October 2023

Ninety One

Investing for a world of change

MTBPS: Finance minister caught between a rock and a hard place

Sisamkele Kobus
Fixed Income Analyst

National Treasury will report a negative hit to revenues in the coming MTBPS

Since the 2022 Medium-term Budget Policy Statement (MTBPS), it had become clear to us that National Treasury's budgetary projections for revenues were too optimistic. Given that the commodity tailwind has all but disappeared, the revenue gains that we had enjoyed over the last few years are unlikely to materialise this year. Notwithstanding the stellar job that SARS has been doing to rebuild the institution and therefore increase efficiency in revenue collections, we believe National Treasury will report a negative hit to revenues in the coming MTBPS.

Revenue collection – not all bad news

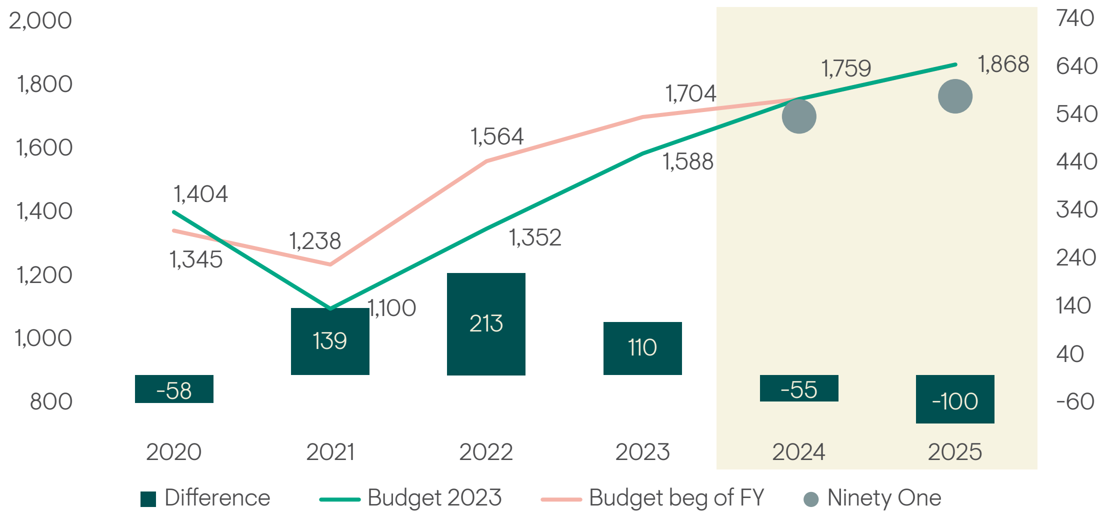
Earlier in the year we were concerned that the slippage in revenues would be larger – closer to R100 billion for this fiscal year alone. However, we now expect revenue slippage to be roughly half that – at R50 billion. This is largely because – with the exception of company income tax – other tax line items are performing relatively OK. Personal income tax, for example, is running at an 8% growth rate year-to-date, but company income tax is currently running at close to 15% lower than last year. The overall result is a better-than-feared performance in revenues to date.

Economic growth – down but not out

When measured against expectations at the beginning of the year, the economy has also performed marginally better than feared. With bouts of stage 6 load shedding earlier this year – understandably a massive hit on economic growth – the economy was at best expected to be flat versus last year. But growth is still weak, so this is not a positive view on the growth picture. Given the intensity of load shedding however, which was expected to persist throughout winter, it has been a lot more resilient.

> The economy has also performed marginally better than feared

Figure 1: Evolution of revenues budgeted and outcome



Source: National Treasury and Ninety One

> The weakness in revenue collection has been coupled with expenditure slippages

Spending pressures mounting

The weakness in revenue collection has been coupled with expenditure slippages. In the February 2023 budget, Finance Minister Enoch Godongwana set expenditure for this current fiscal year at R2.035 trillion, only 1.5% higher than the previous year. Spending is expected to grow by around 5.5% thereafter. Only a very small increase in wages was budgeted for, with the wage growth rate penciled in for the fiscal year 2023/24 at only 1.6%. National Treasury was adamant that they did not want to front-run the wage negotiation process and so penciled in lighter amounts. Of course, they knew this was a risk to their numbers even at the time, but believed it was the prudent thing to do.

The wage negotiation process concluded in April, resulting in a 7.5% increase in the baseline compensation number. The compensation number for the fiscal year 2022/23 stood at R690 billion, which included a cash gratuity of R20-23 billion. This cash gratuity was not included in the baseline (the baseline excluding the cash gratuity for last year, is approximately R668bn). The expected increase is 7.5% to the base of R668bn, which would result in a wage cost of R718bn for 2023/24. Treasury's expected budget for this year was R701bn, thus amounting to slippage of R17bn this fiscal year. Thus, the total cost to Treasury can be broken down into the R20-23bn cash gratuity which now forms part of the base, as well as the R17bn slippage.

The National Treasury may manage to reprioritise some spending, but it will be difficult to get enough from reprioritisation for not only this year but the outer years as well.

> Unfortunately, spending pressures extend beyond the wage bill

Unfortunately, spending pressures extend beyond the wage bill. The SOEs continue to remain a concern for fiscal sustainability. Currently, there is an allocation of R30 billion in the budget for SOEs. This figure excludes the amount earmarked for Eskom, which is now below the "spending line". It's becoming increasingly evident that additional funding may be required. Furthermore, it is worth noting that the COVID grant was originally only budgeted for only until the end of fiscal year 2023/24.

In conclusion, the finance minister is caught between a rock and a hard place. He needs to present a consolidation path amidst mounting pressures from both revenue weakness and spending pressures. The ministry, together with National Treasury, has been floating some ideas to the cabinet, which have been leaked to the media. These include combining some ministries and departments to save funds. Potential policy changes will however probably only be implemented at the Budget in 2024. The MTBPS in November is only likely to reflect a mark to market for the fiscal slippage and not provide a material policy response yet.

Important information

Contact information

Please visit our website at www.ninetyone.com for more information on our range of funds and portfolio products.

To reach our Ninety One unit trust team, please use telephone: 0860 500 900 or email: utclientservicessa@ninetyone.com

To reach our Ninety One Investment Platform team, please use telephone: 0860 500 100 or email: comcentre@ninetyone.com

Financial advisors: please contact our Advisor Service Centre on telephone: 0860 444 487

Alternatively, please contact your Ninety One investment consultant.

1023-0157-Viewpoints and updates