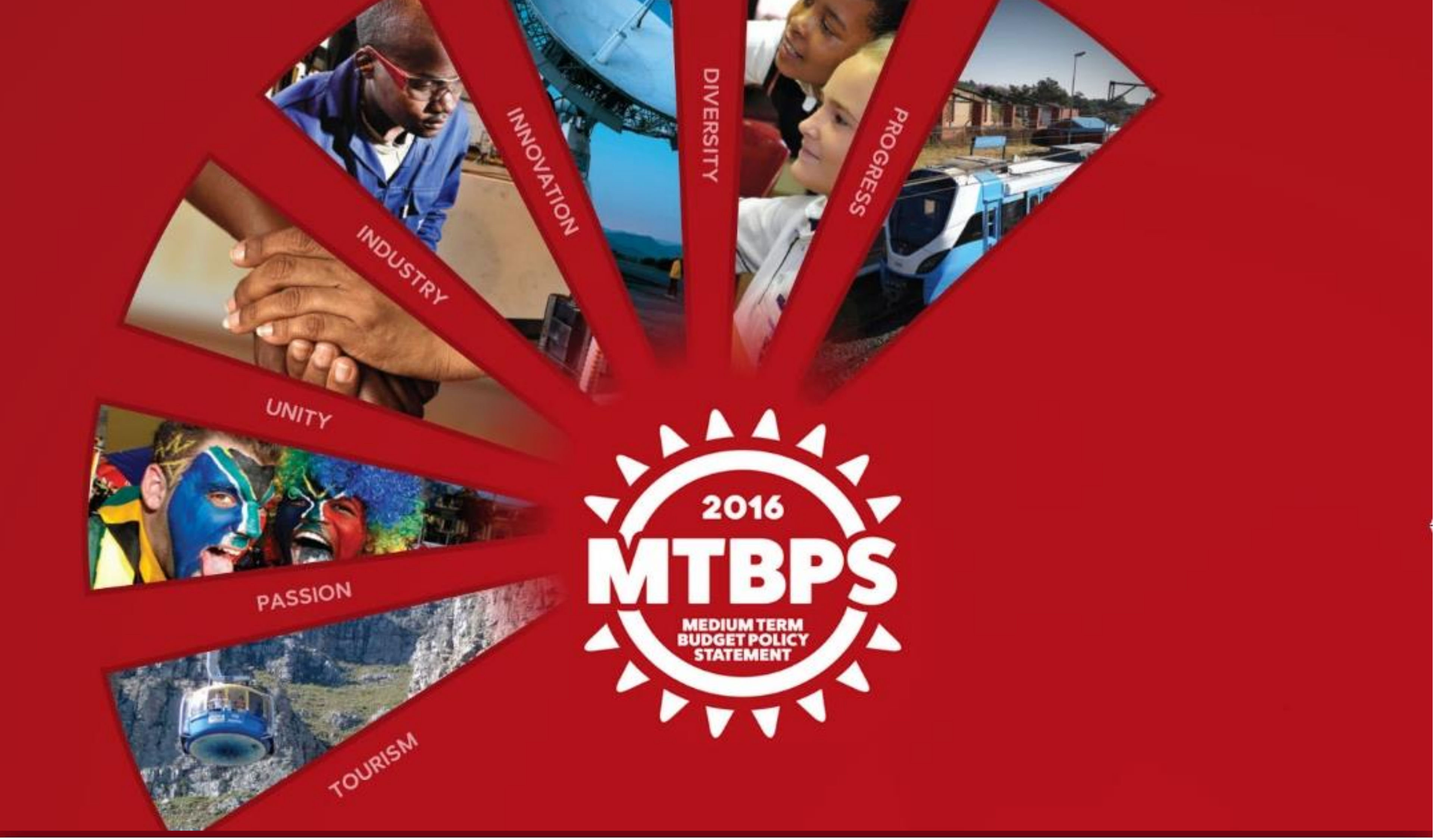


national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Main messages

- South Africa is undergoing a difficult economic transition. This partly reflects global realities. It is also the result of low levels of investor confidence and structural constraints in the domestic economy.
- To grow faster and generate the revenue necessary to fund government policy objectives, the economy needs higher levels of private investment.
- Government remains committed to working with the private sector, labour and civil society to promote inclusive growth and economic transformation.
- Over the medium term, government intends to sustain real spending per capita. However, the public finances face difficult trade-offs in the years ahead.
- The MTBPS proposes a measured fiscal consolidation, reducing the expenditure ceiling by R10 billion next year and adding R13 billion in revenue measures. Combined with the proposals announced in the 2016 Budget, this brings the total tax increase next year to R28 billion.
- Universities and students will receive an additional R17 billion over the medium term. Post-school education and training budgets are the fastest growing, with university subsidies increasing by 10.9 per cent each year on average and NSFAS allocations growing by 18.5 per cent.
- Government continues to prioritise infrastructure investment to ease bottlenecks and raise the economy's potential growth rate. Public-sector infrastructure budgets are estimated at R987.4 billion over the next three years.

Weakness and uncertainty in the global economy

- The recovery from the 2008 crisis remains precarious
- Risks to the global outlook include excessive debt, further deterioration in Chinese growth rates, continued declines in commodity prices and political uncertainty in several major economies
- The outlook for developing economies is mixed: resilience in India and China, a return to moderate growth in Russia an Brazil
- Low interest rates in US, EU and Japan have supported capital inflows to developing economies
- Countries that are highly reliant on foreign savings – including South Africa – will remain vulnerable to global volatility

Global growth projections

Region / country Percentage	Average 2010 – 2014	2015	GDP growth[1] 2016	2017
World	**4.0**	**3.2**	**3.1**	**3.4**
Advanced economies	**1.8**	**2.1**	**1.6**	**1.8**
US	2.1	2.6	1.6	2.2
Euro area	0.7	2.0	1.7	1.5
UK	1.9	2.2	1.8	1.1
Japan	1.5	0.5	0.5	0.6
Emerging markets and developing countries	**5.7**	**4.0**	**4.2**	**4.6**
Brazil	3.3	-3.8	-3.3	0.5
Russia	2.8	-3.7	-0.8	1.1
India	7.3	7.6	7.6	7.6
China	8.6	6.9	6.6	6.2
Sub-Saharan Africa	**5.3**	**3.4**	**1.4**	**2.9**
South Africa[2]	2.5	1.3	0.5	1.3

