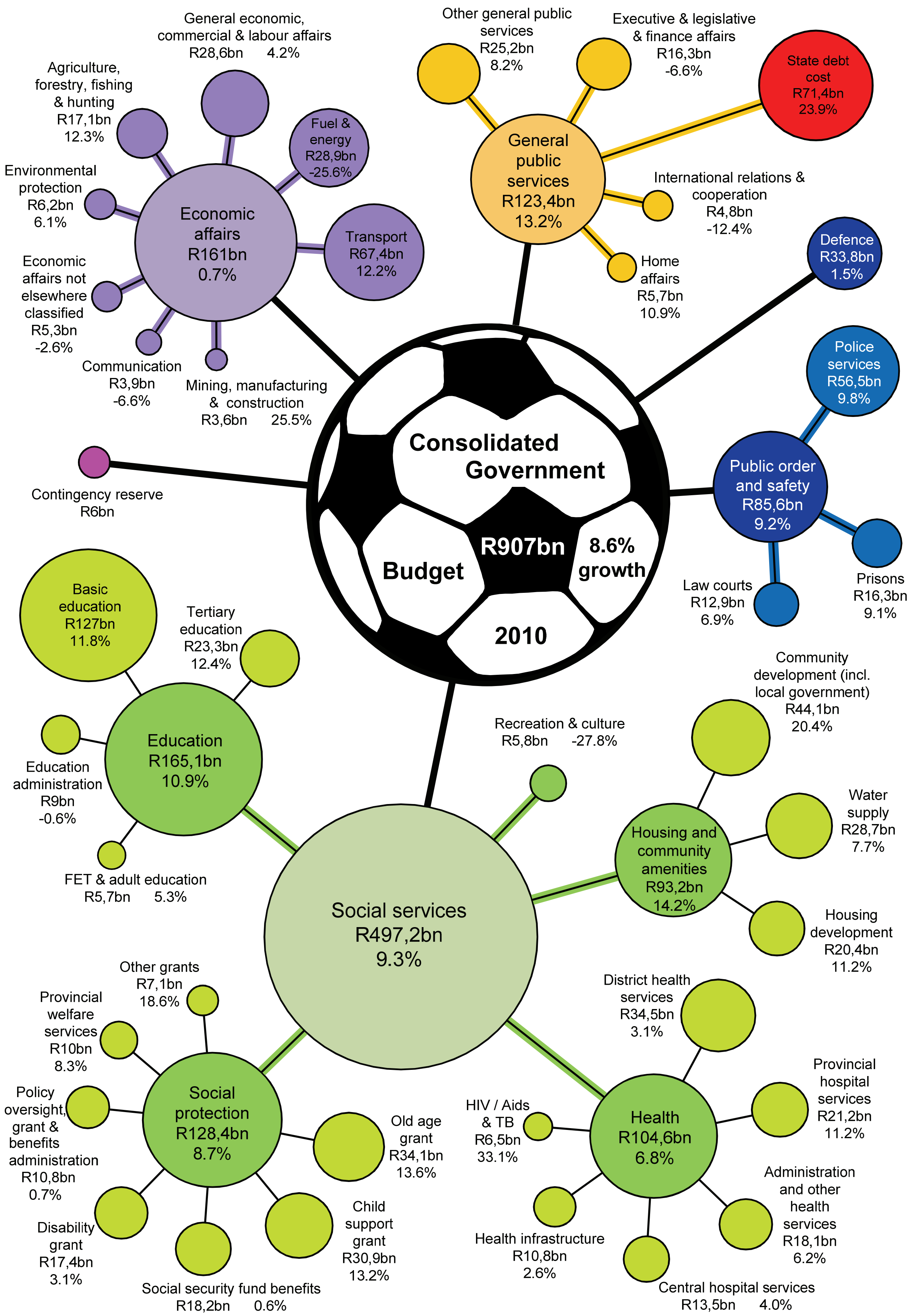


Note: Consolidated government expenditure in R billion, percentages reflect growth relative to 2009/10 estimated outcome.

1

Transforming the South African economy

- The global storm has subsided, and the South African economy is on the path to recovery. Sound macroeconomic and fiscal policies ensured that we were well prepared when the storm broke, and these policies will be maintained.
- Yet South Africa's chronic development challenges extend beyond the ups and downs of the business cycle. Tackling high unemployment and persistent poverty requires urgent measures in the short term, and a well-focused strategy to create jobs, promote economic growth and build a more efficient public sector over the longer term.
- The 2010 Budget lays the basis for doing things differently, setting out core elements of a new path for the economy and the public finances. These proposals focus on the need to expand job creation, bring down the budget deficit gradually, reprioritise resources, improve the quality and efficiency of public spending, and tackle corruption decisively. Microeconomic and financial regulatory reforms are also addressed.

Introduction

The budget is tabled in a new global environment that informs policy development in South Africa

The 2010 Budget is tabled in the context of immense change. The global economic crisis has demonstrated that the old patterns of growth, income distribution, regulation and governance do not meet the needs of the world economy. The growing weight of China and India in international trade signals a change in the global economic balance.

These considerations are informing policy development and new approaches in South Africa. There is renewed determination in government to build on past successes, to be honest about our weaknesses and to achieve better results. Our high levels of poverty and unemployment throw into sharp relief the need to transform our economy.

The policy focus shifts to raising growth and employment, and reducing poverty

As South Africa emerges from recession, the policy focus is shifting from stabilising the economy to longer-term considerations. Our future depends on finding a more inclusive economic trajectory, characterised by more rapid growth in gross domestic product (GDP) and job creation.

Over the coming period, government will maintain support for the economic recovery, take further steps to support employment growth and improve the performance of the state – within a tight fiscal environment. More efficient public service delivery will contribute to improving the livelihoods of all South Africans – especially the poor – and higher productivity and faster growth in the years ahead.

