3

Revenue and expenditure trends in local government

Introduction

The revenues and expenditures of municipalities determine their ability to deliver services. Weaknesses in revenue and expenditure management could constrain the ability of a municipality to contribute to poverty reduction and economic development. They are also likely to reflect the existence of other governance challenges.

This chapter reviews key trends in the revenues and expenditures of all 283 municipalities from 2003/04 to 2006/07 and future budget trends over the medium-term. Other chapters in this Review provide a more detailed analysis of specific expenditure functions.

It is not enough to simply review the size of municipal revenues or expenditures

Simply reviewing the size of municipal revenues or expenditures provides little insight into the challenges that face municipalities, nor does it reveal much about the efficiency or effectiveness of a municipality. Rising expenditures related to the delivery of a particular service may reflect an expansion of services to more citizens or increasingly difficult technical conditions, such as a dispersed population or a municipality reaching a specific stage in the life-cycle of its assets. But it may also reflect higher than average personnel costs or administrative overheads, weak expenditure control systems or inappropriate service standards. Inefficiencies in service delivery might also quickly translate into increased expenditures and perhaps even reduce the availability of resources to address the core objectives of poverty reduction and economic development.

This chapter gives an overview of:

- local government in the system of public finance

- revenue trends
- expenditure trends
- key issues in municipal budgets.

Local government in the system of public finance

Table 3.1 shows that the ratio of municipal expenditure to total government expenditure increases from 20.8 per cent in 2003/04 to 23.4 per cent in 2007/08. This reflects the strong growth in national transfers to local government, particularly associated with the 2010 FIFA World Cup. Over the medium-term the share of local government spending declines to 19.6 per cent in 2009/10. This is due to the ending of the 2010 FIFA World Cup transfers and slower municipal infrastructure spending.

Table 3.1 also shows that municipal operating revenue as a percentage of GDP was fairly stable between 2003/04 and 2007/08, but is set to decrease quite rapidly over the medium-term. It is apparent that this is not being driven by changes in property rates, since rates as a percentage of GDP remain constant at about 1 per cent. Rather most of this trend can be attributed to the fact that national transfers remain largely constant in the medium-term.

Table 3.1 Local government expenditure to GDP, 2003/04 – 2009/10

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
R million		Outcome		Estimate		Medium-term estimates	
Expenditure							
National departments	194 515	216 140	245 635	264 821	299 766	331 165	365 797
Provinces	131 858	142 629	161 764	186 561	214 571	247 860	274 712
Local government	85 850	97 162	112 882	128 106	157 294	160 620	156 514
Total expenditure	**412 222**	**455 931**	**520 281**	**579 488**	**671 631**	**739 645**	**797 023**
Municipal expenditure as percentage of total government expenditure	*20.8%*	*21.3%*	*21.7%*	*22.1%*	*23.4%*	*21.7%*	*19.6%*
Municipal expenditure as percentage of GDP	*6.7%*	*6.8%*	*7.1%*	*7.1%*	*7.7%*	*7.0%*	*6.2%*
Total operating revenue	**73 832**	**87 369**	**96 000**	**106 056**	**118 405**	**122 710**	**127 705**
Municipal revenue as a percentage of GDP	*5.7%*	*6.1%*	*6.1%*	*5.9%*	*5.8%*	*5.4%*	*5.1%*
Property rates	13 980	16 396	17 401	18 521	21 486	22 770	24 136
Property rates as percentage of GDP	*1.1%*	*1.1%*	*1.1%*	*1.0%*	*1.1%*	*1.0%*	*1.0%*
GDP	1 288 979	1 427 445	1 584 743	1 807 316	2 045 533	2 286 906	2 506 870

Source: 2007 and 2008 Budget Review

Revenue trends

Municipalities are largely self-financing

Municipalities are largely self-financing. This means that the bulk of their resources are raised from own revenue sources such as taxes and service charges. This principle is an important feature of any democratic local government system. It ensures that municipalities are directly accountable to local residents for the functions they perform and the services they provide. It empowers residents to play an important role in deciding on the services they prefer and are willing to pay for and ensures that municipalities remain responsive to the needs of their residents.

However, in South Africa there are two important dimensions to this basic principle. First, there is a structural imbalance between available local revenue sources and the expenditure functions that are assigned to local government. Second, not all municipalities have the same capacity to raise revenues, as levels of poverty vary considerably and are particularly high in mostly rural municipalities. In practice, this means that while national government must provide financial support to all municipalities, such support needs to be directed to ensuring all citizens have access to basic services.

Table 3.2 shows that total operating revenue of municipalities (including government grants) grew by 7 per cent annually for the period between 2003/04 and 2006/07 and is projected to further increase by 1.1 per cent per year over the medium-term. This growth is driven largely by increases in national transfers targeted at stepping up funding access to pro-poor basic services, increased funding for 2010 FIFA World Cup commitments and the replacement grant for the Regional Services Levies (RSC) which was abolished in 2006/07.

