ABASA POST 2021 BUDGET SPEECH

02 March 2021

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

OUTLINE

1. Economic Outlook
2. Fiscal Framework
3. Fiscal Challenges
4. Fiscal Response to the Fiscal Crisis & Economic Growth
5. Tax Matters
6. Structural Reforms

MACRO-ECONOMIC OUTLOOK

3.3% ECONOMIC GROWTH

Calendar year:	Actual			Forecast			
	2017	2018	2019	2020	2021	2022	2023
Final household consumption	2.1	1.8	1.0	**-5.9** *-7.9*	**2.9** *4.7*	**2.4** *2.2*	**2.0** *1.9*
Final government consumption	0.2	1.9	1.5	**1.2** *1.0*	**-0.1** *-2.5*	**-1.6** *-2.4*	**-1.7** *-3.6*
Gross fixed capital formation	1.0	-1.4	-0.9	**-18.4** *-19.6*	**-2.4** *-1.4*	**3.9** *3.9*	**3.9** *3.9*
Gross domestic expenditure	1.9	1.0	0.7	**-8.9** *-8.5*	**3.5** *2.9*	**2.7** *1.6*	**1.6** *1.3*
Exports	-0.7	2.6	-2.5	**-10.9** *-12.8*	**5.7** *5.9*	**3.0** *3.0*	**2.8** *2.7*
Imports	1.0	3.3	-0.5	**-16.5** *-14.7*	**6.3** *4.7*	**4.6** *2.8*	**2.5** *2.2*
Real GDP growth	1.4	0.8	0.2	**-7.2** *-7.8*	**3.3** *3.3*	**2.2** *1.7*	**1.6** *1.5*
GDP inflation	5.3	3.9	4.0	**4.6** *4.3*	**3.5** *3.9*	**3.7** *4.2*	**4.1** *4.3*
GDP at current prices (R billion)	4 654	4 874	5 078	**4 935** *4 885*	**5 273** *5 240*	**5 590** *5 553*	**5 915** *5 877*
CPI inflation (Dec 2016 = 100)	5.3	4.6	4.1	**3.3** *3.2*	**3.9** *4.1*	**4.2** *4.4*	**4.4** *4.5*
Current account balance (% of GDP)	-2.5	-3.5	-3.0	***1.7*** *-0.8*	***-0.1*** *-1.6*	***-1.0*** *-2.0*	***-1.4*** *-2.7*

