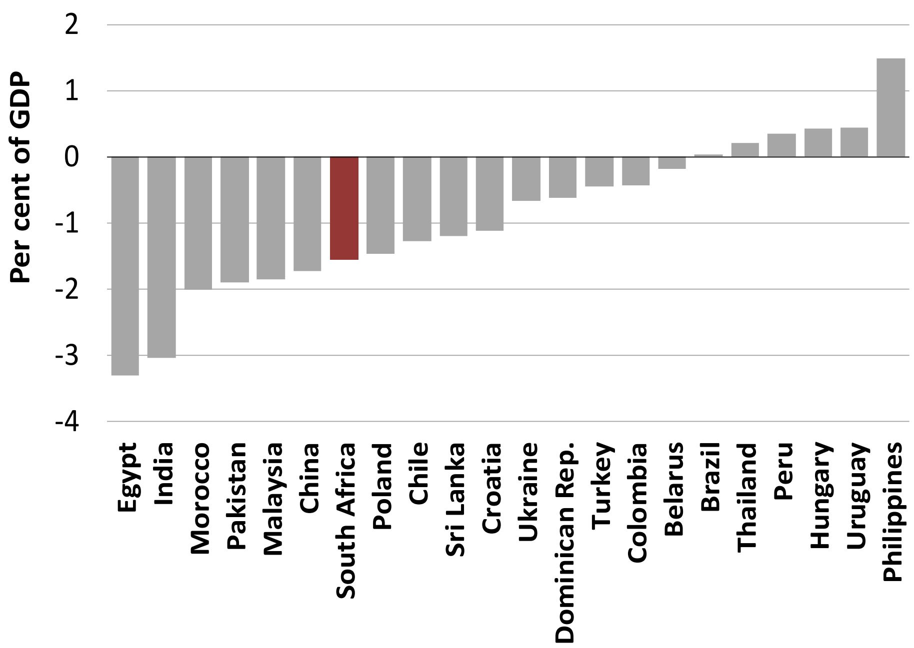
R billion	2020/21	2021/22	2022/23	2023/24
2020 Budget	**1 425.4**	**1 512.2**	**1 609.7**	
Buoyancy	*0.93*	*1.00*	*1.01*	
2020 special adjustments budget	**1 121.3**	**1 291.4**	**1 394.0**	**1 508.9**
Buoyancy	*3.23*	*1.58*	*1.46*	*1.33*
Revised estimates	**1 112.6**	**1 279.5**	**1 392.2**	**1 503.2**
Buoyancy	*3.18*	*1.59*	*1.50*	*1.35*
Change since 2020 Budget	**-312.8**	**-232.7**	**-217.5**	
Change since 2020 special adjustments budget	**-8.7**	**-11.9**	**-1.8**	**-5.7**

Source: National Treasury

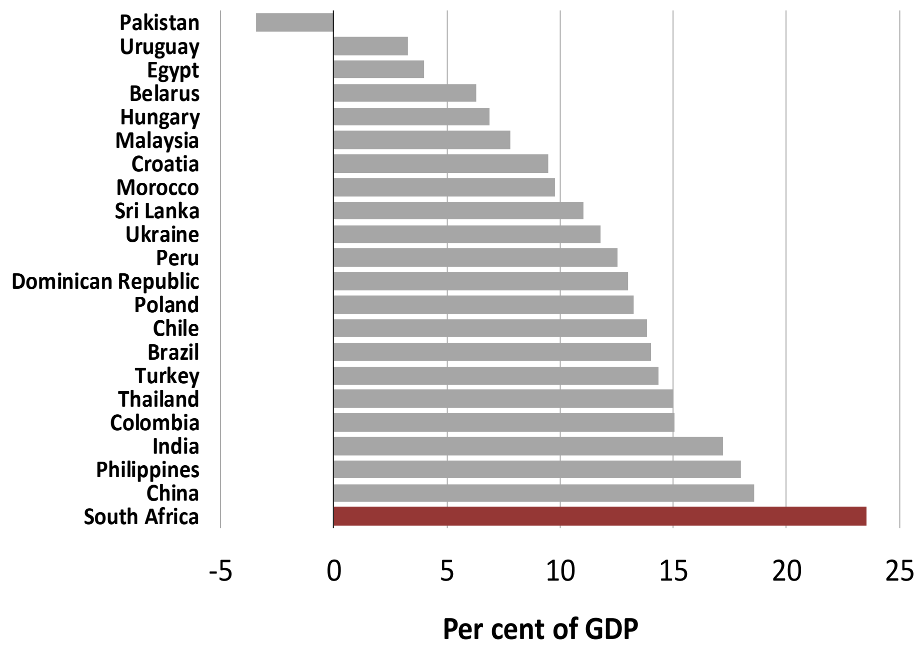
- The extraordinary shock to economic output in 2020/21 translates into large revenue shortfalls that will persist over the medium term.
- Although overall buoyancies appear relatively large up until the end of the MTEF period, this reflects a slow improvement in the tax-to-GDP ratio after the large once-off decrease in 2020/21.
- The tax-to-GDP ratio is only expected to recover to the 2019/20 level by 2027/28.

