COMMENTS ON NATIONAL TREASURY'S ECONOMIC STRATEGY DOCUMENT

Submission by the Organisation Undoing Tax Abuse (OUTA) to the National Treasury, 15 September 2019

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Overview

OUTA welcomes National Treasury's proposed strategy to revive the shell-shocked South African economy and the call for public comment on this. The strategy's emphasis on improving the ease of doing business and fostering an investor-friendly economic climate speaks to the need to preserve our access to affordable debt, but also increases the opportunity for small, medium and micro enterprises to enter new markets. Recent outbreaks of violence against economically competitive foreign nationals in Gauteng attest to a palpably constrained national economy that is making the lives of ordinary citizens extremely difficult and frustrating.

The monopolisation of key industries in has resulted in the dereliction of fiduciary duties (such as systemic contravention of the Public Finance Management Act by senior management and/or board members in Eskom and South African Airways) and an unsustainable reliance on the fact that the provision of basic human needs is indirectly guaranteed by a heavily taxed elite. Instead of diversifying inequality, government should cultivate middle-class growth through strategic public expenditure.

The desirability of disruption and inclusive economic change is clear. However, political disagreement and uncertainty around the prospect of implementation must be overcome by open discussion and constructive debate that builds consensus and solidarity. This policy discussion may be an important step towards redesigning our economy in an inclusive way. Repeated promises to bring about radical economic transformation have been made, yet little public engagement has been facilitated by government to shape economic reforms that are imbued by the people and for the people.

Rapid and dramatic financial failure of several state-owned companies places more pressure on the worrying deficit in the public sector. The need for economic stability and growth amidst structural and systemic challenges in the South African economy demand self-imposed "structural adjustments".

There is much to welcome in this strategy paper. For example, suggestions for simple, competitive and incentivising economic mechanisms such as lowering the cost of doing business and freeing up finance for SMMEs owned by new, historically disadvantaged entrepreneurs. Also, embracing renewable energy sector formalization and allowing households to sell self-generated electricity, and more impactful public spending in labour-intensive sectors that have real potential for growth if properly supported and secured as in agriculture, manufacturing and tourism.

This paper shows a welcome shift in the thinking of a Government that recognises its own limitations. Inclusive planning and reforms are needed to avoid ever-increasing taxes by reversing the centralisation of our economy that has enabled large-scale corruption and maladministration.

Due to time and capacity constraints, we are not able to comment on all aspects of the strategy paper, but overall consider it a good basis for further discussions. We make some specific comments below.

Macroeconomic policy

OUTA agrees that low growth limits the ability of the economy to transform because it threatens the sustainability of critical social spending by government as well as the overall progressivity of tax and fiscal policy. Ordinary party-political policy formulation procedures were not adhered to in the drafting this strategy, which was harshly criticised by unions and party allies. Perhaps the move away from centralised decision-making towards harnessing the creative energy of civil society as well as the established commercial and academic spheres should be welcomed across political divides.

However, economic growth must be qualified by ensuring that it is sensitive to acute environmental and social realities in South Africa. For example, the monopolisation of productive sectors by a handful of companies – as well as the clearly problematic monopolisation of public service delivery – should be disassembled. Populist party politics has exploited the harsh socioeconomic conditions we face to push a governmental ideology in favour of increased centralisation of decision making. In other words, populist solutions largely entail increasing the power of the state to solve all our problems for us. This is demonstrated by the unfortunate reliance of large portions of a rapidly growing population on social grants. This is not sustainable and does not fulfil the constitutional right afforded to all citizens to lead a dignified life with equal access to economic opportunities and the independent pursuit of success.

Although the production and release of the policy strategy has been labelled a political exercise, the circumvention of cumbersome and paralysing political bureaucratic processes in bringing big ideas to the table should be applauded. In the fifth Parliament, the Finance and Appropriations committees showed little determination to seriously influence and change all too familiar patterns of spending and collecting revenue. Critical debates are needed around the purpose and impact of public sector unions (which should involve those unions in the debate), and on the insistence that public officials enjoy disproportionately favourable wage increases regardless of performance outcomes.

