BUDGET 2021

RENEWING THE ECONOMY AND RESTORING PUBLIC FINANCES

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

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OVERVIEW

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- The 2021 Budget is framed by the two policy objectives set out in the 2020 Medium Term Budget Policy Statement: promoting economic recovery and returning the public finances to a sustainable position
- Government's immediate priority is to support a rapid return to economic growth in the wake of the COVID-19 lockdowns. A mass vaccination programme, provided free of charge, will support a reopening of the economy and GDP growth of 3.3 per cent this year.
- Fiscal policy continues to focus on short-term economic support, fiscal consolidation and debt stabilisation. The consolidated budget deficit, which reaches a record 14 per cent of GDP in 2020/21, will narrow to 6.3 per cent of GDP in 2023/24. Government remains on track to achieve a primary fiscal surplus by 2024/25 and stabilise debt in the following year.
- Tax revenue estimates, while higher than projected in October 2020, are R213.2 billion lower than projected in the 2020 Budget. To support the economy, R40 billion in previously proposed tax measures will be withdrawn.
- The 2021 Budget proposes total consolidated spending of R2.02 trillion in 2021/22, with 56.8 per cent of allocations going to learning and culture, health and social development. Rising debt-service costs consume R269.7 billion, or 13.4 per cent of the budget.
- Over the 2021 MTEF period, after budgeting for debt-service costs, the contingency reserve and provisional allocations, 48.7 per cent of nationally raised funds are allocated to national government, 41.9 per cent to provinces and 9.4 per cent to local government.
- Structural reforms will lower barriers to faster, inclusive growth by improving access to reliable electricity, water and sanitation services; enabling cost-effective digital services; promoting the green economy; and supporting industries with high employment potential, such as tourism and agriculture.

GLOBAL GROWTH PROSPECTS BOOSTED BY VACCINE ROLLOUT AND STIMULUS

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Table 2.1 Economic growth in selected countries

Region/country Percentage	2018	2019	2020 Estimate	2021	2022
				Forecast	
World	**3.5**	**2.8**	**-3.5**	**5.5**	**4.2**
Advanced economies	**2.2**	**1.6**	**-4.9**	**4.3**	**3.1**
United States	3.0	2.2	-3.4	5.1	2.5
Euro area	1.8	1.3	-7.2	4.2	3.6
United Kingdom	1.3	1.4	-10.0	4.5	5.0
Japan	0.3	0.3	-5.1	3.1	2.4
Emerging and developing countries	**4.5**	**3.6**	**-2.4**	**6.3**	**5.0**
Brazil	1.3	1.4	-4.5	3.6	2.6
Russia	2.5	1.3	-3.6	3.0	3.9
India	6.1	4.2	-8.0	11.5	6.8
China	6.8	6.0	2.3	8.1	5.6
Sub-Saharan Africa	**3.3**	**3.2**	**-2.6**	**3.2**	**3.9**
Nigeria	1.9	2.2	-3.2	1.5	2.5
South Africa[1]	0.8	0.2	-7.2	3.3	2.2
World trade volumes	**3.9**	**1.0**	**-9.6**	**8.1**	**6.3**

1. National Treasury forecast

Source: IMF World Economic Outlook, January 2021

- Robust growth rates are predominantly a recovery following the sharp contraction in 2020, with the recovery expected to remain fragile and uneven across countries and regions.

DOMESTIC ECONOMIC OUTLOOK

Table 2.2 Macroeconomic performance and projections

	2017	2018	2019	2020	2021	2022	2023
Percentage change		**Actual**		**Estimate**		**Forecast**	
Final household consumption	2.1	1.8	1.0	-5.9	2.9	2.4	2.0
Final government consumption	0.2	1.9	1.5	1.2	-0.1	-1.6	-1.7
Gross fixed-capital formation	1.0	-1.4	-0.9	-18.4	-2.4	3.9	3.9
Gross domestic expenditure	1.9	1.0	0.7	-8.9	3.5	2.7	1.6
Exports	-0.7	2.6	-2.5	-10.9	5.7	3.0	2.8
Imports	1.0	3.3	-0.5	-16.5	6.3	4.6	2.5
Real GDP growth	**1.4**	**0.8**	**0.2**	**-7.2**	**3.3**	**2.2**	**1.6**
GDP inflation	5.3	3.9	4.0	4.6	3.5	3.7	4.1
GDP at current prices (R billion)	**4,654**	**4,874**	**5,078**	**4,935**	**5,273**	**5,590**	**5,915**
CPI inflation	5.3	4.6	4.1	3.3	3.9	4.2	4.4
Current account balance (% of GDP)	-2.5	-3.5	-3.0	1.7	-0.1	-1.0	-1.4

Sources: National Treasury, Reserve Bank and Statistics South Africa

- The National Treasury projects real economic growth of 3.3 per cent in 2021, from a low base of -7.2 per cent in 2020. Growth is forecast to moderate to 2.2 per cent in 2022
- A successful vaccine rollout is likely to boost domestic economic growth, enabling renewed trade and releasing pent-up demand. Conversely, a slow rollout poses the most significant threat to economic recovery.
- The far-reaching COVID-19 economic impacts exacerbated the poor outcomes of the last decade. Broader structural reforms are required to entrench an economic recovery characterised by growing investment and job creation.

