

# The showman must now deliver

Mboweni has been applauded for his opening performance. But can he steal the show?

**Lynley Donnelly**

In some ways this year's medium-term budget policy statement was almost as bad as last year's. The bruising reality check that came with larger deficit and debt figures and lower revenue forecasts brought the optimism of the February budget down with a sharp bump.

But the chief difference between this medium-term budget and last October's was new Finance Minister Tito Mboweni.

The former Reserve Bank governor brought with him the strong views that he is known for and, some analysts argue, credibility to the message of the budget, which was relatively positive, despite the gloomy numbers.

Last year's medium-term budget was delivered by then finance minister Malusi Gigaba, who had been

## MTBPS catches markets off-guard

**Lynley Donnelly**

This week's medium-term budget policy statement (MTBPS) was a bitter pill for markets to swallow and could affect how ratings agencies, especially Moody's, view the country's prospects, according to analysts.

"We expect Moody's to change the outlook of our Baa3 sovereign credit rating from stable to negative, at the very least, with a potential downgrade after the 2019 budget if significant measures are not taken," said Isaah Mhlanga, the executive chief economist of Alexander Forbes Investments.

Key assumptions made in the 2018 February budget were revised as the treasury took account of shrinking economic growth, turmoil in international markets and steep cuts in revenue estimates.

Economic growth forecasts have been cut from the 1.5% announced in February to a much weaker 0.7%, and the budget deficit for this year is now projected to reach 4% of gross domestic product (GDP) compared with the 3.6% expected in February. Revenue collection estimates have been revised down from February by R27.4-billion in 2018-2019, R24.7-billion in 2019-2020 and R33-billion in 2020-2021.

Government debt is now expected to increase to 55.8% of GDP for this year, rising to 58.5% of GDP by 2021-2022, well up from February's estimates of 55.1% and 56.2% respectively.

Moody's is the last remaining ratings agency to class South African government debt as investment

parachuted into the post earlier in the year after the shock axing of Pravin Gordhan and his deputy, Mcebisi Jonas.

The 2017 medium-term budget offered similarly depressing numbers but there was little sense that there was a plan to right the ship.

This time around, Mboweni offered the outline of one, starting with the state's R50-billion reprioritisation of funds for growth and job creation, and its aims to boost investment in the economy.

This medium-term budget was a "difficult story to tell", as Mboweni put it. Economic growth forecasts have been cut from 1.5% to 0.7% for the year, and the budget deficit is now projected to reach 4% of gross domestic product (GDP) compared with 3.6% expected in the February budget. Revenue collection estimates in the coming three years were revised down by around

R85-billion and government debt is now expected to increase to 55.8% of GDP for this year and reach 58.5% by 2021-2022.

In an effort to boost the economy, the state plans to reprioritise R32.4-billion over the next three years, with R15.9-billion being shifted to infrastructure programmes, industrialisation and the expanded public works programme. Another R16.5-billion will be directed to other programmes, including to help to restore the South African Revenue Service.

Another R14.7-billion is earmarked for upgrading informal settlements and R1-billion in housing subsidies is to be used to support low- and middle-income earners to buy homes.

Mboweni, only two weeks into the job, was not largely involved in crafting the detailed policy statement released on Wednesday. Nevertheless, in his speech and when fielding questions from journalists, he signalled his views on several hot-button issues, although

it remains to be seen how some of them sit with his Cabinet colleagues and alliance counterparts.

There is also speculation about how much space Mboweni has to move regarding several tough issues, such as reconfiguring state-owned companies and actively cutting the state wage bill, particularly in a year running up to elections and in what is still below the surface a divided ANC.

But he did not hesitate to tackle some of these issues head-on.

After the last interest rate decision, the ANC released a statement, which was hastily retracted, pleading with the South African Reserve Bank to consider the plight of the poor. The incident has been seen as evidence of political pressure being placed on the bank to go soft on inflation.

Mboweni, in his speech, would have none of this. "Any growth plan must be built on two macro-economic preconditions — a sus-

tainable fiscal position and low and stable inflation. I am confident that governor [Lesetja] Kganyago and his team will continue to work tirelessly to keep inflation down," Mboweni said.

