SUBMISSION

Revised Fiscal Framework and Revenue Proposals Submission

4 November 2024

Attention:

Finance Standing Committee:

Chairperson: Mr MJ Maswanganyi (ANC)

Members: Alexander, Ms W (DA), Bateman, Mr AGBateman, Mr AG (DA), Beesley, Mr AD (Action SA), Gcaleka-Mazibuko, Ms NA (ANC), Hadebe, Mr N (IFP) Lekganyane, Mr MS (ANC) Makhubela, Ms LS (ANC), Maotwe, Ms OMC (EFF), Sekoati, Mr SC (ANC), Van Rooyen, Mr DD (MK)

Dear Members of the Select and Standing Committee on Finance, and Committee Secretaries,

On behalf of the Institute for Economic Justice (IEJ), thank you for the opportunity to make the following written submission and for the opportunity to participate in the public hearings on 6 November 2024 in response to the Revised Fiscal Framework and Revenue Proposals tabled by the Minister of Finance on 30 October 2024.

Given the centrality afforded to public participation in our constitutional democracy, we trust that you will give meaningful consideration to our submissions and their considered and substantiated proposals.

Should you have any questions regarding this submission, please feel free to contact Zimbali Mncube, the IEJ's Tax and Budget Policy Researcher at zimbali.mncube@iej.org.za.

1. Introduction

The Medium-Term Budget Policy Statement (MTBPS) fails to provide the new coalition government (the so-called Government of National Unity, GNU) with a viable financial basis and a credible policy direction to implement its key priorities. We are disappointed that despite the positive sentiment around the GNU, the MTBPS cements the continuation of previous administrations' anti-poor allocations, strategies, and policies.

The MTBPS, as one of the first expressions of the GNU's commitments, must be evaluated against the three areas of priority it has identified for itself for the next five years, these are: to drive inclusive growth and job creation; to reduce poverty and tackle the high cost of living; and to build a capable, ethical and developmental state. It is difficult to see how the MTBPS enables progress on these priorities. Instead, it once again lays bare the ongoing contradiction at the heart of government, between fiscal policy and rights.

2. The fiscal strategy continues to undermine inclusive growth

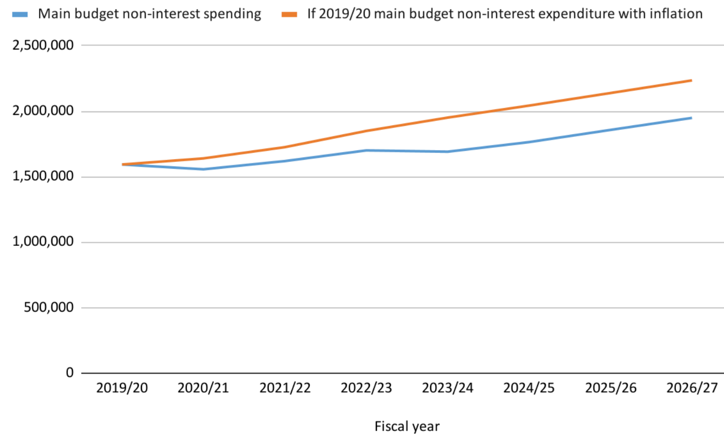
2.1. The fiscal strategy will continue to stifle economic growth. In keeping with the previous administration, the budgetary strategy still prioritises debt stabilisation through budget cuts and the quest for a primary budget surplus above all else.

2.2. While it may be some relief that, in contrast to the 2023 MTBPS, we see no new cuts to consolidated and main budget spending, this must not be misconstrued as a change in overall policy direction.

2.3. Consolidated government spending will be higher by R42.7 billion over the next three years, compared to the February Budget 2024 commitments, consolidated non-interest expenditure is expected to grow by only 4.2% over 2024/25 - 2027/28, below CPI inflation of 4.5% and population growth of 1.5%. A growth of 6% in consolidated non-interest expenditure is necessary just to ensure that a similar level of services can continue to be provided.

2.4. The MTBPS, therefore, continues the trend seen over successive budgets of reductions in spending per user for many vital expenditure categories, which we expand on below.

2.5. We can observe in Figure 1 below what the main budget non-interest expenditure would be over the medium term had it kept in line with inflation since 2019/20 (orange line) compared to where it has ended up (blue line). For example, in the current year, 2024/25, in order to account for inflation since 2019, there would need to be additions of R278.7 billion in main budget non-interest spending.