Table 3.2 Municipal operating revenue, 2003/04 – 2009/10

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
R million		Outcome		Estimate	Medium-term estimates		
Operating Revenue							
Property rates	13 980	16 396	17 401	18 521	21 486	22 770	24 136
Service charges	36 146	38 735	40 201	44 498	49 223	51 549	54 777
Regional Service Levies[1]	4 983	7 009	7 604	386	95	2	0
Investment revenue	1 673	2 115	2 357	2 970	3 845	3 818	4 133
Government grants	8 980	13 742	17 398	27 223	26 571	28 311	28 491
Public contributions and donations	44	588	664	695	–	–	–
Other own revenue	8 025	8 784	10 375	11 763	17 184	16 260	16 167
Total revenue	**73 832**	**87 369**	**96 000**	**106 056**	**118 405**	**122 710**	**127 705**
Percentage of total revenue							
Property rates	18.9%	18.8%	18.1%	17.5%	18.1%	18.6%	18.9%
Service charges	49.0%	44.3%	41.9%	42.0%	41.6%	42.0%	42.9%
Regional Service Levies	6.7%	8.0%	7.9%	0.4%	0.1%	0.0%	0.0%
Investment revenue	2.3%	2.4%	2.5%	2.8%	3.2%	3.1%	3.2%
Government grants	12.2%	15.7%	18.1%	25.7%	22.4%	23.1%	22.3%
Public contributions and donations	0.1%	0.7%	0.7%	0.7%	0.0%	0.0%	0.0%
Other own revenue	10.9%	10.1%	10.8%	11.1%	14.5%	13.3%	12.7%
Total revenue	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

1. RSC levies abolished from 1 July 2006. Interim replacement grant included in Equitable share.

Source: National Treasury local government database

At 42 per cent in 2006/07, service charges are the largest source of operating revenue for municipalities

Service charges' share in total operating revenue declines from 49 per cent in 2003/04 to 42.9 per cent in 2009/10 mainly due to the sharp increase in national transfers. Despite this decreasing share, revenue raised from service charges is budgeted to grow by 1.9 per cent per year over the medium-term in real terms.

Government grants are the second largest source of revenue

At 22.4 per cent of total operating revenue in 2007/08, government grants are the second largest source of revenue. Table 3.2 also shows that for 2006/07 and over the medium-term, the increase to transfers averages 7.3 per cent, which is mainly attributable to the additional grants given to the host cities of the 2010 FIFA World Cup.

Revenue raised through property rates grew by R4.5 billion or 4.2 per cent in real terms between 2003/04 and 2006/07 and is expected to grow further by 3.8 per cent over the medium term. This is largely due to the implementation of the new rating system, where municipalities will charge households according to the market value of both the land and any improvements to it.

Progress report on the implementation of the Municipal Property Rates Act

Although the Municipal Property Rates Act (2004) took effect from 2 July 2005, the new property rating and valuation system only takes effect when a council has adopted its rates policy and has prepared the first valuation roll in terms of the Act. Municipalities are required to bring their valuation records up to date within four years of the effective date of the legislation, i.e. between 1 July 2006 and 1 July 2009. As municipalities require between 6 to 18 months to put in place a new municipal valuation roll, only a limited number of municipalities implemented their first valuation in terms of the Act on 1 July 2006 and 1 July 2007. The majority of municipalities (approximately 90 per cent) are therefore targeting either 1 July 2008 or 1 July 2009 as the implementation date, as indicated in the table below (based on 266 municipal reports):

2006/07 implementation date	=	4 municipalities
2007/08 implementation date	=	23 municipalities
2008/09 implementation date	=	77 municipalities
2009/10 implementation date	=	162 municipalities

Although national and provincial governments are responsible for monitoring and assisting municipalities with the implementation of the new property valuation and rating system, municipalities are primarily responsible for ensuring that property rates bills remain affordable. Municipalities have been advised that when they implement new valuation rolls in terms of the act and their base increases (due to higher property values), appropriate reductions need to be made to the tax rate. In terms of current practice, the following trends have been observed in a selection of municipalities that implemented the Act from 1 July 2007:

Municipality	2006/07 Prior to implementation	2007/08 Implementation	% increase
Bela Bela	16 707	21 950	31.4%
Blue Crane Route	3 269	3 538	8.2%
Breede River Winelands	20 215	42 443	110.0%
Cape Town	2 674 117	3 496 600	30.8%
Greater Tubatse	13 614	27 350	100.9%
Ikwezi	1 020	1 550	52.0%
Inkwanca	2 396	3 533	47.5%
KwaDukuza	83 936	290 083	245.6%
Maruleng	2 400	8 000	233.3%
Matzikama	11 513	13 500	17.3%
Mbonambi	–	3 716	–
Midvaal	43 000	55 527	29.1%
Msukaligwa	27 138	37 408	37.8%
Mthonjaneni	3 220	3 300	2.5%
Musina	8 555	11 513	34.6%
Nkandla	560	712	27.1%
Ntambanana	–	215	–
Sol Plaatje	98 553	105 572	7.1%
Umlalazi	20 111	33 065	64.4%
uMngeni	44 527	61 911	39.0%
uMshwathi	3 270	21 889	569.4%

Source: Department of Provincial and Local Government and National Treasury local government database

Revenue from traffic fines, business licences, rental fees and other fees make up 14.5 per cent of total revenue in 2007/08

Municipalities also generate other revenue in the form of traffic fines, business licences, rental fees, entrance fees for use of municipal facilities and fresh produce markets. Revenue from these sources increases from R8 billion to R17.2 billion between 2003/04 and 2007/08 and is anticipated to decrease slightly to R16.2 billion by 2009/10.