South Africa in global context

Average primary balance, 2009 – 2019



Projected three-year increase in debt



Source: IMF Fiscal Monitor, October 2020

- In comparison with a wide range of other developing countries, South Africa's average primary balance over the last 10 years falls in the middle of the distribution.
- But South Africa's three-year increase in debt to GDP is the among the largest.
- Fiscal distress is mounting in developing countries amid historically high indebtedness. In this environment of rising fiscal pressures, South Africa is losing ground to its peers.

Fiscal metrics are deteriorating

Over the past five years, the fiscal environment has been characterised by:

- Interest payments absorbing a growing share of limited public resources, which increasingly crowds out spending on social and economic investment. Debt-service costs are now 4.8 per cent of GDP, up from 3.3 per cent in 2016/17.
- A sharp drop in public infrastructure investment, mostly driven by declines in spending by state-owned companies. Between 2016/17 and 2019/20, total public infrastructure spending fell from R250 billion to R183 billion, or from 5.7 to 4 per cent of GDP.
- A deteriorating government balance sheet, including state-owned companies and municipalities struggling to pay salaries and other operational costs.

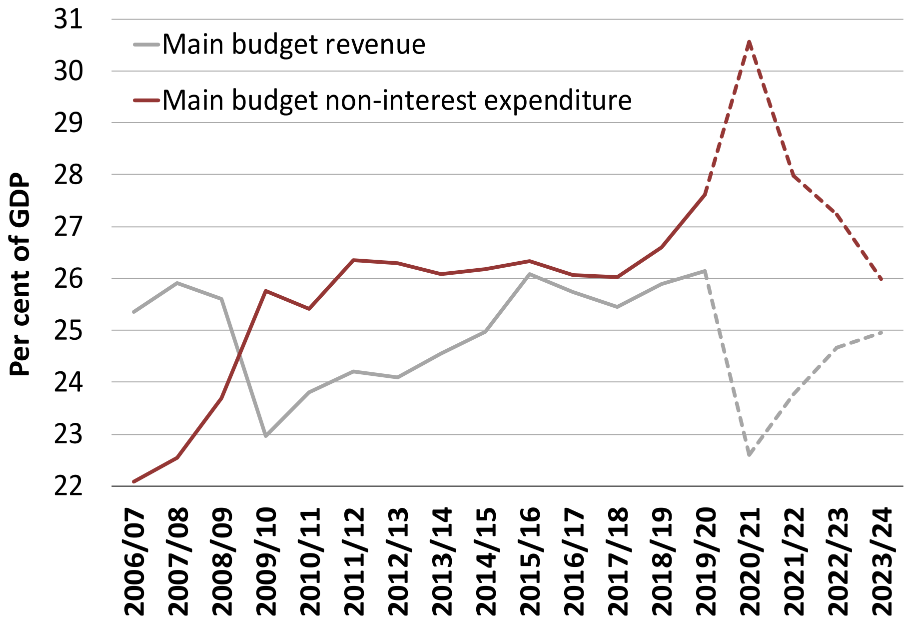
Options to stabilise the fiscus are becoming increasingly limited. Growth reforms are only expected to begin yielding results over the next several years, implying continued weakness in revenue collection over the period ahead.

