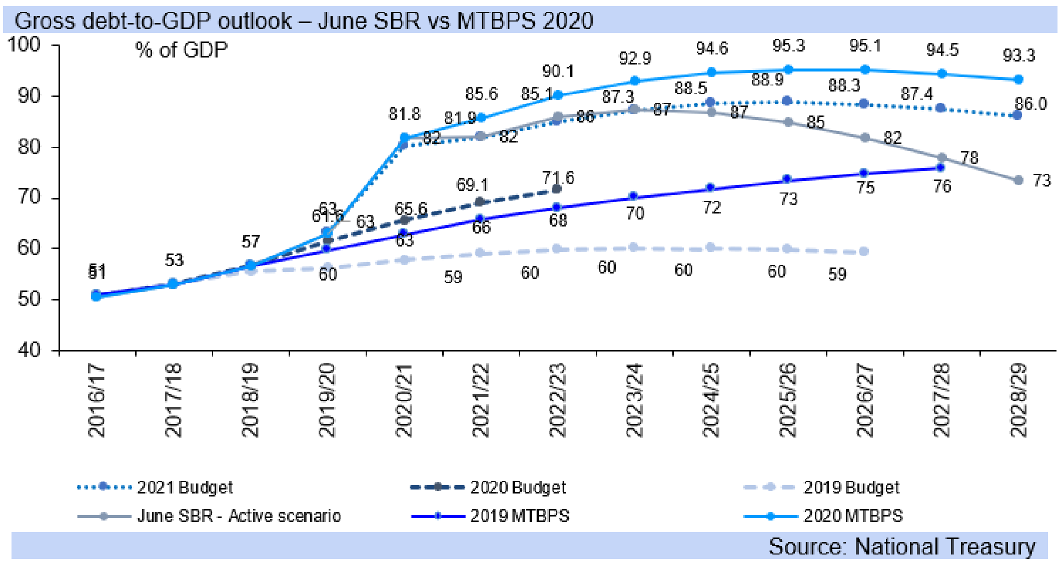
SA Economics

Wednesday 24 February 2021

Budget note: 2021 Budget proves better than markets expected, bringing down the debt peak to 88.9% from 95.3% of GDP, much better from a rating perspective, and seeing the rand target the R14.40/USD mark



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Consolidated government fiscal framework

	2019/20	2020/21	2021/22	2022/23	2023/24
Revenue	**Outcome**	**Estimate**		**Medium-term estimates**	
Budget 2021	**1530.5**	**1362.7**	**1520.4**	**1635.4**	**1717.2**
	29.7%	**27.7%**	**28.4%**	**28.9%**	**28.6%**
MTBPS 2020	*1518.1*	*1276.7*	*`1457.6*	*1595.8*	*1705.7*
	29.5%	*26.3%*	*27.4%*	*28.3%*	*28.6%*
Budget 2020	1,517.0	1,583.9	1,682.8	1,791.3	
	29.4%	29.2%	29.2%	29.2%	
Expenditure					
Budget 2021	**1822.3**	**2052.5**	**2020.4**	**2049.5**	**2095.1**
	35.4%	**41.7%**	**37.7%**	**36.2%**	**34.9%**
MTBPS 2020	*1848.7*	*2037.8*	*1993.5*	*2079.6*	*2139.2*
	35.9%	*41.9%*	*37.5%*	*36.9%*	*35.9%*
Budget 2020	1,843.5	1,954.4	2,040.3	2,141.0	
	35.7%	36.0%	35.4%	34.9%	
Budget Balance					
Budget 2021	***-291.8***	**-689.8**	**-500.0**	**-414.1**	**-377.9**
	-5.7%	**-14.0%**	**-9.3%**	**-7.3%**	**-6.3%**
MTBPS 2020	*-330.6*	*-761.1*	*-535.9*	*-483.9*	*-433.4*
	-6.4%	*-15.7%*	*-10.1%*	*-8.6%*	*-7.3%*
Budget 2020	-326.6	-370.5	-357.5	-349.7	
	-6.3%	-6.8%	-6.2%	-5.7%	

Source: National Treasury

- The 2021 Budget delivered a substantial cut in government's borrowing trajectory, to a peak of 88.9% of GDP from the MTBPS outlook of 95.3% of GDP for gross debt, and this will likely be the key point for the credit rating agencies, which we expect will delay any downgrades.
- SA could even eventually move off Moody's and Fitch's negative outlooks and avoid descending into the single B category. Government will not raise income taxes and adjustments for fiscal drag will be implemented, and withdrew R40bn in previously announced tax increases.
- However, sin tax and fuel price increases, along with increases in excise duties will be implemented. But, of particular good news for the economy, in 2022/23 the company tax rate will be dropped to 27%, adding to what today is proving to be a very pro growth Budget.
- Key is that the primary deficit is to be narrowed to 0.8% of GDP by 2023/24, showing government is serious about fiscal consolidation, and significantly lowering its budget deficit projections to -6.3% of GDP by the end of the MTEF period (Medium-Term Expenditure period).