The medium-term budget revealed that no more money would be found to accommodate the public sector wage agreement signed earlier this year. Instead, departments and the provinces must find the money to accommodate this in their existing budgets.

But, despite a decision destined to pit Mboweni against labour unions, he was confident that the country's labour relations framework would enable "consultation and negotiation and settling of disagreements [in] a more responsible way".

He gave a frank appraisal of what the public sector could learn from the private sector, particularly about matters such as performance management and evaluation.

He recounted his experiences of workplaces where employees who did not receive satisfactory evaluations knew, without having to be told, that they should "pack up your bags and go, because you are below par".

"But whether you can have that kind of thinking in the public service, I doubt. But nevertheless there is something in there about performance evaluation," he said.

He also derided the standard government practice of doling out annual 13th cheques.

He stopped short of calling for retrenchments and said the problem could be addressed when wage levels were scrutinised.

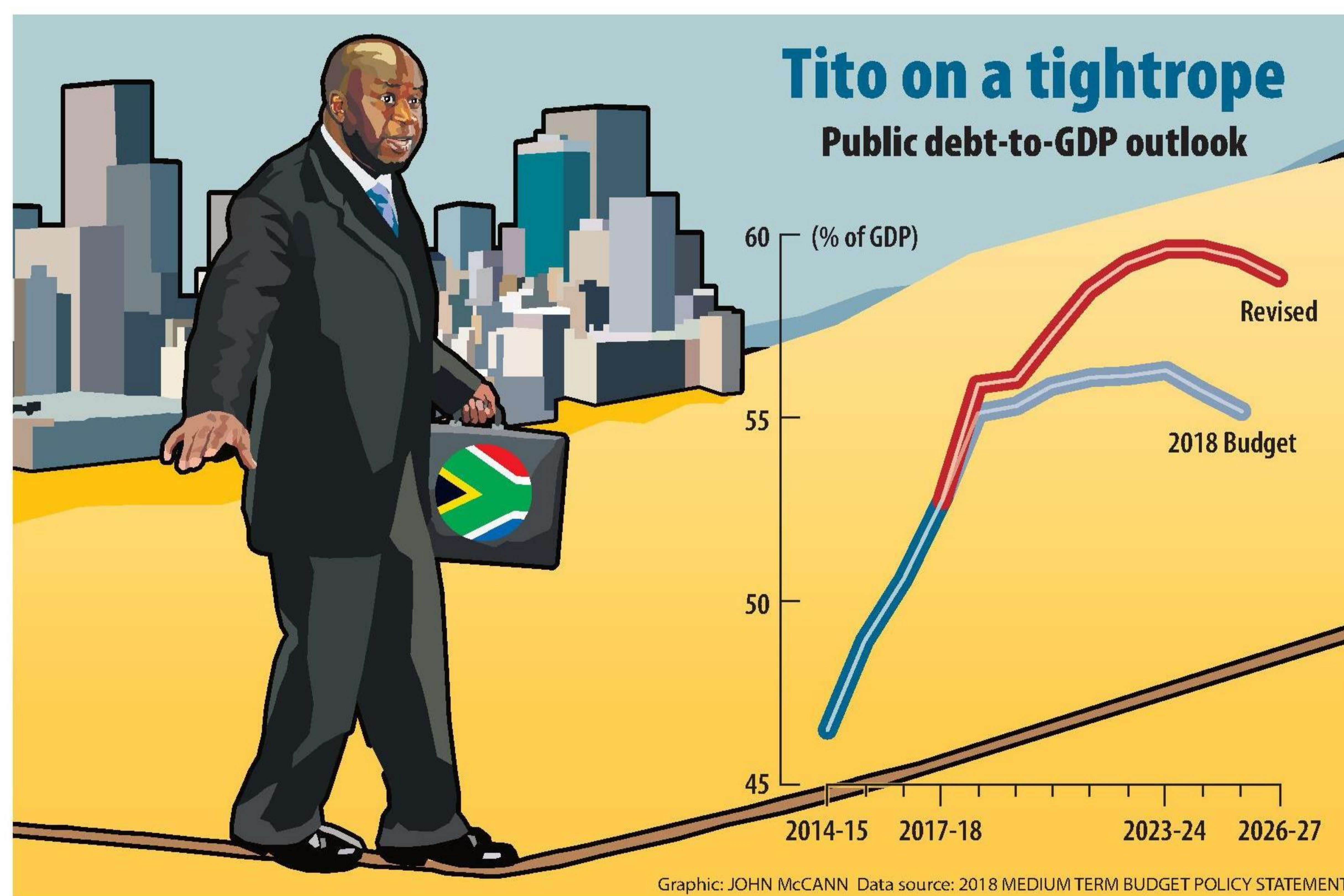
"We can have the same headcount with a lesser wage bill if we agree to do certain things about the level of compensation, for example," he said.

