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A time of crisis, a window of opportunity

- The scope of the present global crisis – the most serious financial and economic contraction since the 1930s – presents all countries with new challenges. Although the medium-term growth outlook is poor, South Africa has made the right choices over the past decade, creating the room for a bold response now. The 2009 Budget advances a series of policy measures to enable South Africa to respond to the changed economic environment and construct a more robust platform for growth once the world economy recovers.
- Government's sound fiscal and monetary policies have reduced but not eliminated the country's exposure to the international downturn. Following six years of strong performance, GDP growth is expected to slow sharply to 1.2 per cent in 2009. While some factors point towards an incipient recovery in global growth towards the end of the year, the outlook is highly uncertain.
- Over the period ahead government is committed to strengthening the economic foundation required for accelerated long-term growth by extending the public-sector infrastructure programme. The fiscal stance provides for sustained growth in public expenditure to cushion the economy and reinforce the social safety net for the poor, while ensuring that debt incurred to finance the country's priorities is kept at sustainable levels now and in future.

A turning point in the world economy

Introduction

The world is in the midst of a deep and synchronised economic slowdown

The impact of the global financial crisis on the world economy has been more severe than anticipated, and the deteriorating international environment significantly affects South Africa's growth prospects. In economic terms, the period ahead will be the most challenging yet faced by South Africa's democracy.

Economic growth is projected to slow to 1.2 per cent of GDP in 2009

Domestic GDP growth is projected to slow to 1.2 per cent in 2009 from an estimated 3.1 per cent in 2008. The period of slower growth ahead is likely to be characterised by rising unemployment, declining business profitability and the closure of some companies. While policy responses to the crisis will reduce the impact on poor and marginalised communities, economic conditions will be difficult for some time.

Government will sustain strong growth in public spending

Slowing economic growth has put pressure on government revenues and reduced the fiscal space for increased expenditure. However, as a result of government's record of sound fiscal management and prudent policy choices over the past decade, the state will be able to increase spending on social services and fixed investment over the medium term.

The new and difficult circumstances call for both bold action and careful policy adjustments to ensure that the economy continues to grow and to improve the living standards of all South Africans. Boldness is required because of the severity of the situation, yet care must be taken so that ill-conceived or poorly executed interventions do not burden future generations.

Five objectives guide government's response to the crisis

The 2009 Budget is framed by five objectives that guide government's policy response over the medium term:

- **Protect the poor**. Government will continue to expand programmes that alleviate poverty and strengthen the social safety net.
- **Build capacity for long-term growth**. Investment in infrastructure will be accelerated. This includes ensuring that public utilities can finance their capital investments and that the development finance institutions play a greater role in lending for infrastructure investment, sharing risk with the private sector.
- **Sustain employment growth**. Government will increase public investment spending, expand labour-intensive employment programmes, and work with business and organised labour to protect work opportunities and accelerate skills development.
- **Maintain a sustainable debt level**. While public debt is set to rise, this expansion must be kept in check so as not to reduce the space to finance development in the longer term.
- **Address sectoral barriers to growth and investment**. Microeconomic and regulatory reforms are needed to ensure that a more competitive, labour-absorbing economy emerges from the current global crisis.

State-owned entities will spend, on average, more than R120 billion a year on infrastructure programmes

Flowing from these objectives, the 2009 Budget provides for strong growth in allocations for labour-intensive employment programmes, municipal infrastructure, education, health, fighting crime and investing in rural development. Consolidated non-interest government expenditure is expected to grow by 5.1 per cent a year in real terms over the next three years. Over the medium term, state-owned enterprises will spend more than R120 billion a year on infrastructure, laying the foundations for faster economic growth in the future.

For the global economy, the downturn highlights the need to address structural trade imbalances, reshape international financial relations, and attack the underlying causes of poverty and inequality. South Africa's challenge, similarly, is to address the obstacles that stand in the way of faster growth and broader participation in economic development. These include labour market arrangements that inhibit job creation, dysfunctional government institutions, weaknesses in education and training, lags in industrial and trade interventions, and uncompetitive cost structures in input sectors such as telecommunications.

Downturn highlights the long-term need to address underlying causes of poverty and inequality

Managing through the downturn

A global crisis

In the 2008 Budget, government pointed to the high probability that global imbalances would begin to unwind in a rapid and disorderly fashion, setting off a severe economic slowdown. The storm is now upon us in the form of a broad-based and synchronised downturn that reaches from developed to emerging economies.

Nearly all developed countries are now in recession. Confidence has yet to be restored in the banking sector and the balance sheets of financial institutions remain under pressure. Credit conditions are deteriorating and demand is in decline. Employment is falling as companies adjust to a period of significantly reduced demand. Last year US employers cut nearly 2.6 million jobs – the fastest payroll reduction since 1945 – bringing the unemployment rate to 7.2 per cent in December 2008. Joblessness is increasing in the UK and in most of the European Union.

Nearly all developed countries are in recession and employment levels are falling rapidly

Growth prospects for emerging markets have deteriorated significantly. Commodity exporters are affected by a sharp decline in the prices of their key exports, weaker demand and a reversal of capital flows. Falling asset prices have led to a sharp reduction in household consumption and declining private-sector investment. In high-growth Asian export economies, sectors such as manufacturing, mining, construction and retail are contracting. China is experiencing factory closures and large-scale job losses. Growth on the African continent is set to decline as commodity prices fall, development assistance flows slow and access to capital dries up.