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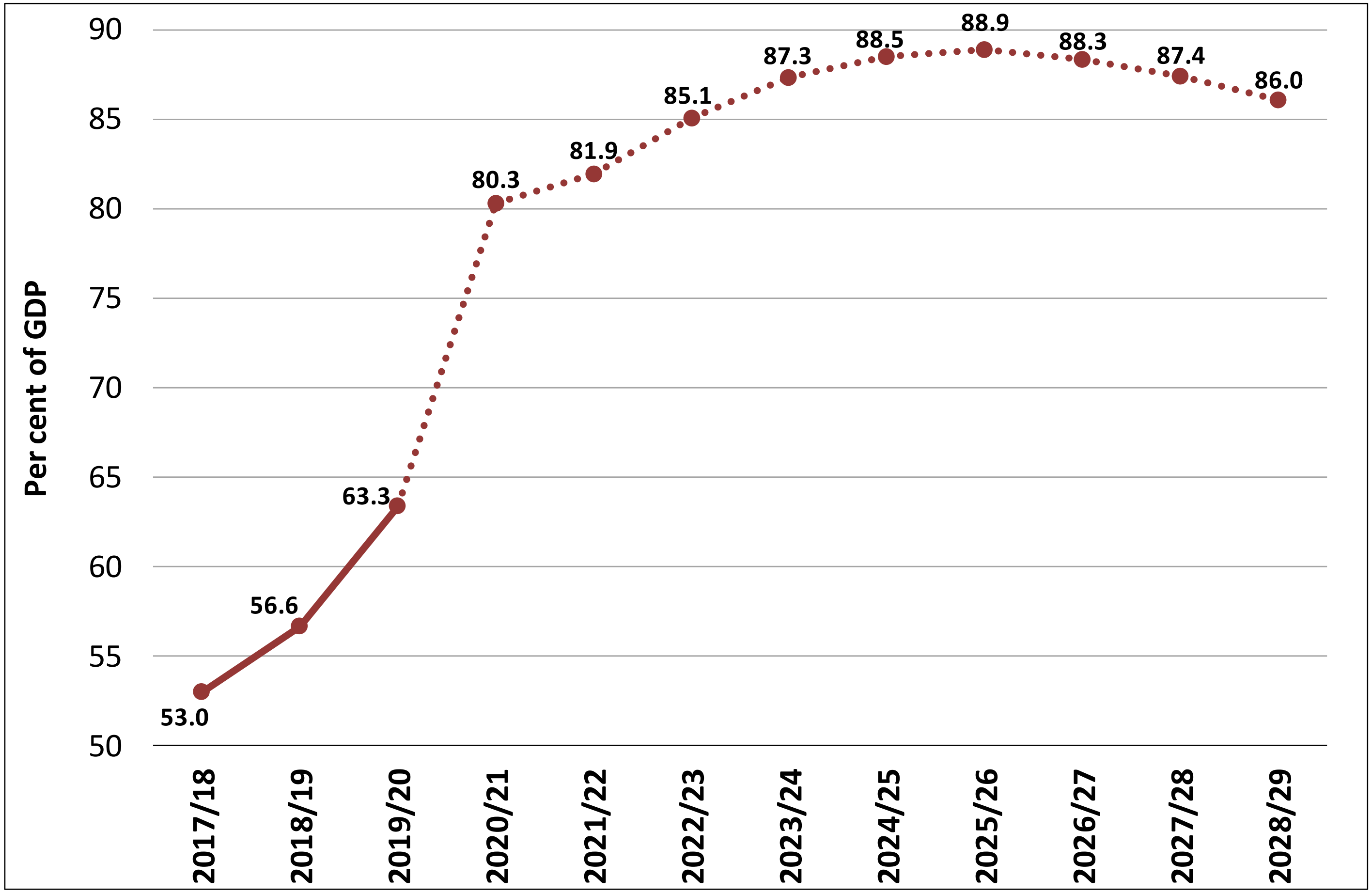
THE 2021 FISCAL FRAMEWORK

Main budget fiscal framework

R million / per cent	2017/18	2018/19 Outcomes	2019/20	2020/21 Estimate	2021/22	2022/23 Projections	2023/24
Revenue	1 196 362	1 275 271	1 345 870	1 200 786	1 351 672	1 453 669	1 522 608
Per cent of GDP	*25.5%*	*25.9%*	*26.1%*	*24.4%*	*25.3%*	*25.7%*	*25.4%*
Expenditure	1 404 940	1 506 598	1 690 923	1 804 879	1 834 252	1 870 833	1 911 046
	29.9%	*30.6%*	*32.8%*	*36.7%*	*34.3%*	*33.0%*	*31.9%*
Baseline allocations	1 242 295	1 324 749	1 486 154	1 572 028	1 552 511	1 557 821	1 567 455
Contingency reserve					12 000	5 000	5 000
Resources over baseline							
Non-interest expenditure	1 242 295	1 324 749	1 486 154	1 572 028	1 564 511	1 562 821	1 572 455
Percent of GDP	*26.4%*	*26.9%*	*28.9%*	*31.9%*	*29.2%*	*27.6%*	*26.2%*
Real growth		*1.9%*	*7.7%*	*2.7%*	*-4.4%*	*-4.2%*	*-3.7%*
Debt service costs	162 645	181 849	204 769	232 852	269 741	308 013	338 591
Per cent of GDP	*3.5%*	*3.7%*	*4.0%*	*4.7%*	*5.0%*	*5.4%*	*5.6%*
Budget balance	-208 578	-231 327	-345 053	-604 094	-482 580	-417 164	-388 438
	-4.4%	*-4.7%*	*-6.7%*	*-12.3%*	*-9.0%*	*-7.4%*	*-6.5%*
Primary balance	-45 933	-49 478	-140 284	-371 242	-212 839	-109 151	-49 846
	-1.0%	*-1.0%*	*-2.7%*	*-7.5%*	*-4.0%*	*-1.9%*	*-0.8%*