More inclusive growth depends on increasing employment, which in turn depends on faster growth

Government has a solid record of economic management, with successive layers of reforms since 1994 contributing to an acceleration of economic growth and employment in the period 2001-2008. Strong growth and sound fiscal management have enabled significant redistribution of income, expansion of social infrastructure and broadening of opportunities for the population. Yet far too many South Africans do not work, and the bulk of the gains in national income inevitably go to those who are employed. More inclusive growth depends on increasing employment – and increasing employment depends in turn on growth.

Success in the global economy requires hard work, effective organisation and clear leadership

South Africa is part of the world economy. In recent years, emerging markets such as Brazil, China and India have become leading trading nations, with expanding economies that are creating jobs and contributing to significantly lower levels of poverty. According to a 2008 World Bank study, more than 80 per cent of the poverty reduction that has taken place over the past decade has occurred in these fast-growing economies. Many other countries are also working to increase competitiveness, attract investment, develop more skilled labour and broaden opportunities for their citizens. South Africa too must compete on this global platform, where progress is registered through hard work, effective organisation and clear leadership.

In his 2010 State of the Nation Address, the President signalled a new approach. Government intends to:

- Deliver more and better services in a caring and efficient manner
- Hold political office bearers and public servants accountable
- Shift resources to new priorities
- Move from debate to effective implementation and decisive action
- Work in partnership with communities, labour and business to achieve our shared objectives.

A new approach to economic management is also required. The key economic objectives include growing the economy, reducing inequality, driving higher productivity, and supporting businesses to expand and create jobs. Given the centrality of job creation in determining South Africa's future, this year's *Budget Review* devotes a full chapter to employment, setting out long-term trends and outlining policy proposals to put more South Africans to work. In particular, proposals to raise youth employment are tabled for consideration.

Highlights of the 2010 Budget

The economy, employment and the fiscal stance

- Economic growth of 2.3 per cent is projected for 2010, increasing to 3.6 per cent by 2012.
- After falling from 27 per cent in 2003 to 22 per cent in 2007, unemployment rose to 24.3 per cent in 2009.
- The 2010 FIFA World Cup is expected to contribute about 0.5 per cent of GDP growth in 2010. To date, government has spent about R33 billion in preparation for the tournament.
- Inflation has fallen over the past year and should average 6 per cent during 2010/11.
- A budget deficit of 7.3 per cent is projected for 2009/10 and 6.2 per cent in 2010/11. By 2012/13, the deficit is expected to reach 4.1 per cent.
- National government net loan debt is projected to rise from R526 billion at the end of 2008/09 to R1.3 trillion in 2012/13.
- To help tackle youth unemployment, a wage subsidy for young people is proposed.
- Total public sector infrastructure investment of R845 billion over the next three years is anticipated.
- Over the next three years, government will spend about R52 billion on public works programmes.

Spending to support economic recovery and improve service delivery

Additions to spending plans over the next three years:

- R12.2 billion for grants, including the extension of the *child support grant* up to 18 years of age.
- R2.7 billion to provide literacy and numeracy workbooks in all 11 official languages for learners in grades R to 9, and R1 billion to increase subsidies for higher education institutions.
- R15.1 billion for occupation-specific dispensations in education, health and correctional services.
- R2.2 billion for a revised salary structure in the South African National Defence Force.
- R8.4 billion to expand provision of antiretroviral therapy.
- R2.5 billion to increase labour intensity in public works, R1.8 billion for clothing and textile production incentives and R1.8 billion for the automotive production development programme.
- R1 billion to the criminal justice sector for efforts to reduce crime and corruption.
- R2.8 billion for public transport, roads and rail infrastructure.
- R2.5 billion for municipal infrastructure to support universal access targets for water and sanitation, and R6.7 billion to municipalities to cover the increased cost of providing free basic electricity.
- R1 billion more for rural development, R1.2 billion for water and sanitation infrastructure for rural households and R1.5 billion for the Land Bank to support rural development.
- R1 billion to speed up provision of housing and R500 million for bulk water infrastructure.
- The old age pension is increased by R70 a month to R1 080 and the child support grant is increased by R10 a month.

Tax proposals

- Personal income tax relief for individuals of R6.5 billion.
- Discontinuation of the SITE (standard tax on employees) system.
- Increases in fuel taxes of 25.5 cents a litre.
- A carbon emissions tax on new motor vehicles.
- A packet of 20 cigarettes will cost R1.24 more.
- A 750 ml bottle of wine will cost 12 cents more.
- A 340 ml can of beer will cost 6.5 cents more.
- A 750 ml bottle of liquor (spirits) will cost R2.22 more.

Faster and more inclusive economic growth

Learning lessons from the global recession

Global recession has resulted in about 34 million job losses

During 2008 and 2009, the world economy suffered its worst decline since the Great Depression. The depth of the downturn is best measured not in GDP data, but in the number of jobs lost. The International Labour Organisation reports that about 34 million people were thrown out of work in the past 18 months, and the World Bank estimates that nearly 200 million people may fall back below the poverty line as a result of the recession.

Coordinated policy response helped to avoid a worldwide depression

The synchronised response to this crisis by the Group of 20 (G-20) nations helped to avert a more severe decline in output and employment. A massive fiscal and monetary expansion in both developed and developing countries stabilised the world economy, and a bailout of major banks prevented a collapse of the global financial system. In the fourth quarter of 2009, global output recorded a modest increase, and the International Monetary Fund projects global GDP growth of 3.9 per cent in 2010. Employment creation is expected to remain subdued, however, and lending by financial institutions is still weak.