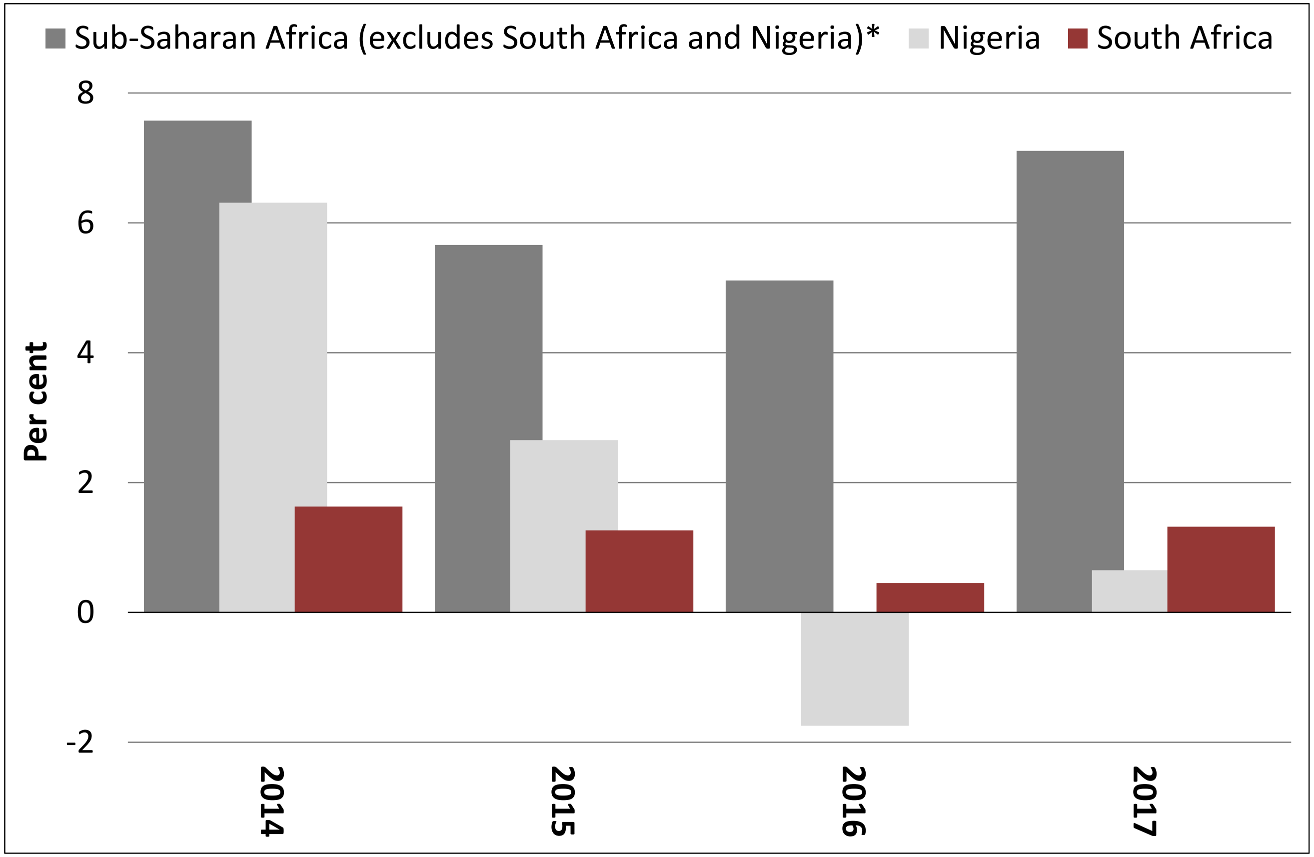
1. IMF World Economic Outlook, October 2016

2. National Treasury forecasts

Slowing growth in sub-Saharan Africa

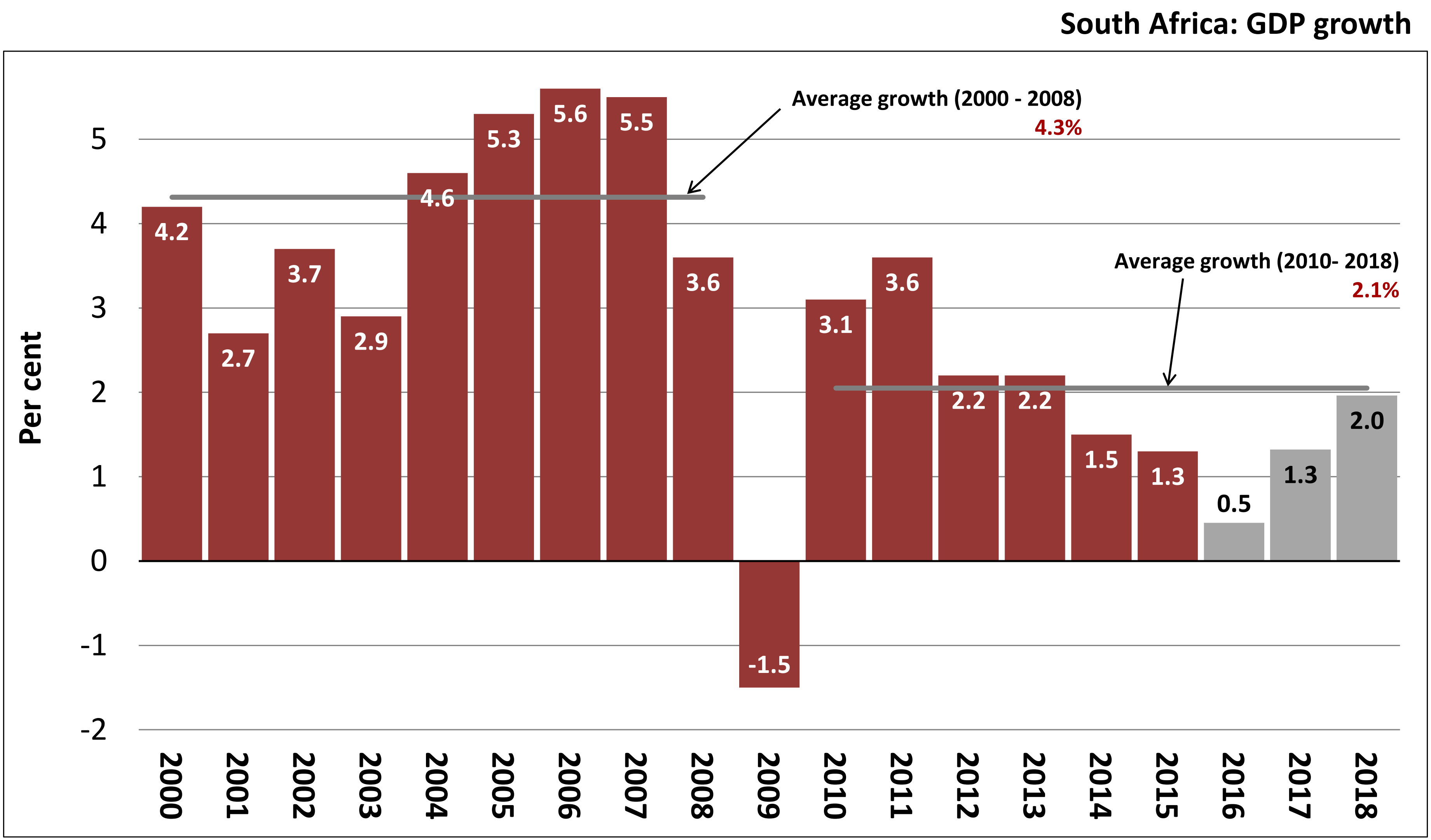
- Outlook for sub-Saharan Africa is marked by low commodity prices and falling export revenues, which have led to foreign-currency shortages
- The 2016 growth forecast for the region has been revised down from 3 per cent to 1.4 per cent, with large economies like Nigeria and Angola hit by low oil prices and disruptions in production
- In contrast, Ethiopia, Kenya and Senegal are expected to record growth rates of over 5 per cent
- Greater regional integration is required to take advantage of the pockets of strong growth

