

2019
MTBPS
SPEECH



national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA



Madam Speaker
President of the Republic
Cabinet Colleagues and Deputy Ministers
MECs
Governor of the South African Reserve Bank
Leaders of all political parties
Representatives of organised business and labour
Honourable Members

Fellow South Africans

Today, it is my singular honour and privilege to table the twenty-third Medium Term Budget Policy Statement of the democratic era.

This is the first Budget Policy Statement of the sixth Administration and Parliament.

THE PURPOSE OF THE MEDIUM TERM BUDGET POLICY STATEMENT

The Medium Term Budget Policy Statement is an important piece of our budgeting process. The first statement was published on the second of December 1997, during the first democratic administration led by President Nelson Mandela.

We publish an MTBPS Review containing:

1. A summary of government's fiscal goals and objectives
2. Projections for the economy and the public finances
3. Long-term projections of the debt-to-GDP ratio assuming different scenarios. The baseline projection assumes we make minimal policy changes
4. A fiscal risk statement.

The Policy Statement does not include detailed spending plans or tax proposals. That is for the annual Budget, which is normally introduced in February.

This Policy Statement today coincides with another important process, the tabling of the bills that adjust in-year spending. In addition, today, we also table the money bills that give effect to the final versions of the tax proposals tabled on Budget Day 2019.

As the 1997 Policy Statement said:

“There is no point in publishing a Policy Statement if it simply means publishing the Budget three months early. The purpose is to open up the debate before the (actual) Budget is finalised.”

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I look forward to this debate. I will follow – in person, on the wireless, on the TV, in the newspapers, via my Facebook page, and the @TreasuryRSA Twitter account.

I table this MTBPS for consideration of the House and of all South Africans.

Today I also table:

1. The Adjustments Appropriation Bill
2. The Rates and Monetary Amounts
3. Amendment of Revenue Laws Bill
4. The Taxation Laws Amendment Bill
5. The Division of Revenue Amendment Bill
6. The Tax Administration Laws Amendment Bill
7. The 2019 Adjusted Estimates of National Expenditure

INTRODUCTION

Madam Speaker

On Budget Day 2019, I brought a resilient Aloe Ferox plant to the House.

Mr President, you might also remember that I presented an Aloe Ferox plant to you.

This little aloe is emerging from a long winter. During that winter, the ground became hard. The leaves fell from the trees and the air was bitterly cold. We toiled, hoping for better days.

Our people became poorer. Some lost their jobs.

Madam Speaker, here we stand at the end of winter. The food cupboards are almost bare.

We have been shuffling about in old and comfortable brown shoes.

Our expenditure continues to exceed our revenue. Our national debt is increasing at an unsustainable pace.

The economy is not performing well.

In these difficult times, we have turned against one another.

We have regrettably turned against our brothers and sisters from the rest of the continent. We should inculcate in the minds of our people that we are all from Africa.

Worst of all, we have turned against our sisters, daughters, and mothers.

This is not who we are.

We should give renewed impetus to the fight against gender-based violence and xenophobia.

So, what shall we do?

Hope is good but it is not a strategy.

As any farmer will tell you, if you want a bumper harvest, you must be prepared to work hard during the end of winter and early spring. Because what you do to the soil then determines how successful your crop will be.

Now is the time. We cannot wait any longer. If we want a successful harvest, we must act today.

As the Bible states:

*“But this I say, they who sow sparingly will also reap sparingly
And they who sow bountifully will also reap bountifully.”*

2 Corinthians 9 verse 6

Rock the boat! Shake the baobab tree! Do the unusual, disrupt the comfort zones. Get things moving!

THE GLOBAL ECONOMY

What is the state of the world?

After a decade-long economic expansion, growth in advanced economies is expected to slow, in part due to trade tensions and the Brexit uncertainty. The International Monetary Fund estimates that these tensions may take away 0.8 percentage points from global growth.

Economic growth in both China and India is expected to slow to 6.1 per cent this year. Growth in both these countries accelerated after far-reaching structural reforms. The average person in China is 7 times richer today than twenty-five years ago. The average person in India has become three and a half times richer over the same period. Meanwhile, the average South African is only 1.3 times richer.

Growth in emerging markets is lower partly because of the global slowdown, but also due to policy missteps, which we should avoid.