Commodity exporters such as South Africa face the double blow of weak demand and falling prices

Global policy responses

The policy response to these events has evolved through three overlapping phases, though loss of confidence in banking and credit markets has not yet been reversed:

- Round one: Rescuing the financial sector – Governments injected liquidity into the financial system and then acted to rescue major banks. In several cases, these bailouts were accompanied by partial nationalisation and state debt guarantees.
- Round two: Easing monetary policy – Central banks cut interest rates to historic lows. In December 2008, the UK bank rate was set to its lowest level in the Bank of England's 314-year history. US interest rates are between zero and 0.25 per cent.

- Round three: Stimulus packages – A massive fiscal expansion is now under way. Most large economies are experiencing a sharp deterioration in their fiscal positions as revenue slows, social security payments expand and the cost of financial rescue packages comes on budget. In addition, governments are reducing tax rates and increasing spending to stimulate demand.

Governments are proposing stimulus measures to boost demand

The International Monetary Fund has recommended that developed countries should implement economic stimulus measures. The US government is presently debating a US$819 billion stimulus plan covering both higher public spending and tax cuts. China has announced a stimulus package worth US$586 billion, focused primarily on infrastructure spending and social security transfers.

Emerging markets are finding it more difficult to respond in a similar way: raising finance given the present conditions of tight credit on global capital markets is difficult and costly.

A retreat into protectionism would make the crisis worse, particularly for emerging markets

The Group of 20 (G20) heads of state meeting in November 2008 adopted resolutions to oppose protectionist policies. A slowdown in world trade would make the economic decline more severe and protracted. This highlights the importance of a speedy resolution of the Doha round of trade negotiations, including a more equitable global trading regime for developing economies.

Crafting South Africa's economic policy response

South Africa's response to the global downturn takes account of several factors:

- Slowing export demand is leading to a contraction of production and employment in several sectors.
- The size of the drop in global demand cannot easily be offset by a small economy such as ours.
- A substantial infrastructure spending increase is already built into government's expenditure plans.
- It is costly to raise finance in the present circumstances as global capital markets strongly favour reserve currencies such as the US dollar and euro.

The fiscal space to respond to periods of slower growth is determined by the management of the public finances during periods of higher growth. Steps taken since 1996 to reduce public debt, and hence debt interest costs, have provided a degree of flexibility that is essential to manage the effects of the present downturn.

South Africa already has elements of a fiscal stimulus response built into its plans

With these considerations in mind, South Africa has chosen to sustain growth in public spending to build on the public-sector investment programme already under way, to expand labour-intensive employment programmes, to broaden social security benefits, to continue to invest in education, health and other public services, and to support well-targeted industrial development. These elements provide a countercyclical boost that will assist in sustaining growth and minimising job losses.

Highlights of the 2009 Budget

The economy and the fiscal stance

- GDP growth is projected at 1.2 per cent in 2009, rising to 4 per cent by 2011.
- Inflation (the rise in the consumer price index) is expected to fall to 5.8 per cent in 2009.
- Gross fixed capital formation growth is projected to average 6.1 per cent over the next three years.
- Government spending on infrastructure totals R787 billion over the next three years, R390 billion of which is capital spending by the state-owned enterprises.
- Consolidated government budget deficit reaches 3.8 per cent in 2009/10, moving to 1.9 per cent by 2011/12.
- Consolidated government spending (excluding interest) grows by 5.1 per cent a year in real terms.

Tax proposals

- Personal income tax relief for individuals amounts to R13.6 billion.
- Taxes on petrol and diesel increase by 40.5 and 41.5 cents per litre respectively.
- A packet of 20 cigarettes will cost 88 cents more.
- A 750 ml bottle of natural wine will cost 10.5 cents more.
- A 340 ml can of beer will cost 7 cents more.
- A 750 ml bottle of liquor (spirits) will cost R3.21 more.
- Incentives for investments in energy-efficient technologies.
- Motor vehicle excise reform to tax carbon emissions and a new tax on energy-intensive light bulbs.

Spending on public services

Additions to spending plans over the next three years

- R24.8 billion to provinces for increasing services, mainly health and education.
- R12 billion more for social grants and R1.2 billion for grant administration fees.
- R4.1 billion for the second phase of the expanded public works programme.
- R4 billion for the school nutrition programme to feed more children more often.
- R5.4 billion for the criminal justice sector overhaul, including fingerprint and DNA databases.
- R4.1 billion for provincial infrastructure, especially school buildings, roads and clinics.
- R4.3 billion for municipal infrastructure and R1 billion for regional bulk water infrastructure.
- R600 million for municipalities to extend free basic services.
- R1.6 billion as an equity injection into South African Airways.
- R3.7 billion more for increased housing provision.
- R1 billion for electricity demand-side management.
- R932 million for the treatment and prevention of HIV and Aids.
- R6.4 billion for public transport, roads and rail infrastructure.
- R1.6 billion for industrial development and support to small enterprises.
- R1.8 billion for rural development, mainly focused on supporting small-scale agriculture.

A lower tax burden, combined with strong growth in public spending, signals a strong fiscal stimulus to the economy over the period ahead. This is consistent with the countercyclical fiscal stance followed in recent years. However, government is also mindful of the difficulties of raising large amounts of debt in the present environment, and that an unsustainable level of borrowing would put South Africa's developmental objectives at risk. For these reasons the degree of fiscal expansion must be kept moderate, and the 2009 Budget also identifies areas where spending will be reduced, placing an obligation on government to become more efficient, effective and economical.