Table 3.3 shows that the equitable share grant is the largest national transfer to municipalities. The total equitable share grant for municipalities has grown by R11.7 billion between 2003/04 and 2006/07 and is set to increase by another R12.1 billion over the medium-term. The rapid growth in local government's equitable share is largely due to increases in the allocations for indigent households.

Table 3.3 Division of nationally collected revenues, 2003/04 – 2009/10

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
R million		Outcome		Estimate		Medium-term estimates	
Division of available funds							
National departments	**148 201**	**167 289**	**194 723**	**212 629**	**246 937**	**273 929**	**302 672**
Provinces	**122 673**	**138 512**	**154 368**	**178 871**	**205 224**	**238 076**	**268 158**
Equitable share	107 538	120 885	135 292	150 753	172 862	199 377	225 466
Conditional grants	15 135	17 627	19 076	28 118	32 362	38 699	42 692
Local government	**11 521**	**13 808**	**16 681**	**26 501**	**37 127**	**41 855**	**47 651**
Equitable share1	6 350	7 678	9 643	18 058	20 676	24 889	30 156
Conditional grants	5 171	6 130	7 038	8 443	16 451	16 966	17 495
Total	**282 395**	**319 609**	**365 772**	**418 001**	**489 288**	**553 860**	**618 481**
Percentage of total							
National departments	52.5%	52.3%	53.2%	50.9%	50.5%	49.5%	48.9%
Provinces	43.4%	43.3%	42.2%	42.8%	41.9%	43.0%	43.4%
Local government	4.1%	4.3%	4.6%	6.3%	7.6%	7.6%	7.7%
Total	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***

1. RSC levies abolished from 1 July 2006. Interim replacement grant included in Equitable share.

Source: National Treasury local government database

Table 3.4 shows that equitable share allocations to the metros grew most rapidly. It increased by 70.1 per cent in real terms from 2003/04 to 2006/07. The equitable share grant to district municipalities increased by 50.3 per cent in real terms; and local municipalities saw their equitable share grow by 12.1 per cent in real terms.

Table 3.4 Equitable share transfers, 2003/04 – 2009/10

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
R million		Outcome		Estimate		Medium-term estimates	
Category A (Metros)[1]	1 273	1 657	2 300	7 348	8 441	10 015	11 983
Category B (Locals)	4 077	4 847	5 873	6 727	7 560	9 281	11 609
Category C (Districts)[1]	1 001	1 174	1 471	3 983	4 674	5 593	6 564
Total	**6 350**	**7 678**	**9 643**	**18 058**	**20 676**	**24 889**	**30 156**
Percentage of total							
Category A (Metros)	*20.0%*	*21.6%*	*23.8%*	*40.7%*	*40.8%*	*40.2%*	*39.7%*
Category B (Locals)	*64.2%*	*63.1%*	*60.9%*	*37.3%*	*36.6%*	*37.3%*	*38.5%*
Category C (Districts)	*15.8%*	*15.3%*	*15.3%*	*22.1%*	*22.6%*	*22.5%*	*21.8%*
Total	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***

1. RSC levies abolished from 1 July 2006. Interim replacement grant included in Equitable share.

Source: National Treasury local govemment database

The distribution of the equitable share has increasingly favoured metros over local municipalities. In 2003/04, metros received only 20 per cent of the equitable share, while local municipalities received 64.2 per cent and district municipalities the remainder. In 2006/07, 40.7 per cent of the total grant went to metros, 37.3 per cent to local municipalities and 22.1 per cent to the district municipalities. The bias towards the metros is a result of both their large and growing poor populations and the introduction of the RSC levy replacement grant, which is transferred through the equitable share mechanism. This replacement grant was also allocated to district municipalities. The trend in 2009/10 shows metros and local municipalities receiving almost the same proportion of the equitable share, at 39.7 per cent and 38.5 per cent respectively.

The growth in grants for all categories of municipalities is intended to assist them in meeting the capital and operating costs of providing basic services to poor households and is not intended to be a substitute for municipalities' own revenue. Non-poor households and firms should still pay the full cost of services they receive and municipalities need to continue their efforts to collect these revenues.

Just as there is an increase in transfers to meet the developmental objectives of local government, there should also be a concerted effort to improve the accountability of the application and performance of these transfers. This should not only be in terms of reporting for compliance purposes, but more in terms of the outcomes of these transfers in reducing poverty and enhancing economic growth. The performance of these transfers should also not only be measured in terms of quantities, such as the number of water connections made but the performance measures should in future graduate to the quality of the service, such as the quality of water provided.

