

## 2019 Budget Overview

(20 February 2019)

“It is time for us to sow the seed of renewal and growth” – Tito Titus Mboweni

### **In summary: Disappointing budget, but Eskom support done in a positive manner.**

- **Negatives:** higher deficit and debt ratio's; upward revision in expenditure ceiling; increased tax burden for individuals.
- **Positives:** Strong statement on SOE's and no Eskom debt take-on; reduction in public sector wage bill; continued emphasis on private sector's important role and Strategic Equity Partnerships.

### **Highlights:**

Upward revision to budget deficit targets and debt ratio.

Budget has mostly been drawn up around Eskom's needs:

- Very strong and positive statement regarding support for Eskom and other SOE's.
- No Eskom debt transfer, but Eskom cash injection of R23bn per year for 3 years, partially financed through public sector wage cutbacks.
- Chief Restructuring Officer to be appointed at Eskom.

Unexpectedly strong statement on envisaged savings in public sector wage bill.

R15bn increase in tax burden for individuals.

No corporate tax changes.

This is still very much an expansionary budget – with total expenditure growth of +7.9% over the next three years (thus real spending growth of +2.3% on avg pa)

### **Impact on ratings:**

Despite the upwards revised expenditure ceiling and budget and debt ratio's, Moody's (as well as S&P and Fitch) should view the Eskom measures as positive. I do expect all three to be fairly hawkish in their post budget statements, but do not expect any ratings or outlook changes from any of the agencies in the immediate short term. They will likely adopt a wait-and-see attitude until after the elections. The risk of short term ratings action remains very much alive though.

### **Impact on markets:**

The immediate focus will likely be on the higher deficit and debt ratios and the increased tax burden on individuals. Therefore, both the bond and equity markets could react negatively upon the release of the budget. However, the Eskom and public sector wage bill announcements as well as the tone of the budget speech (especially when read in conjunction with the Oct 2018 MTBPS and President Ramaphosa's State of the Nation Address two weeks ago) is generally positive. This should help stabilise confidence and help create an enabling environment for further policy measures post elections. I therefore expect both the bond and equity market to eventually view the budget as neutral.

**Impact on the economy:**

Likely negative for consumers, but overall this budget should help in the process of building confidence, plus this is by no means a contractionary budget – with real spending growth of +2.3% on avg pa over the next three years. Thus, this should turn out to be mildly positive for the economy over the medium term. From an inflationary perspective, there will likely be very little impact as the increases in fuel and excise taxes are generally lower than last year. I maintain also that this still a very deflationary environment.

**Impact on consumers:**

Heavy burden for consumers as the tax burden rises by R15bn: from no relief for fiscal drag (i.e. no inflation adjustment of brackets), to fuel levy and excise duty increases. The environment is already tough for consumers, and this increases that burden.

**Impact on corporates:**

No direct impact through any budget-related policy changes, but the strong statements on Eskom, the public sector wage bill and the need to involve the private sector and create an environment where confidence should improve and enabling the private sector to invest is clearly positive.

**Growth and the private sector:**

- Private sector is the key engine for job growth.
- Govt's policies aimed at ending uncertainty that has undermined confidence and constrained private sector investment
- Visa requirements being relaxed

**Budget built on six fundamental prescripts:**

- Achieving a higher rate of economic growth
- Increasing tax collection
- Reasonable affordable expenditure
- Stabilising and reducing debt
- Reconfiguring state-owned enterprises
- Managing the public sector wage bill

**Minister Mboweni on SOE's & Eskom:**

- "The SOEs pose very serious risks to the fiscal framework."
- "Isn't it about time the country asks the question: do we still need these enterprises?"
- "Pouring money into Eskom in its current form is like pouring money into a sieve."
- "I want to make it clear: the national government is not taking on Eskom's debt."
- R23bn per year cash for Eskom over 3 years - effectively R150bn over ten years when amortized.
- Essentially debt and debt service support and not for operating costs.

- But wants a total transformation of electricity sector in exchange. (Treasury comments in budget briefing: “...do not want to waste a good crisis.”)
- Chief Reorganisation Officer (CRO) being appointed to implement recommendations of Presidential Task Team.
- Other SOE support as deficit neutral as possible
- “We must tighten the guarantee rules. If a state-owned enterprise applies for a government guarantee for operational purposes, it will be required to appoint a CRO in concurrence with the National Treasury and its bondholders.”
- Considering end of guarantees for operational purposes. Expiration dates will be strictly enforced.
- Strategic equity partners will be found where possible.
- Further SAA, SA Express, Post Office and SABC support in the pipeline (not yet announced – mix of sale of non-core state assets and usage of contingency reserve). This will be done as deficit neutral as possible. Some asset sales (not specified) already assumed within revenue budgets.