The 2010 FIFA World Cup, lower inflation and a more competitive rand will provide a boost to the economy

The economic reforms implemented over the past decade will help to sustain South Africa's ability to grow and to spend on the drivers of long-term growth. As the global economy begins to show signs of recovery, the impetus from strong private and public investment over the past decade, the economic boost associated with the 2010 FIFA World Cup, the more competitive currency, a healthy banking system, falling inflation and lower interest rates should allow for a gradual recovery in household spending and economic growth over the medium term.

Emerging from the crisis on a sounder footing

Fiscal measures and microeconomic reforms are needed to put the economy on a different footing

Falling commodity prices and the reversal of favourable global growth trends have underlined inherent weaknesses in the domestic economy. Despite four years of 5 per cent-plus GDP growth and strong increases in employment, income inequality remains high, the structure of South Africa's economy is heavily reliant on commodities and skills constraints impede broad-based development. South Africa's response during the period of slower growth ahead will influence both the speed and depth of the recovery. Success will be judged by the economy's ability to sustain higher growth through increased exports and a significant reduction in unemployment. The opportunity here is to combine fiscal measures and microeconomic reforms to put the economy on a sounder footing.

Higher infrastructure spending will lift the 'speed limit' of the economy

Sustaining investment in productive capacity. As highlighted by the electricity failures in the first quarter of 2008, South Africa's ageing physical infrastructure limits economic growth. Accelerated infrastructure investment has generated momentum that will support growth in the short term, enabling a broadening of opportunities in the longer term. Through development finance institutions such as the Development Bank of Southern Africa and the Industrial Development Corporation, government will aim to ensure that feasible projects in both state-owned enterprises and municipalities can access the finances required to sustain improvements in public infrastructure.

Public sector has a key role to play in expanding labour-intensive employment

Expanding employment in public works. The introduction of the second phase of the expanded public works programme draws on lessons learnt over the past five years. The extension of this programme prioritises longer-term jobs in the social and municipal services sectors, in adult literacy initiatives and in programmes delivered through non-governmental organisations. A new performance-based incentive is provided to municipalities to increase the labour-intensity of public works under their supervision. An additional R4.1 billion is allocated for public employment programmes.

High cost structure limits employment, innovation and productivity

Regulatory reform. High input prices raise the cost of doing business, lower employment and reduce economic growth. The competition authorities have made progress in dismantling price-setting cartels in various sectors. Yet major areas of the economy are characterised by dominant companies or parastatals, with insufficient competition to drive innovation and productivity. Government regulation and red tape often contribute to high barriers to entry. The necessary policy response is to lower such barriers, encourage new entrants into the market and foster greater competition. An enhanced regulatory impact assessment framework would assist, together with greater clarity about sectoral strategies and long-term industrial development goals.

Rural development to focus on raising agricultural output and rural incomes

Strengthening agriculture. The sharp rise in food prices during 2008 exposed weaknesses in domestic agriculture. The price increases had a detrimental impact on the poor and highlighted years of declining output in a labour-intensive sector. Food exports have fallen steadily over the past decade while the level of imports has increased, pushing up prices. Given its resources, South Africa could become a major food exporter. The new policy emphasis on rural development is aimed at raising rural incomes, ensuring sustainable growth in food production and drawing small farmers into the food supply chain.

Weak export performance is the Achilles heel of the South African economy

Raising export performance. Weak export performance remains the Achilles heel of the economy. Relative to other emerging markets, South Africa's export performance has lagged, while import growth has been strong. A higher level of exports can contribute to more rapid job creation and sustainable growth.

Table 1.1 Export and import performance, selected emerging markets

Per cent compound growth 2001– 2006	Export growth	Import growth
Brazil	18.8	10.4
China	29.5	26.6
India	23.3	29.0
South Africa	13.7	23.4

Steps are needed to improve competitiveness of key export sectors

Government and the private sector can take several steps to improve the competitiveness of key export sectors as global demand recovers. Some of these interventions are contained in the National Industrial Policy Framework. The announcement of a new phase of support for the motor industry is meant to provide a stable platform for continued export growth. The 2009 Budget includes R17 billion for industrial support, including tax incentives for particular sectors. Government recognises that competitive industries cannot be built behind ongoing protective tariffs or subsidies. Effective targeting of business incentives therefore needs to take careful account of the costs and benefits of selected support measures.

Improving public sector performance. While the reach of South Africa's public services has expanded significantly since the late

1990s, many components of the public sector do not deliver services of an acceptable quality. Public-sector inefficiency imposes costs on ordinary South Africans and reduces economic performance. Considering that general government consumption spending is almost a quarter of the economy, improving value for money and performance in the public sector would make an important contribution to higher growth, employment and welfare.

Progress in these areas will contribute to an earlier recovery that provides more widespread economic benefits for South Africa.

Fifteen years: progress and challenges

In budgeting, government assesses its progress, evaluates the effectiveness of its programmes and identifies weaknesses. Three recent documents provide a composite sketch of progress registered during the formative years of South African democracy: *Towards a Fifteen Year Review* and the *2008 Development Indicators,*[1] both published by The Presidency, and a fiscal incidence study[2] conducted by the National Treasury to gauge the effect of public spending.