Growth in sub-Saharan Africa



national treasury
Department: National Treasury
REPUBLIC OF SOUTH AFRICA

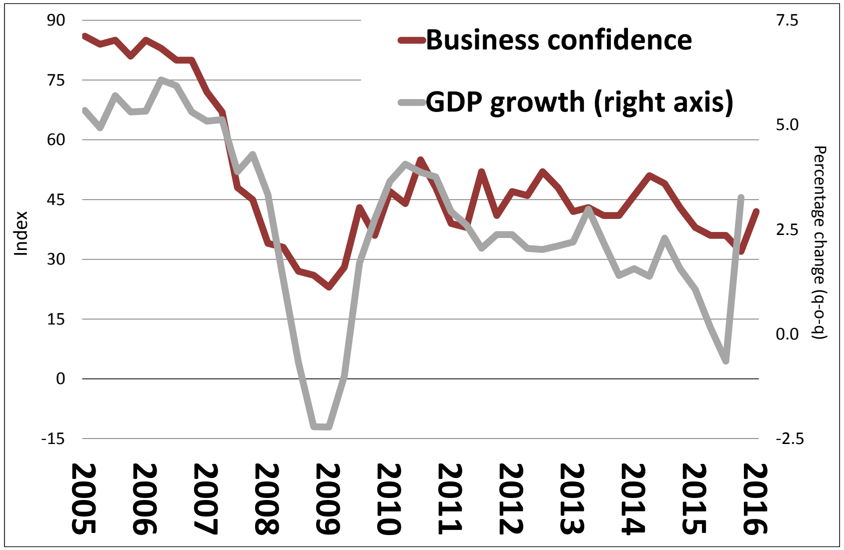
South Africa's trend growth rate has declined



Low confidence remains the largest obstacle to growth

- South Africa's economic performance reflects low levels of business confidence
- Public investment remains relatively buoyant, but private investment has fallen across all sectors and capital formation is expected to contract in 2016 for the first time since 2010
- Several emerging factors support a recovery:
  - Real exchange has depreciated
  - Moderate rebound in commodity prices
  - Consumer spending improves on lower inflation, wage growth and improving household balance sheets
  - Drought conditions ease
  - Electricity supply improves
  - Investment recovers on low borrowing costs and higher capacity utilisation
  - Public investment sustained

South Africa: Growth and business confidence



Macroeconomic projections

Calendar year	2013	2014	2015	2016	2017	2018	2019
		Actual		Est		Forecast	
Percentage change unless otherwise indicated							
Final household consumption	2.0	0.7	1.7	0.6	1.3	1.9	2.3
Final government consumption	3.8	1.8	0.2	0.7	0.1	0.0	0.3
Gross fixed capital formation	7.0	1.5	2.5	-2.9	1.1	2.6	3.1
Exports	3.6	3.3	4.1	0.5	3.0	4.7	5.2
Imports	5.0	-0.5	5.3	-2.9	2.7	4.1	4.7
Real GDP growth	2.3	1.6	1.3	0.5	1.3	2.0	2.2
GDP inflation	6.6	5.7	4.0	6.6	6.0	5.8	5.7
CPI inflation	5.8	6.1	4.6	6.4	6.1	5.9	5.8
Current account balance	-5.9	-5.3	-4.3	-3.9	-3.9	-3.8	-3.8

Source: Reserve Bank and National Treasury

Two fiscal challenges

- **Medium term | Avoiding a low growth trap**
  - Further deterioration of the economy could lead South Africa into a low-growth trap.
  - In this scenario, weak GDP growth produces less tax revenue. Fiscal consolidation that is too aggressive may bolster confidence, but further may also undermine the economy.
  - Taking no action could result in ratings downgrades, capital flight, rapid exchange rate depreciation and a spike in interest rates, resulting in even lower growth outcomes.
  - **To avoid this trap, government proposes a balanced consolidation. This needs to be supported by action to rebuild confidence for investment.**
- **Long term | Realising the aspirations of the constitution within available resources**
  - The Constitution requires government to pursue a progressive expansion of access to public services within its available resources.
  - To realise these aspirations, South Africa needs to accelerate the pace of economic growth.
  - Proposals have been tabled for a substantial expansion of spending commitments. But if implemented simultaneously, the costs would be incompatible with fiscal sustainability.
  - The limited space available to increase taxation cannot accommodate all of these aims. For now, however, long-term policy aspirations far exceed available resources.
  - **Difficult trade-offs are needed to resume the expansion of public resources available for social and economic development.**