PROGRESS HAS BEEN MADE ON ECONOMIC RECOVERY PLAN BUT DECISIVE ACTION IS REQUIRED TO INSPIRE CONFIDENCE

- Generating electricity
  - Embedded generation regulation will be eased within three months; emergency power procurements bids as well as procurement of additional power in line with the IRP2019 will be announced in the coming weeks. Electricity regulations were amended to enable municipalities to procure power from IPPs.
  - Divisional managers and boards of directors have been appointed to support the restructuring of Eskom.
- Creating employment
  - By the end January 2021, over 430 000 jobs of varying duration had been supported through the stimulus and an additional 180 000 jobs are in the recruitment process.
- Supporting industrial growth
  - Investments have been made to support production in the poultry sector (R800 million); in clothing, textiles, footwear and leather (R500 million); and in the automotive sector (R16 billion). In addition, large users of sugar have agreed to procure at least 80 per cent of their supply from local growers.
- Infrastructure rollout
  - An infrastructure investment project pipeline worth R340 billion in network industries such as energy, water, transport and telecommunications has been developed. The blended finance Infrastructure Fund is preparing investments in student housing, digital communications, and water and sanitation.
- Creating an enabling business environment
  - In the past year, 125 000 new companies have been registered through the BizPortal platform, which makes it easier to register a business online.
  - Transnet is taking steps to ease congestion at the Port of Durban and reposition it as a southern hemisphere hub. It has begun improving port access roads, increased skills and capacity, and expanded operating hours.

OPERATION VULINDLELA IS ACCELERATING GROWTH REFORM IMPLEMENTATION

Operation Vulindlela, a joint initiative between the Presidency and National Treasury, is focusing on a subset of key reforms:

- Fast-tracking the procurement of additional electricity, improving municipal distribution and reducing the administrative burden for embedded generation.
- Ensuring that households using analogue televisions switch to digital signals by March 2022 so that there is sufficient spectrum to meet demand.
- Finalising policy to enable the rapid rollout of 5G infrastructure.
- Expanding the electronic visa system and waivers to support tourism.
- Reviewing the regulatory framework and processes that make it difficult to import scarce skills, including finalising the critical skills list.
- Finalising the draft White Paper on National Rail Policy to improve freight and commuter rail services.
- Corporatising the National Ports Authority and taking other measures to increase the efficiency and competitiveness of the ports.
- Reviving the Green Drop and Blue Drop programmes to strengthen water quality monitoring.

