NEDLAC

July 2, 2021

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KEY POINTS

- Economic growth has underperformed global and EM norms for much of the last decade.
- High government spending (4% above inflation for a decade) and higher debt (15% above the EM average) failed to lift growth.
- Structural reforms essential for growth momentum rather than higher deficits and further accumulation of debt
- Fiscal consolidation necessary to avoid a debt/fiscal crisis
- Consolidation cannot be achieved through higher tax alone
- Spending prioritization needs to significantly improve
- Major improvements in procurement and contract management needed to reduce waste, fruitless and irregular spending

DECELERATION AND DECOUPLING

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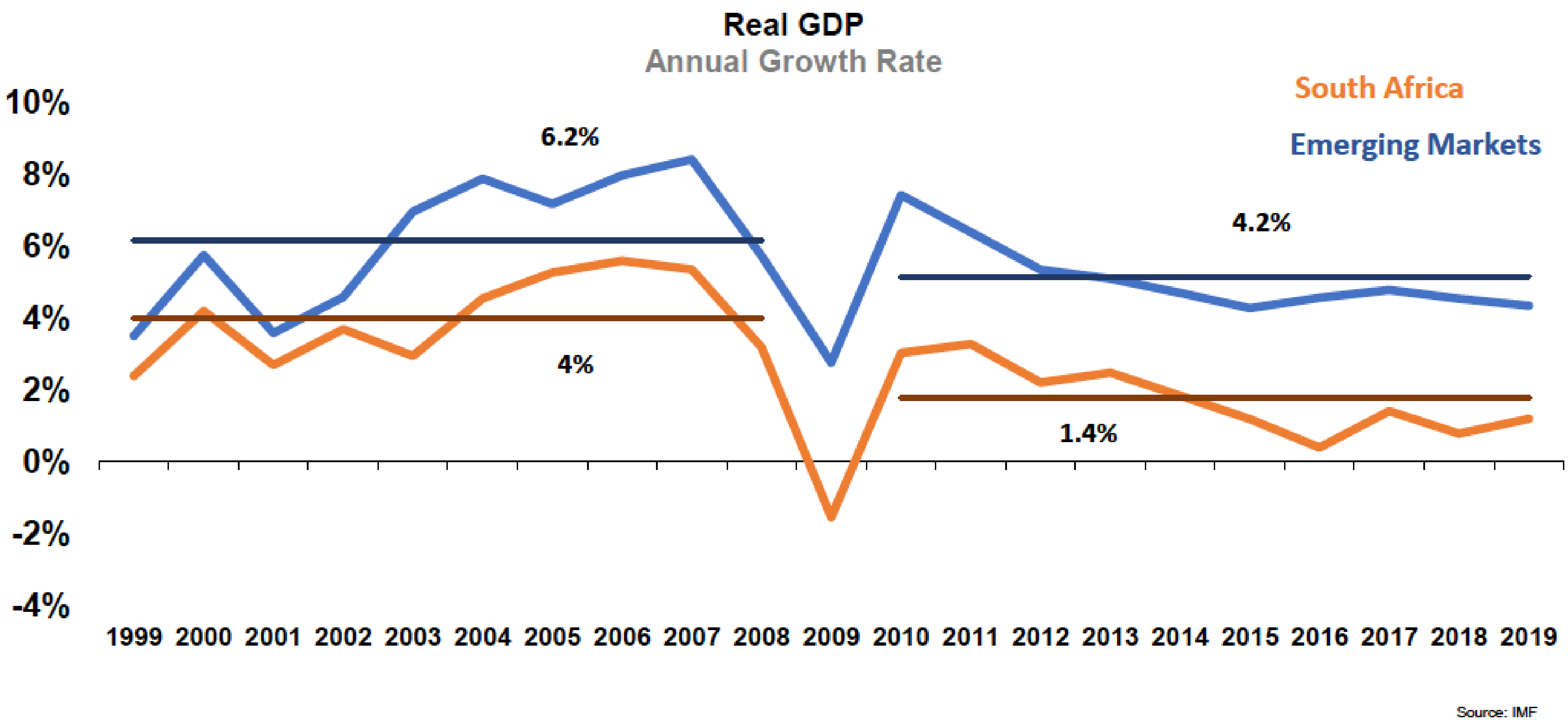
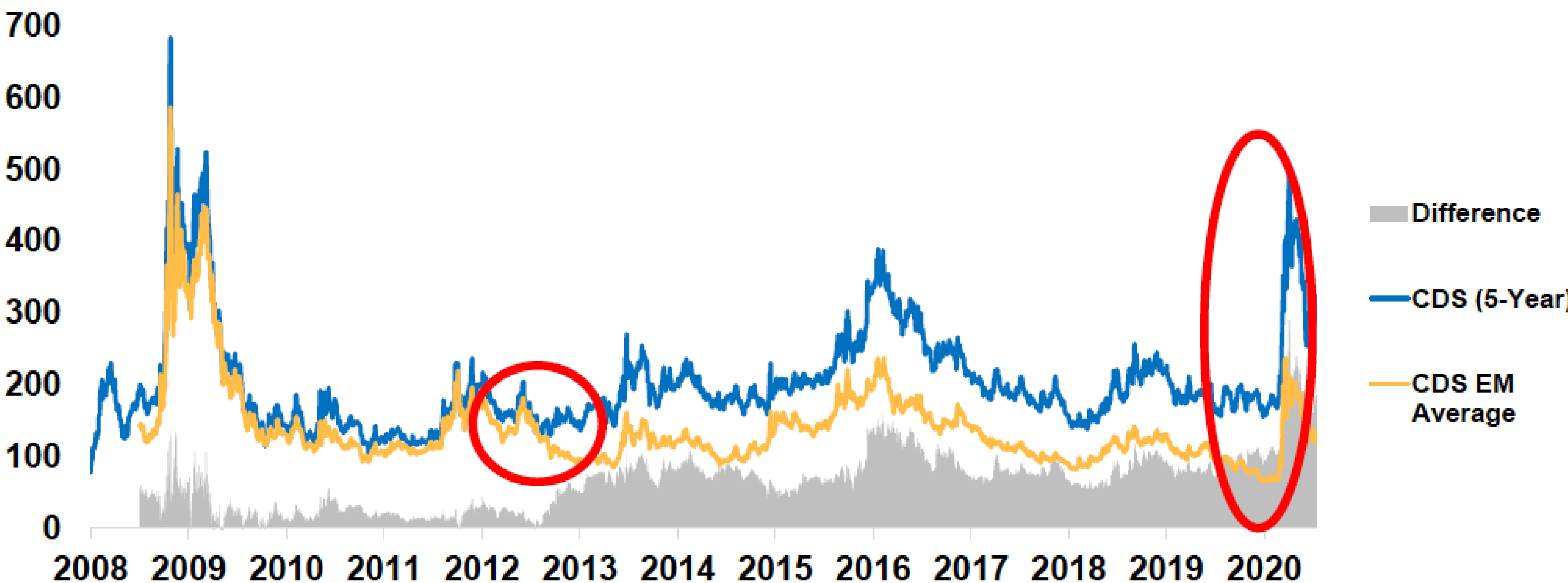