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- The revenue overrun is expected at R99.6bn for this fiscal year (2020/21), with revenue collections now estimated at R1.363tr (trillion), but still well below the R1.531tr of the previous fiscal year (of 2019/20), and 2021/22 is also expected below this at R1.520tr.
- With no fiscal slippage in this Budget it reverses some of the projected serious fiscal deterioration indicated in 2020's SBR and MTBPS, but by no means eliminates the bulk of it, and as a consequence we believe there will certainly be no credit rating upgrades in H1.21.
- We believe the ratings pressures are off for any downgrade in the first half of this year, but SA may stay on the current negative outlooks from Fitch and Moody's as key will be achieving its new budget estimates, and the rating agencies expectations on these.
- The key message today from the Budget is "(r)enewing the economy and restoring the public finances", although this is likely just the start. Nevertheless, there will likely be some concerns as to whether government will actually be able to meet the fiscal objectives laid out today.
- Support and recovery from the COVID-19 crisis remains key, with government to fund a free rollout of the COVID-19 vaccines, while restraint on the expenditure front at R2tr, with support to shift expenditure to investment and away from consumption.

Please scroll down to the many sections below

SA credit ratings - Long term foreign currency

South Africa – S&P Ratings		South Africa – Fitch Rating		South Africa - Moody's Rating	
03/10/1994	BB	22/09/1994	BB	14/10/2004	Baa2
20/11/1995	Upgraded to BB+	19/05/2000	Upgraded to BB+	11/01/2005	Upgraded to Baa1
25/02/2000	Upgraded to BBB-	27/06/2000	Upgraded to BBB-	16/07/2009	Upgraded to A3
07/05/2003	Upgraded to BBB	05/02/2003	Upgraded to BBB	27/09/2009	Downgraded to Baa1
01/08/2005	Upgraded to BBB+	25/08/2005	Upgraded to BBB+	06/11/2014	Downgraded to Baa2
12/10/2012	Downgraded to BBB	10/01/2013	Downgraded to BBB	09/06/2017	Downgraded to Baa3
13/06/2014	Downgraded to BBB-	04/12/2015	Downgraded to BBB-	27/03/2020	Downgraded to Ba1
03/04/2017	Downgraded to BB+	07/04/2017	Downgraded to BB+	20/11/2020	Downgraded to Ba2
24/11/2017	Downgraded to BB	03/04/2020	Downgraded to BB		
29/04/2020	Downgraded to BB-				

Source: Bloomberg

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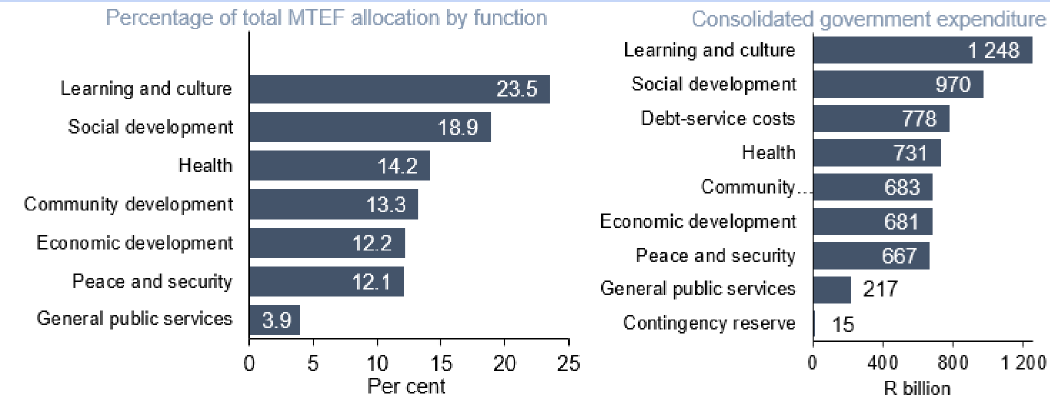
Budget Balances								
	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
						Medium-term		
MTBPS 2011								
Budget 2012								
MTBPS 2012	-3.1%							
Budget 2013	-3.1%							
MTBPS 2013	-3.8%	-3.0%						
Budget 2014	-3.6%	-2.8%						
MTBPS 2014	-3.6%	-2.6%	-2.5%					
Budget 2015	-3.9%	-2.6%	-2.5%					
MTBPS 2015	-3.8%	-3.3%	-3.2%	-3.0%				
Budget 2016	-3.9%	-3.2%	-28%	-2.4%				
MTBPS 2016	-4.1%	-3.8%	-3.4%	-3.2%	-3.1%			
Budget 2017	-3.5%	-3.4%	-3.1%	-2.8%	-2.6%			
MTBPS 2017	-3.4%	-3.3%	-4.3%	-3.9%	-3.9%	-3.9%		
Budget 2018	-3.7%	-3.55%	-4.3%	-3.6%	-3.6%	-3.5%		
MTBPS 2018	-3.7%	-3.6%	-4.0%	-4.0%	-4.2%	-4.2%	-4.0%	
Budget 2019	-3.7%	-3.6%	-4.0%	-4.2%	-4.2%	-4.5%	-4.3%	
MTBPS 2019		-3.5%	-4.0%	-4.2%	-5.9%	-6.5%	-6.2%	
Budget 2020		-3.6%	-4.1%	-4.0%	-6.3%	-6.8%	-6.2%	
MTBPS 2020					-6.4%	-15.7%	-10.1%	-8.6%
Budget 2021					-5.7%	-14.0%	-9.3%	-7.3%
								Source: National Treasury