The eruption of social upheaval and public dissatisfaction can be attributed to misguided policy that seeks to isolate the South African labour market in an ever increasingly international global economy. Heavy criticism has come against the focus on international credit ratings agencies – but the global economy is undergoing rapid change and new multilateral opportunities and developmental financing should be exploited for the benefit of South Africa. Regulated integration of regional and continental labour markets can also boost economic growth by welcoming not only informal sector competition, but also inviting highly skilled professionals and well established, labour-intensive business.

The rigidity of economic policies in South Africa has further marginalised disenfranchised informal entrepreneurs in the central business districts of primary and secondary cities as well as townships around the country. In general, the transformative potential of public spending has been massively under-utilised by perpetually concentrating expenditure in uncompetitive service delivery streams in sectors such as energy, transport and water and, to a lesser extent, information and computer tech.

Sector Specific Reforms

The strategy identifies four major network industries for modernisation: energy, information and communications technology, transport, and water. OUTA agrees that these are crucial sectors for innovation and inclusive growth that can facilitate bottom-up economic transformation. Unfortunately, these were all sectors targeted by organised state-capture networks, due to their highly centralised and capital-intensive value chains. The effects of this structural challenge – and the entrenched criminal networks which may continue to exploit it – cannot be overlooked and must be addressed before pouring more money into these sectors. We cannot pretend this didn't happen.

Energy: The less said about Eskom the better. The financial condition of this state-controlled entity and the harm it has inflicted on the electricity supply industry – and the electricity price – is well documented. We note that the policy document addresses the need for competitive pricing in sectors, including referring to lowering consumer prices in markets which are important to low-income households. However, one of the biggest price problems is the increasingly high price of electricity: this needs addressing more urgently than many other prices, as it effects every industry and sector. Eskom's current strategy of charging higher prices to cover lower sales and a fundamentally unsustainable business model must serve as the primary example of the need for public sector reforms. OUTA requests the revival of the Independent Systems Market Operator Bill, which was abandoned for no apparent reason.

Transport: To demonstrate the degree of dysfunctionality in the rail sector, Transnet spent R37.779bn in the seven years to 2018/19 on acquiring 1 064 locomotives for the general freight business; Transnet estimates the total contract value at R54.5bn.[1] The contact was signed in March 2014 but by the end of 2018, only 497 locomotives – less than half – had been delivered, while exposure of state capture has found that billions of rand were siphoned off in this deal. To better govern the transport sector and avoid further corruption and maladministration in the rail industry, OUTA implores Parliament to facilitate substantive opportunities for participation in the highlighted Economic Regulation of Transport Bill.

Civil society demands a greater spend (by local and provincial government) on public transport alternatives such as bicycle lanes, subsidised and well-regulated midi- and mini-bus networks, as well as properly maintained and managed passenger rail networks as these could alleviate the costs of commuting to work for economic agents that are far removed from informal and formal productive activities. This is a question of reprioritisation. For example, if the City of Johannesburg could afford to spend R2.5bn upgrading the council chamber precinct a few years ago, it can manage to provide safe public transport lanes and inter-modal hubs in areas hosting acute unemployment rates.

[1] Costs are listed in the annual Budget Reviews. Parliament was told in December 2018 that 497 of the locomotives have been delivered so far.

ICT: The Communications Department was captured and has now been merged with Telecommunications and Postal Services. It failed to deliver on key strategic objectives of the communications sector and must rapidly adapt to a booming sector hosting an array of technological innovations in the private sector that makes many of its functions redundant. Expenditure in this sector must be fundamentally adjusted by funding innovative and transformative public-private partnerships that, for example, support small, medium and micro start-ups and accommodate enterprises in informal settlements as opposed to suppressing exponential growth in the private sector. One policy mechanism that can make a big difference here is significantly reducing the cost of data and ensuring that marginalised groups can access the internet affordably or freely.

