

# Introduction and overview

*The Medium Term Budget Policy Statement sets out the economic context and fiscal framework within which the 2002 Budget will be compiled. The proposed division of revenue makes provision for strong real growth over the next MTEF period in national, provincial and local government expenditure.*

## Introduction

This year's *Medium Term Budget Policy Statement* confirms Government's firm intent to address South Africa's social and development challenges within a consistent, growth-oriented fiscal and budgetary framework.

As in the past, the Statement provides a concise overview of macroeconomic developments and fiscal policy considerations. Developments in tax policy are summarised and the proposed medium term expenditure framework (MTEF) for the 2002 Budget is outlined. The key elements of the division of revenue between national, provincial and local government are set out and intergovernmental financial relations are briefly explored.

Since the 2001 Budget was tabled in Parliament in February this year, an already deteriorating international economic trend has been rocked by a shocking series of attacks on the United States and the resulting war against suspected terrorist organisations and the Taliban. The slowdown in world growth and international trade has deepened and may persist into a period of negative growth or recession in several major economies.

The rand has weakened sharply, reflecting in part the flight from perceived risk and to safe havens in global financial

*The MTBPS provides an update on economic and fiscal developments since the February Budget, and outlines proposals for the 2002 MTEF*

*Although international prospects have weakened, fiscal and monetary policies are aimed at sustaining the momentum of South Africa's economic growth and development*

markets. While our trade performance in the first nine months of 2001 has remained impressive, government revenue has grown strongly and there has been a modest recovery in capital spending, confidence in the South African economy has been dented by international events. Growth this year will be somewhat slower than projected in the February budget.

However, South Africa's balance of payments position is healthy and the public finances are sound. Against this background, Government is able to respond to the downturn in the economy with an appropriate mix of tax relief, accelerated infrastructure spending and support for social services and municipal infrastructure development, together with an easing in monetary policy. These measures are aimed at supporting the momentum of growth and economic development.

The *Medium Term Budget Policy Statement* outlines this response and proposes a medium term framework for the 2002 Budget.

## **Budget reform and service delivery improvement**

*Budgetary and financial management reforms focus on strengthening accountability and improving the alignment of planning, budgeting and service delivery*

Government's commitment to improving service delivery calls for modernisation and transformation across a wide range of public administration functions and systems. Budgetary and financial management reforms are key elements of this challenge. Over the past five years, significant progress has been made.

Institutional and legislative changes in 1997 led to the introduction of a new intergovernmental system with three spheres of government: national, provincial and local. Each has its own functions and spending responsibilities. Each has responsibility for its own financial management and expenditure planning, within a well-defined legislative framework.

In the 1998 Budget, Government set out three-year rolling spending plans for national and provincial departments under the Medium Term Expenditure Framework - the MTEF. Medium-term budgeting reinforces the link between Government's policy choices, its budget and the delivery of services, which serves to strengthen political decision-making and accountability.

Steps to deepen the budget process and better align policy, planning and budgeting allow Government to consider policy priorities earlier in the budget cycle. Reforms to the division of revenue process enable the relevant national departments, provinces and local government to have an earlier discussion on the division of revenue between the three spheres of government, enhancing co-operative governance.

These steps are strengthened by implementation of the Public Finance Management Act in 2000. The Act sets out a legislative framework for modernising financial management and enhancing accountability in the public sector. Managers now have greater flexibility to manage but are held accountable for the use of public resources to deliver services.

*The PFMA provides the legislative framework for enhanced accountability*

Looking ahead, Government will focus on steps to:

- Align and integrate the planning, budgeting and reporting processes
- Develop and implement strategic and operational plans within agreed medium-term allocations and reporting on past performance in published annual reports
- Present measurable objectives and outputs to assess performance and progress in service delivery
- Introduce generally recognised accounting practice and procurement reforms across the public sector.

*Better planning, budgeting and reporting on public expenditure will contribute to measuring progress with service delivery*

The 2001 Budget introduced the new national budget format. The *Estimates of National Expenditure* outlines policy developments, legislation and other factors affecting expenditure alongside departmental spending plans. Details of departmental outputs and performance measures provide key information on progress in service delivery.

Similar provincial budget format reforms have contributed to enhanced accountability for provincial services over the last few years.

This year, changes to the formats of the national and provincial adjustments budgets will enable Parliament and the public to gain a better understanding of the proposed amendments to the main February estimates.

*This year the format of the Adjustments Budget is revised, in line with the structure of the main Estimates of National Expenditure*

## Overview of the MTBPS

This *Statement* is the outcome of an extended consultative process in which national departments, provincial treasuries

*The MTBPS is the outcome of an extended policy review process*

and representatives of local government review their policies and programmes and table spending plans for consideration. The Budget Council, the Ministers' Committee on the Budget and Cabinet take the lead in assessing priorities and evaluating policy options. The budget process is informed by a review of the developments in the economy and the international environment and by Government's macroeconomic, social and development objectives.