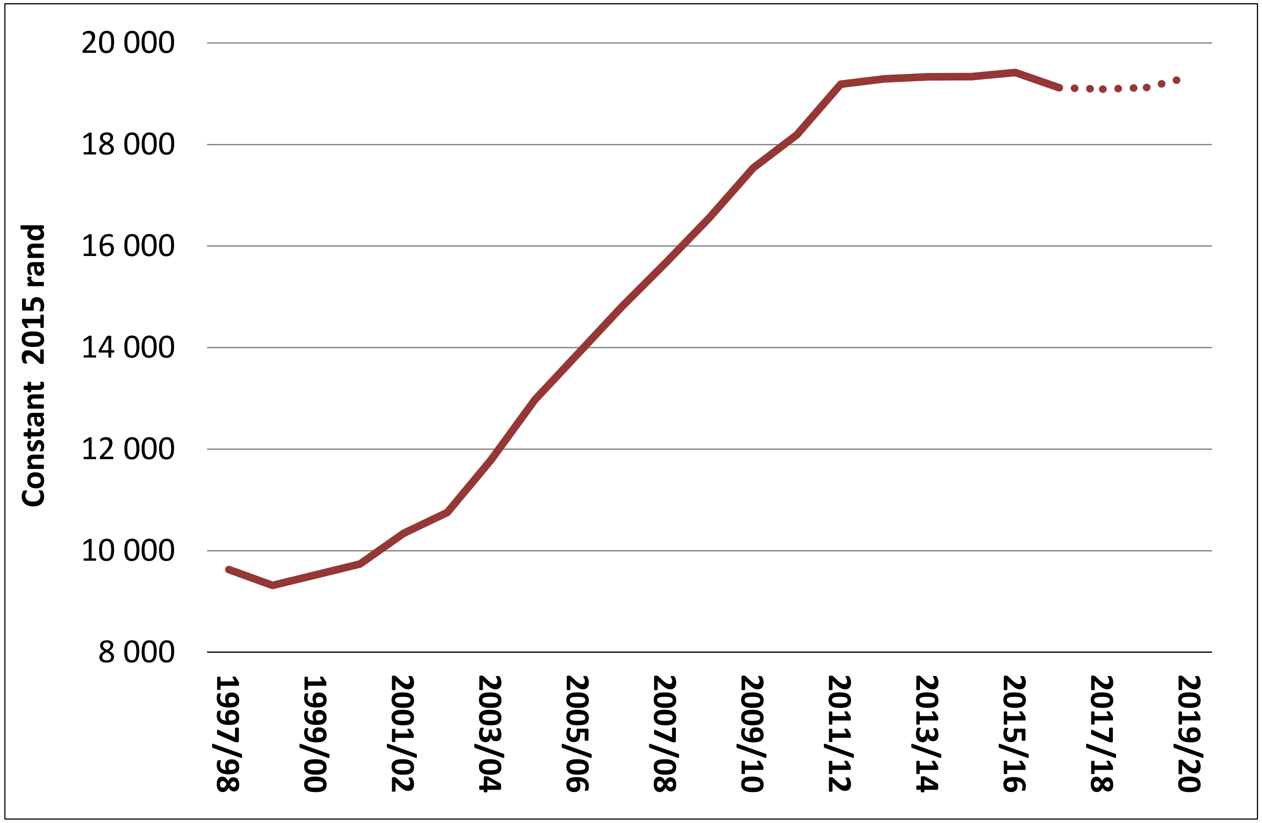
A package of actions to restore confidence

- Maximising the benefits of these developments for the economy depends on decisive actions to restore confidence. Government is creating conditions for higher confidence and investment by:
  - Finalising a regulatory framework for private-sector participation in infrastructure projects, including initiatives in partnership with state-owned companies
  - Addressing legislative and regulatory uncertainties that hold back investment in mining, agriculture and key technology sectors
  - Rationalising, closing or selling off public assets that are no longer relevant to government's development agenda, and strengthening those that are central to achieving NDP objectives
  - Concluding labour market reforms.
- Government is working in partnership with business and labour to build a foundation for faster growth.
- The Presidential Business Working Group and the CEO Initiative are generating targeted support to the economy by creating funds to support small business and offering internships to 1 million young work seekers.

Real government spending is sustained

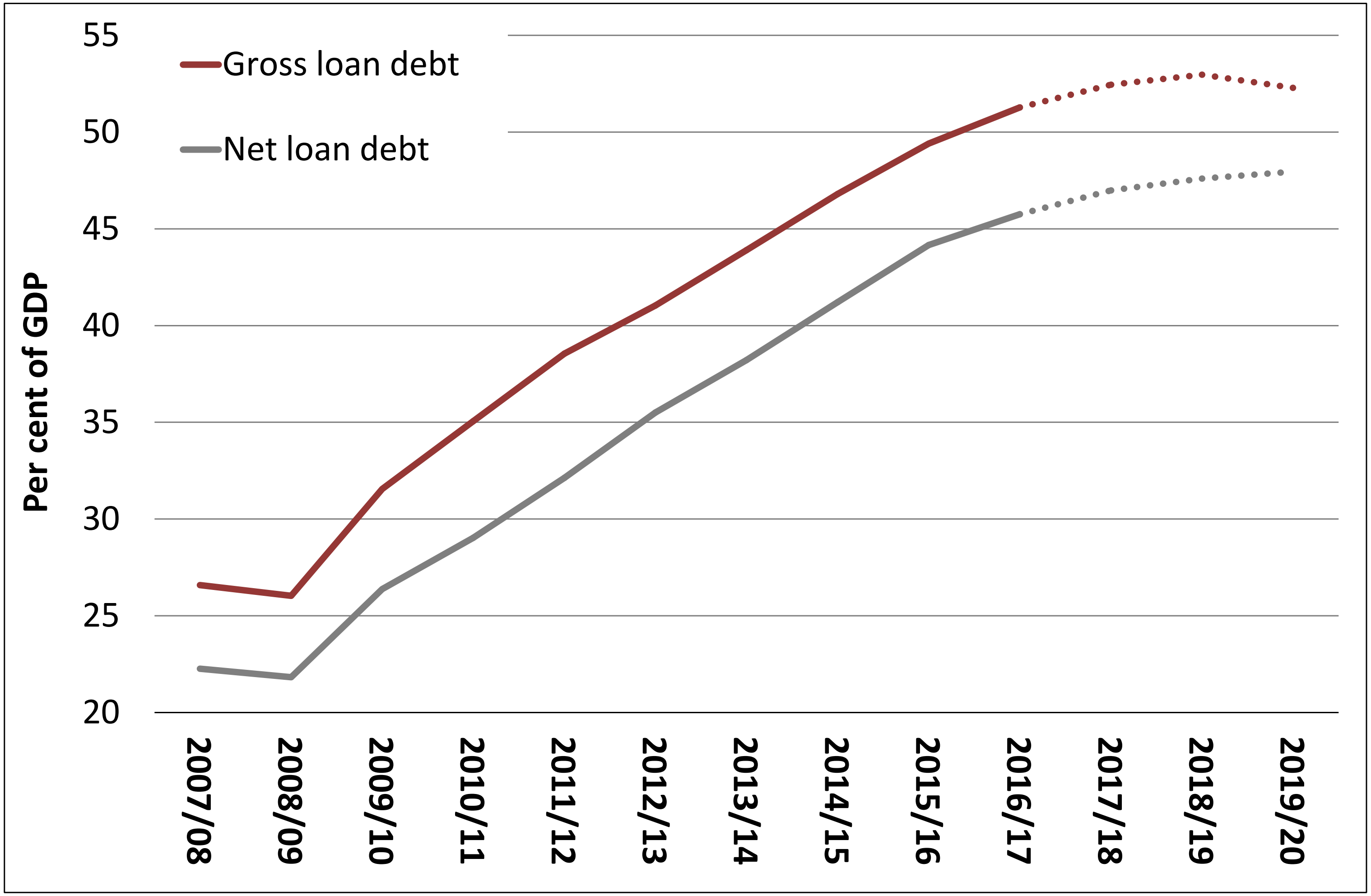
- Real government spending per capita doubled in the first two decades of democracy. The national budget now includes commitments of public resources exceeding R1 trillion per year. Yet the quality of spending needs to be improved.
- Too much public spending is regarded as wasteful, too much is ineffectively targeted and too little represents value for money.
- Since 2009, a growing portion of spending has been funded by borrowing.
- Government debt now exceeds R2 trillion, and rising debt-service costs are crowding out expenditure on priorities like infrastructure and education.
- Low economic growth has limited government's ability to finance its existing commitments and sustain higher levels of debt.