This recession followed almost a decade of rapid economic growth, increased global trade, rising employment and falling poverty in much of the world. Africa experienced its highest growth in three decades. Given the collapse in output that followed, it is important for policy makers and the public to ask the difficult questions about what caused the crisis and what lessons can be learnt, including how policy can counteract greed, dishonesty and over-exuberance in the global financial system.

Excessive debt accumulation leads to economic crises

Excessive and imprudent debt is a feature of crisis episodes throughout history. As economists Carmen Reinhart and Kenneth Rogoff argue: "If there is one common theme to the vast range of the world's financial crises, it is that excessive debt accumulation, whether by the government, banks, corporations, or consumers, often poses greater systemic risks than it seems during a boom. Infusions of cash can make a government look like it is providing greater growth to its economy than it really is. Private sector borrowing binges can inflate housing and stock prices far beyond their long-run sustainable levels, and make banks seem more stable and profitable than they really are."[1]

Global crisis underscores the need for well-developed financial sector regulation

The recession has also yielded important lessons about macroeconomic management. Countries that have done better during the recession, and which are better-placed to grow more rapidly in the years ahead, are characterised by well-developed financial sector regulation, sound macroeconomic policies, low public debt, high savings rates, broad and robust social security nets, and governments capable of responding effectively to the inevitable challenges that arise in a competitive and volatile global economy.

---

[1] Reinhart, C and Rogoff, K. *This Time is Different: Eight Centuries of Financial Folly.* Princeton, 2009.

A new growth and development path for South Africa

This *Budget Review* discusses policy elements that should form part of a comprehensive plan to achieve our social and economic objectives.

The South African economy is recovering from the most severe domestic recession since 1992. About 7 per cent of workers have lost their jobs, with the unemployment rate rising to 24.3 per cent. The short-term impact of the downturn added to already high levels of joblessness. When the number of people who have given up looking for work is included, the statistics are positively alarming: six in 10 South Africans are not working, and almost half of all young people have never held a job.

Spike in joblessness has exacerbated South Africa's problem of structural unemployment

Given that global growth is likely to remain weak for some time, a failure to make crucial policy adjustments now is likely to result in weak job growth, with persistently high unemployment for several years to come. This bleak outlook necessitates bold, decisive action on the part of government, in partnership with business and labour, to chart a new growth path.

New policy approaches are essential to reduce poverty and unemployment

South Africa's history of apartheid and colonialism has determined the shape of our economy. For more than a century, the growth path was defined by extracting minerals, selling them on the world market and using the proceeds to fund a high standard of living for a small minority of the population. The solution cannot simply be to do more of the same – to sell more minerals and to distribute the proceeds to a new, if somewhat larger elite.

The nation's long-term prosperity requires the participation of all South Africans in the economy. Increasing employment is the only sustainable solution to reducing poverty and inequality. Over time, South Africa's firms and factories, offices and service providers, must absorb more labour, and include more people in economic activity.

Job creation is the only sustainable way to reduce poverty and inequality

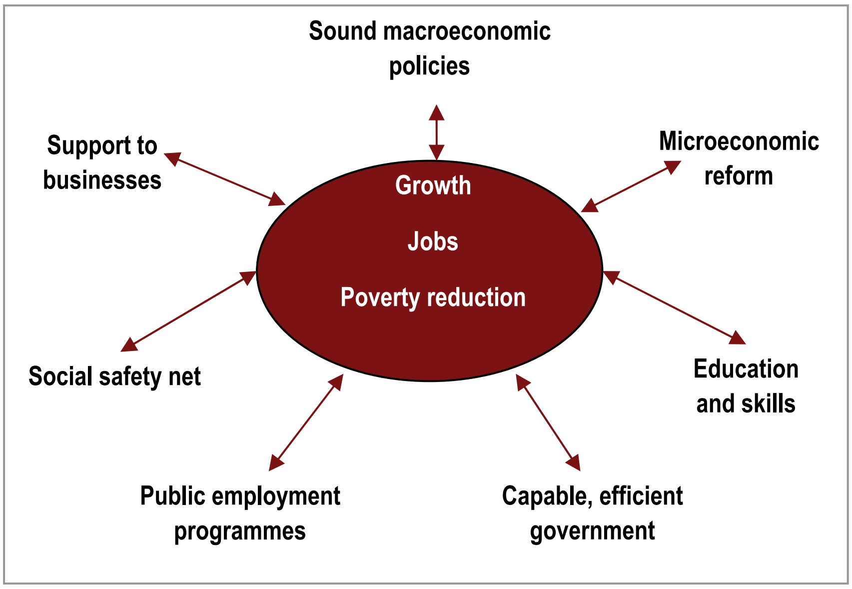
The present policy trajectory will not get us onto a new growth path. Notwithstanding significant successes in economic policy over the past 15 years, South Africa needs a credible plan, supported by an effective implementation strategy, to drive faster and more inclusive growth. There is ample international experience on which to draw. Last year's *Medium Term Budget Policy Statement* summarised the lessons of 13 high-growth countries that were the subject of a prominent international study. In brief, these countries took advantage of the global economy, pursued sound monetary and fiscal policies, had capable governments and were able to make the tough trade-offs required for long-term expansion.

There is no silver bullet to deliver faster growth, employment and poverty reduction. A multidimensional approach is required and, even with successful implementation of sound policies, economic change takes time. It also requires difficult choices to be made about investment options, spending priorities, and technology and trade strategies.

There is no silver bullet: a multidimensional approach is required for faster growth and job creation

The figure below summarises key elements required to achieve faster growth, higher employment and reduced levels of poverty.

Figure 1.1 Drivers of growth, employment and poverty reduction



Policy levers to boost employment and growth over the long term

Over the period ahead, government's policy objectives include making the economy more labour-absorptive, raising productivity, boosting exports and promoting greater levels of investment. These economic objectives, alongside social policy goals such as improved education, training and health outcomes, will contribute to more effective redistribution of resources and capabilities. Ultimately, poverty reduction is about developing people's capabilities and providing a growing economy in which they can work to improve their living conditions.

