

**Did the MTBPS allay our concerns on SA's fiscal position?****Authors: Refilwe Rakale, Research Analyst @ Futuregrowth****Date: 15 November 2021**

Against the backdrop of robust revenue collections and increasing expenditure pressure, the challenge for Finance Minister Godongwana in his maiden Medium-term Budget Policy Statement (MTBPS) was clear: to what extent his team would be able to succeed in the balancing act required to achieve fiscal consolidation. National Treasury reiterated its commitment to the welcomed path of fiscal consolidation; however, in the absence of detail where expenditure is concerned, long-term fiscal sustainability remains a concern.

**Positive tailwinds support improvements in our fiscal metrics**

Historically, the MTBPS has served as a sobering agent, following often lofty expectations and promises made at the February budget. This year's statement veered significantly from this pattern. The vast improvement in fiscal metrics was supported by the strong commodities cycle, which bolstered corporate income tax collections and the GDP rebasing that occurred in September 2021. While the elevated commodity prices have contributed to an actual improvement in forecasts, the upward adjustment to the GDP base allowed for merely cosmetic changes to key macroeconomic metrics (such as the budget deficit and debt-to-GDP ratios) in light of the nominal higher GDP.

**Tax revenue rebounds sharply but market expectations remain above National Treasury's forecast**

The weeks leading up to MTBPS were laden with speculation on the magnitude of the widely-expected revenue overrun after the corporate tax windfall. In line with our expectations, National Treasury revealed a revenue overshoot (relative to the budget tabled in February 2021) of R120 billion for the 2021/22 fiscal year. Over the medium term, revenue outperformance relative to February estimates is expected to slow down to R69.8 billion and R59.5 billion in 2022/23 and 2023/24, respectively. This falls more on the conservative side relative to some market expectations. We welcome Treasury's decision to err on the side of caution. In the absence of tax hikes, a continuation of robust collections hinges on commodity prices remaining somewhat elevated – a risk in our view. Overall, there is upside potential for revenue over the medium term, given Treasury's conservative GDP growth and tax buoyancy assumptions.

Additionally, while this is hard to quantify, anecdotal evidence suggests that there are continued improvements at the South African Revenue Services (SARS), specifically in the specialised audit and investigative functions that were allocated an additional R3 billion in February. This should bode well for revenue beyond the medium-term period. However, it is worth noting that, compared to February 2020 budget (pre-pandemic), revenue from 2020/21 to 2022/23 remains below the forecast by R285 billion. This should serve as a stark reminder that South Africa's fiscal position remains vulnerable.