Economic growth in Mexico is down sharply. Its own state-owned energy company, PEMEX, will cost approximately US\$2.6 billion a year to fix. The Brazilian economy will most likely grow at 0.9 per cent in 2019. There, the state-owned energy company, PETROBRAS, has its own problems.

Closer to home, things are much better.

The African continent has a young, growing, entrepreneurial population. Sub-Saharan Africa is expected to grow by 3.6 per cent next year, the second-fastest growing region after Asia excluding Japan.

Just like Eliud Kipchoge, the Kenyan economy is racing ahead. Growth is expected to be 6 per cent next year. In Ghana, after extremely difficult structural reforms, growth is expected to be 7.5 per cent this year and 5.6 per cent next year. Ethiopia will grow by over 7 per cent.

They clearly have new shoes. Why don't we?

THE SOUTH AFRICAN ECONOMY

In the first quarter of this year, the South African economy contracted by a revised 3.1 per cent on a seasonally adjusted and annualised basis. As the energy constraint lifted, growth rebounded to 3.1 per cent in the second quarter. These two quarters cancelled each other out, and this year growth has been flat.

There are some signs that investment spending is strengthening. In the second quarter, growth in gross fixed capital formation rebounded to 6.1 per cent. Mining grew by 14.4 per cent. In real terms, credit growth has been positive since late 2018. Private sector credit extension rose 6.2 per cent in September. Home loans grew 5 per cent year-on-year, the fastest rate in some time. But corporate credit extension has softened.

In September, headline consumer price inflation was 4.1 per cent. Lower inflation is good for everyone, particularly for the poor and the working class.

In short, it is a mixed picture with some positive signs.

It is our job to chart a course that is strategic, sober, careful and inclusive.

The economy is now forecast to grow at 0.5 per cent in 2019 compared to the 1.5 per cent expected in February. Growth is projected to slowly rise to 1.7 per cent in 2022, supported by household consumption and private-sector investment.

OUR PROPOSED MEASURES TO GROW THE ECONOMY

Fellow South Africans, in the preamble of the Constitution, a commitment is made by all of us to:

“Improve the quality of life of all citizens and free the potential of each person.”

The growth outlook is far too low to support this vision.

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We must accelerate economic performance.

Under the leadership of President Ramaphosa, the structural reform agenda contained in the National Development Plan has been given new life. We have made progress in the following:

1. The new Integrated Resources Plan has been gazetted
2. The Infrastructure Fund is being rolled out
3. The visa regime has been greatly simplified
4. The unabridged birth certificate requirement for young tourists has been abolished
5. We have upgraded a number of industrial parks
6. Cabinet has directed ICASA to accelerate the licensing of high-demand broadband spectrum

Our paper titled *“Economic transformation, inclusive growth, and competitiveness: Towards an Economic Strategy for South Africa”* draws lessons from fast-growing emerging and sub-Saharan African economies.

The paper speaks for itself. But, in brief, we argue that there are a few important growth ingredients:

1. An efficient and capable state
2. Prudent fiscal and monetary policy
3. A competitive and flexible exchange rate
4. A trade regime which promotes open and beneficial trade, particularly with the rest of the African continent
5. A reimagined industrial strategy
6. Opening up ‘network industries’ that is transport, logistics and telecommunications. This means reorganising Eskom and other state-owned companies
7. Lowering barriers to entry
8. Prioritising job-creating sectors, such as agriculture and tourism
9. An overarching legal framework with an independent judiciary and strong property rights
10. A well-functioning financial sector

The country is having a rigorous debate about these proposals. We received over 800 comments. Proposals included ideas on the digital economy, streamlining applications for new ports, and opening up the railways to force heavy freight off our roads, ease congestion and improve safety.

Mr President, your comment at a meeting of the President’s Council of Economic Advisors was:

“Implementation of these initiatives will improve confidence and restore credibility”

To judge from the many supportive comments, many South Africans agree with you, as do local and international businesses: large, medium, small, and tiny; and our friends.

Thank you to everyone who tweeted, facebooked, emailed, phoned, wrote letters, held conferences, wrote articles in various publications and issued press releases.

We can do some of the things quickly. Already, the new Integrated Resources Plan charts a greener course forward on energy. We can accelerate spectrum licensing and a move towards 5G. We can make it easier

to do business.

The President is driving a critical youth employment initiative. We have supported the Youth Employment Service known as YES! through expanding the employment tax incentive. We look forward to the YES! Board bringing forward new innovative ideas.