The policy levers to achieve these objectives include:

- Steps to reduce youth unemployment, including a targeted wage subsidy aimed at lowering the costs and risks of hiring inexperienced work-seekers.
- Supporting labour-intensive industries through industrial policy interventions, skills development, infrastructure investment, public employment programmes and a rural development strategy.
- Raising our savings level, and sustaining high levels of public and private investment.
- Improving the performance and effectiveness of the state, especially the provision of quality education and training at all levels.
- Reforms to increase inclusion and participation in the labour market, alongside efforts to improve competition in product markets, to reduce barriers to job creation and investment, and to lower the non-wage costs of doing business.
- Keeping inflation low, striving for a stable and competitive exchange rate, and providing a buffer against global volatility.
- Raising productivity and competitiveness by cutting red tape, enforcing competition laws, enhancing regulatory oversight, improving the performance of state-owned enterprises, and opening up the economy to investment and trade opportunities that can boost exports.

In developing a new growth path, progress also needs to be made in developing sectoral plans to raise employment and output. For example, South Africa needs a strategy to raise agricultural output, which will have positive benefits for rural employment. Similarly, a plan that removes obstacles to mining investment and exports could boost output and support job creation. These initiatives are led by the economic cluster of ministers, in consultation with industry stakeholders.

There is a need for growth plans in sectors such as agriculture, which can boost job creation

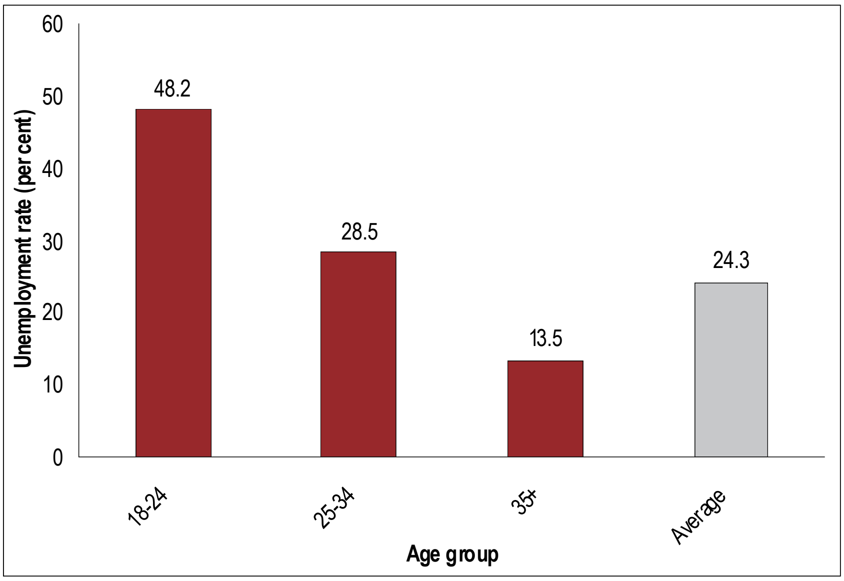
Putting young people to work

The most urgent focus of policy change must be interventions to create jobs for young people. As the graph below shows, unemployment rates for young people are substantially higher than the national average, which is itself high by international standards. Labour market data indicates that firms are reluctant to hire inexperienced work-seekers, and school-leavers lack basic workplace competencies. A 2008 report by the Organisation for Economic Cooperation and Development entitled *Going for Growth* shows that work experience plays an important part in supporting skills development. Chapter 3 of the *Budget Review* discusses some of the reasons for our high unemployment and a range of policy options to address the challenge.

South Africa's employment crisis is characterised by high joblessness among youth

Government aims to accelerate job creation for young people through a targeted wage subsidy, together with improved information services linked to training, to activate employment in the private sector. A further expansion of public employment programmes is also under way, and is supporting local infrastructure projects, literacy programmes, home-based care, school maintenance and early childhood education initiatives.

Figure 1.2 Unemployment rate by age group (December 2009)



Proposals will therefore be tabled to subsidise the cost of hiring younger workers, accompanied by the appropriate flexibility required to encourage firms to take on the risk of hiring inexperienced staff. This will lower the cost and risk of hiring an inexperienced person while creating on-the-job learning opportunities. This proposal complements efforts to raise further education and training (FET) college enrolment, broadening the range of opportunities for young school leavers.

A fiscal stance to sustain and support growth

Low levels of public debt allowed government to respond, reducing the human cost of recession

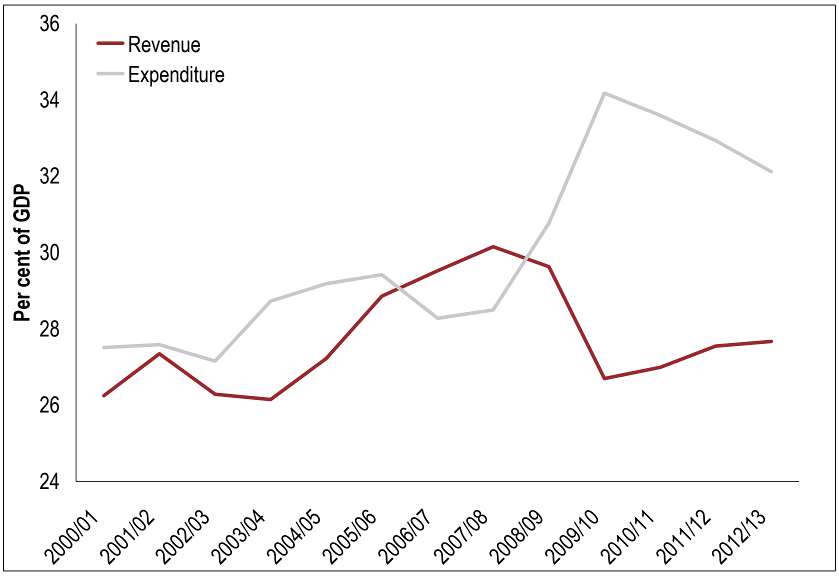
The prudent management of the public finances over the past decade – signalled by the low level of public debt – enabled South Africa to support demand in the economy by sustaining public spending and growing infrastructure investment despite a significant fall in tax revenue. Without these measures, the human cost of the recession would have been far higher. Now that the economy is growing again, government will gradually reduce the deficit and moderate public debt so that fiscal policy can continue to play a supportive and developmental role.