- The Budget Review stresses that “(t)he fiscal position, which was already weak before the current crisis, has deteriorated sharply, requiring urgent steps to avoid a debt spiral. For several years, increasing debt-service costs have exceeded nominal GDP”.
- In particular,“(e)xcluding compensation reductions, real consolidated non-interest expenditure grows by an annual average of 0.4 per cent between 2020/21 and 2023/24.” The high debt costs limit expenditure on other areas.
- Indeed, “debt-service costs exceeding nominal GDP is “a trend expected to continue over the medium term. If this course is not reversed, the economy will not be able to generate sufficient revenue for the state to service debt.”
- “Were that to occur, government would lose the ability to control debt and debt-service costs, as investors conclude that lending rates do not adequately compensate them for risk, leading to greater currency volatility and a protracted capital flow reversal.”
- “Debt-service costs will rise from R232.9 billion in 2020/21 to R338.6 billion in 2023/24. These costs, which were already the fastest-rising item of spending, now consume 19.2 per cent of tax revenue.”
- “Over the next three years, annual debt-service payments exceed government spending on most functions, including health, economic services, and peace and security.” “Funds that could be spent on economic and social priorities are being redirected to pay … bondholders."
- These are the core issues for the sustainability of government finances, and while a lot has been achieved in the projections to reduce the planned borrowing trajectory, it still is

not enough to achieve fiscal sustainability over the long-term without faster economic growth.

- That is, National Treasury and economic predictions generally do not foresee economic growth quickening into the 4-6% range, and nor do we, which is a severe constraint on revenue raising ability.
- To this end the Budget continues to focus most of its expenditure adjustments on the wage bill, with “main budget non-interest expenditure … reduced by R264.9 billion, or 4.6 per cent of GDP “and (m)ost of these adjustments are to the wage bill”.

Percentage of the total MTEF allocation by function, and Consolidated government expenditure by function 2021/22-2023/24



Source: National Treasury,

Baseline reductions by economic classification over the MTEF period				
R million	2020/21	2021/22	2022/23	2023/24
Economic classification				
Current payments		**-35 896**	**-51 926**	**-80 904**
Compensation of employees1		-26 306	-46 139	-72 015
Goods and services		-9 583	-5 779	-8 874
Interest and rent on land		-6	-8	-15
Transfers and subsidies		**-27 832**	**-36 872**	**-66 790**
Provinces and municipalities[2]		-13 274	-17 640	-31 993
Departmental agencies and accounts[3]		-3 245	-4 112	-7 375
Higher education institutions		-1 712	-2 250	-4 081
Foreign governments and international organisations		-98	-131	-238
Public corporations and private enterprises		-729	-949	-1 720
Non-profit institutions		-347	-452	-820
Households		-8 428	-11 337	-20 562
Provisional allocations and use of reserves		**-1 620**	**-1 324**	**-4 633**
Consolidated expenditure		**-65 349**	**-90 122**	**-152 326**
Total reduction to allocations for	**-36 511**	**-81 236**	**-113 599**	**-72 015**
Announced in 2020 Budget	-37 807	-54 929	-67 460	–
Further reduction in 2021 Budget		-26 197	-46 021	-72 015
Other adjustments	1 296	-109	-118	-
				Source: National Treasury

1. Provincial compensation of employees reduction moved from transfers to compensation of employees
2. Excludes compensation of employees, with the balance to be allocated to spending items at the provincial level
3. Excludes compensation of employees, balance to be allocated to spending items at the public entity level

- In particular, "(p)ublic-service compensation absorbed 41 per cent of government revenues in 2019/20 and 47 per cent of revenue in 2020/21. Allowing the wage bill to continue rising in line with recent trends is not sustainable."
- "It would require a substantial reduction in funding for capital investment, and critical public goods and services". South Africa cannot let the future of the country be destroyed by a debt default, and as such has to control current expenditure tightly.
- The Budget adds "(i)n December 2020, following government's decision to not implement a wage increase in 2020/21, the Labour Appeal Court reaffirmed the National Treasury's constitutional role in safeguarding the public finances."
- " In this regard, the approach to future wage negotiations will align with the fiscal position and prevailing economic conditions … the 2021 Budget proposes a significant moderation in spending on the consolidated wage bill, which grows by an average of 1.2 per cent over the medium term."
- South Africa is consequently on a sounder fiscal trajectory. Government is also in the process of "adopting zero-based budgeting principles. Cost containment and efficient spending is vitally key for South African's government finances."