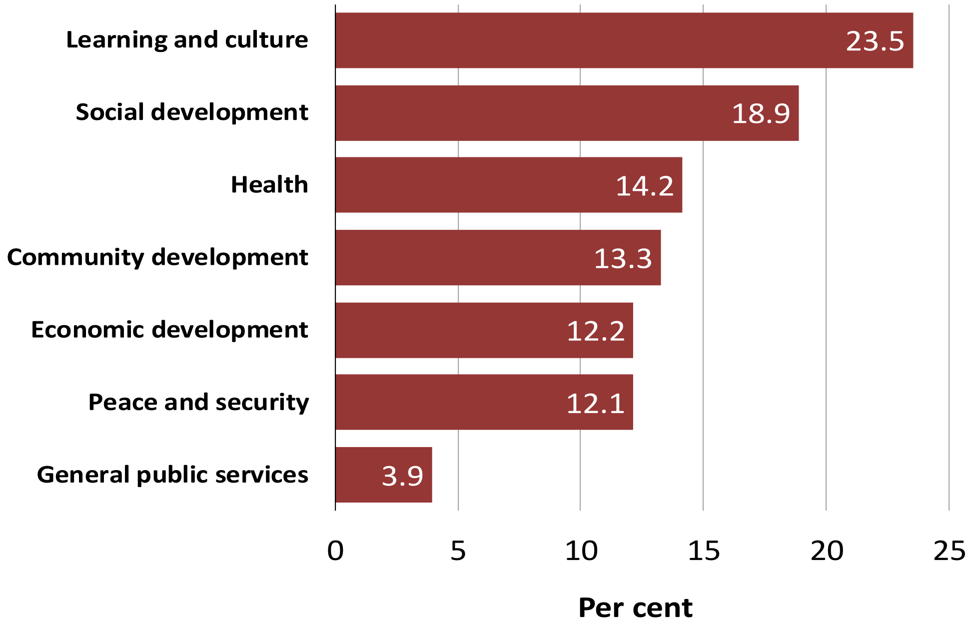
- Compared with the 2020 MTBPS estimates, the expenditure ceiling increases by R2.5 billion in 2020/21, R35.2 billion in 2021/22, R5.7 billion in 2022/23 and R1.1 billion in 2023/24.
- Debt-service costs are expected to reach 5.6 per cent of GDP in 2023/24, from 4.7 per cent of GDP in 2020/21.

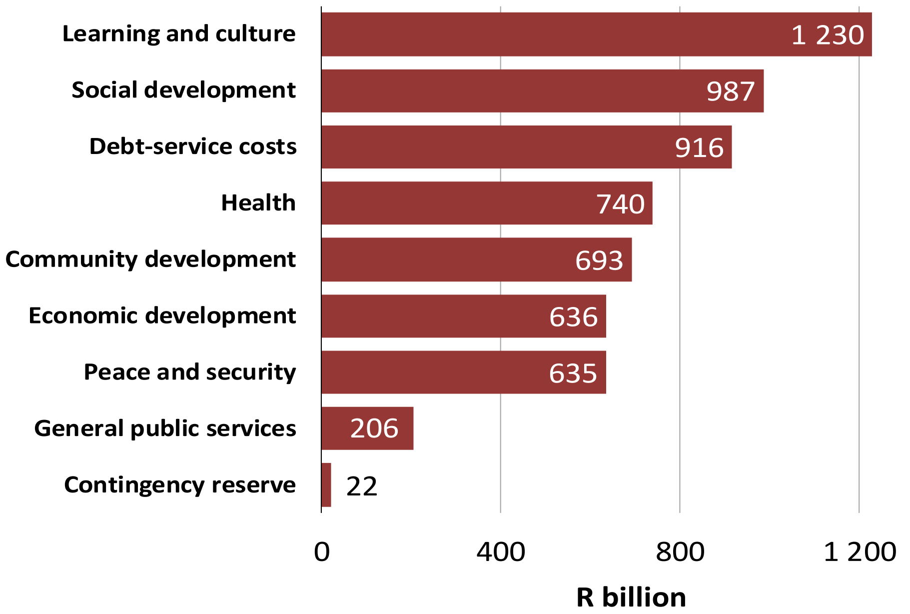
Gross debt outlook



- Under the current economic and fiscal outlook, debt is projected to stabilise at 88.9 per cent of GDP in 2025/26.