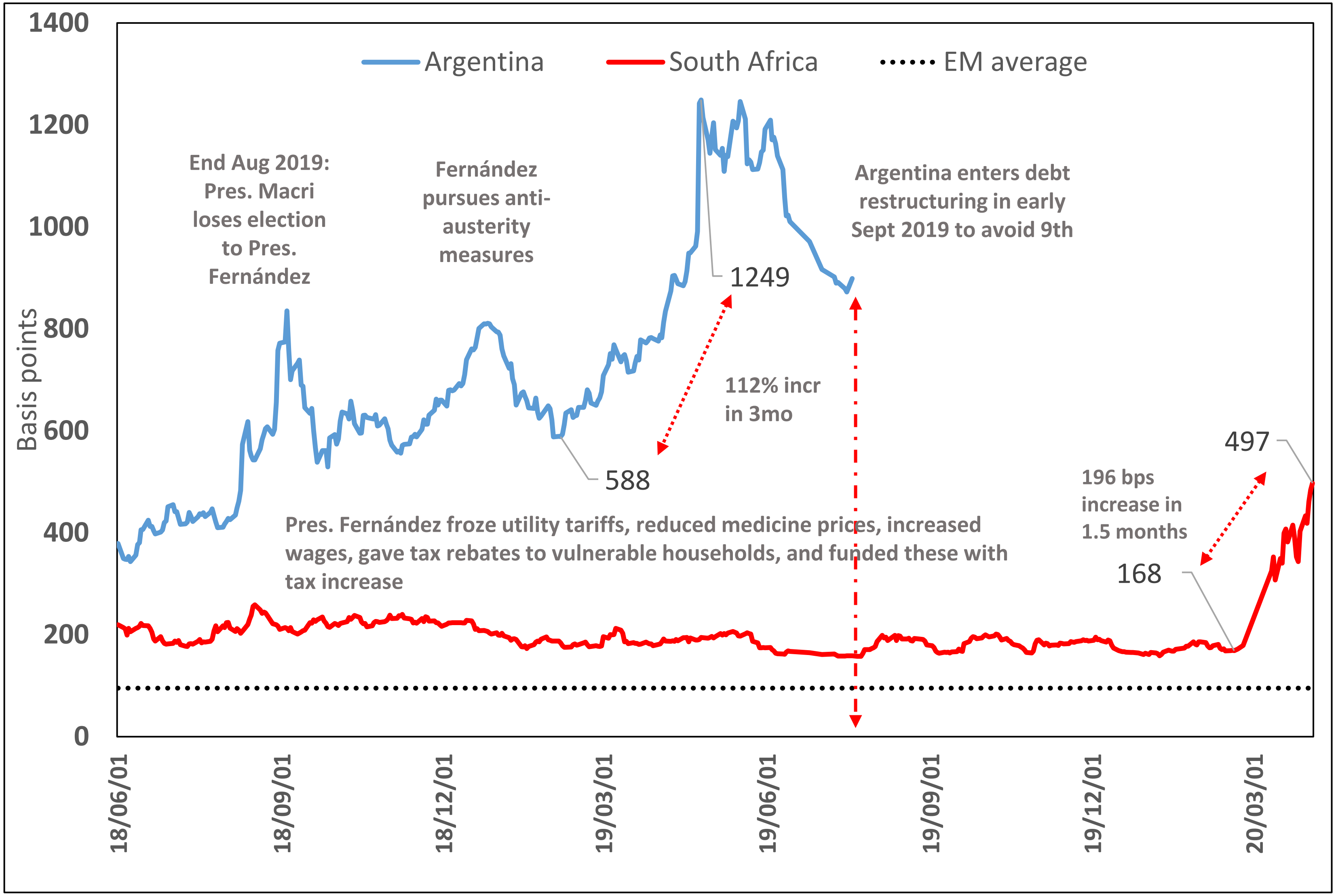
- SA was already underperforming its EM peers before the current crisis, and more so in recent years.
- This illustrates long-run structural weaknesses, rather than the need for cyclically-driven demand stimulus