Institutions of constitutional democracy are firmly entrenched

South Africa's successes have occurred in three broad dimensions. First, the construction of a new democratic order that replaced apartheid rule. The foundations of the new state were laid during the first five years with the adoption of the Constitution, the repeal of apartheid laws, the creation of the Constitutional Court and the establishment of three tiers of government. Independence of the central bank was established, the National Treasury was created, parliamentary oversight over public spending was institutionalised and an open, transparent budget process was introduced.

Government expenditure has provided tangible benefits to poor households

The second dimension of success has been the extension of basic services. Prior to 1994, just over half of all South Africans had electricity in their homes; today more than 80 per cent have access to this basic necessity of modern life. Significant progress has been made in providing houses, water and sanitation, and in extending access to schooling, health care and social grants.

Table 1.2 Access to basic household services

Percentage of households	1996	2001	2007
Using electricity			
for lighting	58	70	80
for cooking	47	51	67
for heating	45	49	59
Water			
Equivalent to or above RDP standard (200m to communal tap)	62	74	88
Tap in dwelling or on site	–	61	70
Sanitation			
Equivalent to or above RDP standard	52	59	73
Flush toilet	–	52	60

[1] Available at www.gov.za

[2] Soon to be available at www.treasury.gov.za

The number of clinic visits increased from 80 million in 2000 to 101 million in 2007. The number of social grant beneficiaries grew fourfold to 13 million. These tangible signs of a better life have been complemented by the introduction of school feeding schemes, free basic services and no-fee schooling.

The number of social grant beneficiaries has grown fourfold to 13 million

The third dimension of success has occurred on the economic front, brought about by a long and sustained economic expansion since 1999. Rising employment, increasing household income, lower taxes and the redistributive nature of the budget have enabled millions of people to move out of poverty. About 2 million more people are working today than in 2001 and the proportion of households with monthly income less than R367 per person (in 2007 prices) has fallen from 53 per cent in 1996 to 41 per cent in 2007. Disposable income has increased strongly during this period.

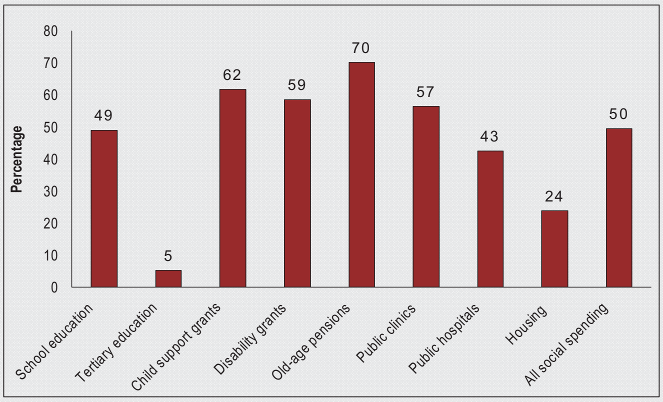
Economic expansion has broadened opportunities and reduced poverty

Public finances have become significantly more pro-poor

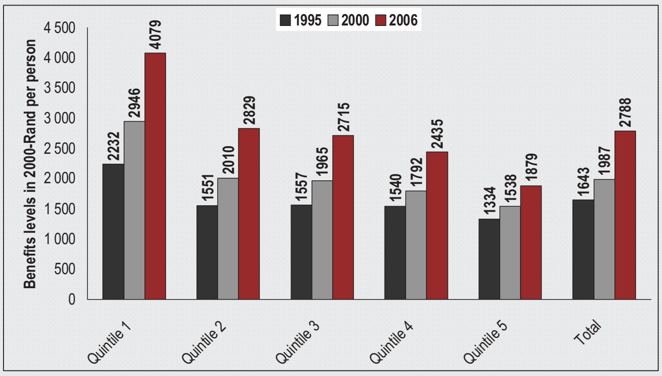
Since 1996, the public finances have undergone significant changes. Spending has grown strongly in social services – which include education, health and social development – and household services such as housing, water, sanitation, electrification and related infrastructure. In 2006, more than 50 per cent of public spending on education, health, social assistance and housing went to the poorest 40 per cent of the population.

Total spending per person on these services has increased from R1 643 in 1995 to R2 788 in 2006 (in constant 2000 prices). Spending per capita on the poorest 20 per cent of the population was R4 079 in 2006. Not only has government spending per person on these programmes increased by 70 per cent in real terms, but spending on the poorest 40 per cent has grown by 83 per cent in real terms.

Share of spending on key programmes going to the poorest 40 per cent of households, 2006



Social spending per person in constant 2000 rands



Source: Fiscal incidence study, National Treasury, 2009

Rising disease burden undermines gains in living standards

Towards a Fifteen Year Review also highlights several areas of weakness. A rising disease burden has placed severe strain on the public health system, to the point where many of the benefits associated with improved living conditions are undermined – for example, in high rates of infant and maternal mortality. In particular, rising HIV infection rates and increased Aids-related deaths have placed a massive social strain on many communities. Unemployment remains high, with over one-third of young people out of work. South Africa has one of the highest crime rates in the world and, despite some successes in reducing crime, citizens remain fearful.

While access to services has improved, the quality of services is often inadequate

While access to services, including primary health care, has improved, the quality of these services remains basic and is often inadequate. For example, there are 25 per cent more learners in schools today than in 1990, but performance in maths and literacy tests lags comparable countries. While more than 70 per cent of pregnant women visit a public clinic at least once during their pregnancy, infant and maternal mortality rates remain high.

