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**TRENDS IN INTERGOVERNMENTAL FINANCES
ADDRESS TO THE NATIONAL COUNCIL OF PROVINCES
TREVOR MANUEL, MINISTER OF FINANCE
1 SEPTEMBER 2004**

Deputy Chair,
Honourable Members,

Ladies and Gentlemen

Members of the NCOP play an invaluable role in protecting the interest of provinces and local government. We in the National Treasury are of the view that we are allies of the NCOP in this endeavor. It is to this end, and not to meet any constitutional or statutory obligation, that we sought to publish the Intergovernmental Fiscal Review from time to time.

Towards the end of the second Parliament, the NCOP had become quite adept to using the IGFR as an instrument which serves both to facilitate the oversight function of provincial legislatures and to equip standing and portfolio committees to help understand spending trends.

This year we decided not to publish a full IGFR, but to limit the publication to an update on the last IGFR, but it is still a document of 152 pages with annexures of 147 pages.

We are tabling this document in this House because the NCOP has a critical oversight role to play in monitoring government expenditure, given the size of our transfers to provincial and local governments. In 2004/05 for example, we transfer 61,8 per cent of the available resource of R316 billion (contingency

reserve of R2,5 billion excluded) to these two spheres – R181,1 billion or 57,3 per cent to provinces, and R14,2 billion or 4,5 per cent to the local sphere. These transfers are effected through the Division of Revenue Act, which is arguably the most important budget legislation that the NCOP is asked to approve every year.

Trends in Intergovernmental Finances

I want to begin by giving you an example of why this document is important for Parliamentary accountability by looking at the education budget. The National Department of Education has a budget of R11,3 billion this year, yet its own spending budget is only R443 million if we exclude transfers to higher education institutions and other transfers. In contrast, the 9 provincial education departments have budgeted and will spend R64,8 billion this year. The question that arises is whether Parliament should not focus on the consolidated budget, namely the consolidated R64,8 billion provincial education budget and the R11,3 billion national budget, taken together. If Parliament were only to look at the national education budget, it would not see the whole picture on education.

For this reason, we have an expectation that all eleven education committees, those at Parliament and at every legislature, should jointly meet and workshop the specific chapter on education. Such a workshop will enable each committee to better perform its responsibility over education in its own legislature.

Deputy Chair, the *Trends in Intergovernmental Finances* we table before you today provides information on the 2004 provincial budgets, and the 2003-04 municipal budgets. It accounts for public expenditures for the last three financial years - that is 2000/01 to 2002/03, as well as the preliminary outcome for the 2003/04 financial year. It spells out in more detail spending plans for the nine provinces and 284 local governments, taking the focus on service delivery one step forward and enabling users to compare provincial and municipal service delivery standards and achievements.

We are confident that the NCOP will facilitate the participation of every provincial legislature and municipal council in the accountability processes by spreading the information in this document as widely as possible.

The 2004 provincial budgets consolidated in this document represent a real expression of cooperative governance. They reflect strong alignment to national priorities articulated in the *2004 Budget Review*. Provinces are budgeting R186,7 billion for their 2004/05 budgets, of which R152,9 billion or 82 per cent is budgeted for the three social services education, health and social development.

Local government budgets for 2003-04 total about R86 billion, including capital expenditure of R16,7 billion. The budgets of our 6 Metros' alone comprises 58,8 per cent of the total municipal budget.

This document allows us to compare between different spheres and different functions. One of the important trends to look at from a delivery perspective is to ensure that we maximize the budgets for the delivery of services, by reducing the costs of personnel (which we now call compensation of employees). Such a trend has been the case in provinces, where the downward trend on personnel started more than three years ago, and is set to continue over the MTEF, resulting in a further decline in the share of personnel from 57,7 per cent in 2000/01 to 44,5 per cent in 2006/07. This will release more resources for delivery, with non-personnel expenditure expected to rise to over 55 per cent over this period. This is in stark contrast to local government, where its share of personnel expenditure has been increasing rapidly and is now at 43 per cent of its operating budget if bulk purchases of water and electricity are excluded from this operating budget. This means that it will be even harder for the local sphere to deliver, if it does not prioritise containing its personnel expenditure.