The broad structure of the Budget





- More than 56 percent of the budget goes towards learning and culture, health, and social development.

3 WAYS IN WHICH THE 2021BUDGET SUPPORTS ECONOMIC RECOVERY

1. Short term support in the form of crucial health, social and employment interventions
2. Composition of spending favours investment over consumption thereby raising potential growth
3. Macro-fiscal stance lowers the risk premium and supports investment

1 - Short term support in the form of crucial health, social and employment interventions

- **Short-term support to the economy**: funding for crucial health and employment interventions support the economic recovery:
  - Vaccines and rollout (total funding of R11 billion *plus contingency reserve of R12bn*)
  - Employment Initiative (R11 billion)
  - Extension of COVID-19 SRD grant (R6.3 billion)

- Through these interventions, government continues to provide relief to households and businesses.

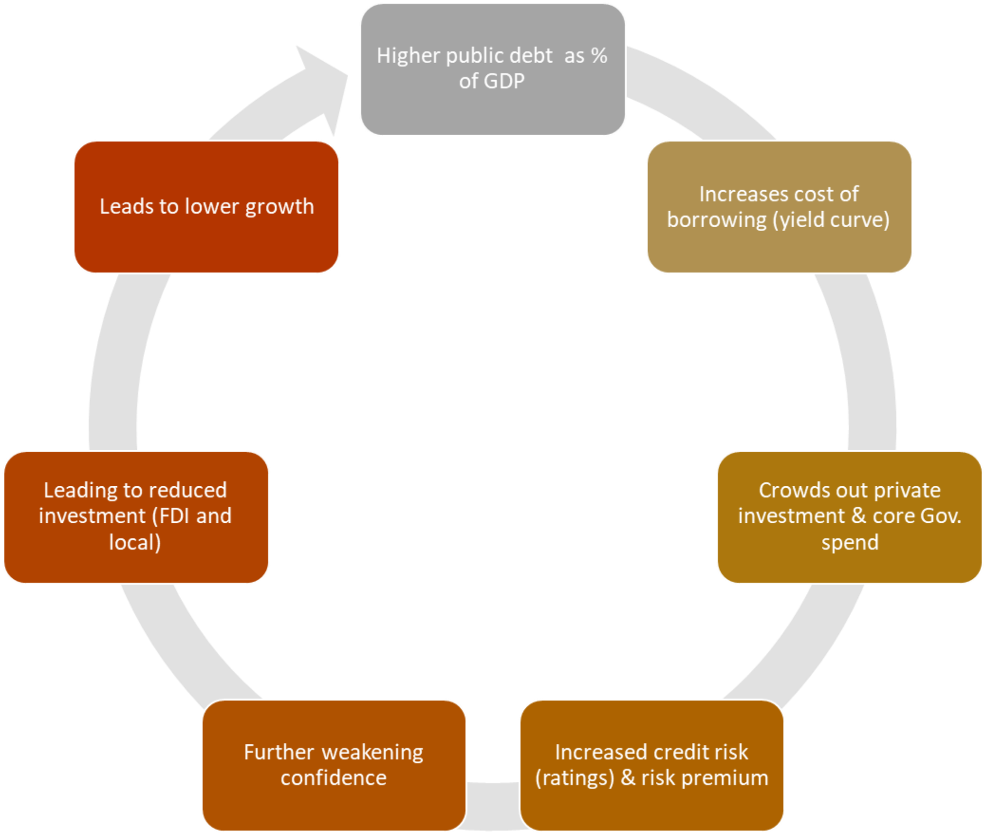
- Apart from the direct health benefits, a successful vaccination programme will allow for the economy to fully reopen.