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- In particular, the Budget says "South Africa does not get good value for money in public spending. Waste and inefficiency reduce developmental impact, and become a glaring problem in the context of limited state resources."
- "In April 2020 government launched a series of spending reviews … (which) highlighted significant restructuring opportunities – including merging or closing entities to reduce duplication of functions – and noted massive inefficiencies in some infrastructure programmes."
- "The reviews have revealed the limits of incremental budgeting, especially where technology has the potential to transform service delivery. And they have observed cases where guaranteed budget increments create perverse incentives to enter into contracts that have high unit costs for the delivery of certain services."
- Overall, "(c)onsolidated expenditure over the 2021 MTEF period is projected to be R6.16 trillion. In line with pro-poor government policies, R987.1 billion or 56.8 per cent of the allocations in 2021/22 go to social services in learning and culture, health and social development."

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Impact of tax proposals on 2021/22 revenue[1]

R billion		
Gross tax revenue (before tax proposals)		**1 365 124**
Budget 2020/21 proposals		–
Direct taxes		**-2,200**
Taxes on individuals and companies		
Personal income tax	**-2,200**	
Increasing brackets by more than inflation	-2,200	
Revenue if no adjustment is made	11,200	
Higher-than-inflation increase in brackets and rebates	-13,400	
Indirect taxes		**2,200**
Taxes on international trade and transactions		
Introduction of export tax on scrap metal	400	
Specific excise duties		
Increase in excise duties on alcohol	1 100	
Increase in excise duties on tobacco	700	
Gross tax revenue (after tax proposals)		**1 365 124**

Source: National Treasury

1. Revenue changes are in relation to thresholds that have been fully adjusted for inflation

Estimates of individual taxpayers and taxable income, 2021/22

Taxable bracket	Registered individuals		Taxable income		Income tax payable before relief		Income tax relief after proposals		Income tax payable after proposals	
R thousand	Number	%	R billion	%	R billion	%	R billion	%	R billion	%
R0 - R80[1]	7,183,913	–	256.2	–	–	–	–	–	–	–
R80 - R150	1,855,292	26.7	211.1	8.6	15.7	3.0	-1.3	9.4	14.5	2.8
R150 - R250	1,691,889	24.3	329.3	13.4	29.5	5.6	-1.8	13.4	27.7	5.4
R250 - R350	1,283,954	18.4	378.4	15.4	54.5	10.3	-2.3	16.8	52.3	10.1
R350 - R500	981,993	14.1	409.1	16.6	76.6	14.5	-2.6	19.5	74.0	14.3
R500 - R750	612,177	8.8	369.1	15.0	88.4	16.7	-2.4	18.1	86.0	16.7
R750 - R1 000	262,643	3.8	226.2	9.2	65.1	12.3	-1.3	10.0	63.8	12.4
R1 000 - R1 500	159,127	2.3	191.1	7.8	61.9	11.7	-0.8	6.1	61.0	11.8
R1 500 +	113,192	1.6	346.3	14.1	137.7	26.0	-0.9	6.6	136.8	26.5
Total	6 960 267	100.0	2,460.7	100.0	529.4	100.0	-13.4	100.0	516.0	100.0
Grand total	14,144,180		2,716.8		529.4		-13.4		516.0	

Source: National Treasury

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

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- "Gross tax revenue for 2020/21 is expected to be R213.2 billion lower than projections in the 2020 Budget. However, due to a recovery in consumption and wages in recent months, and mining sector tax receipts, 2020/21 revenue collections are expected to be R99.6 billion higher than estimated in the 2020 MTBPS."
- "As a result, government will not introduce measures to increase tax revenue in this Budget, and previously announced increases amounting to R40 billion over the next four years will be withdrawn." "Government will not introduce measures to increase tax revenue in the 2021 Budget; previously announced increases amounting to R40 billion will also be withdrawn."
- "Indeed, Since October 2020, there has been a stronger-than-expected rebound in domestic value-added tax (VAT) and customs duties flowing from the rise in consumption once lockdown restrictions eased. Monthly domestic VAT collections since August were higher than the corresponding months in 2019, and fuel levy collections have also improved."
- "A surge in provisional corporate tax payments in December exceeded expectations. This was primarily driven by the mining sector, with companies benefiting from high commodity prices and a favourable exchange rate. Personal income tax collections remain under pressure due to the elevated levels of unemployment flowing from the pandemic."
- "The main tax proposals include an above-inflation increase in personal income tax brackets and rebates, and an 8 per cent increase in alcohol and tobacco excise duties".
- "Gross tax revenue for 2020/21 is expected to be 10.6 per cent lower than in the previous fiscal year and R213.2 billion lower than projected in the 2020 Budget, but higher than estimated in the October 2020 MTBPS."
- "This change is expected to support economic recovery by reducing financial pressure on households and businesses. A gradual recovery in revenue is expected over the medium term. The tax-to-GDP ratio now stands at 24.6 per cent."
- "A strong and sustained economic rebound is required for this ratio to return to pre-COVID-19 levels of 26.3 per cent of GDP. The main tax proposals for 2021/22 include above-inflation increases in personal tax brackets and rebates, and an 8 per cent increase in excise duties on tobacco and alcohol products."
- The main tax proposals for 2021/22 are:
  • An above-inflation increase of 5 per cent in personal income tax brackets and rebates.
  • An inflation-linked general fuel levy increase of 15c/litre for petrol and diesel, and an above-inflation increase of 11c/litre in the Road Accident Fund levy.
  • An 8 per cent increase in alcohol and tobacco excise duties.

