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Overview of the 2004 Budget

Following a decade of structural economic change and comprehensive transformation of public services, the priority now is to accelerate the pace of growth and broaden the scope of development in the years ahead.

Reduced inflation and lower interest rates, well-diversified financial markets, healthy public finances and a favourable environment for trade and industrial development are established features of the South African economy. Improved economic performance over the next ten years will be built on four broad platforms:

- *A rising share of investment and saving out of national income, to provide the infrastructure and industrial capital formation required for sustained output growth*
- *Progress in the quality of education and promotion of training opportunities, to ensure that skills development and productivity enhancement contribute to expanding participation in social and economic development*
- *A poverty reduction strategy that includes promotion of work opportunities, creating sustainable communities and safe neighbourhoods and consolidation of the social security system*
- *Development of markets, support for emerging entrepreneurs, better governance and regulation of private and public sector institutions and rigorous monitoring and measurement of public service delivery.*

The 2004 Budget provides for strong real growth in investment spending, an expansion of labour-based public works programmes, further extension of the child support grant, phasing in of Aids treatment programmes, further extension of land restitution and land reform, stepped up assistance for municipal services and support for broad-based black economic empowerment.

The budget deficit is projected to rise to 3,1 per cent of GDP in 2004/05 before moderating to 2,8 per cent in 2006/07. National budget revenue remains about 24,7 per cent of GDP over the next three years and non-interest expenditure rises by 4,8 per cent a year in real terms over the next three years.

Reconstruction and development – ten years in review

South Africa embarked a decade ago on a comprehensive overhaul of its fragmented apparatus of governance and a restructuring of its divided and under-performing economy.

The RDP provided policies and programmes for the new Government

Guided by principles and priorities coalesced from an extensive process of public consultation, the Reconstruction and Development Programme provided an organising framework for the new Government in 1994. New policies and programmes were developed and new state structures were built across the entire spectrum of public endeavour.

Reprioritisation of expenditure was a key focus in the early years

Social change and development of South Africa's people had to be achieved within a sustainable and responsible fiscal trajectory. In the early years, this was achieved through centralised reprioritisation – setting aside a rising share of the existing resource envelope for RDP projects. The rationalisation and reorganisation of the public service, design of a new system of intergovernmental financial relations, restructuring of public assets and liabilities and development of monitoring and performance evaluation systems were also key priorities in the first phase of transformation.

Macroeconomic restructuring gained momentum in 1996

Greater impetus to economic restructuring began in 1996, with a macroeconomic strategy that emphasised improved industrial competitiveness, inflation reduction, gradual relaxation of exchange controls, strengthened funding of training, tax incentives to stimulate investment, deficit reduction and budget reform focused on the redistributive thrust of expenditure.

A more expansionary fiscal stance began in 2001

Having laid these secure foundations, a more expansionary fiscal policy stance could be adopted in 2001. Alongside this, the emphasis in economic policy has shifted to microeconomic and logistical reforms, encapsulated in the Microeconomic Reform Strategy, that underpin improved industrial performance and market development.

Accelerated growth and broad-based development are priorities for the decade ahead

For the decade ahead, an accelerated pace of growth and development must be achieved. Government's own assessment of progress made in the first decade of democracy – *Towards a Ten Year Review* – points to many achievements and strengths on which to build, but also emphasises the challenge ahead of overcoming the divisions between "two economies" in our developing nation.

Meeting basic needs

The Budget has provided for progressive meeting of social and economic rights

First amongst the principal aims of the Reconstruction and Development Programme was to meet the basic needs of all South Africans. Successive budgets have progressively extended the resource envelope devoted to services in poor communities.

- 1,6 million houses have been built
- 700 new primary health clinics have been constructed, 212 upgraded and 215 mobile clinics established
- Potable water supplies have been extended or improved for some 9 million people. 6,4 million people now benefit from new sanitation facilities
- Electricity has been connected to 4 million homes or institutions
- Rapid growth of mobile telephony has raised the proportion of households with telephones from 29 per cent in 1996 to 42 per cent in 2001; while Telkom has invested in over 150 000 new public

phones and connections to schools, police stations, clinics and hospitals
- Almost 3 million hectares of land has been redistributed, benefiting 700 000 households
- About 4,5 million children benefit from the Primary School Nutrition Programme
- The number of social grant beneficiaries has increased from 2,9 million to over 7,4 million, including recipients of the new child support grant.

Fight against poverty includes both job creation and social security

Yet vulnerability remains deep-rooted, reinforced by rising unemployment and the long shadows cast by social dislocation and exclusion in the past. The fight against poverty will continue, focused increasingly in the years ahead on creating work opportunities and building sustainable communities and safe residential neighbourhoods.

Building the economy

Growth performance improved significantly in the 1990s

Following a decade in which average growth fell to approximately 1 per cent a year and investment and productivity had steadily declined, the challenge of building a dynamic economy able to support rising living standards has been huge. Growth has averaged 2,8 per cent a year over the past decade, productivity has increased strongly and many industries have successfully adapted to international competition.

- Consumer inflation has averaged 7,3 per cent over the past 10 years, compared with 14,3 per cent over the previous decade
- Interest on public debt has fallen from 6,4 per cent of GDP in 1996 to 4,7 per cent in 2003
- Manufactured goods now comprise 38 per cent of exports, up from 25 per cent in 1994
- Private sector investment growth has averaged 5,4 per cent a year since 1993
- Public sector investment over the past decade has included R38 billion in ports, freight rail and air transport, R44 billion in electrical infrastructure. Total telephone fixed-line investment between 1998 and 2002 was R41,7 billion
- Restructuring of state enterprises has yielded R33,7 billion in proceeds, of which R24,8 billion has been paid to the fiscus
- South Africa's role as a financial centre for Africa has steadily grown, with assets in Africa up from R5,4 billion in 1994 to R26,8 billion in 2001.

More rapid investment is needed to underpin broad-based development

To accelerate the pace of economic growth, investment in infrastructure and improved maintenance of public assets remain critical challenges for the decade ahead – both to underpin industrial development and broad-based empowerment and to support social service delivery and renewal of residential environments.

Democratising the State and society

New institutions of governance contribute to democratisation

Construction of a vibrant democratic State, founded on the rule of law, has been an unparalleled success of the past decade. Key elements include:

- A clear Constitutional demarcation of functions and responsibilities of the national, provincial and local spheres of government, and the evolution of a complementary intergovernmental fiscal system
- Rationalisation of the local government sphere into 284 municipalities, with a strong emphasis on extending basic services to historically unserved communities
- Statutorily independent agencies with well-defined responsibilities – a Constitutional Court, the Public Protector, a Human Rights Commission, a Gender Commission, amongst others
- A National Economic Development and Labour Council, providing a forum for vigorous engagement between government and business, labour and community representatives.

A Social Compact could help shape the development strategy for future years

Building on the work of the Growth and Development Summit in 2003, *Towards a Ten Year Review* proposes that an "encompassing framework" that better integrates the activities of government and harnesses efforts of civil society would assist in creating lasting partnerships focused on long-term development goals.