SA VS OTHER EMERGING MARKET – PROBABLY OF DEFAULT



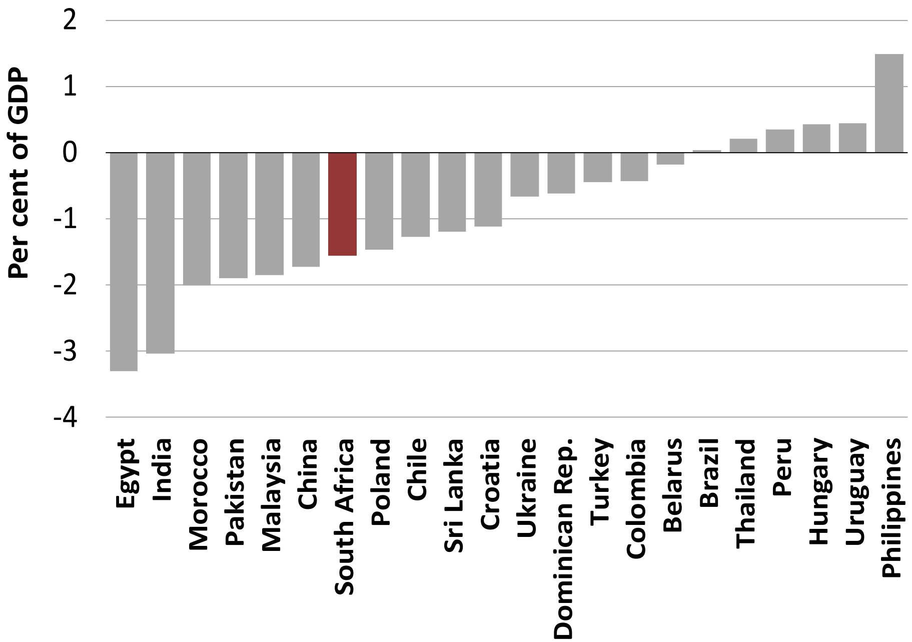
- The CDS spreads are an indicator of the market perception of South Africa's risk of defaulting on its debt
- Sovereign spreads have sustainably decoupled from other EMs since around 2011.
- This means that investors are increasingly differentiating between markets, including in the context of stronger global liquidity

HAS THE CREDIT RISK PROFILE CHANGED?