Today, we publish Version 2 of the document. It is a living document. As such it is 'not a dogma but a guide to action'. Where appropriate, we will consider legislation.

REVENUE PERFORMANCE AND OUTLOOK

To meet our fiscal needs, growth is not enough. We also need a well-functioning and efficient revenue collection agency.

The South African Revenue Service is emerging from its own winter. Cabinet has approved that we implement the findings of the Nugent Commission of Inquiry into Tax Administration and Governance, and I intend to table a bill early next year. The President has appointed Edward Kieswetter as the new Commissioner. Since he started work in May, he has already taken steps to re-invigorate and re-establish the Large Business Centre, and the litigation, integrity and compliance units. Leadership, staffing and procurement failures are also being addressed.

Achieving a more inclusive South Africa relies on honest taxpayers. Without your taxes, South Africa will never succeed. Thank you to all those who have honored their obligations. But you have told us that we must spend your hard-earned money better, and we could not agree more.

We now expect to collect R1.37 trillion this year. This is R53 billion, or 4 per cent, less than we expected. Looking ahead, our revenue forecasts are prudent. We assume an elasticity of one, which means a one-to-one relationship between growth in taxes and economic growth, after adjusting for tax measures.

THE FISCAL FRAMEWORK

The fiscal framework has weakened substantially since the February budget, mainly due to weaker economic growth and lower revenues.

The main changes to the in-year expenditure projections are:

1. R26 billion in additional financial support to Eskom
2. R11 billion to several smaller state-owned companies in financial distress
3. R430 million approved through the Budget Facility for Infrastructure for student housing

These increases are partly offset by drawing on the contingency reserve, provisional allocations and declared unspent funds. That said, savings from the compensation measures announced in the Budget have not materialised as expected.

Thus, in total, non-interest spending rises by R23 billion this year, relative to the February estimate. If we exclude Eskom, non-interest spending would have been R2.9 billion less than projected.

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The consolidated budget deficit is now projected at 5.9 per cent of GDP in the current year.

This year, the national debt exceeded R3 trillion. It is expected to rise to R4.5 trillion in the next three years.

Clearly, we need to do things differently.

As things stand, without any policy adjustments, debt will most likely exceed 70 per cent of GDP by 2022/23.

This is a serious position to be in.

Our little Aloe is not doing well. It needs attention, like our public finances.

Honourable members, there is no status quo option!

Stabilisation involves difficult decisions that imply sacrifices by all of us. Slowing growth in the compensation bill and additional revenue measures will be needed.

The consequence of not acting now would be gravely negative for South Africa. Over time, the country would likely face mounting debt service costs and higher interest rates and may enter a debt trap. The unemployment crisis would worsen, and government debt could balloon. This is an outcome we are determined to avoid.

Additional measures will be announced in the 2020 Budget.

DIVISION OF REVENUE AND MEDIUM-TERM SPENDING PLANS

Over the medium-term, consolidated government spending totals R6.3 trillion as things stand. Our priorities are education, social development and health. They receive R3 trillion over the next three years. Approximately half of non-interest spending goes to national government, and the other half to provinces and municipalities.

We have achieved many social gains over the past 25 years. Our social spending programmes can be sustained over the long-term provided we make reasonable and prudent choices.

On our current trajectory, by the end of the three-year framework, debt service costs will be bigger than spending on health and economic development.

ACHIEVING FISCAL SUSTAINABILITY

Our problem is that we spend more than we earn. It is as simple as that.

How will we fix our problem?

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To stabilise debt, government will target a primary balance by 2022/23. The target measure excludes support to Eskom, because that is part of a separate process.

As a first step, we have identified spending reductions of R21 billion in 2020/21 and R29 billion in 2021/22 mostly in the area of goods and services, and transfers. In addition, non-interest spending in the outer year of the framework is constrained in line with consumer price inflation.

That said, if we want to achieve our target, we will need to find additional measures in excess of R150 billion over the next three years, or about R50 billion a year.

How will we do this?

We will need to deal with the challenges of the wage bill, state-owned companies, executive remuneration and benefits and fiscal leakages.

In the Review accompanying this statement, we set out a detailed analysis of spending on public-sector wages. It shows that 29 000 public servants, plus members of the national executive, members of Parliament, members of the provincial executive, and so forth, each earned more than R1 million last year. After adjusting for inflation, this is more than double the number of civil servants earning more than R1 million in 2006/07.