Developing human resources

Education and training have grown substantially

Education, training and skills development are key foundations of social and economic progress, and preconditions for addressing inequality and division in society. Over the past decade:

- School education enrolment has grown from 10,5 million learners in 1994 to just under 12 million in 2002.
- 56 000 school classrooms have been constructed.
- The literacy rate of 15-24 year-olds has increased from 83 per cent to 96 per cent between 1996 and 2001.
- The National Qualifications Authority has been established, teacher education has been integrated into the higher education sector, and 152 technical colleges have been reorganised into fifty fully-fledged further education colleges.
- A skills development strategy has been launched, 25 sector education and training authorities (SETAs) established, 478 learnership programmes registered, 70 000 learners enrolled and an estimated 29 per cent of workers underwent training in 2002/03.
- Restructuring of higher education is under way, with a view to creating 21 consolidated institutions out of the former 36 universities and technikons.

Over the decade ahead, investment in the quality of education and promotion of work-related training opportunities will remain foremost priorities of Government.

2004 Budget highlights

On the economy

GDP growth was a disappointing 1,9 per cent in 2003, but is expected to strengthen to 2,9 per cent this year, rising to 3,6 per cent and 4,0 per cent in 2005 and 2006.

Consumer price inflation continued to decline during 2003, in part because further appreciation of the rand contributed to declining prices of imported goods. CPIX inflation is expected to average 4,8 per cent in 2004, well within the target range of 3-6 per cent.

The Reserve Bank's repo rate and prime lending rates were reduced by 5½ percentage points in 2003, bringing relief to consumers, lowering the costs of investment and signalling lower inflation expectations for the years ahead.

Gross fixed capital formation increased by 6,1 per cent in 2002 and 8,3 per cent in 2003, providing a foundation for stronger growth and productivity advances in future.

Export volumes have been sluggish in 2002 and 2003 and imports have grown strongly, leading to a moderate deficit on the current account balance in 2003 after a small surplus in 2002. Strong growth in both exports and imports is projected for the period ahead.

Substantial capital inflows have contributed to a marked strengthening of South Africa's overall foreign reserves, and the Reserve Bank's forward foreign exchange liabilities are now more than covered by net foreign reserves.

Building on the spirit of partnership underpinning the Growth and Development Summit Agreement and the Financial Sector Charter, signed in 2003, transformation and broad-based empowerment in the decade ahead will address human resource imbalances, broaden access to economic opportunities, accelerate investment and promote enterprise development – progressively overcoming the inequality and divisions that characterise South Africa's "two economies".

Tax proposals

Personal income taxes are cut, benefiting taxpayers by a total of R4 billion. People under 65 earning below R32 222 a year or over 65 and earning under R50 000 will not pay income tax next year.

Interest income exemption is raised to R11 000 for people under 65 and to R16 000 for senior citizens.

Transfer duty threshold is raised to R150 000. Stamp duties on mortgage loans are eliminated.

The general fuel levy on petrol goes up by 10c a litre, and the Road Accident Fund levy increases by 5c a litre. The diesel rebate for primary producers is increased by 15c a litre.

A packet of 20 cigarettes will cost 64 cents more, a 340ml can of beer 4 cents more, wine goes up 21 c and spirits 176 c per 750ml.

Ad valorem excise duties are eliminated on recorded music, some cosmetic products, print film, watches and clocks, printers and photocopying machines.

Main spending changes over the next three years

An additional R3,2 billion goes to provinces and municipalities for the Expanded Public Works Programme and infrastructure development.

R2,1 billion more for the HIV and Aids treatment programme.

R6 billion for broad-based Black Economic Empowerment Initiatives.

R2,2 billion more for municipal water, sanitation, electricity and refuse services.

Provinces get an additional R19,7 billion for social grants, schools, hospitals and clinic services.

R910 million more for the restructuring of universities and technikons.

R700 million more for land reform and R750 million for a new farmer support programme.

R1,9 billion more for more police personnel, vehicles and IT infrastructure in the fight against crime.

A further R475 million to improve the efficiency of the courts and to cater for vulnerable groups.

An additional R1,1 billion to Defence for peacekeeping operations in Burundi and the DRC.

R850 million more to Home Affairs to improve services to citizens, especially in rural areas.

Economic policy and outlook

International developments and the balance of payments

Global outlook is dominated by US economic growth

Global economic growth has strengthened over the past year and the outlook for 2004 is encouraging. Manufacturing activity is particularly robust in the United States, supported by dollar weakness, very low interest rates and rising military spending. Rapid growth in China continues, and the Japanese economy has showed more confident signs of recovery. However, the euro-zone region – South Africa's main trading partner – remains depressed.

US fiscal and current account deficits are source of volatility

Although continuing to drive global growth, the fiscal and current account deficits in the US economy represent huge global imbalances and have contributed to marked shifts in international capital flows, depreciation of the dollar and strengthening of the euro. Commodity prices have strengthened, and many emerging market economies have benefited from the resurgence of global growth and trade.

Marked appreciation of the rand in 2002 and 2003

Following its extraordinary weakness in late 2001, the rand strengthened in real terms by 29,8 per cent during 2002 and a further 19 per cent last year. The currency, alongside other commodity exporting currencies such as the Australian dollar, has appreciated particularly sharply against the dollar, in which much of South Africa's trade is denominated. It is clear that these global developments have impacted on growth over the past year, significantly affecting certain export industries. Exports have declined in volume terms over the past two years, while import volumes expanded by 3,1 per cent in 2002 and an estimated 8,3 per cent in 2003.

South Africa's policy focus is on long-run structural reforms

For the period ahead, the rand should return to somewhat more competitive levels as inflation differentials between South Africa and our major trading partners declines, and more balanced growth in trade is expected. However, uncertainty in the international growth outlook and considerable volatility in currency movements pose risks for both investors and established businesses. Against the short-term uncertainty of the international trading environment, South Africa's economic policy framework emphasises stability, gradual deepening of financial markets and broadening opportunities over the longer term.

Strong capital inflows in 2002 and 2003

The improvement in South Africa's overall balance of payments position over the past two years is an important source of strength for the period ahead. Net capital inflows (including unrecorded transactions) amounted to R33,4 billion in 2002 and R35,5 billion in the first three quarters of 2003.

Negative net open foreign position eliminated

Following more than twenty years of reliance on Reserve Bank intervention in the forward market to moderate swings in the exchange rate, at taxpayers' expense, the Bank's negative net open foreign position was finally eliminated in 2003, and a positive balance of US$4,0 billion was recorded as at 31 January 2004. Although official reserves remain low by international comparison, the rest of the financial sector had accumulated reserves of some US$16,9 billion (twice the level of official reserves) by 2003, and the foreign exchange and forward markets are now deep and well-developed. Further steps in the gradual liberalisation of exchange controls, which has made the evolution of these markets possible, are set out in Chapter 2 of this Review.

Output and investment trends

Output growth of 3,6 per cent in 2002 and 1,9 per cent in 2003

Following output growth of 3,6 per cent in 2002, preliminary estimates indicate growth of just under 2 per cent in 2003, decidedly lower than the 3,3 per cent projected at the time of the 2003 Budget. Agricultural production has declined sharply and may decline further in 2004 if the drought persists. Manufacturing also declined last year, but has shown promising signs of recovery in 2004. Mining output expanded strongly in 2003, particularly in platinum, diamonds and coal production, while the construction sector benefited from rising investment spending in both the public and private sectors.