#### Public sector wage bill:

- Reduction of R27bn over the next three years
- Allow early retirement without penalties (targets 30 000 of the 126 710 workers in the 55 – 59 age group) – cost to be funded by contingency reserve and GEPF
- Limits on overtime, bonus payments (performance bonus of R2bn pa to be passed out over 4 years) and pay progression
- System of staffing diplomatic missions unjustified and will be reviewed
- Members of Parliament and provincial legislatures and executives at public entities will receive no salary increase this year.

#### Deficit and debt ratio:

- Deficit ratio revised higher:
  - 2018/19 from -4.0% in Oct to -4.2%
  - 2019/20 from -4.2% in Oct to -4.5%
  - 2020/21 from -4.2% in Oct to -4.3%

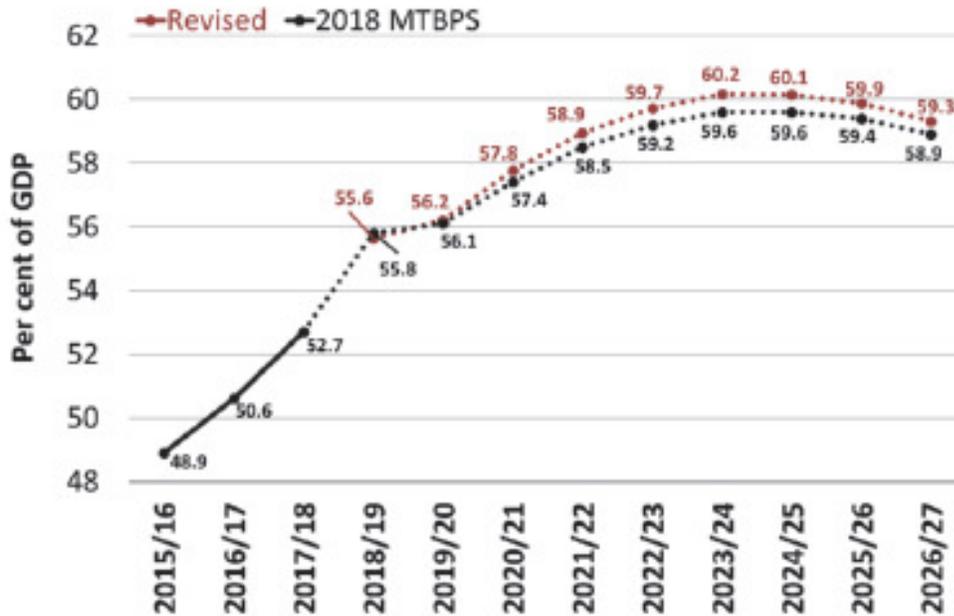
**Table 1.2 Consolidated government fiscal framework**

R billion/percentage of GDP	2018/19	2019/20	2020/21	2021/22
	Revised estimate	Medium-term estimates		
Revenue	1 455.2 28.8%	1 583.8 29.3%	1 696.4 29.2%	1 836.6 29.4%
Expenditure	1 665.4 32.9%	1 826.6 33.7%	1 948.9 33.5%	2 089.0 33.4%
Budget balance	-210.2 -4.2%	-242.7 -4.5%	-252.6 -4.3%	-252.4 -4.0%

Source: National Treasury

- Debt ratio also revised higher (as in the past few budgets ) – only slightly this time:

**Figure 1.3 Gross debt-to-GDP outlook**



**Economic assumptions - Treasury's growth assumptions revised lower:**

(Oct 2018 forecasts in brackets)

	<b>GDP growth</b>	<b>HCE growth</b>	<b>CPI inflation</b>
2018	0.7% (0.7%)	1.5% (1.6%)	4.7% (4.9%)
2019	1.5% (1.7%)	1.5% (1.9%)	5.2% (5.6%)
2020	1.7% (2.1%)	2.1% (2.3%)	5.4% (5.4%)

OMIG current forecast:

2018	0.8%	1.8%	4.6%
2019	1.8%	2.2%	4.6%

**Revenue:**

- Current fiscal year:
  - Downward revision in revenue since Oct MTEF: R15.4bn (VAT refunds higher than expected)
  - SARS estimates of VAT credit book (if refunds are paid out without delay) estimated at R19bn in Oct 2018. That has now been revised higher to R22bn.
- Tax changes - 2019/2020 – additional revenue of R15bn
  - No relief for fiscal drag, but slight upward adjustment to tax-free threshold: +R12.8bn
  - No adjustment for medical tax credits: +R1bn
  - Additional VAT zero rating (white bread flour, cake flour and sanitary pads): -R1.1bn
  - Sugar tax (health promotion levy): increase from 2.1c/gram per 100ml (beyond the first 4 grams which are tax free) to 2.21c/gram.
  - Increased excise duties:
    - between 7.4% and 9% increase in duties for alcoholic beverages and tobacco
  - Fuel tax increase: Total of 29c/l and 25c/l for petrol and diesel respectively.
    - Fuel levy: +15c/l and + 10c/l for petrol and diesel respectively from 3 April
    - From 5 June carbon tax levy of 9c/l and 10c/l for petrol and diesel respectively
    - RAF levy increase of 5c/l from 3 April
  - Carbon tax: Implemented on 1 June 2019.
  - Gambling tax: proposal of 2012 budget (1% levy) dusted off – draft legislation to be introduced this year.

**No adjustments to brackets, only small adjustments to rebates and thresholds:**
**Table 4.4 Personal income tax rates and bracket adjustments**

2018/19		2019/20	
Taxable income (R)	Rates of tax	Taxable income (R)	Rates of tax
R0 - R195 850	18% of each R1	R0 - R195 850	18% of each R1
R195 851 - R305 850	R35 253 + 26% of the amount above R195 850	R195 851 - R305 850	R35 253 + 26% of the amount above R195 850
R305 851 - R423 300	R63 853 + 31% of the amount above R305 850	R305 851 - R423 300	R63 853 + 31% of the amount above R305 850
R423 301 - R555 600	R100 263 + 36% of the amount above R423 300	R423 301 - R555 600	R100 263 + 36% of the amount above R423 300
R555 601 - R708 310	R147 891 + 39% of the amount above R555 600	R555 601 - R708 310	R147 891 + 39% of the amount above R555 600
R708 311 - R1 500 000	R207 448 + 41% of the amount above R708 310	R708 311 - R1 500 000	R207 448 + 41% of the amount above R708 310
R1 500 001 and above	R532 041 + 45% of the amount above R1 500 000	R1 500 001 and above	R532 041 + 45% of the amount above R1 500 000
<b>Rebates</b>		<b>Rebates</b>	
Primary	R14 067	Primary	R14 220
Secondary	R7 713	Secondary	R7 794
Tertiary	R2 574	Tertiary	R2 601
<b>Tax threshold</b>		<b>Tax threshold</b>	
Below age 65	R78 150	Below age 65	R79 000
Age 65 and over	R121 000	Age 65 and over	R122 300
Age 75 and over	R135 300	Age 75 and over	R136 750

*Source: National Treasury*

Thus very limited relief:

**Table 4.5 Estimates of individual taxpayers and taxable income, 2019/20**

Taxable bracket	Registered individuals		Taxable income		Income tax payable before relief		Income tax relief after proposals		Income tax from medical tax credits		Income tax payable after proposals		
	R thousand	Number	%	R billion	%	R billion	%	R billion	%	R billion	%	R billion	%
R0 - R70 <sup>1</sup>	6 369 806		–	183.4	–	–	–	–	–	–	–	–	–
R70 - R150	2 385 046	31.2		254.0	10.0	10.3	1.9	-0.34	28.5	0.05	5.0	10.1	1.8
R150 - R250	1 949 150	25.5		387.4	15.2	36.4	6.6	-0.32	26.9	0.20	23.1	36.2	6.5
R250 - R350	1 169 590	15.3		349.9	13.7	49.6	9.0	-0.19	15.8	0.21	22.1	49.7	9.0
R350 - R500	984 790	12.9		408.5	16.0	75.9	13.7	-0.16	13.2	0.23	21.9	76.0	13.7
R500 - R750	610 331	8.0		367.1	14.4	89.1	16.1	-0.10	8.2	0.15	14.3	89.2	16.1
R750 - R1 000	261 631	3.4		224.7	8.8	66.1	12.0	-0.04	3.5	0.07	6.1	66.2	12.0
R1 000 - R1 500	161 868	2.1		193.9	7.6	65.8	11.9	-0.03	2.2	0.05	4.4	65.8	11.9
R1 500 +	120 751	1.6		362.7	14.2	159.8	28.9	-0.02	1.6	0.04	3.2	159.8	28.9
<b>Total</b>	<b>7 643 157</b>	<b>100.0</b>		<b>2 548.1</b>	<b>100.0</b>	<b>553.0</b>	<b>100.0</b>	<b>-1.18</b>	<b>100.0</b>	<b>1.00</b>	<b>100.0</b>	<b>552.9</b>	<b>100.0</b>
<b>Grand total</b>	<b>14 012 963</b>			<b>2 731.5</b>		<b>553.0</b>		<b>-1.18</b>		<b>1.00</b>		<b>552.9</b>	

