PRESS STATEMENT

MTBPS 2021: The Institute for Economic Justice fears the MTBPS will further retard economic recovery

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Going into the Medium Term Budget Policy Statement (MTBPS), the IEJ is gravely concerned about the country's fiscal trajectory and National Treasury's seeming unwillingness to engage on critical issues.

The problems confronting South Africa are high unemployment, inequality, and poverty, lack of access to basic services, and low economic growth. Although South Africa has recorded four consecutive quarters of growth, the economy is still 1.4% smaller than pre-COVID and the same size as the fourth quarter of 2017 - thus continued rescue for recovery is still needed. A rethinking of policy approaches should focus on investing in the people. This should be done through increasing expenditure towards basic public services, expanded and extended social assistance, and investments in key sectors of the economy for job creation.

In the IEJ's 17 September 2021 pre-MTBPS submission, we noted how the National Treasury continues its decades-old approach of attempting to place the macroeconomic framework as 'off-limits'. Our stance remains that meaningful consultation on South Africa's budget can only occur if the fiscal framework itself is debated.

Slashing public expenditure places the economy at risk

The National Treasury's underlying logic of 'fiscal consolidation' (used in this context as a euphemism for austerity) is economically flawed and will have ramifications for the South African economy. Most importantly, their impact will be felt by the most vulnerable groups in South Africa. The assumption that cutting government spending has relatively little adverse effect on aggregate demand has been discredited. In fact, the effect of government spending cuts on output has proved to be larger than anticipated during recessionary times. As the UNCTAD noted, "the idea of expansionary austerity was […] a failure, leaving a fragile fiscal situation on the eve of the COVID-19 shock". Deep expenditure cuts during periods where the economy is struggling result in fiscal policy being 'procyclical', thereby worsening the downturn. While this may be moderately offset by monetary policy, through reduced interest rates, South Africa has failed to intervene more proactively, such as via bond purchases by the central bank on an appropriate scale.

The austerity measures implemented by National Treasury are underpinned by the desire to achieve a budget surplus by 2024/25. This is not the time to pursue a budget surplus. The pandemic remains upon us, with a looming fourth wave expected in December.

There is more fiscal space than originally thought

Increased tax revenue and international financing has provided additional fiscal space. In February 2021, the former Minister of Finance announced that SARS revenue collections are expected to be R99.6 billion more than the forecasts from the 2020 Medium Term Budget Policy Statement (MTBPS). With the commodities boom commentators are now projecting a tax overrun of around R150 billion. In addition, the IMF recently injected emergency funding, effective August 2021, of R65 billion through its Special Drawing Rights (SDR).

Recent estimates of the debt-to-GDP ratio show it sitting at 68.8%, far below the 80.3% expected. If higher projections were tolerable to the National Treasury in the February 2021 National Budget, why should we institute more austere targets now? Internationally governments have raised their debt levels to finance rescue and recovery plans in the face of the COVID-induced economic crisis.

This fiscal space should be used to expand the country's response to COVID-19 and support rescue and recovery measures.

Social assistance must be prioritised

In the context of disturbingly high rates of poverty and inequality, expanded social assistance continues to be needed. In the 2021 Budget social grants declined by 2.4%. The Child Support Grant, which decreased least, saw a nominal rise of 3.4% - from R445 to R460 - below the 2021/22 expected inflation of 4.2%, resulting in a real decrease of 0.8%. In September, inflation reached a high of 4.9% which will have ramifications for household consumption. Real increases in grants, and their expansion to address the gap in social protection for 18-59 year olds, are imperative in this current socioeconomic environment.

The IEJ and partners continue to call on the government to phase in the introduction of a Universal Basic Income Grant (UBIG). The IEJ rejects National Treasury's unilateral proposal of a 'family grant' which will remove grants from millions currently receiving the SRD grant, and is likely to entail the collapsing of existing grants into a singular grant over time. The proposal does not take seriously intra-household power relations which are gendered, nor does it fully appreciate the highly fluid and porous nature of households in South Africa, amongst other factors as highlighted by civil society organisations (including the IEJ).

A UBIG is able to not only fulfil the constitutional obligations of the state, but reach recipients more effectively and account for exclusion errors more efficiently, without the burdensome, costly, and exclusionary measures required by targeting. It is buttressed by popular support and affordable at meaningful levels, with positive redistributive effects if progressively financed. Its wide coverage offers significant poverty-alleviation effects, while providing an inclusive and empowering basis to rebuild and reshape our disintegrating social contract.

There is no trade-off between job creation and social security extension. There is no credible local or international evidence that expanded social security - including through a UBIG - creates 'dependence' or discourages work seeking. This is a lie told to us by those who wish to limit social assistance.

A fiscal stimulus into jobs is needed

The highly contractionary macroeconomic stance will retard job creation through stifling economic recovery and meaningful expansion.

The pandemic has destroyed a decade's worth of employment growth, yet the state has reduced funding for industrial policy interventions that are crucial to expanding labour intensive sectors in the economy. Industrialisation and export support was allocated around R36 billion in 2021, less than 5% of the budget. The Parliamentary Budget Office has shown that even the Economic

Recovery and Reconstruction Plan proposed by the National Treasury has seen declining budget support. This undermines the President's emphasis on industrial policy tools - such as local procurement and infrastructure build - to promote employment and economic diversification.