Services comprise 65 per cent of GDP

The tertiary sector – wholesale and retail trade, catering and accommodation, transport and communication, financial and business services and community services – now comprise nearly 65 per cent of GDP. The services sector has grown steadily in recent years, particularly in telecommunications, transport and financial services. Tourism-related services came under pressure in the second half of 2003, although numbers of visitors have reportedly continued to grow.

Employment growth of 1,6 per cent a year, while real earnings increase by 2,8 per cent

Preliminary data suggest that employment continued to increase in 2003 at about the average rate of 1,6 per cent a year achieved since 1995, while average real earnings rose by 2,8 per cent between the first quarters of 2002 and 2003. The future effects of HIV and Aids on the labour market have come under close scrutiny over the past year. Treasury estimates indicate that successful implementation of a comprehensive HIV and Aids prevention and treatment programme will significantly reduce its costs and impact on business, in addition to broader social and health benefits.

Robust growth of investment in physical and human capital

Investment in both physical infrastructure and human resources has gained momentum over the past year. Gross fixed capital formation grew by 6,1 per cent in 2002 and 8,3 per cent in 2003, including expenditure on several major mining and industrial projects. Enrolment in higher education grew by about 3 per cent last year after two years of decline, and both expenditure and registration of learners by sector education and training authorities have expanded rapidly.

Growth and Development Summit provides a platform for improving economic performance

The Growth and Development Summit, held in June 2003, provided a special opportunity for business, labour, community and Government representatives to review critical policy considerations directed at improving the performance of the South African economy over the decade ahead. Key initiatives arising from the Summit include:

- Improving the regulatory environment to support business development and boost market efficiency
- Enhancing public infrastructure capacity – including enhancement of labour-based public works programmes – to meet both growth and social development objectives

- Expanding education and training programmes to underpin long-term job creation
- Deepening social security programmes to provide income support to the most vulnerable
- Supporting black economic empowerment initiatives to broaden access to economic activity and opportunity across the economy
- Strengthening partnerships at the sectoral level to encourage growth and job creation.

Inflation and interest rates

CPIX inflation will remain within target range in 2004

After averaging 9,3 per cent in 2002 following the depreciation of the rand, CPIX inflation averaged 6,8 per cent in 2003 and declined to 4,0 per cent over the year to December. Producer prices fell by 1,8 per cent over the year, with the imported component down by 8,2 per cent. Although this trend will reverse once the effect of the rand's appreciation wanes, consumer price inflation is expected to remain well within the target range of 3-6 per cent over the next three years.

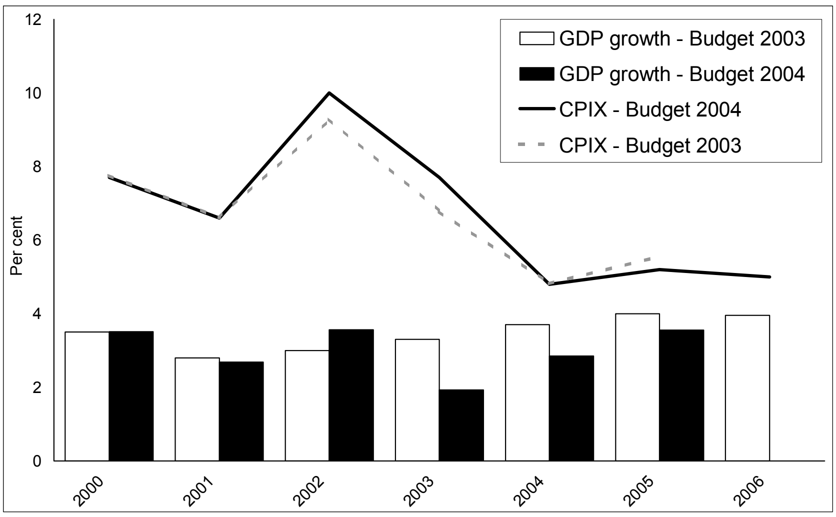
Lower interest rates improve growth prospects

Following increases of four percentage points in 2002, the Reserve Bank reduced the repo rate by 5½ percentage points during 2003. Lower interest rates have contributed to robust consumer spending in recent months, although household debt levels remain moderate, and underpin the prospects for sustaining the momentum of investment growth in the years ahead.

Modifications to inflation-targeting regime

A modification to the inflation targeting regime was announced in the Medium Term Budget Policy Statement in November 2003. The target range, formerly expressed as an annual average, is now a continuous target for the year-on-year rate of increase in CPIX. The range remains 3-6 per cent, until further notice.

Figure 1.1 GDP growth and CPIX inflation



Macroeconomic forecast

Growth expected to average 3,5 per cent over next three years

Economic growth of 2,9 per cent is projected for 2004, rising to 3,6 per cent and 4,0 per cent in 2005 and 2006. CPIX inflation is expected to average 4,8 per cent this year. For the fiscal year 2004/05, real GDP growth of 3,3 per cent is anticipated and CPIX inflation of 5,2 per cent. The outlook for the economy is summarised in table 1.1 and discussed in more detail in Chapter 2.

Table 1.1 Macroeconomic outlook – summary

	2003	2004	2005	2006
	Estimate		Forecast	
Real growth				
Household consumption	2,9%	3,4%	3,4%	3,8%
Capital formation	8,3%	6,6%	6,9%	7,3%
Exports	-2,4%	5,1%	6,2%	6,7%
Imports	8,2%	8,0%	5,9%	6,3%
Gross domestic product	**1,9%**	**2,9%**	**3,6%**	**4,0%**
Consumer price inflation (CPIX)	6,8%	4,8%	5,6%	5,0%
Balance of Payments current account (% of GDP)	-0,8%	-1,3%	-1,8%	-2,1%

Fiscal policy and budget framework

Strong spending growth projected and a stable tax burden

In keeping with the more expansionary fiscal policy stance introduced in 2001, the MTEF period ahead will see strong growth in social spending and infrastructure investment, a stable tax burden relative to GDP and declining debt service costs. The main budget deficit is expected to be 3,1 per cent of GDP in 2004/05, falling to 2,8 per cent by 2006/07.

Fiscal policy trends and targets

Fiscal consolidation allows focus on growth in the period ahead

Against the background of the fiscal consolidation achieved over the past decade – expenditure reprioritisation, a lower budget deficit, improved management of public debt, lower interest rates and a buoyant tax structure – the 2004 Budget aims to invigorate the recovery evident in the last quarter of 2003 while continuing to build firm foundations for long-run growth and development.

Infrastructure investment to gain further momentum

Declining expenditure on fixed capital by both general government and public enterprises has been a weakness in fiscal performance since 1994. However, a turnaround in public sector investment spending began in 2002 and will gain impetus in the years ahead as infrastructure budgets rise and delivery capacity improves. Public-private partnership projects are also now contributing significantly to capital formation and maintenance of public assets.

For the period ahead:

- General government capital formation is targeted to grow by 6 per cent a year

- Government consumption expenditure will stabilise at about 19 per cent of GDP, with growth mainly focused on non-wage spending
- Transfers to households, mainly social grants, are projected to rise from 3,2 per cent of GDP in 2001/02 to 4,8 per cent in 2006/07
- General government tax revenue will remain below 27 per cent of GDP while main budget revenue remains below 25 per cent
- Interest on public debt is expected to decline from 4,9 per cent of GDP in 2002 to 4,2 per cent in 2006.