Main budget spending per capita in 2015 prices



national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Fiscal measures result in debt stabilising as a share of GDP

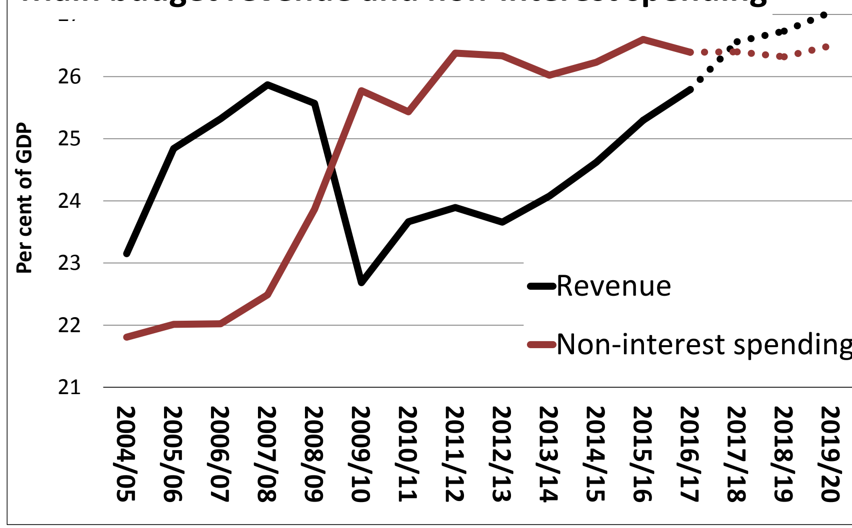


national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

A measured fiscal consolidation (1)

- To create the conditions for more rapid growth, fiscal policy aims to deliver a measured consolidation that avoids a sharp contraction in expenditure, continues to prioritise capital investment and stabilises national debt as a share of GDP.
- Government proposes:
  - Reductions to the expenditure ceiling of R10 billion in 2017/18 and R16 billion in 2018/19.
  - Tax measures to raise an additional R13 billion in 2017/18.
  - Combined with the proposals announced in the 2016 Budget, this brings the total tax increase next year to R28 billion.
  - Government will also propose measures to raise additional revenue of R15 billion in 2018/19.
- Consolidated budget deficit expected to narrow from 3.4 per cent to 2.5 per cent of GDP in outer year

Main budget revenue and non-interest spending



Announced consolidation measures

R billion	2015/16	2016/17	2017/18	2018/19
2015 Budget Review				
Expenditure reductions	10	15	–	–
Revenue increases	17	–	–	–
2016 Budget Review				
Expenditure reductions	–	–	10	15
Revenue increases	–	18	15	15
2016 MTBPS				
Expenditure reductions	–	–	10	16
Revenue increases	–	–	13	–
Total				
Expenditure reductions	10	15	20	31
Revenue increases	17	18	28	15
Total	**27**	**33**	**48**	**46**

Source: National Treasury

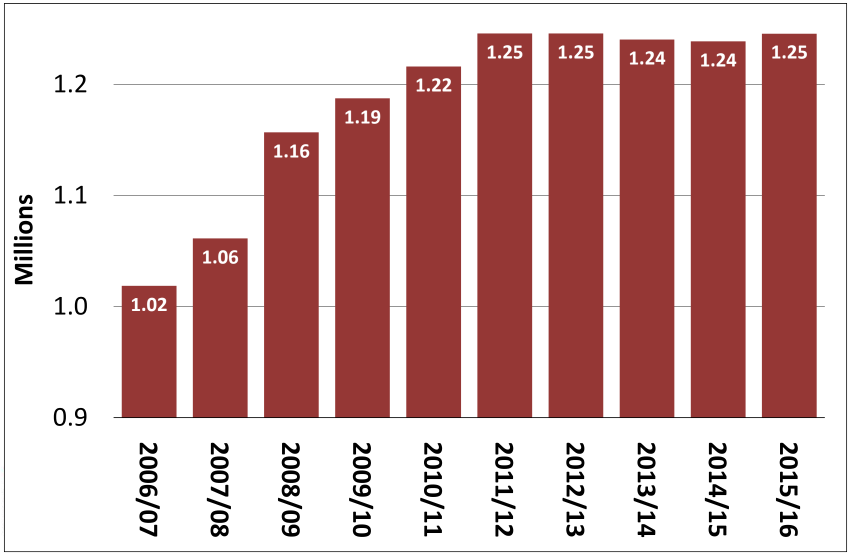
A measured fiscal consolidation (2)