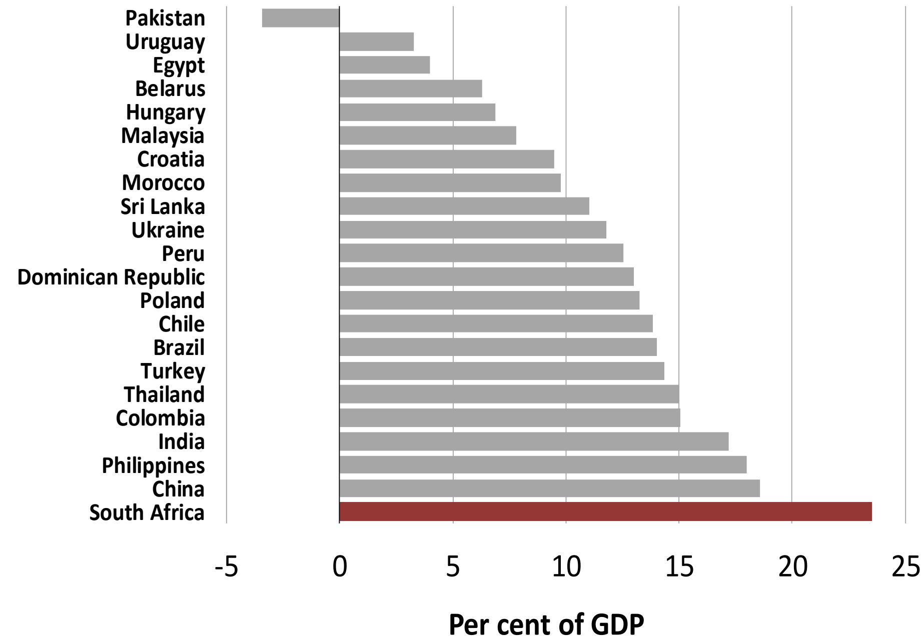


South Africa in global context

Average primary balance, 2009 – 2019



Projected three-year increase in debt



Source: IMF Fiscal Monitor, October 2020

- In comparison with a wide range of other developing countries, South Africa's average primary balance over the last 10 years falls in the middle of the distribution.
- But South Africa's three-year increase in debt to GDP is the among the largest.
- Fiscal distress is mounting in developing countries amid historically high indebtedness. In this environment of rising fiscal pressures, South Africa is losing ground to its peers.

THE DEFICIT HAS BECOME STRUCTURAL

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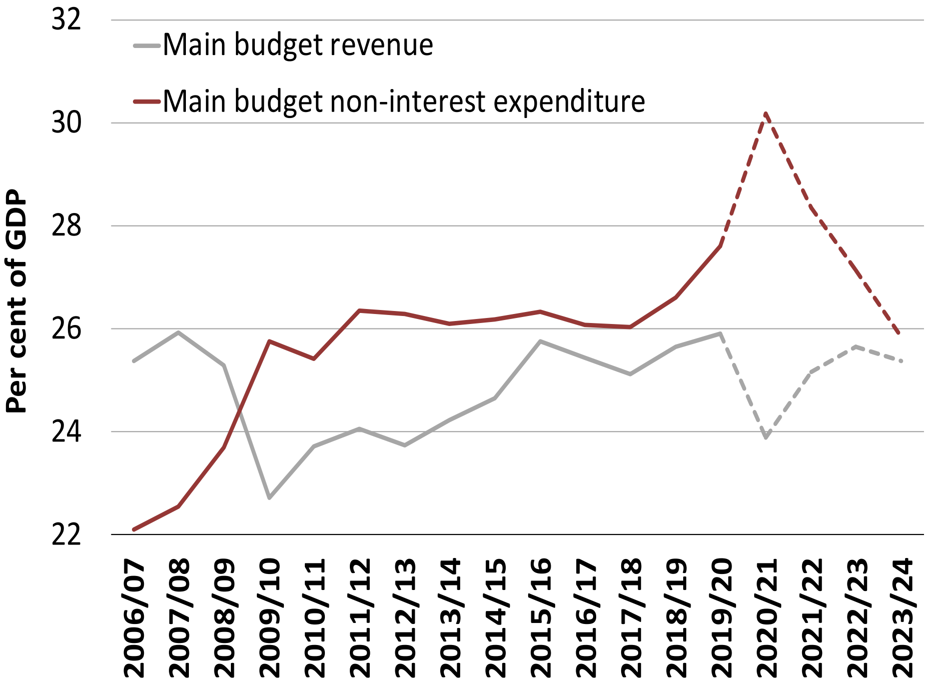
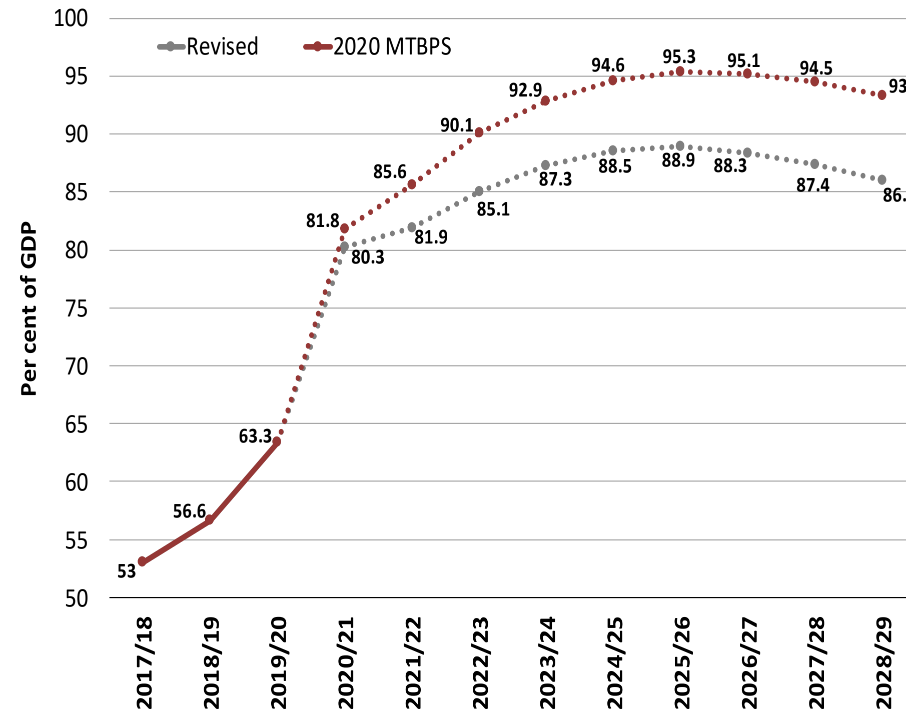
Main budget revenue and expenditure*