Total national government debt: end of period					
R billion	**2019/20**	**2020/21**	**2021/22**	**2022/23**	**2023/24**
	Outcome	**Revised**	**Medium-term estimates**		
Domestic loans[1]	**2 874.1**	**3 529.1**	**3 916.7**	**4 322.3**	**4 707.8**
Short-term	360.7	457.9	466.9	518.9	574.9
Long-term	2 513.4	3 071.2	3 449.8	3 803.4	4 132.9
Fixed-rate	*1 863.2*	*2 287.6*	*2 615.0*	*2 845.1*	*3 161.5*
Inflation-linked	*650.2*	*783.6*	*834.8*	*958.3*	*971.4*
Foreign loans[1]	**387.2**	**420.6**	**466.1**	**497.6**	**526.7**
Gross loan debt	**3 261.3**	**3 949.7**	**4 382.8**	**4 819.9**	**5 234.5**
Less: National Revenue Fund bank balances	-263.6	-292.0	-180.3	-162.1	-142.9
Net loan debt[2]	**2 997.7**	**3 657.7**	**4 202.5**	**4 657.8**	**5 091.6**
As percentage of GDP:					
Gross loan debt	*63.3*	*80.3*	*81.9*	*85.1*	*87.3*
Net loan debt	*58.2*	*74.3*	*78.5*	*82.2*	*84.9*

Source: National Treasury

1. A longer time series is given in Table 10 of the statistical annexure at the back of the Budget Review
2. Estimates include revaluation based on National Treasury's projections of inflation and exchange rates

National government debt-service costs						
	2019/20	**2020/21**		**2021/22**	**2022/23**	**2023/24**
R million	**Outcome**	**Budget**	**Revised**	**Medium-term estimates**		
Domestic loans	187,276	211,144	213,794	249,054	285,056	312,096
Short-term	32,096	25,441	21,133	18,025	21,802	25,566
Long-term	155,180	185,703	192,661	231,029	263,254	286,530
Foreign loans	17,493	18,126	19,058	20,687	22,957	26,495
Total	**204,769**	**229,270**	**232,852**	**269,741**	**308,013**	**338,591**
As a percentage of:						
GDP	*4.0*	*4.2*	*4.7*	*5.0*	*5.4*	*5.6*
Expenditure	*12.1*	*13.0*	*12.9*	*14.7*	*16.5*	*17.7*
Revenue	*15.2*	*16.4*	*19.4*	*20.0*	*21.2*	*22.2*

Source: National Treasury

- The bottom line is essentially that "public finances remain under severe strain, but faster-than-expected revenue growth enables government to support the economy and the health sector, while narrowing the deficit more rapidly than projected in October 2020."
- "Over the medium term, continued expenditure restraint is required for fiscal sustainability, defined as stabilisation of the debt-to-GDP ratio. Efforts to narrow the budget deficit and improve the composition of spending – primarily through restraining wage bill growth – remain on course."
- " The consolidated deficit is projected to narrow from 14 per cent of GDP in the current year to 6.3 per cent in 2023/24. Gross national debt is projected to stabilise at a lower level of 88.9 per cent of GDP in 2025/26."
- "Large risks remain. The global and domestic recovery remains highly uncertain, while spending pressures from state owned companies continue to exert upward pressure on the expenditure ceiling. During 2021, a new round of public-service wage negotiations will take place."