2 - Composition of spending favours investment over consumption thereby raising potential growth

- **Composition of spending**: infrastructure investment grows over the medium term:.
  - Budget 2021 also provides funding for key infrastructure reforms related to the Infrastructure Fund
- **Medium-term support for key areas of expenditure**:
  - Industrialisation and exports (R110 billion)
  - Agriculture and rural development (R84 billion)
  - Job creation and labour affairs (R81.6 billion. *Inclusive of the already allocated amount of R12.6 billion, public employment initiative amounts to R94.2bn*)
  - Economic regulation and infrastructure (R307 billion)
  - Innovation, science and technology (R53 billion)

3 - Our macro-fiscal stance lowers the risk premium and supports investment

- Fiscal reforms are necessary to ensure debt sustainability as high public debt levels are generally associated with lower growth:
  - Especially in small open economies reliant on global savings
  - Public debt “crowds out” private investment, raises the cost of borrowing (increased yield),
  - Leads to higher future taxation and uncertainty, further weakening investor sentiment
- Higher interest rates mean that a larger share of public resources will go toward paying interest, leaving fewer resources to pay down the debt, invest in infrastructure or pay for social programs
- Conversely, lower debt levels will lower borrowing costs, incentivise investment and are associated with higher growth levels
- Lower debt service costs lays the foundation for stronger, sustainable recovery



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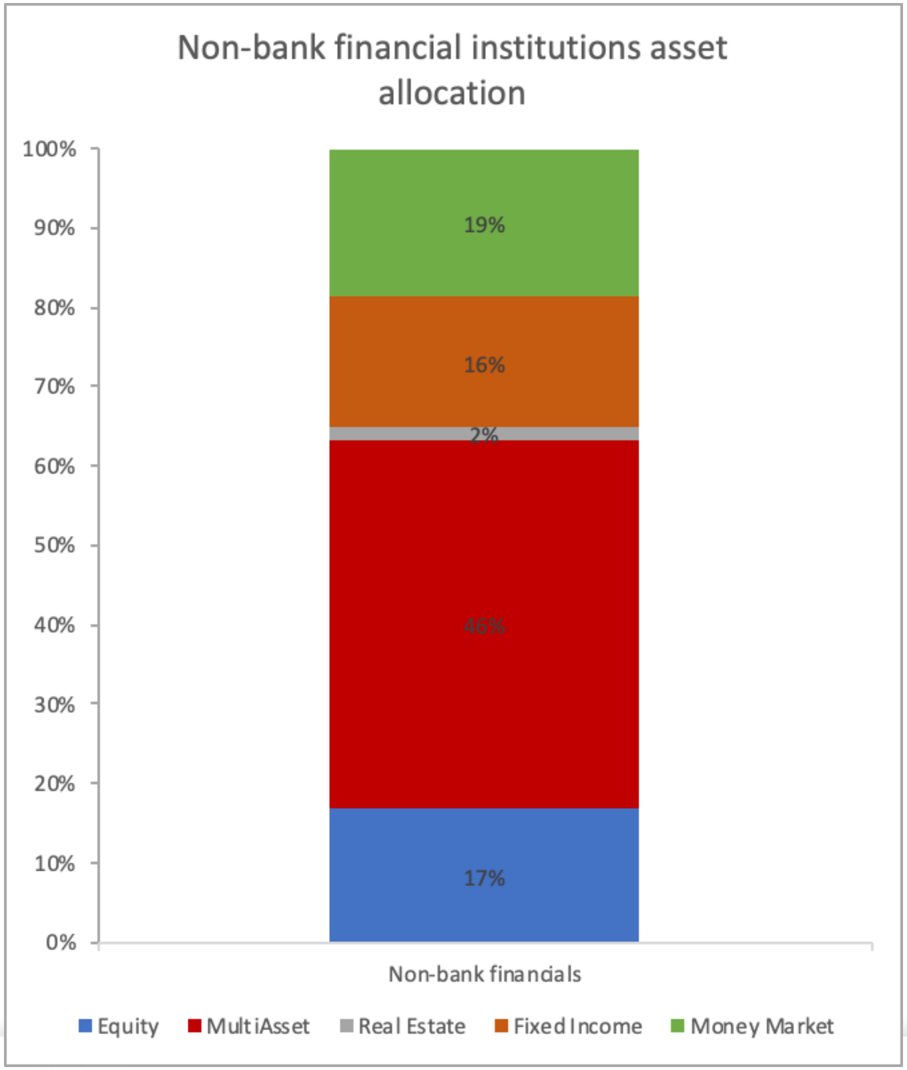
ASSETS UNDER MANAGEMENT (AUM) IN SA NOT GROWING AS FAST AS THE GOVERNMENT GROSS BORROWING REQUIREMENT