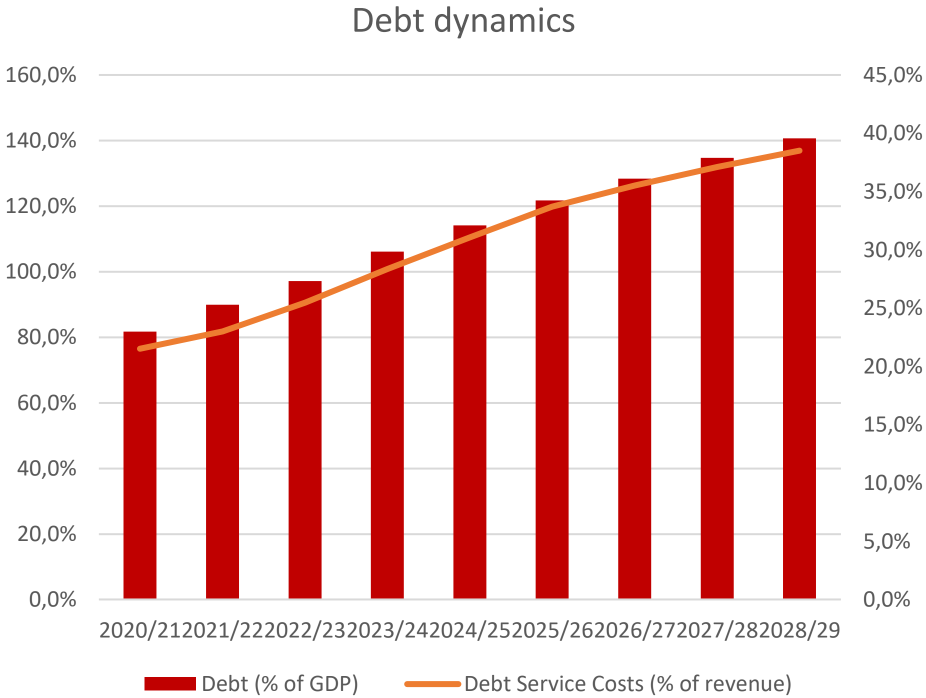
Excludes Eskom financial support and transactions in financial assets and liabilities

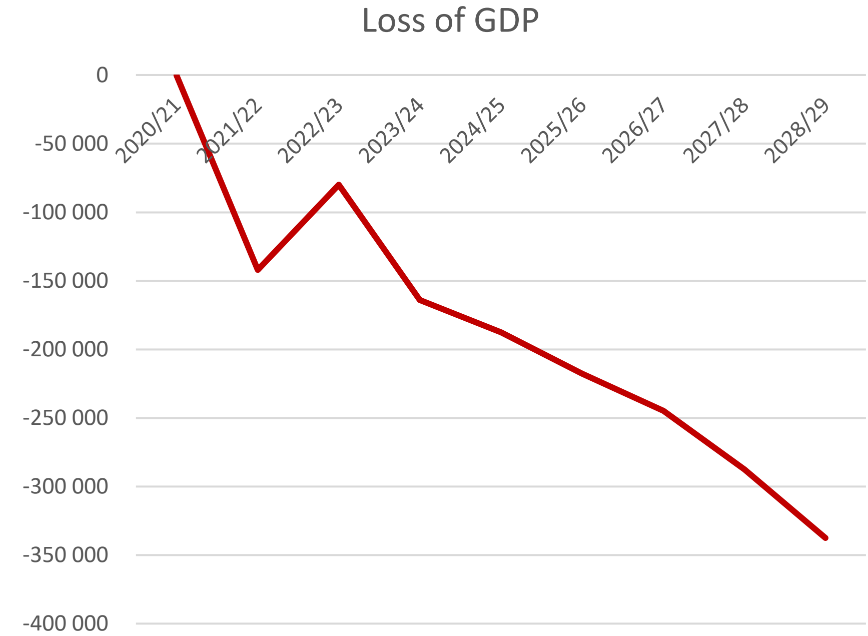
Gross debt-to-GDP outlook



- The main budget primary deficit is projected to narrow over the medium term and gross debt-to-GDP is now projected to stabilise at 88.9 per cent of GDP in 2025/26.