Fiscal crisis in southern Europe demonstrates the importance of sustainable debt levels

The consequences of unsustainable debt levels have been highlighted in recent months. Greece, for example, has faced a sharp rise in its borrowing costs and must take extraordinary austerity measures to reduce a deficit of over 12 per cent of GDP to below 3 per cent in just three years. Ireland, Spain, the United Kingdom and the United States have to cut public spending sharply, including reducing public-sector salaries and scaling back on pension and social protection measures. South Africa does not have to respond in such a severe way because we reduced our debt obligations when the economy was performing well. Nevertheless, we too have to reduce our deficit over time.

Generally, countries with high debt levels (such as Japan, Greece, Italy) can be expected to grow more slowly than countries with low debt or surpluses (China, Chile). South Africa's net loan debt is expected to rise from 22.7 per cent in 2008/09 to about 44 per cent by 2015/16 before stabilising. Given the need for rapid economic growth to boost employment, our economy cannot afford too sharp a rise in debt. Similarly, in the short term, we cannot afford to lower debt too quickly.

Figure 1.3 Consolidated government revenue and expenditure



The budget deficit has increased partly because tax revenue fell by nearly 3 per cent of GDP during the recession. As the economy recovers, so too will revenues, but with a lag. As a result, government will borrow the difference between revenue and expenditure, bringing the deficit to an estimated 7.3 per cent in 2009/10. Government will proceed in a deliberate way to reduce the deficit over the next several years. This will require a more moderate growth in public spending. Over the next three years, public spending is projected to grow by about 2 per cent a year in real terms, compared with average real growth of 7.2 per cent over the period 2005/06 to 2008/09. Within this envelope, spending on key priorities will rise more rapidly. Given a degree of uncertainty in the economic outlook over the period ahead, both tax and spending plans may need to be adjusted to achieve a sustainable fiscal balance.

Government will take deliberate, measured steps to bring the budget back toward a balanced position

To fund infrastructure investment, state-owned enterprises have significantly increased their borrowings. While some of their capital spending requirements may be financed by higher tariffs, these entities will continue to borrow to sustain the expansion of the country's economic infrastructure. For this to be made possible, government has to moderate its claim on the capital markets by reducing its borrowings.

Infrastructure investments by state-owned entities will require higher tariffs and significant borrowings

The development finance institutions are playing an important role in steadying firms that are in difficulty due to the cyclical downturn and in supporting higher levels of investment. The Development Bank of South Africa is taking the lead in supporting municipal infrastructure investment in water and sanitation; the Land Bank is poised to play a more supportive role in agriculture and rural development; and the Industrial Development Corporation works to implement government's industrial policy, supporting growth and innovation in several industrial sectors.

Efficient and effective public services

Over the next few years, government must deliver more services – and deliver them more efficiently – within a tight resource envelope. Achieving this objective requires a new way of working:

- The budget has been reprioritised so that money is moved from low-priority programmes to high-priority programmes.
- A performance culture where people are held accountable for their actions, accompanied by clear, measurable outcomes related to key development priorities.
- Government will manage growth in its consumption expenditure (wages, and goods and services) and obtain better value for money .
- Corruption, particularly in the tender system, will be uprooted.

Reprioritising the budget

The 2010 Budget takes further steps in reprioritising public expenditure. A total of R87 billion has been added to spending plans over the next three years. In general, these resources go to education, health, rural development, creating jobs, fighting crime, infrastructure and human settlements, and improving local government.

The 2010 Budget is characterised by significant reprioritisation of resources

Government is postponing, cancelling or winding down low-priority and ineffectual programmes

The 2010 Budget process focused not only on where government could add more money, but also where savings could be made and spending reduced by postponing, cancelling or winding down low-priority and ineffectual programmes. At national level, about R25.6 billion has been found over the medium-term expenditure framework (MTEF) – the three-year spending plan of government – for reallocation to higher priorities, taking total changes to spending to R112 billion. About R13 billion of savings have been identified at a provincial level.

Efficiency savings have been identified in all departments, with spending on goods and services, travel, accommodation, conferences and catering strictly curtailed. The cancellation of the Airbus A400M military aircraft contract will save about R13 billion over the next seven years.

The Ministers' Committee on the Budget will oversee a comprehensive review of expenditure

The second phase of the savings exercise has already begun, with departments assessing the role, purpose and effectiveness of their programmes and public entities, and whether those functions can be performed at a lower cost. The third phase, a comprehensive expenditure review, will be conducted jointly by the National Treasury and the Presidency, overseen by the Ministers' Committee on the Budget.

A new budget process in Parliament

The Money Bills Amendment Procedure and Related Matters Act (2009), which has just come into effect, prescribes the processes through which parliamentary committees can make recommendations and propose amendments before the annual budget is enacted in law. The act recognises that while the Constitution provides that only the Minister of Finance may introduce appropriation bills and revenue laws, it also envisages that there should be a statutory procedure for money bills to be amended.