Consolidated government fiscal framework

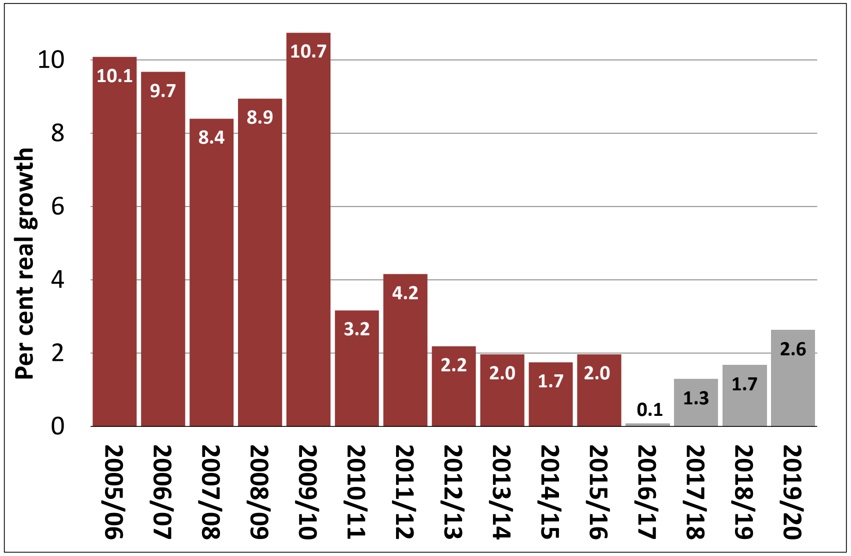
R billion / Per cent of GDP	2015/16 Outcome	2016/17 Revised	2017/18	2018/19	2019/20
			Medium-term estimates		
Revenue	**1 220.9**	**1 301.0**	**1 416.9**	**1 537.9**	**1 670.4**
	29.9%	*29.7%*	*30.1%*	*30.3%*	*30.4%*
Expenditure	**1 373.1**	**1 451.5**	**1 564.0**	**1 676.0**	**1 809.4**
	33.6%	*33.1%*	*33.3%*	*33.0%*	*33.0%*
Budget balance	**-152.2**	**-150.5**	**-147.1**	**-138.2**	**-139.0**
	-3.7%	*-3.4%*	*-3.1%*	*-2.7%*	*-2.5%*
Total net loan debt	**1 804.6**	**2 004.4**	**2 209.2**	**2 417.1**	**2 632.4**
	44.2%	*45.8%*	*47.0%*	*47.6%*	*47.9%*