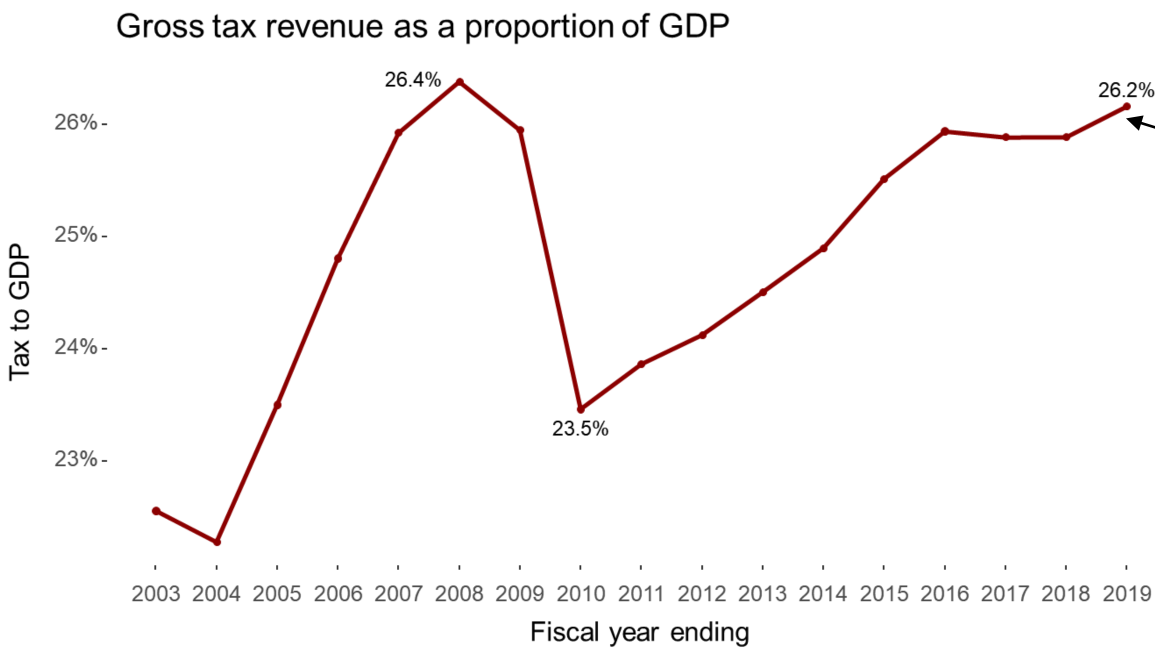
A FISCAL CRISIS CAN HAVE LONG RUN & PROFOUND IMPLICATIONS





- Failure to arrest the debt trajectory will see debt service costs consume around 27% of tax revenue by 2024/25
- The stock of debt crosses the 100% mark in 2023/24, reaching 140% in 2028/29
- Deficits remain elevated at around 12% of GDP for a long-time, severely constraining domestic saving and investment
- A fiscal crisis could deduct more than R2 trillion from nominal GDP over the next decade

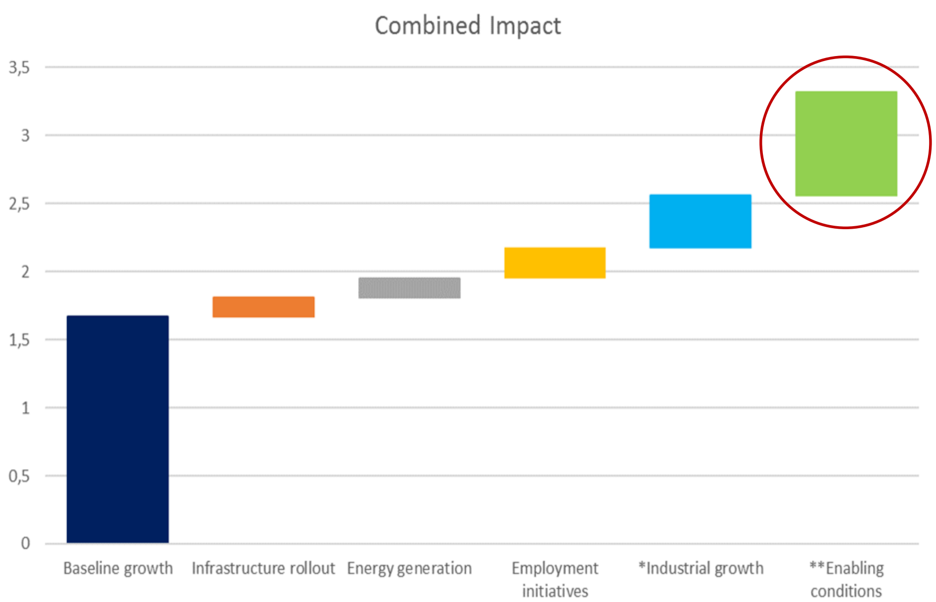
SOUTH AFRICA IS NOT A LOW TAX COUNTRY



Tax-to-GDP actually stayed flat over the two years with large increases in tax rates (2016/17 and 2017/18)

