BUSA
BUSINESS UNITY SOUTH AFRICA

National Office
Unit FFN09, Block 9 Bentley Office Park
67 Wessels Street, Rivonia, Johannesburg
P.O. Box 652807, Benmore, 2010
Tel : +27 11 784 8000| Fax : +27 (0)86 609 8248
Email : busa@busa.org.za | Website : www.busa.org.za
Registration Number : 2014/042417/08

Parliamentary Office
9 Church Square, 1st Floor Graaffs Trust Building
Cape Town CBD
P.O.Box 3867, Cape Town, 8000

BUSINESS' RESPONSE TO THE 2017 MEDIUM TERM BUDGET POLICY STATEMENT (MTBPS)

Delivered by Martin Kingston (Vice President: Business Unity South Africa)

27 October 2017

1. Introduction

- We appreciate and acknowledge the honest and candid disclosure by the Minister in Wednesday's Budget Policy Statement on the poor 'state of health' of the South African economy. Business has repeatedly expressed its concerns about the worsening circumstances facing the South African economy.

- The situation we are in cannot be remedied through fine tuning and small interventions, but requires significant structural changes as a matter of urgency. The Minister has recognised the critical role that the private sector plays and this needs to be fully harnessed if, as a country, we are to reverse the current trajectory. Government needs to work comprehensively and on an integrated basis with the private sector if we are to find our way out of the current crisis. The role of business, as the economic partner to Government, is more important now than ever before if we are going to put the economy on a sustainable growth path that meaningfully addresses our challenges and plays to the country's potential.

- We are encouraged by progress that has been made on the 14 Confidence boosters. We also believe that the Minister has correctly identified necessary actions to boost confidence, including promoting transformation and competitive outcomes, managing fiscal and economic risks associated with SOEs and creating policy certainty. We however caution that this requires a fully aligned approach on behalf of government.

- The indication that in line with the 14 Confidence boosters, that there will be a substantial allocation to support SME start-ups is welcomed. Properly implemented and managed, with the input of business, this will promote economic development, transformation and employment.

- The Minister is correct that there is no 'single bullet' and that a multitude of strategies are required. These will rest not only with Treasury, but with the whole of Government, working together in an integrated, coherent manner. We are deeply concerned that the ongoing political environment has paralysed the administration and prevented the implementation of key initiatives that can remove constraints and ensure that strategic objectives are effectively met. Interventions that must now be expedited include:

  - Finalisation of a least-cost, sustainable and evidenced based Integrated Resource Plan (IRP) and Energy Plan (IEP).

  - Sustainable resolution of the impasse in the mining sector pertaining to the Mining Charter and other regulations which has fundamentally undermined the contribution of the industry with respect to both growth and employment.

  - Development of a clear, sustainable and comprehensive policy on land reform and agriculture that will meet our transformational, economic and food security needs as a country.

  - Finalisation of a forward looking, demand-led education and skills development policy that will lay the foundation for youth employment and economic progress.

  - Serious engagement by Government, including National Treasury, on comprehensive social security and national health insurance plans which are fit for purpose and are practical, viable and sustainable.

2. General Comments

- The 2017 Medium-Term Budget Policy Statement (MTBPS) takes place in a challenging environment for South Africa of marginal economic growth, declining revenue collection, and growing levels of debt accompanied by high unemployment, widening inequality and significant levels of poverty in our country. This is in contrast to the improving global economic environment and the return to growth in BRICS countries such as Russia and Brazil.

- South Africa relies heavily on external capital, including foreign savings required to finance investment and the level of government debt held by non-residents (16.7% of GDP), both of which are significantly influenced by volatile confidence levels.

- We accept that the levels of economic growth revised down from 1.3 % to 0.7% during the course of this year, coupled with low levels of confidence, are unlikely to address the challenges of unemployment, poverty and inequality in the short to medium term.

3. **Fiscal Consolidation**

- Business is concerned with the rising budget deficit (to 4.3% of GDP for 2017 / 2018 and the increasing levels of debt service. Debt servicing is again the fastest rising category of spending. It is equally of concern that gross national debt will increase to 61% of GDP by 2022, with the consequence that debt service costs rise to 15% of main budget revenue within the medium term. This fundamentally erodes the country's ability to channel critical resources to the poorest in our society. The guarantees and other contingent liabilities are a further significant signal that our ability to maintain fiscal discipline is under threat.

- The Minister has correctly recognised that there is no more opportunity to raise taxes to generate further revenue as this will stifle growth and long-term fiscal sustainability. However, we are concerned about the contradictory statements made by the Minister that tax increases may be forthcoming in the 2018 budget, without any details being provided in this regard. Clarity is required.

