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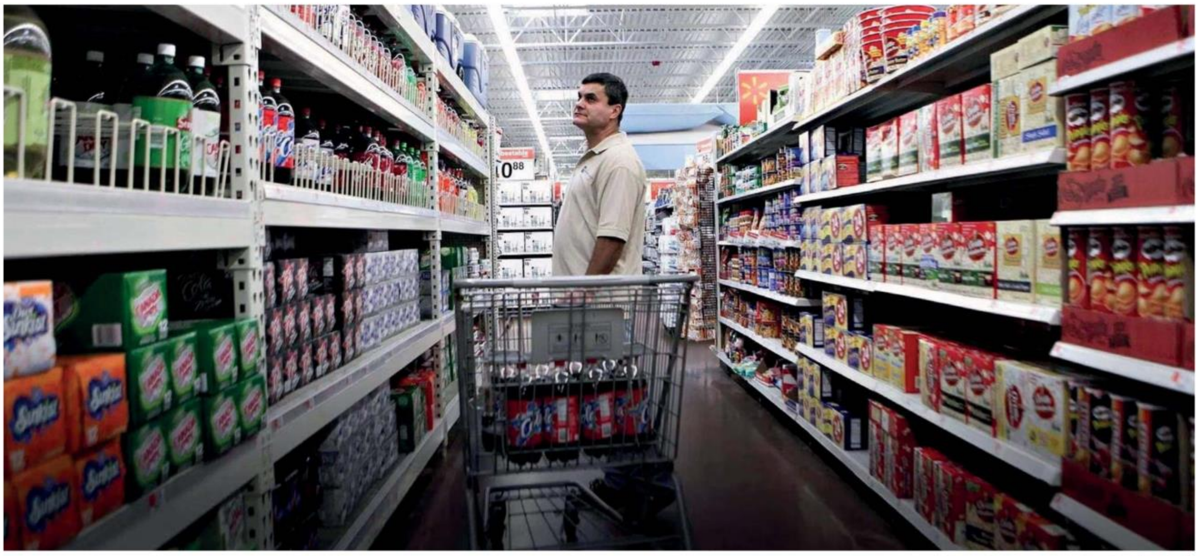
Tips for Treasury on how to stabilise public finances

It is urged to implement cuts to nonessential expenditure, reduce or merge the number of government departments and manage the compensation of public servants



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By **Ray Mahlaka**

To save public finances from collapsing and avoid a debt blowout, the National Treasury is considering unpopular choices that might further stall South Africa's struggling economy, throw the country deep into austerity and harm service delivery.

The country's financial situation has worsened considerably since the Budget was tabled in February, suggesting that the government might be running out of money.

Recent data suggests that South Africa is heading for a larger-than-expected budget deficit this year, as government revenue from tax collection is declining on the back of severe Eskom blackouts and logistical constraints by Transnet – while its expenditure rises.

Data from the Treasury shows government expenditure by July had reached R685-billion (vs R628-billion a year ago), whereas revenue was much lower at R494-billion (vs R510-billion).

To stabilise public finances, the Treasury is considering increasing taxes (mainly VAT by two percentage points), implementing more spending cuts that will harm crucial service delivery programmes, reconfiguring the state by reducing or merging the number of government departments and state-owned enterprises, and managing the compensation of public servants.

A stronger budgeting process is being considered to limit government borrowings by implementing a debt ceiling.

These options are still under discussion and a decision is due to be unveiled when the Medium-Term Budget Policy Statement (MTBPS) is tabled on 1 November. The big question is which route the Treasury will take to respond to the deteriorating fiscal situation.

In his first speaking engagement with editors since his appointment as the Treasury's new director-general on 1 September, Duncan Pieterse said his priority was to restore the strength and credibility of South Africa's fiscal framework.

"The underperformance in revenue collections this year has meant we have to think very differently now about what a credible fiscal framework looks like. One of the tasks we have is placing the trade-offs very starkly and clearly at the centre of the budget process.

"One of our roles is to advise the [finance] minister and Cabinet on the trade-offs and ... we need to put it in very concrete terms," Pieterse said.

Pieterse, who joined the Treasury a decade ago and has headed the economic policy and asset and liability management departments, is emphatic that the implications of not dealing with inefficient spending or reconfiguring the state will push the Treasury to borrow more money or increase taxes.

"Both of these options have consequences in this environment where our debt service costs are much higher and crowd out other costs [because of higher interest rates and yields on borrowings]. When you have increased taxes, they raise much less revenue than we anticipated. But tax increases have a direct impact on the ability of the economy to grow."

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Treasury's options

Daily Maverick asked several economists and market watchers about the options that the Treasury should consider to reform public finances.

Sanisha Packirisamy, an economist at Momentum Investments, does not believe the government will pursue tax hikes, especially on VAT, in the run-up to a national election, "particularly given the tough economic backdrop faced by consumers".

To reduce government spending, Packirisamy said the Treasury could cut down on nonessential expenditure (such as travel, accommodation and catering, and workshops for government officials) and put plans in place to curb headcount in the public sector.

Packirisamy said any expenditure reduction efforts by the Treasury might be undermined by the pressure to provide more financial assistance or bailouts to ailing state-owned enterprises.

Further undermining spending reduction efforts are calls for the government to extend the R350-a-month social relief of distress grant, which expires in March 2024, just before the general election.

The Treasury has not budgeted for the extension of the grant beyond next year (other than having an unallocated reserve of funds initially mooted for the grant), or taken a position on whether it would roll it over to more permanent welfare such as a basic income grant.

Krutham MD Peter Attard Montalto said it would be impossible to remove the grant before an election, adding that the governing ANC had also drawn a firm line against VAT hikes. The Treasury is largely seen to be against the grant, seeing it as a poor and inefficient alternative mechanism to other labour activation and economic participation policies.

With tax hikes not seen as an option, Attard Montalto said that leaves the government to cut expenditure by reconfiguring its functions. Doing so would involve, among other things, shifting the Small Business Development and Tourism departments into the Department of Trade, Industry and Competition, and removing the Department of Public Enterprises (already happening).

The Department of Sport, Arts and Culture would be dissolved, various state organs such as the Government Communication and Information System and the Department of Planning, Monitoring and Evaluation would be moved into the Presidency, and the Department of Public Works and Infrastructure would be moved to the Treasury.

Nedbank economists Isaac Matshego and Nicky Weimar said there was an "urgent need" to contain spending to "restrict the widening of the budget deficit and the consequent increase in public debt and debt service costs". After all, since April, interest payments on government debt have jumped 19.3% to R98.2-billion because of elevated interest rates and high risk premiums on government bonds. **DM**

Ray Mahlaka is a Business Maverick associate editor.