The average wage increase across government was 6.8 per cent in 2018/19, or 2.2 per cent above inflation. After adjusting for inflation, the average government wage has risen by 66 per cent in the last ten years.

We look forward to robust discussions in the relevant bargaining structures and with other stakeholders to achieve a sustainable arrangement.

We are all in this together.

In the same breath we would like to send a message to state-owned companies, public entities and the private sector. Board and Executive Management compensation and benefits should be reduced.

The President has agreed to guidelines which will apply to members of the Cabinet and members of provincial executives:

1. For the foreseeable future, Cabinet, Premiers and MECs' salaries will be frozen at current levels, with the likelihood of an adjustment downwards
2. The cost of official cars will be capped at R700 000 VAT inclusive
3. A new cell phone dispensation will cap the amount claimable from the state
4. All domestic travel will be on economy class tickets
5. There will no longer be payment for subsistence and travel for both domestic and international trips

I encourage the leadership in Parliament to think about how they can further contain their compensation and benefits.

In the 2019 Budget, some measures were announced. These included:

1. Early retirement without penalisation
2. The national macro reorganisation of government
3. Reducing performance bonuses
4. Freezing of salaries for members of the executive and parliamentarians amongst others

Unfortunately, these have not realised as much savings as we hoped.

Early retirement savings are coming through slower than we originally thought. We will reinvigorate the early retirement programme.

FIXING THE FINANCES OF STATE-OWNED COMPANIES

We must also wean state-owned companies off the national budget. They must learn to stand on their own feet.

ESKOM

Government has announced a comprehensive set of structural reforms for Eskom and the energy sector, which we are supporting with R230 billion over the next 10 years. Very difficult budget adjustments have been made.

To meet unanticipated cash needs, we have brought forward R26 billion in 2019/20, R33 billion in 2020/21 and R10 billion in 2021/22. Further delays in operational reforms could mean additional support is required.

We cannot continue to throw money at Eskom. For the sizeable support required, it cannot be business as usual. Eskom must do the following:

1. Run their current plant and equipment better
2. Achieve other operational efficiencies, including much better cash management
3. Fast track the separation of the utility into three parts as endorsed by the political principals.
There should be no doubt about the policy decisions in this regard

The Minister of Public Enterprises has further elaborated on this in the paper released yesterday.

Going forward, new cash flow support will no longer be equity but will be in the form of loans.

Once I am convinced that the Eskom Board and Management has made an irrevocable commitment to implement government's decisions and there is enough progress, we will negotiate the appropriate size of debt relief.

Eskom is a business and should be run that way.

SOUTH AFRICAN AIRWAYS

SAA is unlikely ever to generate sufficient cash flow to sustain operations in its current configuration.

Which then begs the question: how long are we going to be on this flight path? Forever? I think not.

Operational and governance interventions are required urgently!

I am pleased to learn that there are conversations involving SAA and potential equity partners, which would liberate the fiscus from this SAA sword of Damocles.

We have essentially chosen to subsidise the middle class and wealthy flying around the country and other parts of the world, rather than the ordinary workers who sit in old trains from the townships every day, often getting stuck and being late for work. We are also subsidising the wealthy bond holders, who hold government-guaranteed debt but receive higher yields without additional risk.

E-TOLLS

Cabinet has considered several options to resolve the impasse over the Gauteng Freeway Improvement Project.

Government has decided to retain the user pay principle. While there will be a further dispensation and value-added services, compliance will also be strengthened.

Not paying your tolls has already led to our roads deteriorating. We have been unable to maintain the network. I urge the nation to please pay your bills.

We need to build a culture of payment, as government services can only be sustainable if all of us that can pay for services, do so.

OTHER STATE-OWNED COMPANIES

Other state-owned companies that require support from the fiscus will be subject to certain pre-conditions and principles:

1. Government as a shareholder commits to the highest standard of corporate governance.
2. Managers, and their teams, should not receive bonuses or salary increases when they fail to meet basic financial targets and service objectives. In fact, they should take a pay cut and in some cases be relieved of their duties; and
3. Finally, businesses with outdated business models are a major fiscal risk and should be closed.

PRIORITISING INFRASTRUCTURE

It is critical to drive further infrastructure investment. Public-sector infrastructure projects are plagued by poor planning and implementation. This comes out in underspending, which reached 20 per cent of capital budgets last year. The Budget Facility for Infrastructure, a technical entity that reviews complex capital projects, has already strengthened state capacity.