In summary, the procedure is as follows:

- Portfolio committees are expected to table annual budgetary review and recommendation reports, which must assess each department's service delivery performance and may include recommendations on the forward use of resources. These reports are intended to be available to the National Assembly for consideration alongside the *Medium Term Budget Policy Statement* (MTBPS).
- Within 30 days of the Minister tabling the MTBPS, Parliament's finance and appropriation committees must report on the proposed fiscal framework and the division of revenue. In preparing the budget, the Minister must consider these reports and respond to their recommendations.
- Once the budget has been tabled in Parliament, the fiscal framework and revenue proposals are referred to the finance committees, which must prepare a report accepting or amending the framework. If amendments are proposed, the Minister has an opportunity to respond, following which Parliament must approve a fiscal framework.
- Parliament's appropriation committees then have to consider and report on the Division of Revenue Bill, which allocates available resources between national, provincial and local government. Changes may be proposed provided they are consistent with the approved fiscal framework.
- The Appropriation Bill may then be considered and approved. This bill allocates resources between budget votes for national departments and associated entities, including conditional grants to provinces and municipalities. If an amendment to the Appropriation Bill is proposed, it must be consistent with the approved fiscal framework and Division of Revenue Act.

Parliament is therefore able to revise specific allocations within or between national votes, subject to the agreed overall allocations to each sphere. At each step, the Minister of Finance is given the opportunity to comment on any proposed change to the budget. These procedures are designed to ensure that the overall integrity of the budget, the fiscal framework and the division of revenue is maintained, and to assure certainty in fiscal policy, social and economic development, and public service delivery.

The Minister's response to the recommendations of Parliament on the 2009 MTBPS, which have been taken into account in preparing the 2010 Budget, is set out in Annexure A.

The budget also has to strike a careful balance between the major categories of spending (personnel costs, goods and services, capital spending and transfers to households), since each of these have different implications for the economy. In 2008 and 2009, public-sector salaries grew more quickly than anticipated. Part of this growth was necessary to adjust salaries for key categories of professionals. In addition, direct public employment increased rapidly, especially in health, policing and education. Now that these occupation-specific adjustments have occurred, salary increases over the next three years will have to be more moderate to be able to sustain positive growth in employment and infrastructure spending.

Public-sector salary increases over the next three years will have to be more moderate

This year, new legislation comes into effect setting out procedures to effect a longstanding constitutional requirement: the ability of Parliament to amend money bills. To give full effect to the new legislation, Parliament needs greater capacity to support its committees, and the executive will work more closely with the legislature in developing the national budget.

A new role for Parliament in the budget process

Measurable performance and accountable delivery

Government is adopting a new approach to delivery that focuses on outcomes. The Presidency has set out 12 clear, measurable outcomes. Chapter 8 discusses the priority outcomes in detail and describes how resources are allocated to support their achievement. This new approach, together with enhanced planning, monitoring and evaluation capacity, aims to give greater impetus to development and service delivery improvements, and to make a meaningful impact on the lives of South Africans.

'Massive increases in expenditure did not always produce the results we wanted, hence the outcomes and measurable outputs approach.' –
Minister in the Presidency Collins Chabane

The new approach requires the public service to work differently. In each of the priority areas, delivery agreements will be negotiated between the Presidency and the relevant service delivery forum. These will consist of government departments at all levels and other research and implementing agencies. The delivery agreement will then be signed by the President and all the major representatives in a sector. This approach necessitates closer cooperation between government at national, provincial and local level, and agencies and communities involved in the delivery of key services. An example of this approach emerged earlier this year, when teacher unions committed themselves to raise the bar for performance and quality teaching in the classroom, and to stamping out disruption to teaching time.

Similar agreements will be negotiated in each of the 12 areas, with the top priorities set to be completed in the first half of this year. These agreements provide a platform for increased public scrutiny of government's work and performance. These reforms will also strengthen democracy by promoting greater public accountability.

An approach geared to emphasise performance requires a set of complementary reforms to revitalise the public service, and to create a culture of efficiency, effectiveness, productivity and respect for citizens. Better public services also require partnerships with communities, obliging local government to become more responsive.

Procurement reforms and fighting corruption

Over the past decade, to improve efficiency and accountability, decisions on procurement were decentralised to departmental level. An unintended consequence of this process has been the fragmentation of accountability and an increase in abuse of the tender system.

'These [corrupt] tenders are the biggest threat to our revolution.' *– Minister of Higher Education and Training Blade Nzimande*

If government is not able to curb corruption in procurement processes, confidence in our democratic government will rapidly erode. Corruption is part of a broader problem associated with a narrow view of empowerment that has become more widespread. Empowerment is about building capabilities so that people can contribute to economic development and improve their lives and livelihoods, not about extracting large economic rents from government.

To reduce corruption and to lower the costs of procuring certain goods and services, government intends to reform the procurement system. Greater transparency (including electronic procurement systems), arms-length competitive tendering processes and providing greater certainty to industry about procurement pipelines will contribute to achieving better value for money. More centralised procurement arrangements will be adopted where this contributes to greater efficiency and transparency.

Inter-agency cooperation will hasten effective prosecution of those defrauding government

In addition, a supply chain compliance unit has been established in the National Treasury. It will investigate compliance with tender rules and procedures, and work with the Special Investigating Unit to investigate specific tenders where there is suspicion of corruption. Closer cooperation between the Special Investigating Unit, the South African Revenue Service, the Financial Intelligence Centre and the South African Police Service will hasten effective prosecution of people found to be defrauding government through the tender system. An inter-ministerial task team has been established to coordinate anti-corruption initiatives.

Overview of the 2010 Budget

Economic outlook and employment

The recession took a heavy toll on South Africa, with some 870 000 people losing their jobs in 2009 and households squeezed between falling incomes and high levels of debt. As the recovery strengthens, South Africa faces the related challenges of sustaining growth while at the same time making the changes necessary that will allow for more rapid and inclusive economic expansion in years ahead.