Water: The Department of Water and Sanitation (now Department of Human Settlements, Water and Sanitation) has repeatedly been the focus of allegations of systemic corruption, particularly under former Minister Mokonyane. Again, this is a department with a massive budget and many, many infrastructure projects around the country – yet the provision of this essential resource is weak. Project or contract management failed dismally, with too many of these projects starting but not finishing. The Department's budget for such projects seems erratic, with numbers for spending changing each year and no clarity on why projects have stalled. An example is the Sedibeng Bulk Regional Sewerage Scheme and the Sebokeng Waste Water Treatment Works, where upgraded infrastructure should have been completed years ago but is still unfinished; this is one of the reasons the Vaal River is polluted. In the Western Cape, the risk of climate change and concomitant long-term decreases in fresh surface water availability have not been considered in the appropriation and application of money for improved infrastructure and water resource diversification.

In the former DWS, spending was so uncontrolled that it got away with replacing bucket toilets at up to R530 685 per toilet (2015/16), and also managed to run the entire bucket toilet replacement programme twice. We agree that failing water infrastructure is a problem. However, this also points to a significant failure of oversight, particularly by the national and provincial Departments of Cooperative Governance and Traditional Affairs and the Provincial and National Treasuries. Municipalities are supposed to maintain municipal water networks but do not budget for this or, where it is budgeted, don't spend properly, despite charging for the service. As is applicable to all other tentative sectoral policy shifts – OUTA calls for a simultaneous reform of accountability mechanisms that will see a greater connection between beneficiaries of public sector expenditure and those responsible for its execution. Recent increases in direct oversight by parliamentary committees such as the Standing Committee on Public Accounts summoning accounting authorities of various municipalities is a good example of more direct oversight. However, a stronger component of civil society participation (perhaps through more regularised and enfranchising parliamentary constituency engagements) can go a long way in effecting greater accountability.

Labour & Employment

Youth unemployment rates in South Africa are among the highest in the world. Tragic anecdotes of insurmountable barriers to entry in the economy have traditionally been answered by political rhetoric that promises citizens necessary change that can be delivered as a logical effect of voting for one party or another. This has proven to be false and practically short sighted. Entire demographic groups such as the Khoisan have come forward with claims of systemic disenfranchisement due to a lack of allegiance with vested political interests – while elite networks and well-connected individuals and families have accrued disproportionate gains from preferential government spending in capital-intensive sectors such as minerals and energy. We support measures aimed at upskilling the youth so they can participate meaningfully in the economy, not undirected spending which merely pads existing wage bills.

The entire financial model of local government must be transformed to disable municipalities from wasting money on excessive wages and outsourcing of accountability. Similarly, we urge labour unions to refrain from leveraging political power to force organs of state to waste money on a superfluous labour force that becomes unable to adapt to a fast-changing labour market and enter new spaces in the renewable energy sector: this is an issue both in municipalities and in entities like Eskom.

Similarly, undermining the political power of established public sector labour unions cannot be the reason for suppressing the development of competitive market disruption in all sectors currently dominated by state-owned entities.

Skills & Education

The South African primary and secondary education systems are rated among the worst in the world. In general, a progressive and depoliticised curriculum is essential for an innovative thinking and more equal access to economic opportunities in one of the most unequal societies in the world.

As articulated by the President, we are doing the youth an unforgivable disfavour if the practical skills necessary for competence in a highly competitive global economy are not offered as part of basic, primary and secondary education. The strategy states that:

since the highest return to human capital investments are associated with the earliest interventions, an educational life-cycle approach must include a strong emphasis on early childhood development, which has demonstrated the ability to: (i) improve long-term health outcomes; (ii) boost earnings by as much as 25 per cent; and (iii) generate a rate of return on investment of 7 to 10 per cent through better outcomes in education, health, and productivity.

OUTA agrees with this approach to public education since it faces the reality of our current school system’s dismal failure to enlighten every South African child and give them a real chance at independence and prosperity. Extremely ambitious spending programmes that may benefit a fraction of the population cannot reconcile this issue whilst publicly available statistics clearly show the inadequacy of educational quality at the most basic pedagogic levels.

We also support the idea of greater collaboration between the private sector and higher education institutions to decrease youth unemployment. However, the public schooling system criticised above requires well-trained and well-paid teachers, more of them to reduce the teacher:learner ratios, ensuring that teachers are better equipped to determine and deliver primary and secondary school curricula for the sole benefit of the children and their prospects of gainful employment.