In summary, government's track record over the past 15 years has been impressive given the significant challenges faced by the new democratic state. Nevertheless, much more can be done given the resources available. Improved public-sector performance is a key policy priority over the three-year medium-term expenditure framework (MTEF).

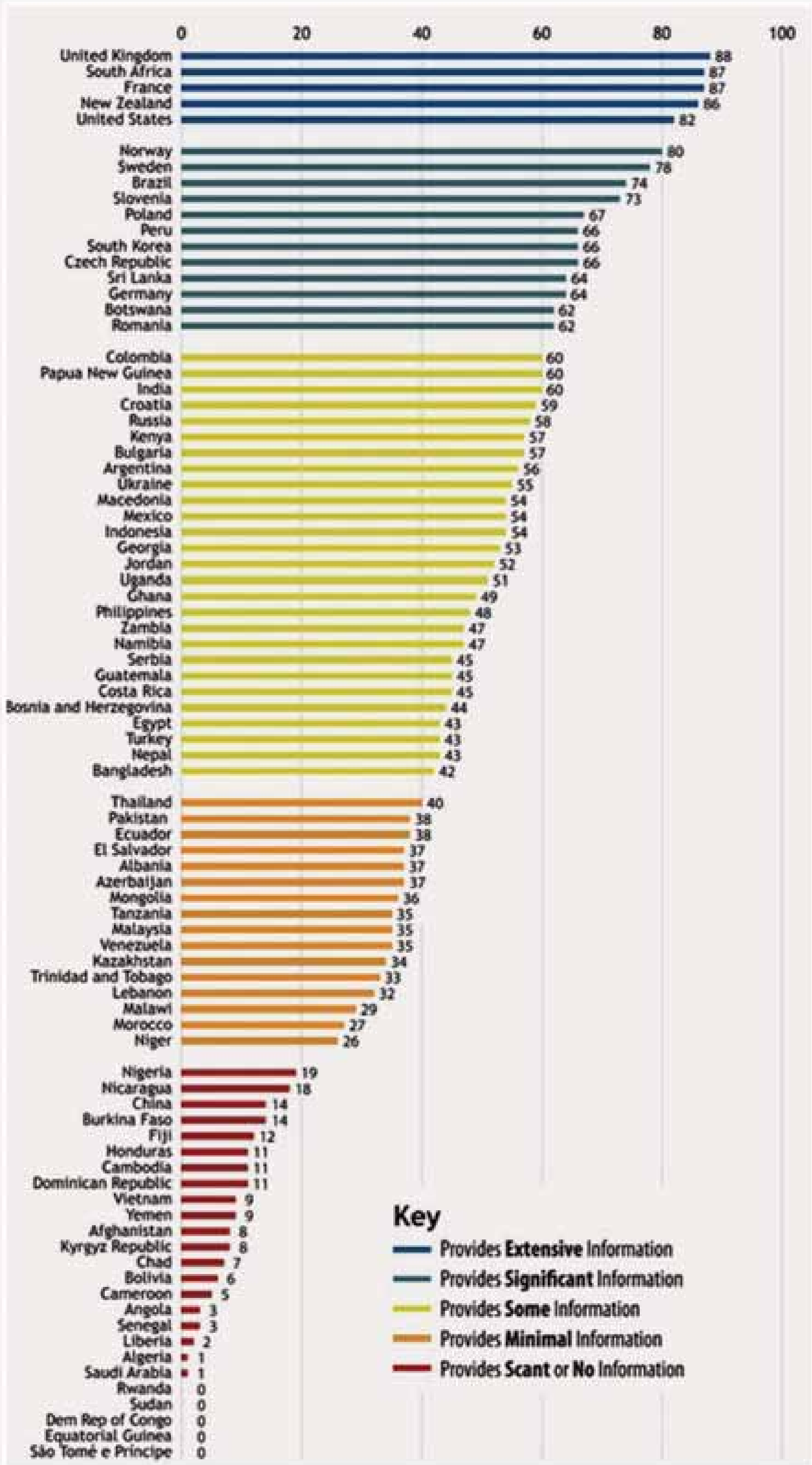
South Africa now ranks 2nd in the world in the transparency of its budget

Transparency, openness and oversight are also important elements of improving public-sector performance. Over the past 15 years South Africa has also made good progress in improving the transparency of the budget process and the usability of the budget documentation.

South Africa now ranks second in the world on the Open Budget Index, which measures the transparency and quality of budget information. Such information, for use by citizens and the legislature, can help to improve accountability, efficiency and performance by government departments and state-owned entities.

Open Budget Index

The Open Budget Initiative is a global research and advocacy programme to promote public access to budget information and the adoption of accountable budget systems.



The International Budget Project (IBP) launched the Initiative with the Open Budget Survey – a comprehensive analysis and survey that evaluates whether governments give the public access to budget information and opportunities to participate in the budget process at the national level.

To easily measure the overall commitment of the countries surveyed to transparency and to allow for comparisons among countries, IBP created the Open Budget Index (OBI) from the Survey. The OBI assigns a score to each country based on the information it makes available to the public throughout the budget process.

The budget is a government's plan for how it is going to use the public's resources to meet the public's needs. Transparency means all of a country's people can access information on how much is allocated to different types of spending, what revenues are collected, and how international donor assistance and other public resources are used.

The IBP believes that open budgets are empowering; they allow people to be the judge of whether or not their government officials are good stewards of public funds.