Public sector borrowing requirement of 3,2 per cent of GDP in 2004/05

The public sector borrowing requirement, which takes into account borrowing by non-financial public enterprises, such as Eskom, Telkom and the Post Office, in addition to borrowing by national government, provinces and municipalities, is expected to increase from 0,6 per cent of GDP in 2002/03 to 3,2 per cent in 2004/05, before easing to 2,7 per cent in 2006/07. The increase in the public sector borrowing requirement takes account of increasing infrastructure investment by public enterprises.

Revised budget framework

Revenue estimates adjusted downwards for lower growth in 2003

Economic growth in 2003/04 has been slower than anticipated at the time of the 2003 Budget, leading to lower revenue flows than initially projected. For the MTEF period, revenue estimates are similarly adjusted down by comparison with the 2003 Budget estimates. However, expenditure on state debt is also adjusted downwards in the 2004 framework, due to both lower interest rates and lower inflation expectations. Main budget revenue is projected to be 24,6 per cent of GDP in 2003/04 and to remain at about this level over the next three years.

Table 1.2 The consolidated national budget framework

R billion	2003/04	2004/05	2005/06	2006/07
National Revenue Fund				
Revenue	**300,3**	**327,0**	**360,3**	**394,0**
Expenditure	**331,7**	**368,9**	**404,7**	**439,1**
Main budget deficit	**-31,4**	**-41,9**	**-44,4**	**-45,1**
Percentage of GDP	*-2,6%*	*-3,1%*	*-3,0%*	*-2,8%*
RDP Fund and foreign technical co-operation				
Revenue	1,6	1,5	1,5	1,5
Expenditure	1,0	1,3	1,3	1,3
Social security funds				
Revenue	12,6	13,9	15,3	16,8
Expenditure	8,9	11,1	12,2	13,2
Consolidated national budget				
Revenue	**314,5**	**342,4**	**377,1**	**412,2**
Percentage of GDP	*25,7%*	*25,7%*	*25,9%*	*25,9%*
Expenditure	**341,6**	**381,3**	**418,1**	**453,6**
Deficit	**-27,1**	**-38,9**	**-41,0**	**-41,3**
GDP	*1 223,2*	*1 331,8*	*1 455,6*	*1 592,6*

Budget deficit of 3,1 per cent in 2004/05

Taking into account the revised revenue estimate and provision for in-year adjustments to expenditure, the budget deficit for 2003/04 is expected to be 2,6 per cent of GDP, up from 1,1 per cent in 2002/03 and slightly higher than the 2,4 per cent estimate at the time of the 2003 Budget. The revised main budget framework provides for an increase in the deficit to 3,1 per cent of GDP in 2004/05.

Social security funds surpluses bring consolidated deficit down to 2,9 per cent of GDP

Table 1.2 shows the consolidated national budget for the period ahead, including the main budget, foreign development assistance and social security funds. Surpluses of the Unemployment Insurance Fund and the Compensation Funds bring the consolidated national deficit down to 2,9 per cent of GDP next year, falling to 2,6 per cent in 2006/07.

National budget spending of R369 billion in 2004/05

The main budget provides for expenditure of R368,9 billion in 2004/05, rising to R439,1 billion in 2006/07. Revenue increases from R327,0 billion to R394,0 billion over the same period.

Contingency reserve provides for drought relief, subsidisation of taxi replacement and critical infrastructure

As in the past, the budget includes an unallocated contingency reserve, rising from R2,5 billion next year to R8 billion in 2006/07. This allows for unforeseen expenditure in-year and new policy priorities in future years. Expenditure on drought relief, recapitalisation of the nation's minibus taxi fleet and further contributions to critical industrial infrastructure will be drawn from this reserve if required, and once operational business plans have been agreed.

Debt costs decline as per cent of GDP

The main budget medium term expenditure framework is outlined in table 1.3. Debt service costs are expected to fall from 3,9 per cent of GDP in 2003/04 to 3,6 per cent by 2006/07.

Table 1.3 Main budget expenditure framework, 2003/04 – 2006/07

R billion	2003/04	2004/05	2005/06	2006/07
Total expenditure	**331,7**	**368,9**	**404,7**	**439,1**
Less:				
Debt service costs	47,3	50,4	54,0	57,9
Contingency reserve	–	2,5	4,0	8,0
Total allocations	**284,4**	**316,0**	**346,7**	**373,1**
Percentage increase	*16,2%*	*11,1%*	*9,7%*	*7,6%*

National, provincial and local allocations of R316 billion in 2004/05

After setting aside provision for debt costs and the contingency reserve, the budget framework provides for an expenditure aggregate of R316,0 billion in 2004/05, rising to R373,1 billion in 2006/07, to be allocated between the national, provincial and local spheres in the 2004 *Division of Revenue Bill*.

Consolidated national and provincial expenditure

New economic classification illustrates growth in transfers to households, government agencies and businesses

The 2004 Budget introduces a new economic classification of expenditure, set out in more detail in table 3.9 and Annexure B. This breakdown of the consolidated expenditure of national and provincial government (including social security funds) illustrates the following trends:

- Real non-interest expenditure allocations grow by 4,2 per cent a year over the 2004 MTEF period

- Transfers to households and non-profit institutions grow by 7,3 per cent a year in real terms, reflecting the steady broadening of the social security system
- Transfers and subsidies to municipalities, government agencies, universities and technikons and business enterprises decrease from 21,0 per cent of non-interest expenditure in 2003/04 to 19,5 per cent in 2006/07
- Payments for capital assets rise by 6,1 per cent a year in real terms over the next three years.

Improved structure of wage and non-wage expenditure

Table 1.4 also illustrates an improving balance between compensation of employees and other current payments over the MTEF period, and the growth in non-interest expenditure accommodated in part by a declining burden of state debt costs.

Table 1.4 Consolidated expenditure – economic classification

R billion	2003/04 Revised estimate	2004/05	2005/06	2006/07
		Medium-term estimates		
Current payments	**167,9**	**184,2**	**197,9**	**211,3**
Compensation of employees	*120,9*	*131,7*	*140,0*	*147,9*
Other current payments	*47,0*	*52,5*	*57,9*	*63,4*
Transfers and subsidies	**120,8**	**131,6**	**147,6**	**159,6**
Other government entities	*55,3*	*59,4*	*65,1*	*68,1*
Business enterprises	*9,4*	*9,5*	*10,2*	*11,0*
Households and non-profit institutions	*56,1*	*62,7*	*72,3*	*80,5*
Payments for capital assets	**15,5**	**17,6**	**19,9**	**21,5**
Unallocated	–	2,5	4,0	8,0
Consolidated non-interest expenditure	**304,1**	**335,8**	**369,4**	**400,4**
Percentage increase	*15,4%*	*10,4%*	*10,0%*	*8,4%*

Procurement reform and public-private partnerships

Chapter 3 provides brief accounts of current procurement reform initiatives, developments in public-private partnerships (PPPs), the role of government in promoting black economic empowerment and progress in infrastructure investment over the past 10 years.