Source: National Treasury

National and provincial employee headcount



Real growth in main budget non-interest spending



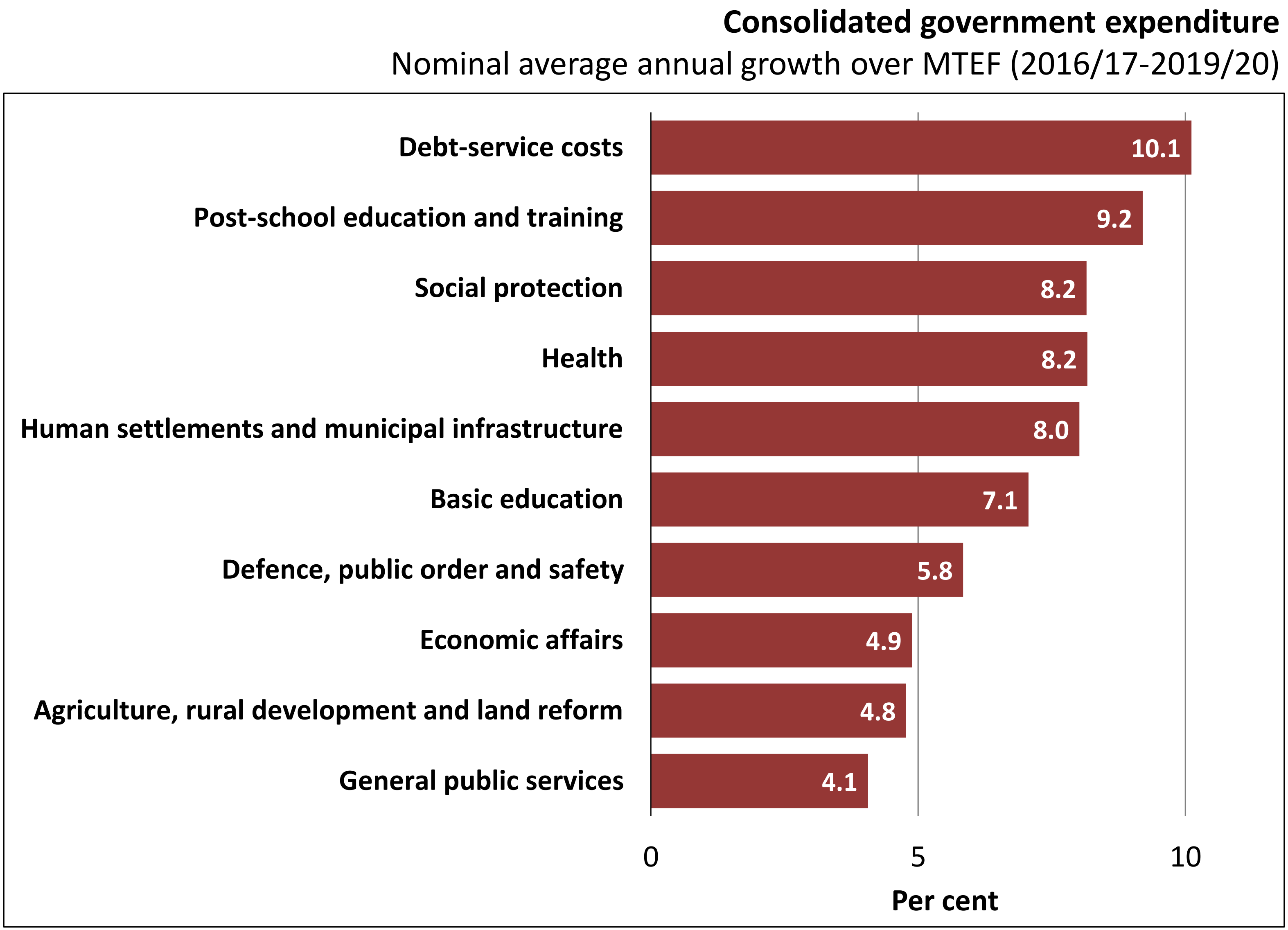
Spending priorities

Consolidated government expenditure

R billion	2016/17 Revised	2017/18 Medium-term estimates	2018/19	2019/20	Average annual growth 2016/17 – 2019/20
Basic education	228.4	244.8	261.9	280.6	7.1%
Health	169.3	184.4	198.9	214.2	8.2%
Defence, public order and safety	189.5	197.9	210.7	224.6	5.8%
Post-school education and training	68.6	76.6	81.1	89.3	9.2%
Economic affairs	207.6	216.4	225.8	239.6	4.9%
Human settlements and municipal infrastructure	181.1	197.6	212.1	228.3	8.0%
Agriculture, rural development and land reform	26.3	26.9	28.4	30.3	4.8%
General public services	67.8	69.8	73.0	76.4	4.1%
Social protection	165.1	180.0	193.3	208.9	8.2%
Total expenditure by function	**1 303.8**	**1 394.3**	**1 485.2**	**1 592.2**	**6.9%**
Debt-service costs	147.7	163.6	180.8	197.2	10.1%
Contingency reserve	–	6.0	10.0	20.0	**–**
Total expenditure	**1 451.5**	**1 564.0**	**1 676.0**	**1 809.4**	**7.6%**

Source: National Treasury

Spending growth



Containing spending on non-essentials

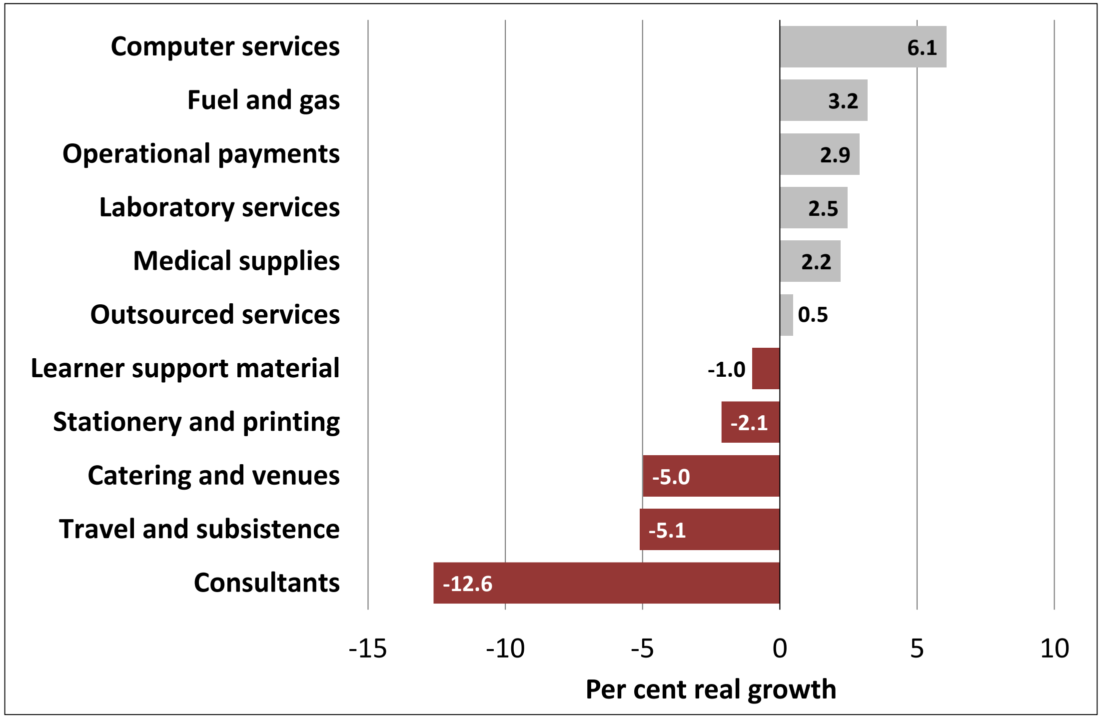
- The Office of the Chief Procurement Officer (OCPO) is working to improve spending efficiency and eliminate opportunities for corruption:
  – Draft Public Procurement Bill to be complete by March 2017
  – The draft Preferential Procurement Regulations are being revised to ensure that at least 30 per cent of public procurement is reserved for designated groups
  – Public procurement systems will be modernised
  – Scope of transversal contracting to expand over next three years

- Cost-containment measures, linked with procurement reforms and budget reductions, have succeeded in curtailing spending on non-essential goods and services.

- Budgets for essential goods and services have grown by as much as 2 per cent in real terms.

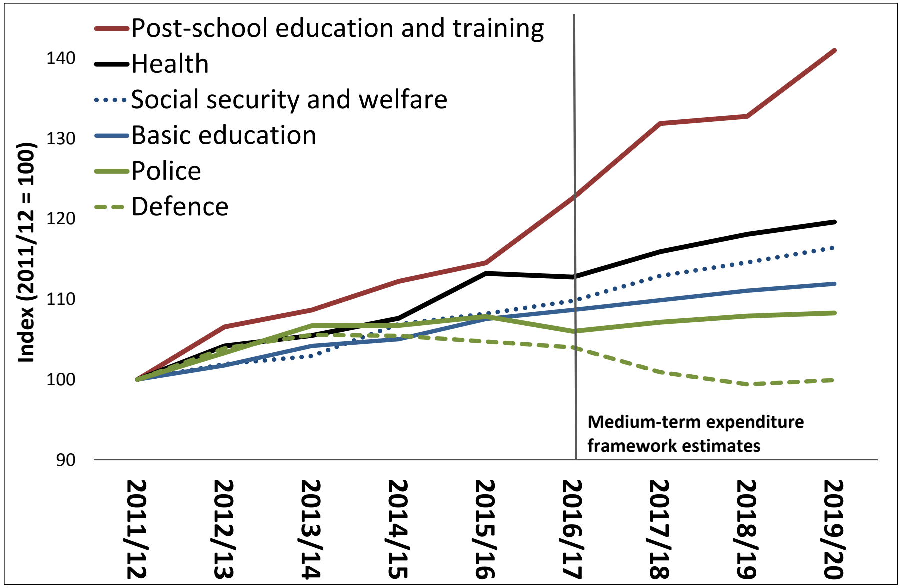
- The National Treasury will publish the results of 27 performance and expenditure reviews