While providing the public with comprehensive and timely information on the government's budget and financial activities and opportunities to participate in decision making can strengthen oversight and improve policy choices, keeping the process closed can have the opposite effect. Restricting access to information creates opportunities for governments to hide unpopular, wasteful, and corrupt spending, ultimately reducing the resources available to fight poverty.

Source: www.openbudgetindex.com

Overview of the 2009 Budget

Macroeconomic overview

Chapter 2 presents government's macroeconomic forecasts, discusses key policy challenges and analyses recent economic trends.

Macroeconomic forecasting is complex given frequent revision of global growth projections

The chapter discusses in some detail the evolution of the international economic crisis, how South Africa is affected, government's economic policy responses and the medium-term outlook. It notes the complexity associated with this year's macroeconomic forecast given the frequent revision of global growth projections as a result of the global slowdown.

This synchronised downturn affects South Africa through declining demand for commodities, falling prices and deterioration in the financing environment. Interest rates remain relatively high, asset prices are falling and consumer confidence has weakened. Household consumption expenditure is expected to decline by 0.2 per cent in 2009 following an increase of more than 6 per cent a year over the previous four years. Growth in private-sector fixed investment, a key driver of economic expansion over the past four years, is likely to slow during 2009.

After four years of economic growth of more than 5 per cent a year, domestic GDP growth slowed to 3.1 per cent in 2008. Growth of 1.2 per cent is expected in 2009.

Table 1.3 Macroeconomic overview

Real growth Percentage	2008 Estimate	2009	2010 Forecast	2011
Household consumption	2.5	-0.2	1.9	3.2
Capital formation	11.5	3.7	5.7	9.0
Exports	2.1	-1.4	3.3	4.9
Imports	3.2	-3.7	6.7	7.7
Gross domestic product	**3.1**	**1.2**	**3.0**	**4.0**
Headline CPI inflation	11.6	5.8	5.3	4.7
Balance of payments current account (percentage of GDP)	-8.1	-6.3	-6.9	-6.9

The current account deficit is expected to narrow significantly in 2009

As the global economy begins to recover towards the end of 2009 and household consumption benefits from lower inflation and interest rates, growth is expected to climb to 3 per cent in 2010 and 4 per cent in 2011. A continuing expansion of public-sector fixed investment and benefits flowing from the 2010 FIFA World Cup will also support the recovery. The current account deficit is expected to narrow to about 6 per cent this year due to smaller dividend payments to international investors and lower demand for imports, partly due to the weaker currency. Nevertheless, the external deficit is likely to remain sizeable owing to imports required for infrastructure investment.

Fiscal and tax policy

Chapter 3 presents a detailed breakdown of government's fiscal stance and the public finance accounts. Chapter 4 discusses revenue trends and tax policy changes.

Fiscal policy aims to sustain spending growth, especially in public investment

Government's countercyclical fiscal stance provides a boost to the domestic economy at a time when global demand is weak. South Africa is in a position to expand public spending despite the decline in revenue projections because public debt is low and the budget was in surplus until last year.

Public spending continues to rise in real terms, with strong growth in infrastructure spending, labour-intensive employment programmes, social transfers to households and social services. A larger contingency reserve of R38 billion allows for the fiscal flexibility required to adjust to unanticipated economic risks, to respond to natural disasters, to further support employment programmes and to bolster the resources of development finance institutions.

Total public investment in infrastructure totals R787 billion over MTEF

Public spending is complemented by a significant expansion in infrastructure investments by the large state-owned enterprises. Eskom, Transnet, the Airports Company of South Africa, the South African National Roads Agency Ltd and entities in the water sector plan to spend more than R397 billion over the next three years on vital economic infrastructure, while general government is expected to spend R391 billion on infrastructure over the same period. Financing these investments during the present economic period will be more challenging, prompting government to increase its level of support for the state-owned enterprises.

Table 1.4 outlines the revenue and expenditure of the consolidated government account, which covers national government and its entities, provinces, extra-budgetary institutions and the social security funds.

Consolidated national government budget deficit of 3.8% of GDP in 2009/10

Given the higher cost of finance on global markets and the need for state-owned enterprises to also access capital markets, government will keep a check on the expansion of the deficit. The consolidated government budget deficit is projected to rise to 3.8 per cent in 2009/10 and is projected to come down once the economy recovers and revenue growth increases. For this reason, the budget also includes measures to ensure greater efficiency and to discontinue ineffective spending programmes.

Table 1.4 Consolidated government budget

R billion	2008/09	2009/10	2010/11	2011/12
Gross tax receipts	655.8	692.6	757.1	832.5
plus: Non-tax receipts	70.8	75.7	83.2	91.0
less: SACU transfers	-28.9	-27.9	-26.2	-27.9
Total receipts	**697.7**	**740.4**	**814.1**	**895.6**
Current payments	431.1	472.4	516.9	558.1
of which: Interest	*58.0*	*60.0*	*66.5*	*73.8*
Transfers and subsidies	239.7	294.6	304.6	304.4
Payments for capital assets	50.3	61.3	66.2	70.6
Contingency reserve	–	6.0	12.0	20.0
Total payments	**721.1**	**834.3**	**899.7**	**953.1**
Budget balance	**-23.4**	**-94.0**	**-85.6**	**-57.4**
Percentage of GDP	*-1.0%*	*-3.8%*	*-3.2%*	*-1.9%*
Gross domestic product	*2 304.1*	*2 474.2*	*2 686.3*	*2 953.0*

Revenue collection under pressure

Tax revenue grew by more than 15 per cent a year between 2004 and 2007. In the last three months of 2008, revenue growth slowed sharply, reflecting tougher conditions in the economy. As a result, the revenue estimate for 2008/09 is being revised downwards by R14.4 billion. Revenue estimates for 2009/10 are also lower than estimated in October 2008. Consolidated national budget revenue is expected to decline as a share of GDP in 2008/09 and 2009/10.