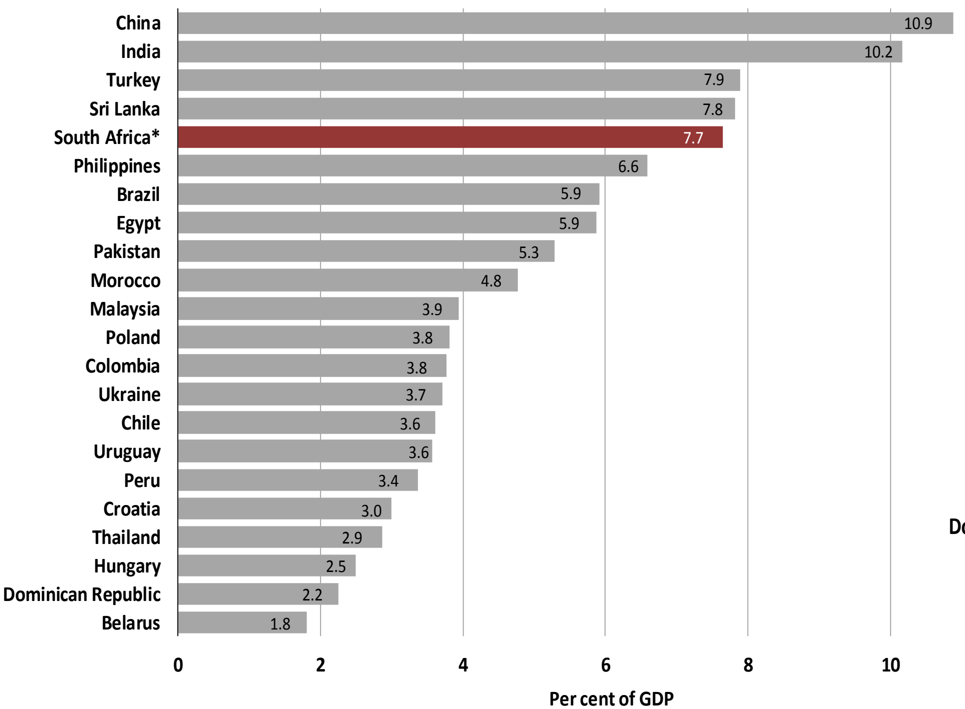
FISCAL STRATEGY

- South Africa's fiscal challenge is to balance the immediate need for support to the economy during the pandemic with ongoing efforts to close a large, pre-existing budget deficit. In this context, the fiscal strategy aims to:
  - Narrow the deficit and stabilise the debt-to-GDP ratio, primarily by controlling non-interest expenditure growth.
  - Provide continued support to the economy and public health services in the short term, without adding to long-term spending pressures.
  - Improve the composition of spending, by reducing growth in compensation while protecting capital investment.
- Efforts to reduce growth in the public-service wage bill remain on course, with the Labour Appeal Court of South Africa confirming that the National Treasury must certify the affordability and sustainability of wage agreements prior to their implementation.
- Significant risks remain. The global outlook is highly uncertain, with the economic recovery largely dependent on responses to COVID-19. Several state-owned companies are requesting additional funding. Negotiations on a new public-service wage agreement are set to take place this year.

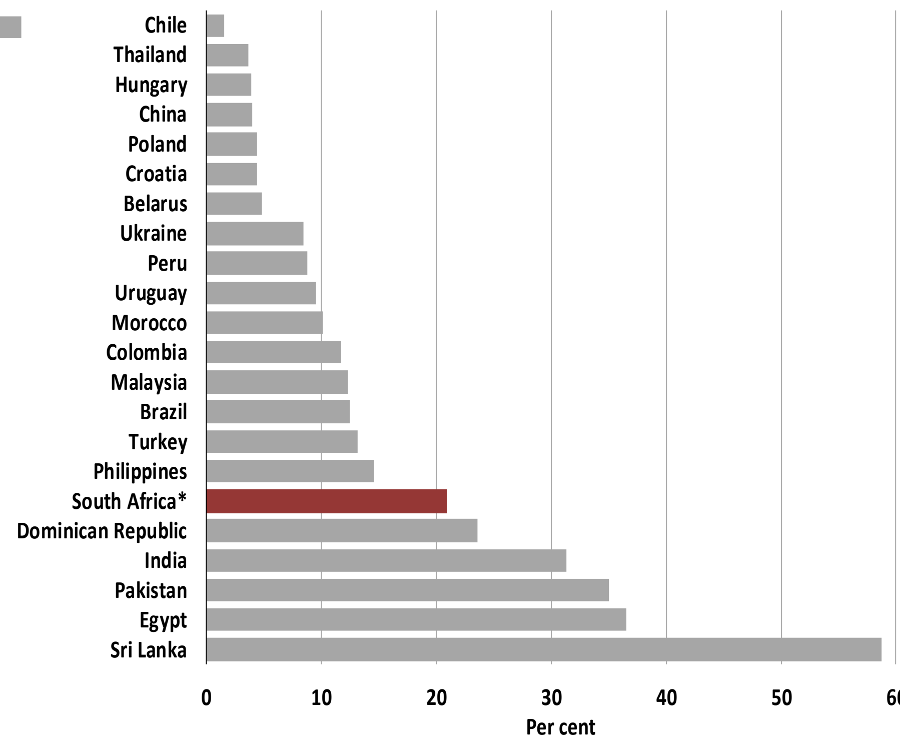
SOUTH AFRICA'S FISCAL POSITION IN GLOBAL CONTEXT

- Over the medium term, debt-service costs are expected to average 20.9 per cent of gross tax revenue. This is twice as large as the median for South Africa's peer group over the period.
- Similarly, South Africa's borrowing remains large by developing-country standards, and debt is projected to grow by 7 per cent of GDP over the next three years.

Average budget deficit, 2021–2023



Average debt-service costs as a share of revenue, 2021–2023



CHANGES IN TAX REVENUE SINCE 2020 BUDGET

- COVID-19 has resulted in elevated levels of uncertainty in economic and fiscal forecasting. This is reflected in large revisions to tax revenue.
- Relative to the 2020 Budget, gross tax revenue for 2020/21 is R213.2 billion below projections. At the time of the 2020 MTBPS, this shortfall was projected at R312.8 billion.
- The upward revision reflects improvements in personal and corporate income taxes, value-added tax, fuel levies and customs duties.
- Government will not implement the additional tax revenue measures announced in the 2020 MTBPS – R5 billion for next year, R10 billion per year in the following two years and R15 billion in 2024/25.