Proposed steps to reduce the fiscal deficit and stabilise the debt-to-GDP ratio over a five-year period

- Relative to the 2020 Budget, main budget non-interest spending (excluding technical adjustments) is reduced by R60 billion in 2021/22, R90 billion in 2022/23 and R150 billion in 2023/24, with constrained spending growth in the following two years.
- The largest share of reductions falls on compensation. Other non-interest spending items are also reduced, while funding for buildings and other fixed structures, provincial and local capital grants, and the Infrastructure Fund is protected.
- To assist with the consolidation, government has projected tax increases of R5 billion in 2021/22, R10 billion in 2022/23, R10 billion in 2023/24 and R15 billion in 2024/25.
- The aim is to reach a main budget primary surplus by 2025/26. This target is expected to result in debt stabilising at 95.3 per cent of GDP in the same year.

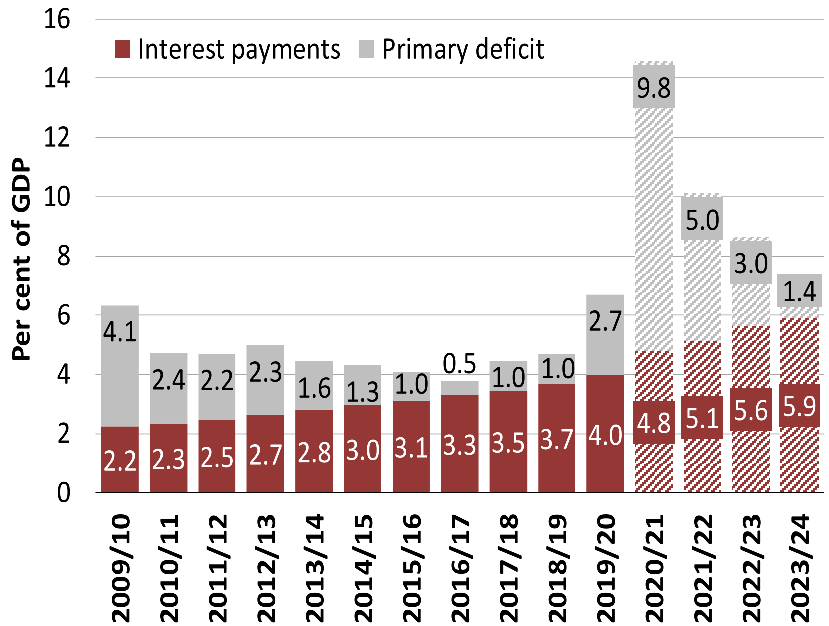
The main budget and primary balances will narrow over the medium term

Main budget primary balance*



*Excludes Eskom financial support and transactions in financial assets and liabilities