2.6. We know, without question, that austerity damages the country's growth prospects while making the rich richer. Recent evidence shows that the effects of austerity on inequality are "exerted for up to two years, and are driven by concentrating income into the top ten per cent of earners". Given that South Africa is already one of the most unequal countries in the world, a continuation on this path means the effects will last longer. As evidence shows, the impacts of austerity on the economy can last up to 15 years. Therefore, austerity can "permanently affect the expected path of GDP, and its effects on sustainability are exactly the opposite than its original goals".

2.7 Given the above-mentioned impacts of austerity, we are concerned that the National Treasury is considering a fiscal rule.

2.8. In Our recent discussion paper, *Are Binding Fiscal Rules the Right Solution for Debt Sustainability in South Africa?*', we show that fiscal rules can undermine legitimate contestation and negotiation of the budget by stakeholders; encourage opaque accounting techniques; stifle growth; and are frequently violated. Internationally, success in implementing fiscal rules depends crucially on government-wide consensus.

2.9. We anticipate the release of National Treasury's discussion document on this issue by the end of March 2025 and look forward to participating in what must be a robust, broad-based, stakeholder consultation process thereafter.

2.10. It is worth noting that in 2021, the National Treasury, in its response to proposals for a fiscal rule argued that "it is important to recognise that it is difficult to implement far-reaching fiscal rules because South Africa's economic growth is persistently weak and the public finances are

managing several large risks beyond the control of fiscal authorities". These risks still exist, and so we question the consideration for a fiscal rule in 2025.

The IEJ recommends that:

2.11. At the minimum, the National Treasury should aim to increase consolidated and main budget non-interest expenditure in a manner that keeps in line with inflation and population growth.

2.12. The National Treasury reconsiders the role of fiscal policy in the economy to a broader objective with new targets, such as unemployment, poverty, inequality, and structural transformation of the economy.

2.13. The National Treasury adopts a development-focused budget that prioritises public investment in physical infrastructure, shifting our economy towards greener energy, greater financial support for the care of children and the elderly, expanding employment in social services like health and education, greater and more targeted spending towards industrialisation and exports and expanding domestic demand, including through stimulus impacts of income transfers on local economies, all of which have been shown to have a positive impact on employment outcomes and GDP growth.

2.14. The Committee commits to undertaking its own independent research on the international experience with fiscal rules, and the implications on economic growth and inequality.

3. Job creation and public employment

3.1 The failure to allocate sufficient spending to public employment in the MTBPS demonstrates the new government's unwillingness to reduce our record-high unemployment and improve the welfare of the public.

3.2. Expenditure for 'job creation and labour affairs' continues to receive a minuscule (0.97%) share of the budget over the next three years.

3.3. Our government seems to view spending on public employment as an unwarranted drain on the fiscus rather than an investment in our collective future and is thus hell-bent on reducing it. This thinking is misguided.

3.4 First and most trivially, a portion of public servants' salaries is recovered through the tax system.

3.5 Second, more public servants (such as teachers and nurses) ensure better service delivery, which is vital, especially for township and rural areas that depend critically on public services. These jobs are foundational to our economy and society.

3.6. Public employment programmes are a net positive for the economy and society by helping with the beneficiary's well-being, higher consumption, and reducing the number of people who may resort to extra-legal means of getting income. Yet, there is no mention of how the Presidential Employment Stimulus will be expanded and improved going forward nor any credible job creation strategy put forward.

The IEJ recommends that:

3.7. The Committee seeks clarity on the future of the Presidential Employment Stimulus and plans for it to be part of the Expanded Public Works Programme.

3.8. A progressive scaling up of all public employment programmes with deliberate steps taken to ensure that they give recipients opportunities for longer-term work.

3.9. With the public sector wage negotiations currently ongoing, the Treasury's provisional allocation may need to be revised so that departments do not, once again, have to manage costs by continuing the freeze on hiring posts.

4. Resourcing Public Services

4.1. The financing of public employment is intimately tied to the issue of providing basic quality public services. The MTBPS acknowledges that the ratio of the number of public servants per public employee has increased from 44 to 48 between 2017/18 to 2023/24. This is the result of a failure to adequately resource public services since the commencement of austerity in 2012.

4.2. The 2024 MTBPS, while moderately increasing real non-interest expenditure by 0.15% (in 2019/20 rands) on average over the next three years, still falls short of the levels required to address this challenge.

4.3. We note that, in 2019/20 rands, spending per uninsured healthcare user will decrease from R4 116.78 in 2024/25 to R3 898.42 by 2027/28. On the other hand, spending per learner (in 2019/20 rands) moderately increases from R18 813.82 in 2024/25 to R19 372.11 by 2027/28.