STRUCTURAL REFORMS WILL RAISE GROWTH AND CREATE JOBS

- 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.
- The biggest impact on growth comes from resolving these structural constraints to growth by 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 reform agenda as articulated in the Economic Reconstruction and Recovery Plan is aimed at removing the brakes on growth.
- **Operation Vulindlela** has been put in place to support Cabinet to accelerate the implementation of **high-impact structural reforms** which are required to achieve higher levels of economic growth.
- For example, the CSIR estimates that there is about 3 400 MW of electricity capacity that could be deployed by the end of 2022 if the appropriate regulatory regime were in place to support embedded (self) generation.

FISCAL STRATEGY

- South Africa's fiscal challenge is to balance the immediate need for support to the economy during the pandemic with ongoing efforts to close a large, pre-existing budget deficit. In this context, the fiscal strategy aims to:
  - Narrow the deficit and stabilise the debt-to-GDP ratio, primarily by controlling non-interest expenditure growth.
  - Provide continued support to the economy and public health services in the short term, without adding to long-term spending pressures.
  - Improve the composition of spending, by reducing growth in compensation while protecting capital investment.
- Efforts to reduce growth in the public-service wage bill remain on course, with the Labour Appeal Court of South Africa confirming that the National Treasury must certify the affordability and sustainability of wage agreements prior to their implementation.
- Significant risks remain. The global outlook is highly uncertain, with the economic recovery largely dependent on responses to COVID-19. Several state-owned companies are requesting additional funding. Negotiations on a new public-service wage agreement are set to take place this year.

MEDIUM TERM SPENDING PRIORITIES

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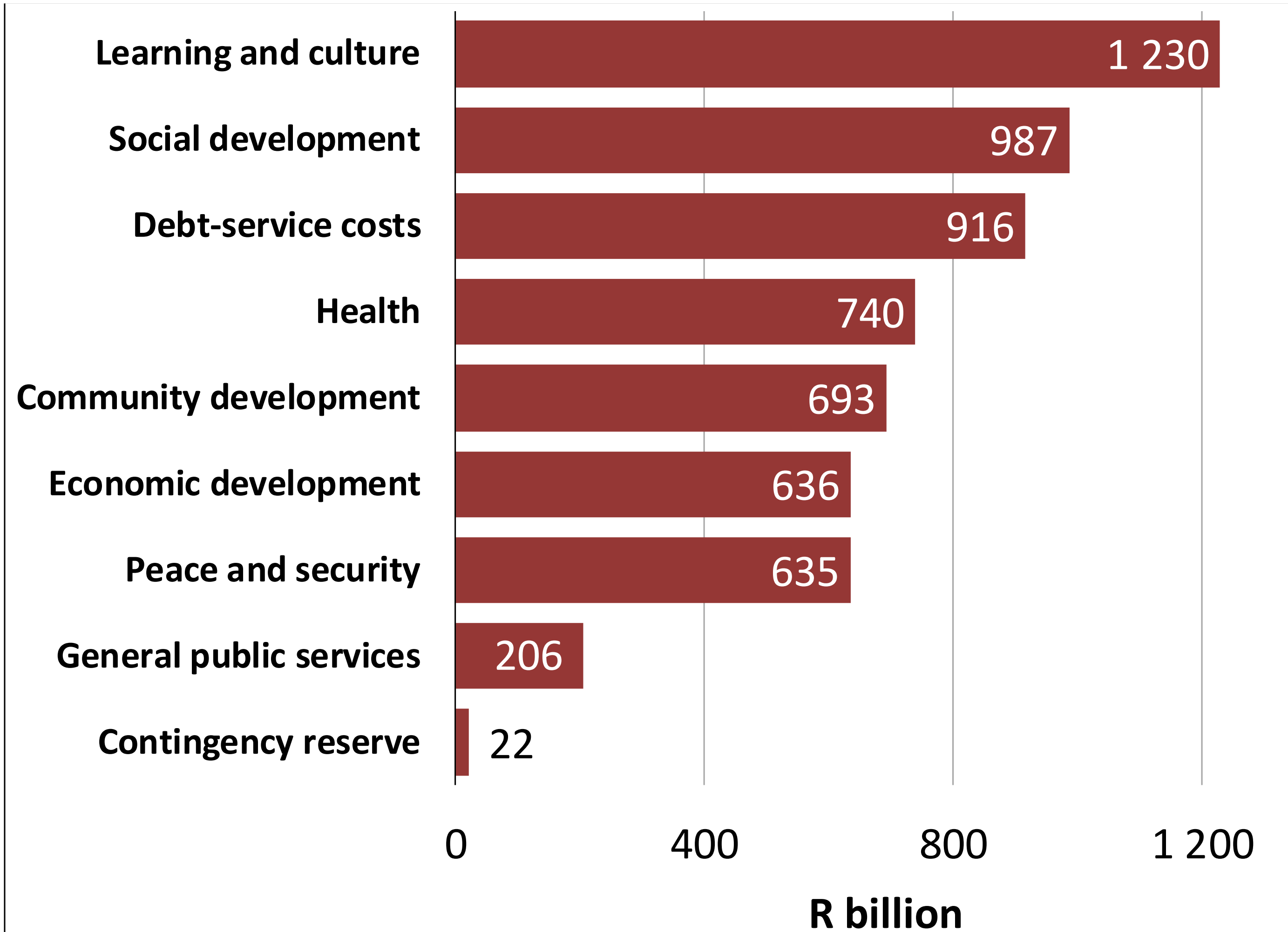
Consolidated government expenditure by function, 2021/22 — 2023/24