Supply Chain Management framework introduced

A new framework for Supply Chain Management in the public sector has been introduced, through regulations issued in December 2003. Responsibility for procurement and management of supplies will in due course be fully devolved to accounting officers, and the State Tender Board will fall away.

Preferential Procurement Act to be amended

During 2004 the Preferential Procurement Policy Framework Act and its regulations will be overhauled, to improve alignment with the Broad-based Black Economic Empowerment Act.

Standardised Provisions and draft BEE Code for PPPs published

Procurement and contract management in terms of the regulations governing PPPs can now take advantage of a detailed compilation of Standardized Provisions, drawing on international best practice and providing benchmark language and templates for the various elements in typical PPP project designs, feasibility assessments and contract documentation. In addition, a draft Code of Good Practice for Black Economic Empowerment in PPPs was released in January 2004, giving direction to this important aspect of project design and evaluation.

Revenue

2003/04 revenue expected to be R4,2 billion lower than budget estimate

In contrast to the buoyant revenue outcomes recorded over the past five years, the revised estimate of main budget revenue for 2003/04 of R300,3 billion is R4,2 billion less than the 2003 Budget estimate. The shortfall is mainly attributable to lower company profits and lower customs receipts than anticipated, in a context of a slowdown in economic growth. As a result of substantial PIT relief over the years, company taxes have grown as a proportion of revenue. While this is a positive development, a negative consequence of this is the increased responsiveness of tax revenue to the business cycle.

SACU payments will increase by R3,6 billion in 2004/05

Although economic performance is expected to rebound in 2004 and beyond, the revised revenue projections leave little room for tax relief this year. Provision has also to be made for a R3,6 billion increase in payments to SA Customs Union partners in 2004/05, as the new revenue sharing formula has not yet been introduced.

The 2004 Budget proposals contain a moderate easing of the tax burden on income together with a somewhat higher tax incidence on tobacco products, alcoholic beverages and fuels.

Tax proposals

Tax proposals include further income tax relief, and higher duties on alcohol and tobacco products

The main tax proposals this year are as follows:

- R4 billion in personal income tax relief
- Provision for broad-based tax-free share transfers to employees
- Tax relief for expenses incurred on government-owned infrastructure projects
- Removal of stamp duty on mortgage bonds and negotiable certificates of deposit
- Interest income exemption raised to R11 000 for taxpayers under age 65 and R16 000 for senior citizens
- Increase in the transfer duty threshold to R150 000
- Removal of *ad valorem* duties on printers, recorded music and some cosmetic products
- Increase in the diesel rebate for primary producers by 15c a litre
- Excise duty increases of 4c per 340ml can of beer, 21c per 750ml bottle of wine, R1,76 per 750ml bottle of spirits and 64c for a packet of 20 cigarettes
- Increases in the general fuel levy by 10c a litre on petrol and diesel, and a 5c a litre increase in the Road Accident Fund levy.

Measures to counter tax avoidance planned

As in past years, various anti-avoidance measures to protect the tax-base will also be introduced in this year's tax legislation.

Table 1.5 summarises the expected 2003/04 main budget revenue outcome and the effects in the year ahead of the tax proposals.

Table 1.5 Summary of tax proposals

R billion	2003/04 Budget estimate	2003/04 Revised estimate	2004/05 Budget estimate	
Tax revenue (gross)	310,0	303,3		336,0
Non-tax revenue	4,2	6,7		6,6
Less: SACU payments	-9,7	-9,7		-13,3
Total revenue	**304,5**	**300,3**		
Revenue before tax proposals				**329,3**
Personal income tax relief			-4,0	
Interest and dividend exemption			-0,1	
Changes to transfer and stamp duties			-0,4	
Alcohol and tobacco excises			1,5	
Increase in fuel levy			0,9	
Removal of duties on printers, recorded music and cosmetics			-0,2	
Tax proposals				**-2,3**
Revenue after tax proposals				**327,0**

Tax administration

Administrative reforms to simplify tax returns

The South African Revenue Service also proposes to introduce simplified individual income tax returns, a single business registration number, procedures for advance rulings on potentially contentious tax questions, an electronic alternative for ensuring compliance with stamp duty requirements and more effective enforcement of taxes associated with property transactions, particularly where ownership changes hands between foreign parties. The SARS Corporate Office will be established during the year ahead, and a transformation of customs administration is in progress.

Asset and liability management

Debt strategy and market developments

Debt management aims to reduce debt costs within acceptable risk limits

In line with the debt management objective of reducing debt service costs subject to acceptable levels of risk, the past year has seen a diversified issuance of inflation-linked, variable rate and fixed income bonds. Now that the negative net open foreign position of the Reserve Bank has been eliminated, foreign debt management will mainly focus on refinancing of maturing foreign loans.

Turnover of R10,7 trillion on the SA bond market

Turnover on the South African bond market was R10,7 trillion in 2003 and yields continued to improve. The net supply of corporate and parastatal bonds increased by almost R36 billion last year. By the end of December 2003, benchmark government bond yields had declined to historically low levels across the yield curve. The real yield on the inflation-linked R189 (maturing in 2013) was 3,96 per cent at the end of 2003.

Euro bond issued in May 2003

South Africa's foreign bonds have continued to trade at highly competitive rates, benefiting from prudent macroeconomic policies and low interest rates in the US, Europe and Japan. In May 2003, Government issued a Euro 1,25 billion 10-year global bond maturing in 2013 at 142 basis points above the equivalent German bond.

Upgrading credit ratings

South Africa's sovereign credit ratings were upgraded by several rating agencies in 2003, contributing to the sound reputation of South Africa's foreign and domestic debt issues amongst international investors.

Borrowing requirements, debt costs and total debt trends

Chapter 5 sets out details of Government's borrowing requirements, financing proposals and anticipated trends in total debt and state debt costs.

Extraordinary payments of R14 billion to SARB over next two years

In addition to financing the budget deficit, provision is made for a further R14 billion in extraordinary payments over the next two years to compensate for forward cover losses incurred on the Gold and Foreign Exchange Contingency Reserve Account.

Net borrowing requirement of R46,2 billion next year

Taking into account budget requirements and extraordinary transactions, a net borrowing requirement of R46,2 billion is anticipated in 2004/05, compared with a revised amount of R37,9 billion in 2003/04. Next year's financing requirement will be met through an increase of R6 billion in domestic short-term loans, a projected R34,3 billion to be raised through net domestic bond issues and R5,9 billion to be raised through foreign loans. Table 1.6 summarises the projected trend in total debt and state debt costs.

Table 1.6 Projected state debt and debt cost, 2003/04 – 2006/07

R billion	2003/04	2004/05	2005/06	2006/07
Net loan debt (end of year)	**450,0**	**506,3**	**564,7**	**620,9**
Percentage of GDP	*36,8%*	*38,0%*	*38,8%*	*39,0%*
Net domestic debt	378,9	423,0	466,1	511,4
Foreign debt	71,1	83,3	98,6	109,5
State debt cost	**47,3**	**50,4**	**54,0**	**57,9**
Percentage of expenditure	*14,3%*	*13,7%*	*13,3%*	*13,2%*
Percentage of GDP	*3,9%*	*3,8%*	*3,7%*	*3,6%*

State debt costs continue to decline as percentage of GDP

Government net loan debt is projected to rise from 36,8 per cent of GDP at the end of March 2004 to 39,0 per cent by the end of 2006/07. However, state debt costs decline steadily relative to GDP and as a share of national expenditure, as maturing debt is replaced with lower-yield bonds.