Table 3.3 Revised gross tax revenue projections

R million	2019/20	2020/21	2021/22	2022/23	2023/24
Revised estimate	**1 355 766**	**1 212 206**	**1 365 124**	**1 457 653**	**1 548 512**
Buoyancy	*1.16*	*2.39*	*1.44*	*1.15*	*1.07*
2020 MTBPS	**1 355 749**	**1 112 579**	**1 279 528**	**1 392 161**	**1 503 186**
Elasticity	*1.16*	*3.18*	*1.59*	*1.50*	*1.35*
2020 Budget	**1 358 935**	**1 425 418**	**1 512 194**	**1 609 657**	
Elasticity	*1.15*	*0.93*	*1.00*	*1.01*	
Projected improvement against 2020 MTBPS	17	99 627	85 597	65 492	45 326
Projected shortfall against 2020 Budget	-3 168	-213 212	-147 070	-152 004	

Source: National Treasury

2021/22 TAX PROPOSALS

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Table 1.3 Impact of tax proposals on 2021/22 revenue[1]

R million		Effect on tax proposals
Gross tax revenue (before tax proposals)		**1 365 124**
Budget 2021/22 proposals		**–**
Direct taxes		**-2 200**
Personal income tax		
Increasing brackets by more than inflation	-2 200	
Revenue if no adjustment is made	11 200	
Higher-than-inflation increase in brackets and rebates	*-13 400*	
Indirect taxes		
Taxes on international trade and transactions		**2 200**
Introduction of export tax on scrap metal	400	
Specific excise duties		
Increase in excise duties on alcohol	1 100	
Increase in excise duties on tobacco	700	
Gross tax revenue (after tax proposals)		**1 365 124**

1. Revenue changes are in relation to thresholds that have been fully adjusted for inflation

Source: National Treasury

- The 2021 Budget includes a higher-than-inflation adjustment to the personal income tax brackets.
- The expected revenue loss will be offset by an increase in excise duties on tobacco and alcohol.

CHANGES IN MAIN BUDGET NON-INTEREST EXPENDITURE

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Table 3.4 Adjustments to main budget non-interest expenditure since 2020 Budget

R million	2021/22	2022/23	2023/24	MTEF total
2020 Budget non-interest expenditure	**1 592 186**	**1 650 080**	**1 722 433**	**4 964 699**
Less: Contingency reserve	*5 000*	*5 000*	*5 000*	*15 000*
Allocated expenditure (2020 Budget)	**1 587 186**	**1 645 080**	**1 717 433**	**4 949 699**
Skills development levy adjustments	-2 772	-2 740	-936	-6 448
Baseline reductions	**-65 349**	**-90 122**	**-152 326**	**-307 797**
Programme baseline reductions and use of reserves	-39 043	-43 983	-80 311	-163 337
Wage bill reductions	-26 306	-46 139	-72 015	-144 460
Baseline allocations	**22 446**	**4 602**	**2 283**	**29 332**
COVID-19 response	15 345	3 000	–	18 345
Other allocations[1]	7 101	1 602	2 283	10 987
Provisional allocations	**11 000**	**1 000**	**1 000**	**13 000**
Allocated in 2021 Budget	**1 552 511**	**1 557 821**	**1 567 455**	**4 677 786**
Plus: Contingency reserve	*12 000*	*5 000*	*5 000*	*22 000*
2021 Budget non-interest expenditure	**1 564 511**	**1 562 821**	**1 572 455**	**4 699 786**
Change in non-interest expenditure since 2020 Budget	*-27 675*	*-87 259*	*-149 978*	*-264 913*

1. Includes the New Development Bank, financial support to state-owned companies and public entities and the rescheduling of some infrastructure reductions introduced in the 2020 MTBPS
Source: National Treasury

- Compared with the 2020 Budget, main budget non-interest expenditure decreases by a net amount of R264.9 billion over the medium-term expenditure framework period.
- Funding is set aside for the COVID-19 response and other interventions, including the public employment initiative, recapitalisation of the Land Bank, and modernisation of SARS systems.

FISCAL FRAMEWORK PROMOTES ECONOMIC RECOVERY

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- Given the continuing pandemic, the fiscal framework provides short-term support to low-income households and funding for the health policy response. Changes since the 2020 MTBPS include:
  - Three-month extensions of the special COVID-19 social relief of distress grant and the Unemployment Insurance Fund's Temporary Employer/Employee Relief Scheme, and funding for the public employment initiative and for provincial hospitals in 2021/22.
  - Up to R10.3 billion is provided for vaccine rollout for the current year and over the next two years.
  - The contingency reserve increases from R5 billion to R12 billion in 2021/22, given uncertainty around vaccination campaign costs. These interventions do not add to longer-term expenditure.