4.4. While increased allocation to basic education is welcome, its long-term impact may be offset since expenditure on other public services such as healthcare is cut. Ultimately, this MTBPS reflects the National Treasury's overall approach of pitting key priorities against one another.

4.5. Failure to adequately resource public services will disproportionately fall on women. Disinvesting in public services means privatising the economy's costs, with women's time for

employment and leisure dedicated to care needs that the government is failing to adequately resource.

4.6. The gender-blindness of this MTBPS is no clearer than in the omission of updates on how the government will implement Gender-Responsive Budgeting (GRB). This is disappointing given the commitment in the 2024 Budget to include a gender budget statement in the MTBPS.

The IEJ recommends that:

4.7. The Committee seeks clarity from National Treasury on the progress of the pilots of Gender-Responsive Budgeting as well as government-wide implementation.

4.8. Human rights impact assessments are conducted, taking into account the impact of the budget on different groups of people in society. These impact assessments must be shared publicly.

4.9. A plan needs to be formulated, with the necessary budget, to fill critical frontline vacancies.

5. Reducing Poverty and Tackling the High Cost of Living

5.1. Between 2024/25 and 2025/26, social grants receive savage and unconstitutional nominal cuts. This is a direct result of National Treasury's failure to provide for the Social Relief of Distress (SRD, R370) grant beyond 2024/25,

5.2. This is despite repeated assurances by the President, Ministers, the Department of Social Development, and other officials that the grant is here to stay, and will form the basis of a system of comprehensive basic income support for adults. Approximately 8 million people per month directly rely on the SRD grant to avoid severe hunger.

5.3. While the government claims that reducing poverty and the high cost of living is a priority, this is rendered hollow by its ongoing refusal to provide income support for working-age adults on a sustainable basis.

5.4. National Treasury pits the SRD grant against other grants in an attempt to divide constituencies in need. While social grant spending on average grows by 1.8% over the medium term (though we do not know exactly how this increase will be allocated), the SRD is completely ignored. However the government has a constitutional obligation to *progressively realise* the right to social assistance. This has been the subject of litigation brought by the IEJ and #PayTheGrants, which was heard in the Pretoria High Court just last week.

5.5 Proposals to digitise the provision of social grants are highly problematic, and will inevitably be exclusionary. The SRD Grant illustrates how an exclusive online digital application system

with verification measures implemented provides a barrier to many who are eligible for the grant. This exclusionary feature of the SRD Grant needs to be corrected, not extended to other grants.

The IEJ recommends that:

5.6. The SRD grant, and the child support grant, must be increased to the Food Poverty Line in 2025/6. and budgeted for ongoing provision into the MTEF while working with stakeholders for pathways towards a basic income grant, and pursuing additional sources of finance and tax revenue for a basic income grant

5.7 Proposals for the digitisation of the grant system need to be suspended, and investigated by parliament, looking at both the international and local evidence.

6. Infrastructure and economic development

6.1. We welcome the funding for infrastructure development, which sees an increase of 7.3% in real terms over the medium term. However, we are very concerned that infrastructure development appears to be framed through the lens of mobilising private-sector finance.

6.2. The shift from state-led infrastructure development to Public-Private Partnerships (PPPs) and incentivising private financial investment in social services has failed, worldwide, to mobilise capital needed for investment. Instead, as research shows, by introducing profit incentives in the provision of basic rights it drives up user fees and hinders access to services, particularly for the most vulnerable.

6.3. Evidence from the UK illustrates, that privatising the provision of water services is no solution, resulting in large dividend payments to private investors with simultaneous under-investment in critical infrastructure. PPPs have similarly driven up the price, and driven down the quality, of water in Nepal and increased road user costs in Peru while needing to be rescued by public money. Overall, this approach to infrastructure development will render public services a luxury for the majority and undermine the capacity of the state.

6.4. The GNU's alleged push to build a developmental state is contradicted by continued underfunding for 'Industrialisation and exports' and 'Agriculture and Rural Development'. These sectors have historically been central for countries that have shifted from backward/underdeveloped to rapidly developing countries. Yet, we instead observe an average real (2019/20 rands) decline of -2.93% and -3.9% over 2024/25 - 2027/28, for 'Industrialisation and exports' and 'Agriculture and Rural Development', respectively.

The IEJ recommends that:

6.5. PPPs should not be adopted as the model for infrastructure development given their long-term impact on the fiscus, the environment, and the impact of widening inequality.

6.6. Publicly-owned development finance institutions (DFIs) should be leveraged to invest more in critical economic infrastructure that could relieve pressure on the fiscus.

6.7. South African DFIs are recapitalised with public funds and granted access to a stable, low-cost, long-term funding line, either directly as a budgetary allocation to the relevant Ministry, through tax sources, or SARB.