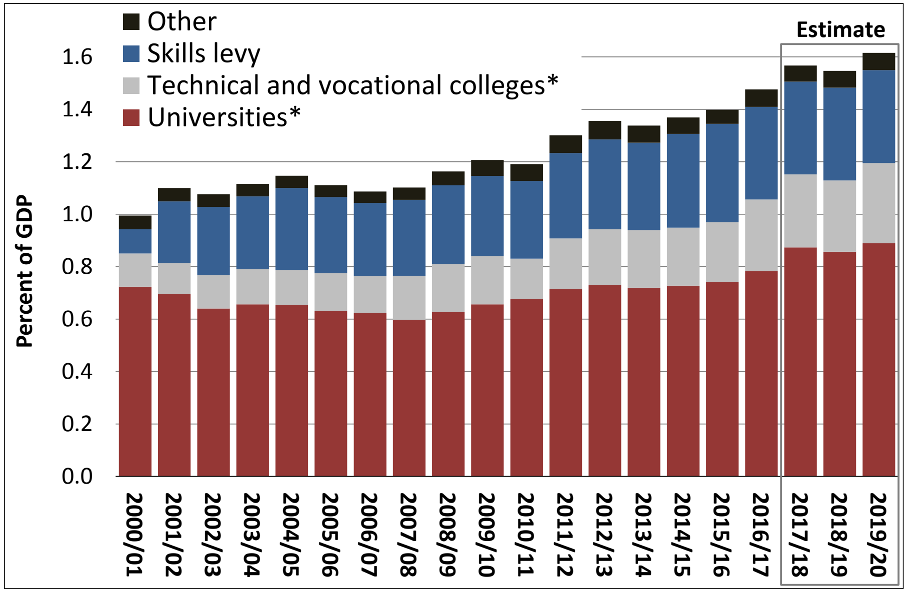
Real spending growth in selected goods and services: 2012/13-2015/16



Funding post school education

- Government has significantly expanded funding of education over the past 20 years.
- Over the past five years, expenditure on post-school education and training has grown much faster than other budgets.
- Allocations have increased from 1 per cent of GDP in 2008 to 1.5 per cent today. But most of this increase benefited vocational colleges, SETAs and the National Skills Fund, rather than universities.
- The 2016 MTBPS proposes to accelerate the growth of spending on post-school education.
- Despite fiscal constraints, subsidies to universities grow at 10.9 per cent each year and transfers to NSFAS grow at 18.5 per cent.





* Includes direct subsidies and NSFAS allocations

Additions to support universities and students

- In the 2016 Budget:
  - R5.7 billion was added to university subsidies to fund the zero per cent fee increase for the 2016 academic year.
  - NSFAS received additional funding of R10.6 billion over the 2016 MTEF period.
- In the 2017 Budget:
  - Government will fund the increase in fees at higher learning institutions for the 2017 academic year, up to a maximum of 8 per cent, for students from households earning up to R600 000 per year.
  - Significant top-ups are also made to NSFAS.

Additions to support universities and students

R million	2016/17	2017/18	2018/19	2019/20	Total
2016 additions	**4 882**	**5 555**	**5 832**	**–**	**16 269**
NSFAS historical debt relief	2 543	–	–	–	2 543
NSFAS extension	2 039	2 992	3 013	–	8 044
Zero fee increase	300	2 563	2 819	–	5 682
2017 additions	**1 543**	**4 988**	**5 346**	**5 717**	**17 594**
NSFAS extension	1 543	2 370	2 560	2 764	9 237
Universities: Fee increase subsidy	–	2 460	2 618	2 775	7 853
TVET colleges: Fee increase subsidy	–	158	168	178	504
Total	**6 425**	**10 543**	**11 178**	**5 717**	**33 863**

Source: National Treasury

Division of revenue

- Division of revenue is broadly stable in the years ahead. Strong growth in allocations to provincial and local government reflects the priority placed on frontline services, as well as the rising cost of these services
- The NT, working with provincial treasuries, national departments, StatsSA, FFC has begun an in-depth review of the provincial equitable share formula
- Given budgetary constraints, all municipalities need to focus on more efficient spending and value for money to improve basic service delivery
- Government will also work with financially sound municipalities to expand their investment programmes on the strength of their own balance sheets

R billion	2016/17	2017/18	2018/19	2019/20	Average annual growth 2016/17 – 2019/20
National allocations	559.8	589.7	631.3	681.5	6.8%
Provincial allocations	500.5	538.1	578.6	621.0	7.5%
Local government allocations	104.9	112.5	121.5	132.3	8.0%
Total allocations	**1 165.2**	**1 240.4**	**1 331.4**	**1 434.8**	**7.2%**
Percentage shares					
National departments	48.0%	47.5%	47.4%	47.5%	
Provincial	43.0%	43.4%	43.5%	43.3%	
Local government allocations	9.0%	9.1%	9.1%	9.2%	

Source: National Treasury

national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Actions on state-owned companies

- Government is taking steps to rationalise several housing development finance institutions, as well as entities in the telecommunications sector
- Advisors will be appointed to provide technical assistance as government considers the possible realignment of its airline shareholdings
- The inter-ministerial committee responsible for overseeing the implementation of the reforms has approved the principles that will guide collaboration between state-owned companies and the private sector to accelerate the delivery of new infrastructure projects
- The newly-established Presidential State-Owned Companies Coordinating Council will play a monitoring and coordinating role. The statutory responsibilities of company boards and executive authorities as set out in the Companies Act (2008) and Public Finance Management Act (1999) remain unchanged
- Over the medium term, any requests for fiscal support will be informed by the principles set out in the 2015 Budget Review
- Government is closely monitoring South African Airways (SAA), the South African Post Office (SAPO), SANRAL and Eskom, with the aim of stabilising these entities and mitigating any risks that may materialise.

Conclusion

- With decisive action, South Africa will emerge from a period of economic weakness. This will enable government to provide greater support to the economy and boost employment.
- Government's economic reform programme is guided by the NDP and, over the short term, the 9-point plan announced in February 2015. These efforts aim to create a more just society and ensure that the benefits of transformation are shared as broadly as possible.
- Implementation of reforms must be accompanied by efforts to tackle corruption. The benefits of empowerment should be accessible on equal basis, not limited to connected insiders.
- The fiscal framework maintains real expenditure per capita and supports macro stability. The sustainability of the fiscal framework depends on the recovery of economic activity.