1. Registered individuals with taxable income below the income-tax threshold

Source: National Treasury

**Table 1.3 Impact of tax proposals on 2019/20 revenue<sup>1</sup>**

R million	
Gross tax revenue (before tax proposals)	1 407 208
Budget 2019/20 proposals	15 000
Direct taxes	13 800
Taxes on individuals and companies	
Personal income tax	13 800
Revenue from not fully adjusting for inflation	12 800
Revenue if no adjustment is made	14 000
Partial bracket creep for personal income tax	-1 200
No adjustment to medical tax credit	1 000
Indirect taxes	1 200
General fuel levy adjustment	-500
Introduction of carbon tax on fuel	1 800
Additional VAT zero-rated items	-1 100
Increase in excise duties on tobacco products	400
Increase in excise duties on alcoholic beverages	600
<b>Gross tax revenue (after tax proposals)</b>	<b>1 422 208</b>

**Expenditure:** +R16bn increase in expenditure ceiling over next three years

- Downward adjustment to baseline expenditure over the next 3 years: R50.3bn
  - Half from downwards adjustment to govt wage bill
  - R12,8bn lower by reducing spending on specific programs.
- BUT, financial support for Eskom: Total of R69bn
  - R23bn per year for next three years

**Table 3.4 Adjustments to the expenditure ceiling since 2018 Budget**

R million	MTEF spending changes			MTEF total
	2019/20	2020/21	2021/22	
<b>2018 Budget non-interest expenditure</b>	<b>1 434 907</b>	<b>1 543 593</b>	<b>1 651 638</b>	<b>4 630 138</b>
Skills development levy adjustment	459	618	706	1 783
<b>2018 MTBPS non-interest expenditure</b>	<b>1 435 366</b>	<b>1 544 211</b>	<b>1 652 345</b>	<b>4 631 922</b>
<b>Budget 2019</b>				
Baseline adjustments <sup>1</sup>	-9 002	-19 711	-21 568	-50 281
Changes to contingency reserve	6 000	-2 000	-6 000	-2 000
Additions to spending <sup>2</sup>	24 000	23 000	28 300	75 300
National Revenue Fund payments adjustment	135	-	-	135
<b>2019 Budget non-interest expenditure</b>	<b>1 456 500</b>	<b>1 545 500</b>	<b>1 653 077</b>	<b>4 655 076</b>
<i>Change in non-interest expenditure from 2018 Budget</i>	<i>21 592</i>	<i>1 907</i>	<i>1 438</i>	<i>24 938</i>
Less:				
Skills development levy	-18 759	-20 437	-22 307	-61 503
Other adjustments <sup>3</sup>	-7 146	-11	-12	-7 168
<b>2019 Budget expenditure ceiling</b>	<b>1 430 595</b>	<b>1 525 052</b>	<b>1 630 758</b>	<b>4 586 405</b>
<i>Change in expenditure ceiling from 2018 Budget</i>	<i>13 998</i>	<i>1 289</i>	<i>732</i>	<i>16 019</i>

1. Baseline reductions and changes to provisional allocations

2. Allocation for Census 2021 and provisional allocations for Eskom and infrastructure fund

3. Provision for SOC funding in 2019/20 through the sale of assets, NRF payments and International Oil Pollution Compensation Fund

Source: National Treasury

**Thus, expenditure ceiling increases by R14bn in 2019/20, R1.3bn in 2020/21 and R0.7bn in 2021/22:**

**Table 3.5 Main budget expenditure ceiling<sup>1</sup>**

R million	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
2017 Budget Review	1 074 970	1 144 225	1 229 823	1 323 553	1 435 408		
2017 MTBPS		1 141 978	1 233 722	1 316 553	1 420 408	1 524 222	
2018 Budget Review			1 232 678	1 315 002	1 416 597	1 523 762	
2018 MTBPS			1 225 455	1 314 865	1 416 597	1 523 762	1 630 026
<b>2019 Budget Review</b>				<b>1 310 156</b>	<b>1 430 595</b>	<b>1 525 052</b>	<b>1 630 758</b>

1. Non-interest spending financed from the National Revenue Fund, excluding skills development levy, special appropriations in 2015/16 for Eskom and the New Development Bank, debt management and Gold and Foreign Exchange Contingency Reserve Account transactions and the International Oil Pollution Compensation Fund