The highly successful Presidential Employment Stimulus (PES) Programme requires greater support. In the first phase the PES offered over 550 000 job opportunities, including 300 000 school-based assistants. As the IEJ previously noted, the National Treasury dragged its feet in funding the second phase, with the budget now reduced from R12.6 billion in Phase 1 to R11 billion in phase two despite rising unemployment. The youth employment component was slashed in the context of extreme youth unemployment.

The program's implementation and skills development may also be undermined by the unfilled teaching vacancies and retrenchments of teachers due to budget cuts. For example, in Kwa-Zulu Natal (KZN) 4 000 teachers are slated for retrenchment due to budget cuts, on top of 2 000 already existing teacher vacancies. It is counterintuitive to try and increase the number of teaching assistants in the short term whilst retrenching teachers who are a key component of the program and play an important role in transferring skills. In addition, budget cuts like these will undermine human capital investment and have long term effects on the realisation of socio-economic rights.

What is needed is a comprehensive job creation and protection initiative that holistically responds to the job crisis in the country and secures the provisioning of essential basic services.

Dealing with debt

Budgets since, at least, 2014/15 have prioritised debt reduction above all else. This has led to declines in real expenditure to departments (such as education and grants) as well as provincial allocations. Considering expected inflation, as of February 2021 Treasury notes "consolidated non-interest spending will contract at an annual real average rate of 5.2 per cent". This is likely to reduce GDP and place upward pressure on the debt-to-GDP ratio. South Africa's increased debt due to the pandemic is not an anomaly, debt is expected to increase globally as countries mobilise resources to respond to the COVID-19 crisis.

Reducing the share of the budget spent on debt servicing costs is a valid objective. There are three ways in which governments attempt to do this: 1. a pursuit of a budget surplus via expenditure cuts (austerity); 2. increasing growth through fiscal expansion (stimulus); 3. and/or monetary policy and regulatory interventions to directly lower the cost of borrowing. The first of these - pursuing a budget surplus through expenditure cuts - has been proven as disastrous. In Greece and Ireland for example, Oxfam found that budget cuts reversed a decade of growth. This led to a contraction of 25% of the GDP in Greece, whilst debt soared to 175% of the GDP and unemployment increased to 25%. As unemployment has increased, inequality has also worsened due to austerity measures. This is also true for Latin America and Sub-Saharan Africa where austerity was implemented through structural adjustment programs. Between 1980 and 2003 the average national gini coefficient increased from 0.50 to 0.53 in Latin America.

Given the well-documented evidence on the impact of budget cuts, South Africa must adopt a combination of the second and third approach. It must pursue a path of carefully targeted expenditure increases to spur sustainable and human-centred economic growth, while actively intervening to lower borrowing costs. The IEJ recently hosted a discussion of these pathways and will release proposals in this regard.

In addition, the government must actively pursue the creation of 'fiscal space'. By modifying sources and levels of funding, governments are able to generate new internal or external resources on a sustainable basis. As UNCTAD notes:

> [F]iscal space cannot be identified as a predetermined level of resources in any economy. Rather, it is dependent on past and current fiscal policy choices, such as the extent of the government's spending, its savings and the level of its debt relative to GDP.

The current approach is likely to limit fiscal space over time. What may appear to be short-term savings, will have long-term negative ramifications for the economy and for socioeconomic rights.

We call on National Treasury to:

- **Implement a comprehensive stimulus package** to stimulate demand, and expand capacity in the economy and create jobs. This stimulus should target hard hit sectors of the economy to support economic recovery. The care sector, construction, and manufacturing can be targeted to ease the burden of unpaid care work, promote labour intensive investment, and support infrastructure for public goods.
- **Recommit to the progressive realisation of human rights.** The duty of the state to promote, protect and fulfil socio-economic rights. Budget cuts must not erode the provisioning of basic services and all legislation and policy should be measured against the extent to which it advances rights, justice and equity. The state should conduct human rights impact assessments, that are gendered, where budget cuts are proposed.
- **Pursue additional sources of tax revenue**. These include the introduction of a Social Security Tax (SST) – ranging between 1.5 to 3% of taxable personal income - which has the potential to raise R67.29 billion in 2022/23, a Resource Rent Tax (RRT) which could raise R38.80 billion assuming a tax rate of 25% on the value of total resource rent, the removal of ineffective tax incentives, amongst others as highlighted above. Greater effort needs to also be made to clamp down on illicit financial flows (IFFs) and tax evasion.
- **Implement a wealth tax.** This will promote a more equitable tax structure in the medium term and create fiscal space. Calculations by the IEJ have shown that "a 1% wealth tax for the top 1% of earners could raise R63 billion" whilst "a 3% wealth tax on the richest 0.1% raises R103 billion".
- **A Universal Basic Income Guarantee (UBIG) is one social expenditure priority that must be implemented**. The UBIG will close the gap that the labour market has not filled in the context of rising vulnerability to poverty, particularly for the 18-59 population group.
- **Increase and improve processes for meaningful participation and transparency**. The National Treasury needs to strive to achieve fiscal sustainability through sustained engagement and collaboration with social partners. There is a difference between information sharing, which Treasury is relatively good at, and meaningful consultation, which is often paid lip service too.
- **Accept that South Africa will have, for the medium term, significantly higher levels of debt, to enable a serious growth strategy, which will ultimately consolidate debt levels.** This would entail setting the debt target at appropriate levels which enable a robust fiscal stimulus, and announcing this. This will stop the regular increases of projected debt levels which undermine credibility of Treasury projections.
- **Commit to counter-cyclical borrowing to finance spending plans.** Measures to contain borrowing costs must also be put in place, including necessary interventions in the bond market by the Reserve Bank.

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