Regarding higher education reforms, OUTA has noted with great concern the abuse of finances by Sector Education and Training Authorities (SETAs) that are controlled and operated by government. The Services SETA is a case in point here, where payments intended for interns and learners were apparently siphoned off. Parliament must pay close attention such problems and find solutions. These institutions are funded by taxpayers and their effectiveness must be consistently monitored and institutional structures and budgets must be adjusted according to observed performance outcomes.

When planning for large scale reforms in the water and energy sectors, it is important for government to fund and manage meaningful skills development programmes that are practically oriented and consider the social and environmental justifications of an emerging renewable energy sector. More generally, redundancies can be capitalised by implementing training and professional development prgrammes in public administration and other scarce skills that can enable constructive re-deployment in the public service at local government level.

Electricity

The technological lock-in and monopolisation of electricity generation has resulted in unthinkable amounts of money being absorbed by a single entity that is overstaffed, operationally inefficient and financially unsustainable. As a result, ordinary economic agents struggle to get by while facing increased Value Added Tax (VAT) as well as ever-increasing electricity tariffs. We are still waiting for the long-promised updated Integrated Resource Plan (IRP). OUTA supports the strategy in its call for the IRP to be updated regularly to reflect changes in economic conditions and technological advancements; we also agree that future electricity tariffs should be managed in a transparent and predictable manner and that the over-reliance of municipal budgets on electricity revenue needs to be corrected (among other local government reforms). Electricity tariffs need addressing: there is a real need for standardised, simplified tariffs rather than the current cumbersome system of hundreds of tariffs, with every municipality using its own set, which makes it extremely difficult for consumers to understand the costs.

Agriculture is seen as a key sector for employment. However, agriculture pays the highest electricity tariffs in the country (an average of 149.79c/kWh for 2018/19, according to Eskom statistics, about double the industrial tariff).

We note the proposal that Eskom's coal-fired power stations be sold off, but wonder about the practicality of this. Who would buy the old stations, particularly given Eskom's struggle to maintain them and the looming decommissioning for some? Who would buy the brand new stations, given the design flaws and that they are probably the world's most expensive power stations?

We support the move away from coal-fired power to renewables, and the suggestion that households be allowed to sell self-generated electricity.

We understand the very real concerns of unions over the loss of employment in coal mines and the need for reskilling. Perhaps some of this may be alleviated in the environmental rehabilitation of coal mines? Substantial ring-fenced funds for such rehabilitation already exist for this express purpose.

Water

OUTA has been campaigning for an Independent Water Regulator (IWR) to improve the universal provision and use of this precious resource and therefore supports the call for such a regulator and for a comprehensive management strategy for investment in water resource development, bulk water supply, and wastewater management. However, there are serious concerns around increasing water tariffs and a feeding a virtually bankrupt Department of Water and Sanitation.

Procurement

OUTA strongly supports the strategy's call for increased effectiveness of the office of the Chief Procurement Officer and perhaps a separate ombudsman to ensure that subcontracting is executed within the confines of relevant procurement legislation.

We recommend a reassessment of the way preferential procurement policy is implemented, as abuses of this appear to be rife, aimed at benefiting small elites at the expense of both other businesses and the public purse transparency is essential in procurement. This is where significant amounts of our country's money disappears or is badly spent. The legal requirements on publication of tenders, bids and awards need to be implemented forcefully, and it would be worth considering adding details of what is ultimately delivered. The public can be helpful monitors when such transparency is enforced.

Value for money

We are in favour of strategic cost cutting in public spending in the context of identifying and blocking waste in the form of corruption and general financial mismanagement. Public debt should be used for capital expenses that can yield returns, not salary bills. Eskom is the best example of exponential bad debt, where bailouts (likely funded by central government debt) are used at least partly for current expenses. We strongly support the Treasury's emphasis on the importance of monitoring and evaluation. In this regard, many of the existing performance indicators (as listed in departmental budgets in the Estimates of National Expenditure) are at best failing to achieve performance goals and, at worst, deliberately manipulated to cover up failure to deliver. Some examples from sectors rightly deemed as crucial in the Treasury's strategy paper:

The Communications Department measures the "number of monitoring reports on the implementation of broadcasting digital migration programme per year" but this doesn't tell us anything about the actual implementation of the programme (a well-known failure).