Capital funding

Municipalities fund their capital expenditure in various ways such as external loans, own revenue and grants

Municipalities fund their capital expenditure in various ways such as external loans, own revenue and grants. Table 3.5 shows that grants and subsidies are still the preferred source of finance for the acquisition of fixed assets by municipalities.

Grants for municipal infrastructure averaged about 45.1 per cent of the capital funding of municipalities for the period 2003/04 to 2006/07, with real annual growth averaging 16.8 per cent. The upswing in the grants between 2007/08 and 2008/09 is because of additional grants allocated to municipalities hosting the 2010 FIFA World Cup. Another reason for the increase in grants over the medium-term is the R1.8 billion set aside for the development of regional bulk water services.

Municipalities are increasingly using external loans to fund their infrastructure programmes. This can be seen in the real growth of 40.5 per cent for the period 2003/04 to 2006/07. However, only 26 out of 283 municipalities use external loans to fund capital expenditure and there is, as yet, little indication that the numbers will increase. (For a detailed discussion on municipal borrowings, see Chapter 6 of this Review).

Table 3.5 Municipal capital funding, 2003/04 – 2009/10

R million	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
		Outcome		Estimate		Medium-term estimates	
Source of finance							
External loans	2 011	3 315	5 278	6 543	7 621	6 678	5 909
Public contributions and donations	371	248	301	287	838	786	701
Grants and subsidies	4 775	6 058	8 186	8 909	20 813	22 118	14 960
Other	3 539	3 702	3 467	5 153	10 464	9 670	8 767
Total source of finance	**10 696**	**13 323**	**17 232**	**20 891**	**39 736**	**39 252**	**30 337**
Percentage of source of finance							
External loans	*18.8%*	*24.9%*	*30.6%*	*31.3%*	*19.2%*	*17.0%*	*19.5%*
Public contributions and donations	*3.5%*	*1.9%*	*1.7%*	*1.4%*	*2.1%*	*2.0%*	*2.3%*
Grants and subsidies	*44.6%*	*45.5%*	*47.5%*	*42.6%*	*52.4%*	*56.3%*	*49.3%*
Other	*33.1%*	*27.8%*	*20.1%*	*24.7%*	*26.3%*	*24.6%*	*28.9%*
Total	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***	***100.0%***

Source: National Treasury local government database

Municipalities also fund their capital expenditure from surpluses generated from their trading activities or from rates. This form of funding has been decreasing over the years, from 33.1 per cent of total funding in 2003/04 to 24.7 per cent in 2006/07 and is set to increase to 28.9 per cent over the medium-term. The real growth rate in this form of funding was 7.5 per cent for the period 2003/04 to 2006/07 and is set to increase to 13.5 per cent over the medium term. This is attributable to municipalities recognising the importance of using their own revenues to finance capital projects.

Outstanding consumer debts

As at December 2007, municipalities were owed a total of R44.2 billion. This represents an increase of 0.3 per cent from the same month in 2006.

Metros are owed the biggest portion of the debt, amounting to R25.4 billion. While this is high, it does represent a decrease of about R2.8 billion from December 2006. This is mainly due to debt write offs by municipalities like Ekurhuleni, the City of Tshwane and the City of Johannesburg, as part of debt management strategies, rather than this revenue actually being collected. These strategies include data cleansing, updating the indigent register and effective implementation of credit control policies.

However, outstanding consumer debts owed to local municipalities have increased by nearly R3 billion between December 2006 and December 2007 as most of them have not yet instituted the same debt management strategies as the metros.

The debts owed to district municipalities are mainly outstanding RSC levies, which are still on the books of the municipalities as they were collectable until June 2008.

Closer scrutiny shows that as at December 2007, metros were owed almost 35 per cent of their total annual budgets, local municipalities 39 per cent and district municipalities 11 per cent. A further breakdown shows that residents owe almost 60 per cent of the total amount, while national and provincial government owes 20 per cent with businesses owing the remaining 20 per cent for all categories of municipalities.