Income support continues to be one of our weapons for fighting poverty, in the short term. One of government's greatest achievements is the increase in the number of social grant beneficiaries, which increased from 2,9 million in April

2000 to 7,9 million in April 2004. We expect that beneficiary numbers will grow in excess of an estimated 20 per cent per year. This will see budgeted total spending on social security grants rise from R37,1 billion in 2003/04 to R54,4 billion in 2006/07. The share of social development spending will rise to 28 per cent of provincial spending in 2006/07 raising social security expenditure to over 3 per cent of GDP. This is a trend that Honourable members must pay to attention in future years, if we want to ensure that we have sufficient policy room to promote growth-generating policies. A particular concern is the rapid growth in disability beneficiaries, which has risen from over 612 614 beneficiaries in April 2000 to 1 270 964 beneficiaries in April 2004, resulting in disability spending rising from R4 billion to R10,2 billion in this period.

Education

Total education spending grows by 1,6 per cent in real terms from R60,3 billion in 2003/04 to R73,7 billion in 2006/07. The highest growth is in non-personnel non-capital expenditure, which rises from R5,2 billion to R7,8 billion over this period. These amounts, however, exclude transfer payments. This is expected to help the sector allocate increasing amounts to learner support materials and reinforce improvements in the quality of school education.

The document also deals with outputs in education. On the one hand, it considers provincial performance in respect of matriculation pass rates. On the other, it reviews provincial attainment in maths and science – key requirements for a skilled work force. Some of us are still trying to understand why Limpopo's matric pass rates in maths and science are much better than those of some of the provinces that spend more per learner than Limpopo. Perhaps this says a lot about efficiency of education spending in that province. I am not saying this because the Governor of the Reserve Bank and DG of Treasury both come from Limpopo!

Health

Provincial health budgets are projected to grow by 3,3 per cent in real terms to R47,4 billion in 2006/07.

Improving health service delivery largely depends on having the right skills in the right place. Implementation of the scarce skills strategy and rural allowances which commenced last year is on track. Additional resources over the next three years provide for the costs of hiring and deploying personnel with scarce skills such as doctors and pharmacists.

Quality health care also depends on adequate medicine and drug availability. Over the next three years, strong growth in non-personnel spending in health should allow our hospitals and clinics to ensure sufficient supplies of medicines, drugs and other medical necessities. Health budgets also include a conditional grant of R3,5 billion to be spent on HIV and Aids programmes over the next three years.

NON-SOCIAL SERVICES

In addition to social services, provinces also budget for housing, provincial roads, agriculture, economic affairs, environment and tourism, and other administrative functions. Spending on non-social services functions, including housing, rises from R31,2 billion in 2003/04 to R33,7 billion 2004/05 which comprises about 18 per cent of total provincial expenditure. It is set to rise to R38,3 billion by 2006/07. Deputy Chair, included in these amounts are funds earmarked for housing delivery and the Expanded Public Works Programme that we referred to in the Budget Speech in February.

Honourable members will be pleased to know that in the First Decade of Democracy, Government spent about R27,6 billion on its housing programme. The Department of Housing has funded over 1,6 million housing opportunities.

Notwithstanding this progress, some challenges still remain, as we also need to create sustainable communities when we build houses.

LOCAL GOVERNMENT SERVICES

Members will note that the information available for the local sphere is not as reliable as that for provinces. The implementation of the Municipal Financial Management Act this year should lay the basis for improving the quality of this information over the next three years.

I have already referred to the challenge facing local government in containing its personnel expenditure. It needs to do so to address the substantial backlogs in the provision of drinking water, proper sanitation and electricity for all our people. The 2001 Census reported a backlog of 11 per cent and 41 per cent in water and sanitation respectively and a 34 per cent backlog in domestic electricity. The major backlog for both electricity and water is in the rural areas, where on-grid electricity and piped water is not economical, and hence other types of supply mechanisms are required. This impacts negatively on Government's call for the rollout of free basic services as one of its major policy initiatives.

A major challenge that local government has to meet is to ensure that its finances remain sound as we restructure the distribution of electricity and create the first REDs.

The recently introduced Municipal Infrastructure Grant will greatly assist in reducing backlogs over a ten-year period. In total, R15 billion will be available through the Municipal Infrastructure Grant over this MTEF of which R8,1 billion has been allocated for water and sanitation. It is our hope that municipalities will rise to the challenge of generating jobs when using these funds, in line with the expanded public works programme.

CONCLUSION

Deputy Chair, I want to end by reiterating the opportunity and challenge this document poses for Parliament. If we are to take our commitment to deliver basic services seriously, every relevant committee in both Houses of Parliament and in the nine provincial legislatures should be interrogating the content of this document. So should every municipal council. I am optimistic that every relevant portfolio and select committee will convene hearings on each relevant chapter, possibly joint hearings involving both committees here at Parliament together with the nine provincial portfolio committees.

Deputy Chair, I submit to this House the 2004 Trends in Intergovernmental Finances.