- Assets under management in South African R16,65 trillion.
  - R10.05 trillion with non-bank financial sector.
  - R6.6 trillion with the banking sector.
- Non-bank financial sector includes: long-term insurers, short-term insurers, official and private pension funds, finance companies.
- Equities make up about 17% of holdings while multi asset portfolios make up 46% of holdings. Fixed income holding increased to 16% while money market funds were 19%.
- **While AuM is significant, the funds are already invested and there are limits to various instruments.**
- New fixed income allocations will not cover what is required in terms of state borrowing
- Expected withdrawals will further reduce gross savings
- New money is not sufficient to cover increasing government borrowing requirements.

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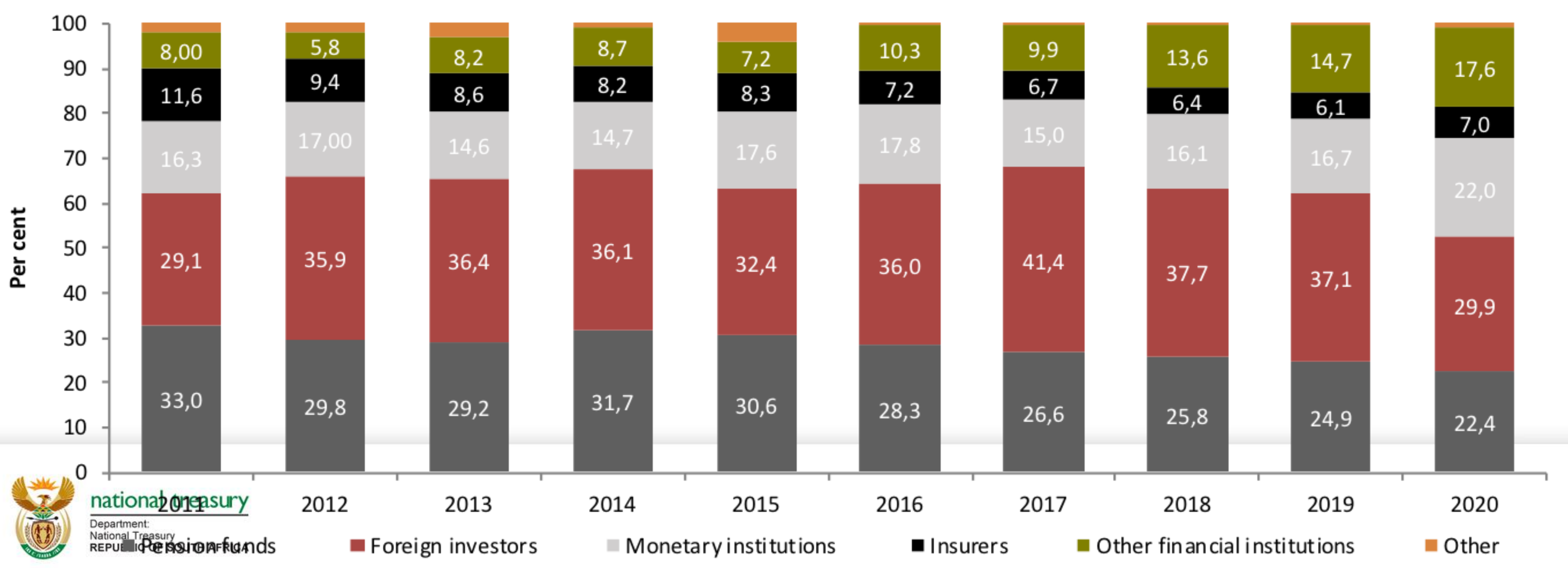
NON-RESIDENCE HOLDINGS OF SA GOVERNMENT BONDS (SAGBS) DECLINING

- International investors remain the largest category of domestic bondholders however in 2020 the foreign bond holdings fell to 29.9 per cent from 37.1 per cent in 2019.
  - Their holdings fell by R8 billion in 2020 relative to an increase of R95 billion in 2019.
- The uncertainty regarding global economic growth prospects in 2020 sparked capital markets volatility and outflows from emerging markets between February 2020 and June 2020.
- As a result of the sudden sell-off by foreign investors and the reduction in the short-term interest rates by the Reserve Bank, **domestic banks and other financial institutions increased their holdings significantly, from 16.7 per cent and 14.7 per cent in 2019 to 22 per cent and 17.6 per cent in 2020 respectively**.