6.8. The central bank issues subsidised credit to targeted sectors or other institutions like state-owned enterprises. This could allow for increased public investment without fiscal implications.

7. Measures to raise revenue

7.1. The MTBPS fails to propose measures to raise the revenue needed to support government programmes. We note that tax collection has been revised down by R22 billion below 2024 Budget expectations. This stems from a failure to consider an effective range of revenue proposals as recommended by IEJ and by this Committee in 2023.

7.2. We would like to emphasise that in 2023, this committee stated that "while the MTBPS does not deal with revenue proposals, the Committee recommends NT seriously consider, beyond their initial response, various revenue proposals proposed by stakeholders during the Committee's public hearings."

7.3. As the Minister of Finance stated in his speech, the G20 provides a unique opportunity for South Africa to build on Brasil's Presidency while putting forward an Africa-focused agenda. Such an agenda, however, needs to be bold following the leadership of the Africa Group, which has spearheaded the resolution of the United Nations Convention on International Tax and Cooperation (UNFCITC).

7.2. The National Treasury's position that South Africa can both implement OECD's GloBe rules and fully participate in the UNFCITC is out of touch with the progressive position of the African Group. There can be no complementarity between democratic and intergovernmental processes at the UN and the OECD's two-pillar solution. Similarly, the GNU's weak position on taxing South Africa's rich more, and silence on the African debt crisis, are out of step with the Global South leadership that Brazil has so provided this year at the G20.

The IEJ recommends that:

7.4. In the short-term, revenue-raising measures are taken to fund the shortfalls in spending.

7.5. The measures should include,

- Removing R65 billion in retirement fund benefits given to those earning above R750 000;
- Removing R12 billion in medical aid tax benefits given to those earning above R500 000;
- Discontinuing the ineffective Employment Tax Incentive and recovering R7 billion;
- Raising R64 billion from a sliding-scale Social Security Tax to resource basic income;
- Raising R38 billion in resource rents; and
- R9 billion to be raised from a luxury VAT rate.

7.6. The CIT be reversed to 28%. Much of the revenue this year has been driven by Corporate Income Tax collections. We question how much more revenue has been lost from cutting CIT from 28% to 27%.

7.7. More measures should be taken to tax wealth. About R70 - R160 billion can be raised in a potential wealth tax and over R40 billion from taxing financial transactions.

7.8. South Africa should use its upcoming Presidency of the G20 to advance a more robust and progressive UN tax convention agenda.

8. Way forward

Fiscal policy and the budget should be seen as tools to maximise economic growth and alleviate unemployment, poverty, and inequality. This should be based on an approach that centres on human rights, taking into account how economic policy decisions affect different groups and pursuing progressive measures to raise revenue to realise socio-economic rights.

Fiscal policy should also aim to stimulate domestic demand, targeting key sectors of the economy to support job creation and structural transformation. In the long term, such a shift will spur growth, alleviate debt levels, and improve tax revenue.

9. Recommendations

1. Use fiscal policy to address unemployment, poverty, and inequality as part of a pro-employment macroeconomic framework as opposed to narrow debt stabilisation.
2. Reverse austerity. Budget allocations must be in line with population growth and CPI growth and based on identified needs.
3. Produce evidence that shows the human rights impacts of its policy of austerity as well as its impact on the economy.
4. The Committee seeks clarity from National Treasury on the progress of the pilots of Gender-Responsive Budgeting as well as government-wide implementation.
5. The Committee seeks clarity on the future of the Presidential Employment Stimulus and plans for it to be part of the Expanded Public Works Programme.

6. A progressive scaling up of all public employment programmes with deliberate steps taken to ensure that they give recipients opportunities for longer-term work.
7. Fully absorb the public sector wage bill into additional spending (not just partially) to not suck up funds that should be spent elsewhere.
8. Increase the SRD and CSG to the FPL and insert the budget for its ongoing provision into the MTEF, while working with stakeholders on pathways towards a UBIG and pursuing additional sources of finance and tax revenue for UBIG.
9. Publicly-owned development finance institutions (DFIs) should be leveraged to invest more in critical economic infrastructure that could relieve pressure on the fiscus.
10. Promote a more equitable tax structure by implementing a wealth tax and ending tax breaks for higher-income earners.
11. South Africa should use its upcoming Presidency of the G20 to advance a more robust and progressive UN tax convention agenda.

The Institute for Economic Justice (IEJ) is a progressive economic policy think tank committed to advancing economic justice, systemic change, and the equitable distribution of resources to ensure rights realisation and planetary wellbeing.

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