**Increased expenditure and a lack of detail perpetuate our concerns**

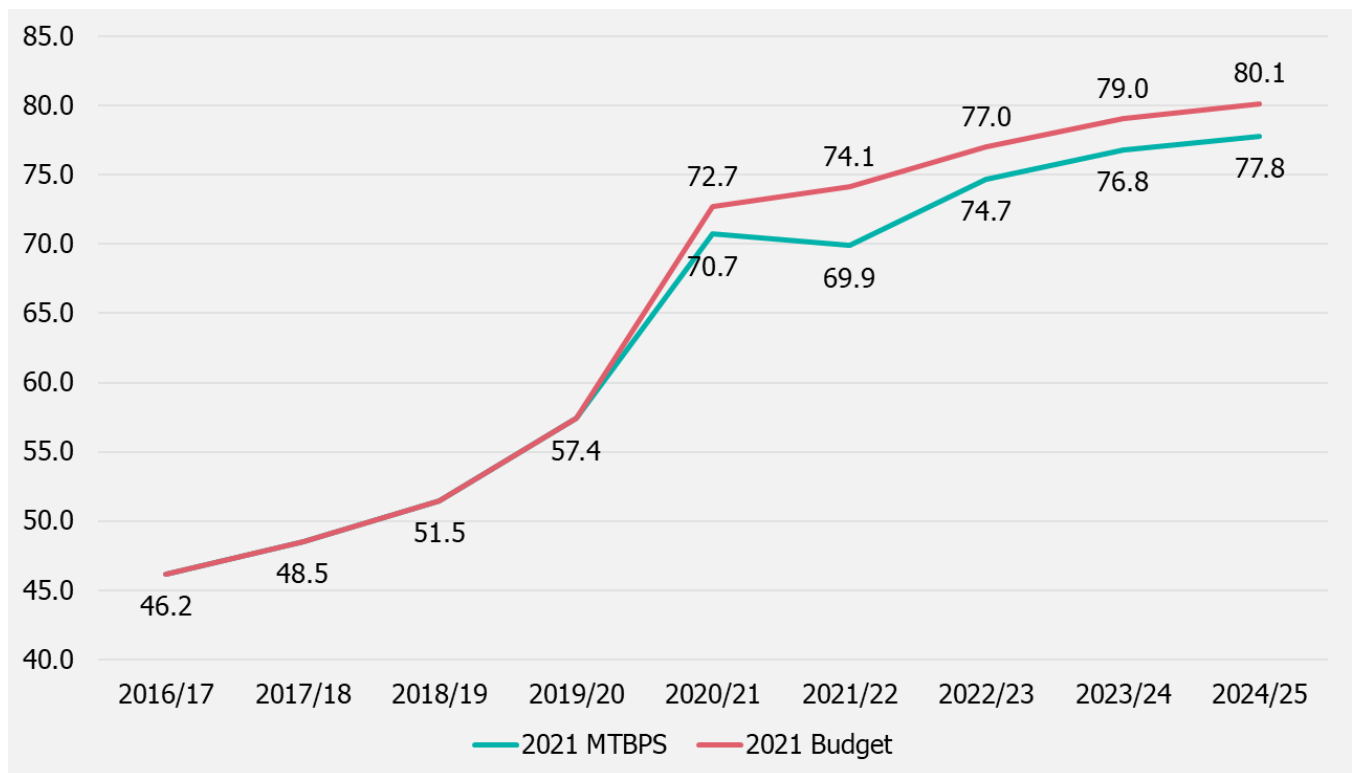
This year's fiscal performance has been marred by increased expenditure pressures that were not featured in February's budget, namely: increased allocation to the Department of Higher Education, the Public Sector Wage Bill and the support package in response to the unrest in July. In February, National Treasury unrealistically factored in an expenditure cut of 1.5% for the current fiscal year. It is unsurprising, therefore, that consolidated expenditure has now been revised higher by a cumulative R164 billion over the medium term. Increases to the public sector wage bill totalling R41 billion (accounting for a cash gratuity of R1 000 per month) have been factored into this increased expenditure.

The MTBPS was relatively light on details about how future bailouts of State-Owned Enterprises and government guarantees will be handled, suggesting that the risk of the crystallisation of contingent liabilities remains one to be monitored closely.

## An improvement in debt metrics leads to a reduction in the borrowing requirement

Better-than-expected revenue collection and GDP rebasing have resulted in the consolidated budget deficit being revised lower to 7.8% of GDP (from 9.3% of GDP for 2020/21) and this is expected to narrow to 4.9% of GDP by 2024/25. Positively, government used some of the tax revenue windfall to decrease the debt burden for 2021/22, which decreased marginally to 69.9% from 70.7% in 2020/21. However, we still do not see a stabilisation of the debt burden over the MTEF, which is expected to reach 77.8% by 2024/25 (see Graph 1). Moreover, the gross debt-to-GDP ratio is now expected to peak at 78.1% in the 2025/26 financial year (down from the 88.9%). Surprisingly, there was no mention of the bloated cash position (as at 30 September 2021, the closing cash balance was R290 billion, which is R103 billion more than the budgeted closing cash balance of R187 billion). A combination of high cash balances, and the potential issuance of a rand-denominated Islamic Sukuk bond and a Floating Rate Note support our expectation of a likely reduction in the weekly nominal and ILB auction issuance.

**Graph 1:** Debt profile does not stabilise under improved fiscal position



Source: National Treasury, Futuregrowth

## A credible commitment to hold the fiscal line – for now

On balance, we view Thursday's MTBPS as credible. We acknowledge National Treasury's continued commitment to holding the fiscal line. This commitment is further evidenced in the expected primary balance moving into a surplus in 2024/25. Assuming a supportive global environment, government could have an opportunity to finally turn the fiscal ship around. However, it would be remiss to ignore the significant expenditure pressures (and thus execution risk) in the outer years of the medium term. We therefore cannot say that the MTBPS completely dispelled our concerns.

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