Main budget deficit



Gross loan debt outlook

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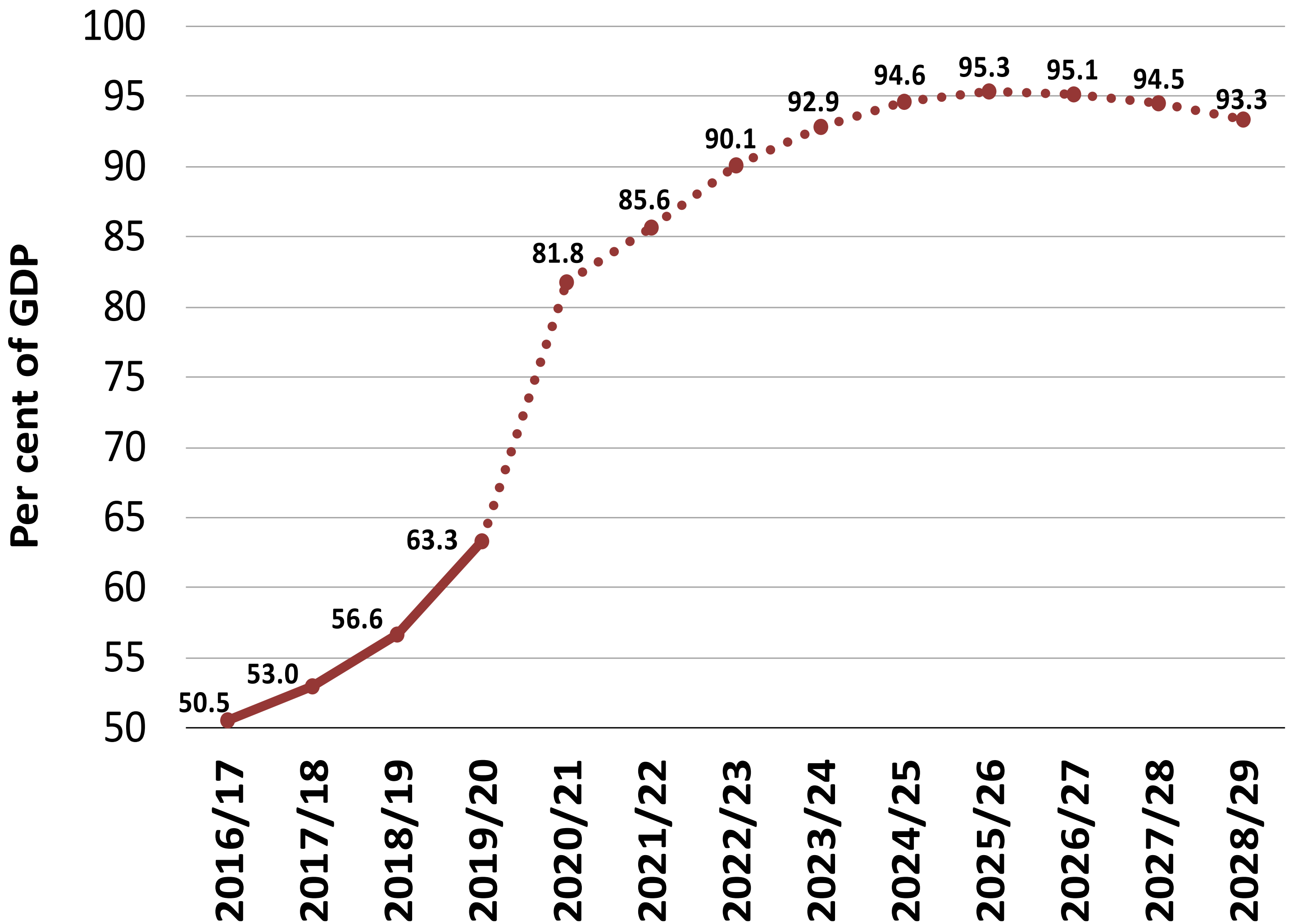

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Fiscal framework

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Table 1.2 Consolidated government fiscal framework