Table 5.2 2021 Budget additions

R million	2021/22	2022/23	2023/24	MTEF total
2021 Budget additions to baseline	**22 446**	**4 602**	**2 283**	**29 332**
COVID-19: Vaccine rollout	5 200	3 000	–	8 200
COVID-19: Managing second and third wave	8 000	–	–	8 000
Extension of the special COVID-19 social relief of distress grant	2 145	–	–	2 145
Other adjustments[1]	7 101	1 602	2 283	10 987

1. Includes the New Development Bank, financial support to state-owned companies and public entities, and the rescheduling of some infrastructure reductions introduced in the 2020 MTBPS

NARROWING THE DEFICIT WILL STABILISE DEBT

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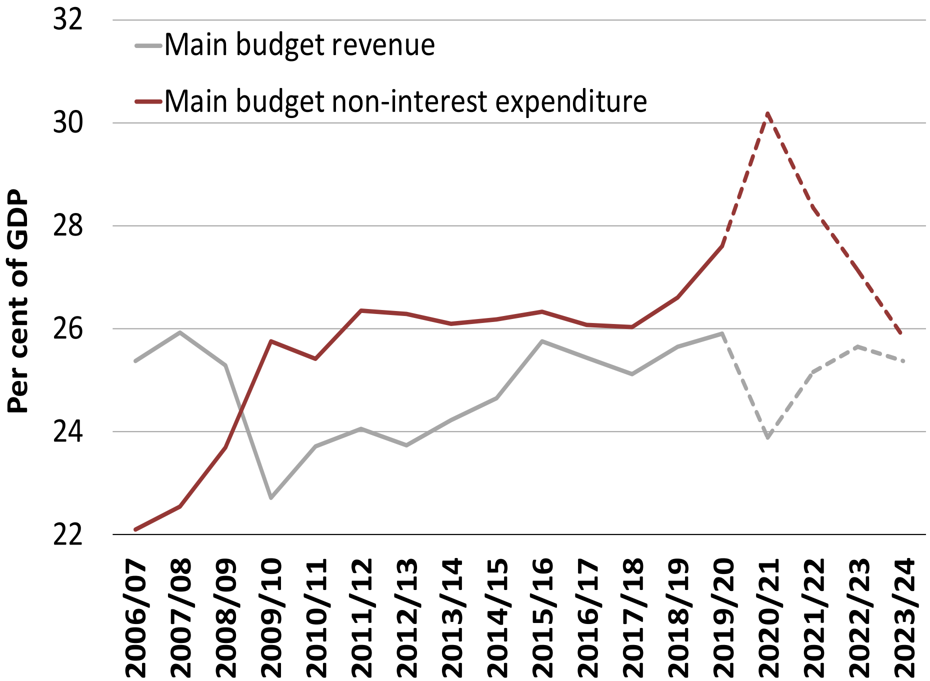
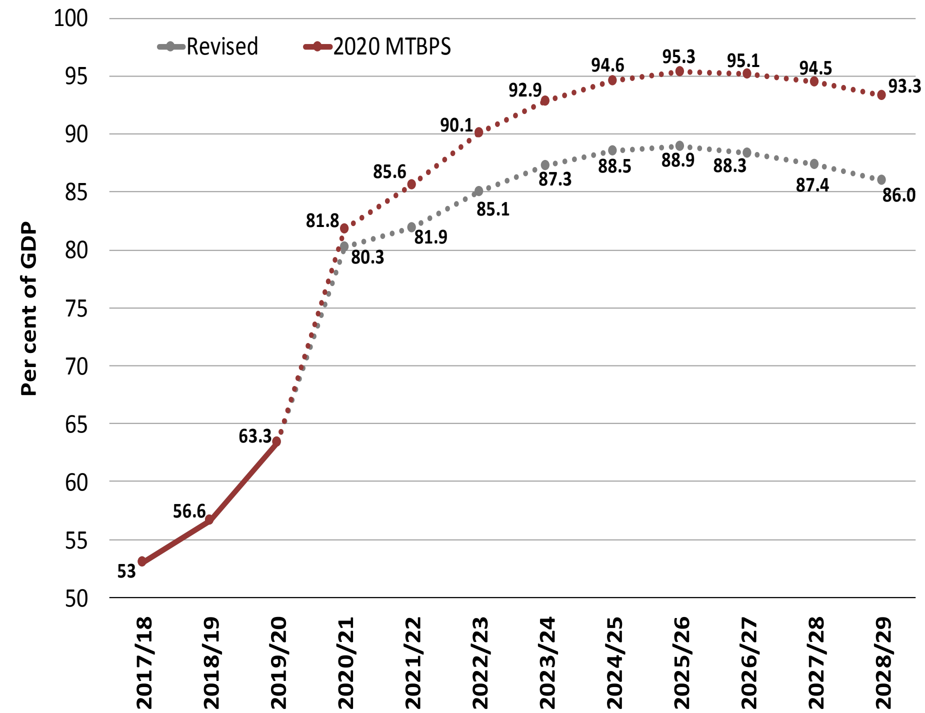
Main budget revenue and expenditure*



Excludes Eskom financial support and transactions in financial assets and liabilities

Gross debt-to-GDP outlook



- The main budget primary deficit is projected to narrow over the medium term and gross debt-to-GDP is now projected to stabilise at 88.9 per cent of GDP in 2025/26.