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- "Since the 2020 Budget Review, the budget deficit has doubled and the in-year revenue shortfall is estimated at R213.2 billion. These changes reflect the impact of the COVID-19 pandemic, as well as government's response".
- "The consolidated deficit in the current year – estimated at 14 per cent of GDP – is the largest on record. Gross national debt is projected to rise from 80.3 per cent of GDP in 2020/21 to 87.3 per cent of GDP by 2023/24, with debt-service costs reaching R338.6 billion in that year".
- Looking forward, "the fiscal strategy aims to: Narrow the deficit and stabilise the debt-to-GDP ratio, primarily by controlling non-interest expenditure growth. Provide continued support to the economy and public health services in the short term, without adding to long-term spending pressures. Improve the composition of spending, by reducing growth in compensation while protecting capital investment."
- "Changes since the 2020 MTBPS include three-month extensions of the special COVID-19 social relief of distress grant and the Unemployment Insurance Fund's Temporary Employer/Employee Relief Scheme, and funding for the public employment initiative and for provincial hospitals in 2021/22."
- "Up to R10.3 billion is provided for vaccine rollout for the current year and over the next two years. Given uncertainty around vaccination campaign costs, the contingency reserve has been increased from R5 billion to R12 billion in 2021/22. These interventions do not add to longer-term expenditure."

Government guarantee exposure[1]

	2018/19		2019/20		2020/21	
R billion	Guarantee	Exposure[2]	Guarantee	Exposure[2]	Guarantee	Exposure[2]
Public institutions	**487.7**	**368.1**	**484.8**	**413.7**	**581.0**	**410.3**
of which:						
Eskom	*350.0*	*285.6*	*350.0*	*326.9*	*350.0*	*316.8*
SANRAL	*38.9*	*39.5*	*37.9*	*39.0*	*37.9*	*45.3*
Trans-Caledon Tunnel Authority	*43.0*	*14.3*	*43.0*	*13.6*	*43.0*	*13.4*
South African Airways	*19.1*	*15.3*	*19.1*	*17.9*	*19.1*	*6.2*
Land and Agricultural Bank of South Africa	*9.6*	*1.0*	*9.6*	*2.6*	*9.6*	*2.6*
Development Bank of Southern Africa	*11.4*	*4.3*	*10.0*	*4.7*	*10.2*	*4.7*
South African Post Office	*2.9*	–	–	–	–	–
Transnet	*3.5*	*3.8*	*3.5*	*3.8*	*3.5*	*3.8*
Denel	*3.4*	*3.4*	*6.9*	*4.4*	*5.9*	*3.4*
South African Express	*2.8*	*0.2*	*1.9*	*0.2*	*0.2*	*0.1*
Industrial Development Corporation	*0.5*	*0.1*	*0.6*	*0.2*	*0.6*	*0.2*
South African Reserve Bank	*0.3*	–	–	–	*100.0*	*13.3*
Independent power producers	**200.2**	**146.9**	**200.2**	**161.4**	**200.2**	**176.7**
Public-private partnerships[3]	**10.5**	**10.5**	**8.7**	**8.7**	**8.0**	**8.0**

Source: National Treasury

1. A full list of guarantees is given in Table 11 of the statistical annexure in the Budget Review
2. Total amount of borrowing, adjustments to inflation-linked bonds as a result of inflation rate changes and accrued interest
3. These amounts only include national and provincial PPP agreements

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Combined financial position of public institutions[1]			
R billion/net asset value	**2017/18**	**2018/19**	**2019/20**
State-owned companies	362.1	342.0	353.0
Development finance institutions	132.7	137.8	100.3
Social security funds	-27.0	-79.6	-147.6
Other public entities[2]	719.0	724.7	793.3
			Source: National Treasury

1. Due to the COVID-19 pandemic, many entities have not released audited financial statements, therefore unaudited financials or last quarter reports were used for 2019/20
2. State-owned institutions without a commercial mandate and listed in either schedule 1 or 3 of the PFMA such as the National Library of South Africa

- “Over the medium term, debt-service costs are expected to average 20.9 per cent of gross tax revenue. This is twice as large as the median for South Africa’s peer group over the period. Similarly, South Africa’s borrowing remains large by developing-country standards, and debt is projected to grow by 7 per cent of GDP over the next three years.”
- "The current fiscal measures aim to correct this imbalance by reducing growth in the compensation bill and reducing the share of spending on public-service wages over the medium term, while sustaining small real spending increases on other items. These measures will improve the composition of spending by reallocating resources towards growth-enhancing infrastructure investment”.
- The public wage bill “accounted for about 34 per cent of consolidated spending in 2019/20. Between 2006/07 and 2019/20, compensation was one of the fastest-growing spending items, increasing faster than GDP growth.”
- By “2019/20 rising compensation spending had become unaffordable and was the main expenditure risk to the sustainability of the public finances. At the general government level (which includes municipalities), South Africa’s wage bill as a share of output is approximately 5 percentage points higher than the Organisation for Economic Co-operation and Development average – and on par with Iceland and Denmark.”
- “The 2020 Budget proposed compensation reductions totalling R160.2 billion for 2020/21 to 2022/23, relative to the pre-Budget baseline. The 2020 MTBPS proposed further downward adjustments to compensation, amounting to R143.2 billion for 2021/22 to 2023/24.”
- “Over the next three years, total consolidated non-interest expenditure is projected to decline in real terms by 0.8 per cent per year. Excluding compensation, however, real noninterest spending continues to grow by 0.4 per cent over the period.”
- “Including COVID-19 adjustments, compensation at the consolidated budget level is projected to grow by 2.1 per cent in the current year and 1.2 per cent per year over the medium term. These growth rates can be achieved through, for example, doing away with

annual cost-of-living adjustment in the public service up until 2023/24, together with measures to reduce headcounts – a combination of early retirement and natural attrition, as well as freezing or abolishing of non-critical posts.”