In addition, government has made progress on a blended finance Infrastructure Fund. The Fund will be hosted by the Development Bank of Southern Africa and will be led by Dr Sean Phillips.

The implementation team for the Fund is at work. They have already identified policy and regulatory hurdles. A pipeline of possible projects amounting to more than R500 billion has been identified. Government has set aside R100 billion over the coming decade to co-finance programmes and projects, with R10 billion in the baseline. Pilot projects receive over R500 million in the current year.

We are working with the private sector to make this Fund a success.

IMPROVING THE EFFECTIVENESS OF THE STATE

We are making progress on improving the efficiency of the state. The state can use its budget better. For example, the South African National Defence Force buys more than R900 million worth of food a year. Operation Koba Tlala, or 'Chase away the hunger' is a deliberate action to buy this food from nearby suppliers.

Where possible, given budgetary constraints, government is shifting resources to areas that urgently need to strengthen capacity. Through reprioritisation, the National Prosecuting Authority receives an additional R1.3 billion, and the South African Revenue Service receives an additional R1 billion for the next two years. These funding shifts will bolster efforts to combat corruption and improve revenue collection.

Earlier this month, Cabinet approved that over 14 000 hectares of land will be released for human settlements development.

National Treasury has reviewed the procurement regulatory framework and developed a Public Procurement Bill. It will be submitted to Parliament in due course.

DERIVING VALUE FROM INTERNATIONAL AND REGIONAL ECONOMIC POLICY

South Africa re-joined the community of nations in 1994 and has played its part in advancing the peaceful international order. In these fiscally constrained times, we must relook at the strategic value of international memberships.

PROVIDING MORE EQUITABLE HEALTH CARE

The National Health Insurance policy aims to provide healthcare more equitably to South Africans.

There are ongoing discussions between the Ministers of Finance and Health, and between our respective departments. Parliament is considering the proposed NHI Bill.

SOUTH AFRICAN RESERVE BANK

We will take stronger measures to fight illegitimate cross-border flows and tax evasion. Our approach to money laundering will be reviewed by the Financial Action Task Force.

Steps are also being taken to strengthen co-operation between the Financial Intelligence Centre, the South African Reserve Bank and SARS.

To promote investment and reduce unnecessary burdensome approvals, by Budget Day, the South African Reserve Bank will propose a more modern, transparent and risk-based approvals framework for cross-border flows. Rules on active currency hedging, loops, and mortgages for individuals living and working in South Africa will be reformed. To support regional integration, the HoldCo regime will be extended to all banks.

Madam Speaker, the South African Reserve Bank has, during a very difficult period, kept inflation stable. They also declared a substantially increased profit share to the government. The Bank is a strange creature of statute – even though we do not own it, the National Revenue Fund receives 90 per cent of the profits, after provisions ordinarily made by bankers.

It is a beautiful arrangement – we do not have to invest any money in the Bank, but we get almost all the profits plus taxes.

CONCLUSION

Madam Speaker, that is my presentation. Government proposes measures to grow the economy. In addition, we are committed to narrowing the deficit, and raising the quality of spending, particularly on large infrastructure projects. As we do this, I trust we have the support of the entire House.

I end my remarks as I began. The winter has been long, but we must prepare for spring and reposition the Republic to grow and to thrive. We need to plant good seeds for our country, both now and for future generations.

Mr President, in June this year you addressed this House and made clear that the policy of our government is:

“...prudent borrowing and stringent expenditure management to stabilise our public finances and lower the debt trajectory.”

That is the work that we must now do, that is what the South African public expects of us.

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We shall return to this House next February with the nation's beloved Aloe Ferox plant having flourished and show a government at work.

As I conclude, may I wish the Springboks all the best this weekend.

My thanks to the President of the Republic for his leadership during this budget process. A word of appreciation to the National Treasury Director General and his team. Their good humour and determination have got us through a difficult MTBPS. My thanks to SARS Commissioner and Team SARS for persevering to restore the integrity of the institution, to the Governor of the South African Reserve Bank for his support and collegiality. To colleagues in the Cabinet, in the Minister's Committee on the Budget, and all those that have supported us in this time. Finally, my appreciation for the Parliamentary Committees who work tirelessly to process the legislation accompanying the Speech.

Thank you.