Table 3.6 Debtors age analysis, 31 December 2006 and 31 December 2007

	0 - 30 Days		31 - 60 Days		61 - 90 Days		Over 90 Days		Total	
R thousand	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Debtors analysis as at 31 December 2007										
Category A (Metros)	3 719 555	14.7%	1 300 603	5.1%	868 440	3.4%	19 493 137	76.8%	25 381 736	57.4%
Category B (Locals)	1 996 506	11.2%	818 689	4.6%	792 657	4.4%	14 261 829	79.8%	17 869 682	40.4%
Category C (Districts)	96 463	10.3%	32 842	3.5%	47 240	5.1%	758 865	81.1%	935 409	2.1%
Total	**5 812 524**	**13.2%**	**2 152 134**	**4.9%**	**1 708 337**	**3.9%**	**34 513 831**	**78.1%**	**44 186 827**	**100.0%**
Debtors analysis as at 31 December 2006										
Category A (Metros)	3 339 731	11.8%	1 130 074	4.0%	739 697	2.6%	22 990 769	81.5%	28 200 271	64.0%
Category B (Locals)	1 557 068	10.4%	650 283	4.4%	755 874	5.1%	11 939 153	80.1%	14 902 377	33.8%
Category C (Districts)	80 010	8.5%	29 786	3.2%	52 010	5.5%	783 487	82.9%	945 293	2.1%
Total	**4 976 809**	**11.3%**	**1 810 143**	**4.1%**	**1 547 581**	**3.5%**	**35 713 409**	**81.1%**	**44 047 941**	**100.0%**
Movement between 2006 and 2007										
Category A (Metros)	379 824		170 529		128 743		-3 497 632		-2 818 535	
Category B (Locals)	439 438		168 406		36 783		2 322 676		2 967 305	
Category C (Districts)	16 453		3 056		-4 770		-24 622		-9 884	
Total	**835 715**		**341 991**		**160 756**		**-1 199 578**		**138 886**	
Growth rate between 2006 to 2007										
Category A (Metros)	11.4%		15.1%		17.4%		-15.2%		-10.0%	
Category B (Locals)	28.2%		25.9%		4.9%		19.5%		19.9%	
Category C (Districts)	20.6%		10.3%		-9.2%		-3.1%		-1.0%	
Total	**16.8%**		**18.9%**		**10.4%**		**-3.4%**		**0.3%**	

Source: National Treasury local government database

Expenditure trends

Table 3.7 shows that actual expenditure by all categories of municipalities has been increasing annually by 14.3 per cent from R85.9 billion in 2003/04 to R128.1 billion in 2006/07 and is set to increase by 6.9 per cent to R156.5 billion over the medium-term. Spending is set to increase by 22.8 per cent between 2006/07 and 2007/08 and then decline over the medium-term. This is driven primarily by the increase in capital expenditure associated, in large part, with the 2010 FIFA World Cup.

The slight dip in the outer year reflects two things. First, the phasing out of 2010 FIFA World Cup related spending. Second, the fact that multi-year budgeting is not yet sufficiently robust amongst municipalities.

Table 3.7 also shows the expenditure split between the different categories of municipalities. Metros account for 59 per cent of total local government expenditure. By virtue of their size, powers and functions and comparatively well established asset bases, metros have seen their spending rise at a comparatively stable real growth rate of 9.2 per cent and 9.8 per cent in 2004/05 and 2005/06 respectively, with an average annual growth rate of 7.5 per cent between 2003/04 and 2006/07. (For a more detailed analysis of spending patterns and other matters relating to metros, see Chapter 4 of this Review).

Table 3.7 Municipal budgets by category, 2003/04 – 2009/10

R million	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
	Outcome			Estimate	Medium-term estimates		
Category A (Metros)	50 565	57 526	66 232	73 544	90 519	94 478	92 464
Category B (Locals)	29 820	33 727	39 332	45 994	54 533	54 832	52 828
Category C (Districts)	5 464	5 908	7 318	8 569	12 243	11 311	11 222
Total	**85 850**	**97 162**	**112 882**	**128 106**	**157 294**	**160 620**	**156 514**
Percentage growth							
Category A (Metros)		13.8%	15.1%	11.0%	23.1%	4.4%	-2.1%
Category B (Locals)		13.1%	16.6%	16.9%	18.6%	0.5%	-3.7%
Category C (Districts)		8.1%	23.9%	17.1%	42.9%	-7.6%	-0.8%
Total		**13.2%**	**16.2%**	**13.5%**	**22.8%**	**2.1%**	**-2.6%**

Source: National Treasury local government database

The 231 local (category B) municipalities account for the second biggest portion of local government expenditure, at 35 per cent. These municipalities vary widely, from rural towns like Ulundi in KwaZulu-Natal or Makhuduthamaga in Limpopo to big cities that are the economic hubs in their regions like Emfuleni, Mangaung, Mbombela, Polokwane, Buffalo City and Rustenburg.

Per capita spending by municipalities

Per capita spending by each municipality varies greatly

Per capita spending by each municipality varies greatly. It is mostly determined by the demographics, the socio-economic context and the powers and functions in a particular municipality. It is also influenced by the history of local government in a particular area and consequently the maturity of the municipality.