- “In addition, government is exploring measures such as harmonising allowances and benefits, reconsidering pay progression rules and reviewing occupation-specific dispensations. Performance bonuses are already being phased out and careful consideration is being applied to amend or abolish some allowances and benefits. “
- The “(w)age bill court case affirms the National Treasury’s constitutional role in safeguarding public finances. Ultimately, the court accepted the argument that the original agreement was invalid and unlawful, and affirmed the National Treasury’s constitutional role in safeguarding the public finances. While government remains committed to collective bargaining and healthy labour relations, this decision helps to maintain an appropriate balance between government’s responsibilities as an employer and as a provider of basic services."

SA Economics

Economic Scenarios: change in expected and severe down probabilities

Scenario		Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
Extreme Up case 1%	USD/Rand (average)	14.25	14.00	13.50	13.25	13.00	12.75	12.75	12.50
	Repo rate (end rate)	3.00	3.00	3.00	3.00	3.00	3.25	3.25	3.25

Impact of Covid-19 pandemic very rapidly resolved - economic growth of 3–5%, then 5-7% for SA. Good governance, growth-creating reforms (structural constraints overcome), strengthening of property rights - individuals obtain title deeds in EWC – no nationalisation. High business confidence and fixed investment growth, substantial FDI inflows, strong fiscal consolidation (government debt falls back to low ratios of 2000s). Strong global growth, commodity boom. Stabilisation of credit ratings, then credit rating upgrades.

Scenario		Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
Up case 2%	USD/Rand (average)	14.50	14.50	14.50	14.00	13.50	14.00	14.50	13.50
	Repo rate (end rate)	3.25	3.50	3.50	3.50	3.50	3.50	3.50	3.50

Quick rebound from Covid-19 pandemic, rising confidence and investment levels - structural problems worked down. No further credit rating downgrades, rating outlooks move to stable and eventually positive, strong fiscal consolidation (government debt projections fall substantially). Global risk-on, global demand quickly returns to trend growth. Limited impact of expropriation without compensation) to abandoned, unused, labour tenants" and government land (individuals are new owners and receive title deeds) does not have a negative effect on economy - no nationalisation.

Scenario		Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
Base case 48%	USD/Rand (average)	15.00	15.40	15.50	15.20	15.30	15.70	15.90	15.60
	Repo rate (end rate)	3.50	3.50	3.50	3.75	3.75	4.00	4.50	4.50

Recovery from the sharp global economic slowdown – sufficient global and domestic monetary and other policy supports to growth and financial markets occur and risk sentiment stabilises then improves. South Africa exits recession in Q3.20. Expropriation of private sector property is limited and does not have a negative impact on the economy or on market sentiment. SA remains in the BB category rating bracket for Moody's – fiscal consolidation (debt to GDP stabilisation) occurs.

Scenario		Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
Lite (domestic) Down case 44%	USD/Rand (average)	16.30	16.50	17.00	16.80	16.50	17.00	17.50	17.00
	Repo rate (end rate)	3.75	3.75	3.75	4.00	4.00	4.25	4.75	4.75

The international environment (including risk sentiment) is that of the base case. South Africa fails to see its debt projections stabilise and falls into single B credit ratings from all three agencies for local and foreign currency. More severe recession in SA than in the expected case. Expropriation of some private commercial sector property without compensation, with some small negative impact on the economy. Business confidence depressed, rand weakness, significant load shedding and weak investment growth. Substantial fiscal consolidation ultimately occurs, preventing ratings falling into CCC grade.

Scenario		Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
Severe down case 5%	USD/Rand (average)	16.50	17.00	17.50	18.00	17.50	17.80	18.00	17.80
	Repo rate (end rate)	4.00	4.00	4.00	4.50	4.50	4.50	5.00	5.00

Lengthy global recession, global financial crisis – insufficient monetary and other policy supports to growth domestically and internationally. Depression in SA, unprecedented rand weakness. Nationalisation of private sector property (title deeds not transferred to individuals). SA rated single B from all three key agencies, with further rating downgrades eventually occurring into CCC grade and lower to D (default) as government finances deteriorate (debt projections elevate even further - fail to ever stabilise. Government borrows from increasingly wider sources as it sinks deeper into a debt trap), eventually include widespread services load shedding, strike action and civil unrest.

