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ASSET MANAGEMENT

From SONA to BUDGET

The South African economy is at a critical junction and the 2020 February budget will be a deciding moment in determining its future path. It now depends on how much of the resolutions and intentions presented in the medium-term budget policy statement (MTBPS) and National Treasury's economic transformation plan is adopted and implemented.

Earlier this month, President Ramaphosa delivered his state of the nation (SONA) speech despite disruptions from the EFF. His speech served as a precursor to the Budget outlining salient features of the economy while providing further clarity on issues such as energy policy, state owned enterprises (SOE's) and the infrastructure fund. He acknowledged that we are at a "decisive moment" in an economy that is in crisis.

The policy on energy focussed on the determination of new generation capacity from renewable energy, the acquisition of additional capacity from existing wind and solar plants and the allowance for municipalities to procure power from independent power producers. In addition, he acknowledged the problems facing the sustainability of public debt which will be dealt with by the Minister of Finance in the budget presentation. The plan by the CEO of Eskom, André de Ruyter, to restructure Eskom into three units (generation, transmission and distribution) was reinforced with each of these entities set to have its own boards and management structures.

The president emphasised support for smaller SOE's but stated the need for a process of rationalisation and the need for these entities to serve their strategic and development purposes. Measures will also be introduced to make business easier such as registration of a business within a day and a greatly reduced waiting period to process and issue water licences. Ambitious projects such as the establishment of a sovereign wealth fund, a state bank, a new university and a smart city begs the question as to where the funding will come from in a struggling economy. Nevertheless, the success of these ventures could very well nurture further successes and boost much needed confidence.

The market has now turned its attention to the national budget that will be presented by minister Tito Mboweni on 26 February 2020. A critical budget that hopefully will arrest, to some degree, the downward path of our fiscal health. Most market participants are expecting a consolidated budget deficit of about 6.5% of GDP. A number much wider than the 5.9% pencilled into the MTPBS.

While there is very little wiggle room on the revenue side, a concerted effort and commitment is required to reduce expenditure. Revenue-raising measures are constrained. The remaining avenues in this regard include the raising of indirect taxes such as sin taxes and excise duties, not adjusting personal income tax brackets for inflation, not adjusting medical tax credits and an increase in the VAT rate. All these measures combined are estimated to only produce increased revenue of about R30bn. A far cry from the estimated R150b needed to achieve sustainability in the fiscus. It is therefore incumbent on the government to address the expenditure side of the country's balance sheet. The elephant in the room is undoubtedly the enormous public sector wage bill which is expected to rise by between 7.1% and 6.0% over the next three years compared to inflation which is expected to average about 4.6% over the period. Now is the time to exercise the will to reduce expenditure which is constantly being exacerbated by the fiscal drag caused by bailouts provided to SOE's.

An inevitable downgrade by ratings agency, Moody's is looming which will see an outflow of capital as South Africa is excluded from the World Government Bond Index.

A challenging yet all important budget lies ahead that promises to provide for interesting reading and interpretation as political will, labour pressure and clinical economic logic is juggled to achieve the best possible outcome.

By Sidney McKinnon