- Over half of allocations go towards learning and culture, health, and social development functions over the medium term.
- Debt-service costs, estimated at R916 billion over the MTEF period, is the third largest spending item by function

HOW BUDGET 2021 SUPPORTS ECONOMIC GROWTH

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- **Fiscal sustainability**: Increasingly unsustainable fiscal outlook acts as drag on economic growth:
  - Budget 2021 presents an improved debt-to-GDP outlook relative to the 2020 MTBPS, which should take pressure off interest rates, reduce crowding out, and improve investor sentiment.
- **Short-term support to the economy**: funding for crucial health and employment interventions support the economic recovery:
  - Three-month extensions of the special COVID-19 social relief of distress grant and the Unemployment Insurance Fund's Temporary Employer/Employee Relief Scheme, and funding for the public employment initiative and for provincial hospitals in 2021/22.
  - Up to R10.3 billion is provided for vaccine rollout for the current year and over the next two years.
  - The contingency reserve increases from R5 billion to R12 billion in 2021/22, given uncertainty around vaccination campaign costs. These interventions do not add to longer-term expenditure.

Table 5.2 2021 Budget additions

R million	2021/22	2022/23	2023/24	MTEF total
2021 Budget additions to baseline	**22 446**	**4 602**	**2 283**	**29 332**
COVID-19: Vaccine rollout	5 200	3 000	–	8 200
COVID-19: Managing second and third wave	8 000	–	–	8 000
Extension of the special COVID-19 social relief of distress grant	2 145	–	–	2 145
Other adjustments[1]	7 101	1 602	2 283	10 987

1. Includes the New Development Bank, financial support to state-owned companies and public entities, and the rescheduling of some infrastructure reductions introduced in the 2020 MTBPS

PUBLIC PROCUREMENT BILL TIMELINE

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Mar 2021

Jan - Mar 2021
Public Comments collated and considered

June 2021

April 2021
Review and Revise Draft Bill incorporating public comments

May 2021
Internal NT Consultation

Aug 2021

July - Aug 2021
Stakeholder consultations:
- DTIC
- DSBD
- DCoG
- DPWI (CIDB & CEB)
- DPME
- ANY OTHER
- NEDLAC

Oct 2021

September 2021

Nov 2021

November 2021
- Obtain Minister's approval to submit draft Bill to Cabinet
- Submit Cab memo and Bill to Cabinet
- Consideration by Cabinet
- Obtain Cabinet's approval to submit to Parliament
- Obtain final certification of draft Bill for introduction in Parliament by State Law Advisers & proofreading of draft Bill

Dec 2021

December 2021
- Introduction of Bill in Parliament
- Consideration of Bill by Parliament

USE OF IT SYSTEMS IN PROCUREMENT

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- A review of Supply Chain Management (SCM) technology in the public service confirmed that fragmented systems undermine the effectiveness and efficiency of procurement function. It was also noted that amongst the estimated 56 different technologies employed at national, provincial and local government, very few examples of SCM Information and Communication Technology (ICT) modernisation could be identified.

- Inefficiencies in procurement are often related to the duplication of effort and cost relating to high-volume-low-value transactions and manual processes. International studies have shown that considerable saving of administrative costs and process efficiency can be achieved by automating supply chain management processes and also improve audit outcomes within Organs of State.

- The National Treasury, together with the Provincial Treasuries, are investigating opportunities to use IT to improve transparency by:
    - Openly publishing procurement plans of all organs of state
    - Publishing all tenders awards and suppliers that are awarded (including ownership)
    - Introducing an online bidding platform for tendering processes in effort to improve transparency in the tender process

THANK YOU

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