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COMMENTARY

SUPPLEMENTARY BUDGET, June 2020

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MKI Economics Commentary is a brief note intended to provide MKI's interpretation of key economic events such as the Budget, MTBPS, Monetary Policy (Interest Rates), Employment, data releases and other topical economic events.

FINANCE MINISTER DELIVERS AN EMERGENCY SUPPLEMENTARY BUDGET

On 24 June 2020 the South African Finance Minister, Tito Mboweni, delivered an emergency supplementary budget occasioned by changed circumstances to the February 2020 budget. The Minister outlined the government's financial response to the Covid-19 pandemic. In the February 2020 budget, the National Treasury had forecast the South African economy to grow by 0.9 % this year. Globally, the world economy was expected to grow by 3.3 %. Expectations are that the global economy will now contract by 5.2% in 2020 while the National Treasury expects the South African economy to contract by 7.2%. This massive global contraction has been touted as one that will bring about "the broadest collapse in per capita incomes since 1870". Unemployment in South Africa has meanwhile increased by one percentage point, reaching 30.1 per cent in the first quarter of 2020, highlighting fragility in the economy even before the COVID-19 pandemic wreaked havoc.

THE SUPPLEMENTARY BUDGET: NOTABLE HIGHLIGHTS

- The supplementary budget seeks to set out a roadmap for stabilizing debt, improve spending patterns and create a foundation for economic revival.
- The emergency budget notes that the country has accumulated too much debt and the economic downturn globally and locally will worsen the situation. The high national indebtedness has condemned the country to higher interest rates. The debt needs to be reduced to reduce interest rates and create space for unleashing investment and growth.
- A mix of fiscal, monetary, and other measures including a social compact to mitigate the COVID-19 induced economic downturn are highlighted
- The Revised Fiscal Framework highlights that the gross tax revenue collected during the first two months of 2020/21 was R142 billion, compared to an initial forecast for the same period of R177.3 billion. This reflects a R35.3 billion lag against the 2020/21 target. This has consequently led to a downward revision of gross tax revenue for the 2020/21 fiscal year from R1.43 trillion to R1.12 trillion. The tax target for this year will thus be missed by over R300 billion.
- A consolidated budget deficit of R761.7 billion, or 15.7 per cent of GDP is expected in 2020/21. This

is compared to a deficit of R370.5 billion, or 6.8 per cent of GDP projected in February.

- Projections are that gross national debt will be close to 81.8 per cent of GDP by the end of this fiscal year. This is compared to an estimate of 65.6 per cent of GDP projected in February.
- A Supplementary Budget has been proposed of R21.5 billion for COVID-19-related health care spending. There is also a proposition for a further allocation of R12.6 billion to services at the frontline of the response to the pandemic.
- To support vulnerable households, an additional allocation of R25.5 billion to the Social Development Department has been proposed, for a total relief package of R41 billion
- There have been revisions to the division of revenue presented in the 2020 Budget as follows: the national share for 2020/21 increases from R758 billion to R790 billion, the provincial share decreases from R649 billion to R645 billion and the local government share increases from R133 billion to R140 billion.
- Government expects to narrow the deficit and stabilise debt at 87.4 percent of GDP in 2023/24. Cabinet has also adopted a target of a primary surplus by 2023/24.
- The principles of zero-based budgeting will be applied to the Medium-Term Expenditure Framework process with the upcoming MTEF piloting the process.

- Tax measures of R40 billion over the next 4 years will also be required. The Government will announce details to these tax proposals in the 2021 Budget.
- The Government will be allocating R3 billion to recapitalize the Land Bank. The bank has been deemed too important to fail.
- The Minister did not announce any new measures around the public wage bill as largely expected, effectively skipping the issue for now.

INFRASTRUCTURE WILL BE AT THE HEART OF GROWTH

While some sections of society have highlighted the lack of detail in the budget and the apparent absence of plans to address a possible looming debt crisis, our view is that the placing of this budget in a broader planning context tied to a solid infrastructure plan cannot be underestimated.

The budget notes a successful Sustainable Infrastructure Development Symposium hosted by the President, that has drawn in sector specialists, technical and financial structuring experts as well as policy departments that have considered 177 infrastructure projects across public and private sectors. Within the current constrained fiscal space, initiatives and resources supporting sustainable capital development are critical. The Government has already committed R100 billion over ten years towards the

Infrastructure Fund. This ensures future meaningful economic growth prospects, tax revenue sources and employment. This is while we note that the loans currently sought by the national government from multilaterals are still in effect debt that needs to be repaid with possible tax burden implications for future generations. They are not revenue. On that note, it is also crucial to note that the South African debt-to-GDP ratio is not the highest among its comparable peer countries even though it needs to be controlled. This is not, however, a call for laxity.

CONCLUDING REMARKS

The Minister should be applauded for clearly indicating that if the country continues on its current path, there will be a debt crisis. The country will enter a sovereign debt crisis, a scenario where it can no longer pay back the interest or principal on its borrowings. Although South Africa is not yet in that situation, the absence of game-changing and timely action can easily take us onto that path.

The loans being sought by government should ideally be channeled towards long-term investment in the country's assets. However, we are not in a normal situation and unconventional measures need to be taken to kick-start a process of renewal. Appropriate government expenditure is therefore necessary.

The resolve to stabilize debt by 2023/24 is quite commendable. However, credibility of that declaration could have been strengthened by indicating the necessary decisions to achieve such a feat. Furthermore, solutions still need to be found, for example, to the ailing public enterprises which are draining the fiscus as well as to delivering meaningful economic growth through major policy reform. ESKOM, especially, deserved mention considering questions remain on how it will survive financially. These are matters that will be critical in determining whether we are successful in stabilizing our debt, grow the economy and address the crippling budget deficits.