Contingent liabilities

Guarantees of R7,7 billion issued in 2003/04

In addition to its debt obligations, Government has various liabilities that are uncertain or contingent on future eventualities. Total outstanding guarantee commitments amounted to R70,7 billion at the end of March 2003, down from R84,2 billion at the end of the previous year. During 2003/04, guarantees of R7,7 billion were provided to public entities, of which R7,0 billion is accounted for by shareholder's assurances provided to Transnet for SAA. Unfunded contingent obligations include an estimated R23,8 billion accrued liability of the Road Accident Fund.

Public enterprise restructuring and corporate governance

Telkom IPO raised R4,2 billion

The initial public offering of shares in Telkom in March 2003 raised an amount of R4,2 billion for the fiscus, and an amount of R2,2 billion was received from the Central Energy Fund in 2002/03. Restructuring initiatives have not yielded significant proceeds for the fiscus over the past year, but progress has been made in forestry restructuring and the disposal of Aventura resorts.

Dividend receipts of R1,2 billion

Dividends amounting to R1,2 billion were paid to the Government by state owned entities in 2003/04, compared with an amount of R1,0 billion in 2002/03. Eskom, the Central Energy Fund and the Airports Company of SA account for 91 per cent of dividend receipts.

Treasury operations of parastatals under scrutiny

The treasury operations of state owned entities are currently under review, with a view to ensuring that appropriate risk management policies and sound governance over financial assets and liabilities are in place.

Medium term expenditure estimates

Policy priorities and the MTEF

Balanced consideration of policy priorities in the MTEF

The underlying objectives of the medium term expenditure framework remain broad-based growth and development and the progressive realisation of the social and economic rights of South Africa's people. In preparing the annual budget, Government seeks to balance competing policy considerations – investment and job creation, poverty relief and social development, upgrading residential neighbourhoods, promoting the rule of law, development and peace in the African continent.

The budget framework builds on progress since 1994

Drawing on *Towards a Ten Year Review* – Government's assessment of progress over the past decade and challenges for the years ahead – the 2004 Budget builds on the foundations laid in the implementation of the Reconstruction and Development Programme, while setting a course for accelerated growth and broad-based development over the decade ahead.

Economic priorities include investment, skills development and BEE

Key priorities for the *Economic and Investment cluster* include enhancing the efficiency of the nation's transport and logistics infrastructure, marketing South Africa as a tourism and investment destination and as a financial centre for Africa, extending skills development and training opportunities, land reform and agricultural development, broadening black economic empowerment and deepening research and technology development.

The *Social Services cluster* has responsibility for the expanded public works programme, consolidating the delivery of social grants, addressing HIV and Aids, restructuring the higher education system and sustainable housing and community development.

Expanded employment programmes contribute to social development

Under the auspices of *Governance and Administration,* the State's service delivery and regulatory capacity needs to be enhanced, civic administration by the Department of Home Affairs has to be upgraded, municipal administration put on a sound footing and partnerships between government and civil society secured.

Improved governance includes service delivery and regulatory capacity building

Priorities of the *Justice, Crime Prevention and Security cluster* include expanding and deepening the skills base of the Police Service, implementing integrated justice sector information systems, promoting social crime prevention programmes, rehabilitation of offenders and reinforcing the rule of law.

SAPS employment to increase, and improved criminal justice IT systems

In pursuit of NEPAD's "core human values", the *International Relations, Peace and Security cluster* contributes to several peace-keeping operations abroad, promotes multilateralism at regional, continental and global levels, plays an active part in building the African Union and seeks to accelerate regional cooperation in transport, energy, communications, environmental development and other areas of mutual advantage.

International priorities include peace-keeping and regional investment promotion

Additional expenditure allocations

In preparing the national budget, the previous year's forward estimates together with a 6 per cent increase for the outer year serve as "baseline allocations". The 2004 Budget provides for additional allocations of R44,5 billion over the next three years, of which R26,3 billion goes to provinces and R3,9 billion to local government.

Additional allocations of R45 billion over the MTEF

Table 1.7 summarises the division of main budget allocations between national, provincial and local government. As percentages of the total, the provincial and local shares rise to 58,0 per cent and 4,6 per cent respectively by 2006/07.

Rising provincial and local shares in the division of revenue

Table 1.7 Division of revenue, 2003/04 – 2006/07

R billion	2003/04	2004/05	2005/06	2006/07
National allocations	110,5	120,6	131,0	139,7
Provincial allocations	161,5	181,1	199,7	216,3
Equitable share	*144,7*	*160,0*	*173,9*	*186,4*
Conditional grants	*16,7*	*21,2*	*25,9*	*30,0*
Local government allocations	12,4	14,2	15,9	17,1
Total allocations	**284,4**	**316,0**	**346,7**	**373,1**
Changes to baseline				
National allocations	1,9	3,2	5,0	6,0
Provincial allocations	2,5	5,5	7,9	13,0
Equitable share	*2,4*	*4,7*	*6,3*	*8,8*
Conditional grants	*0,1*	*0,8*	*1,6*	*4,2*
Local government allocations	–	1,0	1,3	1,6
Total	**4,4**	**9,7**	**14,1**	**20,6**

Increased spending focused on job creation, social services, Aids treatment, social grants and local development programmes

Significant additions to MTEF spending plans include the following:

- R1,5 billion more for provincial infrastructure grants and R1,7 billion more for municipal infrastructure, partially earmarked for labour-based public works programmes
- R19,7 billion more for provincial equitable share allocations, providing for growth in social grant programmes and quality improvements in health services and education, including targeted allocations for poor schools
- R2,1 billion for the enhanced response to HIV and Aids, mainly to finance antiretroviral treatment programmes
- A further R3,3 billion for the child support extension grant, to complete the phasing on of qualifying children under the age of 14
- R778 million earmarked for free basic services and R2,2 billion more for the local government equitable share, further supporting community development initiatives
- R700 million more for land restitution and land reform, and R750 million for a new grant for agricultural support to beneficiaries of land reform programmes
- R1,9 billion to reinforce and expand the SA Police Service, and R475 million to streamline the justice process
- R850 million to improve the quality of Home Affairs services, particularly in rural areas
- R1,1 billion to support peacekeeping operations in Africa, and R427 million to enhance diplomatic representation abroad.

Poverty relief allocations become part of departmental budgets

With effect from next year, the special poverty relief allocations introduced in 1997/98 will be integrated into normal departmental budgets. Continuing programmes, amounting to R1,7 billion in 2004/05, now form part of the Expanded Public Works Programme.

Consolidated expenditure by function

The MTEF comprises the consolidated spending of national and provincial government over the next three years, including donor grants and the social security funds. Table 1.8 sets out projections of consolidated expenditure by function in 2003/04 and 2004/05, and anticipated growth over the MTEF period.

Consolidated expenditure growth of 6,7 per cent since 2000/01

Consolidated non-interest expenditure expanded by 6,7 per cent a year between 2000/01 and 2003/04 in real terms, and continues to increase (before taking into account the unallocated contingency reserve) by an average 3,3 per cent a year over the MTEF period ahead.