Substantial personal income tax relief

The personal income tax schedules are revised. Relief for individuals amounting to R13.6 billion is provided to take account of wage inflation, including compensation for the higher-than-anticipated inflation rate in 2008. For several years, fuel taxes have fallen as share of the pump price. This year, the general fuel levy and the Road Accident Fund levy are increased more sharply, taking into account the general reduction in fuel prices. Specific excise duties are increased broadly in line with inflation.

Tax proposals support initiatives to protect the environment

The tax proposals also support government's increased policy focus on environmental initiatives that mitigate the impact of climate change and promote sustainable development, energy efficiency and investment in new technologies.

Asset and liability management

Chapter 5 discusses developments in the debt markets, government's debt portfolio, borrowing plans, contingent liabilities, credit risk and financial management of state-owned enterprises.

Financing strategy changes in light of higher borrowing requirement

Following several years of either small deficits or budget surpluses, government's borrowings increased in 2008/09 and are set to grow over the next three years as a result of slower revenue growth, sustained public spending increases and support to state-owned enterprises. Net loan debt of national government is projected to rise from 22.6 per cent of GDP in 2008/09 to 27.4 per cent in 2010/11. Despite this increase, debt service costs are projected to remain roughly constant as a share of GDP. Lower interest rates and active debt swap and refinancing programmes will help keep borrowing costs down. As the economy recovers and revenue growth picks up, the borrowing requirement is expected to fall.

As a result of the global financial crisis, access to foreign finance has become much scarcer and more expensive. For this reason, government's financing strategy is premised mainly on borrowing in South Africa's liquid and deep capital market, though a moderate level of external financing is planned.

Government will support state-owned entities to raise capital to fund investments

Government is also working actively with state-owned enterprises to ensure that their capital investment programmes are financed at competitive rates. Government guarantees to state-owned enterprises are set to increase. Eskom has received a guarantee for R176 billion of its existing and new debt. Other requests will be evaluated on a case-by-case basis. The National Treasury is also working with these entities to sequence loan issuances to avoid undue pressure on domestic capital markets.

In addition to greater support to the development finance institutions, government is also exploring partnerships with the private sector to facilitate low-cost housing development as well as risk-sharing on large capital projects.

New partnerships with the private sector being explored

Table 1.5 below shows the outlook for government's debt and projected debt-service costs.

Table 1.5 Projected state debt and debt costs of national government

R billion	2008/09	2009/10	2010/11	2011/12
Net loan debt (end of year)	**520.7**	**634.6**	**728.1**	**810.3**
Percentage of GDP	*22.6%*	*25.6%*	*27.1%*	*27.4%*
Net domestic debt	425.5	527.3	616.8	690.3
Foreign debt	95.2	107.3	111.3	120.0
State debt cost	**54.3**	**55.3**	**60.1**	**66.8**
Percentage of main budget revenue	*8.9%*	*8.6%*	*8.5%*	*8.6%*
Percentage of GDP	*2.4%*	*2.2%*	*2.2%*	*2.3%*

Social security

Over the past five years, government's social grants programme has grown steadily and now covers about 13 million beneficiaries. The social grants system is being expanded in three ways:

The social grants system is being expanded

- Increasing the eligible age for the child support grant to children up to their 15th birthday
- Revising the means test to cover a larger proportion of households
- Lowering the eligible age for men for the old age pension to 60.

The proposed extension of social grants is likely to bring an additional 2 million beneficiaries into the system. Spending on social assistance is projected to rise by 10.2 per cent a year, from R71 billion in 2008/09 to R95 billion in 2011/12.

South Africa's social insurance arrangement is made up of the Unemployment Insurance Fund (UIF), the Road Accident Fund (RAF) and the Compensation Funds. Due to rising unemployment, the UIF expects beneficiary numbers to grow by 7.3 per cent over the course of the MTEF period. The UIF is considering proposals to extend the length of benefits to take account of an expected increase in retrenchments. The Fund's financial position remains healthy, with strong cash surpluses projected well into the future.

Social security funds remain in surplus

The RAF remains in a precarious financial position, with a significant actuarial liability and about 297 000 cases still unprocessed. The RAF levy increases by 17.5 cents a litre to 64 cents. This will allow further progress to be made in reducing the claims backlog, but further reform is required to put it on a sustainable footing.

The Compensation Funds remain in sound financial health. On a consolidated basis, the social security funds will continue to run operating surpluses of about R10 billion a year over the MTEF period.

Compensation Funds are in good financial health

Social security reform task team is focusing on several key policy areas in 2009

Government's efforts to reform the retirement fund industry are focused on ensuring that low-income workers and those with periodic incomes have access to affordable retirement insurance, while improving the governance and cost-effectiveness of retirement funds. The interdepartmental task team on social security and retirement reform will continue its work in 2009, with a view to developing a road map for introducing a national savings fund and broadening income protection for workers. The task team will also consider and provide advice on the insurance aspects of health care reform.