- The announcement that nuclear power will be procured at a pace and scale that the country can afford is cautiously welcomed. Business has consistently indicated its opposition to any commitment at this stage to nuclear power. We are disappointed that there has been inadequate focus on the IRP and the IEP as the basis of any decision on the extent to which nuclear energy will form part of the country's energy mix.

- Business notes the commitments that have been made by the Minister to dealing with the grave challenges confronting SOEs, including appropriately addressing balance sheet constraints at SAA and SAPO. We welcome the commitment to improving governance, management and operational capability at all SOEs. Nevertheless, we believe the Minister should have gone further in acknowledging that SOEs should only be retained in the public sector to the extent that they are fit for purpose and make a demonstrable contribution to the development goals of the country. In that context, we have consistently indicated our reservations about the current circumstances facing Eskom, given its critical role in the economy. We believe that urgent attention should be given to its structure and role in the context of a universally endorsed IEP and IRP particularly as, in the current circumstances, it acts a proxy for the economic health of South Africa and, as the Minister indicated, poses a significant risk to the national economy.

4. **Tax**

   - While business welcomes the commitment to expenditure cuts as a key component of fiscal consolidation, we are concerned about the intention to increase taxes in the 2018 Budget. Any revenue increases should be approached with extreme caution to avoid further undermining economic growth.

   - The R50.8 billion tax revenue shortfall for 2017 / 2018 is of particular concern, as is the projected shortfall of R209 billion over the next three years. Business believes that the fiscal consolidation process must be driven, first and foremost, by reductions in spending through generating greater efficiencies, rather than relying on revenue increases that we believe will be self-defeating and undermine economic activity.

   - Business notes that announcements around taxes will take place in the National Budget in February 2018. In this regard, business supports an efficient, fair and progressive tax system that minimizes disruption to sustainable economic growth. While we reiterate our caution that fiscal consolidation should rely primarily on generating efficiencies in the expenditure, any future tax increases over the medium term will need to maintain an optimal balance between direct taxes such as Corporate Income Tax (CIT) and Personal Income Tax (PIT) and indirect taxes such as VAT.

- When assessed against peers, South Africa has relatively high CIT and Personal Income Tax (PIT) (particularly for a middle-income country) and low levels of VAT. In a context where it is imperative to raise revenues and reduce expenditure, finding the right balance in revenue collection is essential. We note the Davis Tax Commission's findings that an increase in VAT appears to be the economically least disruptive means to raise taxes in the current environment. In view of this, and should tax increases be unavoidable, consideration should be given to raising VAT with appropriate exemptions to ensure that the living standards of the poor are not adversely affected.

- We note that the Minister resisted the temptation to raise the possibility of scrapping tax credits and subsidies for private healthcare. This would place at risk the medical security of 2 million people without a viable alternative from the State, and the benefit of an implemented NHI policy and legislative framework.

- We are disappointed to note that Carbon Tax Bill will be going to Parliament when we have not yet had the opportunity to finalise our ongoing engagement with National Treasury on the matter.

5. **Conclusion**

- Overall, the 2017 MTBPS (while generally balanced) may not have been adequate to restore the requisite levels of confidence to mobilise the support that is required by all stakeholders to avert further downward pressure on the economy. Furthermore, investors and ratings agencies are only likely to respond positively to if they can be persuaded that government has displayed adequate intent to implement SOE reform, reduce expenditure and implement necessary regulatory reforms to grow the economy.

- Together with political and economic uncertainty, enough risks remain in the form of declining revenue collection and taxpayer morality, economic growth, and expenditure growth to cast doubt on many of the targets. We have previously highlighted the fact that ongoing downward revision of targets over the past several years has contributed to falling levels of confidence and credibility.

- Business has explicitly endorsed the need for the country to embark on a sustainable and comprehensive approach to transformation and inclusive growth. The current climate may well not be conducive to achieving this objective timeously and requires the full co-operation of all social partners represented here at Nedlac.
- A key imperative is to implement a systemic and comprehensive approach of decisive action against those involved in corruption both in the public and the private sector.
- Bringing capable and skilled boards and management into SOEs that are appropriately located within the South African economy is critical if we are to restore confidence in these entities.
- We acknowledge that the Minister does not, and cannot speak for other government departments, but we would like to believe that the Minister of Finance can play an instrumental role in addressing the significant challenges that the Minister has identified are facing the economy and in taking the lead on behalf of government in addressing those challenges.
- As the Minister noted in his speech: "*We desperately need businesses that invest thereby creating growth and employment*". Whilst very aware of the challenges we face, business stands ready to work with government and our social partners to move the economy forward.