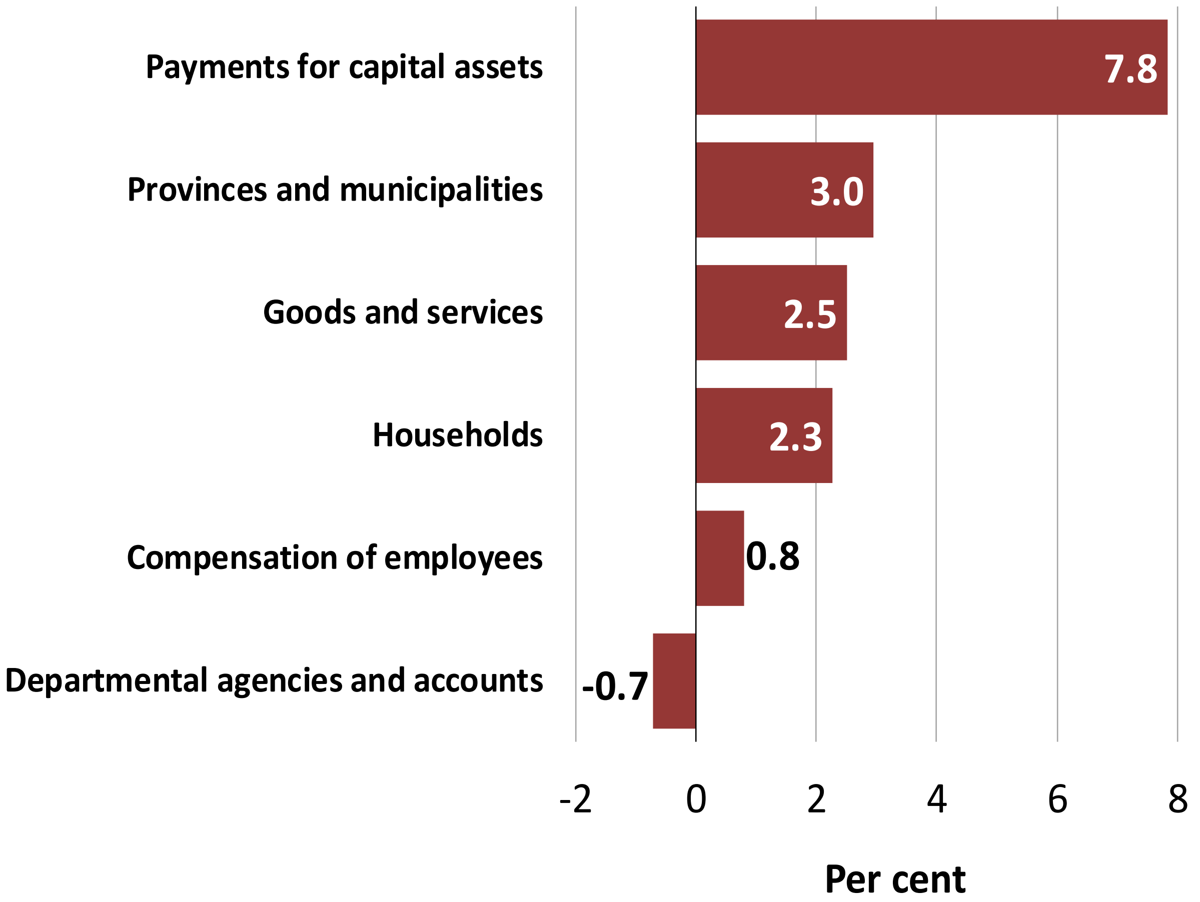
R billion/percentage of GDP	2019/20 Outcome	2020/21 Revised	2021/22 Medium-term estimates	2022/23	2023/24
Revenue	**1 518.1**	**1 276.7**	**1 457.6**	**1 595.8**	**1 705.7**
	29.5%	*26.3%*	*27.4%*	*28.3%*	*28.6%*
Expenditure	**1 848.7**	**2 037.8**	**1 993.5**	**2 079.6**	**2 139.2**
	35.9%	*41.9%*	*37.5%*	*36.9%*	*35.9%*
Budget balance	**-330.6**	**-761.1**	**-535.9**	**-483.9**	**-433.4**
	-6.4%	*-15.7%*	*-10.1%*	*-8.6%*	*-7.3%*
Total gross loan debt	**3 261.3**	**3 974.1**	**4 551.8**	**5 071.3**	**5 536.2**
	63.3%	*81.8%*	*85.6%*	*90.1%*	*92.9%*

Source: National Treasury

- The consolidated deficit includes national and provincial government, social security funds and public entities.
- The consolidated deficit will narrow from 15.7 per cent of GDP in 2020/21 to 10.1 per cent in 2021/22 and 7.3 per cent by the outer year.

The proposed spending reductions will improve the composition of spending from consumption towards investment