Table 3.8 Municipal per capita spending by secondary city, 2003/04 – 2009/10

Rand	Population 2005	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
		Outcome			Estimate	Medium-term estimates		
Buffalo City	695 278	2 078	2 239	2 386	3 372	3 063	3 059	3 157
City of Matlosana	359 202	1 413	1 959	2 223	2 430	3 154	2 845	3 167
Drakenstein	194 417	2 410	2 637	3 118	3 357	4 190	4 495	4 813
Emalahleni	276 413	2 443	2 337	2 646	2 902	3 162	2 883	3 056
Emfuleni	658 420	2 034	2 426	2 229	2 877	2 800	2 534	2 629
George	135 409	2 954	3 797	4 681	5 271	6 632	6 482	6 935
Govan Mbeki	221 747	1 737	2 047	2 990	3 536	3 234	3 313	3 414
Madibeng	346 675	983	1 154	1 440	1 934	1 830	1 944	2 360
Mangaung	645 440	2 258	2 459	1 911	2 156	3 569	3 836	3 515
Matjhabeng	408 170	1 734	2 860	1 691	2 177	2 511	2 628	2 847
Mbombela	476 593	982	1 123	1 376	2 457	3 363	3 661	2 112
Mogale City	289 835	2 321	2 126	2 130	2 250	2 805	2 844	2 966
Msunduzi	552 837	2 340	2 523	2 933	2 761	3 549	3 759	3 967
Newcastle	332 981	1 262	1 138	1 360	1 874	2 047	–	–
Polokwane	508 277	1 298	1 553	1 755	1 157	4 719	4 471	2 515
Rustenburg	387 096	1 934	2 464	3 098	3 216	4 429	4 906	4 431
Sol Plaatje	201 465	2 470	2 396	2 753	2 843	3 652	3 775	3 860
Stellenbosch	118 709	2 906	3 374	4 123	4 248	5 544	5 784	6 149
Steve Tshwete	142 772	2 148	2 772	3 112	3 092	4 283	4 069	3 977
Tlokwe	128 353	2 488	2 828	2 799	2 977	3 516	3 752	3 963
uMhlathuze	289 190	2 387	2 579	2 850	3 664	4 571	4 671	4 522
Total	**7 369 279**	**1 920**	**2 198**	**2 320**	**2 684**	**3 436**	**3 393**	**3 221**

Source: Stats SA, Census 2005 and National Treasury local government database

Table 3.8 shows the population for 2005 and the per capita spending for the 21 secondary cities. The highest per capita spending in 2007/08 is in George at R6 632 per person, while the lowest is Madibeng (Brits: North West) at R1 830 per person.

Table 3.9 shows that municipalities in Western Cape spend the highest amount per capita, at R6 334 for 2007/08, while Gauteng municipalities spend on average R5 665 per capita. This is despite rapid increases in the populations of both these provinces. According to the Community Survey 2007, Gauteng gained 440 411 more households and 1.2 million more people. Western Cape gained 195 000 more households and 754 000 more people over the same period.

Table 3.9 Municipal per capita spending by province, 2003/04 – 2009/10

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
Rand		**Outcome**		**Estimate**		**Medium-term estimates**	
Eastern Cape	1 367	1 507	1 608	1 836	2 545	2 355	2 204
Free State	1 782	1 790	1 900	2 249	2 583	2 594	2 542
Gauteng	3 293	3 674	4 233	4 769	5 665	6 016	6 029
KwaZulu-Natal	1 678	1 883	2 104	2 353	2 814	2 847	2 882
Limpopo	674	759	975	1 129	1 903	1 836	1 492
Mpumalanga	973	1 058	1 362	1 708	2 130	2 149	1 980
Northern Cape	1 663	1 952	2 184	2 427	2 842	2 832	2 668
North West	1 132	1 326	1 837	2 113	2 477	2 816	2 640
Western Cape	3 201	3 946	4 755	5 316	6 334	6 363	6 235
Total	**1 931**	**2 185**	**2 539**	**2 881**	**3 538**	**3 613**	**3 520**

Source: Stats SA, Census 2005 and National Treasury local government database

The lowest municipal per capita spending is in Limpopo, where R1 903 was spent in 2007/08. Indeed the fact that per capita spending by municipalities is lowest in Limpopo, Mpumalanga and North West indicates that the low level of spending is probably linked to the historical under-development of local government in these regions. It also indicates the importance of efforts to grow the local economies, as well as the fact that a lot of work still needs to be done to address poverty in these provinces.

Operating expenditure

Municipalities' actual operating expenditure increased in real terms by 4.6 per cent annually from 2003/04 to 2006/07 and is estimated to grow by 4.1 per cent in the medium-term.

Personnel costs account for the largest component of operating expenditure

Personnel costs account for the largest component of operating expenditure, averaging 29.4 per cent of total operating expenditure. Between 2003/04 and 2006/07, real growth in personnel expenditure is 3.3 per cent and is set to increase by 5.8 per cent over the medium-term. The higher nominal year-on-year increase in personnel expenditure of 8.9 per cent for the period 2003/04 to 2006/07 does not include amounts spent on private contractors and consultants working for municipalities. (For a detailed discussion on personnel trends in local government, refer to Chapter 12 of this Review).

Table 3.10 Municipal operating expenditure, 2003/04 – 2009/10

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
R million		Outcome		Estimate		Medium-term estimates	
Operating expenditure							
Employee costs	21 577	23 433	25 015	27 895	34 820	36 354	38 433
Remuneration of councillors	596	787	955	1 417	–	–	–
Repairs and maintenance	4 459	4 868	5 245	5 925	8 532	8 943	9 587
Depreciation and amortisation	2 505	3 945	4 253	4 980	–	–	–
Finance charges	4 216	3 409	3 123	3 180	7 483	8 029	8 759
Materials and bulk purchases	17 198	18 243	19 480	21 481	23 827	25 027	26 715
Grants and subsidies	1 435	2 021	2 141	2 339	–	–	–
Other expenditure	19 742	25 557	27 604	28 884	42 897	43 016	42 683
Total expenditure	**71 729**	**82 264**	**87 815**	**96 100**	**117 558**	**121 368**	**126 176**