Note: Event risk begins Q1.21. Source: Investec

SA Economics

Local Currency – Long term ratings			
	S&P	Moody's	Fitch
Brazil	BB-	Ba2	BB-
Russia	BBB	Baa3	BBB
India	BBB-	Baa3	BBB-
Turkey	BB-	B2	BB-
Mexico	BBB+	Baa1	BBB-
South Africa	**BB**	**Ba2**	**BB-**
China	A+	A1	A+
Nigeria	B-	B2	B
Kenya	B+	B2	B+
Namibia	NR	Ba3	BB
Ghana	B-	B3	B
Botswana	BBB+	A2	NR
Mozambique	B-	Caa2	CCC
Zambia	CCC-	Ca	CC
Ethiopia	B-	B2	CCC
Rwanda	B+	B2	B+
Uganda	B	B2	B+
Angola	CCC+	Caa1	CCC
Dem. Rep of Congo	CCC+	Caa1	NR

Source: Bloomberg

SA Economics

Credit ratings

	S & P	Moody's	Fitch	R & I
	AAA	Aaa	AAA	AAA
	AA+	Aa1	AA+	AA+
	AA	Aa2	AA	AA
	AA-	Aa3	AA-	AA-
Investment grade	A+	A1	A+	A+
	A	A2	A	A
	A-	A3	A-	A-
	BBB+	Baa1	BBB+	BBB+
	BBB	Baa2	BBB	BBB
	BBB-	Baa3	BBB-	BBB-
	BB+	Ba1	BB+	BB+
	BB	Ba2	BB	BB
	BB-	Ba3	BB-	BB-
	B+	B1	B+	B+
	B	B2	B	B
Speculative grade	B-	B3	B-	B-
	CCC+	Caa1	CCC	CCC+
	CCC	Caa2	CC	CCC
	CCC-	Ca3	C	CCC-
	CC	Ca	RD	CC
	C	C	D	C
	D	WR	WD	
	NR		PIF	

Source: Bloomberg

- Indeed, "(w)age negotiations will take place in the Public Service Co-ordinating Bargaining Council. Government will negotiate on the basis of fairness, equity and affordability. A pact that exceeds budgeted amounts would present a risk to the fiscal framework."
- This is key as "a three-year inflation linked agreement would raise the total shortfall to R112.9 billion by 2023/24. And an agreement similar to the one achieved in 2018 – 1 percentage point higher than inflation – would create a compensation shortfall of R132.7 billion (or 2.2 per cent of GDP) by 2023/24."
- SA needs to stick to its Budget estimates and then attempt to improve them, but faster economic growth is the key. Economic growth of 4-6% + will rely on structural reforms, which is not the remit of National Treasury, but government itself, and these need to quicken.
- The lowering in SA's debt trajectory has seen markets view the Budget positively, and in combination with global financial market sentiment still risk-on in nature towards EM portfolio assets the rand even momentarily pierced the R14.40/USD mark today.
- Additionally, the highly accommodative stance of the Fed on QE has also fuelled investor appetite for EM assets. SA's bond yields also improved today. South Africa has also followed the global trend of extending its relief measures, albeit winding them down where applicable, with fiscal consolidation still a policy priority.

SA Economics

- Higher taxes over the past decade have been a key contributor to the slowdown in economic growth, from above 3% y/y early in the decade to 0.2% y/y by its end (2019). The tax buoyancy ratio indicates that there is little absorption left for higher taxes and as such the outcome today is positive.
- Well before the COVID-19 crisis hit, South Africa has increased its borrowing substantially. The current huge projected borrowings, even though there has been some reduction in today's Budget, still does not tally with debt sustainability and risks being pushed into the single B credit rating categories.
- Today's Budget projections are an improvement, but the rating agencies will wait to see if government manages to stabilise its projected debt quantum, then lower it, before thinking of any rating upgrades. We do believe the severe down case probability has fallen however, to 5% on this Budget, and the expected case lifted to 48%.
- SA's still has highly deteriorated fiscal metrics compared to at the start of the 2010s decade. A few reforms have occurred, but not substantial fiscal consolidation. South Africa's current projections still do not show marked fiscal consolidation, and so do not bring the fiscal deficit down to the accepted 3.0% of GDP, or the debt projection down to around 60% of GDP for EMs/Middle income economies.

Foreign Currency – Long term ratings			
	S&P	Moody's	Fitch
Brazil	BB-	Ba2	BB-
Russia	BBB-	Baa3	BBB
India	BBB-	Baa3	BBB-
Turkey	BB-	B2	BB-
Mexico	BBB	Baa1	BBB-
South Africa	**BB-**	**Ba2**	**BB-**
China	A+	A1	A+
Nigeria	B-	B2	B
Kenya	B+	B2	B+
Namibia	NR	Ba3	BB
Ghana	B-	B3	B
Botswana	BBB+	A2	NR
Mozambique	CCC+	Caa2	CCC
Zambia	SD	Ca	RD
Ethiopia	B-	B2	CCC
Rwanda	B+	B2	B+
Uganda	B	B2	B+
Angola	CCC+	Caa1	CCC
Dem. Rep of Congo	CCC+	Caa1	NR
			Source: Bloomberg

SA Economics