THE CONSOLIDATED DEFICIT NARROWS OVER THE MEDIUM TERM

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Table 3.5 Consolidated fiscal framework

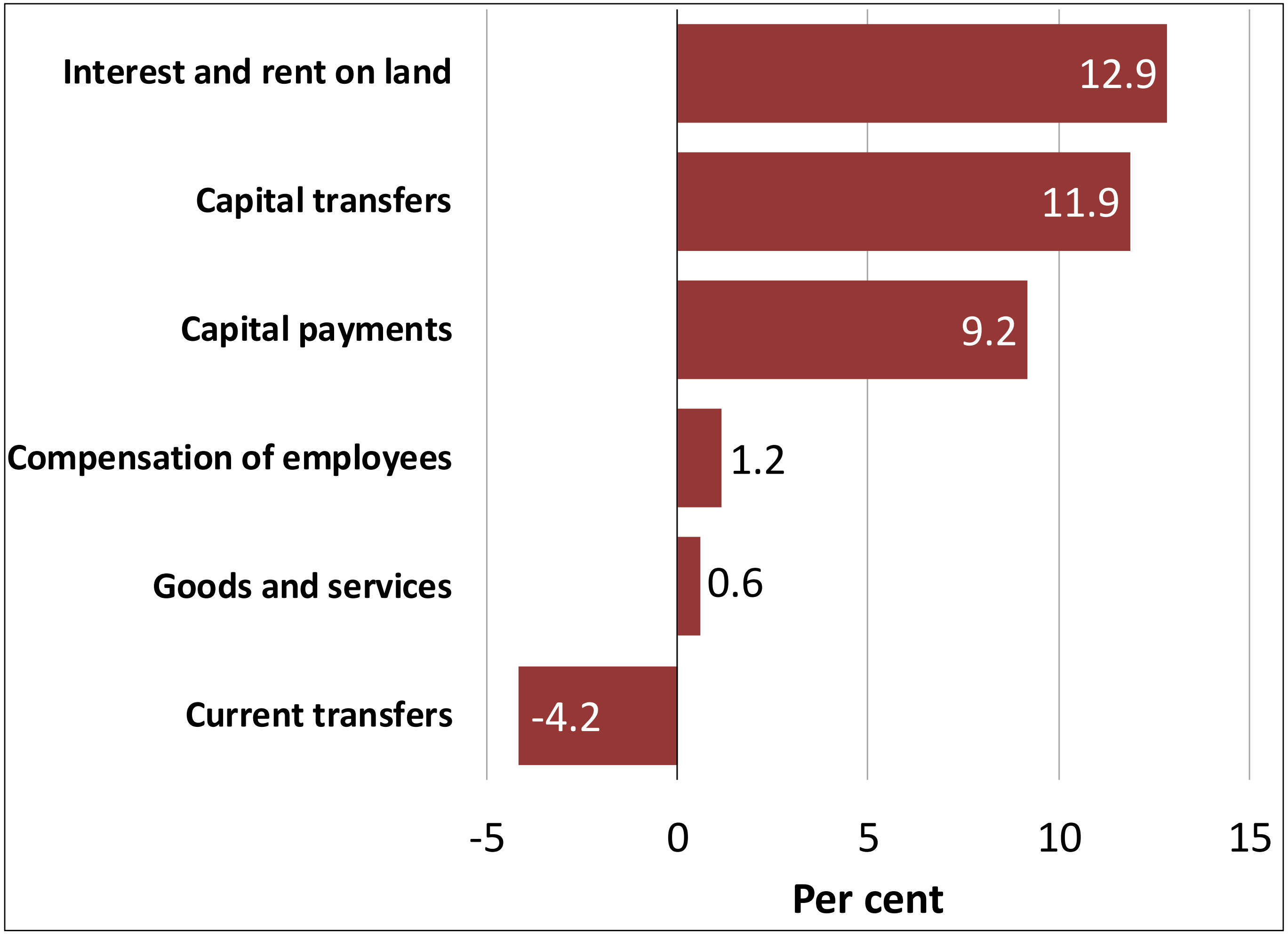
R billion/percentage of GDP	2017/18	2018/19 Outcome	2019/20	2020/21 Revised estimate	2021/22	2022/23 Medium-term estimates	2023/24
Revenue	**1 350.3**	**1 447.8**	**1 530.5**	**1 362.7**	**1 520.4**	**1 635.4**	**1 717.2**
	28.7%	*29.4%*	*29.7%*	*27.7%*	*28.4%*	*28.9%*	*28.6%*
Expenditure	**1 540.9**	**1 643.6**	**1 822.3**	**2 052.5**	**2 020.4**	**2 049.5**	**2 095.1**
	32.8%	*33.4%*	*35.4%*	*41.7%*	*37.7%*	*36.2%*	*34.9%*
Non-interest expenditure	*1 368.0*	*1 451.5*	*1 608.5*	*1 810.8*	*1 742.0*	*1 733.1*	*1 747.8*
	29.1%	*29.5%*	*31.2%*	*36.8%*	*32.5%*	*30.6%*	*29.1%*
Budget balance	**-190.6**	**-195.7**	**-291.8**	**-689.8**	**-500.0**	**-414.1**	**-377.9**
	-4.1%	*-4.0%*	*-5.7%*	*-14.0%*	*-9.3%*	*-7.3%*	*-6.3%*