The Department of Higher Education and Training usefully measures statistics like "number of students enrolled in higher education institutions per year" and "number of first-year students in foundation programmes per year", but not the numbers (and percentages) of first-years who pass or those who graduate with undergraduate degrees. This department measures the number of new artisans registered for training each year, and helpfully measures the number qualified each year (just 77% of those registered) but has no measurement for the number of learners, interns and artisans funded through the SETAs who are in employment a year later or five years later. Numbers of "work-based opportunities" isn't very helpful, as these could be very short stints: it's a figure that looks good but doesn't give much insight into long-term employability. The SETAs cost South Africa R16bn a year (2019/20) in support of the very essential cause of youth employment, but there is very little indication that this money is generating the returns it should.

The Transport Department performance indicators include the number of bus trips on the bus rapid transit systems in the municipalities. However, for some municipalities (City of Johannesburg, City of Tshwane and George) these numbers look made up as they are so neatly rounded. Is this hiding the failures of these systems? The Department measures the number of Autopax bus passengers each year (2.97 million in 2018/19, a significantly higher number than use trains) but also show passenger unhappiness. There are no measurements for the number of buses refurbished, or what percentage that is of the fleet, or the number of new buses bought. This is an important sector for poorer customers. The Department of Water and Sanitation counts the number of wastewater systems assessed for compliance with Green Drop regulatory standards and the number of water supply systems assessed for compliance with Blue Drop regulatory standards each year but offers no information on how many of these met those standards.

Capable State and a new Compact

OUTA reiterates the strategy's emphasis on a capable state that must be supported by a new compact between the government, private sector, and other social partners such as academia and civil society.

The document states that this endeavour should prioritise strengthening the capability of the public sector and state-owned entities – the importance of such an effort cannot be overstated. The capability of the public sector to effectively and affordably deliver crucial services to ordinary South Africans has been eroded to an alarming extent. Trust in public officials' ability and willingness to deliver much needed services has also been virtually wiped out. This jeopardizes tax morality and contributes to widespread social pathologies and unrest. Over and above the potential avenues for reform dealt with earlier in this submission, the reconstruction of accountability mechanisms that transcend party politics is essential for the implementation of any transformative growth. OUTA's focus on state-owned entities as well as consistent activity in Parliament has laid bare the severe shortcomings in oversight and effective corporate governance underpinning the state's paralysis.

Civil society research has yielded an attractive proposal to completely reconfigure the current model of government shareholder management – which is essentially representative shareholding of the ordinary people of South Africa who effectively fund and own all capital at the state's disposal. This requires an overarching "SOE Act" that can reconcile the apparent loopholes and omissions of current legislation governing the financial and corporate management of state-owned entities and other organs of state. However, we call for the revival of the Government Shareholder Management Bill – which can provide for precisely such reforms. Civil society has grown restless with seemingly endless scandals of corruption and the normalisation of maladministration and non-compliance with core financial management laws such as the PFMA, MFMA, Companies Act and others. Importantly, much of the prevailing systemic and structural shortfalls in the public sector can be ascribed to overly centralised and opaque governance and accountability mechanisms provided for in current legislation.

The Report of the High-Level Panel on the Assessment of Key Legislation and Fundamental Change clearly indicates that more direct accountability of political leaders that act as custodians of taxpayers' money to the public, including civil society institutions representing public interests, is needed. On the prospect of increased private sector involvement in the operations of public service delivery outlined throughout the proposed economic strategy, OUTA strongly recommends that Parliament highlights the importance of forcing big business to explicitly and formally align itself with the public interest.

In pursuit of more effective and lawful public-private partnerships, the involvement of academic and civil society institutions is essential to ensure a strong element of public participation and objective credibility of new policy developments.