To support more inclusive growth, regulatory reforms that encourage employment are needed

Chapter 2 sets out government's economic forecasts and points to the policy changes needed to place the economy on a more competitive footing. Key interventions required include regulatory reforms that lower business costs and encourage employment, further efforts to support investment and savings, and supporting a more labour-intensive industrial policy.

Chapter 3 focuses specifically on employment. It analyses long-term trends, discusses job losses during the recession, and reviews research on the factors behind youth unemployment. The chapter provides strong evidence to suggest that while South Africa's labour market regulations are well structured, there are unintended consequences that may contribute to high unemployment, such as bargaining arrangements focused on raising the minimum wage that price inexperienced workers out of the job market. The chapter discusses a range of policy interventions that could contribute to higher employment growth.

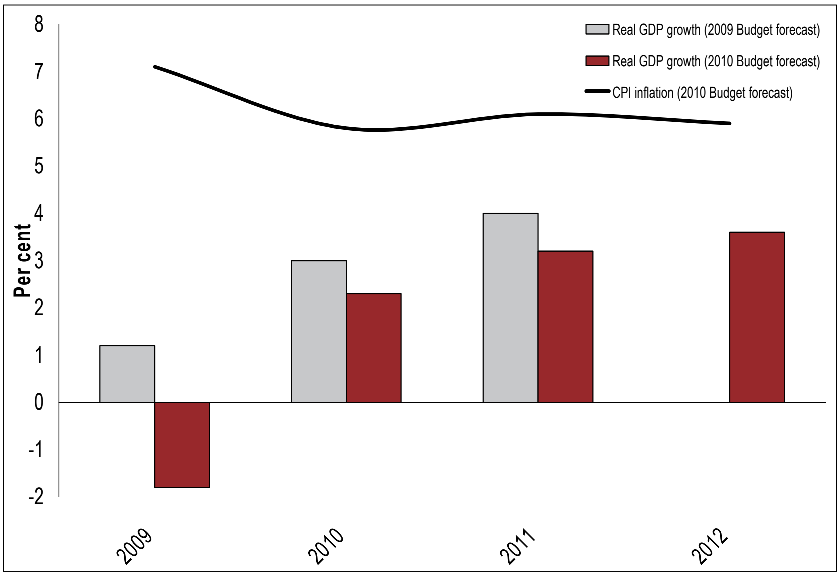
The domestic economy is projected to grow by 2.3 per cent this year

Following a 1.8 per cent GDP contraction in 2009, the South African economy is projected to grow by 2.3 per cent this year, rising to 3.6 per cent by 2012. Factors driving higher growth include a recovery in the global economy, higher commodity prices and sustained growth in government spending. There are, however, significant risks to the global outlook. In particular, large budget deficits in developed countries and asset price bubbles in Asia are cause for concern.

The FIFA World Cup should contribute about 0.5 per cent of GDP in 2010

Expansionary fiscal and monetary policies have supported the economy during the recession and continue to support the recovery. Nevertheless, high levels of debt continue to constrain household consumption expenditure. Slower demand growth and the uncertain economic outlook have reduced private-sector capital investment. As the recovery takes hold, private investment will pick up. The 2010 FIFA World Cup is also expected to provide a boost to the economy, contributing about 0.5 per cent of GDP this year.

Figure 1.4 Macroeconomic forecasts (calendar year)



Government affirms its commitment to low inflation and a more competitive and stable exchange rate

Chapter 2 also provides a detailed outline of government's policy stance on inflation and the exchange rate. A commitment to lowering our inflation rate (and therefore long-term interest rates) relative to those of our major trading partners is emphasised, alongside countercyclical monetary and fiscal policies that will contribute to a more competitive and stable exchange rate.

Fiscal and tax policy

Chapter 4 discusses fiscal policy. South Africa's healthy public finances enabled a significant stimulus over the past year, and fiscal policy will continue to contribute to the domestic economic recovery. In addition, low levels of public debt achieved between 2004 and 2008 have allowed public corporations to increase infrastructure investment, further supporting growth in the short and long term.

The budget balance has widened by over 8 per cent of GDP since 2007/08. Public spending has increased by about 5 per cent of GDP and revenue has fallen by over 3 per cent of GDP.

Government will reduce the budget deficit gradually, which will require slower growth in public spending

The fiscal policy discussion sets out the path by which the budget will be brought back towards a sustainable position. Government is projecting to reduce the deficit gradually, from about 7.3 per cent of GDP in 2009/10 to about 4 per cent by 2012/13. This will require slower (though still positive) growth in public spending, and a gradual rise in tax revenue.

Table 1.1 Consolidated government budget

R billion	2009/10	2010/11	2011/12	2012/13
Gross tax receipts	565.4	650.3	734.5	811.9
plus: Non-tax receipts	64.2	73.1	82.1	87.6
less: SACU transfers	-27.9	-15.0	-11.2	-22.8
Total receipts	**657.6**	**738.4**	**827.7**	**922.3**
Current payments	480.4	527.9	580.1	623.7
of which: Interest	*62.3*	*77.6*	*95.7*	*112.5*
Transfers and subsidies	268.6	284.0	315.0	337.3
Payments for capital assets	53.5	68.2	69.4	73.6
Payments for financial assets	32.8	20.9	0.8	0.0
Contingency reserve	–	6.0	12.0	24.0
Total payments	**835.3**	**907.0**	**977.4**	**1 058.6**
Budget balance	**-177.8**	**-168.6**	**-149.6**	**-136.3**
Percentage of GDP	*-7.3%*	*-6.2%*	*-5.0%*	*-4.1%*
Gross domestic product	*2 449.9*	*2 699.9*	*2 967.6*	*3 295.7*

Chapter 5 discusses tax policy and proposals. Tax policy continues to focus on improving compliance and broadening the tax base.