Table 1.8 Consolidated expenditure growth

R billion	2003/04 Revised estimate	2004/05 Budget estimate	% Average growth 2003/04–2006/07
Education	69,8	75,9	7,2%
Health	39,7	42,6	8,4%
Welfare and social security	51,5	59,9	13,6%
Housing and other social services	16,3	18,3	8,3%
Police, prisons and courts	36,0	40,2	9,0%
Defence & intelligence	22,4	23,1	4,3%
Economic services	45,0	49,4	9,9%
General administration	23,5	24,0	5,9%
Non-interest expenditure	**304,1**	**333,3**	**8,9%**
State debt cost	47,3	50,4	7,0%
Unallocated	–	2,5	–
Total expenditure	**351,5**	**386,3**	**9,3%**

Social services account for 59 per cent of non-interest spending

Education, health, welfare and other social services take up 59,0 per cent of non-interest allocations in 2004/05. Social security and welfare services grow rapidly in the years ahead, both as a result of the phasing in of the child support grant and because of growing numbers of disability grant beneficiaries.

Improved courts and expansion of police service

Police, prisons and courts expenditure take up 12,0 per cent of the total currently, up from 11,5 per cent 10 years ago. Growth in the criminal justice sector is mainly for improved court administration and expansion of the Police Service. Defence and intelligence spending has declined from 10,5 per cent of non-interest expenditure in 1994/95 to 6,9 per cent next year, and is set to decline further over the MTEF period ahead as outlays on the special defence procurement programme decline after 2005/06.

Land reform, agricultural development and investment in infrastructure to increase

Economic services have remained about 15 per cent of non-interest expenditure over the past decade. Investment in water schemes, transport services and communication have grown strongly, accommodated in part by the phasing out of the general export incentive scheme in the 1990s. For the period ahead, spending on land reform, agricultural support and investment in industrial infrastructure will increase rapidly.

Provincial and local government finance

Government prioritises provincial and municipal functions

The rising shares of the overall national budget allocated to provinces and municipalities over the MTEF period ahead reflect the priority of social services, local development and upgrading of residential neighbourhoods in Government's planning for the decade ahead.

Provincial grants and spending trends

Provincial treasuries are in sound position

Provinces rely largely on transfers from the national fiscus to finance their spending responsibilities, but also raised revenue from fees, licences and other charges amounting to about R6,0 billion in 2003/04. Conditional grants to provinces increase strongly in the 2004 Budget, mainly because of increases in the child support extension grant, HIV and Aids grants and infrastructure allocations.

A breakdown of transfers to provinces in 2004/05 is set out in table 1.9.

Equitable share formula accounts for main provincial allocations

The equitable share makes up 88,3 per cent of transfers to provinces and grows by 8,8 per cent a year over the MTEF period. It is distributed between provinces on the basis of a redistributive formula with seven components, explained in some detail in chapter 7 and in Annexure E. The equitable share formula has been revised this year to take account of new demographic, education and economic data, and a more comprehensive review will be undertaken with a view to implementation in 2005.

Table 1.9 Transfers to provinces, 2004/05

R billion	Equitable share	Conditional grants				Total
		Health	Housing	Social Develop-ment	Other[1]	
Eastern Cape	27,0	0,6	0,6	1,0	0,9	30,1
Free State	10,6	0,6	0,4	0,3	0,3	12,2
Gauteng	24,5	2,6	1,1	0,3	0,5	29,0
KwaZulu-Natal	33,1	1,2	0,8	0,9	1,0	36,9
Limpopo	21,8	0,3	0,4	0,6	0,8	24,0
Mpumalanga	11,6	0,2	0,3	0,3	0,4	12,8
Northern Cape	3,8	0,2	0,1	0,1	0,2	4,4
North West	13,3	0,3	0,4	0,5	0,4	14,9
Western Cape	14,3	1,6	0,5	0,2	0,3	16,9
Total	**160,0**	**7,7**	**4,6**	**4,1**	**4,8**	**181,1**

1. Includes grants in the national departments of Agriculture, Education, Provincial and Local Government, Sport and Recreation South Africa and National Treasury.

Health grants are increased to accommodate Aids treatment programmes

Grants administered by the national Department of Health remain the largest provincial transfer programmes outside of the equitable share. The grants compensating provinces for the costs of major tertiary hospital services and professional training have been reconfigured this year. Allocations for hospital rebuilding, equipment and revitalisation receive further increases. A total of R1,9 billion is added to the Health HIV and Aids grant over the MTEF period to support the comprehensive response to HIV and Aids, including the roll-out of antiretroviral treatment programmes.

Shift of school nutrition programme to education departments

Responsibility for the primary school nutrition programme, which receives R832 million in 2004/05, shifts from Health to Education departments next year. The education financial management and quality enhancement grant has been terminated and the funds incorporated into the provincial equitable share.

Infrastructure grants to support labour-intensive projects and agriculture

The provincial infrastructure grant is increased by R1,5 billion over the next three years. It will contribute to expanding spending on labour-intensive projects, and will also provide support for agricultural development initiatives. A new grant to support implementation of the Comprehensive Farmer Support Programme receives R750 million over the MTEF period, enabling provinces to enhance their assistance to emerging farmers.

Increased allocations for child support grants

The child support extension grant administered by the national Department of Social Development will increase sharply over the period ahead to accommodate the phasing in of children up to the age of 14 in 2005/06. In addition, R1,2 billion is set aside for emergency food relief over the next three years, as part of the broadening of Government's approach to income security and poverty relief.

Social grants and infrastructure spending to grow strongly

Preliminary estimates of the functional and economic breakdown of provincial spending for the years ahead are set out in chapter 7. The strongest growth is in social grants payments to households, and in capital expenditure on social and economic infrastructure.

Local government finance

Transformation of the municipal landscape provides a foundation for improving service delivery

Municipalities have undergone a thorough transformation over the past decade – amalgamation of previously segregated authorities, repeal of archaic legislation and rationalisation of the number and structure of local governments. National government transfers to municipalities supplement their own revenue to enable them to fulfil their developmental roles. Key priorities for the years ahead include expansion and provision of free basic services, acceleration of infrastructure delivery to poor households, extension of services to areas not presently served, creation of jobs through the expanded public works programme and enhancing capacity through legislative and financial management reforms.

Growth in transfers to local government to meet basic household needs

National budget transfers to local government make up about 14,4 per cent of total local government revenue. Transfers will increase by 11,3 per cent a year over the MTEF period, and include additional allocations amounting to R3,9 billion.

Consolidation of infrastructure grants allocated by formula

A significant step forward this year is the consolidation of the Municipal Infrastructure Grant, which receives R1,7 billion in additional funding. Allocations are formula-based, using poverty-weighted criteria, providing greater certainty to municipalities and enhancing forward planning. Municipalities will be required to apply labour-intensive methods for identified categories of expenditure, under the guidance of the national Department of Public Works.

Enhancement of the local government equitable share

A further R2,2 billion over the next three years goes to the local government equitable share, which contribute to free basic electricity, water and sanitation services for poor households. No major changes to the equitable share distribution formula take effect this year, but its funding has also been supplemented by capping the capacity building grants at R400 million a year from 2005/06, with the balance shifted to the equitable share.