Medium-term allocations and the division of revenue

Extra R161 billion provided to extend service provision and account for higher costs

The 2009 Budget sustains strong growth in public spending. About R161 billion is added to the spending plans of government over the next three years, both to counter the effects of higher costs as well as to expand or extend service provision in key areas. The main budget priorities include:

- Education
- Health
- Fighting crime
- Investing in rural development
- Extending basic household infrastructure.

In addition to these priorities, the budget places particular attention on a series of cross-cutting priorities. These include public employment programmes, improving the capacity of the public service and mitigating the impact of climate change.

After adjusting for once-off spending such as the loan to Eskom, non-interest expenditure grows by an average of 5.1 per cent in real terms over the next three years.

Departments were asked to make efficiency savings and reduce wastage

This year national departments were again asked to make efficiency savings, to discontinue ineffective programmes and to reduce wastage. About R19 billion has been removed from the spending plans tabled in the 2008 *Medium Term Budget Policy Statement*, reflecting a commitment by government to eliminate unnecessary expenditure.

Chapter 7 discusses additional allocations in the 2009 Budget in detail. Table 1.6 summarises the consolidated government budget for the next three years, which includes spending by provinces, the social security funds, public entities and national government agencies.

Table 1.6 Consolidated expenditure

R billion	2008/09 Revised estimate	2009/10 Budget estimate	% Average growth 2008/09–2011/12
General public services	48.1	51.3	5.2%
Defence	30.8	34.7	7.3%
Public order and safety	67.8	75.5	10.9%
Economic affairs	126.2	179.6	8.4%
Environmental protection	5.1	5.6	8.2%
Housing and community amenities	65.3	73.2	12.1%
Health	80.8	86.9	9.2%
Recreation and culture	9.9	7.7	-18.3%
Education	127.3	140.4	10.0%
Social protection	105.4	118.1	9.9%
Contingency reserve	–	6.0	
Non-interest expenditure	**666.8**	**779.1**	**9.1%**
State debt cost	54.3	55.3	7.2%
Total expenditure	**721.1**	**834.3**	**9.7%**

Transfers to provinces and municipalities reflect focus on education, health, agriculture and housing

Chapter 8 describes the division of nationally collected revenue between the three spheres of government. Provinces receive an additional R47.8 billion over the next three years while municipalities receive R11.3 billion more. These transfers reflect government's priorities, especially the focus on education, health, agriculture and housing at a provincial level and water, sanitation and electricity infrastructure at a municipal level.

Table 1.7 shows the division of revenue. Transfers to provinces grow by 10.7 per cent a year while transfers to municipalities grow by 14.2 per cent a year. Chapter 8 also discusses aggregated provincial budget trends.

Table 1.7 Division of revenue

R billion	2008/09	2009/10	2010/11	2011/12
National allocations	288.3	343.1	352.8	361.3
Provincial allocations	247.7	284.5	309.7	335.9
Equitable share	*204.0*	*231.1*	*253.7*	*272.9*
Conditional grants	*43.7*	*53.5*	*56.0*	*63.0*
Local government allocations	43.6	49.7	57.7	65.0
Total allocations	**579.6**	**677.3**	**720.2**	**762.1**
Changes to baseline				
National allocations	17.3	45.1	32.1	24.3
Provincial allocations	6.7	13.3	12.8	21.7
Equitable share	*4.6*	*5.6*	*7.4*	*11.8*
Conditional grants	*2.0*	*7.7*	*5.5*	*9.8*
Local government allocations	1.8	2.0	2.8	6.4
Total	**25.8**	**60.5**	**47.8**	**52.4**

Conclusion

Sound public finances will help to sustain growth during the more challenging period ahead

The 2009 Budget is tabled during a deep global economic crisis with an uncertain trajectory. Political stability and a sound macroeconomic framework have enabled South Africa to benefit from global growth patterns over the past seven years. To make further progress, the country will have to ensure macroeconomic stability while tackling the constraints to faster and shared growth. Government's economic priorities include sustaining infrastructure spending, using countercyclical fiscal policy to cushion the economy against falling demand, and ensuring that measures taken today enhance competitiveness and broaden opportunities for all South Africans in the years ahead. Over the short term, government will work to sustain output and employment, and protect poor and marginalised communities, while focusing on long-term growth and sustainability.

Meeting the challenges ahead will require a capable and effective state, new ideas and new approaches to solving problems, new partnerships, and a willingness to adapt to changing circumstances, together with confidence in the choices we have made.

Other budget documentation

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

- The *Budget Speech* delivered by the Minister of Finance on Budget Day outlines the main policy features of the budget.
- The *Division of Revenue Bill* sets out the division of nationally raised revenue across the three spheres of government.
- The *Appropriation Bill* sets out the amounts to be appropriated by Parliament for each national vote, and the purpose of each programme.
- The *Estimates of National Expenditure* provides detailed information on allocations to national departments, key policy developments and measurable objectives for each programme. This year the *Estimates* covers significantly more public entities. After the tabling of provincial budgets, separate chapters of the *Estimates* will be published for each vote, providing more detailed information from provincial budgets and public entities.
- The *Estimates of National Revenue* sets out the main revenue estimates both before and after tax policy changes.
- The *People's Guide* is a popular summary of the budget produced in all 11 official languages, and in Braille.

Two annexures to the 2008 *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.