Tax revenue for 2009/10 is sharply below the original budget estimate, reflecting the impact of the recession

In 2009/10, tax revenue is expected to be about R69 billion below the original budget estimate, reflecting significant weakness in the economy. Revenue growth is expected to recover but with a lag. In particular, taxes from company profits are likely to continue falling for the first part of 2010, only increasing in late 2010 and 2011.

Government will take further steps to broaden the tax base and improve tax compliance so that the burden of meeting the cost of public services is shared equitably.

Chapter 6 sets out the scale and strategy of the borrowing programme, and provides an assessment of the economic implications of this borrowing. It also provides more detail on the investment and borrowing plans of the major state-owned enterprises. The plans of development finance institution are summarised.

A large public-sector borrowing requirement is a necessary corollary to sustaining the infrastructure programme

Progress in reducing the budget deficit must take account of a large public-sector borrowing requirement, which is necessary to sustain capital spending by state-owned enterprises and municipalities. If national government does not moderate its borrowing requirement, public enterprises may find it difficult to raise the debt necessary to sustain their large infrastructure programmes. Government also recognises that households and businesses will have to adjust, over time, to higher tariffs for electricity and water, consistent with the economic cost of these services.

Net loan debt of national government is projected to increase from R525.7 billion in April 2008 to R1.3 trillion by March 2013, the end of the present MTEF period. This significant increase in borrowings has to be raised in domestic and foreign capital markets which are still recovering from the effects of the global recession. Furthermore, South Africa and the major state-owned enterprises have to compete on capital markets with other countries that have significant borrowing requirements.

Social security and health care financing

The social security system has proven resilient, but there is a need for further reform

South Africa's social security system has proven resilient during the turbulent economic conditions of the past year. Almost 14 million South Africans are now receiving social grants, and this number is set to increase in the coming years as a result of the extension of the *child support grant* to recipients' 18th birthday. Meanwhile, the Unemployment Insurance Fund (UIF) has been able to cope with the surge in unemployment and the resultant increase in claims.

There is, however, considerable room for improvement in the social security system. Government is examining ways to bring down the cost of administering the grants system and countering fraudulent claims. At the same time, statutory funds such as the UIF, the Compensation Funds and the Road Accident Fund (RAF) could all provide improved service and better coverage. In December 2009, Cabinet approved fundamental changes to the RAF, creating a no-fault system that will expand access to benefits to a wider group of road accident victims and focus resources on those most seriously injured. Reforms to the UIF and Compensation Funds are also under consideration.

A national health insurance system is under consideration

Voluntary social insurance is also under scrutiny. Lower-income workers are ill-served by the existing retirement funding arrangements. An inter-ministerial committee is reviewing options for a universal savings arrangement to help low-income workers save for retirement, and provide them and their dependants with greater protection in the event of disability, unemployment or death. Government is also examining ways to improve access to health care and ease the burden on the public health system. Under consideration is a system of national health insurance that will build on existing resources in both the public and private sectors.

Medium-term spending plans and the division of revenue

Chapters 8 and 9 set out the spending plans of government over the next three years, focusing on changes to spending plans tabled in 2009. South Africa's system of intergovernmental fiscal relations provides for budgets at national, provincial and municipal level. The national fiscus transfers significant resources to sub-national government in line with nationally determined priorities. The 2010 Budget reflects significant reprioritisation between spending areas and within departments to fund new priorities and achieve targets.

Education, health, rural development, public safety, jobs, housing and local government are the priorities

The priorities of government, guided by the medium-term strategic framework, are education, health, rural development, fighting crime and creating jobs. Given their importance, human settlements and associated infrastructure, and local government, have been identified as additional priorities. While the bulk of new resources are allocated to these functions, a significant share of additional spending goes to fund higher-than-budgeted salary increases and occupation-specific dispensations for certain professionals.

Chapter 8 provides an account of how spending plans relate to government's outcome targets, further strengthening accountability.

Half of additional expenditure is channelled to provinces and municipalities

Public spending growth averages about 8.2 per cent a year or 2.2 per cent in real terms. This is below the rapid pace of growth in previous budgets and reflective of the more constrained fiscal and economic environment. Given that provinces and municipalities deliver several of the key priorities of government, transfers to these spheres grow by 7.8 per cent and 13.4 per cent respectively.

Table 1.2 Division of revenue

R billion	2009/10	2010/11	2011/12	2012/13
National allocations	346.1	359.1	370.7	393.8
Provincial allocations	290.8	322.9	350.5	369.3
Equitable share	*236.9*	*261.0*	*280.7*	*294.8*
Conditional grants	*53.9*	*61.9*	*69.9*	*74.6*
Gautrain loan	*4.2*	*–*	*–*	*–*
Local government allocations	50.1	58.8	66.6	73.2
Total allocations	**691.2**	**740.8**	**787.9**	**836.3**
Changes to baseline				
National allocations	3.0	6.6	9.7	16.9
Provincial allocations	10.4	13.2	14.6	17.8
Equitable share	*9.0*	*10.7*	*11.3*	*11.9*
Conditional grants	*1.5*	*2.5*	*3.3*	*5.8*
Local government allocations	0.4	0.9	1.7	5.3
Total	**13.9**	**20.7**	**26.0**	**39.9**

Other budget documentation

In addition to the *Budget Review*, the National Treasury produces a series of other documents related to the Budget:

- The Budget Speech
- The Division of Revenue Bill
- The Appropriation Bill
- The *Estimates of National Expenditure*
- The *People's Guide*.

Two annexures to the 2010 *Budget Review* are available on the National Treasury website: Annexure W1 (Explanatory memorandum to the division of revenue) and Annexure W2 (Structure of the government accounts). These documents and other fiscal and financial publications are available at: www.treasury.gov.za.