Average nominal consolidated spending growth, 2020/21 – 2023/24*



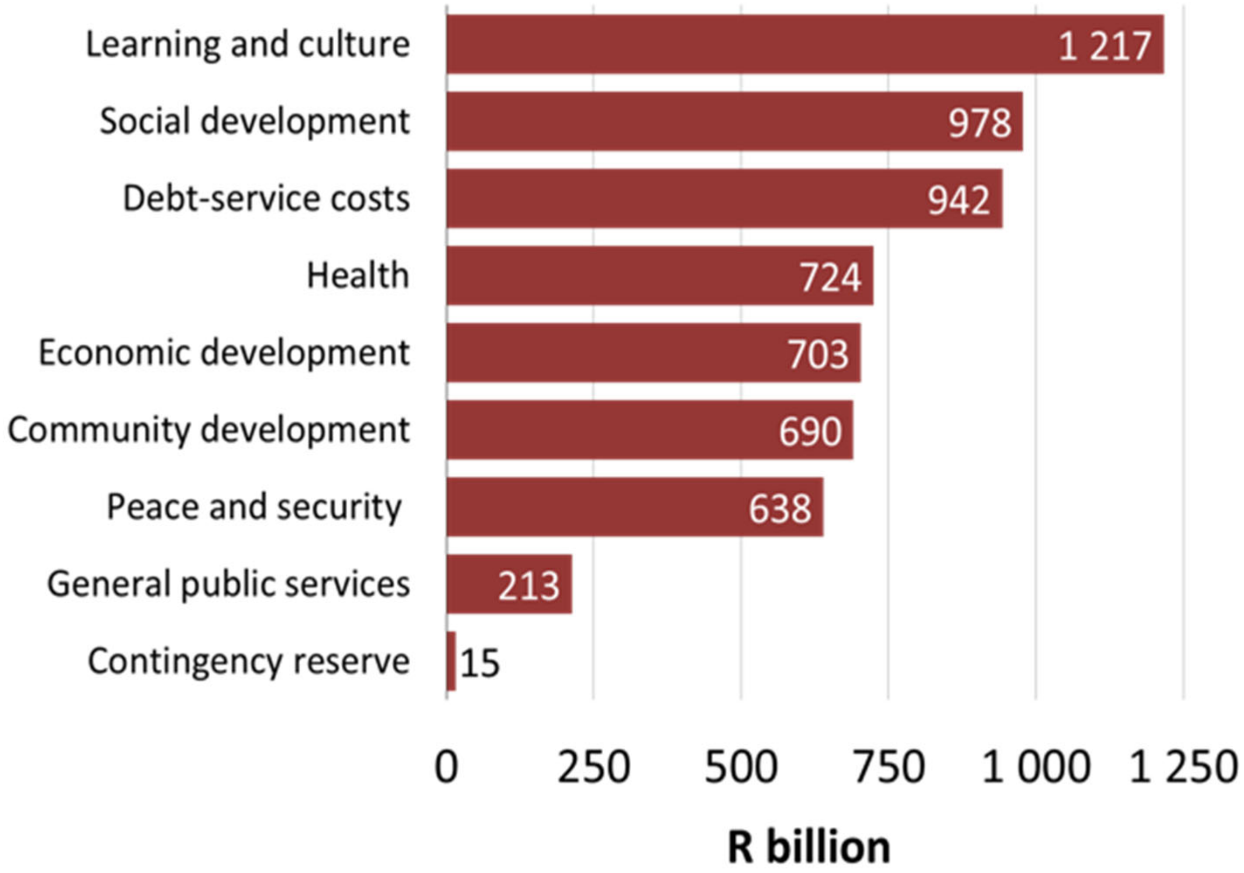
*Excludes COVID-19 fiscal relief measures in 2020/21

Achieving wage bill reductions

- Government proposes growth in the public-service wage bill of 1.8 per cent in the current year and average annual growth of 0.8 per cent over the 2021 MTEF period.
- Government has not implemented the third year of the 2018 wage agreement. Notwithstanding that the matter is before the labour court, government is actively engaging with labour unions to find a solution to a more sustainable cost of employment.
- Furthermore, the Budget Guidelines propose a wage freeze for the next three years.
- Additional options to be explored include harmonising the allowances and benefits available to public servants, reconsidering pay progression rules and reviewing occupation-specific dispensations.