Source: National Treasury local government database

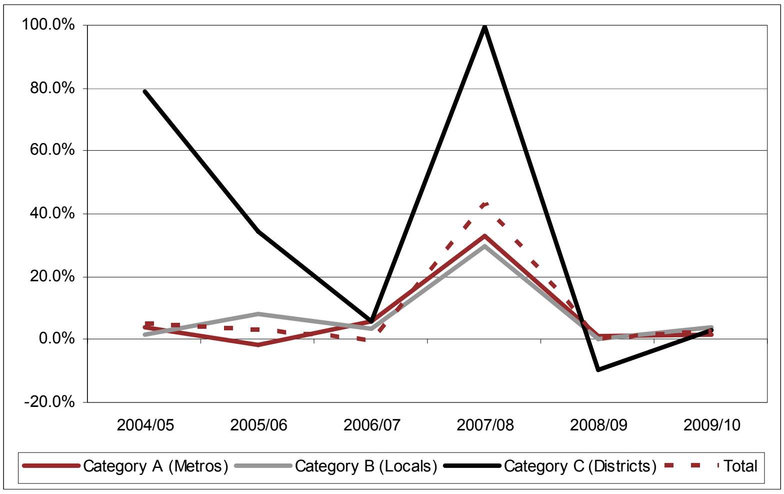
Bulk purchases take up almost 21.8 per cent of municipalities' operating expenditure and have remained stable over the seven-year period. The cost of bulk purchases of electricity and water have increased from R17.2 billion in 2003/04 to R21.5 billion 2006/07. Real growth in expenditure on bulk services has been minimal, amounting to an average of 2.1 per cent for the period 2003/04 to 2006/07. This reflects the below inflation increases in the price of bulk services for the period up until 2007/08. Current data indicates that municipal expenditure on bulk services is set to increase by 2.2 per cent between 2006/07 and 2010/11. However, given expected increases in the bulk prices of both electricity and water, expenditure on this item is likely to grow more rapidly than currently estimated by municipalities. (See chapters 7 and 8 for more detailed discussions on water and electricity expenditures).

Infrastructure has to be maintained to keep it in good working order

The growth in capital expenditure on new infrastructure assets in previously under-serviced areas means that over time, this infrastructure has to be maintained to keep it in good working order. In historically serviced areas, the continued maintenance of existing infrastructure also requires the same attention. Expenditure on repairs and maintenance has grown from R4.5 billion in 2003/04 to R8.5 billion in 2007/08 and will be increasing by R1 billion over the medium-term. In real terms this represents an average annual increase of 4.3 per cent between 2003/04 and 2006/07 and is set to increase further by 11.6 per cent in the medium-term. Yet maintenance expenditure remains low, constituting only 6.6 per cent of total expenditure since 2003/04. It is projected to remain at this level over the medium-term while the asset base of municipalities continues to grow. Ideally allocations to repairs and maintenance should be directly linked to the life-cycle management of municipal assets. However, in most municipalities expenditure on maintenance tends to be reactive, rather than proactively determined as part of a routine and periodic maintenance programme linked to managing municipal assets. What a municipality should be spending on maintenance will depend on how effectively it has maintained its assets in the past, the age of its assets and the extent of utilisation of its assets. However, given existing backlogs, most municipalities should probably be budgeting between 10 per cent and 15 per cent of operating expenditure for repairs and maintenance.

Figure 3.1 shows that growth trend for repairs and maintenance was low between 2003/04 and 2006/07, picks up in 2007/08 and then dips over the medium-term. As mentioned above, the medium term trend suggests a lack of multi-year budgeting skills and proper asset management processes in some municipalities. It is anticipated that with increased emphasis being placed on better asset management, the budget for repairs and maintenance will be revised upward in future years.

Figure 3.1 Repairs and maintenance real expenditure growth, 2004/05 – 2009/10



Source: National Treasury local government database

Capital expenditure

Spending on municipal infrastructure has increased from R10.7 billion in 2003/04 to R20.9 billion 2006/07 and is set to increase by nearly R10 billion over the medium-term. In real terms this amounted to an average annual growth of 18.5 per cent between 2003/04 and 2006/07. However, the real growth rate is set to decline to 7.6 per cent over the medium-term.