Source: National Treasury

- The fiscal framework reduces growth in the wage bill and the share of spending on wages, while sustaining real spending increases on capital payments, specifically for buildings and other fixed structures.
- The Infrastructure Fund has initial support of R18 billion over the MTEF to enhance collaboration and attract private-sector investment.

CAPITAL TRANSFERS AND PAYMENTS GROW FASTER

Average spending growth over the MTEF by economic classification, 2021/22 — 2023/24



- After interest payments, capital transfers and capital payments grow fastest.
- Consolidated wage bill is projected to grow by an annual average of 1.2 per cent over the medium term.
- Decline in current transfers reflects a slowdown from high spending growth in 2020/21 due to the COVID-19 social relief of distress grant.

MEDIUM TERM SPENDING PRIORITIES

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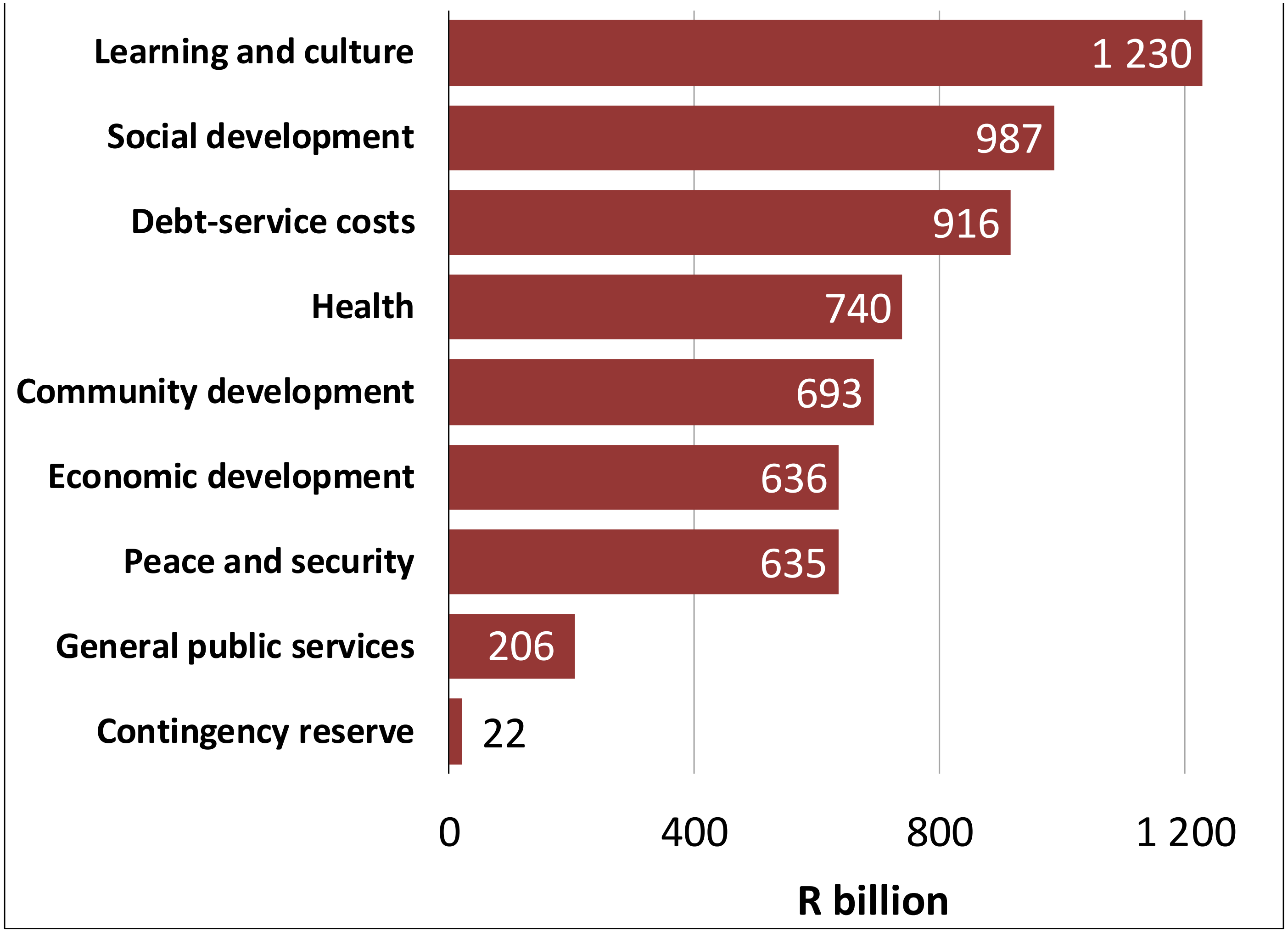
Consolidated government expenditure by function, 2021/22 — 2023/24