Expenditure priorities

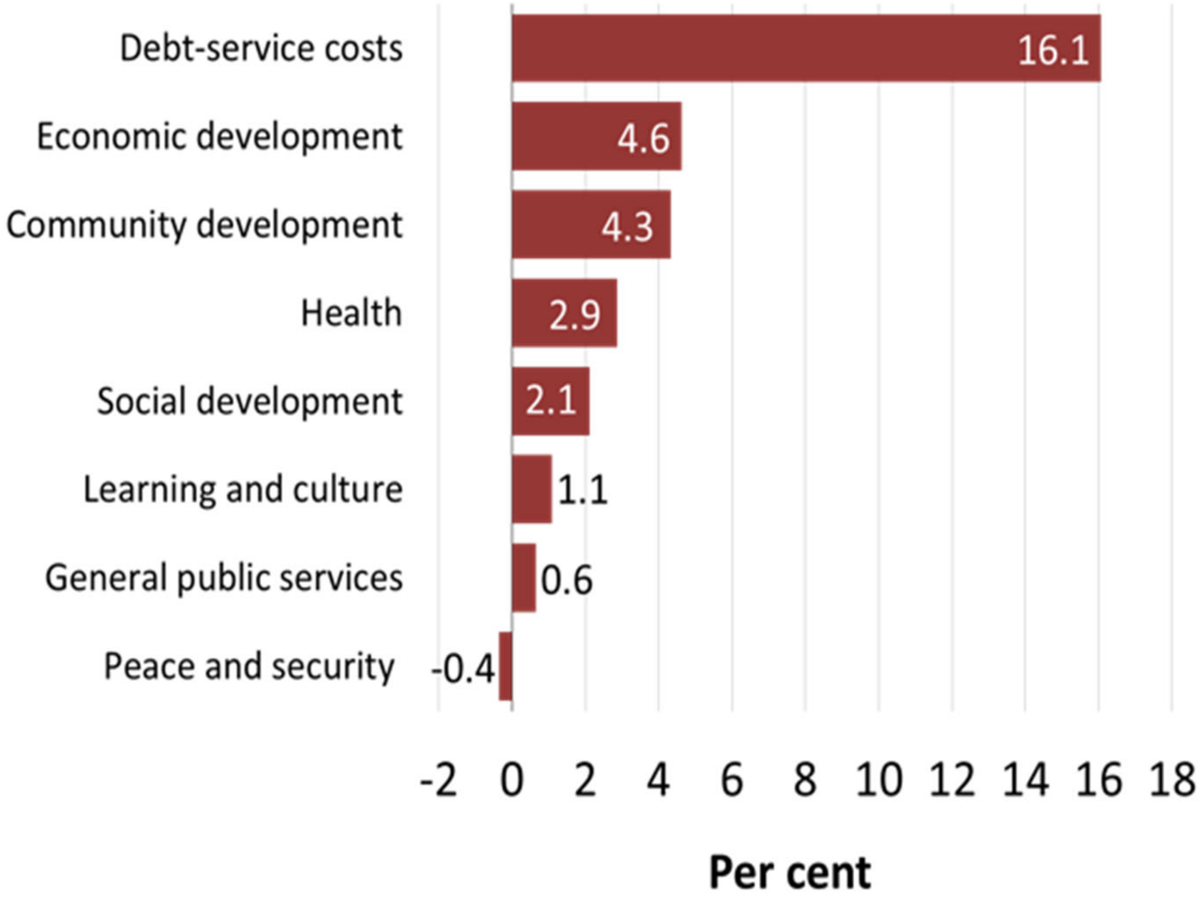
Average nominal growth in consolidated spending, 2020/21 – 2023/24



- Consolidated government spending is expected to total R6.21 trillion over the MTEF period, increasing from R2.04 trillion in 2020/21 to R2.14 trillion in 2023/24, at an average annual growth rate of 1.6 per cent.
- Over the medium term, the learning and culture function continues to receive the largest allocation of funds, mainly for basic and post-school education and training.

Fastest-growing functions

Consolidated government expenditure by function, 2021/22 – 2023/24



- Economic development and community development are the fastest-growing functions mainly due to above-inflation growth in road infrastructure and expanded access to basic services in line with economic recovery plan