Improved capital spending in future years

Chapter 7 includes a summary of the structure and trends of municipal budgets, illustrating the growth in operating costs since 1996/97 and relative decline in capital expenditure. Current initiatives to consolidate infrastructure grants and strengthen investment in infrastructure serving poor communities should contribute to an improved pattern of municipal spending in the years ahead.

Budget priorities – past, present and future

General government expenditure trends

Long-run spending trends are shaped by policy priorities

Budgetary reprioritisation, improved quality of expenditure management and new directions in public policy take many years to influence service delivery and social development fully. Long-run trends in public spending are accordingly an important index not just of shifts in past budgets but also of public service capacity and challenges for the years ahead.

Table 1.10 Consolidated general government spending by function, 1982/83, 1992/93 and 2002/03

R million	1982/83[1]	1992/93[2]	2002/03[3]	Average annual real growth 1982/83–1992/93	Average annual real growth 1992/93–2002/03
Protection Services	**4 819**	**22 451**	**58 132**	**1,9%**	**1,9%**
Defence and intelligence	3 477	10 729	20 772	-2,2%	-1,1%
Police	897	8 576	24 928	9,5%	3,1%
Prisons	276	1 968	7 458	6,3%	5,8%
Justice	169	1 178	4 975	6,1%	7,0%
Social Services	**9 501**	**56 821**	**181 764**	**4,5%**	**4,0%**
Education	4 349	27 154	68 686	4,9%	1,6%
Health	2 394	12 487	40 828	3,1%	4,3%
Welfare (incl. social security)	1 511	11 222	46 704	6,8%	6,8%
Housing	179	1 656	9 467	9,1%	10,3%
Community development	1 068	4 302	16 078	0,4%	5,7%
Economic Services	**4 664**	**17 141**	**45 130**	**-0,5%**	**2,0%**
Water schemes, related services	357	847	4 445	-4,8%	9,3%
Fuel and energy	37	653	2 588	16,4%	6,3%
Transport and communication	2 482	7 054	22 009	-3,0%	3,8%
Other economic services	1 788	8 587	16 088	2,2%	-1,4%
General government services and unallocable expenditure	**2 384**	**12 977**	**35 021**	**3,5%**	**2,3%**
Interest	3 168	18 687	49 012	4,3%	2,0%
Consolidated expenditure	**24 536**	**128 077**	**369 059**	**3,1%**	**3,0%**
Non-interest expenditure	**21 368**	**109 390**	**320 047**	**2,9%**	**3,1%**

1. *Source: Statistics South Africa, Statistical Release P9119.*
2. *Source: Statistics South Africa, Statistical Release P9119, adjusted for extraordinary payments towards drought relief and the Central Energy Fund.*
3. *Consolidated national, provincial and social security funds, plus estimated expenditure of local government and extra-budgetary institutions.*

Health, social security, housing and water services have been fastest growing functions

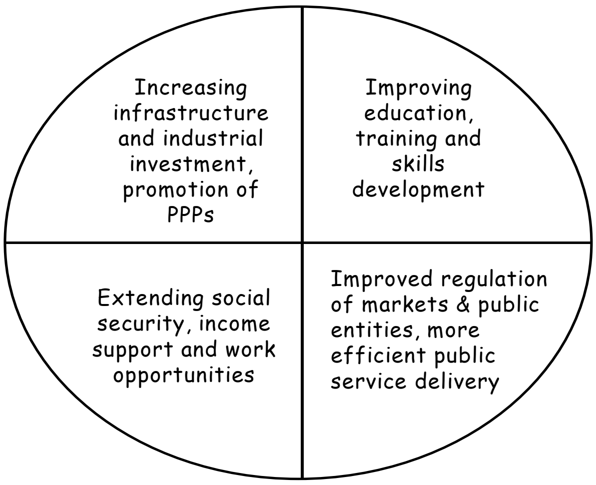
Table 1.10 illustrates the trends between 1982/83 and 1992/93, and 1992/93 and 2002/03, in the functional breakdown of consolidated expenditure of general government – including municipalities, extra-budgetary accounts, agencies and funds and universities and technikons. Strong growth in justice, health, social security and welfare spending is evident, as is the rapid expansion of housing and water services. Defence expenditure has steadily declined in real terms, and subsidies to agriculture and industry (included in other economic services) have also fallen sharply.

Policy priorities for 2004 and beyond

Budget Review aims to encourage debate on public priorities

The budget framework and spending plans explained in more detail in later chapters of this Review provide for an acceleration of public spending on services in the years ahead, and several further shifts in priority and emphasis. The 2004 Budget draws strongly on the priorities and programmes of earlier budgets, emphasising the consolidation and reinforcement of the reconstruction and development initiatives that are under way.

Figure 1.2 Policy priorities for the decade ahead



A better balance between social security and education spending needs to be sought

This year's Budget has also drawn on Government's assessment of progress and challenges for the years ahead, *Towards a Ten Year Review.* While further work is needed on specific policy options, plans, sequencing and financial implications, the main elements of a longer term development strategy are readily apparent. Government recognises, for example, that a more appropriate balance needs to be struck between the quantum of social security spending and that of education and infrastructure development. There are several clear threads that run through the framework outlined in the rest of this Review. Improved economic performance over the next ten years calls for sustained progress on several fronts:

- A rising share of investment and saving out of national income, to provide the infrastructure and industrial capital formation required for sustained output growth.
- Improvements in the quality of education and promotion of training opportunities, to ensure that skills development and productivity enhancement contribute to expanding participation in social and economic development.

- A poverty reduction strategy that includes promotion of work opportunities, creating sustainable communities and safe neighbourhoods and consolidation of the social security system.
- Development of markets, support for emerging entrepreneurs, better governance and regulation of private and public sector institutions and rigorous monitoring and measurement of public service delivery.

Budget documentation

The Review provides background to the Minister's presentation to Parliament

The *Budget Review* aims to explain current trends, and inform future debate, on the links between public policy priorities and South Africa's public finances. It accompanies the presentation to Parliament of the annual *Budget Speech* by the Minister of Finance. It provides an overview of the economic outlook, fiscal policy, revenue and expenditure plans, financing and developments in the public finances.

Annexures to the *Review* include a glossary of economic and financial terms, a statistical appendix, details of the tax proposals, an explanatory memorandum on the division of revenue and a concise summary of the budget proposals.

The national, provincial and local shares are set out in the Division of Revenue Bill

At the time of the Budget, the Minister of Finance tables the *Division of Revenue Bill* and an *Appropriation Bill* in the National Assembly, through which the executive seeks Parliamentary authority for its spending plans for the forthcoming year.

A new economic classification format is introduced in this year's budget

The *Estimates of National Expenditure* elaborate on the national spending plans, detailing the objectives of each Government department, three-year spending estimates, programmes, outputs and a set of service delivery indicators. The *Estimates* include "measurable objectives" for the main divisions, or programmes, of each budget vote. This year a new economic classification of expenditure is introduced, providing a more rigorous categorisation of current payments, transfers to other spheres of government, public entities, businesses or households, and of payments for capital assets.

In addition, the *Estimate of Revenue for the year ending 31 March 2005* sets out revenue projections before and after tax proposals, and a *People's Guide* provides a straightforward summary of budget highlights, published in five official languages.