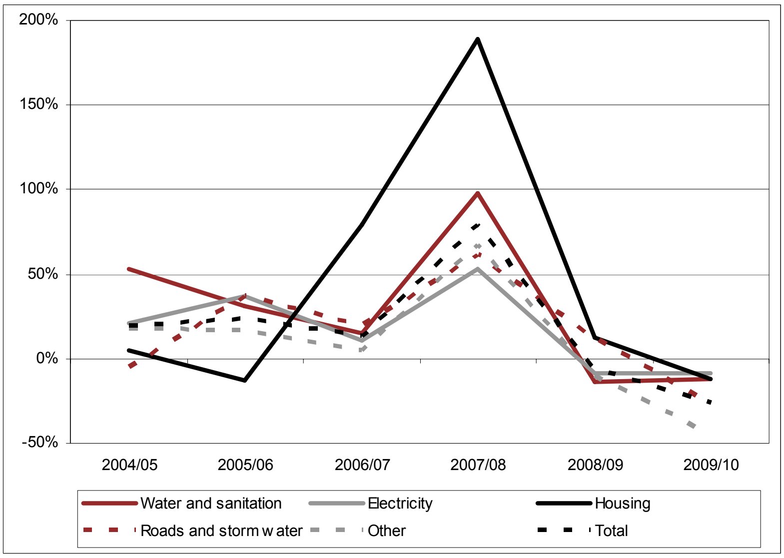
Table 3.11 Municipal capital expenditure, 2003/04 – 2009/10

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
R million	Outcome			Estimate	Medium-term estimates		
Water and sanitation	1 839	2 925	4 014	4 957	10 397	9 434	8 664
Electricity	1 267	1 599	2 295	2 725	4 426	4 255	4 063
Housing	658	718	658	1 269	3 893	4 586	4 221
Roads and storm water	1 775	1 751	2 517	3 222	5 536	6 466	5 013
Other	5 157	6 329	7 747	8 718	15 484	14 510	8 376
Total	**10 696**	**13 323**	**17 232**	**20 891**	**39 736**	**39 252**	**30 337**

Source: National Treasury local government database

Figure 3.2 shows that the real growth in capital spending between 2003/04 and 2006/07 was most significant in water and sanitation, at 32 per cent, followed by spending on electricity infrastructure, at 22.4 per cent. Growth in housing expenditure, though not a major function of municipalities, also showed an upswing at 18 per cent.

Figure 3.2 Real growth in capital expenditure, 2004/05 – 2009/10



Source: National Treasury local government database

Growth in expenditure on roads and storm water also increased significantly, at 15.7 per cent in real terms between 2003/04 to 2006/07. Other capital expenditure forms a significant portion of total capital expenditure (averaging 43.1 per cent) and comprises of land and buildings, fleet vehicles, specialised vehicles like ambulances, computers and so on. Spending on this item has grown at a real average annual rate of 13 per cent between 2003/04 and 2006/07, but growth is set to decline to a negative 6.2 per cent. This is also attributable to the lack of planning that underpins the outer years' projections.

Key issues in municipal budgets

Growing grant dependence

The growth in government transfers has occurred at a faster pace than the increase in own revenue generated by municipalities. This has created a situation where municipalities are increasingly dependent on grants to fund their operating costs. This is creating a dependency syndrome, which in future might be unsustainable. The equitable share constituted 8.6 per cent of the total operating revenue in 2003/04. This has risen to an estimated 17.5 per cent in 2007/08.

Inadequate maintenance expenditure

Among the reasons for the low expenditure on repairs and maintenance is the ease with which these expenditures can be deferred in favour of new capital projects or other operating costs. This results in the degradation of the value of assets and the need for their replacement earlier than might otherwise be the case. Two factors appear to underlie this problem. First, the under-pricing of municipal services relative to their true cost of delivery, including maintenance costs. Second, poor management practices in municipalities, particularly the absence of up to date asset registers, often result in maintenance schedules either not being set or being ignored.

Outstanding consumer debts

Most municipalities have failed to overcome the challenge posed by outstanding consumer debts

Most municipalities have, as yet, failed to overcome the challenge posed by outstanding consumer debts. If municipalities had collected half of these debts, they would have had about 18 per cent more revenue with which to fund delivery of services. This would have added substantially to their ability to address service delivery backlogs.

The increase in outstanding consumer debts also highlights possible governance problems. Good governance includes the ability of an organisation to implement adopted policies. Unfortunately, many municipalities pay lip-service to the implementation of their credit control policies.

The amount of debts that municipalities choose to write off as uncollectable impacts on the amount of debt older than 90 days in the debtors' age analysis. Municipalities appear to be resistant to write-off debt because there is a perception that this will send a negative signal to communities regarding the consequences for non-payment. This is despite the fact that all avenues may have been exhausted to collect the debt. Municipalities should ensure that arrear debtors are not inflated by the ongoing inclusion of debtors that are not collectable. This will require council to approve policies to at least annually review and address this issue.

Under-pricing of services

The over reliance by municipalities on national grants points to the possibility of under-pricing of services. This is more so even in services that have the potential to finance themselves. This practice has the potential to negatively affect investments in repairs and maintenance of existing municipal infrastructure.

Conclusion

Slow but steady progress is being made by local government since the introduction of new legislation to govern municipalities. This is evidenced by a healthy growth in municipal revenues and expenditure.

However, the disparities between the per capita expenditure levels between municipalities are still very large. This highlights the importance of national government transfers to local government, particularly to the poorer municipalities. However, it also highlights the need for municipalities to price their services correctly, so as to ensure they are able to fund their services on a sustainable basis. Lastly, the importance of having sound indigent policies, linked to robust debt collection strategies cannot be over emphasised.