Division of revenue framework

R billion	2017/18	2018/19 Outcome	2019/20	2020/21 Revised	2021/22	2022/23 Medium-term estimates	2023/24
Division of available funds							
National departments	**592.6**	**634.3**	**749.7**	**806.7**	**718.7**	**732.7**	**736.9**
Provinces	**538.6**	**572.0**	**613.1**	**628.3**	**629.4**	**641.8**	**645.6**
Equitable share	441.3	470.3	505.6	520.7	514.0	522.0	523.1
Conditional grants	97.2	101.7	107.6	107.6	115.4	119.8	122.5
Local government	**111.1**	**118.5**	**123.3**	**139.9**	**138.7**	**146.5**	**149.1**
Equitable share	55.6	60.8	65.6	85.7	78.0	83.1	83.7
General fuel levy sharing with metropolitan municipalities	11.8	12.5	13.2	14.0	14.6	15.3	15.4
Conditional grants	43.7	45.3	44.5	40.2	46.1	48.0	50.0
Provisional allocations not assigned to votes	–	–	–	–	37.6	31.3	34.9
Projected underspending	–	–	–	-2.1	–	–	–
Total	**1 242.3**	**1 324.8**	**1 486.2**	**1 572.7**	**1 524.3**	**1 552.2**	**1 566.5**
Percentage shares							
National departments	47.7%	47.9%	50.4%	51.2%	48.3%	48.2%	48.1%
Provinces	43.4%	43.2%	41.3%	39.9%	42.3%	42.2%	42.1%
Local government	8.9%	8.9%	8.3%	8.9%	9.3%	9.6%	9.7%

Source: National Treasury

- Over the medium term, government proposes to allocate 48.2 per cent of available non-interest expenditure to national departments, 42.2 per cent to provinces and 9.6 per cent to local government.
- Over this period, national government resources decline at an annual average of 3 per cent, provincial resources increase by 0.9 per cent and local government resources increase by 2.1 per cent.

Financing and Debt Management Strategy

Table 3.8 National government gross borrowing requirement and financing

R billion	2019/20 Outcome	2020/21 Revised	2021/22	2022/23	2023/24
			Medium-term estimates		
Gross borrowing					
Main budget balance	**-345,1**	**-707,8**	**-537,4**	**-486,6**	**-437,5**
Redemptions	**-70,7**	**-66,9**	**-65,5**	**-150,6**	**-155,7**
Domestic long-term loans	-19,4	-52,5	-60,9	-134,2	-112,9
Foreign loans	-51,2	-14,4	-4,6	-16,4	-42,8
Total	**-415,8**	**-774,7**	**-602,9**	**-637,2**	**-593,2**
Financing					
Domestic short-term loans (net)	36,1	143,0	67,0	71,0	62,0
Domestic long-term loans	305,4	462,5	472,2	500,8	436,8
Foreign loans	76,1	121,4	49,4	49,3	66,6
Change in cash and other balances	-1,8	47,8	14,3	16,1	27,8
Total	**415,8**	**774,7**	**602,9**	**637,2**	**593,2**

Source: National Treasury

- The debt portfolio remains within all its strategic benchmarks
- Active debt management strategy has served to mitigate risks from elevated market volatility. Gross borrowing requirements are marginally lower than the estimate in the June SAB
- NT does not anticipate increasing auction levels in the current year

Risks to the fiscal outlook

The major short- to medium-term risks to the fiscal framework include:

- Uncertainty around the speed of the economic recovery – including the medium-term effects of the lockdown, both domestically and internationally. Globally, several developed economies have returned to strict lockdowns.
- Implementation risks for expenditure reductions, particularly on the wage bill. Both the upcoming decision on the final year of the current wage agreement and the upcoming wage talks pose significant risks to the expenditure ceiling.
- Additional spending pressures from state-owned companies. Several companies, including South African Airways, are insolvent and have insufficient funds to cover operational expenses.

Conclusion

- Government is committed to closing the budget deficit and stabilising the national debt-to-GDP ratio.
- A combination of expenditure and revenue measures will narrow the main budget deficit from 14.6 per cent of GDP in 2020/21 to 7.3 per cent by 2023/24. Gross national debt is projected to stabilise at 95.3 per cent of GDP by 2025/26.
- Achieving these targets will require large reductions in non-interest spending over the next three years. The majority of these reductions will be applied to the wage bill. Government will aim to protect funding for infrastructure investment.
- Fiscal consolidation will thus be growth-supporting, especially in the context of the President's Economic recovery plan
- To assist with the consolidation, government has projected tax increases of R5 billion in 2021/22, R10 billion in 2022/23, R10 billion in 2023/24 and R15 billion in 2024/25.
- Learning and culture receives the largest funding allocation, while economic development and community development are the fastest-growing functions.