### **Policy priorities for the 2002 Budget**

*Addressing poverty and vulnerability remain at the centre of Government's Reconstruction and Development Programme*

In shaping this policy framework for the 2002 Budget, Cabinet has been clear that addressing poverty and vulnerability remains the central challenge in setting budget priorities and preparing spending plans. Government's Reconstruction and Development Programme, now in its eighth year, has delivered houses, electricity, water, land, free health care, education and training, protection of civil and workers' rights and improved transport and communication to millions of South Africans. But the war on poverty is not over. Several of these programmes have shifted in direction or gathered new impetus following a period of policy review and consolidation. And in other areas, there are new challenges to address.

*The MTBPS outlines a balanced framework of spending on social, economic, protection and administrative functions*

Alongside our own social and development policy commitments, South Africa is playing a leading part in the New Partnership for the Development of Africa. Ranging from eco-tourism to the information superhighway, from regional trade promotion to participation in United Nations peace-keeping operations, new engagements on the continent and in partnership with other developing nations have brought new opportunities and demands on resources.

The *Medium Term Budget Policy Statement* sets out the framework within which Government seeks to balance the competing claims on the State's budgetary resources - education, health, municipal and welfare services; defence, justice and crime prevention; economic services and infrastructure development; and the central administrative and diplomatic responsibilities of the national government.

### **Macroeconomic developments**

*Economic growth is projected to rise from 2,4% this year to 3,5% a year over the MTEF period*

Chapter 2 of this *Statement* draws attention to the progress made in reducing inflation, growth and diversification of trade and improvements in productivity across many sectors of the economy. However, formal job creation remains

disappointing and both savings and investment need to be reinforced if faster economic growth is to be sustained in the years ahead. Revised projections indicate economic growth of 2,4 per cent this fiscal year, rising to average about 3,5 per cent a year over the forthcoming MTEF period.

### **Fiscal policy and taxation**

In Chapter 3, fiscal policy considerations and the budget framework are set out. The growth-oriented fiscal stance announced in last year's *Medium Term Budget Policy Statement* remains a key point of departure for the years ahead. Government aims to reinforce investment and job creation, broaden and enhance public service delivery and target additional resources at reducing poverty and vulnerability. In a context of heightened international uncertainty, South Africa's economic growth and development can build on a stable and robust fiscal stance and budget framework.

Chapter 4 reviews developments in tax policy. Tax stability, certainty and an internationally competitive and attractive rate structure are critical for promoting investment and economic activity. Against the background of the tax reforms undertaken in the past two years, the 2002 Budget will herald a period of consolidation. The personal income tax structure will again be adjusted to provide relief to lower and middle income taxpayers and with a view to narrowing the gap between the maximum personal rate and the rate of tax on companies. Further amendments to the list of public benefit activities will extend the range of organisations qualifying for tax-exempt status. Refinements in the tax treatment of the banking sector are in progress. During the course of next year, a thorough review of the tax treatment of retirement saving will be undertaken.

*Fiscal policy and tax proposals aim to reinforce investment and boost public service delivery*

Founded on the success of the SA Revenue Service in strengthening tax administration, the budget framework provides for steady growth in revenue together with further relief in tax rates and a fairer distribution of the burden of tax.

*Robust revenue growth reflects strengthening of tax administration and sound revenue policies*

### **The MTEF and division of revenue**

Chapter 5 describes changes to the MTEF and the division of revenue proposed for the 2002 Budget. Expenditure increases will be focused on health services and social grants, municipal infrastructure and housing, improved police and justice services and critical administrative services to citizens. Budgetary provision for the

*Expenditure increases will focus on health services, municipal infrastructure and housing and improved policing*

electrification programme will be stepped up. It is noted that shortfalls in the operating budgets of the Post Office and Unemployment Insurance Fund will have to be met over the next three years, allowing for a period of restructuring in order to restore self-sufficiency. The proposed budget framework provides for strong growth in transfers to municipalities, recognising their critical role in extending basic services to under-served households and communities.

The provincial and local government shares of the national budget are described in more detail in Chapter 6. The equitable share allocations to provinces are summarised and various conditional grant programmes in support of provincial and municipal services are indicated. Details of these funding flows are set out in the annual Division of Revenue Bill.

## Conclusion

The 2001 *MTBPS* sets out the economic context for the 2002 Budget and outlines the fiscal policy considerations, tax policy and expenditure priorities that underlie Government's budget proposals for the next three years.

*Comment on the MTBPS  
should be forwarded to the  
National Treasury*

The *Medium Term Budget Policy Statement* aims to encourage informed debate in Parliament and engagement throughout civil society with the social, economic and developmental challenges that the Budget must address.

Comment on this *Statement* and the proposals set out for the 2002 Budget can be emailed to [mtbps@treasury.gov.za](mailto:mtbps@treasury.gov.za), or posted to:

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