Source: National Treasury

## Some expenditure detail:

	15/16	16/17	17/18	18/19	19/20	20/21	21/22
<b>GDP</b>	4873.2	4413.8	4721.8	5853.1	5413.8	5812.4	6243.1
<b>Revenue</b>	<b>1215.3</b>	<b>1285.9</b>	<b>1353.5</b>	<b>1455.2</b>	<b>1583.8</b>	<b>1696.4</b>	<b>1836.6</b>
X change	25.8	25.1	28.7	28.8	23.3	23.2	23.4
X of GDP	25.8	25.1	28.7	28.8	23.3	23.2	23.4
<b>Expenditure</b>	<b>1355.3</b>	<b>1443</b>	<b>1543.8</b>	<b>1665.4</b>	<b>1826.6</b>	<b>1948.9</b>	<b>2089</b>
X change	3.7	6.5	7.8	7.5	3.7	6.7	7.2
X of GDP	27.9	32.7	32.7	28.3	33.7	33.5	33.4
Non int/wage/capital	588.2	628.8	679.3	737.3	816.9	867.3	923.9
X change	-8.5	5.3	8.8	8.5	10.1	6.2	5.5
<b>Interest costs</b>	<b>138.5</b>	<b>154.4</b>	<b>169.8</b>	<b>188.7</b>	<b>209.4</b>	<b>232.7</b>	<b>255.9</b>
X change	14.3	11.5	10.8	11.1	11.8	11.1	10.8
X of total expenditure	18.2	10.7	11.8	11.3	11.5	11.3	12.2
Reserve	0.0	0.0	0.0	0.0	13.0	6.0	6.0
Non-interest expenditure	1216.8	1288.6	1374.0	1476.7	1617.2	1716.2	1833.1
X change	3.2	5.3	6.6	7.5	3.5	6.1	6.8
Social grants	153.0	165.0	178.3	192.7	207.1	222.7	238.7
X change	7.8	7.8	8.1	8.1	7.5	7.5	7.2
<b>Interest &amp; wage &amp; social protection exp</b>	<b>764.7</b>	<b>831.0</b>	<b>895.5</b>	<b>966.6</b>	<b>1043.6</b>	<b>1123.0</b>	<b>1207.7</b>
X change	8.5	8.7	7.8	7.5	8.8	7.6	7.5
X of total expenditure	56.4	57.6	58.8	58.8	57.1	57.6	57.8
<b>Personnel</b>	<b>473.2</b>	<b>511.6</b>	<b>547.4</b>	<b>585.2</b>	<b>627.1</b>	<b>667.6</b>	<b>713.1</b>
X change	8.3	8.1	7.8	6.5	7.2	6.5	6.8
X of total expenditure	34.3	35.5	35.5	35.1	34.3	34.3	34.1
Non-wage expenditure	882.1	931.4	996.4	1080.2	1199.5	1281.3	1375.9
X change	10.5	5.6	7.8	8.4	11.8	6.8	7.4
<b>Non-interest / non-wage expenditure</b>	<b>743.6</b>	<b>777.0</b>	<b>826.6</b>	<b>891.5</b>	<b>930.1</b>	<b>1048.6</b>	<b>1120.0</b>
X change	3.3	4.5	6.4	7.5	11.1	5.3	6.8
Capital Expenditure	155.4	148.2	147.3	154.2	173.2	181.3	196.1
X change	11.8	-4.6	-8.6	4.7	12.3	4.7	8.2
X of total expenditure	11.5	10.3	9.5	9.3	9.5	9.3	9.4
Current expenditure (total - capital)	1199.9	1294.8	1396.5	1511.2	1653.4	1767.6	1832.9
X change	4.4	7.3	7.3	8.2	3.4	6.3	7.1
Current expenditure (Excl interest incl wages)	1061.4	1140.4	1226.7	1322.5	1444.0	1534.9	1637.0
X change	3.2	7.4	7.6	7.8	3.2	6.3	6.7
<b>Balance</b>	<b>-140.0</b>	<b>-157.1</b>	<b>-190.3</b>	<b>-210.2</b>	<b>-242.8</b>	<b>-252.5</b>	<b>-252.4</b>
X of GDP	-3.4	-3.6	-4.0	-4.2	-4.5	-4.3	-4.0
Primary	-1.5	-2.7	-20.5	-21.5	-33.4	-19.8	3.5
X of GDP	1.1	-1.1	-1.4	-1.4	-1.6	-1.3	1.1

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