Mboweni also wants to be "open-minded" about letting some private sector thinking filter into the state's approach to public enterprises and even possibly land reform.

Mboweni's frankness and his tough talk about corruption and the "heists" of public funds by dodgy officials may not be enough though.

"The speech was very much Mboweni. Blunt, to the point, full of home truths ... talking about the inappropriate balance between the wage bill and core spending, talking of the need for difficult decisions on SOEs. All very much him, and very much representative of the classic [treasury] conservative-centre-left view as well," said Peter Attard Montalto, the head of capital markets research at Intellidex, in a note. But fundamentally there was not enough political capital in the government or the ANC to undertake some of these difficult reforms, he said.

"Mboweni will be effective at speaking truth to these political blockages in government and the [ANC] NEC [national executive committee]. But he has been on the NEC for some time speaking truth to power and so we don't see what will shift suddenly now."



grade — albeit by only one notch — and its ratings outlook is stable.

In a credit report last week, Moody's noted that South Africa's debt could be downgraded "if it were to become clear that the government will not stabilise its debt burden and contingent liabilities [from state-owned enterprises], and that prospects for a revival in growth falter".

The outcome of the MTBPS could affect Moody's position, according to Citi's South Africa chief economist, Gina Schoeman. This could be seen in some of the figures it published in its report. For example, it had forecast government debt levels moving to 55.5% of GDP in 2018-2019 and 55.6% in 2019-2020, compared with the treasury's revised figures of 55.8% and 56.1% for the same period.

But she did not think it would result in an immediate downgrade. "It wasn't as awful as the 2017 MTBPS and that comes down to institutional strength."

Finance Minister Tito Mboweni sent important signals to the mar-

ket about the reform of state-owned companies and privatisation, she said.

"They [the treasury] haven't announced anything there but he's really paving the way as to which direction that's going," she said.

The treasury made no additional budget allocations to fund increases granted in the public sector wage agreement signed between the state and unions earlier this year. Instead, departments and provinces must find ways to pay for the increases from their existing budgets.

That was positive because it showed political will, said Schoeman.

Nevertheless, it was difficult to reconcile the positive message of Mboweni's speech and the treasury's renewed realistic forecasts with the scale of the changes in the numbers, she said.

"The realism is not necessarily a bad thing; it's just that the change has been quite drastic," she said, adding that "the markets don't like this".

The rand slid by about 2% on the day and government 10-year bond yields leapt from just over 9% before

Mboweni delivered his speech to more than 9.3%.

But Mboweni was relatively sanguine about the market reaction.

"Once the markets look at what is contained in the statement overall, I think they will get a sense of a balance," he said.

Maarten Ackerman, the chief economist of wealth management firm Citadel, said an important factor was Mboweni's emphasis on the need to address the mismanagement of funds, reduce irregular expenditure and ensure that government spending was more efficient. So too was his focus on prioritising investment rather than on consumption spending.

Although the markets did sell off, with bond yields rising and the currency slipping notably, "we should not discount the positives contained in this important MTBPS", Ackerman said.

"The economy may look a little bit weaker over the medium term, [but] eventually these policies will restore confidence and attract investment back into South Africa."