Holdings of domestic government bonds (%), 2011 – 2021



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TAX MATTERS

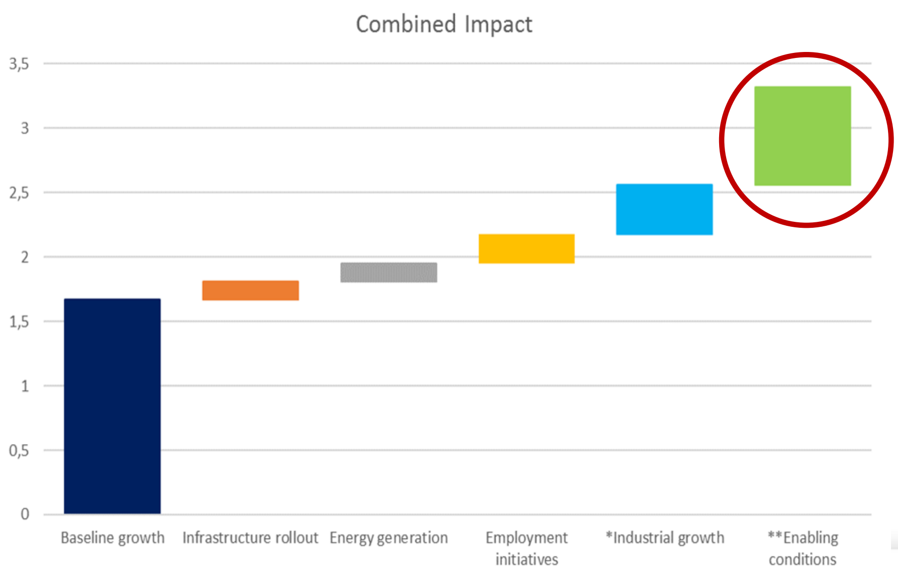
- **Gross tax revenue for 2020/21 10.6 per cent lower than previous fiscal year**. That is R213.2 billion lower than projected in the 2020 Budget
- **Government will not introduce measures to increase tax revenue in the 2021 Budget**; previously announced increases amounting to R40 billion will be withdrawn. This change is expected to support economic recovery by reducing financial pressure on households and businesses.
- **A gradual recovery in revenue is expected over the medium term.** The tax-to-GDP ratio now stands at 24.6 per cent. A strong and sustained economic rebound is required for this ratio to return to pre-COVID-19 levels of 26.3 per cent of GDP by 2027/28.
- The main tax proposals for 2021/22 include above-inflation increases in personal tax brackets and rebates, and 8 per cent increases in excise duties on tobacco and alcohol products.

STRUCTURAL REFORMS

Government's the role in the economy extends beyond just the Budget

Structural reforms will raise growth sustainably at little to no cost to the fiscus

- Modelling of the ERRP illustrates the difficulty in creating growth through sector-strategies
- The biggest impact on growth comes from “enabling conditions”- measures that make it easier and cheaper to do business. This **means** creating an environment in which private sector activity can flourish.



- “The state provides the institutions and infrastructure that enable the economy and society to operate” – National Development Plan
- Our structural weaknesses (i.e. unreliable electricity supply, high levels of concentration, excessive red tape, high cost of doing business) limit the rate at which the economy can grow and create jobs.
- Our structural reform agenda as articulated in the ERRP is aimed at removing the brakes on growth.
- OV has been put in place to support Cabinet to accelerate the implementation of structural reforms which are required to achieve higher levels of economic growth.

Structural Reforms

- Government has identified **Structural Reforms** as one of the urgent Tasks to grow the economy.
- **Electricity** – allow private generation, hence Independent power producers, enabling enable municipalities to procure power from independent power producers,
- **Digital communications sector** – allocation of spectrum
- **Water sector** - independent water economic regulator
- **Transport logistics -** competitive ports, rail network

Thank you