- Over half of allocations go towards learning and culture, health, and social development functions over the medium term.
- Debt-service costs, estimated at R916 billion over the MTEF period, is the third largest spending item by function

THE DIVISION OF REVENUE IS REDISTRIBUTIVE

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Table 1.5 Division of revenue

R billion	2020/21	2021/22	2022/23	2023/24
National allocations	804.5	763.3	736.3	739.0
Provincial allocations	628.3	639.5	643.3	646.8
Equitable share	*520.7*	*523.7*	*524.1*	*525.3*
Conditional grants	*107.6*	*115.8*	*119.3*	*121.5*
Local government allocations	138.5	138.1	146.1	148.4
Provisional allocations not assigned to votes	–	11.6	32.1	33.2
Total allocations	**1 571.3**	**1 552.5**	**1 557.8**	**1 567.5**
Percentage shares				
National	*51.2%*	*49.5%*	*48.3%*	*48.2%*
Provincial	*40.0%*	*41.5%*	*42.2%*	*42.2%*
Local government	*8.8%*	*9.0%*	*9.6%*	*9.7%*

Source: National Treasury

- Allocations through the intergovernmental fiscal system provide higher per capita allocations to rural provinces and municipalities.
- Government is developing indicators focused specifically on rural areas for the provincial equitable share formula to strengthen the equity of intergovernmental transfers.

- Over the 2021 MTEF period, after budgeting for debt-service costs, the contingency reserve and provisional allocations, 48.7 per cent of nationally raised funds are allocated to national government, 41.9 per cent to provinces and 9.4 per cent to local government.

FINANCIAL POSITION OF PUBLIC-SECTOR INSTITUTIONS

- Many state-owned companies are at risk of defaulting on their debts. SOCs in financial distress will need to expedite the implementation of reforms.
- The net asset value of development finance institutions fell by 27 per cent to R100.3 billion in 2019/20, mostly due to losses at the Industrial Development Corporation and the Land Bank.
- The Land Bank, which defaulted on its debt in April 2020, receives R7 billion in recapitalisation over the medium term to put it on a sustainable development path.

Table 1.7 Combined financial position of public institutions

R billion/net asset value	2017/18	2018/19	2019/20[1]
State-owned companies	362.1	342.0	353.0
Development finance institutions	132.6	137.8	100.3
Social security funds	-27.0	-79.6	-147.6
Other public entities[2]	719.0	724.7	793.3

1. Due to the COVID-19 pandemic, many entities have not released audited financial statements, therefore unaudited financials or last quarter reports were used for 2019/20

2. State-owned institutions without a commercial mandate and listed in either schedule 1 or 3 of the PFMA such as the National Library of South Africa

Source: National Treasury

RISKS TO THE FISCAL FRAMEWORK

- New waves of COVID-19 infections and associated disruptions to economic activity pose the most serious risk to growth
- The fiscal framework assumes compensation budgets ceilings are maintained. A departure from this assumption in the forthcoming wage agreement will be unaffordable and compromise debt stabilisation.
- The financial position of public entities and local government remains weak as a consequence of poor financial management.
- The medium-term debt redemptions of state-owned companies total R182.8 billion. Without rapid improvements in financial management and the resolution of longstanding policy disputes – including the user-pay principle – they will continue to put pressure on the public finances.

CONCLUSION

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- Budget 2021 strikes a difficult balance between providing immediate support for the economy and shoring up the country's public finances. Medium-term fiscal policy focuses on:
  - Extending temporary support in response to COVID-19
  - Narrowing the budget deficit and stabilising debt
  - Exercising continued restraint in non-interest expenditure growth while improving the composition of expenditure.
- Returning the public finances to a sustainable position will require ongoing restraint in expenditure growth and implementation of structural reforms to support economic growth.
- The current fiscal strategy reduces growth in the compensation bill and decreases the share of spending on public-service wages over the medium term, while sustaining small real spending increases on other items.
- Significant risks remain for the economic and fiscal outlook